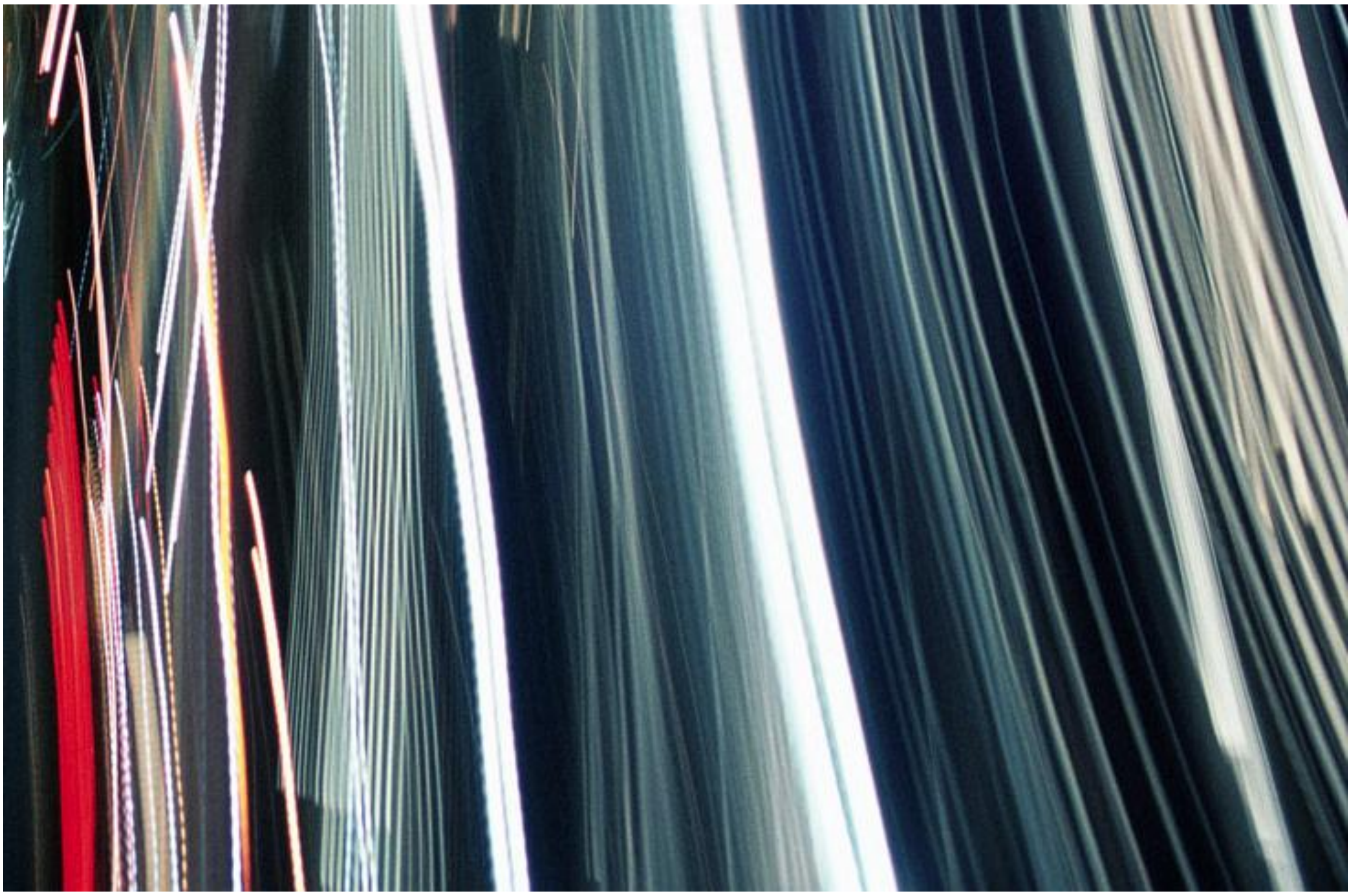


Management Board's report on activities of the Capital Group of PGE Polska Grupa Energetyczna S.A. for the 6-month period

ended June 30, 2014

Contents

1 General information about the PGE Capital Group

Capital Group of PGE Polska Grupa Energetyczna S.A. („PGE Capital Group", the „Group", „PGE Group") is the largest vertically integrated company in energy sector in Poland with respect to revenues, installed capacity and electricity produced.

The parent company of PGE Capital Group is PGE Polska Grupa Energetyczna S.A. ("PGE S.A.", the "Company").

1.1 Description of organisation and activity of the Capital Group

PGE Group currently organizes its activities in five main business segments:

Mining and Conventional Generation („Conventional Generation")

Includes extraction of lignite and generation of electricity and heat from conventional sources and distribution of heat.

Distribution of electricity

Includes supply of electricity to final off-takers through the grid and HV, MV and LV power infrastructure.

Renewable Energy

Includes electricity generation from renewable sources and in pumped storage power plants.

Retail sales of electricity

Includes sale and supply of electricity to final off-takers.

Wholesale Trading

Includes trading of electricity, related products and fuels.

The Group also comprises of company, whose main activities are preparation and execution of project of construction of nuclear power plant within Polish nuclear power plant program and a company which organizes financing for the Group.

In addition, the Group comprises of companies providing IT and telecommunication services and supporting services to companies from the energy and mining sectors like:

- construction, renovation and modernization works and investments in electricity equipment,
- comprehensive diagnostic tests and measurements of electro-energy machines and equipment,
- management of by-products of coal combustion, development and implementation of above technologies usage
- rehabilitation of degraded areas.

