Assessment of CIECH S.A.'s standing in 2010
conducted by the Supervisory Board of CIECH S.A.,
including the internal control system
and the system for managing the Company's material risks

Acting pursuant to rule III.1.1) of the *Code of Best Practice for WSE Listed Companies,* which should be applied by companies listed at the Warsaw Stock Exchange, the Supervisory Board presents to the Ordinary General Meeting of CIECH S.A. a brief assessment of the Company's standing in 2010, including the internal control system and the system for managing the Company's material risks.

1. Assessment of the company's standing in 2010

In 2010, CIECH S.A. generated a net result in the amount of PLN (5,038 thousand), with the balance sheet total amounting to PLN 2.424.578 thousand, and cash decreased by PLN 12,805 thousand. The net profitability amounted to (0.2%). The net result for 2010 was negatively influenced by debt servicing costs and negative balance of FX differences. The fact of selling shares in Zakłady Azotowe Tarnów S.A. also had a negative impact on the result.

In 2010, CIECH S.A.’s sales revenues amounted to PLN 2,222,233 thousand and were lower than those in 2009 by 17%. The revenues were positively affected by an increase in prices in the organic segment. Moreover, the revenue earned by the silicates and glass sector in the Agro-Silicon Division was higher than in 2009, which is mainly owing to changing commission contract into a trade operator contract in case of sulphur sales.

In 2010, the gross profit on sales amounted to PLN 310,420 thousand, while in the same period last year it amounted to 335,115 thousand. The operating profit for 2010 amounted to PLN 133,595 thousand, compared to PLN 147.139 thousand in the comparative period. At the end of 2010, the EBIT margin amounted to 6% (7.7% a year earlier), while the EBITDA margin was 6.2% (8.1% a year earlier).

As at 31 December 2010, equity amounted to PLN 490,898 thousand, which means a decrease in equity by PLN 26,198 thousand compared to the end of 2009. The decrease in equity is the result of the generated net loss PLN (5,038) thousand, increased by the positive effect of including in the equity a valuation of some effective instruments for hedge accounting, amounting to PLN (30,719) thousand. By contrast, the decrease in equity was offset by a growth in revaluation capital by PLN 9,559 thousand.

As at 31 December 2011, CIECH S.A.’s total long-term and short-term liabilities amounted to PLN 1,933,680 thousand, which means an increase in liabilities by 32% compared to a year earlier. The increase was mainly due to a growth in liabilities on loans and borrowings by PLN 562,900 thousand compared to the previous year. At the same time, the loan structure changed: short-term loans and borrowings increased by PLN 689,160 thousand to PLN 1,167,117 thousand. Compared to the previous year, long-term loans and borrowings as at the end of 2010 decreased by PLN 126,260 thousand. The increase in short-term financial liabilities is a result of a consolidation of Group’s debt, which released refinancing of all loans previously granted to Ciech Group companies (excluding German companies). CIECH S.A. is the borrower.

The net debt (financial liabilities less cash) at the end of 2010 amounted to PLN 1,431,922 thousand and decreased over the course of the year by PLN 574,214 thousand. As of 31 December 2010, the financial leverage ratio (defined as net debt in relation to the sum of net debt and equity) was 74%. The debt rate (calculated as the relation of long-term and short-term liabilities to total assets) increased over 12 months of 2010 from 74% to 80%. This rate indicates a greater use of borrowing, the cost of which is lower than the cost of equity.

In 2010, the operating cash flow decreased by PLN 34,025 thousand and amounted to PLN 32,008 thousand. The main cause of decrease in cash in this area was an increase of interest paid by PLN 52,869 thousand up to PLN 85,406 thousand, which is a result of the consolidation of Ciech Group loans. In 2010, the Company incurred capital expenditures in connection with the purchase of shares of Zachem S.A. and Organika-Sarzyna S.A. and with the increase of share capital in a subsidiary Soda Deutschland Ciech. The main source of inflows were proceeds from borrowings granted, proceeds from the disposal of shares in ZA Tarnów, as well as proceeds from the disposal of part of property at Powązkowska Street. The surplus of investment expenditures over investment inflows in 2010 amounted to PLN 14,251 thousand.

