

**REPORT FOR THE ORDINARY GENERAL MEETING OF SHAREHOLDERS
FOR THE PERIOD FROM 1 JANUARY TO 31 DECEMBER 2011
COVERING ASSESSMENT OF THE COMPANY'S SITUATION
WITH CONSIDERATION TO EVALUATION OF THE INTERNAL CONTROL
SYSTEM AND RISK MANAGEMENT SYSTEM**

I. Assessment of the Company's situation

Revenue from sales amounted to PLN 1 916.717 million, a PLN 367 million increase on the figure for 2010 and PLN 42.68 million higher than specified in the plan for 2011. The net result of PLN 207.672 million is PLN 51.874 million above the plan and constitutes a PLN 147.219 improvement on 2010. These results indicate a surplus in relation to the plan for 2011.

The Company's asset and financial situation shows a significant improvement on 2010, expressed through revenue growth and an improvement in profitability ratios and performance indicators.

Liquidity ratios were subject to a slight deterioration, but remained at an acceptable level.

There were significant changes in asset structure in 2011. Non-current assets increased by PLN 911.556 million to PLN 1 973.543 million, constituting 79.7% of total Company assets. An increase in investment in subsidiaries, associates and jointly controlled entities constituted the largest item - transactions connected with the acquisition of a 66% stake in Z.Ch. Police S.A. and a 40.86% stake in ZAK S.A.

The Supervisory Board believes that both acquisitions were fitting and were executed on conditions which were highly beneficial to the Company. The acquisition of a majority stake in Z.Ch. Police and almost complete control over ZAK S.A. provide significant opportunities for effective operations within a large group since there are many synergies. These possibilities were partially taken advantage of in 2011 in the areas of logistics, ammonia and nitric acid supplies and joint purchases of sulphur, coal and natural gas. The economy, recovering from the recession in 2008-2009, is notable for factors including increased demand for the Company's core products, i.e. fertilisers and plastics. These are symptoms of the on-going growth in demand for these products in the coming years.

II. Assessment of the internal control and risk management systems

Principles of internal control

In accordance with the *Organisational Regulations at Zakłady Azotowe w Tarnowie-Mościcach S.A.* and the *Internal Control Regulations at Zakłady Azotowe w Tarnowie-Mościcach S.A.* (constituting an appendix to Internal Order no. 36/2005 of 5 October 2005), internal control within the Company is organised as follows:

1) each employee controls his/her own work, which consists of systematic inspection of the

correctness of the work performed with regard to the provisions contained in the Internal Control Regulations and the tasks resulting from the employee's scope of duties,

2) functional control is ensured by management personnel and consists of performing systematic activities aimed at assessing the correctness of operations performed during and immediately after performance. All areas of the Company's operations are subject to this type of control.

Functional control is ensured by: the President of the Management Board - Managing Director, Members of the Management Board, Chief Financial Officer, Directors of Departments/Centres, the managers of specific organisational units, and other employees required to ensure control within a specific objective and subjective area.

3) organisational control is ensured by separate organisational units tasked with specialist control functions in specific scopes; this type of control concerns all decisions and actions and documents reflecting economic transactions, together with the implementation of the accounting policies applied within the Company.

Institutional control is ensured by: the Department of Economic Control and Inventory, the HR Department, Technical Safety, Employment Protection and Environment Department and other organisational units pursuant to separate internal regulations.

4) systematic and periodic inventory, the means for organising which are specific in the Inventory Instructions.

The organisation (system), principles and means of internal control operations are established in the *Internal Control Regulations of Zakłady Azotowe w Tarnowie-Mościcach S.A.*

In order to adapt internal and legal regulations concerning internal control to the applicable standards currently in force, in 2009 the Company implemented "Standards for the Performance and Documentation of Economic Control at Zakłady Azotowe w Tarnowie-Mościcach S.A."

Internal audit covering the Group was implemented on 29 November 2011 pursuant to internal order no. 41/2011, establishing the Internal Audit Office, a new organisational unit within Company structure which is directly subordinate to the President of the Management Board.

