THE LOTOS GROUP

CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENEDED DECEMBER 31 ST 2006
PREPARED IN ACCORDANCE WITH THE INTERNATIONAL FINANCIAL REPORTING STANDARDS
ALONG WITH THE AUDITOR'S OPINION

CONSOLIDATED BALANCE SHEETS

as at December 31st 2006 and December 31st 2005

PLN '000	Note	Dec 31 2006	Dec 31 2005
ASSETS			
Non-current assets			
Property, plant and equipment, including:	11	3,500,285	3,294,043
Prepayments for tangible assets under construction	11	148,018	17,737
Goodwill	16	67,058	54,588
Intangible assets	15	55,858	51,086
Investment property	14	4,849	5,888
Investments in associated undertakings	17	83,381	83,336
Financial assets	18	23,642	20,193
Deferred tax asset	37	32,057	26,593
Other non-current assets	12	30,111	28,016
Total non-current assets		**3,945,259**	**3,581,480**
Current assets			
Inventories	21	1,707,442	1,432,939
Trade and other receivables, including:	22	1,276,475	1,060,348
- income tax receivables		33,068	8,705
Prepayments	13	13,562	11,288
Current financial assets	20	203,531	135,760
Cash and cash equivalents	23	772,387	767,794
Total current assets		**3,973,397**	**3,408,129**
Assets held for sale		**7,819**	**-**
Total assets		**7,926,475**	**6,989,609**

CONSOLIDATED BALANCE SHEETS
as at December 31st 2006 and December 31st 2005

PLN '000	Note	Dec 31 2006	Dec 31 2005
EQUITY AND LIABILITIES			
Equity			
Share capital	25	113,700	113,700
Reserve funds		970,951	970,951
Retained earnings/(deficit)		4,146,823	3,466,911
Currency-translation differences		(3,556)	2,266
Equity attributable to equity holders of the parent		**5,227,918**	**4,553,828**
Equity attributable to minority interests	28	**306,416**	**254,281**
Total equity		**5,534,334**	**4,808,109**
Non-current liabilities			
Interest-bearing loans and borrowings	29	330,706	294,198
Non-current provisions	30	208,082	191,802
Deferred tax liability	37	201,064	218,677
Other (financial) liabilities		10,801	11,230
Total non-current liabilities		**750,653**	**715,907**
Current liabilities			
Trade payables, accruals and deferred income, and other liabilities, including:	31	1,385,106	1,273,519
- income tax expense		3, 413	65,302
Interest-bearing loans and borrowings	29	173,526	111,452
Current provisions	30	80,579	79,660
Other financial liabilities		2,277	962
Total current liabilities		**1,641,488**	**1,465,593**
Total liabilities		**2,392,141**	**2,181,500**
Total equity and liabilities		**7,926,475**	**6,989,609**

CONSOLIDATED INCOME STATEMENTS
for the years ended December 31st 2006 and December 31st 2005

PLN '000	Note	Year ended Dec 31 2006	Year ended Dec 31 2005
Sales revenue	32	12,810,883	9,645,545
Cost of sales	33	(10,987,999)	(8,053,554)
Gross profit on sales		**1,822,884**	**1,591,991**
Other operating income	34	28,099	35,645
Excess of net assets' fair value over acquisition cost		-	266,625
Selling costs	33	(666,177)	(501,650)
General and administrative expenses	33	(316,101)	(273,986)
Other operating expenses	35	(70,359)	(48,718)
Operating profit		**798,346**	**1,069,907**
Financial income	36	133,295	75,742
Financial expenses	36	(41,561)	(52,557)
Share in investments in associated undertakings	17	25,811	28,472
Sale of investments in associated undertakings		-	16,090
Pre-tax profit		**915,891**	**1,137,654**
Corporate income tax	37	(181,239)	(168,815)
Net profit on continued operations		**734,652**	**968,839**
Attributable to:			
Equity holders of the parent		679,912	915,124
Minority interests	28	54,740	53,715
Net earnings per share			
- basic	27	5.98	9.47
- diluted		-	-

Notes on pp. 9-88 are an integral part of these consolidated financial statements

CONSOLIDATED CASH FLOW STATEMENTS

for the years ended December 31st 2006 and December 31st 2005

PLN '000	Note	Year ended Dec 31 2006	Year ended Dec 31 2005
Cash flows from operating activities			
Net profit		**734,652**	**968,839**
Adjustments:			
Share in net profit/(loss) of subordinated undertakings valued with equity method		(25,811)	(28,472)
Depreciation and amortisation		297,356	263,615
Foreign exchange gains/(losses)		(6,556)	568
Net interest and dividend paid		11,098	7,059
(Profit)/loss on investing activities		27,651	(17,340)
Current income tax		181,239	168,815
Income tax paid		(290,568)	(135,467)
Increase in receivables	24	(189,154)	(163,192)
Increase in inventories	24	(274,491)	(458,772)
Increase in liabilities and accruals and deferred income	24	175,099	271,859
(Decrease in prepayments and accrued income	24	(7,243)	(8,868)
Increase/(decrease) in provisions	24	19,201	(3,435)
Other	24	1,968	(267,027)
Net cash provided by/(used in) operating activities		**654,441**	**598,182**
Cash flows from investing activities			
Sale of non-current financial assets		-	41,648
Dividends received		2,527	33,469
Interest received		10,951	315
(Acquisition)/sale of property, plant and equipment and intangible assets		(540,625)	(799,195)
Acquisition of non-current financial assets, including:		(3,449)	(119,554)
Acquisition of subsidiary undertakings, net of cash acquired		-	(117,680)
(Acquisition)/sale of debt securities		531	-
(Acquisition)/ sale of current financial assets		(45,397)	(90,193)
Other, net		(146,052)	17,448
Net cash provided by/(used in) investing activities		**(721,514)**	**(916,062)**
Net cash provided by/(used in) investing activities			
Increase in loans and borrowings		68,399	351,349
Share issue		-	1,015,000
Repayment of loans and borrowings		(118,888)	(396,018)
Interest paid		(20,814)	(16,513)
Dividends paid to parent undertaking's shareholders		-	(15,740)
Dividends paid to minority shareholders		(2,521)	(3,022)
Other, net		(4,327)	(4,740)
Net cash provided by/(used in) financing activities		**(78,151)**	**930,316**
Change in cash due to foreign exchange (gains)/losses		1,595	346
Change in net cash		**(143,629)**	**612,782**
Cash at beginning of period	24	767,794	155,012
Cash at end of period	24	624,165	767,794
- restricted cash	24	23,143	1,572

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

for the years ended December 31st 2006 and December 31st 2005

(PLN '000)	Share capital	Reserve funds	Retained earnings/ (deficit)	Translation reserve	Equity attributable to equity holders of the parent	Equity attributable to minority interests	Total equity
Jan 1 2005	**78,700**	**-**	**2,563,930**	**-**	**2,642,630**	**14,882**	**2,657,512**
Net profit for the year ended Dec 31 2005	-	-	915,124		915,124	53,715	968,839
Share issue	35,000	-	-	-	35,000	-	35,000
Share premium	-	980,000	-	-	980,000	-	980,000
Issue expenses including income tax	-	(9,049)	-	-	(9,049)	-	(9,049)
Other	-	-	3,597	2,266	5,863	185,684	191,547
Dividend	-	-	(15,740)	-	(15,740)	-	(15,740)
Dec 31 2005 (comparable data)	**113,700**	**970,951**	**3,466,911**	**2,266**	**4,553,828**	**254,281**	**4,808,109**
Jan 1 2006	**113,700**	**970,951**	**3,466,911**	**2,266**	**4,553,828**	**254,281**	**4,808,109**
Net profit for the twelve months ended December 31st 2006	-	-	679,912	-	679,912	54,740	734,652
Dividend	-	-	-	-	-	(2,521)	(2,521)
Other	-	-	-	(5,822)	(5,822)	(84)	(5,906)
Dec 31 2006	**113,700**	**970,951**	**4,146,823**	**(3,556)**	**5,227,918**	**306,416**	**5,534,334**

NOTES TO THE FINANCIAL STATEMENTS

1. General Information

Grupa LOTOS S.A. (“the Company”, “the Parent Undertaking”), the Parent Undertaking of the Group of Grupa LOTOS S.A. (“the Group”), was established by virtue of the Notarial Deed dated September 18th 1991. On April 10th 2002, the Company was entered into the National Court Register maintained by the District Court of Gdańsk, XII Commercial Division of the National Court Register (currently the District Court for Gdańsk – Północ, VII Commercial Division of the National Court Register) under entry No. KRS 0000106150. The Company was assigned the Industry Identification Number (REGON) 190541636.

The Company’s registered office is situated at ul. Elbląska 135, 80-718 Gdańsk.

In 2003, by virtue of its decision of May 28th 2003, the District Court of Gdańsk, XII Commercial Division of the National Court Register, changed the Company’s name from Rafineria Gdańska Spółka Akcyjna to Grupa LOTOS Spółka Akcyjna.

The Group’s core business consists in the production and processing of refined petroleum products and their wholesale and retail sale. The Group’s business also includes exploration and extraction of crude oil and natural gas reserves.

2. Composition of the Group

Name	Registered office	Business profile	Method of consolidation /valuation of shares	Percentage of share capital held by the Group	
				Dec 31 2006	**Dec 31 2005**
Parent Undertaking					
Grupa LOTOS S.A.	Gdańsk	production and processing of refined petroleum products (mainly fuels) and their wholesale	Not applicable	Not applicable	Not applicable
Direct Subsidiary Undertakings					
LOTOS Paliwa Sp. z o.o.	Gdańsk	wholesale and retail sale of fuels, light fuel oil, management of the LOTOS service station network	full	100.00%	100.00%
LOTOS Partner Sp. z o.o.	Gdańsk	sales of fuels and provision of services for retail networks of international concerns; logistic services	full	100.00%	100.00%
LOTOS Mazowsze S.A.	Mława	sales of LPG, heavy fuel oil and special products (sulphur, plasticizers, fuels containing recycled components)	full	100.00%	100.00%
LOTOS Oil S.A.	Gdańsk	production and sale of lubricating oils and lubricants, and domestic sales of base oils	full	100.00%	100.00%
LOTOS Asfalt Sp. z o.o.	Gdańsk	production and sale of bitumens	full	100.00%	100.00%
LOTOS Ekoenergia S.A.	Gdańsk	construction of basic PKRT units; the company has not commenced operations	full	100.00%	100.00%
LOTOS Kolej Sp. z o.o.	Gdańsk	railway transport	full	100.00%	100.00%

Name	Registered office	Business profile	Method of consolidation /valuation of shares	Percentage of share capital held by the Group	
				Dec 31 2006	**Dec 31 2005**
LOTOS Serwis Sp. z o.o.	Gdańsk	maintenance of mechanical and electric operations and controlling devices, repairs	full	100.00%	100.00%
LOTOS Lab Sp. z o.o.	Gdańsk	laboratory testing	full	100.00%	100.00%
LOTOS Straż Sp. z o.o.	Gdańsk	fire protection	full	100.00%	100.00%
LOTOS Ochrona Sp. z o.o.	Gdańsk	personal and property protection	full	100.00%(1)	87.44%
LOTOS Parafiny Sp. z o.o.	Jasło	production and sale of paraffin	full	100.00%	100.00%
LOTOS Czechowice S.A. (parent undertaking of another group, formerly Rafineria Czechowice S.A.(2))	Czechowice	storage and distribution of fuels(3)	full	80.04%	80.04%
LOTOS Jasło S.A. (parent undertaking of another group, formerly Rafineria Jasło S.A.(4))	Jasło	production and processing of refined petroleum products and their wholesale and retail sale	full	80.01%	80.01%
Petrobaltic S.A. (parent undertaking of another group)	Gdańsk	acquisition of reserves, crude oil and natural gas production	full	69.00%	69.00%
UAB LOTOS Baltija	Litwa	wholesale and retail sale of lubricating oils in Lithuania, Belarus, Ukraine and Latvia	not consolidated	100.00%	100.00%
BiproRaf Sp. z o.o. (5))	Gdańsk	design services for oil industry	not consolidated	50.00%	50.00%
Rafineria Nafty Glimar S.A.w upadłości (in bankruptcy)	Gorlice	refining (currently discontinued due to the company's bankruptcy)	not consolidated due to lack of control	91.54%	91.54%
LOTOS Hydrokompleks Sp. z o.o.	Gorlice	construction and subsequent operation of hydrocomplex unit; the company has not commenced operations	not consolidated	100.00%	100.00%
LOTOS Park Technologiczny Sp. z o.o.	Gorlice	Business and management consultancy services	full	86.91%	90.00%
Laboratorium „Badacz” Sp. z o.o.	Jasło	services	not consolidated	(6)	100.00%
Indirect Subsidiary Undertakings					
RCEkoenergia Sp. z o.o	Czechowice-Dziedzice	services	full	80.04%	80.04%
LOTOS Biopaliwa Sp. z o.o. (7) (former RCParafiny Sp. z o.o.)	Czechowice-Dziedzice	no operations	full	80.04%	80.04%
RCRemo Sp. z o.o.	Czechowice-Dziedzice	services	-	(8)	80.04%
CBA Racer Sp. z o.o.	Czechowice-Dziedzice	services	-	(9)	80.04%
RCSerwis Sp. z o.o.	Czechowice-Dziedzice	services	(10)	86.91%	80.04%
RCPaliwa Sp. z o.o. in liquidation(11)	Czechowice-Dziedzice	trading (not commenced)	equity method	80.04%	80.04%
RCTransport Sp. z o.o.	Czechowice-Dziedzice	services	-	(12)	80.04%
LOTOS Tank Sp. z o.o.(13)	Jasło	trading	full/equity method	86.01%	86.01%
Rafineria Jasło Monto-Rem Sp. z o.o.	Jasło	services	full	(8)	79.56%
Plastekol Organizacja Odzysku S.A.	Jasło	services	full	53.61%	53.61%

Name	Registered office	Business profile	Method of consolidation /valuation of shares	Percentage of share capital held by the Group	
				Dec 31 2006	**Dec 31 2005**
Rafineria Jasło Sped-Kol Sp. z o.o.	Jasło	no operations – lease of assets to LOTOS Kolej	not consolidated	(14)	80.01%
Petrosoft.pl Technologie Informatyczne Sp. z o.o.	Jasło	services	not consolidated	80.01%	80.01%
Chemipetrol Sp. z o.o.	Jasło	trading – assets transferred to LOTOS Parafiny in exchange for shares	not consolidated	80.01%	80.01%
Miliana Shipping Company Ltd.	Cyprus	services	full	68.93%	68.93%
Aphrodite Offshore Services Ltd.	Netherlands Antilles	services	not consolidated	69.00%	69.00%

(1) On December 20th 2006, Grupa LOTOS S.A. acquired the remaining 12.56% of shares in LOTOS Ochrona Sp. z o.o. under a share purchase agreement. On March 8th 2007, the District Court for Gdańsk-Północ of Gdańsk, VII Commercial Division of the National Court Register, registered a change in the share capital structure of LOTOS Ochrona Sp. z o.o. The share capital of LOTOS Ochrona Sp. z o.o. amounts to PLN 302.5 thousand and is divided into 605 equal indivisible shares with a par value of PLN 500 per share, conferring rights to 605 votes.

(2) On December 19th 2005, the District Court of Katowice registered the change of the name of Rafineria Czechowice S.A. to LOTOS Czechowice S.A.

(3) On March 31st 2006, the Company discontinued the processing of crude oil.

(4) On January 2nd 2006, the District Court of Rzeszów registered the change of the name of Rafineria Jasło S.A. to LOTOS Jasło S.A.

(5) As described in Note 40 of the Notes to the financial statements, on January 15th 2007, Grupa LOTOS S.A. sold 35 shares in Przedsiębiorstwo Projektowo-Usługowe BiproRaf Sp. z o.o. (PPU BiproRaf Sp. z o.o.) to KTI Poland S.A. of Warsaw for the price of PLN 2,750 thousand.

(6) On January 3rd 2006 Laboratorium Badacz Sp. z o.o. was liquidated and merged into LOTOS Lab Sp. z o.o. by transferring all its assets to LOTOS Lab Sp. z o.o.

(7) Name changed to LOTOS Biopaliwa Sp. z o.o. with effect from May 10th 2006.

(8) On June 30th 2006, LOTOS Serwis Sp. z o.o. acquired Rafineria Jasło Monto-Rem Sp. z o.o. of Jasło and RC Remo Sp. z o.o. of Czechowice-Dziedzice.

(9) On December 28th 2006, CBA Racer Sp. z o.o. was incorporated into LOTOS Czechowice S.A.

(10) Shares contributed to LOTOS Park Technologiczny Sp. z o.o. by LOTOS Czechowice S.A.

(11) By virtue of the decision of November 27th 2006, issued in response to the petition for the opening of liquidation proceedings of November 9th 2006, the opening of the liquidation proceeding concerning RC Paliwa Sp. z o.o. was registered by the District Court of Katowice, VIII Commercial Division of the National Court Register.

(12) On February 16th 2006, LOTOS Czechowice S.A. signed an agreement on sale, to Paul Klacska Sp. z o.o., of 100% of shares in RCTransport Sp. z o.o., that is 3,213 shares with a par value of PLN 500 per share and total par value of PLN 1,606.5 thousand. The selling price of all the shares is PLN 2,800 thousand.

(13) On April 11th 2007, Grupa LOTOS S.A. and LOTOS Jasło S.A. executed an agreement on the sale of 700 shares in LOTOS Tank Sp. z o.o. (see Note 40). The total price paid for the shares was PLN 642.5 thousand. Following the transaction, Grupa LOTOS S.A. holds 100% of shares in LOTOS Tank Sp. z o.o.

(14) On March 8th 2007, the company was deleted from the National Court Register of the District Court of Rzeszów, XII Commercial Division of the National Court Register.

As at December 31st 2006 and December 31st 2005, the Company’s share in the total vote at the General Shareholders Meetings of its subsidiary undertakings equalled the Company’s share in the share capital of these undertakings.

3. Composition of the Supervisory and Management Boards of the Parent Undertaking

August 23rd 2005 saw the appointment of the Supervisory Board of Grupa LOTOS S.A. for the sixth term of office. The composition of the Supervisory Board was as follows:

Cezary Nowosad – Chairman of the Supervisory Board
Janusz Rachoń – Deputy Chairman of the Supervisory Board
Katarzyna Dawidczyk – Secretary of the Supervisory Board
Grzegorz Urban
Beata Zawadzka
Anna Andrzejczak
Piotr Krupa
Robert Karwowski
Jacek Mościcki

On January 30th 2006, the Extraordinary General Shareholders Meeting removed the following persons from the Supervisory Board:

Cezary Nowosad – Chairman of the Supervisory Board
Janusz Rachoń – Deputy Chairman of the Supervisory Board
Katarzyna Dawidczyk – Secretary of the Supervisory Board
Anna Andrzejczak
Grzegorz Urban
Piotr Krupa
Robert Karwowski

and appointed the following persons:

Jan Szomburg – Chairman of the Supervisory Board
Jan Stefanowicz – Deputy Chairman of the Supervisory Board
Grzegorz Szczodrowski – Secretary of the Supervisory Board
Jacek Tarnowski
Henryk Siodmok

On June 16th 2006, Mr Jan Szomburg resigned from the office of the Chairman of the Supervisory Board of Grupa LOTOS S.A.

As at December 31st 2006 and as at the date of release of these financial statements, the composition of the Supervisory Board of Grupa LOTOS S.A was as follows:

Jan Stefanowicz – Deputy Chairman of the Supervisory Board
Grzegorz Szczodrowski – Secretary of the Supervisory Board
Jacek Tarnowski
Henryk Siodmok
Beata Zawadzka
Jacek Mościki

Until June 19th 2006 the Management Board appointed for the fifth term of office was composed of:
Paweł Olechnowicz – President of the Management Board
Marek Sokołowski – Vice-President of the Management Board
Wojciech Kowalczyk – Vice-President of the Management Board

On June 19th 2006, the Supervisory Board of Grupa LOTOS S.A. adopted a resolution on the appointment of the Management Board for the sixth term of office. The composition of the Management Board is as follows:

Paweł Olechnowicz – President of the Management Board
Marek Sokołowski – Vice-President of the Management Board
Mariusz Machajewski – Vice-President of the Management Board

Furthermore, taking into consideration the position of the majority shareholders – Nafta Polska S.A. and the State Treasury – the Supervisory Board resolved to organise a contest for the position of the President and certain other positions on the Management Board of Grupa LOTOS S.A. It was decided that after closing of the contest the Management Board should be composed of not fewer that five members

On September 29th 2006, the Supervisory Board of Grupa LOTOS S.A. defined the composition of the Management Board of the sixth term of office and the division of responsibilities between its members. Furthermore, after acquainting itself with the results of the qualification procedure, holding interviews with the candidates, and obtaining the recommendation of the President of the Management Board, the Supervisory Board resolved to appoint the following persons to the Company's Management Board:
Marek Sokołowski – to the position of Vice-President of the Management Board responsible for production and development, and
Jarosław Kryński – to the position of Vice-President of the Management Board responsible for sales.

As at December 31st 2006 and as at the date of release of these consolidated financial statements, the composition of the Management Board of Grupa LOTOS S.A was as follows:

Paweł Olechnowicz – President of the Management Board, CEO
Marek Sokołowski – Vice-President of the Management Board, Production and Development Director
Jarosław Kryński – Vice-President of the Management Board, Chief Commercial Officer
Mariusz Machajewski – Vice-President of the Management Board, Chief Financial Officer

4. Approval of the Consolidated Financial Statements

These financial statements were approved for publication by the Management Board on April 17th 2007.

5. Going Concern

These consolidated financial statements were prepared on the assumption that the companies of the Group would continue their business activities in the foreseeable future. As at the date of signing these consolidated financial statements no facts or circumstances have been identified that might pose a threat to the Group's companies continuing as going concerns in the 12 months following the balance-sheet date.

In 2007, one of the Group's companies – LOTOS Jasło S.A. has commenced the implementation of an extensive restructuring programme aimed at reducing the staff headcount and eliminating unprofitable production areas. The programme provides for maintenance and expansion of profitable areas of the company's business as well as new investment projects related to production, which are to ensure positive financial results and the company's continuing its operations.

As the technical and technological condition of processing units at LOTOS Czechowice S.A., the Group's company, is not adequate in view of the changing environment, as well as the ever-increasing quality requirements for oil products and growing expectations of customers in this respect, the range of the company's products which can be successfully placed on the market has been decreasing.

As a result of the aforementioned factors oil processing by LOTOS Czechowice S.A. ceased to be economically viable and as such was discontinued on March 31st 2006.

Following the discontinuation, the company's core business comprises storage and distribution of fuels.

A project that should facilitate future efficient operation of the Group's companies located in Czechowice is the continued construction of a fatty acid methyl esters (FAME) production unit by a subsidiary of LOTOS Czechowice S.A. The fatty acid methyl esters are used as biofuels to Diesel engines or biocomponents of diesel oil. The FAME project is of great significance to the exploitation of infrastructure and human resources of LOTOS Czechowice.

6. Duration of the Group

The duration of the Parent Undertaking and its subsidiaries is unlimited.

7. Balance-Sheet Date and the Period Covered by These Consolidated Financial Statements

These consolidated financial statements of the LOTOS Group comprise the balance-sheet data as at December 31st 2006 and the comparable data as at December 31st 2005. The income statement, the cash-flow statement and the statement of changes in the Group's equity present the data for January 1st – December 31st 2006 along with the comparable data for January 1st – December 31st 2005.

The financial information as at December 31st 2006 and for the year then ended contained in these consolidated financial statements was audited. The financial information as at December 31st 2005 and for the year ended on December 31st 2005 was audited by a chartered auditor, who issued an audit opinion on April 27th 2006.

8. Measurement Currency and Reporting Currency

The measurement and reporting currency of these consolidated financial statements is the Polish złoty (PLN). These consolidated financial statements are presented in the złoty (PLN), and all the figures are presented in thousands of złoty, unless indicated otherwise.

9. Basis for the Preparation of the Consolidated Financial Statements

These consolidated financial statements were prepared in accordance with the International Financial Reporting Standards ("IFRS") and the EU-endorsed IFRS.

The IFRS include the standards and interpretations approved by the International Accounting Standards Board ("IASB") and by the International Financial Reporting Interpretation Committee ("IFRIC").