1.2 Factors important for the development of the PGE Capital Group

In the opinion of the Company Management Board, the following factors will influence the Company's and the Group's results and performance within at least next quarter:

MARKET ENVIRONMENT

- Demand:
  - demand for electricity and heat;
  - seasonality and weather conditions;
- Electricity market:
  - Wholesale electricity prices;
  - Prices and tariffs on electricity and heat retail sale markets;
  - Tariffs for transmission and distribution of heat and tariffs for electricity distribution;
- Related markets:
  - prices of property rights (certificates of origin of electricity);
  - availability and prices of fuels used in generation of electricity and heat, in particular prices of hard coal, fuel gas and biomass, as well as costs of fuels transportation to the generating units;
  - prices of CO2 emission rights;
- Power infrastructure:
  - availability of cross-border transmission capacities;
  - growth of generating capacity in national electro-energy system, including renewable energy and cogeneration;
  - development and modernisation of energy grid;
- Macroeconomic environment:
  - GDP dynamics, particularly in industrial production;
  - interest rates and exchange rates, values of which affect evaluation of assets and liabilities shown by the Group;
- Implementation of efficiency and investment programs in PGE Group.

REGULATORY ENVIRONMENT

- Domestic:
  - Implementation and possible changes to the Poland's energy policy;
  - Changes in scope of services like:
    - projected modification of current Operational Reserve mechanism;
    - implementation of cold reserve mechanism;
    - implementation of further packages for demand reduction services;
  - amendments to the Energy Law, particularly in scope of optimisation of support scheme for renewable energy sources and for co-generation and amendments to other acts;
  - results of explanatory proceedings before the ERO President in case of issue of certificates of origin of energy produced from biomass for some of the branches of PGE GiEK S.A.;
  - decisions of the ERO President related to realisation of the Act on coverage of stranded costs resulting at generators in relation to accelerated termination of long-term contracts ("LTC Act") and court's rulings on the disputes between the ERO President and generators from the PGE Group entitled to receive compensations under LTC Act with regard to the annual adjustments of the stranded costs for 2009 and 2010 and annual adjustments of costs generated in gas-fuelled units for 2009-2012;

  - Issue of implementation of the ETS directive into the domestic law – inter alia CO2 derogations. Currently process of obtaining free allowances in exchange for pursuing investments from the National Investment Plan, does not have a clear legal basis.
  - Issue of implementation of the Energy Efficiency Directive into the domestic law;
  - possible different decision in law, tax and other contingent liabilities disputes, from which most relevant were presented in Note 21 to the consolidated financial statements;

- International:

  - regulations of 2030 climate and energy package – including European Commission proposals from January 2014 with regard to 40% CO2 reduction targets, 27% RES share target, proposal of Stabilisation Capacity Mechanism aimed at CO2 prices increase;
  - revision of BAT (Best Available Techniques) – uncertainty with regard to future norms of SO2, NOx dust and new pollutions (including mercury) emissions from 2020;
  - draft directive with regard to national limits of emissions of pollution to the atmosphere (so called NEC Directive) and its impact on the power sector.
  - Works on connection of Poland to market coupling mechanisms (connection of markets).

1.3 Strategy of the PGE Capital Group for years 2014 - 2020

In response to the recent developments in the electricity market and in order to better utilise strengths of the PGE Group, a new Strategy of the PGE Capital Group for years 2014-2020 was adopted. Adoption of the strategy was preceded by development of a broad range of possible market scenarios. During these works, an investment portfolio had been reviewed in order to yield the most robust returns to the stakeholders.

The strategy has acknowledged significant changes in the PGE Group's market environment and is based on understanding of key market trends and on key competences and competitive advantages of PGE Group:

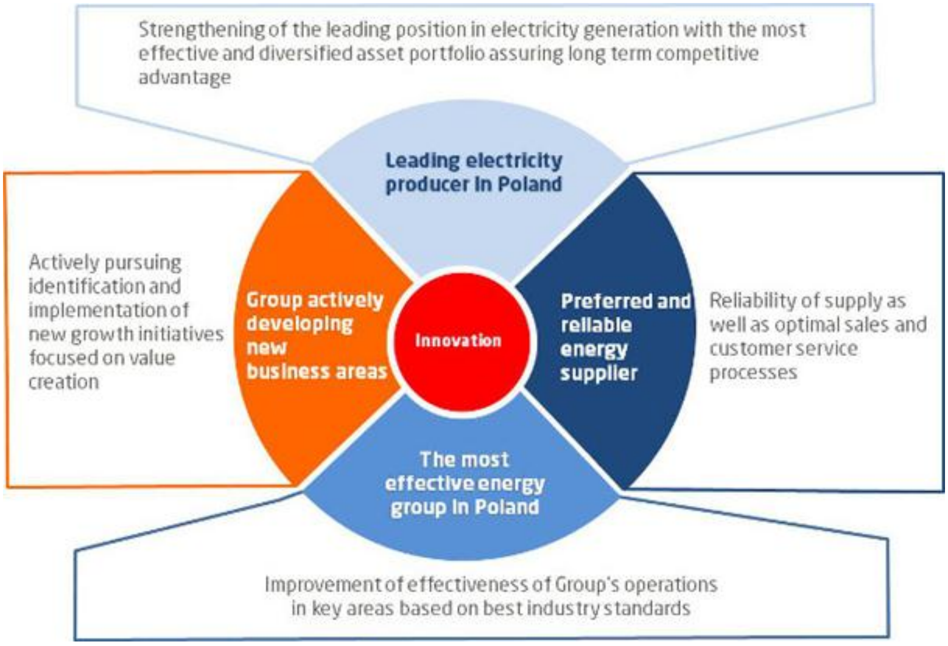
- PGE is the largest vertically integrated power utility in Poland with regard to energy production and installed capacity;
- PGE is leading in the cost efficient, base-load generation technologies in Poland and has the youngest generation asset base.

