Grupa LOTOS S.A.

DIRECTORS’ REPORT ON THE OPERATIONS OF GRUPA LOTOS S.A.
IN 2010

This is a translation of a document originally issued in Polish
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I CORPORATE GOVERNANCE

1 RESPONSIBLE BUSINESS

1.1 PRINCIPLES OF RESPONSIBLE BUSINESS

Grupa LOTOS S.A.’s mission is to pursue innovative growth in the areas of oil production, oil processing and distribution of products which meet the most stringent quality standards, in a manner that is environmentally friendly, compliant with the energy security policy, guarantees full customer satisfaction, and ensures continuous development of employees and capitalisation on their capabilities.

Grupa LOTOS S.A. seeks to become the highest ranked oil company in the Baltic Sea region in terms of the quality of petroleum products, customer service and professional management.

The LOTOS Group's goal is to strive towards innovative and sustainable growth in the areas of:

- exploration for, production and processing of hydrocarbons,
- trading in top quality petroleum products,
- in order to ensure constant growth in shareholder value, guarantee full customer satisfaction, and

enable continuous development of employees and efficient use of their potential.

The objective is to be achieved:

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

The strategic objective of the Grupa LOTOS S.A. until 2015 is to create shareholder value by best leveraging its existing potential and implementing development programmes in three key business areas: exploration and production, oil refining and marketing.

Grupa LOTOS S.A.’s responsibility towards the society and towards the natural environment is the responsibility for delivering products in such a manner that does not lead to degradation of the natural environment or of social capital. The third pillar of the Group’s strategy is business responsibility for its products towards the state, the market, business partners, customers and employees. This forms an inherent part of the Group’s management strategy focusing on the growth of its value and through such growth generating definite benefits to the society and business in general.
1.2 CORPORATE GOVERNANCE PRINCIPLES APPLICABLE TO GRUPA LOTOS S.A.

As of July 1st 2010, Grupa LOTOS S.A. follows corporate governance principles contained in the document Best Practices for WSE Listed Companies, which was adopted by the Supervisory Board of the Warsaw Stock Exchange (WSE) on July 4th 2007 and revised on May 19th 2010.


On January 8th 2010, Grupa LOTOS S.A. gained access to Electronic Database (EBI) and may now disclose its Corporate Governance reports by electronic means, in accordance with Resolution 718/2009 of the Management Board of the Warsaw Stock Exchange dated December 16th 2009.

In 2010, Grupa LOTOS S.A. did not release any reports regarding non-compliance with the principles outlined in Best Practices for WSE Listed Companies.

On January 1st 2008, in connection with the coming into force of corporate governance principles set forth in Best Practices for WSE Listed Companies, and acting in accordance with the “comply or explain” rule and with Par. 29.3 of the WSE Rules, the Management Board of the Company reported that Grupa LOTOS S.A. did not apply the following corporate governance principles:

- **principle 1.11 contained in Section II**

“A company should operate a corporate website and publish: ... information known to the Management Board based on a statement by a member of the Supervisory Board on any relationship of a member of the Supervisory Board with a shareholder who holds shares representing no less than 5% of all votes at the company’s General Meeting.”

Grupa LOTOS S.A. does not comply with the principle as it holds no information on a possible relationship between Supervisory Board members and a shareholder who holds shares representing 5% or more of the total vote at the General Shareholders Meeting.

- **principle 6 contained in Section III**

“At least two members of the Supervisory Board should meet the criteria of being independent from the company and entities with significant connections with the company. The applicable independence criteria are contained in Annex II to the Commission Recommendation of February 15th 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board. Irrespective of the provisions of item b) of the said Annex, a person who is an employee of the company, or its subsidiary or associated company, cannot be deemed to meet the independence criteria described in the Annex. In addition, a relationship with a shareholder which precludes the independence of a member of
the Supervisory Board as understood in this principle is an actual and significant relationship with any shareholder who has the right to exercise at least 5% of all votes at the General Meeting.”

Grupa LOTOS S.A. does not comply with the principle as it has been notified of the independence of only one Supervisory Board member – Mr. Rafał Lorek. The Company will follow the principle after it has been notified that at least two independent members are appointed to the Supervisory Board or that at least two existing members are deemed independent, in accordance with Annex II to the Commission Recommendation of February 15th 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board.

principle 8 contained in Section III

“Annex I to the Commission Recommendation of February 15th 2005 on the role of non-executive or supervisory directors … should apply to the tasks and operation of the committees of the Supervisory Board.”

Grupa LOTOS S.A. does not comply with the principle due to the fact that it has no information regarding the independence of the members of the Supervisory Board who should serve on the existing Supervisory Board committees, as required by Annex I to the Commission Recommendation of February 15th 2005 on the role of non-executive or supervisory directors.

The Company will follow the principle after it has been notified that a proper number of members who meet the independence criteria have been appointed to the existing Supervisory Board committees, and that the tasks and operation of committees are consistent with the requirements set forth in Annex I to the Commission Recommendation of February 15th 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board.

1.3 NON-OBLIGATORY BEST PRACTICES IN CORPORATE GOVERNANCE

Grupa LOTOS S.A. takes steps to introduce best practices in such areas as environmental protection, health and safety at work and security of management systems, which have not been regulated by the Polish law.

Since November 19th 2009, Grupa LOTOS S.A. has been included in the first index of socially responsible companies in the CEE region, the RESPECT Index (Responsibility, Ecology, Sustainability, Participation, Environment, Community, Transparency), which includes 16 companies listed on the regulated market of the WSE and granted A rating as a result of being leaders in sustainable development, corporate disclosure and communication with the financial markets.
The RESPECT Index also takes into account the criteria of profitability related to dividend payments and pre-emptive rights, which provides insight into the economic standing of the companies included in the Index.

1.4  INTERNAL AUDIT AND RISK MANAGEMENT SYSTEMS IN THE PROCESS OF PREPARING FINANCIAL STATEMENTS

As prescribed by the Minister of Finance’s Regulation on current and periodic information to be published by issuers of securities and conditions for recognition as equivalent of information whose disclosure is required under the laws of a non-member state, dated February 19th 2009, the Management Board of Grupa LOTOS S.A. is responsible for the internal audit system and its effective functioning in the process of preparing financial statements.

The guidelines to be followed in the preparation, approval and publication of financial statements are laid down in “Rules for the Preparation, Approval and Publication of Annual, Semi-Annual and Quarterly Reports of the LOTOS Group”. In line with the existing procedure, preparation of consolidated and separate financial statements is overseen by Head of the Finance and Accounting Centre’s Office together with the person responsible for keeping the accounting books of the Parent Company (Chief Accountant). Responsibility for preparing the consolidated and separate financial statements lies with the Financial Reporting Office of the Parent Company.

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

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

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

2  SHAREHOLDER STRUCTURE

2.1  SHAREHOLDERS HOLDING SIGNIFICANT BLOCKS OF SHARES

At the Company’s request, on January 19th 2010 the National Depository for Securities assimilated 57,987,030 ordinary bearer shares in Grupa LOTOS S.A., created through a
conversion of 57,987,030 ordinary registered shares (code No.: PLLLOTOS00033), with 55,635,609 ordinary bearer shares in Grupa LOTOS S.A., code No.: PLLLOTOS00025. The assimilated shares were assigned code No.: PLLLOTOS00025. 113,622,639 shares in Grupa LOTOS S.A. were marked with code No. PLLLOTOS00025 and 77,361 shares were marked with code No. PLLLOTOS00033.

On April 12th 2010, the National Depository for Securities assimilated 8,250 ordinary bearer shares in Grupa LOTOS S.A., created through a conversion of 8,250 ordinary registered shares (code No. PLLLOTOS00033) effected on April 12th 2010, with 113,622,639 ordinary bearer shares in Grupa LOTOS S.A. (code No. PLLLOTOS00025). The assimilated shares were assigned code No.: PLLLOTOS00025.

As of December 31st 2010, 113,630,889 shares in Grupa LOTOS S.A. were marked with code No. PLLLOTOS00025, and 69,111 shares in Grupa LOTOS S.A. were marked with code No. PLLLOTOS00033.

On January 10th 2011, 16,173,362 Series C shares in Grupa LOTOS S.A. were registered with the National Depository for Securities under code No. PLLLOTOS00025. Following the registration, the total number of shares marked with ISIN code PLLLOTOS00025 was 129,804,251.

On January 22nd 2010, an aggregate of 14,000,000 ordinary bearer shares in Grupa LOTOS S.A. held by the State Treasury were sold in block transactions by the Ministry of State Treasury, through a securities account held at Bank Handlowy w Warszawie S.A. in accordance with orders placed on January 22nd 2010, concerning:

1) sale of 4,222,564 shares – orders accepted by Dom Maklerski Banku Handlowego S.A.,
2) sale of 3,162,425 shares – orders accepted by IPOPEMA Securities S.A.,
3) sale of 3,311,825 shares – orders accepted by Dom Inwestycyjny BRE Banku S.A.,
4) sale of 3,303,186 shares – orders accepted by ING SECURITIES.

Following the disposal of a significant block of shares representing 10.78% of Grupa LOTOS S.A.’s share capital, the State Treasury holds 69,076,392 ordinary bearer shares in Grupa LOTOS S.A., which represent 53.19% of the Company’s share capital.

To the Company’s knowledge based on the notifications received from the Shareholders, the shareholder structure of Grupa LOTOS S.A. as at December 31st 2010 was as follows:

<table>
<thead>
<tr>
<th>Shareholders</th>
<th>Number of shares</th>
<th>Number of votes</th>
<th>Par value of shares</th>
<th>% of share capital held</th>
</tr>
</thead>
<tbody>
<tr>
<td>State Treasury</td>
<td>69,076,392</td>
<td>69,076,392</td>
<td>69,076,392</td>
<td>53.19%</td>
</tr>
<tr>
<td>ING OFE</td>
<td>6,524,479</td>
<td>6,524,479</td>
<td>6,524,479</td>
<td>5.02%</td>
</tr>
<tr>
<td>Other shareholders</td>
<td>54,272,491</td>
<td>54,272,491</td>
<td>54,272,491</td>
<td>41.79%</td>
</tr>
<tr>
<td>Total</td>
<td>129,873,362</td>
<td>129,873,362</td>
<td>129,873,362</td>
<td>100.00%</td>
</tr>
</tbody>
</table>

On February 7th 2011, the Management Board of Grupa LOTOS S.A. received a notification to the effect that following a disposal of the Company shares, settled on February 2nd 2011, ING
Otwarty Fundusz Emerytalny reduced its share in the total vote at the Company's General Shareholders Meeting below the 5% threshold.

To the Company's knowledge, the shareholder structure of Grupa LOTOS S.A. as at the date of release of Grupa LOTOS S.A.’s Report for 2010, i.e. as at April 15th 2011, was as follows:

**Major shareholders holding 5% or more of Grupa LOTOS S.A.’s share capital as at the date of release of Grupa LOTOS S.A.’s Report for 2010**

<table>
<thead>
<tr>
<th>Shareholders</th>
<th>Number of shares</th>
<th>Number of votes</th>
<th>Par value of shares</th>
<th>% of share capital held</th>
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</thead>
<tbody>
<tr>
<td>State Treasury</td>
<td>69,076,392</td>
<td>69,076,392</td>
<td>69,076,392</td>
<td>53.19%</td>
</tr>
<tr>
<td>Other shareholders</td>
<td>60,796,970</td>
<td>60,796,970</td>
<td>60,796,970</td>
<td>46.81%</td>
</tr>
<tr>
<td>Total</td>
<td>129,873,362</td>
<td>129,873,362</td>
<td>129,873,362</td>
<td>100.00%</td>
</tr>
</tbody>
</table>

2.2 **HOLDERS OF SECURITIES WHICH CONFER SPECIAL CONTROL POWERS, ALONG WITH THE DESCRIPTION OF THE POWERS**

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

2.3 **LIMITATION OF VOTING RIGHTS**

One share in Grupa LOTOS S.A. confers the right to one vote at the General Shareholders Meeting, with the proviso that as long as the State Treasury or Nafta Polska S.A. holds the Company shares conferring the rights to at least one-fifth of the total vote at the General Shareholders Meeting, the rights of the Company shareholders are limited so that none of them can exercise at the General Shareholders Meeting more than one-fifth of the total number of votes at the Company as at the day of the General Shareholders Meeting. The limitation described in the preceding sentence does not apply to the State Treasury, Nafta Polska S.A., or their subsidiaries. The exercise of a voting right by a subsidiary is deemed as the exercise of that right by the parent company within the meaning of the Polish Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organised Trading, and Public Companies, dated July 29th 2005, with the reservation that a parent undertaking and a subsidiary are also understood as an undertaking whose votes conferred by the shares held (directly or indirectly) in the Company may be aggregated with the votes of other undertaking(s) in accordance with the provisions of the Public Offering Act concerning holding, disposal or acquisition of significant blocks of shares in the Company. A shareholder whose voting right was limited shall in each case retain the right to exercise at least one vote.
2.4 RESTRICTIONS ON TRANSFERABILITY OF THE SECURITIES

Grupa LOTOS S.A. did not issue any shares with restricted transferability.

3 THE COMPANY’S GOVERNING BODIES

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

Making amendments to the Articles of Association of Grupa LOTOS S.A. falls within the scope of powers of the General Shareholders Meeting and requires that a relevant resolution be adopted by the General Shareholders Meeting of the Company with absolute majority of votes.

After the General Shareholders Meeting adopts a resolution on amending the Company’s Articles of Association, the Management Board of Grupa LOTOS S.A. notifies a registry court of the amendments. An amendment to the Articles of Association takes effect upon being registered by the court.

Subsequently, the Supervisory Board compiles a consolidated text of the Articles of Association which incorporates the amendments, provided that the General Shareholders Meeting authorises the Supervisory Board to do so.

3.2 GENERAL SHAREHOLDERS MEETING OF GRUPA LOTOS S.A.

The General Shareholders Meeting of Grupa LOTOS S.A. operates in accordance with:
- the Articles of Association of Grupa LOTOS S.A. – consolidated text incorporating amendments introduced by Resolutions No. 24–32 and 34 of the Annual General Shareholders Meeting, dated June 30th 2009;

A General Shareholders Meeting takes place at the Company’s registered office and is convened by the Management Board of Grupa LOTOS S.A., as provided for in the Articles of Association or in the Commercial Companies Code, by publishing an announcement on the Company’s website and in the manner determined for publication of current reports, in accordance with the provisions of the Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organised Trading, and Public Companies. The announcement should be published at least twenty-six days before the date of the General Shareholders Meeting.
An Annual General Shareholders Meeting should be held no later than within six months after the end of the financial year. In 2010, the Annual General Shareholders Meeting was held on June 28th. The right to convene an Annual General Shareholders Meeting rests also with the Supervisory Board in the event that the Management Board fails to convene it within the specified time frame.

An Extraordinary General Shareholders Meeting is convened by the Management Board on its own initiative, by the Supervisory Board (if the Supervisory Board deems it appropriate), or by shareholders representing at least half of the Company’s share capital or at least half of the total vote at the Company.

Moreover, a shareholder or shareholders representing at least one-twentieth of the share capital may demand that an Extraordinary General Shareholders Meeting be convened, and that particular items be placed on the agenda of the Extraordinary General Shareholders Meeting. Any such requests must be made in writing or in electronic form and submitted to the Management Board. If an Extraordinary General Shareholders Meeting is not convened within two weeks of the submission of such a request to the Management Board, the Registry Court may authorise the requesting shareholders to convene the Extraordinary General Shareholders Meeting. A request to convene a General Shareholders Meeting and include particular items on its agenda, made by parties entitled to do so, should be presented with grounds. The Supervisory Board, or the shareholder or shareholders demanding that an Extraordinary General Shareholders Meeting be convened, are obliged to provide the Management Board with draft resolutions proposed for adoption together with written grounds for the demand to convene the Meeting, early enough to enable inclusion of the draft resolutions on the agenda, in accordance with the Commercial Companies Code. The Management Board is obliged to announce alterations to the agenda introduced at shareholders’ request immediately, and in any event not later than eighteen days prior to the scheduled date of the General Shareholders Meeting. The announcement shall be made in the same manner in which the convening of the General Shareholders Meeting is announced. A General Meeting convened upon a shareholders’ request should be held on the date given in the request and, if this date cannot be kept, on the nearest date that would allow the General Shareholders Meeting to consider the matters on its agenda.

A shareholder or shareholders representing at least one-twentieth of the Company’s share capital may, prior to a General Shareholders Meeting, provide the Company with draft resolutions concerning the matters which have been or are to be included in the Meeting’s agenda, with grounds for proposing such items presented in writing or by electronic means. The Company will immediately publish such draft resolutions along with written grounds on its website.

Only persons who are the Company shareholders sixteen days prior to the date of a General Shareholders Meeting (i.e. on the date of registration of participation in the General Shareholders Meeting) are entitled to participate in the General Shareholders Meeting. Holders of rights under registered shares or provisional certificates (świadectwa tymczasowe) as well as pledgees and usufructuaries holding voting rights are entitled to participate in the General Shareholders Meeting provided that they are entered in the Share Register on the registration date. The list of shareholders entitled to participate in a General Shareholders Meeting is prepared and signed by the Management Board.
A Shareholder may participate in a General Shareholders Meeting and exercise voting rights in person or by proxy. A power of proxy to participate in a General Shareholders Meeting and exercise voting rights must be in a written or electronic form (the latter does not require an electronic signature verified with a valid qualifying certificate). If the person acting as a proxy is a Management Board member, a Supervisory Board member, a liquidator, an employee of the Company or a member of the governing bodies or an employee of a subsidiary or cooperative of the company, the powers of proxy may authorise the holder to represent the shareholder at one General Shareholders Meeting only. The proxy is obliged to disclose to the shareholder the circumstances suggesting an actual or potential conflict of interests and must vote in accordance with the voting instructions of the appointing shareholder. Proxies are also obliged to disclose their status while registering their participation in a General Shareholders Meeting, prior to the receipt of the voting card. Information on the Proxy’s status is entered in the attendance roll.

Any matter to be discussed at a General Shareholders Meeting is subject to prior consideration by the Supervisory Board. No resolution may be adopted on matters not included in the agenda of the General Shareholders Meeting, unless the Company’s entire share capital is represented at the Meeting and no objections to the adoption of such resolution are raised by any of the persons participating in the Meeting, with the exception of motions to convene an Extraordinary General Shareholders Meeting and procedural motions. The General Shareholders Meeting adopts resolutions by absolute majority of votes, unless the Articles of Association or the Commercial Companies Code provide otherwise. Votes are cast in an open ballot. However, a secret ballot is ordered during elections and in the case of motions to dismiss a member of a governing body of the Company or its liquidator, or to hold them liable, motions concerning personnel-related matters, as well as in situations where at least one shareholder so demands.

Resolutions and proceedings of a General Shareholders Meeting are recorded by a notary public. The minutes should include information on the validity of the Meeting, its capacity to adopt resolutions, resolutions adopted, number of votes cast in favour of each resolution and objections. Evidence of convening the Meeting, along with the names and signatures of persons participating in the Meeting, should be enclosed with the minutes. The minutes are signed by the Chairperson of the General Shareholders Meeting and the notary public, and their copy is stored in the minutes archive at the Company’s registered office.

According to the Articles of Association of Grupa LOTOS S.A., the powers of the General Shareholders Meeting include in particular:

1. Reviewing and approving of the annual financial statements of the Company, the annual Directors’ Report on the Company’s operations, as well as the consolidated financial statements of the Group and the Directors’ Report on the Group’s operations, for the previous financial year,

2. Granting discharge to members of the Supervisory and Management Boards in respect of their duties,

3. Making decisions with respect to profit distribution or coverage of loss, as well as on the use of funds/special accounts created out of profits, subject to specific regulations which provide for a different use of such funds/special accounts,

4. Appointing and removing Supervisory Board members and defining rules of their remuneration,
5. Increasing or reducing share capital,
6. Making decisions concerning claims for repair of damage inflicted in the establishment of the Company or in exercise of its supervision or management,
7. Disposing of or leasing a business or its organised part and creating limited property rights in a business or its organised part,
8. Approving purchase of real estate, perpetual usufruct rights to or an interest in real estate, whose value, determined on the basis of a valuation by an appraiser, exceeds PLN 5,000,000, as well as approving disposal of real estate, perpetual usufruct rights to or an interest in real estate, whose value, determined on the basis of a valuation by an appraiser, exceeds PLN 200,000,
9. Issuing consent to encumber or dispose of shares in Przedsiębiorstwo Poszukiwań i Eksploatacji Złóż Ropy i Gazu Petrobaltic S.A. and shares in Przedsiębiorstwo Przeladunku Paliw Płynnych Naftoport Sp. z o.o.,
10. Amending the Company’s Articles of Association,
11. Creating and liquidating funds/special accounts, including the reserve account,
12. Approving share retirement or buyback of shares for retirement, and defining the terms of such retirement,
13. Issuing bonds,
14. Dissolving, liquidating or transforming the Company or merging the Company with another company,
15. Approving purchase of shares issued by the Company (treasury shares) and creating pledges on treasury shares in the circumstances defined in Art. 362.1.2 of the Commercial Companies Code,
16. Approving incentive programmes,
17. Dissolving the Company,
18. Transferring the Company’s registered office abroad,
19. Changing the Company’s business in a way that would limit its operations in the area of production, processing and sale of refined petroleum products,
20. Selling or leasing the Company’s business or its organised part whose activities include production, processing and sale of refined petroleum products, as well as encumbering such business or its organised part with limited property rights,
21. Merging the Company with another company,
22. Dividing the Company,
23. Establishing preferential rights on shares,
24. Establishing a European company, joining such company or transforming the Company into a European company,
25. Amending the provisions of Par. 10.1 of the Articles of Association.
Proceedings of the General Shareholders Meeting

The person opening a General Shareholders Meeting (Chairperson of the Supervisory Board or Supervisory Board member designated by the Chairperson of the Supervisory Board, or in their absence, President of the Management Board or a person designated by the Management Board) orders an immediate election of the Chairperson of the Meeting from among the persons entitled to participate in the General Shareholders Meeting, with the exception of instances when:

- An Extraordinary General Shareholders Meeting is convened by shareholders holding at least a half of the share capital or at least a half of the total vote at the Company – then the Chairperson of the General Shareholders Meeting is elected by these shareholders;
- The Management Board does not convene an Extraordinary General Shareholders Meeting at the request of shareholders holding at least one-twentieth of the share capital, and the registry court authorises the requesting shareholders to convene the General Shareholders Meeting – then the Chairperson of the General Shareholders Meeting is designated by the court.

The Chairperson of a General Shareholders Meeting conductsthe meeting and is authorised to interpret the Rules of Procedure of the General Shareholders Meeting. The responsibilities of the Chairperson include ensuring the efficient conduct of the meeting, ensuring that the rights and interests of all shareholders are respected, giving floor to the participants, receiving motions and draft resolutions, submitting them for discussion, ordering and conducting voting, and ascertaining that all items on the agenda have been addressed. In particular, the Chairperson should prevent any abuse of rights by the participants of a General Shareholders Meeting and ensure that the rights and interests of minority shareholders are respected. In accordance with the Rules of Procedure of the General Shareholders Meeting, a Meeting should be attended by members of the Management and Supervisory Boards, and the auditor if financial matters are discussed at the Meeting.

