

**Assessment of the standing of KGHM Polska Miedź S.A.
for financial year 2020, including an evaluation
of the internal control, risk management and compliance
systems and the internal audit function**

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1. Introduction

In accordance with section II.Z.10.1 of the „Best Practice for GPW Listed Companies” the Supervisory Board of KGHM Polska Miedź S.A. hereby presents an „Assessment of the standing of KGHM Polska Miedź S.A. for financial year 2020, including an evaluation of the internal control, risk management and compliance systems and the internal audit function”. This assessment was prepared based on documents submitted by the Management Board, discussions held with the participation of the Management Board and other persons invited to attend meetings of the Supervisory Board, and also takes into account the financial statements and the reports of the Management Board on the activities of KGHM Polska Miedź S.A. and of the KGHM Polska Miedź S.A. Group, and based on the conclusions from the audit of the Company’s accounts by a Certified Auditor.

2. Economic results of KGHM Polska Miedź S.A. in 2020

2.1 Mine and metallurgical production

In 2020 extraction of ore (dry weight) amounted to 29.7 million tonnes, which was 0.2 million tonnes less than in 2019. The average copper content in extracted ore was slightly lower than in the prior year and amounted to 1.49%. In the case of silver in ore, content lower and amounted to 48.0 g/t.

As a result the amount of copper in extracted ore was lower than in 2019 by 7.3 thousand tonnes of Cu and amounted to 442.0 thousand tonnes. The volume of silver in ore decreased by 33 tonnes and amounted to 1 423 tonnes.

In 2020, 29.7 million tonnes of ore (dry weight) were processed (or 0.2 million tonnes less than in 2019). The lower amount of ore extracted by the mines directly affected the amount of copper in concentrate, which amounted to 392.7 thousand tonnes.

The production of concentrate (dry weight) decreased as compared to 2019 by 23 thousand tonnes, while the amount of copper and silver in concentrate was lower than the amount produced in 2019 respectively by 6.2 thousand tonnes and 31 tonnes.

In consequence of the above the Company produced 560.4 thousand tonnes of electrolytic copper, of which 413.3 thousand tonnes (74%) was from own concentrate. This means a decrease as compared to metallurgical production in 2019 by 0.9% due to the limited supply of copper scrap in the first half of the year, which prevented full utilisation of the production assets, and due to the maintenance shutdown at the Głogów I Copper Smelter and Refinery. By supplementing own concentrate with purchased metal-bearing materials in the form of scrap, copper blister and imported concentrate, existing technological capacity was effectively used in the second half of the year.

The production of other metallurgical products (silver, wire rod and OFE rod) derives from the level of electrolytic copper production and depends on the type of raw material used, and above all on market demand.

The production of metallic silver in 2020 amounted to 1 323 tonnes, or a decrease by 77 tonnes (-6%) as compared to 2019. Production of metallic gold was also lower, with production by the Company of 96.8 thousand troy ounces (a decrease by 6.9 thousand troy ounces, or 7%).

2.2 Macroeconomic conditions in 2020

In 2020, the average annual price of copper was 6 181 USD/t, or an increase compared to the prior year by 3%. The price of silver, which averaged 20.54 USD/ounce, increased by 27%.

The average annual USD/PLN exchange rate (per the NBP) in 2020 amounted to 3.90 USD/PLN and was 2% higher than in 2019 (3.84 USD/PLN).

2.3 Revenues from sales

In 2020, the volume of copper sales by KGHM Polska Miedź S.A. amounted to 561.0 thousand tonnes and was 1% higher than in 2019. Sales of metallic silver by KGHM Polska Miedź S.A. in 2020 amounted to 1 369 tonnes and were lower than the level of sales in 2019 by 24 tonnes (2%). The volume of gold sales in 2020 amounted to 100.1 thousand troy ounces, or a decrease by 1% as compared to 2019 (101.4 thousand troy ounces).

Total revenues from contracts with customers of KGHM Polska Miedź S.A. in 2020 amounted to PLN 19 326 million and were 9% higher as compared to revenues achieved in 2019 (PLN 17 683 million).

Revenues from copper sales in 2020 amounted to PLN 14 258 million, or a difference of +6% compared to the level of sales revenue in the prior year (PLN 13 474 million).

Revenues from metallic silver sales in 2020 amounted to PLN 3 453 million and were higher by 24% as compared to the level of sales revenue in 2019, mainly due to the higher prices of this metal compared to 2019. Revenues from gold sales in 2020 amounted to PLN 690 million, and in 2019 to PLN 543 million. The difference was due to higher gold prices in 2020.

