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Consolidated report on payments to governments for 2018



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1. Basis of preparation

This consolidated report on payments to governments (the “report on payments” or the “report”) has been prepared in accordance with the Polish Accounting Act of September 29th 1994 (consolidated text: Dz.U. of 2018, item 395) (the “Act”). The Act implements into Polish law the provisions of Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC. In accordance with the Act, the LOTOS Group (the “LOTOS Group”, or the “Group”) prepares a report on payments to governments for each financial year with respect to extraction activities carried out through its upstream segment, which is engaged in the acquisition of crude oil and natural gas deposits and oil and gas production. The consolidated report on payments covers Grupa LOTOS S.A., as the Parent, and the entities it controls. Entities over which the Parent has joint control are not covered in this report.

2. Reporting rules

Types of activities covered in the report

In this report, the Group discloses payments made to governments in 2018 in connection with the operations of its upstream segment. These operations comprise exploration, prospecting, discovery, development, and extraction of minerals, oil, natural gas deposits or other materials (“upstream operations”). Payments related to the downstream segment, comprising production and processing of refined petroleum products and their wholesale and retail sale, as well as auxiliary, transport, and maintenance activities, are not covered in this report.

Recipient government authority

Government means any national, regional or local authority of the countries covered by this report, including a department, agency or undertaking controlled by that authority.

Payment

Payment means an amount paid, whether in money or in kind, accounted for on a cash basis. This means that the Group discloses a payment in the period when it is made. Cash basis is the opposite of accrual basis, where the disclosure is made in the period in which the liability arises. Payments made to the Group are also disclosed in the report on payments to governments in the period in which they are received by the Group and are presented at negative values. In the case of in-kind payments, the report discloses their volumes and values along with information on how the values were determined.

Project

In accordance with applicable regulations, payments are reported on a project basis (as a category within disclosure on a country basis). A project is defined as the operational activities that are governed by a single contract, licence, lease, concession or similar legal agreements and form the basis for payment liabilities to a government. Nonetheless, if a number of such agreements are substantially interconnected, they are considered a project. Substantially interconnected legal agreements should be understood as a set of operationally and geographically integrated contracts, licences leases, concessions or related agreements with substantially similar terms that are signed with a government, giving rise to payment liabilities. Such agreements can be governed by a single contract, joint venture, production sharing agreement, or other overarching legal agreement. The Group determines that agreements or licences are substantially interconnected as a set of operationally and geographically integrated agreements if they are jointly managed, situated within a specific area, and based on shared infrastructure. The number of projects depends on contractual arrangements within a country rather than on the scale of operations.

Sometimes it may be impossible to disclose a payment at project level. In such cases, the Group discloses obligations imposed at the country level rather than at project level. Corporate income tax is a typical case in point.

Materiality threshold

The Group presents a payment in this report if a single payment or a sum of related payments in a given financial year is equivalent to PLN 424.7 thousand or more.

Transaction currency

The functional currency of the Parent and the presentation currency of this consolidated report on payments to governments is the Polish złoty (“złoty”, “PLN”). This report has been prepared in thousands of złoty. Payments in foreign currencies are disclosed in this report after translation into the presentation currency based on the arithmetic mean of the mid rates quoted by the NBP for the last day of each full month of the financial year.

Joint operations

Settlements relating to field work performed jointly with other interest holders are made between the operator and consortium members by way of cash calls, which are then settled using the operator's billings issued after subsequent steps are completed.

Payments relating to joint operations, made by the Group directly to governments, are recognised in this report in full only if the Group is the project operator, even if the payments are spread pro rata between the other partners.

Payments are not disclosed in this report if other consortium members act as the operator as part of joint operations, and transfer the Group's share in payments to governments.

Payment categories

The reporting entities are required to disclose the total amount of payments made annually to governments in a given country, in money or in kind, for individual projects, if the payments are made with respect to:

- **Production entitlements**

The obligation to transfer a contractually agreed portion of output to the government of a country. These are usually in-kind payments. No production entitlements were paid in the period ended December 31st 2018.

- **Taxes**

This report includes taxes levied on income, production or profits of the Group entities, as well as taxes on dividends, royalties and interest received. Taxes levied on consumption, such as value added taxes, personal income taxes or sales taxes (including excise tax and tax on civil law transactions), as well as environmental taxes, customs and excise duties, are not subject to disclosure in this report.

- **Royalties**

Royalties are payments for oil and gas production licences, representing a share of production that is due to the holder of the licence. Royalties may be paid in money or in kind.