After presentation of each item on the agenda, the Chairperson of a General Shareholders Meeting opens the discussion and gives floor in the order in which the participants request to speak. Subject to the General Shareholders Meeting’s consent, several related items on the agenda may be discussed jointly. While taking the floor, the speakers may speak only on the matters included on the agenda and discussed at a given moment. During the discussion of each item on the agenda, each shareholder is entitled to a five-minute speech and three-minute reply. The shareholders may propose amendments and additions to draft resolutions included on the agenda until discussion on a given item to which the resolution pertains is closed. At the request of a person participating in the General Shareholders Meeting, his or her written statement is included in the minutes.

In formal matters, the Chairperson gives the floor to speakers out of turn. Each shareholder may submit a motion concerning a formal matter. Motions concerning the procedure of the Meeting or voting are considered motions on formal matters. The Chairperson resolves on formal matters; if need arises, the Chairperson may seek opinion of a person he or she appoints. If a matter contained in a formal motion cannot be resolved by reference to the Commercial Companies Code, Articles of Association or the Rules of Procedure of the General Shareholders Meeting, the Chairperson submits the motion to the General Shareholders Meeting for voting. If no
objections are lodged, the Chairperson declares that a given item on the agenda has been addressed. When all the items on the agenda are addressed, the Chairperson closes the Meeting.

With a majority of two-thirds of votes, the General Shareholders Meeting may decide on adjourning the Meeting by up to 30 days. Short recesses ordered by the Chairperson in justified circumstances may not be aimed at impeding the exercise of shareholders’ rights.

3.3 GRUPA LOTOS S.A.’S SUPERVISORY BOARD

The Supervisory Board of Grupa LOTOS S.A. operates on the basis of:
- Grupa LOTOS S.A.’s Articles of Association – consolidated text incorporating amendments introduced by Resolutions Nos. 24-32 and No. 34 of the Annual General Shareholders Meeting, dated June 30th 2009,

Composition of the Supervisory Board of Grupa LOTOS S.A. in 2010:

As at January 1st 2010, the composition of Grupa LOTOS S.A.’s Supervisory Board of the seventh term of office was as follows:

- Wiesław Skwarko – Chairman,
- Leszek Starosta – Deputy Chairman,
- Mariusz Obszyński – Secretary,
- Radosław Barszcz – Member,
- Małgorzata Hirszel – Member,
- Jan Stefanowicz – Member,
- Ireneusz Fąfara – Member.

On February 11th 2010, the Extraordinary General Shareholders Meeting of Grupa LOTOS S.A. removed Messrs Mariusz Obszyński, Radosław Barszcz and Jan Stefanowicz from the Supervisory Board, and appointed Messrs Oskar Pawłowski, Michał Rumiński and Rafał Wardziński to the Supervisory Board to serve for the remainder of the seventh term of office. According to the statement of reasons to the shareholder’s proposal, changes in the composition of the Supervisory Board would enhance its supervision over the Company’s operations.

In connection with Mr Ireneusz Fąfara's resignation from his position on Grupa LOTOS S.A.’s Supervisory Board, submitted on March 29th 2010, until June 28th 2010 the number of the Supervisory Board members was limited to six persons, thus falling below the number determined in Resolution No. 34 of the Annual General Shareholders Meeting, dated June 30th
2008, which specifies that the Supervisory Board of Grupa LOTOS S.A. of the seventh term of office should be composed of seven members.

In view of the Shareholder State Treasury’s proposal to increase the number of the Supervisory Board members in order to enhance its operations and performance of its duties, on June 28th 2010 the Annual General Shareholders Meeting adopted Resolution No. 20 requiring the Supervisory Board to be composed of eight members and appointing Ms Ewa Sibrecht-Ośka and Mr Rafał Lorek as members of the Supervisory Board of the seventh term of office.

As at December 31st 2010 and as at the date of release of this Report, the composition of the Supervisory Board of the seventh term of office was as follows:

- Wiesław Skwarko – Chairman,
- Leszek Starosta – Deputy Chairman,
- Oskar Pawłowski – Secretary,
- Małgorzata Hirszel – Member,
- Michał Rumiński – Member,
- Rafał Wardziński – Member,
- Ewa Sibrecht-Ośka – Member,
- Rafał Lorek – Member.

As required by Grupa LOTOS S.A.’s Articles of Association, the Supervisory Board is composed of six to nine members, including the Chairperson, Deputy Chairperson and Secretary. The number of the Supervisory Board members is determined by the General Shareholders Meeting. On June 28th 2010, pursuant to Resolution No. 20, the General Shareholders Meeting decided that the Supervisory Board should be composed of eight members.

Supervisory Board members are appointed and removed from office by the General Shareholders Meeting in a secret ballot, by an absolute majority of votes. The General Shareholders Meeting may appoint new members to the Supervisory Board from an unlimited number of candidates. Notwithstanding the above, as long as the State Treasury remains a shareholder in the Company, the State Treasury, represented by the competent minister, is entitled to appoint and remove one member of the Supervisory Board. The Chairperson of the Supervisory Board is appointed by the General Shareholders Meeting. The Deputy Chairperson and the Secretary are elected by the Supervisory Board from among its other members.

The term of office of the Supervisory Board is a joint term of three years. Any or all Supervisory Board members may be removed from office at any time prior to the expiry of their term.

The Supervisory Board takes decisions during its meetings, which are held as need arises, however not less frequently than once every two months. A meeting of the Supervisory Board may be held if all Supervisory Board members have been duly invited. Meetings of the Supervisory Board are held in Gdańsk, at the Company’s registered office, however, the Chairperson may choose a different venue where justified by special circumstances. Supervisory Board meetings are convened by the Chairperson at his or her own initiative or at the request of authorised persons, i.e. a member of the Supervisory Board and a member of the Management
Board, in which case a Supervisory Board meeting should be convened within two weeks from the receipt of a relevant request, otherwise the person requesting the convening of a Supervisory Board meeting may convene the meeting on his or her own. Supervisory Board meetings are convened by way of sending written invitations to the members of the Supervisory Board at least seven days prior to the planned meeting date, except where a Supervisory Board meeting is convened at a written request of the Management Board to deal with matters of urgency. In such cases the Chairperson should convene a Supervisory Board meeting within two days from the receipt of a relevant request. Under special circumstances, a meeting of the Supervisory Board may be held without being formally convened if all Supervisory Board members are present and agree to holding the meeting and including specific items on its agenda.

The Supervisory Board adopts its resolutions with an absolute majority of valid votes cast, in the presence of at least a half of the Supervisory Board members, except resolutions concerning appointment and removal from office of any or all members of the Management Board of Grupa LOTOS S.A. which require the presence of at least two-thirds of the Supervisory Board members to be adopted.

Moreover, the Supervisory Board may adopt resolutions in writing or by means of remote communication, subject to Art. 388.4 of the Commercial Companies Code. However, such manner of voting is not allowed for voting on the election of the Chairperson or Deputy Chairperson of the Supervisory Board, appointment of a Management Board member, and removal or suspension from office of such persons. Adoption of a resolution in this manner requires prior delivery of the draft resolution to all Supervisory Board members. Resolutions adopted in this manner are presented at the next meeting of the Supervisory Board, along with the voting results.

Each Supervisory Board meeting is recorded in the form of minutes, containing information on the venue and time of the meeting, its agenda, names of the persons present at the meeting, proceedings of the meeting, wording of the adopted resolutions, the manner of voting and voting results, as well as objections and dissenting opinions of the Supervisory Board members. The minutes are approved and signed by all members of the Supervisory Board who are present at the meeting. The minutes are kept in a file of minutes.

Between Supervisory Board meetings, declarations of will and letters addressed to the Supervisory Board are accepted by the Chairperson or, in his or her absence, by the Deputy Chairperson.

The Supervisory Board exercises ongoing supervision over the Company’s business, across all areas of its operations. The Supervisory Board may issue its opinions on all matters related to the Company’s business, and submit motions and proposals to the Management Board.

Powers of the Supervisory Board include:

1. Appointing and removing the President, Vice-Presidents, and other Management Board members, and proposing rules of remuneration for the Management Board members,

2. Suspending from office (for good reason) any or all Management Board members, and delegating Supervisory Board member(s) to temporarily substitute for Management Board members who are unable to perform their duties,

3. Approving the Rules of Procedure of the Management Board,
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4. Selecting an auditor to audit the financial statements of the Company and its Group, in accordance with the provisions of the Polish Accountancy Act,

5. Reviewing financial statements for compliance with accounting records and documents, as well as the actual state of affairs, reviewing the Directors’ Report and the Management Board’s recommendations concerning distribution of profit or coverage of loss, and submitting written reports on the findings of such reviews to the General Shareholders Meeting,

6. Issuing opinions on all matters submitted for consideration to an Annual or Extraordinary General Shareholders Meeting,

7. Granting consent to Management Board members to serve on managing or supervisory bodies of other companies and to receive remuneration for such service,

8. Granting approval to implement investment projects and to assume obligations related to such projects, if the value of the resulting expenditure or encumbrances exceeds the equivalent of a half of the Company’s share capital,

9. Defining the content and scope of detail of annual budgets and long-term strategies and deadlines for their submission by the Management Board,

10. Approving long-term strategies of Grupa LOTOS S.A. and the LOTOS Group,

11. Issuing opinions on annual budgets,

12. Awarding annual bonuses to the President, Vice-Presidents and members of the Management Board, unless specific laws or regulations provide otherwise,

13. Approving the rules for managing special accounts and the Rules of Procedure for the Supervisory Board,

14. Granting approval to:

   - establish a foreign branch within the meaning of the provisions of Double-Tax Treaties signed by Poland;
   - dispose of non-current assets whose value exceeds the equivalent of one-twentieth of the net value of the Company’s assets;
   - contract another liability or make another disposal whose value – whether in a single or a series of related legal transactions which fall outside the scope of day-to-day management – exceeds the equivalent of a half of the Company’s share capital, unless such transactions require approval of the General Shareholders Meeting;
   - make equity investments abroad, if their value exceeds one-twentieth of the Company’s share capital, and any investments in property, plant and equipment;
   - exercise the Company’s voting rights at the general shareholders meetings of all subsidiaries and other companies, if the value, at acquisition cost, of the shares the Company holds in a given company exceeds one-fifth of the Company’s share capital (in the case of voting on the following matters: distribution of profit or coverage of loss, increase or reduction of share capital, merger with another company, transformation of the company, sale and lease of the company’s business and
encumbering it with usufruct rights, or amendment of the company's articles of association);

- establish companies under commercial law and acquire interests in companies, as well as make payments for shares of a company or sell shares in a company, if the value, at acquisition cost, of the Company's equity investment before or after the acquisition of the shares, exceeds one-twentieth of the Company's share capital, except for acquisitions of shares by way of conversion of claims pursuant to the Polish Act on Financial Restructuring of Enterprises and Banks and Acquisition of Shares in Public Trading in Securities, dated February 3rd 1993;

- purchase real estate, perpetual usufruct rights to or an interest in real estate, whose value, determined on the basis of an appraiser's valuation, does not exceed PLN 5,000,000; and dispose of real estate, perpetual usufruct rights or an interest in real estate, whose value, determined on the basis of an appraiser's valuation, does not exceed PLN 200,000.

In 2010, the Supervisory Board met nine times and adopted 41 resolutions, two of them being written resolutions.

Committees of the Supervisory Board

The Supervisory Board may set up standing or ad-hoc committees composed of its members to examine specific matters. The committees report their activities to the Supervisory Board as need arises; standing committees must report to the Supervisory Board at least once a year.

A committee is composed of three to five members. The chairperson of a committee, who manages the committee's work, is appointed by the Supervisory Board from among the committee members. The chairperson, acting on his or her own initiative or upon request of a committee member, convenes committee meetings. The right to convene a committee meeting is also vested in the Chairperson of the Supervisory Board or a Supervisory Board member designated by the Chairperson. All Supervisory Board members have the right to participate in the committees’ work.

The chairperson of a committee, or a person designated by the chairperson, has the right to request the Supervisory Board to adopt resolutions regarding preparation of opinions or expert opinions for the committee, concerning the scope of the committee's remit or engagement of an adviser.

The committees adopt their decisions at meetings. A notice of a meeting should be delivered to the committee members and to other Supervisory Board members not later than five days prior to the meeting or, in urgent cases, not later than one day prior to the meeting.

Committees adopt resolutions by absolute majority of votes, unless provided otherwise in the resolution establishing the committee.

Minutes are taken at each committee meeting. The minutes should be signed by all attending committee members and contain the resolutions, conclusions and reports of the committee.

The following standing committees operate within the Supervisory Board of Grupa LOTOS S.A.:
Strategy and Development Committee

The Strategy and Development Committee is responsible for providing to the Supervisory Board opinions and recommendations regarding planned projects with material effect on the Company's assets, and in particular:

- Issuing opinions on long-term development strategies of the Company and the Group,
- Evaluating the impact of planned and implemented projects on the Company's assets,
- Monitoring the implementation of projects financed with proceeds from share issues performed as part of share capital increases,
- Evaluating actions, agreements and other documents related to the activities aimed at acquisition, sale, encumbrance or any other action with respect to the Company's material assets,
- Issuing opinions on all strategic documents submitted to the Supervisory Board by the Management Board.

In 2010 and as at the date of release of this report, the Strategy and Development Committee was composed of:

From January 1st to February 11th 2010
- Wiesław Skwarko – Chairman,
- Radosław Barszcz
- Leszek Starosta
- Jan Stefanowicz
- Małgorzata Hirszel.

As a result of the changes in the composition of the Supervisory Board effected by the General Shareholders Meeting on February 11th 2010 (dismissal of J. Stefanowicz, M. Obszyński and R. Barszcz; appointment of R. Wardziński, M. Rumiński and O. Pawłowski), the new Supervisory Board at its first meeting resolved to fill the vacant posts on the Strategy and Development Committee by appointing Rafał Wardziński and Michał Rumiński as Committee members.

From March 2nd to December 31st 2010 and as at the date of release of this report, the Strategy and Development Committee was composed of:

- Wiesław Skwarko – Chairman,
- Rafał Wardziński,
- Leszek Starosta
- Michał Rumiński,
- Małgorzata Hirszel.
Organisation and Management Committee

The Organisation and Management Committee is responsible for providing to the Supervisory Board opinions and recommendations regarding the management structure, including organisation-related solutions, remuneration system and recruitment of personnel, with a view to enabling the Company to achieve its strategic objectives, and in particular:

- Assessing candidates for members of the Management Board,
- Issuing recommendations as to the terms of employment for newly appointed members of the Management Board,
- Evaluating activities of the members of the Management Board,
- Performing periodic reviews and evaluation of the Company’s remuneration system,
- Assessing the human resources management system adopted at the Company.

In 2010 and as at the date of release of this report, the Organisation and Management Committee was composed of:

From January 1st to February 11th 2010

- Leszek Starosta – Chairman,
- Małgorzata Hirszel,
- Mariusz Obszyński.

As a result of the changes in the composition of the Supervisory Board effected by the General Shareholders Meeting on February 11th 2010 (dismissal of J. Stefanowicz, M. Obszyński and R. Barszcz; appointment of R. Wardziński, M. Rumiński and O. Pawłowski), the new Supervisory Board at its first meeting resolved to fill the vacant posts on the Organisation and Management Committee by appointing Michał Rumiński and Oskar Pawłowski as Committee members.

From March 2nd to August 2nd 2010, the Organisation and Management Committee was composed of:

- Leszek Starosta – Chairman,
- Małgorzata Hirszel,
- Michał Rumiński,
- Oskar Pawłowski.

As a result of the decision of the General Shareholders Meeting of June 28th 2010, regarding changes in the composition of the Supervisory Board (appointment of E. Sibrecht-Ośka and R. Lorek), the new Supervisory Board at its first meeting resolved to appoint Ewa Sibrecht-Ośka as member of the Organisation and Management Committee.

From August 2nd to December 31st 2010 and as at the date of release of this report, the Organisation and Management Committee was composed of:

- Leszek Starosta – Chairman,
Audit Committee

The Audit Committee is responsible for the provision of ongoing advisory support to the Supervisory Board with respect to correct implementation of the policies related to budgetary and financial reporting, the Company’s internal audit function, and cooperation with its auditors, and in particular:

1. Monitoring the process of financial reporting;
2. Monitoring the effectiveness of the Company’s internal audit and risk management systems;
3. Monitoring the performance of auditing procedures, including the monitoring of the process of reviewing annual and consolidated financial statements;
4. Monitoring the work and reports of independent auditors, including the monitoring of independence of auditors and of entities qualified to review financial statements;
5. Reviewing particular economic events relevant to the Company’s business;
6. Providing ongoing information to the Supervisory Board on any material matters with respect to the Audit Committee’s activities.

In 2010 and as at the date of release of this report, the Audit Committee was composed of:

From January 1st to February 11th 2010
- Jan Stefanowicz – Chairman,
- Mariusz Obszyński,
- Wiesław Skwarko,
- Radosław Barszcz,
- Ireneusz Fałara.

As a result of the changes in the composition of the Supervisory Board effected by the General Shareholders Meeting on February 11th 2010 (dismissal of J. Stefanowicz, M. Obszyński and R. Barszcz; appointment of R. Wardziński, M. Rumiński and O. Pawlowski), the new Supervisory Board at its first meeting resolved to fill the vacant posts on the Audit Committee by appointing Oskar Pawlowski and Rafał Wardziński as Committee members, and Ireneusz Fałara as the Chairman of the Audit Committee.

From March 2nd to March 29th 2010:
- Ireneusz Fałara – Chairman,
- Wiesław Skwarko,
Following the resignation of Ireneusz Fąfara from the Supervisory Board on March 29th 2010, the vacancy on the Audit Committee lasted from March 29th until August 2nd 2010. Pursuant to Par. 2.3 of the Rules of Procedure for the Audit Committee, until appointment of the new chairman, the Committee's meetings were convened by the Chairman of the Supervisory Board – Wiesław Skwarko.

In view of the General Shareholders Meeting’s decision of June 28th 2010, regarding changes in the composition of the Supervisory Board (appointment of E. Sibrecht-Ośka and R. Lorek), the new Supervisory Board at its first meeting on August 2nd 2010 resolved to fill the vacant posts on the Audit Committee by appointing Rafał Lorek as Committee member and Michał Rumieński as Chairman of the Audit Committee.

Consequently, from August 2nd to December 31st 2010 and as at the date of release of this report, the Audit Committee was composed of:

- Michał Rumieński – Chairman,
- Wiesław Skwarko,
- Oskar Pawłowski,
- Rafał Wardziński,
- Rafał Lorek (independent member of the Supervisory Board)

Delegation of Specific Duties to Individual Supervisory Board Members

The Supervisory Board performs its duties collectively. It may also delegate its members to perform specific supervisory duties individually.

1. Mr Wiesław Skwarko

By virtue of a resolution of August 12th 2008, Mr Wiesław Skwarko was delegated to exercise close, ongoing supervision over the implementation of the 10+ Programme, including:

- monitoring the progress of work under the project and the project’s timely implementation,
- supervising the raw materials procurement strategy for the project,
- overseeing the delivery of the finished product sales strategy,
- supervising consistent management of logistics during the project's implementation;

2. Mr Leszek Starosta

By virtue of a resolution of August 12th 2008, Mr Leszek Starosta was delegated to exercise close, ongoing supervision over the implementation of the 10+ Programme, including:

- supervising legal aspects of the contracts executed and performed as part of the project,
supervising procedures for the contract execution,

- supervising the administration proceedings related to the project's implementation.

3.4 MANAGEMENT BOARD OF GRUPA LOTOS S.A. AND RULES GOVERNING APPOINTMENT AND REMOVAL OF THE MANAGEMENT STAFF

The Management Board of Grupa LOTOS S.A. operates on the basis of:

- Grupa LOTOS S.A.’s Articles of Association – consolidated text incorporating amendments introduced by Resolutions Nos. 24-32 and No. 34 of the Annual General Shareholders Meeting, dated June 30th 2009,


Composition and Activities of the Management Board of Grupa LOTOS S.A. in 2010

From January 1st to December 31st 2010 and as at the date of release of this Report, the Management Board of Grupa LOTOS S.A. of the seventh term of office was composed of four members(*):

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

*) In 2009, in connection with the expiry of the Management Board's term of office, the Supervisory Board announced a competition for five posts on the Management Board of the joint seventh term of office, including the post of President of the Management Board, responsible for strategic management and coordination of the Management Board's activities, and four Management Board members in charge of the production, trade, finance, and upstream divisions. Four candidates were elected by the Supervisory Board in the procedure of recruiting Management Board members. On June 25th 2009, the Supervisory Board adopted a resolution appointing the four candidates as members of the Management Board of Grupa LOTOS S.A. for the joint seventh term of office. However, due to the lack of suitable candidates for the position of Vice-President of the Management Board responsible for the upstream division, the Supervisory Board resolved to close the recruitment process on July 17th 2009. Therefore, pursuant to the decision of the Supervisory Board, the President of Grupa LOTOS S.A.'s Management Board will remain in charge of the oil and gas exploration and production until a new Management Board member is appointed.
The Management Board manages all affairs of Grupa LOTOS S.A. and represents the Company towards third parties, with the exception of the actions which rest with the General Shareholders Meeting or the Supervisory Board and matters which fall outside the scope of day-to-day management, which require prior resolution by the Management Board, as well as matters assigned to particular Management Board members under the Rules of Procedure of the Management Board.

Meetings of the Management Board are held as need arises. They are convened by the President of the Management Board or, in his or her absence, a Management Board member authorised by the President, who also chairs the meetings in absence of the President. The notices of the meeting are delivered to the Management Board members at least two days prior to the date of the meeting. The notice should contain the meeting agenda, conclusions and materials (in the form of appendices) relating to the matters included in the meeting agenda. A resolution will be deemed validly adopted if all Management Board members have been notified of the Management Board meeting and if at least three-fifths of the Management Board members are in attendance at that meeting. Resolutions are adopted by a simple majority of votes in favour of a resolution; abstaining votes are disregarded. Voting is open. A secret ballot may be held at the request of the President or two members of the Management Board. In the case of a voting tie, the President of the Management Board has the casting vote. The Management Board may also adopt resolutions in writing or by means or remote communication. Adoption of a resolution in this manner requires prior submission of the draft resolution to all Management Board members. Resolutions adopted in this manner are presented at the next meeting of the Management Board, along with the voting results.

Each Management Board meeting is recorded in the form of minutes. The minutes should contain information on which Management Board members are present at the meeting, the venue and date of the meeting, its agenda, names of the persons present at the meeting, proceedings of the meeting, wording of the adopted resolutions, the manner of voting and voting results, as well as objections and dissenting opinions of the Management Board members. The minutes are approved and signed by all members of the Management Board who are present at the meeting. The minutes are kept at the Management Board Office.

Rules Governing Appointment and Removal of Management Staff and the Scope of Their Powers

In accordance with the Articles of Association of Grupa LOTOS S.A., the Management Board is composed of three to seven members, including the President and Vice-Presidents of the Management Board. The number of the Management Board members is determined by a resolution of the Supervisory Board. The Supervisory Board appoints the Management Board, by first appointing the President of the Management Board, and then – acting upon the President’s proposal – the Vice-Presidents and the other Management Board members. The term of office of the Management Board is a joint term of three years.

