

**POLISH FINANCIAL SUPERVISION AUTHORITY**

**Annual report R 2011**

(In accordance with § 82, section 1, point 3 of the Decree of the Minister of Finance dated 19 February 2009  
– Journal of Laws No. 33, point 259)

**for issuers of securities involved in production, construction, trade or services activities**

for the financial year **2011** comprising the period from **1 January 2011** to **31 December 2011**  
containing the financial statements according to International Financial Reporting Standards in PLN.

publication date: 30 March 2012

<b>KGHM Polska Miedź Spółka Akcyjna</b> (name of the issuer)	
<b>KGHM Polska Miedź S.A.</b> (name of issuer in brief) <b>59 – 301</b> (postal code) <b>M. Skłodowskiej – Curie</b> (street) <b>(48 76) 74 78 200</b> (telephone) <b>IR@BZ.KGHM.pl</b> (e-mail) <b>692-000-00-13</b> (NIP)	<b>Basic materials</b> (issuer branch title per the Warsaw Stock Exchange) <b>LUBIN</b> (city) <b>48</b> (number) <b>(48 76) 74 78 500</b> (fax) <b>www.kghm.pl</b> (website address) <b>390021764</b> (REGON)

PricewaterhouseCoopers Sp. z o.o.  
(entity entitled to audit financial statements)

SELECTED FINANCIAL DATA	in '000 PLN		in '000 EUR	
	year 2011 period from 1 January 2011 to 31 December 2011	year 2010 period from 1 January 2010 to 31 December 2010	year 2011 period from 1 January 2011 to 31 December 2011	year 2010 period from 1 January 2010 to 31 December 2010
I. Sales	20 097 392	15 945 032	4 854 325	3 981 878
II. Operating profit	13 687 640	5 638 148	3 306 113	1 407 988
III. Profit before income tax	13 653 597	5 605 567	3 297 891	1 399 852
IV. Profit for the period	11 334 520	4 568 589	2 737 741	1 140 892
V. Other comprehensive income	324 514	83 931	78 383	20 960
VI. Total comprehensive income	11 659 034	4 652 520	2 816 124	1 161 852
VII. Number of shares issued	200 000 000	200 000 000	200 000 000	200 000 000
VIII. Earnings per ordinary share (in PLN/EUR)	56.67	22.84	13.69	5.70
IX. Net cash generated from operating activities	8 768 122	5 346 791	2 117 853	1 335 229
X. Net cash generated from/(used in) investing activities	3 589 742	(3 125 246)	867 066	(780 453)
XI. Net cash used in financing activities	(2 993 020)	(606 194)	(722 934)	(151 382)
XII. Total net cash flow	9 364 844	1 615 351	2 261 985	403 394
	<b>At 31 December 2011</b>	<b>At 31 December 2010</b>	<b>At 31 December 2011</b>	<b>At 31 December 2010</b>
XIII. Non-current assets	11 696 705	12 125 041	2 648 231	3 061 647
XIV. Current assets	17 556 484	7 704 255	3 974 933	1 945 372
XV. Total assets	29 253 189	19 829 296	6 623 164	5 007 019
XVI. Non-current liabilities	2 249 946	2 380 314	509 406	601 044
XVII. Current liabilities	3 867 732	2 992 505	875 687	755 626
XVIII. Equity	23 135 511	14 456 477	5 238 071	3 650 349

**Average EUR/PLN exchange rate of the National Bank of Poland**

	<b>31 December 2011</b>	<b>31 December 2010</b>
Average exchange rate for the period	4.1401	4.0044
Average exchange rate at the end of the period	4.4168	3.9603

**This report is a direct translation from the original Polish version. In the event of differences resulting from the translation, reference should be made to the official Polish version.**

# **KGHM POLSKA MIEDŹ S.A.**

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## **ANNUAL REPORT R 2011 COMPRISES:**

- 1. AUDITOR'S OPINION AND REPORT ON ITS AUDIT OF THE FINANCIAL STATEMENTS**
  - 2. DECLARATION BY THE MANAGEMENT BOARD ON THE ACCURACY OF THE PREPARED FINANCIAL STATEMENTS**
  - 3. DECLARATION BY THE MANAGEMENT BOARD REGARDING THE ENTITY ENTITLED TO AUDIT FINANCIAL STATEMENTS**
  - 4. PRESIDENT'S LETTER**
  - 5. FINANCIAL STATEMENTS**
  - 6. REPORT OF THE MANAGEMENT BOARD ON THE COMPANY'S ACTIVITIES**
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**Lubin, March 2012**

**KGHM POLSKA MIEDŹ S.A.**

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**AUDITOR'S OPINION AND REPORT  
ON ITS AUDIT OF THE FINANCIAL  
STATEMENTS FOR 2011**

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Lubin, March 2012



**Independent Registered Auditor's Opinion  
to the General Shareholders' Meeting and the Supervisory Board  
of KGHM Polska Miedź Spółka Akcyjna**

We have audited the accompanying financial statements of KGHM Polska Miedź Spółka Akcyjna (hereinafter called "the Company") with its registered office in Lubin, 48 Marii Skłodowskiej-Curie Street, which comprise the statement of financial position as at 31 December 2011, showing total assets and total liabilities and equity of PLN 29.253.189 thousand, the statement of comprehensive income for the period from 1 January to 31 December 2011, showing a total comprehensive income of PLN 11.659.034 thousand, the statement of changes in equity, the statement of cash flows for the financial year and additional information on adopted accounting policies and other explanatory notes.

The Company's Management Board is responsible for preparing the financial statements and the Directors' Report in accordance with the applicable regulations, and for the correctness of the accounting records. The Management Board and Members of the Supervisory Board are required to ensure that the financial statements and the Director's Report meet the requirements set out in the Accounting Act of 29 September 1994 (uniform text, Journal of Laws of 2009, No. 152, item 1223 with further amendments, hereinafter referred to as "the Act").

Our responsibility was to perform an audit of the accompanying financial statements and to express an opinion on whether the financial statements comply in all material respects with the applicable accounting policies and whether they present fairly, in all material respects, the Company's financial position and results, and whether the accounting records constituting the basis for their preparation are properly maintained.

We conducted our audit in accordance with the following:

- a. the provisions of Chapter 7 of the Act;
- b. national standards of auditing issued by the National Chamber of Registered Auditors.

Our audit was planned and performed to obtain reasonable assurance that the financial statements were free of material misstatements and omissions. The audit included examining, on a test basis, accounting documents and entries supporting the amounts and disclosures in the financial statements. The audit also included an assessment of the accounting policies applied by the Company and significant estimates made in the preparation of the financial statements as well as an evaluation of the overall presentation thereof. We believe that our audit provides a reasonable basis for our opinion.

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*PricewaterhouseCoopers Sp. z o.o., Aleja Armii Ludowej 14, 00-638 Warszawa, Polska  
Telefon +48 22 523 4000, Faks +48 22 508 4040, [www.pwc.pl](http://www.pwc.pl)*



**Independent Registered Auditor's Opinion  
to the General Shareholders' Meeting and the Supervisory Board  
of KGHM Polska Miedź Spółka Akcyjna (cont.)**

In our opinion, and in all material respects, the accompanying financial statements:

- a. present fairly the Company's financial position as at 31 December 2011 and of the results of its operations for the year then ended, in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union;
- b. comply in form and content with the applicable laws and the Company's Memorandum of Association;
- c. have been prepared on the basis of properly maintained accounting records.

The information in the Directors' Report for the year ended 31 December 2011 has been prepared in accordance with the provisions of the Decree of the Minister of Finance dated 19 February 2009 concerning the publication of current and periodic information by issuers of securities and the conditions of acceptance as equal information required by the law of other state, which is not a member state (*"the Decree"* – Journal of Laws of 2009, No. 33, item 259, with further amendments) and is consistent with the information presented in the audited financial statements.

Conducting the audit on behalf of PricewaterhouseCoopers Sp. z o.o., Registered Audit Company No. 144:

Marcin Sawicki

Key Registered Auditor  
No. 11393

Wrocław, 27 March 2012 r.



**KGHM Polska Miedź S.A.**

**Report on the financial statements  
as at and for the year ended 31 December 2011**

**Report on the financial statements  
for the financial year ended 31 December 2011  
to the General Shareholders' Meeting and Supervisory Board  
of KGHM Polska Miedź Spółka Akcyjna**

**This report contains 14 consecutively numbered pages and consists of:**

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I. General information about the Company .....	2
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**KGHM Polska Miedź S.A.**  
**Report on the financial statements**  
**as at and for the year ended 31 December 2011**

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**I. General information about the Company**

- a. KGHM Polska Miedź Spółka Akcyjna („The Company”) was founded as a result of transformation of a state-owned enterprise, Kombinat Górniczo-Hutniczy Miedzi on the basis of art. 5 of the Act dated 13 July 1990 concerning the privatisation of state-owned enterprises (*Jurnal of Laws* No. 51, item 298, with subsequent amendments). The Notarial Deed was drawn up on 9 September 1991 at the Notary public’s Office No. 18 in Warsaw and registered with Rep. no. 8648/91. On 29 June 2001 the District Court Register decided to enter the Company in the Commercial Register with the reference number KRS 23302.
- b. The Company has its seat in Lubin, 48 Marii Skłodowskiej-Curie Street.
- c. In the audited year, the Company operated on the basis of a concession granted by the Minister of the Environmental Protection, Natural Resources and Forestry.
- d. On 14 June 1993 the Company was assigned a tax identification number (NIP) 692-000-00-13 for the purpose of making tax settlements and on 13 August 2003 the Company was assigned a REGON number 390021764 for statistical purposes.
- e. As at 31 December 2011 the Company’s registered share capital amounted to PLN 2.000.000.000 and consisted of 200.000.000 shares, with a nominal value of PLN 10 per share. As at 31 December 2011 the Company’s equity was positive and amounted to PLN 23.135.511 thousand.

- f. As at 31 December 2011 the shareholders of the Company were:

Shareholder’s name	Number of shares held	Par value of shares held (PLN)	Type of shares held	Votes (%)
The Polish State Treasury	63.589.900	635.899.000	ordinary	31,79
Other shareholders	136.410.100	1.364.101.000	ordinary	68,21
	<b>200.000.000</b>	<b>2.000.000.000</b>		<b>100,00</b>

- g. In the audited period the Company’s core business was:
  - metal ore mining,
  - production of non-ferrous metals, precious metals, and salts,
  - casting of light metals and non-ferrous metals,
  - waste management,
  - wholesale trading on the basis of direct payment or contract,
  - geological and exploratory activities, research and technical analyses,
  - professional rescue services.
- h. During the audited year the Management Board of the Company comprised:
  - Herbert Wirth                      President,
  - Maciej Tybura                      I Vice President (Finance),
  - Wojciech Kędzia                      Vice President (Production).

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**KGHM Polska Miedź S.A.**  
**Report on the financial statements**  
**as at and for the year ended 31 December 2011**

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**I. General information about the Company (cont.)**

i. The Company has the following related entities:

- the Polish State Treasury (the Company's parent entity in accordance with IAS 27) and its subsidiaries,
- entities incorporated into the capital group, in which the Company is the parent entity together with their associates,
- key members of the Company's management.

Transactions with related parties were described in note no. 35 to the financial statement.

- j. The Company is an issuer of securities admitted for trading on the Warsaw Stock Exchange. In accordance with the choice of selecting accounting policies permitted by the Accounting Act, from 2007, the Company has decided to prepare its financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.
- k. As the parent company of the KGHM Polska Miedź S.A. Group, the Company has also prepared consolidated financial statements according to IFRS as adopted by the European Union as at 27 March 2012. To better understand the Company's financial position and its results of operations as the Parent Company, the financial statements should be read in conjunction with the consolidated financial statements.

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**KGHM Polska Miedź S.A.**  
**Report on the financial statements**  
**as at and for the year ended 31 December 2011**

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**II. Information about the audit**

- a. The audit of the financial statements as at and for the year ended 31 December 2011 was conducted by PricewaterhouseCoopers Sp. z o.o. having its seat in Warsaw, Al. Armii Ludowej 14, registered audit company no. 144. The audit was conducted on behalf of the registered audit company under the supervision of the key registered auditor Marcin Sawicki (no. 11393).
- b. PricewaterhouseCoopers Sp. z o.o. was appointed registered auditor to the Company by Resolution No. 31/VII/10 of the Supervisory Board dated 16 April 2010 in accordance with paragraph 20, point 2 of the Company's Articles of Association.
- c. PricewaterhouseCoopers Sp. z o.o. and the key registered auditor conducting the audit are independent of the audited entity within the meaning of art. 56, clauses 2-4 of the Act on registered auditors and their council, entities entitled to provide an audit of the financial statements and public supervision of 7 May 2009 (Journal of Laws of 2009, No. 77, item 649, with further amendments).
- d. The audit was performed on the basis of an agreement dated 25 May 2010 and conducted in the following periods:
  - interim audit                      from 31 October to 18 November 2011;
  - final audit                              from 23 January to 27 March 2012.

### **III. The Company's results and financial position**

The financial statements do not take into account the effects of inflation. The consumer price index (on a December to December basis) amounted to 4.6% in the audited year (3.1% in 2010).

The following comments are based on information obtained during the audit of the financial statements.

- As at the end of the financial year the Company's total assets amounted to PLN 29.253.189 thousand. During the year total assets increased by PLN 9.423.893 thousand (i.e. by 47,5%). This increase was financed by net profit (in the value of PLN 11.334.520 thousand), other comprehensive income (in the value of PLN 324.514 thousand), an increase in current income tax liabilities (by PLN 918.923 thousand), while the liabilities due to valuation of derivatives were decreased (by PLN 324.765 thousand). In 2011 the Company paid a dividend of PLN 2.980.000 thousand to its shareholders.
- Total revenues amounted to PLN 20.097.392 thousand and increased by 26,0% when compared to the previous year. The Company's core activities in the current financial year consisted of production and sale of copper, precious metals and smelter by-products. This growth was mainly due to favourable conditions on international and domestic industrial goods markets during 2011, which were reflected in an increase in sales volume of copper and copper products. The additional factor for the growth was an increase of the average price of copper and silver when compared with the prior period (of 16,9% and 73,9% respectively). In the same period the average exchange rate of US Dollar decreased by 2,0% when compared to 2010. The revenues include also profit on foreign currencies' and commodities' hedge transactions amounted to PLN 241.565 thousand.
- The operating expenses (the total of cost of sales, selling and administrative expenses) increased by PLN 1.446.153 thousand (15,6%) when compared to 2010. The change was mainly due to the growth of material and energy costs.
- Profitability measured with net profit amounted to 56% and was 27 percentage points higher than in the previous year. The change in the Company's profitability was primarily due to high prices of metals, mainly copper, on international commodity markets during 2011 and sale of shares of Polkomtel S.A.
- The Company's financial ratios and structure of debt has changed. The Company's debt ratio amounted to 21% at the end of audited year (27% at the end of the previous year). The payables turnover amounted to 26 days (25 days in the previous year).
- The Company's liquidity has changed. The current ratio amounted to 4,5 (2,6 in 2010), whereas the quick ratio amounted to 3,9 (1,9 in 2010).

**KGHM Polska Miedź S.A.**  
**Report on the financial statements as at and for the year ended 31 December 2011**

**IV. Discussion of financial statement components**

**STATEMENT OF FINANCIAL POSITION as at 31 December 2011**

	Note	31.12.2011	31.12.2010	Change	Change	31.12.2011	31.12.2010
		PLN'000	PLN'000	PLN'000	(%)	Structure (%)	Structure (%)
<b>ASSETS</b>							
<b>Non-current assets</b>							
Property, plant and equipment		7.277.903	6.551.111	726.792	11,1	24,9	33,0
Intangible assets		150.777	86.718	64.059	73,9	0,5	0,4
Shares and investment certificates in subsidiaries	1	2.012.209	2.643.046	(630.837)	(23,9)	6,9	13,3
Investments in associates	2	-	1.159.947	(1.159.947)	(100,0)	-	5,9
Deferred tax assets		168.462	359.833	(191.371)	(53,2)	0,6	1,8
Available-for-sale financial assets	3	992.068	749.824	242.244	32,3	3,4	3,8
Held-to-maturity investments		111.665	84.115	27.550	32,8	0,4	0,4
Derivatives	4	899.400	403.839	495.561	>100,0	3,0	2,1
Trade and other receivables		84.221	86.608	(2.387)	(2,8)	0,3	0,4
		<b>11.696.705</b>	<b>12.125.041</b>	<b>(428.336)</b>	<b>(3,5)</b>	<b>40,0</b>	<b>61,1</b>
<b>Current assets</b>							
Inventories		2.355.741	2.011.393	344.348	17,1	8,1	10,1
Trade and other receivables	5	1.502.944	2.393.986	(891.042)	(37,2)	5,1	12,1
Available-for-sale financial assets	3	-	405.193	(405.193)	(100,0)	-	2,0
Held-to-maturity investments		2.147	4.129	(1.982)	(48,0)	-	0,1
Derivatives	4	859.653	294.021	565.632	>100,0	2,9	1,5
Cash and cash equivalents	6	12.835.999	2.595.529	10.240.470	>100,0	43,9	13,1
Non-current assets held for sale		-	4	(4)	(100,0)	-	-
		<b>17.556.484</b>	<b>7.704.255</b>	<b>9.852.229</b>	<b>&gt;100,0</b>	<b>60,0</b>	<b>38,9</b>
<b>Total assets</b>		<b>29.253.189</b>	<b>19.829.296</b>	<b>9.423.893</b>	<b>47,5</b>	<b>100,0</b>	<b>100,0</b>

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**KGHM Polska Miedź S.A.**  
**Report on the financial statements as at and for the year ended 31 December 2011**

**IV. Discussion of financial statement components (cont.)**

**STATEMENT OF FINANCIAL POSITION as at 31 December 2011 (cont.)**

	Note	31.12.2011 PLN'000	31.12.2010 PLN'000	Change PLN'000	Change (%)	31.12.2011 Structure (%)	31.12.2010 Structure (%)
<b>EQUITY</b>	7						
Share capital	8	2.000.000	2.000.000	-	-	6,9	10,0
Other accumulated comprehensive income		535.673	211.159	324.514	>100,0	1,8	1,1
Retained earnings	9	20.599.838	12.245.318	8.354.520	68,2	70,4	61,8
		<b>23.135.511</b>	<b>14.456.477</b>	<b>8.679.034</b>	<b>60,0</b>	<b>79,1</b>	<b>72,9</b>
<b>LIABILITIES</b>							
<b>Non-current liabilities</b>							
Trade and other payables		11.579	14.249	(2.670)	(18,7)	-	0,1
Borrowings and financial lease liabilities		35	8.490	(8.455)	(99,6)	-	-
Derivatives	4	538.320	711.580	(173.260)	(24,3)	1,8	3,6
Liabilities due to employee benefits		1.216.355	1.128.246	88.109	7,8	4,2	5,7
Provisions for other liabilities and charges		483.657	517.749	(34.092)	(6,6)	1,7	2,6
		<b>2.249.946</b>	<b>2.380.314</b>	<b>(130.368)</b>	<b>(5,5)</b>	<b>7,7</b>	<b>12,0</b>
<b>Current liabilities</b>							
Trade and other payables		1.827.536	1.727.939	99.597	5,8	6,3	8,7
Borrowings and financial lease liabilities		58	2.965	(2.907)	(98,0)	-	-
Current income tax liabilities	10	1.587.847	668.924	918.923	>100,0	5,4	3,4
Derivatives	4	330.347	481.852	(151.505)	(31,4)	1,1	2,4
Liabilities due to employee benefits		107.471	93.041	14.430	15,5	0,4	0,5
Provisions for liabilities and other charges		14.473	17.784	(3.311)	(18,6)	-	0,1
		<b>3.867.732</b>	<b>2.992.505</b>	<b>875.227</b>	<b>29,2</b>	<b>13,2</b>	<b>15,1</b>
<b>Total liabilities and equity</b>		<b>29.253.189</b>	<b>19.829.296</b>	<b>9.423.893</b>	<b>47,5</b>	<b>100,0</b>	<b>100,0</b>

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**KGHM Polska Miedź S.A.**  
**Report on the financial statements as at and for the year ended 31 December 2011**

**IV. Discussion of financial statement components (cont.)**

**STATEMENT OF COMPREHENSIVE INCOME for the period from 1 January to 31 December 2011**

	Note	2011 PLN'000	2010 PLN'000	Change PLN'000	Change (%)	2011 (%) of revenues	2010 (%) of revenues
Revenues		20.097.392	15.945.032	4.152.360	26,0	100,0	100,0
Cost of sales		(9.877.794)	(8.617.125)	(1.260.669)	14,6	(49,1)	(54,0)
<b>Gross profit</b>		<b>10.219.598</b>	<b>7.327.907</b>	<b>2.891.691</b>	<b>39,5</b>	<b>50,9</b>	<b>46,0</b>
Selling costs		(111.043)	(103.171)	(7.872)	7,6	(0,6)	(0,6)
Administrative expenses		(745.002)	(567.390)	(177.612)	31,3	(3,7)	(3,6)
Other operating income	1, 2, 11	5.092.919	711.202	4.381.717	>100,0	25,3	4,5
Other operating expenses	11	(768.832)	(1.730.400)	961.568	(55,6)	(3,8)	(10,9)
<b>Operating profit</b>		<b>13.687.640</b>	<b>5.638.148</b>	<b>8.049.492</b>	<b>&gt;100,0</b>	<b>68,1</b>	<b>35,4</b>
Finance costs		(34.043)	(32.581)	(1.462)	4,5	(0,2)	(0,2)
<b>Profit before income tax</b>		<b>13.653.597</b>	<b>5.605.567</b>	<b>8.048.030</b>	<b>&gt;100,0</b>	<b>67,9</b>	<b>35,2</b>
Income tax expense	10, 12	(2.319.077)	(1.036.978)	(1.282.099)	>100,0	(11,5)	(6,5)
<b>Profit for the period</b>	9	<b>11.334.520</b>	<b>4.568.589</b>	<b>6.765.931</b>	<b>&gt;100,0</b>	<b>56,4</b>	<b>28,7</b>
Other comprehensive income		324.514	83.931	240.583	>100,0	1,6	0,5
<b>Total comprehensive income</b>		<b>11.659.034</b>	<b>4.652.520</b>	<b>7.006.514</b>	<b>&gt;100,0</b>	<b>58,0</b>	<b>29,2</b>

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**KGHM Polska Miedź S.A.**  
**Report on the financial statements as at and for the year ended 31 December 2011**

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**IV. Discussion of financial statement components (cont.)**

**Presentation of the Company's financial position and results**

The following ratios characterize the Company's activities, results of operations during the audited year and its financial position as at the end of the reporting period compared with previous years:

	<b>2011 r.</b>	<b>2010 r.</b>	<b>2009 r.</b>
Asset ratios			
- receivables turnover	24 days	29 days	23 days
- inventory turnover	80 days	82 days	84 days
Profitability ratios			
- net profitability of sales	56%	29%	23%
- gross margin	68%	35%	28%
- return on capital employed	60%	37%	24%
Liability ratios			
- gearing ratio	21%	27%	25%
- payables turnover	26 days	25 days	27 days
	<b>31.12.2011 r.</b>	<b>31.12.2010 r.</b>	<b>31.12.2009 r.</b>
Liquidity ratios			
- current ratio	4,5	2,6	2,4
- quick ratio	3,9	1,9	1,4
Other ratios			
- effective tax rate	17,0%	18,5%	17,2%

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#### **IV. Discussion of financial statement components (cont.)**

##### **The statement of financial position as at 31 December 2011**

###### **1. Shares and investment certificates in subsidiaries**

In the audited year, the value of shares and investment certificates in subsidiaries decreased by PLN 630.837 thousand, i.e. by 23,9%, compared to the previous year. This decrease results mainly from the disposal of the subsidiary Telefonía Dialog S.A. (at a book value of PLN 824.926 thousand).

###### **2. Investments in associates**

The value of investments in associates decreased due to disposal of shares of Polkomtel S.A. in the amount of PLN 1.159.947 thousand in 2011.

###### **3. Available-for-sale financial assets**

The value of available-for-sale financial assets (long- and short-term) amounted to PLN 992.068 thousand at the end of the audited period and decreased by PLN 162.949 thousand in comparison to 2010. The main reason of change was sale of the certificates in open-end investments funds (at a book value as at 31 December 2010 of PLN 405.193 thousand) and acquisition of additional shares of Tauron Polska Energia S.A.

The balance of available-for-sale financial assets as at the end of financial year consisted mainly of shares of companies listed on stock exchanges in Poland and Canada.

###### **4. Derivatives**

At the end of the accounting period assets related to valuation of derivatives (long- and short-term) amounted to PLN 1.759.053 thousand and increased by PLN 1.061.193 thousand comparing to the previous year.

At the end of the accounting period liabilities related to valuation of derivatives (long- and short-term) amounted to PLN 868.667 thousand and decreased by PLN 324.765 thousand comparing to 2010.

###### **5. Current trade and other receivables**

The balance of trade and other receivables decreased by PLN 893.429 thousand comparing to the previous year and amounted to PLN 1.587.165 thousand on 31 December 2011. The main reason for the drop was a decrease of the balance of trade receivables compared to the previous year and termination of deposits with a maturity over 3 to 12 months, which have been entered in 2010 by the end of 2011.



**KGHM Polska Miedź S.A.**  
**Report on the financial statements**  
**as at and for the year ended 31 December 2011**

**IV. Discussion of financial statement components (cont.)**

**6. Cash and cash equivalents**

Cash and cash equivalents contained deposits amounted to PLN 12.811.794 thousand, interest on deposit amounted to PLN 15.751 thousand and cash on hand and in bank amounted to PLN 8.454 thousand. The growth by PLN 10.240.470 thousand compared to the previous year was mainly due to an increase of cash flows from operating activities and obtaining cash flows from disposal of shares of Polkomtel S.A. and Telefonía Dialog S.A.

**7. Equity**

	<b>31.12.2010</b>	<b>Net profit for 2011</b>	<b>Other comprehen- sive income</b>	<b>Dividend paid</b>	<b>31.12.2011</b>
	<b>PLN'000</b>	<b>PLN'000</b>	<b>PLN'000</b>	<b>PLN'000</b>	<b>PLN'000</b>
Share capital	2.000.000	-	-	-	2.000.000
Other accumulated comprehensive income	211.159	-	324.514	-	535.673
Retained earnings	12.245.318	11.334.520	-	(2.980.000)	20.599.838
<b>Total</b>	<b>14.456.477</b>	<b>11.334.520</b>	<b>324.514</b>	<b>(2.980.000)</b>	<b>23.135.511</b>

In the audited period the amount of share capital did not change.

**8. Share capital – ownership structure**

As at 31 December 2011 the only shareholder of the Company holding more than 5% of share capital was the Polish State Treasury. The State Treasury held 63.589.900 ordinary shares with nominal value of PLN 635.899 thousand, which constituted 31,79% of voting rights at the General Shareholders Meeting.

**9. Retained earnings – profit**

The profit for the audited year amounted to PLN 11.334.520 thousand.

In accordance with the Resolution no. 6/2011 of the General Shareholders' Meeting dated 15 June 2011, the profit for the previous year of PLN 4.568.589 thousand was appropriated as follows:

- PLN 2.980.000 thousand	paid as dividend to shareholders,
- PLN 1.588.589 thousand	transferred to supplementary capital (retained earnings).

**10. Current income tax liabilities**

As at the end of the reporting period the balance of current income tax liabilities amounted to PLN 1.587.847 thousand and increased by PLN 918.923 thousand when compared with the previous accounting period. The increase was mainly due to significantly higher taxable profit obtained by the Company in 2011.

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**IV. Discussion of financial statement components (cont.)**

**Statement of comprehensive income for the period from 1 January to 31 December 2011**

**11. Other operating income and expenses**

The profit on other operating activities for the audited period amounted to PLN 4,324,087 thousand and increased by PLN 5,343,285 thousand when compared with previous year's loss, mainly due to profit from disposal of investment in subsidiary and associate in the amount of PLN 2,662,245 thousand, recognition of result on settlement and valuation of derivatives in the amount of PLN 320,919 thousand (in the previous year in the amount of PLN (1,172,284) thousand) and obtaining foreign exchange gains amounted to PLN 895,164 thousand (in the previous year foreign exchange losses in the amount of PLN 30,445 thousand).

**12. Income tax**

The amount of deferred and current income tax for the audited period equaled to PLN 2,319,077 thousand and increased by PLN 1,282,099 thousand comparing to 2010 due to significantly higher taxable profit obtained by the Company in 2011.

**V. Statements of the independent registered auditor**

- a. The Management Board of the Company provided all the information, explanations, and representations required by us in the course of the audit and provided us with a representation letter confirming the completeness of the information included in the accounting records and the disclosure of all contingent liabilities and subsequent events which occurred up to the date on which that letter was signed.
- b. The scope of the audit was not limited.
- c. The Company has up-to-date documentation of its accounting policies, approved by the Management Board. The Company's accounting policies were tailored to its needs and ensured the recognition of all events with a material effect on the assessment of its financial position and results, taking into consideration the prudence principle. There were no changes to the accounting policies compared with the previous year.
- d. The closing balances as at the end of the previous year were correctly brought forward as the opening balances of the current financial year in all material respects.
- e. The counts of assets and liabilities were carried out and reconciled in accordance with the Accounting Act, and the results were included in the accounting records for the audited year.
- f. The financial statements of the Company for the period from 1 January to 31 December 2010 were approved by Resolution No. 5/2011 passed by the General Shareholders' Meeting on 15 June 2011, filed with the National Court Register in Wrocław on 20 June 2011 and published in Monitor Polski B No. 2421 on 14 December 2011.
- g. The financial statements for the previous financial year were audited by PricewaterhouseCoopers Sp. z o.o. The registered auditor issued an unqualified opinion.
- h. We have assessed the operation of the accounting system. Our assessment covered in particular:
  - the accuracy of the documentation relating to business transactions;
  - the fairness, accuracy and verifiability of the books of account, including computerized books of account;
  - the methods used for controlling access to data and the computerized data processing system;
  - the safeguarding of the accounting documentation, books of account, and financial statements.

This assessment, together with our verification of individual items of the financial statements, provides the basis for expressing a general and comprehensive opinion on these financial statements. The audit was not intended to provide a comprehensive opinion on the operations of the said system.
- i. The notes to the financial statements present all significant information required by IFRS as adopted by the European Union.
- j. The information in the Directors' Report for the year ended 31 December 2011 has been prepared in accordance with the provisions of the Decree of the Minister of Finance dated 19 February 2009 concerning the publication of current and periodic information by issuers of securities and the conditions of acceptance as equal information required by the law of other state, which is not a member state (Journal of Laws of 2009, No. 33, item 259, as amended) and consistent with that presented in the financial statements.

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**KGHM Polska Miedź S.A.**  
**Report on the financial statements**  
**as at and for the year ended 31 December 2011**

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**VI. Final information and comments**

This report has been prepared in connection with our audit of the financial statements of KGHM Polska Miedź Spółka Akcyjna, 48 Marii Skłodowskiej-Curie Street, Lubin. The financial statements were signed by the Company's Management Board and the person entrusted with maintaining the books of account on 27 March 2012.

This report should be read in conjunction with the Independent Registered Auditor's unqualified Opinion to the General Shareholders' Meeting and the Supervisory Board of KGHM Polska Miedź Spółka Akcyjna dated 27 March 2012, concerning the said financial statements. The opinion on the financial statements expresses a general conclusion drawn from the audit and involves assessing the materiality of individual audit findings rather than being a sum of all the evaluations of individual financial statement components. This assessment takes account of the impact of the facts noted on the truth and fairness of the financial statements as a whole.

Conducting the audit on behalf of PricewaterhouseCoopers Sp. z o.o., Registered Audit Company No. 144:

Marcin Sawicki

Key Registered Auditor  
No. 11393

Wrocław, 27 March 2012

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**KGHM POLSKA MIEDŹ S.A.**

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**DECLARATION BY THE MANAGEMENT  
BOARD ON THE ACCURACY OF THE  
PREPARED FINANCIAL STATEMENTS**

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Lubin, March 2012

## **DECLARATION BY THE MANAGEMENT BOARD ON THE ACCURACY OF THE PREPARED FINANCIAL STATEMENTS**

According to our best judgement the annual financial statements and the comparative data have been prepared in accordance with accounting principles currently in force, and give a true, fair and clear view of the financial position of KGHM Polska Miedź S.A. and the profit for the period of the Company. The annual report on the Company's activities presents a true picture of the development and achievements, as well as the condition, of KGHM Polska Miedź S.A., including a description of the basic exposures and risks.

<b>SIGNATURES OF ALL MEMBERS OF THE MANAGEMENT BOARD</b>			
<b>Date</b>	<b>First, Last name</b>	<b>Position/Function</b>	<b>Signature</b>
27 March 2012	Herbert Wirth	President of the Management Board	
27 March 2012	Maciej Tybura	I Vice President of the Management Board	
27 March 2012	Wojciech Kędzia	Vice President of the Management Board	

<b>SIGNATURE OF PERSON RESPONSIBLE FOR ACCOUNTING</b>			
<b>Date</b>	<b>First, Last name</b>	<b>Position/Function</b>	<b>Signature</b>
27 March 2012	Ludmiła Mordylak	Chief Accountant of KGHM Executive Director of Accounting Services Center	

**KGHM POLSKA MIEDŹ S.A.**

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**DECLARATION BY THE MANAGEMENT  
BOARD REGARDING THE ENTITY  
ENTITLED TO AUDIT FINANCIAL  
STATEMENTS**

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Lubin, March 2012

**DECLARATION BY THE MANAGEMENT BOARD REGARDING THE ENTITY ENTITLED TO AUDIT FINANCIAL STATEMENTS**

The entity entitled to audit financial statements, and which has audited the annual financial statements, was selected in compliance with legal provisions. This entity, as well as the certified auditors who have carried out this audit, have met the conditions for issuing an impartial and independent audit opinion, in compliance with appropriate legal provisions and professional standards.

<b>SIGNATURES OF ALL MEMBERS OF THE MANAGEMENT BOARD</b>			
<b>Date</b>	<b>First, Last name</b>	<b>Position/Function</b>	<b>Signature</b>
27 March 2012	Herbert Wirth	President of the Management Board	
27 March 2012	Maciej Tybura	I Vice President of the Management Board	
27 March 2012	Wojciech Kędzia	Vice President of the Management Board	

<b>SIGNATURE OF PERSON RESPONSIBLE FOR ACCOUNTING</b>			
<b>Date</b>	<b>First, Last name</b>	<b>Position/Function</b>	<b>Signature</b>
27 March 2012	Ludmiła Mordylak	Chief Accountant of KGHM Executive Director of Accounting Services Center	



**KGHM POLSKA MIEDŹ S.A.**

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**PRESIDENT'S LETTER**

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**Lubin, March 2012**

## Dear Shareholders!

The year 2011 will undoubtedly go down in history as a uniquely vital chapter in the chronicle of KGHM Polska Miedź S.A. This was due to numerous momentous events. The most important of these was start of the successfully-completed friendly purchase of the Canadian mining company Quadra FNX Mining Ltd, the successful divestiture from the telecommunications sector and the commencement of the smelting investment program. There were also numerous events and distinctions in the area of corporate social responsibility and events related to the celebration of KGHM's Golden Jubilee, i.e. its 50<sup>th</sup> anniversary. The slogan for the jubilee – *Polish Copper, more valuable than gold* – was perfectly confirmed by the record results for 2011.

KGHM achieved a profit for the period of PLN 11.3 billion, meaning an increase versus the prior year by PLN 6.8 billion and the greatest result in the Company's history. The result was substantially impacted by the conclusion in the fourth quarter of 2011 of the sale of the telecom assets. The pre-tax profit on the sale of Polkomtel S.A. and Dialog S.A. amounted to PLN 2.7 billion. For the full year 2011, KGHM also recorded a positive result on hedging transactions, which amounted to PLN 562.5 million.

Electrolytic copper production versus 2010 was higher by 24 thousand tonnes, (an increase of 4.4%) and reached the highest level in the Company's history, i.e. 571 thousand tonnes. The increase in production was due to the higher processing of own concentrate and to the participation of purchased copper-bearing materials in the form of scrap, copper blister and imported concentrate. Last year, KGHM also produced 1 260 tonnes of silver, i.e. by 99 tonnes more (an increase of 8.5%) than in 2010.

At the beginning of December 2011, we submitted a binding offer for the purchase of all of the shares of the Canadian mining company Quadra FNX. The shareholders of this company, by more than the required number of votes cast, in February 2012, voted in favour of acceptance of our offer, which enabled finalisation of the transaction. The per-share price paid was CAD 15, while the total transaction value, which KGHM financed from its own funds, amounted to CAD 2.9 billion, i.e. PLN 9.1 billion. Based on the recommendations of independent analysts as to the valuation of the shares of Quadra FNX during the period prior to the announcement of the transaction, i.e. in December of last year, it appears that the price paid by KGHM for the Canadian company's shares was 20 percent lower than market consensus. Following the transaction the name of the Canadian company was changed to KGHM International. Already in 2012 KGHM's production will be increased by almost 100 thousand tonnes of copper.

The KGHM Group now owns a diversified portfolio of assets in countries of low—investment risk as well as a portfolio of projects ensuring growth of the production base. This includes 9 mines in Poland, Canada, the USA and Chile, and 5 projects at the investment and pre-investment stage: Sierra Gorda in Chile, Głogów Głęboki Przemysłowy in Poland, Afton-Ajax and Victoria in Canada and Malmbjerg in Greenland. Also included are exploration projects in Weisswasser in Germany, Wartowice, Szklary and Gaworzyce-Radwanice in Poland and Kirkwood, Falconbridge, Footwall and Foy in Canada.

The funds for the transaction arose among others from the transaction concluded in November for the sale of the assets held by KGHM in Polkomtel SA and the finalisation in December 2011 of the sale of Dialog SA. KGHM is consistently realising its strategy of concentrating on its core business, assuming diversification in terms of geography and producing assets. That aspect of the strategy assuming the engagement by KGHM in the energy sector remains in force, including recently in the field of shale gas.

One of the most important programs undertaken last year is the program of investment at the Głogów smelter. The modernisation of pyrometallurgy, replacement of the sulphuric acid plant, and construction of a fourth Dörschel furnace were the most important projects. These investments involve not only the process of production, but also have an impact

on environmental protection, safety and working conditions. 10 large projects valued at over PLN 2 billion are being realised at the Głogów smelter.

We are continuing exploration programs in the region of the Old Copper Belt and in the Saxon region of Weisswasser in Germany. The materials obtained from the preliminary drillings are encouraging for further testing.

The process was begun of renewing licenses for the extraction of copper ore from the deposits located in the mining regions of the Copper Belt. Ministerial agreement for KGHM Polska Miedź S.A. will mean the possibility of continuing the Company's activities for another 50 years.

The year 2011 brought KGHM a variety of distinctions documenting its significant role in the Polish economy, and underscoring the Company's corporate social responsibility.

KGHM's receipt of the special "Index of Success" award for most-effective company in Central-Eastern Europe was due among others to the high evaluation of the activities of the Management Board aimed at reducing costs and improving efficiency. In addition, the award committee for the Index of Success appreciated the actions undertaken by KGHM in areas such as environmental protection, the sponsoring of cultural activities and sport, charitable activities and the support of local society.

KGHM was awarded first place in the ranking Pearls of the Polish Economy. The Company was honoured in the category producers and service providers. KGHM was also a winner in the category Great Pearls. This ranking comprised the largest companies, those with revenues of at least one billion Polish zloties.

Of particular importance for the Company is the title „One who is changing Polish industry”. This award was granted for effective management of a major business structure and for clearly-described goals, their consistent realisation, and also for matching them to the long-term growth prospects of the Company. The award committee recognised that KGHM took advantage of the propitious moment in the copper cycle to expand internationally and to realise its plans to create a global copper company through the plan to purchase Quadra FNX in Canada. The award committee also recognised that these plans offered KGHM a new opportunity for growth and the chance to effectively compete with the global leaders in the resources sector.

KGHM again found itself amongst the finalists of the competition Leaders of Philanthropy organised by the Donors Forum, winning second place. KGHM also received a Special Award for „Consistent Engagement in the Competition and Development of Corporate Philanthropy in Poland”. Confirmation of the achievements of KGHM in the field of corporate social responsibility is its permanent place amongst the companies of the Respect Index on the Warsaw Stock Exchange.

Dear Shareholders, KGHM Polska Miedź S.A. has truly become a global company. The Company has gained a historic opportunity to make a quantum leap in its development and in its long-term value. I ensure you that we will take full advantage of this opportunity.

Herbert Wirth

President of the Management Board

Lubin, 27 March 2012

**KGHM POLSKA MIEDŹ S.A.**

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**FINANCIAL STATEMENTS  
FOR 2011**

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**Lubin, March 2012**

KGHM Polska Miedź S.A.  
Annual financial statements prepared in accordance with IFRS  
as adopted by the European Union  
for the period from 1 January 2011 to 31 December 2011  
(amounts in tables in thousand PLN, unless otherwise stated)

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## Statement of financial position

		At	
	Note	31 December 2011	31 December 2010
<b>Assets</b>			
<b>Non-current assets</b>			
Property, plant and equipment	5	7 277 903	6 551 111
Intangible assets	6	150 777	86 718
Shares and investment certificates in subsidiaries	7	2 012 209	2 643 046
Investments in associates	7	-	1 159 947
Deferred tax assets	20	168 462	359 833
Available-for-sale financial assets	8	992 068	749 824
Held-to-maturity investments	9	111 665	84 115
Derivatives	10	899 400	403 839
Trade and other receivables	11	84 221	86 608
		<b>11 696 705</b>	<b>12 125 041</b>
<b>Current assets</b>			
Inventories	12	2 355 741	2 011 393
Trade and other receivables	11	1 502 944	2 393 986
Available-for-sale financial assets	8	-	405 193
Held-to-maturity investments	9	2 147	4 129
Derivatives	10	859 653	294 021
Cash and cash equivalents	13	12 835 999	2 595 529
Non-current assets held for sale	14	-	4
		<b>17 556 484</b>	<b>7 704 255</b>
<b>Total assets</b>		<b>29 253 189</b>	<b>19 829 296</b>
<b>Equity and liabilities</b>			
<b>Equity</b>			
Share capital	15	2 000 000	2 000 000
Accumulated other comprehensive income	16	535 673	211 159
Retained earnings	17	20 599 838	12 245 318
<b>Total equity</b>		<b>23 135 511</b>	<b>14 456 477</b>
<b>Liabilities</b>			
<b>Non-current liabilities</b>			
Trade and other payables	18	11 579	14 249
Borrowings and finance lease liabilities	19	35	8 490
Derivatives	10	538 320	711 580
Employee benefits liabilities	21	1 216 355	1 128 246
Provisions for other liabilities and charges	22	483 657	517 749
		<b>2 249 946</b>	<b>2 380 314</b>
<b>Current liabilities</b>			
Trade and other payables	18	1 827 536	1 727 939
Borrowings and finance lease liabilities	19	58	2 965
Current corporate tax liabilities		1 587 847	668 924
Derivatives	10	330 347	481 852
Employee benefits liabilities	21	107 471	93 041
Provisions for other liabilities and charges	22	14 473	17 784
		<b>3 867 732</b>	<b>2 992 505</b>
<b>Total liabilities</b>		<b>6 117 678</b>	<b>5 372 819</b>
<b>Total equity and liabilities</b>		<b>29 253 189</b>	<b>19 829 296</b>

The accounting policies and other explanatory information presented on pages 7 to 103 represent an integral part of these financial statements

## Statement of comprehensive income

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Sales	23	20 097 392	15 945 032
Cost of sales	24	(9 877 794)	(8 617 125)
<b>Gross profit</b>		<b>10 219 598</b>	<b>7 327 907</b>
Selling costs	24	(111 043)	(103 171)
Administrative expenses	24	(745 002)	(567 390)
Other operating income	26	5 092 919	711 202
Other operating costs	27	(768 832)	(1 730 400)
<b>Operating profit</b>		<b>13 687 640</b>	<b>5 638 148</b>
Finance costs	28	(34 043)	(32 581)
<b>Profit before income tax</b>		<b>13 653 597</b>	<b>5 605 567</b>
Income tax expense	31	(2 319 077)	(1 036 978)
<b><u>Profit for the period</u></b>		<b><u>11 334 520</u></b>	<b><u>4 568 589</u></b>
<b>OTHER COMPREHENSIVE INCOME DUE TO:</b>			
Available-for-sale financial assets		(197 525)	148 019
Cash flow hedging instruments		598 160	(44 401)
Income tax related to items presented in other comprehensive income		(76 121)	(19 687)
<b><u>Other comprehensive net income for the financial period</u></b>		<b><u>324 514</u></b>	<b><u>83 931</u></b>
<b>TOTAL COMPREHENSIVE INCOME</b>		<b><u>11 659 034</u></b>	<b><u>4 652 520</u></b>
<b>Earnings per share for the annual period</b>			
(in PLN per share)	32		
- basic		56.67	22.84
- diluted		56.67	22.84

The accounting policies and other explanatory information presented on pages 7 to 103 represent an integral part of these financial statements

## Statement of changes in equity

	Note	Share capital	Accumulated other comprehensive income due to:		Retained earnings	Total equity
			Available-for-sale financial assets	Cash flow hedging instruments		
<b>At 1 January 2011</b>		<b>2 000 000</b>	<b>121 385</b>	<b>89 774</b>	<b>12 245 318</b>	<b>14 456 477</b>
Dividends for 2010 resolved and paid	33	-	-	-	(2 980 000)	(2 980 000)
<b>Total comprehensive income</b>		<b>-</b>	<b>(159 995)</b>	<b>484 509</b>	<b>11 334 520</b>	<b>11 659 034</b>
Profit for the period	17	-	-	-	11 334 520	11 334 520
Other comprehensive income	16	-	(159 995)	484 509	-	324 514
<b>At 31 December 2011</b>		<b>2 000 000</b>	<b>(38 610)</b>	<b>574 283</b>	<b>20 599 838</b>	<b>23 135 511</b>

<b>At 1 January 2010</b>		<b>2 000 000</b>	<b>1 489</b>	<b>125 739</b>	<b>8 276 729</b>	<b>10 403 957</b>
Dividends for 2009 resolved and paid		-	-	-	(600 000)	(600 000)
<b>Total comprehensive income</b>		<b>-</b>	<b>119 896</b>	<b>(35 965)</b>	<b>4 568 589</b>	<b>4 652 520</b>
Profit for the period	17	-	-	-	4 568 589	4 568 589
Other comprehensive income	16	-	119 896	(35 965)	-	83 931
<b>At 31 December 2010</b>		<b>2 000 000</b>	<b>121 385</b>	<b>89 774</b>	<b>12 245 318</b>	<b>14 456 477</b>

The accounting policies and other explanatory information presented on pages 7 to 103 represent an integral part of these financial statements



## Statement of cash flows

		For the period	
	Note	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Cash flow from operating activities</b>			
Profit for the period	17	11 334 520	4 568 589
Adjustments to profit for the period	34	(1 281 495)	1 436 897
Income tax paid		(1 284 903)	(658 695)
<b>Net cash generated from operating activities</b>		<b>8 768 122</b>	<b>5 346 791</b>
<b>Cash flow from investing activities</b>			
Purchase of shares and investment certificates in subsidiaries		(201 440)	(731 224)
Proceeds from sale and liquidation of shares in subsidiaries		981 874	1 534
Proceeds from sale of shares in an associate		3 672 147	-
Purchase of available-for-sale financial assets		(1 565 831)	(1 296 141)
Proceeds from sale of available-for-sale financial assets		1 548 193	310 994
Purchase of property, plant and equipment and intangible assets		(1 406 454)	(1 156 709)
Advances granted for purchase of property, plant and equipment and intangible assets		(59 374)	(65 329)
Proceeds from sale of property, plant and equipment and intangible assets	34	6 280	4 717
Purchase of held-to-maturity investments financed from the resources of Mine Closure Fund		(25 568)	(20 567)
Establishment of deposits		(450 000)	(350 000)
Termination of deposits		800 000	-
Loans granted		-	(40 000)
Repayments of loans granted		5 030	71 162
Interest received		11 543	4 932
Dividends received		277 330	146 658
Other investment expenses		(3 988)	(5 273)
<b>Net cash generated from/(used in) investing activities</b>		<b>3 589 742</b>	<b>(3 125 246)</b>
<b>Cash flow from financing activities</b>			
Repayments of loans		-	(3 000)
Payments of finance leases liabilities		(13 009)	(3 118)
Interest paid		(11)	(76)
Dividends paid	17	(2 980 000)	(600 000)
<b>Net cash used in financing activities</b>		<b>(2 993 020)</b>	<b>(606 194)</b>
<b>Total net cash flow</b>			
Exchange gains on cash and cash equivalents		875 626	4 980
<b>Movements in cash and cash equivalents</b>		<b>10 240 470</b>	<b>1 620 331</b>
<b>Cash and cash equivalents at beginning of the period</b>	13	<b>2 595 529</b>	<b>975 198</b>
<b>Cash and cash equivalents at end of the period</b>	13	<b>12 835 999</b>	<b>2 595 529</b>
including restricted cash and cash equivalents		3 036	1 751

The accounting policies and other explanatory information presented on pages 7 to 103 represent an integral part of these financial statements

## **Accounting policies and other explanatory information**

### **1. General information**

#### **Company name, registered office, business activities**

KGHM Polska Miedź S.A. (the "Company") with its registered office in Lubin at 48 M. Skłodowskiej-Curie Street is a stock company registered at the Wrocław Fabryczna Regional Court, Section IX (Economic) in the National Court Register, entry no. KRS 23302, operating on the territory of the Republic of Poland. The Company was assigned a tax identification number (NIP) 692-000-00-13 and a statistical REGON number 390021764. KGHM Polska Miedź S.A. has a multi-divisional organisational structure, which comprises its Head Office and 10 divisions: 3 mines (Lubin Mine, Polkowice-Sieroszowice Mine, Rudna Mine), 3 smelters (Głogów Smelter, Legnica Smelter, the Cedynia Wire Rod Plant), the Ore Enrichment Plant (OEP), the Tailings Plant, the Mine-Smelter Emergency Rescue Unit and the Data Center. The shares of KGHM Polska Miedź S.A. are listed on the Warsaw Stock Exchange. According to the classification of the Warsaw Stock Exchange, KGHM Polska Miedź S.A. is classified under the "basic materials" sector.

The principal activities of the Company comprise:

- mining of copper and non-ferrous metals ore,
- excavation of gravel and sand,
- production of copper, precious and non-ferrous metals,
- production of salt,
- casting of light and non-ferrous metals,
- forging, pressing, stamping and roll forming of metal - powder metallurgy,
- waste management,
- wholesale based on direct or contractual payments,
- warehousing and storage of goods,
- holding management activities,
- geological and exploratory activities,
- general construction activities with respect to mining and production facilities,
- generation and distribution of electricity, steam and hot water, production of gas and distribution of gaseous fuels through a supply network,
- scheduled and non-scheduled air transport, and
- telecommunication and IT activities.

Activities involving the exploitation of copper ore, salt deposits and common minerals are carried out based on licenses held by KGHM Polska Miedź S.A., which were issued by the Minister of Environmental Protection, Natural Resources and Forestry in the years 1993-2004, most of which expire on 31 December 2013. KGHM Polska Miedź S.A. is at the stage of obtaining licenses for subsequent years. In the opinion of the Management Board, the licensing process, which occurs periodically, is of an administrative nature, while the probability of not obtaining a license is, in the opinion of the Management Board, minimal.

#### **Period of operation**

KGHM Polska Miedź S.A. has been conducting its business since 12 September 1991. The Company has an unlimited period of operation.

The legal antecedent of KGHM Polska Miedź S.A. was the State-owned enterprise Kombinat Górniczo-Hutniczy Miedzi in Lubin transformed into a State-owned joint stock company in accordance with principles set forth in the law dated 13 July 1990 on the privatisation of State-owned enterprises.

#### **Management Board**

From 1 January to 31 December 2011, the Management Board consisted of (including segregation of duties):

- Herbert Wirth      President of the Management Board,
- Maciej Tybura      I Vice President of the Management Board (Finance),
- Wojciech Kędzia      Vice President of the Management Board (Production).

At the date of authorisation of these financial statements for issue, the composition of the Management Board of KGHM Polska Miedź S.A. had not changed.

## **1. General information (continued)**

### **Authorisation of the annual financial statements (financial statements)**

These financial statements were authorised for issue and signed by the Management Board of the Company on 27 March 2012.

### **Going concern**

The financial statements were prepared under the assumption that the Company will continue as a going concern during a period of at least 12 months from the end of the reporting period in an unaltered form and business scope, and there are no reasons to suspect any intentional or forced discontinuation or significant limitation of its current activities. At the date of signing of the annual financial statements the Management Board of the Company is not aware of any facts or circumstances that may cast doubt about the going concern in the foreseeable future.

In order to fully understand the financial position and the results of the activities of KGHM Polska Miedź S.A. as the parent entity of the Group, these financial statements should be read jointly with the annual consolidated financial statements for the period ended 31 December 2011. These financial statements will be available on the website of the Company [www.kghm.pl](http://www.kghm.pl) on dates consistent with the current report concerning dates of publication of the annual report of the Company and the consolidated annual report of the Group for 2011.

### **Seasonal or cyclical activities**

The Company is not affected by seasonal or cyclical activities.

## **2. Main accounting policies**

### **2.1. Basis of preparing financial statements**

These financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union, using the same principles for the current and comparable periods.

These financial statements have been prepared on the historical cost basis (adjusted for the effects of hyperinflation in respect of property, plant and equipment and equity), except for available-for-sale financial assets and derivatives measured at fair value.

The carrying amount of recognised hedged assets and liabilities is adjusted for the changes in fair value attributable to the hedged risk.

### **Since 1 January 2011 the following standards and interpretations applied by the Company have been in force**

- Amendment to IAS 32 Financial instruments: *Presentation, Classifications of rights issues*
- Amended IFRS 1 First-time Adoption of IFRS, *Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters*,
- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments,
- Amended IAS 24 Related Party Disclosures and changes to IFRS 8 *Operating Segments*,
- Amendments to IFRIC 14 Prepayments of a Minimum Funding Requirement ,
- Amendments to International Financial Reporting Standards 2010.

All of the above changes to the standards and interpretations have been adopted by the European Union up to the date of publication of these financial statements.

The Company, based on the updated IAS 24, made use of the exemptions provided for in paragraph 25, and presents information on transactions between KGHM Polska Miedź S.A. and the government (the Republic of Poland) and with entities controlled or jointly controlled by the government, or over which the government has significant influence, pursuant to the requirements set forth in paragraph of 27 IAS 24.

Besides, the Company estimates that application of the above-mentioned standards did not affect significantly its financial statements.

Up to the date of publication of these financial statements, further standards and interpretations have been published by the International Accounting Standards Board which as at this date have not come into force, while some of them have been adopted for use by the European Union.

## **2. Main accounting policies (continued)**

### **2.1 Basis of preparing financial statements (continued)**

#### **Standards and interpretations which are not in force but have been adopted for use by the European Union:**

##### **Amendments to IFRS 7 Disclosures - Transfers of Financial Assets**

On 7 October 2010, the International Accounting Standards Board issued *Disclosures - Transfers of Financial Assets - Amendments to IFRS 7 Financial Instruments: Disclosures*. The amendments issued enhance existing disclosure requirements. The purpose of the amendments is to increase the transparency of information on risks involving transactions in which financial assets were transferred.

Not every transferral of financial assets by an entity to a third party results in its simultaneous, total or partial derecognition from the financial statements. This occurs when an entity transferring assets does not simultaneously transfer contractual rights to receive cash flows associated with these assets, retaining substantially all of the risks and rewards of their ownership, or continues to be involved in derecognised financial assets at the reporting date. The amendment to IFRS 7 expands the scope of required disclosures by information regarding transferred financial assets which were not entirely derecognised from the financial statements. The additional disclosures encompass the nature and carrying amount of the assets transferred and the risks and rewards associated with them.

For assets transferred, in which an entity continues to be involved, the amended IFRS 7 requires the disclosure of information enabling the evaluation of the nature of the involvement and of the risks associated with the continuing involvement of the entity, by each class of continuing involvement, including in particular the carrying amount and fair value of financial assets and liabilities representing the continued involvement of the entity in the derecognised financial assets.

Until now, the only type of financial assets transferred by the Company whose transferral did not qualify for derecognition from the financial statements involved the disposal of Company debtors with respect to recourse factoring. Should there occur such transactions or others which will involve the aforesaid amendments to IFRS 7, the Company will provide disclosures in the financial statements pursuant to the new requirements.

Amendments are effective for annual periods beginning on or after 1 July 2011.

#### **Standards and interpretations which are not in force and have not been adopted by the European Union up to the date of publication of these financial statements**

##### **IFRS for Small and Medium-sized Entities**

On 9 July 2009, the International Accounting Standards Board issued a standard for Small and Medium-sized Entities (SMEs). This Standard deals with principles and problems of significance for SMEs, simplifying requirements and reducing the scope of disclosures required in the full version of the Standards. Its requirements have been adapted to the needs and capabilities of SMEs.

This Standard does not refer to financial statements of the Company.