The approved Internal Audit Regulations clearly specify the objectives, authorisations and liability of the Audit Office.

These regulations cover:

- the mission of the Internal Audit Office,
- standards of professionalism,
- scope of operations,
- place of the Internal Audit Office within the risk management process,
- authorisations of the audit team,
- cooperation with external entities,
- the principles for planning the operations of the Internal Audit Office,
- means of task reporting,
- principles for drafting and storing audit documentation.

Within the Company and the Azoty Tarnów Group, internal audit is understood as independent, objective assurance and advisory activities which are aimed at creating value

and streamlining Group operations. It is supported in achieving its objectives through a systematic and disciplined approach to assessing and improving the effectiveness of the risk management process, the system of internal control and corporate governance.

A SAP ERP system has been in operation at the Company since 2009, and since 1 April 2009 has been the primary system. It is protected by passwords, has limited access functions and work within the system requires an individual licence.

The IT system specification fulfils the requirements of art. 10, sec. 1, point 3, letter c of the Polish Accounting Act. The accounts and the links between accounting records and documents and the financial statements fulfil the requirements of section 2 of the Polish Accounting Act.

The accounts, accounting documents, documentation concerning the means of managing the accounts and the approved financial statements of the Company are stored in accordance with section 8 of the Polish Accounting Act.

The accounting and IT systems ensure compliance of the accounting records with statutory regulations.

Risk management

There is a Currency Risk Management Procedure in force within the Company (Internal Order no. 2/2009), which governs actions to be taken to limit financial risk. Based on this order, a Currency Risk Committee is active at the Company, which is chaired by the Director of the Finance Department. The Director of the Finance Department approves the currency risk, interest rate risk and credit risk policies for each calendar year.

The Company identifies the following types of financial risk:

Currency risk

For many years the Company has been active both in export sales and the purchase of the commodities needed for production, making payments in foreign currencies (in particular USD and EUR). In connection with this, the Company is exposed to currency risk with regard to net foreign currency exposure in the above currencies, resulting from the balance of foreign currency trading from commercial operations and deliveries, together with commercial, finance and investment receivables and liabilities. In particular, this risk may appear as an increase in the cost of supplies or a drop in effective revenues from sale, denominated in PLN. Profitability of exports as well as foreign currency-denominated domestic sales are adversely influenced by a stronger domestic currency and positively affected by a weaker domestic currency. The Company uses a range of instruments and activities to hedge foreign currency positions, including natural hedging through increasing the value of future foreign currency liabilities in the field of supplies and investment acquisitions, forward contracts and currency swaps. It is also possible to create symmetrical options structures such as corridors or options spreads with put-call symmetry. The Company executes hedging transactions with a 12-month timeframe if it is possible to hedge EUR or USD against PLN above the planned assumed rate and within a 3-month timeframe if it is possible to hedge the exchange rate at which foreign currency sales were made, however below the assumed exchange rate.

The Company only executes foreign currency hedging transactions at banks with which a framework agreement providing comprehensive specification of the principles for execution and clearing of this type of transaction has previously been entered into.

The execution of hedging transactions within a timeframe exceeding 12 months or exceeding the principles specified in the Currency Risk Management Policy requires Management Board acceptance.

Interest rate risk

The Company is exposed to interest rate risk on its financial liabilities - chiefly loans and borrowings denominated in PLN and EUR based on floating interest rates, and financial assets - mainly bank deposits denominated in PLN which are based on variable and fixed market interest rates.

The Company first and foremost uses natural hedging, based on the application of a common interest rate basis for PLN-denominated loans, borrowings and financial assets.

Hedging other exposure may be implemented through executing only the following transactions:

- forward rate agreements
- interest rate swaps
- currency interest rate swaps

These transactions are mainly executed for periods up to 12 months and require the acceptance of the Vice-President of the Management Board for financial affairs.

The execution of hedging transactions within a timeframe exceeding 12 months or exceeding the principles specified in the Interest Rate Risk Management Policy requires Management Board acceptance.