2.4 Cost of sales, selling costs and administrative expenses

The Company's cost of sales, selling costs and administrative expenses (cost of products, merchandise and materials sold plus selling costs and administrative expenses) in 2020 amounted to PLN 16 161 million and was 6% higher as compared to 2019. A major factor affecting the Company's cost of sales, selling costs and administrative expenses was the utilisation of inventories, which led to a higher sales volume.

The cost of producing copper in concentrate - C1 was as follows: in 2019: 1.74 USD/lb and in 2020: 1.62 USD/lb. This cost was impacted by the weakening of the PLN versus the USD as well as the increase in silver and gold prices, which led to an increase in the valuation of by-products.

2.5 Financial results

The Company recorded a profit for 2020 in the amount of PLN 1 779 million, or PLN 515 million (+41%) higher than in the prior year.

The change in the result was mainly due to the following factors:

- an increase by PLN 1 643 million in revenues from contracts with customers, comprised of:
- an increase in revenues by PLN 1 216 million due to higher prices of copper (+181 USD/t, +3%), silver (+4.33 USD/oz t, +27%) and gold (+370 USD/oz t, +27%),
- an increase in revenues by PLN 258 million from sales of basic products (Cu, Ag, Au) due to a more favourable average annual USD/PLN exchange rate (a change from 3.84 to 3.90 USD/PLN),
- a higher adjustment of revenues due to hedging transactions, from PLN 245 million to PLN 323 million (+PLN 78 million),
- an increase in revenues by PLN 42 million due to a higher volume of sales of copper (+4.0 thousand tonnes, +1%), with a lower volume of sales of silver (-24 t, -2%) and gold (-1.2 thousand troy ounces, -1%),
- an increase by PLN 49 million in other revenues from sales, including from the sale of merchandise, waste and production materials (+PLN 132 million) with lower revenues from the sale of refined lead (-PLN 27 million), sulphuric acid (-PLN 13 million) and rock salt (-PLN 12 million).
- an increase in cost of sales, selling costs and administrative expenses by PLN 870 million, of which:
- higher costs by PLN 207 million due to the utilisation of inventories (change in 2020: + PLN 576 million; in 2019: + PLN 369 million),
- higher consumption of purchased metal-bearing materials by 4.9 thousand tonnes of copper (+3%) at a purchase price higher by 3%, resulting in higher costs by PLN 196 million,
- an increase in other costs by PLN 467 million, comprised mainly of an increase in the value of goods and materials sold by PLN 159 million and in other expenses by nature by PLN 294 million.
- a decrease by PLN 319 million in impairment losses on shares and investment certificates in subsidiaries,
- a decrease by PLN 163 million due to a change in differences between impairment losses recognised and reversed on financial instruments measured at amortised cost, from +PLN 102 million to -PLN 61 million.
- a deterioration by PLN 104 million of the result on changes in the fair value of financial assets measured at fair value through profit or loss, from +PLN 84 million to -PLN 20 million,
- a deterioration by PLN 103 million of the result on the measurement and realisation of derivatives,
- an increase in the result by PLN 53 million due to provisions recognised and released,
- an increase by PLN 49 million in the refund of excise tax from prior years,

- impact of exchange differences (-PLN 38 million),
- unwinding of the discount effect (+PLN 33 million),
- change in the balance of income and costs due to interest on borrowings (+PLN 32 million),
- an increase in income tax by PLN 325 million.

2.6 Assets, equity and liabilities of the Company

As at 31 December 2020, total assets amounted to PLN 39 342 million, or an increase as compared to the end of 2019 by PLN 3 353 million, or 9%, mainly due to increases in the following items:

- cash and cash equivalents by PLN 1 619 million,
- property, plant and equipment and intangible assets by PLN 1 097 million, including mining and metallurgical property, plant and equipment by 1 070 million PLN, arising from the realisation of investments – expenditures on property, plant and equipment and intangible assets in 2020 amounted to PLN 2 422 million,
- non-current financial instruments by PLN 1 259 million, including derivatives (+PLN 666 million) and loans granted (+PLN 431 million),

alongside a decrease in the value of inventories (-PLN 228 million), tax assets (-PLN 218 million) and cash pooling (-PLN 207 million).

There was an increase in equity and liabilities, mainly due to increases in the following items:

- equity by PLN 837 million, including with respect to the profit for 2020 in the amount of PLN 1 779 million and an increase in negative capital from the measurement of financial instruments (-PLN 692 million),
- derivatives (+PLN 1 443 million),
- trade and similar payables (+PLN 874 million),
- employee benefits liabilities (+PLN 513 million),

alongside a decrease in liabilities due to borrowings, lease and debt securities by PLN 659 million.