##### **IFRS 9 Financial instruments**

On 12 November 2009 the International Accounting Standards Board published IFRS 9 *Financial instruments*. This standard is the result of the initial stage of work by the Board aimed at withdrawal of IAS 39 *Financial Instruments: Recognition and Measurement* and replacement by a new one, IFRS 9. This standard essentially simplifies the principles for classifying financial assets, introducing only two categories: assets measured at fair value, and assets measured at amortised cost. This classification, at the initial recognition, should result from the business model adopted by the entity for managing the assets and from the contractual cash flows appropriate for the given asset. This standard also provides guidance with respect to the measurement of financial assets, their reclassification and the recognition of profits and losses arising from these assets. This standard becomes effective for annual periods beginning on or after 1 January 2015 and will affect the financial statements of the Company, in particular with respect to presentation. Potential changes in value which could impact the financial statements of the Company could arise due to changes in the measurement of equity instruments, which due to the lack of an active market are measured at cost less any impairment. It is however expected that the changes will not have a significant impact on the financial statements of the Company.

On 28 October 2010, the International Accounting Standards Board reissued IFRS 9 *Financial Instruments*. This reissue is the result of the conclusion of a further phase of the Board's work aimed at replacing IAS 39 *Financial Instruments: Recognition and Measurement*. To IFRS 9 the Board added requirements regarding

## **2. Main accounting policies (continued)**

### **2.1 Basis of preparing financial statements (continued)**

the classification and measurement of financial liabilities, the majority of which were transferred to the new standard directly from IAS 39.

Under IFRS 9, liabilities representing derivatives which are related to and settled through the delivery of an unquoted equity instrument are measured at fair value, as in the case of investments in unquoted equity instruments and derivative financial assets related to these investments.

In addition, the standard introduces the requirement to recognise changes in the fair value of financial liabilities measured at fair value through profit or loss resulting from changes in credit risk related to these liabilities, in other comprehensive income. The remaining amount of change in the fair value of liabilities is presented in profit or loss, unless recognition of the affects of these changes in the credit risk of these liabilities would create or enlarge an accounting mismatch; in such a case the entity would recognise the full amount of the change in the fair value in profit or loss.

This standard will be effective for annual periods beginning on or after 1 January 2015, and will affect the Company's financial statements, in particular with regard to presentation, although it is estimated that the impact will be immaterial.

#### **Amendments to IFRS 1 First-time Adoption of IFRS**

On 20 December 2010, the International Accounting Standards Board issued an amendment called *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters of IFRS, as an amendment to IFRS 1 First-time Adoption of IFRS*.

Changes to this standard are effective for annual periods beginning on or after 1 July 2011 and will not have an effect on the financial statements of the Company.

#### **Amendments to IAS 12 Income Taxes**

On 20 December 2010, the International Accounting Standards Board issued an amendment to IAS 12 called *Deferred Tax: Recovery of Underlying Assets*. The purpose of this update is to provide practical guidance in the estimation of the amount of deferred income tax in a situation where investment property is measured through the use of the fair value model from IAS 40 *Investment Property*. In accordance with IAS 12, the measurement of deferred income tax assets and liabilities, i.e. the determination of an income tax rate and the taxable base, depends on the manner in which an entity intends to recover (realise) the value of the assets. In certain tax jurisdictions a different income tax rate is applied to income from the disposal of property than is applied to income received from the use of such property. Sometimes therefore, entities cannot be certain as to the manner in which the value of a given asset will be eventually recovered (realised) in the future. In such a situation the aforementioned amendment to IAS 12 recommends that the entity should assume that it will recover (realise) the value of the asset through its sale. This same principle should be applied by entities owning non-depreciable and revalued assets covered by IAS 16.

Changes to this standard are effective for annual periods beginning on or after 1 January 2012 and will not have an effect on the financial statements of the Company, due to the unified tax rate applied in Poland to income obtained by corporations.

#### **IFRS 10 Consolidated Financial Statements**

On 12 May 2011, the International Accounting Standards Board published IFRS 10 *Consolidated Financial Statements*. The new standard supersedes SIC 12 *Consolidation – Special Purpose Entities* and IAS 27 *Consolidated and Separate Financial Statements* with regard to consolidated financial statements.

The purpose of introducing the new standard was primarily to unify definitions of control, which due to inconsistencies between IAS 27 and SIC 12 led to various interpretations by economic entities.

IFRS 10 establishes a revised concept of control as being the deciding factor in whether to include an entity in consolidated financial statements, comprising three elements:

- power over the investee,
- exposure, or rights, to variable returns from its involvement with the investee, and
- the ability to use its power over the investee to affect the amount of the investor's returns.

This standard will be effective for annual periods beginning on or after 1 January 2013, and will have an effect on the financial statements of the Company in terms of deciding whether or not to exercise control.

## **2. Main accounting policies (continued)**

### **2.1 Basis of preparing financial statements (continued)**

#### **IFRS 11 Joint Arrangements**

On 12 May 2011, the International Accounting Standards Board published IFRS 11 *Joint Arrangements*. The new standard supersedes IAS 31 *Interests In Joint Ventures* and SIC 13 *Jointly Controlled Entities – Non-Monetary Contributions by Venturers*.

IFRS 11 describes two types of joint arrangements: joint operations and joint ventures. The classification of a joint arrangement as a joint operation or a joint venture depends upon the rights and obligations of the parties to the arrangement. The standard eliminates incoherence by eliminating proportional consolidation as a method for recognising a joint venture, allowing solely for the valuation of assets in a jointly-controlled entity by the joint operator using the equity method.

This standard will be effective for annual periods beginning on or after 1 January 2013, and will not have an effect on the financial statements of the Company.

#### **IFRS 12 Disclosure of Interests in Other Entities**

On 12 May 2011, the International Accounting Standards Board published IFRS 12 *Disclosure of Interests in Other Entities*. This standard will be applicable to entities having interests in subsidiaries, joint ventures, associates or unconsolidated structured entities.

The new standard combines the disclosure requirements regarding interests in other entities which are currently described in IAS 27, IAS 28 and IAS 31, introducing coherence and completeness in disclosures, and also expanding their scope. The purpose of introducing the changes was to ensure that users of financial statements have a better opportunity to evaluate the nature of, and risks associated with, the interests of a given entity in other entities, and to understand the effects of those interests on the investor's financial position, profit or loss and cash flows. The standard sets forth the minimum scope of disclosures which the investor can expand, if it is felt that additional disclosures are required to meet the purposes of the standard. In addition, the investor may decide as to the level of aggregation and disaggregation of disclosed information and may select those areas which the investor wishes to emphasise in its disclosures.

This standard will be effective for annual periods beginning on or after 1 January 2013. IFRS 12 does not address those financial statements for which entities will apply the amended IAS 27 *Separate Financial Statements*, and as a result the standard will not affect the Company's financial statements.

#### **IFRS 13 Fair Value Measurement**

On 12 May 2011, the International Accounting Standards Board published IFRS 13 *Fair Value Measurement*. This standard is the result of the process carried out by the IASB, introducing unified accounting standards in terms of international and American standards.

IFRS 13 introduces a new definition of fair value, unified conceptual assumptions and amended disclosure requirements with respect to fair value measurements, without expanding the scope of fair value measurements. The new requirements are to be applied to those standards (with certain exceptions), which at present require or allow for the measurement of assets and liabilities to fair value, in respect of which the current guidelines regarding fair value measurements and disclosures are incoherent.

IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. the exit price). Consequently, the standard provides guidelines as to the method of measurement to fair value, both at the moment of initial recognition as well as on subsequent reporting period end days.

In the current standards, a broad range of disclosures concerning measurement to fair value are mainly in respect of financial instruments. The application of IFRS 13 will encompass those disclosures as well as other assets and liabilities which are subject to fair value measurement.

This standard will be effective for annual periods beginning on or after 1 January 2013. The Company estimates that although IFRS 13 will affect the presentation of disclosures involving measurement to fair value in the financial statements, this will depend on those assets and liabilities held at the date of application which are measured to fair value.

#### **IAS 27 Separate Financial Statements**

On 12 May 2011, the International Accounting Standards Board published the amended IAS 27 *Separate Financial Statements*, which supersedes the existing IAS 27 *Consolidated and Separate Financial Statements* in that part involving separate financial statements. The change in the standard is a result of the Board's „Consolidation” project, as a result of which the existing content of IAS 27 was divided between IFRS 10

## **2. Main accounting policies (continued)**

### **2.1 Basis of preparing financial statements (continued)**

*Consolidated Financial Statements* and IAS 27, which will only deal with separate financial statements. Likewise, the requirements regarding separate financial statements set forth in IAS 28 and IAS 31 were transferred to the amended IAS 27.

The definitions and terminology of the amended standard were unified with IFRS 10, IFRS 11 and IFRS 12. This standard will be effective for annual periods beginning on or after 1 January 2013. The Company estimates that application of the amended standard will not materially affect its separate financial statements.

#### **IAS 28 Investments in Associates and Joint Ventures**

On 12 May 2011, the International Accounting Standards Board published the amended IAS 28 *Investments in Associates and Joint Ventures*, which superseded the existing IAS 28 *Investments in Associates*. The change in the standard was due to the Board project „Joint Ventures”.

In this project, the IASB decided to include accounting for joint ventures within the scope of the amended IAS 28, as the new standard IFRS 11 *Joint Arrangements* will only allow for the measurement of interests in joint ventures using the equity method. As a result, an entity should apply IFRS 11 solely for the purpose of determining the type of enterprise in which it participates, and upon determining that the interests are in a joint venture, the investment is recognised and is measured using the equity method, in accordance with the amended IAS 28. Although the amended standard introduces no changes in the methodology of measurement using the equity method, it no longer contains requirements concerning disclosures, as these were included in IFRS 12.

The amended standard will be effective for annual periods beginning on or after 1 January 2013, and will not affect the financial statements of the Company.

#### **Presentation of Other Comprehensive Income Amendments to IAS 1 Presentation of Financial Statements**

On 16 June 2011, the International Accounting Standards Board published amendments to IAS 1 *Presentation of Financial Statements* titled *Presentation of Other Comprehensive Income*.

Changes were introduced in the title of one of the basic financial statements, from „Statement of comprehensive income” to „Statement of profit or loss and other comprehensive income”, leaving the possibility to present the statement of profit or loss separately. Entities may apply titles for these statements other than those set forth in IAS 1.

Also introduced were clear rules regarding positions which should be presented through profit or loss and through other comprehensive income.

The amended IAS 1 also introduces the requirement to separately group positions presented in other comprehensive income based on their potential reclassification to profit or loss in accordance with other IFRSs.

The amendments to IAS 1 will be effective for annual periods beginning on or after 1 July 2012, and will not have a material effect on the financial statements of the Company.

#### **Amended IAS 19 Employee Benefits**

On 16 June 2011, the International Accounting Standards Board published an amended IAS 19 *Employee Benefits*. Work on the standard was carried out in conjunction with the American Financial Accounting Standards Board to unify certain regulations concerning employee benefit programs between IFRS and US GAAP.

The amendments to the standard introduce significant changes with respect to accounting for specified employee benefit programs. Among the items eliminated was the so-called 'corridor' approach enabling deferral in the recognition of actuarial gains and losses. This results in the necessity to recognise actuarial gains and losses when they arise. Elimination of this recognition option introduces consistency and clarity to the presented data. The requirement for early recognition (usually in the period in which they initially arise), was also introduced for costs of past employment.

Changes in the standard also involve the means of presentation of changes arising in the assets and liabilities of specified benefit programs. Among others the principle of recognising changes arising as a result of measurement of assets and liabilities of a program in other comprehensive income was introduced.

The amendment significantly expands the scope of disclosures for specified benefit programs, mainly with respect to the nature of these programs and the risk to which an entity is exposed due to participation in a program.

## **2. Main accounting policies (continued)**

### **2.1 Basis of preparing financial statements (continued)**

The amended IAS 19 will be effective for annual periods beginning on or after 1 January 2013. The Company estimates that application of the amended standard will result in a change in the presentation of actuarial gains and losses in other comprehensive income, not as until now in profit or loss and as a one-off recognition in other comprehensive income of unsettled costs of past employment recognised until now through the straight-line method for a period of 13.5 years. The result of this would be to decrease other comprehensive income at 1 January 2013 by the amount of PLN 2 531 thousand, due to costs of past employment which were not amortised to 1 January 2013.

#### **IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine**

On 19 October 2011, the International Accounting Standards Board published Interpretation IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine*. The Interpretation is applied to the recognition of costs of accessing ore through the removal of overburden during the production phase of a surface mining operation. The Interpretation regulates among others the manner of recognition of these costs as an element of assets, their initial measurement and subsequent measurements of these assets. The Interpretation will be effective for annual periods beginning on or after 1 January 2013, and will not be applicable to nor have an impact on the Company's financial statements.

#### **Mandatory Effective Date and Transition Disclosures from IAS 39 to IFRS 9. Amendments to IFRS 9 and IFRS 7**

On 16 December 2011, the International Accounting Standards Board published the document *Mandatory Effective Date and Transition Disclosures* as an amendment to IFRS 9 and IFRS 7. This document amends the effective date of IFRS 9 from on or after 1 January 2013 to on or after 1 January 2015, and allows for early application. The Board also amended IFRS 7, requiring additional disclosures in terms of the transition from IAS 39 to IFRS 9. Deferment of the Mandatory Effective Date to apply IFRS 9 is a result of the Board's deferral of the work on the remaining parts of the project aimed at replacing IAS 39 by IFRS 9 to later periods. The change introduced will cause a deferment in application by the Company of the standard in respect of the initial deadline, due to the high probability that IFRS 9 will be adopted by the European Union only in its complete form.

#### **Offsetting Financial Assets and Financial Liabilities. Amendments to IAS 32 Financial Instruments: Presentation**

On 16 December 2011, the International Accounting Standards Board published the document *Offsetting Financial Assets and Financial Liabilities* as an amendment to IAS 32. The Board supplemented the Application Guidance accompanying the standard with respect to the conditions for offsetting and presenting financial assets and liabilities in a net amount in the statement of financial position. Under paragraph 42 of IAS 32, an entity may offset financial assets and liabilities, if (a) it currently has a legally enforceable right to set off the recognised amounts, and (b) it intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously. Due to practical doubts in interpretation, in terms of the legally enforceable right to set off and in terms of recognising a given settlement as a net settlement (even for gross cash flows) with the participation of settlement institutions, the Board introduced additional explanations, enabling uniform implementation of the requirements of para. 42 of IAS 32 by financial institutions. The amendments will be effective for annual periods beginning on or after 1 January 2014, and will not have an impact on the Company's financial statements.

#### **Disclosures - Offsetting Financial Assets and Financial Liabilities Amendments to IFRS 7 Financial Instruments: Disclosures**

On 22 December 2011, the International Accounting Standards Board published the document *Disclosures - Offsetting Financial Assets and Financial Liabilities* as an amendment to IFRS 7. The amendments introduce additional information disclosure requirements, which enable users of financial statements to evaluate the impact, or potential impact, of offsetting agreements, with the actual or potential impact from realisation of a legally enforceable right to set off financial assets and liabilities recognised by an entity in its statement of financial position. Additional detailed disclosures will deal with all those amounts which an entity may potentially offset in its statement of financial position, regardless of whether or not an entity made use of this right. The amendments will be effective for annual periods beginning on or after 1 January 2013, and will affect the Company's financial statements through the expanded scope of disclosures.

**These financial statements do not apply standards or interpretations prior to their effective date or prior to adoption by the European Union.**



## 2. Main accounting policies (continued)

### 2.2 Accounting policies

#### 2.2.1 Property, plant and equipment

The following are considered to be items of property, plant and equipment:

- assets held by the entity for use in production, supply of goods and services or for administrative purposes,
- assets which are expected to be used during more than one year,
- assets which are expected to generate future economic benefits that will flow to the entity, and
- assets whose value can be measured reliably.

Upon initial recognition, items of property, plant and equipment are measured at cost.

Borrowing costs incurred for the purchase or construction of a qualifying item of property, plant and equipment are recognised in the cost. Principles for the capitalisation of borrowing costs are presented in point 2.2.22.

Foreign exchange differences arising from foreign currency liabilities, related to the purchase or construction of an item of property, plant and equipment, are recognised in profit or loss in the period in which they are incurred.

Upon initial recognition, in the costs of property, plant and equipment are included the anticipated costs of future assets' dismantling and removal and cost of restoring the sites on which they are located, the obligation for which an entity incurs either when the item is installed or as a consequence of having used the item for purposes other than to produce inventories. In particular, in the initial cost of items of property, plant and equipment are included discounted decommissioning costs of assets relating to underground mining, as well as of other facilities which, in accordance with binding laws, must be liquidated upon the conclusion of activities.

Mine decommissioning costs recognised in the initial cost of an item of property, plant and equipment are depreciated in the same manner as the item of property, plant and equipment to which they relate, beginning from the moment an asset is brought into use, throughout the period set out in the asset group decommissioning plan within the schedule of mines decommissioning.

The decommissioning costs of other facilities recognised in the initial cost of an item of property, plant and equipment are amortised beginning from the moment an item of property, plant and equipment is brought into use, throughout the period of use and in accordance with the method used for the depreciation of those items of property, plant and equipment to which they have been assigned.

Property, plant and equipment acquired before 31 December 1996 and brought into use after this date, for which expenditures were incurred to the end of 1996, were restated to account for the effects of hyperinflation in accordance with IAS 29, *Financial reporting in hyperinflationary economies*.

As at the end of the reporting period, items of property, plant and equipment are carried at cost less accumulated depreciation and accumulated impairment losses. (Described in detail in note 2.2.9)

Subsequent expenditures on items of property, plant and equipment (for example to increase the usefulness of an item, for spare parts or renovation) are recognised in the carrying amount of a given item only if it is probable that future economic benefits associated with the item will flow to the entity, and the cost of the item can be measured reliably. All other expenditures on repairs and maintenance are recognised in profit or loss in the period in which they are incurred.

Items of property, plant and equipment (excluding land) are depreciated using the straight-line method over their anticipated useful life. The residual value and useful life of an asset and the method of depreciation applied to items of property, plant and equipment are reviewed at least at the end of each financial year.

The useful lives, and therefore the depreciation rates of items of property, plant and equipment used in the production of copper, are adapted to the plans for the closure of operations.

For individual groups of assets, the following useful lives have been adopted:

- buildings and civil engineering objects: 25 - 60 years,
- technical equipment and machines: 4 - 15 years,
- motor vehicles: 3 - 14 years,
- other property, plant and equipment, including tools and instruments: 5 - 10 years.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.1 Property, plant and equipment (continued)**

Depreciation begins when an item of property, plant and equipment is available for use. Depreciation ceases at the earlier of the date that the asset is classified as held for sale (or included as part of a disposal group which is classified as held for sale) in accordance with IFRS 5 *Non-current assets held for sale and discontinued operations* or when it is derecognised upon disposal or retirement.

The basis for the calculation of depreciation is the cost of an item of property, plant and equipment less its estimated residual value.

The individual significant parts of an item of property, plant and equipment (components), whose useful lives are different from the useful life of the given asset as a whole and whose cost is significant in comparison to the cost of the item of property, plant and equipment as a whole, are depreciated separately, applying depreciation rates reflecting their anticipated useful lives.

An asset's carrying amount is written down to its recoverable amount, if the carrying amount of the asset (or a cash-generating unit to which it belongs) is greater than its estimated recoverable amount.

The asset's carrying amount includes costs of necessary regular major overhauls, including costs of overhauls for the purpose of certification.

Specialised spare parts with a significant initial cost and an anticipated useful life of more than 1 year are recognised as an item of property, plant and equipment. Spare parts and servicing-related equipment whose use is restricted to only certain items of property, plant and equipment are recognised in a similar manner. Other spare parts and servicing-related equipment with an insignificant cost are recognised as inventories and accounted for in profit or loss at the moment they are used.

A fixed asset is derecognised when it is sold, decommissioned or if no future economic benefits are expected to be derived from its use or disposal.

#### **2.2.2 Intangible assets**

Intangible assets include:

- development costs,
- software,
- acquired concessions, patents, licenses,
- other intangible assets, and
- intangible assets not yet available for use (under construction).

On initial recognition, intangible assets are measured at cost.

Any borrowing costs incurred for the purchase or construction of a qualifying item of intangible assets are recognised in the cost. Principles for the capitalisation of borrowing costs are presented in point 2.2.22.

If payment for an intangible asset is deferred for a period which is longer than standard for ordinary buyer's credit (in practice a period of over 1 year is assumed), its purchase price should reflect the amount which would be paid in cash. The difference between this amount and the total payment is recognised in profit or loss as interest cost (a discount of liabilities) in financial costs in the period of repayment (settlement) of liabilities. Exchange differences which arise from liabilities in a foreign currency which are related to the acquisition or construction of an item of intangible assets are recognised in profit or loss in the period in which they are incurred.

At the end of the reporting period intangible assets are measured at cost less accumulated amortisation and impairment losses (described in detail in note 2.2.9).

Intangible assets are amortised using the straight-line method over their anticipated useful lives, which for individual groups of intangible assets are as follows:

- Development costs – 5 – 15 years,
- Software – 2 – 5 years,
- Concessions, licenses and patents – 5 years,
- Other intangible assets, including rights to geological information – 50 years.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.2 Intangible assets (continued)**

KGHM Polska Miedź S.A. does not report intangible assets with indefinite useful lives, however it has reported intangible assets not yet available for use (under construction). The Company does not amortise such items of intangible assets, however they are tested for impairment annually. Any potential impairment loss is recognised in profit or loss.

The amortisation method and the amortisation rate of intangible assets are subject to review at least at the end of each financial year.

#### **Development costs**

The Company carries out development projects which are primarily aimed at reducing copper production costs, increasing the production capacity of smelters and mines, improving the technical parameters of manufactured products, and improving copper production technology.

An intangible asset arising from development is recognised if the entity can demonstrate:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale,
- the intention to complete the intangible asset and use or sell it,
- its ability to use or sell the intangible asset,
- the manner in which the intangible asset will generate probable future economic benefits,
- the availability of adequate technical, financial and other resources to complete the development and use or sell the intangible asset, and
- its ability to measure reliably the expenditures attributable to the intangible asset that have been incurred during its development.

The cost of internally-generated development work recognised as an item of intangible assets is the sum of expenditure incurred from the date when the intangible asset arising from development first meets the criteria for recognition.

Capitalised development costs, until the moment when the given development project is successfully completed and the decision has been taken to implement it, are recognised as an intangible asset not yet available for use and are not amortised. Such intangible assets are, however, tested annually for impairment. The amount of the impairment is recognised in profit or loss.

Internally generated intangible assets are amortised using the straight-line method over the period of their anticipated use.

Research expenditure is recognised as an expense as incurred.

#### **2.2.3 Equity investments**

##### **Subsidiaries**

In the financial statements, investments in subsidiaries which are not classified as held for sale in accordance with IFRS 5 are recognised at cost, in accordance with IAS 27, *Consolidated and Separate Financial Statements*, less any impairment losses, in accordance with IAS 36, *Impairment of Assets*, where impairment losses are measured by comparing their carrying amount with the higher of the following amounts:

- fair value, less costs to sell, and
- value in use.

Combinations of business entities under common control are accounted for by applying the pooling of interests method.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.3 Equity investments (continued)**

##### **Associates**

Associated entities are those entities over which the Company has significant influence but not control, and in which it participates in setting both the financial and operational policy of a given entity, which is commonly associated with the ownership of from 20% to 50% of the total number of votes in the entity's governing bodies or the possibility of affecting its operations in another manner.

In the financial statements of the Company, shares in associates which are not classified as held for sale in accordance with IFRS 5 are recognised at cost, in accordance with IAS 27, *Consolidated and Separate Financial Statements*, less any impairment losses, in accordance with IAS 36, *Impairment of Assets*, where impairment is measured by a comparison of the carrying amount with the higher of two amounts:

- fair value, less costs to sell, and
- value in use.

At the end of the reporting period no associates were held by the Company.

#### **2.2.4. Financial Instruments**

##### **2.2.4.1 Classification of financial instruments**

Financial instruments are classified into one of the following categories:

- financial assets measured at fair value through profit or loss,
- loans and receivables,
- held-to-maturity investments,
- available-for-sale financial assets,
- financial liabilities measured at fair value through profit or loss,
- other financial liabilities,
- derivative hedging instruments.

Financial instruments are classified based on their characteristics and the purpose for which they were acquired. Classification is made upon initial recognition of the financial asset or liability. Classification of derivatives depends on their purpose and on whether they qualify for hedge accounting according to the requirements of IAS 39. Derivatives are classified as derivative hedging instruments, instruments initially designated as hedging instruments excluded from hedge accounting and as financial instruments measured at fair value through profit or loss.

The carrying amount of cash flows due to financial instruments with a maturity more than 12 months from the end of the reporting period is classified as a non-current asset or non-current liability. The carrying amount of cash flows due to financial instruments with a maturity period of less than 12 months from the end of the reporting period is classified as a current asset or current liability.

The Company has adopted the following principles for the classification of financial instruments to the above specified categories of financial assets and liabilities:

##### **Financial assets and liabilities measured at fair value through profit or loss**

This category includes financial assets and financial liabilities held for trading and financial assets and liabilities designated at fair value through profit or loss at their initial recognition. A financial asset is classified to this category if it is acquired principally for the purpose of selling in the near term or if it is designated by the entity upon initial recognition as at fair value through profit or loss. A financial asset or financial liability may be designated by the entity when initially recognised at fair value through profit or loss only if:

- a) such classification eliminates or significantly reduces a measurement or recognition inconsistency (also defined as "an accounting mismatch"), that would otherwise arise from measuring these financial instruments or recognising gains or losses using a different basis; or
- b) a group of financial instruments is managed properly and the performance of the group is evaluated on the fair value basis, in accordance with a documented risk management or investment strategy.

Available-for-sale financial assets and liabilities include derivatives, unless they have been designated as hedging instruments.

Assets in this category are classified as current if they are available for sale and if the carrying amount is realised within a period of up to 12 months from the end of the reporting period.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.4 Financial instruments (continued)**

##### **2.2.4.1 Classification of financial instruments (continued)**

###### **Loans and receivables (L&R)**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market.

Loans and receivables are classified as current assets, except for maturities greater than 12 months after the end of the reporting period. Loans and receivables with maturities greater than 12 months after the end of the reporting period are classified as non-current assets.

Loans and receivables in the statement of financial position are included in the item: trade and other receivables.

Cash and cash equivalents are classified as loans and receivables. Cash and cash equivalents are a separate item in the statement of financial position.

###### **Held-to-maturity investments (HtM)**

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Company has the positive intention and ability to hold to maturity, except for assets classified as measured at fair value through profit or loss or available for sale, as well as financial assets meeting the definition of loans and receivables.

###### **Available-for-sale financial assets (AfS)**

Available-for-sale financial assets are non-derivative financial assets that are either designated as "available-for-sale" or not classified to any of the other categories. This category primarily includes financial assets which do not have a fixed maturity date and which do not meet the criteria for being included in other categories.

Available-for-sale financial assets are included in non-current assets unless the Company intends to dispose of the investment within 12 months from the end of the reporting period.

###### **Other financial liabilities**

Financial liabilities included in this category are those that were not classified at their initial recognition as measured at fair value through profit or loss.

###### **Hedging instruments (HI)**

Derivatives designated and qualifying for hedge accounting are classified into a separate category called: Hedging instruments. The Company presents as hedging instruments the entire fair value of instruments designated to this category and qualifying for hedge accounting, even if the Company excludes the time value of a derivative from effectiveness measurement.

###### **Instruments initially designated as hedging instruments excluded from hedge accounting**

Derivatives initially designated as qualifying for hedge accounting, and then excluded from hedge accounting, are presented as Instruments initially designated as hedging instruments excluded from hedge accounting.

Instruments initially designated as hedging instruments excluded from hedge accounting are measured at fair value through profit or loss.

##### **2.2.4.2. Initial measurement and derecognition of financial instruments**

Transactions respecting the purchase and sale of investments, including regular way purchases or sales, are recognised at the trade date, initially at fair value plus transaction costs, with the exception of financial assets and liabilities measured at fair value through profit or loss, which are initially recognised at fair value. Investments are derecognised when the rights to the cash flows from the investments have expired or have been transferred and the Company has transferred substantially all of the risks and rewards of their ownership. Where substantially all of the risks and rewards of ownership have not been transferred, investments are derecognised when the Company loses control over a given asset.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.4 Financial instruments (continued)**

##### **2.2.4.3. Measurement of financial instruments at the end of the reporting period**

###### **Financial assets and financial liabilities measured at fair value through profit or loss, available-for-sale financial assets and hedging instruments**

Financial assets and financial liabilities measured at fair value through profit or loss, available-for-sale financial assets and derivative hedging instruments are subsequently measured at fair value. Available-for-sale financial assets, which do not have a fixed maturity date, and the fair value of which cannot be determined in a reliable manner, are carried at cost.

Gains and losses on financial assets which are classified as financial assets measured at fair value through profit or loss are recognised in profit or loss in the period in which they arise.

Gains and losses on financial assets which are classified as available-for-sale are recognised in other comprehensive income, except for impairment losses and exchange gains or losses on monetary assets and gains or losses on interest calculated using the effective interest rate, which are recognised in profit or loss. When available-for-sale financial assets are derecognised, the total cumulative gains and losses which had been recognised in other comprehensive income are reclassified to profit or loss as an adjustment from reclassification.

The disposal of investments of the same type but with a different cost basis is accounted for using the FIFO method, i.e. the assets disposed of are valued successively at the prices of those assets which were acquired earlier.

###### **Loans and receivables, held-to-maturity investments**

Loans and receivables and held-to-maturity investments are measured at amortised cost using the effective interest rate method.

###### **Other financial liabilities**

After initial recognition, the entity measures all financial liabilities, apart from those classified as at fair value through profit or loss, at amortised cost using the effective interest rate method except for:

- financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition.  
If the transfer of financial assets does not qualify them for derecognition because the entity retained virtually all of the risks and rewards associated with ownership of the transferred asset, then the entity continues to fully recognise the transferred asset and simultaneously recognises a financial liability in the amount of the payment received.  
In subsequent periods, the entity recognises all revenues received from the transferred asset and all expenditures incurred in respect of the financial liability;
- financial guarantee agreements, measured at the higher of:
  - the amount determined in accordance with note 2.2.14 Provisions, or
  - the amount initially recognised less cumulative amortisation recognised according to IAS 18 *Revenue*.

##### **2.2.4.4. Fair value**

Fair value is considered to be the purchase price of a financial instrument or, in case of financial liabilities, the sales price of an instrument, unless there are any indicators that a financial instrument was not purchased at fair value.

At the end of the reporting period, the fair value of financial instruments, for which an active market exists, is established based on the current bid/ask prices. If the market for a financial asset or liability is not active (and in relation to non-quoted securities), the Company establishes fair value using appropriate valuation techniques. Valuation techniques used include comparison with recent arm's length market transactions, if available, reference to the current fair value of another instruments that are substantially the same, discounted cash flow analysis, option pricing models and other valuation techniques/models which are commonly used by market participants, adjusted to the characteristics and parameters of the fair valued financial instrument and the situation of the issuer.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.4 Financial instruments (continued)**

##### **2.2.4.4. Fair value (continued)**

Estimated fair value reflects the amount recoverable or payable to close out an outstanding position at the end of the reporting period. Where possible, transactions are fair valued based on market prices. In the case of purchase or sale of commodity forwards, fair value was estimated based on forwards prices for the maturity dates of specific transactions. In the case of copper, the official London Metal Exchange closing prices and volatility estimates as at the end of the reporting period are obtained from the Reuters news service. For silver and gold, the London Bullion Market Association fixing price at the end of the reporting period is used. In the case of volatility and forward prices, quotations of Banks/Brokers are used. Currency interest rates and currency volatility ratios obtained from Reuters are used. Forwards and swaps on the copper market are priced based on a forward market curve. Silver and currency forward prices are calculated based on fixing and respective interest rates. Levy approximation to the Black-Scholes model is used for Asian options pricing on commodity markets, whereas the standard Garman-Kohlhagen model is used for European options pricing on currency markets.

The fair value of unquoted debt securities is determined as the present value of future cash flows discounted using the prevailing interest rate.

The fair value of participation units of open-end cash investment funds is determined based on the valuations made by those funds. The fair value of share in close-end investment funds classified as available-for-sale financial assets is determined based on the information included in the financial statements of the funds. The fair values of other financial instruments held by the Company are determined based on market prices or on valuation techniques which use as input data only observable market variables from active markets.

##### **2.2.4.5. Impairment of financial assets**

At the end of each reporting period an assessment is made of whether there is objective evidence that a financial asset or a group of financial assets is impaired. The following are considered significant objective indicators (evidence of impairment): significant financial difficulty of the debtor, legal action being taken against the debtor, the disappearance of an active market for a given financial instrument, the occurrence of significant unfavourable changes in the economic, legal or market environment of the issuer of a financial instrument, and the continuing substantial decrease or prolonged decrease of the fair value of a equity instrument below its cost.

If any such evidence exists for available-for-sale financial assets, the cumulative loss that had been recognised directly in other comprehensive income – calculated as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from other comprehensive income and reclassified to profit or loss as an adjustment from reclassification.

Impairment losses on equity instruments recognised in profit or loss shall be reversed through other comprehensive income. The reversal of impairment losses on debt financial instruments is recognised in profit or loss if, in a period subsequent to the period of the recognition of the impairment loss, the fair value of these instruments increased due to events occurring after the recognition of the impairment loss.

If evidence of potential impairment of loans and receivables or of held-to-maturity investments measured at amortised cost exists, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate (i.e. the effective interest rate calculated at the initial recognition for fixed interest rate assets, and the effective interest rate computed at the last revaluation for floating interest rate assets). Any impairment loss is recognised in profit or loss. The carrying amount of such financial assets includes the impairment loss (due to credit losses) recorded in a separate account.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.4 Financial instruments (continued)**

##### **2.2.4.5. Impairment of financial assets (continued)**

Receivables and loans, as well as held-to-maturity investments which are measured at amortised cost, are individually tested for impairment at the end of each reporting period. Receivables, against which no impairment allowance was made, but for which the possibility of impairment exists due to their specific credit risk (related for example to the type of activity or structure of the clients) are tested for impairment as a group (assets' portfolio). Due to the nature of the sales of KGHM Polska Miedź S.A. and a restrictive policy towards credit risk, the Company analyses receivables primarily on an individual basis (regardless of their significance) in terms of the existence and recognition of impairment allowances. An impairment loss is reversed, if in subsequent periods the impairment is reduced, and this reduction may be attributed to events occurring after recognition of the impairment loss. The reversal of an impairment loss is recognised in profit or loss.

##### **2.2.4.6. Embedded derivatives**

###### **Initial recognition of derivatives**

Embedded derivatives are separated from host contracts and accounted for separately as at the date of transaction, if all of the following conditions are met:

- the hybrid (combined) instrument is not measured at fair value, with changes in fair value recognised in profit or loss,
- the characteristics and risk of the embedded derivative are not closely related to the characteristics and risk of the host contract, and
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative.

Re-assessment of contracts for possible separation of embedded derivative is made whenever there is a significant change to the contract that significantly modifies cash flows arising from the contract.

These criteria in particular are deemed as being met especially for contracts involving metals sales or the purchase of copper-bearing materials, in which prices are set after the date of sale or purchase.

In such cases the Company accounts for the embedded derivative separately from the host sale/purchase contract. From the moment of separation, the embedded derivative instrument is measured at fair value at the end of each reporting period. From the date of separation, the embedded derivative is classified as a financial asset or liability measured at fair value through profit or loss. Any change in the balance of the embedded derivative is accounted for as an adjustment respectively of revenues from sales or costs of sales.

##### **2.2.4.7 Hedge accounting**

Hedging, for accounting purposes, involves proportional offsetting of the effects of changes in the fair value or changes in cash flows arising from a hedging instrument and a linked hedged item. Hedges include fair value hedges, cash flow hedges and hedges of net investment in foreign operations. Financial assets which are not derivatives, or financial liabilities which are not derivatives, may be designated as hedging instruments only for the currency risk hedging relationships.

The Company does not recognise either fair value hedges or hedges of net investment in foreign operations. Hedging instruments are designated as cash flow hedges.



## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.4 Financial instruments (continued)**

##### **2.2.4.7 Hedge accounting (continued)**

###### **Derivatives used in cash flow hedges**

The Company hedges cash flows. In a cash flow hedge, a derivative used as a hedging instrument is an instrument which:

- hedges the exposure to volatility of cash flows which is attributable to a particular type of risk associated with an asset or liability recognised in the statement of financial position, or a highly probable forecast transaction, and
- will affect profit or loss.

Gains and losses arising from changes in the fair value of the hedging instrument in a cash flow hedge are recognised in other comprehensive income, to the extent by which the change in fair value represents an effective hedge of the associated hedged item. The portion which is ineffective is recognised in profit or loss as other operating income or costs. Gains or losses arising from the hedging instrument in cash flow hedges are recognised in profit or loss as a reclassification adjustment, in the same period or periods in which the hedged item affects profit or loss.

Hedge effectiveness is the degree to which changes in the cash flows of the hedged item that are attributable to the hedged risk are offset by changes in the cash flows of the hedging instruments.

If the hedged firm commitment or forecast future transaction subsequently results in the recognition of a non-financial asset or non-financial liability in the statement of financial position, then, at the time the item is recognised, all associated gains and losses are included in the initial cost or other carrying amount of the asset or liability.

The designated hedges relate to the future transactions forecasted as assumed in the Sales Plan for a given year. These plans are prepared based on the production capacities for a given period. The Company estimates that the probability of these transactions occurring is very high, as from a historical point of view, sales were always realised at the levels assumed in Sales Plans.

When entering into hedging transactions, the Company documents the relationship between hedging instruments and the hedged items, as well as the objective of entering into a particular transaction. The Company also documents its assessment, both at the date of inception of the hedge as well as on an on-going basis, of whether the hedging instruments are and will be highly effective in offsetting changes in the cash flows of the hedged items.

###### **Discontinuation of hedge accounting**

The Company ceases to account for derivatives as hedging instruments when they expire, are sold, terminated or settled, or when the Company revokes its designation of a given instrument as a hedging instrument. The Company may designate a new hedging relationship for a given derivative, change the intended use of the derivative, or designate it to hedge another type of risk. In such a case, for cash flow hedges, gains or losses which arose in the periods in which the hedge was effective are retained in other comprehensive income until the hedged item affects profit or loss.

If the hedge of a firm commitment or forecast future transaction ceases to exist, because the hedged item no longer meets the definition of a firm commitment, or because it is probable that the forecast transaction will not occur, then the net gain or loss recognised in other comprehensive income is immediately transferred to profit or loss as a reclassification adjustment.

##### **2.2.5 Inventories**

Inventories consist of the following items:

- materials,
- half-finished products and work in progress,
- finished goods, and
- merchandise.

**Inventory additions** are measured in accordance with the following principles:

- materials and merchandise – at cost,
- finished goods, half-finished products – at actual manufacturing cost,
- work in progress – based on valuation of the work-in-progress inventories.

## 2. Main accounting policies (continued)

### 2.2 Accounting policies (continued)

#### 2.2.5 Inventories (continued)

**Inventory disposals** are measured in accordance with the following principles:

- materials and merchandise – at average cost based on the weighted average cost of a given item,
- finished goods, half-finished products and work in progress – valuation as the difference between inventories closing balance and the value of any additions, and giving due regard to the balance at the beginning of the reporting period, using the weighted average cost method.

**Inventories** are measured in accordance with the following principles:

- materials and merchandise – at average cost as set for inventory disposal,
- finished goods, half-finished products and work in progress – based on cumulative actual manufacturing costs and giving due regard to the balance at the beginning of the reporting period.

At the end of the reporting period inventories are measured, using the above-mentioned policies, but not higher than the net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

#### 2.2.6 Trade and other receivables

Trade receivables are recognised initially at fair value. After initial recognition, trade receivables are measured at amortised cost using the effective interest rate, less allowance for impairment, while trade receivables with the maturity period of up to 12 months from the receivable origination date are not discounted.

Impairment allowances on trade receivables are recognised when there is objective evidence that an entity will not be able to collect all amounts due. The amount of the impairment allowance is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate.

The amount of the impairment allowance is recognised in profit or loss.

Receivables not representing financial assets are recognised initially at their nominal value and measured at the end of the reporting period at the amount due.

Receivables with a maturity period of over 12 months from the end of the reporting period are classified as non-current assets. Current assets include receivables with a maturity period of up to 12 months from the end of the reporting period.

**The category trade and other receivables includes:**

- **trade receivables** – these are receivables which arise from the principal operating activities of the Company,
- **receivables due to fixed assets under construction and intangible assets, and**
- **other receivables**, including:
  - loans granted,
  - other financial receivables, i.e. receivables meeting the definition of financial assets,
  - other non-financial receivables, including among others advances for deliveries and for fixed assets, for fixed assets under construction and intangible assets and for shares in subsidiaries, co-subsidiaries and associates; receivables from employees, if they are settled other than by cash payment; and also budget receivables, and
  - prepayments.

#### 2.2.7 Cash and cash equivalents

Cash and cash equivalents includes cash in hand and in bank accounts, on-demand deposits, other safe current investments with original maturities of three months or less from the date of their placement, acquisition or issuance and with high liquidity. Cash and cash equivalents also include interest on cash equivalents.

#### 2.2.8 Non-current assets (or disposal groups) held for sale

Non-current assets (or disposal groups) are classified as held for sale, if their carrying amount is to be recovered principally through sale transactions rather than through continuing use, under condition that they are available for immediate sale in their present condition subject only to terms that are customary for sales of such assets (or disposal groups) and their sale must be highly probable.

Before the initial classification of assets (or disposal groups) as held for sale, the carrying amount of the asset is measured in accordance with applicable standards. At the moment of reclassification these assets are measured at the lower of their carrying amount and their fair value less costs to sell.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.9 Impairment of non-financial assets**

Intangible assets not yet available for use, are not amortised, but are tested annually for impairment. A depreciable non-financial asset is tested for impairment whenever an event or change in circumstances indicates that its carrying amount may not be recoverable. Amongst the fundamental and most important external indications of possible impairment are the continuation over the long term of a situation in which the carrying amount of Company net assets exceeds their market value, as well as unfavourable technical, market and economic changes to the environment in which the Company operates, including on the destination markets for the Company's products. Another possible indication of impairment may be an increase in market interest rates and premiums for risk reflected in calculations of the discount rates used to calculate the value in use of Company assets.

Internal factors taken into account in determining whether Company assets have been impaired primarily include the substantial decrease in actual net cash flow in relation to the net cash flow from operating activities assumed in the Budget, and, with respect to individual assets, any physical damage, loss of utility and the generation of lower economic benefits than expenditures incurred on their acquisition or construction, if a given asset independently generates cash flow.

An impairment loss is recognised as the amount of the carrying value of the given asset which exceeds its recoverable amount. The recoverable amount is the higher of two amounts: fair value less costs to sell, and value in use.

For the purpose of impairment assessment, assets are grouped at the lowest level at which they generate cash inflows that are largely independent of those from other assets (cash-generating units).

Cash-generating units are determined separately each time an impairment test is to be performed.

If an impairment test indicates that the recoverable amount (i.e. the higher of the asset's fair value less costs to sell and its value in use) of a given asset or cash-generating unit is lower than its carrying amount, an impairment loss is recognised as the difference between the recoverable amount and the carrying amount of a given asset or cash-generating unit. Any impairment loss is allocated to assets within the cash-generating units proportionally to their share of the carrying amount of the entire unit. If such allocation is made, the carrying amount of the asset may not be lower than the highest of the following amounts: fair value less costs to sell, value in use and zero.

Non-financial non-current assets, other than goodwill, for which an impairment loss was recognised in prior periods, are tested at the end of each reporting period to determine whether there is any indication of the possibility that an impairment loss may be reversed.

#### **2.2.10 Equity**

Equity in the financial statements of the Company consists of:

1. Share capital at nominal value,
2. Accumulated other comprehensive income, which consists of:
  - accumulated gains/losses from measurement, set at the fair value of the cash flow hedging instruments in the portion reflecting an effective hedge,
  - accumulated gains/losses from the fair value measurement of available-for-sale financial assets, and
  - income tax related to accumulated gains/losses presented in accumulated other comprehensive income.
3. Retained earnings, composed of:
  - undistributed profit or unabsorbed losses from previous years (accumulated profit/loss from prior years),
  - reserve capital created in accordance with the Commercial Partnerships and Companies Code,
  - reserve capital created and used in accordance with the Statutes of the Company,
  - profit or loss for the period.

In equity "total comprehensive income" represents: profit or loss for the period and other comprehensive income for the reporting period.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.11 Liabilities**

Liabilities are present obligations of the Company arising from past events, the settlement of which is expected to result in an outflow of resources embodying economic benefits.

Liabilities comprise:

- liabilities arising from bank loans, other loans (borrowings) and finance lease liabilities,
- trade payables,
- other financial liabilities, and
- other non-financial liabilities.

Current trade payables are recognised in the statement of financial position at their nominal value. The carrying amount of these liabilities reflects the approximate amount representing the level of amortised cost, calculated using the effective interest rate.

Liabilities not classified as financial liabilities are measured at the amount due.

#### **2.2.12 Accrued expenses**

Accrued expenses are due and payable liabilities arising from goods received or services performed, for which the payment has not yet been made, an invoice has not been received or a formal agreement has not been reached with the supplier, including amounts due to employees.

Accruals include among others:

- salary and the related surcharges paid on a one-off basis, relating to annual periods,
- accrued taxes and local fees, and
- short-term accruals for unused annual leave.

#### **2.2.13 Deferred income**

Deferred income includes mainly monetary resources received to finance the acquisition or manufacture of fixed assets under construction or development work, which are recognised as income over the periods necessary to match it with the depreciation of the assets financed by these resources.

#### **2.2.14 Provisions**

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, such that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Provisions are recognised, in particular, in respect of the following:

- future costs of mine decommissioning, after the conclusion of mining activities,
- future costs of decommissioning of technological facilities (in the copper smelters) and other facilities in cases where the law provides for the obligation to dismantle and remove such assets after the conclusion of mining activities and to restore the sites to their original condition,
- the effects of court proceedings and of disputed issues,
- guarantees granted.

Provisions are recognised in an amount representing the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. If the effect of the time value of money is material, the amount of the provision shall be the present value of the expenditure expected to be required to settle the obligation.

The provision for future decommissioning costs of mines and other facilities is recognised based on the estimated expected costs of decommissioning of such facilities and of restoring the sites to their original condition. Estimation of this provision is based on specially-prepared studies using ore exploitation forecasts (for mining facilities), and technical-economic expertise prepared either by specialist firms or within the Company. Provisions are reviewed quarterly at the end of the reporting period.

The amount of provisions set at 1 January 2004, i.e. at the transition date for application of IFRS for the purposes of preparing the consolidated financial statements, recognised in the cost of property, plant and equipment, was calculated based on the optional exemption set out in IFRS 1 *First-time Adoption of IFRS*. Beginning from 1 January 2004, all changes arising from changes in the amount of provisions are recognised in accordance with IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.14 Provisions (continued)**

Revaluations of the estimated provision for the costs of future decommissioning of mines and other technological facilities reflect:

- decreases due to its utilisation,
- increases due to the passage of time (unwinding of the discount) – recognised in financial costs,
- increases/decreases due to changes in the discount rate – recognised in the initial value of property, plant and equipment\*,
- increases/decreases due to changes in assumptions, including changes in construction-assembly prices – recognised in the initial value of property, plant and equipment \*,
- increases due to the acquisition of new assets under the future decommissioning program,
- decreases due to early, unplanned liquidation of assets under the future decommissioning program.

\*Changes in the discount rate or in the estimated decommissioning cost adjust the value of the relevant item of property, plant and equipment, unless the amount of this change exceeds the carrying amount of property, plant and equipment. Any surplus above this amount is immediately recognised in profit or loss of the current period in other operating income.

The discount rate calculation methodology used to measure provisions is described in Note 3.4.

In accordance with IAS 1 *Presentation of Financial Statements* provisions are presented in the statement of financial position as either current or non-current.

#### **2.2.15 Employee benefits**

The Company pays benefits due to one-off retirement-disability rights, post-mortem benefits, coal equivalent payments and jubilee bonuses according to the Collective Labour Agreement.

The amount of the liability due to these benefits is equal to the present value of the defined benefit obligation at the end of the reporting period, and reflects actuarial gains and losses and the costs of past employment. The value of defined benefit obligations is estimated at the end of the reporting period by independent actuaries using the Projected Unit Credit Method. The present value of the defined benefit obligation is determined by discounting estimated future cash outflow using the interest rates on treasury bonds expressed in the currency of future benefit payment, with maturities similar to those of the liabilities due to be paid. According to IAS 19 *Employee Benefits*, the discount rate should be based on the market yields of highly liquid commercial bonds with low risk. Should there be no developed market for such bonds, and such a situation does exist in Poland, the market yields on government bonds at the end of the reporting period should be applied.

Actuarial gains and losses are recognised in profit or loss in the period in which they arose.

Costs of past employment related to defined benefit plans are accounted for in profit or loss systematically, using the straight-line method, over the period until the benefits become vested.

KGHM Polska Miedź S.A. participates in a contribution plan on behalf of employees within the confines of an Employee Retirement Plan. With respect to this Plan, KGHM Polska Miedź S.A. has no legal or constructive obligation to pay employee benefits if the related insurance firm does not have sufficient assets to cover its obligations in respect of the Plan participants after their period of employment.

#### **2.2.16 Income taxes (including deferred tax)**

Income taxes in profit or loss comprise: current tax and deferred tax.

Current income tax is calculated in accordance with current tax laws.

Deferred tax is determined using tax rates and laws that are expected to apply to the period when the asset is realised or the liability is settled based on tax rates and tax laws that have been enacted or substantively enacted at the end of the reporting period.

A deferred tax liability is recognised for all taxable temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. This liability is not discounted.

A deferred tax asset is recognised for all deductible temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax assets are recognised if it is probable that taxable profit will be available against which the deductible temporary differences and carry-forward of unused tax losses can be utilised.

## 2. Main accounting policies (continued)

### 2.2 Accounting policies (continued)

#### 2.2.16 Income taxes (including deferred tax) (continued)

Deferred tax assets and deferred tax liabilities are recognised irrespective of the period in which their realisation is to occur.

Deferred tax assets and deferred tax liabilities are not recognised if they arise from the initial recognition of an asset or liability in a transaction that:

- is not a business combination, and
- at the time of the transaction, affects neither the accounting profit nor taxable profit.

Deferred tax is recognised in profit or loss for a given period, unless the deferred tax:

- arises from transactions or economic events which are directly recognised in other comprehensive income – in which case the deferred tax is also recognised in the appropriate other comprehensive income item, or
- arises from a business combination – in which case the deferred tax affects goodwill or gain on a bargain purchase.

Deferred tax assets and deferred tax liabilities are offset if the Company has a legally enforceable right to set off current tax assets and current tax liabilities, and if the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority.

#### 2.2.17 Contingent liabilities

Contingent liability is:

- a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity, or
- b) a present obligation that arises from past events but is not recognised because:
  - it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation, or
  - the amount of the obligation (liability) cannot be measured with sufficient reliability.

The contingent liabilities include, among others:

- guarantees and promissory notes issued for the benefit of third-parties in connection with contracts,
- liabilities due to compensation for damages arising in the course of business activities, resulting from matters which remain unresolved,
- conditionally-suspended penalties for economic use of the natural environment, and
- other contingent liabilities arising from contracts.

#### 2.2.18 Statement of comprehensive income

All items of income and expenses for a given reporting period are presented in the **Statement of comprehensive income**. This statement comprises income and expenses for the period, recognised directly in **profit or loss** of the period, as well as profit and loss for the period recognised outside profit or loss, i.e. in **other comprehensive income**.

The Company recognises profit and loss for the period outside profit or loss if individual standards allow or require it. Consequently, the Company recognises profit and loss of the period in **other comprehensive income** involving the fair value measurement of financial assets classified as available for sale, and of profit and loss from fair value measurement of the effective portion of future cash flow hedging instruments, reflecting taxation.

**Profit or loss** (comprising the previously-applied concepts of „income statement” and „statement of profit and loss”) for the given period is the total amount resulting from the deduction of costs from income, excluding items of other comprehensive income. The cost of sales format is applied as the basic costs accounting method.

## 2. Main accounting policies (continued)

### 2.2 Accounting policies (continued)

#### 2.2.19 Revenues

Revenues from sales are recognised at the fair value of the consideration received or receivable, less VAT, rebates and discounts. In the case of sales for which the price is set after the date of recognition of a given sale, revenues are accounted for based on the forward prices from the date of sale. Revenues from sales which are recognised at such an amount are adjusted at the end of each reporting period by any change in the fair value of embedded derivatives, which are separated from the host sales contract in accordance with point 2.2.4.6.

Sales revenues are adjusted for the gain or loss from the settlement of derivatives hedging future cash flows, in accordance with the principle that the portion of gain or loss on a derivative hedging instrument that is determined to be an effective hedge is recognised in the same item of profit or loss in which the gain or loss on the hedged item is recognised at the moment when the hedged item affects profit or loss.

Recognised in sales are revenues arising from ordinary operating activities of the Company, i.e. revenues from sales of products, services, merchandise and materials, reflecting any rebates granted and any other decreases in selling prices.

In addition, revenue for the given reporting period which affects the profit or loss of the period includes: **other operating income**, which is indirectly related to the activities carried out, in particular:

- income and gains from financial investments,
- gains from the measurement and realisation of trading derivatives and the ineffective portion of gains from the realisation and fair value measurement of derivative hedging instruments,
- foreign exchange gains, with the exception of exchange differences arising on liabilities representing sources of finance for the Company's activities,
- reversal of impairment losses on held-to-maturity investments, available-for-sale financial assets, and loans and shares in subsidiaries and associates,
- release of unused provisions, previously charged to other operating costs, and
- gains on disposal of property, plant and equipment and intangible assets,

**finance income**, representing primarily income related to financing of the activities of the Company, including:

- net foreign exchange gains arising exclusively on liabilities from sources of financing of the Company's activities (loans, bank loans, bonds, finance leases etc.),
- gains on realisation and fair value measurement of derivative hedging instruments used to hedge liabilities financing the Company's activities.

#### **Moment of recognition of revenues**

Revenues from the sale of products, merchandise and materials are recognised when:

- the Company has transferred to the buyer the significant risks and rewards of ownership of the merchandise, finished goods and materials,
- the Company has ceased to have a continued involvement in the management of merchandise, finished goods and materials sold to the extent usually associated with inventory management function, and no longer exercises effective control over those items,
- the amount of revenue can be measured in a reliable manner,
- it is probable that the economic benefits associated with the transaction will flow to the Company, and
- the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Revenues from the sale of services are recognised when:

- the amount of revenue can be measured reliably,
- it is probable that the economic benefits associated with the transaction will flow to the Company,
- the stage of completion of the transaction at the end of the reporting period can be measured reliably, and
- the costs connected with the transaction and the costs to complete the transaction can be measured reliably.

The transferral of the subject of transaction is done when substantially all of the risks and rewards of ownership of the merchandise are transferred to the buyer, in accordance with the INCOTERMS delivery base used for a given transaction.

Interest income is recognised on an accrual basis, using the effective interest method.

Income from dividends is recognised when the shareholder's right is set.

#### 2.2.20 Costs

The Company recognises as costs any probable decrease, in the reporting period, of economic benefits of a reliably-determined amount, in the form of a decrease in the value of assets, or an increase of provisions and liabilities, which lead to a decrease in equity or an increase in negative equity in a manner other than the withdrawal of funds by its owners.

## 2. Main accounting policies (continued)

### 2.2 Accounting policies (continued)

#### 2.2.20 Costs (continued)

Costs are recognised in profit or loss based on the direct relation between costs incurred and specific income achieved, i.e. applying the matching principle, through prepayments and accruals.

In the case of purchases of copper-bearing materials for which the price is set after the date of recognition of a given purchase, inventories are accounted for at the expected purchase price on the date of recognition of the inventories. Cost of sales at the end of each reporting period is adjusted by any change in the fair value of embedded derivatives, which are separated from the host purchase contract in accordance with point 2.2.4.6.

Costs are accounted for both by nature and by the cost centres, and are reported in profit or loss using the costs by function (cost of sales) format as the primary cost reporting format.

The total cost of products, merchandise and materials sold comprises:

- the manufacturing cost of products sold,
- the cost of merchandise and materials sold,
- selling costs, and
- administrative expenses.

In addition, costs for the given reporting period which affect profit or loss for the period include:

**other operating costs**, indirectly connected with performed activities, including in particular:

- costs and losses on financial investments,
- losses from the measurement and realisation of traded derivatives and the ineffective portion of losses arising from the realisation and fair value measurement of derivative hedging instruments,
- foreign exchange losses, with the exception of exchange differences arising on liabilities representing sources of finance for the Company's activities,
- impairment losses on held-to-maturity investments, available-for-sale financial assets, loans and on shares in subsidiaries and associates,
- provisions recognised for disputed issues, penalties, compensation and other costs indirectly related to operating activities,
- donations granted,
- losses on disposal of property, plant and equipment and intangible assets,

**finance costs** related to financing of the activities of the Company, including in particular:

- overdraft interest,
- interest on short- and long-term loans, bank loans and other sources of finance, including unwinding of the discount from non-current liabilities,
- net foreign exchange losses arising on liabilities which are sources of financing of the Company's activities,
- changes in provisions arising from the approach of the maturity date of a liability (the so-called unwinding of the discount effect).