- **Dividends**

These include dividends paid to the State Treasury, other than dividends paid on the same terms as to other shareholders, unless they are paid in lieu of production entitlements or royalties. No dividend payments were made to governments in the year ended December 31st 2018.

- **Bonuses**

Bonuses are payments received, relating primarily to the achievement of or failure to achieve a certain production level and to a discovery of mineral deposits. No bonuses were paid in the period ended December 31st 2018.

- **Licence fees and other fees**

This category comprises licence fees, rental fees, entry fees, and other considerations for licences or concessions. Administrative fees that are not explicitly related to upstream operations are beyond the scope of this report.

- **Payments for infrastructure improvements**

These are payments related to construction (improvement) of infrastructure (roads, bridges), except where the infrastructure is used only for operating purposes. No payments for infrastructure improvements were made in the period ended December 31st 2018.

3. Payments by country

The tables below present payments to governments made by the LOTOS Group in the financial year 2018, broken down by country, type of payment, and the recipient government authority.

Country	Production entitlements	Taxes	Royalties	Fees	Bonuses	Payments for infrastructure improvements	Total
Poland	-	9,275	-	11,694	-	-	20,969
Norway	-	219,177	-	4,697	-	-	223,874
Lithuania	-	316	9,921	1,617	-	-	11,854
Total	-	228,768	9,921	18,008	-	-	256,697

POLAND

Recipient government authority	Production entitlements	Taxes	Royalties	Fees	Bonuses	Payments for infrastructure improvements	Total
Pomeranian Tax Office	-	8,875	-	-	-	-	8,875
Gdańsk Municipal Office	-	400	-	248	-	-	648
National Fund for Environmental Protection	-	-	-	10,324	-	-	10,324
Ministry of the Environment	-	-	-	1,038	-	-	1,038
Municipality and Town Municipal Offices	-	-	-	84	-	-	84
Total	-	9,275	-	11,694	-	-	20,969

Project	Production entitlements	Taxes	Royalties	Fees	Bonuses	Payments for infrastructure improvements	Total
B-3 Project	-	-	-	4,424	-	-	4,424
B-8 Project	-	5,937	-	6,147	-	-	12,084
Łeba Project	-	-	-	254	-	-	254
Rozewie Project	-	-	-	252	-	-	252
Młynary Project	-	-	-	91	-	-	91
Gotland Project	-	-	-	194	-	-	194
Payments not allocated to projects	-	3,338	-	332	-	-	3,670
Total	-	9,275	-	11,694	-	-	20,969

NORWAY

Recipient government authority	Production entitlements	Taxes	Royalties	Fees	Bonuses	Payments for infrastructure improvements	Total
The Norwegian Tax Administration	-	219,177	-	4,697	-	-	223,874
Total	-	219,177	-	4,697	-	-	223,874

Project	Production entitlements	Taxes	Royalties	Fees	Bonuses	Payments for infrastructure improvements	Total
PL029 (Sleipner West)	-	-	-	4,697	-	-	4,697
Payments not allocated to projects	-	219,177	-	-	-	-	219,177
Total	-	219,177	-	4,697	-	-	223,874

LITHUANIA

Recipient government authority	Production entitlements	Taxes	Royalties	Fees	Bonuses	Payments for infrastructure improvements	Total
Tax inspection (LR VMI)	-	316	9,921	1,600	-	-	11,837
Palanga Municipality	-	-	-	9	-	-	9
Kretinga Municipality	-	-	-	4	-	-	4
Gargždų Municipality	-	-	-	4	-	-	4
Total	-	316	9,921	1,617	-	-	11,854

Project	Production entitlements	Taxes	Royalties	Fees	Bonuses	Payments for infrastructure improvements	Total
Palanga	-	-	1,536	183	-	-	1,719
Kretinga	-	-	6,047	503	-	-	6,550
Klaipėda	-	-	2,338	863	-	-	3,201
Plungė	-	-	-	64	-	-	64
Gargždų	-	-	-	4	-	-	4
Payments not allocated to projects	-	316	-	-	-	-	316
Total	-	316	9,921	1,617	-	-	11,854

Signatures of Grupa LOTOS Management Board Members

This report has been authorised for publication.

President of the Management Board

Mateusz Aleksander Bonca

Vice President of the Management Board, Chief Investment and Innovation Officer

Patryk Demski

Vice President of the Management Board, Chief Refining and Marketing Officer

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