Financial aspirations of the PGE Group resulting from the strategy are as follows:

- Sustaining EBITDA level in the range of PLN 8-9 billion in 2015-2020;
- Maintaining the current policy of dividend pay-outs (40-50% of consolidated annual net profit);
- PLN 1.5 billion of sustained influence on EBIT (after 2016) as the effect of planned activities relating to improvement of effectiveness;
- Maintaining the long term ratings;
- Approx. PLN 50 billion of CAPEX in 2014-2020;
- At least 1.5 % of annual net profit as of 2015 intended for R&D activities.

Key strategic objective is to maximize long-term PGE shareholder value. This will be achieved thanks to the pursuing of the adopted strategic aspirations:

- Leading electricity producer in Poland - strengthening of the leading position in electricity generation with the most effective and diversified asset portfolio assuring long term competitive advantage;
- Preferred and reliable energy supplier - Reliability of supply as well as optimal sales and customer service process;
- The most effective energy group in Poland - Improvement of effectiveness of Group's operations in key areas based on best industry standards;
- Group actively developing new business areas - actively pursuing identification and implementation of new growth initiatives oriented on building the value of the Group;
- Innovation - continuous analysing of the market environment, identifying and using innovative solutions to create Group's value and achieve strategic goals.



Leading electricity producer in Poland

In order to strengthen the leading position in electricity generation in Poland, PGE Group intends to spend approx. PLN 34 billion in 2014-2020 for replacement, modernisation and construction of new generation assets. This value includes modernization and replacement expenditures with regard to existing assets in amount of approx. PLN 16.3 billion and capital expenditures for construction of new capacities in amount of approx. PLN 15.2 billion. PGE Group also plans to spend PLN 1.7 billion for construction of new RES capacities and PLN 0.7 billion for preparation of commencement of nuclear program until 2016.

Key actions in this field include:

- Modernisation and construction of highly efficient conventional units based on domestic fuel resources. By 2019 PGE Group will commission new highly efficient hard coal units in Opole and lignite-fired unit Turów with a total capacity of approx. 2,290 MW.
- Development of cogeneration in connection with the long-term support scheme. Currently, PGE Group has 187 MWe of cogeneration capacities under construction. There are also ca. 1,100 MWe in the pipeline, however their further development is conditional upon long-term support system implementation.
- Diversification of generation portfolio through implementation of zero-carbon investments (nuclear, RES) in business models ensuring their economic predictability. PGE Group intends to continue developing project of construction of first Polish nuclear power plant and developing new capacities in onshore wind power plants. Both initiatives will be realized only in business models assuring their economic predictability. Construction of the first nuclear power plant is the key investment lowering the carbon intensity of generation portfolio of PGE Group, however development of the long-term support system is necessary for further project development with account taken to project financing and interest of the off-takers. Making the investment decision and application for the "fundamental decision" will be possible in 2017 and will be based on the form of support system and results of the integrated proceeding. In years 2014- 2016 PGE Group will have additional 234 MW of onshore wind farms operational. Construction or acquisition of other RES projects will be dependent on the future support system and therefore their potential for creating the PGE Group's value.

- Maintaining a position of leading operator of the regulatory assets. PGE expands and modernises regulatory assets to fully utilise their potential of cooperation with Polskie Sieci Elektroenergetyczne S.A. ("PSE S.A."). Further investments are planned until 2020 to assure highest operating standards and uninterrupted availability of assets. The ultimate form of the investment programme will depend on the form as well as terms and conditions of agreements for provision of system services.
- Provision of resource base for conventional generation as an strategic option for future growth depending on the direction of EU climate policy. Złoczew and Gubin projects are currently at the stage of obtaining the required administrative permits. In both cases the licenses for extraction are expected to be obtained after 2016. Exploitation of lignite deposits will be considered within the development strategy of the whole generation portfolio.

Preferred and reliable energy supplier

PGE Group plans to reorganise the sales process based on effective trading strategy. In every customer segment the PGE Group will focus on understanding the needs of the customers and improvement of customer service quality. In particular it includes:

- In corporate customers segment, PGE Group intends to focus on effective margin management at the Group level and on securing optimal contracts of generating units if PGE Capital Group;
- In SME segment, PGE Group intends to focus on retention of historical customers while maintaining the margin levels, acquisition of new customers through improved customer service and expansion of product offering;
- In households segment, PGE Group intends to acquire new customers, expand product offering, lower the service and sales costs and build modern IT tools supporting sale processes.

In the distribution segment, assuring reliability of supply through operational and investment efficiency will be the main goal. PGE Group is committed to improve grid reliability - we intend to achieve a goal of 50% SAIDI[1] reduction by 2020 mainly by refocusing the investment outlays on projects to the largest extent limiting the level of undelivered energy and by increasing operational performance. Total capital expenditures in the distribution segment in years 2014-2020 will amount to approx. PLN 12.3 billion.

The most effective energy group in Poland

PGE Group ambition is to be the most efficient power utility in Poland. It includes improvement of operational efficiency, dialogue with the stakeholders concerning the regulatory environment and implementation of best corporate governance practices. Key actions in this field include:

- Organisation restructuring allowing for costs reduction and revenues increase. Effects of continuation of activities relating to efficiency improvement will have a sustainable influence on EBIT of ca. PLN 1.5 billion after 2016. The target will be achieved through implementation of operational effectiveness improvement programmes in conventional generation and distribution, reduction of grid losses and interruptions in supply in distribution and rationalization of fixed costs in renewable energy.
- Active dialogue with the stakeholders concerning the regulatory environment. In particular PGE Group will strive to guarantee economic predictability of investment projects and to create agreements with the key stakeholders who shape the regulatory environment in Poland and in the European Union.
- Implementation of best corporate governance practices regarding human resources management, business decisions support and efficiency management as well as optimization and standardisation of supporting processes.