The full scope of financial and economic results of KGHM Polska Miedź S.A. were presented in the separate and consolidated financial statements for 2020, and the Management Board's Report on the activities of KGHM Polska Miedź S.A. and of the KGHM Polska Miedź S.A. Group in 2020. The Supervisory Board in resolutions 41/X/2021 and 43/X/2021 dated 23 March 2021, positively evaluated the aforementioned financial statements, presenting them for approval by the Ordinary General Meeting of KGHM Polska Miedź S.A.

3. Key events in 2020 and selected issues requiring attention

3.1 Capital expenditures

In 2020, total capital expenditures amounted to PLN 2 480 million.

In 2020, capital expenditures (excluding expenditures incurred on uncompleted development work and leasing per IFRS 16 unrelated to an investment project) amounted to PLN 2 417 million.

Capital expenditures were higher than expected due to the decision to re-classify some operating expenses as capital expenditures in accordance with accounting policy.

Around 66% of the capital expenditures incurred on property, plant and equipment were utilised for the advancement of projects involving the replacement of equipment and maintaining mine production in the core business, mainly aimed at maintaining mine production at the planned level.

The remaining capital expenditures involve development projects which affect the core business, production volume, the implementation of activities optimising the use of existing infrastructure, maintaining production costs and adaptation of the company's operations to changes in standards, laws and regulations.

In 2020, the Supervisory Board gave particular attention to overseeing the following development projects:

<p>Development of the Żelazny Most Tailings Storage Facility (in 2020 expenditures incurred amounted to PLN 417 million)</p>	<p>Work continued on Development of the Żelazny Most Tailings Storage Facility:</p> <ul style="list-style-type: none"> - As at the end of 2020 a total of 88% of the physical work on building the Southern Quarter together with slurry, water and power infrastructure has been carried out, and 78% of the physical work on building Stage 1 of the Tailings Segregation and Thickening Station (TSTS).
<p>Replacement of the machine park in the mines (in 2020 expenditures incurred amounted to PLN 203 million)</p>	<p>With respect to modernisation and replacement of mining machinery, 161 pieces of mining equipment were purchased (in the replacement category)</p>
<p>Deposit Access Program – DAP (in 2020 total expenditures incurred on the project amounted to PLN 539 million, including PLN 258 million on outfitting of the mines, PLN 121 million na PSK przy GG-1, PLN 72 million na budowę szybów, i PLN 33 million na układ głównego odwadniania przy SW-4, PLN 55 million koszty finansowania zewnętrznego)</p>	<p>Construction of the GG-1 shaft</p> <ul style="list-style-type: none"> - Work on sinking the GG-1 shaft reached a depth of 1231.2 m . Sinking was completed through the rock salt interval. Work continues on the final concrete-tubing construction under Stage V. <p>Construction of the GG-2 „Odra” shaft</p> <ul style="list-style-type: none"> - Procedures were advanced on altering the planning documents (SUIKZ and MPZP). Commercial conditions with land owners were decided to purchase land. <p>Access and development tunnels</p> <ul style="list-style-type: none"> - 40.3 kilometers of tunneling were excavated (versus a planned 40.9 km) along with infrastructure in the Rudna and Polkowice-Sieroszowice mines, - Tunneling reached the D and T,W-169 intersections. - Necessary infrastructure was installed in the mines: ventilation and power networks, system for hauling belt conveyors, retention reservoirs, the ice water distribution system, the power and dewatering systems. <p>Surface-based Air Conditioning Station (PSK) and Ice Water Transportation System (SPWL)</p> <ul style="list-style-type: none"> - continued construction of the PSK at the GG-1 shaft. The cooling building shell was built, final work on the power building, - Assembly of three-chamber feeder no. 1, - Technical drillholes TK-7 and TK-8 were sunk. - 94% of surface piping was laid.
<p>Program to adapt the technological installations of KGHM to the requirements of BAT Conclusions for the nonferrous metals industry and to restrict emissions of arsenic (BATAs) (in 2020 expenditures incurred amounted to PLN 162 million)</p>	<p>In 2020, under the BATAs Program, 14 projects were advanced, of which the following was completed:</p> <ul style="list-style-type: none"> - An installation to eliminate arsenic-bearing dusts from concentrate drier gases (Legnica Copper Smelter and Refinery) was built and brought on-line. - An installation to eliminate arsenic-bearing dusts from above the anode casting machine (Legnica Copper Smelter and Refinery) was built and brought on-line. - A de-lead slag transport installation (Głogów Copper Smelter and Refinery) was built and brought on-line. - The construction of bypass gases pipelines from the flash furnaces (Głogów Copper Smelter and Refinery) was completed. - A warehouse and storage area for lead-bearing materials (Głogów Copper Smelter and Refinery) was built.