Mandates of the Management Board members expire not later than on the date of the General Shareholders Meeting approving the financial statements for the last full financial year during the term of office, but the President, Vice-Presidents, other Management Board members and the
entire Management Board may be dismissed or suspended for sound reasons by the Supervisory Board at any time before the end of their term of office. Supervisory Board adopts resolutions on appointment to or removal from office of any or all Management Board members by way of a vote cast in the presence of at least two-thirds of the Supervisory Board members. A Management Board member's mandate may also expire following a member’s resignation.

Management of the Company's affairs by the Management Board is subject to limitations resulting from the provisions of law, the Articles of Association, and resolutions of the General Shareholders Meeting and the Supervisory Board. The Management Board represents the Company in dealings with third parties and in all legal activities, with the exception of the Company’s actions concerning the Management Board members.

Management Board resolutions are required with regard to the following matters:

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

15. Establishing the agenda for a General Shareholders Meeting,

16. Matters falling outside the scope of ordinary management of the enterprise,

17. Matters which have been objected to by at least one of the members of the Management Board,

18. Matters which must be resolved by way of Management Board resolutions if so required by the President of the Management Board or at least half of the members of the Management Board, and which fall within the scope of responsibilities of particular members of the Management Board,


In 2010, the Management Board held in total 51 meetings, in which it adopted 128 resolutions.

Any matters not specified above are assigned to individual members of the Management Board in line with the division of powers and responsibilities, as provided below:

**Pawel Olechnowicz, President of the Management Board and CEO**, is in charge of the overall management and coordination of the operations of Grupa LOTOS S.A. and, by virtue of the Supervisory Board's decision, acts as Vice-President of the Management Board responsible for Oil & Gas Exploration and Production until appointment of a new Management Board member, holding responsibility for these areas.

**Marek Sokołowski, Vice-President of the Management Board, Chief Operation Officer**, is in charge of the overall management and coordination of the activities of the production division, technology division, technology development division and refinery extension division (which is implementing the 10+ Programme), and holds overall responsibility for managing, coordinating and directing them.

**Mariusz Machajewski, Vice-President of the Management Board, Chief Financial Officer**, is in charge of the overall coordination of the Company's economic and financial affairs and its accounting functions, and holds responsibility for their management.
Maciej Szozda, Vice-President of the Management Board, Chief Commercial Officer, is charged with the overall management of the Company’s operations and holds responsibility for managing them.

II INFORMATION ON GRUPA LOTOS S.A.

1 DESCRIPTION OF GRUPA LOTOS S.A.

1.1 ORGANISATIONAL STRUCTURE OF GRUPA LOTOS S.A. AND GRUPA LOTOS S.A.’S BRANCHES (PLANTS)

The corporate structure of Grupa LOTOS S.A. reflects the division of duties and relations between various functions and tasks performed at the Company, as well as establishes the hierarchy of organisational units and management. As at December 31st 2010, the corporate structure of Grupa LOTOS S.A. comprised the following units:

- 18 divisions, including 7 divisions reporting directly to the Chief Executive Officer,
- 38 offices,
- 20 departments,
- 7 complexes.

A division is a group of organisational units reporting to specific executive officers who hold decision-making powers within a certain area of the business. Organisational units are separated mainly based on the criterion of the function performed.

The basic responsibility of an office is to support the Chief Executive Officer’s or the division heads’ decision-making process.

A department is responsible for performing a specific function assigned to it, and ranks one level below an office in the organisational hierarchy.

A complex is an operating component of the enterprise, directly performing operating and executory functions.

Grupa LOTOS S.A. has no branches (plants) within the meaning of the Polish Accountancy Act.
1.2 CHANGES IN ORGANISATION AND MANAGEMENT OF GRUPA LOTOS S.A.

Changes in Grupa LOTOS S.A.’s Organisational Rules and Corporate Structure in 2010:

As of February 1st 2010, Grupa LOTOS S.A. adopted resolutions concerning changes in its corporate structure which involved the establishment of a new organisational unit, the Hydrogen and Sulphur Complex designated as PZW, reporting to the Production Director (OP), as well as amendments to its Organisational Rules, involving amendments to Chapter I “List of Amendments to the Organisational Rules”, Chapter VI “Organisation of the Company's Management”, a change to the scope of duties of the Production Director (OP), a change to the scope of operations of the Hydrocracker Complex (PZH), and organisational changes related to the establishment of the Hydrogen and Sulphur Complex (PZW). On the same date, the Management Board of Grupa LOTOS S.A. adopted the consolidated text of the Organisational Rules of Grupa LOTOS S.A.’s enterprise.

On February 15th 2010, the Management Board of the Company passed a resolution concerning amendments to Chapter VIII “Business Areas and Principles of Segmental Management at the LOTOS Group” of the Organisational Rules in connection with the changed business profile of LOTOS Gaz S.A.

As of April 1st 2010, amendments were made to the Organisational Rules, involving expansion of the scope of duties of the Sales Director (HA).

On April 20th 2010, the Company’s Management Board adopted a resolution concerning amendments to Chapter II “Introductory Provisions” and Chapter VIII “Business Areas and Principles of Segmental Management at the LOTOS Group” of the Organisational Rules, in connection with renaming of Przedsiębiorstwo Poszukiwań i Eksploatacji Złóż Ropy i Gazu Petrobaltic S.A. as LOTOS Petrobaltic S.A., as well as changes to the scope of operations of the Technical Supervision Department (TD).

As of July 6th 2010, Grupa LOTOS S.A.’s Management Board adopted a resolution concerning amendments to the Company's Organisational Rules and corporate structure, involving liquidation of the Communication and CSR Office (JK), reporting to the Communication, Administration and CSR Director (NJ), and establishment in its place of a Sponsorship, Social Affairs and CSR Office (JS) and an Event Organization Department (JW), as well as transfer of the telecommunication and video conference services, and network printing supervision from the division of the Communication, Administration and CSR Director (NJ) to the IT Management Office (DI). The changes resulted in amendments to Chapter VI “Organisation of the Company's Management”, as well as to the scope of duties of the Communication, Administration and CSR Director (NJ), the Strategy and Exploration & Production Director (ND), the Strategic Studies Office (DS), the Investor Relations Office (FI) and the IT Management Office (DI). New provisions were added to the Rules, detailing the scope of duties of the Sponsorship, Social Affairs and CSR Office (JS) and the Event Organization Department (JW). In addition, the scope of operations of a number of units, including the Press Office (NR), the Management Board Assistance Office (JZ), the Corporate Service Office (JO) and the Administration Office (JA), was defined in greater detail.

As of September 1st 2010, changes to the corporate structure of Grupa LOTOS S.A. took effect whereby exploration and production activities were taken outside the scope of
1.3 OWNERSHIP CHANGES AT THE LOTOS GROUP IN 2010

LOTOS Czechowice S.A. and LOTOS Jasło S.A.

In 2010, Grupa LOTOS S.A. purchased the employee shares of LOTOS Jasło S.A. and LOTOS Czechowice S.A. held by natural persons. The shares were acquired through voluntary sale. Following the transactions, Grupa LOTOS S.A.'s interest in LOTOS Czechowice S.A. and LOTOS Jasło S.A. increased as follows:

- LOTOS Czechowice S.A. – from 85.04% to 97.55%,
- LOTOS Jasło S.A. – from 85.01% to 98.12%.

The purchase of shares from minority shareholders is a part of the process of streamlining Grupa LOTOS S.A.'s assets. Gaining full control over the companies by Grupa LOTOS S.A. will broaden the range of restructuring possibilities for these entities.

LOTOS Exploration and Production Norge AS

On November 15th 2010, the General Shareholders Meeting of LOTOS E&P Norge AS resolved to increase the company's share capital through the issue of one Series A preference share with a par value of NOK 1.00. Following the increase, the company's share capital amounted to NOK 430,000,001.00. The new share was acquired at a par value of NOK 1.00 by Grupa LOTOS S.A., which became the company's minority shareholder. On December 2nd 2010, the increase in the share capital was registered by the Norwegian register of entrepreneurs, Brønnøysundregistrene.

LOTOS Biopaliwa Sp. z o.o., RCEkoenergia Sp. z o.o. and LOTOS Exploration and Production Norge AS

As part of the efforts to enhance ownership supervision over its secondary subsidiaries: LOTOS Biopaliwa Sp. z o.o., RCEkoenergia Sp. z o.o. and LOTOS Exploration and Production Norge AS, Grupa LOTOS S.A. executed the following transactions:

- on November 5th 2010, one share in LOTOS Biopaliwa Sp. z o.o. with a par value of PLN 500.00 was acquired from LOTOS Czechowice S.A. (the value of the transaction was PLN 3,008.50 and was equal to the value of LOTOS Biopaliwa Sp. z o.o.'s net assets per share as at September 30th 2010);
- on November 5th 2010, one share in RCEkoenergia Sp. z o.o. with a par value of PLN 1,000.00 was acquired from LOTOS Czechowice S.A. (the value of the transaction was PLN 1,081.21 and was equal to the value of RCEkoenergia Sp. z o.o.'s net assets per share as at September 30th 2010);
- on November 15th 2010, one Series A preference share with a par value of NOK 1.00 was acquired in the increased share capital of LOTOS Exploration and Production Norge AS (the share was acquired at a par value of NOK 1.00).

Following the above described equity transactions, the shareholder structure of the companies was as follows:

- LOTOS Biopaliwa Sp. z o.o.: LOTOS Czechowice S.A. holds 99.995% of shares in the company, while Grupa LOTOS S.A. holds 0.005% of its share capital;
- RCEkoenergia Sp. z o.o.: LOTOS Czechowice S.A. holds 99.995% of shares in the company, while Grupa LOTOS S.A. holds 0.005% of its share capital;
- LOTOS Exploration and Production Norge AS: LOTOS Petrobaltic S.A. holds 99.9999998% of shares in the company, while Grupa LOTOS S.A. holds 0.0000002% of its share capital.

UAB LOTOS Baltija

On December 9th 2010, LOTOS Petrobaltic S.A. purchased from Grupa LOTOS S.A. 5,876 shares in UAB LOTOS Baltija, representing 100% of the company's share capital, for a total price of PLN 484,758.23, (approximately PLN 82.50 per share). The transaction was carried out as part of the process of streamlining the LOTOS Group's Lithuanian assets and constitutes an inherent element of the exploration and production strategy of the LOTOS Group.

LOTOS Park Technologiczny Sp. z o.o.

On March 31st 2010, the District Court of Rzeszów registered a reduction in the share capital of LOTOS Park Technologiczny Sp. z o.o. in the Register of Entrepreneurs of the National Court Register. The reduction in the company's share capital is a result of the process of retiring company shares, commenced in 2009. Following the registration, the company's share capital was reduced from PLN 17,307,000.00 to PLN 50,000.00 by way of voluntary retirement of 34,514 shares, as a result of which Grupa LOTOS S.A. became the sole shareholder of the company. The retirement of the company shares was a closing point in one of the stages of the restructuring process at the Southern Refineries, conducted by the company as an SPV set up specifically for this purpose.

Events Subsequent to the Balance-Sheet Date (December 31st 2010)

PLASTEKOL Organizacja Odzysku S.A. and LOTOS Jaslo S.A.

On February 11th 2011, LOTOS Jaslo S.A. executed a final agreement on the sale of the entire interest of 955 shares in PLASTEKOL Organizacja Odzysku S.A., representing 95.5% of the company's share capital, for the net price of PLN 1,700,000.00 (approximately PLN 1,780 per share). The shares were acquired by IGT Polska Sp. z o.o. of Jaslo. A preliminary agreement on the sale of the block of shares in PLASTEKOL Organizacja Odzysku S.A. was signed by the parties on October 11th 2010.
UAB Meditus, AB Geonafta

On December 14th 2010, LOTOS Petrobaltic and UAB Hermis Capital entered into a conditional agreement on the sale of 100% shares in UAB Meditus, which holds a 59.41% interest in AB Geonafta. The transaction was executed with a view to gaining full control over AB Geonafta. On February 3rd 2011, following completion of the conditional agreement of December 2010, LOTOS Petrobaltic S.A. came to hold 100% of shares in UAB Meditus, thus gaining full control over AB Geonafta (the shareholder structure of AB Geonafta is as follows: UAB Meditus holds 59.41% of the company shares, while LOTOS Petrobaltic S.A. – 40.59%). The decision to increase shareholding in AB Geonafta, a Lithuania-based company, to 100% is an element of the LOTOS Group's strategy for the upstream segment, aimed at diversifying the assets portfolio with the appraised fields, while maintaining geological risk at a relatively low level. LOTOS Petrobaltic S.A. has been the shareholder of AB Geonafta for ten years, holding 40.59% of its shares. For twenty years, AB Geonafta and its group members: UAB Minijos Nafta, UAB Genciu Nafta, and UAB Manifoldas have bee involved in exploration for and production of crude oil in Lithuania. The acquisition of AB Geonafta by LOTOS Petrobaltic S.A. will allow for an improvement in the production capacity (crude oil production) of LOTOS Petrobaltic S.A. by approximately 50%. The transaction will also strengthen LOTOS Petrobaltic S.A.’s onshore oil and gas production capability.

LOTOS Jasło S.A. and LOTOS Czechowice S.A.

Q1 2011 saw the completion of the squeeze-out of shares in LOTOS Jasło S.A. and LOTOS Czechowice S.A., pursuant to Art. 418 of the Commercial Companies Code. The purchase of shares from minority shareholders is a part of the process of streamlining Grupa LOTOS S.A.’s assets.

On April 7th and April 8th 2011, relevant entries were made in the share registers of the companies. Consequently, Grupa LOTOS S.A. holds 100% of the shares in LOTOS Jasło SA and 100% of the shares in LOTOS Czechowice SA.

LOTOS Petrobaltic S.A.

In Q1 2011, a process of purchasing LOTOS Petrobaltic S.A.’s employee shares, held by natural persons, was commenced. The shares are acquired through voluntary sale. The purchase of shares from minority shareholders is a part of the process of streamlining Grupa LOTOS S.A.’s assets and constitutes an inherent element of the exploration and production strategy of the LOTOS Group.

LOTOS Gaz S.A. w likwidacji (in liquidation)

On January 10th 2011, the company's Extraordinary General Shareholders Meeting resolved to dissolve the company and place it in liquidation. The resolution followed from the decision to discontinue the company's operations.
1.4 GRUPA LOTOS S.A.'S EMPLOYMENT STRUCTURE

As at December 31st 2010, Grupa LOTOS S.A. employed 1,310 staff (1,303 FTEs).

Employment structure by job category – Grupa LOTOS S.A.:

<table>
<thead>
<tr>
<th>Item</th>
<th>Men</th>
<th>Women</th>
<th>Total</th>
<th>FTEs</th>
</tr>
</thead>
<tbody>
<tr>
<td>blue-collar jobs</td>
<td>509</td>
<td>5</td>
<td>514</td>
<td>513</td>
</tr>
<tr>
<td>white-collar jobs</td>
<td>404</td>
<td>392</td>
<td>796</td>
<td>790</td>
</tr>
<tr>
<td>Total</td>
<td>913</td>
<td>397</td>
<td>1,310</td>
<td>1,303</td>
</tr>
</tbody>
</table>

Grupa LOTOS S.A.’s employment structure by education level:

<table>
<thead>
<tr>
<th>Education</th>
<th>white-collar jobs</th>
<th>blue-collar jobs</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>University degree</td>
<td>605</td>
<td>78</td>
<td>683</td>
</tr>
<tr>
<td>Secondary education (technical)</td>
<td>149</td>
<td>312</td>
<td>461</td>
</tr>
<tr>
<td>Secondary education (general)</td>
<td>33</td>
<td>35</td>
<td>68</td>
</tr>
<tr>
<td>Vocational education</td>
<td>8</td>
<td>74</td>
<td>82</td>
</tr>
<tr>
<td>Primary-level education</td>
<td>1</td>
<td>15</td>
<td>16</td>
</tr>
<tr>
<td>Total</td>
<td>796</td>
<td>514</td>
<td>1310</td>
</tr>
</tbody>
</table>

1.5 CHANGES IN ORGANISATIONAL OR CAPITAL LINKS BETWEEN THE PARENT UNDERTAKING AND OTHER ENTITIES

Undertakings in which the Company directly holds shares in the share capital or in the total vote in the undertaking’s constitutive body:

<table>
<thead>
<tr>
<th>Name</th>
<th>Registered office</th>
<th>Business profile</th>
<th>Percentage of share capital held by the Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>LOTOS Paliwa Sp. z o.o.</td>
<td>Gdańsk</td>
<td>Wholesale and retail sale of fuels, light fuel oil, management of the LOTOS service station network</td>
<td>100.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Gaz S.A.(1)</td>
<td>Mława</td>
<td>The company is not conducting</td>
<td>100.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>100.00%</td>
</tr>
<tr>
<td>Company Name</td>
<td>City</td>
<td>Operations</td>
<td>Ownership 1</td>
</tr>
<tr>
<td>-----------------------------------</td>
<td>------------</td>
<td>-----------------------------------------------------------------------------</td>
<td>-------------</td>
</tr>
<tr>
<td>LOTOS Oil S.A.</td>
<td>Gdańsk</td>
<td>Production and sale of lubricating oils and lubricants, and domestic sale of base oils</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Asfalt Sp. z o.o.</td>
<td>Gdańsk</td>
<td>Production and sale of bitumens</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Ekoenergia Sp. z o.o.</td>
<td>Gdańsk</td>
<td>The company has not commenced operations</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Kolej Sp. z o.o.</td>
<td>Gdańsk</td>
<td>Railway transport</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Serwis Sp. z o.o.</td>
<td>Gdańsk</td>
<td>Maintenance of mechanical and electric operations and controlling devices, repairs</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS LAB Sp. z o.o.</td>
<td>Gdańsk</td>
<td>Laboratory testing</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Straż Sp. z o.o.</td>
<td>Gdańsk</td>
<td>Fire safety</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Ochrona Sp. z o.o.</td>
<td>Gdańsk</td>
<td>Personal and property protection</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Parafiny Sp. z o.o.</td>
<td>Jasło</td>
<td>Production and sale of paraffin</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Tank Sp. z o.o.</td>
<td>Gdańsk(5)</td>
<td>Wholesale of petroleum products</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Czechowice S.A. (parent undertaking of another group)</td>
<td>Czechowice-Dziedzice</td>
<td>Storage and distribution of fuels</td>
<td>97.55% (5)</td>
</tr>
<tr>
<td>LOTOS Jaslo S.A. (parent undertaking of another group)</td>
<td>Jasło</td>
<td>Services related to distribution of petroleum products, storage of fuels, building and maintenance of fuel stocks; production and processing of refined petroleum products and their wholesale and retail sale</td>
<td>98.12% (5)</td>
</tr>
<tr>
<td>LOTOS Petrobaltic S.A. (parent undertaking of another group)</td>
<td>Gdańsk</td>
<td>Acquisition of crude oil and natural gas reserves and their exploitation</td>
<td>99.32%</td>
</tr>
<tr>
<td>LOTOS Park</td>
<td></td>
<td>The company is not conducting</td>
<td></td>
</tr>
</tbody>
</table>
Grupa LOTOS S.A.

DIRECTORS’ REPORT ON THE OPERATIONS OF GRUPA LOTOS S.A. IN 2010

<table>
<thead>
<tr>
<th>Technologiczny Sp. z o.o.</th>
<th>Jasło operations</th>
<th>100.00%(^{(7)})</th>
<th>100.00%(^{(7)})</th>
</tr>
</thead>
<tbody>
<tr>
<td>UAB LOTOS Baltija</td>
<td>Lithuania Business and legal advisory services</td>
<td>-(^{(9)})</td>
<td>100.00%</td>
</tr>
<tr>
<td>LOTOS Biopaliwa Sp. z o.o.</td>
<td>Czechowice-Dziedzice Production of fatty acid methyl esters (\text{(FAME)})^{(10)}</td>
<td>0.005%(^{(11)})</td>
<td>-</td>
</tr>
<tr>
<td>RCEkoenergia Sp. z o.o.</td>
<td>Czechowice-Dziedzice Production and distribution of electricity, heat and gas</td>
<td>0.005%(^{(11)})</td>
<td>-</td>
</tr>
<tr>
<td>LOTOS Exploration &amp; Production Norge AS</td>
<td>Norway Oil exploration and production on the Norwegian continental shelf, provision of services related to oil exploration and production</td>
<td>0.00(^{(12)})%</td>
<td>-</td>
</tr>
</tbody>
</table>

\(^{(1)}\) Until July 23rd 2009, LOTOS Gaz S.A. controlled KRAK-GAZ Sp. z o.o., a subsidiary. On April 30th 2009, KRAK-GAZ Sp. z o.o. filed a bankruptcy petition with the District Court for Kraków Śródmieście, VIII Commercial Division for Bankruptcy and Recovery. On July 23rd 2009, the District Court for Kraków Śródmieście, VIII Commercial Division for Bankruptcy and Recovery, resolved to declare KRAK-GAZ Sp. z o.o.’s bankruptcy by liquidation of the company’s assets.

On January 10th 2011, the General Shareholders Meeting of LOTOS Gaz S.A. adopted a resolution to dissolve LOTOS Gaz S.A. by way of its liquidation.

\(^{(2)}\) On May 6th 2010, a change in the company’s legal form (from a joint stock company to a limited liability company) was registered. Currently the company operates under the name LOTOS Ekoenergia Sp. z o.o.

\(^{(3)}\) On August 12th 2009, the registered office of LOTOS Tank Sp. z o.o. was relocated from Jasło to Gdańsk.

\(^{(4)}\) On July 9th 2009, an agreement was signed providing for the acquisition by the State Treasury of Grupa LOTOS S.A. shares. In exchange, the State Treasury made non-cash contributions to Grupa LOTOS S.A. in the form of 30.32% of shares in LOTOS Petrobaltic S.A., 5% of shares in LOTOS Czechowice S.A. and 5% of shares in LOTOS Jasło S.A.

\(^{(5)}\) By December 31st 010, Grupa LOTOS S.A. acquired from non-controlling interests an additional 12.51% of shares in LOTOS Czechowice S.A. and 13.11% of shares in LOTOS Jasło S.A.

\(^{(6)}\) On March 31st 2010, a change in the name of Przedsiębiorstwo Poszukiwań i Eksploatacji Złóż Ropy i Gazu Petrobaltic Spółka Akcyjna to LOTOS Petrobaltic Spółka Akcyjna (abbreviated name: LOTOS Petrobaltic S.A.) was entered in the National Court Register.

\(^{(7)}\) On November 20th 2009, the then shareholders of LOTOS Park Technologiczny Sp. z o.o. sold their shares to LOTOS Park Technologiczny Sp. z o.o.: - LOTOS Serwis Sp. z o.o. – the entire stake of 12,314 shares, - LOTOS Jasło S.A. – the entire stake of 9,866 shares, - LOTOS Petrobaltic S.A. – the entire stake of 2,834 shares, - Partner Holding Management Sp. z o.o. - the entire stake of 100 shares.