Liquidity ratios as at the end of 2010 improved compared to the 2010 level, however, current liquidity ratios remain below 1 at the end of the year. This was caused by the financing structure (large share of short-term loans), nevertheless, this does not constitutes risk for the liquidity. Activities commenced in 2010 and completed in the first quarter of 2011, in the form of successfully conducted issue of D Series Shares and signing on 10 February 2011 a new long-term loan agreement contributed to the significant improvement of CIECH S.A.'s financial standing already in the first months of 2011. This was reflected by liquidity ratios which exceeded 1.

The CIECH Group continues the reorganisation programme of S.C. Uzinele Sodice Govora Ciech Chemical Group SA (USG). The programme's main focus was to improve the current cost efficiency of production as well as the production efficiency and stability in the long term by completing investment projects. In the opinion of the Management Board, the implementation of a restructuring programme adapted to the company's financial capabilities will bring positive results for USG in the coming years.

In particular, the Supervisory Board focused its attention in 2010 on the restructuring of the CIECH Capital Group's debt.

In April 2010, the process of refinancing the Group's debt was completed (without the German company). As a result, on 26 April 2010, a loan agreement was signed by CIECH S.A., as the borrower, its subsidiaries, as guarantors, and a bank consortium (Bank Polska., Kasa Opieki SA Bank Handlowy w Warszawie SA, BRE Bank SA, Powszechna Kasa Oszczędności Bank Polski SA, ING Bank Śląski SA. Bank Millennium SA and DNB Nord Polska). During negotiations between the banks and CIECH S.A., the short-term arrangements maintaining the provisions of old loan agreements concluded by the CIECH CK were in force. In addition, the restructuring of German companies was completed.

In 2010, the Management Board started negotiating a new loan agreement for refinancing the Ciech Group's financial debt under the Loan Agreement concluded on 26 April 2010, in which the financing parties were the commercial banks. On 8 February 2011, once the Supervisory Board has examined the terms of the new Loan Agreement, the Supervisory Board gave its approval and issued a positive opinion in connection with the Ciech Group's refinancing process. As a result, on 10 February 2011, a loan agreement was concluded for refinancing the Ciech Group's existing financial debt under the Loan Agreement concluded on 26 April 2010. On 15 February 2011, the European Bank for Reconstruction and Development (EBRD) entered that agreement.

The strategy that received a positive opinion of the Company's Supervisory Board defines the main growth directions and capital investment and divestment activities in relation to companies producing and trading in products from the so-called "basic portfolio", divided into commodity groups by divisions operating within CIECH S.A. The Supervisory Board would like to point out that actions taken in 2010 concentrated on integration within the Soda Division, which contributed to the strengthening of its structure and as a result enabled the Division to compete effectively with major market players. In addition, the performance of obligations taken in the previous years within the Organic Division continued – fulfilment of the conditions of privatisation agreements concerning companies forming the Division. Measures organising the Group's structure continued, mainly with regard to further divestment of companies not being part of the core business.

The Management Board of CIECH S.A., pursuant to the assumptions of the applied strategy, expects that in 2011 the results will be better than those produced in 2010, both in terms of revenues, EBITDA and net profit. However, the most important tasks for the CIECH Group in 2011 will be restructuring, including a further reduction of costs, and divestments.

The implementation of the Restructuring Plan will be of key importance for the shaping of Ciech Group's future results. The Plan assumes an implementation in years 2010-2015 of restructuring initiatives aimed at improving the financial situation of CIECH S.A. and increasing its capacity to repay the debt and to develop its activities.

The main prerequisites behind implementing divestment projects were:

- focus on soda and organic products,
- high sensitivity to economic fluctuations on agrochemical markets
- relatively small importance of the silicates and glass market activities,
- withdrawal from companies whose operations are not directly linked to CIECH S.A.'s activities.

2. Assessment of CIECH S.A.'s internal control system

Establishing an effective internal control system is the responsibility of the Company's Management Board.

In the opinion of the Supervisory Board, the existing control system of the CIECH Group is continuously improved, delivers an independent assessment of the defined standards and streamlines the whole Group's operation.

CIECH S.A.'s Internal Control System includes functional control by the management of individual organisational units of CIECH S.A. and other employees as part of their duties. Another element of the internal control system is institutional control exercised by the Control and Internal Audit Department, which provides independent advice and assessment of the effectiveness of CIECH S.A.'s management processes, helping the CIECH Chemical Group achieve its long-term goals and tasks.