3.2 Development of the Żelazny Most Tailings Storage Facility

Based on the permit received in 2016 to develop the Main Facility to a crown height of 195 meters a.s.l. and a permit to further operate the Tailings Storage Facility, the dam is being built up successively as part of the ongoing operations of the Division. In March 2018, a building permit was issued for the Southern Quarter. Construction of the Southern Quarter will enable the additional deposition of waste tailings in the amount of around 170 million m³.

Following the signing of a contract for construction of the Southern Quarter with the company Budimex, construction is underway on Development of the Żelazny Most Tailings Storage Facility, ensuring the ability to deposit waste tailings to 2037. In 2019, expenditures incurred on advancing the Project to develop the Żelazny Most Tailings Storage Facility amounted to PLN 417 million, including PLN 27.8 million of external financing.

Phase 1 was completed along with receipt of an operating permit. Completion of Phase 1 enables the storage of tailings immediately following the start-up of the Tailings Segregation and Thickening Station. At the same time the project includes the commencement of slimes deposition. At the end of 2020, 88% of construction work on the Southern Quarter along with water management and power infrastructure, the commencement of slimes deposition for the Southern Quarter - Phase 1 was completed.

The project includes work related with the development of a Tailings Segregation and Thickening Station (TSTS). Construction work was completed involving the assembly of the operations building, along with the power building for the TSTS. Execution of the TSTS project included that part related with hydrocyclone technology, while advanced work related with thickening technology enabled the selection of a thickener. Work is underway on the architecture and internal instalations for the operations building, internal instalations, water piping, ventilation and power building. Work is underway on assembling the operating aspects of the TSTS. Work is underway on internal power infrastructure and construction of infrastructure around the TSTS. As at the end of 2020, work on the physical scope of Stage 1 of the TSTS amounted to 78%.

3.3 Situation in the international assets

Sierra Gorda mine in Chile

Sierra Gorda concentrated on implementing its optimisation program oriented towards improving the operation of the mine, the processing plant, infrastructure and the tailings storage facility.

As a result there was a decrease in the number of unplanned maintenance shutdowns caused by breakdowns and an increase in daily average ore throughput, which in turn led to an increase in the amount of ore processed by 8% compared to 2019. The amount of copper in the ore was also higher, and therefore copper recovery was also higher. These factors led to an increase in payable copper production of more than 37% compared to the amount recorded in 2019.

In 2020, production of copper in concentrate amounted to 148.7 thousand tonnes, while production of molybdenum in concentrate amounted to 16.3 million pounds (on a 100% basis, and on a 55% basis respectively: 81.8 thousand tonnes and 9.0 million pounds).

Despite the higher processing of ore there was a drop in molybdenum production by 4.0 million pounds, or nearly 20% compared to 2019, as a result of lower molybdenum content in mined ore and lower recovery.

The Sierra Gorda mine remains focused on increasing the plant's cost effectiveness and operating efficiency.

In 2020, supplementary work continued aimed at preparing for the next stage of engineering work and further project development of the Oxide project. At present most of the oxide ore planned for processing has already been excavated and is currently stored near the site of the future copper leaching and recovery (SX-EW) plant.

In 2020, despite the epidemiological situation caused by the COVID-19 pandemic, the operations of the Sierra Gorda mine were not materially interrupted thanks to the safety measures taken and mobilisation of the workforce.

In 2020, adjusted EBITDA amounted to USD 626 million, of which proportionally to the interest held (55%) PLN 1 346 million is attributable to the KGHM Group. This is an increase of approx. 101% compared to 2019, adjusted EBITDA amounted to USD 312 million (PLN 660 million on a 55% basis).

Operating assets of KGHM International

In 2020, the production assets of KGHM International (excluding Sierra Gorda) produced in total 66.9 thousand tonnes of copper, 0.4 thousand tonnes of nickel, 1.8 tonnes of silver and 66.1 thousand ounces of TPM (gold, palladium and platinum).

Thanks to the safety measures taken and preventative actions, there were no work stoppages caused by the SARS-CoV-2 virus.

KGHM INTERNATIONAL LTD. underwent restructurisation, involving the transfer of management and support processes to the Company's Head Office, resulting from the adopted strategy of implementation of a model of cooperation and integration of key international assets with the domestic operations.