Group actively developing new business areas

PGE will actively identify and develop new products and business areas. Initially identified growth directions are dual fuel offering (purchase of electricity and gas from one supplier), modern electricity infrastructure (e-mobility infrastructure, distributed generation and storage, electrification of home heating).

[1] SAIDI - System Average Interruption Duration Index – minutes lost; unplanned electricity outages (excluding catastrophic events)

Innovation

Apart from initially identified growth directions, PGE Group will continuously analyse market environment, identify and use innovative solutions to achieve its strategic goals. PGE Group aspiration is to spend at least 1.5 % of annual net profit as of 2015 on R&D activities with maximization of external financing.

2 Activity of the PGE Capital Group

2.1 Factors and events affecting results

2.1.1 Macroeconomic situation

The PGE Group runs its activities mainly on the Polish market. Therefore it is dependent mainly on macroeconomic trends existing in Poland. At the same time, in connection with the growing integration, the domestic economy is increasingly dependent on the economic situation in European Union as well as in the international markets.

As a rule, there is a positive correlation between the growth of electricity demand and economic growth. Thus, the macroeconomic situation of Poland affects the financial results achieved by the PGE Group.

During the first half of 2014, macroeconomic conditions were stronger than in the same period the previous year. Sold industrial production was up 4.3% y/y. Retail sales during the first half of 2014 advanced at an average rate of 4.7% from the same period in 2013.

Industrial production showed relatively dynamic growth in the first quarter, followed by a noticeable slowdown in the second. Production growth was varied across industry branches. In the first half of 2014, the manufacturing sector advanced 6.0% y/y, while mining and quarrying decreased by 6.5% and production and supply of electricity, gas and heat fell by 5.7%.

Business tendency surveys for manufacturing and retail, as measured by Poland's Central Statistical Office ("GUS"), went by up 7.0 and 1.0 points respectively in June 2014, compared with -4.0 and -9.0 points in June 2013. In manufacturing, of particular note were the prevalent positive views regarding current order books, despite slower growth in domestic and a decrease in export orders.

According to GUS estimates Poland's GDP growth at constant prices accelerated to 3.4% in the first quarter of 2014, i.e. above the 3.1-3.2% range expected by the Ministry of Economy and significantly higher than the 0.4% posted in first quarter of 2013. GDP growth in the second quarter of 2014 reached 3.2% y/y while economists surveyed by the Polish Press Agency ("PAP") expected to see 3.3% in GDP growth. National Bank of Poland forecasts in its report on inflation of July 2014 that in this and next year Polish economy will grow at a rate of 3.6% and GDP will grow by 3.5% in year 2016.

Despite a substantial improvement in the macro situation, gross electricity consumption in the first half of 2014 declined by 0.32% from the same period in 2013. This is a result of mild weather conditions during the winter period, especially the markedly higher average daily temperatures. Also lower, by 4.7%, was domestic electricity production, while electricity imports grew more than twofold, bringing a change in the cross-border balance from a 2.34 TWh net export position in the first half of 2013 to a net import of 1.23 TWh in the first half of this year.

The prices of manufacturing production sold have been declining since October 2013. In the first half of 2014, manufacturing prices decreased by 1.2% y/y. The biggest drop in the period from January to June (-7.6% y/y), just as in the previous five months, was noted in the mining and quarrying sector. A 0.9% increase in prices was recorded in the segment covering production and supply of electricity, gas and heat.

CPI growth in the first half of 2014 reached 0.4% and was much slower than in 2013 and a far cry from the inflation target set by the National Bank of Poland ("NBP"). The lower inflation is aided by decreases in average prices in education (-6.2%), communications (-2.2%), transport (-1.5%), clothing and footwear (-4.6%) and energy sources (-0.2%).

An extended period of inflation below the NBP's target has an impact on the Monetary Policy Council's interest rate decisions. This, coupled with lower-than-expected macroeconomic readings, puts pressure on the MPC to further ease monetary policy. The MPC has been maintaining the reference rate at a historically low level of 2.5% since July 2013.

Table: Key economic indicators for Poland.

Key economic indicators	H1 2014	H1 2013
CPI *(% change y-o-y)*[1]	0.40	0.90
PPI *(% change y-o-y)*[1]	-1.20	-1.40
Sold industrial production *(% change y-o-y)*[1]	4.30	-0.40
Sold production – energy *(% change y-o-y)*[2]	-5.70	-0.40
Gross domestic electricity consumption *(% change y-o-y)*[3]	-0.32	-0.36
Gross domestic electricity consumption *(TWh)*[4]	78.49	78.74
Manufacturing PMI *(points, half-year average)*[4]	52.70	48.28

Source: [1] Central Statistical Office of Poland, [2] Central Statistical Office of Poland - electricity, gas, steam and heated water production and distribution sector

[3] PSE S.A., [4] HSBC, Markit Economics

Diagram: GDP change vs. change in gross electricity consumption.