LOTOS Park Technologiczny Sp. z o.o. acquired its own shares with a view to their voluntary retirement by way of reduction of the share capital. Following the transaction, the shareholder structure of LOTOS Park Technologiczny Sp. z o.o. was as follows: - LOTOS Park Technologiczny Sp. z o.o. – 99.71%, - Grupa LOTOS S.A. - 0.29%.
Grupa LOTOS S.A. retained control over LOTOS Park Technologiczny Sp. z o.o. given the GM powers vested in Grupa LOTOS S.A. as the only shareholder. On March 31st 2010, a reduction in the share capital of LOTOS Park Technologiczny Sp. z o.o. to PLN 50 thousand was registered. The share capital of LOTOS Park Technologiczny Sp.z o.o. is divided into 100 shares. Following registration of the changes in the National Court Register, Grupa LOTOS S.A. holds a 100% stake in LOTOS Park Technologiczny Sp. z o.o.

(8) On September 21st 2009, the reduction of the share capital of UAB LOTOS Baltija from LTL 720.2 thousand to LTL 381.9 thousand was registered. Following the reduction, the Company’s share capital is divided into 5,876 ordinary registered shares with a par value of LTL 65 per share.

(9) On December 9th 2010, Grupa LOTOS S.A. entered into an agreement with LOTOS Petrobaltic S.A. on sale of 5,876 shares in UAB LOTOS Baltija, representing 100% of the company’s share capital.

(10) On March 1st 2009, LOTOS Biopaliwa Sp. z o.o. commenced operations.

(11) On November 5th 2010, Grupa LOTOS S.A. acquired from LOTOS Czechowice S.A. one share in LOTOS Biopaliwa Sp. z o.o., representing 0.005% of the company’s share capital, and one share in RCEkoenergia Sp. z o.o., representing 0.005% of the company’s share capital.

(12) On November 15th 2010, the share capital of LOTOS Exploration and Production Norge AS was raised by NOK 1, to NOK 430,000,001 (the equivalent of PLN 207,346,000, translated at the mid-exchange rate for NOK quoted by the National Bank of Poland for November 15th 2010). The new share, representing 0.0000002% of the company’s share capital, with a par value of NOK 1 (the equivalent of PLN 0.4822 translated at the mid-exchange rate for NOK quoted by the National Bank of Poland for November 15th 2010) was acquired by Grupa LOTOS S.A.

2 KEY OPERATING ACTIVITIES

2.1 RESEARCH AND TECHNICAL DEVELOPMENT ACHIEVEMENTS OF GRUPA LOTOS S.A.

Following the launch of the crude and vacuum distillation unit (CDU/VDU) built under the 10+ Programme, in 2010 Grupa LOTOS S.A. started to produce and market a new product: naphtha. Additionally, the Company’s R&D efforts focused on developing technologies for production of speciality products, based on further conversion of feedstock from the oil unit. The key R&D achievements in 2010 included:

- launch of the commercial production and sale of reduced-toxicity oil plasticizer for use in caoutchouc and rubber products, QUANTILUS T50. The new type of plasticizer is a TDAE (treated distillate aromatic extract) plasticizer which meets the EU requirements for plasticizers used in the tyre industry, effective as of January 1st 2010
- launch of the production and sale of low-oil Paraffin 64/25/0.5 as the main component for paraffin products (waxes),
- production and sale of the first batch of Ceresine as a component for production of white ceresine meeting the requirements set by the American Food and Drug Administration (FDA),
- launch of the sale of Filtrates made of medium and heavy slack wax, used as inputs for production of paraffin emulsions and anti-caking agents for artificial fertilisers. They are also used as impregnation agents for chipboard and kindling,
- launch of the sale of V1500 Bitumen used in production of various aggregate and bitumen mixtures,
- launch of the sale of 50 SDA Bitumen used for bitumen production based on air oxidation or blending.
In 2010, development work also focused on oil products produced by LOTOS Oil. The most important R&D activities related to lubricants included:

- commencement of research into ways of improving the quality of oils for passenger cars, in reliance on the Company’s own base oils. The research is scheduled to be completed in 2011,
- introduction of ten new types of engine oils (Lotos Quazar C-4, Lotos Quazar S, LOTOS Quazar K, Lotos Traffic PRO 025A/B, Lotos Traffic PRO 505.01),
- extension of 42 Approvals for lubricants,
- obtaining 6 Approvals for new oils.

### 2.2 KEY PRODUCTS, GOODS AND SERVICES OF GRUPA LOTOS S.A.

Grupa LOTOS S.A.’s sales revenue by products, goods for resale and services

<table>
<thead>
<tr>
<th>PLN '000</th>
<th>Jan 1 – Dec 31 2010</th>
<th>% share</th>
<th>Jan 1 – Dec 31 2009</th>
<th>% share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gasoline</td>
<td>5,904,912</td>
<td>22.4%</td>
<td>4,999,740</td>
<td>25.5%</td>
</tr>
<tr>
<td>Raw gasoline</td>
<td>239,858</td>
<td>0.9%</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Reformate</td>
<td>347,652</td>
<td>1.3%</td>
<td>211,631</td>
<td>1.1%</td>
</tr>
<tr>
<td>Diesel oil</td>
<td>15,223,879</td>
<td>57.8%</td>
<td>11,391,263</td>
<td>58.1%</td>
</tr>
<tr>
<td>Light fuel oil</td>
<td>952,332</td>
<td>3.6%</td>
<td>657,624</td>
<td>3.4%</td>
</tr>
<tr>
<td>Heavy fuel oil</td>
<td>1,269,871</td>
<td>4.8%</td>
<td>362,354</td>
<td>1.8%</td>
</tr>
<tr>
<td>Aviation fuel</td>
<td>559,800</td>
<td>2.2%</td>
<td>642,273</td>
<td>3.3%</td>
</tr>
<tr>
<td>Bunker fuel</td>
<td>77,182</td>
<td>0.3%</td>
<td>118,251</td>
<td>0.6%</td>
</tr>
<tr>
<td>Components for bitumen production</td>
<td>946,494</td>
<td>3.6%</td>
<td>694,958</td>
<td>3.5%</td>
</tr>
<tr>
<td>Base oils</td>
<td>441,498</td>
<td>1.7%</td>
<td>272,120</td>
<td>1.4%</td>
</tr>
<tr>
<td>Liquid gas</td>
<td>146,759</td>
<td>0.6%</td>
<td>98,406</td>
<td>0.5%</td>
</tr>
<tr>
<td>Other refinery products</td>
<td>136,515</td>
<td>0.5%</td>
<td>81,949</td>
<td>0.4%</td>
</tr>
<tr>
<td>Total petroleum products and goods for resale</td>
<td>26,246,752</td>
<td>99.7%</td>
<td>19,530,569</td>
<td>99.6%</td>
</tr>
<tr>
<td>Other goods for resale and materials</td>
<td>9,577</td>
<td>0.0%</td>
<td>8,358</td>
<td>0.0%</td>
</tr>
<tr>
<td>Services</td>
<td>88,354</td>
<td>0.3%</td>
<td>82,637</td>
<td>0.4%</td>
</tr>
<tr>
<td>Total</td>
<td>26,344,683</td>
<td>100.0%</td>
<td>19,621,564</td>
<td>100.0%</td>
</tr>
</tbody>
</table>
Elimination of excise duty and fuel charge

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>thousand tonnes</td>
<td>% share</td>
</tr>
<tr>
<td>Gasoline</td>
<td>1,448</td>
<td>16.75%</td>
</tr>
<tr>
<td>Raw gasoline</td>
<td>106</td>
<td>1.22%</td>
</tr>
<tr>
<td>Reformate</td>
<td>154</td>
<td>1.78%</td>
</tr>
<tr>
<td>Diesel oil</td>
<td>4,073</td>
<td>47.09%</td>
</tr>
<tr>
<td>Light fuel oil</td>
<td>386</td>
<td>4.46%</td>
</tr>
<tr>
<td>Heavy fuel oil</td>
<td>962</td>
<td>11.12%</td>
</tr>
<tr>
<td>Aviation fuel</td>
<td>251</td>
<td>2.90%</td>
</tr>
<tr>
<td>Bunker fuel</td>
<td>36</td>
<td>0.42%</td>
</tr>
<tr>
<td>Components for bitumen production</td>
<td>859</td>
<td>9.93%</td>
</tr>
<tr>
<td>Base oils</td>
<td>184</td>
<td>2.13%</td>
</tr>
<tr>
<td>Liquid gas</td>
<td>60</td>
<td>0.69%</td>
</tr>
<tr>
<td>Other refinery products</td>
<td>130</td>
<td>1.51%</td>
</tr>
<tr>
<td><strong>Total petroleum products and goods for resale</strong></td>
<td><strong>8,649</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

In 2010, sales volumes of Grupa LOTOS S.A. rose significantly - by 17.4% or 1,284 thousand tonnes, to 8,649 thousand tonnes - relative to 2009. Despite a less favourable sales structure due to the transition period related to the connection of new units built under the 10+ Programme to the existing refinery facilities, sales of high-margin products increased significantly.

Like in the previous year, diesel oil accounted for the largest share in the total sales volume. The volume of diesel oil sales amounted to 4,073 thousand tonnes in 2010, up by 10.4% on the 2009 figure. The share of diesel oil in the total sales volume stood at 47.09%. The second largest item in the structure of Grupa LOTOS S.A.’s sales was gasoline, whose share in total sales volume reached 16.75%. The volume of gasoline sales amounted to 1,448 thousand tonnes in 2010, up by 10.6% on the 2009 figure. The third largest item in the Company's sales structure and the last one with a share in total sales exceeding 10% was heavy fuel oil. Its share in total sales was 11.12%. Sales of this product group amounted to 962 thousand tonnes, up by 144.2% on the previous year, primarily on account of the transition period referred to above. In the sales
structure of Grupa LOTOS S.A. only two products - aviation fuel and bunker fuel - recorded lower sales. Their sales volume was 251 thousand tonnes (-31.4% yoy) and 36 thousand tonnes (-48.6% yoy), respectively.

2.3 CHANGES IN SALES MARKETS AND SOURCES OF SUPPLY OF MATERIALS, GOODS FOR RESALE AND SERVICES

Grupa LOTOS S.A.’s net sales revenue by markets

<table>
<thead>
<tr>
<th>PLN '000</th>
<th>Jan 1 – Dec 31 2010</th>
<th>% share</th>
<th>Jan 1 – Dec 31 2009</th>
<th>% share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic sales:</td>
<td>23,377,318</td>
<td>88.7%</td>
<td>18,168,618</td>
<td>92.6%</td>
</tr>
<tr>
<td>- products</td>
<td>22,991,656</td>
<td>87.3%</td>
<td>16,071,424</td>
<td>81.9%</td>
</tr>
<tr>
<td>- goods for resale and materials</td>
<td>385,662</td>
<td>1.4%</td>
<td>2,097,194</td>
<td>10.7%</td>
</tr>
<tr>
<td>Export sales:</td>
<td>2,967,365</td>
<td>11.3%</td>
<td>1,452,946</td>
<td>7.4%</td>
</tr>
<tr>
<td>- products</td>
<td>2,967,337</td>
<td>11.3%</td>
<td>1,428,382</td>
<td>7.3%</td>
</tr>
<tr>
<td>- goods for resale and materials</td>
<td>28</td>
<td>0.0%</td>
<td>24,564</td>
<td>0.1%</td>
</tr>
<tr>
<td>Total</td>
<td>26,344,683</td>
<td>100.0%</td>
<td>19,621,564</td>
<td>100.0%</td>
</tr>
<tr>
<td>of which: excise duty and fuel charge</td>
<td>(8,220,008)</td>
<td></td>
<td>(6,924,652)</td>
<td></td>
</tr>
<tr>
<td>TOTAL</td>
<td>18,124,675</td>
<td></td>
<td>12,696,912</td>
<td></td>
</tr>
</tbody>
</table>

Grupa LOTOS S.A.’s sales revenue by products and markets (thousands of tonnes)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic sales</td>
<td>Gasoline</td>
<td>1,158</td>
<td>1,144</td>
</tr>
<tr>
<td></td>
<td>Diesel oil</td>
<td>4,055</td>
<td>3,621</td>
</tr>
<tr>
<td></td>
<td>Diesel oil for heating purposes</td>
<td>386</td>
<td>327</td>
</tr>
<tr>
<td></td>
<td>Heavy fuel oil</td>
<td>103</td>
<td>87</td>
</tr>
<tr>
<td></td>
<td>Aviation fuel</td>
<td>75</td>
<td>145</td>
</tr>
<tr>
<td></td>
<td>Bunker fuel</td>
<td>36</td>
<td>39</td>
</tr>
<tr>
<td></td>
<td>Components for bitumen production</td>
<td>859</td>
<td>786</td>
</tr>
</tbody>
</table>
The significant growth in Grupa LOTOS S.A.’s sales volumes in 2010 was accompanied by higher export sales. In 2010 domestic sales increased by 589 thousand tonnes (up by 9.2% year on year – in line with the previous year’s trend), while export sales grew by 696 thousand tonnes (up by 72% year on year). The key factors driving up domestic sales of Grupa LOTOS in 2010 included an increase in the volume of diesel oil sold (up by 434 thousand tonnes, or 11.9% year on year, to 4,055 thousand tonnes), and a rise in the volume of components for bitumen production sold (up by 73 thousand tonnes, or 9.3%, to 859 thousand tonnes) and a higher volume of diesel oil for heating purposes (light fuel oil) sold (up by 59 thousand tonnes or 18% year on year). In 2010, the higher volume of export sales was primarily attributable to larger exports of heavy fuel oil (up by 179.8% year on year, to 859 thousand tonnes), gasoline (up by 75.8%, to 290 thousand tonnes), and reformate (up by 37.5%, to 154 thousand tonnes) as well as the launch of a new product - raw gasoline, whose sales volume was 106 thousand tonnes in 2010.

**Grupa LOTOS S.A.’s Key Customers in 2010**

Both in 2010 and 2009, the only customer accounting for more than 10% of Grupa LOTOS S.A.’s total sales revenue was LOTOS Paliwa Sp. z o.o. (a wholly-owned subsidiary of Grupa LOTOS S.A.), whose share was 45.79% in 2010 (2009: 47.47%).

---

**Table:**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>thousand tonnes</td>
<td>% share</td>
</tr>
<tr>
<td>Base oils</td>
<td></td>
<td>125</td>
<td>1.8%</td>
</tr>
<tr>
<td>LPG (Liquefied Petroleum Gas)</td>
<td></td>
<td>60</td>
<td>0.9%</td>
</tr>
<tr>
<td>Other refinery products</td>
<td></td>
<td>130</td>
<td>1.9%</td>
</tr>
<tr>
<td>Domestic sales, total</td>
<td></td>
<td>6,989</td>
<td>80.8%</td>
</tr>
<tr>
<td>Export sales</td>
<td>Gasoline</td>
<td>290</td>
<td>17.5%</td>
</tr>
<tr>
<td></td>
<td>Raw, gasoline</td>
<td>106</td>
<td>6.4%</td>
</tr>
<tr>
<td></td>
<td>Reformate</td>
<td>154</td>
<td>9.3%</td>
</tr>
<tr>
<td></td>
<td>Diesel, oil</td>
<td>18</td>
<td>1.1%</td>
</tr>
<tr>
<td></td>
<td>Heavy, fuel, oil</td>
<td>859</td>
<td>51.7%</td>
</tr>
<tr>
<td></td>
<td>Aviation, fuel</td>
<td>175</td>
<td>10.6%</td>
</tr>
<tr>
<td></td>
<td>Bunker, fuel</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td></td>
<td>Base, oils</td>
<td>59</td>
<td>3.6%</td>
</tr>
<tr>
<td>Export sales, total</td>
<td></td>
<td>1,661</td>
<td>19.2%</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>8,649</td>
<td>19.2%</td>
</tr>
</tbody>
</table>
### Grupa LOTOS S.A.‘s purchases of raw materials, goods for resale and petroleum materials by region

<table>
<thead>
<tr>
<th></th>
<th>PLN '000</th>
<th>Jan 1 – Dec 31 2010</th>
<th>% share</th>
<th>Jan 1 – Dec 31 2009 (restated)</th>
<th>% share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic purchases</td>
<td>1,717,257</td>
<td>10.2%</td>
<td></td>
<td>1,362,766</td>
<td>11.6%</td>
</tr>
<tr>
<td>Foreign purchases</td>
<td>15,189,574</td>
<td>89.8%</td>
<td></td>
<td>10,403,960</td>
<td>88.4%</td>
</tr>
<tr>
<td>Total purchases</td>
<td>16,906,831</td>
<td>100.0%</td>
<td></td>
<td>11,766,726</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

### Grupa LOTOS S.A.‘s supply structure

<table>
<thead>
<tr>
<th></th>
<th>PLN '000</th>
<th>Jan 1 – Dec 31 2010</th>
<th>% share</th>
<th>Jan 1 – Dec 31 2009</th>
<th>% share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Raw materials</td>
<td>16,595,408</td>
<td>88.2%</td>
<td></td>
<td>10,480,155</td>
<td>65.4%</td>
</tr>
<tr>
<td>Goods for resale</td>
<td>310,507</td>
<td>1.7%</td>
<td></td>
<td>1,285,694</td>
<td>8.0%</td>
</tr>
<tr>
<td>Services</td>
<td>832,045</td>
<td>4.4%</td>
<td></td>
<td>760,558</td>
<td>4.7%</td>
</tr>
<tr>
<td>Materials</td>
<td>166,298</td>
<td>0.9%</td>
<td></td>
<td>176,951</td>
<td>1.1%</td>
</tr>
<tr>
<td>Other purchases(1)</td>
<td>902,092</td>
<td>4.8%</td>
<td></td>
<td>3,333,698</td>
<td>20.8%</td>
</tr>
<tr>
<td>Total</td>
<td>18,806,350</td>
<td>100.0%</td>
<td></td>
<td>16,037,056</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

(1) Including tangible assets, tangible assets under construction, prepayments for tangible assets under construction and intangible assets.

### Grupa LOTOS S.A.‘s supply structure – petroleum products for resale

<table>
<thead>
<tr>
<th></th>
<th>PLN '000</th>
<th>Jan 1 – Dec 31 2010</th>
<th>% share</th>
<th>Jan 1 – Dec 31 2009</th>
<th>% share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Diesel oil</td>
<td>190,407</td>
<td>61.3%</td>
<td></td>
<td>966,844</td>
<td>75.2%</td>
</tr>
<tr>
<td>Gasolines</td>
<td>120,100</td>
<td>38.7%</td>
<td></td>
<td>318,850</td>
<td>24.8%</td>
</tr>
<tr>
<td>Total</td>
<td>310,507</td>
<td>100.0%</td>
<td></td>
<td>1,285,694</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

### Grupa LOTOS S.A.‘s supply structure – raw materials, semi-finished products and chemicals

<table>
<thead>
<tr>
<th></th>
<th>PLN '000</th>
<th>Jan 1 – Dec 31 2010</th>
<th>% share</th>
<th>Jan 1 – Dec 31 2009</th>
<th>% share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Crude oil</td>
<td>13,867,780</td>
<td>83.6%</td>
<td></td>
<td>7,245,454</td>
<td>69.2%</td>
</tr>
<tr>
<td>Diesel oil</td>
<td>1,063,699</td>
<td>6.4%</td>
<td></td>
<td>1,727,935</td>
<td>16.5%</td>
</tr>
<tr>
<td>MTBE/ETBE gasoline components</td>
<td>264,101</td>
<td>1.6%</td>
<td></td>
<td>188,049</td>
<td>1.8%</td>
</tr>
<tr>
<td>FAME</td>
<td>889,947</td>
<td>5.4%</td>
<td></td>
<td>578,296</td>
<td>5.5%</td>
</tr>
<tr>
<td>Gasoline</td>
<td>54,640</td>
<td>0.3%</td>
<td></td>
<td>212,750</td>
<td>2.0%</td>
</tr>
<tr>
<td>Heavy fuel oil</td>
<td>42,188</td>
<td>0.3%</td>
<td></td>
<td>103,494</td>
<td>1.0%</td>
</tr>
</tbody>
</table>
Grupa LOTOS S.A.
DIRECTORS’ REPORT ON THE OPERATIONS OF GRUPA LOTOS S.A.
IN 2010

<table>
<thead>
<tr>
<th>PLN '000</th>
<th>Jan 1 – Dec 31 2010</th>
<th>% share</th>
<th>Jan 1 – Dec 31 2009</th>
<th>% share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ethyl alcohol</td>
<td>156,821</td>
<td>0.9%</td>
<td>116,162</td>
<td>1.1%</td>
</tr>
<tr>
<td>Additives</td>
<td>20,322</td>
<td>0.1%</td>
<td>31,252</td>
<td>0.3%</td>
</tr>
<tr>
<td>Gasoil</td>
<td>87,648</td>
<td>0.5%</td>
<td>47,076</td>
<td>0.4%</td>
</tr>
<tr>
<td>Fuel oil components</td>
<td>-</td>
<td>0.0%</td>
<td>198,864</td>
<td>1.9%</td>
</tr>
<tr>
<td>Other</td>
<td>149,178</td>
<td>0.9%</td>
<td>31,699</td>
<td>0.3%</td>
</tr>
<tr>
<td>Total</td>
<td>16,596,324</td>
<td>100.0%</td>
<td>10,481,031</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

Grupa LOTOS S.A.’s Major Suppliers

In 2010, there were two suppliers whose shares in Grupa LOTOS S.A.’s purchases exceeded 10% of its total sales revenue: Mercuria Energy Trading of Switzerland and Petraco Oil Company Ltd. of the United Kingdom. The two suppliers’ shares in the purchases made by Grupa LOTOS S.A. amounted to 36.87% and 19.82%, respectively. To the best of the Company’s knowledge, by the date of publication of this Director’s Report on the Operations of Grupa LOTOS S.A. there were no formal links between Grupa LOTOS S.A. and any of the abovementioned suppliers.

2.4 EXTERNAL AND INTERNAL FACTORS MATERIAL FOR THE DEVELOPMENT OF GRUPA LOTOS S.A., AS WELL AS KEY RISKS AND THREATS, AND THE DEGREE OF THE ISSUER’S EXPOSURE TO SUCH RISKS OR THREATS

The key external factors material for the development of the Company include:

- **Quotation prices of crude oil and petroleum products** – changes of market prices of crude oil and petroleum products have a material impact on the Company’s financial performance,

- **PLN/USD exchange rate** – the performance of the Company is also, to a large/considerable extent, affected by foreign exchange rates, particularly the PLN/USD exchange rate, due to the fact that the prices of crude oil and of some products are quoted in the American dollar and due to Grupa LOTOS S.A.’s debt in that currency,

- **Petroleum products demand and supply levels** – the Company's performance is materially affected by changes in the level of supply and demand for petroleum products, which represent the key product group of the Company. The demand for diesel oil is expected to rise in the long run, while the demand for motor gasolines is expected to stabilise. These trends are reflected in the investment plans for the Company.
The key internal factors material for the development of the Company include:

- **Development of upstream business** – the planned development of the upstream business is expected to strengthen the Company's independence from external sources of raw materials, further improve its financial performance and enhance the Company's value,

- **Implementation of the 10+ Programme** – the implementation, completed in 2010, will in the long run be a material driver of Grupa LOTOS S.A.'s development and performance. The full start-up of the installations provided for in the Programme will allow the Gdańsk refinery to increase its processing capacity (to 10.5 million tonnes per annum) and the oil conversion ratio, which will have a positive effect on the product slate,

- **Further expansion of the fuel retail sales network** – the implementation of the service station network development programme is the key factor in strengthening the Company's position in the area of retail sales of fuels under the LOTOS brand.