In 2020, exploration work was continued to increase the level of recognition of some of the mineral resources of the Victoria project and actions aimed at maintaining good relations with key stakeholders in the project. Work commenced on preparing and securing selected elements of the infrastructure, as a preparatory phase in the further development of the project.

3.4 Occupational health and safety in KGHM Polska Miedź S.A. in 2020

In 2020 the Company recorded a substantial decrease in the total number of workplace accidents (as defined by the Act dated 30 October 2002 on social insurance) due to workplace accidents and occupational illnesses, with a year-on-year change from 299 to 213 injured (a decrease by 86 accidents). The number of workplace accidents in 2020 in KGHM Polska Miedź S.A., excluding accidents due to natural causes (roof collapses, distressings, tremors, rock falls) was lower by 54 (a decrease from 248 to 194). The number of workplace accidents in the mines due to natural causes connected with the rockmass in 2020 amounted to 19 and was lower by 32 events. The vast majority of workplace accidents (around 97.2%) qualified as light injuries, caused mainly by loss of balance by employees, contact (striking) with or by moveable/ immoveable objects, as well as the breaking off of pieces of rock from the rockmass.

The LTIR_{KGHM} ratio (Lost Time Injury Frequency Rate KGHM) in 2020, or the total number of workplace accidents (as defined by the Act dated 30 October 2002 on social insurance) in the Company, being the number of accidents per million hours worked by the employees of KGHM Polska Miedź S.A., amounted to 7.3. This was lower by 29.0% than the amount recorded in 2019 (10.3), as well as 60.6% lower than the amount recorded in 2010. This is the best result to date in the Company's history, one achieved thanks to the attitude and commitment of all of the Company's employees.

The life and health of employees and workplace safety in general is the chief priority in the hierarchy of values of the KGHM Polska Miedź S.A. Group. For several years the Company has advanced its vision of „Zero accidents due to human and technical errors, zero occupational illnesses among our employees and contractors”. In 2020, the Employee Safety Improvement Program „Think About The Consequences” continued as well as the Program to prevent the most common hazards to workplace safety by utilising innovative technology, in accordance with the updated Company Strategy to the year 2023. The Company applies high OHS standards, both towards its own employees as well as towards those providing services on the grounds of KGHM Polska Miedź S.A., as demonstrated by the Company's receipt in the current year of certification of a safety management system which is compliant with the ISO 45001:2018 standard. KGHM Polska Miedź S.A. was also awarded with the „Leader's Gold Card of Workplace Safety for the years 2021 - 2022”. In the Mining Divisions the Company implemented integrated guidelines to protect miners from dust and particulate matter in the workplace. Due to the ongoing pandemic, apart from the numerous technical and organisational solutions implemented, a uniform „SarsCov-2 pandemic external risk assessment card” was also implemented.

3.5 Preparation of the Company and Group to the current situation in Poland and abroad

Due to the ongoing SARS-CoV-2 coronavirus pandemic, which is the cause of the COVID-19 illness, there still remains uncertainty as to the further development of the pandemic situation both domestically and globally and its potential negative impact on the functioning of the KGHM Polska Miedź S.A. Group. In response to the rapidly changing situation, the key risk factors on which the pandemic has an impact were subjected to ongoing monitoring and detailed analysis, particularly in areas such as production, sales, supply chains, management of personnel and finances.

Currently the risk of interruptions to the operations of production companies in the KGHM Polska Miedź S.A. Group due to the coronavirus is judged to be low, which to a large extent is due to the preparations by the

organisation to function under extreme epidemic conditions as regards production and the logistics of deliveries, supplies and distribution.

In 2020 the COVID-19 epidemic had the greatest impact on the Company's secondary activities involving hotel and spa services.

In the current situation the most important actions for KGHM are those aimed at ensuring the safety of its employees and maintaining operational and supply chain continuity, as well as systematic management of the risk arising from the negative impact of copper prices on markets.

Since the start of the pandemic, KGHM has undertaken wide-ranging and intensive activities aimed at reducing the risk of infection amongst employees as well as persons with whom they have contact (family, co-workers, contractors and clients). There continues to be a lack of any substantial heightened level of absenteeism amongst employees of the Company's core business related to the pandemic. Solutions already-implemented aimed at ensuring employee safety are constantly being analysed and assessed, while additional solutions are continuously being implemented to reduce the risk of spread of the virus amongst employees.

Actions taken within the Group's companies to protect employee safety are on the one hand the result of guidelines and decisions made by the government and central offices, and on the other hand result from formal internal regulations and guidelines provided to the employees of the KGHM Group.

