

Lubelski Węgiel Bogdanka S.A.

Audit Report on Financial Statements

for the financial year from 1 January 2010 to 31 December 2010

Audit Report on the Financial Statements for the General Shareholders Meeting and the Supervisory Board of Lubelski Węgiel Bogdanka S.A.

This Report contains 11 pages and comprises the following parts:

	Page
I. General information about the Group	2
II. Information about the conducted audit	3
III. Performance and financial standing of the Group	4
IV. Selected items of the consolidated financial statements	5
V. Statements of the independent certified auditor	9
VI. Final information and conclusions.....	10

I. General information about the Company

- (a) The Company was created following the restructuring of the state enterprise named Kopalnia Węgla Kamiennego Bogdanka. The deed of transformation into a company wholly owned by the State Treasury was prepared in the form of a notarial deed in the Notary's Office of Notary Jacek Wojdyło in Katowice on 1 March 1993 and recorded under Rep. No. 855/1993. On 26 March 2001 the District Court in Lublin, XI Division of the National Court Register, entered the Company to the Register of Entrepreneurs under entry No. KRS 0000004549.
- (b) In the audited financial year the Company conducted its operations pursuant to a licence for hard coal mining issued by the Minister for the Protection of the Environment, Natural Resources and Forestry on 27 August 1997.
- (c) For the purpose of tax settlements the Company was assigned the following tax identification number: NIP 713-000-57-84. For statistical purposes the Company holds the following industry identification number: REGON 430309210.
- (d) The registered share capital of the Company as at 31 December 2010 amounted to PLN 170,067,950 and was divided into 34,013,590 shares with a par value of PLN 5.00 per share.
- (e) In the audited period the Company was involved in the following operations:
- mining and agglomeration of hard coal;
 - manufacture of clay building materials.
- (f) In the audited year the Management Board of the Company was comprised of the following members:
- | | | |
|---|--------------------|--|
| • | Mirośław Taras | President of the Board |
| • | Krystyna Borkowska | Vice-President of the Board |
| • | Waldemar Bernaciak | Vice-President of the Board |
| • | Zbigniew Stopa | Vice-President of the Board |
| • | Janusz Chmielewski | Member of the Board up to 10 June 2010 |
- (g) The entities related to the Company are:
Łęczyńska Energetyka Sp. z o.o.
- (h) The Company issues securities admitted to trading on the Warsaw Stock Exchange. Using the option to choose the accounting principles provided for in the Act, starting from 2009 the Company draws up financial statements according to the International Financial Reporting Standards (IFRS) as endorsed by the European Union.
- The decision on the drawing up financial statements according to those standards was made by the General Shareholders Meeting by virtue of resolution No. 1 of 14 November 2008.
- (i) The Company, as the parent undertaking of the Group, also prepared the consolidated financial statements, as at 18 March 2011, according to the International Financial Reporting Standards (IFRS) as endorsed by the European Union. In order to understand the financial standing and results from operations of the Company as the parent undertaking of the Group, the separate financial statements should be read in conjunction with the consolidated financial statements.

II. Information about the conducted audit

- (a) PricewaterhouseCoopers Sp. z o.o. was appointed as the Company's auditor in a resolution no. 76/VII/2010 adopted by the Supervisory Board of 28 September 2010 pursuant to Article 32.1.4) of the Articles of Association of the Company.
- (b) PricewaterhouseCoopers Sp. z o.o. and key certified auditor conducting the audit are independent of the audited entity within the meaning of Articles 56.2 to 56.4 of the Act on Certified Auditors and their Professional Self-Government, Entities Authorised to Audit Financial Statements and Public Supervision of 7 May 2009 (Dz. U. No. 77, item 649).
- (c) The audit was conducted pursuant to an agreement entered into on 19 October 2010 on the following dates:
- preliminary audit from 17 December 2010 to 23 December 2010;
 - final audit from 24 January 2011 to 18 March 2011.