**Major Risks and Threats**

Grupa LOTOS operates in an environment and conditions which entail a large number of risks. The risks inherent in the various areas of the Company's operations are first identified and assessed, and then reviewed to determine what further measures need to be taken. Compared with the previous reporting period, some of the operating, financial and market-related risks were relatively reduced thanks, among other things, to the efforts aimed to mitigate the impact of the global financial crisis, the completion of the implementation phase of the 10+ Programme and the introduction of various measures aimed to mitigate the risks identified earlier.

**Risks Related to the Government’s Strategy for the Oil and Gas Sector (Legal Risks of Strategic Character)**

Given Poland’s membership in the European Union, the normative acts of the Polish government are not the only source of legal risk, which may also stem from EU directives. In order to identify that risk, Grupa LOTOS keeps track of the trends in EU policies with regard to both proposed and existing directives affecting the oil sector, and cooperates with state authorities responsible for the development and implementation of the government strategy for the oil sector. In addition, the Company is involved in the process of issuing opinions on the draft and effective legislation concerning its area of interest, particularly mandatory stocks of oil and fuels, as well as biocomponents and biofuels.

The key risk in the area of biofuels and biocomponents is associated, like in the previous year, with the Polish authorities' failure to implement regulations transposing into national law the provisions of Directives 2009/30/EC and 2009/28/EC of the European Parliament and of the Council of April 23rd 2009, which provide for a higher biofuel content in standard fuels (B7, E10). Due to the lack of legal solutions provided for in the directives and the fact that National Indicative Targets (NCW) are annually increased, Grupa LOTOS is forced to market higher volumes of unprofitable biofuel B100.

In the area of mandatory stocks, it remains unclear in which direction the regulations will evolve. The time when mandatory stocks may start to be taken over from market operators by relevant governmental agencies is unknown, as is the speed of the process. According to the current draft law, the takeover of mandatory stocks is to span ten years. Another problem, which may
already be felt in 2011, will be a shortage of storage capacities to store mandatory stocks, especially of crude oil.

A serious risk arising from the prolonged legislative process in Poland is the impossibility to predict dates of entry into force of various legal regulations and the related consequences for the Company and the entire industry.

It is also time to take into account the risks associated with the introduction from 2013 of more stringent CO₂ emission requirements and with changes to the rules governing the allocation of CO₂ emission allowances. The authorities have yet to announce the relevant decisions, which makes it impossible to develop an appropriate model on which specific investment decisions would be based.

Risks Related to Changes and Interpretations of the Tax Law

The legal environment in which Grupa LOTOS operates has for many years been marked by significant instability. Newly enacted regulations and changes in interpretations of the provisions already in force affect the Company’s operations, its objectives, as well as the tax policy and the amount of tax liabilities.

It should be noted, however, that changes in tax laws may be a source of both opportunities and risks for the Company. Grupa LOTOS looks at many new interpretations of those laws as an opportunity to benefit from tax optimisation. There are interpretations which confirm the correctness of the Company's approach to certain transactions. However, it is equally probable that changes in the interpretations of tax laws may give rise to tax risk in transactions where such risk was non-existent before.

Differences in interpretations of tax laws are frequent, both between various tax authorities and between such authorities and businesses, which leads to uncertainties and conflicts, and in foreign transactions may compromise the Company’s reputation as a reliable business partner. This in turn may prompt the Company to give up profitable ventures or transactions for the sake of fiscal security.

These factors mean that the tax risk of doing business in Poland is significantly higher than in countries where tax regimes are better developed.

Another factor which necessitates a great deal of caution in managing tax risks is related to high potential penalties which may be imposed in the case of a fiscal offence or other violation of tax legislation, and the generally restrictive approach manifested by the Polish tax authorities. When conducting business activities, an entrepreneur has to reckon with the risk that an erroneous interpretation of the law, a human error on the part of its employee or incompetence of civil servants may inadvertently result in tax arrears, as a consequence of which it may face charges of committing an offence.

Given the frequent interpretive changes and enactment of new legal regulations, which are often inconsistent, convoluted or incompatible with the EU laws, Grupa LOTOS reviews and updates its internal procedures on an ongoing basis to ensure compliance with the requirements currently in force and to identify and mitigate any tax risks, and in particular their effect on the Company's financial statements. The process involves employees who actively participate in numerous training courses concerned with tax issues.
In situations where a tax risk related to a possibility of disparate interpretations is identified, Grupa LOTOS avails itself of the right to request an individual written interpretation issued by the Minister of Finance. Compliance with such interpretations eliminates the tax risk to the extent covered by a given interpretation.

Furthermore, Grupa LOTOS, as a member of Poland’s major organisations of employers and entrepreneurs, takes an active role in issuing opinions on draft legislation. This is primarily aimed at improving the quality of tax legislation, but also allows the Company's governing bodies to adequately respond to any changes in the legal environment.

**Financial Risks**

The key financial risk from the point of view of the Company’s operations is the risk related to prices of raw materials and petroleum products. The Company is in the process of developing a new policy for managing that risk, which will include the objectives connected with the introduction, with effect from January 1st 2011, of a new model of trade in raw materials and petroleum products within the Group.

**Currency risk management** - the management horizon is determined in line with the rollover budgeting period. The US dollar (USD) is the natural currency of the operating market of Grupa LOTOS. Consequently, Grupa LOTOS has a structurally long position in USD on its operating activity. For this reason, it was decided that USD was the most appropriate currency for contracting and repaying long-term loans to finance the 10+ Programme.

**Interest rate risk management** is connected with the cash flows which depend on future interest rates, in particular the expected schedule of repayments under the loan extended to finance inventories and the implementation of the 10+ Programme, and the resulting interest calculated on the basis of a floating rate (LIBOR USD).

**Management of risk related to prices of carbon dioxide (CO₂) emission allowances** - the management horizon is determined by the subsequent phases of the Kyoto protocol; the current management horizon runs until the end of 2012.

**Liquidity risk management process** consists in monitoring the forecast cash flows and available sources of financing, and then matching the maturities of assets and liabilities, analysing the working capital and maintaining access to various sources of financing. Liquidity management is consolidated to cover the whole Group.

Measures designed to mitigate the risk of restricting or change in conditions of access to external financial include contracting loans with a wide group of financial institutions, the correct, complete and timely fulfillment of disclosure obligations, analysis and compliance with the financial indicators and covenants, as well as with other obligations towards banks stipulated in the loan agreements. In addition, Grupa LOTOS monitors the credit ratings and general standing of the banks with which it contracts financing.

**Management of credit risk relating to counterparties in financial transactions** consists in ongoing monitoring of the credit exposure in relation to the limits granted. The counterparties must have an appropriate credit rating, assigned by leading rating agencies, or hold guarantees from institutions meeting the minimum rating requirement. Grupa LOTOS S.A. enters into financial transactions with reputable firms with sound credit standing, and diversifies the group of institutions with which it cooperates.
As regards management of credit risk relating to counterparties in non-financial transactions, all customers requesting trade credit or payment limits undergo verification of their creditworthiness, whose results determine the amount of credit or limits to be granted. Decisions related to evaluation of business partners are made by the Credit Committees, set up within the marketing segment of the LOTOS Group.

As at December 31st, the carrying value of financial assets and liabilities (trade and other receivables, borrowings, deposits, security deposits (margins), financial assets - derivative financial instruments, other financial assets, cash and cash equivalents, trade and other payables, loans, financial liabilities - derivative financial instruments) denominated in foreign currencies (USD and EUR) and restated in PLN as at the balance-sheet date - which are sensitive to currency risk - amounted to PLN 7,100,822 thousand net.

A change in USD exchange rate up or down by 4% could potentially lead to a change in the value of financial assets and liabilities as at December 31st 2010 of PLN ±321,858 thousand net.

A change in EUR exchange rate up or down by 4% could potentially lead to a change in the value of financial assets and liabilities as at December 31st 2010 of PLN ±38,764 thousand net.

As at December 31st 2010, the Company held futures for the purchase of carbon dioxide (CO2) emission allowances (EUA – Emissions Unit Allowance), measured at fair value.

As at December 31st 2010, the financial assets related to positive valuation of the futures for the purchase of carbon dioxide (CO2) emission allowances amounted to PLN 615 thousand.

As at December 31st 2010, the financial liabilities related to negative valuation of the futures for the purchase of carbon dioxide emission allowances were PLN 463 thousand.

A change in the price of carbon dioxide (CO2) emission allowances up or down by 10% could potentially lead to a change in the fair value of financial assets and liabilities related to the futures for the purchase of carbon dioxide emission allowances of PLN ±176 thousand.

As at December 31st 2010, the carrying value of financial assets and liabilities (borrowings, deposits, security deposits (margins), cash and cash equivalents, derivative financial instruments, liabilities under loans, finance lease and derivative financial instruments) which are sensitive to interest rate risk amounted to PLN -5,795,115 thousand net.

A change in interest rates up or down by 0.2% could potentially lead to a change in the value of financial assets and liabilities as at December 31st 2010 of, respectively, PLN 3,212 thousand and -3,353 thousand net.

The financial risk management policies and instruments and the impact of the key risk factors on the individual items of financial results have been presented in the Notes to the consolidated financial statements.

Risks Related to the Upstream Business

Risks related to the upstream business include production and technical risks, exploration risks, risks related to the geological characteristics of the fields or weather-related risks. All of them are monitored and appropriate strategies are implemented with a view to mitigating them.

One of the major risks are process risks associated with the production of hydrocarbons. These include risks of oil spills, marine collisions, fires, gas eruptions and other failures. A number of
preventive measures are applied, such as leakage testing, monitoring of fire risk parameters and eruption risk prevention, for example by securing the boreholes. Additionally, procedures have been put in place applicable in day-to-day work and when a threat of failure occurs. An important measure helping to reduce the risk is the provision of regular training courses and practical exercises for staff. In the event of an incident or accident, a thorough analysis is conducted, and the event itself is discussed at the training courses held at that time, with a view to preventing its recurrence.

**Technical risks** are associated with the equipment used to exploit hydrocarbons. It is mitigated through ongoing monitoring of the condition and performance of the equipment, as well as technical supervision (according to the schedule of periodic reviews) and performance of necessary tests. Regular training courses are also provided to staff to teach them how to operate the equipment/components in order to minimise the risk of human error.

**The exploration risk** follows largely from incorrect estimation of in-place resources. Therefore, such resources are always estimated (in accordance with the SPE 2007 resources classification system) for three scenarios P10/P50/P90, which means that quantities are given that can be potentially recovered with the 10%, 50% and 90% probability. In addition, the internal Chance of Success (CoS) rate is applied when evaluating the potential of the play covered by geological testing. Moreover, in the design phase there is the risk of having to conduct additional, in-depth geological analyses of plays with high production potential.

Other risks in the upstream area are related, among other things, to possible occurrence or intensification of phenomena which may cause loss of wells or declines in well rates (e.g. falling reservoir pressures, entry of water), as well as bad weather, which may lead to a suspension of work or production.

**Risks Related to the Supply of Raw Materials**
Grupa LOTOS continues its efforts related to the strategy of diversification of crude oil supplies, focusing on two key aspects of this strategic goal:

- **security of crude oil supplies**: steady expansion of presence on the international oil market, regular contracting of various types of oil, while creating conditions to radically increase their share in total supplies to the refinery in case of a threat to the continuity of supplies from the main direction, increasing the role of own production,

- **improvement of competitiveness**: by fully capitalising on the coastal location of the Gdańsk refinery and the possibility to source oil supplies through two independent channels: Russian oil through the Druzhba Pipeline and various types of oil available through Naftoport.

An appropriate selection of types of oil and directions of supplies is the result of optimisation efforts, carried out on an ongoing basis, to maximise the integrated margin.
Risks Related to Operating Activities

The management of risks related to operating activities covers various areas: from process and technology-related risks, to workplace safety and environmental risks, to legal risks relating to the respective areas.

Risks Related to Implementation of the 10+ Programme

Risks related to the implementation of the 10+ Programme, which were quite significant in recent years, have either markedly diminished or been altogether eliminated. This is attributable to the mitigation measures applied by Grupa LOTOS with respect to those risks, as well as the fact that the implementation phase of the 10+ Programme (construction of all units) has been completed, as a consequence of which the likelihood of the occurrence of such risks is now minimal.

Detailed analyses of major risks in the area of this investment project were carried out, which allowed the Company to determine the best ways of dealing with them. The greatest risk was associated with possible delivery or fitting in of defective installations/equipment and materials, which could necessitate repairs and replacements, driving up costs and causing delays. The measures applied, including the preparation of a list of preferred suppliers and a list of entities with which contracts should be avoided, monitoring of critical equipment, inspection of fixtures, performance of the appropriate amount of diverse testing (e.g. tests of the chemical composition and thickness of selected pipeline components, identification of materials and quality of joints) and compliance with internal standards, allowed us to reduce the above risks. In terms of quality control, the measures undertaken helped to avert events which could have critically affected the project. Thanks to implemented controls, some risks were detected at a stage when it was still possible to eliminate them completely. In the few cases where any of the risks materialised, the scope of control was extended, which allowed to eliminate the risk of similar events in further work. It should be noted, however, that there is still a risk that any latent defects in the materials supplied may be identified during their lifetime. Despite the fact that a majority of the units built as part of the 10+ Programme have already been proven, tested and put into operation, the risk of identifying defects during the start-up and initial period of operation still exists with respect to those units which are currently in the start-up phase. Any such event may disorganise and/or delay the start-up work, affecting the implementation schedule of the entire Programme. Furthermore, in some cases, late detection of such defects, after a facility has already been put into service, may give rise to risks associated with workplace safety, fires and explosions.

The 10+ Programme also involves a number of other risks which have been subject to supervision and monitoring, as a result of which the project has so far been implemented according to schedule and within budget. Currently, the main risk related to the 10+ Programme has to do with the Company's ability to complete the entire project by the deadlines specified in the loan agreement and perform the required tests.

However, on the basis of experience gained while carrying out the 10+ Programme and managing the related risks, measures were designed to reduce the identified risks, also when new projects are implemented in various areas Grupa LOTOS’ business.
Environmental Risks

Grupa LOTOS’ operating activities entail certain environmental risks, the most important of them being:

- risk of failure to comply with the requirements of environmental laws (Polish and EU),
- risk related to shortage of CO₂ emission allowances,
- risk of serious industrial failure (described in detail further on, in the section devoted to the process and technology-related risks).

The likelihood that the risk of non-compliance with the legal requirements might materialise is minimised through ongoing monitoring of the Polish and EU laws, efficient implementation of their provisions and taking an active and effective role in the legislative process. Any identified environmental law requirements are notified, in the form of information or orders, to all those at Grupa LOTOS for whom such requirements are relevant. The processes of obtaining permits are carried out with a sufficient time reserve, taking into account the risk that administrative proceedings might last longer than expected, which guarantees that the relevant documents will be obtained in time. Grupa LOTOS is making intensive efforts to mitigate the risk related to the need to secure a sufficient number of CO₂ emission allowances. Legislative changes at the level of Polish and EU laws are monitored on a routine basis. The Company has ongoing liaison with the National Administrator, while applications for new allowances are prepared sufficiently in advance.

For the refining units which participate in the EU Emissions Trading Scheme, including units constructed as part of the 10+ Programme which were commissioned in 2010 (CDU/VDU, HDS, HGU and ASR), the number of allowances will suffice until the end of the current trading period, i.e. 2012. Additional allowances were granted for the CHP, whose emissions have increased in
connection with the supply of heat supporting the operation of the above units. Given that the last units covered by the 10+ Programme are being commissioned, in the near future Grupa LOTOS will apply for allowances from the national reserve for the MHC and ROSE units and for the CHP, whose emissions will increase further as the new refinery production units will be connected with the CHP. It is expected that a relevant decision is made by the National Administrator in mid-2011.

Process and Technology-Related Risks, Risks Related to Workplace Safety

One of the key risks for Grupa LOTOS, addressed by specially designed preventive and preparatory measures, is the risk of industrial failure. Emergency events may disrupt the work of refining units, cause excessive emissions of pollutants into the environment or accidents at work. To prevent such events, a variety of precautions are taken, such as diagnosing the technical condition of the units and equipment, establishing an appropriate inspection agenda on the basis of analyses, e.g. corrosion reports, using lists of eligible vendors of equipment and providers of technical services, and the implementation of various operational procedures, including with respect to acceptance and inspection of supplies.

Grupa LOTOS also carries out criticality analyses of the equipment, as part of which it identifies and assesses risks and implements appropriate action plans for individual items of equipment, depending on their degree of criticality. All equipment supporting the work of units has been classified on the basis of the following criteria:

- safety for humans and the environment,
- the importance from the perspective of the refinery,
- the importance from the perspective of the units,
- probability of failure,
- complexity of repair.

The classification of a piece of equipment to a specific criticality group determines the selection and application of an optimal strategy for maintenance of its operations.

The refinery also uses technologies and equipment meeting the BAT criteria (Best Available Techniques). Process units are equipped with adequate safety and security solutions, including multi-layered security systems (prevention, protection and counteraction layers). Alarm, emergency stop and shutdown systems are deployed in order to prevent uncontrolled development of an emergency situation and serious damage to machinery and equipment.

In order to mitigate the effects of the risk, failure response training and exercises are provided on a regular basis to all employees of the refinery, to ensure prompt and effective response to any actual failures.

If an emergency event does occur, a thorough analysis of its causes is performed (Root Cause Analysis). Based on its findings, measures are implemented designed to prevent the recurrence of such failures in future. Information gathered about the various failures and incidents is used in subsequent assessments of the technology-related risk.

Given the nature of Grupa LOTOS' production processes, workplace safety is an issue of utmost importance for the Company. Many jobs are exposed to hazardous or noxious factors,
which is why each job is assessed in terms of inherent occupational risks, including risks related to explosive atmosphere, noise, vibration or presence of chemical and biological substances. On the basis of that assessment, individual and collective security systems are deployed.

New technical and organisational measures are also put in place to ensure safe working conditions for all persons staying and/or working on the premises of and for Grupa LOTOS. Regular checks of the procedures are undertaken and the requirements are enforced. In many cases, the rules implemented at Grupa LOTOS are more stringent than those required by law.

Grupa LOTOS attaches particular importance to raising employee awareness of occupational safety. This objective is being accomplished for instance through a series of above-standard initiatives and programmes designed to promote awareness of the health and safety-at-work issues in accessible and interesting ways. The Company also implements incentive schemes in that area.

All the above activities are designed to ensure safe conditions of the work and processes taking place at Grupa LOTOS, which is a priority concern for the Company.

Risk management in the operating area is also related to limiting the likelihood of failure to comply with the legal requirements applicable to the operations of Grupa LOTOS. This risk is minimised through ongoing monitoring of the Polish and EU laws, efficient implementation of their provisions and taking an active and effective role in the legislative process.

Risk of Stricter Quality Requirements for Petroleum Products

Grupa LOTOS S.A. keeps a close eye on the proposed new standards and regulations relevant for its production and sales. The source of information about future changes in the quality requirements is Technical Committee 222 at the Polish Committee for Standardisation, responsible for petroleum products and process liquids. Thanks to active participation in the work of the subcommittees of Technical Committee 222, Grupa LOTOS is able to issue opinions on proposed EU standards at the stage of their development.

Grupa LOTOS has an additional impact on the level of quality requirements, in particular requirements applicable to engine fuels, through participation in the works of an industry association, the Polish Organisation of Oil Industry and Trade (POPiHN). The Group’s participation in that body’s work substantially reduces the risks of delayed compliance with future quality standards for petroleum products. In 2010, a change was expected in the quality requirements for gasolines and diesel oils regarding the admissible content of biocomponents. The change, whereby the admissible content of FAME was to be raised to 7% of the total volume, was not effected, and is now expected in 2011. Work is also under way to admit to trading gasolines with ethanol content of up to 10% of the volume. Grupa LOTOS is already prepared for those changes and thus they do not pose any threat to the Company’s continuing as a going concern.

Marketing Risks

Risk management in the area of Grupa LOTOS’ marketing activities covers both market-related and financial risks associated with the liquidity of its counterparties. For a description of the Group’s strategy for managing the credit risk of its non-financial counterparties, see the financial risks section.
One of the key marketing risks to which Grupa LOTOS is exposed is the **risk of declining margins** due to price competition. The most important measure addressing the price risk is the ongoing monitoring of parameters related to prices and margins, in conjunction with the monitoring of sales volumes and results. The Group is planning to introduce tools and mechanisms that will allow it to fine-tune pricing to optimise achieved margins. In addition, in the retail sector, the Group is diversifying into market segments less susceptible to downward pressure on margins due to competition (both existing and potential), while making efforts aimed to foster sustained customer loyalty, for example by enhancing the loyalty scheme at LOTOS service stations, the Navigator and LOTOS Biznes schemes.

Grupa LOTOS also manages the **risk of reduced demand**. High availability of fuels (increased supply in the domestic market plus imports) is likely to drive down the market prices, which in turn may adversely affect the volume of the Group's sales. To mitigate that risk, sales are made through various distribution channels, while the production processes are continuously enhanced.

Risk management in the marketing area is also focused on maintaining uninterrupted supplies of products to the market. At Grupa LOTOS, the process is coordinated by the Supply Chain Management Committee, whose role is to guide the Group's operating activities in the area of production, procurement, logistics and sales, in terms of the whole supply chain. Additionally, any logistical constraints are taken into account in the process of operational planning and optimisation. Moreover, the availability times of the distribution centres are constantly monitored.

In order to minimise the risks associated with loss of products as a result of theft or improper handling during storage or transport, agreements are only concluded with eligible suppliers, while the parameters throughout the logistic chain are constantly monitored.

Mitigation measures are also taken to address the risk arising from the proposed legislative changes in respect of mandatory stocks, which may increase the costs of logistics.

In order to ensure effective and prompt response to the various risks and emergencies, Grupa LOTOS has developed crisis scenarios for the most strategic areas, including oil supplies, oil processing, fuel production, product storage and logistics.

### 2.5 GRUPA LOTOS S.A.'S DEVELOPMENT PROSPECTS TAKING INTO ACCOUNT THE ASSUMED MARKET STRATEGY

The Strategy for the LOTOS Group until 2015, approved on November 16th 2010, provides for the continuation of the current policy oriented towards stimulating sustainable growth of the core business, i.e. the exploration for and production of hydrocarbons, deep crude conversion focused on the production of fuels, and trade in high-margin petroleum products, with a focus on the overriding strategic objective of building shareholder value.

In the marketing area, the strategic objective is to maximise the economic benefits from trading in gasoline, diesel oil and aviation fuel by flexibly adjusting product streams and further strengthening the market position. Sales of other products will be optimised to achieve the best possible economic effect. In order to maximise the integrated margin, the LOTOS Group will focus on optimum use of its assets and coordination of its activities in the four key areas of the supply chain, including planning, procurement, production and distribution. If activities in these four areas are harmonised, the Group will have quicker access to information supporting
decision making, and thus will be able to respond more rapidly to the changing market environment.

In the refining area, the Company's strategic objective is to maintain its highly competitive position among the European refineries and to ensure optimum use of its assets, including the already existing ones and those it will come to hold following completion of new development projects.