The KGHM Group has undertaken a variety of actions aimed not only at effectively preventing the spread of the virus and protecting the employees of the Group from the risk of infection, but also aimed at the wide-scale support of local and national efforts to assist hospitals and other healthcare centers.

In all of the Polish and international companies of the KGHM Group a variety of internal actions and procedures of a prophylactic and preventative nature have been instituted, such as:

- the distribution of personal protective measures (disinfectant liquids and masks),
- special infolines and email addresses have been set up, where employees can obtain all types of information regarding management, the principles and manner of working under special conditions, including occupational safety and hygiene,
- all travel was suspended as regards international delegations and domestic participation by employees in conferences and training,
- the possibility of home office work was introduced,
- the measurement of body temperature was introduced, including the use of thermal cameras,
- the disinfection of common areas was introduced, including at building entrances, communication passages, washrooms, personal equipment distribution areas, dressing rooms and toilets,
- hand disinfectants were made available at building entrances and washrooms,
- additional equipment was provided for industrial ozonation in the Divisions of KGHM Polska Miedź S.A.,
- in the mines of KGHM Polska Miedź S.A. the number of people travelling in cages was reduced and the frequency of trips into the mines was increased, while special curtains to separate employees in the cages were installed,
- on-line OHS courses were set up,
- an informational campaign was launched using informational media: intranet, posters and billboards, to enable the continuous distribution of current rules and announcements by the government and healthcare services,
- training was provided to employees on how to prevent and restrict the spread of the virus and how to mitigate the impact of infection,
- all food service establishments on company grounds switched to the sole providing of outtake,
- collections were carried out, legal assistance, and the organisation of material and psychological support for employees – at the Robinson mine in the USA an Employee Assistance program was set up.

Thanks to the actions taken and implemented, there are currently no signals that would indicate any threats to the continuity of sales. Sales are made to reliable customers with whom the Company has been in relations for many years and with whom it is in constant contact. Most of the company's customers have not indicated any significant negative consequences of the epidemic on their business.

Nonetheless, should the impact of the pandemic on the global economy continue, the situation could also potentially have a negative financial and organisational impact on the KGHM Polska Miedź S.A. in the future.

4. Assessment of the risk management system in the Company in 2020

The KGHM Polska Miedź S.A. Group defines risk as uncertainty, being an integral part of the activities conducted and having the potential to result in both opportunities and threats to achievement of the business goals. The current and future, actual and potential impact of risk on the KGHM Polska Miedź S.A. Group's activities is assessed. Based on this assessment, management practices are reviewed and adjusted in terms of responses to individual risk factors.

Under the Corporate Risk Management Policy and Procedure and the Rules of the Corporate Risk and Compliance Committee updated in 2019, the process of corporate risk management in the Group is consistently performed. KGHM Polska Miedź S.A. oversees the process of managing corporate risk in the Group, while in the companies of the Group, documents regulating the management of corporate risk are consistent with those of the Parent Entity.

Each year, the process of managing corporate risk is subjected to an efficiency audit (compliant with the guidelines of Best Practice for GPW Listed Companies 2016").

Risk factors in various areas of the Group's operations are continuously identified, assessed and analysed in terms of their possible limitation. Each key risk in the KGHM Polska Miedź S.A. Group undergoes in-depth analysis in order to develop a Risk Response Plan and Corrective Actions. Other risk factors undergo monitoring by the Department of Corporate Risk Management and Compliance, and in terms of financial risk by the division of the Executive Director for Treasury Operations - Corporate Treasurer.

The corporate risk management process adopted by the KGHM Polska Miedź S.A. Group is inspired by the solutions adopted by the ISO 31000:2018 standard, best practice in risk management and the specific nature of the KGHM Polska Miedź S.A. Group

A tool used in identifying risk in the KGHM Polska Miedź S.A. Group is the Risk Model. Its structure is based on a given risk's source and is divided into the following 5 categories: **Technological, Values chain, Market, External and Internal**. Several dozen sub-categories have been identified and defined for each of these categories, covering particular areas of the operations or management.

Organisational structure of risk management in KGHM Polska Miedź S.A.