With the exception of the Parent Undertaking and foreign undertakings, the Group companies maintain their accounting books in accordance with the accounting standards specified in the Polish Accountancy Act of September 29th 1994 (the "Act") and the provisions issued thereunder ("Polish Accounting Standards" – "PAS"). These consolidated financial statements include adjustments which are absent from the accounting books of the Group's undertakings, and which have been introduced to adjust the financial information concerning these undertakings to the IFRS.

The accounting policies and calculation methods adopted in the preparation of these consolidated financial statements are the same as those used in the preparation of the consolidated financial statements for the year ended December 31st 2005.

Starting from January 1st 2006, the following standards were amended by the International Accounting Standards Board:

- IAS 19: *Employee Benefits*
- IAS 21: *The Effects of Changes in Foreign Exchange Rates*
- IAS 39: *Financial Instruments: Recognition and Measurement*.

The following standards and interpretations have been in effect since January 1st 2006:

- IFRS 6: *Exploration for and Evaluation of Mineral Resources*
- IFRIC 4: *Determining whether an Arrangement contains a Lease*
- IFRIC 5: *Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds*
- IFRIC 6: *Liabilities Arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment*.

The Company has reviewed the new standards and the amendments to the existing ones. The new standards and the changes to the existing ones do not apply to these consolidated financial statements, with the exception of IFRS 6: *Exploration for and Evaluation of Mineral Resources*, whose adoption had no material impact on the Group's accounting policies.

The following standards and interpretations have been issued by the International Accounting Standards Board or the International Financial Reporting Interpretation Committee but have not entered into force yet:

- Amendment to IAS 1: *Presentation of Financial Statements: Capital Disclosures* (applies to annual periods beginning after January 1st 2007),
- Amendment to IAS 23: *Borrowing Costs* (effective as of January 1st 2009, not yet adopted by the European Union),
- IFRS 7: *Financial Instruments: Disclosures* (applies to annual periods beginning after January 1st 2007),
- IFRS 8: *Operating Segments* (applies to annual periods beginning after January 1st 2009),
- IFRIC 7: *Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies* (applies to annual periods beginning after March 1st 2006),
- IFRIC 8: *Scope of IFRS 2* (applies to annual periods beginning after May 1st 2006),
- IFRIC 9: *Reassessment of Embedded Derivatives* (applies to annual periods beginning after June 1st 2006),
- IFRIC 10: *Interim Financial Reporting and Impairment* (applies to annual periods beginning after November 1st 2006),
- IFRIC 11: *Group and Treasury Share Transactions* (applies to annual periods beginning after March 1st 2007),
- IFRIC 12: *Service Concession Arrangements* (applies to annual periods beginning after January 1st 2008).

The Management Board expects that the implementation of the standards and interpretations listed above will not have a material effect on the accounting policies applied by the Group.

Due to the introduction of IRFS 7 and amendments to IAS 1, the Group is obliged to provide further disclosures concerning the capital and financial instruments held by the Group in the year beginning on January 1st 2007. The Group is currently analysing the abovementioned requirements in order to make adequate disclosures in the financial statements prepared for the year beginning on January 1st 2007.

The Group does not prepare information on individual business segments, as it does not meet the requirements stipulated in IFRS 14: *Segment Reporting*.

10. Accounting Policies

The consolidated financial statements have been prepared using the historical cost method, except for financial derivatives, which are measured at fair value.

The key accounting policies adopted by the Group are presented below.

10.1. Basis for Consolidation

These consolidated financial statements have been prepared on the basis of the financial statements of the Parent Undertaking and financial statements of the material undertakings it controls, prepared as at December 31st 2006.

The financial statements of the subsidiaries, subject to the restatements made to ensure compliance with the IFRS, are prepared for the same reporting period as the financial statements of the Parent Undertaking, with the use of consistent accounting policies and in accordance with uniform accounting policies applied for transactions and economic events of a similar nature. Adjustments are made in order to eliminate any discrepancies in the adopted accounting policies.

All significant balances and transactions between the Group's undertakings, including significant unrealised profits on intra-group transactions, have been eliminated in their entirety. Unrealised losses are eliminated unless they are indicative of an impairment of value.

Subsidiary undertakings are consolidated starting from the date when the Group assumes control over them and cease to be consolidated when the control is lost. The Company is deemed to exert control when it holds, directly or through its subsidiary undertakings, more than 50% of votes in a given undertaking unless it is possible to prove that the ownership of over 50% of votes is not tantamount to exerting control. The Company's ability to influence a given undertaking's financial and operational policies is also deemed exerting control.

10.2. Investments in Associated Undertakings

Investments in associated undertakings are recognised using the equity method. Associated undertakings are the undertakings over which the Parent Undertaking has significant influence, either directly or indirectly through its subsidiary undertakings, and which are neither its subsidiary undertakings nor interests in joint ventures. The financial statements of associated undertakings serve as a basis for the equity method valuation of the shares held by the Parent Undertaking. Associated undertakings' financial years coincide with the Parent Undertaking's financial year.

Investments in associated undertakings are initially recognised in the balance-sheet at acquisition cost, adjusted for subsequent changes in the Parent Undertaking's share in the net assets of the associated undertakings, and reduced by impairment losses, if any. The income statement includes the Parent Undertaking's share of the profits and losses of the associated undertakings. In the case of a change recognised directly in an associated undertaking's equity, the Parent Undertaking recognises its share in such change and, if applicable, discloses it in the statement of changes in equity.

10.3. Intangible Assets

Intangible assets are recognised if the Group is likely to obtain future economic benefits attributable directly to the assets. Initially, intangible assets are recognised at acquisition or production cost, if they are acquired in separate transactions. Intangible assets acquired as part of the acquisition of a business are recognised at fair value as at the acquisition date. Following initial recognition, intangible assets are valued at acquisition or production cost less accumulated amortisation and impairment losses.

The Group capitalises and recognises as an intangible asset both the licence fees for the exploration and identification of crude oil and natural gas reserves as well as the fees under the concluded mining use agreements for the exploration and identification of crude oil and natural gas reserves. The commencement and execution of the exploration work is conditional upon obtaining relevant licence and establishing the mining use.

Intangible assets are amortised using the straight-line method over their estimated useful lives.

The expected useful lives of the Group's intangible assets range from 2 to 21 years.

The amortisation period and the amortisation method for an intangible asset are reviewed at the end of each financial year. Changes in the expected useful life or pattern of consumption of the future economic benefits embodied in the asset are reflected by changing the amortisation period or amortisation method, respectively, and are accounted for as changes in accounting estimates.

Useful lives are also reviewed each year and, if required, they are adjusted with effect from the beginning of the following financial year.

With the exception of capitalised expenditure on research and development, expenditure on intangible assets produced by the Company is not capitalised and is disclosed under expenses for the period in which they were incurred.

10.4. Goodwill of Subordinated Undertakings

The goodwill relating to acquisition of a business undertaking is initially recognised at acquisition cost, equal to the excess of the cost of the business combination over the acquiring undertaking's share in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquired undertaking. Following the initial recognition, goodwill is carried at acquisition cost less cumulative impairment losses. Goodwill is tested for impairment once a year. It is not amortised.

As at the date of assuming control, the acquired goodwill is allocated to every identifiable cash-generating unit. The Company calculates any impairment of value by estimating recoverable value of the cash-generating unit relevant to a given part of goodwill. If the recoverable value of a cash-generating unit is lower than its carrying value, the Company recognises impairment losses. If goodwill comprises a part of a cash-generating unit and the Company sells a part of the business of the cash-generating unit, the goodwill connected with the sold business is included in the carrying value of the sold business for the purpose of calculating gains or losses on disposal of the part of business. In such a case, goodwill pertaining to the sold business should be measured using the relative value of the sold business, *pro-rata* to the interest in the retained part of the cash-generating unit.

10.5. Property, Plant and Equipment

Property, plant and equipment, other than land, are valued at acquisition or production cost, less accumulated depreciation and impairment losses.

Land is valued at acquisition cost less any impairment losses. In the case of perpetual usufruct of land, acquisition cost is understood to mean the amount paid to a third party.

Initial cost of property, plant and equipment comprises the acquisition cost plus all costs directly related to their acquisition and adaptation for use. This cost also includes the cost of replacing component parts of plant and equipment, which is recognised when incurred, if relevant recognition criteria are fulfilled. Costs incurred on an asset which is already in service, such as repairs, overhauls or operating fees, are expensed in the reporting period in which they were incurred.

Property, plant and equipment (including their components), other than land, are depreciated using the straight-line method over their estimated useful lives. The depreciation rates are as follows:

Buildings and structures	1,14% - 30%
Plant and equipment	1,4% - 50%
Vehicles	6% - 50%
Other property, plant and equipment	6,67% - 33,33%

An item of property, plant and equipment may be derecognised from the balance sheet if it is sold or if the company does not expect to realise any economic benefits from its further use. Gains or losses on derecognition of an asset (calculated as the difference between net proceeds from its sale, if any, and the carrying value of the asset) are disclosed in the income statement in the period when the asset was derecognised.

The residual value, useful economic life and depreciation method are reviewed – and adjusted if required – with effect from the beginning of the next year.

The costs of each overhaul are included in the carrying value of property, plant and equipment, if relevant recognition criteria are fulfilled.

In its financial statements, under tangible assets, the Group discloses an asset corresponding to the value of provision for the liquidation of a mining plant. This issue is regulated under IAS 16: *Property, Plant and Equipment*, which reads: "The cost of an item of property, land and equipment comprises … the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period." The Group's obligation to incur costs of liquidation of the Offshore Oil Rig results directly from the reasons specified in IAS 16. Under Paragraph 63 of the same standard, the entities applying the IAS are obliged to test the value of an asset periodically, at least at each balance-sheet date. It should further be emphasised that the International Financial Reporting Interpretations Committee (IFRIC) has issued Interpretation IFRIC 1: *Changes in Existing Decommissioning, Restoration and Similar Liabilities*. The Interpretation directly refers to, *inter alia*, IAS 16, including in particular to the revaluation of an asset recognised as future liquidation cost. Revaluation of an asset so recognised may be caused by:

– change in estimated cash used to ensure the performance of the liquidation obligation,
– change in the current market discount rate,

10.6. Assets under Construction

Investments in progress are valued at the amount of aggregate costs directly attributable to the acquisition or production of such assets, including financial expenses, less impairment losses, if any. Investments in progress are not depreciated until completed and placed in service.

Investments in progress comprise property, plant and equipment which is under construction or assembly and are recognised at acquisition or production cost.

Financial expenses capitalised under tangible assets under construction include servicing costs of the debt incurred to finance the assets.

The cost of exploration for crude oil and natural gas reserves is capitalised as tangible assets under construction until the size of the deposit and the economic viability of production are determined. Upon confirmation of the existence of deposits whose exploitation is technically and economically viable, the expenditure incurred on the exploration activities is transferred to tangible assets and is subsequently depreciated. If exploration drillings do not result in discovery of any deposits whose exploitation is technically and economically viable, valuation allowances for tangible assets under construction are charged to the financial result of the period in which it is found that there is no possibility of any economic utilisation of the discovered deposits.

10.7. Expenditure on Exploration and Evaluation of Resources

Assets related to exploration and evaluation of mineral resources comprise expenditure on exploration and evaluation of mineral resources disclosed as assets in accordance with the accounting policies adopted by the Group. The expenditure on exploration and evaluation of mineral resources includes expenses incurred by the Group in connection with exploration and evaluation of mineral resources before technical and economic viability of exploitation of the mineral resources can be proven. The exploration and evaluation of mineral resources involves the exploration for mineral resources, including crude oil, natural gas and similar non-renewable resources, after the company has obtained the licence to conduct exploration work in a given area, and the determination of the technical and commercial viability of exploitation of the mineral resources.

The Group classifies assets related to exploration and evaluation of mineral resources as property, plant and equipment or intangible assets, depending on the type of the acquired assets, and applies this classification policy in a consistent manner. After the technical and commercial viability of exploitation of mineral resources has been proven, the Group no longer classifies such assets as related to exploration and evaluation of mineral resources. The Group presents and discloses valuation allowances for assets related to exploration and evaluation of mineral resources in accordance with IFRS 6 and evaluates such assets in accordance with IAS 36. Valuation allowances are charged against the financial result, in accordance with IAS 36.

The Group examines a need to make valuation allowances for assets related to exploration and evaluation of mineral resources by considering, *inter alia*, the following circumstances related to a given area of exploration:

– the term for which the company was granted the licence to conduct exploration work expired in the course of the current financial period or will expire in the near future, and no extension of the term is envisaged;

– the budget or the financial plan do not provide for significant expenditure for further exploration and evaluation of mineral resources;

– exploration and evaluation of mineral resources did not result in discovery of any commercial mineral resources and the company decided to discontinue its exploration activities;

– available data suggests that despite continuation of the development work, the carrying value of the assets related to exploration and evaluation of mineral resources could not be fully recovered, even if the development work is successfully completed or the assets are sold.

10.8. Impairment Losses on Non-Financial Assets

As at each balance-sheet date, the Group assesses whether there is any evidence of impairment of any of its assets. If the Group finds that there is such evidence, or if the Group is required to perform annual impairment tests, the Group estimates the recoverable value of the given asset.

The recoverable value of an asset is equal to the higher of the fair value of the asset or cash generating unit, less the transaction costs, or its value in use. The recoverable value is determined for the individual assets, unless a given asset does not generate separate cash inflows largely independent from those generated by other assets or asset groups. If the carrying value of an asset is higher than its recoverable value, the value of the asset is impaired and an impairment loss is recognised up to the established recoverable value. In assessing value in use, the projected cash flows are discounted to their present value using a pre-tax discount rate which reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses related to the assets used in the continued operations are disclosed under the cost categories corresponding to the function of the asset with respect to which impairment has been identified.

As at each balance-sheet date, the Group assesses whether there is evidence that any impairment loss recognised in the previous periods with respect to a given asset is no longer necessary or should be reduced. If there is such evidence, the Group estimates the recoverable value of the given asset. The recognised impairment loss is reversed only when following the recognition of the last impairment loss there has been a change in the estimates used to determine the recoverable value of the asset. In such a case, the carrying value of the asset is increased up to its recoverable value. The increased value may not exceed the carrying value of the asset that would have been determined (net of accumulated amortisation/depreciation) if the impairment loss related to that asset had not been recognised in the previous years. Reversal of an asset impairment loss is immediately recognised as revenue in the income statement, unless the asset has been revalued, in which case the reversal of an impairment loss is treated as an increase in the revaluation capital reserve. Following reversal of an impairment loss, in the subsequent periods the amortisation/depreciation charge related to the given asset is adjusted so that over the remaining useful life of that asset its verified carrying value, less its residual value, can be regularly written off.

10.9. Investment Property

Investment property is valued at acquisition cost less accumulated depreciation and impairment losses.
Investment property, including investments in land, perpetual usufruct of land, buildings and structures, include property which the Company does not use for its own purposes but which will generate benefits in the form of value appreciation or income from rent.

10.10. Inventories

Inventories are valued at the lower of: their acquisition or production cost or their net realisable value.

Costs incurred in order to bring each inventory item to its present location and conditions are accounted for in the following manner:

- materials and goods for resale – acquisition cost calculated on weighted average basis,
- finished goods and work-in-progress – the cost of direct materials and labour and an appropriate portion of indirect production costs, established on the basis of normal capacity.

Net realisable value is the selling price estimated as at the balance sheet date net of VAT, excise taxes and fuel charge, less any rebates, discounts and other similar items, and less the estimated costs to complete and costs to sell.

10.11. Trade Receivables and Other Receivables

Trade receivables, which typically mature in 14 to 55 days, are valued and recognised at amounts initially invoiced, accounting for valuation allowances for doubtful receivables. Valuation allowances for receivables are estimated when the collection of the full amount of receivables is no longer probable. Uncollectible receivables are written off through the income statement when recognised as unrecoverable accounts.

If the effect of time value of money is significant, the value of receivables is determined by discounting the projected future cash flows to their present value using a pre-tax discount rate reflecting the current market estimates of the time value of money. If the discount method is applied, an increase in receivables over time is recognised as financial income.

10.12. Foreign Currency Transactions

Transactions denominated in foreign currencies are reported in the functional currency of the Group's companies (Polish złoty) as at the transaction date, using the following exchange rates:

1) buy or sell rate of the bank at which the transaction is effected – in the case of sale and purchase of currencies and payment of receivables and payables; or

2) mid exchange rate quoted for the given currency by the National Bank of Poland as at that date unless a different exchange rate in specified in another document binding on a given undertaking.

Monetary assets and liabilities denominated in foreign currencies as at the balance-sheet date are translated into the złoty at relevant złoty mid exchange rates quoted by the National Bank of Poland as at that date. The resulting foreign exchange gains and losses are carried as financial income/(expense) or cost of sales, except for foreign exchange gains and losses which are considered a part of external financing cost and are capitalised under non-current assets. Non-monetary assets and liabilities recognised at historic cost expressed in a foreign currency are recognised at the historic exchange rate effective as at the date of the transaction. Non-monetary assets and liabilities disclosed at fair value expressed in a foreign currency are translated as at the balance-sheet date at the exchange rate effective as at the date of determining the fair value.

Exchange rates applied for the purposes of balance-sheet valuation:

Mid exchange rate quoted by NBP as at	Dec 31 2006	Dec 31 2005
USD	2.9105	3.2613
EUR	3.8312	3.8598

The financial statements of foreign undertakings are translated into the Polish currency at the following exchange rates:
- items of the balance sheet – at the mid exchange rate quoted by the National Bank of Poland for the balance-sheet date;
- items of the income statement – at the exchange rate computed as the arithmetic mean of mid exchange rates quoted by the National Bank of Poland for the days ending each financial month. The resulting currency-translation differences are recognised directly in equity as a separate component.

The US dollar is the functional currency of foreign subsidiary undertakings. As at the balance-sheet date, assets and liabilities of these foreign undertakings are translated into the currency used by the Group for presentation purposes at the exchange rate prevailing on the balance-sheet date, while their income statements are translated at the weighted average exchange rate for a given financial year. The resulting currency-translation differences are recognised directly in equity as a separate component. At the time of disposal of a foreign undertaking, the accumulated deferred currency-translation differences recognised in equity and relating to this foreign undertaking are transferred to the income statement.

10.13. Cash and Cash Equivalents

Cash in hand and at banks, as well as and non-current deposits held to maturity are valued at face value.

Cash and cash equivalents as disclosed in the consolidated cash-flow statement comprise cash in hand and cash at banks, overdraft facilities as well as those bank deposits maturing within three months which are not classified as placements.

10.14. Accruals and Deferrals

The Group recognises prepayments if they relate to future reporting periods.

Accrued expenses are recognised at probable values of current-period liabilities.

Employees of the Group undertakings are entitled to holidays in accordance with the rules set forth in the Polish Labour Code, The Group recognises the cost of employee holidays on an accrual basis using the liability method, The amount of the provision for unused holidays is calculated on the basis of the difference between the balance of holidays actually used and the balance of holidays used established proportionately to the passage of time.

10.15. Equity

Equity is recognised in the consolidated financial statements by categories, in accordance with the rules set forth in applicable laws and in the Articles of Association.

The share capital of the LOTOS Group is the share capital of the Parent Undertaking and is recognised at its par value, in the amount specified in the Company's Articles of Association and in the relevant entry in the National Court Register.

10.16. Provisions

Provisions are created when the Group has an obligation (legal or following from commercial practice) resulting from past events, and when it is probable that the discharge of this obligation will cause an outflow of funds representing economic benefits, and the amount of the obligation may be reliably estimated. If the Group anticipates that the costs for which provisions have been made will be recovered, e.g. under an insurance agreement, the recovery of such funds is recognised as a separate item of assets, but only when such recovery is practically certain to occur. The cost related to a given provision is disclosed in the income statement, less any recoveries. If the effect of the time value of money is significant, the amount of provisions is determined by discounting projected future cash flows to their present value at gross discount rates reflecting the current market estimates of the time value of money and risks, if any, related to a given obligation. If the discount method is applied, an increase in provisions as a result of lapse of time is recognised as financial expenses.

10.17. Retirement Severance Pays and Length-of-Service Awards

In accordance with the company remuneration systems applied by the LOTOS Group companies, the Group's employees are entitled to length-of-service awards and severance pays upon retirement due to old age or disability. Length-of-service awards are paid out after a specific period of employment. Old-age and disability retirement severance pays are one-off and paid upon retirement. Amounts of severance pays and length-of-service awards depend on the length of employment and the average remuneration. The Company creates a provision for future liabilities under retirement severance pays and length-of-service awards in order to assign costs to the periods in which they are incurred. According to IAS 19, length-of-service awards are classified as other long-term employee benefits, while retirement severance pays – as defined post-employment benefit plans. The present value of the obligations as at each balance-sheet date is calculated by an independent actuary. The calculated value of the obligations is equal to the amount of discounted future payments, taking into account the employment turnover, and relate to the period ending at the given balance-sheet date. Information concerning demographics and employment turnover is sourced from historical data. Actuarial gains and losses are recognised in the income statement.

10.18. Profit Distribution for Employee Benefits and Special Accounts

According to business practice followed in Poland, company shareholders have the right to allocate a part of profit for employee benefits in the form of contributions to the Company's social benefits fund and for other special accounts. In the financial statements prepared in accordance with the IFRS such distributions are charged to operating expenses of the period which the distribution concerns.

10.19. Interest-Bearing Bank Loans, Borrowings, and Debt Securities

All bank loans, borrowings, and debt securities are initially recognised at acquisition cost equal to the fair value of funds received, less cost of obtaining the loan.

Following initial recognition, interest-bearing loans, borrowings, and debt securities are valued at amortised acquisition cost, using the effective interest rate method. Amortised acquisition cost includes cost of obtaining the loan as well as discounts or premiums obtained at settlement of the liability. Gains or losses are charged to the income statement upon removal of the liability from the balance sheet or recognition of value impairment.

10.20. Costs of External Financing

Costs of external financing are disclosed as the costs of the period in which they were incurred, except for the costs which relate directly to the acquisition, construction or production of an asset being completed, which costs are capitalised as a part of the acquisition or production cost of such an asset,

To the extent that the funds are borrowed specifically for the purpose of acquiring the asset being completed, the amount of the costs of external financing which may be capitalised as part of such asset is determined as the difference between the actual costs of external financing incurred in connection with a given loan in a given period and the proceeds from temporary investments of the borrowed funds.

To the extent that the funds are borrowed without a specific purpose and are later allocated for the acquisition of an asset being completed, the amount of the costs of external financing which may be capitalised is determined by applying the capitalisation rate to the capital expenditure on that asset.

10.21. Government Subsidies

If there is reasonable certainty that the subsidy will be received and that all related conditions will be fulfilled, government subsidies are recognised at fair value.

If a subsidy concerns a cost item, it is recognised as income in matching with the expenses it is to compensate for. If it concerns an asset, its fair value is recognised as deferred income, and then it is written off annually in equal parts through profit or loss over the estimated useful life of the asset.

10.22. Emission Credits

The Group recognises carbon dioxide emission credits in its financial statements based on the net liability method – the Group recognises only those liabilities that result from exceeding the emission credits limit granted to it, and the liability is recognised only after the Company actually exceeds the limit. Income from the sale of unused emission credits is recognised in the income statement at the time of sale.

10.23. Income Tax

Mandatory decrease of profit/(increase of loss) comprises: current income tax (CIT) and deferred income tax. The current portion of the income tax is calculated based on the net profit/(loss) (taxable income) for a given financial year. The net profit (loss) established for tax purposes differs from the net profit (loss) established for financial reporting purposes due to the exclusion of the income which is taxable and the costs which are deductible in future years and the expenses and income items which will never be subject to deduction/taxation. The tax charges are calculated based on the tax rates effective for a given financial year.

For the purposes of financial reporting, the Company creates a deferred tax liability using the balance-sheet liability method in relation to all temporary differences existing as at the balance-sheet date between the tax base of assets and liabilities and their carrying value as disclosed in the consolidated financial statements.

Deferred tax liability is recognised for all taxable temporary differences:

- except to the extent that the deferred tax liability arises from the initial recognition of goodwill or the initial recognition of an asset or liability in a transaction which is not a business combination, and, at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss), and
- in the case of taxable temporary differences associated with investments in subsidiary or associated undertakings, and interests in joint ventures, unless the investor is able to control the timing of the reversal

of the temporary differences and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets are disclosed in relation to all deductible temporary differences, unused tax assets, and unused tax losses brought forward in the amount of the probable taxable income which would enable these differences, assets and losses to be used:

- except to the extent that the deferred tax asset related to deductible temporary differences arises from the initial recognition of an asset or liability in a transaction which is not a business combination, and, at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss), and
- in the case of deductible temporary differences associated with investments in subsidiary or associated undertakings and interests in joint ventures, the related deferred tax asset is recognised in the balance sheet to the extent it is probable that in the foreseeable future the temporary differences will be reversed and taxable income will be generated which will enable the deductible temporary differences to be offset.