The main objective of internal functional control is to ensure the correctness, reliability and punctuality of the performed operations, as well as to prevent and identify any irregularities and malpractice in the operation of the CIECH Group's organisational units. As part of functional control, a given organisational unit's risks or the risks related to a product are identified, and efforts are made to keep such risks at a level defined by CIECH S.A. In practice, functional control is exercised by every employee as part of their duties, based on the defined procedures.

The purpose of institutional control, i.e. internal audit, which is exercised by the Control and Internal Audit Department, is to audit the correctness, legality and reliability of operations performed by individual organisational units of CIECH S.A. and to assess compliance of actions taken with internal procedures. The internal audit also verifies the effectiveness of functional control and identifies any instances of mismanagement and malpractice in different areas.

The Control and Internal Audit Department fulfils its tasks according to an annual control plan approved by the President of the Management Board and conducts additional current audits of particular issues, as ordered by CIECH S.A.'s Management Board. To a great extent, the controlled areas involve major risks to the CIECH Group's business.

3. Assessment of CIECH S.A.'s risk management system

The Company's Management Board is responsible for introducing rules for risk management in the Company and for implementing the risk management process.

In the Supervisory Board's opinion, the Company's risk management system is effective and ensures an optimal level of material risks to which the Company is exposed as part of its business.

The key objective of the CIECH Group's risk management system is to ensure financial security and operational efficiency, allowing the CIECH Group to generate profits and continuously grow value for its shareholders. The principal objective of the system for managing the business risk is to lay a foundation for introducing risk management methods, procedures, requirements and reports required for keeping the CIECH Chemical Group's risk at an acceptable level.

The risk management process in the CIECH Chemical Group has been designed to facilitate the identification of potential threats and to ensure the achievement of the CIECH Chemical Group's strategic goals. The risk management system covers all materials risks to which the Company is exposed as part of its business operations. The consequences of business decisions are analysed for the materiality of the risk related to such decisions. Keeping the risk at an acceptable level helps define the respective risk management method. Risk management supports decision making by identifying areas with a potentially adverse effect on goodwill.

The Company actively manages operational and financial risk, aiming to reduce the fluctuation of cash flows and maximise the Company’s goodwill.

Pursuant to the provisions of the loan agreement of 26 April 2010, the Ciech Group undertook not to enter into any derivatives transaction, excluding hedging transactions agreed with banks. CIECH S.A. prematurely terminated all active option transactions and as at the end of 2010 was not party to any active option transactions. Owing to lack of available treasury limits in banks, at present, the Company may not enter into any derivatives transactions. Surplus of negative foreign exchange differences over positive differences in CIECH S.A. in 2010 amounted to approx. PLN 79 million.

CIECH S.A. is exposed to the following financial risks:

1. customers credit reliability risk,
2. liquidity risk,
3. market risk, including:

- currency risk,
- interest rate risk,
- raw material and product price risk.

While fulfilling its goals, the Company aims to avoid excessive market risk. This aim is realised by identifying, monitoring and hedging cash flow fluctuation risk and monitoring the size and costs of debt. When assessing risk, the Group takes into account the portfolio effect resulting from the variety of conducted business activities. Risk effects are materialised in the cash flow statement, balance sheet and the statement of results for CIECH S.A.

Financial risk management covers processes of identifying, measuring and establishing the manner of responding to that risk, including processes related to currency exchange rates and interest rate fluctuations. The Company monitors risk areas which are the most important for the Company’s activity.

Currency risk

Currency risk is an intrinsic component of running commercial activity denominated in foreign currencies. Due to the nature of its import and export operations, the Ciech Group is subject to FX exposure connected with considerable surplus of exports over imports. Sources of currency risk which threatened companies within the Group in 2010 included: purchase of raw materials, product sale, loans and borrowings raised and cash in foreign currencies. Unfavourable changes in currency exchange rates may worsen the Ciech Group's financial results.