Supervisory Board (Audit Committee)				
Performs annual assessment of the effectiveness of the risk management process and monitors the level of risk factors and ways to address them.				
Management Board				
Has ultimate responsibility for the risk management system and supervision of its individual elements.				
1st line of defense	2nd line of defense			3rd line of defense
Management	Risk Committees			Audit
<p>Managers are responsible for identifying, assessing and analysing risk factors and for the implementation, within their daily duties, of responses to risk. The task of the management staff is ongoing supervision of the application of appropriate responses to risk within the tasks realised, to ensure the expected level of risk is not exceeded.</p>	Support the effectiveness of the risk management process.			
	Corporate Risk and Compliance Committee	Market Risk Committee	Credit Risk Committee	Financial Liquidity Committee
	Manages corporate risk and continuously monitors key risk factors	Manages risk of changes in metals prices (e.g.: copper and silver) as well as exchange and interest rates	Manages risk of failure of customers to meet their obligations	Manages risk of loss of liquidity, understood as the ability to pay financial liabilities on time and to obtain financing for operations
	<i>Corporate Risk Management Policy</i>	<i>Market Risk Management Policy</i>	<i>Credit Risk Management Policy</i>	<i>Financial liquidity Management Policy</i>
	Department of Corporate Risk Management and Compliance	Executive Director for Treasury Operations - Corporate Treasurer		
<i>Reports to the Management Board</i>	<i>Reports to the Vice President of the Management Board (Finance)</i>			The Internal Audit Plan is based on assessing risk and subordinated business goals, assessed is the current level of risk factors and the degree of efficiency with which they are managed.
				<i>Internal Audit Rules</i>
				Executive Director for Audit and Control
				<i>Reports to the President of the Management Board</i>

Market, credit and liquidity risk

The goal of market, credit and liquidity risk management in the KGHM Polska Miedź S.A. Group is to restrict the undesired impact of financial factors on cash flow and results in the short and medium terms and to enhance the Group's value over the long term. The management of risk includes both the elements 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. In the Parent Entity these issues are covered in the following documents:

- Market Risk Management Policy and the Rules of the Market Risk Committee,
- Credit Risk Management Policy and the Rules of the Credit Risk Committee, and
- Financial Liquidity Management Policy and the Rules of the Financial Liquidity Committee,

The „Market Risk Management Policy in the KGHM Polska Miedź S.A. Group” covers selected mining companies in the Group (KGHM Polska Miedź S.A., KGHM INTERNATIONAL LTD., FXN Mining Company Inc., Robinson Nevada Mining Company, KGHM AJAX MINING Inc. and Sociedad Contractual Minera Franke). The goals of market risk management at the Group level are achieved as a result of their being carried out in individual companies of the Group, with coordination of these activities by the Parent Entity, KGHM Polska Miedź S.A. Within the Company, key tasks are centralised involving the process of market risk management in the Group (such as coordination of the identification of sources of exposure to market risk, the proposal of hedging strategies, contacts with financial institutions aimed at concluding, confirming and settling derivatives transactions and calculating measurements to fair value).

Financial liquidity management is carried out in accordance with the „Financial Liquidity Management Policy in the KGHM Group” which in a comprehensive manner regulates financial liquidity management in the Group carried out by individual Group companies, while its organisation and coordination as well as the supervision thereof is performed in the Parent Entity.

Credit risk management in the Parent Entity is carried out in accordance with the Management Board-approved Credit Risk Management Policy. The Parent Entity serves as an advisor to the Group’s companies with respect to managing credit risk. The „Credit Risk Management Policy in the KGHM Polska Miedź S.A. Group” applies to selected Group companies, the goal of which is to introduce a comprehensive, joint approach and the most important elements of the credit risk management process.

The Supervisory Board of KGHM Polska Miedź S.A. positively assesses the functioning of the risk management system in the KGHM Polska Miedź S.A. Group, while the comprehensive approach to risk management is consistent with the strategy of development, continuous striving towards operational excellence and the principles of sustainable and responsible business. In the opinion of the Supervisory Board, the KGHM Polska Miedź S.A. Group in 2020 exercised due diligence in the planning and execution of actions aimed at minimising exposure to risk, by both reducing the susceptibility to individual risk factors as well as reducing the probability of materialisation of negative events. It should however be remembered that the process of risk management is always connected with uncertainty as to the effectiveness of risk mitigation, especially as regards those areas beyond the direct control of the KGHM Polska Miedź S.A. Group.

5. Evaluation of the compliance system in the Company in 2020

The Company recognises that compliance is an important element in its effective functioning, which requires that decisive actions to be taken to ensure that this goal is achieved. In order to standardise the approach to compliance, defined as compliance with the requirements resulting from applicable legal regulations (external and internal) or voluntarily accepted legal obligations and standards, in 2020 the Management Board of KGHM Polska Miedź S.A. adopted the Compliance Management Policy in the KGHM Polska Miedź S.A. Group along with the Compliance Management Procedure and Methodology in KGHM Polska Miedź S.A. The process of compliance management, which is connected with the process of corporate risk management in the KGHM Polska Miedź S.A. Group, is an important business tool serving to prevent the occurrence of events which could result in sanctions being imposed.