2.6 ENVIRONMENTAL ISSUES

Reduction of Environmental Impact

For many years, the Company's strategy for reducing its environmental impact has been based on the principles of sustainable growth, in compliance with the environmental standards prescribed by law and with due regard to corporate social responsibility. The sustainability and corporate social responsibility principles also entail the delivery of high quality products, leaving the smallest environmental footprint possible, and promotion of pro-environmental attitudes among employees using various communication channels. The environmental impact of the individual industrial processes and the refinery as a whole is mitigated through:

- Reduction of emissions of pollutants into the atmosphere by using equipment and measures designed to help protect the environment, such as tightening and air-tight sealing systems and other emission reduction methods. 2010 saw the completion of an investment task involving replacement of burners in the CHP plant's boilers with low-NOx emission burners.

- Reduction in the amount of water and wastewater discharged from the Group's wastewater treatment plant, through reuse of treated wastewater in the production of process water. The parameters of wastewater discharged by the three-stage treatment plant are better than required by law.

- Reduction in the volume of waste through proper waste management. The volume of waste generated during crude processing is insignificant, with 95% of the waste being used in recovery and recycling processes.

Development Plans

In the years to come, the environmental impact of the individual industrial processes and the refinery as a whole will be mitigated by switching to natural gas as the basic fuel for the refinery and feedstock in hydrogen production, and by utilising discharge gases currently burned in flares. When the projects are completed, the level of atmospheric emissions will be significantly reduced.

Grupa LOTOS is also involved in the construction of a high-efficiency gas-fired power plant, which will partly replace the existing oil-fuelled CHP plant.

The emissions to air, ground and water are to be reduced through implementation of the following development plans aimed at reducing environmental impact of the LOTOS Group companies:
RCEkoenergia – upgrade of the OR32 boiler designed to increase its efficiency and thus reduce emissions to air;

LOTOS Petrotalctic – completion of the investment task involving construction of a water injector system, which will prevent hydrocarbon-contaminated water from being discharged into sea;

LOTOS Asfalt – air-tight sealing of the tank park and infusing processes designed to reduce unintentional emission of hydrocarbons;

LOTOS Jasło – investment projects aimed at protecting the storage facility park against possible spills;

LOTOS Czechowice – investment projects connected with the construction of anti-spill trays at railway handling stands.

3 AGREEMENTS, RELATED-PARTY TRANSACTIONS AND COURT PROCEEDINGS

3.1 EVENTS AND AGREEMENTS SIGNIFICANT FOR THE OPERATIONS OF GRUPA LOTOS S.A.

Significant Agreements

Significant Agreement between Grupa LOTOS S.A. and BP Polska S.A.

On December 31st 2009, Grupa LOTOS S.A. and BP Polska S.A. of Kraków executed an agreement on the sale of liquid fuels by Grupa LOTOS S.A. to BP Polska S.A. The agreement was concluded for a specified period from January 1st to December 31st 2010 and its estimated value totals PLN 2.4bn. The maximum value of the contractual penalties is estimated at PLN 44m. The agreement does not contain any provisions under which the parties would be entitled to seek any additional compensation above the contractual penalties. The other terms and conditions of the agreement do not differ from standard provisions commonly applied in agreements of such type.

Significant Agreement between Grupa LOTOS S.A. and LOTOS Asfalt Sp. z o.o.

On February 26th 2010, Grupa LOTOS S.A. entered into an agreement with LOTOS Asfalt Sp. z o.o. of Gdańsk (a wholly-owned subsidiary of Grupa LOTOS S.A.), under which Grupa LOTOS S.A. will sell marine fuel to LOTOS Asfalt Sp. z o.o. The agreement was concluded for an indefinite period, starting on March 1st 2010. Its estimated value over five subsequent years totals approximately PLN 570m. The maximum value of the contractual penalties is estimated at approximately PLN 5.5m. The agreement does not contain any provisions which would prevent the parties from seeking additional compensation above the contractual penalties. The other terms and conditions of the agreement do not differ from standard provisions commonly applied in agreements of such type.

Significant Agreement between LOTOS Paliwa Sp. z o.o. and Anwim S.A.

On April 1st 2010, the turnover generated by LOTOS Paliwa Sp. z o.o. (a wholly-owned subsidiary of Grupa LOTOS S.A.) under the agreement of July 23rd 2007 with Anwim S.A. of Warsaw reached PLN 616m in the last 12 months. The agreement, concluded for an indefinite
period, concerns the sale of liquid fuels by LOTOS Paliwa Sp. z o.o. to Anwim S.A. It provides for standard contractual penalties whose value may exceed the equivalent of EUR 200 thousand and depends on the quantity of non-supplied or uncollected products. The agreement does not contain any provisions which would prevent the parties from seeking additional compensation above the contractual penalties. The other terms and conditions of the agreement do not differ from standard provisions commonly applied in agreements of such type.

**Agreement on Supplies of Crude Oil between Grupa LOTOS S.A. and Mercuria Energy Trading S.A.**

On May 7th 2010, the total value of the agreements concluded between Grupa LOTOS S.A. and Mercuria Energy Trading S.A. of Geneva since the execution of the last significant agreement between these entities, i.e. since December 4th 2009, reached USD 239.9m (PLN 787.2m, translated at the mid-exchange rate for USD quoted by the National Bank of Poland for May 7th 2010). In terms of value, the largest of those agreements is the agreement of May 7th 2010 on the supply of 150,000 tonnes of REBCO crude oil. The agreement provides for supplies of the crude through the Druzhba Pipeline. As at the agreement date, its estimated value was USD 85.6m (PLN 280.9m, translated at the mid-exchange rate for USD quoted by the National Bank of Poland for May 7th 2010). The agreement does not include any condition precedent or specify any date of events giving rise to a claim (dies a quo), it does not provide for any contractual penalties and its terms and conditions do not differ from the terms and conditions commonly applied in agreements of such type.

**Significant Agreement between Grupa LOTOS S.A. and PGNiG S.A.**

On June 16th 2010, Grupa LOTOS S.A. and Polskie Górnictwo Naftowe i Gazownictwo S.A. of Warsaw entered into an agreement providing for the supply of natural gas to Grupa LOTOS S.A. starting from December 16th 2011. Pursuant to the agreement, upon justified request by Grupa LOTOS S.A., the starting date of the gas supplies may be postponed by six months, i.e. until June 15th 2012. The agreement was concluded for an indefinite period. The estimated value of the agreement in the period of five years amounts to approximately PLN 2,208m. The estimated maximum contractual penalties may exceed 10% of the agreement’s value, and their amount depends on the quantity of gas ordered but not taken off by Grupa LOTOS S.A. The agreement does not contain any provisions under which the parties would be entitled to seek any additional compensation above the contractual penalties. The other terms and conditions of the agreement do not differ from standard provisions commonly applied in agreements of such type. The agreement has been concluded in order to ensure higher supplies of network natural gas to Grupa LOTOS S.A.’s refinery, which will replace the fuels currently used, including LPG, light gasoline, and – to some extent – fuel oil. LPG is currently used in the fuel gas system and together with light gasoline is used to produce hydrogen. The projected annual supplies of natural gas in 2012 will be 403 million cubic metres, and the target annual volume is 447 million cubic metres. In addition to savings which will be generated thanks to the replacement of the aforementioned fuels with network gas, the change will increase the production of liquefied fuels and limit CO2 emissions by Grupa LOTOS S.A.’s refinery.

**Significant Agreement between Grupa LOTOS S.A. and Mitsubishi International GmbH**

On November 15th 2010, Grupa LOTOS S.A. executed an agreement with Mitsubishi International GmbH of Dusseldorf, Germany, to sell xylene fraction to Mitsubishi International GmbH. Supplies of xylene fraction under the agreement are due to start between May 15th 2012
at the earliest and November 15th 2012 at the latest. The agreement was concluded for a term of 42 months, counting from the day on which the supplies start. Each party has the right to terminate the agreement in the period of six months after the supplies start, if any of the circumstances specified in the agreement arise. The estimated value of the agreement over its term amounts to PLN 805.3m (net of VAT). The agreement does not provide for any contractual penalties and so each party may only assert claims up to the value of the agreement. The other terms and conditions of the agreement do not differ from standard provisions commonly applied in agreements of such type. The objective behind the agreement is to further diversify Grupa LOTOS S.A.’s product portfolio, while reducing the share of aromatic hydrocarbons in the range of gasoline components produced by the Gdańsk refinery, as some of the product leaving the catalytic reforming unit (the reformate) will be further processed at the xylene separation unit. At present, any surplus volumes of reformate are exported. Thanks to the production and sale of the xylene fraction, which is used as petrochemical feedstock, Grupa LOTOS S.A. will be able to generate a sustainably higher margin on sales, compared with that generated on reformate exports. The agreement was classified as significant as its estimated value exceeded 10% of Grupa LOTOS S.A.’s equity.

Agreement on Supplies of Crude Oil between Grupa LOTOS S.A. and Petraco Oil Company Ltd.

On December 13th 2010, Grupa LOTOS S.A. signed an agreement with Petraco Oil Company Ltd of Guernsey on the supply of REBCO crude oil to Grupa LOTOS S.A. in December 2010. The agreement provides for supplies of the crude through the Druzhba Pipeline. The aggregate value of agreements concluded between the two companies during the last 12 months totals approx. USD 290m (PLN 882.91m translated using the mid-exchange rate for USD quoted by the National Bank of Poland for December 13th 2010), and reached the value of a significant agreement, as it exceeded 10% of Grupa LOTOS S.A.’s equity. The largest transaction (in terms of value) concluded between the two companies was the agreement of October 1st 2010 providing for the supplies of REBCO crude oil. Its value amounts to USD 119.31m (PLN 343.28m translated using the mid-exchange rate for USD quoted by the National Bank of Poland for October 1st 2010). The agreement does not include any condition precedent or specify any date of events giving rise to a claim (dies a quo), it does not provide for any contractual penalties and its terms and conditions do not differ from the terms and conditions commonly applied in agreements of such type.

Significant Fuel Sales Agreement between Shell Polska Sp. z o.o. and Grupa LOTOS S.A.

On December 29th 2010, Grupa LOTOS S.A. entered into an agreement with Shell Polska Sp. z o.o. of Warsaw on the sale of liquid fuels by Grupa LOTOS S.A. to Shell Polska Sp. z o.o. The agreement was concluded for a specified period, from January 1st to December 31st 2011, and its value (VAT exclusive) is estimated at about PLN 4bn. The maximum value of the contractual penalties is estimated at PLN 64m. The agreement does not contain any provisions under which the parties would be entitled to seek any additional compensation above the contractual penalties. The other terms and conditions of the agreement do not differ from standard provisions commonly applied in agreements of such type. The agreement was classified as significant as its estimated value exceeded 10% of Grupa LOTOS S.A.’s equity.
Agreements Concluded after the Balance-Sheet Date

**Significant Agreement on Sale of Liquid Fuels to BP Europa SE**

On January 10th 2011, Grupa LOTOS S.A. entered into an agreement with BP Europa SE of Hamburg, operating in Poland through BP Europa SE Polish Branch of Kraków, on sale of liquid fuels by Grupa LOTOS S.A. to BP Europa SE Polish Branch of Kraków.

The agreement was concluded for a specified period from January 10th to December 31st 2011. Its estimated net value is approx. PLN 1.7bn.

The maximum value of the contractual penalties is estimated at approx. PLN 29m.

The agreement does not contain any provisions under which the parties would be entitled to seek any additional compensation above the contractual penalties.

The other terms and conditions of the agreement do not differ from the terms and conditions commonly used in agreements of such type.

**Agreement on Supplies of Crude Oil between Grupa LOTOS S.A. and Petraco Oil Company Ltd.**

On February 28th 2011, Grupa LOTOS S.A. signed an agreement with Petraco Oil Company Ltd of Guernsey on the supply of REBCO crude oil to Grupa LOTOS S.A. in March 2011. The agreement provides for supplies of the crude through the Druzhba Pipeline.

The total value of agreements concluded between the two parties in the period from the release date of the previous report (Current Report No. 32/2010 of December 13th 2010) until today amounts to ca. USD 301.3m (i.e. PLN 866.69m translated at the USD mid-exchange rate quoted by the National Bank of Poland for February 28th 2011) and has reached the value of a significant agreement, i.e. more than 10% of Grupa LOTOS S.A.’s equity.

In terms of value, the largest of these agreements is the agreement of February 28th 2011 on the supply of REBCO crude oil, which is worth USD 197.0m (i.e. PLN 566.67m translated at the USD mid-exchange rate quoted by the National Bank of Poland for February 28th 2011).

The agreement does not include any condition precedent or specify any date of events giving rise to a claim (dies a quo), it does not provide for any contractual penalties and its terms and conditions do not differ from the terms and conditions commonly used in agreements of such type.

**Agreement on Supplies of Crude Oil between Grupa LOTOS S.A. and Eminent Energy Trading S.A.**

On April 6th 2011, Grupa LOTOS S.A. signed an agreement with Eminent Energy Ltd of Nicosia on the supply of REBCO crude oil to Grupa LOTOS S.A. in April 2011. The agreement provides for supplies of the crude through the Druzhba Pipeline.

The total net value of agreements concluded between the two parties in the last 12 months amounts to ca. USD 240.56m (i.e. PLN 670.27m) and has reached the value of a significant agreement, i.e. more than 10% of Grupa LOTOS S.A.’s equity.

In terms of value, the largest of these agreements is the agreement of April 6th 2011 on the supply in April 2011 of REBCO crude oil to Grupa LOTOS S.A., which is worth USD 84.82m
(VAT exclusive) (i.e. PLN 237.38m translated at the USD mid-exchange rate quoted by the National Bank of Poland for April 6th 2011).

The agreement does not include any condition precedent or specify any date of events giving rise to a claim (dies a quo), it does not provide for any contractual penalties and its terms and conditions do not differ from the terms and conditions commonly used in agreements of such type.

Events Significant for the Operations of Grupa LOTOS S.A.

10+ Programme

The 10+ Programme is the largest CAPEX project to have ever been undertaken by the LOTOS Group. Its goal was to increase the throughput capacities and depth of conversion of the Gdańsk refinery, and consequently to improve the Company’s competitive position. 2010 saw the completion and launch of a number of key production units constructed as part of the 10+ Programme.

As at the end of December 2010, the 10+ Programme reached a 100% completion status, meaning it was completed as scheduled. All the work connected with the engineering design, procurement and construction has been completed for all the basic and auxiliary installations.

MHC (mild hydrocracking) unit, the largest facility constructed as part of the 10+ Programme, was assigned the RFSU (Ready For Start Up) status on October 10th 2010. On October 27th, feedstock was fed into the unit. The first product streams obtained in mid-January 2011 were of very high quality, with the conversion ratio – measured as a percentage of the highest value products – standing at 70% (the design conversion ratio is 60%). The main purpose of the MHC unit is to intensify oil processing and obtain a higher yield of top quality fuel components from each barrel of crude oil, which is a distinguishing parameter of the most advanced refineries in Europe and globally.

The residuum oil supercritical extraction (ROSE) unit, as the last of the 10+ Programme facilities, was assigned the RFSU (Ready For Start Up) status on December 31st 2010, in line with the schedule. Commercial launch of the unit is expected to take place at the end of February 2011.

Work on the 10+ Programme was carried out without major disruptions. Since the launch of the 10+ Programme, Grupa LOTOS S.A. applied measures aimed at minimising the identified execution risks. The work was entrusted to experienced contractors with sound technical and financial standing, able to execute projects irrespective of changing market conditions. The ongoing financial and economic crisis had no material impact on the implementation of the 10+ Programme.
**Crude Oil Exploration and Production**

The volume of crude oil and natural gas reserves held by the LOTOS Group is as follows:

<table>
<thead>
<tr>
<th></th>
<th>Dec 31 2010</th>
<th>Dec 31 2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Crude oil (2P*)</td>
<td>6.2 million tonnes</td>
<td>6.4 million tonnes</td>
</tr>
<tr>
<td>Crude oil (2C**)</td>
<td>1.3 million tonnes</td>
<td>0.8 million tonnes</td>
</tr>
<tr>
<td>Natural gas (2P*)</td>
<td>0.5 billion cubic metres</td>
<td>4.5 billion cubic metres</td>
</tr>
<tr>
<td>Natural gas (2C**)</td>
<td>6.5 billion cubic metres</td>
<td>2.4 billion cubic metres</td>
</tr>
</tbody>
</table>

*2P – proved and probable reserves
**2C – contingent resources

As at December 31st 2010, the Group reclassified gas reserves from 2P (proved and probable reserves) to 2C (contingent resources), until there are any concrete arrangements regarding the terms of potential cooperation with a business partner as part of a joint venture and development of the B-4 and B-6 fields advances, enabling commercial production.

In 2010, LOTOS Petrobaltic S.A.’s key operations included:

- production from the B3 field, including water injection into the reservoir from the Offshore Oil and Gas Facility located at the Baltic Beta Platform,
- production from the B8 field using the existing wells at the Petrobaltic platform (Q1 2010),
- continued work on the base engineering design of the production centre and related infrastructure for the B8 field,
- workover of the B3-11 well,
- major overhaul of the Petrobaltic platform,
- modernisation of the B3-6 subsea wellhead at the B3 field using the Petrobaltic drilling platform,
- further analytical and design work in preparation for development of the B8 field.

In Q1 2010, following completion of the pre-qualification round APA 2009, LOTOS Exploration & Production Norge AS was granted a 50% interest in, and the operator status with respect to, license PL556 located in the Norwegian Sea and a 10% interest in license PL497B (an extension of license PL497). Having performed relevant work, the company submitted applications for the APA 2010 license round and the 21st license round. APA 2010 awards were announced at the beginning of 2011. LOTOS E&P Norge was granted licence PL 503B (an extension of licence PL 503 already held by the company). The 21st licence round awards will be announced in Q2 2011.
The company conducted exploration work under the licences it holds, both as the operator (licences PL498, PL503 and PL556) and as an interest holder (licences PL316/316B – YME, PL316DS, PL316CS, PL455, PL497 and PL515). The work included drilling an exploration well in the licence PL316DS area (no hydrocarbons were identified). The company decided not to apply for extension of licences PL316CS and 316DS, as a result of which these licences expired in June 2010. In Q4 2010, an agreement was signed with Bergen Oilfield Services AS to perform 3D seismic surveys for licence PL503, over an offshore area of 1.5 thousand sq. km (planned for summer 2011).

Under the production licence PL 316/316B, development work continued as part of the YME production project. The company completed the drilling campaign. Six wells were drilled in the Gamma structure and three in the Beta structure. Work was conducted on the production platform, which arrived at the Rosenberg shipyard in Norway on September 16th 2010. Three legs were installed and the leg lowering system and stability of the platform were tested. Work at the platform currently continues in the Rosenberg shipyard until the weather conditions improve sufficiently to allow the platform to be towed and installed on the YME field. According to Talisman, the YME field operator, production from the field is expected to start in mid-2011.

**Strategy for the LOTOS Group until 2015**

On November 16th 2010, the Supervisory Board of Grupa LOTOS S.A. approved the Strategy for the LOTOS Group until 2015. The approved Strategy provides for the continuation of the current policy oriented towards stimulating sustainable growth of the core business, i.e. the exploration for and production of hydrocarbons, deep crude conversion focused on the production of fuels, and trade in high-margin petroleum products, with a focus on the overriding strategic objective of building shareholder value.

In line with the approved Strategy, the LOTOS Group considers corporate governance and corporate social responsibility as the cornerstones of its corporate system of values and conduct. In all aspects of its business, the LOTOS Group acts in line with the principles of sustainable growth.

The key elements of the Strategy are described below.

1. **Upstream Segment**

In line with the approved Strategy, the LOTOS Group will embark on more intense activities in order to capitalise on the high margins projected to prevail in the long term in the hydrocarbon production segment relative to the refining segment. The key assumptions are to increase overall production potential and gain access to larger oil and gas reserves.

The strategic objective in the upstream segment is to increase hydrocarbon production, in line with the priorities of Poland’s energy policy until 2030, through:

- enhanced security of supplies of crude oil for processing at the refinery owing to direct access to hydrocarbon reserves;
- higher hydrocarbon production achieved thanks to implementation of programmes for increasing oil and gas production from off-shore and on-shore fields, domestically and abroad.

This means that by 2015, with financing based on the LOTOS Group’s own resources, the Group will attain output of about 24 thousand boe per day (approximately 1.2 million tonnes per annum).
The production target of 1.2 million tonnes in 2015 will be met through development of the B8 field and continued production from the B3 field. As far as the Norwegian Continental Shelf is concerned, the Strategy envisages production from the YME field, exploration under the licences already held and obtaining more exploration licences.

The Group will continue its efforts to gain its own potential under exploration licences in order to create production capacities in the future (taking advantage of the favourable tax environment created by the Norwegian government).

The first significant effects of the exploration work, in the form of the Group’s higher interest in proved crude oil reserves and increased oil production are not expected to be seen before 2016–2020. Therefore, in order to raise its production to 1.2 million tonnes in 2015, the Group will also purchase an interest in a licence with proved crude oil reserves, which are already being developed.

With a view to implementing its strategic objective in the upstream segment, the LOTOS Group will seek to raise capital and establish cooperation with partners having access to oil and gas reserves, in order to increase its recoverable proved reserves of hydrocarbons to approx. 330 million boe and to lift its production to about 100 thousand boe per day (equivalent to approximately 5 million tonnes of oil per annum) in 2020.

The Group will endeavour to obtain access to reserves located in the areas which are characterised by moderate risk levels and which are not of direct interest to major oil companies, including:

- off-shore: the Baltic Sea, the Norwegian Sea, the North Sea and the Barents Sea,
- on-shore: Poland and Lithuania.

2. Downstream Segment

Marketing Area

In the marketing area, the strategic objective is to maximise the economic benefits from trading in gasoline, diesel oil and aviation fuel by flexibly adjusting product streams and further strengthening the market position. Sales of other products will be optimised to achieve the best possible economic effect.

The quantitative objectives are:

- to reach and maintain a market position with a 30% share in the domestic market of gasolines, diesel oil and light fuel oil,
- to attain a sales volume which is by 15% higher than the Gdańsk refinery’s fuel production capacity.

As regards the service station network, the LOTOS Group’s objective is to dynamically grow the countrywide network of LOTOS service stations in order to build a fully controlled and highly efficient product sales channel.

This objective will be achieved through:

- development of the CODO and DOFO service station networks in the premium and economy segments,
Grupa LOTOS S.A.

DIRECTORS’ REPORT ON THE OPERATIONS OF GRUPA LOTOS S.A. IN 2010

- intensified sales efforts and optimised sales structure.

Development of the distribution network will achieved by exploiting the following possibilities:

- organic growth, i.e. construction of new stations,
- purchase or lease of stations from independent operators,
- acquisitions, if interesting opportunities to buy service station networks emerge on the Polish market.

The quantitative objective is to achieve a 10% share in the domestic retail market within the time horizon of the Strategy, through quantitative and qualitative growth of the service station network and higher sales volumes.

In order to maximise the integrated margin, the LOTOS Group will focus on optimum use of its assets and coordination of its activities in the four key areas of the supply chain, including planning, procurement, production and distribution. If activities in these four areas are harmonised, the Group will have quicker access to information supporting decision making, and thus will be able to respond more rapidly to the changing market environment.

In the logistics area, the measures to be taken will be oriented towards integrating all components of the logistics chain, including those controlled by the Group and by the third parties.