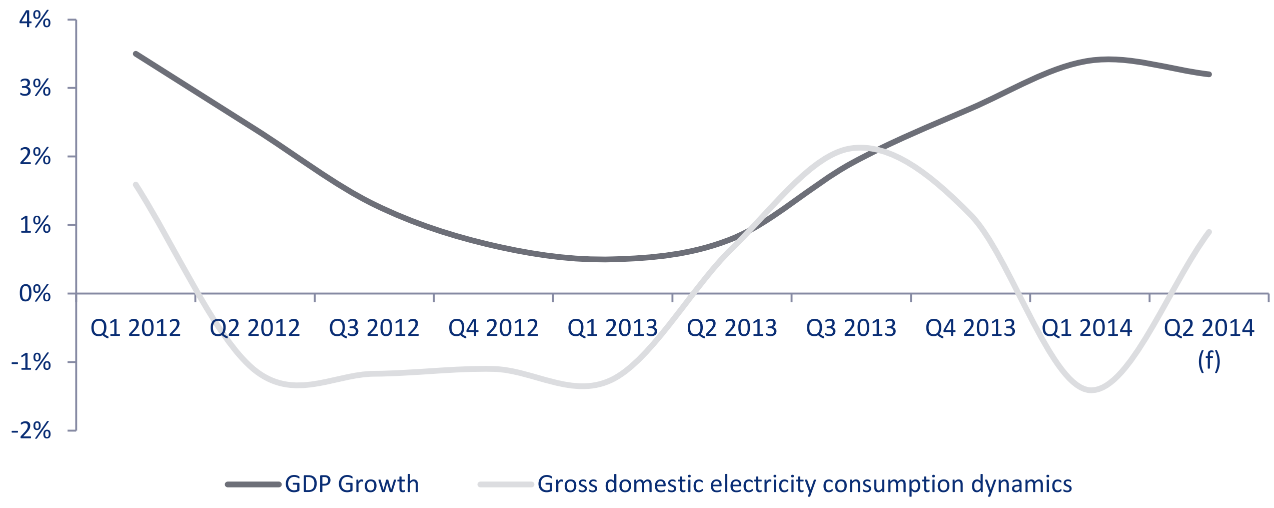


Diagram: Sold industrial production and retail sales dynamics in Poland (y-o-y)

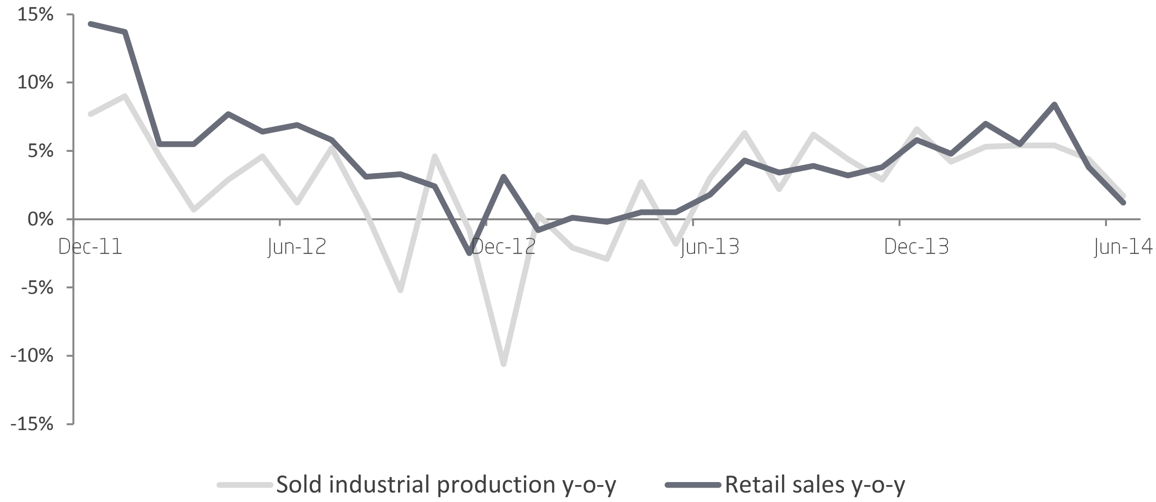
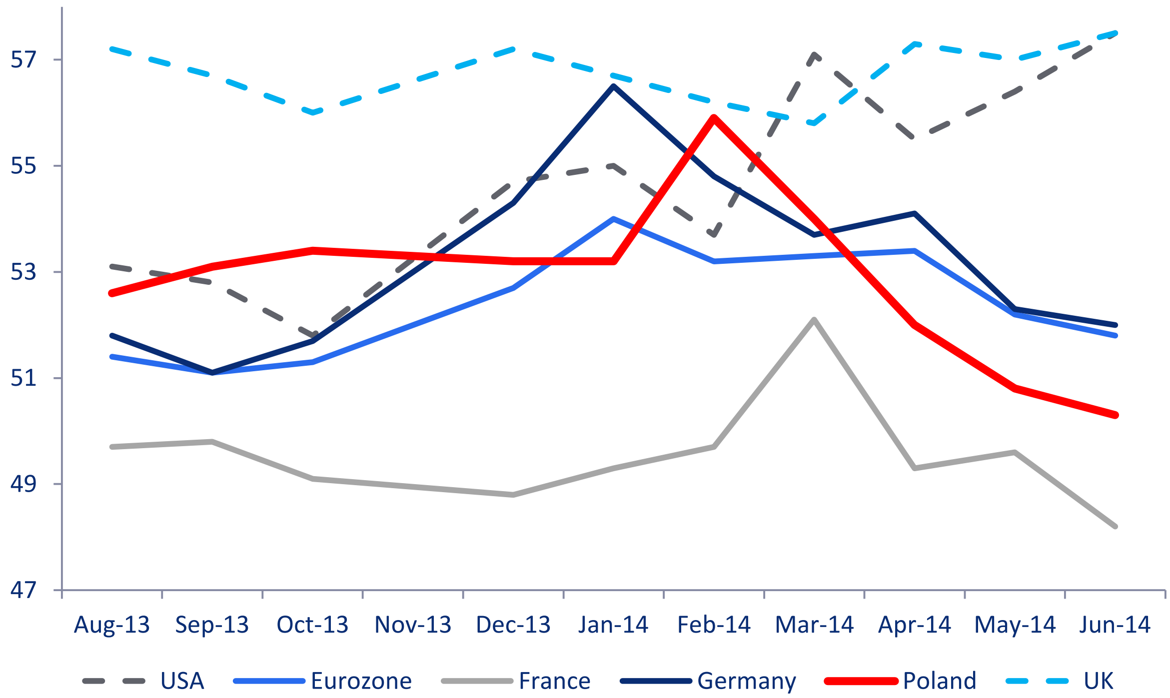