#### 2.2.21 Foreign currency transactions and the measurement of items denominated in foreign currencies

##### Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Company operates, i.e. in the functional currency. The financial statements are presented in the Polish zloty (PLN), which is the functional and presentation currency of the Company.

##### Transactions and balances

At the moment of initial recognition, foreign currency transactions are translated into the functional currency:

- at the actual exchange rate applied, i.e. at the buy or sell exchange rate applied by the bank in which the transaction occurs, in the case of the sale or purchase of currencies and the payment of receivables or liabilities,
- at the average exchange rate set for a given currency by the NBP (National Bank of Poland) prevailing on the date of the transaction. The exchange rate prevailing on the date of the transaction is the average NBP rate announced on the last working day proceeding the transaction day.

At the end of each reporting period:

- foreign currency monetary items are translated at the closing rate prevailing on that date, i.e. the average exchange rate set for a given currency by the NBP,
- non-monetary items measured at historical cost in a foreign currency are translated using the exchange rate (i.e. average exchange rate set for a given currency by the NBP) prevailing on the transaction date, and



## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.21 Foreign currency transactions and the measurement of items denominated in foreign currencies (continued)**

- non-monetary items measured at fair value in a foreign currency are translated using the exchange rate (i.e. average exchange rate set for a given currency by the NBP) at the date when the fair value was determined.

Foreign exchange gains or losses arising on the settlement of a foreign currency transaction, or on the measurement and translation of foreign currency monetary assets and liabilities (other than derivatives), are recognised in profit or loss. Foreign exchange gains or losses arising on the measurement of foreign currency derivatives, are recognised in profit or loss as a fair value measurement provided they do not represent the change in the fair value of the effective cash flow hedge. In such a case they are recognised in other comprehensive income, in accordance with hedge accounting principles.

Foreign exchange gains or losses arising on non-monetary items, such as equity instruments, are recognised as an element of changes in fair value, if such instruments are measured at fair value through profit or loss, or in other comprehensive income at fair value, if such equity instruments are classified as available-for-sale financial assets.

#### **2.2.22 Borrowing costs**

Borrowing costs, which are directly attributable to the acquisition, construction or production of a qualifying asset, affect its initial value as an element of its cost. Such costs are capitalised when it is probable that they will result in future economic benefits to the entity, and the costs can be measured reliably.

Other borrowing costs are accounted for as costs in profit or loss in the period in which they are incurred.

Borrowing costs consist of interest and other borrowing-related costs incurred, and include in particular:

- interest costs calculated using the effective interest method in accordance with IAS 39,
- financial charges due to financial leasing contracts recognised in accordance with IAS 17,
- exchange differences arising from foreign currency borrowings, to the extent that they are regarded as an adjustment to interest costs.

A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

Borrowing costs for loans which were drawn without a specified purpose, but which were allocated to finance the acquisition or production of a qualifying asset, affect the initial value of the qualifying asset by the amount of the capitalisation rate applied to the expenditures on that asset. The capitalisation rate is the weighted average of all borrowing costs of an entity that are outstanding during a given period, other than borrowings made specifically for the purpose of obtaining a qualifying asset.

Exchange differences on borrowings drawn in a foreign currency (both specific and general) affect the initial value of the qualifying asset to the extent in which it represents an adjustment of interest costs. The amount of the exchange differences adjusting the interest cost is the difference between the cost of interest on similar financing which the Company would have drawn in its functional currency and the financing cost incurred in the foreign currency.

#### **2.2.23 Leases**

A lease is classified as a finance lease if it transfers to the lessee substantially all of the risks and rewards incidental to ownership of assets. The leased asset is capitalised at the inception of the lease at an amount equal to the fair value of the leased asset or, if lower, the present value of the minimum lease payments.

A depreciable asset acquired in a finance lease is depreciated over the shorter of its useful life and the lease term.

Where the substantial part of the risks and rewards incidental to ownership of an asset is retained by the lessor, a lease contract is classified as an operating lease. Liabilities due to operating leases not recognised in the statement of financial position, in particular with regard to payments to the State Treasury and to territorial self-government entities due to perpetual usufruct of land, as well as liabilities due to other operating leases agreements, are presented in note 37.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.24 Government grants**

Non-monetary grants are accounted for at fair value.

Monetary grants for assets are presented in the statement of financial position as deferred income.

Grants are not recognised until there is a reasonable assurance that the entity will comply with the conditions attaching to them, and that the grants will be received.

Monetary grants are recognised systematically as income over the periods necessary to match them with the related costs which they are intended to compensate, on a systematic basis. They are not credited directly to equity.

A grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs is recognised as income of the period in which it becomes receivable, together with disclosure of this fact.

Grants related to income are presented as income, separately from the related costs which the grants are intended to compensate. Grants are recognised as income regardless of whether they were received in the form of cash or as a decrease of liabilities.

#### **2.2.25 Segment reporting**

Segment reporting involves the grouping of segments by the component of an entity:

- that engage in business activities from which it may earn revenues and incur expenses,
- whose operating results are reviewed regularly by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and
- for which discrete financial information is available.

The activities of KGHM Polska Miedź S.A. represent both a single operating segment and the reporting segment „The production of copper, precious metals and other smelter products”. The Management Board of the Company is the main decision-making body as to the allocation of resources and assessing segment results (the chief operating decision maker, or CDM). Management information provided to the CDM is prepared at the Company level. The mining and production activities of KGHM Polska Miedź S.A. are organised as a combined line of production whose final stage is the sale of the final product to the external customer through the Head Office.

#### **2.2.26 Capital management**

The management of capital in KGHM Polska Miedź S.A. is aimed at maintaining the capacity to continue operations, including the realisation of planned investments, in a manner allowing the Company to generate returns for its shareholders and bring benefits to other stakeholders.

In accordance with market practice, the effective use of capital is monitored among others based on the following ratios:

1. The equity ratio, calculated as the relation of net tangible assets (equity less intangible assets) to total assets,
2. The ratio showing the relationship of borrowings and finance lease liabilities to EBITDA. EBITDA is operating profit plus depreciation/amortisation, and
3. The average weighted cost of capital ratio, calculated as the average weighted cost of equity and borrowed capital. The planned level of this ratio is used to evaluate the effectiveness of planned investment projects.

In order to maintain financial liquidity and the creditworthiness to obtain external financing at a reasonable cost, the Company assumes that the *equity ratio* shall be maintained at a level of not less than 0.5, and the *ratio of Net Debt/EBITDA* at a level of up to 2.0.

#### **2.2.27 Earnings per share**

Earnings per share for each period are calculated by dividing the profit for the given period by the average weighted number of shares outstanding in that reporting period.

#### **2.2.28 Statement of cash flows**

Cash flows from operating activities are presented using the indirect method.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.29 Payments to subsidiaries**

Returnable payments to reserve capital of subsidiaries by the Company are accounted for as either non-current or current financial receivables. Non-returnable payments, including those used to cover losses in the financial statements, are accounted for as an increase in the value of investments. The entity which receives a non-returnable payment accounts for it in retained earnings as an additional payment to reserve capital.

#### **2.2.30 Acquisition of newly-issued shares in the increased share capital**

Acquisition of newly issued shares is accounted for at the date of signing of the agreement (for stock companies) or of signing of the notarial act (for limited liability companies). If the deed of a limited liability company formation allows for an increase in its share capital to a specified amount without any change to the deed of company formation, then the acquisition of shares is accounted for at the date of passage of the relevant resolution by the General Shareholders' Meeting.

#### **2.2.31 Exploration for and evaluation of mineral resources**

Property, plant and equipment (as fixed assets under construction) and intangible assets (as intangible assets not yet available for use - exploration and evaluation expenditures) used in the exploration for and evaluation of mineral resources from the moment the right is acquired to carry out exploratory activities are recognised as exploration and evaluation assets. These assets are presented in the financial statements as a separate asset group under property, plant and equipment and/or intangible assets. At the end of the reporting period exploration and evaluation expenditures are presented in a separate column under intangible assets (note 6).

Exploration and evaluation assets do not include expenditures on development work related to mineral resources or expenditures incurred:

- a) prior to the commencement of exploration for and evaluation of mineral resources, i.e. expenditures incurred prior to the acquisition of legal rights to carry out exploratory activities within a specified area, and
- b) after the technical feasibility and commercial viability of extracting a mineral resource is demonstrable.

Activities related to the exploration for and evaluation of mineral resources include expenditures on work performed as part of a geological project, such as geochemical analysis of terrain, geological charting, exploratory drilling, taking samples for chemical, mineralogical and geophysical analysis, performing geological, hydrological and geological-engineering documentation, whose goal is to develop documentation in the form of an ore management project and the technical feasibility and commercial viability of the ore management project.

Exploration and evaluation assets are measured at the moment of initial recognition at cost. As at the end of each reporting period expenditures are measured at cost less any impairment. Testing for impairment is required at the moment:

- when the technical feasibility and commercial viability of extracting a mineral resource is demonstrable, i.e. prior to reclassification of these assets to another asset group (including to fixed assets under construction or intangible assets not yet available for use other than those used in the exploration for and evaluation of mineral resources), and
- when the facts and circumstances indicate that the carrying amount of the exploration and evaluation assets may exceed their recoverable amount.

Any potential impairment losses are recognised prior to reclassification.

For the purposes of testing for impairment, individual exploration and evaluation assets are tested separately, and if this is not possible, they are allocated to the cash-generating unit which is the entity performing the exploration for and evaluation of mineral resources.

#### **2.2.32 Property rights resulting from certificates of origin of energy from renewable resources and cogeneration.**

Based on the Energy Act and on executive decrees of the Minister of the Economy, power generation companies involved in the trade in and sale of electricity to end users are required to purchase and present for redemption property rights resulting from certificates of origin of energy or the making of substitute fees. This obligation is considered as met if, for a given financial year, the share of total volume of electricity resulting from certificates of origin of energy in the total annual sale of electricity to end users conforms to the limits set forth in decrees of the Minister of the Economy.

## **2. Main accounting policies (continued)**

### **2.2 Accounting policies (continued)**

#### **2.2.32 Property rights resulting from certificates of origin of energy from renewable resources and cogeneration (continued)**

In order to ensure compliance with the requirement to present for redemption property rights or to make substitute fees, at the end of the reporting periods the Company recognises provisions for the costs of acquiring property rights. As an energy distributor, the Company recognises provisions against the value (cost of acquisition) of merchandise sold. The amount of this provision is the lesser of two amounts: the market value of a given certificate of origin or the amount of the substitute fees representing the amount of energy sold. Settlement of the provision and the redemption of property rights is made at the date of redemption of these rights by the President of the Energy Regulation Office or at the date of incurring substitute fees.

The Company recognises the acquired property rights in the statement of financial position as merchandise.

Property rights at the date of acquisition are measured at cost, equivalent to the value of a given certificate of origin based on current market price, or the amount of the renegotiated contractual price if such rights are purchased in off-session market transactions.

At the end of the reporting period property rights are measured at cost less any impairment, though in no case higher than their net sale price.

Penalties for failure to purchase the obligatory amount of property rights resulting from certificates of origin of energy from renewable resources or cogeneration, or to make substitute fees, is recognised in other operating costs.

## **3. Important estimates and assumptions**

In preparing the financial statements, the Management Board of the Company makes use of estimates based on assumptions and opinions which affect the applied accounting principles and presented assets, liabilities, income and costs. The assumptions and estimates on which they are based result from historical experience and the analysis of various factors which are considered as prudent, while their results represent the basis for professional judgement as to the value of the item which they concern. In certain vital questions the Management Board relies on the opinions of independent experts.

Estimates and assumptions of importance for the financial statements of the Company are presented below.

### **3.1 Useful life of property, plant and equipment**

The Management Board of the Company annually reviews the residual value, depreciation methods and useful lives of depreciable property, plant and equipment subject to depreciation. At 31 December 2011 the Management Board determines that the useful lives of assets applied by the Company for purposes of depreciation reflect the expected period of future economic benefits from these assets.

### **3.2 Financial instruments**

In accordance with the guidelines of IAS 39 relating to the classification of non-derivatives with fixed payments or determinable maturity, these assets are classified as held-to-maturity investments. In making this judgement, the intended use and possibility of holding such investments to maturity are evaluated. Should the Company fail to hold such instruments to maturity, apart from the situation described in IAS 39, it would have to reclassify all such assets recognised in this group as available-for-sale. In such a situation, the reclassified investments would be measured at fair value, and not at amortised cost.

#### **Embedded derivatives**

At the end of each reporting period the Company analyses the materiality of the impact of separated embedded derivatives on the financial statements. Following this analysis, the Company determined that separation of these instruments at 31 December 2011 would not have a significant effect on the financial statements.

#### **Afton-Ajax project**

In accordance with the agreement signed on 12 October 2010, KGHM Polska Miedź S.A. acquired 51% of shares of the company KGHM AJAX MINING INC. formed together with Abacus Mining & Exploration Corp. (Abacus), through a cash contribution in the amount of USD 37 million (carrying amount of shares in the financial statements as at 31 December 2011: PLN 109 763 thousand). Abacus has brought to KGHM AJAX MINING INC. all the rights it owns to the Afton-Ajax deposit. The cash was used to carry out a Bankable Feasibility Study and for further exploration. In accordance with this agreement, KGHM Polska Miedź S.A. holds the option to acquire further 29% of shares of KGHM AJAX MINING INC., for an amount calculated as a multiple of USD 0.025

### 3. Important estimations and assumptions (continued)

#### 3.2 Financial instruments (continued)

per pound of copper in 29% of the probable and proven industrial ore resources, though not higher than USD 35 million (at 31 December 2011: PLN 119 609 thousand). On 22 December 2011 the work on the Bankable Feasibility Study was completed and KGHM Polska Miedź S.A. received the document. The Study confirmed the chief geologic and mining parameters of the Afton-Ajax project, which until now had been estimated. Measured & Indicated mineral resources increased to 512 million tonnes of ore containing 0.31% copper and 0.19 g/t of gold, versus the previous 442 million tonnes of ore containing 0.30% copper and 0.19 g/t of gold. Proven & Probable mineral reserves were calculated at 1.34 million tonnes of copper and 2.75 million ounces of gold. Average annual production of copper and gold in concentrate amounts respectively to 50 000 tonnes of copper and 100 000 ounces of gold. Mine life was calculated at 23 years.

Applying conservative market assumptions, NPV ratio is positive. Under the base scenario, the investment payback period is approx. 8 years, while at current metals prices this period is less than 3 years. Capital expenditure, estimated at USD 795 million (the equivalent of PLN 2 687 million, according to the average USD/PLN exchange rate of the National Bank of Poland of 21 December 2011), reflects several important changes aimed at optimising technological solutions through increasing metals recovery during processing, decreasing operating costs, and reducing environmental impact (such as changes in preliminary milling and ore transport systems, technological solutions at the processing plant, and in the waste storage system).

The cost of producing one tonne of copper was calculated in the range of USD 1740 – USD 2800. Mine construction will last two years. Considering the progress to date and the time needed to obtain further permits and administrative approval, the start-up date for the mine has been set at 2015.

The Bankable Feasibility Study was prepared in accordance with Canadian standard NI 43-101 by a consortium of independent consultants under the direction of Tetra Tech WEI (Wardrop).

Counting from the date of receipt of the Bankable Feasibility Study, the Parent Entity had 14 days to review the document, and had another 90 days to decide on the realisation of the option to purchase an additional 29% interest in the company KGHM AJAX MINING INC.

If the option to acquire additional 29% of shares of KGHM AJAX MINING INC. is exercised, KGHM Polska Miedź S.A. will be obliged to organise a capital expenditure of the project financing in the amount of USD 795 million (the equivalent of PLN 2 687 million, according to the average USD/PLN exchange rate of the National Bank of Poland of 21 December 2011).

If this option is not executed by KGHM Polska Miedź S.A., Abacus will have an exclusive right for a period of 90 days to buy back all of the shares belonging to KGHM Polska Miedź S.A. for an amount representing the equivalent of their fair market value, though not higher than USD 37 million (at 31 December 2011: PLN 126 444 thousand). If Abacus decides not to acquire the shares from KGHM Polska Miedź S.A. within this timeframe, KGHM shall transfer, within 60 days, 2% of its shares in KGHM AJAX MINING INC. to Abacus, increasing the share of this company to 51% for the amount of USD 1 451 thousand (at 31 December 2011: PLN 4 959 thousand).

Under IAS 39, KGHM Polska Miedź S.A. is required to measure the options included in this agreement as derivatives. However, at the moment of publication of the financial statements at 31 December 2010 and 30 June 2011, the Parent Entity was not able to make a reliable estimation of the fair value of these options, as work on the Bankable Feasibility Study had not yet been concluded. After receiving this document on 22 December 2011, its results and the possibility of calculating the fair value of these options as at 31 December 2011 have been analysed. Due to the assumptions in the methodology applied in the Bankable Feasibility Study and the nature of the scenarios foreseen for the project, in the opinion of the Parent Entity the possibility of determining the reliable fair value of these options is very limited. There exists therefore the risk of substantial uncertainty in estimating the fair value of these options. As a result of facts described above and based on IAS 39.46(c) it was determined that these options should be measured at cost, as derivatives related to an investment in an equity instrument which is not a traded market instrument and whose fair value cannot be reliably measured. Cost at initial recognition is therefore the amount of the premium paid for these options, which in this case is immaterial.

The deadline for making a corporate decision in the matter described above is 4 April 2012.

#### 3.3 Impairment of shares in subsidiaries and associates

In order to determine the value in use of shares, the Management Board prepares an estimate of projected cash flows which are anticipated due to the continuance of investments, and of rates used to discount these cash flows to present value. In determining present value, assumptions are applied in respect of projected company financial results over the next several years, based on future events and circumstances which could

### **3. Important estimations and assumptions (continued)**

#### **3.3. Impairment of shares in subsidiaries and associates (continued)**

differ from amounts actually achieved, and which in future reporting periods could lead to adjustments in the values of shares in subsidiaries and associates. In the current period, analysis of the value of shares in terms of the arising of evidence of potential impairment did not indicate the existence of any impairment.

#### **3.4 Provisions**

1. Provisions for future employee benefits – retirement or disability benefits, jubilee bonuses, post-mortem benefits and post-employment coal equivalent payments are estimated using actuarial methods. A change in the financial factors being the basis for estimation, i.e.
  - an increase in the discount rate by 1% would cause a decrease in the provision by PLN 121 688 thousand,
  - a decrease in the discount rate by 1% would cause an increase in the provision by PLN 167 693 thousand,
  - an increase in the coal price and salary increase rates by 1% would cause an increase in the provision by PLN 177 518 thousand,
  - a decrease in the coal price and salary increase rates by 1% would cause a decrease in the provision by PLN 132 131 thousand.
2. Provisions for decommissioning costs of mines and other facilities.

These provisions represent the discounted to present value estimated future decommissioning costs of mines and other facilities. Revaluation of this provision at the end of the reporting period is affected by the following indicators:

- a) the index of changes in prices in the construction-assembly sector published by the Central Statistical Office (GUS),
- b) the real discount rate calculated based on the profitability of treasury bonds with maturities nearest to the planned financial outflow (nominal discount rate) and the forecast rate of inflation.

Discount rates (nominal and inflation) are set separately for future periods, i.e. one, two and three years, and jointly for periods from the fourth year.

A 1% increase in the real discount rate (assumed in the reporting period at the level of 5.8%) used by the Management Board to estimate the amount of the provision for decommissioning costs of mines and other facilities would cause a decrease in the carrying amount of the provision by PLN 115 966 thousand. However, a 1% decrease in the real discount rate would cause an increase in the carrying amount of the provision by PLN 152 987 thousand.

#### **3.5 Contingent liabilities**

1. Contingent liabilities due to projects and inventions are estimated at their maximum possible payable amount based on the calculated, anticipated effects of implementation.
2. The value of remaining contingent liabilities are set at their maximum possible payable amount based on the possible risk of the need to realise the liabilities.

#### **3.6 Deferred tax assets/liabilities**

The deferred tax assets/liabilities are measured using the tax rates which are expected to apply at the moment when the asset is realised or the liability is settled, based on tax laws that have been enacted or substantively enacted at the end of the reporting period.

The probability of realising the deferred tax asset with future tax income is based on the Company Budget approved by the Supervisory Board. The projected financial results indicate that the Company will achieve taxable income, based on which the probability of settling a deferred tax asset is determined as high and is recognised in its full amount.

### **4. Business segments**

Based on the analysis of the organisational structure, the system of internal reporting and the management model, it was determined that the Company represents a single operating and reporting segment, which may be defined as „Production of copper, precious metals and other smelter products”.

The core business of the Company is the production of copper and silver. Production is a fully integrated process, in which the end-product of one stage is the half-finished product used in the next stage. Copper ore extracted in the mines is transported to enrichment plants where it is enriched. As a result of this process, copper concentrate is produced, which is then supplied to the smelters. At the smelters, concentrate is smelted and fire refined into copper anodes, which is then subjected to electrolytic refining into copper cathodes. From these cathodes wire rod and round billets are produced. Anode slimes, which arise from the process of copper electrowinning, is a raw material used to produce precious metals. Lead-bearing dust which is generated from the smelting processes is used to produce lead.

#### 4. Business segments (continued)

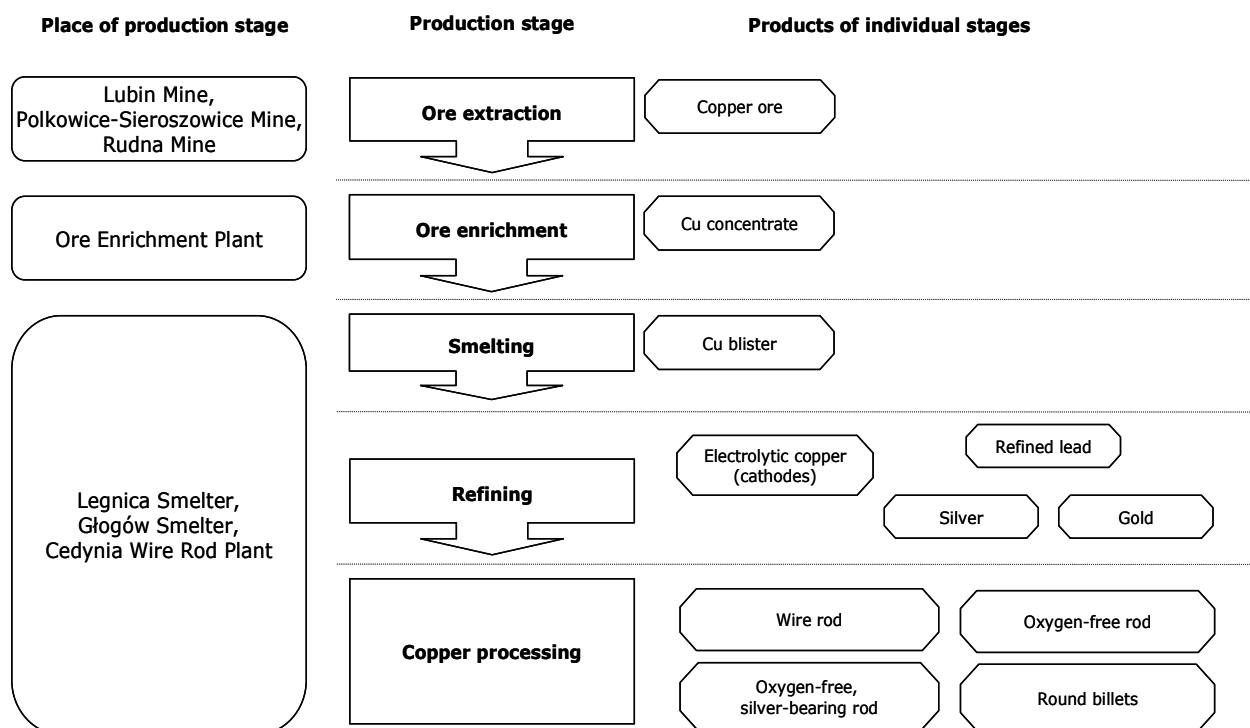
Nickel sulphate and copper sulphate are recovered from the processing of used electrolyte. Gases generated from the smelting furnaces are used to produce sulphuric acid. Economic use is also made of smelter slags, which are sold as road-building materials.

Settlements between further stages of the production process are based on valuation at cost, and as a result the internal organisational units (mines, processing plants, smelters) in the production cycle do not show a profit from sales. The financial data which are prepared for management accounting purposes are based on the same accounting principles which are used to prepare the financial statements. The body which performs regular reviews of the internal reports for purposes of making major operational decisions is the Management Board of the Company, as the body responsible for allocating resources and for the financial results of the Company. The internal reports of the Company on its results are prepared on a monthly basis, and do not contain profits/losses on the separate stages of the production process, concentrating on an analysis of costs of their realisation.

The organisational structure of KGHM Polska Miedź S.A. includes eleven divisions: mines, ore enrichment plants, smelters and a Head Office. The Head Office carries out marketing and sales of the Company's basic products - copper cathodes, round billets, wire rod and silver, the management of financial assets and centralisation of finance and accounting services.

#### Production of basic products

In 2011 the Company produced approx. 571 thousand tonnes of electrolytic copper (in 2010 547 thousand tonnes of electrolytic copper respectively) and 1 260 tonnes of silver (in 2010 1 161 tonnes of silver respectively).



#### Segment assets and liabilities

	At	
	31 December 2011	31 December 2010
<b>Assets</b>	<b>29 253 189</b>	<b>19 829 296</b>
<b>Liabilities</b>	<b>6 117 678</b>	<b>5 372 819</b>

The main item in the segment's assets is cash and cash equivalent, which at 31 December 2011 amounted to PLN 12 835 999 thousand (at 31 December 2010, PLN 2 595 529 thousand), amounting to 43.88% of total assets (detailed information may be found in note 13).

#### 4. Business segments (continued)

A significant item in the segment's assets is property, plant and equipment, which at 31 December 2011 had a net carrying amount of PLN 7 277 903 thousand (as at 31 December 2010, PLN 6 551 111 thousand), representing 24.88% of assets. Accumulated depreciation of property, plant and equipment at 31 December 2011 amounted to PLN 7 792 664 thousand, and impairment losses amounted to PLN 4 086 thousand (as at 31 December 2010, respectively PLN 7 383 612 thousand and PLN 6 408 thousand). The property, plant and equipment and intangible assets of the segment are all located in Poland (detailed information may be found in note 5).

The carrying value of inventories as at 31 December 2011 amounted to PLN 2 355 741 thousand (as at 31 December 2010 PLN 2 011 393 thousand), (detailed information may be found in note 12).

A significant item in the segment's assets is also investments in subsidiaries measured at cost less any impairment. As at 31 December 2011 the value of shares and investment certificates in subsidiaries amounted to PLN 2 012 209 thousand (as at 31 December 2010, PLN 2 643 046 thousand).

No investments in associates were recognised as at 31 December 2011 (as at 31 December 2010 PLN 1 159 947 thousand).

#### Capital expenditures of the segment

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Development</b>	<b>853 097</b>	<b>742 932</b>
in mining	538 046	629 734
in metallurgy	97 113	81 809
in other divisions	217 938	31 389
<b>Replacement</b>	<b>660 801</b>	<b>519 153</b>
in mining	518 507	355 363
of which mining machinery	210 883	190 486
in metallurgy	121 291	148 970
in other divisions	21 003	14 820
<b>Uncompleted capitalised development</b>	<b>4 611</b>	<b>646</b>
<b>Total</b>	<b>1 518 509</b>	<b>1 262 731</b>

For purposes of making decisions on the allocation of resources, reports are prepared for managing purposes on expenditures on tangible investments, which are presented with a breakdown by expenditures on development and replacements.

#### Segment profit or loss

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Sales</b>	<b>20 097 392</b>	<b>15 945 032</b>
Interest income	182 920	62 748
Interest cost	(1 245)	(739)
Amortisation/depreciation	(672 373)	(615 468)
Revaluation of provisions for employee benefits	(102 539)	(29 766)
Other operating income on measurement and realisation of derivatives	1 025 017	463 604
Other operating costs on measurement and realisation of derivatives	(704 098)	(1 635 888)
Income tax	(2 319 077)	(1 036 978)
<b>Profit for the period</b>	<b>11 334 520</b>	<b>4 568 589</b>
ROA* - return on assets (%)	38.7	23.0
ROE** - return on equity (%)	49.0	31.6
<b>EBITDA (operating profit + amortisation/depreciation)</b>	<b>14 360 013</b>	<b>6 253 616</b>



#### 4. Business segments (continued)

$$* \text{ ROA (return on assets) } = \frac{\text{profit/loss for the period}}{\text{total assets}} \times 100$$

$$** \text{ ROE (return on equity) } = \frac{\text{profit/loss for the period}}{\text{equity}} \times 100$$

#### Geographical areas

The geographical breakdown of revenues from sales reflects the location of end clients.

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Germany		4 268 263	3 655 801
Poland		4 109 029	3 921 110
Great Britain		2 667 950	1 516 183
China		2 416 289	1 890 685
The Czech Republic		1 190 381	1 090 468
Italy		1 177 596	789 398
France		652 514	580 299
Hungary		517 076	411 799
Austria		457 198	339 843
Belgium		351 644	284 489
Switzerland		286 952	243 132
Slovakia		60 033	86 139
Other countries		1 942 467	1 135 686
<b>Total</b>	<b>23</b>	<b>20 097 392</b>	<b>15 945 032</b>

#### Main clients

In 2011 the revenues from any customer exceeded 10% of the revenues of KGHM Polska Miedź S.A. (In 2010 revenues from sales from two customers achieved 10% of the revenues of KGHM Polska Miedź S.A. and amounted to PLN 1 716 774 thousand and PLN 1 641 879 thousand respectively).

#### 5. Property, plant and equipment

	At	
	31 December 2011	31 December 2010
Land	17 637	16 093
Buildings	2 666 018	2 645 282
Technical equipment and machinery	2 768 464	2 583 179
Motor vehicles	65 413	55 474
Other fixed assets	15 104	14 390
Fixed assets under construction	1 745 267	1 236 693
<b>Total</b>	<b>7 277 903</b>	<b>6 551 111</b>

KGHM Polska Miedź S.A.  
Annual financial statements prepared in accordance with IFRS  
as adopted by the European Union  
for the period from 1 January 2011 to 31 December 2011  
(amounts in tables in thousand PLN, unless otherwise stated)

## 5. Property, plant and equipment (continued)

### Change in property, plant and equipment in the period from 1 January 2011 to 31 December 2011

	Note	Land	Buildings	Technical equipment and machinery	Motor vehicles	Other fixed assets	Fixed assets under construction	Total
<b>At 1 January 2011</b>								
Gross carrying amount		16 093	6 355 195	6 111 776	155 341	63 087	1 239 639	<b>13 941 131</b>
Accumulated depreciation		-	(3 709 913)	(3 525 462)	(99 540)	(48 697)	-	<b>(7 383 612)</b>
Impairment losses		-	-	(3 135)	(327)	-	(2 946)	<b>(6 408)</b>
Net carrying amount		<b>16 093</b>	<b>2 645 282</b>	<b>2 583 179</b>	<b>55 474</b>	<b>14 390</b>	<b>1 236 693</b>	<b>6 551 111</b>
<b>Changes in 2011</b>								
Settlement of fixed assets under construction		1 590	219 775	686 860	20 138	5 052	(933 415)	-
Self-constructed		-	-	-	-	-	24 132	<b>24 132</b>
Purchases		-	-	-	-	-	1 417 772	<b>1 417 772</b>
Depreciation	24	-	(154 921)	(492 705)	(10 203)	(4 320)	-	<b>(662 149)</b>
Disposal, scrapping/decommissioning or write-off		-	(3 207)	(9 000)	-	(18)	-	<b>(12 225)</b>
Change in amount of provision for costs of decommissioning		-	(41 253)	-	-	-	-	<b>(41 253)</b>
Other changes		(46)	342	130	4	-	85	<b>515</b>
<b>At 31 December 2011</b>								
Gross carrying amount		17 637	6 517 116	6 557 355	170 752	63 579	1 748 214	<b>15 074 653</b>
Accumulated depreciation		-	(3 851 098)	(3 788 080)	(105 011)	(48 475)	-	<b>(7 792 664)</b>
Impairment losses		-	-	(811)	(328)	-	(2 947)	<b>(4 086)</b>
Net carrying amount		<b>17 637</b>	<b>2 666 018</b>	<b>2 768 464</b>	<b>65 413</b>	<b>15 104</b>	<b>1 745 267</b>	<b>7 277 903</b>

### Change in property, plant and equipment in the period from 1 January 2010 to 31 December 2010

	Note	Land	Buildings	Technical equipment and machinery	Motor vehicles	Other fixed assets	Fixed assets under construction	Total
<b>At 1 January 2010</b>								
Gross carrying amount		15 990	6 136 839	5 801 992	146 557	63 996	884 074	<b>13 049 448</b>
Accumulated depreciation		-	(3 631 590)	(3 326 833)	(97 537)	(48 373)	-	<b>(7 104 333)</b>
Impairment losses		-	(1 194)	(3 135)	(327)	-	(2 946)	<b>(7 602)</b>
Net carrying amount		<b>15 990</b>	<b>2 504 055</b>	<b>2 472 024</b>	<b>48 693</b>	<b>15 623</b>	<b>881 128</b>	<b>5 937 513</b>
<b>Changes in 2010</b>								
Settlement of fixed assets under construction		114	281 168	582 019	15 933	2 954	(882 188)	-
Self-constructed		-	-	-	-	-	11 453	<b>11 453</b>
Purchases		-	-	-	-	-	1 226 025	<b>1 226 025</b>
Depreciation	24	-	(137 494)	(455 556)	(8 857)	(4 090)	-	<b>(605 997)</b>
Disposal, scrapping/decommissioning or write-off		-	(3 704)	(17 019)	(167)	(97)	-	<b>(20 987)</b>
Change in amount of provision for costs of decommissioning		-	(624)	-	-	-	-	<b>(624)</b>
Other changes		(11)	1 881	1 711	(128)	-	275	<b>3 728</b>
<b>At 31 December 2010</b>								
Gross carrying amount		16 093	6 355 195	6 111 776	155 341	63 087	1 239 639	<b>13 941 131</b>
Accumulated depreciation		-	(3 709 913)	(3 525 462)	(99 540)	(48 697)	-	<b>(7 383 612)</b>
Impairment losses		-	-	(3 135)	(327)	-	(2 946)	<b>(6 408)</b>
Net carrying amount		<b>16 093</b>	<b>2 645 282</b>	<b>2 583 179</b>	<b>55 474</b>	<b>14 390</b>	<b>1 236 693</b>	<b>6 551 111</b>

## 5. Property, plant and equipment (continued)

Depreciation of property, plant and equipment used in production or in providing services was recognised as a cost of sales in the amount of PLN 643 967 thousand (for the period from 1 January to 31 December 2010, PLN 592 410 thousand), administrative expenses in the amount of PLN 13 276 thousand (for period from 1 January to 31 December 2010, PLN 13 587 thousand), the remaining cost of depreciation of property, plant and equipment in the amount of PLN 4 906 thousand was settled in inventories.

KGHM Polska Miedź S.A. uses also property, plant and equipment (motor vehicles) based on a finance lease agreement in the gross amount at 31 December 2011 of PLN 298 thousand and accumulated depreciation of PLN 203 thousand (at 31 December 2010 the gross amount of PLN 297 thousand and accumulated depreciation of PLN 144 thousand).

### KGHM Polska Miedź S.A. as a lessor leased out the following property, plant and equipment based on operating lease agreements

	At 31 December 2011				At 31 December 2010			
	Cost	Depreciation for the period	Accumulated depreciation	Net carrying amount	Cost	Depreciation for the period	Accumulated depreciation	Net carrying amount
Land	3 762	-	-	3 762	4 064	-	-	4 064
Buildings	74 880	1 827	41 540	33 340	68 412	1 693	38 491	29 921
Technical equipment and machinery	6 115	255	5 236	879	5 213	135	4 628	585
Other property, plant and equipment	719	15	638	81	694	12	657	37
<b>Total</b>	<b>85 476</b>	<b>2 097</b>	<b>47 414</b>	<b>38 062</b>	<b>78 383</b>	<b>1 840</b>	<b>43 776</b>	<b>34 607</b>

### Amount of compensation from insurance companies, recognised in profit or loss, with respect to property, plant and equipment for which an impairment loss was recognised

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Amount of compensation recognised in profit or loss	1 265	3 463

## 5. Property, plant and equipment (continued)

### Major investment projects recognised under fixed assets under construction

	At	
	31 December 2011	31 December 2010
Construction of the SW-4 shaft	471 432	392 400
Głogów Głęboki – Przemysłowy	295 997	208 329
Construction of gas-steam blocks in Głogów and Polkowice Powerplants	179 593	9 305
Ventilation and air conditioning equipment in the mines	136 399	215 643
Investments related to mining region infrastructural development in mines	111 431	48 216
Program of Pyrometallurgy Modernisation	78 226	12 813
Sulphuric Acid Plant in Głogów I Smelter, Głogów II Smelter and Legnica Smelter	69 294	34 950
Exchange of floatation machinery in the Ore Enrichment Plants	69 252	60 872
Purchase of mine machinery and technical equipment	50 781	19 613
Conformatory work	42 366	10 019
Power and communications infrastructure	36 557	35 353
Investments in power and communications infrastructure, related buildings and other investments in the Ore Enrichment Plants	32 031	15 151
Shafts and primary equipments in mines	23 009	24 540
Conveyor belt and pipeline transport investments	20 064	6 273
Intensification of lead production – development of the 4th Doerschel furnace at the Głogów smelter	-	37 037
<b>Total</b>	<b>1 616 432</b>	<b>1 130 514</b>

### Capital commitments at the end of the reporting period, not yet recognised in the statement of financial position

	At	
	31 December 2011	31 December 2010
Purchase of property, plant and equipment	1 367 401	721 753
Purchase of intangible assets	19 211	15 725
<b>Total capital commitments</b>	<b>1 386 612</b>	<b>737 478</b>

## 6. Intangible assets

	At	
	31 December 2011	31 December 2010
Development costs	684	850
Software	1 545	1 608
Acquired concessions, patents, licenses	20 025	20 223
Other intangible assets	50 705	33 389
Exploration and evaluation assets	53 647	16 318
Other intangible assets not yet available for use	24 171	14 330
<b>Total</b>	<b>150 777</b>	<b>86 718</b>

### Change in intangible assets in the period from 1 January 2011 to 31 December 2011

Note	Development costs	Software	Acquired concessions, patents, licenses	Other intangible assets	Exploration and evaluation assets	Other intangible assets not yet available for use	Total
<b>At 1 January 2011</b>							
Gross carrying amount	8 807	19 053	70 642	38 316	16 318	15 124	<b>168 260</b>
Accumulated amortisation	(7 957)	(17 445)	(50 419)	(4 927)	-	-	<b>(80 748)</b>
Impairment losses	-	-	-	-	-	(794)	<b>(794)</b>
Net carrying amount	<b>850</b>	<b>1 608</b>	<b>20 223</b>	<b>33 389</b>	<b>16 318</b>	<b>14 330</b>	<b>86 718</b>
<b>Changes in 2011</b>							
Transfer from intangible assets not yet available for use	101	580	8 070	18 361	-	(27 112)	-
Purchases	-	-	-	-	37 361	35 670	<b>73 031</b>
Self-constructed	-	-	-	-	44	3 530	<b>3 574</b>
Other changes	-	1	-	-	(76)	(2 247)	<b>(2 322)</b>
Amortisation	24 (267)	(644)	(8 268)	(1 045)	-	-	<b>(10 224)</b>
<b>At 31 December 2011</b>							
Gross carrying amount	7 700	19 515	78 712	56 677	53 647	25 245	<b>241 496</b>
Accumulated amortisation	(7 016)	(17 970)	(58 687)	(5 972)	-	-	<b>(89 645)</b>
Impairment losses	-	-	-	-	-	(1 074)	<b>(1 074)</b>
Net carrying amount	<b>684</b>	<b>1 545</b>	<b>20 025</b>	<b>50 705</b>	<b>53 647</b>	<b>24 171</b>	<b>150 777</b>

### Change in intangible assets in the period from 1 January 2010 to 31 December 2010

	Development costs	Software	Acquired concessions, patents, licenses	Other intangible assets	Exploration and evaluation assets	Other intangible assets not yet available for use	Total
<b>At 1 January 2010</b>							
Gross carrying amount	8 654	18 822	67 605	37 825	790	14 714	<b>148 410</b>
Accumulated amortisation	(7 608)	(16 980)	(42 729)	(4 153)	-	-	<b>(71 470)</b>
Impairment losses	-	-	-	-	-	(793)	<b>(793)</b>
Net carrying amount	<b>1 046</b>	<b>1 842</b>	<b>24 876</b>	<b>33 672</b>	<b>790</b>	<b>13 921</b>	<b>76 147</b>
<b>Changes in 2010</b>							
Transfer from intangible assets not yet available for use	213	353	3 048	491	-	(4 105)	-
Purchases	-	-	-	-	15 528	4 985	<b>20 513</b>
Other changes	-	-	-	-	-	(471)	<b>(471)</b>
Amortisation	24 (409)	(587)	(7 701)	(774)	-	-	<b>(9 471)</b>
<b>At 31 December 2010</b>							
Gross carrying amount	8 807	19 053	70 642	38 316	16 318	15 124	<b>168 260</b>
Accumulated amortisation	(7 957)	(17 445)	(50 419)	(4 927)	-	-	<b>(80 748)</b>
Impairment losses	-	-	-	-	-	(794)	<b>(794)</b>
Net carrying amount	<b>850</b>	<b>1 608</b>	<b>20 223</b>	<b>33 389</b>	<b>16 318</b>	<b>14 330</b>	<b>86 718</b>

In the current period, the Company capitalised exploration and evaluation expenditures incurred in the amount of PLN 37 405 thousand (at 31 December 2010, PLN 15 528 thousand) for management of the „Szkłary” nickel deposit and exploration for new reserve regions „Gaworzyce”, „Radwanice” and „Niecka Grodziecka”.

## 6. Intangible assets (continued)

### Major items in intangible assets

<b>As at 31 December 2011</b>		
	<b>Carrying amount</b>	<b>Remaining amortisation period (in years)</b>
Exploration for and evaluation of the Niecka Grodziecka deposit	29 670	-
Rights to geological information on the Głogów Głęboki deposit	27 441	43
License for exploration for Radwanice-Gaworzyce deposit	20 759	-
Established mining rights for extracting copper ore from the Głogów Głęboki deposit	3 733	44
Rights to geological information on Sieroszowice	8 469	50
Rights to geological information on Rudna I	5 051	50
<b>As at 31 December 2010</b>		
	<b>Carrying amount</b>	<b>Remaining amortisation period (in years)</b>
Rights to geological information on the Głogów Głęboki	28 088	44
Established mining rights for extracting copper ore from the Głogów Głęboki deposit	3 820	45

The amortisation of intangible assets utilised in the production or in the providing of services was settled as cost of sales in the amount of PLN 9 303 thousand (for the period from 1 January to 31 December 2010: PLN 8 604 thousand), in administrative expenses in the amount of PLN 901 thousand (for the period from 1 January to 31 December 2010: PLN 867 thousand), other amortisation of intangible assets in the amount of PLN 20 thousand was recognised in inventories.

### Perpetual usufruct rights of land

The Divisions of the Company used land based on perpetual usufruct rights comprising a total area at 31 December 2011 of 5 700 hectares and there were no changes in comparison with the area at 31 December 2010.

	<b>At 31 December 2011 (in hectares)</b>
Lubin Mine	45
Polkowice-Sieroszowice Mine	119
Rudna Mine	91
Ore Enrichment Plants	63
Głogów Smelter	2 046
Legnica Smelter	206
Cedynia Wire Rod Plant	48
Tailings Plant	3 072
Mine-smelter Emergency Rescue Unit	2
Data Center	2
Head Office	6

The Company received these rights free of charge based on laws in force. The land subject to perpetual usufruct is industrial area related to the core business of the Company, which also includes protective zones in which environmental quality limits have been exceeded due to the activities carried out by the Company. Due to the nature of the use of the above-mentioned land, the Company has not determined a fair value for these perpetual usufruct rights at 31 December 2011.

Liabilities not recognised in the statement of financial position of the Company, due to the perpetual usufruct of land, were estimated on the basis of annual fee rates resulting from recent administrative decisions and the remaining useful life of the land subject to this right.

## 6. Intangible assets (continued)

### Perpetual usufruct rights of land (continued)

Total value of future minimum fees due to perpetual usufruct of land	At	
	31 December 2011	31 December 2010
Under one year	7 724	7 235
From one to five years	31 182	29 533
Over five years	375 922	372 006
<b>Total:</b>	<b>414 828</b>	<b>408 774</b>

Fees due to perpetual usufruct of land recognised in profit or loss	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
	7 703	7 212

## 7. Investments in subsidiaries and associates

	Note	Shares and investment certificates in subsidiaries	Investments in associates
<b>At 1 January 2011</b>			
Amount at cost		3 963 824	1 159 947
Impairment losses		(1 320 778)	-
<b>Net carrying amount at 1 January 2011</b>		<b>2 643 046</b>	<b>1 159 947</b>
Changes in 2011			
- purchase of shares		122 726	-
- acquisition of newly-issued shares		78 596	-
- adjustment of cost		(330)	-
- reclassification of shares of a subsidiary and an associate to non-current assets held for sale	26	(824 926)	(1 159 947)
- liquidation of KGHM Polish Copper Ltd.		(6 903)	-
<b>At 31 December 2011</b>			
Amount at cost		2 113 800	-
Impairment losses		(101 591)	-
<b>Net carrying amount at 31 December 2011</b>		<b>2 012 209</b>	
<b>At 1 January 2010</b>			
Amount at cost		3 236 002	1 159 947
Impairment losses		(1 320 778)	-
<b>Net carrying amount at 1 January 2010</b>		<b>1 915 224</b>	<b>1 159 947</b>
Changes in 2010			
- acquisition of shares, certificates		454 403	-
- acquisition of newly-issued shares		274 925	-
- sales of shares		(1 500)	-
- adjustment of cost due to refund of a tax on civil-law transactions		(6)	-
<b>At 31 December 2010</b>			
Amount at cost		3 963 824	1 159 947
Impairment losses		(1 320 778)	-
<b>Net carrying amount at 31 December 2010</b>		<b>2 643 046</b>	<b>1 159 947</b>

## 7. Investments in subsidiaries and associates (continued)

In 2011 KGHM Polska Miedź S.A. purchased for cash shares in the following entities:

	<b>acquisition value</b>
NITROERG S.A.	121 272
KGHM Kupfer AG (until 15 May 2011 – KGHM HMS Bergbau AG)	1 454
<b>Total:</b>	<b>122 726</b>

and acquired for cash newly-issued shares in the following companies:

	<b>acquisition value</b>
CBJ sp. z o.o.	6 697
KGHM Kupfer AG (until 15 May 2011 – KGHM HMS Bergbau AG)	52 364
Miedziowe Centrum Zdrowia S.A.	4 480
KGHM Metraco S.A.	15 000
Fermat 1 S.á.r.l.	55
<b>Total:</b>	<b>78 596</b>

In 2011 KGHM Polska Miedź S.A. reclassified of shares of the subsidiary Dialog S.A. and shares of the associate Polkomtel S.A. to non-current assets held for sale in the total amount of PLN 1 984 873 thousand. In the fourth quarter of 2011 KGHM Polska Miedź S.A. sold non-current assets held for sale: shares of Dialog S.A. and Polkomtel S.A.



## 7. Investments in subsidiaries and associates (continued)

### Investments in subsidiaries (direct share)

As at 31 December 2011

Entity	Head office	Subject of activities	% of share capital held	% of voting power	Carrying amount of shares/ investment certificates
CBJ sp. z o.o.	Lubin	technical research and analyses	100	100	11 822
„Energetyka” sp. z o.o.	Lubin	generation, distribution and sale of electricity and heat	100	100	402 305
KGHM CUPRUM sp. z o.o. – CBR	Wrocław	R&D activities	100	100	8 506
KGHM Ecoren S.A.	Lubin	production of other goods from non-metallic mineral resources	100	100	387 287
KGHM Kupfer AG (until 15 May 2011 – KGHM HMS Bergbau AG)	Berlin	copper and other deposits exploring and mining	100	100	55 429
KGHM I FIZAN	Wrocław	cash investing in securities, monetary market instruments and other property rights	100	100	347 814
KGHM II FIZAN	Wrocław	cash investing in securities, monetary market instruments and other property rights	100	100	7 350
KGHM III FIZAN	Wrocław	cash investing in securities, monetary market instruments and other property rights	100	100	5 000
KGHM Kupferhandelsges. m.b.H.i.L.	Vienna	copper trading	100	100	925
KGHM LETIA S.A.	Legnica	promotion of innovation	85.45	85.45	23 552
KGHM Metraco S.A.	Legnica	trade, agency and representative services	100	100	28 470
KGHM TFI S.A.	Wrocław	creation and management of investment funds and management of financial instruments portfolios	100	100	2 800
„MIEDZIOWE CENTRUM ZDROWIA” S.A.	Lubin	medical services	100	100	40 766
PeBeKa S.A.	Lubin	underground and mining construction, construction of tunnels	100	100	84 122
PHP "MERCUS" sp. z o.o.	Polkowice	trade, production of bundled electrical cables	100	100	32 133
POL-MIEDŹ TRANS Sp. z o.o.	Lubin	transport services	100	100	150 569
Zagłębie Lubin S.A.	Lubin	participation in and organisation of professional sporting events	100	100	98 076
DFM ZANAM – LEGMET Sp. z o.o.	Polkowice	repair and construction of machinery	100	100	48 631
INOVA Spółka z o.o.	Lubin	inspection and control of machinery, R&D work	100	100	13 185
KGHM (SHANGHAI) COPPER TRADING CO., LTD.	Shanghai	trade, intermediation and trade consulting services	100	100	1 565
KGHM AJAX MINING INC.	Vancouver	mining of copper and gold ore	51	51	109 763
BIPROMET S.A.	Katowice	design services, general realisation of construction projects, supply completion	66	66	30 812
NITROERG S.A.	Bieruń	production and sale of explosives, blasting materials, emulsions, nitrocel	85	85	121 272
Fermat 1 S.á r.l.	Luxembourg	holding activity	100	100	55
					<b>2 012 209</b>

## 7. Investments in subsidiaries and associates (continued)

### Investments in subsidiaries (direct share)

As at 31 December 2010

Entity	Head office	Subject of activities	% of share capital held	% of voting power	Carrying amount of shares/ investment certificates
CBJ sp. z o.o.	Lubin	technical research and analyses	100	100	5 125
DIALOG S.A.	Wrocław	telecommunications services, telecommunications, IT and information services	100	100	824 926
„Energetyka” sp. z o.o.	Lubin	generation, distribution and sale of electricity and heat	100	100	402 305
KGHM CUPRUM sp. z o.o. – CBR	Wrocław	R&D activities	100	100	8 506
KGHM Ecoren S.A.	Lubin	production of other goods from non-metallic mineral resources	100	100	387 287
KGHM HMS Bergbau AG	Berlin	copper and other deposits exploring and mining	74.90	74.90	1 611
KGHM I FIZAN	Wrocław	cash investing in securities, monetary market instruments and other property rights	100	100	347 814
KGHM II FIZAN	Wrocław	cash investing in securities, monetary market instruments and other property rights	100	100	7 350
KGHM III FIZAN	Wrocław	cash investing in securities, monetary market instruments and other property rights	100	100	5 000
KGHM Kupferhandelsges. m.b.H.	Vienna	copper trading	100	100	925
KGHM LETIA S.A.	Legnica	promotion of innovation	85.45	85.45	23 552
KGHM Metraco S.A.	Legnica	trade, agency and representative services	100	100	13 470
KGHM Polish Copper Ltd. in liquidation	London	copper trading	100	100	6 903
KGHM TFI S.A.	Wrocław	creation and management of investment funds and management of financial instruments portfolios	100	100	2 800
„MIEDZIOWE CENTRUM ZDROWIA” S.A.	Lubin	medical services	100	100	36 286
PeBeKa S.A.	Lubin	underground and mining construction, construction of tunnels	100	100	84 122
PHP "MERCUS" sp. z o.o.	Polkowice	trade, production of bundled electrical cables	100	100	32 133
POL-MIEDŹ TRANS Sp. z o.o.	Lubin	transport services	100	100	150 569
Zagłębie Lubin S.A.	Lubin	participation in and organisation of professional sporting events	100	100	98 076
DFM ZANAM – LEGMET Sp. z o.o.	Polkowice	repair and construction of machinery	100	100	48 631
INOVA Spółka z o.o.	Lubin	inspection and control of machinery, R&D work	100	100	13 185
KGHM (SHANGHAI) COPPER TRADING CO., LTD.	Shanghai	trade, intermediation and trade consulting services	100	100	1 895
KGHM AJAX MINING INC.	Vancouver	mining of copper and gold ore	51	51	109 763
BIPROMET S.A.	Katowice	design services, general realisation of construction projects, supply completion	66	66	30 812
					<b>2 643 046</b>

## 7. Investments in subsidiaries and associates (continued)

### Investments in an associate

As at 31 December 2011 KGHM Polska Miedź S.A. does not hold investments in associates.

#### As at 31 December 2010

Entity	Head office	Subject of activities	% of share capital held	% of voting power	Carrying amount of shares
POLKOMTEL S.A.	Warsaw	projecting, installation, exploitation and management of telecommunication systems and networks	24.39	24.39	1 159 947
					<b>1 159 947</b>

## 8. Available-for-sale financial assets

	Note	At	
		31 December 2011	31 December 2010
Shares in unlisted companies		9 500	9 500
Shares in listed companies		982 568	740 324
<b>Non-current available-for-sale financial assets</b>	<b>29</b>	<b>992 068</b>	<b>749 824</b>
Participation units of liquid open-end investment funds		-	405 193
<b>Current available-for-sale financial assets</b>	<b>29</b>	<b>-</b>	<b>405 193</b>
<b>Available-for-sale financial assets, total</b>	<b>29</b>	<b>992 068</b>	<b>1 155 017</b>

The increase in the value of non-current available-for-sale financial assets during the reporting period was due to the purchase of the shares of Tauron Polska Energia S.A. In 2011 participation units of liquid open-end investment funds with a carrying amount of PLN 405 193 thousand and a profit on sale of PLN 16 855 thousand were sold.

## 9. Held-to-maturity investments

	Note	At	
		31 December 2011	31 December 2010
Cash held in the Mine Closure Fund		111 665	84 115
<b>Non-current held-to-maturity investments</b>	<b>29</b>	<b>111 665</b>	<b>84 115</b>
Cash held in the Mine Closure Fund		2 147	4 129
<b>Current held-to-maturity investments</b>	<b>29</b>	<b>2 147</b>	<b>4 129</b>
<b>Total held-to-maturity investments</b>	<b>29</b>	<b>113 812</b>	<b>88 244</b>

The Company is required by the Law on Geology and Mining, dated 4 February 1994 (Journal of Laws No. 228 item 1947 dated 14 November 2005 with subsequent amendments) and the Decree of the Minister of the Economy of 24 June 2002 regarding the specific principles for the creation and functioning of mine closure funds (Journal of Laws No. 108, item 951) to accumulate cash in a separate bank account called the Mine Closure Fund (MCF) to cover future decommissioning costs of mines and other facilities.

At 31 December 2011 the balance of held-to-maturity investments comprised MCF bank deposits in the amount of PLN 113 811 thousand and cash on MCF bank account in the amount of PLN 1 thousand. Information on the fair value of held-to-maturity investments was presented in Note 29.2.