The carrying value of a deferred tax asset is verified as at each balance-sheet date and is subject to appropriate reduction to the extent it is no longer probable that taxable income sufficient for a partial or full realisation of this deferred tax asset would be generated.

Deferred tax assets and deferred tax liabilities are calculated using tax rates expected to be effective at the time of realisation of particular asset or release of particular provision, based on tax rates (and tax legislation) effective as at the balance-sheet date or tax rates (and tax legislation) certain to be effective as at the balance-sheet date in the future.

Income tax related to items posted directly to equity is disclosed under equity and not in the income statement.

Deferred tax assets and deferred tax liability are recognised in the balance sheet in the amount obtained after they are offset for particular undertakings consolidated within the Group.

10.24. Financial Instruments

At the time of their initial recognition, financial instruments are valued at acquisition cost (price), equal to the fair value of the payment made for them. The transaction costs are included in the initial value of the financial instruments.

Following the initial recognition, financial instruments are classified under one of the following four categories and are valued as follows:

- Financial instruments which are recognised at fair value through profit or loss.
- Financial instruments held to maturity which are recognised at amortised cost using the effective interest rate.
- Loans and accounts receivable which are recognised at amortised cost using the effective interest rate; the related gains and losses are disclosed in the income statement. Accounts receivable which mature in the short term and do not have a specified interest rate are recognised at amounts due.
- Financial instruments available for sale which are recognised at fair value; the revaluation gains/losses are charged to the revaluation capital reserve until the investment is sold or its value is reduced. Then, the cumulative revaluation gain/loss is charged to the income statement.

The fair value of financial instruments for which a ready market exists is determined in relation to the prices quoted on that market as at the relevant balance-sheet date. If there is no quoted market price, the fair value is estimated using appropriate valuation techniques.

Financial liabilities other than under financial instruments at fair value through profit or loss are recognised at amortised cost using the effective interest rate.

Financial instruments are derecognised from the balance sheet when the Group loses control over contractual rights comprising particular financial instruments; this is usually the case when a financial instrument is sold or when all the cash flows related to a given instrument are transferred to a third party.

10.25. Derivative Financial Instruments

Derivatives used by the Group to hedge against interest rate risk and currency risk include in particular FX forwards and interest rate swaps. Derivative financial instruments of this type are measured at fair value. Derivative instruments are recognised as assets if their value is positive and as liabilities if their value is negative. Gains or losses resulting from changes in the fair value of a derivative which does not comply with hedge accounting are charged directly to the net profit or loss for the financial year. Fair value of FX forwards is established by reference to the forward rates of contracts with similar maturity prevailing at a given time. Fair value of interest rate swaps is established by reference to the market value of similar instruments.

10.26. Impairment of Financial Assets

As at each balance-sheet date the Company determines whether there is objective evidence of impairment of a financial asset or a group of financial assets.

Assets Carried at Amortised Cost

If there is objective evidence that the value of loans and receivables measured at amortised cost has been impaired, the impairment loss is recognised in the amount equal to the difference between the carrying value of a financial asset and the present value of estimated future cash flows (excluding future losses relating to irrecoverable receivables, which have not yet been incurred), discounted using the initial effective interest rate (i.e. the interest rate used at the time of initial recognition). The carrying value of an asset is reduced directly or by creating relevant provisions. The amount of loss is recognised in the income statement.
First the Company determines whether there exists objective evidence of impairment with respect to each financial asset that is deemed material, and with respect to financial assets that are not deemed material individually. If the analysis shows that there exists no objective evidence of impairment of an individually tested asset, regardless of whether it is material or not, the Company includes the asset into the group of financial assets with similar credit risk profile and tests it for impairment together with the other assets from this group. Assets which are tested for impairment individually, and with respect to which an impairment loss has been recognised or a previously recognised loss is deemed to remain unchanged, are not taken into account when a group of assets are jointly tested for impairment.
If an impairment loss decreases in the next period, and the decrease may be objectively associated with an event that occurred subsequent to the impairment loss recognition, the recognised impairment loss is reversed. The subsequent reversal of an impairment loss is recognised in the income statement to the extent that the carrying value of the asset does not exceed its amortised cost as at the reversal date.

Financial Assets Carried at Cost

If there exists objective evidence of impairment of a non-traded equity instrument which is not carried at fair value since such value cannot be reliably determined, or of a related derivative instrument which must be settled by delivery of such non-traded equity instrument, the amount of impairment loss is established as the difference between the carrying value of the financial asset and the present value of estimated future cash flows discounted with the market rate applicable to similar financial assets prevailing at a given time.

Financial Assets Available for Sale

If there exists objective evidence of impairment of a financial asset available for sale, the amount of the difference between the acquisition cost of that asset (less any principal payments and depreciation/amortisation charges) and its current fair value, reduced by any impairment losses previously recognised in the income statement, is derecognised from equity and charged to the income statement. Reversal of an impairment loss concerning equity instruments qualified as available for sale may not be recognised in the income statement. If the fair value of a debt instrument available for sale increases in the next period, and the increase may be objectively associated with an event that occurred subsequent to the impairment loss recognition in the income statement, the amount of the reversed impairment loss is recognised in the income statement.

10.27. Recognition of Revenue

Revenue is recognised in the amount of probable economic benefits to be derived by the Group which may be reliably estimated.

10.28. Sales of Goods for Resale and Products

Sales revenue is disclosed at the fair value of payments received or due, and it represents the accounts receivable for the products, goods for resale and services provided in the ordinary course of business, less discounts, VAT and other sales-related taxes (excise tax, fuel charge). The sales of products and goods for resale are recognised at the moment of delivery, when material risk and benefits resulting from the ownership of the products and goods have been transferred to the purchaser.

10.29. Interest

Interest income is recognised as the interest accrues (using the effective interest rate), unless the receipt of the interest is doubtful.

10.30. Dividends

Dividend is recognised as financial income as of the date on which the appropriate governing body of the Company adopts a resolution concerning distribution of profit, unless the resolution specifies another dividend record date.

10.31. Management Board's Estimates

The preparation of financial statements in accordance with the International Financial Reporting Standards requires a number of judgments and estimates which affect the value of items disclosed in the financial statements and in the notes thereto. Although the judgments and estimates are based on the Management Board's best knowledge of the current and future events and actions, the actual results might differ from the estimates. The areas in which the Management Board prepared estimates include provisions, property, plant and equipment, as well as intangible assets, goodwill, merger transactions and financial assets. The material assumptions used in the estimates are described in the relevant notes.

Valuation of Provisions

Provisions for employee benefits were estimated with actuarial methods.

Depreciation/Amortisation Charges

Depreciation/amortisation charges are determined based on the expected useful lives of property, plant and equipment and intangible assets. The Group reviews the useful lives of its assets annually, on the basis of current estimates.

Fair Value of Financial Instruments

The fair value of financial instruments for which no active market exists is determined by means of appropriate valuation methods. In selecting appropriate methods and assumptions, the Group relies on professional judgment.

Deferred Tax Asset

The Group recognises a deferred tax asset if it is assumed that taxable profit will be generated in the future against which the asset can be used. If the taxable profit deteriorates in the future, this assumption may prove invalid.

10.32. Net Earnings per Share

Earnings per share for each period are calculated by dividing the net profit for a given period by the weighted average number of shares in this reporting period. The Group does not disclose the diluted earnings/loss per share, since there are no dilutive instruments outstanding.

10.33. Contingent Liabilities and Receivables

A contingent liability is understood as a duty to discharge an obligation which is conditional upon the occurrence of certain circumstances. Contingent liabilities are not recognised in the balance sheet, however information on contingent liabilities is disclosed, unless the likelihood of the outflow of funds embodying economic benefits is negligible. Contingent receivables are not recognised in the balance sheet, however information on contingent receivables is disclosed if the inflow of funds embodying economic benefits is likely to occur.

11. Property, Plant and Equipment and Prepayments for Tangible Assets under Construction

PLN '000	Dec 31 2006	Dec 31 2005
Land	375,817	362,075
Buildings and structures	1,677,234	1,520,335
Plant and equipment	746,967	764,594
Vehicles and other tangible assets	357,624	375,968
Tangible assets under construction	342,643	271,071
Prepayments for tangible assets under construction	148,018	17,737
Total	**3,648,303**	**3,311,780**

Changes to Property, Plant and Equipment and Prepayments for Tangible Assets under Construction

PLN '000	Land	Buildings and structures, including:	mineral resources exploration and evaluation assets	Plant and equipment	Vehicles and other means of transport	Tangible assets under construction, including:	mineral resources exploration and evaluation assets	Prepayments for tangible assets under construction	Total
Gross book value as at Jan 1 2005	**239,713**	**1,150,536**	**-**	**801,560**	**143,351**	**136,474**	**-**	**8,173**	**2,479,807**
Increase, including:	128,528	531,128	72,159	276,058	389,791	139,028	75,693	23,516	1,488,049
- purchase	15	287	-	2,539	36,821	744,862	23,080	20,505	805,029
- transfer from investments	103,045	304,954	-	177,593	49,547	(688,299)	(65)	-	(53,160)
- inclusion of new undertakings in consolidation	25,468	225,101	72,159	90,832	294,527	82,465	52,678	388	718,781
- other	-	786	-	5,094	8,896	-	-	2,623	17,399
Decrease, including:	(280)	(6,542)	-	(17,988)	(20,130)	(4,252)	-	(13,952)	(63,144)
- sale	(280)	(548)	-	(425)	(5,924)	(20)	-	-	(7,197)
- liquidation	-	(798)	-	(11,004)	(2,106)	-	-	-	(13,908)
- donations, transfer for no consideration	-	(93)	-	-	-	-	-	-	(93)
- other	-	(5,103)	-	(6,559)	(12,100)	(4,232)	-	(13,952)	(41,946)
	-------	-------	-------	-------	-------	-------	-------	-------	-------
Gross book value as at Dec 31 2005	**367,961**	**1,675,122**	**72,159**	**1,059,630**	**513,012**	**271,250**	**75,693**	**17,737**	**3,904,712**
Gross book value as at Jan 1 2006	**367,961**	**1,675,122**	**72,159**	**1,059,630**	**513,012**	**271,250**	**75,693**	**17,737**	**3,904,712**
Increase, including:	23,809	266,777	55,857	126,897	57,557	86,759	(17,453)	163,874	725,673
- purchase	-	93	-	410	4,759	548,185	38,404	145,723	699,170
- transfer from investments	23,809	265,767	55,857	122,826	33,285	(461,889)	(55,857)	-	(16,202)
- other	-	917	-	3,661	19,513	463	-	18,151	42,705
Decrease, including:	(9,555)	(8,141)	-	(10,705)	(27,155)	(4,674)	-	(33,593)	(93,823)
- sale	(5,707)	(2,099)	-	(2,762)	(5,323)	(572)	-	-	(16,463)
- liquidation	-	(3,639)	-	(3,794)	(4,963)	(685)	-	-	(13,081)

PLN '000	Land	Buildings and structures, including:	mineral resources exploration and evaluation assets	Plant and equipment	Vehicles and other means of transport	Tangible assets under construction, including:	mineral resources exploration and evaluation assets	Prepayments for tangible assets under construction	Total
- donations, transfer for no consideration	-	(158)	-	-	(12)	-	-	-	(170)
- other	(3,848)	(2,245)	-	(4,149)	(16,857)	(3,417)	-	(33,593)	(64,109)
Gross book value as at Dec 31 2006	**382,215**	**1,933,758**	**128,016**	**1,175,822**	**543,414**	**353,335**	**58,240**	**148,018**	**4,536,562**
Accumulated depreciation as at Jan 1 2005	**4,278**	**79,383**	**-**	**166,784**	**89,732**	**-**	**-**	**-**	**340,177**
Increase, including:	1,609	75,850	6,494	138,191	52,047	-	-	-	267,697
- depreciation	1,609	74,835	6,494	132,477	45,981	-	-	-	254,902
- other	-	1,015	-	5,714	6,066	-	-	-	12,795
Decrease	(1)	(685)	-	(10,139)	(4,853)	-	-	-	(15,678)
Accumulated depreciation as at Dec 31 2005	**5,886**	**154,548**	**6,494**	**294,836**	**136,926**	**-**	**-**	**-**	**592,196**
Accumulated depreciation as at Jan 1 2006	**5,886**	**154,548**	**6,494**	**294,836**	**136,926**	**-**	**-**	**-**	**592,196**
Increase, including:	1,939	97,181	9,665	135,324	59,129	-	-	-	293,573
- depreciation	1,939	97,147	9,665	134,242	52,449	-	-	-	285,777
- other	-	34	-	1,082	6,680	-	-	-	7,796
Decrease	(1,756)	(1,837)	-	(5,239)	(12,530)	-	-	-	(21,362)
Accumulated depreciation as at Dec 31 2006	**6,069**	**249,892**	**16,159**	**424,921**	**183,525**	**-**	**-**	**-**	**864,407**
Impairment losses as at Jan 1 2005	**-**	**-**	**-**	**-**	**156**		**-**	**-**	**156**

PLN '000	**Land**	**Buildings and structures, including:**	mineral resources exploration and evaluation assets	**Plant and equipment**	**Vehicles and other means of transport**	**Tangible assets under construction, including:**	mineral resources exploration and evaluation assets	**Prepayments for tangible assets under construction**	**Total**
Increase	-	239	-	200	5	189	-	-	633
Decrease	-	-	-	-	(43)	(10)	-	-	(53)
Impairment losses as at Dec 31 2005	**-**	**239**	**-**	**200**	**118**	**179**	**-**	**-**	**736**
Impairment losses as at Jan 1 2006	**-**	**239**	**-**	**200**	**118**	**17**	**-**	**-**	**736**
Increase	329	6,959	-	4,244	2,150	10,518	8,147	-	24,200
Decrease	-	(566)	-	(510)	(3)	(5)	-	-	(1,084)
Impairment losses as at Dec 31 2006	**329**	**6,632**	**-**	**3,934**	**2,265**	**10,692**	**8,147**	**-**	**23,852**
Net book value as at Jan 1 2005	**235,435**	**1,071,153**	**-**	**634,776**	**53,463**	**136,474**	**-**	**8,173**	**2,139,474**
Net book value as at Dec 31 2005	**362,075**	**1,520,335**	**65,665**	**764,594**	**375,968**	**271,071**	**75,693**	**17,737**	**3,311,780**
Net book value as at Dec 31 2006	**375,817**	**1,677,234**	**111,857**	**746,967**	**357,624**	**342,643**	**50,093**	**148,018**	**3,648,303**

As at December 31st 2006, the net value of the items of property, plant and equipment serving as collateral for the Group's liabilities was PLN 521,638 thousand.

The cost of servicing the liabilities incurred to finance tangible assets under construction in the year ended December 31st 2006 and in the year ended December 31st 2005 amounted to PLN 1,231 thousand and PLN 3,194 thousand, respectively.

As at December 31st 2006 and December 31st 2005, the net value of an asset related to the liquidation of a mining plant amounted to PLN 68,096 thousand and PLN 59,879 thousand, respectively.

The cost of amortisation of mineral resources exploration and evaluation assets in the years ended December 31st 2006 and December 31st 2005 amounted to PLN 10,286 thousand and PLN 7,094 thousand, respectively.

In the period ended December 31st 2006, the costs of impairment losses on mineral resources exploration and evaluation assets amounted to PLN 8,147 thousand.

Prospects for Development of Gas Reserves from the B-4 and B-6 Areas

The item "Tangible assets under construction" includes expenditure of PLN 48m incurred by Petrobaltic S.A. in connection with exploration of gas reserves from the B-4 and B-6 areas. Petrobaltic S.A. commissioned an analysis of the economic viability of development of these reserves. According to the findings of the analysis, significant capital expenditure is required to obtain profitable commercial production of hydrocarbons. Despite the envisaged excess of revenue from sale of products to be obtained by exploitation of the reserves, over the cost of their development and production, no expenditure on this project is expected in the medium term. The Management Board of Petrobaltic S.A. maintains that, regardless of the necessity to make significant investments, in view of the strategic nature of the reserves their development is possible if the investment plans of Petrobaltic S.A. and Grupa LOTOS S.A. are synchronised.

Comprehensive Technical Upgrade Programme

With respect to the execution of the Comprehensive Technical Upgrade Programme (PKRT, the Project), which is of key importance for the Company' s development and future growth of the shareholder value, the Company's efforts in the first half of 2006 focused on further technological development, negotiating agreements concerning various areas of the Project and contacts with selected financial institutions. Additionally, the Company continued the work on expanding the scope of the Project, on its technological development, on updating the Project's financial assumptions, and on selecting the contractors for the implementation of investment tasks under the Project.

The end of January and beginning of February 2006 saw the completion of work by the licensors of three main technologies for the Project – Shell Global Solutions and KBR – related to developing the front-end engineering designs of the Project's main units. The ROSE unit front-end engineering design was delivered to Grupa LOTOS S.A. by KBR in January, and the front-end engineering designs for MHC and IGCC units were delivered by SGSI in February 2007.

On January 31st 2006, the terms of cooperation were agreed upon and the parties signed agreements on the preparation of the front-end engineering design for the PKRT Project and the provision of engineering services relating to the development of the Project (FEED-PB Agreement) with the selected bidders, i.e. Fluor and the consortium of UHDE/Technip. The total value of these agreements amounted to PLN 101,736 thousand and increased the value of assets under construction. The Company is now analysing the two submitted designs in order to develop a single comprehensive design best suited to its needs. At the current stage of analysis, the Company is unable to determine the extent to which the designs can be practically used in the future in the preparation of the final version of the front-end engineering design for PKRT.

On April 11th 2006, an agreement was signed with STASCO, for the supply of additional feedstock for the Project units.

Given the rapid changes of conditions prevailing on global oil markets, the rise in the prices of crude oil and petroleum products, as well as higher costs of materials, investment equipment, labour and services in the oil industry, Grupa LOTOS S.A. mandated Purvin&Gertz, an independent market consultant, to update the assumptions adopted in the Project's financial model. Concurrently, the estimate of capital expenditure on the Project execution was updated.

Relying on the modelling results, based on updated assumptions, it was decided to change the Project's scope and structure. In addition to the main PKRT units (IGCC, MHC, ROSE), a new crude distillation unit will be built (CDU), thanks to which it will not be necessary to import additional feedstock for PKRT units. Moreover, in order to enable the Company to produce more atmospheric and vacuum distillates while meeting quality requirements for diesel oils, to be effective from 2009 (10ppm S), the PKRT project will also encompass the construction of a diesel oil hydro-desulphurisation unit (HDS) and construction of storage tanks required in connection with expanded production scale. The HDS production unit will be built based on the licence from Chevron Lummus Global.

On June 27th 2006, the Supervisory Board of Grupa LOTOS S.A. approved the sending of letters of intent by Grupa LOTOS S.A., which have the financial effect of concluding agreements, concerning the delivery of four reactors for the MHC unit forming part of the PKRT Project. The assumption of financial obligations related to the delivery of the MHC reactors is one of the milestones in the PKRT execution schedule. To the extent described above, the work related to the construction of the reactors was executed in accordance with the schedule. As at December 31st 2006, the Company made a prepayment for the delivery in question amounting to PLN 75,290 thousand.

Upon completion of a two-stage tender for the construction of the HDS unit for diesel oil, which resulted in selection of the contractor and commencement of contract negotiations, on November 11th 2006 the Company's Management Board signed an EPC contract for the construction of the unit with ABB Lummus Global. Under the terms of the contract, the scope of the work comprises engineering, procurement and construction of the HDS unit. The unit will be constructed under a licence from Chevron Lummus Global. It will enable the Group to meet the quality requirements which are to apply to diesel oils as of 2009 (sulphur content of 10 ppm).

We continued our efforts to commence the construction of a new CDU unit as part of the Front End Engineering Design Contract of August 2006 concluded with Uhde Edeleanu. Given the significant progress of the work, in December 2006 invitations to tender for the construction of the CDU unit were sent to six leading engineering companies. Based on the bids submitted in February 2007, Grupa LOTOS S.A. held negotiations, a result of which the selected contractor will commence work in April 2007. Following the construction of the new CDU unit, the annual oil throughput in the Gdańsk refinery of Grupa LOTOS S.A. will increase to 10.5m tonnes in 2010 and the Company will no longer have to depend on imports of additional feedstock for the PKRT units.

After the signing of relevant agreements with Fluor and the UHDE/Technip consortium in the first quarter of 2006, the subsequent quarters of 2006 were the time of intensive work on the development of the Front End Engineering Design for the PKRT Project, and on the preparation of UHDE's and Technip's bids for the Project implementation (excluding the scope of work covered by the contracts for the construction of HDS and CDU units). The bids for the execution of the Project were submitted in mid December 2006. Grupa LOTOS S.A. is currently conducting negotiations with the bidders to optimise the scope and terms and conditions of the submitted bids. The negotiations are scheduled to be completed in April 2007.

In 2006, all the preparatory work on the construction site located on the Gdańsk refinery grounds was practically completed. The work included soil survey, soil removal, ground levelling, draining, providing electricity to the site, building temporary roads, etc. In 2007, work has commenced to prepare the construction backup facilities.