Given its newly expanded throughput capacity, the LOTOS Group is planning to continue its policy of diversifying crude oil supply directions and sources by:

- maintaining the availability of supply sources of crude delivered both via pipelines and by sea;
- flexibly selecting crude oil grades and directions of supply in order to maximise the integrated margin;
- intensifying its presence on the international oil market,
- increasing the share of its own production in crude oil supplies.

Operating Area

In the refining area, the LOTOS Group’s strategic objective is to maintain its highly competitive position among the European refineries and to ensure optimum use of its assets, including the already existing ones and those it will come to hold following completion of new development projects.

- The conditions for further development of the LOTOS Group’s refinery in Gdańsk (“the Refinery”) depend on:
- the crude oil processing economics and the developments seen in the petroleum industry in the aftermath of the economic crisis;
- the increasing risk associated with marketing of heavy products;
- the gradual implementation of more stringent environmental and quality requirements and standards;
• the technological configuration of the Refinery following completion of the 10+ Programme; and
• diversification of feedstock used to produce energy carriers.

Having considered the factors discussed above and also the need to:
• enhance its operational flexibility,
• ensure energy security while simultaneously reducing the cost of generating energy, and
• reduce operating risk,

the LOTOS Group intends to extend the scope of its operations to include power generation, and thus capitalise on the potential synergies between the refining and the power sectors.

As the Group has long-standing experience mainly in crude oil processing, it intends to implement its business diversification strategy requiring higher competence in the power generation area by engaging in cooperation with external partners having a strong position in the power sector.

The Refinery’s technological development will be oriented towards a further improvement of the conversion ratio through further processing of the asphaltene residue from the ROSE process, with due consideration to the existing technological and economic conditions.

The Strategy provides for an option to find strategic external partners for joint ventures.

3. Financial Strategy

The LOTOS Group will operate based on the principle of self-financing of its business units, which means, among other things, that the Group will not be retaining any businesses which operate at permanently negative margins. Taking advantage of market opportunities, the Group’s assets will be restructured in order to improve operating efficiency and the core business focus.

Margins

The financial strategy objective regarding profitability is that the Group achieves the target EBITDA margin and return on average capital employed (ROACE). It is assumed that at the end of the period covered by the Strategy, the ratios will be as follows:

• EBITDA margin: 9% as a minimum,
• ROACE: 12% as a minimum.

Balance-Sheet Structure

The objective of the LOTOS Group’s financial policy is to maintain long-term liquidity, while using an appropriate level of financial leverage to support the achievement of the principal goal of maximising the return on equity attributable to the shareholders. The achievement of the above objectives, in line with the industry practice, will be done by striving to develop the desired financing structure reflected by the ratio of net interest-bearing debt to equity. On a consolidated basis, the ratio will not exceed 0.4 at the end of the Strategy term.
Dividend Policy

Dividend payments will be subordinated to the objective of optimising the financing structure of the LOTOS Group. The amount of dividend to be paid out from profit for the years covered by the Strategy is planned at up to 30% of net profit.

The dividend policy of subsidiary undertakings will be determined by the Management Board of Grupa LOTOS S.A. upon considering their financial standing and development programmes.

4. Capital Expenditure until 2015

The capital expenditure to be incurred in connection with implementation of the Strategy in the years 2011–2015 will be up to PLN 5.7bn.

Structure of capital expenditure until 2015

<table>
<thead>
<tr>
<th>Business area</th>
<th>Expenditure 2011–2015 (PLN billion)</th>
<th>Expenditure structure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Upstream segment</td>
<td>3.9</td>
<td>68 %</td>
</tr>
<tr>
<td>Downstream segment, including:</td>
<td>1.8</td>
<td>32 %</td>
</tr>
<tr>
<td>Operating area</td>
<td>0.8</td>
<td>14 %</td>
</tr>
<tr>
<td>Marketing area</td>
<td>1.0</td>
<td>18 %</td>
</tr>
<tr>
<td>Group total</td>
<td>5.7</td>
<td>100%</td>
</tr>
</tbody>
</table>

At present, the LOTOS Group relies mainly on long-term debt instruments to implement its development programmes. Depending on the market conditions, the LOTOS Group may:

- find partners for its investment projects,
- implement projects through Special Purpose Vehicles,
- raise funds on capital markets through its subsidiaries,
- outsource auxiliary production,
- outsource storage capacities,
- sell and lease back selected assets,
- sell non-core assets.

Moreover, to optimise the capital structure or find partners with appropriate resources or experience, involvement of third-party investors in the implementation of the investment projects may also be considered. The level of involvement of such partners in a project will depend on their impact on the activities of the LOTOS Group.
### 5. Key Macroeconomic and Pricing Assumptions Adopted to Formulate the Main Objectives of the Financial Policy until 2015

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dtd Brent (USD/bbl)</td>
<td>76</td>
<td>77</td>
<td>78</td>
<td>78</td>
<td>79</td>
</tr>
<tr>
<td>Ural DAF Adamowo (USD/bbl)</td>
<td>74</td>
<td>75</td>
<td>75</td>
<td>76</td>
<td>76</td>
</tr>
<tr>
<td>Crack Gasoline 10ppm – Cargoes CIF NWE (USD/t)</td>
<td>120</td>
<td>125</td>
<td>132</td>
<td>139</td>
<td>140</td>
</tr>
<tr>
<td>Crack Diesel 10ppm – Cargoes CIF NEW (USD/t)</td>
<td>128</td>
<td>128</td>
<td>125</td>
<td>125</td>
<td>127</td>
</tr>
<tr>
<td>Crack Gasoil 0.1% - Cargoes CIF NEW (USD/t)</td>
<td>99</td>
<td>95</td>
<td>96</td>
<td>97</td>
<td>101</td>
</tr>
<tr>
<td>Crack Fuel Oil 3.5% - Barges FOB Rotterdam (USD/t)</td>
<td>-160</td>
<td>-163</td>
<td>-170</td>
<td>-181</td>
<td>-192</td>
</tr>
<tr>
<td>EUR/PLN</td>
<td>3.71</td>
<td>3.71</td>
<td>3.71</td>
<td>3.71</td>
<td>3.71</td>
</tr>
<tr>
<td>USD/PLN</td>
<td>3.04</td>
<td>3.04</td>
<td>3.04</td>
<td>3.04</td>
<td>3.04</td>
</tr>
<tr>
<td>3M LIBOR USD</td>
<td>1.15%</td>
<td>2.15%</td>
<td>3.00%</td>
<td>3.50%</td>
<td>4.15%</td>
</tr>
<tr>
<td>3M WIBOR</td>
<td>4.50%</td>
<td>5.00%</td>
<td>5.50%</td>
<td>5.50%</td>
<td>5.50%</td>
</tr>
</tbody>
</table>

### 6. Development Directions until 2020

Following the implementation of the strategic tasks planned for completion by 2015, the LOTOS Group will continue to focus on measures aimed at increasing the Company’s shareholder value. The development of the upstream segment is expected to have a key role here.

The main objectives to be achieved by 2020 in the upstream segment include:

- Increasing access to recoverable hydrocarbon reserves, with an intention to achieve the output of approx. 330 million boe (barrel of oil equivalent) in 2020, which is to be achieved through:
  - focusing initially on projects that are partially developed or at the final stage of development and, subsequently, on prospective projects (new licenses), which require higher expenditure but offer greater economic benefits,
  - continuing production of/exploration for oil and gas in the Baltic Sea (the Polish Shelf),
  - continuing exploration/production operations in the North Sea,
  - purchasing licenses which make it possible to avoid engaging significant resources (both financial and human),
  - continuing operations on the projects where reserves are already developed;
- Considering the possibility of commencing onshore exploration/production operations in Poland and Lithuania;
- Monitoring niche areas which are not of key interest to major oil companies:
  - Central Europe, Commonwealth of Independent States,
  - North Africa.
Both exploration and production operations may be carried out with the direct participation of:

- the LOTOS Group companies,
- third-party partners.

The major areas of activity outside the upstream sector include:

a. increasing Poland’s energy security through the development of operations in the area of international trade in crude oil and petroleum products and optimisation of the distribution and logistics system;

b. further improving the economic effectiveness of crude oil processing through the optimal management of heavy residue, ensuring full utilisation of the Group’s assets as well as technical/technological and commercial conditions;

c. measures undertaken to optimise the power management processes at the LOTOS Group’s refinery through the extension of its connections with other power systems;

d. pursuing modernisation initiatives resulting from the implementation of the Operational Excellence Programme, which are necessary to maintain the Group’s highly competitive position in the region.

Decisions concerning the planned development-oriented measures will be made based on appropriate feasibility studies, and will be implemented gradually as the LOTOS Group’s financing capabilities allow it. The Group does not exclude the possibility of entering into arrangements with third parties based on equity involvement or establishing joint ventures with strategic partners.

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

In the year ended December 31st 2010, transactions with related parties were executed on standard market terms. Details of the transactions have been presented in Note 32.1 to the financial statements of Grupa LOTOS S.A. for the year ended December 31st 2010.

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

Compensation Agreements

Apart from standard employment contracts concluded by Grupa LOTOS S.A. with the management staff in 2010, no agreements were executed that provide for compensation to the management staff in the event they resign or are dismissed without a good reason or in the event they resign or are dismissed as a result of the Company’s takeover by another entity.
### Remuneration paid or payable to members of the Management Board of Grupa LOTOS S.A.:

<table>
<thead>
<tr>
<th>Name</th>
<th>PLN '000 (Year ended as at Dec 31 2010)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paweł Olechnowicz</td>
<td>302</td>
</tr>
<tr>
<td>Marek Sokołowski</td>
<td>301</td>
</tr>
<tr>
<td>Mariusz Machajewski</td>
<td>301</td>
</tr>
<tr>
<td>Maciej Szozda</td>
<td>261</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,165</strong></td>
</tr>
</tbody>
</table>

### Remuneration paid or payable to the members of the Management Board of Grupa LOTOS S.A. for serving on the supervisory boards and the boards of directors of direct and indirect subsidiaries:

<table>
<thead>
<tr>
<th>Name</th>
<th>PLN '000 (Year ended as at Dec 31 2010)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paweł Olechnowicz</td>
<td>158</td>
</tr>
<tr>
<td>Marek Sokołowski</td>
<td>92</td>
</tr>
<tr>
<td>Mariusz Machajewski</td>
<td>91</td>
</tr>
<tr>
<td>Maciej Szozda</td>
<td>91</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>432</strong></td>
</tr>
</tbody>
</table>

### Remuneration paid or payable to members of the Supervisory Board of Grupa LOTOS S.A.:

<table>
<thead>
<tr>
<th>Name</th>
<th>PLN '000 (Year ended Dec 31 2010)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wiesław Skwarko(^1)</td>
<td>3</td>
</tr>
<tr>
<td>Leszek Starosta</td>
<td>42</td>
</tr>
<tr>
<td>Mariusz Obszyński,</td>
<td>9</td>
</tr>
<tr>
<td>Radosław Barszcz</td>
<td>9</td>
</tr>
<tr>
<td>Małgorzata Hirszel</td>
<td>42</td>
</tr>
<tr>
<td>Jan Stefanowicz</td>
<td>9</td>
</tr>
<tr>
<td>Ireneusz Fałara</td>
<td>14</td>
</tr>
<tr>
<td>Oskar Pawłowski,</td>
<td>33</td>
</tr>
</tbody>
</table>
On November 1st 2010, Mr Wiesaw Skwarko withdrew the representation to the effect that he forgoes the remuneration due to him for serving as a member of the Supervisory Board of Grupa LOTOS S.A.

As at December 31st 2010, the Company did not grant any loans or similar benefits to members of its management and supervisory staff.

3.4 INFORMATION ON THE AGREEMENT WITH A QUALIFIED AUDITOR OF FINANCIAL STATEMENTS

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

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

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

The total remuneration for the audit, review and verification procedures is set forth below.

<table>
<thead>
<tr>
<th>PLN '000</th>
<th>2010</th>
<th>2009(^{1)})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit of the annual non-consolidated and consolidated financial statements</td>
<td>351(^{2})</td>
<td>466</td>
</tr>
<tr>
<td>Confirmation services, including:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>- review of non-consolidated and consolidated financial statements</td>
<td>234(^{2})</td>
<td>243</td>
</tr>
<tr>
<td>Other services</td>
<td>10(^{3})</td>
<td>-</td>
</tr>
<tr>
<td>Tax advisory services</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>595</strong></td>
<td><strong>839</strong></td>
</tr>
</tbody>
</table>

\(^{1)}\) On November 1st 2010, Mr Wiesaw Skwarko withdrew the representation to the effect that he forgoes the remuneration due to him for serving as a member of the Supervisory Board of Grupa LOTOS S.A.
3.5 COURT, ARBITRATION OR ADMINISTRATIVE PROCEEDINGS

In 2010 no court, arbitration or administrative proceedings were pending concerning the Issuer’s or its subsidiary’s liabilities or debts with a value equal to or exceeding 10% of the Issuer’s equity. For information on other material proceedings, see Note 46 to the consolidated financial statements for 2010.

III FINANCIAL STANDING OF GRUPA LOTOS S.A.

1 KEY FINANCIAL AND ECONOMIC DATA CONTAINED IN THE ANNUAL NON-CONSOLIDATED FINANCIAL STATEMENTS AND ASSESSMENT OF FACTORS AND NON-RECURRING EVENTS WITH A BEARING ON GRUPA LOTOS S.A.’S PERFORMANCE

1.1 STATEMENT OF COMPREHENSIVE INCOME

Sales Revenue

In 2010, GRUPA LOTOS S.A. recorded sales revenue of PLN 18,124.7m, up by 42.7% on 2009. The main drivers of the increase were higher prices of crude oil and petroleum products on global markets and a 17.4% rise in sales volume. In 2010, the average price of Brent dtd was 79.5 USD/bbl, which represented a year-on-year increase of 28.9%. The average net selling price in 2010 was PLN 2,095 per tonne, which represented a rise of PLN 372 per tonne (21.6%) relative to 2009.

Net revenue from sales of products accounted for 98.6% of total sales revenue. In 2009, net revenue from sales of products accounted for 90.0% of total sales revenue. Net revenue from domestic sales represented 83.6% of total net sales revenue (88.6% in 2009).
Macroeconomic conditions

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>DATED Brent FOB prices</td>
<td>USD/bbl</td>
<td>79.50</td>
<td>61.67</td>
</tr>
<tr>
<td>Urals CIF Rotterdam prices</td>
<td>USD/bbl</td>
<td>78.26</td>
<td>61.15</td>
</tr>
<tr>
<td>Brent/Ural differential</td>
<td>USD/bbl</td>
<td>1.24</td>
<td>0.52</td>
</tr>
<tr>
<td>Crack margin</td>
<td>USD/bbl</td>
<td>3.09</td>
<td>2.94</td>
</tr>
<tr>
<td>Crack margin: Gasoline</td>
<td>USD/t</td>
<td>138.91</td>
<td>122.04</td>
</tr>
<tr>
<td>Crack margin: Diesel oil (10 ppm)</td>
<td>USD/t</td>
<td>92.41</td>
<td>74.07</td>
</tr>
<tr>
<td>Crack margin: Light fuel oil</td>
<td>USD/t</td>
<td>71.70</td>
<td>55.54</td>
</tr>
<tr>
<td>Crack margin: Aviation fuel</td>
<td>USD/t</td>
<td>120.04</td>
<td>98.47</td>
</tr>
<tr>
<td>Crack margin: Heavy fuel oil</td>
<td>USD/t</td>
<td>-161.69</td>
<td>-122.85</td>
</tr>
<tr>
<td>Average annualised PLN/USD exchange rate</td>
<td>PLN/USD</td>
<td>3.02</td>
<td>3.12</td>
</tr>
<tr>
<td>Average annualised PLN/EUR exchange rate</td>
<td>PLN/EUR</td>
<td>3.99</td>
<td>4.33</td>
</tr>
</tbody>
</table>

The total volume of petroleum products and goods sold by Grupa LOTOS S.A. in 2010 reached 8,649.4 thousand tonnes, i.e. 17.4% up on the volume sold in 2009. Diesel oils accounted for the largest share in total sales (47.1%). In 2010, the volume of diesel oil sales was 4,072.8 thousand tonnes, which is 384.3 tonnes more than in 2009. The largest increase in volume (by 568.0 thousand tonnes) was recorded in the case of heavy fuel oils. In 2010, the volume of domestic sales rose by 588.9 thousand tonnes, or 9.2%, while export sales increased by 695.1 thousand tonnes, or 72.0%. The share of domestic sales in the total sales volume fell by 6.1 percentage points.

Operating Profit/(Loss)

In 2010, Grupa LOTOS S.A.’s cost of sales was PLN 17,104.2m, which represented a year-on-year increase of 41.2%. The unit cost of sales was PLN 1,977 per tonne, or 20.2% more than in 2009. As the unit cost of sales increased to a smaller extent than the average net selling price, this had a positive effect on Grupa LOTOS S.A.’s gross profit, driving it up by PLN 440.1m relative to 2009, to PLN 1,020.4m.

The year-on-year rise in gross profit in 2010 was driven mainly by higher crack margins on refinery products. The average crack spreads on ULSD 10 ppm, Gas oil 0.1 and JET fuel increased year on year, respectively to USD 92.41 per tonne (up by 24.8%), USD 71.70 per tonne (up by 29.1%), and USD 120.04 per tonne (up by 21.9%). The average crack spread on Gasoline 10 ppm increased in 2010 by 13.8%, to USD 138.91 per tonne. Higher cracks on fuels had a positive effect on the 2010 gross profit of approximately PLN 222.3m relative to 2009. A rise in the average Brent/Ural differential by 0.72 USD/bbl, to 1.24 USD/bbl, contributed about PLN 113.8m to the year-on-year increase in gross profit.

Fluctuations of the USD exchange rate throughout the year resulted in foreign exchange losses on operating activities of PLN 254.1m, connected mainly with feedstock purchases. In 2009, foreign exchange losses on operating activities stood at PLN 178.6m.
A major driver of the improvement in the 2010 gross profit was replacement of imported goods and components with the Group's own crude oil processing products. In 2010, the volume of crude oil processed by the Gdańsk refinery was 8,095.7 thousand tonnes, which means a 48.2% increment on the previous year. The increase in the volume of processed crude oil was primarily due to the processing of crude oil in the integrated CDU/VDU unit, constructed as part of the 10+ Programme. Additionally, in 2009 the volume of processed crude oil was below the average level due to the overhaul shutdown at Grupa LOTOS S.A.'s refinery in 2009. In 2010, the increase in the volume of processed crude oil was the main reason of an 85.4% reduction in the volume of goods for resale sold and a 34.3% drop in the volume of production feedstock other than crude oil.

Selling costs incurred by the Company in 2010 amounted to PLN 449.0m and were by PLN 89.5m higher than in 2009, mainly owing to a 17.4% increase in the sales volume (including a 72.0% rise in exports). The average selling cost per one tonne stood at PLN 51.9 in 2010, up by 6.4% year on year, mainly due to higher share of exports in the total sales structure. General and administrative expenses were by PLN 36.0m, or 16.8%, higher than in 2009. This was primarily the effect of a significant reduction in expenses in 2009, connected with the implementation of the Package of Anti-Crisis Measures.

In 2010, the Company reported a net loss on other operating activities of PLN -12.3m. The amount included, among other items, impairment losses on tangible assets under construction of PLN 14.2m. In 2009, net loss on other operating activities was PLN -5.9m.

The discussed factors contributed to Grupa LOTOS S.A. generating operating profit of PLN 308.3m in 2010, compared with operating profit of PLN 0.1m in 2009.

**Financing Activities**

In 2010, Grupa LOTOS S.A. recorded net finance income of PLN 212.1m, resulting chiefly from dividends received (PLN 251.9m), realised foreign exchange gains on foreign currency transactions in bank accounts (PLN 355.8m), foreign exchange losses related to revaluation of loans and borrowings (PLN -176.1m), and negative valuation and settlement of derivatives used as market risk hedges (PLN -193.4m). The high value of net finance income recorded in 2009, amounting to PLN 701.8m, was chiefly the effect of foreign exchange gains of PLN 578.7m, related chiefly to the revaluation of loans and borrowings (PLN 366.1m) and foreign exchange differences on transactions in bank accounts (PLN 209.9m).

The excess of negative valuation of derivatives hedging the market risk, charged to finance expenses, amounted to PLN -120.2m and related to interest rate hedging transactions (IRS) (PLN -73.8m), foreign exchange risk hedging transactions (PLN -38.9m), and other hedging transactions (PLN -7.5m). In 2009, the excess of positive valuation of derivative instruments, charged to finance income, amounted to PLN 219.1m.

In 2010, the effect of valuation of open forward and futures contracts was charged to finance expenses in the amount of PLN -73.2m and included: PLN -37.9m on foreign exchange risk hedging transactions (FX forwards), PLN -33.9m on interest rate hedging transactions (IRS), and PLN -1.4m on other transactions. In 2009, the effect of valuation of open forward and futures contracts charged to finance expenses totalled PLN -217.0m.
Grupa LOTOS S.A.

DIRECTORS’ REPORT ON THE OPERATIONS OF GRUPA LOTOS S.A.
IN 2010

Net Profit/(Loss)

The differences between net finance income recorded by Grupa LOTOS S.A. in 2010 and 2009 resulted in a 21.4% decline in the 2010 net profit on continuing operations (to PLN 465.0m).

1.2 STATEMENT OF FINANCIAL POSITION

As at December 31st 2010, total assets of Grupa LOTOS S.A. amounted to PLN 14,686.7m, having risen over the year by PLN 2,127.1m. The PLN 459.1m (5.7%) increase in the value of non-current assets from the level reported as at December 31st 2009 was chiefly due to a PLN 2,759.0m increase in the value of property, plant and equipment connected with the implementation of the 10+ Programme. As at December 31st 2010 the 10+ Programme was fully completed, as a result of which the value of tangible assets under construction fell by PLN 2,284.0m.

In 2010, the value of current assets rose by PLN 1,668.0m. The increase was attributable primarily to PLN 1,404.3m higher valuation of inventories (including a PLN 784.0m rise in mandatory stocks), due to higher prices of crude oil and petroleum products as at the end of 2010 relative to the prices at the end of 2009 and due to a higher volume of mandatory stocks (increase in stocks of fuels and heavy fuel oil by 216.4 thousand cubic metres and decrease in stocks of crude oil by 5.7 thousand tonnes). The PLN 293.0m increase in trade and other receivables was attributable chiefly to rising prices of petroleum products in 2010 and a 17.4% increase in the volume of products and goods sold.

As at December 31st 2010, the share of non-current assets in Grupa LOTOS S.A.’s total assets fell from 64.0% in 2009 to 57.9% in 2010. The share of current assets rose mainly on the back of a higher share of inventories in total assets.

Grupa LOTOS S.A.’s equity reached PLN 5,945.1m as at the end of 2010, having risen in 2010 by PLN 465.0m as a result of net profit generated in 2010. The share of equity in total equity and liabilities fell from 43.6% in 2009 to 40.5% in 2010.

In 2010, non-current liabilities of Grupa LOTOS S.A. fell by PLN 588.8m, chiefly as a result of a lower level of non-current loans after a portion of non-current debt related to the financing of inventories was transferred to current debt and also due to the repayment of first instalments of the loans contracted to finance the 10+ Programme, due in the second half of 2011. Other non-current financial liabilities fell in 2010 by PLN 112.7m following a drop in the non-current portion of negative valuation of financial instruments, which at the end of 2010 amounted to PLN 107.5m. At the end of 2010, non-current liabilities amounted to PLN 4,384.8m, of which PLN 4,141.0m were loans and borrowings.