## 10. Derivatives

		At	
	Note	31 December 2011	31 December 2010
<b><u>Non-current assets</u></b>			
hedging instruments		896 375	402 234
trade instruments		3 025	1 605
<b>Non-current assets due to derivatives, total:</b>		<b>899 400</b>	<b>403 839</b>
<b><u>Current assets</u></b>			
hedging instruments		850 530	211 186
trade instruments		9 123	5 574
instruments initially designated as hedging instruments excluded from hedge accounting		-	77 261
<b>Current assets due to derivatives, total:</b>		<b>859 653</b>	<b>294 021</b>
<b>Total assets due to derivatives</b>	<b>29</b>	<b>1 759 053</b>	<b>697 860</b>
<b><u>Non-current liabilities</u></b>			
hedging instruments		427 049	606 154
trade instruments		111 064	105 426
Instruments initially designated as hedging instruments excluded from hedge accounting		207	-
<b>Non-current liabilities due to derivatives, total:</b>		<b>538 320</b>	<b>711 580</b>
<b><u>Current liabilities</u></b>			
hedging instruments		125 754	294 161
trade instruments		204 184	187 237
instruments initially designated as hedging instruments excluded from hedge accounting		409	454
<b>Current liabilities due to derivatives, total:</b>		<b>330 347</b>	<b>481 852</b>
<b>Total liabilities due to derivatives</b>	<b>29</b>	<b>868 667</b>	<b>1 193 432</b>

## 10. Derivatives (continued)

TRADE INSTRUMENTS	Volume/ Notional	Avg. weighted price/ex. rate	At 31 December 2011				At 31 December 2010			
			Financial assets		Financial liabilities		Financial assets		Financial liabilities	
	Cu [t] Ag ['000 troz] Currency ['000 USD]	Cu [USD/t] Ag [USD/troz] Currency [USD/PLN]	Current	Non- current	Current	Non- current	Current	Non- current	Current	Non- current
<b>Type of derivative</b>										
<b>Derivatives – Commodity contracts - Metals</b>										
<b>- Copper</b>										
Swaps/forwards										
Swap/forwards - purchased							375			
Options										
Sold call options	7 922	1			(188 331)	(16 474)			(98 644)	(61 438)
Purchased put options	117 000	4 633	8 713	2 818			742	1 605		
Sold put options	136 500	4 643			(8 713)	(12 061)			(742)	(23 580)
<b>TOTAL</b>			<b>8 713</b>	<b>2 818</b>	<b>(197 044)</b>	<b>(28 535)</b>	<b>1 117</b>	<b>1 605</b>	<b>(99 386)</b>	<b>(85 018)</b>
<b>Derivatives – Commodity contracts - Metals</b>										
<b>- Silver</b>										
Options										
Purchased call options	3 600	62.00	410	207						
Sold put options	7 200	19.90			(4 183)	(22 599)				
<b>TOTAL</b>			<b>410</b>	<b>207</b>	<b>(4 183)</b>	<b>(22 599)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Derivatives – Currency contracts</b>										
Options USD										
Purchased call options							454			
Purchased put options							4 003			
Sold put options	1 020 000	2.6529			(2 957)	(59 930)			(87 851)	(20 408)
<b>TOTAL</b>			<b>-</b>	<b>-</b>	<b>(2 957)</b>	<b>(59 930)</b>	<b>4 457</b>	<b>-</b>	<b>(87 851)</b>	<b>(20 408)</b>
<b>TOTAL TRADE INSTRUMENTS</b>			<b>9 123</b>	<b>3 025</b>	<b>(204 184)</b>	<b>(111 064)</b>	<b>5 574</b>	<b>1 605</b>	<b>(187 237)</b>	<b>(105 426)</b>

KGHM Polska Miedź S.A.  
Annual financial statements prepared in accordance with IFRS  
as adopted by the European Union  
for the period from 1 January 2011 to 31 December 2011  
(amounts in tables in thousand PLN, unless otherwise stated)

**10. Derivatives (continued)**

HEDGING INSTRUMENTS		Volume/ Notional	Avg. weighted price/ ex. rate	Maturity/ settlement period		Period of profit/loss impact		At 31 December 2011				At 31 December 2010			
								Financial assets		Financial liabilities		Financial assets		Financial liabilities	
Type of derivative	Cu [t] Ag ['000 troz] Currency ['000 USD]	Cu [USD/t] Ag [USD/troz] Currency [USD/PLN]		From	Till	From	Till	Current	Non- current	Current	Non- current	Current	Non- current	Current	Non- current
<b>Derivatives – Commodity contracts - Metals - Copper</b>															
Options															
Collar	42 000	8 350-11 750		Jan-13	Dec-13	Feb-13	Jan-14		253 654		(49 212)	817		(61 730)	
Collar- seagull	136 500	7 000-9 300		Jan-12	June-13	Feb-12	July-13	156 744	90 889	(96 075)	(60 413)	26 198	208 333	(224 011)	(593 707)
Purchased put options – producer's put	88 500	8 278		Jan-12	Dec-12	Feb-12	Jan-13	313 489	39 363			25 300	45 704		
<b>TOTAL</b>								<b>470 233</b>	<b>383 906</b>	<b>(96 075)</b>	<b>(109 625)</b>	<b>52 315</b>	<b>254 037</b>	<b>(285 741)</b>	<b>(593 707)</b>
<b>Derivatives – Commodity contracts - Metals - Silver</b>															
Options															
Purchased put options	7 200	35.00		Jan-12	Dec-12	Feb-12	Jan-13	183 366	19 008			1 333	406		
Collar	3 600	37.00-62.00		Jan-12	Dec-12	Feb-12	Jan-13	107 594	10 811	(410)	(207)				
Collar- seagull	3 600	40.00-65.00		Jan-13	Dec-13	Feb-13	Jan-14		172 364		(6 001)				
<b>TOTAL</b>								<b>290 960</b>	<b>202 183</b>	<b>(410)</b>	<b>(6 208)</b>	<b>1 333</b>	<b>406</b>	<b>-</b>	<b>-</b>
<b>Derivatives – Currency contracts</b>															
Options USD															
Purchased put options	360 000	2,6000		Jan-12	June-12	Jan-12	June-12	731				86 063			
Collar	900 000	3.2400-4.2600		Jan-12	Dec-13	Jan-12	Dec-13	64 778	94 796	(23 787)	(95 064)		79 369		(5 678)
Collar- seagull	1 020 000	3.3000-4.2471		Jan-12	Dec-14	Jan-12	Dec-14	23 828	215 490	(5 482)	(216 152)	71 475	68 422	(8 420)	(6 769)
<b>TOTAL</b>								<b>89 337</b>	<b>310 286</b>	<b>(29 269)</b>	<b>(311 216)</b>	<b>157 538</b>	<b>147 791</b>	<b>(8 420)</b>	<b>(12 447)</b>
<b>TOTAL HEDGING INSTRUMENTS</b>								<b>850 530</b>	<b>896 375</b>	<b>(125 754)</b>	<b>(427 049)</b>	<b>211 186</b>	<b>402 234</b>	<b>(294 161)</b>	<b>(606 154)</b>

## 10. Derivatives (continued)

### INSTRUMENTS INITIALLY DESIGNATED AS HEDGING INSTRUMENTS EXCLUDED FROM HEDGE ACCOUNTING

Type of derivative	Volume	Avg. weighted price	Maturity/ settlement period		Period of profit/loss impact		At 31 December 2011				At 31 December 2010			
							Financial assets		Financial liabilities		Financial assets		Financial liabilities	
	Ag ['000 troz]	Ag [USD/troz]	From	Till	From	Till	Current	Non- current	Current	Non- current	Current	Non- current	Current	Non- current
<b>Derivatives – Metals - Silver</b>														
Options														
Sold call options	3 600	62.00	Jan-12	Dec-12	Feb-12	Jan-13			(409)	(207)				
<b>TOTAL</b>							-	-	(409)	(207)				
<b>Derivatives – Currency contracts</b>														
Options USD														
Collar											77 261		(454)	
<b>TOTAL</b>											77 261	-	(454)	-
<b>TOTAL INSTRUMENTS INITIALLY DESIGNATED AS HEDGING INSTRUMENTS EXCLUDED FROM HEDGE ACCOUNTING</b>							-	-	(409)	(207)	77 261	-	(454)	-

Derivatives initially designated as hedging instruments under IAS 39 which, due to the restructure of hedging positions, changed their nature, i.e. a change from hedging transactions to trade transactions, were excluded from hedge accounting and are presented as a separate category of financial instruments in the table „Instruments initially designated as hedging instruments excluded from hedge accounting”.

## 11. Trade and other receivables

		At	
	Note	31 December 2011	31 December 2010
<b>Trade and other non-current receivables</b>			
Payment to subsidiaries		47 948	45 210
Other financial receivables		1 055	1 149
Loans granted		35 210	40 240
<b>Total loans and financial receivables, net</b>	<b>29.1</b>	<b>84 213</b>	<b>86 599</b>
Non-financial receivables, net		8	9
<b>Trade and other non-current receivables, net</b>		<b>84 221</b>	<b>86 608</b>
<b>Trade and other current receivables</b>			
Trade receivables		1 114 611	1 735 014
Deposits		-	351 130
Loans granted		7 261	6 551
Payment to subsidiaries		16 167	15 955
Other financial receivables		39 352	43 301
Receivables due to unsettled derivative *		29 834	-
Impairment allowances		(34 560)	(29 600)
<b>Total loans and financial receivables, net</b>	<b>29.1</b>	<b>1 172 665</b>	<b>2 122 351</b>
Non-financial receivables, net		340 412	287 084
Impairment allowances		(10 133)	(15 449)
<b>Total non-financial current receivables, net</b>		<b>330 279</b>	<b>271 635</b>
<b>Total trade and other current receivables, net</b>		<b>1 502 944</b>	<b>2 393 986</b>
<b>Total trade and other current and non-current receivables, net</b>		<b>1 587 165</b>	<b>2 480 594</b>

\*The amount of receivables due to unsettled derivatives represents the derivatives whose date of settlement falls on 4 January 2012 for the balance as at 31 December 2011 and 5 January 2011 for the balance as at 31 December 2010.

## 12. Inventories

	At	
	31 December 2011	31 December 2010
Materials	190 103	167 496
Half-finished products and work in progress	1 618 890	1 649 380
Finished goods	544 506	194 509
Merchandise	2 242	8
<b>Total carrying amount of inventories</b>	<b>2 355 741</b>	<b>2 011 393</b>

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Write-down of inventories in the financial period</b>			
Write-down of inventories recognised in cost of sales	24	2 572	802
Reversal of write-down recognised in cost of sales	24	307	374

As at 31 December 2011, the balance of merchandise includes property rights resulting from certificates of origin for energy from renewable resources and cogeneration in the amount of PLN 2 242 thousand, with respect to green energy (3 816 229 allowances), yellow energy (5 324 606 allowances), red energy (35 022 200 allowances) and violet energy (175 000 allowances).  
In accordance with executive regulations respecting property rights, the Company, based on the amount of energy sold to end users, and based on the amount of energy purchased on the Warsaw Stock Exchange



## 12. Inventories (continued)

through the brokerage Dom Maklerski Banku Ochrony Środowiska S.A., is required to present for redemption property rights resulting from certificates of origin in the following amounts:

- 15 233 964 allowances - green energy,
- 4 833 856 allowances - yellow energy,
- 32 518 653 allowances - red energy,
- 171 574 allowances - violet energy.

For the acquisition of lacking rights resulting from certificates of origin for energy from renewable resources for obligatory redemption the Company created a provision in the amount of PLN 3 195 thousand for the purchase of 11 417 735 allowances for green energy.

## 13. Cash and cash equivalents

	Note	At	
		31 December 2011	31 December 2010
Cash in hand		80	56
Cash at bank		8 374	50 178
Other financial assets with a maturity of up to 3 months from the date of acquisition		12 827 545	2 545 295
<b>Total cash and cash equivalents</b>	<b>29.1</b>	<b>12 835 999</b>	<b>2 595 529</b>

Other financial assets with a maturity of up to 3 months from the date of acquisition include deposits in the amount of PLN 12 811 794 thousand (as at 31 December 2010: PLN 2 538 807 thousand), and deposit interest in the amount of PLN 15 751 thousand (as at 31 December 2010: PLN 6 488 thousand).

Components of cash and cash equivalents presented in the statement of cash flows are the same as those presented in the statement of financial position.

## 14. Non-current assets held for sale

As at 31 December 2011, no non-current assets held for sale had the Company in the statement of financial position (as at 31 December 2010 they were immaterial).

## 15. Share capital

As at 31 December 2011, the share capital of the Company, in accordance with the entry in the National Court Register, amounted to PLN 2 000 000 thousand and was divided into 200 000 000 shares, series A, fully paid, having a face value of PLN 10 each. All shares are bearer shares. The Company has not issued preference shares. Each share gives the right to one vote at the general meeting. The Company does not have treasury shares.

Subsidiaries and associates do not have shares of KGHM Polska Miedź S.A.

In the years ended 31 December 2011 and 31 December 2010 there were no changes in the registered share capital or in the number of shares.

In 2011 there were no changes in significant packets of shares of KGHM Polska Miedź S.A. In 2010 the State Treasury decreased its share in the share capital and the total number of votes at the General Meeting from 41.79% to 31.79%.

At 31 December 2011 and at the date of preparation of these financial statements, the shareholder structure of the Company is as follows:

<b>shareholder</b>	<b>number of shares/votes</b>	<b>total nominal value of shares</b>	<b>percentage held in share capital/ total number of votes</b>
State Treasury	63 589 900	635 899 000	31.79%
Other shareholders	136 410 100	1 364 101 000	68.21%
Total	200 000 000	2 000 000 000	100.00%

## 16. Accumulated other comprehensive income

	Note	Accumulated other comprehensive income due to:		Total accumulated other comprehensive income
		Available-for-sale financial assets	Cash flow hedging financial instruments	
<b>At 1 January 2011</b>		<b>121 385</b>	<b>89 774</b>	<b>211 159</b>
Fair value losses on available-for-sale financial assets		(186 833)	-	(186 833)
Impact of effective cash flow hedging transactions entered into		-	839 725	839 725
Amount transferred to profit or loss – adjustment due to the reclassification of available-for-sale financial assets		(10 692)	-	(10 692)
Amount transferred to profit or loss – adjustment due to the reclassification of hedging instruments			(241 565)	(241 565)
Deferred income tax	20	37 530	(113 651)	(76 121)
<b>Other comprehensive income</b>		<b>(159 995)</b>	<b>484 509</b>	<b>324 514</b>
<b>At 31 December 2011</b>		<b>(38 610)</b>	<b>574 283</b>	<b>535 673</b>
<b>At 1 January 2010</b>		<b>1 489</b>	<b>125 739</b>	<b>127 228</b>
Fair value gains on available-for-sale financial assets		152 734	-	152 734
Impact of effective cash flow hedging transactions entered into		-	97 786	97 786
Amount transferred to profit or loss – adjustment due to the reclassification of available-for-sale financial assets		(4 715)	-	(4 715)
Amount transferred to profit or loss – adjustment due to the reclassification of hedging instruments		-	(142 187)	(142 187)
Deferred income tax	20	(28 123)	8 436	(19 687)
<b>Other comprehensive income</b>		<b>119 896</b>	<b>(35 965)</b>	<b>83 931</b>
<b>At 31 December 2010</b>		<b>121 385</b>	<b>89 774</b>	<b>211 159</b>

## Accumulated other comprehensive income components

	At			
	31 December 2011		31 December 2010	
	Gross value	Net value	Gross value	Net value
<b>Accumulated other comprehensive income due to available-for-sale financial assets</b>	<b>(47 668)</b>	<b>(38 610)</b>	<b>149 857</b>	<b>121 385</b>
Fair value gains/(losses)	(47 668)	(38 610)	149 857	121 385
<b>Accumulated other comprehensive income due to cash flow hedging instruments</b>	<b>708 992</b>	<b>574 283</b>	<b>110 832</b>	<b>89 774</b>
Gains on measurement	708 992	574 283	110 832	89 774
<b>Total accumulated other comprehensive income</b>	<b>661 324</b>	<b>535 673</b>	<b>260 689</b>	<b>211 159</b>

Accumulated other comprehensive income is not subject to distribution.

## 17. Retained earnings

	Note	Reserve capital created in accordance with the Commercial Partnerships and Companies Code, art. 396	Reserve capital created from profit in accordance with the Statutes	Profit/(loss) from prior years	Retained earnings, total
<b>At 1 January 2011</b>		<b>660 000</b>	<b>7 016 729</b>	<b>4 568 589</b>	<b>12 245 318</b>
<b>Profit for the period</b>		-	-	<b>11 334 520</b>	<b>11 334 520</b>
Transfer to reserve capital		-	1 588 589	(1 588 589)	-
Dividend approved and paid	33	-	-	(2 980 000)	(2 980 000)
<b>At 31 December 2011</b>		<b>660 000</b>	<b>8 605 318</b>	<b>11 334 520</b>	<b>20 599 838</b>
<b>At 1 January 2010</b>		<b>660 000</b>	<b>5 076 544</b>	<b>2 540 185</b>	<b>8 276 729</b>
<b>Profit for the period</b>		-	-	<b>4 568 589</b>	<b>4 568 589</b>
Transfer to reserve capital		-	1 940 185	(1 940 185)	-
Dividend approved and paid		-	-	(600 000)	(600 000)
<b>At 31 December 2010</b>		<b>660 000</b>	<b>7 016 729</b>	<b>4 568 589</b>	<b>12 245 318</b>

Based on the Commercial Partnerships and Companies Code, the Company is required to create reserve capital for any potential (future) or existing losses, to which no less than 8% of a given financial year's profit is transferred until the reserve capital has been built up to no less than one-third of the registered share capital. The reserve capital created in this manner may not be employed otherwise than in covering the loss reported in the financial statements.

As at 31 December 2011 the statutory reserve capital in the Company amounts to PLN 660 000 thousand, and is recognised in equity under Retained earnings.

## 18. Trade and other payables

		At	
	Note	31 December 2011	31 December 2010
<b>Trade and other non-current payables</b>			
Trade payables		90	2 232
of which payables due to purchase, construction of property, plant and equipment and intangible assets		-	1 379
Other financial liabilities		10 595	10 683
<b>Total financial liabilities (scope of IFRS7)</b>	<b>29.1</b>	<b>10 685</b>	<b>12 915</b>
Deferred income		894	1 334
<b>Total non-financial liabilities</b>		<b>894</b>	<b>1 334</b>
<b>Total trade and other non-current payables</b>		<b>11 579</b>	<b>14 249</b>
<b>Trade and other current payables</b>			
Trade payables		914 076	850 478
of which payables due to purchase, construction of property, plant and equipment and intangible assets		384 966	300 612
Payables due to unsettled derivatives*		17 073	49 690
Other financial liabilities		11 267	10 283
<b>Total financial liabilities (scope of IFRS7)</b>	<b>29.1</b>	<b>942 416</b>	<b>910 451</b>
Other financial liabilities ( IAS 19 – Employee benefits)		148 090	140 009
<b>Total financial liabilities</b>		<b>1 090 506</b>	<b>1 050 460</b>
Liabilities due to taxes and social security		214 093	200 055
Other non-financial liabilities		41 162	41 973
Special funds		136 600	110 013
Deferred income		8 924	741
Accruals		336 251	324 697
<b>Total non-financial liabilities</b>		<b>737 030</b>	<b>677 479</b>
<b>Total trade and other current payables</b>		<b>1 827 536</b>	<b>1 727 939</b>
<b>Total trade and other non-current and current payables</b>		<b>1 839 115</b>	<b>1 742 188</b>

\*The amount of payables due to unsettled derivatives represents the derivatives whose date of settlement falls on 4 January 2012 for the balance at 31 December 2011 and 5 January 2011 for the balance at 31 December 2010.

These instruments were measured to fair value at the average settlement price for the month of December 2011 and of December 2010 respectively. For details see note 30.1.5.

As at 31 December 2011 the largest item within accruals is a provision for future payment due to the annual bonus in the amount of PLN 274 577 thousand (at 31 December 2010, PLN 264 703 thousand). The annual bonus is paid after approval of the financial statements in accordance with the Collective Labour Agreement for the Employees of KGHM Polska Miedź S.A.

## 19. Borrowings and finance lease liabilities

	Note	At	
		31 December 2011	31 December 2010
Non-current finance lease liabilities		35	8 490
Current finance lease liabilities		58	2 965
<b>Borrowings and finance lease liabilities</b>	<b>29.1</b>	<b>93</b>	<b>11 455</b>

### 19.1 Finance lease liabilities

#### Finance lease liabilities as at 31 December 2011

	2012 (current)	2013	2014	2015	Total
<b>Nominal value of minimum lease payments</b>	<b>65</b>	<b>37</b>	-	-	<b>102</b>
Future finance costs due to finance leases	(7)	(2)	-	-	(9)
<b>Present value of minimum lease payments</b>	<b>58</b>	<b>35</b>	-	-	<b>93</b>

In 2011, earlier repayment was made to the State Treasury of liabilities due to paid access to geological information.

#### Finance lease liabilities as at 31 December 2010

	2011 (current)	2012	2013	2014	Total
<b>Nominal value of minimum lease payments</b>	<b>2 995</b>	<b>2 995</b>	<b>2 968</b>	<b>2 931</b>	<b>11 889</b>
Future finance costs due to finance leases	(30)	(67)	(130)	(207)	(434)
<b>Present value of minimum lease payments</b>	<b>2 965</b>	<b>2 928</b>	<b>2 838</b>	<b>2 724</b>	<b>11 455</b>

## 20. Deferred tax

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Deferred tax assets at the beginning of the reporting period		865 443	601 467
Deferred tax liabilities at the beginning of the reporting period		505 610	434 405
<b>Net deferred tax assets at the beginning of the reporting period</b>		<b>359 833</b>	<b>167 062</b>
<b>Changes during the year</b>			
Charged to profit for the period	31	(469 838)	(326 065)
Credited to profit for the period	31	354 588	538 523
Decrease in accumulated other comprehensive income	16	(574 234)	(231 257)
Increase in accumulated other comprehensive income	16	498 113	211 570
<b>Net deferred tax assets at the end of the reporting period, of which:</b>		<b>168 462</b>	<b>359 833</b>
Deferred tax assets at the end of the reporting period		978 128	865 443
Deferred tax liabilities at the end of the reporting period		809 666	505 610

### Deferred tax assets prior to offsetting

	At 1 January 2011 based on the rate of 19%	Credited/(Charged) to profit for the period due to a change in the balance of temporary differences	Increase in accumulated other comprehensive income due to change in the balance of temporary differences	At 31 December 2011 based on the rate of 19%
Provision for decommissioning of mines and other facilities	101 797	(7 102)	-	94 695
Measurement of forward transactions	428 480	(4 519)	-	423 961
Re-measurement of hedging instruments	-	-	79 470	79 470
Depreciation differences	20 814	7 205	-	28 019
Future employee benefits liabilities	232 045	19 482	-	251 527
Measurement of available-for-sale financial assets	9 713	1 331	14 096	25 140
Other	72 594	2 722	-	75 316
<b>Total</b>	<b>865 443</b>	<b>19 119</b>	<b>93 566</b>	<b>978 128</b>
	At 1 January 2010 based on the rate of 19%	Credited/(Charged) to profit for the period due to a change in the balance of temporary differences	Increase in accumulated other comprehensive income due to change in the balance of temporary differences	At 31 December 2010 based on the rate of 19%
Provision for decommissioning of mines and other facilities	99 453	2 344	-	101 797
Measurement of forward transactions	174 330	254 150	-	428 480
Depreciation differences	19 330	1 484	-	20 814
Future employee benefits liabilities	226 387	5 658	-	232 045
Measurement of available-for-sale financial assets	8 543	1 170	-	9 713
Other	73 424	(830)	-	72 594
<b>Total</b>	<b>601 467</b>	<b>263 976</b>	-	<b>865 443</b>

## 20. Deferred tax (continued)

### Deferred tax liabilities prior to offsetting

	At 1 January 2011 based on the rate of 19%	Charged to profit for the period due to a change in the balance of temporary differences	(Increase)/Decrease in accumulated other comprehensive income due to change in the balance of temporary differences	At 31 December 2011 based on the rate of 19%
Measurement of forward transactions	66 539	113 561	-	<b>180 100</b>
Re-measurement of hedging instruments	21 058	-	193 121	<b>214 179</b>
Depreciation differences	387 770	18 117	-	<b>405 887</b>
Measurement of available-for-sale financial assets	28 473	-	(23 434)	<b>5 039</b>
Other	1 770	2 691	-	<b>4 461</b>
<b>Total</b>	<b>505 610</b>	<b>134 369</b>	<b>169 687</b>	<b>809 666</b>

	At 1 January 2010 based on the rate of 19%	Charged to profit for the period due to a change in the balance of temporary differences	(Increase)/Decrease in accumulated other comprehensive income due to change in the balance of temporary differences	At 31 December 2010 based on the rate of 19%
Measurement of forward transactions	37 138	29 401	-	<b>66 539</b>
Re-measurement of hedging instruments	29 494	-	(8 436)	<b>21 058</b>
Depreciation differences	365 977	21 793	-	<b>387 770</b>
Measurement of available-for-sale financial assets	350	-	28 123	<b>28 473</b>
Other	1 446	324	-	<b>1 770</b>
<b>Total</b>	<b>434 405</b>	<b>51 518</b>	<b>19 687</b>	<b>505 610</b>



## 21. Employee benefits

A general description of the Employee Retirement Plan was presented in Note 2.2.15

### Changes in future employee benefits

	Note	TOTAL liabilities	Jubilee awards	Retirement and disability benefits	Coal equivalent	Post-mortem benefit
<b>Present value of obligations - at 1 January 2011</b>	<b>25</b>	<b>1 227 190</b>	<b>237 276</b>	<b>200 033</b>	<b>764 059</b>	<b>25 822</b>
Interest costs		66 428	12 649	10 977	41 376	1 426
Current service cost		36 990	14 911	10 279	11 010	790
Benefits paid		(75 814)	(29 478)	(11 203)	(34 546)	(587)
Actuarial losses/(gains)		73 249	454	533	73 375	(1 113)
<b>Present value of obligations - at 31 December 2011</b>	<b>25</b>	<b>1 328 043</b>	<b>235 812</b>	<b>210 619</b>	<b>855 274</b>	<b>26 338</b>
Past service cost unrecognised at the end of the reporting period		(4 217)	-	(4 217)	-	-
<b>Carrying amount of liabilities in statement of financial position - at 31 December 2011</b>		<b>1 323 826</b>	<b>235 812</b>	<b>206 402</b>	<b>855 274</b>	<b>26 338</b>
of which:						
Carrying amount of non-current liabilities		1 216 355	202 530	175 337	814 546	23 942
Carrying amount of current liabilities		107 471	33 282	31 065	40 728	2 396
<b>Present value of obligations - at 1 January 2010</b>	<b>25</b>	<b>1 199 110</b>	<b>232 680</b>	<b>188 436</b>	<b>753 304</b>	<b>24 690</b>
Interest costs		66 104	12 549	10 559	41 592	1 404
Current service cost		36 140	14 263	10 066	11 074	737
Benefits paid		(80 106)	(34 821)	(11 847)	(32 315)	(1 123)
Actuarial losses/(gains)		5 942	12 605	2 819	(9 596)	114
<b>Present value of obligations - at 31 December 2010</b>	<b>25</b>	<b>1 227 190</b>	<b>237 276</b>	<b>200 033</b>	<b>764 059</b>	<b>25 822</b>
Past service cost unrecognised at the end of the reporting period		(5 903)	-	(5 903)	-	-
<b>Carrying amount of liabilities in statement of financial position - at 31 December 2010</b>		<b>1 221 287</b>	<b>237 276</b>	<b>194 130</b>	<b>764 059</b>	<b>25 822</b>
of which:						
Carrying amount of non-current liabilities		1 128 246	209 007	166 704	729 007	23 528
Carrying amount of current liabilities		93 041	28 269	27 426	35 052	2 294

### Present value of future employee benefits

31 December 2011	1 328 043
31 December 2010	1 227 190
31 December 2009	1 199 110
31 December 2008	1 058 261
31 December 2007	930 256

## 21. Employee benefits (continued)

### Total costs due to future employee benefits recognised in profit or loss

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Total costs recognised in profit or loss</b>			
Interest costs		66 428	66 104
Current service cost		36 990	36 140
Actuarial losses		73 249	5 942
Past service cost	25	1 686	1 686
		<b>178 353</b>	<b>109 872</b>

For purposes of re-measuring the provision at the end of the current period, the Company assumed parameters based on available forecasts of inflation, an analysis of increases in coal prices and in the lowest salary, and also based on the anticipated profitability of non-current government bonds.

<b>Main actuarial assumptions at 31 December 2011:</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016 and beyond</b>
- discount rate	5.80%	5.80%	5.80%	5.80%	5.80%
- rate of increase in coal prices	8.00%	3.30%	3.00%	3.00%	3.00%
- rate of increase in the lowest salary	8.20%	4.00%	4.00%	4.00%	4.00%
- expected inflation	2.50%	2.50%	2.50%	2.50%	2.50%
- future expected increase in salary	5.30%	3.80%	3.50%	3.50%	3.50%

<b>Main actuarial assumptions at 31 December 2010:</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015 and beyond</b>
- discount rate	5.50%	5.50%	5.50%	5.50%	5.50%
- rate of increase in coal prices	0.00%	3.00%	3.00%	3.00%	3.00%
- rate of increase in the lowest salary	5.20%	4.00%	4.00%	4.00%	4.00%
- expected inflation	2.50%	2.50%	2.50%	2.50%	2.50%
- future expected increase in salary	3.50%	4.00%	4.00%	4.00%	4.00%

Changes in actuarial gains/losses are caused by a change in assumptions relating to the discount rate, increases in coal prices and increases in salary.

## 22. Provisions for other liabilities and charges

	Note	TOTAL	Decommissioning costs of mines and other technological facilities	Costs of scrapping property, plant and equipment	Disputed issues and court proceedings	Other provisions
<b>Provisions at 1 January 2011</b>		<b>535 533</b>	<b>514 006</b>	<b>5 600</b>	<b>1 975</b>	<b>13 952</b>
Provisions recognised in other operating costs	27	3 064	-	-	2 688	376
Changes in provisions arising from updating of estimates recognised in other operating (income)/costs	26,27	(493)	(2 654)	(32)	-	2 193
Changes in provisions arising from updating of estimates recognised in fixed assets		(41 253)	(41 253)	-	-	-
Changes in provisions arising from the approach of the maturity date of a liability (unwinding of the discount) recognised in finance costs	28	32 052	31 491	216	-	345
Utilisation of provisions		(6 428)	(3 118)	(699)	(1 036)	(1 575)
Release of provisions recognised in other operating income	26	(1 479)	-	(166)	(1 303)	(10)
Adjustment due to transfer to Mine Closure Fund		(22 866)	(22 866)	-	-	-
<b>Provisions at 31 December 2011</b>		<b>498 130</b>	<b>475 606</b>	<b>4 919</b>	<b>2 324</b>	<b>15 281</b>
of which:						
<b>Non-current provisions</b>		<b>483 657</b>	<b>467 680</b>	<b>2 730</b>	<b>-</b>	<b>13 247</b>
<b>Current provisions</b>		<b>14 473</b>	<b>7 926</b>	<b>2 189</b>	<b>2 324</b>	<b>2 034</b>

		TOTAL	Decommissioning costs of mines and other technological facilities	Costs of scrapping property, plant and equipment	Disputed issues and court proceedings	Other provisions
<b>Provisions at 1 January 2010</b>		<b>533 306</b>	<b>510 903</b>	<b>5 307</b>	<b>1 507</b>	<b>15 589</b>
Provisions recognised in other operating costs	27	2 083	217	293	1 271	302
Changes in provisions arising from updating of estimates recognised in other operating (income)/costs	26, 27	(1 067)	(899)	-	-	(168)
Changes in provisions arising from updating of estimates recognised in fixed assets		(624)	(624)	-	-	-
Changes in provisions arising from the approach of the maturity date of a liability (unwinding of the discount) recognised in finance costs	28	32 174	31 842	-	-	332
Utilisation of provisions		(6 961)	(4 590)	-	(327)	(2 044)
Release of provisions recognised in other operating income	26	(1 522)	(987)	-	(476)	(59)
Adjustment due to transfer to Mine Closure Fund		(21 856)	(21 856)	-	-	-
<b>Provisions at 31 December 2010</b>		<b>535 533</b>	<b>514 006</b>	<b>5 600</b>	<b>1 975</b>	<b>13 952</b>
of which:						
<b>Non-current provisions</b>		<b>517 749</b>	<b>500 739</b>	<b>4 546</b>	<b>-</b>	<b>12 464</b>
<b>Current provisions</b>		<b>17 784</b>	<b>13 267</b>	<b>1 054</b>	<b>1 975</b>	<b>1 488</b>

## 22. Provisions for other liabilities and charges (continued)

As at 31 December 2011 the largest item of provisions for other liabilities is an estimate for the costs of future decommissioning (liquidation) of mines and other technological facilities with the carrying value of PLN 475 606 thousand (as at 31 December 2010: PLN 514 006 thousand), estimated in accordance with the methodology defined in the International Financial Reporting Standards. The decrease in the provision in 2011 was mainly caused by the change in long term forecast yield on bonds.

The programme and schedule of decommissioning of technological facilities and estimates of decommissioning costs have been worked on since 2001 in cooperation with the subsidiary, KGHM Cuprum Sp. z o.o. CBR. Revaluations of the basic decommissioning costs are made periodically based on the changes of the price index for the construction-assembly industry, which are published by the Main Statistical Office (GUS), and movements in tangible fixed assets encompassed by the plan.

Subsequent updates are made should there occur significant economic events affecting the amount of the provision, while also utilising experience gained during the decommissioning of individual facilities. The last update to the decommissioning plan was made in 2011. As a result of work carried out, the present decommissioning plan reflects the technological objects mine decommissioning schedule of 2009 and on-going updating of a decommissioning costs forecast. According to the update, the greatest impact on the change in estimates came from labour costs, verified on the basis of Company forecasts and, to a lesser extent, other costs estimated using indices for price changes in the production-assembly sector published by GUS. The update assumes that mine production by KGHM Polska Miedź S.A. in the existing licensed areas will end in 2042.

The largest facility earmarked for decommissioning (restoration), which at the same time accounts for the largest share in the provision, is the "Żelazny Most" tailings pond, together with the hydro-transportation network and cubage hydro-technical facilities. The area and type of this tailings pond requires several stages of site restoration and development, because "Żelazny Most" tailings pond will be operational until the last working day of the mines and enrichment plants. According to the current plan, preparatory works for the tailings pond's liquidation and its partial restoration will commence in 2025 and will last until 2037. In 2038, the main stage of the tailings pond's liquidation will commence and is expected to be completed in 2047.

The amount of the provision recognised in the statement of financial position is the equivalent of the estimated costs of future decommissioning of individual facilities discounted to their present value, which were estimated assuming the use of existing mine decommissioning technology, applying current prices. The amount of the provision is revalued by the Company at the end of each quarter by applying in the model the discounting ratios described in Note 3.5. At the end of the reporting period the amount of the provision was updated, using the discount rate applied in the model for future employee benefit provisions (Note 21), which is near the rate of return on long-term bonds. Risk related to the provision was reflected in forecasts of cash flow through the index of changes in prices in the construction-assembly sector.

The balance of the decommissioning provision is adjusted for the amount transferred to the Mine Closure Fund of KGHM Polska Miedź S.A., which has been created based on the act – Geological and Mining, i.e. 5% of depreciation of the mines' fixed assets for each year which is set in accordance with the Corporate Income Tax Act. Cash transfers made to the Mine Closure Fund are invested by the Company in secure short-term securities (Note 9) or short-term deposits and income from these investments increases the Fund's balance.

### Provisions by the facilities of the highest importance in the amount of provision for decommissioning of mines and other technological facilities

Division	Facility	At	
		31 December 2011	31 December 2010
Tailings Plant	"Żelazny Most" tailings pond	90 068	92 328
Tailings Plant	Other waste storage areas	45 729	44 460
Rudna Mine	Central part of Rudna Mine (shafts: RI, RII, RV)	40 327	41 325
Ore Enrichment Plant	Polkowice OEP	38 985	38 517
Ore Enrichment Plant	Rudna OEP	38 848	39 789
Polkowice-Sieroszowice Mine	Western part of Polkowice Mine (shafts: P-I, P-II)	31 036	31 764
Ore Enrichment Plant	Lubin OEP	29 835	30 979
Lubin Mine	Central part of Lubin Mine (shafts: LI, LII)	26 910	26 937
Rudna Mine	Western part of Rudna Mine (shafts: RIII, RIV, RX)	23 972	25 642
Lubin Mine	Western part of Lubin Mine (shafts: LIV, LV)	23 917	24 038

## 23. Sales

### Net revenues from the sale of products, merchandise and materials (by type of activity)

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Copper, precious metals, smelter by-products		19 831 704	15 698 874
Salt		72 153	64 108
Merchandise		64 108	72 778
Services		60 256	56 619
Scrap and production materials		55 733	41 408
Other goods		12 953	10 741
Other materials		485	504
<b>Total</b>	<b>4</b>	<b>20 097 392</b>	<b>15 945 032</b>

### Net revenues from the sale of products, merchandise and materials (by destination)

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>domestic</b>		<b>4 109 029</b>	<b>3 921 110</b>
Copper, precious metals, smelter by-products		3 843 351	3 687 824
Salt		72 153	64 108
Merchandise		64 108	60 794
Services		60 246	55 731
Scrap and production materials		55 733	41 408
Other goods		12 953	10 741
Other materials		485	504
<b>foreign</b>		<b>15 988 363</b>	<b>12 023 922</b>
Copper, precious metals, smelter by-products		15 988 353	12 011 050
Merchandise		-	11 984
Services		10	888
<b>Total</b>	<b>4</b>	<b>20 097 392</b>	<b>15 945 032</b>

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Average copper price on LME (USD/t)	8 811	7 539
Average exchange rate (USD/PLN) per NBP	2.96	3.02

## 24. Expenses by nature

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Depreciation of property, plant and equipment and amortisation of intangible assets	5,6	672 373	615 468
Employee benefits expenses	25	2 855 007	2 661 477
Materials and energy		5 910 950	4 777 879
External services		1 256 045	1 029 023
Taxes and charges		318 166	300 165
Advertising costs and representation expenses		42 780	23 857
Property and personal insurance		22 800	18 308
Research and development costs not capitalised in intangible assets		6 006	4 460
<b>Other costs, of which:</b>		<b>18 243</b>	<b>11 405</b>
Write-down of inventories	12	2 572	802
Reversal of write-down of inventories	12	(307)	(374)
Allowance for impairment of receivables	29.3	297	24
Reversal of allowance for impairment of receivables	29.3	(856)	-
Losses from the disposal of financial instruments	29.3	5 897	2 337
Business trip expenses		7 342	4 900
Other operating costs		3 298	3 716
<b>Total expenses by nature</b>		<b>11 102 370</b>	<b>9 442 042</b>
Cost of merchandise and materials sold (+) of which:		106 851	107 176
Allowance for impairment of receivables	29.3	-	3
Change in inventories of finished goods and work in progress (+/-)		(320 854)	(170 460)
Cost of manufacturing products for internal use (-)		(154 528)	(91 072)
<b>Total cost of sales, selling costs and administrative expenses</b>		<b>10 733 839</b>	<b>9 287 686</b>

## 25. Employee benefits expenses

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Remuneration		2 012 470	1 933 097
Costs of social security and other benefits		739 998	698 614
Costs of future benefits (provisions) due to retirement benefits, jubilee awards and similar employee benefits, of which:		102 539	29 766
Present value of obligation	21	100 853	28 080
Past service cost	21	1 686	1 686
<b>Employee benefits expenses</b>		<b>2 855 007</b>	<b>2 661 477</b>

## 26. Other operating income

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Income and gains from financial instruments classified under other operating activities, resulting from:	29.3	2 117 171	528 256
Measurement and realisation of derivatives		1 025 017	463 604
Interest		180 081	59 419
Foreign exchange gains		895 164	-
Gains from measurement of non-current liabilities		-	167
Gains from sale		16 855	4 925
Reversal of allowance for impairment of other receivables		54	141
Profit on sale of an associate	7	2 512 200	-
Profit on sale of subsidiaries	7	150 045	34
Non-financial interest		2 839	3 329
Reversal of allowance for impairment of non-financial receivables	11	2 681	1 484
Dividends received		277 330	146 658
Release of unused provisions for:		6 940	6 028
Decommissioning of mines		5 179	3 973
Disputed issues and court proceedings		1 303	476
Liabilities towards municipal authorities due to signed donation agreements		250	1 520
Other		208	59
Penalties and compensation		15 659	8 209
Excess payments of property tax		70	2 169
Surpluses identified in current assets		-	8 779
Other operating income/gains		7 984	6 256
<b>Total other operating income</b>		<b>5 092 919</b>	<b>711 202</b>

## 27. Other operating costs

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Costs and losses on financial instruments classified under other operating activities, resulting from:	29.3	711 349	1 666 441
Measurement and realisation of derivatives		704 098	1 635 888
Interest		227	24
Foreign exchange losses		-	30 445
Losses on measurement of non-current liabilities		1 716	-
Allowance for impairment of loans		12	13
Allowances for impairment of other receivables		5 296	71
Allowances for impairment of other non-financial receivables	11	-	3 358
Losses on the sale of property, plant and equipment and intangible assets		10 423	17 614
Allowance for impairment of intangible assets not yet available to use		280	-
Donations granted		15 113	12 503
Interest on overdue non-financial liabilities		450	114
Provisions for:		8 032	5 522
Decommissioning of mines		2 525	2 305
Disputed issues, pending court proceedings		2 688	1 271
Liabilities towards municipal authorities (gminas) due to signed donation agreements		2 443	1 352
Other		376	594
Penalties and compensation paid		844	498
Contributions to a voluntary organisation		10 808	8 202
Non-culpable shortages in tangible current assets, cash and losses from fortuitous events		530	3 423
Other operating costs/losses		11 003	12 725
<b>Total other operating costs</b>		<b>768 832</b>	<b>1 730 400</b>

## 28. Finance costs

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Interest due to:	29.3	568	601
Loans		61	116
Finance leases		507	485
Net foreign exchange losses/(gains) on borrowings	29.3	1 150	(459)
Changes in provisions arising from the approach of the maturity date of a liability (unwinding of the discount), due to:	22	32 052	32 174
Measurement of provisions for decommissioning of mines		31 491	31 842
Measurement of other provisions		561	332
Losses due to measurement of non-current liabilities	29.3	273	265
<b>Total finance costs</b>		<b>34 043</b>	<b>32 581</b>



## 29. Financial instruments

### 29.1 Carrying amount

**At 31 December 2011**  
**Categories of financial instruments**

Note		Categories of financial instruments								
Classes of financial instruments		Available-for-sale financial assets	Held-to-maturity investments	Financial assets at fair value through profit or loss	Loans and receivables	Financial liabilities at fair value through profit or loss*	Other financial liabilities		Hedging instruments	Total
							Financial liabilities measured at amortised cost	Financial liabilities due to factoring and liabilities out of the scope of IAS 39		
Listed shares	8	982 568	-	-	-	-	-	-	-	982 568
Unlisted shares	8	9 500	-	-	-	-	-	-	-	9 500
Trade receivables (net)	11	-	-	-	1 089 286	-	-	-	-	1 089 286
Cash and cash equivalents and deposits	9, 13	-	113 812	-	12 835 999	-	-	-	-	12 949 811
Other financial assets (net)	11	-	-	-	167 592	-	-	-	-	167 592
Derivatives - Currency	10	-	-	-	-	(62 887)	-	-	59 138	(3 749)
Derivatives - Commodity contracts - Metals	10	-	-	12 148	-	(252 977)	-	-	1 134 964	894 135
Trade payables	18	-	-	-	-	-	(914 166)	-	-	(914 166)
Other financial liabilities	18, 19	-	-	-	-	-	(38 935)	(93)	-	(39 028)
		992 068	113 812	12 148	14 092 877	(315 864)	(953 101)	(93)	1 194 102	15 135 949

\* Instruments initially designated as hedging instruments, excluded from hedge accounting, were included in the categories of financial liabilities at fair value through profit or loss

## 29. Financial instruments (continued)

### 29.1 Carrying amount (continued)

		At 31 December 2010							
		Categories of financial instruments							
Classes of financial instruments	Note	Other financial liabilities							Total
		Available-for-sale financial assets	Held-to-maturity investments	Financial assets at fair value through profit or loss*	Loans and receivables	Financial liabilities at fair value through profit or loss*	Financial liabilities measured at amortised cost	Financial liabilities due to factoring and liabilities out of the scope of IAS 39	
Listed shares	8	740 324	-	-	-	-	-	-	<b>740 324</b>
Unlisted shares	8	9 500	-	-	-	-	-	-	<b>9 500</b>
Participation units of investment funds	8	405 193	-	-	-	-	-	-	<b>405 193</b>
Trade receivables (net)	11	-	-	-	1 712 403	-	-	-	<b>1 712 403</b>
Cash and cash equivalents and deposits	9, 11, 13	-	88 244	-	2 946 659	-	-	-	<b>3 034 903</b>
Other financial assets (net)	11	-	-	-	145 417	-	-	-	<b>145 417</b>
Derivatives - Currency	10	-	-	81 718	-	(108 713)	-	-	<b>257 467</b>
Derivatives - Commodity contracts - Metals	10	-	-	2 722	-	(184 404)	-	-	<b>(753 039)</b>
Trade payables	18	-	-	-	-	-	(852 710)	-	<b>(852 710)</b>
Other financial liabilities	18, 19	-	-	-	-	-	(70 656)	(11 455)	<b>(82 111)</b>
		<b>1 155 017</b>	<b>88 244</b>	<b>84 440</b>	<b>4 804 479</b>	<b>(293 117)</b>	<b>(923 366)</b>	<b>(11 455)</b>	<b>4 617 347</b>

\* Instruments initially designated as hedging instruments excluded from hedge accounting were included in the categories of financial assets at fair value through profit or loss and financial liabilities at fair value through profit or loss.

## 29. Financial instruments (continued)

### 29.2 Fair value

Classes of financial instruments	Note	At		At	
		31 December 2011		31 December 2010	
		Carrying amount	Fair Value	Carrying amount	Fair Value
		29.1		29.1	
Listed shares	8	982 568	982 568	740 324	740 324
Unlisted shares*	8	9 500	-	9 500	-
Participation units of investment funds	8	-	-	405 193	405 193
Trade receivables (net)	11	1 089 286	1 089 286	1 712 403	1 712 403
Cash and cash equivalents and deposits	9, 11, 13	12 949 811	12 950 210	3 034 903	3 034 920
Other financial assets (net)	11	167 592	167 592	145 417	145 417
Derivatives – Currency, of which:	10	(3 749)	(3 749)	257 467	257 467
Assets		399 623	399 623	387 047	387 047
Liabilities		(403 372)	(403 372)	(129 580)	(129 580)
Derivatives - Commodity contracts - Metals, of which:	10	894 135	894 135	(753 039)	(753 039)
Assets		1 359 430	1 359 430	310 813	310 813
Liabilities		(465 295)	(465 295)	(1 063 852)	(1 063 852)
Trade payables	18	(914 166)	(914 166)	(852 710)	(852 710)
Other financial liabilities	18, 19	(39 028)	(39 028)	(82 111)	(82 111)

The methods and assumptions used by the Company for measuring the fair value of specific financial instruments are presented in notes 2.2.4.4 Fair value and 3 Important estimates and assumptions.

\*The Company is unable to reliably measure the fair value of shares held in companies which are not listed on active markets, classified as available-for-sale financial assets. In the annual statement of financial position of the Company this group of assets is disclosed at cost less impairment.

## 29. Financial instruments (continued)

### 29.3 Items of income, costs, gains and losses recognised in profit or loss by category of financial instruments

For the period from 1 January 2011 to 31 December 2011		Note	Financial assets/ liabilities measured at fair value through profit or loss	Available-for- sale financial assets	Loans and receivables	Other financial liabilities		Hedging instruments	Total financial instruments
						Financial liabilities measured at amortised cost	Financial liabilities due to factoring and liabilities out of the scope of IAS 39		
Interest income/(costs) recognised in:			-	-	180 081	(288)	(507)	-	179 286
Other operating income	26		-	-	180 081	-	-	-	180 081
Other operating costs	27		-	-	-	(227)	-	-	(227)
Finance costs	28		-	-	-	(61)	(507)	-	(568)
Foreign exchange gains/(losses) recognised in:			-	-	1 006 081	(110 917)	(1 150)	-	894 014
Other operating income	26		-	-	1 006 081	(110 917)	-	-	895 164
Finance costs	28		-	-	-	-	(1 150)	-	(1 150)
Gains/(Losses) on measurement of non- current liabilities recognised in:			-	-	-	(1 989)	-	-	(1 989)
Other operating costs	27		-	-	-	(1 716)	-	-	(1 716)
Finance costs	28		-	-	-	(273)	-	-	(273)
Impairment allowances recognised in:			-	-	(5 605)	-	-	-	(5 605)
Expenses by nature	24		-	-	(297)	-	-	-	(297)
Other operating costs	27		-	-	(5 308)	-	-	-	(5 308)
Reversal of impairment allowances			-	-	910	-	-	-	910
Expenses by nature	24		-	-	856	-	-	-	856
Other operating income	26		-	-	54	-	-	-	54
Adjustment to sales due to hedging transactions		30	-	-	-	-	-	241 565	241 565
Gains/(losses) from disposal of financial instruments recognised in:			-	16 855	(5 897)	-	-	-	10 958
Expenses by nature	24		-	-	(5 897)	-	-	-	(5 897)
Other operating income	26		-	16 855	-	-	-	-	16 855
Gains on measurement and realisation of derivatives		26	1 025 017	-	-	-	-	-	1 025 017
Losses on measurement and realisation of derivatives		27	(704 098)	-	-	-	-	-	(704 098)
<b>Total net gain/(loss)</b>			<b>320 919</b>	<b>16 855</b>	<b>1 175 570</b>	<b>(113 194)</b>	<b>(1 657)</b>	<b>241 565</b>	<b>1 640 058</b>

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Annual financial statements prepared in accordance with IFRS  
as adopted by the European Union  
for the period from 1 January 2011 to 31 December 2011  
(amounts in tables in thousand PLN, unless otherwise stated)

**29. Financial instruments (continued)**

**29.3 Items of income, costs, gains and losses recognised in profit or loss by category of financial instruments (continued)**

For the period from 1 January 2010 to 31 December 2010	Note	Financial assets/ liabilities measured at fair value through profit or loss	Available-for- sale financial assets	Loans and receivables	Other financial liabilities		Hedging instruments	Total financial instruments
					Financial liabilities measured at amortised cost	Financial liabilities due to factoring and liabilities out of the scope of IAS 39		
Interest income/(costs) recognised in:		-	-	59 419	(140)	(485)	-	58 794
Other operating income	26	-	-	59 419	-	-	-	59 419
Other operating costs	27	-	-	-	(24)	-	-	(24)
Finance costs	28	-	-	-	(116)	(485)	-	(601)
Foreign exchange gains/(losses) recognised in:		-	(691)	50 039	(79 793)	459	-	(29 986)
Other operating costs	27	-	(691)	50 039	(79 793)	-	-	(30 445)
Finance costs	28	-	-	-	-	459	-	459
Gains/(losses) on measurement of non- current liabilities recognised in:		-	-	-	(98)	-	-	(98)
Other operating income	26	-	-	-	167	-	-	167
Finance costs	28	-	-	-	(265)	-	-	(265)
Impairment allowances recognised in:		-	-	(108)	-	-	-	(108)
Expenses by nature	24	-	-	(24)	-	-	-	(24)
Other operating costs	27	-	-	(84)	-	-	-	(84)
Reversal of impairment allowances	26	-	-	141	-	-	-	141
Adjustment to sales due to hedging transactions	30	-	-	-	-	-	142 187	142 187
Profit/(losses) from disposal of financial instruments recognised in:		-	4 925	(2 337)	-	-	-	2 588
Expenses by nature	24	-	-	(2 337)	-	-	-	(2 337)
Other operating income	26	-	4 925	-	-	-	-	4 925
Gains on measurement and realisation of derivatives	26	463 604	-	-	-	-	-	463 604
Losses on measurement and realisation of derivatives	27	(1 635 888)	-	-	-	-	-	(1 635 888)
<b>Total net gain/(loss)</b>		<b>(1 172 284)</b>	<b>4 234</b>	<b>107 154</b>	<b>(80 031)</b>	<b>(26)</b>	<b>142 187</b>	<b>(998 766)</b>

## 29. Financial instruments (continued)

### 29.4 Financial instruments recognised at fair value in the statement of financial position

#### 29.4.1 Fair value hierarchy

Classes of financial instruments	Note 29.2	At 31 December 2011	
		Level 1	Level 2
Listed shares		982 568	-
Derivatives - currency, of which:		-	(3 749)
Assets		-	399 623
Liabilities		-	(403 372)
Derivatives financial instruments – metals, of which:		-	894 135
Assets		-	1 359 430
Liabilities		-	(465 295)
Other financial receivables		-	29 834
Other financial liabilities		-	(17 073)

Classes of financial instruments	Note 29.2	At 31 December 2010	
		Level 1	Level 2
Listed shares		740 324	-
Participation units of investment funds		405 193	-
Derivatives - currency, of which:		-	257 467
Assets		-	387 047
Liabilities		-	(129 580)
Derivatives – metals, of which:		-	(753 039)
Assets		-	310 813
Liabilities		-	(1 063 852)
Other financial liabilities		-	(49 690)

#### Methods and – when a valuation technique is used - assumptions applied in determining fair values of each class of financial assets or financial liabilities.

##### Level 3

In 2011, no financial instruments were measured at fair value which were classified to level III.

##### Level 2

###### Other financial receivables and liabilities

Receivables and liabilities due to unsettled derivatives at the end of the reporting period. Their date of settlement falls after the last day of the reporting period. These instruments were measured to fair value, based on the reference price for the settlement of these transactions.

###### Derivatives - currency

In the case of forward currency purchase or sell transactions, forward prices from the maturity dates of individual transactions are used to determine their fair value. Calculation of the forward price for currency exchange rates is based on fixing and appropriate interest rates. Interest rates for currencies and the volatility ratios for exchange rates are from Reuters. The standard German-Kohlhagen model is used to measure European options on currency markets.

###### Derivatives – metals

In the case of forward commodity purchase or sell transactions, forward prices from the maturity dates of individual transactions are used to determine their fair value. In the case of copper, official closing prices from the London Metal Exchange as well as volatility ratios at the end of the reporting period are from Reuters. With respect to silver and gold the fixing price set by the London Bullion Market Association is used, also at the end of the reporting period. In the case of volatility and forward prices, quotations given by Banks/Brokers are used. Forwards and swaps on the copper market are priced based on the forward market curve, and in the case of silver forward prices are calculated based on fixing and the respective interest rates. Levy approximation to the Black-Scholes model is used for Asian options pricing on commodity markets.

## 29. Financial instruments (continued)

### 29.4 Financial instruments recognised at fair value in the statement of financial position (continued)

#### 29.4.1 Fair value hierarchy (continued)

##### Level 1

##### Listed shares

The shares listed on the Warsaw Stock Exchange were measured based on the closing price from 30 December 2011 – the last working day in the reporting period. The shares listed on the TSX Venture Exchange were measured applying a share price and the average National Bank of Poland fixing for the Canadian dollar at the valuation date.

There was no transfer of instruments by the Company between levels 1 and 2 in either the reporting or the comparative periods.

#### 29.4.2 Financial instruments - measure of fair value at level 3 of the fair value hierarchy

Shares in investment funds	Note	At	
		31 December 2011	31 December 2010
<b>Beginning of the period</b>		-	<b>7 930</b>
Gains recognised in other comprehensive income		-	-
Losses recognised in other comprehensive income		-	1 838
Settlement		-	6 092
<b>Total</b>	<b>29.4.1</b>	-	-

There was no transfer by the Company to level 3 of instruments classified to levels 1 and 2, nor was there any transfer of instruments classified to level 3 out of this level in either the reporting period or the comparative periods.

### 30. Financial risk management

The Company is exposed to risk in each area of its activities. Understanding those risks and the principles of their management allows the Company to better meet its objectives.

Financial risk management includes the processes of risk identification, measurement and determination of appropriate methods to deal with those risks.

The Company is predominantly exposed to the following types of financial risk:

- Market risk:
  - Risk of changes in commodity prices,
  - Risk of changes in foreign exchange rates (Currency Risk),
  - Price risk related to investments in debt securities and participation units in investment funds,
  - Price risk related to investments in shares of listed companies,
  - Risk of changes in interest rates (Interest Rate Risk),
- Liquidity risk,
- Credit risk.

An appropriate policy, organisational structure and procedures support the financial risk management process.

#### 30.1 Market risk

##### 30.1.1. Principles of market risk management

The Company declares an active approach to managing its market risk exposure. The objectives of market risk management are:

- To limit fluctuations in profit or loss before tax,
- To increase the probability of meeting budget assumptions,
- To maintain the healthy financial condition of the Company,
- To support the process of undertaking strategic decisions relating to investing activity, with particular attention to sources of capital for this activity.

All the market risk management objectives should be considered as a whole, and their realisation is determined mainly by the internal situation of the Company and market conditions.

The Company applies an integrated approach to market risk management at which it is exposed. This means a comprehensive approach to the whole spectrum of identified market risks, rather than to each of them individually. For example, hedging transactions on the commodity market are related to contracts entered into on the currency market, as hedging prices of metals directly impact the probability of achieving planned revenues from sales, which in turn represent a hedged item for strategies on the currency market. As a result, the Company has significantly greater flexibility in building hedging strategies.

The Company applies a consistent and step-by-step approach to market risk management. Over time consecutive hedging strategies are implemented, embracing an increasing share of production and sales revenues as well as an extended time horizon. Consequently, hedging is possible against unexpected plunges in both copper and silver prices as well as rapid appreciation of the PLN versus the USD. Thanks to this approach, it is also possible to avoid engaging significant volumes or notionals at a single price level.

The Company continuously monitors metal and currency markets, which are the basis for decisions on implementing hedging strategies. The Company applies hedge accounting to hedge the risk of changes of cash flows due to commodity and currency risk.

##### 30.1.1.1 Techniques for market risk management

The primary technique for market risk management is the use of hedging strategies involving derivatives. Apart from this, natural hedging is also used.