Diagram: Manufacturing PMI in particular countries (in points)

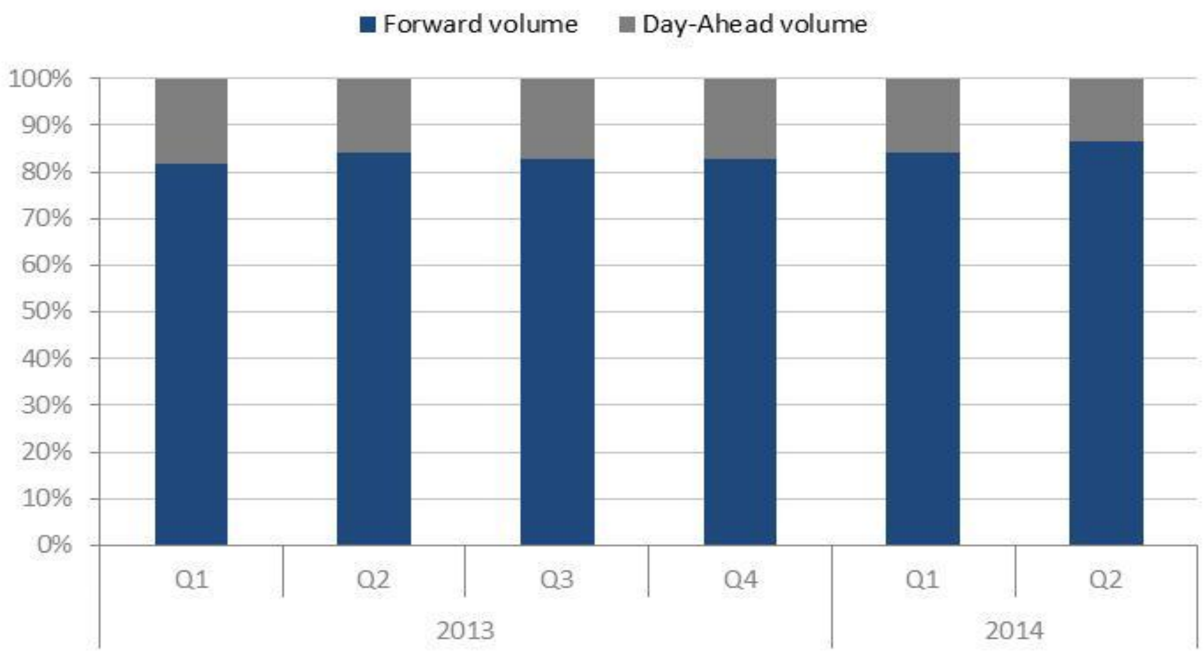


2.1.2 Electricity prices

DOMESTIC MARKET – TRADING VOLUMES

In the first half of 2014, liquidity at the day ahead market, which is managed by the power exchange TGE S.A., increased by 15% on the same period last year. This trend continued throughout both the first and second quarter. Overall trading volume at the Day Ahead Market was 12.16 TWh. The futures market showed similar behaviour, with total trading volume increasing in the first half of 2014 by 34% to 82.60 TWh. This means that trading volumes at TGE have now exceeded domestic electricity consumption, which during the period from January to June 2014 was 78.49 TWh (according to data from PSE S.A.). An excess of trading volumes over domestic use indicates growth in speculative trading, which has a positive impact on market liquidity.

Chart: Quarterly trading volumes on the day ahead market (RDN) and futures market (RTT) in 2013-2014.