III. Performance and financial standing of the Company

The financial statements do not take into account the impact of inflation. In the audited year the consumer price index (December to December) was equal to 3.1% (2009: 3.5%).

The comments below are presented based on knowledge that has been obtained during the audit of the financial statements.

- At the end of the financial year the Company's assets amounted to PLN 2,812,176,000. During the year the balance sheet total went up by PLN 352,657,000, i.e. by 14.3%. This growth resulted first of all from an increase in the value of tangible fixed assets of PLN 532,604,000 and was partly set off by a decrease of cash (presented in current assets) of PLN 201,118,000 as compared to the prior year. Those changes were brought about by continuation of the investment process commenced in previous years.
- The total sales revenue amounted to PLN 1,221,540,000 and went up by 10.0% as compared to the prior year. The basic operations of the Company in the current year entailed the excavation and sale of hard coal. The increase in revenue was caused mainly by the increased volume of coal sales in relation to the prior year.
- The largest item of operating costs comprised employee benefits, which amounted in the audited period to PLN 390,927,000 and accounted for 32.7% of costs by nature of expense. Those costs were at a level comparable to that in the prior year (PLN 398,189,000).
- The profitability in terms of profit after tax equalled 18,6% and was higher by 1.3 percentage points than that generated in the prior year. The change in the Company's profitability was brought about basically by increased output of trading coal in the total excavation.
- The liquidity ratios, and namely current ratio and quick ratio equalled 1.6 and 1.4, respectively, and as compared to the prior year went down from 3.2 and 3.0, respectively, which was caused mainly by the use of cash funds for carrying out investment activities in the Stefanów Field.

IV. Selected items of the financial statements

STATEMENT OF FINANCIAL POSITION as at 31 December 2010

	31 Dec. 2010 PLN '000	31 Dec. 2009 PLN '000	Change PLN '000	Change (%)	31 Dec. 2010 Structure (%)	31 Dec. 2009 Structure (%)
ASSETS						
Fixed assets						
Tangible fixed assets	2,054,412	1,521,808	532,604	35.0	73.1	61.9
Intangible fixed assets	10,917	12,084	(1,167)	(9.7)	0.4	0.5
Long-term investments	73,341	73,341	-	-	2.6	3.0
Cash and cash equivalents	50,909	46,158	4,751	10.3	1.8	1.9
	2,189,579	1,653,391	536,188	32.4	77.9	67.3
Current assets						
Stocks	58,463	49,223	9,240	18.8	2.1	2.0
Trade debtors and other receivables	120,364	113,719	6,645	5.8	4.3	4.6
Overpaid income tax	4,456	2,754	1,702	61.8	0.2	0.1
Cash and cash equivalents	439,314	640,432	(201,118)	(31.4)	15.5	26.0
	622,597	806,128	(183,531)	(22.8)	22.1	32.7
Total assets	2,812,176	2,459,519	352,657	14.3	100.0	100.0

STATEMENT OF FINANCIAL POSITION as at 31 December 2010 (continued)