All of the potential hedging strategies and the selection of those preferred reflect the following factors: current and forecasted market conditions, the internal situation of the Company, the suitability of instruments to be applied and the cost of hedging.

The Company transacts only those derivatives for which it has the ability to assess their value internally, using standard pricing models appropriate for a particular type of derivative, and which can be traded without significant loss of value with a counterparty other than the one with whom the transaction was initially entered into. In evaluating the market value of a given instrument, the Company relies on information obtained from particular market leading banks, brokers and information services.



### **30. Financial risk management (continued)**

#### **30.1 Market risk (continued)**

##### **30.1.1. Principles of market risk management (continued)**

##### **30.1.1.1 Techniques for market risk management (continued)**

It is permitted to use the following types of instruments:

- Swaps,
- Forwards and futures,
- Options,
- Structures combining the above instruments.

The instruments applied may be, therefore, either of standardised parameters (publicly traded instruments) or non-standardised parameters (over-the-counter instruments).

##### **30.1.1.2 Hedge effectiveness requirement**

Hedging transactions can be entered into only if there is an appropriate derivative for the base instrument traded in a liquid market with a quoted reference price. Prior to the transaction the Company is required to confirm and document the existence of strong negative correlation between changes in value of the reference instrument and changes in value of actually-hedged exposure. Hedge effectiveness is subject to constant evaluation and monitoring.

##### **30.1.1.3 Measurement of market risk**

The Company quantifies its market risk exposure using a consistent and comprehensive measure.

Market risk management is supported by simulations (such as scenario analysis, stress-tests, backtests) and calculated risk measures. The risk measures being used are mainly based on mathematical and statistical modelling, which uses historical and current market data concerning risk factors and takes into consideration the current exposure of the Company to market risk.

Since 2007 "Earnings at Risk" has been used as one of the risk measures employed in market risk management. This measure indicates the lowest possible level of pre-tax profit for a selected level of confidence (for example, with 95% confidence the pre-tax profit for a given year will be not lower than...). The EaR methodology enables the calculation of pre-tax profit incorporating the impact of changes in market prices of copper, silver and foreign exchange rates in the context of budgeted results.

However, due to the fact that no single risk measure possesses the ability to completely reflect reality, mainly because of underlying assumptions concerning market factors, it is customary to employ quantitative models merely as a tool supporting the decision making process and as a source of additional information. Such models are not the only basis for decision making in the market risk management process.

##### **30.1.1.4 Restrictions on entering into hedging transactions**

Due to the risk of unexpected production cutbacks (for example because of force majeure) or failure to achieve planned foreign currency revenues, as well as purchases of metals contained in purchased copper-bearing materials, the Company has set limits with respect to commitment in derivatives:

- up to 70% of monthly copper volume sales,
- up to 80% of monthly silver volume sales,
- up to 70% of monthly foreign-currency revenues from the sale of products.

These limits are in respect both of hedging transactions as well as of the instruments financing these transactions.

Thanks to an integrated approach to market risk management, the Company gains substantially greater flexibility in constructing its hedging strategy. In order to achieve the defined profile of exposure to market risk, it is possible to define/implement a „comprehensive“ hedging strategy, i.e. one which incorporates both the metals and the currency markets.

The maximum time horizon within which the Company makes decisions concerning the hedging of market risk is set up in accordance with the technical and economic planning process, and amounts to 5 years. However, it must be emphasised that regardless of the tool used to measure market risks, the results of such measurement for long time horizons (especially over 2 years) may be subject to significant uncertainty, and therefore are treated as estimates.

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.2 Commodity risk

The Company is exposed to the risk of changes in market prices of copper, silver and gold. The price formulas used in physical delivery contracts are mainly based on average monthly quotations from the London Metal Exchange for copper and from the London Bullion Market for silver and gold. The Company's commercial policy is to set the price base for physical delivery contracts as the average price of the appropriate future month. As a result the Company is exposed to the risk of decline in metals prices from the moment of entering into a sale contract until the moment of setting the contractual average metal price from the month of dispatch.

In a situation where a non-standard formula is used to set the sales price, the Company may enter into transactions (so-called adjustment hedge transactions) which change the price base agreed with the customer to the average price of the appropriate month. These transactions lead to a harmonisation of the base price applied to physical sales of products, and therefore harmonisation of the exposure to the risk of fluctuations in metals prices.

Therefore, the analysis of the Company's exposure to the market risk should be performed on a net basis, i.e. by deducting the volume of metals contained in materials purchased from external sources, from the volume of sales.

Exposure of the Company to commodity risk is presented below:

	For the period			
	from 1 January 2011 to 31 December 2011		from 1 January 2010 to 31 December 2010	
	Sales	Purchases	Sales	Purchases
Copper ['000 tonnes]	567	143	545	130
Silver [tonnes]	1 179	52	1 247	9

Sensitivity of the Company's financial instruments to commodity risk at the end of the reporting period is presented in Note 30.1.7 Sensitivity analysis of commodity and currency risk.

##### 30.1.3 Currency risk

The Company is exposed to the risk of changes in currency rates, as it is generally accepted on commodities markets that physical contracts are either concluded or denominated in USD. However, the base (functional) currency for the Company is the PLN.

As a result, the Company receives the equivalent in PLN or exchanges the USD it receives for PLN. This leads to the risk associated with fluctuations in the USD/PLN exchange rate during the period from the moment of entering into the trade contract to the moment of determining the exchange rate. In a situation wherein foreign clients pay in local currency for the copper or precious metals which they have imported, the Company is also exposed to fluctuations in the exchange rates of other currencies, e.g.: EUR/PLN, GBP/PLN.

Sensitivity of the Company's financial instruments to currency risk at the end of the reporting period is presented in Note 30.1.7 Sensitivity analysis of commodity and currency risk.

##### 30.1.4 Commodity and currency risk management

In 2011 copper price hedging strategies represented approx. 35% (in 2010 33%) of the sales of this metal realised by the Company. With respect to silver sales this figure amounted to approx. 9% (in 2010 18%). In the case of the currency market, hedged revenues from sales represented approx. 19% (in 2010 16%) of total revenues from sales realised by the Company.

In 2011 the Company implemented copper price hedging strategies with a total volume of 151 thousand tonnes and a time horizon falling from September 2011 to December 2013. The Company made use of options (Asian options), including: option strategies (collars and producer's puts). In addition, the Company performed a restructure, implemented in the first and third quarters of 2010, of seagull options for 2012 with a total volume of 97.5 thousand tonnes through the buyback of sold puts. Restructure enables the full use of put options purchased within this structure in the case of any decrease in the price of copper in 2012.

In 2011 the Company implemented silver price hedging strategies with a total volume of 14.4 million troz and a time horizon falling in 2012 and 2013. The Company made use of options (Asian options) including puts, seagulls and collars. Additionally, the Company performed a restructure, implemented in the analysed period, of a collar strategy for 2012, through the buyback of sold calls for 3.6 million troz, and simultaneously sold puts of the same nominal amount and with an execution price below the price of the put options held (from the collar structure). A put spread structure was thereby gained. Restructure guarantees greater flexibility in the selection of derivatives implemented for 2012 and enables full participation in any eventual increases in the price of silver in this period for the hedged nominal amount of 3.6 million troz. In addition – in case of a deep fall in prices in this period – it restricts benefits from the put options held to the level of executed put options sold.

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.4 Commodity and currency risk management (continued)

In the case of the forward currency market, in 2011 the Company implemented transactions hedging revenues from sales with a total nominal amount of USD 1 920 million and a time horizon falling in years 2012-2014. The Company made use of options (European options), and option strategies (collars and seagulls).

During this period no adjustment hedge transactions were implemented on the copper, silver or currency market.

The Company remains hedged for a portion of copper sales planned in the period from January to December 2012 (205.5 thousand tonnes), in 2013 (61.5 thousand tonnes), and also for a portion of silver sales planned in the period from January to December 2012 (10.8 million troz) and in 2013 (3.6 million troz). With respect to revenues from sales (currency market) the Company holds a hedging position in 2012 (USD 960 million), in 2013 (USD 960 million) and 2014 (USD 360 million).

Following is a condensed table of hedging positions, by type of hedged asset and instruments used at 31 December 2011. The hedged nominal/volume in the months included in the presented periods is equally balanced.

#### HEDGING POSITION (condensed information) – COPPER MARKET

HEDGING POSITION (Condensed Information) – COPPER MARKET							
Period	Instrument		Volume [tonnes]	Execution price [USD/t]	Average weighted premium [USD/t]	Effective hedge price [USD/t]	
I half of 2012	Collar <sup>1</sup>	Sold call option	19 500	9 300	(447)	6 453	
		Purchased put option		6 900		participation restricted to 9 300	
	Collar <sup>1</sup>	Sold call option	19 500	9 000	(478)	6 322	
		Purchased put option		6 800		participation restricted to 9 000	
	Collar <sup>1</sup>	Sold call option	19 500	9 500	(440)	6 760	
		Purchased put option		7 200		participation restricted to 9 500	
	Producer's puts <sup>2</sup>		19 500	8 000	9.90% <sup>3</sup>	minimal effective hedging price 7 279	
	Producer's puts <sup>2</sup>		24 750	8 300	8.66% <sup>3</sup>	minimal effective hedging price 7 639	
Total		102 750					
II half of 2012	Collar <sup>1</sup>	Sold call option	19 500	9 300	(454)	6 446	
		Purchased put option		6 900		participation restricted to 9 300	
	Collar <sup>1</sup>	Sold call option	19 500	9 000	(459)	6 341	
		Purchased put option		6 800		participation restricted to 9 000	
	Collar <sup>1</sup>	Sold call option	19 500	9 500	(453)	6 747	
		Purchased put option		7 200		participation restricted to 9 500	
	Producer's puts <sup>2</sup>		19 500	8 500	8.74% <sup>3</sup>	minimal effective hedging price 7 817	
	Producer's puts <sup>2</sup>		24 750	8 300	8.66% <sup>3</sup>	minimal effective hedging price 7 639	
Total		102 750					
TOTAL 2012		205 500					
I half of 2013	Seagull <sup>2</sup>	Sold call option	19 500	9 500	(383)	6 817	
		Purchased put option		7 200		restricted to 4 700	
		Sold put option		4 700		participation restricted to 9 500	
	Collar	Sold call option	10 500	12 000	(460)	8 040	
		Purchased put option		8 500		participation restricted to 12 000	
	Collar	Sold call option	10 500	11 500	(333)	7 867	
		Purchased put option		8 200		participation restricted to 11 500	
	Total		40 500				
II half of 2013	Collar	Sold call option	10 500	12 000	(460)	8 040	
		Purchased put option		8 500		participation restricted to 12 000	
	Collar	Sold call option	10 500	11 500	(333)	7 867	
		Purchased put option		8 200		participation restricted to 11 500	
	Total		21 000				
TOTAL 2013		61 500					

<sup>1</sup> Tables presenting the condensed list of open hedging positions, include restructured items: the type of instrument was changed from seagull to collar. The cost of restructuring (premium for repurchase of options) was added to the cost of implementation (i.e. the average weighted premium) and the effective hedge price/exchange rate was changed.

<sup>2</sup> Due to current hedge accounting laws, transactions embedded within a producer's put – a purchased put option – are shown in the table containing a detailed list of derivatives positions – „Hedging instruments”, while call options are shown in the table „Trade instruments”, transactions included in the seagull structure – purchased put options and sold call options – are shown in the table „Hedging instruments”; while sold put options are shown in the table „Trade instruments”.

<sup>3</sup> Payable at the moment of settlement.

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.4 Commodity and currency risk management (continued)

#### HEDGING POSITION (condensed information)– SILVER MARKET

Period	Instrument		Volume [million troz]	Execution price [USD/troz]	Average weighted premium [USD/troz]	Effective hedge price [USD/troz]
I half of 2012	Purchased put option		1.80	30.00	(2.89)	27.11
	Put spread <sup>4</sup>	Purchased put option	1.80	40.00	(1.18)	38.82
		Sold put option <sup>5</sup>		19.80		restricted to 19.80
	Collar	Sold call option	1.80	62.00	(1.63)	35.37
		Purchased put option		37.00		participation restricted to 62.00
	Total		5.40			
II half of 2012	Purchased put option		1.80	30.00	(2.89)	27.11
	Put spread <sup>4</sup>	Purchased put option	1.80	40.00	(1.18)	38.82
		Sold put option <sup>5</sup>		19.80		restricted to 19.80
	Collar	Sold call option	1.80	62.00	(1.63)	35.37
		Purchased put option		37.00		participation restricted to 62.00
	Total		5.40			
TOTAL 2012			10.80			
I half of 2013	Seagull <sup>5</sup>	Sold call option	1.80	65.00	(1.98)	38.02
		Purchased put option		40.00		restricted to 20.00
		Sold put option		20.00		participation restricted to 65.00
	Total		1.80			
II half of 2013	Seagull <sup>5</sup>	Sold call option	1.80	65.00	(1.98)	38.02
		Purchased put option		40.00		restricted to 20.00
		Sold put option		20.00		participation restricted to 65.00
	Total		1.80			
TOTAL 2013			3.60			

#### HEDGING POSITION (condensed information) – CURRENCY MARKET

Period	Instrument		Notional [million USD]	Execution price [USD/PLN]	Average weighted premium [PLN per 1 USD]	Effective hedge price [USD/PLN]
I half of 2012	Seagull <sup>5</sup>	Sold call option	90	4.4000	(0.0990)	3.2010 restricted to 2.70 participation restricted to 4.40
		Purchased put option		3.3000		
		Sold put option		2.7000		
	Collar	Sold call option	90	4.5000	(0.1527)	3.2473 participation restricted to 4.50
		Purchased put option		3.4000		
	Purchased put option		360	2.6000	(0.0947)	2.5053
	Total		540			
II half of 2012	Seagull <sup>5</sup>	Sold call option	90	4.4000	(0.0767)	3.2233 restricted to 2.70 participation restricted to 4.40
		Purchased put option		3.3000		
		Sold put option		2.7000		
	Collar	Sold call option	90	4.5000	(0.1473)	3.2527 participation restricted to 4.50
		Purchased put option		3.4000		
	Collar	Sold call option	240	4.2000	(0.0650)	3.1350 participation restricted to 4.20
		Purchased put option		3.2000		
	Total		420			
TOTAL 2012		960				

<sup>4</sup> Tables presenting the condensed list of open hedging positions, include restructured items: the type of instrument was changed from collar to put spread. The cost of restructuring (premium for repurchase of options) was added to the cost of implementation (i.e. the average weighted premium) and the effective hedge price/exchange rate was changed.

<sup>5</sup> Due to current hedge accounting laws, transactions embedded within a seagull – a purchased put option or a sold call option – are shown in the table „Hedging instruments“, while sold put options are shown in the table „Trade instruments“; sold put options included in the put spread structure, also are shown in the table „Trade instruments“.

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.4 Commodity and currency risk management (continued)

#### HEDGING POSITION (condensed information) – CURRENCY MARKET (continued)

<b>I half of 2013</b>	Seagull <sup>6</sup>	Sold call option	240	4.0000	(0.0332)	3.1168 restricted to 2.60 participation restricted to 4.00
		Purchased put option		3.1500		
		Sold put option		2.6000		
	Collar	Sold call option	240	4.2000	(0.0650)	3.1350 participation restricted to 4.20
		Purchased put option		3.2000		
	<b>Total</b>		<b>480</b>			
<b>II half of 2013</b>	Seagull <sup>6</sup>	Sold call option	240	4.0000	(0.0230)	3.1270 restricted to 2.60 participation restricted to 4.00
		Purchased put option		3.1500		
		Sold put option		2.6000		
	Collar	Sold call option	240	4.2000	(0.0650)	3.1350 participation restricted to 4.20
		Purchased put option		3.2000		
	<b>Total</b>		<b>480</b>			
	<b>TOTAL 2013</b>		<b>960</b>			
<b>I half of 2014</b>	Seagull <sup>6</sup>	Sold call option	180	4.5000	(0.0506)	3.4494 restricted to 2.70 participation restricted to 4.50
		Purchased put option		3.5000		
		Sold put option		2.7000		
	<b>Total</b>		<b>180</b>			
<b>II half of 2014</b>	Seagull <sup>6</sup>	Sold call option	180	4.5000	(0.0345)	3.4655 restricted to 2.70 participation restricted to 4.50
		Purchased put option		3.5000		
		Sold put option		2.7000		
	<b>Total</b>		<b>180</b>			
	<b>TOTAL 2014</b>		<b>360</b>			

##### 30.1.5. Impact of derivatives on the Company's statement of financial position

As at 31 December 2011, the fair value of open positions in derivatives amounted to PLN 890 386 thousand, PLN 1 759 053 thousand relate to financial assets and PLN 868 667 thousand relate to financial liabilities.

Derivatives whose date of settlement was 4 January 2012 were measured at fair value and accounted for in trade and other receivables as receivables due to unsettled derivatives or trade and other payables as payables due to unsettled derivatives.

The fair value of payables/liabilities due to unsettled derivatives, whose date of settlement was 4 January 2012 amounted to:

- PLN 29 834 thousand accounted for in other finance receivables (Note 11)
- PLN 17 073 thousand accounted for in other finance liabilities (Note 18).

Other information concerning derivatives is presented in Note 10 Derivatives and in Note 29 Financial instruments.

##### 30.1.6. Impact of derivatives on the Company's profit or loss and other comprehensive income

In 2011, the result on derivatives amounted to PLN 562 484 thousand. The effective portion of the change in the fair value of hedging instruments that was transferred from accumulated other comprehensive income to profit or loss in the reporting period, as an adjustment from reclassification, increased revenues from sales by PLN 241 565 thousand. The gains on the measurement of derivatives amounted to PLN 257 538 thousand, while the gains on the realisation of derivatives amounted to PLN 63 381 thousand. Adjustment to other operating income arising from the measurement of derivatives results mainly from changes of the time value of options, which will be settled in future periods, and in accordance with the hedge accounting principles applied by the Company, the change in the time value of options is not recognised in accumulated other comprehensive income.

<sup>6</sup> Due to current hedge accounting laws, transactions embedded within a seagull – a purchased put option and a sold call option – are shown in the table „Hedging instruments“, while sold put options are shown in the table „Trade instruments“.

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.6. Impact of derivatives on the Company's profit or loss and other comprehensive income (continued)

The impact of derivatives on the profit or loss of the current and comparable periods is presented below:

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Impact on sales</b>	<b>241 565</b>	<b>142 187</b>
<b>Impact on other operating activities</b>	<b>320 919</b>	<b>(1 172 284)</b>
Gains/(losses) from realisation of derivatives	63 381	(135 420)
Gains/(losses) from measurement of derivatives	257 538	(1 036 864)
<b>Total impact of derivatives on profit or loss:</b>	<b>562 484</b>	<b>(1 030 097)</b>

The Company accounts for cash flow hedging instruments according to the principles presented in note 2.2.4.7 of Main accounting policies – Hedge accounting. Those principles require recognition in other comprehensive income of the effective portion of the change in the fair value of hedging transactions during the period in which these transactions are designated as a hedge of future cash flows. The amounts recognised in accumulated other comprehensive income are subsequently transferred to profit or loss in the period in which the hedged transaction is settled.

In 2011 the Company recognised in gains due to the ineffective portion of cash flow hedges – the amount of PLN 259 897 thousand (in 2010: loss PLN 1 328 573 thousand), of which PLN 221 660 thousand is a gain on the measurement of hedging instruments (in 2010: loss PLN 1 170 400 thousand) and PLN 38 237 thousand is a gain on the realisation of the ineffective portion of hedging instruments (in 2010: loss PLN 158 173 thousand).

The effectiveness of hedging instruments used by the Company during the period is evaluated and measured by comparing the changes in the forward prices of hedged items with the changes in the prices of forward contracts or – in the case of options – the changes in the intrinsic value of options.

The tables below present the balances and movements in accumulated other comprehensive income resulting from the recognition of the effective portion of the gain or loss from changes in the fair value of derivatives designated as hedging future cash flows.

#### AMOUNTS RECOGNISED IN OTHER COMPREHENSIVE INCOME

	At	
	31 December 2011	31 December 2010
<b>Accumulated other comprehensive income</b>		
– commodity price risk hedging transactions (copper and silver) – derivatives	708 992	(98 940)
<b>Accumulated other comprehensive income</b>		
– currency risk hedging transactions – derivatives	-	209 772
<b>Total accumulated other comprehensive income</b>		
<b>- financial instruments hedging future cash flows (excluding the deferred tax effects)</b>	<b>708 992</b>	<b>110 832</b>

#### Gains/(losses) on derivatives hedging future cash flows recognised in other comprehensive income

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Accumulated gain or loss achieved on financial instruments hedging future cash flows at the beginning of the reporting period</b>	<b>110 832</b>	<b>155 233</b>
Amount recognised in the reporting period due to hedging transactions	839 725	97 786
Amount reclassified from accumulated other comprehensive income to revenues from sales	(241 565)	(142 187)
<b>Accumulated other comprehensive income due to instruments hedging future cash flows at the end of the reporting period (excluding the deferred tax effects)</b>	<b>708 992</b>	<b>110 832</b>

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.7. Sensitivity analysis of commodity and currency risk

In accordance with "Market risk management policy", the Company identifies the following major market risks to which it is exposed.

Currently the Company is mainly exposed to the risk of changes in copper and silver prices and changes in the USD/PLN, EUR/PLN and GBP/PLN currency exchange rates.

For sensitivity analysis of commodity risk factors (copper and silver) the mean reverting Schwartz model (the geometrical Ornstein-Uhlenbeck process) is used, while the Black-Scholes model (the geometrical Brownian motion) is used for the USD/PLN, EUR/PLN and GBP/PLN exchange rates. Quantiles from the model at the levels of 5% and 95% have been used as potential changes in a half-year time horizon. Commodity models have been calibrated to historical prices adjusted for the effects of the PPI inflation index in the USA, while currency models have been calibrated to the current structure of forward interest rates.

Potential changes in prices and currency rates have been presented in terms of percentages of the prices and currency rates used in the fair value measurement of financial instruments at the end of the reporting period. Following is a sensitivity analysis for each significant type of market risk to which the Company was exposed at the end of the reporting period, showing what the impact would be on profit or loss and equity of potential changes in specific risk factors divided by classes of financial assets and financial liabilities.

Scope of historical data (daily data):

- for copper: 01 January 1978 to 30 December 2011 – settlement prices
- for silver: 01 January 1978 to 30 December 2011 – fixing prices
- for USD/PLN, EUR/PLN and GBP/PLN exchange rates: 01 January 2000 to 30 December 2011 – fixing NBP.

The parameters of the Schwartz model were calibrated by the method of highest reliability to real historical prices (adjusted by the PPI inflation index in the USA for Cu and Ag). The trend in the Black-Scholes model (currencies) was calibrated to the forward market curve for interest rates, while variability is the exponentially weighted historical variability.

Potential price changes at the end of the reporting period:

31 December 2011	Copper	Silver	USD/PLN	EUR/PLN	GBP/PLN
SPOT / FIX	7 590	28.18	3.4174	4.4168	5.2691
DOWN 95%	5 196	17.06	2.8094	3.8497	4.5139
	-32%	-39%	-18%	-13%	-14%
UP 95%	10 254	41.89	4.1824	5.1795	6.2085
	35%	49%	22%	17%	18%

31 December 2010	Copper	Silver	USD/PLN	EUR/PLN	GBP/PLN
SPOT / FIX	9 650	30.63	2.9641	3.9603	4.5938
DOWN 95%	6 461	19.71	2.4294	3.4875	3.9389
	-33%	-36%	-18%	-12%	-14%
UP 95%	12 965	41.91	3.6292	4.5628	5.4067
	34%	37%	22%	15%	18%

In analysing the sensitivity of the item "Derivatives – Currency" and "Derivatives – Commodity contracts - Metals" it should be noted that the Company holds a position in derivatives hedging future cash flows from the sale of copper and silver. It should also be noted that the Company is exposed to risk in respect of the planned volume of copper and silver sales from its own production, adjusted by its position in hedging instruments.

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.7. Sensitivity analysis of commodity and currency risk (continued)

#### Currency structure of financial instruments exposed to market risk at 31 December 2011

FINANCIAL ASSETS AND LIABILITIES	VALUE AT RISK Currency structure			
	['000 PLN]	['000 USD]	['000 EUR]	['000 GBP]
Trade receivables (net)	854 533	145 610	79 616	1 002
Cash and cash equivalents and deposits	8 008 373	1 795 587	387 009	30 896
Other financial assets (net)	53 874	9 423	2 299	2 186
Derivatives – Currency contracts	(3 749)	-	-	-
Derivatives – Commodity contracts - Metals	894 135	261 642	-	-
Trade payables	(41 782)	(4 167)	(6 235)	(1)
Other financial liabilities	(27 284)	(6 845)	(881)	-

#### Currency structure of financial instruments exposed to market risk at 31 December 2010

FINANCIAL ASSETS AND LIABILITIES	VALUE AT RISK Currency structure			
	['000 PLN]	['000 USD]	['000 EUR]	['000 GBP]
Trade receivables (net)	1 385 755	292 965	87 938	36 815
Cash and cash equivalents and deposits	457 225	96 018	35 846	6 674
Other financial assets (net)	27 482	620	5 233	1 070
Derivatives – Currency contracts	257 467	lack of data	-	-
Derivatives – Commodity contracts - Metals	(753 039)	(254 053)	-	-
Trade payables	(104 620)	(24 957)	(7 738)	-
Other financial liabilities	(70 767)	(18 275)	(3 322)	(750)



KGHM Polska Miedź S.A.  
Annual financial statements prepared in accordance with IFRS  
as adopted by the European Union  
for the period from 1 January 2011 to 31 December 2011  
(amounts in tables in thousand PLN, unless otherwise stated)

**30. Financial risk management (continued)**

**30.1 Market risk (continued)**

**30.1.7. Sensitivity analysis of commodity and currency risk (continued)**

**SENSITIVITY ANALYSIS AS AT 31 December 2011**

FINANCIAL ASSETS AND LIABILITIES	VALUE AT RISK	31.12.2011  CARRYING AMOUNT	CURRENCY RISK												COMMODITY RISK							
			USD/PLN				EUR/PLN				GBP/PLN				COPPER PRICES [USD/t]				SILVER PRICES [USD/troz]			
			4.18		2.81		5.18		3.85		6.21		4.51		10 254		5 196		41.89		17.06	
			+ 22%		- 18%		+ 17%		- 13%		+18%		-14%		+ 35%		- 32%		+ 49%		- 39%	
			Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity
	[ '000 PLN]	[ '000 PLN]																				
Trade receivables (net)	854 533	1 089 286	90 227		(71 710)		49 185		(36 572)		762		(613)									
Cash and cash equivalents and deposits	8 008 373	12 949 811	1 112 636		(884 291)		239 089		(177 773)		23 509		(18 899)									
Other financial assets (net)	53 874	167 592	5 839		(4 641)		1 420		(1 056)		1 663		(1 337)									
Derivatives – Currency contracts	(3 749)	(3 749)	(539 646)	(334 240)	109 897	561 586																
Derivatives – Commodity contracts – Metals	894 135	894 135	39 064	161 092	(31 047)	(128 031)									(624 797)	(758 310)	(216 349)	1 884 125	70 169	(412 651)	(151 731)	544 558
Trade payables	(41 782)	914 166	(2 582)		2 052		(3 852)		2 864													
Other financial liabilities	(27 284)	39 028	(4 242)		3 371		(544)		405													
IMPACT ON PROFIT OR LOSS			701 296		(876 369)		285 298		(212 132)		25 934		(20 849)		(624 797)		(216 349)		70 169		(151 731)	
IMPACT ON OTHER COMPREHENSIVE INCOME				(173 148)		433 555									(758 310)		1 884 125		(412 651)		544 558	

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**30. Financial risk management (continued)**

**30.1 Market risk (continued)**

**30.1.7. Sensitivity analysis of commodity and currency risk (continued)**

SENSITIVITY ANALYSIS AS AT 31 December 2010																					
FINANCIAL ASSETS AND LIABILITIES	VALUE AT RISK	31.12.2010  CARRYING AMOUNT	CURRENCY RISK										COMMODITY RISK								
			USD/PLN				EUR/PLN				GBP/PLN		COPPER PRICES [USD/t]				SILVER PRICES [USD/troz]				
			3.63		2.43		4.56		3.49		5.41		3.94		12 965		6 461		41.91		19.71
			+ 22%		- 18%		+ 15%		- 12%		+18%		-14%		+ 34%		- 33%		+ 37%		- 36%
			Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	Profit or (loss)	Equity	
Trade receivables (net)	1 385 755	1 712 403	157 829		(126 885)		42 916		(33 677)		24 241		(19 529)								
Cash and cash equivalents and deposits	457 225	3 034 903	51 728		(41 586)		17 494		(13 728)		4 394		(3 540)								
Other financial assets (net)	27 482	145 417	334		(269)		2 554		(2 004)		705		(568)								
Derivatives – Currency contracts	257 467	257 467	(158 080)	(104 629)	(127 999)	529 874															
Derivatives – Commodity contracts - Metals	(753 039)	(753 039)	(121 136)	(15 730)	97 386	12 646								182 070	(1 827 586)	612 600	750 806	(1 278)	14 128		
Trade payables	(104 620)	(852 710)	(13 445)		10 809		(3 779)		2 964												
Other financial liabilities	(70 767)	(82 111)	(9 845)		7 915		(1 621)		1 272		(494)		398								
IMPACT ON PROFIT OR LOSS			(92 615)		(180 629)		57 564		(45 173)		28 846		(23 239)		182 070		612 600		(1 278)		
IMPACT ON OTHER COMPREHENSIVE INCOME				(120 359)		542 520								(1 827 586)		750 806			1 744		

### 30. Financial risk management (continued)

#### 30.1 Market risk (continued)

##### 30.1.8 Price risk related to investments in debt securities and participation units of investment funds

As at 31 December 2011, the Company held no participation units of investment funds and debt securities.

##### 30.1.9 Price risk related to the purchase of shares of listed companies

At 31 December 2011, the carrying amount of shares held by the Company which were listed on the Warsaw Stock Exchange and on the TSX Ventures Exchange was PLN 982 568 thousand. These investments expose the Company to the risk of a substantial change in accumulated other comprehensive income due to changes in the prices of the shares held, caused by the current macroeconomic situation.

#### Sensitivity analysis of listed companies shares to price changes

Shares of one company are listed on the Warsaw Stock Exchange and shares of one company are listed on the TSX Venture Exchange.

	At 31 December 2011 CARRYING AMOUNT (in PLN '000)	Percentage change of share price		At 31 December 2010 CARRYING AMOUNT [PLN '000]	Percentage change of share price	
		+50%	-14%		+22%	-36%
Listed shares	982 568			740 324		
IMPACT ON OTHER COMPREHENSIVE INCOME		491 284	(137 560)		162 871	(266 517)

##### 30.1.10 Interest rate risk

Interest rate risk is the danger of the negative impact of changes in interest rates on the financial position of the Company. The Company is exposed to this risk due to loans granted and periodically unallocated cash and cash equivalents, which are invested on the financial market (mainly bank deposits). A loan was granted, with interest based on the variable interest rate WIBOR 1M (balance at 31 December 2011: PLN 40 968 thousand, of which long-term loans amount to PLN 35 210 thousand, short-term to PLN 5 758 thousand). The decrease in market interest rates results in a decrease in the expected amount of income due to decreased cash flow due to loans granted and interest income on periodically unallocated cash and cash equivalents.

The Company, both during the reporting period as well as the comparable period, did not make use of interest rate risk hedging instruments.

#### 30.2 Credit risk

Credit risk is defined as the risk that counterparties will not be able to meet their contractual obligations. Exposure to credit risk is related to three main areas:

- the creditworthiness of the customers with whom physical sale transactions are undertaken,
- the creditworthiness of the financial institutions (banks/brokers) with whom, or through whom, hedging transactions are undertaken,
- the creditworthiness of companies in which equity investments are made.

Areas in which credit risk exposure has different characteristics from those mentioned above:

- cash and cash equivalents and deposits,
- derivatives,
- trade receivables,
- loans granted,
- debt securities and participation units of investment funds,
- guaranties granted.

### 30. Financial risk management (continued)

#### 30.2 Credit risk (continued)

##### 30.2.1 Credit risk related to cash and cash equivalents and bank deposits

All entities with which deposit transactions are entered into by the Company operate in the financial sector. These are solely banks registered in Poland or operating in Poland as branches of foreign banks, which belong to European and American financial institutions with the highest<sup>7</sup> 20% of deposits (as at 31 December 2010 – 2% of deposits), medium-high<sup>8</sup> 52% of deposits (as at 31 December 2010 – 89% of deposits) and medium<sup>9</sup> credit ratings 28% of deposit (as at 31 December 2010 – 9% of deposits), an appropriate level of equity and a strong, stable market position. As at 31 December 2011 the maximum exposure of the Company to a single bank in respect of deposited cash and cash equivalents amounts to 25% (as at 31 December 2010 – 27%).

##### 30.2.2 Credit risk related to derivative transactions

All entities with which derivative transactions were entered into by the Company in 2011 operated in the financial sector. These were financial institutions (mainly banks), with the highest (22.2%), medium-high (72.2%) or medium (5.6%) credit ratings. Based on fair value at 31 December 2011, the maximum share of a single entity with respect to credit risk arising from derivative transactions entered into by the Company amounted to 23.6%.

All entities with which derivative transactions were entered into in 2010 by the Company operated in the financial sector. These are financial institutions (mainly banks), with the highest (40.7%), medium-high (48.2%) or medium (11.1%) credit ratings. Based on fair value at 31 December 2010, the maximum share of a single entity with respect to derivative transactions entered into by the Company amounted to 30%.

#### Measurement of derivative transactions entered into by the Company<sup>10</sup>

	At	
	31 December 2011	31 December 2010
<b>Balance on the measurement of derivatives</b>	<b>903 147</b>	<b>(545 262)</b>
Financial assets	1 788 887	697 860
Financial liabilities	(885 740)	(1 243 122)

Due to diversification of risk in terms both of the nature of individual entities and of their geographical location, as well as to cooperation with highly-rated financial institutions, and also taking into consideration the fair value of assets and liabilities arising from derivative transactions, the Company is not materially exposed to credit risk as a result of derivative transactions entered into.

In order to reduce cash flows as well as credit risk, the Company carries out net settlement (based on framework agreements entered into with its customers) to the level of the positive balance of fair value measurement of transactions in derivatives with a given counterparty.

<sup>7</sup> By highest rating is meant a rating from AAA to AA- as determined by Standard & Poor's and Fitch, and from Aaa to Aa3 as determined by Moody's.

<sup>8</sup> By medium-high rating is meant a rating from A+ to A- as determined by Standard & Poor's and Fitch, and from A1 to A3 as determined by Moody's.

<sup>9</sup> By medium rating is meant a rating from BBB+ to BBB- as determined by Standard & Poor's and Fitch, and from Baa1 to Baa3 as determined by Moody's.

<sup>10</sup> The measurement of transactions includes the measurement of both open positions as well as transactions which were settled:

- on 4 January 2012, which were presented in the Company's statement of financial position under other unsettled derivative instruments receivables/payables (Note 11, 18) – balance as at 31 December 2011.

- on 5 January 2011, which were presented in the Company's statement of financial position at 31 December 2010 under other financial liabilities – balance as at 31 December 2010.

### 30. Financial risk management (continued)

#### 30.2 Credit risk (continued)

##### 30.2.3 Credit risk related to trade and other financial receivables

The Company has been cooperating for many years with a number of geographically diversified clients. The vast majority of sales go to EU countries.

##### **Geographical concentration of credit risk for trade receivables arising from sales of copper and silver in the Company:**

	At					
	31 December 2011			31 December 2010		
	Poland	EU (excl. Poland)	Other Countries	Poland	EU (excl. Poland)	Other Countries
Net receivables from sales of copper and silver	23.1%	49.5%	27.4%	34.9%	34.0%	31.1%

The Company makes the majority of its sales transactions based on prepayments. The Company monitors the creditworthiness of all its customers<sup>11</sup> on an on-going basis, in particular those to whom buyer's credit has been granted.

Buyer's credit is only provided to proven, long-term customers, while sales of products to new customers are always secured. The Company has secured the majority of its receivables by promissory notes<sup>12</sup>, frozen funds on bank accounts, registered pledges<sup>13</sup>, bank guarantees, mortgages, letters of credit and documentary collection. Additionally, the majority of customers who hold buyer's credit on contracts have ownership rights confirmed by a date certain<sup>14</sup>.

To reduce the risk of insolvency by its customers, the Company has entered into a receivables insurance contract, which covers receivables from entities with buyer's credit which have not provided strong collateral or have provided collateral which does not cover the total amount of the receivables. Taking into account the collateral held and the credit limits received from the insurance company, at 31 December 2011 the Company had secured 82.4% of its trade receivables.

The total value of the Company's net trade receivables as at 31 December 2011, excluding the fair value of collaterals, in respect of which the Company may be exposed to credit risk, amounts to PLN 1 089 286 thousand (at 31 December 2010: PLN 1 712 403 thousand).

The concentration of credit risk in the Company results from the fact that key clients (the majority of whom operate within the European Union) are allowed extended terms of payment. Consequently, at 31 December 2011 the balance of receivables from 7 of the Company's largest clients, in terms of trade receivables at the end of the reporting period, represented 51.5% of the trade receivables balance (at 31 December 2010: 66%). Despite the concentration of this type of risk, the Company believes that due to the availability of historical data and the many years of experience cooperating with its clients, as well as to the hedging used, the level of credit risk is low.

##### 30.2.4 Credit risk related to loans granted

At 31 December 2011 the carrying amount of loans granted by the Company amounted to PLN 40 968 thousand (including interest of PLN 728 thousand). The loans were granted to the company Energetyka Sp. z o.o.

KGHM Polska Miedź S.A. continuously monitors the assets and financial results of the borrower. At present credit risk of the loan is immaterial.

<sup>11</sup> Due to the lack of data necessary to measure credit risk, risk arising from derivatives transactions entered into by customers was not taken into consideration.

<sup>12</sup> In order to speed up any potential collection of receivables, a promissory note is usually accompanied by a notarial enforcement declaration.

<sup>13</sup> At the end of the reporting period date the Company held pledges on aggregate tangible assets or rights representing an organisational whole, whose elements (variable) are recognised in a customer's trade accounts.

<sup>14</sup> A confirmed notarial clause which is applied in trade contracts means that rights to ownership of merchandise are transferred to the buyer only after payment is received despite physical delivery. Application of this clause is aimed solely at hedging credit risk and simplifying any eventual legal claims with regard to deliveries. The Company transfers the substantial risks and rewards of ownership, and therefore such transactions are treated as sales and accounted for as income.

### 30. Financial risk management (continued)

#### 30.2 Credit risk (continued)

##### 30.2.5 Credit risk related to investments in debt securities and participation units of investment funds

At 31 December 2011, the Company held no participation units of investment funds or debt securities.

##### 30.2.6 Other information related to credit risk

**Aging analysis of financial assets overdue as at the end of the reporting period, for which no impairment loss has been recognised**

	At 31 December 2011					
	Total value	Up to 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	Over 1 year
Trade receivables	46 677	45 266	12	1	1	1 397
Other receivables	367	125	1	-	240	1

	At 31 December 2010					
	Total value	Up to 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	Over 1 year
Trade receivables	42 775	36 891	61	-	5 544	279
Other receivables	516	245	270	1	-	-

Except for trade receivables and other financial receivables, no other classes of financial instruments were identified as overdue but not impaired at the end of the reporting period.

Allowances for impairment of financial assets, category: loans and financial receivables, by class are presented in the tables below:

#### Allowances for impairment of loans and financial receivables

##### a) trade receivables (category: loans and receivables)

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Impairment allowance at the beginning of the period</b>	<b>11</b>	<b>22 611</b>	<b>21 769</b>
Impairment allowance recognised in profit or loss	24	297	27
Impairment allowance reversed through profit or loss	24	(856)	-
Revaluation of impairment allowance on foreign exchange differences		3 276	822
Impairment allowance utilised during the period		(3)	(7)
<b>Impairment allowance at the end of the period</b>	<b>11</b>	<b>25 325</b>	<b>22 611</b>

##### b) other financial assets (category: loans and receivables)

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Impairment allowance at the beginning of the period</b>		<b>6 989</b>	<b>3 813</b>
Impairment allowance recognised in profit or loss	27	5 308	84
Impairment allowance reversed through profit or loss	26	(54)	(141)
Revaluation of impairment allowance on foreign exchange differences		205	50
Impairment allowance utilised during the period		-	(7)
Reversal of impairment allowance on costs of legal proceedings		(10)	(3)
Impairment allowance recognised on costs of legal proceedings		-	3 193
Other		(3 203)	-
<b>Impairment allowance at the end of the period</b>	<b>11</b>	<b>9 235</b>	<b>6 989</b>

### 30. Financial risk management (continued)

#### 30.2.6 Other information related to credit risk (continued)

##### c) shares (category: available-for-sale financial assets)

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>Impairment allowance at the beginning of the period</b>		<b>58 579</b>	<b>58 579</b>
Reclassification of shares in subsidiaries to available-for-sale financial assets		-	-
<b>Impairment allowance at the end of the period</b>	<b>8</b>	<b>58 579</b>	<b>58 579</b>

### 30.3 Liquidity risk and capital management

The Company is exposed to financial liquidity risk, where financial liquidity is understood as the ability to settle financial liabilities on time.

The Company manages its financial liquidity in accordance with policy „Financial Liquidity Management Policy” approved by the Management Board. This document describes in a comprehensive manner the process of managing financial liquidity in the Company, based on best practice for such procedures and instruments.

In 2011, as well as in the comparable period, due to positive cash flow and the significant amount of cash balances, the Company made use to a slight extent of external financing in the form of bank and other loans from financial institutions and settled all of its liabilities in a timely manner.

In 2011, the Company held a customs guarantee with a maturity to 1 March 2013. This guarantee represents a contingent liability, which does not materially affect the liquidity risk of the Company.

Should the Company find it necessary to take advantage of external financing, the probability would exist of an increased liquidity risk.

#### Contractual maturities for financial liabilities as at 31 December 2011

Financial liabilities	Contractual maturities from the end of the reporting period					Total (without discounting)	Carrying amount
	Up to 3 months	3-12 months	1-3 years	3-5 years	Over 5 years		
Trade payables	913 795	281	90	-	-	<b>914 166</b>	<b>914 166</b>
Derivatives – Currency contracts	-	-	-	-	-	-	<b>403 372</b>
Derivatives – Commodity contracts - metals	10 384	46 366	5 126	-	-	<b>61 876</b>	<b>465 295</b>
Other financial liabilities	26 741	1 656	5 031	4 969	1 656	<b>40 053</b>	<b>39 028</b>
<b>Total financial liabilities by maturity</b>	<b>950 920</b>	<b>48 303</b>	<b>10 247</b>	<b>4 969</b>	<b>1 656</b>	<b>1 016 095</b>	

### 30. Financial risk management (continued)

#### 30.3 Liquidity risk and capital management (continued)

##### Contractual maturities for financial liabilities as at 31 December 2010

	Contractual maturities from the end of the reporting period					Total (without discounting)	Carrying amount
	Up to 3 months	3-12 months	1-3 years	3-5 years	Over 5 years		
<b>Financial liabilities</b>							
Trade payables	850 479	-	1 810	478	-	<b>852 767</b>	<b>852 710</b>
Derivatives – Currency contracts	19 002	50 211	-	-	-	<b>69 213</b>	<b>129 580</b>
Derivatives – Commodity contracts - metals	12 767	42 978	30 671	-	-	<b>86 416</b>	<b>1 063 852</b>
Other financial liabilities	58 357	4 600	10 550	5 921	3 157	<b>82 585</b>	<b>82 111</b>
<b>Total financial liabilities by maturity</b>	<b>940 605</b>	<b>97 789</b>	<b>43 031</b>	<b>6 399</b>	<b>3 157</b>	<b>1 090 981</b>	

Financial liabilities arising from derivatives are calculated as their intrinsic values, excluding the effects of discounting.

The Company manages its capital in order to maintain the capacity to continue its operations, including the realisation of planned investments, in a manner enabling it to generate returns for the shareholders and benefits to other stakeholders.

In accordance with market practice, the Company monitors its capital, among others based on the *equity ratio* and the *ratio of Net Debt/EBITDA*. The *equity ratio* is calculated as the relation of net assets (equity less intangible assets) to total assets. The ratio of *Net Debt/EBITDA* is calculated as the relation of borrowings and finance lease liabilities minus unallocated cash and cash equivalents and short term investments with a maturity up to 1 year to EBITDA (operating profit plus depreciation and amortisation).

In order to maintain financial liquidity and the creditworthiness to acquire external financing at an optimum cost, the Company assumes that the *equity ratio* shall be maintained at a level of not less than 0.5, and the *ratio of Net Debt/EBITDA* at a level of up to 2.0.

The above-described ratios as at 31 December 2011 and 31 December 2010 are presented below:

	31 December 2011	31 December 2010
Equity	23 135 511	14 456 477
Less: intangible assets	150 777	86 718
Net assets	22 984 734	14 369 759
Total assets	29 253 189	19 829 296
<b>Equity ratio</b>	<b>0.79</b>	<b>0.72</b>
Operating profit	13 687 640	5 638 148
Plus: depreciation/amortisation	672 373	615 468
EBITDA	14 360 013	6 253 616
Borrowings and finance lease liabilities	93	11 455
Unallocated cash and cash equivalents	12 832 963	2 593 778
<b>Ratio of net debt/EBITDA</b>	<b>0.00</b>	<b>0.00</b>

Due to the low level of debt of the Company as at 31 December 2011, the *ratio of net debt/EBITDA* amounted to 0.00.

The equity ratio was above the assumed minimum level and amounted to 0.79 at 31 December 2011.

In 2011 and 2010 there were no external equity requirements imposed on the Company.



### 31. Income tax

Income tax	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Current income tax		2 212 305	1 256 172
Adjustments to income tax from prior periods		(8 478)	(6 736)
Deferred income tax	20	115 250	(212 458)
<b>Total</b>		<b>2 319 077</b>	<b>1 036 978</b>

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Profit before income tax	13 653 597	5 605 567
Tax calculated at tax rates in force	2 594 183	1 065 058
Non-taxable income	(57 600)	(28 430)
Expenses not deductible for tax purposes	11 488	7 086
Tax-deductible expenses due to reversal of an impairment loss in connection with the sale of a subsidiary	(220 516)	-
Adjustments to income tax from prior periods	(8 478)	(6 736)
<b>Income tax expense</b>	<b>2 319 077</b>	<b>1 036 978</b>

The rate applied to the taxation of income in accordance with tax law in force in corporate income tax amounted to 19 % (in 2010: 19%). The effective interest rate was 16.99% (in 2010: 18.50%).

### 32. Earnings per share

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Profit for the period	11 334 520	4 568 589
Weighted average number of ordinary shares ('000)	200 000	200 000
Basic/diluted earnings per share (PLN/share)	56.67	22.84

There are no dilutive ordinary shares.

### 33. Dividend paid

In accordance with Resolution No. 6/2011 of the Ordinary General Meeting of KGHM Polska Miedź S.A. dated 15 June 2011 regarding the appropriation of Company profit for financial year 2010, the amount of PLN 2 980 000 thousand, representing PLN 14.90 per share, was allocated as a shareholders dividend. The right to dividend date was set at 11 July 2011, and dividend payment date at 12 August 2011. All shares of the Company are ordinary shares.

### 34. Explanations to the statement of cash flows

Adjustments to profit for the period	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Income tax recognised in profit or loss		2 319 077	1 036 978
Depreciation/amortisation	24	672 373	615 468
Losses on sales of property, plant and equipment and intangible assets		10 423	17 614
Gains on sales of available-for-sale financial assets		(16 855)	(4 925)
Impairment loss on loan, property, plant and equipment, intangible assets, and on shares in subsidiaries		292	13
Interest and share in profits (dividends)		(287 686)	(151 978)
Profit on sale of subsidiary and associates		(2 662 245)	(34)
Foreign exchange gains		(870 772)	(742)
Change in provisions		106 388	32 616
Change in derivatives		(546 233)	579 782
Reclassification of accumulated other comprehensive income to profit or loss as a result of realisation of derivatives		(241 565)	(142 187)
Other adjustments		146	305
<b>Changes in working capital:</b>		<b>235 162</b>	<b>(546 013)</b>
Inventories		(344 347)	(120 875)
Trade and other receivables		544 614	(684 838)
Trade and other payables		34 895	259 700
<b>Total adjustments to profit for the period</b>		<b>(1 281 495)</b>	<b>1 436 897</b>

### Proceeds from sales of property, plant and equipment and intangible assets

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Net carrying amount of sold property, plant and equipment and intangible assets and costs related to disposal	16 703	22 318
Losses on sales of property, plant and equipment and intangible assets	(10 423)	(17 614)
Negative change in receivables due to sales	-	13
<b>Proceeds from sales of property, plant and equipment and intangible assets</b>	<b>6 280</b>	<b>4 717</b>

### 34. Explanations to the statement of cash flows (continued)

#### Expenditures for acquisition of exploration and evaluation assets recognised in operating activities

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Acquisition of exploration and evaluation assets recognised in profit or loss	(24 221)	(4 025)
Positive/(Negative) change in liabilities recognised in operating activities due to exploration and evaluation assets recognised in profit or loss	4 359	(189)
<b>Expenditures for acquisition of exploration and evaluation assets recognised in operating activities</b>	<b>(19 862)</b>	<b>(4 214)</b>

#### Expenditures for exploration and evaluation assets recognised in investing activities

	Note	For the period	
		from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
Purchase	6	(37 361)	(15 528)
Adjustment to purchase	6	76	-
Internally-produced assets	6	(44)	-
Positive change in liabilities due to acquisition of exploration and evaluation assets		4 359	1 737
<b>Expenditures for exploration and evaluation assets recognised in investing activities</b>		<b>(32 970)</b>	<b>(13 791)</b>

### 35. Related party transactions

Sales	For the period from 1 January 2011 to 31 December 2011		
	Sales of products	Sales of merchandise and materials	Other transactions
To subsidiaries	678 918	68 285	4 044
To other related entities	439	35	15
<b>Total sales to related entities</b>	<b>679 357</b>	<b>68 320</b>	<b>4 059</b>

Sales	For the period from 1 January 2010 to 31 December 2010		
	Sales of products	Sales of merchandise and materials	Other transactions
To subsidiaries	1 052 748	60 487	6 404
To other related entities	438	39	21
<b>Total sales to related entities</b>	<b>1 053 186</b>	<b>60 526</b>	<b>6 425</b>

During the period from 1 January 2011 to 31 December 2011, KGHM Polska Miedź S.A. received dividends from an associate in the amount of PLN 250 013 thousand (from 1 January 2010 to 31 December 2010 dividend from associates in the amount of PLN 146 658 thousand).

During the period from 1 January 2011 to 31 December 2011, no sales of property, plant and equipment, intangible assets and investment property to related entities of the Company were reported.

Purchases	For the period from 1 January 2011 to 31 December 2011			
	Purchase of services	Purchase of merchandise and materials	Purchase of property, plant and equipment, intangible assets, investment property	Other transactions
From subsidiaries	800 131	3 187 552	633 167	5 146
From other related entities	1 721	66	12	-
<b>Total purchases from related entities</b>	<b>801 852</b>	<b>3 187 618</b>	<b>633 179</b>	<b>5 146</b>

### 35. Related party transactions (continued)

Purchases	For the period from 1 January 2010 to 31 December 2010			
	Purchase of services	Purchase of merchandise and materials	Purchase of property, plant and equipment, intangible assets, investment property	Other transactions
From subsidiaries	653 364	2 983 108	610 259	2 572
From other related entities	1 925	74	10	-
<b>Total purchases from related entities</b>	<b>655 289</b>	<b>2 983 182</b>	<b>610 269</b>	<b>2 572</b>

### Remuneration of the Management Board paid in 2011

	Period when function served	Earnings from subsidiaries and associates	Benefits, other earnings	Total earnings in 2011
		Salaries		
<b>Members of the Management Board serving function as at 31 December 2011</b>				
Herbert Wirth	01.01-31.12.2011	1 406	306	1 870
Maciej Tybura	01.01-31.12.2011	1 227	119	1 533
Wojciech Kędzia	01.01-31.12.2011	985	102	1 158
<b>Other Members of the Management Board *</b>				
Ryszard Janeczek	-	96	-	96
<b>Total</b>		<b>3 714</b>	<b>527</b>	<b>4 657</b>

\* the item „Salaries” includes salaries during the termination period

### Remuneration of the Supervisory Board paid in 2011

	Period when function served	Remuneration for the period when function served	Earnings from other contracts	Other benefits	Total earnings in 2011
		in the Supervisory Board			
Marcin Dyl	01.01-31.12.2011	96	-	17	113
Arkadiusz Kawecki	01.01-31.12.2011	88	-	22	110
Jacek Kuciński	01.01-31.12.2011	110	-	24	134
Marek Panfil	01.01-31.12.2011	88	-	20	108
Marzenna Weresa	01.01-31.12.2011	88	-	9	97
Jan Rymarczyk	01.01-31.12.2011	88	-	21	109
Franciszek Adamczyk	15.06-31.12.2011	47	-	10	57
Lech Jaroń	20.10-31.12.2011	17	51	3	71
Maciej Łaganowski	20.10-31.12.2011	17	28	-	45
Paweł Markowski	20.10-31.12.2011	18	70	-	88
Józef Czyczerski	01.01-15.06.2011	41	72	-	113
Leszek Hajdacki	01.01-15.06.2011	41	90	4	135
Ryszard Kurek	01.01-15.06.2011	41	125	5	171
<b>Total</b>		<b>780</b>	<b>436</b>	<b>135</b>	<b>1 351</b>

### 35. Related party transactions (continued)

#### Remuneration of the Management Board paid in 2010

	Period when function served	Salaries	Earnings from subsidiaries and associates	Benefits, other earnings	Total earnings in 2010
<b>Members of the Management Board serving function as at 31 December 2010</b>					
Herbert Wirth	01.01-31.12.2010	912	313	96	1 321
Maciej Tybura	01.01-31.12.2010	750	116	143	1 009
Wojciech Kędzia	19.11-31.12.2010	132	10	1	143
<b>Other Members of the Management Board *</b>					
Ryszard Janeczek	01.01-15.10.2010	483	50	59	592
Mirosław Krutin	-	91	-	-	91
<b>Total</b>		<b>2 368</b>	<b>489</b>	<b>299</b>	<b>3 156</b>

\* the item „Salaries” includes salaries during the termination period

#### Remuneration of the Supervisory Board paid in 2010

	Period when function served	Remuneration for the period when function served in the Supervisory Board	Earnings from other contracts	Other benefits	Total earnings in 2010
Marcin Dyl	01.01-31.12.2010	90	-	17	107
Arkadiusz Kawecki	01.01-31.12.2010	84	-	23	107
Jacek Kuciński	01.01-31.12.2010	101	-	29	130
Marek Panfil	01.01-31.12.2010	84	-	20	104
Marek Trawiński	01.01-17.02.2010	15	-	3	18
Marzenna Weresa	01.01-31.12.2010	84	-	14	98
Jan Rymarczyk	17.05-31.12.2010	51	-	10	61
Józef Czyczerski	01.01-31.12.2010	84	104	1	189
Leszek Hajdacki	01.01-31.12.2010	84	173	6	263
Ryszard Kurek	01.01-31.12.2010	84	173	8	265
<b>Total</b>		<b>761</b>	<b>450</b>	<b>131</b>	<b>1 342</b>

### 35. Related party transactions (continued)

	At	
	31 December 2011	31 December 2010
<b>Trade and other receivables from related entities</b>		
From subsidiaries	269 922	202 741
From other related entities	-	64
<b>Total receivables from related entities</b>	<b>269 922</b>	<b>202 805</b>

	At	
	31 December 2011	31 December 2010
<b>Trade and other payables towards related entities</b>		
Towards subsidiaries	431 871	317 907
Towards other related entities	-	337
<b>Total payables towards related entities</b>	<b>431 871</b>	<b>318 244</b>

During the current reporting period, two individual transactions were identified between KGHM Polska Miedź S.A. and the government and entities controlled or jointly controlled by the government, or over which the government has significant influence, which would be considered as significant in terms of unusual scope and amount.

1. On 2 February 2011, KGHM Polska Miedź S.A. signed an agreement with the Minister of the State Treasury for the acquisition of 5 260 820 shares of the company NITROERG S.A. in Bieruń with a nominal value of PLN 10 per share, for PLN 120 052 thousand. The controlling interest acquired represents 85% of the share capital of NITROERG S.A. in Bieruń.
2. KGHM Polska Miedź S.A. participated in the selling process by the Ministry of the State Treasury of the shares of TAURON Polska Energia S.A., submitting a purchase order for the shares of TAURON Polska Energia S.A. As a result of this transaction, on 23 March 2011 KGHM Polska Miedź S.A. purchased 71 000 000 shares of TAURON Polska Energia S.A. at PLN 6.15 per share. The transaction was realised as part of an accelerated book building process. Following this transaction, KGHM Polska Miedź S.A. owns a total of 182 110 566 shares of TAURON Polska Energia S.A., representing 10.39% of the share capital.