12. Other Non-Current Assets

PLN '000	Dec 31 2006	Dec 31 2005
Other prepayments and accrued income	13,912	8,548
Non-current receivables	16,199	19,468
Total	**30,111**	**28,016**

13. Prepayments and Accrued Income

PLN '000	Dec 31 2006	Dec 31 2005
Property insurance	4,213	3,397
IT services	68	211
Overhauls	17,896	13,391
Other	5,297	2,837
Total	**27,474**	**19,836**
Current portion	13,562	11,288
Non-current portion	13,912	8,548

14. Investment Property

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Opening balance	5,888	231
Increase:	-	15,957
Change in the Group's composition	-	15,957
- other	-	-
Decrease:	(1,039)	(10,300)
- sale	(214)	(10,300)
- other	(825)	-
Closing balance	**4,849**	**5,888**

15. Intangible Assets

PLN '000	Dec 31 2006	Dec 31 2005
Development expense	392	504
Software	7,626	5,426
Patents, trademarks and licences	44,984	43,824
Other	2,856	1,332
Total	**55,858**	**51,086**

Changes in Intangible Assets

PLN '000	Development expense	Software	Patents, trademarks and licences, including:	mineral resources exploration and evaluation assets	Other	mineral resources exploration and evaluation assets	Total
Gross book value as at Jan 1 2005	**100**	**5,352**	**46,759**	**-**	**881**	**-**	**53,092**
Increase, including:	533	4,710	8,010	956	1,591	794	14,844
- purchase	-	386	299	-	647	-	1,332
- transfer from investments	-	3,611	6,707	-	123	-	10,441
- inclusion of new undertakings in consolidation	227	713	967	956	821	794	2,728
- other	306	-	37	-	-	-	343
Decrease, including:	-	(736)	(91)	-	(621)	-	(1,448)
- sale	-	(71)	-	-	-	-	(71)
- liquidation		(415)	-	-	-	-	(415)
- other	-	(250)	(91)	-	(621)	-	(962)
Gross book value as at Dec 31 2005	**633**	**9,326**	**54,678**	**956**	**1,851**	**794**	**66,488**
Gross book value as at Jan 1 2006	**633**	**9,326**	**54,678**	**956**	**1,851**	**794**	**66,488**
Increase, including:	-	4,736	9,601	176	2,299	-	16,636
- purchase	-	35	62	176	-	-	97
- transfer from investments	-	4,485	9,465	-	2,252	826	16,202
- contribution in kind	-	-	-	-	-	-	-
- other	-	216	74	-	47	-	337
Decrease, including:	(105)	(169)	(214)	-	(2)	-	(490)
- sale	-	(11)	-	-	-	-	(11)
- liquidation	(105)	(40)	(6)	-	-	-	(151)
- other	-	(118)	(208)	-	(2)	-	(328)
Gross book value as at Dec 31 2006	**528**	**13,893**	**64,065**	**1,132**	**4,148**	**1,620**	**82,634**

PLN '000	Development expense	Software	Patents, trademarks and licences, including:	mineral resources exploration and evaluation assets	Other	mineral resources exploration and evaluation assets	Total
Accumulated amortisation as at Jan 1 2005	**100**	**2,586**	**4,718**	**-**	**62**	**-**	**7,466**
Increase, including:	56	1,738	6,140	300	457	249	8,391
- amortisation	56	1,738	6,137	300	457	249	8,388
- other	-	-	3	-	-	-	3
Decrease	-	(481)	(4)	-	-	-	(485)
Accumulated amortisation as at Dec 31 2005	**156**	**3,843**	**10,854**	**300**	**519**	**249**	**15,372**
Accumulated amortisation as at Jan 1 2006	**156**	**3,843**	**10,854**	**-**	**519**	**249**	**15,372**
Increase, including:	110	2,696	8,233	331	773	290	11,812
- amortisation	110	2,696	8,000	331	773	290	11,579
- other	-	-	233	-	-	-	233
Decrease	(103)	(324)	(6)	-	-	-	(433)
Accumulated amortisation as at Dec 31 2006	**163**	**6,215**	**19,081**	**631**	**1,292**	**539**	**26,751**
Impairment losses as at Jan 1 2005	**-**	**49**	**-**	**-**	**-**	**-**	**49**
Increase	-	8	-	-	-	-	8
Decrease	(27)	-	-	-	-	-	(27)
Impairment losses as at Dec 31 2005	**(27)**	**57**	**-**	**-**	-	**-**	**30**
Impairment losses as at Jan 1 2006	**(27)**	**57**	**-**	**-**	**-**	**-**	**30**
Increase	-	-	-	-	-	-	-

PLN '000	Development expense	Software	Patents, trademarks and licences, including:	mineral resources exploration and evaluation assets	Other	mineral resources exploration and evaluation assets	Total
Decrease	-	(5)	-	-	-	-	(5)
Impairment losses as at Dec 31 2006	**(27)**	**52**	**-**	**-**	**-**	**-**	**25**
Net book value as at Jan 1 2005	**-**	**2,717**	**42,041**	**-**	**819**	**-**	**45,577**
Net book value as at Dec 31 2005	**504**	**5,426**	**43,824**	**656**	**1,332**	**545**	**51,086**
Net book value as at Dec 31 2006	**392**	**7,626**	**44,984**	**501**	**2,856**	**1,081**	**55,858**

16. Business Combinations

Consolidation Goodwill

PLN '000	Dec 31 2006	Dec 31 2005
Carrying value of consolidation goodwill:		
LOTOS Partner Sp. z o.o.	1,862	1,862
LOTOS Mazowsze S.A.	10,009	10,009
Total	**11,871**	**11,871**
Carrying value of acquisition goodwill		
- purchase of ESSO service stations network	44,256	42,717
- purchase of Slovnaft Polska S.A. service stations network	10,931	-
Total	**55,187**	**42,717**
Total goodwill	**67,058**	**54,588**

As at December 31st 2006, the Group recognised goodwill arising from the acquisition of the organised parts of business of ExxonMobil Poland and Slovnaft Polska in the net amount PLN 44,256 thousand and PLN 10,931 thousand, respectively. In accordance with IAS 36, the Group tested the goodwill relating to ExxonMobil Poland and Slovnaft Polska for impairment. In order to determine the value in use, a discounted cash-flow analysis (DCF) was conducted in relation to 39 service stations of the acquired ESSO Service Station Network and 12 service stations of the Slovnaft network, which were recognised as separate cash-generating units, with WACC assumed at 7.9%. The analysis was based on the future cash-flow forecast (EBITDA without financial costs) prepared by Pekao Access in March 2006 in connection with the financing of the transactions with a syndicated loan advanced by Pekao S.A. and PKO BP S.A. The terminal value for the discounted cash flows was calculated on the basis of the growing perpetuity formula, for which the constant growth rate of 2.8% was assumed after the period covered by the forecast. The value in use was determined by way of a goodwill valuation test carried out by the Company and was as follows:

- PLN 284,509 thousand – ESSO service stations
- PLN 84,531 thousand – Slovnaft service stations.

The carrying value of the assets purchased from ExxonMobil Poland and Slovnaft Polska amounts to:

- PLN 283,621 thousand – ESSO service stations
- PLN 57,412 thousand – Slovnaft service stations.

In view of an excess of the value in use over the book value of the assets, as shown by the test, the Group did not recognise any goodwill impairment loss.

No goodwill valuation allowances were made by the Group in 2005.

Acquisition of ESSO Service Station Network

On August 24th 2005, LOTOS Paliwa Sp. z o.o. entered into a preliminary conditional agreement on purchase of ESSO service station network in Poland from ExxonMobil Poland Sp. z o.o. The transaction concerns an organised part of ExxonMobil Poland's business, comprising in particular:

- 39 service stations along with real estate owned, held in perpetual usufruct or under long-term leases,
- 14 undeveloped lots for new service stations, owned or held in perpetual usufruct (including three lots covered by call options).

The preliminary agreement provided for a transfer of 24 employees of ExxonMobil Poland Sp. z o.o., who had been engaged in the expansion of the ESSO network in Poland.
As part of the transaction, Grupa LOTOS S.A. and ExxonMobil are to conduct domestic and international cooperation in serving ESSO customers at LOTOS stations in Poland and LOTOS customers holding fleet cards at service stations accepting ESSO cards outside Poland (in a number of European countries). It also provides for a continuation of the loyalty scheme for ESSO retail customers. Furthermore, LOTOS Paliwa Sp. z o.o. agreed to purchase (for additional consideration) assets connected with day-to-day operations of the acquired stations (stocks of fuels, receivables from agents and loyalty card holders, etc.).
On December 14th 2005, LOTOS Paliwa Sp. z o.o. and ExxonMobil Poland Sp. z o.o. completed the transaction by concluding the final agreement. The net price for the organised part of business was PLN 283,318 thousand, of which PLN 250,728 thousand accounts for the 39 service stations. LOTOS Paliwa Sp. z o.o. financed the transaction with funds from the additional contributions to equity made by Grupa LOTOS S.A. and from the loan granted under the agreement concluded in 2004 between LOTOS Paliwa Sp. z o.o. and a bank syndicate (Bank Pekao S.A. and PKO BP S.A.).

As at December 31st 2005, the expenditure incurred by LOTOS Paliwa Sp. z o.o. to purchase the organised part of business amounted to PLN 248,048 thousand, of which PLN 215,458 thousand was spent to acquire 33 stations. Acquisition of the ESSO stations resulted in the recognition of goodwill in the amount of PLN 42,717 thousand, representing the difference between the acquisition cost and the fair value of the acquired assets.

The goodwill disclosed in the consolidated financial statements for 2005 increased by PLN 1,539 thousand as a result of the final transaction settlement and acquisition of other service stations as part of the transaction. As at December 31st 2006, LOTOS Paliwa Sp. z o.o.'s expenditure on acquisition of the organised part of business amounted to PLN 282,843 thousand, including PLN 250,253 thousand for 39 stations.
Following the acquisition of ESSO service stations network, the goodwill in the amount of PLN 44,256 thousand was recognised, representing the difference between the acquisition cost and the fair value of the acquired assets. The difference relates to one cash-generating unit. No cash was acquired in the transaction. The recoverable value of cash-generating units was determined on the basis of their fair value.
The acquisition cost (cost of merger of the organised part of Exxon Mobil Poland's business) included additional expenses incurred by LOTOS Paliwa Sp. z o.o. in relation to tax and financial advisory services, cost of external financing, leasehold payments and building permits.

As at December 31st 2006, the final amount of goodwill following from the transaction is as follows:

PLN '000	**Dec 31 2006**
Merger cost (acquisition cost)	295,352
Non-current assets	251,096
Goodwill	44,256

Acquisition of Slovnaft Polska S.A.'s Service Station Network

In connection with Current Report No. 76/2005 of September 28th 2005, concerning the conclusion by LOTOS Paliwa Sp. z o.o. of a preliminary conditional agreement on acquisition of the network of Slovnaft service stations in Poland from Slovnaft Polska S.A., having fulfilled all conditions precedent of the agreement, on March 9th 2006 LOTOS Paliwa Sp. z o.o. closed the transaction with Slovnaft Polska S.A. by concluding the final agreement.
The transaction consisted in the acquisition of an organised part of Slovnaft Polska S.A.'s business, comprising:

- 12 Slovnaft service stations situated in southern Poland, in an area of strategic importance to the development of the LOTOS network,
- 2 undeveloped lots for new service stations (the sale agreement for one of the lots is a conditional agreement).

The net price of the transaction was EUR 15,000 thousand. LOTOS Paliwa Sp. z o.o. financed the transaction with funds from additional contributions to equity made by Grupa LOTOS S.A., representing one of the objectives of the public offering, and with a loan granted under the agreement concluded in 2004 between LOTOS Paliwa Sp. z o.o. and a bank syndicate (Bank Pekao S.A. and PKO BP S.A.).

As at December 31st 2006, the expenditure incurred by LOTOS Paliwa Sp. z o.o. on the purchase of the organised part of business amounted to PLN 57,434 thousand (12 service stations).

Upon acquisition of the Slovnaft service station network, goodwill of PLN 10,931 thousand was recognised, representing the difference between the acquisition price and the fair value of the acquired net assets. The difference concerns one cash generating unit. No cash was acquired in the transaction. The recoverable value of cash generating units was determined based on their fair value.

(PLN '000)	**Dec 31 2006**
Merger cost (acquisition cost)	59,356
Non-current assets	48,425
Goodwill	10,931

Acquisition of Shares in Rafineria Czechowice S.A., Rafineria Jasło S.A., Rafineria Nafty Glimar S.A. and Petrobaltic S.A.

February 3rd 2005 saw finalisation of the agreement of January 13th 2005 whereby Grupa LOTOS S.A. purchased from Nafta Polska S.A. shares in the following companies:

- 80.04% of shares in Rafineria Czechowice S.A.,
- 80.01% of shares in Rafineria Jasło S.A.,
- 91.54% of shares in Rafineria Nafty Glimar S.A. in bankruptcy,
- 69.00 % of shares in Petrobaltic S.A.

The aggregate value of the shares purchased under the agreement amounted to PLN 257,276 thousand and was fully paid by Grupa LOTOS S.A. with cash.

Since:

- as at the transaction date, both Grupa LOTOS S.A. and the undertakings whose shares were acquired were controlled by Nafta Polska S.A.,
- IFRS 3: *Business Combinations* does not specify consolidation methods for transactions between jointly controlled entities,

the Parent Undertaking had the right to choose the method of accounting for the transaction from among the methods under other accounting standards or under IFRS 3: *Business Combinations*. The Company chose the purchase method described in detail in IFRS 3 as the binding consolidation method.

Pursuant to IFRS 3, as at the date on which an entity is taken over, i.e. as at the acquisition date, the acquirer is obliged to allocate the cost of the business combination by recognising the acquiree's identifiable assets, liabilities and contingent liabilities at their fair values at that date. Any difference between the acquisition cost and the acquirer's share in the value of the assets, liabilities and contingent liabilities so measured constitutes the (negative) goodwill.
The allocation is made exclusively with respect to those assets and liabilities that exist on the acquisition date.
In addition, IFRS 3 prohibits, in relation to the acquired net assets, the creation of provisions for operating losses of future periods as they are an item arising after the acquisition.

As at the date of these consolidated financial statements, the Company, in accordance with the above policies, performed a separate valuation of goodwill for each acquired company and recognised the difference between the acquisition cost and its hare in the net fair value of the identifiable assets, liabilities and contingent liabilities.

Since control over the assets of Rafineria Nafty Glimar S.A. ("Glimar Refinery") has been assumed by a bankruptcy administrator, the company is not consolidated by Grupa LOTOS S.A. As at December 31st 2005, the carrying value of the Glimar Refinery shares is PLN 0.

The purchase prices and the fair values of each of the companies' key items of net assets as at the acquisition date (February 3rd 2005) were as follows:

(PLN '000)	Rafineria Jasło	Rafineria Czechowice	Petrobaltic
Merger cost (purchase price)	**0.001**	**13,918**	**245,931**
Share in the share capital of the acquired undertakings	80.01%	80.04%	69,00%
Current assets, including:	102,768	222,533	141,817
Cash and cash equivalents	3,576	23,950	114,643
Non-current assets	121,728	92,293	631,814
Total assets	**224,496**	**314,826**	**773,631**
Provisions and other	11,646	67,388	159,175
Non-current liabilities	15,051	-	36,977
Current liabilities and accruals and deferred income	108,499	129,761	54,528
Total liabilities	**135,196**	**197,149**	**250,680**
Net assets	**89,300**	**117,677**	**522,951**
Company's share in net assets	**71,449**	**94,189**	**360,836**
Excess of company's share in net assets over the acquisition cost	**71,449**	**80,271**	**114,905**
Total negative goodwill charged to consolidated income statement*		**266,625**	

* Negative goodwill does not represent cash flows.

The prices of shares in companies acquired in the transaction were determined by the parties to the sale agreement of January 13th 2005 based on reports by independent consultancy companies acting individually at the request of Nafta Polska S.A. as the seller and Grupa LOTOS S.A. as the buyer.

The companies were valued in accordance with generally accepted market practice, primarily with the use of an income-based method, i.e. the discounted cash flow method (DCF). This method involves calculating the total value of projected cash flows, taking into account changes in the time value of money, based on a company's business plan containing complete projections of its financial performance. This approach presents the value of the whole company as an operating business organisation for a potential investor intending to conduct the company's business in line with the approved business plan.

The DCF valuation of the Southern Refineries was based on business plans and financial projections submitted by the Management Boards of the companies, and the values arrived at in this valuation were lower than those finally agreed upon in the agreement of January 13th 2005. The objective of the acquisition of the Southern Refineries and Petrobaltic S.A. by Grupa LOTOS S.A. was to implement the assumptions of the Strategy for the Oil Industry in Poland, including general restructuring of the Southern Refineries which would enable them to continue at least part of their operations in the changing legal environment (e.g. introduction of stricter requirements with respect to product standards and the environmental protection, abolition of excise tax credit) and market environment.

When acquiring the shares, Grupa LOTOS S.A. intended to carry out the restructuring and ensure continued operations of the Southern Refineries and Petrobaltic S.A. to the extent permitted by legal and market conditions. This means that the use of the DCF valuation method was in accordance with the market standards, and the economic value of shares in the acquired companies was not materially different from the amounts agreed upon in the agreement.

The excess of the value of Grupa LOTOS S.A.'s share in the acquired net assets of the consolidated companies over their acquisition cost (disclosed in the consolidated income statements at PLN 267m) results from the application of IFRS 3 and measurement of the identifiable individual assets, liabilities and contingent liabilities of the acquired companies at fair value as at the acquisition date. The valuation method applied to the acquired net assets for the purposes of IFRS 3 differs significantly from the valuation method applied to the companies' shares for the purposes of the transaction. In the first case, the fair value of individual non-current assets was determined by way of an independent valuation by asset appraisal experts, while the value of individual liabilities and contingent liabilities was determined and disclosed based on the Company's best estimates, taking into account e.g. the results of environmental protection experts' work.

For the purposes of IFRS 3, the fair value of individual items of property, plant and equipment was determined in the following manner:

- The fair value of real estate was measured using the comparative approach, the price comparison method, and the statistical market analysis techniques; the first assets to be valued were separate pieces of real estate held by each of the companies, and subsequently the fair value of the whole real estate (including land), broken down by individual items of property, plant, and equipment, was determined with the use of appropriate asset classification rules,
- Movables were valued using the multiples method, taking into account the adjusted initial value of tangible assets (including official adjustments of value), the technical condition, the technical and economic wear and tear (percentage), and the effect of macroeconomic factors (such as inflation, changes in the value of currency, etc).

The valuation showed an increase in the value of those assets which are disclosed as off-balance-sheet items in accordance with the PAS (perpetual usufruct of land) as well as those which have been fully depreciated but are still used in the business activities of the companies and continue to deliver economic benefits. Moreover, the value of the acquired companies' liabilities and contingent liabilities which had not been disclosed in the financial statements of the companies or were disclosed in lower amounts, was also increased as a result of the valuation.

Compared with the initially estimated goodwill arising from the business combinations, as presented in the consolidated interim financial statements, a significant change occurred, namely negative goodwill was identified, and presented in the consolidated interim financial statements in the balance sheet under provisions.

By acquiring the Southern Refineries and Petrobaltic S.A., Grupa LOTOS S.A. assumed liabilities whose fair value cannot be reliably estimated at present. It is also difficult to determine whether an outflow of economic benefits will be necessary to settle the liabilities. Therefore, the liabilities were not disclosed as at the acquisition date (February 3rd 2005). The negative goodwill write-off disclosed in these consolidated financial statements due to the requirements of IFRS 3 was not decreased by the undetermined fair value of such future liabilities. The effects, if any, of discharging these liabilities will have to be disclosed in future consolidated financial statements of the Group.

17. Investments in Associated Undertakings

Company name	Registered office	Business area	Dec 31 2006	Dec 31 2005
Energobaltic Sp. z o.o. (1)	Gdańsk	Production activities	32.16%	32.16%
UAB Naftos Gavyba	Klaipeda, Lithuania	Services	29.46%	29.46%

(1) See Note 19.

The Group's share in the associated undertakings is as follows: 46.6% in Energobaltic Sp. z o.o. and 42.7% in UAB Naftos Gavyba.

PLN '000	Dec 31 2006	Dec 31 2005
Investments in associated undertakings valued with equity method		
Naftos Gavyba Group	83,381	58,425
Total	83,381	58,425
Other non-current financial assets (1)	-	24,911
Total investments in associated undertakings	**83,381**	**83,336**

(1) As at December 31st 2005, the Group recognised assets invested in UAB Naftos Gavyba, its associated undertaking. The recognised amount is the funds provided to UAB Naftos Gavyba by Petrobaltic in 2000 to finance the purchase of AB Geonafta shares, subject to a condition precedent (Conditional Agreement on Purchase of Ownership Rights to Shares, dated July 18th 2000; the Agreement). Transfer of the shares was conditional upon UAB Naftos Gavyba performing its investment commitments towards AB Geonafta, as specified in the privatisation agreement of AB Geonafta. In 2001–2005, UAB Naftos Gavyba performed all of its investment commitments, which consumed LTL 56m, and acquired 41 million AB Geonafta shares. The most recent increase in AB Geonafta's share capital took place on April 25th 2005. Performance of these obligations was financed in full with UAB Naftos Gavyba's own funds sourced from dividends paid out in consecutive years by AB Geonafta. With the condition precedent fulfilled on April 25th 2005, Petrobaltic could take over the shares in AB Geonafta specified in the Agreement.

As at December 31st 2006, the Group recognised assets invested in UAB Naftos Gavyba, its associated undertaking, in the total amount of PLN 24.7m, The assets are presented the consolidated financial statements of the Group for 2006 under "Other current financial assets".

By the date of these financial statements, UAB Naftos Gavyba had not made any entry in the share register of AB Geonafta which would constitute the transfer the ownership rights to the shares purchased by Petrobaltic under a condition precedent. On March 24th 2006, an agreement supplementary to the Agreement of July 18th 2000 was signed by Petrobaltic S.A. and UAB Naftos Gavyba to postpone the deadline for transferring the ownership rights to the shares in AB Geonafta to August 31st 2007. Consequently, as at December 31st 2006, the prepayment of PLN 24.7m was reclassified in the Group's balance sheet from non-current investment to current investments.

On March 30th 2007, the General Shareholders Meeting of UAB Naftos Gavyba, an associated undertaking, approved the financial statements for 2006 and resolved to allocate the profit generated in 2006 and a portion of undistributed retained earnings in the amount of LTL 100m to dividend payment.

Following changes in the shareholder structure of Naftos Gavyba (UAB Naftos Tekme acquired all the UAB Naftos Gavyba shares not held by Petrobaltic S.A, thus becoming the largest shareholder in the company with a 57.3% stake in its share capital), the Management Board of Petroblatic S.A. decided to suspend the proposed actions relating to termination of the conditional AB Geonafta share purchase agreement. To determine the future strategy of Petrobaltic S.A., its Management Board recommended that appropriate legal and economic analyses be performed.

Net assets of material undertakings valued with equity method:

PLN '000	Dec 31 2006	Dec 31 2005
Naftos Gavyba Group	195,270	136,825
Energobaltic Sp. z o.o.	24,118	15,071

Liabilities and provisions for liabilities of material undertakings valued with equity method:

PLN '000	December 31 2006	December 31 2005
Naftos Gavyba Group	73,203	68,630
Energobaltic Sp. z o.o.	118,761	136,240

Sales revenue of undertakings valued with equity method:

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Naftos Gavyba Group	102,488	101,524
Energobaltic Sp. z o.o.	24,424	30,233

Net profit/(loss) of undertakings valued with equity method:

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Naftos Gavyba Group	60,458	62,460
Energobaltic Sp. z o.o.	9,047	(5,049)

Share in profit (loss) of undertakings valued with equity method:

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Naftos Gavyba Group	25,815	26,598
Naftoport Sp. z. o.o.	-	2,355
Other undertakings valued with equity method	(4)	(481)
	=========	=========
Total	**25,811**	**28,472**
	=========	=========

18. Financial Assets

PLN '000	Dec 31 2006	Dec 31 2005
Shares in companies	12,900	11,985
Other non-current financial assets	10,742	8,208
	=========	=========
Total	**23,642**	**20,193**
	=========	=========

19. Methods and Material Assumptions Adopted for Measuring Financial Assets and Liabilities at Fair Value

Overview of Financial Instruments

The Group is exposed to market risk, including, in particular, fluctuations of the refining margin, exchange rates and interest rates. It manages those risks using derivatives and other financial instruments. The Parent Undertaking does not issue any derivative financial instruments held for trading.

The Parent Undertaking has implemented written guidelines for currency risk management; these guidelines define the risk tolerance level and the general risk management policy. The Company has also developed procedures designed to ensure timely and detailed monitoring and control of hedging transactions. At the meetings of the Risk Management Committee ("RMC"), results of currency risk management and results on derivatives hedging commodity risk are presented. The RMC is also responsible for recommending management strategies for individual risk types to the Management Board and proposing hedging transactions exceeding predefined risk limits.

As it does not meet formal requirements, the Group does not apply hedging accounting; accordingly, any change in fair value of derivatives is charged to the income statement.

Description of Financial Instruments

Financial Assets and Liabilities Held for Trading

Financial assets held for trading comprise treasury bills and investment certificates. The Parent Undertaking discloses derivative transactions with positive fair values under financial assets held for trading. These transactions include unrealised forwards and swaps. Derivative transactions with negative fair value disclosed under financial liabilities held for trading are swap contracts.

Financial Assets Available for Sale

Non-current financial assets available for sale measured at fair value as at December 31st 2006 and December 31st 2005 include mainly shares and equity interests for which there is no active market.

Loans Advanced and Receivables

1. On September 23rd 2003 and April 8th 2004, Grupa LOTOS S.A. signed with Rafineria Nafty Glimar S.A. loan agreements for the financing of operating and investing activities, including, in particular, the Glimar Hydrocomplex investment project, for an aggregate amount of PLN 90m. By December 31st 2004, Grupa LOTOS S.A. had advanced PLN 48m to Rafineria Nafty Glimar S.A. under these agreements. Additionally, in connection with the Letter of Comfort signed by Grupa LOTOS S.A. on February 12th 2004 for Bank Przemysłowo-Handlowy S.A., the Company undertook commitments relating to the co-financing of the Glimar Hydrocomplex investment project and maintaining of an appropriate financial standing of Rafineria Nafty Glimar S.A. In the opinion of the Company's Management Board, these commitments do not represent financial liabilities as at the balance-sheet date.

As at December 31st 2006 and December 31st 2005, assets under the advanced loans were fully covered by an allowance. As at the above dates, the Company also created a provision for the remaining amounts due under these agreements
On January 19th 2005, the District Court of Nowy Sącz declared Rafineria Nafty Glimar S.A. of Gorlice bankrupt.