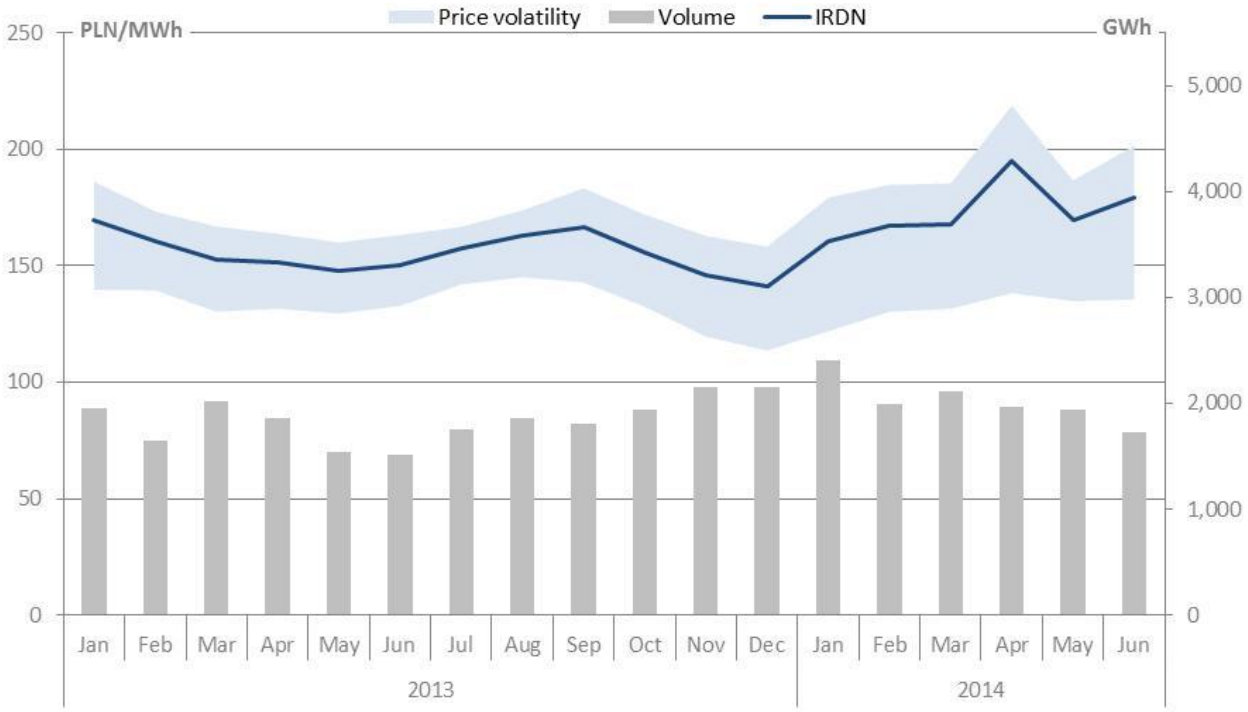


DOMESTIC MARKET – PRICES

Day ahead market

In the first half of 2014, prices on TGE's day ahead market were in an uptrend, while in the first half of 2013 they continued multi-month declines (which began at the end of April and start of May 2012), bottoming out in the second quarter of 2013. The average price on the day ahead market (the IRDN index) in the first half of 2014 was PLN 174.11/MWh, compared with PLN 156.70/MWh in the same period of 2013, denoting an increase of more than 11%. In the first quarter of both 2014 and 2013, prices were at a similar level (up 3% y/y), however 2014's second quarter was significantly higher (+21% y/y). In April 2014, the IRDN index went up dynamically, while in the second quarter of 2013 it stayed at one of the lowest levels in its history. The first half of 2014 saw not only growth in peak prices (the sIRDN index went up 14% y/y) but also a decrease in off-peak pricing (the offIRDN index was down by 1% y/y). This directly translated into more pronounced price swings – the sIRDN index constitutes 146% of the offIRDN index, while a year ago it was 126%.

Chart: Monthly prices and price volatility at the day ahead market in 2013-2014 (TGE)*.



** arithmetic average price from all power exchange transactions concluded at the session (IRDN) and prices spread (sIRDN, offIRDN)*

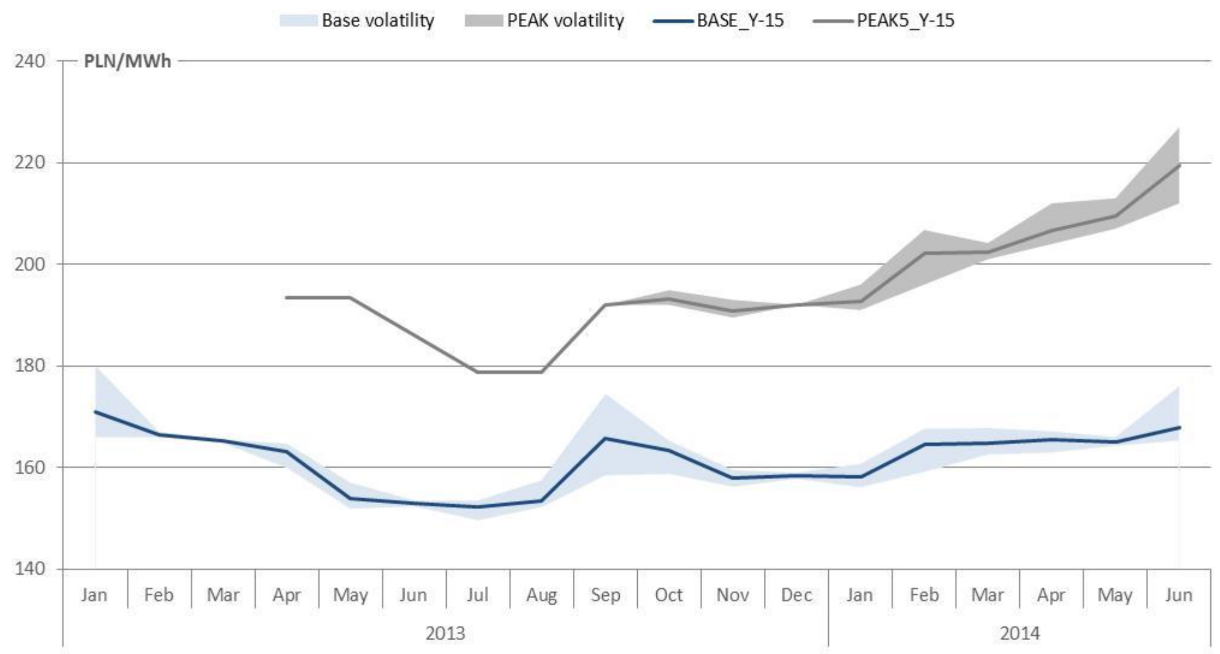
Prices on the day ahead market in Poland in the first half of 2014 were mainly affected by a change in the way in which payments for active generating Schedular Units (JGwa) are made under the operational reserve mechanism, which is a system control service.

<u>Futures market</u>

In the first half of 2014, the futures market saw price increases in both BASE and PEAK contracts. The growth resulted from an update of the System Balancing and System Constraint Management part of the Transmission Grid Operation and Maintenance Manual (IRiESP), which updated the means in which the operational capacity reserve works. In addition, positive economic newsflow from Poland, particularly as regards higher GDP growth and industrial production, supported the continuing uptrend on the futures market.