	31 Dec. 2010	31 Dec. 2009	Change	Change	31 Dec. 2010	31 Dec. 2009
	PLN '000	PLN '000	PLN '000	(%)	Structure (%)	Structure (%)
SHAREHOLDERS' EQUITY						
Ordinary shares	301,158	301,158	-	-	10.7	12.2
Other capitals	1,086,588	894,535	192,053	21.5	38.6	36.4
Retained profits	570,133	534,824	35,309	6.6	20.3	21.7
	1,957,879	1,730,517	227,362	13.1	69.6	70.3
LIABILITIES						
Long-term liabilities						
Loans and borrowings	200,000	250,000	(50,000)	(20.0)	7.1	10.2
Deferred income tax liabilities	56,378	59,903	(3,525)	(5.9)	2.0	2.4
Employee benefits liabilities	107,798	97,976	9,822	10.0	3.8	4.0
Provisions for other liabilities and charges	67,314	63,079	4,235	6.7	2.4	2.6
Grants	19,451	-	19,451	-	0.7	-
Trade creditors and other liabilities	5,808	7,834	(2,026)	(25.9)	0.2	0.3
	456,749	478,792	(22,043)	(4.6)	16.2	19.5
Short-term liabilities						
Loans and borrowings	50,000	-	50,000	-	1.8	-
Employee benefits liabilities	29,709	26,338	3,371	12.8	1.1	1.1
Provisions for other liabilities and charges	82,689	63,596	19,093	30.0	2.9	2.6
Trade creditors and other liabilities	235,150	160,276	74,874	46.7	8.4	6.5
	397,548	250,210	147,338	58.9	14.2	10.2
Total equity and liabilities	2,812,176	2,459,519	352,657	14.3	100.0	100.0

IV. Selected items of the financial statements (continued)

STATEMENT OF COMPREHENSIVE INCOME

For the financial year from 1 January to 31 December 2010

	2010 PLN '000	2009 PLN '000	Change PLN '000	Change %	2010 Structure	2009 Structure
Revenue on sales	1,221,540	1,110,851	110,689	10.0	100.0	100.0
Costs of products, goods and materials sold	(815,379)	(755,201)	(60,178)	8.0	(66.8)	(68.0)
Gross profit	406,161	355,650	50,511	14.2	33.2	32.0
Selling costs	(36,069)	(41,652)	5,583	(13.4)	(2.9)	(3.7)
Administrative costs	(67,888)	(64,485)	(3,403)	5.3	(5.5)	(5.8)
Other income	3,535	6,030	(2,495)	(41.4)	0.3	0.5
Other expenses	(3,343)	(2,140)	(1,203)	56.2	(0.3)	(0.2)
Other net losses	(27,650)	(22,602)	(5,048)	22.3	(2.3)	(2.0)
Operating profit	274,746	230,801	43,945	19.0	22.5	20.8
Financial income	23,569	16,002	7,567	47.3	1.9	1.4
Financial expenses	(13,543)	(7,067)	(6,476)	91.6	(1.1)	(0.6)
Net financial income	10,026	8,935	1,091	12.2	0.8	0.8
Profit before taxation	284,772	239,736	45,036	18.8	23.3	21.6
Income tax	(57,410)	(47,683)	(9,727)	20.4	(4.7)	(4.3)
Net profit for the financial year	227,362	192,053	35,309	18.4	18.6	17.3
Total income for the period	227,362	192,053	35,309	18.4		

IV. Selected items of the financial statements (continued)

Selected items characterising the economic and financial position as well as financial results of the Company

The following items characterise the Company's business activity, its financial results for the financial year as well as the economic and financial situation as at the balance-sheet date in comparison with previous periods:

	2010	2009	2008
Activity ratios			
- Receivables turnover rate	23 days	27 days	28 days
- Inventory turnover rate	24 days	20 days	18 days
Return ratios			15,4%
- Net profit margin	18.6%	17.3%	20.7%
- Gross margin on sales	24.8%	22.5%	15.3%
- Return on equity	12.3%	13.5%	32.8%
Debt ratios			
- Debt ratio	30.4%	29.6%	32.8%
- Liabilities turnover rate	24 days	23 days	21 days
	31 Dec. 2010	31 Dec. 2009	31 Dec. 2008
Liquidity ratios			
-Liquidity ratio I	1.6	3.2	0.7
-Liquidity ratio II	1.4	3.0	0.6