As at December 31st 2010, current liabilities totalled PLN 4,356.8m, having increased from December 31st 2009 by 106.9%. Trade payables, accruals and deferred income and other liabilities rose in 2010 by PLN 1,010.5m, chiefly as a result of a 68.2% increase in the volume and a 111.9% increase in the value of crude oil purchased in December 2010 compared with December 2009. Current loans and borrowings rose in 2010 by PLN 1,076.3m, to PLN 1,548.2m, mainly as a result of reclassification of non-current loans to current loans. Other current financial liabilities rose by 153.1m in 2009, mainly as a result of higher negative valuation of financial instruments, which amounted to PLN 166.3m at the end of 2010.
As at December 31st 2010, financial debt of Grupa LOTOS S.A. amounted to PLN 5,689.2m, up by PLN 554.6m on the 2009 end-of-year figure. The ratio of financial debt (adjusted by free cash) to equity was 95.3%, which represented a rise of 1.8 percentage points compared with December 31st 2009.

1.3 STATEMENT OF CASH FLOWS

As at the end of 2010, Grupa LOTOS S.A.’s cash balance (taking into account its debt under overdraft facilities) was PLN -178.4m. Total net cash flows generated in 2010 amounted to PLN 272.4m, up by PLN 549.7m on the negative change in cash recorded in 2009.

In 2010, net cash provided by operating activities amounted to PLN 281.1m. In the same period, net cash used in investing activities was PLN -407.2m, mainly as a result of expenses incurred to purchase non-current assets under the ongoing 10+ Programme. The Company posted net cash provided by financing activities in the amount of PLN 401.5m, including in particular proceeds under contracted loans.

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

The main factors and events affecting Grupa LOTOS S.A.’s operating performance in 2010 include:

1) Record high crude oil throughput in 2010: an increase of 48.2% relative to 2009, to 8.1 million tonnes, in connection with the use of the integrated CDU/VDU unit constructed under the 10+ Programme;
2) Completion of the 10+ Programme, as a result of which the annual capacities of the Gdańsk refinery have been increased to 10.5 million tonnes;
3) Higher production volumes, which made it possible to replace imported goods with own products and thus improve generated margins;
4) Impairment losses on tangible assets under construction at the Parent Undertaking were increased.

1.5 EXPLANATION OF DIFFERENCES BETWEEN ACTUAL FINANCIAL PERFORMANCE AND PREVIOUSLY PUBLISHED FORECASTS

Grupa LOTOS S.A. did not publish any separate performance forecasts for 2010.
2 INVESTMENTS

2.1 INVESTMENTS IN TANGIBLE AND INTANGIBLE ASSETS

The table presents capital expenditure incurred by Grupa LOTOS S.A. in 2010 (PLN ‘000).

<table>
<thead>
<tr>
<th>Tangible assets under construction and purchases of property, plant and equipment and intangible assets, including:</th>
<th>Capital expenditure Jan 1 2010 - Dec 31 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction and assembly work</td>
<td>415,505</td>
</tr>
<tr>
<td>Procurement from external suppliers – purchases</td>
<td>326,304</td>
</tr>
<tr>
<td>Purchases of intangible assets</td>
<td>7,138</td>
</tr>
<tr>
<td>Other capital expenditure</td>
<td>101,227</td>
</tr>
<tr>
<td>Prepayments for tangible assets under construction</td>
<td>47,557</td>
</tr>
<tr>
<td>Settled prepayments</td>
<td>(192,098)</td>
</tr>
<tr>
<td>Total</td>
<td>705,663</td>
</tr>
</tbody>
</table>

2.2 EQUITY INVESTMENTS

In 2010, Grupa LOTOS S.A. did not make any equity investments outside of the group of related undertakings.

2.3 ASSESSMENT OF FEASIBILITY OF PLANNED INVESTMENTS, INCLUDING EQUITY INVESTMENTS, IN VIEW OF AVAILABLE FUNDS

In 2010, Grupa LOTOS S.A. financed investments using its own resources, as well as external funds raised in connection with the 10+ Programme. Together with Grupa LOTOS S.A.’s own resources, the contracted external financing fully covers the Company’s financing needs connected with the ongoing and planned investment projects.

3 FINANCING SOURCES

3.1 LOAN AGREEMENTS AND BORROWINGS
## Grupa LOTOS S.A.

**DIRECTORS’ REPORT ON THE OPERATIONS OF GRUPA LOTOS S.A.**

**IN 2010**

### Loans as at December 31st 2010:

<table>
<thead>
<tr>
<th>Bank name; form of incorporation</th>
<th>Registered office</th>
<th>Loan amount as per agreement</th>
<th>Outstanding loan amount (current portion)</th>
<th>Outstanding loan amount (non-current portion)</th>
<th>Maturity date</th>
<th>Financial terms and conditions (interest rate, interest payment schedule etc.)</th>
<th>Type of security</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>PLN</strong> ('000)</td>
<td><strong>Foreign currency ('000)</strong></td>
<td><strong>PLN</strong> ('000)</td>
<td><strong>Foreign currency ('000)</strong></td>
<td><strong>PLN</strong> ('000)</td>
<td><strong>Foreign currency ('000)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pekao S.A.</td>
<td>Warsaw</td>
<td>150,000</td>
<td>30,165</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>Overdraft facility</td>
</tr>
<tr>
<td><strong>Bank Consortium (1)</strong></td>
<td>-</td>
<td>-</td>
<td>USD 400,000</td>
<td>1,187,413</td>
<td>USD 400,553</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Bank Consortium (2)</strong></td>
<td>-</td>
<td>-</td>
<td>USD 1,125,000</td>
<td>91,439</td>
<td>USD 30,775</td>
<td>3,120,146</td>
<td>USD 1,049,856</td>
</tr>
<tr>
<td><strong>Bank Consortium (3)</strong></td>
<td>-</td>
<td>-</td>
<td>USD 425,000</td>
<td>37,214</td>
<td>USD 12,550</td>
<td>1,020,870</td>
<td>USD 344,228</td>
</tr>
<tr>
<td><strong>Bank Consortium (4)</strong></td>
<td>-</td>
<td>-</td>
<td>USD 200,000 or equivalent</td>
<td>76,328</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>108,329</td>
<td>USD 36,547</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>17,322</td>
<td>EUR 4,374</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>106,493</td>
<td>-</td>
<td>-</td>
<td>1,424,395</td>
<td>USD 480,425</td>
<td>4,141,016</td>
<td>USD 1,394,084</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>17,322</td>
<td>EUR 4,374</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1,548,210</td>
<td>-</td>
<td>4,141,016</td>
<td>-</td>
</tr>
</tbody>
</table>

The banks’ margins on the contracted loans are in the range of 0.65pp. – 1.80pp.
The following table shows loans as at December 31st 2009:

<table>
<thead>
<tr>
<th>Bank name; form of incorporation</th>
<th>Registered office</th>
<th>Loan amount as per agreement</th>
<th>Outstanding loan amount (current portion)</th>
<th>Outstanding loan amount (non-current portion)</th>
<th>Maturity date</th>
<th>Financial terms and conditions (interest rate, interest payment schedule etc.)</th>
<th>Type of security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pekao S.A.</td>
<td>Warsaw</td>
<td>100,000</td>
<td>2,263</td>
<td>-</td>
<td>Overdraft facility</td>
<td>- 1M WIBOR + bank’s margin</td>
<td>submission to enforcement</td>
</tr>
<tr>
<td>Bank Consortium (1)</td>
<td>-</td>
<td>-</td>
<td>1,670</td>
<td>USD 1,139,513</td>
<td>Mar 15 2010  Dec 20 2011</td>
<td>based on 3M or 6M LIBOR USD, depending on the interest period selected at a given time + bank’s margin</td>
<td>registered pledge over inventories, registered pledge over bank accounts, assignment of rights under inventory insurance agreements, assignment of rights under inventory storage agreements, submission to enforcement</td>
</tr>
<tr>
<td>Bank Consortium (2)</td>
<td>-</td>
<td>-</td>
<td>6,477</td>
<td>USD 2,750,485</td>
<td>Mar 15 2010  Jan 15 2021</td>
<td>based on 1M, 3M or 6M LIBOR USD, depending on the interest period selected at a given time + bank’s margin</td>
<td>mortgage, registered pledge over existing and future movables, registered pledge over bank accounts, assignment of rights under agreements for the implementation and management of the 10+ Programme, assignment of rights under insurance agreements relating to the Gdańsk refinery, assignment of licence, hedging and sale agreements with a value of over PLN 10,000 thousand per year, submission to enforcement</td>
</tr>
<tr>
<td>Bank Consortium (3)</td>
<td>-</td>
<td>-</td>
<td>1,760</td>
<td>USD 772,661</td>
<td>Mar 15 2010  Jan 15 2021</td>
<td>fixed interest rate</td>
<td></td>
</tr>
<tr>
<td>Bank Consortium (4)</td>
<td>-</td>
<td>-</td>
<td>278,567</td>
<td>-</td>
<td>Overdraft facility</td>
<td>- 3M WIBOR + bank’s margin</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>26</td>
<td>EUR 6</td>
<td>Overdraft facility</td>
<td>- 3M EURIBOR + bank’s margin</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>181,163</td>
<td>USD 63,559</td>
<td>-</td>
<td>- 3M LIBOR USD + bank’s margin</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>280,830</td>
<td>-</td>
<td>191,070</td>
<td>66,804 USD</td>
<td>USD 1,633,998</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td></td>
<td>191,070</td>
<td>-</td>
<td>4,662,659</td>
<td>-</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>26</td>
<td>EUR 6</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>471,926</td>
<td>-</td>
<td>4,662,659</td>
<td>-</td>
<td>-</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The banks’ margins on the contracted loans are in the range of 0.65pp. – 1.80pp.
Loans Advanced by Grupa LOTOS S.A.

Loans Advanced to Rafineria Nafty GLIMAR S.A.

On September 23rd 2003 and April 8th 2004, Grupa LOTOS S.A. and Rafineria Nafty GLIMAR S.A. signed loan agreements for the financing of operating and investing activities, including the Glimar Hydrocomplex project, for a total 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 executed by Grupa LOTOS S.A. on February 12th 2004 for the benefit of Bank Przemysłowo-Handlowy S.A., the Company undertook commitments relating to the co-financing of the Glimar Hydrocomplex project and maintaining 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 2010 and December 31st 2009, the assets under loans advanced were fully covered by an impairment charge.

Loans Advanced to LOTOS Exploration and Production Norge AS

On April 30th 2009, Grupa LOTOS S.A. signed an agreement providing for a loan to LOTOS Exploration and Production Norge AS in the amount of USD 13,000 thousand (i.e. PLN 42,717 thousand, as translated at the USD exchange rate quoted by the National Bank of Poland for April 30th 2009). The loan is intended for financing of the expenditure related to the YME Production Project. The original loan repayment date was July 31st 2009, but it was extended until December 1st 2011. The loan bears interest at a floating annual interest rate based on 3M LIBOR plus margin.

On October 14th 2009, Grupa LOTOS S.A. signed an agreement providing for a loan to LOTOS Exploration and Production Norge AS in the amount of USD 7,000 thousand (i.e. PLN 19,776 thousand, as translated at the USD exchange rate quoted by the National Bank of Poland for October 14th 2009). The loan is intended for financing of the expenditure related to the YME Production Project. The loan principal and interest was repaid on November 16th 2009 in view of the terms and conditions of the notes issued by LOTOS Exploration and Production Norge AS. The agreement provided for repayment of the principal and interest by July 30th 2010. The loan bears interest at a floating rate based on 6M LIBOR plus margin.

On October 22nd 2010, Grupa LOTOS S.A. signed an agreement to grant a loan of USD 7,000 thousand (i.e. PLN 20,031 thousand, translated at the mid-exchange rate for USD quoted by the National Bank of Poland for October 22nd 2010) to LOTOS Exploration and Production Norge AS. The loan is intended for financing of further implementation of the YME Production Project. The principal amount along with interest is to be repaid by September 30th 2011. The loan bears interest at a floating annual interest rate based on 3M LIBOR plus margin.

LOTOS Exploration and Production Norge AS created security in the form of blank promissory notes with a “protest waived” clause and a promissory note declaration for the benefit of Grupa LOTOS S.A. in order to secure the repayment of the loan (principal, interest...
and possible default interest, as well as any other liabilities which may arise in connection with the execution and performance of the agreement).

**Loan Advanced to LOTOS Gaz S.A.**

On June 29th 2010, Grupa LOTOS S.A. signed an agreement to grant a loan of PLN 2,000 thousand to LOTOS Gaz S.A. In accordance with an annex to the agreement, the loan principal is to be repaid by December 31st 2011. Security for the repayment of the loan (including principal, interest and default interest, if any, as well as any other liabilities that may arise in connection with the execution and performance of the loan agreement) will be provided in the form of an assignment by LOTOS Gaz S.A. of future accounts receivable related to payment of the price for the sale of its assets, subject to a condition precedent that LOTOS Gaz S.A. is not discharging its obligations towards Grupa LOTOS S.A. By December 31st 2010, LOTOS Gaz S.A. repaid the amount of PLN 1,100 thousand under the loan.

**3.2 SURETIES, GUARANTEES AND OTHER CONTINGENT AND OFF-BALANCE-SHEET LIABILITIES**

As at December 31st 2010, the total value of contingent liabilities under sureties and guarantees issued was PLN 28,572 thousand.

As at December 31st 2010, the total value of contingent liabilities under promissory notes was PLN 440,000 thousand.

For a detailed description of the Company’s contingent liabilities in the year ended December 31st 2010, see Note 31 to the financial statements for the year ended December 31st 2010.

**3.3 ASSESSMENT OF FINANCIAL RESOURCES MANAGEMENT**

In 2010, Grupa LOTOS S.A. was able to meet all of its liabilities towards third parties. In the period from January 1st to December 31st 2010, the Company used investment and working capital overdraft facilities. As at December 31st 2010, the Company had available funds in the amount of PLN 511.6m under working capital facilities. As at December 31st 2010, the balance of overdraft facilities amounted to PLN 202.0m. For detailed information on the debt structure, see Note 28 to the financial statements for the year ended December 31st 2010.

A synthetic assessment of Grupa LOTOS S.A.’s overall economic and financial standing was based on a ratio analysis covering profitability, liquidity, turnover, and debt levels.
### PROFITABILITY RATIOS

<table>
<thead>
<tr>
<th>Ratio</th>
<th>2010</th>
<th>2009 (comparative data)</th>
</tr>
</thead>
<tbody>
<tr>
<td>EBIT (PLNm)</td>
<td>308.3</td>
<td>0.1</td>
</tr>
<tr>
<td>EBIT margin (1)</td>
<td>1.70%</td>
<td>0.00%</td>
</tr>
<tr>
<td>EBITDA (2) (PLNm)</td>
<td>523.9</td>
<td>139.3</td>
</tr>
<tr>
<td>EBITDA margin (3)</td>
<td>2.89%</td>
<td>1.10%</td>
</tr>
<tr>
<td>Net profit/loss (PLNm)</td>
<td>465.0</td>
<td>591.3</td>
</tr>
<tr>
<td>Net margin (4)</td>
<td>2.57%</td>
<td>4.66%</td>
</tr>
<tr>
<td>Return on equity (ROE) (5)</td>
<td>7.82%</td>
<td>10.79%</td>
</tr>
<tr>
<td>Return on assets (ROA) (6)</td>
<td>3.17%</td>
<td>4.71%</td>
</tr>
<tr>
<td>Return on average capital employed (ROACE) (7)</td>
<td>2.17%</td>
<td>0.00%</td>
</tr>
</tbody>
</table>

### LIQUIDITY RATIOS

<table>
<thead>
<tr>
<th>Ratio</th>
<th>2010</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current ratio (8)</td>
<td>1.42</td>
<td>2.14</td>
</tr>
<tr>
<td>Quick ratio (9)</td>
<td>0.43</td>
<td>0.77</td>
</tr>
<tr>
<td>Capital employed (10) (PLNm)</td>
<td>1 826.7</td>
<td>2 409.6</td>
</tr>
<tr>
<td>Capital employed to total assets (11)</td>
<td>12.44%</td>
<td>19.19%</td>
</tr>
</tbody>
</table>

### COLLECTION/PAYMENT PERIODS

<table>
<thead>
<tr>
<th>Period</th>
<th>2010</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average collection period (days) (12)</td>
<td>31.35</td>
<td>37.31</td>
</tr>
<tr>
<td>Average payment period (days) (13)</td>
<td>27.23</td>
<td>21.03</td>
</tr>
</tbody>
</table>

### CAPITAL STRUCTURE AND DEBT RATIOS

<table>
<thead>
<tr>
<th>Ratio</th>
<th>2010</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt ratio (14)</td>
<td>59.52%</td>
<td>56.37%</td>
</tr>
<tr>
<td>Net financial debt (PLNm) (15)</td>
<td>5 548.4</td>
<td>5 029.0</td>
</tr>
<tr>
<td>Net debt to equity ratio (financial leverage) (16)</td>
<td>93.33%</td>
<td>91.77%</td>
</tr>
<tr>
<td>Debt to equity ratio (17)</td>
<td>147.04%</td>
<td>129.19%</td>
</tr>
</tbody>
</table>

(1) operating profit (loss)/net sales revenue
(2) EBIT + amortisation/depreciation
(3) EBITDA/net sales revenue
(4) net profit (loss)/net sales revenue
(5) net profit (loss)/equity at the end of period
(6) net profit (loss)/assets at the end of period
(7) EBIT* 0.81/(equity + non-current/current loans and borrowings - cash - current financial assets) at the end of period
(8) current assets/current liabilities (as at the end of period)
(9) (current assets - inventories)/current liabilities (as at the end of period)
(10) current assets - current liabilities (as at the end of period)
(11) capital employed/assets (as at the end of period)
(12) (average trade receivables/net sales revenue)*365
(13) (average trade payables/cost of sales)*365
(14) total liabilities/assets (as at the end of period)
(15) non-current/current loans and borrowings - cash - current financial assets (as at the end of period)
(16) (non-current/current loans and borrowings - cash - current financial assets)/equity (as at the end of period)
(17) total liabilities/equity (as at the end of period)
An analysis of the above figures and ratios allows to identify the following changes in 2010:

- an improvement in EBIT margin, EBITDA margin and ROACE due to significantly higher operating result,
- lower net profit in connection with higher sales revenue, total assets and equity resulted in deterioration of the net margin, as well as ROE and ROA ratios reflecting the rate of return on invested equity and the profitability of asset,
- a considerable increase in current liabilities (up by 106.9%) led to a drop in current ratio (down by 33.7%) and quick ratio (down by 43.5%),
- a PLN 582.9m decrease in capital employed, in connection with the fact that current liabilities (up by PLN 2,250.9m) were growing faster than current assets (up by PLN 1,668.0m), and a decline in capital employed to total assets,
- shortening of the collection period and lengthening of the payment period in 2010: collection period shortened by six days due to the fact that average trade receivables were growing slower (up by 20.0%) than sales revenue (up by 42.7%); payment period lengthened by six days due to the fact that average trade payables were increasing faster (up by 82.8%) than cost of sales (up by 41.2%),
- a 3.2 percentage point increase in the share of liabilities in the financing of assets, owing to liabilities growing faster (up by 23.5%) than assets (up by 16.9%); a 1.6 percentage point rise in net financial debt to equity ratio (financial leverage), due to net financial debt increasing faster (up by 10.3%) than equity (up by 8.5%); a 17.9 percentage point increase in liabilities to equity ratio, driven by a 23.5% growth in liabilities with an 8.5% rise in equity.

3.4 USE OF ISSUE PROCEEDS TO IMPLEMENT THE ISSUE OBJECTIVES

Grupa LOTOS S.A. did not issue and securities in 2010.
The year 2010 began on a bearish note on the Warsaw Stock Exchange. In February, the main indices rallied, however it was not until the second half of the year that the upward trend settled in. Over the whole year, the WIG and WIG20 indices advanced 16.5% and 12.3%, respectively. The index comprising fuel companies – WIG FUELS – posted gains of 21.9%, while the RESPECT Index as much as 29.2%.

At the beginning of the year, the LOTOS stock clearly underperformed the market, bottoming out at its annual low of PLN 25.05 on the February 25th session. Thereafter, the stock started to follow the market, but only the release of the Company's new strategy in November provided a sufficient impulse to propel its dynamics past the 100% mark compared with the year’s beginning, translating into positive returns, only slightly below the WIG20 performance. On December 17th, the Company’s stock price reached its annual peak of PLN 37.85 per share. As at the end of 2010, its dynamics, relative to the period’s beginning, was 110.3%, which meant a rise of 10% and PLN 3.40 in absolute terms. On December 31st 2010, the stock closed at PLN 36.35. The average daily volume of trading in 2010 was 234.5 thousand shares. The Company’s market capitalisation as at the end of 2010 was a little more than PLN 4.7bn.
2	AGGREGATE NUMBER AND PAR VALUE OF GRUPA LOTOS S.A. SHARES AND SHARES IN GRUPA LOTOS S.A.’S RELATED UNDERTAKINGS, HELD BY MANAGEMENT AND SUPERVISORY STAFF

To the best of the Company’s knowledge, only the following members of management and supervisory staff hold shares in Grupa LOTOS S.A.

To the best of the Company’s knowledge, the following members of management and supervisory staff held shares in Grupa LOTOS S.A. as at December 31st 2010:

<table>
<thead>
<tr>
<th>Number of Grupa LOTOS S.A. shares</th>
<th>Par value (PLN)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management Board, including:</td>
<td>8,636</td>
</tr>
<tr>
<td>Mr Marek Sokolowski</td>
<td>8,636</td>
</tr>
<tr>
<td>Supervisory Board</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
<td>8,636</td>
</tr>
</tbody>
</table>

To the best of the Company’s knowledge, as at December 31st 2010 members of the management and supervisory staff did not hold any shares in the related undertakings of Grupa LOTOS S.A.
3 KNOWN AGREEMENTS WHICH MAY GIVE RISE TO CHANGES IN THE SHAREHOLDER STRUCTURE

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

4 CONTROL SYSTEMS FOR EMPLOYEE STOCK OPTION PLANS

In 2010, no control system for employee stock option plans existed at Grupa LOTOS S.A.

5 BUY-BACK OF OWN SHARES

In 2010, none of the LOTOS Group companies bought back its own shares.

6 PAYMENT OF DIVIDEND FOR 2009

Grupa LOTOS S.A. did not pay any dividend for 2009.
## SIGNATURES OF THE MANAGEMENT BOARD MEMBERS

<table>
<thead>
<tr>
<th>Role</th>
<th>Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>President of the Management Board, Chief Executive Officer</td>
<td>Pawel Olechnowicz</td>
</tr>
<tr>
<td>Vice-President of the Management Board, Chief Financial Officer</td>
<td>Mariusz Machajewski</td>
</tr>
<tr>
<td>Vice-President of the Management Board, Chief Operation Officer</td>
<td>Marek Sokolowski</td>
</tr>
<tr>
<td>Vice-President of the Management Board, Chief Commercial Officer</td>
<td>Maciej Szozda</td>
</tr>
</tbody>
</table>