2. On November 12th 2001 an agreement was concluded under which Petrobaltic S.A. granted loans to Energobaltic Sp. z o.o. Petrobaltic S.A.'s receivables under the loan (including accrued interest) amounted to

USD 6,623 thousand as at December 31st 2006 (USD 6,879 thousand as at December 31st 2005), which represented the equivalent of PLN 20,022 thousand (PLN 20,825 thousand as at December 31st 2005). On the basis of an analysis of the economic and financial standing of Energobaltic Sp. z o.o., performed based on the 2005 financial statements, and considering the projections for the following years and the related risk of a loss of liquidity in the event of failure of the measures taken by the Management Board of Energobaltic Sp. z o.o. to restructure the company's indebtedness, i.e. to postpone the repayment of bank loans and shareholder loans, a valuation allowance was made for the full value of the loan. A valuation allowance was also made for the value of shares held in Energobaltic Sp. z o.o.

Financial Assets Held to Maturity

Financial assets held to maturity comprise purchased treasury bonds.

Commodity Risk

The most material component of commodity risk is the refining margin defined as the difference between the price of product sold and the price of raw materials purchased. At its meetings, the RMC adopts decisions concerning proposed hedging transactions. These decisions are subject to final approval by the President of the Management Board.

Interest Rate Risk

The exposure of Parent Undertaking to market risk arising in connection with interest rate fluctuations primarily relates to loans with variable interest rates, reinvestment of free cash, and the balance of future cash flows. The Company does not use derivative financial instruments to hedge its investment portfolio. In order to ensure liquidity of this portfolio, the Company invests a significant portion of assets in debt securities for which there is a ready secondary market or another market on which such securities may be sold.

Currency Risk

Main sources of currency risk are raw material imports, product exports, domestic sales indexed to foreign currencies and loans denominated in foreign currencies. Currency risk management is based on planned net foreign currency positions, in line with the assumptions stipulated in "Currency Risk Management Strategy for Grupa LOTOS S.A.", which also defines the maximum limit of the total foreign currency position and the gross global position to which the Company may be exposed in a budget year. The limit is expressed as a percentage of the Company's equity. The risk management falls within the powers of the RMC or the risk management division, depending on current risk exposure.

Credit risk

As a rule, the Group executes transactions with recognised companies of good credit standing. All customers requesting trade credit undergo verification of their financial reliability. Moreover, thanks to ongoing monitoring of receivables, the risk of uncollectible receivables is low.

In terms of the Group's other financial assets, such as cash and cash equivalents, financial assets available for sale and certain derivatives, the Group's credit risk arises as a result of the other party's inability to make the payment, and the maximum exposure to this risk is equal to the carrying value of such instruments.

The Company has developed a system for determining limits of exposure with respect to individual counterparties in a transaction, based on ratings granted by recognised rating agencies, solvency ratios, and value of equity of both Grupa LOTOS S.A. and the counterparties. Results on hedging transactions are taken into account in exposure measurement. There is no material concentration of the credit risk within the Group.

20. Current Financial Assets

PLN '000	Dec 31 2006	Dec 31 2005
Positive valuation of financial instruments, including:	190	5,328
- Currency forwards	190	2,016
- Currency swaps	-	24
- Currency and interest rate swaps	-	3,288
Repo transactions	-	30,024
Treasury bonds	178,300	3,879
Treasury bills	-	93,140
Other, including:	25,041	3,389
- prepayments for shares (1)	24,726	-
Total	**203,531**	**135,760**

(1) The assets invested in AB Geonafta, a subsidiary undertaking. (See Note 17).

Financial Assets and Liabilities

Changes in financial assets and liabilities by category in consecutive reporting periods:

(PLN '000)	Financial assets held for trading	Financial liabilities held for trading	Loans advanced and receivables	Financial assets held to maturity	Financial assets available for sale
Opening balance as at Jan 1 2006	**128,492**	**-**	**177**	**3,879**	**6,395**
Gross value	120,013	-	48,216	3,783	6,813
Revaluation	8,479	-	(48,039)	96	(418)
Increase, including:	16,693,347	-	213	-	35
Acquisition	16,693,068	-	213	-	-
Other	-	-	-	-	35
Revaluation	279	-	-	-	-
Decrease, including:	(16,643,349)	-	(190)	-	-
Sale	(16,634,870)	-	(190)	3,783	-
Revaluation	(8,479)	-	-	96	-
Closing balance as at Dec 31 2006	**178,490**	**-**	**200**	**-**	**6,430**
Gross value	178,211	-	48,239	-	6,848
Revaluation	279	-	(48,039)	-	(418)
Balance-sheet disclosure					
Non-current investments	-	-	92	-	6,395
Current investments	178,490	-	108	-	35
Current liabilities	-	-	-	-	-
	-----------	-----------	-----------	-----------	-----------
Total	**178,490**	**-**	**200**	**-**	**6,430**
	===========	===========	===========	===========	===========

(PLN '000)	Financial assets held for trading	Financial liabilities held for trading	Loans advanced and receivables	Financial assets held to maturity	Financial assets available for sale
Opening balance as at Jan 1 2005	**43,234**	**-**	**-**	**3,952**	**1,509**
Gross value	22,029	-	48,039	3,783	1,927
Revaluation	21,205	-	(48,039)	169	(418)
Increase, including:	8,111,541	-	3,097	-	6,312
Acquisition	8,091,910	-	177	-	-
Revaluation	8,479	-	2,920	-	-
Other	-	-		-	6,312
Inclusion of new undertakings in consolidation	11,152	-	-	-	-
Decrease, including:	(8,026,283)	-	(2,920)	(73)	(1,426)
Sale	(8,005,078)	-	-	-	(1,426)
Revaluation	(21,205)	-	(2,920)	(73)	-
Closing balance as at Dec 31 2005	**128,492**	**-**	**177**	**3,879**	**6,395**
Gross value	120,013	-	48,216	3,783	6,813
Revaluation	8,479	-	(48,039)	96	(418)
Balance-sheet disclosure					
Long-term investments	-	-	-	-	6,395
Current investments	128,492	-	177	3,879	-
Current liabilities	-	-	-	-	-
	-----------	-----------	-----------	-----------	-----------
Total	**128,492**	**-**	**177**	**3,879**	**6,395**
	===========	===========	===========	===========	===========

Value of derivative transactions as at December 31st 2006 (PLN '000):

Company	Type of forward transaction	Transaction execution date	Transaction settlement date*	Forward rate	Currency pair	Notional amount bought (USD '000)	Notional amount bought (PLN '000)	Fair value as at Dec 31 2006 (PLN '000)**
Grupa Lotos S.A.	Currency forward	Dec 20 2006	Jan 2 2007	2.9	USD/PLN	-	43,198	460
Grupa Lotos S.A.	Currency swap	Dec 28 2006	Jan 2 2007	3.8	EUR/PLN	-	10,393	(10)
Grupa Lotos S.A.	Currency forward	Dec 28 2006	Jan 10 2007	1.3	EUR/USD	13,179	-	(33)
Grupa Lotos S.A.	Currency forward	Dec 15 2006	Jan 19 2007	1.3	EUR/USD	13,089	-	243
							Total	**660**

Company	Type of forward transaction	Transaction execution date	Transaction settlement date*	Forward rate	Currency pair	Notional amount bought (USD '000)	Notional amount bought (PLN '000)	Fair value as at Dec 31 2006 (PLN '000)**
Grupa Lotos S.A.	Currency forward	Dec 21 2006	Jan 29 2007	2.9	USD/PLN	-	57,700	(455)
Grupa Lotos S.A.	Currency forward	Dec 28 2006	Mar 16 2007	2.9	USD/PLN	-	43,533	(15)
							Total	**(470)**

TOTAL	**190**

* It is possible to settle the transaction early by taking an offsetting position and discounting the payment, or by means of other procedures defined by banks.
** The fair value of a transaction is calculated on the basis of its discounted market value established by marking to market. The resulting amount is the amount of a hypothetical offsetting position (closing the transaction) taken on the valuation date. In the case of currency swaps, in order to determine their fair value, such transactions are valued using forward rates calculated on the basis of fixing rate quotations of the National Bank of Poland and the zero-coupon interest rate curve (CLOSE YIELD), as published by Reuters on the valuation date.

Value of derivative transactions as at December 31st 2005 (PLN '000):

Company	Type of forward transaction	Transaction execution date	Transaction settlement date *	Forward rate	Currency pair	Notional amount sold (EUR '000)	Notional amount sold (PLN '000)	Fair value as at Dec 31 2005 (PLN '000)**
Grupa LOTOS S.A.	Currency forward	Jul 6 2005	Apr 24 2006	2.7	CHF/PLN	-	53,747	3,501
Grupa LOTOS S.A.	Currency forward	Dec 20 2005	Jan 12 2006	3.2	USD/PLN	-	32,152	(501)
Grupa LOTOS S.A.	Currency forward	Dec 30 2005	Feb 2 2006	3.9	EUR/PLN	-	5,028	(5)
Grupa LOTOS S.A.	Currency swap	Dec 30 2005	Jan 31 2006	2.8	JPY/PLN	-	99,655	24
							Total	**3,019**

Company	Type of forward transaction	Transaction execution date	Transaction settlement date *	Forward rate	Currency pair	Notional amount bought (USD '000)	Notional amount bought (PLN '000)	Fair value as at Dec 31 2005 (PLN '000)**
Grupa LOTOS S.A.	Currency forward	Dec 20 2005-Tue	Jan 5 2006-Thu	1.2	EUR/USD	24,000		(1,219)
Grupa LOTOS S.A.	Currency forward	Dec 27 2005-Tue	Jan 6 2006-Fri	3.2	USD/PLN		25,860	229
Grupa LOTOS S.A.	Currency forward	Dec 29 2005-Thu	Jan 6 2006-Fri	3.2	USD/PLN		32,581	31
Grupa LOTOS S.A.	Currency forward	Dec 30 2005-Fri	Jan 9 2006-Mon	3.3	USD/PLN		22,849	(20)
							Total	**(979)**
							TOTAL	**2,040**

* It is possible to settle the transaction early by taking an offsetting position and discounting the payment, or by means of other procedures defined by banks.
** The fair value of a transaction is established by marking to market. The resulting amount is the amount of a hypothetical offsetting position (closing the transaction) taken on the valuation date. In the case of currency swaps, in order to determine their fair value, such transactions are valued using forward rates calculated on the basis of spot rates and swap points quotations published by Reuters at 11am on the valuation date.

Company	Type of forward transaction*	Transaction execution date	Contract term	Currency pair	Exchange rate	Notional amount bought (EUR '000)	Bank's reference rate	Reference rate	Fair value as at Dec 31 2005 (PLN '000)**
Grupa LOTOS S.A.	Currency and interest rate swap	Sep 4 2003	Sep 8 2003 – Apr 24 2006	CHF/PLN	2.9	57,200	LIBOR CHF/ 6M	5,2	(8,291)
					Total	**57,200**			**(8,291)**

Company	Type of forward transaction*	Transaction execution date	Contract term	Currency pair	Exchange rate	Notional amount sold (EUR '000)	Bank's reference rate	Reference rate	Fair value as at Dec 31 2005 (PLN '000)**
Grupa LOTOS S.A.	Currency and interest rate swap	Sep 4 2003	Sep 8 2003 – Apr 24 2006	USD/PLN	4.0	57,200	5,2	2,8	11,579
					Total	**57,200**			**11,579**
					TOTAL	**114,400**			**3,288**

* Purpose of the transaction:

- to hedge a long-term CHF-denominated loan bearing interest at the variable 6M CHF LIBOR rate. The purpose of the transaction was to mitigate the risk related to a change (increase) in the CHF/PLN exchange rate (affecting the principal) as well as the risk of a change (increase) in the 6M CHF LIBOR rate (affecting the repayment of interest);

- to hedge future receivables under domestic sales, sensitive to the USD exchange rate. The potential future receivables from domestic sales are dependent, by and large, on the USD/PLN exchange rate and are larger than the liabilities arising primarily in connection with the purchases of raw materials made in the U.S. dollars. Given the above, in order to safeguard its core business, Grupa LOTOS S.A. has a long currency position, and thus, it is exposed to the risk related to a decrease in the USD/PLN exchange rate. The purpose of the transaction was to mitigate the risk related to a change (decrease) in the USD/PLN exchange rate.

** Valuation of the financial instrument as at end of period is disclosed at fair value.

The fair value of the financial instruments corresponds to their carrying value.

21. Inventories

PLN '000	Dec 31 2006	Dec 31 2005
Finished products	506,672	418,958
Semi-finished products and work in progress	234,953	273,078
Goods for resale	101,414	15,216
Materials	864,403	725,687
Net inventories	**1,707,442**	**1,432,939**

Valuation Allowances for Inventories

PLN '000	Dec 31 2006	Dec 31 2005
Finished products	29,672	9,629
Semi-finished products and work in progress	5,886	2,353
Goods for resale	1,482	1,107
Materials	7,325	8,727
Total valuation allowances for inventories	**44,365**	**21,816**

During the year ended December 31st 2006, the Group made a valuation allowance for inventories in the amount of PLN 38,082 thousand and reversed a valuation allowance for inventories in the amount of PLN 15,533 thousand.

During the year ended December 31st 2005, the Group made a valuation allowance for inventories in the amount of PLN 19,192 thousand and reversed a valuation allowance for inventories in the amount of PLN 9,671 thousand.

As at December 31st 2006, the carrying value of finished products recognised at net selling prices was PLN 239,829 thousand (PLN 148,879 thousand as at December 31st 2005).

As at December 31st 2006, the value of inventories which serve as collateral for the Group's liabilities amounted to PLN 9,115 thousand.

Mandatory Liquid Fuel Stocks

Pursuant to Art. 19a.5 of the Polish State Reserves and Mandatory Fuel Stocks Act of May 30th 1996 (Dz.U. of 2003 No. 24, item 197, Dz.U. of 2004 No. 42, item 386, Dz.U. of 2005 No. 132, item 1110 and No. 143, item 1201), producers and importers of liquid fuels are obliged to create mandatory liquid fuel stocks, hereinafter referred to as "stocks," based on the volume of liquid fuels produced or imported – from an EU member state or another state – in the previous year, taking into account the schedule for reaching the volume of liquid fuel stocks required at the end of a given year, in accordance with the appendix to the Regulation of the Minister of Economy on the schedule for the creation of liquid fuel stocks, dated December 19th 2005 (Dz.U. of 2005 No. 266, item 2240).
This schedule specifies the path to reach in 2008, and subsequent years, the level of stocks corresponding to 76-day average internal fuel consumption at the end of the year. Thus, together with the existing economic reserves accounting for a 14-day consumption, the 90-day stocks required by the EU regulations will be reached.
In each subsequent year, the required level of stocks should be increased by the stocks volume required for such number of days as is specified for each subsequent year in the Regulation of the Minister of Economy on the schedule for the creation of liquid fuel stocks, dated December 19th 2005.

Mandatory fuel stocks may be stored in the form of finished products, semi-finished products and crude oil. However, the total volume of stocks in the form of semi-finished products and crude oil (taking into account the capacity for processing crude oil into fuels) may not exceed the share of each type of fuels in the stocks, as stipulated in the Regulation of the Minister of Economy on the detailed procedure for the creation and determination of the volume of liquid fuel stocks, dated May 12th 2006 (Dz.U. of 2006 No. 92, item 642).

In the balance sheet, the Group disclosed the following mandatory stocks:

PLN '000	Dec 31 2006	Dec 31 2005
Mandatory stocks	1,027,858	800,688

22. Trade and Other Receivables

PLN '000	Dec 31 2006	Dec 31 2005
Trade receivables, including:	1,180,699	926,267
- from related undertakings	615	501
Receivables from the state budget	77,843	107,517
Other receivables, including:	17,933	26,564
- from related undertakings	154	47
Net receivables	**1,276,475**	**1,060,348**
Valuation allowance for receivables	136,289	134,178
Gross receivables	**1,412,764**	**1,194,526**

For information on transactions with related undertakings see Note 44.

The payment period for trade receivables in the normal course of business is 14–55 days. The concentration of risk related to sales is limited due to the large number of the Group's business partners.

As at December 31st 2006, the Group's receivables of PLN 14,153 thousand were assigned by way of security for the Group's liabilities.

Impairment Losses on Receivables

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Beginning of period	**134,178**	**92,244**
Recognised	19,350	55,988
Reversed	(17,239)	(14,054)
End of period	**136,289**	**134,178**

23. Cash and Cash Equivalents

PLN '000	Dec 31 2006	Dec 31 2005
Cash in hand and cash at banks	723,213	762,753
Other cash	49,174	5,041
Total	**772,387**	**767,794**

Cash at banks bears interest at variable rates set according to the interest rate for one-day bank deposits. Short-term deposits are placed for various periods ranging from one day to one month, depending on the Company's current demand for cash, and bear interest at the interest rates set for them. As at December 31st 2006, the amount of undrawn funds available to the Group under loans in respect of which all conditions precedent had been fulfilled, was PLN 401,096 thousand (as at December 31st 2005: PLN 763,681 thousand).

As at December 31st 2006, restricted cash amounted to PLN 23,143 thousand (as at December 31st 2005: PLN 1,572 thousand). As at December 31st 2006, restricted cash related mainly to a bank guarantee of PLN 21,668 thousand, provided by LOTOS Biopaliwa to secure the payment under an agreement for the construction of a biodiesel production unit, concluded with MAN Ferrostal of Germany.

The restricted cash is disclosed in the balance sheet under "Other cash".

24. Cash structure for the cash-flow statement

PLN '000	Dec 31 2006	Dec 31 2005
Cash at banks	721,321	761,024
- current accounts	586,272	515,259
- deposits up to 1 year	135,049	245,765
Cash in hand	1,892	1,729
Other cash	49,174	5,041
Overdraft facilities	(148,222)	-
Total cash	**624,165**	**767,794**

Breakdown of the Group's Activities as Disclosed in the Cash-Flow-Statement

Operating activities include transactions and events related to the core business of an undertaking and other activities which are not included in investing or financing activities.

Investing activities include transactions and events which consist in the purchase or sale of property, plant and equipment (tangible assets, investments in progress), intangible assets, long-term investments and current financial assets (excluding cash and cash equivalents), as well as related monetary costs and benefits, excluding those related to income tax.

Financing activities include transactions and events which consist in the raising and repayment of funds from sources other than operating activities, as well as related monetary costs and benefits, excluding those related to income tax. The occurrence of cash flows in the financing activities gives rise to changes in the amount of equity and financial indebtedness and the proportion between them.

Causes of differences between the balance-sheet changes in certain items and changes disclosed in the cash-flow-statement

Receivables PLN ‘000	**Dec 31 2006**	**Dec 31 2005**
Balance-sheet change in net non-current and current receivables	(212,858)	(335,213)
Change in income tax receivables	24,363	(4,972)
Inclusion of new undertakings in consolidation	-	153,099
Other	(659)	23,894
Change in receivables as disclosed in the cash-flow-statement	(189,154)	(163,192)

Liabilities PLN ‘000	**Dec 31 2006**	**Dec 31 2005**
Balance-sheet change in current and non-current liabilities	211,055	620,642
Change in current and non-current loans	(98,582)	45,468
Change in investment liabilities	914	23,806
Inclusion of new undertakings in consolidation	-	(331,509)
Change in income tax liabilities	61,889	(64,847)
Other	177	(21,701)
Change in liabilities as disclosed in the cash-flow-statement	175,099	271,859

Inventories PLN ‘000	**Dec 31 2006**	**Dec 31 2005**
Balance-sheet change in inventories	(274,503)	(604,319)
Inclusion of new undertakings in consolidation	-	145,508
Other	12	39
Change in inventories as disclosed in the cash-flow-statement	(274,491)	(458,772)

Provisions PLN’000	**Dec 31 2006**	**Dec 31 2005**
Balance-sheet change in provisions	414	201,587
Inclusion of new undertakings in consolidation	-	(181,800)
Change in deferred tax liability	17,613	(27,717)
Other	2,002	4,495
Change in provisions as disclosed in the cash-flow statement	19,201	(3,435)

Prepayments and accrued income PLN’000	**Dec 31 2006**	**Dec 31 2005**
Balance-sheet change in prepayments and accrued income	(7,638)	(14,620)
Inclusion of new undertakings in consolidation	-	6,232
Other	395	(480)
Change in prepayments and accrued income as disclosed in the cash-flow statement	(7,243)	(8,868)

Cash PLN'000	Dec 31 2006	Dec 31 2005
Balance-sheet change in cash	4,593	612,782
Interest-bearing overdraft facilities	(148,222)	-
Other	-	-
Change in cash as disclosed in the cash-flow statement	(143,629)	612,782

Other Items of the Cash-Flow-Statement

The item "Other, net" under cash flows from investing activities includes the following adjustments:

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Excess of share in net assets over acquisition cost	-	(266,625)
Other	1,968	(402)
Total other, net	1,968	(267,027)

The item "Other, net" under cash flows from investing activities includes the following adjustments:

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Prepayments for tangible assets under construction	(148,018)	-
Other	1,966	17,448
Total other, net	(146,052)	17,448

25. Share Capital

The structure of Grupa LOTOS S.A.'s share capital as at December 31st 2006 and December 31st 2005 was as follows:

	Number of shares	Number of votes	Par value of shares (PLN)	% of share capital
State Treasury	7,878,030	7,878,030	7,878,030	6.93 %
Nafta Polska S.A.	59,025,000	59,025,000	59,025,000	51.91 %
Other shareholders	46,796,970	46,796,970	46,796,970	41.16 %
Total	113,700,000	113,700,000	113,700,000	100.00 %

As a result of the acquisition of Grupa LOTOS S.A. shares in transactions carried out on the Warsaw Stock Exchange, which were settled on March 6th 2007, ING Nationale-Nederlanden Polska OFE came into possession of the Company shares conferring the right to over 5% of the total vote at the General Shareholders Meeting of Grupa LOTOS S.A. Prior to the abovementioned transactions, ING Nationale-Nederlanden Polska held 5,676,589 shares in Grupa LOTOS S.A., which represented 4.99% of the share capital and conferred the right to 5,676,589 votes at the General Shareholders Meeting, accounting for 4.99% of the total vote. As at March 7th 2007, 5,876,589 Grupa LOTOS S.A. shares were registered in the securities account of ING

Nationale-Nederlanden Polska, which account for 5.17% of the Company's share capital and confer the right to 5,876,589 votes at the General Shareholders Meeting, representing 5.17% of the total vote.

Share Issue

On May 17th 2005, Grupa LOTOS S.A. applied to the Warsaw Stock Exchange for admission to trading on the main market of:

- 58,229,340 Series A ordinary registered shares,
- 20,470,660 Series A ordinary bearer shares,
- 35,000,000 Series B ordinary bearer shares,
- 35,000,000 rights to Series B new shares.

On June 3rd 2005, pursuant to Resolution No. 178/2005, the Management Board of the Warsaw Stock Exchange admitted the following shares of Grupa LOTOS S.A., with a par value of PLN 1 per share, to trading on the main market:

- 58,229,340 Series A ordinary registered shares,
- 20,470,660 Series A ordinary bearer shares,
- up to 35,000,000 Series B ordinary bearer shares, subject to a condition that the Company's share capital is increased through the issue of Series B shares.

Pursuant to Resolution No. 178/2005 of June 3rd 2005, the Management Board of the Warsaw Stock Exchange admitted up to 35,000,000 rights to Series B shares of Grupa LOTOS S.A. to trading on the main market.

On June 4th and June 6th 2005, the Company allotted Series B shares in the Retail Offering and the Institutional Offering, respectively. Upon the allotment, the Public Offering was announced as successful.

1. The Public Offering comprised 35,000,000 Series B Shares:

   The shares were offered as follows:

   - 8,800,000 shares in the Retail Offering,
   - 26,200,000 shares in the Institutional Offering, including:
     - 16,500,000 shares in the Polish Institutional Offering, and
     - 9,700,000 shares in the International Institutional Offering.

2. The reduction rate in the Retail Offering was 96.58%. Retail investors placed the aggregate number of 31,646 subscription orders for 257,634,549 Series B shares.

3. In the Institutional Offering, during the book-building process Polish and international institutional investors declared demand for 86,192,129 offered shares. In the Institutional Offering, Series B shares were allotted in accordance with the subscription orders placed.

4. All the shares offered by the Company, i.e. 35,000,000 Series B shares, were allotted as a result of the subscription.

5. The shares were acquired at the issue price of PLN 29.00.

6. The aggregate number of orders placed in the Public Offering for Series B shares was 31,763, including:

   - 31,646 in the Retail Offering, and
   - 117 in the Institutional Offering.