Interest rate risk

The Group finances its activity mainly through interest bearing debt, including loans and bonds, corresponding expenditure borne by the Group is dependent on the reference rate and margin (in case of the loan agreement of 26 April 2010 and the agreement regarding the loan granted to Soda Deutschland by Commerzbank AG, margin dependent on financial result). Therefore, the Group is exposed to risk of change of financial costs due to changing interest on existing debt. This may result in increased financial costs and, consequently, deteriorate the Ciech Group's financial result. IRS instrument hedges interest payments based on a variable interest rate due on account of the loan agreement between Soda Deutschland and Commerzbank AG.

Raw material price risk

A significant portion of the Ciech Group’s activity is the import and export of chemical raw materials. The raw materials markets are characterised by a cyclical nature connected with fluctuations of the global economy. The growing prices of raw materials cause a decrease in margins of sales intermediaries and a decrease in demand from customers. On the other hand, falling prices are usually a symptom of decreasing demand and the beginning of an economic downturn. On the domestic market, raw materials are subject to similar tendencies. The maintenance of a stable pace of economic growth and stable prices of chemical raw materials will have a positive impact on the commercial activity of the Ciech Group. Considerable fluctuations of demand and prices caused either by fast economic growth or economic stagnation will have negative influence on the activity related to trading in chemical raw materials by the Ciech Group. In most segments of the Ciech Group’s activity, goods are not subject to significant price fluctuations. Nevertheless, the organic segment is exposed to price risk. This correlated with the condition of global economy, current demand and supply situation of final customers, the level of prices of basic raw materials and energy. The Ciech Group reduces price risk through regulating price policy concluding agreements with suppliers, hedging and insuring supplies and containing an appropriate price formula.

Credit risk

Credit risk means a threat that the borrower will not fulfil obligations stipulated in the agreement and expose the lender to financial loss. From the Ciech Group's point of view, credit risk is linked to:

- trade receivables from customers,
- own borrowings granted,
- granted guarantees and sureties,
- cash and bank deposits.

The Ciech Group is exposed to the credit risk connected with the credit rating of customers being parties to product and goods sales transactions. This risk is reduced through internal procedures for determining credit limits for customers and through management of trade receivables (the Group uses securities in form of letters of credit, bank guarantees, mortgages, receivables insurance and non-recourse factoring). Customers’ credit rating is assessed and appropriate collaterals are obtained from the borrowers, allowing for a reduction of potential losses in the case of failure to repay the debt. The credit risk assessment for customers is performed prior to concluding an agreement and cyclically at subsequent supplies of goods, in accordance with the binding procedures. The risk of the receivables portfolio is assessed weekly. On certain markets where more risky terms of payment are applied, the Group companies use services provided by companies specialising in insuring receivables. Credit risk connected with cash in bank and bank deposits is low as the Ciech Group enters into transaction with high-rating banks which have a stable market position.

Liquidity risk

The Ciech Group is exposed to liquidity risk due to a high portion of short-term borrowing (overdraft facilities and working capital loans), limited opportunities to obtain new funding given the high level of existing debt as well as the risk of failure to maintain existing long-term funding as a result of violation of obligations laid down in the loan agreements. The following measures are applied to reduce liquidity risk:

- regular monitoring of the Ciech Group companies’ liquidity,
- monitoring and optimising working capital,
- adjusting the level and schedule of capital expenditures,
- intra-group borrowings and sureties for the liabilities of the Group’s companies,
- current monitoring of the fulfilment of loan agreements provisions, including maintenance of current and forecasted financial ratios stipulated in loan agreements,
- seeking other sources of funding - issuance of shares.

To reduce the risk related to borrowing, in 2010, the process aimed at refinancing and consolidating debt continued and in April 2010, consortium loan agreement was concluded with the banks financing the Ciech Group. Moreover, in 2010, the Management Board started negotiating a new loan agreement for refinancing the Ciech Group's financial debt under the Loan Agreement concluded on 26 April 2010.

In consideration of the above, the Supervisory Board believes that the internal control system and the risk management system in the CIECH Group are important elements of the Group's management system, allowing it to operate in a more safe and stable manner, and to achieve its long-term strategic goals. The presented standards are applied in all companies of the Group.

To sum up, CIECH S.A.'s Supervisory Board gives a positive assessment of the Company's and the CIECH Capital Group's growth perspectives.

CHAIRPERSON OF THE SUPERVISORY BOARD

Ewa Sibrecht - Ośka