For the period from 1 January to 31 December 2010, none of the transactions with the aforementioned companies was individually significant, either in terms of their nature or amount.

The remaining transactions, which were collectively significant, between the Company and the government and entities controlled or jointly controlled by the government, or over which the government has significant influence, were within the scope of normal, daily economic operations, carried out at arm's length. These transactions involved the purchase by the Company of materials and services to meet the needs of its current operating activities (fuel, energy, transport services). Turnover from these transactions in the period from 1 January 2011 to 31 December 2011 amounted to PLN 769 372 thousand (for the period from 1 January 2010 to 31 December 2010: PLN 723 895 thousand), the unsettled balance of liabilities from these transactions at 31 December 2011 amounted to PLN 45 968 thousand (at 31 December 2010: PLN 103 124 thousand), and the unsettled balance of receivables at 31 December 2011 amounted to PLN 1 414 thousand (at 31 December 2010: PLN 2 945 thousand). Revenues from sales from State Treasury companies during the period from 1 January 2011 to 31 December 2011 amounted to PLN 55 424 thousand (for the period from 1 January 2010 to 31 December 2010: PLN 49 655 thousand).

### 36. Remuneration of entity entitled to audit the financial statements and of entities related to it

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
<b>PricewaterhouseCoopers Sp. z o.o.</b>	<b>963</b>	<b>719</b>
From contract for the review and audit of financial statements	834	710
audit of annual financial statements of the Company and of annual consolidated financial statements of the Group	532	408
review of interim financial statements of the Company and of interim consolidated financial statements of the Group	302	302
From realisation of other contracts	129	9
<b>Other companies of the PricewaterhouseCoopers Group in Poland</b>	<b>41</b>	<b>598</b>
From other contracts	41	598

### 37. Liabilities not recognised in the statement of financial position due to operating leases

Total value of future minimum fees due to perpetual usufruct of land was presented in note 6.

#### Total value of future minimum lease payments

	<b>At</b>	
	<b>31 December 2011</b>	<b>31 December 2010</b>
Up to one year	18 656	6 826
From one to five years	11 615	11 979
Over five years	1 413	468
<b>Total:</b>	<b>31 684</b>	<b>19 273</b>

	<b>For the period</b>	
	<b>from 1 January 2011 to 31 December 2011</b>	<b>from 1 January 2010 to 31 December 2010</b>
<b>Lease payments recognised in profit or loss</b>	<b>12 424</b>	<b>7 596</b>

### 38. Contingent assets and liabilities

	<b>At</b>	
	<b>31 December 2011</b>	<b>31 December 2010</b>
<b>Contingent assets</b>	<b>373 223</b>	<b>205 634</b>
Guarantees received	167 018	132 214
Disputed State Budget issues	7 093	17 518
Promissory notes receivables	77 007	22 573
Inventions, implementation of projects	36 595	33 329
Real estate tax on mining facilities	85 489	-
Other	21	-
<b>Contingent liabilities</b>	<b>141 430</b>	<b>127 143</b>
Guarantees	5 000	5 000
Disputed issues, pending court proceedings	13 769	15 566
Preventive safety measures in respect of mine-related damages	8 000	2 475
Liabilities due to implementation of projects and inventions	113 967	104 098
Other	694	4

### 39. Social Fund assets and liabilities

KGHM Polska Miedź S.A., in accordance with the obligation resulting from the Social Fund Act dated 4 March 1994, creates a Social Fund. The Fund's purpose is to subsidise the Company's social activity, housing loans to employees and other social expenditures.

The Company has netted the assets of the Fund with the liabilities towards the Fund, as these assets are not subject to control of the Company and do not meet the definition of an asset. Accordingly, the net balance (liability towards Social Fund) at 31 December 2011 amounts to PLN 1 952 thousand, and the net balance (liability towards Social Fund) at 31 December 2010 amounted to PLN 1 505 thousand.

Details on assets, liabilities and costs related to the Social Fund are presented in the table below.



### 39. Social Fund assets and liabilities (continued)

Social Fund assets and liabilities	At	
	31 December 2011	31 December 2010
Housing loans granted to employees	114 476	108 143
Other receivables	417	250
Cash and cash equivalents	19 749	18 680
Liabilities towards Social Fund	136 594	128 578
<b>Net balance</b>	<b>(1 952)</b>	<b>(1 505)</b>
<b>Transfers made to the Social Fund during the financial period</b>	<b>104 816</b>	<b>99 712</b>

### 40. Employment structure

	For the period	
	from 1 January 2011 to 31 December 2011	from 1 January 2010 to 31 December 2010
White-collar employees	4 568	4 462
Blue-collar employees	14 010	14 003
<b>Total:</b>	<b>18 578</b>	<b>18 465</b>

### 41. Subsequent events

#### Purchase of Quadra FNX Mining Ltd.

On 5 March 2012 the company 0929260 B.C. Unlimited Liability Company with its registered head office in Vancouver as an indirect subsidiary of KGHM Polska Miedź S.A., purchased from the former shareholders of Quadra FNX Mining Ltd. with its registered head office in Vancouver ("Quadra FNX") 193 334 154 shares of Quadra FNX („Shares”), for the price of CAD 15.00 per share (representing the equivalent of PLN 47.31 at the average CAD/PLN exchange rate of the National Bank of Poland of 5 March 2012), and the total price of CAD 2 900 012 thousand (representing the equivalent of PLN 9 147 219 thousand at the average CAD/PLN exchange rate of the National Bank of Poland of 5 March 2012). The shares were paid for in cash obtained by 0929260 B.C. U.L.C. based on financing agreements entered into within the KGHM Polska Miedź S.A. Group, deriving from the internal funds of KGHM Polska Miedź S.A.

KGHM Polska Miedź S.A. became the wholly-owner of Quadra FNX (the shares purchased by 0929260 B.C. U.L.C. represent 100% of the share capital of Quadra FNX and 100% of the votes at the General Meeting of this company), and shares of Quadra FNX were delisted from the trade on the Toronto Stock Exchange. Purchase of the shares is of a long-term, equity investment nature for the KGHM Polska Miedź S.A. Group. The name and logo of the purchased company were changed to KGHM INTERNATIONAL LTD. The shares do not have a nominal value.

The transaction was closed and shares were purchased in execution of the agreement dated 6 December 2011 signed by KGHM Polska Miedź S.A. and Quadra FNX under a Plan of Arrangement recommended by the Board of Directors of Quadra FNX, after the end of the reporting period after fulfilment of the following conditions precedent:

- Canada's Competition Bureau was not opposed to the purchase of all of the Quadra FNX shares by KGHM Polska Miedź S.A. or an affiliate thereof.
- The United States Federal Trade Commission was not opposed to purchase of the Quadra FNX shares,
- on 20 February 2012 the shareholders of Quadra FNX at the General Meeting of the company approved by the required majority of votes the purchase of Quadra FNX shares described in the binding conditional agreement entered into between KGHM Polska Miedź S.A. and Quadra FNX,
- on 21 February 2012 the Supreme Court of British Columbia, Canada, issued the final order approving the transaction described in the binding conditional agreement entered into between KGHM Polska Miedź S.A. and Quadra FNX,
- Canadian Minister of Industry granted approval under the Investment Canada Act for the transaction of purchase of Quadra FNX shares, described in the binding conditional agreement entered into between KGHM Polska Miedź S.A. and Quadra FNX.

#### **41. Subsequent events (continued)**

The operations of KGHM INTERNATIONAL LTD. (until 12 March 2012 Quadra FNX) are focused on mine production of metals (including copper, nickel, gold, platinum, palladium) in the following mines: Robinson and Carlota in the USA, Franke in Chile, and McCreedy West, Levack (with the Morrison deposit) and Podolsky in Canada. Activities include also pre-operational mining projects at various stages of development: Sierra Gorda in Chile (the company's major development project, involving one of the largest new copper and molybdenum deposits in the world), Victoria in Canada and Malmbjerg in Greenland. In addition, the company is pursuing the Kirkwood, Falconbridge and Foy exploration projects in the region of Sudbury in Canada, and also owns a minority stake of Capstone Mining.

As a result of the purchase of Quadra FNX, the KGHM Polska Miedź S.A. Group advanced to fourth place globally in terms of documented copper resources and eighth place in terms of copper production.

The signing of the agreement is consistent with the strategy of the KGHM Polska Miedź S.A. Group aimed at increasing the resource base as well as copper production. The acquisition described above will increase annual mined copper production in the Group by over 100 thousand tonnes beginning from 2012, and in 2018 by over 180 thousand tonnes, meaning a 25% increase versus the pre-acquisition level of Company production. In addition, following the start-up of project Victoria in Canada and Sierra Gorda in Chile in 2014, the transaction will lead to a substantial decrease in average unit copper production costs in the entities directly and indirectly managed by KGHM Polska Miedź S.A.

#### **Changes in the Supervisory Board of the Company**

The Extraordinary General Meeting of KGHM Polska Miedź S.A., on 19 January 2012, dismissed from the Supervisory Board of KGHM Polska Miedź S.A. the following persons:

1. Franciszek Adamczyk,
2. Marcin Dyl,
3. Arkadiusz Kawecki,
4. Jan Rymarczyk,
5. Marzenna Weresa.

The Extraordinary General Meeting appointed to the Supervisory Board of the Company the following persons:

1. Krzysztof Kaczmarczyk,
2. Mariusz Kolwas,
3. Aleksandra Magaczewska,
4. Robert Oliwa,
5. Jacek Poświata.

#### **Forecast of results for 2012**

On 27 March 2012, the Supervisory Board of KGHM Polska Miedź S.A. approved the Budget for 2012. The bases for development of the Budget were the results for 2011 and the assumptions of individual operating plans. Detailed information regarding the forecast is presented in the Report of the Management Board on the Company's Activities, point 3.8.

<b>SIGNATURES OF ALL MEMBERS OF THE MANAGEMENT BOARD</b>			
<b>DATE</b>	<b>FIRST, LAST NAME</b>	<b>POSITION / FUNCTION</b>	<b>SIGNATURE</b>
27 March 2012	Herbert Wirth	President of the Management Board	
27 March 2012	Maciej Tybura	I Vice President of the Management Board	
27 March 2012	Wojciech Kędzia	Vice President of the Management Board	

<b>SIGNATURE OF PERSON RESPONSIBLE FOR ACCOUNTING</b>			
<b>DATE</b>	<b>FIRST, LAST NAME</b>	<b>POSITION / FUNCTION</b>	<b>SIGNATURE</b>
27 March 2012	Ludmiła Mordylak	Chief Accountant of KGHM Executive Director of Accounting Services Center	

**KGHM POLSKA MIEDŹ S.A.**

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**REPORT OF THE MANAGEMENT  
BOARD ON THE COMPANY'S  
ACTIVITIES IN 2011**

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Lubin, March 2012

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Table 1. Aggregated data regarding KGHM Polska Miedź S.A. in the years 1997-2011

## KGHM POLSKA MIEDŹ S.A. IN THE YEARS 1997-2011

(data for the years 1997-2005 per published annual reports, and since 2006 per IFRS)

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Change 2010=100	CAGR (%) ****
<b>Statement of comprehensive income</b>																	
Sales	4 089	3 642	4 113	4 983	4 218	4 488	4 741	6 158	8 000	11 670	12 183	11 303	11 061	15 945	20 097	126.0	12.0
Profit from operations	905	240	348	941	173	152	431	1 445	2 707	4 139	4 880	3 392	3 197	6 657	9 364	140.7	18.2
EBITDA*	1 212	631	319	1 198	144	753	956	1 761	2 937	4 784	5 101	4 078	3 646	6 254	14 360	x2.3	19.3
Profit before income tax	914	310	(58)	795	(147)	310	569	1 446	2 635	4 380	4 656	3 554	3 067	5 606	13 654	x2.4	21.3
Profit for the period	502	179	(170)	618	(190)	255	412	1 397	2 289	3 605	3 799	2 920	2 540	4 569	11 335	x2.5	24.9
<b>Statement of financial position</b>																	
Total assets	4 937	4 975	4 884	5 757	7 557	8 155	8 695	8 948	10 977	12 251	12 424	13 901	13 953	19 829	29 253	147.5	13.6
Non-current assets	3 558	3 698	3 579	4 177	4 735	6 440	6 621	6 552	7 079	7 017	7 431	8 704	9 509	12 125	11 697	96.5	8.9
Current assets	1 364	1 242	1 250	1 381	2 657	1 715	2 074	2 397	3 899	5 234	4 992	5 174	4 444	7 704	17 556	x2.3	20.0
Equity	4 021	4 096	3 470	4 067	3 696	4 011	4 007	5 337	6 214	8 116	8 966	10 591	10 404	14 456	23 136	160.0	13.3
Liabilities and provisions	846	775	1 187	1 380	3 634	4 144	4 689	3 612	4 763	4 136	3 458	3 309	3 549	5 373	6 118	113.9	15.2
<b>Financial ratios</b>																	
Earnings per share (EPS)	2.51	0.89	(0.85)	3.09	(0.95)	1.27	2.06	6.99	11.45	18.02	18.99	14.60	12.70	22.84	56.67	x2.5	24.9
Dividend per share (DPS) **	0.25	0.10	-	1.00	-	-	-	2.00	10.00	16.97	9.00	11.68	3.00	14.90	x	x	x
Price per share / Earnings per share (P/E)	5.4	14.0	(30.8)	8.3	(13.7)	10.6	12.7	4.5	5.5	4.9	5.6	1.9	8.3	7.6	2.0	26.3	(7.0)
Current liquidity	2.2	2.3	2.6	2.3	1.0	1.2	1.2	1.2	1.4	1.9	2.5	3.1	2.4	2.6	4.5	173.1	5.2
Quick liquidity	1.0	0.9	1.0	0.9	0.7	0.6	0.7	0.8	1.0	1.3	1.7	2.2	1.4	1.9	3.9	x2.1	9.8
Return on assets (ROA)	10.2	3.6	(3.5)	10.7	(2.5)	3.1	4.7	15.6	20.9	29.4	30.6	21.0	18.2	23.0	38.7	168.3	10.0
Return on equity (ROE)	12.5	4.4	(4.9)	15.2	(5.1)	6.3	10.3	26.2	36.8	44.4	42.4	27.6	24.4	31.6	49.0	155.1	10.3
Debt ratio	14.2	13.5	14.3	15.9	38.2	34.2	38.8	24.0	28.2	33.8	27.8	23.8	25.4	27.1	20.9	77.1	2.8
Durability of financing structure	86.1	87.1	85.7	84.1	63.4	79.0	76.8	75.0	70.6	77.0	83.8	88.0	86.8	84.9	86.8	102.2	0.1
<b>Production results</b>																	
Electrolytic copper production	440.6	446.8	470.5	486.0	498.5	508.7	529.6	550.1	560.3	556.6	533.0	526.8	502.5	547.1	571.0	104.4	1.9
Metallic silver production	1 029	1 098	1 093	1 119	1 163	1 192	1 358	1 344	1 244	1 242	1 215	1 193	1 203	1 161	1 260	108.5	1.5
<b>Macroeconomic data (average annual)</b>																	
Copper prices on LME	2 276	1 653	1 574	1 814	1 578	1 558	1 780	2 868	3 684	6 731	7 126	6 952	5 164	7 539	8 811	116.9	10.2
Silver prices on LBM	4.88	5.54	5.23	4.95	4.37	4.60	4.88	6.66	7.31	11.55	13.38	14.99	14.67	20.19	35.12	173.9	15.1
Exchange rate	3.28	3.49	3.96	4.35	4.10	4.08	3.89	3.65	3.23	3.10	2.77	2.41	3.12	3.02	2.96	98.0	(0.7)
<b>Other</b>																	
Market value of Company shares at the end of the period PLN/share	13.50	12.50	26.20	25.80	13.00	13.50	26.20	31.30	62.50	89.00	105.80	28.12	106.00	173.00	110.60	63.9	16.2
Capital expenditure	649	487	379	584	433	360	424	616	651	709	828	1 140	1 070	1 263	1 514	119.9	6.2
Equity investments ***	493	200	229	468	271	105	146	707	613	24	155	793	170	1 321	643	48.7	1.9
Electrolytic copper production cost	5 527	5 556	5 836	6 156	6 328	6 305	6 237	6 660	7 723	10 497	11 160	11 736	11 170	12 983	13 566	104.5	6.6
Electrolytic copper production cost	1 685	1 590	1 472	1 417	1 544	1 545	1 603	1 825	2 388	3 381	4 031	4 878	3 582	4 302	4 578	106.4	7.4

\* operating profit (in the years 1997-2006 profit (loss) before extraordinary items and taxation adjusted by interest cost) + depreciation/amortisation

\*\* dividend for financial year

\*\*\* purchase/acquisition of shares and investment certificates

\*\*\*\* CAGR - Compound Annual Growth Rate, t0=1997

## 1. Company profile

### 1.1. Company organisation

In 2011 the multi-divisional organisational structure of the Company, acting under the name KGHM Polska Miedź S.A., comprised a Head Office and 10 Divisions.

**Diagram 1. Organisational structure of the Company as at 31 December 2011**



### Supervisory Board of the Company

Under the Company's Statutes, the Members of the Supervisory Board are appointed and dismissed by the General Meeting. In 2011 the 7th-term Supervisory Board of KGHM Polska Miedź S.A. commenced work in the following composition:

- Jacek Kuciński Chairman
- Marcin Dyl Deputy Chairman
- Marek Panfil Secretary
- Arkadiusz Kawecki
- Jan Rymarczyk
- Marzenna Weresa

as well as the following employee-elected members:

- Józef Czyzerski
- Leszek Hajdacki
- Ryszard Kurek

**Table 2. Decisions by Company bodies regarding the composition of the Supervisory Board in 2011\***

Date	Event
15.06.2011	<p>The Ordinary General Meeting resolved to:</p> <ul style="list-style-type: none"> <li>– dismiss all of the Members of the 7th-term Supervisory Board,</li> <li>– set the number of members of the Supervisory Board at 10 persons,</li> <li>– appoint 7 Members of the Supervisory Board to the 8th term (Franciszek Adamczyk, Marcin Dyl, Arkadiusz Kawecki, Jacek Kuciński, Marek Panfil, Jan Rymarczyk, Marzenna Weresa)</li> </ul> <p>As a result of a decision of the Ordinary General Meeting, the 3 employee-elected members were not appointed to the 8th-term Supervisory Board</p>
22.06.2011	<p>The Supervisory Board selected a Chairman (Jacek Kuciński), Deputy Chairman (Marcin Dyl) and Secretary (Marek Panfil)</p>
20.10.2011	<p>The Extraordinary General Meeting appointed 3 employee-elected members elected in a repeat election to the 8th-term Supervisory Board - Lech Jaroń, Maciej Łaganowski and Paweł Markowski</p>
19.01.2012	<p>The Extraordinary General Meeting made the following changes to the composition of the Supervisory Board:</p> <ul style="list-style-type: none"> <li>– 5 members were dismissed: Franciszek Adamczyk, Marcin Dyl, Arkadiusz Kawecki, Jan Rymarczyk and Marzenna Weresa,</li> <li>– appointed: Krzysztof Kaczmarczyk, Mariusz Kolwas, Aleksandra Magaczewska, Robert Oliwa and Jacek Poświata</li> </ul>

\* Reflecting decisions made to the date of preparation of this report

## Management Board of the Company

In accordance with the Statutes of KGHM Polska Miedź S.A. the Members of the Management Board are appointed and dismissed by the Supervisory Board. In 2011 the 7th-term Management Board of KGHM Polska Miedź S.A. performed its work in the following form:

- |                   |  |
|-------------------|--|
| – Herbert Wirth   | President of the Management Board,                   |
| – Maciej Tybura   | I Vice President of the Management Board (Finance),  |
| – Wojciech Kędzia | Vice President of the Management Board (Production). |

Following is the segregation of duties amongst individual Members of the Management Board:

**President of the Management Board** – organises and directs the work of the Management Board, engages in actions on behalf of the Head Office, as an employer, in matters dealing with labour law in respect of the employees of the Head Office and on behalf of the Divisions, as an employer, in matters dealing with labour law in respect of the directors of the Divisions of KGHM Polska Miedź S.A.

The President of the Management Board is the head of the company under art. 2 point 14 of the Act dated 5 August 2010 on the protection of classified information. He is responsible for matters dealing with the protection of classified information, IT, physical and technical protection and security, and the protection of personal data and tasks involving defence and crisis management.

In addition the **President of the Management Board** directs Company affairs in the following areas:

- employee affairs, including the following policies: social, remuneration, CSR, human resources, training and personnel,
- Company image, public relations and investor relations,
- ownership policy in respect of the companies of the KGHM Polska Miedź S.A. Group,
- auditing and internal control,
- organisational, legal and administrative services,
- property management,
- research and development,
- tangible and equity investments,
- energy management and development, energy security,
- economic strategy and new economic initiatives,
- industrial and intellectual property rights,
- environmental policy,
- IT – supervision of the Data Center Division.

The **I Vice President of the Management Board (Finance)** serves in the place of the President of the Management Board in his absence and directs Company affairs in the following areas:

- economic and financial policy, controlling and budgeting,
- accounting and reporting, taxation and bookkeeping policy,
- risk management,
- Company commercial policy,
- procurement policy for the Group.

The **Vice President of the Management Board (Production)** directs Company affairs in the following areas:

- supervising the activities of the Company's Division, with the exception of the Data Center Division,
- mining, smelting and geology-related activities,
- planning, monitoring and optimisation of production,
- efficiency improvement programs,
- safety and working conditions.

## Information on the employment contracts and remuneration of Members of the Management Board of KGHM Polska Miedź S.A.

The employment contracts which are signed with Members of the Management Board provide for the payment of remuneration, composed of the basic monthly salary, variable salary, bonuses and additional benefits resulting from the Collective Labour Agreement for the Employees of KGHM Polska Miedź S.A. along with sector rules not tied to the basic monthly salary. Payment of the variable salary is contingent on the fulfilment of criteria set for the Management Board by the Supervisory Board, and amounts up to 40% of the annual basic salary. Additionally, the Supervisory Board, based on assessment of the work of the Management Board, may grant the Members of the Management Board up to 10% of the annual basic salary.



Potentially-due remuneration with respect to variable salary for 2011, the payment of which is decided by the Supervisory Board, is presented in Table 3:

**Table 3. Potentially-due remuneration for Members of the Management Board for 2011**

Name	Position	Potentially-due remuneration for 2011
Herbert Wirth	President, Member of the Management Board	PLN 242 thousand
Maciej Tybura	I Vice President, Member of the Management Board	PLN 213 thousand
Wojciech Kędzia	Vice President, Member of the Management Board	PLN 194 thousand

The employment contracts which are signed with Members of the Management Board provide that, in case of the dismissal of a Member of the Management Board and the termination of their contract prior to the time stipulated in the contract, the said Member of the Management Board shall receive compensation due to the loss of an existing source of income and to the premature termination of a contract in an amount equal to 10 basic monthly salaries. Employment contracts describe those cases in which a Member of the Management Board shall not receive the above-mentioned compensation.

The employment contracts with the Members of the Management Board of KGHM Polska Miedź S.A. do not provide for compensation with respect to forbidding any activities which would be competitive towards KGHM. One of the points of the chapter „Forbidding of employment and forbidding of competition” of the employment contract states: „The parties shall regulate in a separate contract the principles of forbidding competition following termination of employment and of the amount of compensation due in this regard.” At the date of preparation of this Report such contracts had not been signed.

The employment contracts with Management Board Members also regulate the following matters:

- coverage by the Company of costs required for the proper fulfilment of the employment contracts (travel, flights, room, board, travel insurance and representation costs, incurred pursuant to the budget),
- the use of business cars and rental of a flat for Management Board members (the costs associated with the use of a business car and flat are defined in a separate contract),
- medical benefits (in each calendar year of the life of the contract the Company purchases a medical packet for Management Board members worth up to PLN 10 thousand),
- life insurance premiums (once every year the Company covers or reimburses the amount of the premiums to an amount up to one monthly basic salary, with the principles and manner of settlement being agreed by the parties in a separate contract).

Detailed information on remuneration paid, bonuses or benefits for Members of the Management Board and Supervisory Board can be found in Note 35 of the financial statements of KGHM Polska Miedź S.A. for 2011.

## 1.2. Production results

The main objectives set forth by the Management Board with respect to production in 2011 were:

- optimal utilisation of the resource base and of the production capacity of the Company,
- optimisation of the copper content in ore and concentrate, and
- maximum utilisation of the production capacity of the smelting divisions.

The objectives set forth required fulfilment of the following tasks:

with respect to **mining**:

- improving the ore selection system by:
  - selecting an appropriate size for the support pillars and the geometry of working areas in order to restrict the risk of rock collapse,
  - applying so-called partial backfill in thick ore seams,
  - increasing the scope of selective mining (i.e. leaving a larger amount of barren rock at the bottom of the mine) and utilising wheeled machines which are an appropriate height for the thickness of the ore,
- increasing the scope of drift work to prepare new working areas in the mines and improve knowledge of the deposit,

with respect to **ore enrichment**:

- adapting the production capacity of specific areas of the Ore Enrichment Plants to the amount and quality of ore supplied,
- improving enrichment parameters through the successive replacement of floatation equipment,
- maintaining the production of concentrates in an amount and quality necessary for optimal use of the production capacity of the furnace sections of the smelters,
- commencing the separation of concentrate produced at the OEP of the Rudna mine into two types of concentrate with varied organic carbon content,

with respect to **smelting**:

- preparation of infrastructure and terrain at the Głogów smelter required for the further modernisation of the smelter – construction of a flash furnace,
- modernisation begun on the overhead pouring units at the Głogów smelter,
- construction of a 4th Doerschel furnace at the Głogów smelter,
- modernisation of the electrolyte purification unit at the Głogów smelter,
- realisation of the first stage of modernisation of the sulphuric acid plant at the Głogów smelter,
- replacement of 6 cranes in the electrorefining unit at the Głogów smelter,
- general maintenance on the Contirod line at the Cedynia plant in Orsk.

#### Mine production

Ore extraction by dry weight in 2011 was higher by 0.4 million tonnes than in 2010, and amounted to 29.7 million tonnes. The increase in extraction in 2011 was due to an increase in daily extraction on working days and an intensification of work on days legally free from work.

The average copper content in extracted ore amounted to 1.61% and was lower than that achieved in 2010 (1.64%), due to work in regions with lower copper ore mineralisation.

Despite the increase in ore extraction, the decrease in its quality led to a decrease in copper content in extracted ore by 1.3 thousand tonnes. In 2011, the amount of ore processed increased by 0.6 million tonnes versus the prior year, which directly led to an increase in production of copper in concentrate by 1.2 thousand tonnes. The amount of silver in concentrate was lower than achieved in 2010 by 14 tonnes.

**Table 4. Mine production**

	Unit	2009	2010	2011	Change 2010=100
Copper ore (dry weight) *	M t	29.7	29.3	29.7	101.4
Copper content in ore	%	1.68	1.64	1.61	98.2
Copper content in ore	'000 t	499.5	480.6	479.3	99.7
Silver content in ore	t	1 411	1 390	1 356	97.6
Copper concentrate *	'000 t	1 928.9	1 841.2	1 875.2	101.8
Copper content in concentrate	'000 t	439.0	425.4	426.7	100.3
Silver content in concentrate	t	1 206	1 181	1 167	98.8

\* Dry weight

#### Smelter production

The production of electrolytic copper increased versus 2010 by 23.9 thousand tonnes, i.e. 4.4% and reached the highest level in the Company's history, i.e. 571.0 thousand tonnes. The increase in production was due to higher processing of own concentrate and higher use of purchased copper-bearing materials in the form of scrap, copper blister and imported concentrate. The augmentation of own concentrates with purchased copper-bearing materials enabled the effective utilisation of existing technological abilities.

The production of other smelter products (silver, wire rod, OFE and CuAg rod and round billets) depends on the level of electrolytic copper production, the type of raw materials used and on market demand.

In relation to 2010, the production of metallic gold decreased by 72 kg (9.3%), while the production of silver and lead increased respectively by 99 tonnes (8.5%) and 4.3 thousand tonnes (20.6%).

**Table 5. Smelter production**

	Unit	2009	2010	2011	Change 2010=100
Electrolytic copper	'000 t	502.5	547.1	571.0	104.4
of which from purchased copper-bearing materials	'000 t	103.8	120.0	124.6	103.8
Wire rod, OFE and CuAg rod	'000 t	191.4	253.4	242.7	95.8
Round billets	'000 t	14.9	18.7	20.3	108.6
Metallic silver	t	1 203	1 161	1 260	108.5
Metallic gold	kg	814	776	704	90.7
Refined lead	'000 t	21.6	20.9	25.2	120.6

## Main directions in production

The main production goals set out by the Management Board in 2012 are:

- optimal utilisation of the resource base and of the production capacity of the Company, and
- optimisation of the copper content in ore and concentrate.

With respect to mining, the key goals for 2012 will be:

- continued drift preparation work being realised at the Rudna Mine in the direction of the Głogów Głęboki Przemysłowy deposit,
- the application of new drift preparation work technology using drift combines, and
- restricting depletion in extracted ore.

With respect to ore enrichment, the key goals for 2012 will be:

- continued replacement of floatation machinery,
- optimisation of the enrichment process,
- continued separation of concentrate produced at the OEP of the Rudna mine into two types of concentrate with varied organic carbon content.

With respect to smelting, the key goals for 2012 will be:

- continued modernisation of technology at the Głogów smelter,
- completion of modernisation of the overhead pouring units at the Głogów smelter,
- construction of a concentrate warehouse at the Głogów smelter – completion of project,
- modernisation of casting forms unit and caissons at the Głogów smelter,
- development of unit for the thermal elimination of oil emulsions in the Contirod line of the Cedynia wire rod plant.

## Process of gaining licenses for mining regions currently being worked

Due to the fact that in December 2013 the 20-year licenses for five of the mining regions currently being worked by KGHM Polska Miedź S.A. expire, the Company has applied for licenses to be issued for these regions for the maximum period provided for by law, which is 50 years.

To ensure the licensing process goes smoothly, KGHM Polska Miedź S.A. maintains permanent contact with the appropriate bodies:

- the local governments of mining municipalities,
- decision-granting institutions (supervisory bodies in terms of geology, mining and the environment),
- consultative institutions (from the academic and scientific communities),
- as well as engaging the support of two leading domestic law firms, specialising in problems related to general geological and mining law.

In the Company's opinion, the following ensure the licenses will be granted on time:

- making an early start on new license issuance procedures,
- being ahead of schedule on preparing required licensing documentation,
- having appropriate infrastructure and a leading position in the region, as well as the domestic and European markets.

Continuity in terms of the licenses held and requested means that other entities have no „open window” to exploit in the licensing process.

### 1.3. Product sales structure

In 2011, versus the prior year, the Company increased the volume of copper sales by 21.6 thousand tonnes (4.0%). The structure of sales changed, i.e. the volume of cathode sales increased by 11.2% (31.0 thousand tonnes) alongside slightly lower sales of copper wire rod by 5.7% (13.5 thousand tonnes).

The volume of sales of precious metals was lower versus the prior year - silver sales amounted to 1 179 tonnes and were lower by 5.5% (68 t), while gold sales decreased by 21.4% (180 kg) and amounted to 660 kg.

**Table 6. Sales volume for basic products**

	Unit	2009	2010	2011	Change 2010=100
Copper and copper products	'000 t	509.9	545.3	566.9	104.0
- of which export *	'000 t	390.5	406.0	445.8	109.8
Silver	t	1 198	1 247	1 179	94.5
- of which export *	t	1 150	1 214	1 147	94.5
Gold	kg	818	840	660	78.6
- of which export *	kg	755	647	435	67.2

\* including sales to European Union countries

**Table 7. Revenues from the sale of products (in '000 PLN)**

	2009	2010	2011	Change 2010=100
Copper and copper products	8 815 919	12 837 041	15 179 193	118.2
- of which export *	6 733 784	9 521 850	11 942 097	125.4
Silver	1 731 718	2 467 928	4 066 646	164.8
- of which export *	1 663 074	2 404 682	3 959 755	164.7
Gold	84 721	101 504	111 866	110.2
- of which export *	78 563	78 706	80 297	102.0
Other products and services	332 978	423 869	619 361	146.1
- of which export *	4 023	6 700	6 214	92.7
<b>Total</b>	<b>10 965 336</b>	<b>15 830 342</b>	<b>19 977 066</b>	<b>126.2</b>
<b>- of which export *</b>	<b>8 479 444</b>	<b>12 011 938</b>	<b>15 988 363</b>	<b>133.1</b>

\* including sales to European Union countries

Total revenues from the sale of KGHM Polska Miedź S.A. products in 2011 amounted to PLN 19 977 066 thousand, and were higher by 26.2% than revenues achieved in 2010, mainly due to higher copper and silver prices and an increase in the amount of copper sold. Revenues from the sale of copper and copper products were higher by 18.2%. Revenues from silver sales versus their level in 2010 were higher by 64.8%, while revenues from gold sales were higher by 10.2%.

Revenues from the sale of products in 2011 reflect the result from the settlement of hedging instruments in the amount of PLN 241 565 thousand (in the prior year PLN 142 187 thousand).

### Geographical structure of product sales

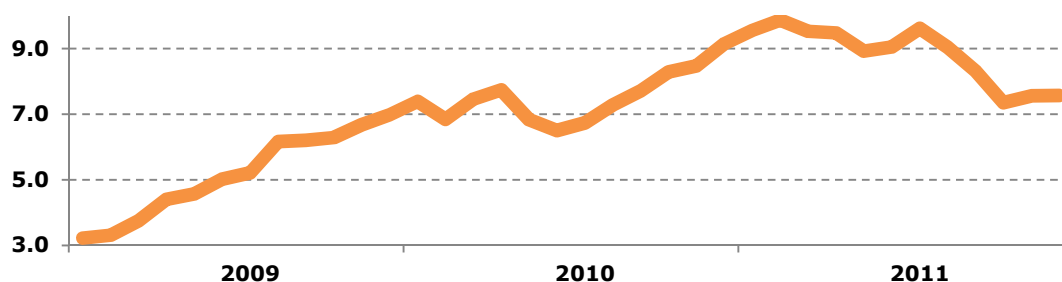
In 2011 the volume of domestic sales of copper and copper products represented 21.4% of total copper sales, with export and European Union sales accounting for 78.6%. During this period, the largest foreign customers for copper produced by KGHM Polska Miedź S.A. were Germany, China, Italy and the Czech Republic. During 2011 domestic silver sales amounted to 2.7% of the total volume of silver sales, while export and European Union sales accounted for 97.3% of sales volume. The largest foreign customers for silver were Great Britain, the USA and Belgium.

### Macroeconomic sales conditions

In 2011 the highest prices in history were recorded, for both industrial as well as precious metals. The maximum official copper price on the London Metal Exchange was recorded on 14 February and amounted to 10 148 USD/t. The highest official silver price in history on the London Bullion Market Association was recorded on 28 April, when the price of this metal reached 48.7 USD/troz.

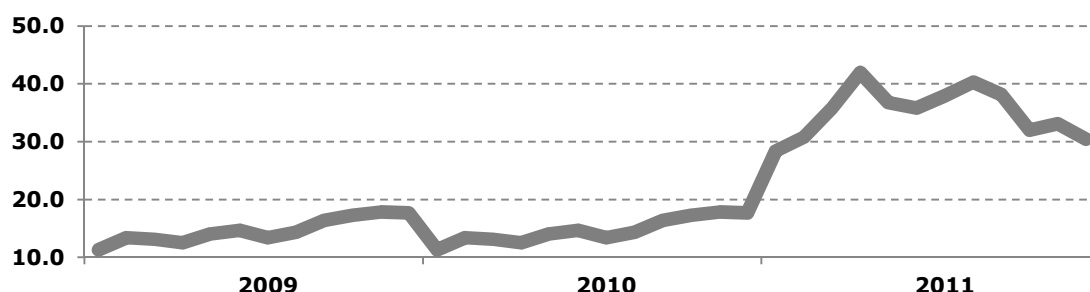
The average annual **electrolytic copper price** in 2011 on the London Metal Exchange (LME) amounted to 8 811 USD/t and was 16.9% higher than in 2010, when it reached 7 539 USD/t.

**Chart 1. Copper prices on the LME ('000 USD/t)**



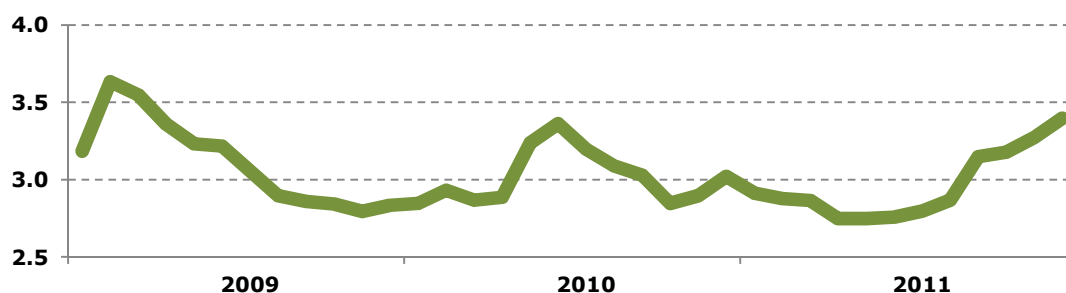
The average annual **silver price** on the London Bullion Market Association (LBMA) in 2011 amounted to 35.12 USD/troz (1 129 USD/kg), which means an increase by 73.9% versus the average price in 2010: 20.19 USD/troz (649 USD/kg).

**Chart 2. Silver prices on the LBMA (USD/troz)**



From the start of the year until April 2011, the Polish zloty systematically strengthened versus the USD and EUR. However, at the start of May the situation on the financial market diametrically changed. The Polish currency began to lose its value versus the currencies of developed countries, with the pace of weakening increasing towards the end of the year. **The average USD/PLN exchange rate (NBP)** in 2011 amounted to 2.96 USD/PLN and was lower versus the prior year by 2.0% (3.02 USD/PLN).

**Chart 3. USD/PLN exchange rate per the NBP**



The macroeconomic factors of greatest importance for the Company's operations are presented in Table 8.

**Table 8. Macroeconomic factors of importance for the Company's operations**

	Unit	2009	2010	2011	Change 2010=100
Average copper prices on the LME	USD/t	5 164	7 539	8 811	116.9
Average silver prices on the LBMA	USD/troz	14.67	20.19	35.12	173.9
Average NBP USD/PLN exchange rate	USD/PLN	3.12	3.02	2.96	98.0

### Position of the Company on the copper and silver markets

The position of the Company on the copper market with respect to the ranking of copper production in concentrate and the ranking of refined copper production was as follows:

- according to preliminary estimated data from CRU International, in 2011 global copper mine production amounted to 16 001 thousand tonnes. In this period, KGHM Polska Miedź S.A. produced 426.7 thousand tonnes of copper in concentrate, representing 2.7% of global production.
- global production of refined copper, according to preliminary estimates of the CRU, amounted to 18 805 thousand tonnes. Refined copper production in the Company amounted to 571.0 thousand tonnes, representing 3.0% of global production.

In 2011 global silver mine production amounted to 776 million ounces (estimated data from CRU International). During this period the Company produced 37.5 million ounces of silver in concentrate, representing 4.8% of global production of this metal.

### 1.4. Contracts significant for the activities of the Company

**Table 9. Contracts significant for the activities of the Company signed in 2011**

Date	Value of contract	Description of contract
<b>Trade contracts</b>		
<b>18.01.2011</b>	from USD 622 901 thousand to USD 753 428 thousand (from PLN 1 796 943 thousand to PLN 2 173 490 thousand)*	The sale of copper wire rod and oxygen-free copper rod in 2011 entered into with Tele-Fonika Kable Sp. z o.o. S.K.A.
<b>4.02.2011</b>	USD 692 093 thousand (PLN 1 967 205 thousand)*	The sale of copper cathodes in 2011 entered into with MKM Mansfelder Kupfer und Messing GmbH
<b>15.06.2011</b>	from PLN 4 033 517 thousand to PLN 4 400 200 thousand*	The sale of copper wire rod in the years 2012-2013 entered into with nkt cables GmbH Cologne and its subsidiaries (i.e. nkt cables Warszawice Sp. z o.o., nkt cables Kladno s.r.o., nkt cables Velke Mezerici k.s., nkt cables Vrchlabi k.s., nkt cables a/s Asnaes)
<b>20.12.2011</b>	from USD 1 827 713 thousand to USD 3 655 426 thousand (from 6 300 126 thousand to 12 600 252 thousand)*	The sale of copper cathodes in the years 2012-2016 entered into with China Minmetals Corporation
<b>Equity investment and divestment agreements (detailed information on the execution of these agreements may be found on pages 123-126)</b>		
<b>30.06.2011</b>	PLN 3 672 147 thousand (relating to the 24.39% share owned by KGHM in Polkomtel S.A.)	Preliminary agreement to sell 100% of the shares of Polkomtel S.A. signed by KGHM, Polski Koncern Naftowy ORLEN S.A., PGE Polska Grupa Energetyczna S.A., Vodafone Americas Inc, Vodafone International Holdings B.V. and Węglkokoks S.A. (as sellers) and Spartan Capital Holdings Sp. z o.o. (purchaser)
<b>29.09.2011</b>	PLN 968 927 thousand **	Contingent binding agreement for the sale of 100% of the shares of Telefonía DIALOG S.A. entered into with Netia S.A. (purchaser)
<b>9.11.2011</b>	PLN 3 672 147 thousand (relating to the 24.39% share owned by KGHM in Polkomtel S.A.)	Final agreement for the sale of 100% of the shares of Polkomtel S.A. realising the agreement dated 30 June 2011
<b>6.12.2011</b>	CAD 2 872 524 thousand (9 442 944 thousand)*	Binding conditional agreement to purchase 191 501 611 shares of Quadra FNX Mining Ltd. entered into with Quadra FNX Mining Ltd.
<b>16.12.2011</b>	PLN 968 927 thousand	Dispositive agreement on sale of 100% of the shares of Telefonía DIALOG S.A. with the brokerage Dom Inwestycyjny BRE Banku S.A. (acting in its own name, though on behalf of Netia S.A.).

\* amount estimated using the exchange rate from the date of signing of the agreement or the day after

\*\* final value of sale reflecting adjustment by the amount set forth in the agreement

There was no instance of dependence on a single or multiple customers or suppliers. In 2011 the share of any customer exceeded 10% of the revenues from sales of KGHM.

The only supplier whose share of supply exceeded 10% of the revenues from sales of KGHM Polska Miedź S.A. is the subsidiary KGHM Metraco S.A. in Legnica, whose sales to KGHM Polska Miedź S.A. represent 27% of the value of purchases.

The high level of supplies from this company is related to the operating model of the Group, based on which a business goal of KGHM Metraco S.A. is the comprehensive servicing of KGHM Polska Miedź S.A., with respect to specific raw materials and products ensuring continuity of the production line of KGHM Polska Miedź S.A., based on its own logistical and expediting operations.

## Information on contracts for the auditing or review of the separate or consolidated financial statements

The entity entitled to audit the separate financial statements of the Company and the consolidated financial statements of the KGHM Polska Miedź S.A. Group is PricewaterhouseCoopers Sp. z o.o. with its registered head office in Warsaw, Al. Armii Ludowej 14, 00-638 Warsaw.

The contract which was signed on 25 May 2010 is in force for review of the half-year financial statements and for the audit of the annual financial statements for the years 2010, 2011 and 2012.

Detailed information on the amount of remuneration of the entity entitled to audit the financial statements for the review and audit of the financial statements, and remuneration for other purposes is shown in Note 36 of the financial statements.

### 1.5. Employment and remuneration

#### Employment and structure

Employment in KGHM Polska Miedź S.A. at the end of 2011 amounted to 18 615 persons, which was slightly lower than at the end of the prior year. Average annual employment in KGHM Polska Miedź S.A. amounted to 18 578. Due to further centralisation of accounting and investment functions in the Head Office, there was a change in the employment structure.

**Table 10. End-of-period employment**

	2009	2010	2011	Change 2010=100
Mines	12 397	12 645	12 604	99.7
Smelters	3 931	3 869	3 810	98.5
Other divisions	2 085	2 125	2 201	103.6
<b>Total</b>	<b>18 413</b>	<b>18 639</b>	<b>18 615</b>	<b>99.9</b>

#### Average remuneration

With respect to remuneration policy, in 2011 work was continued on activities to increase the motivational aspect of remuneration. The increase in remuneration was due to individual increases in salary categories and the payment of premiums and bonuses, among others based on supervisor evaluations.

In 2011, in comparison to 2010, the total average salary increased by 3.9%, and excluding the annual bonus based on Company profit, by 4.1%.

**Table 11. Total average monthly remuneration**

	2009	2010	2011	Change 2010=100
Mines	8 476	8 994	9 371	104.2
Smelters	6 769	7 306	7 429	101.7
<b>Total</b>	<b>8 097</b>	<b>8 640</b>	<b>8 980</b>	<b>103.9</b>

#### Relations with the trade unions

In 2011, a variety of meetings were held with the trade unions, among others with respect to the demands put forth by the unions:

1. An increase in basic salary rates by PLN 300 for each salary category,
2. Inclusion in the Collective Labour Agreement for the Employees of KGHM Polska Miedź S.A. of the Employee Retirement Plan in force in the Company,
3. An increase to 7% of the contribution to the Employee Retirement Plan,
4. Inclusion in the Collective Labour Agreement of the medical package in force in the Company,
5. A final agreement on acceptable conditions to buy out the employee coal equivalent due under paragraph 50 of the Collective Labour Agreement – followed by a referendum, and after receiving the positive opinion of the employees, signing by the entitled parties to the Collective Labour Agreement.

During the course of negotiations, the Management Board presented the following position regarding the aforementioned demands:

#### Ad.1.

The Management Board of KGHM Polska Miedź S.A. does not accept a remuneration policy aimed at salary increases unassociated with increases in productivity, the impact of the effects of work at various job positions on the results of the Company, and working conditions. Any increase in funds for remuneration should in the

first instance be allocated to jobs which are directly related to production and should stimulate an increase in productivity. The actions begun in 2011 will be continued. Taking into consideration the possibility of creating additional funds through increased production, the Company will increase the initially-planned amount of funds for remuneration, to be allocated to motivational salary solutions, i.e. an increase in salary categories of individual employees and to the payment of bonuses and premiums from the motivational fund.

**Ad.2. and 4.**

The Management Board of KGHM Polska Miedź S.A. consented to the inclusion in the Collective Labour Agreement of clauses related to the functioning in the Company of employee retirement plans and medical packages, based on principles of voluntary participation of employees taking advantage of these benefits.

**Ad.3.**

The Management Board sees the possibility of increasing contributions to the Employee Retirement Plan by 1 percentage point, to 6 percent, under condition that rights to the entitlements due following retirement or disability will only cover existing employees and retirees, and will not be extended to future employees.

**Ad.5**

The Management Board proposed the buyout of the coal equivalent for the pre-tax amount of PLN 17 thousand per employee and retiree, and consented to put this proposal to a referendum. The buyout of the coal equivalent would have been contingent on the removal from the Collective Labour Agreement of provisions related to entitlement to the coal equivalent following retirement. In the referendum held on 8-9 November 2011, the majority of employees voted against the resolution. As a result, the Company withdrew from the proposed buyout of the coal equivalent.

**Assumptions for 2012**

In 2012 there are no substantial changes foreseen in the level of employment, while with respect to remuneration policy over the next several years it is assumed that the annual increase in average remuneration excluding payment of the annual bonus for earned profit will amount to 1 percentage point above inflation. The final amount and rate of change in total average remuneration will depend on realisation of the aforementioned assumptions and the amount of profit earned. In 2012, a new system of remuneration will be proposed to the trade unions.



## 2. Investments and development

### 2.1. Company Strategy

On 23 February 2009, the Supervisory Board of KGHM Polska Miedź S.A. approved the Strategy of KGHM Polska Miedź S.A. for the years 2009 – 2018. In realising the Strategy, KGHM Polska Miedź S.A. intends to become a major, global copper producer and to increase copper production in the Group to approx. 700 thousand tonnes annually.

Due to the sale of the telecom assets in 2011 (Telefonia DIALOG S.A., Polkomtel S.A.) the Supervisory Board of the Company, on 10 October 2011, approved the updated Strategy of the Company, removing the strategic goal „Continued investment in the telecommunications sector”.

The Strategy for the years 2009-2018 is based on five pillars:

**Pillar I - Improving productivity**, aimed at reversing/halting the trend of rising unit production costs through:

- investments in new technology,
- modernisation of infrastructure,
- optimisation of production procedures and organisation.

**Pillar II - Developing the resource base**, aimed at increasing the production of mined copper in the Group to 700 thousand tonnes annually, through:

- developing the system for mining deep ore,
- mining new regional ore deposits,
- acquisitions in the mining sector,
- intensifying the processing of scrap.

**Pillar III - Diversifying sources of revenues and gaining independence from energy prices**, which assumes that by 2018 approx. 30% of the Company revenues will be generated from outside the core business, through:

- entrance into the power sector.

**Pillar IV - Regional support** - the creation of 750 new jobs and development of social activities through:

- the creation of jobs using the infrastructure of KGHM Letia S.A.,
- supporting regional sport, health, arts, education and the regional environment.

**Pillar V - Developing organisational know-how and capabilities** through:

- management through goals,
- transparent information and data,
- Company staff development, and
- building a holding structure.

### 2.2. Realisation of the Strategy in the years 2009-2011

In 2011, KGHM Polska Miedź S.A. consistently implemented the approved Strategy by investing in a continuously updated portfolio of strategic projects to achieve the intended goals of each pillar's strategic initiatives.

#### Pillar I – Improving productivity

Of fundamental importance to building Company value in the long term was the continuation of activities in the copper sector as the basic source of Company revenues. As a result, work on strategic tasks was continued, of which, apart from investment projects described in the section „Capital expenditure” of this report (pages 126-127), of particular importance are the following:

- the „Effectiveness” program, of which, since 2009, 38 programs have been implemented: 22 with respect to TOP cost reduction programs and 16 process transformation programs (based on Lean Management) aimed at improving production efficiency,  
With respect to cost reduction programs, 260 workshops were held (involving 2 500 employees), thanks to which it was possible to select for implementation over 300 savings-related initiatives and many process-related initiatives improving labour organisation. Measurable effects from the implementation of individual initiatives are continuously recognised in the operating plans of the Parent Entity. With respect to process transformation programs, a variety of initiatives were initiated aimed at improving productivity (such as better use of work time in mining, optimisation of the production process in smelting). The following areas are being analysed in terms of initiating further efficiency improvement programs.

- the project to centralise procurement in the KGHM Group – the Central Procurement Office opened in 2009 continued to follow a common procurement policy for the Division and the KGHM Group, thanks to which the Company gained substantial added value and savings in the area of procurement, mainly investments.

## **Pillar II – Developing the resource base**

Taking advantage of its solid market position, production skills and capacity to finance capital-intensive investments, KGHM Polska Miedź S.A. intensively realised its Strategy with respect to development of its resource base.

### **Global resource projects**

In execution of its strategic efforts to increase production to 700 thousand tonnes of mined copper and to achieve diversification in terms of production costs, KGHM Polska Miedź S.A.:

- acquired in 2010 the Afton-Ajax copper/gold project located in British Columbia, Canada,
- began the process of the friendly acquisition of the mining company Quadra FNX Mining Ltd listed on the Toronto Stock Exchange in Canada.

Detailed information on these activities may be found in the section Equity investments (page 125-126) of this report.

### **Regional projects**

To secure the production of electrolytic copper from its own concentrate at a stable level over the long term, in 2011 the Company continued work on developing its resource base in south-western Poland and in the region of Lusatia (Germany, Saxony):

- work was continued on the project commenced in 2006 of accessing the region „Głogów Głęboki Przemysłowy” (Deep Głogów),
- a program of geological work was carried out in the licensed mine region „Gaworzyce-Radwanice”,
- a project was commenced to explore the mine region „Synklina Grodziecka”, located in the vicinity of the so-called Old Copper Belt near the city of Bolesławiec,
- assumptions were prepared for the geological project of exploration of the copper ore deposit „Nowiny” located near the German border in the south-eastern part of the Żar pericline,
- work was continued on the copper ore exploration project „Weisswasser” in Germany,
- geological documentation work was carried out in the licensed region of the nickel ore deposit „Szklary”, north of Żabkowice Śląskie,
- technological and organisational requirements for realisation of a project to increase salt production from 425 thousand tonnes to 1 million tonnes/year.

### **Scrap processing unit at the Legnica smelter**

As part of the process of preparing decisions on the potential realisation of the project, conceptual work was carried out, which will be continued in 2012, to develop decisions regarding the future of the project.

## **Pillar III – Diversifying sources of revenues and gaining independence from energy prices**

In 2011, KGHM continued to realise its investments in the energy sector. From the point of view of KGHM, power generation is one of the most attractive sectors, as it is not correlated with conditions on the metals markets and represents a stable source of revenues. The most important projects for the Company in this regard are the following projects:

- **„Construction of gas-steam blocks at the Głogów and Polkowice power plants”** with installed capacity of 90 MWe and planned power generation of 560 GWh, all of which will be used to meet the power needs of KGHM Polska Miedź S.A. Realisation of this project to generate power from internal sources will satisfy over 30% of KGHM's power needs starting from 2013.
- **„Construction of a power generation source with a sector partner based on the utilisation of natural gas as the raw material for its generation, on the grounds of the existing Blachownia Power Plant”** - work was continued in cooperation with the sector partner Tauron Wytwarzanie S.A., including:
  - selection of the natural gas scenario for the investment,
  - the Principles of Cooperation between Tauron, KGHM and PKE were updated, with respect to expansion of the agreement from 2009 by provisions relating to the natural gas scenario and timeline,
  - the Partnership Agreement was updated and the project's business assumptions were developed,
  - the proceedings were pursued before the European Commission as the appropriate monopoly control body regarding concentration based on establishment of the joint venture Elektrownia Blachownia Nowa sp. z o.o.,
  - the process was begun of obtaining corporate approvals to establish the special purpose vehicle.

– **„Production of synthetic gas through the underground gasification of brown coal in the Copper Belt (LGOM)”**

During the first stage of the project, a study was performed to develop a preliminary concept for management of the brown coal deposit in terms of constructing a pilot installation for the underground gasification of the deposit. A project was developed for the geological exploration and investigation of the brown coal deposit in the region of Głogów in category C1. A request was filed for a license to explore and investigate selected sections of the brown coal deposit in the LGOM region. In 2012 geological and investigative work is planned on the deposit.

**Pillar IV – Regional support**

A significant element of the Company's business operations and increasing its value is corporate social responsibility. In 2011 work was performed on the preparation of a **Strategy of Corporate Social Responsibility (CSR)** for KGHM Polska Miedź S.A., which will enable the creation of a comprehensive system for looking at questions involving the corporate social responsibility of the Company and integration of actions undertaken up to now in this regard. Thanks to combining CSR strategy with the business pillars of the Strategy, it will be possible to properly manage relations with the Company's stakeholders, and in this way to achieve the Company's strategic goals.

Due to the specific nature of the mining and smelting industry, KGHM has a particular responsibility for its operations. Some important examples of CSR initiatives dedicated to the region and meeting its needs are:

- the commencement in 2011 of a Program to Promote Health and Counteract Environmental Threats,
- a project to utilise and revitalise the terrain of the former „Obora” sand pit,
- social and charitable programs for the region,
- tasks undertaken related to the KGHM LETIA S.A. Technology Park aimed at creating an attractive region to conduct business and to invest in activities based on new technology.

In 2011, KGHM Polska Miedź S.A. was honoured with the prestigious Fray International Sustainability Award for significant contribution to the initiation, implementation and development of balanced and environmentally-friendly solutions in mining and processing.

**Pillar V – Developing organisational know-how and capabilities**

In human resource management solutions in KGHM Polska Miedź S.A., work continued on implementation of a **Social Potential Management System**, realising projects aimed at:

- development of the education and improvement system,
- career planning and skills management and the management of knowledge,
- optimising the process of recruitment and adaptation,
- the employee evaluation system, internal communication system and shaping the organisational culture,
- ensuring appropriate employee motivation.

Among activities related to improving and developing organisational and management potential in the Company, the following should be noted:

- completion of the **accounting and financial services reorganisation project**, based on the creation of a modern, centralised accounting and finance organisation to ensure the high quality and functionality of the financial and accounting services,
- the introduction of a **new management model for the KGHM Polska Miedź S.A. Group** based on a separate business supervisory unit to facilitate the management and supervision of Group companies,
- the commencement of a project to develop and implement methodological standards for the **management of projects, programs and portfolios** in KGHM Polska Miedź S.A.,
- equity investments in health and curative spas, renewable energy and new technology realised under the auspices of the Closed-End Investment Funds managed by KGHM TFI S.A.

To meet the changes occurring in the external environment of KGHM Polska Miedź S.A., at the end of 2011 work began aimed at maintaining the current effective implementation of the Strategy as well as preparing assumptions for updating the Strategy with respect to the assumptions made in the Pillars.