Credit risk

Credit risk mainly concerns trade receivables, and to a lesser extent fixed-term deposits and funds held in bank accounts.

Considering the procedures in place within the Company and its diversified client portfolio, credit risk is relatively insignificant. On the other hand, the substantial portion of the cash surplus is subject to virtual cash-pooling, connected with a current account loan granted to the Group by PKO BP S.A. This allows the Group to optimise its interest costs and income, while simultaneously limiting credit risk.

The Company maintains a unified credit risk policy, making assessment and inspecting the creditworthiness of customers on an on-going basis, using economic intelligence reports, debtor registers and credit histories.

Trade receivables from unrelated entities are insured under the trade credit insurance policies held with Korporacja Ubezpieczeń Kredytów Eksportowych S.A. and Atradius Credit Insurance N.V. S.A. These policies cap credit risk at the level of the Group's deductible (5% to 10% of the value of insured receivables). These insurance policies ensure that the financial position of business partners is constantly monitored and receivables are collected whenever necessary. Should the partner become physically or legally bankrupt, insurance compensation is received, totalling 90-95% of the insured receivables.

Furthermore, some trade receivables from unrelated parties are protected by letters of credit and guarantees which remain outside the scope of insurance.

Trade credit, in turn, is extended primarily based on approval by the insurance company, and sometimes due to a positive trading history as well as creditworthiness as concluded from credit bureau reports, financial statements and payment history.

Whenever no positive trading history exists between a counterparty and the Group or when transactions are occasional, and the credit limit cannot be insured, a prepayment is required.

Risk of changes in market prices for products

The Company is a manufacturer of chemicals - a product group where price is highly dependent on the price of commodities. This concerns in particular products based on natural gas and petrochemicals, where demand is subject to severe fluctuations. Taking into account the lack of beneficial financial instruments hedging price risk for its core commodities and products, the Company limits risk through taking steps aimed at diversifying sources of supply for strategic commodities, together with the introduction of price formulae linking product price with commodity price in order to limit risk resulting from variability in petrochemical products.

The Company has identified the following key risks for Company operations and development:

Electricity price risk

Price projections for the energy industry up to 2015 and beyond show a significant increase (approx. 20-40%) in the costs of generating energy, resulting from implementation of the Industrial Emissions Directive (IED) and the introduction of market trading in CO₂ emission units. The key step towards building competitive advantage is modernisation of the Company's own power and heat generation facilities. The Company systematically monitors the electricity market and attempts to systematically optimise costs and maximise the use of electricity generated on site.

Risk of limitations in natural gas supplies

Interruptions in gas supplies may be caused both by economic and political factors. The sole gas supplier is PGNiG, for which a significant source of supplies is Russian monopoly Gazprom. In order to limit the impact of this risk on its financial results, the Company is investing in the capacity to generate gas from local sources, which is supplied by PGNiG without the intermediation of Gaz-System S.A. The Company is thus attempting to diversify its gas supplies through reducing its use of mains gas, which may be limited to various degrees in accordance with energy law.

Risk of tariff policy liberalisation in fertiliser trading

Russia's planned accession to the WTO may lead to a stabilisation in prices, particularly during the payment of direct subsidies. Due to the fact that manufacturing costs in Russia are significantly lower than in Poland, a price drop cannot be ruled out. The Company systematically monitors the fertiliser market situation and ensures a flexible pricing policy.

Risk of excise duties

An anti-dumping tariff came into force in February 2011 on the export of caprolactam to

China from Europe and the US. A 20.4% tariff was imposed on Azoty Tarnów. In October 2011 this was eventually reduced to 4.9%.

As one of the world's largest manufacturers and exporters of nitrogen fertilisers, China has also introduced a 110% export tariff on urea and phosphorous fertilisers. Chinese government actions are aimed at ensuring an adequate supply of fertilisers in the domestic market in 2012, however they also impact supply in the global market, which subsequently impacts prices. The Company systematically observes and monitors the Chinese and South-East Asian caprolactam and polyamide markets, taking applicable precautionary measures.