By virtue of Resolutions No. 179/2005 and 180/2005 of June 8th 2005, the Management Board of the Warsaw Stock Exchange decided to:

- introduce, by way of an ordinary procedure, 20,545,970 Series A ordinary bearer shares of Grupa LOTOS S.A., with a par value of PLN 1.00 per share (ISIN code: PLLOTOS00025) to trading on the main market,

- introduce 35,000,000 rights to Series B ordinary bearer shares of Grupa LOTOS S.A., with a par value of PLN 1.00 per share (ISIN code: PLLOTOS00041), to trading on the main market.

The abovementioned shares and rights to Series B ordinary bearer shares of Grupa LOTOS S.A. were first quoted on the Warsaw Stock Exchange on June 9th 2005.

The Management Board of the Warsaw Stock Exchange set the last listing date for 35,000,000 rights to Series B ordinary bearer shares of Grupa LOTOS S.A., with a par value of PLN 1.00 per share (ISIN code: PLLOTOS00041), at July 7th 2005.

On June 28th 2005, the Company's Management Board received the decision of the District Court of Gdańsk, XII Commercial Division of the National Court Register, concerning registration of Grupa LOTOS S.A.'s share capital increase through the issue of Series B shares. The share capital increase was registered by the Court on June 28th 2005. Following the registration, the share capital amounted to PLN 113,700,000 and was divided into 113,700,000 shares. The total number of votes attached to all the shares issued by Grupa LOTOS S.A. after the registration of the share capital increase is 113,700,000 votes.

The issue price was set at PLN 29.00 per share. The issue proceeds were PLN 1,015,000 thousand. The share premium was PLN 980,000 thousand and was disclosed under reserve funds, net of the expenses directly related to the share issue, adjusted for income tax of PLN 9,049 thousand (See "Statement of changes in equity"). The net proceeds from the share issue (net of the expenses directly related to the share issue, adjusted for income tax) reached PLN 1,005.9m.

26. Dividends

On June 19th 2006, the Annual General Shareholders Meeting adopted a resolution concerning the distribution of the 2005 net profit of the Parent Undertaking. Pursuant to the resolution, the Company's entire net profit for the year ended December 31st 2005, amounting to PLN 532,268 thousand, was allocated to the Company's reserve funds. In these financial statements, the Company discloses the distributed profit/loss under "Retained earnings".

As at the date of these financial statements, the Company's Management Board has not made any decisions regarding distribution of the 2006 profit.

On May 13th 2005, the General Shareholders Meeting of the Parent Undertaking approved the 2004 dividend amount of PLN 15,740 thousand (PLN 0.20 per share). Pursuant to the Resolution of the General Shareholders Meeting of Grupa LOTOS S.A. on the distribution of the Company's net profit for the year ended December 31st 2004, adopted on May 13th 2005, the dividend payment date was set at June 22nd 2005. Starting January 1st 2005, the Parent Undertaking will distribute its net profit computed in accordance with the IFRS.

27. Earnings per Share

	Year ended Dec 31 2006	Year ended Dec 31 2005
Net profit attributable to equity holders of the parent (PLN '000) (A)	679,912	915,124
Weighted average number of shares (in thousands) (B)*	113,700	96,632*
Earnings per share (PLN '000) (A/B)	5.98	9.47

* Earnings per share for the year ended December 31st 2005 were computed on the basis of the weighted average number of shares in the period January 1st – December 31st 2005.

28. Minority Interests

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Opening balance	254,281	14,882
Inclusion of new undertakings in consolidation	-	203,454
Share in profit/(loss) of subsidiary undertakings	54,740	53,715
Changes in shareholder structure of subsidiary undertakings	(84)	(16,272)
Dividends paid out by subsidiary undertakings	(2,521)	(2,521)
Other	-	1,023
Balance as at end of period	**306,416**	**254,281**

29. Loans and Borrowings

PLN '000	Dec 31 2006	Dec 31 2005
Bank loans	492,682	392,100
Other loans	11,550	13,550
Total	**504,232**	**405,650**
Including:		
Non-current portion	330,706	294,198
Current portion	173,526	111,452

Loans and Borrowings by Lender

PLN '000	Dec 31 2006	Dec 31 2005
Non-current portion		
Kredyt Bank S.A.	44,987	50,987
BRE Bank S.A.	-	2,233
NFOŚiGW	9,300	11,550
PeKaO S.A	20,900	30,874
PKO BP S.A.	1,456	2,809
Bank syndicate (PKO BP S.A. and PeKaO S.A)	254,063	195,745
Total non-current portion	**330,706**	**294,198**
Current portion		
Kredyt Bank S.A.	7,715	7,776
BRE Bank S.A.	-	2,912
PeKaO S.A	25,605	32,542
ING Bank Śląski S.A.	49,487	31,898
PKO BP S.A.	19,212	29,985
Podkarpacki Bank Spółdzielczy S.A.	-	4,300
Bank Handlowy w Warszawie S.A.	61,639	2
NFOŚiGW	2,250	2,000
Bank syndicate (PKO BP S.A. and PeKaO S.A)	37	37
Bank Millennium S.A.	1,941	-
Raiffeisen Bank Polska S.A.	3,600	-
BZ WBK S.A.	2,040	-
Total current portion	**173,526**	**111,452**
Total	**504,232**	**405,650**

Bank Loans by Currency

PLN '000	EUR loans	USD loans	PLN loans	Total
2007	3,965	65,019	104,542	173,526
2008	-	6,653	59,027	65,680
2009	-	6,653	57,571	64,224
2010	-	6,653	57,871	64,524
2011	-	943	54,571	55,514
after 2011	-	-	80,764	80,764
Total	**3,965**	**85,921**	**414,346**	**504,232**

The table above presents loans according to their maturity dates. As at December 31st 2006, the average effective interest rate of the loans was approx. 5.08%.

Loans and borrowings as at December 31st 2006:

Bank's name; form of incorporation	Registered office	Loan amount as per agreement		Outstanding loan amount (current portion)		Outstanding loan amount (non- current portion)		Maturity date		Financial terms and conditions (interest rate, interest payment schedule etc.)	Type of security
		PLN	Currency	PLN	Currency	PLN	Currency	Current portion	Non-current portion		
Kredyt Bank S.A.	Gdańsk branch	60,000	-	7,714	-	44,987	-	Dec 31 2007	Jun 30 2015	1M WIBOR + bank's margin	Mortgage, blank promissory note, assignment by way of security of receivables under insurance policies
Pekao S.A.	Warsaw	25,000	-	1	-	-	-	Mar 31 2007	-	1M WIBOR + bank's margin	Power of attorney for the bank to charge the account with amounts due, representation on submission to enforcement
Bank syndicate (PKO BP S.A. and Pekao S.A.)	Warsaw	340,000	-	37	-	254,063	-	Jun 30 2007	Dec 31 2014	3M WIBOR + bank's margin	Security (deposit) mortgage for each lender, representation on submission to enforcement, assignment by way of security of receivables under insurance policies, trade agreements, lease agreements, registered pledge on assets
Bank Pekao S.A.	Jasło branch	6,000	-	3,696	-	-	-	Mar 26 2007	-	1M WIBOR + bank's margin	Blank promissory note, power of attorney to bank account, assignment of receivables by way of security, blanket security (deposit) mortgage, registered pledge
Raiffeisen Bank Polska S.A.	Rzeszów branch	7,200	-	3,600	-	,	,	Jan 20 2007	-	1M WIBOR + bank's margin	power of attorney to bank account, registered pledge on inventories, assignment of receivables by way of security
Bank Handlowy w Warszawie S.A.	Warsaw	4,000	-	848	-	-	-	overdraft facility	-	T/N WIBOR + bank's margin	Representation on submission to enforcement, assignment of receivables by way of security

Bank's name; form of incorporation	Registered office	Loan amount as per agreement		Outstanding loan amount (current portion)		Outstanding loan amount (non- current portion)		Maturity date		Financial terms and conditions (interest rate, interest payment schedule etc.)	Type of security
		PLN	Currency	PLN	Currency	PLN	Currency	Current portion	Non-current portion		
ING Bank Śląski S.A.	Warsaw	30,000	-	19,841	-	-	-	overdraft facility	-	1M WIBOR + bank's margin	Mortgage, assignment by way of security
PKO BP S.A.	Krosno branch	15,000	-	7,224	-	-	-	overdraft facility	-	1M WIBOR + bank's margin	Mortgage, promissory note, pledge, assignments by way of security
PKO BP S.A.	Krosno branch	4,500	-	1,353	-	1,456	-	Oct 10 2007	Dec 31 2008	1M WIBOR + bank's margin	Assignment of receivables by way of security and mortgage
NFOŚiGW	Warsaw	15,000	-	2,250	-	9,300	-	Sep 30 2007	Sep 30 2010	half of the bill rediscount rate	Surety
Bank PEKAO S.A.	Warsaw	56,409	14,800 USD	6,653	2,286 USD	20,900	7,181 USD	Dec 31 2007	Feb 28 2011	1M LIBOR + bank's margin	Pledge on property, plant and equipment
Bank Millennium S.A.	Warsaw	30,000	-	1,941	-	-	-	overdraft facility	-	1M WIBOR + bank's margin	Representation on submission to enforcement
Bank Handlowy w Warszawie S.A.	Warsaw	-	40,000 USD or equivalent	28,050	-	-	-	overdraft facility	-	T/N WIBOR + bank's margin	Representation on submission to enforcement
				32,547	11,183 USD	-	-		-	SW LIBOR USD + bank's margin	
				194	51 EUR	-	-		-	SW EURIBOR + bank's margin	
ING Bank Śląski S.A.	Warsaw	-	9,000 USD or equivalent	56	-	-	-	overdraft facility	-	1M WIBOR + bank's margin	Representation on submission to enforcement
				25,819	8,871 USD	-	-		-	1M LIBOR USD + bank's margin	
				3,771	984 EUR	-	-		-	1M EURIBOR + margin	
PKO BP S.A.	Warsaw	100,000	-	10,635	-	-	-	overdraft facility	-	1M WIBOR + bank's margin	Representation on submission to enforcement
BZ WBK S.A.	Warsaw	30,000	-	2,040	-	-	-	overdraft facility	-	1M WIBOR + bank's margin	Representation on submission to enforcement

Bank's name; form of incorporation	Registered office	Loan amount as per agreement		Outstanding loan amount (current portion)		Outstanding loan amount (non- current portion)		Maturity date		Financial terms and conditions (interest rate, interest payment schedule etc.)	Type of security
		PLN	Currency	PLN	Currency	PLN	Currency	Current portion	Non-current portion		
Bank Pekao S.A.	Warsaw	100,000	-	15,255	-	-	-	overdraft facility	-	1M WIBOR + bank's margin	Representation on submission to enforcement
Kredyt Bank S.A.	Warsaw	10,000	-	1	-	-	-	overdraft facility	-	O/N WIBOR + bank's margin	Representation on submission to enforcement
TOTAL				**173,526**	**22,340 USD**	**330,706**	**7,181 USD**				
					1,035 EUR						

The banks' margins on the contracted loans are in the range of 0.05% – 2.0%.

Loans and borrowings as at December 31st 2005:

Bank's name; form of incorporation	Registered office	Loan amount as per agreement		Outstanding loan amount (current portion)		Outstanding loan amount (non- current portion)		Maturity date		Financial terms and conditions (interest rate, interest payment schedule etc.)	Type of security
		PLN	Currency	PLN	Currency	PLN	Currency	Current portion	Non-current portion		
Kredyt Bank S.A. O/Gdańsk	Warsaw	60,000	-	7,776	-	50,987		Dec 31 2006	Jun 30 2015	1M WIBOR + bank's margin	Mortgage, blank promissory note, assignment by way of security of receivables under insurance policies
PeKaO S.A.	Warsaw	25,000	-	25,000	-	-	-	May 19 2006	-	1M WIBOR + bank's margin	Power of attorney for the bank to charge the account with amounts due, representation on submission to enforcement
Bank syndicate (PKO BP S.A. and PeKaO S.A.)	Warsaw	340,000	-	37	-	195,745	-		Dec 31 2014	3M WIBOR + bank's margin	Security (deposit) mortgage for each lender, representation on submission to enforcement, assignment by way of security of receivables under insurance policies, trade agreements, lease agreements, registered pledge on assets
PKO BP S.A.	Warsaw	25,000	-	16,834	-	-	-	overdraft facility – revolving limit	Nov 3 2008	1M WIBOR + bank's margin	Representation on submission to enforcement
BRE BANK S.A.	Gdańsk	5,000	-	1,667	-	2,233	-	Sep 30 2006	Sep 30 2008	1M WIBOR + bank's margin	Registered pledge, assignment of receivables by way of security, blank promissory note
BRE BANK S.A.	Gdańsk	1,900	-	1,245	-	-	-	Aug 31 2006	-	1M WIBOR + bank's margin	Assignment of receivables, blank promissory note
Bank Handlowy w Warszawie S.A.	Warsaw	2,000	-	2	-	-	-	Jan 2 2006 overdraft facility	-		
PKO BP S.A.	Krosno branch	5,000	-	5,000	-	-	-	Aug 30 2006	-	1M WIBOR + bank's margin	Promissory note, assignments by way of security, pledge on inventories

Bank's name; form of incorporation	Registered office	Loan amount as per agreement		Outstanding loan amount (current portion)		Outstanding loan amount (non- current portion)		Maturity date		Financial terms and conditions (interest rate, interest payment schedule etc.)	Type of security
		PLN	Currency	PLN	Currency	PLN	Currency	Current portion	Non-current portion		
Podkarpacki Bank Spółdzielczy S.A.	Sanok	4,300	-	4,300	-	-	-	Sep 29 2006	-	1M WIBOR + bank's margin	Mortgage, promissory note, pledge, assignments by way of security
ING Bank Śląski S.A.	Krosno branch	4,500	-	1,500	-	-	-	Sep 30 2006		1M WIBOR + bank's margin	Pledge on inventories and property, plant and equipment
PKO BP S.A.	Krosno branch	7,000	-	6,798	-	-	-	Jul 29 2006	-	1M WIBOR + bank's margin	Mortgage, promissory note
ING Bank Śląski S.A.	Warsaw	30,000	-	29,408	-	-	-	Aug 8 2006	-	1M WIBOR + bank's margin	Mortgage, assignments by way of security, pledge
PKO BP S.A.	Krosno branch	4,500	-	1,353	-	2,809	-	Oct 10 2006	Dec 31 2008	1M WIBOR + bank's margin	Assignment of receivables by way of security and mortgage
NFOŚiGW	Warsaw	15,000	-	2,000	-	11,550	-	Sep 30 2006	Sep 30 2010	half of the bill rediscount rate	Surety
PeKaO S.A.	Krosno branch	500	-	88	-	-	-	Jun 30 2006	-	1M WIBOR + bank's margin	Assignment by way of security
ING Bank Śląski S.A.	Katowice	990	-	990	-	-	-	Sep 8 2006	-	1M WIBOR + bank's margin	Assignment by way of security, pledge on inventories
PeKaO S.A.	Warsaw	56,409	14,800 USD	7,454	2,286 USD	30,874	9,466 USD	Dec 31 2006	Feb 28 2011	1M LIBOR + bank's margin	Pledge on property, plant and equipment
Total				**111,452**	**2,286 USD**	**294,198**	**9,466 USD**				

The banks' margins on the contracted loans are in the range of 0.05% – 2.0%.

30. Provisions

PLN '000	Dec 31 2006	Dec 31 2005
Non-current provisions		
Provision for land reclamation	34,846	37,190
Length-of-service awards and retirement severance pays	54,232	49,771
Provision for the Offshore Oil Rig	92,517	77,198
Other provisions	26,487	27,643
Total non-current provisions	**208,082**	**191,802**
Current provisions		
Provision for land reclamation	5,476	3,142
Length-of-service awards and retirement severance pays	7,472	12,751
Provision for the Offshore Oil Rig	2,400	2,400
Other provisions	65,231	61,367
Total current provisions	**80,579**	**79,660**
Total	**288,661**	**271,462**

Computation of the provisions for employee benefits as at December 31st 2006 was based on the following assumptions:
- the long-term annual growth rate of remuneration is 3.4% for 2007 and 1.8% for subsequent years;
- the discount rate for future payments of employee benefits is 5.0% (i.e. it equals the return on the safest long-term securities traded on the Polish capital market as at December 20th 2006);
- the probability of employee attrition is based on the historical data on employee turnover at the Group and statistical data on employee attrition in the industry;
- the adopted mortality and life expectancy ratios are based on the Life Expectancy Tables of Poland for 2005 published by the Polish Central Statistics Office (GUS) and assume that the Group's employee population is representative of the average Polish population in terms of mortality;
- it is assumed that the Group employees will retire according to the standard system, i.e. men – after reaching the age of 65, women – after reaching the age of 60, except for those employees who, based on the information provided by the companies, meet the conditions for early retirement.

Computation of the provisions for employee benefits as at December 31st 2005 was based on the following assumptions:
- the long-term annual remuneration growth rate is 1.8% (i.e. it equals the long-term annual inflation rate expected as at the balance-sheet date);
- discount rate for future payments of the benefits is 5.1% (i.e. it equals the return on the safest long-term securities traded on the Polish capital market as at the balance-sheet date);
- the probability of employee attrition is based on the data submitted by the Group companies on employee turnover in 2001–2005;
- the adopted mortality and life expectancy ratios are based on the Life Expectancy Tables of Poland for 2004 published by the Polish Central Statistics Office (GUS) and assume that the Group's employee population is representative of the average Polish population in terms of mortality;
- it is assumed that the Group employees will retire according to the standard system, i.e. men – after their 65th birthday, women – after the 60th birthday, except for those employees who, based on the information provided by the Group companies, meet the conditions necessary to retire early.

The changes in provisions were as follows:

PLN '000	Provision for land reclamation (1)	Length-of-service awards and retirement severance pays	Provision for the Offshore Oil Rig (2)	Other provisions*	Total
As at Jan 1 2005	**2,050**	**44,045**	**-**	**51,497**	**97,592**
Increase	39,915	30,342	82,026	63,241	215,524
Decrease	(1,633)	(11,865)	(2,428)	(25,728)	(41,654)
As at Dec 31 2005	**40,332**	**62,522**	**79,598**	**89,010**	**271,462**
As at Jan 1 2006	**40,332**	**62,522**	**79,598**	**89,010**	**271,462**
Increase	2,904	10,491	17,640	32,835	63,870
Decrease	(2,914)	(11,309)	(2,321)	(30,127)	(46,671)
As at Dec 31 2006	**40,322**	**61,704**	**94,917**	**91,718**	**288,661**

(1) The provision relates mainly to the cost of liquidation of process waste (PLN 14,194 thousand), reclamation of land related to the DRW-100, DRW-600, Furfurol and ABT units (PLN 19,650 thousand) and the cost of liquidation and disposal of assets, including the recovery of assets (PLN 5,351 thousand) at Lotos Czechowice S.A.

(2) As at December 31st 2006, the Management Board of Petrobaltic S.A. analysed the costs needed to be incurred to liquidate the Offshore Oil Rig in the B-3 mining area, which was also used in the previous years, and in the B-8 mining area, where the trial production operations commenced in 2006. As a result of the analysis, it was found that the costs necessary to be incurred in future on the liquidation of the Offshore Oil Rig in the B-3 mining area increased relative to the value of the provision created for this purpose and presented in the balance sheet as at December 31st 2005. The increase amounted to PLN 9,872 thousand and reflected both the changes in the expected expenses due to price changes, and the lapse of time and the related change in the time value of money. The change in the time value of money was determined by applying a 5% discount rate to the value of the provision for the liquidation of the Offshore Oil Rig as at December 31st 2005 (PLN 79,570 thousand).

The amount so computed, i.e. PLN 3,978 thousand, was charged to financial expenses for 2006, while the remaining balance, i.e. PLN 5,895 thousand, increased the value of the relevant asset related to the provision for the liquidation of the rig, in accordance with IFRIC 1.

The value of the provision created for the first time in connection with the launch of production activities in the B-8 mining area amounted to PLN 7,767 thousand. The Parent Undertaking created a relevant provision for reclamation in the above amount and an asset with the value equal to the amount of that provision.

(*)The item "Other provisions" includes the following items:

PLN '000	Provision for RN Glimar[1]	Provision for Energobaltic[2]	Provision for interest to the state budget	Other	Total
As at Jan 1 2005	41,107	-	-	10,390	51,497
Increase	-	24,188	3,416	35,637	63,241
Decrease	-	-	-	(25,728)	(25,728)
As at Dec 31 2005	41,107	24,188	3,416	20,299	89,010
As at Jan 1 2006	41,107	24,188	3,416	20,299	89,010
Increase	-	-	-	32,835	32,835
Decrease	-	-	(3,416)	(26,711)	(30,127)
As at Dec 31 2006	41,107	24,188	-	26,423	91,718

[1] Grupa LOTOS S.A. and Rafineria Nafty Glimar S.A. signed loan agreements for the financing of operating and investing activities, including, in particular, the Glimar Hydrocomplex investment project, for an aggregate amount of PLN 90m. By December 31st 2004, Grupa LOTOS S.A. had advanced PLN 48m to Rafineria Nafty Glimar S.A. under these agreements. On January 19th 2005, the District Court of Nowy Sącz declared Rafineria Nafty Glimar S.A. of Gorlice bankrupt. As at December 31st 2006 and December 31st 2005, the assets under the loans advanced were fully covered by an allowance. As at the above dates, the Company also created a provision for the remaining receivables under these agreements.

[2] In 2001, Petrobaltic S.A. advanced a loan to Energobaltic Sp. z o.o., an associated company. Pursuant to the shareholders agreement ("the Shareholders Agreement"), Petrobaltic S.A. is obliged to offer to the other shareholder and lender of Energobaltic Sp. z o.o., that is Rolls-Royce Power Ventures (Władysławowo) Limited ("RRPV") to purchase the claims under the loan advanced by RRPV to Energobaltic in the event that the aggregate amount of waste gas supplied by Petrobaltic S.A. to Energobaltic Sp. z o.o. in 2005 is lower than the minimum offtake amount provided for in the Gas Supply Agreement for that year.

31. Liabilities, Accruals and Deferred Income

PLN '000	Dec 31 2006	Dec 31 2005
Trade payables, including:	738,696	844,341
to related undertakings	993	3,270
Tax and social security payable, including: [1]	511,674	319,236
- income tax	3,413	65,302
Special accounts	10,853	8,182
Salaries and wages payable	16,771	7,432
Accrued expenses	40,227	32,615
Deferred income under subsidies	16,560	13,144
Investment liabilities	38,498	39,412
to related undertakings	603	1,953
Other liabilities, including:	11,827	9,157
to related undertakings	1,001	871
Total	**1,385,106**	**1,273,519**

[1] The value of tax liabilities was reduced by the fuel charge of PLN 14,759 thousand incurred in relation to imported diesel oil. Grupa LOTOS S.A. will apply to the relevant customs office for reimbursement of the amount, which in the Company's opinion is recoverable.

Transactions with related undertaking are described in Note 44. Trade payables do not bear interest and are, as a rule, settled on a 7-30 day basis. Other liabilities do not bear interest, and their average payment period is three months. The amount resulting from the difference between VAT receivable and VAT payable is paid to the relevant tax authorities on a monthly basis. Interest payable is usually settled on a monthly basis during a financial year.

Pursuant to Art. 4.1.2. of the Excise Tax Act of January 23rd 2004 (Dz. U. No. 29, item 257, of February 26th 2004), a tax liability arises e.g. at the moment of taking harmonised excise goods out of a bonded warehouse. The Parent Undertaking and some other Group companies operate registered bonded warehouses, in which harmonised excise goods are subject to suspended-excise-tax procedure and may be the object of the actions provided for in the Excise Tax Act.

The Act on Employee Benefits Fund of March 4th 1994, as amended, stipulates that each employer of more than 20 staff (in full-time job equivalents) should create the Social Benefits Fund. In accordance with the statute and internal rules of procedure, the Group creates such fund and makes regular contributions to it, which are charged to costs. The purpose of the Social Benefits Fund is to subsidise social activities of the Group companies, finance loans to employees and other social spending.

The table below sets forth the Company's Social Benefits Fund's assets and liabilities.