### 2.3. Equity investments

As at 31 December 2011, KGHM Polska Miedź S.A. directly owned shares of 23 subsidiaries, 2 other companies (in which the share is less than 20%) and investment certificates in 3 closed-end non-public investment funds. Seven direct subsidiaries (KGHM Ecoren S.A., PHP „MERCUS” sp. z o.o., POL-MIEDŹ TRANS Sp. z o.o., „Energetyka” sp. z o.o., BIPROMET S.A., Fermat 1 S.à r.l. and KGHM I FIZAN) have their own capital groups.

KGHM Polska Miedź S.A. has equity investments in entities engaged in various businesses. They offer products and services both related to the core business of KGHM Polska Miedź S.A. (including exploring for and mining deposits of copper ore and other metals, mine construction, power generation and heat production, mining machinery and equipment, production of explosives and research and development) as well as services unrelated to the core business of KGHM Polska Miedź S.A., such as transportation, health-related services and cash investing.

In 2011, the subsidiaries of KGHM Polska Miedź S.A. did not enter into significant transactions with related entities under other than arm's length conditions.

In February 2011, the Management Board of KGHM Polska Miedź S.A. decided to implement a new management model for the KGHM Polska Miedź S.A. Group. Introduction of the new model is aimed at adapting supervision over the activities of the Group to the strategy and investment policy of KGHM Polska Miedź S.A., which involves increasing the activities of the Group with regard to acquisitions and realising activities aimed at increasing value. The new management model is based on introducing supervision over the activities of Group companies based on separate business units. The companies of the Group and projects are distributed within these units as follows:

- **Production** – includes Group companies supporting the core business (CB) and planned acquisitions (resource assets in production). This unit will also include companies/resource projects once they have begun production,
- **International expansion and resource base development** – includes exploration companies and pre-production companies/ projects,
- **Equity-portfolio investments** – includes companies of a financial investment nature and investment funds managed by KGHM TFI S.A.,
- **Diversified investments in the Energy sector** – includes strategic energy investments and other energy investments not related directly to the CB,
- **Commerce and hedging** – includes domestic and foreign trade companies,
- A group of entities realising Corporate Social Responsibility - CSR,
- An Insurance Services Center – includes TUW-CUPRUM.

The management model adopted involves the expansion of supervision over Group companies, beyond that exercised up to now (performed by appropriate organisational units of the Head Office), to include business supervision carried out by individual separated units through the managers of these units designated by the Management Board of KGHM Polska Miedź S.A.

Diagram 2 presents entities by business units, in which KGHM Polska Miedź S.A. directly held shares and investment certificates as at 31 December 2011. The remaining entities of the Group, which are not directly related with KGHM Polska Miedź S.A., are supervised under the units in which their parent entities are located.

**Diagram 2. Entities in which as at 31 December 2011 KGHM Polska Miedź S.A. directly held shares and investment certificates**

**KGHM Polska Miedź S.A.**

**Production**

PeBeKa S.A. (100%)

DFM ZANAM-LEGMET  
Sp. z o.o. (100%)

KGHM CUPRUM  
sp. z o.o. – CBR (100%)

INOVA Spółka z o.o.  
(100%)

„Energetyka” sp. z o.o.  
(100%)

CBJ sp. z o.o. (100%)

BIPROMET S.A. (66%)

**International expansion and resource base development**

KGHM Kupfer AG \*  
(100%)

Fermat 1 S.à r.l. (100%)

KGHM AJAX MINING INC.  
(51%)

Abacus Mining & Exploration  
Corporation (7.6%)

**Equity-portfolio investments**

KGHM Ecoren S.A.  
(100%)

PHP „MERCUS” sp. z o.o.  
(100%)

POL-MIEDŹ TRANS Sp. z  
o.o. (100%)

KGHM TFI S.A. (100%)

KGHM I FIZAN (100%)

KGHM I FIZAN (100%)

KGHM III FIZAN (100%)

NITROERG S.A. (85%)

**Commerce and hedging**

KGHM Metraco S.A.  
(100%)

KGHM (SHANGHAI) COPPER  
TRADING CO., LTD. (100%)

KGHM Kupferhandelsges.  
m.b.H.i.L (in liquidation) (100%)

**Diversified investments in the Energy sector**

TAURON Polska  
Energia S.A. \*\* (10.39%)

**Group of entities realising Corporate Social Responsibility**

„MIEDZIOWE CENTRUM  
ZDROWIA” S.A. (100%)

Zagłębie Lubin S.A.  
(100%)

KGHM LETIA S.A.  
(85.45%)

**Insurance Services Center**

TUW - CUPRUM (100%)

**Other companies**

KGHM CONGO S.P.R.L.  
in liquidation (100%)

\* name changed, previously KGHM HMS Bergbau AG

\*\* share of KGHM Polska Miedź S.A. according to current report dated 23 March 2011

### Significant changes in the KGHM Group

In 2011, total equity investments amounted to PLN 639 771 thousand, meaning a decrease versus the prior year by PLN 681 346 thousand. These amounts also reflect expenditures on the purchase of listed companies shares.

#### Sale of the shares of Polkomtel S.A.

On 9 November 2011, an agreement was entered into for the sale of 100% of the shares of Polkomtel S.A. The agreement was signed by KGHM Polska Miedź S.A., PKN Orlen S.A., PGE Polska Grupa Energetyczna S.A., Vodafone Americas Inc, Vodafone International Holdings B.V. and Węglokoks S.A. and Spartan Capital Holding Sp. z o.o., in performance of the preliminary agreement for the sale of 100% of Polkomtel S.A.'s shares signed on 30 June 2011 between the parties. The transfer of ownership of the shares took place on the date the agreement was signed, i.e. 9 November 2011.

Pursuant to the agreement, KGHM Polska Miedź S.A. sold the shares it held in Polkomtel S.A. representing 24.39% of the share capital of Polkomtel S.A. (all of the shares held by KGHM Polska Miedź S.A.), for the total price of PLN 3 672 147 thousand. Profit on the transaction, before taxation, amounted to PLN 2 512 200 thousand.

#### Sale of the shares of DIALOG S.A.

On 16 December 2011, KGHM Polska Miedź S.A. sold to Netia S.A. 19 598 000 shares of DIALOG S.A. with its registered head office in Wrocław with a nominal value of PLN 25 per share and a total nominal value of PLN 489 950 thousand, representing 100% of the share capital of DIALOG S.A.

The sale of these shares took place in performance of obligations arising from the contingent binding agreement on the sale of the shares of DIALOG S.A. entered into between KGHM Polska Miedź S.A. and Netia S.A. on 29 September 2011 („Contingent Agreement”). The final price at which the Company sold these shares was calculated in accordance with the formula set forth in the Contingent Agreement, and amounted to PLN 968 926 898. Profit on the transaction, before taxation, amounted to PLN 144 001 thousand.

#### Purchase of the shares of NITROERG S.A.

On 2 February 2011, an agreement was signed with the Minister of the State Treasury for the purchase by KGHM Polska Miedź S.A. of 85% of the shares of NITROERG S.A. in Bieruń, for PLN 120 052 thousand. The shares were paid in cash.

The control held by KGHM Polska Miedź S.A. over „NITROERG” S.A. (one of the largest producers of explosive materials), enables the strengthening of competitiveness in supplying the production needs of the core business, as well as new future resource projects (in accordance with realisation of the strategy of increasing the copper ore resource base).

#### Purchase of the shares of KGHM HMS Bergbau AG (currently KGHM Kupfer AG)

On 20 April 2011, KGHM Polska Miedź S.A. purchased from HMS Bergbau AG, 25.1% of the shares of KGHM HMS Bergbau AG for EUR 128 thousand, i.e. PLN 509 thousand. The share of the KGHM Polska Miedź S.A. Group in the share capital of KGHM HMS Bergbau AG following purchase amounts to 100%.

On 27 April 2011, the Ordinary General Meeting of KGHM HMS Bergbau AG resolved to increase the share capital of the company from EUR 50 thousand to EUR 800 thousand. The newly-issued shares, with a nominal value of EUR 1 per share and an issue price of EUR 17.71, were acquired by KGHM Polska Miedź S.A. and paid in cash in the amount of PLN 52 364 thousand on 27 April 2011.

On 16 May 2011, the court registered change of name of the company from KGHM HMS Bergbau AG to KGHM Kupfer AG.

KGHM Polska Miedź S.A. decided to purchase the shares of KGHM HMS Bergbau AG from the German shareholder, in order to independently continue the exploration project „Weisswasser” (exploration for and investigation of deposits of copper and other metals in the region).

#### Purchase of the shares of Uzdrowisko „Świeradów-Czerniawa” sp. z o.o.

On 20 September 2011, the investment fund KGHM I FIZAN, a subsidiary of KGHM Polska Miedź S.A., purchased from the State Treasury 87.74% shares of Uzdrowisko „Świeradów-Czerniawa” sp. z o.o. with its registered head office in Świeradów Zdrój for the total amount of PLN 21 000 thousand.

The purchase by KGHM I FIZAN of shares of Uzdrowisko „Świeradów-Czerniawa” sp. z o.o. is a subsequent step in the realisation of the investment policy of the fund, comprising among others the development of a Polish Spa Group, which will enable enrichment of the offering of spa and tourism services and utilisation of the effects of synergy.



### **Foundation of the companies Fermat 1 S.à r.l. and Fermat 2 S.à r.l.**

On 30 December 2011, KGHM Polska Miedź S.A. founded a company under the name Fermat 1 S.à r.l. with its registered head office in Luxembourg. The share capital of the newly-founded entity is EUR 12 500. KGHM Polska Miedź S.A. acquired 100% of the share capital of Fermat 1 S. à r.l., paid in cash in the amount of EUR 12 500.

On 30 December 2011, Fermat 1 S.à r.l. founded a company under the name Fermat 2 S.à r.l. with its registered head office in Luxembourg. The share capital of the newly-founded entity is EUR 12 500. Fermat 1 S. à r.l. acquired 100% of the share capital of Fermat 2 S.à r.l., paid in cash in the amount of EUR 12 500.

In addition, at the start of 2012, Fermat 2 S.à r.l. founded a special purpose company under the name 0929260 B.C. Unlimited Liability Company in Canada, while Fermat 1 S.à r.l. founded a company under the name Fermat 3 S.à r.l. in Luxembourg.

The foundation of these entities is related to the creation of an optimal transaction structure for acquiring the shares of Quadra FNX.

### **Combination of subsidiaries: Walcownia Metali Nieżelaznych Sp. z o.o. and WM „ŁABĘDY” S.A.**

In January 2011, the companies Walcownia Metali Nieżelaznych Sp. z o.o. and WM „ŁABĘDY” S.A. were combined through the founding of a new entity called Walcownia Metali Nieżelaznych „ŁABĘDY” S.A.

The share capital of the newly-founded company amounts to PLN 49 145 thousand and was set based on the sum of the share capital of the combined entities amounting to PLN 97 898 thousand, less the share of the company WM „Łabędy” S.A. in the share capital of Walcownia Metali Nieżelaznych spółka z o.o. prior to the combination, in the amount of PLN 45 985 thousand, and the coverage of losses from prior years in the amount of PLN 2 768 thousand. The share of the Group in the share capital of the newly-founded company amounts to 84.96%.

### **Liquidation of companies**

Due to the conclusion of liquidation procedures, the following companies were de-registered:

- KGHM Polish Copper Ltd. in liquidation - de-registered on 23 December 2011,
- „Serwis-Erg” Sp. z o.o. in liquidation - de-registered on 18 October 2011,
- FADROMA S.R. SP. Z O.O. in liquidation - de-registered on 12 August 2011.

### **Opening of proceedings to liquidate KGHM Kupferhandelsges. m.b.H.**

On 30 May 2011 the Extraordinary General Shareholders' Meeting of KGHM Kupferhandelsges. m.b.H. with its registered head office in Vienna resolved to dissolve and liquidate the company as at 1 June 2011 and to appoint a liquidator. The request to liquidate the company was filed at the Commercial Court in Vienna.

The decision to liquidate KGHM Kupferhandelsges.m.b.H. is connected with the takeover by KGHM Polska Miedź S.A. of the commercial activities of this company.

### **Major equity investments by KGHM Polska Miedź S.A.**

Major equity investments include the following:

- Investments with respect to international expansion and resource base development. This unit includes exploration companies, companies founded to support resource projects and other related. Although the amount of capital committed to these entities at the moment of preparation of this report is not significant, from the point of view of realisation of the Strategy of KGHM Polska Miedź S.A., these investments should be considered as important. Below is a description of the status of realisation of the Afton-Ajax project as well as activities undertaken towards the purchase of Quadra FNX Mining Ltd.
- Investments with respect to production, which includes companies supporting the core business of KGHM Polska Miedź S.A. and are tasked with ensuring its operational continuity.

In terms of the amount of capital committed, a significant equity investment involves the shares of TAURON Polska Energia S.A. (carrying amount PLN 974 292 thousand). This investment also plays a part in the realisation of the strategy of diversification into the energy sector. In 2011, KGHM Polska Miedź S.A. purchased 71 292 212 shares of TAURON Polska Energia S.A. for the total amount PLN 438 448 thousand, mainly from the State Treasury in an accelerated bookbuilding transaction. Following realisation of this transaction, KGHM Polska Miedź S.A. owned a total of 182 110 566 shares of TAURON Polska Energia S.A., representing 10.39% of the share capital (pursuant to a current report dated 23 March 2011). The carrying amount of the shares of TAURON Polska Energia S.A. was PLN 974 292 thousand.

#### **KGHM AJAX MINING INC.**

In execution of its strategic efforts to increase production to 700 thousand tonnes of mined copper and to achieve diversification in terms of production costs, KGHM Polska Miedź S.A. acquired in 2010 the Afton-Ajax copper/gold project located in British Columbia, Canada, being the first step in KGHM's realisation of its strategy to become a global mining company.

In accordance with a signed investment agreement on the joint advancement of the Afton-Ajax project, the Company acquired 51% of shares in the company founded with the Canadian company Abacus Mining & Exploration Corporation - AJAX MINING INC. – together with options to acquire further 29% of the shares. Execution of this option is possible following publication of the Bankable Feasibility Study, and simultaneously obliges the Company to organise project financing. In addition, 8.75% of the shares of Abacus Mining & Exploration were acquired (at the end of 2011 this share amounted to 7.6%).

In 2011, the Bankable Feasibility Study for the Afton-Ajax project was completed. The document describes the specific technical and economic conditions related to the construction and operation of the future copper and gold mine located in the vicinity of the town of Kamloops in Canada.

The Study confirmed the chief geologic and mining parameters of the Ajax project, which until now had been estimated in a preliminary report from 2009. Measured & Indicated mineral resources increased to 512 million tonnes (previous 442 million tonnes) of ore containing 0.31% (0.30%) copper and 0.19 g/t (0.19 g/t) of gold. Proven & Probable mineral reserves were calculated at 1.34 million tonnes of copper and 2.75 million ounces of gold. Average annual production of copper and gold in concentrate amounts respectively to 50 thousand tonnes of copper and 100 thousand ounces of gold. Mine life was calculated at 23 years.

The cost of producing one tonne of mined copper (C1 – cash costs reflecting the value of associated metals) was calculated within the range of 1 740 USD – 2 800 USD.

Mine construction will last two years. Considering the progress to date and the time needed to obtain further permits and administrative approval, the start-up date for the mine has been set at 2015. Capital expenditure for the project was estimated at USD 795 million. Having received the BFS, KGHM Polska Miedź S.A. is considering whether to exercise its option to increase its share in AJAX MINING INC. from 51% to 80% (the deadline for making this decision, under the agreement, is 4 April 2012).

#### **Process of purchase of Quadra FNX Mining Ltd.**

KGHM Polska Miedź S.A. and Quadra FNX Mining Ltd. (hereafter Quadra FNX) signed on 6 December 2011 a binding conditional agreement, under which KGHM could purchase from existing shareholders, under a Plan of Arrangement recommended by the Board of Directors of Quadra FNX, 191 501 611 shares, representing 100% of the share capital of Quadra FNX.

In accordance with the agreement, the purchase price was CAD 15.00 per share, i.e. the total price on the date of signing the agreement amounts to CAD 2.87 billion (the equivalent of PLN 9.44 billion at the average CAD/PLN exchange rate of the National Bank of Poland of 6 December 2011), representing a premium of 41% above the 20 trading day volume-weighted average price (VWAP).

Closure of the transaction was made contingent on the fulfilment of conditions precedent, consisting of gaining shareholder approval as expressed by a majority 2/3 of the votes at the General Meeting of Quadra FNX, approval of the Supreme Court of British Columbia in Canada for the transaction and regulatory approvals by appropriate monopoly-control bodies, and by the Canadian Minister of Industry.

All the conditions precedent foreseen in the agreement were fulfilled and on 5 March 2012 there was a closure of the transaction.

The company 0929260 B.C. Unlimited Liability Company with its registered head office in Vancouver, as an indirect subsidiary of KGHM, purchased on 5 March 2012 from the former shareholders of Quadra FNX 193 334 154 shares of Quadra FNX, for the price of CAD 15.00 per share, i.e. the total price of CAD 2 900 012 thousand (the equivalent of PLN 9 147 219 thousand at the average CAD/PLN exchange rate of the National Bank of Poland of 5 March 2012). The aforementioned number of shares includes 1 832 543 shares of Quadra FNX which arose after the date of signing of the agreement as a result of a conversion of instruments (options and warrants) issued by Quadra FNX, which are convertible to shares.

The decision was simultaneously taken to delist the shares of Quadra FNX from the trade on the Toronto Stock Exchange and to change on 12 March 2012 the company's name to KGHM International Ltd.

To realise this transaction, a structure has been created within which, in December 2011, the companies Fermat 1 S.à r.l. and Fermat 2 S.à r.l. with their registered head offices in Luxembourg were founded, while at the start of 2012 the company Fermat 3 S.à r.l. in Luxembourg was founded as well as a company under the name 0929260 B.C. Unlimited Liability Company in Canada. All of these entities are wholly-owned subsidiaries of KGHM Polska Miedź S.A.

Purchase of Quadra FNX will enable an increase in production in the KGHM Polska Miedź S.A. Group by over 100 thousand tonnes of copper annually, starting from 2012, and by 2018 by over 180 thousand tonnes.



Furthermore, commencement of the Sierra Gorda project in Chile (2014) and Victoria in Canada will lead to a substantial reduction in the unit cost of copper production in the KGHM Polska Miedź S.A. Group. Purchase of these shares was financed from the Company's internal cash resources, from a surplus arising from operating activities and the sale of the telecom assets (the shares of Polkomtel S.A. and DIALOG S.A.).

### Intentions as regards equity investments

The intentions of KGHM Polska Miedź S.A. as regards equity investments are mainly aimed at:

- development of the resource base, aimed at increasing mined copper production in the Group,
- realisation of investments in the energy sector,
- financial support of Group companies to realise investment programs,
- diversification of investment risk through participation in the Closed-End Investment Funds managed by KGHM TFI S.A.

Development of the resource base is the chief assumption of the strategy realised by KGHM Polska Miedź S.A. Equity investments in this regard are aimed at financing exploration work, mine investments and acquisitions of mining entities.

Equity investments realised in the energy sector are aimed at diversifying income sources and gradually becoming independent of changes in energy prices. Investment projects realised in this regard reflect among others the acquisition of alternative energy sources.

Plans with respect to equity investments include also further acquisitions of the investment certificates of Closed-End Investment Funds (managed by KGHM TFI S.A. – a wholly-owned subsidiary of KGHM Polska Miedź S.A.). This investment is of a long-term nature, is not related with the core business and does not require operational involvement in the activities of Fund companies. The Funds are of a sector nature, and their chief areas of focus are: protection of health, renewable energy sources, new technology and property.

Realising a strategy of responsibility towards local communities, KGHM Polska Miedź S.A. intends to continue investments of social importance.

In addition, activities will be continued aimed at liquidating the company KGHM CONGO S.P.R.L. with its registered head office in Lubumbashi in the Democratic Republic of Congo, and at liquidating KGHM Kupferhandelsges. m.b.H.and.L in Vienna, which was begun in 2011.

## 2.4. Capital expenditure

In 2011, capital expenditures amounted to PLN 1 518 509 thousand and were higher than in the prior year by 20%. The realised amount of investments is lower than assumed (according to the forecast dated 21 December 2011 – PLN 1 645 000 thousand) although, due to more favourable prices, their physical scope is near the planned one.

**Table 12. Capital expenditure ('000 PLN)**

	2009	2010	2011	Change 2010=100
Mining	833 507	985 097	1 056 553	107.3
Smelting	218 998	230 798	218 404	94.6
Other activities	17 307	47 097	238 941	x5.1
Capitalised uncompleted development	394	644	4 611	x7.2
<b>Total</b>	<b>1 070 206</b>	<b>1 263 636</b>	<b>1 518 509</b>	<b>120.2</b>

In terms of the capital expenditures in 2011 presented in Table 12, development-related investments amounted to PLN 853 097 thousand (an increase of 15% versus the prior year).

Analysis of the capital expenditures realised in the Company showed a segregation of projects into small, repeatable projects related primarily to the need to replace assets, and projects of significantly greater difficulty, size and risk which have a substantial impact on the Company's development and the realisation of its strategy.

As a result of the aforementioned analysis, assumptions were developed to reorganise investment activities and to segregate capital expenditures into:

- **centrally-realised projects** – development- and replacement-related investments of particular importance for the Company, which in 2011 amounted to PLN 616 918 thousand (41%),
- **locally-realised projects** – these are replacement-related projects, and typical/repeatable development projects, minor conformatory and purchases, which in 2011 amounted to PLN 896 980 thousand (59%).

Responsibility for the management of centrally-realised investments is assigned to project leaders, and for those locally-realised to Division directors. In classifying projects as central or local, the following is considered:

- the unrepeatability of the activity and its result – uniqueness of the product,
- the degree of complication of the project (is it interdisciplinary),
- whether the project is high risk,
- the need to segregate the organisational structure of the project if the functional structure does not permit its realisation.

The major investment projects realised in 2011 are presented in Table 13:

**Table 13. Major projects and facilities realised in 2011**

Mining
Construction of the SW-4 shaft – work continued on sinking the shaft – since work started the depth of the shaft has reached 872.9 meters, while 212.5 meters of drifts have been excavated
Głogów Głęboki-Przemysłowy - work continued on realisation of drifts with infrastructure - in 2011, 2 375 meters of drifts were excavated and preparatory work to sink the GG-1 shaft was performed (work was completed on the drilling of 18 freeze holes)
With respect to modernisation and replacement of the machinery park in the mines, 226 mining machines were purchased
In the mining divisions, work was carried out on investments related to development of the infrastructure of the mining sections, ventilation and cooling equipment and investments in the conveyor belts and pipelines
With respect to the replacement of floatation machinery, 25 floatation machines were renovated and work was completed on the machinery development project for the years 2012- 2013
As part of the exploration project „Investigation and documentation of the Synklina Grodziecka region of the „Niecka grodziecka” deposit, 7 drillholes were made with work begun on an 8th hole. The results obtained from chemical analysis of ore series core samples from the first three drillholes showed that they meet the criteria applied to the deposits mined by KGHM. The remaining core samples are undergoing testing
Facilities were realised related to improving and maintaining the safe operation of the Żelazny Most tailings treatment pond and to elimination of its environmental impact
Realisation was continued on the project „Development of the Żelazny Most mining tailings treatment pond to ensure the ability to store floatation tailings after 2016”
As part of the project Licensing 2013, geological information was purchased for 7 of the basic mining areas of KGHM Polska Miedź S.A.
Realisation began on the project Achieving rock salt production of 1 million tonnes/year; geological information was purchased on the deposit, tenders were held and equipment delivery began
As part of the project „Development and implementation in the mines of KGHM Polska Miedź S.A. of technology for the mechanical extraction of ore” (automated extraction machinery), the testing site for the ACT complex was prepared
Realisation was continued on the project „Ore Extraction Information Management System” – IT applications were realised, whose task is to support the ore extraction management process in terms of the project's main goal, which is the creation of conditions for the organisation and realisation of production control (analysis of various extraction scenarios)
As part of the project „System for the operation and servicing of underground machinery (CMMS)” a system for the operation and servicing of machinery was implemented at the Lubin mine, with preparation of the system for implementation in 2012 at the other mining divisions
Smelting
As part of the Pyrometallurgy Modernisation Program – during the reporting period preparatory work was performed so as to realise the investment without operational interference with working equipment
The 4th Doerschel furnace was brought into operation
Investments were realised involving among others renovation of the sulphuric acid plant, the concentrate warehouse, modernisation of a smelting furnace and the scrap warehouse, replacement of electrofilters and construction of the electrolyte tubs
Other
As part of the project „Construction of Gas-Steam Blocks in the Powerplants in Głogów and Polkowice”, foundation construction continued by the General Investment Contractor in the Powerplants in Głogów and Polkowice, with delivery and assembly of recovery boilers and gas turbo units

## 2.5. Environmental protection

### Activities of the Company on behalf of environmental protection

The idea of balanced growth, and in particular respect for the environment, is an important element of the strategy of KGHM Polska Miedź S.A. The extraction of copper ore, followed by its processing at all stages of production, is inextricably linked to its impact on various aspects of the environment. Adherence to strict environmental standards, mandated by law, is possible thanks to the systematic modernisation of installations serving the environment, both those built in the past as well as new investments in this area. In 2011 the Company spent PLN 213 675 thousand on the realisation of projects related to environmental protection. The increase in investments versus the year 2010 by PLN 134 706 thousand is due to Construction of Gas-Steam Blocks in the Powerplants in Głogów and Polkowice. Expenditures on this investment amounted to PLN 170 287 thousand.

### Environmental fees

Total environmental fees paid by the Divisions of KGHM Polska Miedź S.A. in 2011 amounted to PLN 25 479 thousand. The amount of fees paid was lower by PLN 1 228 thousand than fees paid in 2010, despite the annual increase in fees due to inflation.

In 2011 the largest fees paid by the Company were for waste discharge: PLN 16 261 thousand, including PLN 16 257 thousand for the drainoff of excess water from the Żelazny Most waste treatment tailings pond.

### Legal aspect and intentions

KGHM Polska Miedź S.A. operates eight installations whose functioning, in accordance with the Act on Environmental Protection, requires the possession of integrated permits. These include:

- an installation for the production of metallic copper using shaft furnace and flash furnace technology, an installation for the production of precious metals, an installation for the production of lead and an installation for tailings waste – settling pond unit IV, and other installations at the smelter which do not require integrated permits at the Głogów smelter,
- an installation titled The Biechów industrial waste storage facility at the Głogów smelter,
- an installation titled The Biechów II industrial waste storage facility at the Głogów smelter,
- an installation for the production of refined lead at the Legnica smelter,
- an installation for the production of metallic copper from copper concentrate and of products recovered from metallurgical and electronic processes, the tailings waste facility „Polowice”, a temporary storage facility for lead-bearing concentrates and other installations on the grounds of the Legnica smelter,
- an installation for the melting, continuous casting and drawing of copper rod at the Cedynia Wire Rod Plant,
- an installation for the storage of tailings from the floatation of copper ore at the Tailings Plant, and
- an installation for the neutralisation of sulphuric acid waste at the Ore Enrichment Plants.

On 23 January 2012 the Voivodeship Administrative Court in Warsaw issued a judgment after reviewing an appeal of the farmer's society Stowarzyszenie Samoobrona Ekologiczna Rolników Indywidualnych „PRONATURA” regarding a change of a decision on integrated permits. The court revoked the decision which was appealed against and stated that it cannot be executed until the judgment becomes legally binding. The decision of the VAC is not yet legally binding.

The change in the decision involved among others the construction and operation of a fourth Doerschel furnace. The Głogów smelter remains in possession of integrated permits which enable operation of the Lead Section and of the three other Doerschel furnaces without exceeding the permitted parameters of this installation. The Głogów smelter operates in accordance with the aforementioned integrated permits.

The remaining Divisions of the Company possess environmental sector administrative decisions.

In 2011 the most important task of a formal-legal nature carried out by the Company was preparation of a report on the environmental impact of a project involving the extraction of ore from the Company's mine regions and the submission of an application for the issuance of a decision regarding the environmental conditions for this project, which is necessary in the process of obtaining a license for the underground extraction of copper ore after 2013.

Work was also completed on a report on the environmental impact of the Żelazny Most waste treatment facility, and a decision was obtained regarding the environmental conditions for this facility. A mining waste management program was developed which was approved by the Marshal of Lower Silesia. An application was also submitted for the granting of permission to operate a mining waste treatment facility, in which was included the approved program together with a decision on environmental conditions. This work was required by the Law on mining waste, according to which Żelazny Most is a mining waste treatment facility, and by 1 May 2012 the Company is obliged to conform its operations with this law.

Due to on-going changes in environmental law and the resulting changes in modernisation and in installations, it was necessary to prepare appropriate documentation for all of the smelters, mines and ore enrichment plants, and to apply either for the issuance of new or for changes in existing environmental decisions.

The Company has achieved a high level of technical solutions which enable the operation of installations in accordance with prevailing environmental law. Amongst the most important investments planned in the near term are the following:

- continuation of a program to promote health and prevent environmental threats – aimed at the inhabitants of former protective zones,
- adaptation of administrative decisions to legal changes,
- preparing the Company to participate in the European system for trading CO<sub>2</sub>,
- obtaining a decision on environmental conditions for enterprises involved in the underground excavation of ores,
- work related to ensuring the security of the Żelazny Most tailings pond, such as strengthening the containment dam,
- continued modernisation of atmospheric protection equipment at the smelters,
- work related to the restoration of land following liquidation of a shaft at the Polkowice – Sieroszowice mine,
- registration by 1 June 2018 with respect to REACH: selenium and gold as end substances and silver chloride and copper chloride as indirect substances,
- detailed analysis of new ECHA guidelines, which tighten permissible conditions for indirect products.

### 3. Review of financial position

#### 3.1. Assets

As at 31 December 2011, total assets amounted to PLN 29 253 189 thousand, meaning an increase by PLN 9 423 893 thousand (48%) versus the end of 2010.

**Table 14. Current and non-current assets ('000 PLN)**

	31.12.2009	31.12.2010	31.12.2011	Change 2010=100	Structure
Property, plant and equipment	5 937 513	6 551 111	7 277 903	111.1	24.9
Shares and investment certificates in subsidiaries and associates	3 075 171	3 802 993	2 012 209	52.9	6.9
Deferred tax asset	167 062	359 833	168 462	46.8	0.6
Available-for-sale financial assets	17 700	1 155 017	992 068	85.9	3.4
Derivatives	321 281	697 860	1 759 053	×2.5	6.0
Trade and other receivables	1 424 771	2 480 594	1 587 165	64.0	5.4
Inventories	1 890 286	2 011 393	2 355 741	117.1	8.1
Cash and cash equivalents	975 198	2 595 529	12 835 999	×4.9	43.9
Other assets	144 048	174 966	264 589	151.2	0.9
<b>Total assets</b>	<b>13 953 030</b>	<b>19 829 296</b>	<b>29 253 189</b>	<b>147.5</b>	<b>100.0</b>

The most important changes in major items of assets in 2011 were in:

- Cash and cash equivalents – carrying amount: PLN 12 835 999 thousand (an increase by PLN 10 240 470 thousand)

In 2011, KGHM Polska Miedź S.A. earned an operating profit in the amount of PLN 9 363 553 thousand, which generated cash resources. In addition, the Company concluded the sale of its telecom assets, increasing the result on other operations by PLN 2 662 245 thousand. Cash generated from basic and other operations were mainly invested in short-term deposits to prepare for the financing of the Company's investment projects (Quadra FNX Mining Ltd. and AJAX MINING INC.).

- Property, plant and equipment – carrying amount: PLN 7 277 903 thousand (an increase by PLN 726 792 thousand)

The main cause of the increase in property, plant and equipment was the realisation of investments – expenditures in this regard amounted to PLN 1 513 898 thousand, of which replacement-related investments amounted to PLN 660 801 thousand.

- Shares and investment certificates – carrying amount: PLN 2 012 209 thousand (a decrease by PLN 1 790 784 thousand)

In November and December 2011, the Company finalised the sale of its telecom assets (Polkomtel S.A., DIALOG S.A.), which decreased the carrying amount of investments in subsidiaries and associates in total by PLN 1 984 873 thousand. Also in 2011, the company Nitroerg S.A., a leading Polish producer of explosive materials, joined the KGHM Polska Miedź S.A. Group (carrying amount of the shares: PLN 121 272 thousand). In addition, due to an increase in the share capital, the carrying amount of the shares of KGHM Kupfer AG increased by PLN 53 818 thousand (realisation of exploration work) and of KGHM Metraco S.A. by PLN 15 000 thousand (realisation of the project „Construction and operation of the Sulphuric Acid Trading Base”).

- Derivatives – carrying amount: PLN 1 759 053 thousand (an increase by PLN 1 061 193 thousand.)

The change in derivatives (net) was due to a change in the forward prices of metals, the settlement of derivatives in 2011 and the opening of new transactions on the copper, silver and currency markets.

- Receivables – carrying amount: PLN 1 587 165 thousand (a decrease by PLN 893 429 thousand)

There was a substantial decrease in Company trade receivables (by PLN 623 118 thousand). This decrease also affected deposits with a maturity of over 12 months (mid-term) presented as financial receivables. By the end of 2011 these deposits were terminated, which decreased receivables by PLN 351 130 thousand.

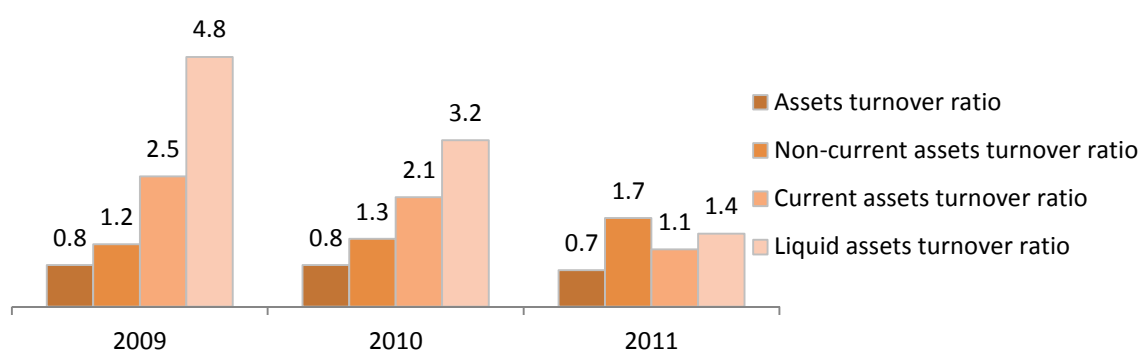
- Available-for-sale financial assets – carrying amount: PLN 992 068 thousand (a decrease by PLN 162 949 thousand).

The change versus 2010 was due to an increase in non-current assets and a decrease in current assets:

- non-current - an increase by PLN 242 244 thousand, mainly due to the acquisition of further shares of Tauron Polska Energia S.A., alongside a negative impact of measurement (a decrease in share price on the WSE). The shares of Tauron Polska Energia S.A. are the main item in non-current available-for-sale financial assets,
- current – at the end of 2010, current available-for-sale financial assets consisted of participation units of open-end liquid investment funds in the amount of PLN 405 193 thousand. In the third quarter of 2011, the Company sold all of the assets it held in this regard.

The sale of the shares of Polkomtel S.A. and DIALOG S.A. led to a substantial increase in cash and cash equivalents, alongside a worsening in assets effectiveness ratios, being relations of revenues from sales to total assets and current assets. The non-current assets turnover ratio increased from 1.3 to 1.7.

**Chart 4. Assets effectiveness ratios**



*Ratios calculated based on end-of-year balances, pursuant to methodology described in Appendix A.*

### 3.2. Equity and liabilities

In 2011 the basic source for financing assets was equity, whose share in total assets increased from 73% to 79%. In 2011 the Company did not make use of borrowing. At the end of the year there were finance lease liabilities.

**Table 15. Equity and liabilities ('000 PLN)**

	31.12.2009	31.12.2010	31.12.2011	Change 2010=100	Structure
<b>Equity</b>	<b>10 403 957</b>	<b>14 456 477</b>	<b>23 135 511</b>	<b>160.0</b>	<b>79.1</b>
Share capital	2 000 000	2 000 000	2 000 000	100.0	6.8
Accumulated other comprehensive income	127 228	211 159	535 673	×2.5	1.8
Retained earnings	8 276 729	12 245 318	20 599 838	168.2	70.4
<b>Current and non-current liabilities</b>	<b>3 549 073</b>	<b>5 372 819</b>	<b>6 117 678</b>	<b>113.9</b>	<b>20.9</b>
Trade and other payables	1 393 521	1 742 188	1 839 115	105.6	6.3
Borrowings and finance lease liabilities	17 685	11 455	93	0.8	0.0
Derivatives	334 857	1 193 432	868 667	72.8	3.0
Current corporate tax liability	78 183	668 924	1 587 847	×2.4	5.4
Employee benefits liabilities	1 191 521	1 221 287	1 323 826	108.4	4.5
Provisions for other liabilities and charges	533 306	535 533	498 130	93.0	1.7
<b>Total liabilities and provisions</b>	<b>13 953 030</b>	<b>19 829 296</b>	<b>29 253 189</b>	<b>147.5</b>	<b>100.0</b>

There were significant changes in the following items of equity and liabilities:

- Equity – carrying amount PLN 23 135 511 thousand (an increase by PLN 8 679 034 thousand)

The increase in equity is mainly the result of a raise in retained earnings by PLN 8 354 520 thousand, due to the higher profit for the period (PLN 11 334 520 thousand in 2011; PLN 4 568 589 thousand in 2010), alongside a higher than in 2010 dividend payout (PLN 2 980 000 thousand in 2011, PLN 600 000 thousand in 2010)

- Current corporate tax liability – carrying amount PLN 1 587 847 thousand (an increase by PLN 918 923 thousand)

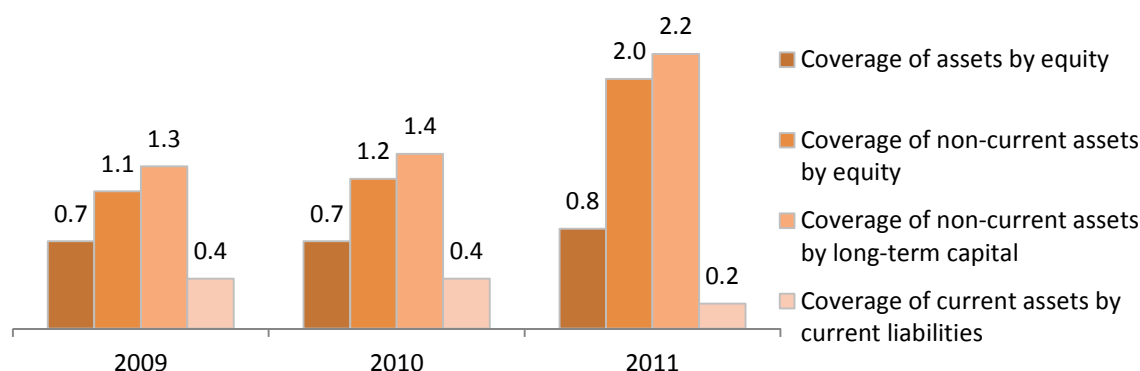
The increase in the current corporate tax liability was due to the higher amount of taxable income. Both in 2010 as well as in 2011, the Company paid monthly instalments on income tax in advances.

- Derivatives – carrying amount: PLN 868 667 thousand (a decrease by PLN 324 765 thousand.)

Due to a change in forward metals prices, the forward USD/PLN exchange rate, the settlement of instruments during the year and the opening of new transactions on the copper, silver and currency markets, liabilities due to derivatives (net) changed. In the case of the copper market there was a decrease in liabilities by PLN 632 571 thousand, while for the silver and currency markets there was an increase in liabilities by respectively PLN 34 015 thousand and PLN 273 791 thousand.

The increase in current assets due to the Company's anticipated investment projects was the primary reason for the decrease in the ratio describing the coverage of current assets by current liabilities. The other assets financing ratios increased versus their levels at the end of 2010.

**Chart 5. Assets financing ratios**



*Ratios calculated based on year-end balances, in accordance with methodology described in Appendix A.*

#### Contingent assets and liabilities

As at 31 December 2011, contingent assets of the Company amounted to PLN 373 223 thousand and related mainly to guarantees received (in the amount of PLN 167 018 thousand), mainly related to securities to cover potential claims by the Company due to the non-execution or improper execution of agreements by contractors) and to overpayment of the tax on underground mines (PLN 85 489 thousand). Other contingent assets primarily involve disputed State budget issues, promissory note receivables and implementation of projects and inventions.

Contingent liabilities at the end of 2011 amounted to PLN 141 430 thousand, including PLN 113 967 thousand due to implementation of projects and inventions.

### 3.3. Financial resources of the Company

The structure of the Company's cash and cash equivalents is presented in the table below:

**Table 16. Structure of cash and cash equivalents ('000 PLN)**

	31.12.2009	31.12.2010	31.12.2011	Change 2010=100
Cash*	8 685	50 234	8 454	16.8
Other monetary assets with a maturity up to 3 months	966 513	2 545 295	12 827 545	×5.0
<b>Total</b>	<b>975 198</b>	<b>2 595 529</b>	<b>12 835 999</b>	<b>×4.9</b>

\* in hand and on-demand bank deposits

Financial income from the depositing of periodically unallocated cash and cash equivalents and financial investments is presented below:

**Table 17. Income from the depositing of periodically unallocated cash and cash equivalents and short-term investments ('000 PLN)**

	31.12.2009	31.12.2010	31.12.2011	Change 2010=100
On-demand bank deposits	887	3 985	1 820	45.7
Securities and participation units	-	4 158	16 855	×4.1
Fixed term bank deposits	69 453	46 514	171 172	×3.7
<b>Total</b>	<b>70 339</b>	<b>54 657</b>	<b>189 847</b>	<b>×3.5</b>

Periodically unallocated cash and cash equivalents generated income in the amount of PLN 189 847 thousand. The increase in income was due to the significant increase in the Company's cash and cash equivalents and to higher interest rates.

#### Bank and other loans received

In 2011, KGHM Polska Miedź S.A. did not make use of financing in the form of bank loans. As at 31 December 2011, the Company did not hold financing in the form of loans.

#### Loans granted and received and financial guarantees

On 21 December 2009, KGHM Polska Miedź S.A. granted a loan to „Energetyka” sp. z o.o. in the amount of PLN 50 300 thousand. Interest on the loan is based on WIBOR 1M + a margin of 2.77%, with interest payable monthly. Repayment is in forty equal instalments in the amount of PLN 1 258 thousand payable at the end of each quarter, beginning from 31 March 2010. In 2011, „Energetyka” sp. z o.o. made partial repayment on the loan in the amount of PLN 5 030 thousand. As at 31 December 2011, the balance of the loan granted was PLN 40 968 thousand.

In 2011, the Company granted no financial guarantees, although it held a customs guarantee with a maturity to 1 March 2013. The guarantee is a contingent liability which do not significantly affect the Company's liquidity risk.

#### Evaluation of investment goals realisation versus the resources held, reflecting possible changes in the structure of financing these activities

The cash and cash equivalents currently held by the Company and its creditworthiness guarantee the realisation of its investment goals, both in terms of equity investments as well as capital expenditures.



### 3.4. Statement of comprehensive income

In 2011, the Company realised a profit for the period in the amount of PLN 11 334 520 thousand, the highest in the history of KGHM Polska Miedź S.A.

**Table 18. Statement of comprehensive income – basic items ('000 PLN)**

	2009	2010	2011	Change 2010=100
Sales	11 060 540	15 945 032	20 097 392	126.0
Operating costs	7 863 635	9 287 686	10 733 839	115.6
<b>Profit from operations</b>	<b>3 196 905</b>	<b>6 657 346</b>	<b>9 363 553</b>	<b>140.6</b>
Profit on other operating activities	(98 813)	(1 019 198)	4 324 087	x
– Profit on the sale of companies	-	34	2 662 245	x
– Exchange differences	(61 664)	(30 445)	895 164	x
– Measurement and realisation of derivatives	(538 637)	(1 172 284)	320 919	x
– Dividends	454 848	146 658	277 330	189.1
– Other	46 640	36 839	168 429	×4.6
<b>Operating profit (EBIT)</b>	<b>3 098 092</b>	<b>5 638 148</b>	<b>13 687 640</b>	<b>×2.4</b>
Finance costs	31 523	32 581	34 043	104.5
Profit before income tax	3 066 569	5 605 567	13 653 597	×2.4
<b>Profit for the period</b>	<b>2 540 185</b>	<b>4 568 589</b>	<b>11 334 520</b>	<b>×2.5</b>
EBITDA (EBIT + depreciation/amortisation)	3 645 745	6 253 616	14 360 013	×2.3

In relation to 2010, profit for the period increased by 2.5-times, i.e. by PLN 6 765 931 thousand. The most important factors impacting the change in the result are presented in Table 19.

**Table 19. Basic factors impacting the change in the financial result**

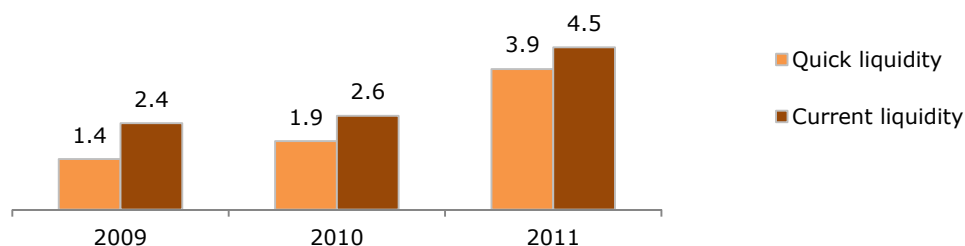
Item	Impact on change in result ('000 PLN)	Description
<b>Change in prices of basic products (Cu, Ag)*</b>	+3 752 055	Copper prices higher by 17% and silver by 74%
<b>Sale of telecom assets</b>	+2 656 201	Profit realised on Polkomtel S.A. sales, before taxation (PLN 2 512 200 thousand) and DIALOG S.A. (PLN 144 001 thousand) increased the result on other operating activities
<b>Impact of hedging transactions</b>	+1 592 581	Includes the change in the result due to measurement and realisation of derivatives (+PLN 1 493 203 thousand) and the change in adjustment of revenue due to hedging (+PLN 99 378 thousand)
<b>Operating costs</b>	(1 446 158)	An increase in the total unit cost of electrolytic copper production in PLN/t by 4.5%
<b>Income tax</b>	(1 282 099)	An increase in the financial result caused higher taxation. In addition, the change in the level of taxation was impacted by tax-deductible costs related to the sale of DIALOG S.A, which were higher than the recognised cost of sale of the shares due to recognition of an impairment loss (as at 31 December 2010 deferred tax on this difference was not recognised). The impact on the tax amounted to PLN 220 516 thousand.
<b>Exchange differences</b>	+925 609	The high level of cash and cash equivalents in foreign currencies accumulated due to planned investment expenditures and changes in the exchange rate gave this item major significance in the statement of comprehensive income
<b>Change in volume of sales of basic products (Cu, Ag)*</b>	+368 894	An increase in the volume of copper sales by 21.6 thousand t alongside lower silver sales by 68 t
<b>Change in exchange rate*</b>	(280 892)	A change in the exchange rate from 3.02 USD/PLN to 2.96 USD/PLN

\* Impact on sales

## Financial ratios

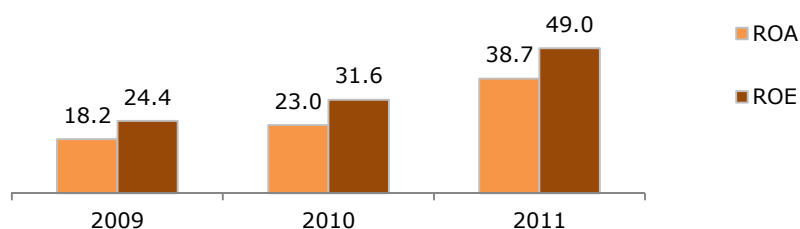
The levels of the basic liquidity, the assets and equity profitability and the financing ratios is shown in Charts 6, 7 and 8.

**Chart 6. Liquidity ratios**



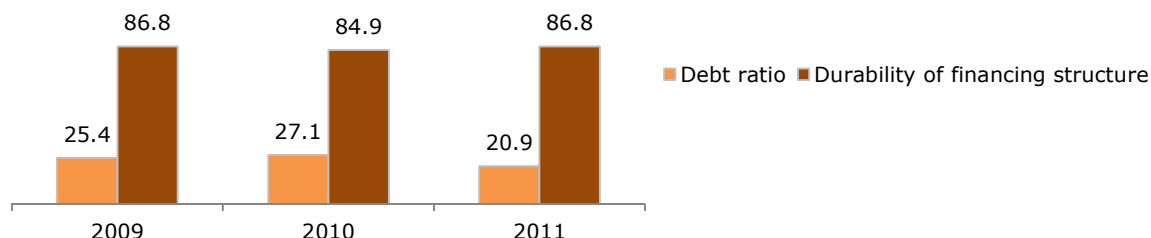
Liquidity ratios show the relationship of current assets, or their more liquid part, to current liabilities. The increase in the liquidity ratios was mainly due to an increase in cash and cash equivalents.

**Chart 7. Profitability ratios**



The increase in the profit brought an improvement in the return on assets (ROA) and the return on equity (ROE) ratios.

**Chart 8. Financing ratios**



The decrease in the debt ratio is due to a lower rate of increase of liabilities (13.9%) than equity (60.0%). On the contrary, the financing structure durability ratio increased from 84.9 to 86.8, mainly due to an increase in the share of equity and non-current liabilities in the financing sources structure.

## Capital market ratios

The activities of the Company are described by the following ratios:

**Table 20. Capital market ratios**

		2009	2010	2011
EPS (PLN)	Profit for the period / number of shares	12.70	22.84	56.7
P/CE	Price per share / financial surplus per share *	6.9	25.9	1.9
P/E	Price per share / earnings per share	8.3	7.6	2.0
MC/S	Market capitalisation**/ revenues from sales	1.9	2.2	1.1
P/BV	Price per share / book value per share ***	2.0	2.4	1.0

\* Financial surplus = profit for the period + depreciation/amortisation

\*\* Market capitalisation represents total shares outstanding times share price from the last day of the year (200 million shares x PLN 106.00 in 2009; PLN 173.00 in 2010; PLN 110.60 in 2011)

\*\*\* Carrying amount of the equity at the end of the reporting period

The capital market ratios were substantially impacted in 2011 by the high profit earned by the Company and by the fall in the share price of KGHM from PLN 173.00 at the end of 2010 to PLN 110.60 at the end of 2011.

### 3.5. Operating costs

The Company's operating costs are decisively impacted by the costs of electrolytic copper production, whose share in the Company's costs is over 93%.

**Table 21. Unit cost of electrolytic copper production - total (PLN/t)**

	2009	2010	2011	Change 2010=100
Pre-precious metals credit cost of copper production	13 944	15 540	17 534	112.8
Value of anode slimes	2 774	2 557	3 968	155.2
Total unit cost of copper production	11 170	12 983	13 566	104.5
Electrolytic copper production ('000 t)	502.5	547.1	571.0	104.4

The pre-precious metals credit unit cost of copper production (unit cost prior to decrease by the value of anode slimes containing among others silver and gold) in 2011 increased versus 2010 by 1 994 PLN/t, i.e. by 12.8%, mainly due to an increase in the value of purchased copper-bearing materials (+1 010 PLN/t) due to a higher volume of consumption by 4% (4.6 thousand tonnes of copper) and of purchase prices by 22%.

**Table 22. Unit cost of electrolytic copper production – from own concentrate (PLN/t)**

	2009	2010	2011	Change 2010=100
Pre-precious metals credit unit cost of copper production	13 153	13 661	14 875	108.9
Value of anode slimes	3 403	3 174	4 576	144.2
Total unit cost of copper production	9 750	10 487	10 299	98.2
Electrolytic copper production from own concentrate ('000 t)	398.6	427.0	446.4	104.5

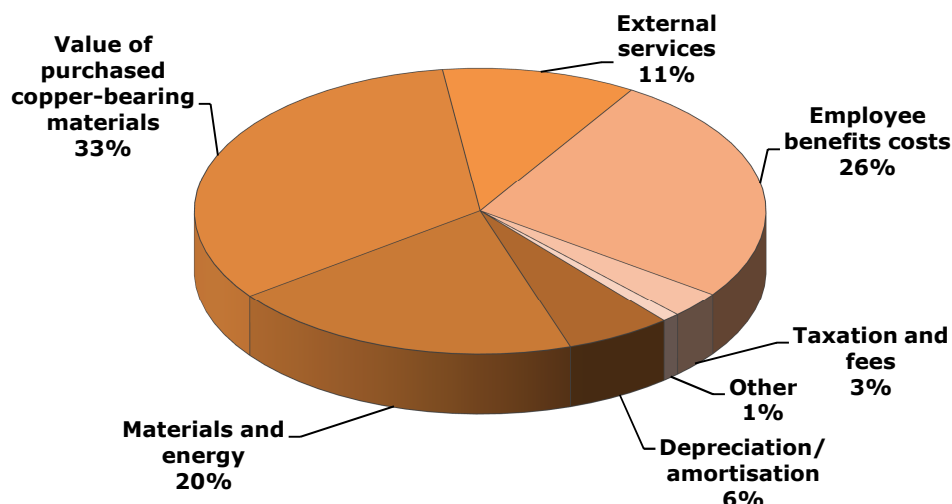
The pre-precious metals credit unit cost of copper production from own concentrate increased by 1 214 PLN/t, i.e. by 8.9%, mainly due to an increase in the expenses by nature described below (excluding purchased copper-bearing materials), alongside the positive impact of a higher volume of copper production from own concentrate (+4.5% in relation to 2010).

In 2011 total expenses by nature increased by PLN 1 660 328 thousand, i.e. by 17.6%, mainly due to:

- the higher value of purchased copper-bearing materials (PLN 880 640 thousand) due to an increase in purchase prices and in the volume of consumption by 10.7 thousand tonnes of copper (of which 4.6 thousand tonnes relates to electrolytic copper production),
- external services (PLN 227 028 thousand) – mainly due to an increase in the scope of mining preparation work (+9 km) (PLN 118 197 thousand),
- materials and fuel (PLN 214 731 thousand) – mainly due to an increase in prices,
- labour costs (PLN 193 530 thousand) – mainly due to higher provisions for future employee benefits by PLN 72 773 thousand,
- depreciation/amortisation (PLN 56 905 thousand) – due to an increase in realised investments in property, plant and equipment (+20%).

The structure of expenses by nature in 2011 is shown in Chart 9. With respect to prior years, the change in the structure is mainly due to higher consumption of purchased copper-bearing materials (in 2009: 23%, in 2010: 30%) alongside the lower share of employee benefits costs (in 2009: 31%, in 2010: 28%)

**Chart 9. Structure of expenses by nature in 2011**



### 3.6. Risk management in the Company in 2011

The goal of financial risk management in KGHM Polska Miedź S.A. is to restrict the undesired impact of financial factors on cash flow and Company results in the short and medium terms and to build Company value over the long term. Financial risk management includes both the processes of risk identification and measurement as well as its restriction to acceptable levels. The process of risk management is supported by an appropriate policy, organisational structure and procedures applied in the Company.

In 2011, KGHM Polska Miedź S.A. was exposed to many types of financial risk, and in particular to market risks (risk of changes in metal prices and exchange rates), credit risk and liquidity risk.

#### Market risk

In 2011, the Company was mainly exposed to the risk of changes in the prices of metals sold on the market: copper, silver and gold. In addition, of major significance for KGHM was the risk of changes in currency rates, in particular the USD/PLN rate. It is a generally accepted practice on the commodity markets that contracts for the physical supply of metals are either concluded or denominated in USD, although the base currency for the Company is the PLN. To restrict market risk, the Company, to the extent possible, uses natural hedging (incurring costs in USD), however the basic technique in market risk management involves hedging strategies utilising derivatives.

Similarly as in prior years, in 2011 the Company applies a consistent and step-by-step approach to market risk management. Over time consecutive hedging strategies are implemented, embracing an increasing share of production and sales revenues as well as an extended time horizon. Consequently, this allowed the Company to hedge itself against unexpected plunges in both copper and silver prices as well as rapid appreciation of the PLN versus USD in the period from September 2011 to December 2014.

In 2011, the Company applied the following market risk hedging instruments:

- options contracts (European and American),
- structures built from options contracts.

In addition, the Company performed a restructure of several options strategies implemented in 2011 and in prior years.

In 2011, the result on derivatives was PLN 562 484 thousand. The effective portion of the measurement of hedging instruments transferred from accumulated other comprehensive income to profit or loss in the reporting period as a reclassification adjustment caused an increase in revenues from sales by PLN 241 565 thousand. Gain due to the measurement of derivatives amounted to PLN 257 538 thousand, while gain due to the realisation of derivatives amounted to PLN 63 381 thousand. The adjustment of other operating income due to the measurement of derivatives results mainly from changes in the time value of options which are to be settled in future periods. In accordance with the hedge accounting principles applied by the Company, changes in the time value of options are not recognised in accumulated other comprehensive income.