Risk of change in legal regulations

Constantly changing legal regulations, both within the EU and domestically, bring the risk that adapting to new legislation may incur costs which could have a negative impact on financial results (in as far as they are unbeneficial to the Company). Both domestic and EU legislation is monitored by the Company and systematically analysed for its impact on Company operations.

Environmental risk

The Company's operations are hazardous to the natural environment. In this respect the Company must hold the applicable environmental permits and must ensure an acceptable level of environmental protection and chemical rescue services in the event of an industrial incident.

The Company holds all permits necessary for its operations, including integrated environmental permits for installations covered by IPPC requirements.

Risk connected with change in environmental regulations is significant for the Company's operations. Environmental risk management consists of the constant monitoring of and reaction to the introduction of new legal regulations. Factors having a significant impact on Azoty Tarnów's operations include the following:

- planned change to the ordinance on fees for landfilling of waste - change in the classification of waste and new (higher) fees for landfilling,
- waste management bill - new regulation (implementation of an EU directive), introducing a range of amendments in waste management, including through the introduction of new definitions,
- implementation of the Industrial Emissions Directive (IED) - introduction of new regulations concerning protection of soil and groundwater, specification of new requirements as mandatory standards and a new approach to integrated permits pursuant to BAT conclusions,
- change to the European Commission decision concerning installations for the manufacture of ammonia in the event of the detection of carbon dioxide, resulting in the necessary to acquire additional greenhouse gas emission units.

Risk of industrial incidents

In principle, the nature of Azoty Tarnów's operations exposes the Company to a certain degree of risk. Small failures in production lines requiring production stoppages for their removal may impact on sales results. During such periods there may be a drop in supply of products and an increase in costs connected with repairs and maintenance, causing a

temporary drop in the profitability of some products.

The Company has implemented a Failure Prevention Programme (internal order no. 39/2010) and an Internal Operational Rescue Plan (internal order no. 33/2010). These documents describe the hazards and govern the means of preventing and reacting to incidents and failures.

Information on external inspections

25 January 2011 - Provincial Environmental Protection Inspectorate, Tarnów Branch - incident at the caprolactam plant - no post-inspection orders issued.

1-28 February 2011 - State Fire Service in Tarnów - inspection of the observance of fire safety regulations, fulfilment of safety requirements, inspection of the transport of hazardous goods - post-inspection orders implemented.

2 February 2011 - District Environmental Health Inspectorate in Tarnów - inspection at the Commercial Plastics Centre concerning safe working conditions, observance of obligations under the act on chemical substances, observance of the act on prevention of drug addiction, assessment of the technical and sanitary condition of the premises - no post-inspection orders issued.

26 February 2011 - Customs Authority in Nowy Sącz - Logistics - customs clearance (inspection at the Company was performed on the basis of an application submitted by the Company for a permit to apply simplified procedures in logistics and change of customs clearance). The opinions issued by the Customs Authority also state that the customs clearance area at the Company guarantees full customs inspection and other activities provided for under customs law.

17 March 2011 - Provincial Environmental Protection Inspectorate in Krakow, Branch in Tarnów - railway tanker incident - no post-inspection orders issued.

23 March 2011 - District Environmental Health Inspectorate in Tarnów - inspection at the catalyser plant - no post-inspection orders issued.

5 April 2011 - District Environmental Health Inspectorate in Tarnów - WKS and SHA departments (scope: observance of anti-drug addiction regulations, categories 2 and 3) - no irregularities found.

5 April 2011 - District Environmental Health Inspectorate in Tarnów - WKS and SHA departments (scope: working conditions, observance of regulations concerning harmful substances, assessment of the technical and sanitary condition of the premises) - post-inspection orders implemented.

20 April 2011 - District Environmental Health Inspectorate in Tarnów - lactam department (scope: observance of regulations concerning category 2 precursors - potassium permanganate) - no irregularities found.

10 May 2011 - District Environmental Health Inspectorate in Tarnów - water treatment facility for the intake on the Dunajec river (scope: systematic assessment of sanitary and technical conditions at the water treatment plant) - no irregularities found.