V. Statements of the independent certified auditor

- (a) In the course of our audit the Management Board of the Company provided the required information, explanations and declarations, and presented a statement regarding complete recognition of all accounting data in books and disclosure of all contingent liabilities, as well as notified material subsequent events up to the date of the statement.
- (b) The scope of our audit was not restricted in any way.
- (c) The Company had an up-to-date documentation describing the accounting principles (policies), approved by the Management Board. The accounting principles adopted by the Company were adjusted to its needs and ensured that all events material for the assessment of the Company's financial standing and financial result according to the prudence principle, were clearly recognised. The continuity of applied policies with the preceding period was maintained.
- (d) The closing balance of the end of the preceding financial year was in all materials aspects correctly entered to the books as the opening balance of the current period.
- (e) We assessed the correctness of the functioning of the accounting system. In particular our assessment focused on:
- correctness of documenting business operations;
 - reliability, faultlessness and verifiability of accounting books, including electronically maintained books,
 - methods of securing access to data and the system of data processing in computer,
 - protection of accounting documentation, accounting books and financial statements.
- The assessment combined with the audit of the accuracy of individual items of the financial statements serve as a basis for issuing a general, complete and unqualified opinion on the correctness and reliability of these statements. It was not our purpose to issue a comprehensive opinion on the functioning of the abovementioned system.
- (h) The supplementary information presents all material information required by the IFRS as endorsed by the European Union.
- (i) The information included in the Company's Directors' report on operations for the year from 1 January 2010 to 31 December 2010 satisfies the requirements of the Regulation of the Minister of Finance dated 19 February 2009 on current and periodic information provided by issuers of securities and on conditions under which information required by legal regulations of a third country may be recognised as equivalent (Dz.U. No. 33, item 259) and correspond to the information included in the audited financial statements.
- (j) The inventory-taking of the assets and shareholders' equity and liabilities was carried out and settled in compliance with the Accounting Act, and the results were recorded in the accounting books for the year subject to the audit.
- (k) The financial statements for the prior year were audited by PricewaterhouseCoopers Sp. z o.o. The certified auditor issued an unqualified opinion.
- (l) The Company's financial statements for the financial year from 1 January 2009 to 31 December 2009 were approved by a resolution no. 6 adopted by the General Shareholders Meeting on 10 June 2010. They were filed with the National Court Register in Lublin on 18 June 2010 and published in the *Monitor Polski B* gazette no. 417/2340 on 22 February 2011.

PricewaterhouseCoopers Sp. z o.o.

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VI. Final information and conclusions

This report has been prepared in connection with audit of the financial statements of Lubelski Węgiel Bogdanka S.A. with registered office in Bogdanka, 21-013 Puchaczów. The audited financial statements included:

- (a) statement of financial position as at 31 December 2010, with the total assets as well as the total liabilities and equity amounting to PLN 2,812,176,000;
- (b) statement of comprehensive income for the period from 1 January 2010 to 31 December 2010, with the comprehensive income amounting to PLN 227,362,000,
- (c) statement of changes in equity for the period from 1 January 2010 to 31 December 2010, with an increase in equity by PLN 227,362,000;
- (d) statement of cash flows for the period from 1 January 2010 to 31 December 2010, with the net cash outflows amounting to PLN 201,118,000;
- (e) supplementary information about the adopted accounting principles and other explanatory notes.

The financial statements were signed by the Management Board of the Company and the person who was entrusted the maintenance of the accounting books, on 18 March 2011. This report should be read together with the independent auditor's opinion for the General Shareholders Meeting and the Supervisory Board of Lubelski Węgiel Bogdanka S.A. dated 18 March 2011 regarding the above financial statements. The opinion on the financial statements presents a general conclusion from the conducted audit. Such conclusion does not represent the sum of assessments following from auditing individual items of the financial statements or issues, but assumes that a relevant weight (significance) is assigned to particular findings, taking into account the impact of determined facts on a true and fair picture and correctness of the financial statements.

Person conducting the audit on behalf of PricewaterhouseCoopers Sp. z o.o., a company entered into a list of entities authorised to audit financial statements under entry 144:

Tomasz Reinfuss

Key Certified Auditor

Register Number 90038

Katowice, 18 March 2011.