In 2011, the Company was exposed to a limited degree to interest rate risk because of loans granted with interest based on a variable interest rate of WIBOR 1M (balance as at 31 December 2011: PLN 40 968 thousand, of which long-term loans amounted to PLN 35 210 thousand, short-term to PLN 5 758 thousand). In 2011, the Company did not make use of interest rate risk hedging instruments.

### Credit risk

Credit risk is defined as the risk that counterparties will not be able to meet their contractual obligations. In 2011, KGHM Polska Miedź S.A. was exposed to this risk, mainly in three areas of credit risk, related to:

- trade receivables,
- cash and cash equivalents and bank deposits,
- hedging transactions.

For many years the Company has sold its products to a large number of geographically diversified clients. The Company makes the majority of its sales transactions based on prepayments. Buyer's credit is only provided to proven, long-term customers, while sales of products to new customers are always secured. The Company continuously monitors the creditworthiness of its customers, in particular those to whom buyer's credit is provided. In 2011, the Company secured the majority of its receivables by promissory notes, frozen funds on bank accounts, registered pledges, bank guarantees, corporate guarantees, mortgages, letters of credit and documentary collection. In addition, the majority of customers which hold buyer's credit on contracts have ownership rights confirmed by a date certain.

To reduce the risk of insolvency by its customers, the Company has entered into a receivables insurance contract, which covers receivables from entities with buyer's credit which have not provided strong collateral or have provided collateral which does not cover the total amount of the receivables. Taking into account the collateral held and the credit limits received from the insurance company, as at 31 December 2011, the Company had secured 82.4% of its trade receivables. Despite the concentration of this type of risk, the Company believes that due to the availability of historical data and the many years of experience cooperating with its clients, as well as to the hedging used, the level of credit risk is low.

All of the entities with whom the Company entered into depositary transactions in 2011 (cash and cash equivalents and bank deposits) operated in the financial sector. These are exclusively banks registered in Poland or operating in Poland as branches of foreign banks, belonging to European and American financial institutions with high and medium ratings, and having an appropriate level of equity and strong and stable market positions. As at 31 December 2011, the maximum share of a single entity with respect to the amount of funds deposited by the Company amounted to 25%.

All of the entities with whom the Company enters derivative transactions operate in the financial sector. These are financial institutions (mainly banks), with the highest and medium ratings. According to fair value as at 31 December 2011, the maximum share of a single entity with respect to credit risk arising from derivative transactions entered into by the Company amounted to 23.6%. Due to diversification of risk in terms both of the nature of individual entities and of their geographical location, as well as taking into consideration the fair value of liabilities arising from derivative transactions, the Company is not materially exposed to credit risk as a result of derivative transactions entered into. To restrict cash flow and simultaneously restrict credit risk, the Company performs net settlement (based on framework agreements entered into with customers) to the level of positive balance of fair value measurement of hedging transactions with the given counterparty.

In 2011, the Company secured the majority of its receivables by promissory notes, frozen funds on bank accounts, registered pledges, bank guarantees, corporate guarantees, mortgages, letters of credit and documentary collection. In addition, the majority of customers which hold buyer's credit on contracts have ownership rights confirmed by a date certain.

To reduce the risk of insolvency by its customers, the Company has entered into a receivables insurance contract, which covers receivables from entities with buyer's credit which have not provided strong collateral or have provided collateral which does not cover the total amount of the receivables. Taking into account the collateral held and the credit limits received from the insurance company, as at 31 December 2011, the Company had secured 82.4% of its trade receivables.

## Liquidity risk

The Company is exposed to financial liquidity risk, where financial liquidity is understood as the ability to settle financial liabilities on time. The Company manages its financial liquidity in accordance with the policy „Financial Liquidity Management Policy” approved by the Management Board, which describes in a comprehensive manner the process of managing financial liquidity in the Company, based on best practice for such procedures and instruments.

In 2011, as well as in the comparable period, due to positive cash flow and the significant amount of cash balances, the Company made only slight use of external financing in the form of bank and other loans from financial institutions and settled all of its liabilities in a timely manner.

In accordance with market practice, the Company monitors its capital, among others based on the equity ratio and the ratio of Net Debt/EBITDA. The equity ratio is calculated as the relation of net assets (equity less intangible assets) to total assets. The ratio of Net Debt/EBITDA is calculated as the relation of borrowings and finance lease liabilities minus unallocated cash and cash equivalents and short term investments with a maturity up to 1 year to EBITDA (EBITDA is operating profit plus depreciation and amortisation).

In order to maintain financial liquidity and the creditworthiness to acquire external financing at a reasonable cost, the Company assumes that the equity ratio shall be maintained at a level of not less than 0.5, and the ratio of Net Debt/EBITDA at a level of up to 2.0.

Due to the low level of the Company debt as at 31 December 2011, the ratio of Net Debt/EBITDA was below 0.01. The equity ratio was above the assumed minimum level and as at 31 December 2011 amounted to 0.78. Neither in 2011 nor in 2010 were any external equity requirements imposed on the Company.

### 3.7. Realisation of projected financial results for 2011

In a current report dated 31 January 2011, the Company published its Budget assumptions for 2011 as accepted by the Supervisory Board on the same day. The Budget assumed the achievement in 2011 of revenues from sales in the amount of PLN 16 067 million and profit of PLN 8 345 million.

Along with the improvement in macroeconomic conditions during the year, the Company updated its forecast. The final projection of financial results was published in a current report on 21 December 2011. Basic assumptions, projected results and their realisation are shown in Table 23.

**Table 23. Realisation of projected Company financial results for 2011**

		Forecast (31.01.2011)	Forecast update (5.09.2011)	Forecast update (22.12.2011)	Execution 2011	Realisation of forecast (%)
<b>Sales</b>	<b>million PLN</b>	<b>16 067</b>	<b>18 934</b>	<b>20 084</b>	<b>20 097</b>	<b>100.1</b>
<b>Profit for the period</b>	<b>million PLN</b>	<b>8 345</b>	<b>9 643</b>	<b>11 192</b>	<b>11 335</b>	<b>101.3</b>
Average annual copper price	USD/t	8 200	9 000	8 827	8 811	99.8
Average annual silver price	USD/troz	25.00	32.00	35.11	35.12	100.0
Exchange rate	USD/PLN	2.80	2.80	2.97	2.96	99.7
Electrolytic copper production	'000 t	543.0	570.3	570.3	571.0	100.2
- of which from purchased copper-bearing materials	'000 t	111.0	128.0	128.0	124.6	97.3
Silver production	t	1 027	1 144	1 144	1 260	110.1
Capital expenditure	million PLN	1 892	1 732	1 645	1 514	92.0
Equity investments *	million PLN	9 046	10 757	642	640	99.7

\* includes purchase of shares and investment certificates, increases of share capital and owner loans and payments to subsidiaries

Due to the continuous updating of the forecast for 2011, the final realisation of financial results was not different from the planned amounts.

### 3.8. Projected Company financial situation

On 27 March 2012, the Supervisory Board of KGHM Polska Miedź S.A. approved the Budget for 2012. The bases for development of the Budget were the results for 2011 and the assumptions of individual operating plans. The basic assumptions of the Budget for 2012 are presented in Table 24:

**Table 24. Assumptions of Company's Budget for 2012**

		Execution 2011	Budget 2012	Change 2011=100
<b>Sales</b>	<b>PLN million</b>	<b>20 097</b>	<b>19 418</b>	<b>96.6</b>
<b>Profit for the period</b>	<b>PLN million</b>	<b>11 335</b>	<b>3 804</b>	<b>33.6</b>
Average annual copper price	USD/t	8 811	8 000	90.8
Average annual silver price	USD/troz	35.12	30.00	85.4
Exchange rate	USD/PLN	2.96	3.09	104.4
Unit cost of electrolytic copper production from own concentrate	PLN/t	10 299	15 729	152.7
Electrolytic copper production	'000 t	571.0	562.0	98.4
- of which from purchased copper-bearing materials	'000 t	124.6	147.3	118.2
Silver production	t	1 260	1 098	87.1
Capital expenditure	PLN million	1 514	2 100	138.7
Equity investments *	PLN million	640	10 671	x 16.7

\* Purchase of shares and investment certificates, increases of share capital and owner loans and payments to subsidiaries

The decrease in profit by PLN 7 531 million, i.e. by 66%, is mainly due to: recognition in the result for 2011 of the sales of telecom assets, a change in exchange differences, effects of the introduction of the minerals extraction tax and the deterioration of macroeconomic conditions.

The increase in the cost of electrolytic copper production from own concentrate versus 2011 by 53% is mainly due to the minerals extraction tax. Under comparable conditions, the above cost would be higher by 22%, of which mainly due to lower electrolytic copper production from own concentrate. In 2011, the relatively high level of production from own concentrates was due to the use of concentrate inventory accumulated in prior years due to the maintenance cycle. The volume of copper production in concentrate in KGHM Polska Miedź S.A. remains at a stable level.

The substantial increase in equity investments is due to the purchase in the first quarter of 2012 of Quadra FNX Mining Ltd. shares.

The results of the Company will be substantially impacted by the inclusion in the projection of payment of the minerals extraction tax, beginning from May 2012. Detailed information regarding the on-going legislative process for the introduction of the aforementioned tax is presented below.

#### Information on the legislative process with respect to the minerals extraction tax

On 14 December 2011, the Finance Minister presented a draft law for the mineral extraction tax (hereafter: Draft Law), which may potentially result in a substantial tax burden for KGHM Polska Miedź S.A. In accordance with laws regulating lobbying during the formation of a law, the Company announced its interest in work on the Draft Law.

On 27 January 2012, the first parliamentary reading was held of the Draft Law, and was subsequently sent for further work by the Committee of Public Finance. On 14 February 2012, the Committee of Public Finance approved the report on the government's Draft Law for the mineral extraction tax, in which the Committee recommended adoption of the Draft Law as amended by the Committee.

On 2 March 2012, Parliament adopted the aforementioned Law, and on 14 March 2012 the Senate gave its approval without enacting changes. It was then sent to the President for approval. The Law will come into force within 14 days of being announced in the Journal of Laws.

The mineral extraction tax will be calculated from the amount of copper and silver contained in produced concentrate.

Given the macroeconomic conditions in 2011, in particular with respect to average copper prices (8 810.90 USD/t), average silver prices (35.12 USD/troz), the average exchange rate (2.9636 USD/PLN) and production of copper (420 665 t) and silver (1 166 598 kg) contained in concentrate, under the government's Draft Law together with the amendments adopted by the Parliamentary Committee of Public Finance on 14 February 2012, the amount of the tax in annual terms would amount to PLN 2 488 227 thousand, reducing the current results of the Company.

Respectively, given the macroeconomic conditions and production realised in 2010, the mineral extraction tax would have reduced the results of the Company by PLN 1 676 370 thousand.



### 3.9. Disputed issues

As at 31 December 2011, the total value of ongoing disputed issues both by and against KGHM Polska Miedź S.A. amounted to PLN 121 693 thousand, including receivables of PLN 32 563 thousand and liabilities of PLN 89 130 thousand. The total value of the above disputed issues does not exceed 10% of the equity of the Company.

The largest proceedings involving the liabilities and receivables of KGHM Polska Miedź S.A. at the end of 2011 concerned the following:

Related liabilities due to:	
<b>Royalties for use of invention project no. 1/97/KGHM</b>	<p>Value of amount under dispute: PLN 42 413 thousand. The claim was filed with the Regional Court in Legnica on 26 September 2007 by 14 co-authors of invention project no. 1/97/KGHM. KGHM Polska Miedź S.A. received a summons on 14 January 2008.</p> <p>Each of the plaintiffs in this complaint is demanding royalties equivalent to the given plaintiff's share in the economic effects achieved for the 8th period of the project's application (calendar year 2006).</p> <p>The parties responded to the opinions representing further evidence admitted by the Court in this matter and are awaiting a date for a further hearing. Proceedings are in progress.</p> <p>In the Company's opinion the royalties being pursued by the Court are undue, as KGHM Polska Miedź S.A. covered the amounts due to the authors of the project resulting from use of an invention project.</p>
<b>Return of costs of protecting against mining damage</b>	<p>Value of amount under dispute: PLN 16 409 thousand. A claim was filed against KGHM Polska Miedź S.A. with the Regional Court in Legnica by the company Prestiż MGC Inwest Sp. z o. o. Sp. k. in August 2009 for payment of the amount of PLN 16 409 thousand due to the return of costs of work to protect against mine damages incurred during construction of the Centrum Handlowo-Usługowe „CUPRUM ARENA” in Lubin. Proceedings are in progress.</p> <p>In the Company's opinion the claim is unfounded and should be dismissed.</p>
<b>Royalties for use of invention project no. 2/97/KGHM</b>	<p>Value of amount under dispute: PLN 11 760 thousand. A claim was filed with the Regional Court in Legnica by eleven co-authors and two heirs of authors of invention project no. 2/97/KGHM. The plaintiffs are demanding additional compensation due to the use by KGHM Polska Miedź S.A. of a patent from the submitted project no. 2/97/KGHM. Proceedings have been suspended until the case can be heard by the Patent Office of the Republic of Poland for the annulment of patent no. 185036.</p> <p>In March 2011, the Deciding Board of the Patent Office annulled the invention patent. In December 2011, the authors submitted a cassation appeal against the decision of the Regional Administrative Court to pass the authors' claim for a hearing by the Patent Office on the annulment of the invention patent.</p> <p>In the Company's opinion the claim does not deserve to be considered due to the lack of patentability of invention project no. 2/97/KGHM, based on failure to meet the unobviousness requirement.</p>
Related receivables due to:	
<b>Return of undue royalties for use of invention project no. 1/97/KGHM</b>	<p>In January 2008 the Company filed a counter claim against 14 project co-authors for payment of undue royalties paid in the amount of PLN 25 195 thousand for use of invention project no. 1/97/KGHM in the 6<sup>th</sup> and 7<sup>th</sup> periods (calendar years 2004-2005). The court has combined both these matters – the claims of 14 co-authors for the payment of royalties for use of invention project no. 1/97/KGHM in the amount of PLN 42 413 thousand with the claims of the Company for the payment of undue royalties paid for use of invention project no. 1/97/KGHM in the amount of PLN 25 195 thousand, for mutual hearing. Proceedings are in progress.</p> <p>In the Company's opinion the payment of royalties to the project's authors was unfounded.</p>



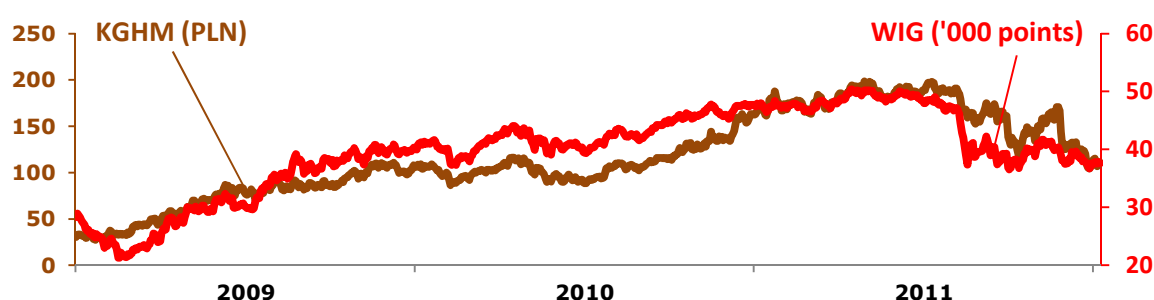
## 4. Ownership structure and Company quotations

### 4.1. The Company on the stock exchange

In July 1997 KGHM Polska Miedź S.A. debuted on the Warsaw Stock Exchange. The shares of the Company are traded on the primary market in a continuous trading system, and are a component of the WIG, WIG20, WIG Surowce indices, as well as the RESPECT Index - an index of socially responsible companies and the WIGdiv index - comprising companies with the highest dividend payout ratios, and which regularly pay dividends to their shareholders.

The Company's share price in 2011 broke its own historic records numerous times. At the close of session on 20 April 2011 the Company's share price was PLN 198.40, and was the highest closing price in 2011, as well as in the Company's market history. The Company's share price returned to the PLN 198 level at the start of July 2011. Thereafter the Company's quotations entered a bearish period. Overall, in 2011 the share price fell by 36.1%, from PLN 173.00 at the closing session of 2010 to PLN 110.60 on the last trading day of 2011. During this period, the Warsaw Stock Exchange WIG index fell by 20.8%, and the WIG20 by 21.9%.

**Chart 10. Share price of KGHM Polska Miedź S.A. versus the WIG index**



In 2011 the shares of KGHM Polska Miedź S.A. were amongst the most liquid on the Warsaw Stock Exchange. The Company's share of turnover in value terms amounted to 17.2%. The average per-session trading volume of the Company's shares on the Warsaw Stock Exchange in 2011 amounted to 1 070 047.

Key data on the share performance of KGHM Polska Miedź S.A. on the Warsaw Stock Exchange in the years 2009-2011 are presented in the following Table 24.

**Table 25. Key share quotation data of the Company on the Warsaw Stock Exchange**

	Unit	2009	2010	2011
Number of shares issued	million	200	200	200
Closing price from the last day of trading in the year	PLN	106.00	173.00	110.60
Market value of the Company at year's end	million PLN	21 200	34 600	22 120
Highest closing price in the year	PLN	110.70	173.00	198.40
Lowest closing price in the year	PLN	27.50	86.50	104.60
Average trading volume per session	'000	1 222	966	1 070
Dividend paid in the financial year from appropriation of profit for the prior year	PLN/share	11.68	3.00	14.90

#### **4.2. Information on the ownership structure and on the issued shares of the Company**

As at 31 December 2011, the share capital of the Company, in accordance with the entry in the National Court Register, amounted to PLN 2 000 000 000 and was divided into 200 000 000 shares, series A, having a face value of PLN 10 each. All shares are bearer shares. The Company has not issued preference shares. Each share grants the right to one vote at the General Meeting.

In 2011 there was no change either in registered share capital or in the number of issued shares.

As far as the Management Board of the Company is aware, there was also no change in the structure of ownership of significant blocks of shares of KGHM Polska Miedź S.A. The only shareholder who in 2011 held 5% or more of the Company's share capital was the Polish State Treasury, which held 63 589 900 shares of KGHM Polska Miedź S.A., granting the same number of votes and representing 31.79% of the share capital of the Company and in the total number of votes. During 2011 this situation did not change.

The Management Board of the Company is unaware of any agreements which could result in changes in the proportion of shares held by present shareholders in the future.

Based on information held by the Company, members of the Company's Supervisory Board and Management Board were not in the possession of shares of KGHM Polska Miedź S.A. or of related entities, either at 31 December 2010 or at 31 December 2011.

In 2011, the Company did not have an employee share incentive program.

## 5. Report on the application of corporate governance principles

In July 2007, the Supervisory Board of the Warsaw Stock Exchange resolved the principles of corporate governance for joint-stock companies that are issuers of shares, convertible bonds or bonds with priority rights admitted to exchange trading. These corporate governance principles as described in the document "Code of Best Practice for WSE Listed Companies" represent an annex to resolution no. 12/1170/2007 of the Supervisory Board of the WSE dated 4 July 2007 which came into force on 1 January 2008, and remained in force until 30 June 2010. Since 1 July 2010 a changed group of principles had been in force representing an annex to resolution no. 17/1249/2010 of the Supervisory Board of the WSE dated 19 May 2010. Subsequent changes to the document "Code of Best Practice for WSE Listed Companies" were introduced by resolutions of the Supervisory Board of the WSE nos. 15/1282/2011 dated 31 August 2011 and 20/1287/2011 dated 19 October 2011. The amended principles came into force on 1 January 2012. The contents of the document "Code of Best Practice for WSE Listed Companies" are available on the official website of the Warsaw Stock Exchange under the section on corporate governance ([www.corp-gov.gpw.pl](http://www.corp-gov.gpw.pl)), as well as on the website of the Company ([www.kghm.pl](http://www.kghm.pl)) under the section on corporate governance.

KGHM Polska Miedź S.A., whose shares are listed on the Warsaw Stock Exchange, has made every effort to apply the corporate governance principles described in document „Code of Best Practice for WSE Listed Companies”. The Company has endeavoured at every stage of its operations to carry out all of the recommendations respecting best practice for listed companies as well as suggestions directed to management boards, supervisory boards and shareholders.

In order to realise a transparent and effective information policy, one ensuring rapid and secure access to information for shareholders, analysts and investors, the Company made the broadest possible use of both traditional as well as modern technology for the distribution of information about the Company (recommendation I.1 of the "Code of Best Practice for WSE Listed Companies"). In 2011 the Company decided not to comply only with the recommended on-line transmission of General Meetings, but has registered these meetings and immediately made them available on the Company website in both Polish and English, accessible under the section Investor Zone/Transmissions. The Company has undertaken actions aimed at preparing to provide access to General Meeting on-line transmissions.

In accordance with recommendation I.9, the Company offers equal participation to men and women to fulfil management and supervisory functions. At present however, there are no women on the Management Board of the Company. Although in 2008 a competition was held for the position of President of the Management Board, there were no women applicants for the position, with the same situation applying to competitions held in 2010 involving the positions of President of the Management Board and Vice President of the Management Board (Production).

### 5.1. General Meeting

The General Meeting of KGHM Polska Miedź S.A. is the Company's highest body. It meets in either an ordinary or an extraordinary form, based on prevailing law, the Statutes of the Company and the Bylaws of the General Meeting. The Company's corporate documents are available on its website.

The duties of the General Meeting include in particular:

- examining and approving the report of the Management Board on the Company's activity and the financial statements, including the consolidated financial statements of the Company group, for the prior financial year,
- adopting resolutions on the distribution of profits or coverage of losses,
- acknowledging the fulfilment of duties performed by members of the bodies of the Company,
- changing the subject of the Company's activity,
- amending the Company Statutes,
- increasing or decreasing the share capital,
- the manner and conditions for retiring shares,
- merging, splitting and transforming the Company,
- dissolving and liquidating the Company,
- issuing convertible bonds or senior bonds,
- consenting to the disposal and lease of an enterprise or of an organised part thereof, as well as the attachment of limited property rights to same,
- all decisions relating to claims for redress of damage suffered during the foundation of the Company, or from management or supervisory activities,
- purchase of the Company's own shares, which are to be offered to employees or persons who were employed by the Company or by related companies for a period of at least three years,
- establishing principles of the remuneration of members of the Supervisory Board.

The schedule of work on organising the General Meetings of the Company is planned in such a way as to ensure that the obligations towards shareholders are properly met and to enable them to execute their rights.

In accordance with the Statutes of KGHM Polska Miedź S.A., the State Treasury may convene an Ordinary General Meeting if the Management Board does not do so in the statutory timeframe as well as an Extraordinary General Meeting if it considers its convening as warranted.

The introduction of changes to the Company Statutes requires a resolution by the General Meeting and an entry in the National Court Register of a constitutive nature. Changes in the Company Statutes are made by the General Meeting in conformance with prevailing laws, in the manner and form prescribed by the Commercial Partnerships and Companies Code.

Amongst the regulations of the Commercial Partnerships and Companies Code, in respect of the organisation of General Meetings and shareholder rights, the Company applies only those regulations which are obligatory, i.e. those which require the publication of announcements and materials for the General Meeting on the Company website and the use of electronic forms of contact with shareholders. Regulations enabling shareholders to participate in General Meetings using electronic means of communication are not applied.

## **5.2. Shareholders and their rights**

The only shareholder of the Company holding at least 5% of the share capital and simultaneously granting the right to the same number of votes at the General Meeting on both 1 January 2011 and 31 December 2011 was the Polish State Treasury.

This shareholder held 63 589 900 shares of KGHM Polska Miedź S.A., which represented 31.79% of the share capital and of the total number of votes at the General Meeting.

Shareholders of the Company exercise their rights in a manner and within the limits prescribed by prevailing law, the Statutes of the Company and the Bylaws of the General Meeting.

Shareholders are entitled to exercise their voting during General Meetings either personally or through a proxy. All of the shares are bearer shares. Each share grants the right to one vote. There is no limitation to the transferral of ownership rights to the shares of the Company or with respect to the execution of voting rights on the shares of the Company, other than those generally prescribed by laws in force. The Company has not issued securities which would grant special control rights in respect of the Company.

## **5.3. Supervisory Board**

The Supervisory Board of KGHM Polska Miedź S.A. is the permanent supervisory body of KGHM Polska Miedź S.A., in all of the Company's functional areas. According to the Statutes, the Supervisory Board is comprised of 7 to 10 members, appointed by the General Meeting, of which 3 members are elected by the Company's employees. The members of the Supervisory Board are appointed for a mutual term of office, which lasts three years. The Supervisory Board operates on the basis of prevailing law, the Statutes of the Company and the Regulations of the Supervisory Board.

The composition of the 7th-term Supervisory Board as at 1 January 2011 was as follows:

- |                     |                 |
|---------------------|-----------------|
| – Jacek Kuciński    | Chairman        |
| – Marcin Dyl        | Deputy Chairman |
| – Marek Panfil      | Secretary       |
| – Arkadiusz Kawecki |                 |
| – Jan Rymarczyk     |                 |
| – Marzenna Weresa   |                 |

as well as the following employee-elected members:

- Józef Czycherski
- Leszek Hajdacki
- Ryszard Kurek

Due to expiry of the mandate of the 7th-term Supervisory Board, the Ordinary General Meeting on 15 June 2011:

- dismissed all of the Members of the 7th-term Supervisory Board,
- confirmed the validity of the elections carried out in the Company on 11-12 May 2011, as a result of which the employees of KGHM Polska Miedź S.A. elected three members to the Supervisory Board,
- set the number of members of the Supervisory Board at 10 persons, and
- appointed the following persons to the Supervisory Board of the Company: Franciszek Adamczyk, Marcin Dyl, Arkadiusz Kawecki, Jacek Kuciński, Marek Panfil, Jan Rymarczyk and Marzenna Weresa.

On 20 October 2011, the Extraordinary General Meeting of KGHM Polska Miedź S.A. appointed to the Supervisory Board of KGHM Polska Miedź S.A. Lech Jaroń, Maciej Łaganowski and Paweł Markowski, elected by the employees of the Company in elections held on 19-20 September 2011.

The composition of the 8th-term Supervisory Board as at 31 December 2011 was as follows:

- |                       |                 |
|-----------------------|-----------------|
| – Jacek Kuciński      | Chairman        |
| – Marcin Dyl          | Deputy Chairman |
| – Marek Panfil        | Secretary       |
| – Franciszek Adamczyk |                 |
| – Arkadiusz Kawecki   |                 |
| – Jan Rymarczyk       |                 |
| – Marzenna Weresa     |                 |

as well as the following employee-elected members:

- Lech Jaroń
- Maciej Łaganowski
- Paweł Markowski

On 19 January 2012, the General Meeting of KGHM Polska Miedź S.A. dismissed the following persons from the Supervisory Board: Franciszek Adamczyk, Marcin Dyl, Arkadiusz Kawecki, Jan Rymarczyk and Marzenna Weresa, and appointed the following persons: Krzysztof Kaczmarczyk, Mariusz Kolwas, Aleksandra Magaczewska, Robert Oliwa and Jacek Poświata.

Consequently, the composition of the Supervisory Board, at the date of preparation of this report, was as follows:

- |                          |                 |
|--------------------------|-----------------|
| – Jacek Kuciński         | Chairman        |
| – Marek Panfil           | Deputy Chairman |
| – Mariusz Kolwas         | Secretary       |
| – Krzysztof Kaczmarczyk  |                 |
| – Aleksandra Magaczewska |                 |
| – Robert Oliwa           |                 |
| – Jacek Poświata         |                 |

as well as the following employee-elected members

- Lech Jaroń,
- Maciej Łaganowski,
- Paweł Markowski.

### **Supervisory Board Committees**

Under the auspices of the Supervisory Board are three committees: the Audit Committee, the Remuneration Committee and the Strategy Committee. These committees assist the Supervisory Board with respect to preparing evaluations and opinions and the taking of other actions aimed at decision-making by the Supervisory Board.

The Audit Committee is responsible for supervision in the areas of financial reporting, the internal control system, risk management and internal and external audits.

The Remuneration Committee is responsible for supervising the realisation of contracts signed with the Management Board, the remuneration system and benefits paid out in the Company and Group, training and other benefits provided by the Company, as well as audits performed by the Supervisory Board in this regard.

The Strategy Committee, set on 28 March 2011, supervises the realisation of Company strategy, the Company's annual and multi-year operating plans, supervising the coherence of these documents, and also provides its opinion to the Supervisory Board on the strategic projects presented by the Management Board of the Company and any changes thereto, as well as on the Company's annual and multi-year operating plans.

The rights, scope of action and manner of work of these Committees are described by regulations approved by the Supervisory Board.

The specific duties and composition of the Committees are as follows:

#### **Audit Committee**

In accordance with the Regulations of the Supervisory Board the duties of the Audit Committee are as follows:

- supervision, on behalf of the Supervisory Board, of the process of financial reporting in the Company, including the process of reporting to the Supervisory Board,
- analysis and/or evaluation of the accounting principles applied in the Company,
- the review of transactions with parties related to the Company, and of unusual transactions,
- the analysis and monitoring of post-control conclusions arising from the risk management process,

- conduct of the process of selecting independent auditors to audit the financial statements of the Company in order to recommend their acceptance by the Supervisory Board, and participation in commercial negotiations prior to the Company signing a contract with an auditor,
- continuous co-operation with the independent auditor of the Company during the audit, analysis and formulation of conclusions from the audit and opinion of the auditor respecting the financial statements, the auditor's letter to the Management Board and/or Supervisory Board, and the preparation of draft statements and evaluations required by the by-laws for Company bodies and other administrative institutions,
- providing an opinion on the internal audit plan and the internal audit regulations of the Company, and of changes of the director of internal audit,
- analysis of the conclusions reached and the recommendations made by an internal audit of the Company, with monitoring of the degree of implementation of these recommendations by the Management Board of the Company,
- the monitoring of decrees and Company's regulations as regards accounting, finances and hedging against trade and financial risks, and exposure of the Company to serious harm.

The Act dated 7 May 2009 on certified auditors and their self-governing body, entities entitled to audit financial statements and on public supervision, required public companies to appoint Supervisory Board Audit Committees and listed tasks which should be in particular the responsibility of such Committees.

The law in addition calls for Audit Committees to include at least 3 members, of which at least one member should meet the criteria for independence and hold qualifications in the areas of accounting or financial review.

The following Members of the Supervisory Board served on the Audit Committee of the Supervisory Board of KGHM Polska Miedź S.A. throughout 2011:

- Marek Panfil Chairman
- Marcin Dyl
- Marzenna Weresa

Following the changes in the Supervisory Board on 19 January 2012, the composition of the Audit Committee at the date of preparation of this report was as follows:

- Marek Panfil Chairman
- Lech Jaroń
- Krzysztof Kaczmarczyk
- Mariusz Kolwas
- Robert Oliwa.

### **Remuneration Committee**

In accordance with the Regulations of the Supervisory Board the duties of the Remuneration Committee are as follows:

- to carry out the recruitment and employment of members of the Management Board by developing and organising draft documents and procedures to be submitted to the Supervisory Board for their acceptance,
- to develop draft agreements and samples of other documents related to the hiring of members of the Management Board, and supervision over the realisation of the contractual obligations entered into by the parties,
- to supervise realisation of the system of remuneration of the Management Board, in particular to prepare documents related to variable salary and premiums, in order to submit a recommendation to the Supervisory Board,
- to monitor and make periodic analyses of the remuneration system of the management staff of the Company and, if necessary, to formulate recommendations to the Supervisory Board,
- to supervise realisation of additional benefits received by the Management Board arising from labour contracts, such as: insurance, automobiles, housing, etc.

As at 1 January 2011 the following Members of the Supervisory Board served on the Remuneration Committee of the Supervisory Board of KGHM Polska Miedź S.A.:

- Arkadiusz Kawecki Chairman
- Leszek Hajdacki
- Jacek Kuciński

Following appointment of the Members of the Supervisory Board to the new 8th-term Supervisory Board, the composition of the Committee changed, and as at 31 December 2011 the following Members of the Supervisory Board served on the Remuneration Committee of the Supervisory Board of KGHM Polska Miedź S.A.:

- Arkadiusz Kawecki Chairman
- Franciszek Adamczyk
- Jacek Kuciński

Following the changes in the Supervisory Board on 19 January 2012, the composition of the Remuneration Committee at the date of preparation of this report was as follows:

- Jacek Kuciński,
- Maciej Łaganowski,
- Paweł Markowski.

#### **Strategy Committee**

In accordance with the Regulations of the Supervisory Board the duties of the Strategy Committee are as follows:

- the performance of tasks on behalf of the Supervisory Board of the Company respecting supervision of matters related to Company strategy and the Company's annual and multi-year operating plans,
- monitoring the realisation by the Management Board of the Company of the Company's strategy, and evaluating to what extent the existing strategy is appropriate in dealing with changes in the actual situation,
- monitoring the realisation by the Management Board of the Company's annual and multi-year operating plans, and evaluating whether they require modification,
- evaluating the consistency of the Company's annual and multi-year operating plans with the realisation by the Management Board of the Company's strategy, and presenting proposed changes to any of these Company documents,
- submitting to the Supervisory Board of the Company its opinions in respect of the strategic projects presented by the Management Board of the Company and any changes thereto, as well as on the Company's annual and multi-year operating plans.

The composition of the Strategy Committee of the Supervisory Board of KGHM Polska Miedź S.A. from the date of its appointment, i.e. 28 March 2011, included the following Members of the Supervisory Board:

- Jacek Kuciński
- Ryszard Kurek
- Jan Rymarczyk

Following appointment of the Members of the Supervisory Board to the new 8th-term Supervisory Board, the composition of the Committee changed, and as at 31 December 2011 the following Members of the Supervisory Board served on the Strategy Committee of the Supervisory Board of KGHM Polska Miedź S.A.:

- Franciszek Adamczyk
- Jacek Kuciński
- Jan Rymarczyk

Following the changes in the Supervisory Board on 19 January 2012, the composition of the Strategy Committee at the date of preparation of this report was as follows:

- Krzysztof Kaczmarczyk,
- Jacek Kuciński,
- Aleksandra Magaczewska,
- Jacek Poświata.

After the end of the year the Audit, Remuneration and Strategy Committees submit a report of their activities to the Supervisory Board.

#### **5.4. Management Board**

The Management Board conducts the business of the Company and represents it externally. The duties of the Management Board include all those matters pertaining to the functioning of the Company which have not otherwise been assigned by law or the Statutes to the duties of other Company bodies. The Management Board operates based on prevailing law, the Statutes of the Company and the Regulations of the Management Board. The authority of the Management Board to pass decisions on the issuance or redemption of shares is statutorily limited. In accordance with §29 sec.1 point of 6 the Statutes of the Company, any increase in share capital or issuance of shares requires the approval of the General Meeting. The same holds true for the issuance of bonds. The Management Board of the Company does not have the authority to increase the share capital or issue the shares of the Company under conditions specified in art. 444-446 of the Commercial Partnerships and Companies Code.

The Management Board is comprised of 1 to 7 persons appointed for a mutual term of office. The term of office of the Management Board lasts three years. The number of members of the Management Board is set by the Supervisory Board, which appoints and dismisses the President of the Management Board, and at his request appoints and dismisses the remaining members of the Management Board, including those serving as First Vice President and as the Vice Presidents of the Management Board. The Supervisory Board appoints and dismisses the employee-elected member of the Management Board.

The composition of the Management Board and the segregation of duties amongst its Members from 1 January to 31 December 2011 was as follows:

- Herbert Wirth                      President of the Management Board
- Maciej Tybura                    I Vice President of the Management Board (Finance)
- Wojciech Kędzia                Vice President of the Management Board (Production)

#### **5.5. Description of the basic characteristics of internal control and risk management systems applied in the Company with respect to the process of preparing financial statements and consolidated financial statements**

KGHM Polska Miedź S.A. has an internal control and risk management system, for whose proper and effective functioning in the process of preparing the separate financial statements of KGHM Polska Miedź S.A. and the consolidated financial statements of the Group the Management Board of KGHM Polska Miedź S.A. is responsible. The system of internal control and risk management in this regard is based on the identification and assessment of areas of risk, with the simultaneous defining and undertaking of actions aimed at its minimisation or total elimination.

KGHM Polska Miedź S.A. uses its many years of experience in the identification, documentation, record maintenance and control of economic operations and established audit and inspection procedures supported by modern information technology used in the registration, processing and presentation of economic and financial data.

In order to ensure truth and accuracy in the keeping of the accounting records of KGHM Polska Miedź S.A. and the uniformity of applied accounting principles in preparing the financial statements of Group subsidiaries, the following has been introduced for continuous use:

- an Accounting Policy for KGHM Polska Miedź S.A. and the Group, in accordance with International Financial Reporting Standards, continuously updated based on new regulations,

and in addition, for KGHM Polska Miedź S.A.

- Principles for Financial Management and for an Economic System,
- Documentation for an IT system for the processing of accounting data,
- Sector Principles of Balance Sheet Depreciation of Property, Plant and Equipment and Amortisation of Intangible Assets, and
- Sector Chart of Accounts in accordance with IFRS,

as well as a variety of internal procedures respecting systems for the control and evaluation of risk arising from the activities of KGHM Polska Miedź S.A. and the Group, along with the established scope and principles of financial reporting.

KGHM Polska Miedź S.A. keeps accounting records in an integrated IT system. The modular structure of this system ensures a transparent segregation of processes and duties, coherence of accounting records and control between ledgers: special purpose ledger, general ledger and subledgers. Access to this data at various levels and in various units is available via a well-developed reporting system. KGHM Polska Miedź S.A. continuously adapts the IT information system to changing accounting principles or other legal standards, thanks to the high operational flexibility available to the IT system modules. The technical servicing of the system is ensured by the highly experienced specialists employed by KGHM Polska Miedź S.A. KGHM Polska Miedź S.A. has full documentation of the IT system, both in the part meant for end-users, as well as in the technical part encompassing configuration, parameterization and calculation algorithms of the system. In accordance with article 10 of the Accounting Act dated 29 September 1994, documentation of the IT accounting system is periodically verified and updated, and confirmed each time by the heads of the units, i.e. the Management Board of KGHM Polska Miedź S.A. and the management boards of subsidiaries.

In order to ensure the proper use and protection of systems and data, as well as secure access to data and hardware, KGHM Polska Miedź S.A. has introduced appropriate organisational and systemic solutions. Access to the resources of the financial and accounting system and financial reporting – separate and consolidated – is limited to the respective entitlements of authorised employees solely with respect to the duties which they carry out. These entitlements are subject to regular audits. Control over this access is carried out at each stage of financial statements preparation, beginning with the entering of source data, through the processing of data, to the generation of output information.

Control of the accounting principles applied in the process of preparing the financial statements of KGHM Polska Miedź S.A. and in the subsidiaries of the Group is based on functionally-developed reporting systems with control mechanisms, which continuously verify the conformity of these principles with the existing Accounting Policy and other documents representing the basis for the preparation of financial statements.



The body which supervises the process of financial reporting in KGHM Polska Miedź S.A. and which cooperates with the independent auditor is the Audit Committee, which is appointed by the Supervisory Board of KGHM Polska Miedź S.A. The Audit Committee, in accordance with its duties as set forth in the Act dated 7 May 2009 on certified auditors and their self-governing body, entities entitled to audit financial statements and on public supervision (Journal of Laws 2009.77.649), in particular:

- monitors the process of financial reporting in terms of compliance with the Accounting Policy approved by KGHM Polska Miedź S.A. and prevailing laws,
- monitors the effectiveness of internal control systems, internal audit and risk management,
- monitors the independence of the certified auditor and of the entity entitled to audit financial statements, and
- recommends to the Supervisory Board an entity entitled to audit financial statements.

Monitoring of the process of financial reporting and assessment of the financial statements by the Supervisory Board is the final step of the review and control carried out by an independent body, ensuring the truth and accuracy of the data presented in the separate and consolidated financial statements of KGHM Polska Miedź S.A.

A fundamental element of risk management with respect to the process of preparing financial statements of KGHM is examining the functioning of control mechanisms and the existence of risk in the operations of KGHM Polska Miedź S.A., carried out by internal audit. The tasks realised by internal audit are based on the "Integrated Audit Plan of KGHM Polska Miedź S.A. for the years 2011-2015" and the annual „Integrated Audit Plan" for the given calendar year, approved by the Management Board of KGHM Polska Miedź S.A. These documents were developed based on International Professional Standards in Internal Audit Practice published by the Institute of Internal Auditors, and received a positive opinion by the Audit Committee of the Supervisory Board. The goal of internal audit is to provide the Management Board and Supervisory Board of the Company with independent and objective information on and evaluations of the risk management and internal control systems, and analyses of business processes in KGHM Polska Miedź S.A.

The internal control system in KGHM Polska Miedź S.A. encompasses all of the processes functioning in KGHM Polska Miedź S.A., including those areas which directly or indirectly affect the correctness of the financial statements. Internal (institutional) control is performed by a separate department in the organisational structure. Apart from institutional control, the obligation fully remains for each employee in KGHM Polska Miedź S.A. to control their own performance, and for every level of management staff to perform their control – within supervisory-related duties.

The effectiveness of the internal control and risk management procedures in the process of preparing financial statements in KGHM Polska Miedź S.A. is the high assessment of the quality of these statements, confirmed the top position in the competition The Best Annual Report, in which KGHM Polska Miedź S.A. has participated for years.

## Appendix A: Methodology of calculating ratios used in the report

### Assets effectiveness ratios

$$\begin{aligned}\text{Assets turnover ratio} &= \frac{\text{sales}}{\text{total assets}} \\ \text{Non-current assets turnover ratio} &= \frac{\text{sales}}{\text{non-current assets}} \\ \text{Current assets turnover ratio} &= \frac{\text{sales}}{\text{current assets}} \\ \text{Liquid assets turnover ratio} &= \frac{\text{sales}}{\text{current receivables} + \text{cash and cash equivalents}}\end{aligned}$$

### Assets financing ratios

$$\begin{aligned}\text{Coverage of assets by equity} &= \frac{\text{equity}}{\text{total assets}} \\ \text{Coverage of non-current assets by equity} &= \frac{\text{equity}}{\text{non-current assets}} \\ \text{Coverage of non-current assets by long-term capital} &= \frac{\text{equity} + \text{non-current liabilities}}{\text{non-current assets}} \\ \text{Coverage of current assets by current liabilities} &= \frac{\text{current liabilities}}{\text{current assets}}\end{aligned}$$

### Economic activity ratios

$$\begin{aligned}\text{Current liquidity} &= \frac{\text{current assets}}{\text{current liabilities}} \\ \text{Quick liquidity} &= \frac{\text{current assets} - \text{inventories}}{\text{current liabilities}} \\ \text{ROA (return on assets)} &= \frac{\text{profit for the period}}{\text{total assets}} \times 100 \\ \text{ROE (return on equity)} &= \frac{\text{profit for the period}}{\text{equity}} \times 100 \\ \text{Debt ratio} &= \frac{\text{total liabilities}}{\text{equity and liabilities}} \times 100 \\ \text{Durability of financing structure} &= \frac{\text{equity} + \text{non-current liabilities}}{\text{equity and liabilities}} \times 100\end{aligned}$$

## **Appendix B: Current reports of the Company published in 2012 – to the date of preparation of the annual report**

### **Lack of opposition of Canadian and American antimonopoly bodies to purchase of the shares of Quadra FNX Mining Ltd (4 January 2012)**

The Company was informed that Canada's Competition Bureau is not opposed to the purchase all of the shares of Quadra FNX Mining Ltd. by KGHM Polska Miedź S.A. or an affiliate thereof. The United States Federal Trade Commission also announced that it is not opposed to the purchase of shares of Quadra FNX Mining Ltd.

### **Approval of the shareholders of Quadra FNX Mining Ltd (20 February 2012)**

The shareholders of Quadra FNX Mining Ltd at the General Meeting of the company convened on 20 February 2012, approved by the required majority of votes the transaction described in the binding conditional agreement entered into between KGHM Polska Miedź S.A. and Quadra FNX Mining Ltd on 6 December 2011.

As a result of this transaction, KGHM, through its special purpose wholly controlled subsidiary, founded under British Columbia law, will acquire from the existing shareholders, under a Plan of Arrangement recommended by the Board of Directors of Quadra FNX Mining Ltd, the shares of Quadra FNX Mining Ltd, representing 100% of the share capital of this company.

### **Court approval of the purchase of Quadra FNX Mining Ltd (22 February 2012)**

On 21 February 2012 the Supreme Court of British Columbia issued the final order approving the transaction described in the binding conditional agreement entered into between KGHM Polska Miedź S.A. and Quadra FNX Mining Ltd dated 6 December 2011.

### **Approval of the Canadian Minister of Industry for the transaction of the acquisition of Quadra FNX Mining Ltd (29 February 2012)**

The Canadian Minister of Industry, in accordance with the Investment Canada Act, issued on 28 February 2012 approval for the transaction described in the binding conditional agreement entered into between KGHM and Quadra FNX Mining Ltd dated 6 December 2011.

Receipt of this approval fulfilled the final condition precedent for closure of the transaction.

### **Significant agreements, acquisition of significant assets in the KGHM Group (5 March 2012)**

In relation to the purchase of 100% of the shares of Quadra FNX Mining Ltd. with its registered head office in Vancouver ("Quadra FNX") by an indirect subsidiary of KGHM Polska Miedź S.A. ("KGHM") – the company 0929260 B.C. Unlimited Liability Company with its registered head office in Vancouver („0929260 B.C. U.L.C."), on 5 March 2012 the following transactions took place in the KGHM Group to optimise the purchase structure:

1.

KGHM increased the equity of Fermat 1 S.a.r.l. with its registered head office in Luxembourg ("Fermat 1") by USD 2 936 840 thousand (representing the equivalent of PLN 9 208 462 thousand). As a result of the increase in equity, KGHM acquired 29 368 400 newly-issued shares in the company Fermat 1 with a per-share nominal value of USD 1. The difference between the nominal value of the shares and the value of the contribution was transferred to the reserve capital of Fermat 1.

2.

Fermat 1 increased the equity of Fermat 2 S.a.r.l. with its registered head office in Luxembourg ("Fermat 2") by USD 1 063 740 thousand (representing the equivalent of PLN 3 335 357 thousand). As a result of the increase in equity, Fermat 1 acquired 10 637 400 newly-issued shares in the company Fermat 2 with a per-share nominal value of USD 1. The difference between the nominal value of the shares and the value of the contribution was transferred to the reserve capital of Fermat 2.

3.

An agreement was entered into between Fermat 1 and the company Fermat 3 S.a.r.l. with its registered head office in Luxembourg, a wholly-owned subsidiary of Fermat 1 („Fermat 3"), based on which Fermat 1 granted to Fermat 3 an interest-free loan in the amount of USD 1 873 100 thousand (representing the equivalent of PLN 5 873 105 thousand).

4.

A loan agreement was entered into between Fermat 3 and Fermat 2, based on which Fermat 3 granted to Fermat 2 a loan in the amount of USD 1 873 100 thousand (representing the equivalent of PLN 5 873 105 thousand) to be converted into the shares of Fermat 2. This conversion will occur at a future date to be determined by the parties. The value at which the shares of Fermat 2 will be acquired by Fermat 3 based on

conversion will be equal to the nominal value of the loan described in point 3, increased by the fair market value of the proceeds directly or indirectly derived from the loan.

5.

Fermat 1 and Fermat 3 entered into a forward share purchase agreement, concerning purchase by Fermat 1 from Fermat 3 of the shares of Fermat 2, which Fermat 3 will acquire in the future from the conversion of the loan described in point 4 into the capital of Fermat 2. The purchase price amounts to USD 1 873 100 thousand (representing the equivalent of PLN 5 873 105 thousand). The amount due from purchase of the shares of Fermat 2 will be payable on a date subsequent to the acquisition by Fermat 3 of the shares of Fermat 2 based on conversion. The purchase price of the shares of Fermat 2 owed to Fermat 3 from Fermat 1 will be offset with the receivables of Fermat 3 toward Fermat 1 due to the loan described in point 3.

6.

An agreement was entered into between Fermat 2 and the company 0929260 B.C. U.L.C., a wholly-owned subsidiary of Fermat 2, based on which Fermat 2 granted to 0929260 B.C. U.L.C. a loan in the amount of USD 1 873 100 thousand (representing the equivalent of PLN 5 873 105 thousand). Interest on the loan will be set at the level of the yield to maturity of the senior notes issued by Quadra FNX on 17 June 2011. The interest will be paid at the end of each calendar year. Repayment of the loan will occur at a future date to be determined by the parties.

In addition, Fermat 2 acquired in exchange for a cash contribution in the amount of CAD 1 050 621 thousand (representing the equivalent of PLN 3 313 868 thousand) newly-issued shares in the company 0929260 B.C. U.L.C. The funds obtained by 0929260 B.C. U.L.C. from the loan and from the increase in share capital will be used to finance the purchase of 100% of the shares of Quadra FNX. The assets acquired under these events are of a long-term, equity investment nature.

Amounts in foreign currency in the above-mentioned text were calculated using the average exchange rate of the National Bank of Poland of 5 March 2012.

#### **Purchase of 100% of Quadra FNX shares (5 March 2012)**

On 5 March 2012 the company 0929260 B.C. Unlimited Liability Company with its registered head office in Vancouver („0929260 B.C. U.L.C.”), as an indirect subsidiary of KGHM Polska Miedź S.A., purchased from the former shareholders of Quadra FNX Mining Ltd. with its registered head office in Vancouver ("Quadra FNX") 193 334 154 shares of Quadra FNX, for the price of CAD 15.00 per share (representing the equivalent of PLN 47.31 at the average CAD/PLN exchange rate of the National Bank of Poland of 5 March 2012), and the total price of CAD 2 900 012 thousand (representing the equivalent of PLN 9 147 219 thousand at the average CAD/PLN exchange rate of the National Bank of Poland of 5 March 2012).

The shares were purchased in execution of the agreement dated 6 December 2011 entered into between KGHM and Quadra FNX under a Plan of Arrangement recommended by the Board of Directors of Quadra FNX. The shares purchased by 0929260 B.C. U.L.C. represent 100% of the share capital of Quadra FNX and 100% of the votes at the General Meeting of this company. The shares do not have a nominal value. The aforementioned number of shares includes 1 832 543 shares of Quadra FNX which arose after the date of signing of the Agreement as a result of a conversion of instruments (options and warrants) issued by Quadra FNX, which are convertible to shares.

The decision was simultaneously taken to delist the shares of Quadra FNX from trade on a regulated Canadian market and to change the company's name to KGHM International Ltd. Closure of the transaction took place following fulfilment of the conditions precedent foreseen in the Agreement.

Purchase of the Quadra FNX shares was paid for in cash obtained by 0929260 B.C. U.L.C. based on financing agreements entered into within the KGHM Group, deriving from the internal funds of KGHM and is of a long-term, equity investment nature. The carrying amount of the shares purchased by 0929260 B.C. U.L.C. will be recognised in the account books of 0929260 B.C. U.L.C. at the aforementioned purchase price, plus transaction costs.

#### **Signing of a loan agreement by Sierra Gorda SCM (8 March 2012)**

On 8 March 2012, Sierra Gorda SCM, held by Quadra FNX Mining Ltd („Quadra FNX”), Sumitomo Metal Mining Co., Ltd. and Sumitomo Corporation, signed a loan agreement with financial institutions for USD 1 billion (representing the equivalent of PLN 3.12 billion at the average National Bank of Poland exchange rate for USD/PLN of 8 March 2012). The loan will be used to finance the Sierra Gorda Project („Sierra Gorda”) in Chile.

Sierra Gorda is a joint venture of Quadra FNX and Sumitomo Group companies in which Quadra FNX holds 55%, Sumitomo Metal Mining Co., Ltd., holds 31.5% and Sumitomo Corporation holds 13.5 %. Sierra Gorda is the major development project of Quadra FNX, advancing one of the largest new porphyry copper and molybdenum deposits in the world. It is estimated that capital expenditure for the project will amount to approximately USD 3 billion. Start-up of Sierra Gorda is expected in 2014. Planned annual production: approx. 220 thousand tonnes of copper, 11 thousand tonnes of molybdenum and 2 tonnes of gold for over 20 years.

The loan was granted by the following financial institutions: Japan Bank for International Cooperation, and four private banks: Mizuho Corporate Bank, Ltd., Sumitomo Mitsui Banking Corporation, The Bank of Tokyo-Mitsubishi UFJ, Ltd. and The Sumitomo Trust & Banking Co., Ltd. The loan was granted for a period of 9.5 years. Interest on the loan is based on standard market terms applied to this type of financing, and was set based on LIBOR + a bank margin. This is a project finance type of loan, without recourse to Quadra FNX. During construction of the project, the loan is secured by a completion guarantee issued by Sumitomo Metal Mining and Sumitomo Corporation. Following commencement of the project, repayment of the loan will be guaranteed by long term copper and molybdenum off-take agreements.

Other information published:

- information on candidates for Membership of the Supervisory Board of the Company (18 January 2012),
- resolutions adopted by the Extraordinary General Meeting on 19 January 2012 (19 January 2012),
- list of shareholders at the EGM on 19 January 2012 (19 January 2012),
- dates of publication of periodic reports in 2012 (12 January 2012),
- Members of the Supervisory Board appointed on 19 January 2012 by the Extraordinary General Meeting of KGHM Polska Miedź S.A. (27 January 2012),
- forecast of results for 2012 (27 March 2012).

## **Appendix C: List of tables, diagrams and charts**

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**Appendix D: Major events affecting the Company's activities in 2011 \***

Date	Description	Page
<b>18.01.2011</b>	Agreement for the sale of copper wire rod and oxygen-free rod with Tele-Fonika Kable Sp. z o.o. S.K.A.	115
<b>31.01.2011</b>	Forecast of financial results for 2011	139
<b>2.02.2011</b>	Purchase of shares of Nitroerg S.A.	123
<b>4.02.2011</b>	Agreement for the sale of copper cathodes in 2011 with MKM Mansfelder Kupfer und Messing GmbH	115
<b>23.03.2011</b>	Purchase of 71 million shares of TAURON Polska Energia S.A.	124
<b>15.06.2011</b>	Ordinary General Meeting of KGHM Polska Miedź S.A. – changes in the composition of the Supervisory Board	108
<b>15.06.2011</b>	Agreement for the sale of copper wire rod with nkt cables GmbH Cologne and its subsidiaries	115
<b>30.06.2011</b>	Preliminary agreement to sell 100% of the shares of Polkomtel S.A.	115,123
<b>11.07.2011</b>	The right to dividend date for 2010 (14.90 PLN/share)	
<b>12.08.2011</b>	Dividend payment date for 2010	
<b>5.09.2011</b>	Adjusted forecast of financial results for 2011	139
<b>29.09.2011</b>	Contingent binding agreement with Netia S.A. for the sale of 100% of the shares of Telefonía DIALOG S.A.	115,123
<b>20.10.2011</b>	Extraordinary General Meeting of KGHM Polska Miedź S.A. – changes in the composition of the Supervisory Board	108
<b>8-9.11.2011</b>	Employee referendum on the buyout of the coal equivalent	117
<b>9.11.2011</b>	Sale of the shares of Polkomtel S.A.	115,123
<b>6.12.2011</b>	Contingent binding agreement regarding the purchase of shares of Quadra FNX Mining Ltd.	115,125
<b>16.12.2011</b>	Sale of the shares of Telefonía DIALOG S.A.	115,123
<b>20.12.2011</b>	Agreement for the sale of copper cathodes in 2012-2016 entered into with China Minmetals Corporation	115
<b>21.12.2011</b>	Adjusted forecast of financial results for 2011	139
<b>21.12.2011</b>	Conclusion of work on the Bankable Feasibility Study for the Ajax project	125
<b>14.12.2011, 30.12.2011, 13.01.2012</b>	Publication by the Minister of Finance of subsequent draft versions of the Law on the minerals extraction tax	140
<b>19.01.2012</b>	Extraordinary General Meeting of KGHM Polska Miedź S.A. – changes in the composition of the Supervisory Board	108
<b>14.02.2012</b>	Approval of the draft Law on the minerals extraction tax by the parliamentary Committee of Public Finance	140
<b>20.02.2012</b>	General Meeting of Quadra FNX Mining Ltd. – approving the transaction purchase of Quadra FNX Mining Ltd. by KGHM Polska Miedź S.A.	125
<b>2.03.2012</b>	Adoption by the Parliament of Act on the mineral extraction tax	140
<b>5.03.2012</b>	Conclusion of purchase of 100% of the shares of Quadra FNX Mining Ltd	125
<b>12.03.2012</b>	Change of the name of Quadra FNX Mining Ltd. to KGHM International Ltd.	125
<b>14.03.2012</b>	Approval by the Senate of the Act on the minerals extraction tax	140
<b>27.03.2012</b>	Forecast of results for 2012	140

\* Reflecting events after the end of the reporting year – to the date of preparation of the annual report

<b>SIGNATURES OF ALL MEMBERS OF THE MANAGEMENT BOARD</b>			
<b>Date</b>	<b>First, Last name</b>	<b>Position/Function</b>	<b>Signature</b>
27 March 2012	Herbert Wirth	President of the Management Board	
27 March 2012	Maciej Tybura	I Vice President of the Management Board	
27 March 2012	Wojciech Kędzia	Vice President of the Management Board	