10 June 2011 - District Environmental Health Inspectorate in Tarnów - chloride product department (subject to closure) - inspection concerning a biocidal product (calcium hypochlorite) - no irregularities found.

28-30 June 2011 - District Environmental Health Inspectorate in Tarnów - fertilisers department - inspection concerning 1) working conditions, 2) chemical substances and compounds, 3) the sanitary and technical condition of the premises - no irregularities found.

12 July 2011 - Provincial Environmental Protection Inspectorate (Tarnów Branch) - inspection concerning observance of regulations and administrative decisions relating to environmental protection in connection with ammonia emissions on 11 July 2011 as the result of a faulty safety valve in a compressor operating at the first cooling plant - no irregularities found.

15 July 2011 - District Environmental Health Inspectorate in Tarnów - fertiliser storage and freight forwarding department - inspection concerning 1/ working conditions, 2/ harmful substances and compounds, 3/ the technical and sanitary condition of the premises. Post-inspection orders implemented.

11 August 2011 - Provincial Environmental Protection Inspectorate - observance of regulations and administrative decisions connected with an incident at the fertiliser centre's nitric acid department - post-inspection orders implemented.

16 August 2011 - District Environmental Health Inspectorate in Tarnów - modified granulates department. Inspection concerning the sanitary and technical condition of the department - no post-inspection comments or remarks.

17-26 August 2011 - State Fire Service in Tarnów - collection of information needed to analyse a serious industrial incident and formulate recommendations for facility management - post-inspection orders implemented.

23-26 August 2011 - District Environmental Health Inspectorate in Tarnów - inspection relating to hazardous substances and compounds. Post-inspection orders implemented systematically.

21 September 2011 - District Environmental Health Inspectorate in Tarnów - fertiliser centre, fertiliser storage and freight forwarding department - verification that the orders under the District Environmental Health Inspectorate of 29 July 2011 were being implemented. Post-inspection orders implemented systematically.

3-31 October 2011 - Provincial Environmental Protection Inspectorate in Krakow - observance of environmental protection regulations (POM and compounding) - planned inspection - post-inspection orders implemented.

3-31 October 2011 - Provincial Environmental Protection Inspectorate in Krakow, Branch in Tarnów - inspection at the caprolactam and polyamide facility - planned inspection - post-inspection orders implemented.

5 October 2011 - District Environmental Health Inspectorate in Tarnów - investigation into an occupational medical condition - requested information provided to the inspector.

11 October 2011 - Provincial Environmental Protection Inspectorate in Krakow, Branch in Tarnów - environmental protection inspection at the PTFE and fluorine compounds facility. No post-inspection orders issued.

12-31 October 2011 - Provincial Environmental Protection Inspectorate in Krakow, Branch in Tarnów - inspection at the fertilisers plant - planned inspection - post-inspection orders issued (5 points) - deadline for implementation of point 1 - 28 September 2012, other points - 31 December 2011 - the Company provided timely notification to the inspectorate of the means of implementing post-inspection orders.

12 October 2011 - District Environmental Health Inspectorate in Tarnów - commissioning of an ash recovery installation. No comments or recommendations.

19 October 2011 - Provincial Environmental Protection Inspectorate in Krakow, Branch in Tarnów - EC II infrastructure - planned inspection - no post-inspection orders issued.

21 October 2011 - District Environmental Health Inspectorate - inspection of carcinogenic substances at the oxidation department. No post-inspection orders issued.

Conclusion:

The Supervisory Board is positive in its assessment of the Company's internal control system and management of its key risks.

Signatures of members of the Supervisory Board of Zakłady Azotowe w Tarnowie-Mościcach S.A.

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Monika Kacprzyk-Wojdyga
/Chairperson of the
Supervisory Board/

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Ewa Lis
/Deputy Chairperson
of the Supervisory Board/

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Jan Wais
/Secretary of the Supervisory
Board/

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Tomasz Klikowicz

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Artur Kucharski

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Marek Mroczkowski

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Jacek Obłękowski

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Zbigniew Paprocki