PLN '000	Dec 31 2006	Dec 31 2005
Assets related to the Company's Social Benefits Fund		
Cash in separate bank account of the Company's Social Benefits Fund	2,982	2,770
Receivables from employees under the Company's Social Benefits Fund	5,626	6,662
Other	251	152
Total	8,859	9,584
Liabilities related to the Company's Social Benefits Fund		
Liabilities under the Company's Social Benefits Fund	8,816	9,146
Other	43	438
Total	8,859	9,584

32. Sales Revenue

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Sales of products	17,873,077	12,934,840
Sales of services	79,920	59,937
Total sales of products	17,952,997	12,994,777
Sales of goods for resale	390,739	850,819
Sales of materials	8,033	2,823
Total sales of goods for resale and materials	398,772	853,642
Total	**18,351,769**	**13,848,419**
- including to related undertakings	10,848	9,756
Elimination of excise tax and fuel charge	(5,540,886)	(4,202,874)
Total	**12,810,883**	**9,645,545**

The transactions with associated undertakings are presented in Note 44 to the financial statements.

33. Cost by Type

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Depreciation and amortisation	297,356	263,290
Raw materials and energy used	10,174,024	7,308,386
Contracted services	642,037	500,787
Taxes and charges	82,970	65,750
Salaries and wages	306,960	274,593
Social security and other benefits	103,658	81,627
Other costs by type	108,236	105,150
Goods for resale and materials sold	303,486	640,545
Total	**12,018,727**	**9,240,128**
Adjustments:		
Change in products and adjustments in cost of sales	(48,450)	(410,938)
Total operating expenses, including:	**11,970,277**	**8,829,190**
Cost of sales	10,987,999	8,053,554
Selling costs	666,177	501,650
General and administrative expenses	316,101	273,986

34. Other Operating Income

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Gain on disposal of property, plant and equipment	7,050	4,335
Subsidies	634	732
Release of provisions	942	3,513
Reversal of valuation allowance for receivables	6,617	9,349
Compensation received	5,639	4,020
Other operating income	7,217	13,696
Total	**28,099**	**35,645**

35. Other Operating Expenses

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Loss on disposal of property, plant and equipment	380	54
Revaluation of non-financial assets	30,645	24,258
Created provisions	12,205	4,048
Other operating expenses	27,129	20,358
Total	**70,359**	**48,718**

36. Net Financial Income and Expenses

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Dividend received	2,527	581
Interest	31,693	25,071
Foreign exchange gains	34,943	20,247
Gains on disposal of investments	7,540	16,078
Settlement of derivatives	53,739	12,805
Other	2,853	960
Total financial income	**133,295**	**75,742**
Interest	(30,324)	(29,021)
Foreign exchange losses	(392)	(1,796)
Loss on disposal of investments	-	(50)
Revaluation of financial assets	(5,322)	(14,423)
Other	(5,523)	(7,267)
Total financial expenses	**(41,561)**	**(52,557)**
Net financial income (expenses)	**91,734**	**23,185**

37. Corporate Income Tax

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Corporate income tax	204,316	208,496
Deferred tax	(23,077)	(39,681)
	=========	=========
Total tax	181,239	168,815
	=========	=========

The current portion of the income tax was calculated at the rate of 19% on the tax base.

The difference between the tax amount disclosed in the profit income statement and the amount calculated by applying the tax rate to pre-tax profit results from the following items:

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Income before tax	912,491	1,137,654
Corporate income tax at the applicable rate (19% in 2006 and 2005)	173,373	216,154
	---------	---------
Permanent differences, including:	41,397	(249,154)
Excess of net assets' fair value over acquisition cost	-	(266,625)
Share in investments in associated undertakings	(25,811)	(28,472)
Other permanent differences	67,208	45,943
	---------	---------
Tax effect of differences	7,866	(47,339)
	---------	---------
Corporate income tax	181,239	168,815
Effective tax rate	0.20	0.15

As at December 31st 2006 and December 31st 2005, the net deferred tax liability comprises the following items:

PLN '000	Dec 31 2006	Dec 31 2005
Deferred tax asset:		
Provision for employee benefits	10,361	9,612
Difference between current tax value and book value of fixed assets	1,706	1,835
Valuation allowance for inventories	4,424	2,491
Foreign exchange losses on foreign-currency settlements	2,009	1,460
Tax loss amortised over time	21	457
Valuation allowance for accounts receivable	13,982	11,899
Unrealised margin assets	15,496	11,551
Other	27,345	16,323
Total deferred tax asset	**75,344**	**55,628**
Deferred tax liability:		
Difference between current tax value and book value of tangible assets	241,018	244,774
Positive valuation of foreign-currency settlements	-	-
Positive valuation of derivatives	36	1,012
Other	3,297	1,926
Total deferred tax liability	**244,351**	**247,712**
Net deferred tax asset/(liability)	**(169,007)**	**(192,084)**

Since the Group companies are separate taxpayers, deferred tax asset and deferred tax liability are calculated at each company individually.

Consequently, consolidated balance-sheets present deferred tax assets and liabilities as follows:

PLN '000	Dec 31 2006	Dec 31 2005
Deferred tax asset:	32,057	26,593
Deferred tax liability:	(201,064)	(218,677)
Net deferred tax asset/(liability)	**(169,007)**	**(192,084)**

Taxable temporary differences are expected to expire in 2007–2084.

38. Contingent and Off-Balance-Sheet Liabilities

Material Contingent and Off-Balance-Sheet Liabilities of Grupa LOTOS S.A.

Surety Agreement of February 9th 2004 Concluded with the National Fund for Environmental Protection and Water Management

Under the agreement, the Company issued an irrevocable surety to repay the loan contracted by Rafineria Jasło S.A. (currently LOTOS Jasło S.A.) from the National Fund for Environmental Protection and Water Management under a loan agreement of December 10th 2003. The surety covers the loan amount of up to PLN 15,000 thousand. In connection with the surety agreement, on February 6th 2004 Rafineria Jasło S.A. (currently LOTOS Jasło S.A.) and the Company signed on securing the Company's interest with respect to the surety.

As at the date of these consolidated financial statements, the surety issued with respect to the loan, subject to annex of October 20th 2005, is a registered pledge on the plastics processing units with the net value of PLN 8,155 thousand, owned by LOTOS Jasło S.A. The pledge was established under the registered pledge agreement of February 18th 2004.

Irrespectively of the above, under the agreement Rafineria Jasło S.A. will seek to obtain a bank guarantee or surety to replace the surety issued by the Company. Should LOTOS Jasło S.A. breach the provisions of the agreement, it will pay the Company a contractual penalty in the amount of 10% of the surety; with the proviso that if the damage exceeds the contractual penalty, the Company is entitled to seek compensation for the total amount of the damage.

Material Liabilities of the Parent Undertaking under Promissory Notes

1. The validity of the blank promissory note of March 16th 2006 for PLN 200,000 thousand, issued to secure the Company's tax liability connected with the suspended excise tax collection procedure, was extended until June 16th 2008. The original validity term of the blank promissory note expired on March 16th 2007.

2. The validity of the blank promissory note of July 7th 2005 for PLN 200,000 thousand, issued to secure the Company's tax liability connected with the suspended excise tax collection procedure, was extended until July 7th 2007. The original validity term of the blank promissory note expired on July 7th 2006.

3. On July 4th 2006, at the request of Grupa LOTOS S.A., Bank Millennium S.A. issued a bank guarantee for the benefit of the Head of the Customs Chamber in Gdynia in order to secure liabilities towards the customs office, liabilities connected with tax and other charges that may arise in the period from July 4th 2006 to May 4th 2007, for the aggregate amount of up to PLN 160,000 thousand. The bank's commitment under the guarantee expire on July 3rd 2007.

4. On May 23rd 2005, at the request of Grupa LOTOS S.A., Bank PKO BP S.A. issued three performance bonds, for the amount of PLN 8.6m, for the benefit of the Military Property Agency (Agencja Mienia Wojskowego). On July 24th 2006 they were supplemented with another three guarantees for the total amount of PLN 20.06m. The total value of the guarantees is PLN 28,656 thousand. Their validity term expires on December 31st 2007.

5. On November 6th 2006, at the request of Grupa LOTOS S.A., Citibank Handlowy issued a bank guarantee in the form of a letter of credit for USD 74,998 thousand. The letter of credit was issued to secure a commercial transaction: payment for supplies of crude oil from Kuwait. The contingent liability related to the letter of credit expired on January 11th 2007.

6. On December 1st 2006, at the request of Grupa LOTOS S.A., Deutsche Bank Polska issued a bank guarantee in the form of a stand-by letter of credit for USD 12,000 thousand, for the benefit of Morgan Stanley Capital Group. The letter of credit was issued to secure a commercial transaction: payment for diesel oil. The contingent liability related to the letter of credit expired on January 31st 2007.

Material Contingent and Off-Balance-Sheet Liabilities of Petrobaltic S.A.

Liabilities to Bank Ochrony Środowiska S.A.

In connection with the loan advanced by Bank Ochrony Środowiska S.A. (the "Bank") to Energobaltic Sp. z o.o. (Energobaltic) under (i) the investment loan agreement of September 11th 2001, and (ii) the preferential investment loan agreement of September 11th 2001 concerning environmental protection, on December 12th 2001, Petrobaltic S.A. made a representation to the Bank whereby it agreed:

- to increase the share capital of Energobaltic Sp. z o.o. by an amount equal to the company's cumulative net loss incurred in the period from the abovementioned loan agreements date to the date of the first sale (confirmed by an invoice) of power from the CHP plant in Władysławowo (according to the Issuer's information, such sale was made on July 3rd 2003), if the loss exceeds 20% of Energobaltic's share capital;
- to apply a part of net profit (in the amount not exceeding the amount assumed in the Bank-approved final projection for the project financed with the loan) towards share capital increase in Energobaltic Sp. z o.o.;
- not to dispose of or encumber its shares in Energobaltic Sp. z o.o. without a prior consent of the Bank.

Liabilities to Rolls-Royce Power Ventures Limited (Władysławowo)

Under the Shareholder Agreement, in the event that the aggregate amount of waste gas supplied by Petrobaltic S.A. to Energobaltic Sp. z o.o. is lower than the minimum offtake amount provided for in the gas supply agreement for the year, Petrobaltic S.A. is obliged to offer to the other shareholder and lender of Energobaltic Sp. z o.o., that is Rolls-Royce Power Ventures (Władysławowo) Limited ("RRPV"), to purchase the claims under the loan advanced by RRPV to Energobaltic.

In connection with the expected reduction of the volume of waste gas supplied to Energobaltic Sp. z o.o. by Petrobaltic S.A. in 2005, on September 22nd 2005, RRPV sent a letter stating that if Petrobaltic S.A. did not comply with the provisions of Art. 16.1.6 of the Gas Supply Agreement, it would issue a default notice under Art. VIII Section 1 of the Shareholder Agreement.

Following receipt of the notice, under the Shareholder Agreement Petrobaltic is obliged to offer to RRPV to purchase the claims under the loan advanced by RRPV to Energobaltic. If RRPV accepts the offer, Petrobaltic will be obliged to gradually (2012–2016) purchase RRPV's claims under the loan, at maturity of each principal installment, at a 2% discount. As at December 31st 2006, the total amount of the loan advanced by RRPV to Energobaltic Sp. z o.o. was USD 6.1m (USD 5.1m in principal plus interest).

Following the purchase of RRPV's shares in Energobaltic Sp. z o.o., Petrobaltic S.A. would hold 1,598 shares representing 88.04% of the aggregate number of the shares.

As at today, no such notice has been issued. Therefore, as we were advised in an opinion issued by an external law firm, the conditional offer could be executed only in 2008 if Petrobaltic is in breach of the terms and conditions of the Gas Supply Agreement in 2007. However, in view of the poor financial standing of Energobaltic Sp. z o.o. and the level of gas supplies lower than expected as a result of delays in the commencement of production at the B8 reservoir, the Management Board of Petrobaltic S.A., guided by the conservative valuation principle, maintained the provision for future liabilities which might arise under the Shareholder Agreement. The provision covers the loan advanced by RRPV to Energobaltic Sp. z o.o. (less the 2% discount) and the par value of RRPV's shares in Energobaltic Sp. z o.o.

In the event that the aggregate amount of waste gas supplied by Petrobaltic S.A. to Energobaltic Sp. z o.o. in 2005 is lower than the minimum offtake amount provided for in the gas supply agreement for the year, Petrobaltic S.A. is obliged to offer to the other shareholder and lender of Energobaltic Sp. z o.o., that is Rolls-Royce Power Ventures (Władysławowo) Limited ("RRPV"), to purchase the claims under the loan advanced by RRPV to Energobaltic. If RRPV performs in accordance with the shareholder agreement, Petrobaltic S.A. may be obliged to gradually (2007–2011) purchase RRPV's claims under the loan at maturity of each principal instalment. If RRPV accepts Petrobaltic S.A.'s offer to purchase the claims, it will mean fulfilment of the condition precedent for RRPV's offer, made in 2001, to sell all the shares held by RRPV in Energobaltic at the time a default notice is served under the gas supply agreement. As at the date of these consolidated financial statements, no such notice was delivered. Any breach of the terms and conditions of the gas supply agreement in the following years entitles RRPV to issue such a notice within the timeframes provided for in the agreement. In view of the above, Petrobaltic S.A. created a provision of PLN 24,188 thousand related to the shareholder agreement and disclosed under other provisions (current portion).

Material Contingent and Off-Balance-Sheet Liabilities of LOTOS Jasło S.A.

Liabilities under Promissory Notes towards Nafta Polska S.A.

Rafineria Jasło S.A. (currently LOTOS Jasło S.A.) has issued nine blank promissory notes to Nafta Polska S.A. Under the promissory note declarations of January 19th 2000, the promissory notes secure the liabilities of the Rafineria Jasło S.A. under claims concerning environmental damage on the property specified in the agreement of January 19th 2000 between Rafineria Jasło S.A. and Carbon Black Polska Sp. z o.o. The promissory notes may be filled in by Nafta Polska if Rafineria Jasło S.A. fails to perform any of its obligations under the agreement. As provided for in the declarations, each promissory note may be filled in with up to PLN 1,000 thousand.

Under an agreement of January 19th 2000 between Nafta Polska S.A. and Rafineria Jasło S.A., if no obligation arises on the part of Nafta Polska S.A. to provide any performance, in whole or in part, under the performance bond agreement relating to the agreement on environmental issues with Carbon Black Polska Sp. z o.o. by the time Nafta Polska S.A. is removed from the enterprise register, Nafta Polska S.A. will place the unrealised promissory notes in court deposit so that they can be returned after the court's decision on removing Nafta Polska S.A. from the enterprise register becomes final. Similarly, the unrealised promissory notes will be returned to Rafineria Jasło S.A. after 10 years following the agreement date if Nafta Polska S.A. is not removed from the enterprise register and is not obliged to any performance under the surety agreement.

Liabilities under Promissory Notes towards the Minister of Economy

Rafineria Jasło S.A. (currently LOTOS Jasło S.A.) has also issued a blank promissory note to the Minister of Economy. Under the promissory note declaration issued on November 13th 2002, the promissory note is to secure performance of Rafineria Jasło S.A.'s obligations under an agreement on financial support for a new investment project, concluded between the Minister of Economy and Rafineria Jasło S.A. on November 1st 2002. The promissory note may be filled in with an amount of up to PLN 5,674 thousand.

Other Liabilities under Promissory Notes

Furthermore, as at December 31st 2006, LOTOS Jasło S.A. had a liability under a blank promissory note issued to secure a working capital overdraft facility granted by PKO BP S.A., the Krosno branch, for the amount of PLN 15,000 thousand, with the validity term expiring on July 28th 2011.

Other Contingent Liabilities of the Group

As at December 31st 2006 the Group's liabilities arising from the material agreements related to expenditure on property, plant and equipment (PKRT, FAME) amounted to PLN 699m.

39. Carbon Dioxide Emission Credits

As at December 31st 2006 the Group reported excess of carbon dioxide emission credits over the actual carbon dioxide emission.

40. Material Events Subsequent to the Balance-Sheet Date

1. On January 15th 2007, Grupa LOTOS S.A. disposed of 35 shares in Przedsiębiorstwo Projektowo-Usługowe BiproRaf Sp. z o.o. (PPU BiproRaf Sp. z o.o.) to KTI Poland S.A. of Warsaw. The shares, with the total par value of PLN 35 thousand, are equal and indivisible, and represent 50% of the share capital of PPU BiproRaf Sp. z o.o. Grupa LOTOS S.A. sold the shares for PLN 2,750 thousand. The transaction was executed as part of the programme aimed at streamlining the structure of the LOTOS Group.

2. On February 27th 2007, the Management Board of Grupa LOTOS S.A. signed the plan of merger of Grupa LOTOS S.A. and LOTOS Partner Sp. z o.o., prepared in accordance with Art. 499.1 of the Commercial Companies Code. The two companies will be merged pursuant to Art. 492.1.1 of the Commercial Companies Code, through the transfer of all assets of LOTOS Partner Sp. z o.o. to Grupa LOTOS S.A. As the acquirer holds 100% of shares in the acquired company, the merger will be executed pursuant to Art. 515.1 of the Commercial Companies Code, i.e. without increasing the share capital of Grupa LOTOS S.A. The merger is executed as part of the restructuring of the LOTOS Group, aimed at streamlining its organisational structure. The objective of the restructuring programme is to provide the LOTOS Group with more operating flexibility and facilitate quicker response to changes in the market environment. The merger of Grupa LOTOS S.A. and LOTOS Partner Sp. z o.o. is an element of the restructuring of the sales division within the entire LOTOS Group and should not have a material effect on the consolidated financial results of the LOTOS Group.

3. On March 26th 2007, LOTOS Mazowsze S.A. concluded a conditional preliminary agreement on the purchase of 34,500 shares in KRAK-GAZ Sp. z o.o. from natural persons. The conclusion of the final purchase agreement is conditional upon the Competition and Consumer Protection Office's approval of the business concentration involving the acquisition by LOTOS Mazowsze S.A. of control over KRAK-GAZ Sp. z o.o. by purchasing its shares. The shares, with a total par value of PLN 3,450 thousand, are equal and indivisible, and represent 100% of the share capital of KRAK-GAZ Sp. z o.o. The acquisition is deemed a long-term investment by LOTOS Mazowsze S.A. The shares were acquired for PLN 16,367.9 thousand, and the transaction was financed with LOTOS Mazowsze S.A.'s own financial resources. The core business of KRAK-GAZ Sp. z o.o. consists in wholesale and retail distribution of LPG. The acquisition of the equity interest in the company by LOTOS Mazowsze S.A. is part of Grupa LOTOS S.A.'s strategy aimed at increasing its share in the domestic LPG market.

4. On February 27th 2007, Grupa LOTOS S.A. executed an agreement on a loan of PLN 1,200 thousand to LOTOS Park Technologiczny Sp. z o.o. Under the terms of the agreement, the loan was to be disbursed in tranches. The first tranche of PLN 600 thousand was advanced on the agreement date, and the second one, also of PLN 600 thousand, on March 30th 2007. In accordance with the terms of the agreement, the loan is repayable in full by the end of 2007.

5. On March 30th 2007, the General Shareholders Meeting of UAB Naftos Gavyba approved the financial statements for 2006 and resolved to allocate the profit generated in 2006 and a portion of undistributed retained profits in the amount of LTL 100m to dividend payment.

6. On April 11th 2007, Grupa LOTOS S.A. and LOTOS Jasło S.A executed an agreement providing for the purchase of 700 shares of LOTOS Tank Sp. z o.o. The shares, with the total par value of PLN 350 thousand, are equal and indivisible, and represent 70% of the share capital of LOTOS Tank Sp. z o.o. Grupa LOTOS S.A. acquired the shares for PLN 642.5 thousand, using its own financial resources. As a result of the transaction, Grupa LOTOS S.A. holds 1,000 shares, representing 100% of LOTOS Tank Sp. z o.o.'s share capital. The shares were acquired by Grupa LOTOS S.A. in pursuance of its strategy. The acquisition is a part of the consistently implemented programme aimed at streamlining the structure of the LOTOS Group, and the programme for the restructuring of the Southern Refineries. The value of the assets purchased under the agreement as disclosed in the accounting books of LOTOS Jasło S.A. is PLN 355.2 thousand.

41. Material Court, Arbitration or Administrative Proceedings, Other Risks of the Parent Undertaking or Its Subsidiaries

Material Proceedings Pending before Public Administration Authorities in Connection with the Parent Undertaking's Business

On March 21st 2005, the President of the Competition and Consumer Protection Office issued a decision whereby anti-trust proceedings were instigated *ex officio* to investigate the issue of a suspected agreement between Polski Koncern Naftowy ORLEN S.A. of Płock and Grupa LOTOS S.A. of Gdańsk, concerning a simultaneous discontinuation of the production and distribution of the universal U95 gasoline. In the opinion of the Company's Management Board, given that in fact the production and sale of the U95 universal gasoline were not discontinued, the allegations of the Competition and Consumer Protection Office are unfounded. In April 2005, the Management Board motioned for issuing a decision to the effect that Grupa LOTOS S.A. has not been found to use competition-limiting practices.

In July 2005, the Parent Undertaking appealed to the Anti-Monopoly Court against the Competition and Consumer Protection Office's decision limiting access to a part of the evidence gathered in the case. Independent of the appeal, in September 2005, the Company filed another request with the Court to issue a decision to the effect that Grupa LOTOS S.A. does not use competition-liming practices. In October 2005 the Company received another decision of the Competition and Consumer Protection Office concerning limitation of access to a part of the evidence, against which the Company appealed to the Anti-Monopoly Court. The Regional Anti-Monopoly Court dismissed the appeals. The Parent Undertaking appealed to the Warsaw Court of Appeals against the Regional Anti-Monopoly Court's decisions, but these appeals were dismissed as well. The case is pending.

Material Proceedings Pending before Public Administration Authorities in Connection with the Business of LOTOS Czechowice S.A.

Tax Proceedings and Court and Administrative Proceedings Related to Taxes

Proceedings Related to the Value Added Tax for Certain Months of 1998
In connection with the tax inspections and the issued decisions related to the value added tax, on December 29th 2003 Rafineria Czechowice S.A. (currently LOTOS Czechowice S.A.) filed complaints with the Supreme Administrative Court against three decisions of the Director of the Tax Chamber of Katowice, concerning the value added tax for October 1998, July 1998 and May 1998. The total value of the disputed claims amounted to PLN 1,229 thousand. Decisions were issued in all of the above cases. Cassation complaints have been filed against all of the above decisions by Rafineria Czechowice S.A. (currently LOTOS Czechowice S.A.), in the case of the tax for July 1998, and by the Tax Chamber Director, in the case of the tax for October 1998, for July 1998 and for May 1998.
LOTOS Czechowice S.A. paid the amounts of VAT together with default interest. There is a possibility that as a result of the tax and court proceedings the amounts paid will be returned together with high interest.

In December 2005, LOTOS Czechowice S.A. received the following decisions of the Supreme Administrative Court:
- a decision repealing the decision of the Provincial Administrative Court issued in December 2004 (with respect to the tax for October 1998) in the part concerning determination of the tax liability, tax arrears and default interest; the above issues were submitted for re-examination to the Provincial Administrative Court, and with respect to other issues the cassation complaint was dismissed;
-a decision repealing the decision of the Provincial Administrative Court issued in December 2004 (with respect to the tax for May 1998) in the part concerning determination of the tax liability, tax arrears and default interest; the above issues were submitted for re-examination to the Provincial Administrative Court, and with respect to other issues the cassation complaint was dismissed;

- a decision upholding the decision of the Provincial Administrative Court issued in December 2004 (with respect to the tax for July 1998); the Supreme Administrative Court resolved not to award costs of cassation proceedings.

LOTOS Czechowice S.A. filed cassation complaints with the Supreme Administrative Court against rulings by the Provincial Administrative Court of Gliwice of April 27th 2006 in the following cases:
- the case relating to the tax for May 1998 (PLN 318 thousand),
- the case relating to the tax for October 1998 (PLN 618 thousand).

By virtue of decision of November 27th 2006, the Provincial Administrative Court of Gliwice dismissed the cassation complaint concerning the tax for October 1998.
The Provincial Administrative Court of Gliwice is considering the case of overpayment of VAT for August 1998 in the amount of PLN 292.7 thousand, without setting the date of the court hearing.
No negative tax consequences for LOTOS Czechowice S.A. may arise in connection with these proceedings; they may only be a source of additional income.