There exist in KGHM Polska Miedź S.A. a variety of organisational units (such as the Department of Corporate Risk Management and Compliance, the Department of Supply Chain Security, the Ethics and Anti-Corruption Procedures Unit, The Regulatory and Strategic Analysis Department and the Legal Department) as well as systemic solutions (such as employee access to legal databases, formalised internal procedures for legal interpretations, processes to identify legal requirements and to assess their compliance in terms of the ISO standards in force in the Company), which are aimed at ensuring compliance.

In 2020 a number of new or updated corporate rules were introduced in the various operational areas of the KGHM Polska Miedź S.A. Group aimed at ensuring the highest possible level of compliance of its activities with existing laws, as well as the voluntary adoption of legal obligations. Moreover, KGHM Polska Miedź S.A. is systematically developing its compliance system, as demonstrated by the actions taken in 2020. In consideration of the above, the Supervisory Board positively assesses the compliance system of the KGHM Polska Miedź S.A. Group.

6. Evaluation of the internal audit and internal control systems

The internal audit system is aimed at ensuring effective and efficient Company operations, the accuracy of financial reporting and the compliance of the Company’s actions with laws in force and internal regulations.

The internal control system comprises the areas of oversight, all of the internal procedures, the function of compliance with laws, the financial reporting system, organisational structures, IT systems audits and other control mechanisms aiding in the achievement of the Company’s goals as well as having an impact on its security and the stability of its functioning. The purpose of the internal control system is the rational realisation of effective and efficient operations, the accuracy of information disclosed, in particular as regards financial statements as well as the adequacy and operational efficiency of the audits conducted.

The internal control system is supervised in the Company by:

Assessment of the standing of KGHM Polska Miedź S.A. for financial year 2020, including an evaluation of the internal control, risk management and compliance systems and the internal audit function

- the actions of the Company's Management Board, involving the establishment of an appropriate and effective internal control system,
- monitoring the efficiency of the internal control system by the Supervisory Board's Audit Committee, and
- oversight by the owners of individual business areas over their respective organisational units.

In addition, in terms of institutional control, actions are undertaken by specialised units, in particular in the Security and Preventing Losses division and the Audit and Control division, such as the Security Department, the Supply Chain Security Department and the Internal Control Department.

The internal audit function plays a special role, and is performed by a separate organisational unit in the structure of KGHM Polska Miedź S.A. – the Internal Audit Department, headed by the Executive Director for Audit and Control. The internal audit function is overseen by the Supervisory Board's Audit Committee, which issues opinions on internal audit regulations and the internal audit plan, and receives an annual report on the execution of audit plans.

The Internal Audit Department systematically evaluates and monitors the control mechanisms and identifies potential risks in individual processes occurring in the Company and in the entire Group, as well as uncovers irregularities and violations of existing procedures.

Auditing activities focus on assessing risk and evaluating and monitoring the functioning of the internal control systems in individual processes occurring in the Company and Group.

The work of internal auditing in KGHM Polska Miedź S.A. is based on the principle of independence, and may encompass all areas of the Company's and Group's operations. In cases where the employees of the Internal Audit Department do not possess sufficient competence in an area which is to be assessed, the Department makes use of internal or external experts.

In 2020, the Department performed 31 audits. Most were performed in several, or a dozen or so, Group entities simultaneously. These tasks were performed both in the divisions as well as in companies of the KGHM Polska Miedź Group, including those outside Poland.

As a result of audits performed in 2020, recommendations were formulated for implementation. The observations, results and recommendations from the comprehensive work were described in the Report on the Implementation of the Internal Audit Plan for 2020 of the KGHM Polska Miedź S.A. Group.

The audits carried out uncovered irregularities and violations of, among others, a formal and legal nature, violations of employee duties, and also inefficient management of resources in various units of the KGHM Group. The recommendations made in respect of the controlled units were aimed at eliminating the identified irregularities and strengthening the internal control system by implementing corrective procedures. The implementation of recommendations is continuously monitored by the Internal Audit Department.

In the opinion of the Supervisory Board of KGHM Polska Miedź S.A., the internal audit and internal control systems are effective and are an important element in managing risk as regards the functioning of the audit mechanisms for the operations of KGHM Polska Miedź S.A. In the opinion of the Supervisory Board, the independent and objective information about the internal control system and the system for managing risk as well as the analysis of business processes within the KGHM Polska Miedź S.A. Group which are supplied by the internal audit system, provide added value and promote the organisation's enhanced operational performance.