Proceedings Related to Excise Tax for Certain Months of 1998

As a result of the inspections carried out by the tax authorities, there are six tax proceedings pending against LOTOS Czechowice S.A., related to the decisions concerning excise tax for certain months of 1998, against which the LOTOS Czechowice S.A. submitted appeals to the administrative court. The total value of the disputed claims under appeal proceedings is PLN 2,881 thousand.
The Supreme Administrative Court set October 26th 2005 as the date for the court hearing concerning excise tax for September 1998, August 1998 and June 1998. By virtue of the Supreme Administrative Court's ruling, the Provincial Administrative Court's decision regarding excise tax for September 1998, August 1998 and June 1998 was reversed in whole and remanded for reconsideration.
LOTOS Czechowice S.A. paid the amounts of excise tax together with default interest. There is a possibility that as a result of the tax and court proceedings the amounts paid will be returned together with high interest

LOTOS Czechowice S.A. filed cassation complaints with the Supreme Administrative Court against decisions by the Provincial Administrative Court of Gliwice of April 27th 2006 in the following cases:
- the case relating to the tax for September 1998 (PLN 52.5 thousand),
- the case relating to the tax for August 1998 (PLN 842 thousand),
- the case relating to the tax for June 1998 (PLN 468.8 thousand),

Considering the case of the tax for October 1998 in the amount of PLN 1,138.8 thousand, the Provincial Administrative Court of Gliwice suspended the proceedings.
No negative tax consequences for LOTOS Czechowice S.A. may arise in connection with these proceedings; they may only be a source of additional income.
By virtue of the Provincial Administrative Court's decision of October 16th 2006 issued in the proceedings regarding the tax for August 1998 (with respect to the request for returning the difference between the court fee actually paid and the court fee due), the Provincial Administrative Court decided to return PLN 57.9 thousand to LOTOS Czechowice S.A..

Proceedings Related to Excise Tax for Certain Months of 2000 and 2001

By virtue of its decisions of December 7th 2004, the Head of the Customs Office of Bielsko-Biała instigated ex *officio* two proceedings with respect to Rafineria Czechowice S.A. (currently LOTOS Czechowice) in order to determine the amount of excise tax liability, and reopened seven proceedings in order to determine the excise tax liability for March. The proceedings were closed – on March 31st 2005, the Head of the Customs Office issued a decision under which Rafineria Czechowice S.A. (currently LOTOS Czechowice S.A.) paid its tax arrears (plus interest) in the amount of PLN 273 thousand.

Proceedings Related to Corporate Income Tax for 1999

On January 21st 2005, LOTOS Czechowice S.A. received from the Head of the Second Tax Office of the Katowice Province in Bielsko-Biała a decision of January 19th 2005, on instigation ex officio of tax proceedings related to the 1999 corporate income tax. On June 20th 2005, the Head of the Second Tax Office of the

Katowice Province issued a decision closing the proceedings. On July 15th 2005, PLN 856 thousand was transferred to the bank account of LOTOS Czechowice S.A. as payment under the challenged decision. In July 2005 LOTOS Czechowice S.A. appealed against the decision, as a result of which the amount to be reimbursed may be increased by approximately PLN 241 thousand. On September 15th 2005, LOTOS Czechowice S.A. was notified that the appeal would be dealt with by November 18th 2005.

On November 2nd 2005, LOTOS Czechowice S.A. submitted a request for the prolongation of the time allowed for presenting its position with respect to the evidence gathered in the case up until November 10th 2005. On November 21st 2005, LOTOS Czechowice S.A. received a decision of the Director of the Tax Chamber, dated November 18th 2005, upholding the challenged decision issued by the first instance authority. On December 21st 2005, LOTOS Czechowice S.A. filed a complaint against the decision issued by the Director of the Tax Chamber of Katowice on November 18th 2005. The value of the disputed claims was PLN 282,932. In February 2006, LOTOS Czechowice S.A. received from the Provincial Administrative Court of Gliwice a letter of the Director of the Tax Chamber, dated January 19th 2006, in which he requested that the Czechowice Refinery's appeal be dismissed.

By virtue of its decision I SA/GI 125/06 of June 9th 2006, the Provincial Administrative Court of Gliwice reversed the decision appealed against and awarded the return of the costs of proceedings in the amount of PLN 9.6 thousand for the benefit of LOTOS Czechowice S.A. from the Director of the Tax Chamber of Katowice.

The decision of the Director of the Tax Chamber of Katowice of March 13th 2007 reversed the decision of the Head of the Second Tax Office of the Katowice Province in Bielsko-Biała and determined the return of PLN 241.5 thousand for the benefit of LOTOS Czechowice S.A..

Inspection Related to Corporate Income Tax for 2000

On July 25th 2006, LOTOS Czechowice S.A. received from the Head of the Second Tax Office of the Katowice Province in Bielsko-Biała an authorisation for a tax inspection, dated July 24th 2006, concerning corporate income tax for 2000. In August 2006, LOTOS Czechowice S.A. received the post-inspection report. LOTOS Czechowice S.A. submitted its explanations and objections to the report in September 2006. On September 29th 2006, LOTOS Czechowice received decisions issued by the Head of the Second Tax Office for the Katowice Province in Bielsko-Biała concerning the institution, *ex offfcio*, of tax proceedings for the determination of corporate income tax liability for 2000 and interest on the tax arrears. By virtue of the decision of December 12th 2006 issued by the Head of the Second Tax Office for the Katowice Province in Bielsko-Biała, the 2000 corporate income tax liability was increased by PLN 31 thousand. LOTOS Czechowice S.A. paid the amount along with due interest.

Inspection Related to Excise Tax for Certain Months of 2004

The Head of the Customs Office of Bielsko-Biała conducted an inspection at LOTOS Czechowice S.A. in order to determine the correct amount of the excise tax payable for the period January 1st 2004 – September 30th 2004. As a result of the inspection, tax proceedings were instigated *ex officio* on May 18th 2005. On May 5th 2006, LOTOS Czechowice S.A. received four decisions issued by the Head of the Customs Office of Bielsko-Biała, determining the amount of excise tax liability for January, February, and March 2004. The proceedings concerning determination of the amount of excise tax liability for April 2004 were discontinued. On May 19th 2006, the company appealed to the Director of the Customs Chamber against the abovementioned decisions and filed motions for suspending their execution. In August 2006, LOTOS Czechowice S.A. received decisions issued by the Head of the Customs Office and discontinuing the proceedings concerning the tax liability for May–September 2004. On October 17th 2006, LOTOS Czechowice S.A. received a decision issued by the Director of the Customs Chamber of Katowice and setting December 13th 2006 as the deadline for the examination of the appeals against the decisions issued by the Head of the Customs Office of Bielsko-Biała, determining the amount of excise tax liability for January, February, and March 2004. In the decision of February 9th 2007, the Director of the Customs Chamber of Katowice set April 13th 2007 as the date for concluding the proceedings. As at the date of approval of these consolidated financial statements the issue was not resolved.

Proceedings Concerning Excise Tax Liabilities in the Period September 1st – December 31st 2003

On April 12th 2006, the Head of the Customs Office instigated proceedings to determine the correct amount of the excise tax payable for the period September 1st – December 31st 2003. Before conclusion of the proceedings, it is difficult to determine whether the excise tax liabilities will be reassessed, and if so, what their amounts will be. By virtue of his decision of March 19th 2006, the Head of the Customs Office in Bielsko-Biała set the deadline for the settlement of the matter at May 30th 2007.

In relation to the potential excise tax liabilities for the period September–December 2003 and January–March 2004, taking into account the conducted legal and tax analysis, including the analysis carried out by external tax advisers as well as an expert witness designated by the Head of the Customs Office, LOTOS Czechowice is of opinion that there is hardly any risk of unfavourable outcome of the dispute with the tax authorities, therefore no provisions were created in the financial statements with regard to these potential liabilities.

Material Proceedings Pending before Public Administration Authorities in Connection with Lotos Paliwa Sp. z o.o.'s Business

On March 30th 2006, LOTOS Paliwa Sp. z o.o received a decision of the Gdańsk Tax Office of March 28th 2006 relating to the determination of the value added tax liability for January 2005. Acting pursuant to Art. 109 of the Act on Value Added Tax of March 11th 2004 (Dz. U. No. 54, item 535, as amended), the Head of the Tax Office assessed an additional tax liability of the company, related to the settlement of the purchase of an organised part of business of LOTOS Mazowsze S.A. The financial statements of LOTOS Paliwa Sp. z o.o. for the year ended December 31st 2005 give no account of the effects of this event since the Management Board of the company appealed against the decision and believes that the appeal will be considered favourably for LOTOS Paliwa Sp. z o.o. On July 25th 2006, LOTOS Paliwa Sp. z o.o. received decision of the Head of the Gdańsk Tax Chamber, dated July 21st 2006, in which the Head of the Gdańsk Tax Chamber revoked in full the decision of the Gdańsk Tax Office determining the value added tax liability for January 2005 and assessing an additional tax liability, and remanded the case for re-examination by the Gdańsk Tax Office. The case will be settled in the first instance by April 30th 2007, as stated in the notice issued by the Head of the Gdańsk Tax Office concerning failure to settle the case by the set deadline, dated March 15th 2007.

The proceeding are pending in connection with the right to deduct VAT in relevant periods, arising from settlement of the acquisition of an organised part of LOTOS Mazowsze business, and in order to determine whether additional tax sanctions in this respect are compliant with the constitution. As a result of corrections, VAT was reimbursed to LOTOS Paliwa in the amount disclosed in the financial statements under liabilities under tax, duty, social security and other benefits payable.
As regards potential tax liabilities under sanctions connected with the settlement of acquisition of an organised part of LOTOS Mazowsze business and corrections related to the VAT-7 tax returns, taking into account the conducted legal and tax analysis, including the analysis carried out by external tax advisers, the Manageemnt Board of LOTOS Paliwa is of opinion that there is hardly any risk of unfavourable outcome of the dispute with the tax authorities, therefore no provisions were created in the financial statements with regard to these potential liabilities.

Material Proceedings Instigated against the Company.

Proceedings upon Action Brought by PETROECCO JV Sp. z o.o. for Compensation for Damages Incurred as a Result of Monopolistic Practices

On May 18th 2001, PETROECCO JV Sp. z o.o. brought an action against the Company whereby it seeks the courts' decision awarding an amount of PLN 6,975 thousand, together with statutory interest as at May 1st 1999, as compensation for damages incurred as a result of the Company's monopolistic practices, which involved selling BS base oils in a manner favouring some customers, whose orders were executed to a disproportionately higher extent than the orders of PETROECCO JV Sp. z o.o.

The alleged use of the monopolistic practices by the Company was confirmed by a decision of the Competition and Consumer Protection Office of September 26th 1996, in which the Authority ordered the Company to abandon such practices. The Company appealed against the decision. The Provincial Court of Warsaw – the Anti-Monopoly Court, changed, by virtue of its decision of October 22nd 1997, only the wording of the decision and ordered the Company to abandon monopolistic practices. The cassation complaint against this decision filed by the Company was dismissed by the Supreme Court by virtue of its decision of June 2nd 1999.
The Regional Court of Gdańsk, by virtue of its decision of December 21st 2002, dismissed the action for compensation, fully complying with the Company's objection referring to the statute of limitation. However, this decision was overruled on December 4th 2003 by the Gdańsk Court of Appeals, in case No. I ACa 824/03, and submitted for re-examination by the District Court of Gdańsk. The Court of Appeals found that the reference to the statute of limitation was not justified. According to the Court, it was only on June 2nd 1999 (the date of the Supreme Court's ruling) that PETROECCO JV Sp. z o.o. became aware that the damage it incurred resulted from monopolistic practices giving rise to the Company's liability in tort, and it is as of that date, in the Court's opinion, that the three-year period of limitation of compensation claims should be counted.

As at the date of these consolidated financial statements, the case is pending before the Regional Court of Gdańsk (First Instance Court) and its file No. is IX GC 134/04. The Company defends itself by raising substantive charges (it questions the fact that any damage was incurred by PETROECCO JV Sp. z o.o., the amount of the alleged damage, and the existence of the cause and effect relationship between the monopolistic practices and the damage). Following the hearing of June 2005, the Regional Court of Gdańsk ordered a court expert in accountancy and economics to draw up a report concerning the extent of damages which the plaintiff incurred as a result of Grupa LOTOS S.A.'s activities.

In its decision of July 2006, the Regional Court of Gdańsk requested a second expert witness opinion regarding the extent of losses suffered by the plaintiff due to Grupa LOTOS S.A.'s activities. In the issued opinion, the expert witness indicated that based on the materials presented by PETROECCO JV Sp. z o.o. it was impossible to establish the amount of the losses or even state whether the losses were actually incurred. Besides, the expert pointed out that an opinion should be requested from an expert witness in a field other than accountancy. The lack of evidence required to issue such an opinion prevented the plaintiff from causing the appointment of another expert witness. The hearing was held on March 27th 2007. The ruling was scheduled to be announced on April 10th 2007, then postponed until April 20th 2007.

Proceedings upon Action Brought by the Minister of State Treasury for Invalidation of the Share Purchase Agreement Concerning Shares in Naftoport Sp. z o.o.

On November 3rd 2005, Grupa LOTOS S.A. was served a nullity suit submitted by the Minister of State Treasury, concerning the agreement of August 18th 1998 between Grupa LOTOS S.A. and Polska Żegluga Morska, a state-owned company, concerning the sale of two shares in Naftoport Sp. z o.o., valued at PLN 3,340 thousand. On April 21st 2006, a ruling rejecting the claim in its entirety was passed. On June 8th 2006, the Minister of State Treasury appealed against a court ruling of April 21st 2006. On June 30th 2006, the Company filed its response to the appeal. On December 28th 2006, the Court of Appeals passed a ruling reversing the challenged decision of April 21st 2006 and declaring the agreement on the sale of two shares in Naftoport Sp. z o.o. as invalid. On April 6th 2007, the Company filed a cassation complaint and a request to arrest enforcement of the decision of the second instance.

Tax Settlements

Tax settlements and other regulated areas of activity (e.g. customs or foreign exchange control) are subject to inspection by competent administration authorities, which are authorised to impose high penalties and sanctions. As the legal regulations regarding these issues in Poland are relatively new, they are often ambiguous and inconsistent. Differences in the construction of tax legislation are frequent, both within governmental authorities and between those authorities and enterprises, leading to uncertainty and conflicts. Consequently, the tax-related risk in Poland is significantly higher than in countries where tax systems are better developed.

Tax settlements may be subject to tax inspection for a period of five years from the end of the calendar year in which the tax payment was made. As a result of such inspections, additional tax liabilities may be assessed with respect to the tax settlements made by the Company. In the Company's opinion, as at December 31st 2006, relevant provisions for identified and measurable tax risk have been created.

Court Proceedings Instigated by the Company or the Companies of Its Group

Court Proceedings Instigated by Rafineria Jasło S.A. (currently LOTOS Jasło S.A.) against a Private Individual

On December 4th 2003, the Regional Court of Krosno issued, in the course of binding advice procedure, a decision in favour of Rafineria Jasło S.A. (currently LOTOS Jasło S.A.), whereby it ordered payment of PLN 4,829 thousand, together with interest, representing claims under unpaid invoices for goods sold (file No. VIII GNc 292/03). The order for payment became final. Due to the fact that on April 2nd 2004 the debtor was declared bankrupt, with a possibility of concluding an arrangement, Rafineria Jasło S.A. (currently LOTOS Jasło S.A.) submitted to the judge-commissioner its claims in the total amount of PLN 7,668 thousand, including: (i) PLN 6,138 thousand – outstanding principal of the payment due for the goods sold; (ii) PLN 1,498 thousand – delayed payment interest; and (iii) PLN 32 thousand – costs of litigation before the Regional Court of Krosno related to the case. The claims of up to PLN 2,580 thousand, including the principal and interest, are not subject to the arrangement as they are secured on the bankruptcy estate by a security mortgage.

Material Proceedings Pending before the Competent Arbitration Court in Connection with the Activities of Petrobaltic S.A. and its Subsidiary

AB Geonafta, a subsidiary of Naftos Gavyba (hereinafter referred to as the Subsidiary) is a party to court proceedings against AB Svenska Petroleum Exploration (hereinafter referred to as SPE) related to the establishing of UAB Genciu Nafta, whose founders and shareholders are the Subsidiary and SPE. The litigation concerns applying the provisions of the Subsidiary's Articles of Association, and it was referred to the International Court of Arbitration at the International Chamber of Commerce (hereinafter referred to as the Arbitrator), which reached a final decision on October 30th 2003. The outcome of this case will remain unknown until the Arbitrator's award takes effect in the Lithuanian jurisdiction.

Once the Arbitrator's decision has been confirmed and allowed, the Subsidiary will bear the following costs:

a. The Subsidiary together with the Lithuanian government will reimburse SPE for the amount of USD 12,579 thousand along with interest calculated at the rate of 6% annually on that amount for the period from January 1st 2002 to the reimbursement date. If the Arbitrator's decision is confirmed in the Lithuanian jurisdiction, the Subsidiary will seek to have the Lithuanian government cover the liability in its entirety;
b. The Subsidiary shall reimburse SPE for the amount of USD 312 thousand to cover the costs of court proceedings.

Once the Arbitrator's decision has been confirmed and allowed, the Subsidiary will obtain the following sums:

a. SPE will reimburse the Subsidiary for the amount of USD 1,325 thousand along with interest calculated at the rate of 6% annually on that amount for the period from April 6th 2002 to the reimbursement date;
b. The Subsidiary will have the right to demand that the elected President of the Management Board and the Chief Executive Officer of UAB Genciu Nafta be the candidates put forward by the Subsidiary's representatives;
c. The Subsidiary will have the right to demand that its share in the profits from oil production by UAB Genciu Nafta be increased from 50% to 75%, with effect as of January 1st 2002;
d. The Subsidiary will have the right to demand that UAB Genciu Nafta repay the debt which it owes to the Subsidiary in the amount of LTL 664 thousand.

In 2004, dividend in the amount of LTL 5,973 thousand and an outstanding payment for deliveries and services

in the amount of LTL 885 thousand were allegedly remitted to the Subsidiary by UAB Minijos Nafta. The funds were blocked by a court enforcement officer in Copenhagen due to the claims filed by SPE against the Subsidiary. The subsidiary appealed against the court enforcement officer's decision to the Danish Supreme Court.
As at the date of these financial statements AB Geonafta has not settled the abovementioned payment and the amounts due in connection with the court proceedings, as their outcome remains unknown and will remain so until the Arbitrator's award takes effect in the Lithuanian jurisdiction. On July 1st 2005, UAB Minijos Nafta's liability towards AB Geonafta expired as AB Geonafta obtained both sums in the aggregate amount of LTL 6,858 thousand.

42. Remuneration of the Management Board and the Supervisory Board and Information on Loans and Other Similar Benefits Advanced to Members of the Parent Undertaking's Management and Supervisory Staff

The remuneration paid and payable to the members of the Management Board and the Supervisory Board of the Parent Undertaking was as follows:

PLN '000	Year ended Dec 31 2006	Year ended Dec 31 2005
Management Board	548	497
Supervisory Board	237	286
Management Board – subsidiary or associated undertakings	86	43
Total *	**871**	**826**

*The value of remuneration provides for changes in the composition of the Management and Supervisory Boards of Grupa LOTOS S.A. made during the reporting period.

Information on loans and similar benefits advanced to members of the management and supervisory staff:

PLN '000	Dec 31 2006	Dec 31 2005
Management Board	-	20
Total	-**	20*

*10- year loan from the Company Social Benefits Fund, bearing interest at 4% p.a.

** On June 19th 2006, the composition of the Management Board of Grupa Lotos S.A. changed. As at June 19th 2006, the value of advanced loans was PLN 18.5 thousand.

43. Employment Structure

Average employment by category:

	Year ended Dec 31 2006	Year ended Dec 31 2005
Blue-collar workers	3,320	3,146
White-collar workers	2,103	1,994
Total	5,423	5,140

44. Transactions with Related Undertakings

Transactions with related undertakings are executed on arms length terms.

(PLN '000)	Sales to related undertakings	Purchases from related undertakings	Receivables from related undertakings	Liabilities to related undertakings
	year ended Dec 31 2006	year ended Dec 31 2006	as at Dec 31 2006	as at Dec 31 2006
Associated undertakings valued with equity method	4,444	3,259	103	3,213
Non-consolidated undertakings	6,404	7,260	666	1,396
Total	**10,848**	**10,519**	**769**	**4,609**

In the period January 1st – December 31st 2006, the total income on sale of property, plant and equipment and intangible assets of the LOTOS Group to related undertakings was PLN 76 thousand.

In the period January 1st – December 31st 2006, the total value of property, plant and equipment and intangible assets purchased by the LOTOS Group from related undertakings was PLN 5,600 thousand.

Furthermore, during the 12 months ended December 31st 2006, a member of the Management Board of Grupa LOTOS S.A. sold, during ordinary trading sessions at the Warsaw Stock Exchange, a total of 42,755 shares of Grupa LOTOS S.A. for an average price of PLN 42.65 per share. The total value of the transactions amounted to PLN 1,823.5 thousand.

(PLN '000)	Sales to related undertakings	Purchases from related undertakings	Receivables from related undertakings	Liabilities to related undertakings
	year ended Dec 31 2005	year ended Dec 31 2005	as at Dec 31 2005	as at Dec 31 2005
Associated undertakings valued with equity method	4,887	3,907	229	1,440
Non-consolidated undertakings	4,869	17,253	319	4,654
Total	**9,756**	**21,160**	**548**	**6,094**

In the period January 1st – December 31st 2005, the total income on sale of property, plant and equipment and intangible assets of the LOTOS Group to related undertakings was PLN 31 thousand.

In the period January 1st – December 31st 2005, the total value of property, plant and equipment and intangible assets purchased by the LOTOS Group from related undertakings was PLN 7,791 thousand.

45. Entity with Significant Influence over the Group

As at December 31st 2006, Nafta Polska S.A. held a 51.91% stake in Grupa LOTOS S.A. Nafta Polska S.A. is controlled by the State Treasury, which, as at December 31st 2006, directly held a 6.93% stake in Grupa LOTOS S.A. As at December 31st 2006, the State Treasury held, directly and indirectly, 58.84% of shares in Grupa LOTOS S.A.

The aggregate value of transactions concluded between Grupa LOTOS S.A. and Nafta Polska during the year ended December 31st 2006 was PLN 7 thousand.

During the year ended December 31st 2005, apart from the transaction referred to in Note 16, the value of transactions between Grupa LOTOS S.A. and Nafta Polska S.A. amounted to PLN 23,932 thousand, including the dividend paid in the amount of PLN 11,805.

46. Other Information

The Act on Special Rights Vested in the State Treasury and How These Rights Should Be Exercised in Companies of Material Importance to Public Order or Safety ("strategic companies"), dated June 3rd 2005 (Dz.U. No. 132, item 1108) ("the Act") introduced the institution of observers on behalf of the State Treasury. Grupa LOTOS S.A. was included in the list of strategic companies referred to in Art. 8 of the Act, published in the Polish Council of Ministers' Regulation on the list of companies of material importance to public order or safety, dated December 13th 2005 (Dz.U. of December 29th 2005). The responsibility of the observers acting on behalf of the State Treasury at strategic companies is to monitor the operations of these companies regarding, among other things, the following issues:

- management of company assets of material importance to its operations,
- changes of the actual business profile, changes of the intended use or discontinuation of the use of a company's asset of material importance,
- adoption by the General Shareholders Meeting of resolutions concerning dissolution of the company, relocation of its registered office abroad, change of its business profile, sale or lease of its business or an organised part of its business, or encumbrance of the business or its organised part with limited property rights,

– if there is reasonable suspicion that such a legal action would violate public order or safety.

The assumptions of the state's policies concerning social or economic life spheres of material importance to public order or safety will be published in *Monitor Polski*.

The observers are authorised to request from companies any documents or explanations regarding the above issues, and, having analysed them, they are required to submit the obtained materials to the Minister of the State Treasury, together with their position expressed in writing and the statement of reasons.

The State Treasury Minister is required in certain cases, and in other cases he is authorised, to voice his objection to an action of a given strategic company of which he has been notified by the observers. Provided that it is not appealed against, such an objection renders a given legal action invalid as of the date on which it was performed.

Until the approval of these financial statements, Grupa LOTOS S.A. has received no statement on the appointment of an observer for the Company.

47. Signatures of the Management Board Members and the Person Responsible for Keeping the Accounting Books of Grupa LOTOS S.A.

President of the Management Board, CEO	 Paweł Olechnowicz
Vice-President of the Management Board, Chief Financial Officer	 Mariusz Machajewski
Vice-President of the Management Board, Chief Commercial Officer	 Jarosław Kryński
Vice-President of the Management Board, Production and Development Director	 Marek Sokołowski
Chief Accountant	 Tomasz Południewski