The BASE_Y_2015 annual contract in the second quarter of 2014 reached an average price of PLN 166.31/MWh, denoting more than 2% increase on the previous quarter and more than 5% on the second quarter of 2013. The PEAK5_Y-15 product averaged PLN 213.65/MWh in the second quarter of 2014, meaning that its price increased by 6% from the beginning of 2014 and by 11% from the second quarter of 2013.

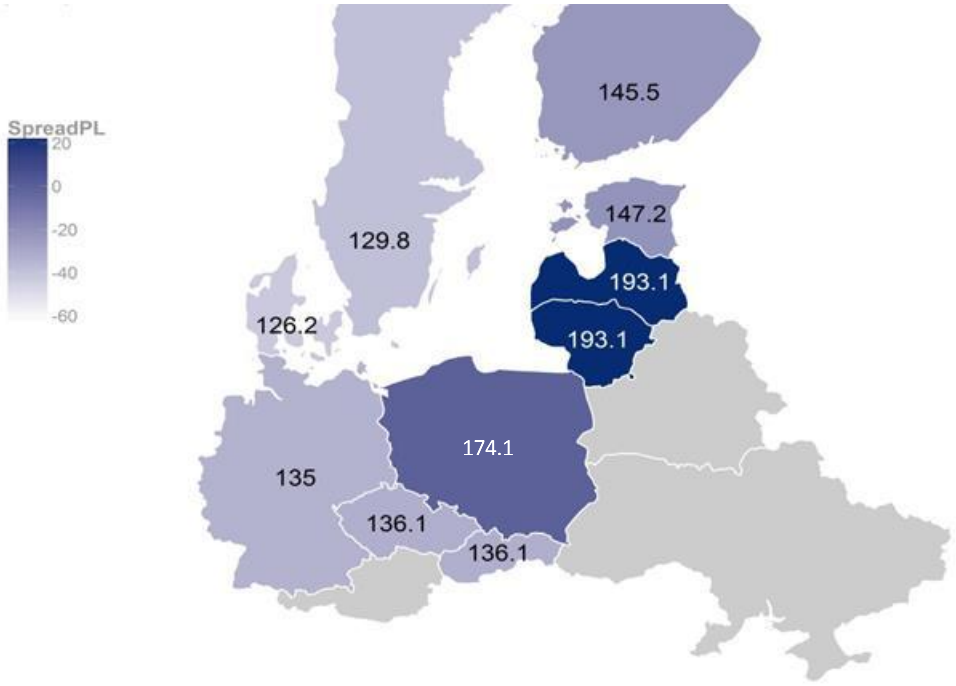
Chart: Average prices and price volatility on the futures market in 2013-2014 (TGE).



INTERNATIONAL MARKETS

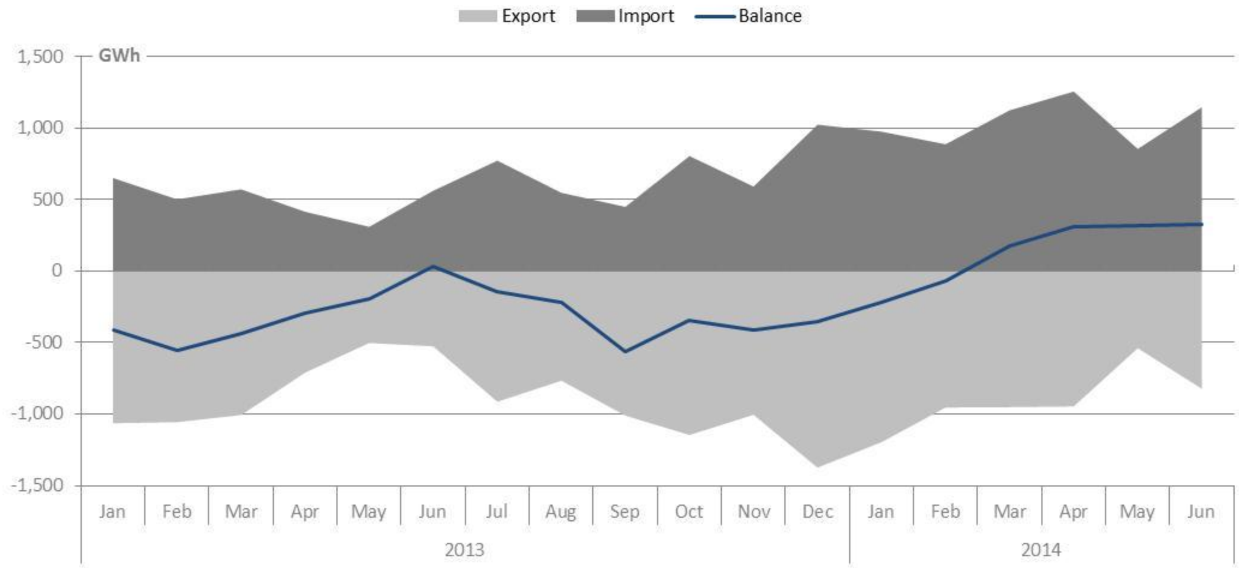
The first half of 2014 saw a disruption in the trend seen in recent years, whereby prices in the Polish market were below those in Sweden, Germany, Czech Republic and Slovakia. In the first half of 2014, the average price on the German market fell by nearly 14% in comparison with the first half of 2013, and the Nordics declined by almost as much. In Poland, on the other hand, average prices on the day ahead market in the first two quarters of 2014 remained above those in the same period of 2013. An increase in average prices, coupled with substantial declines in foreign markets, led to a situation where Poland became the most expensive out of the markets mentioned above. This resulted in a change to a negative cross-border exchange balance.

Chart: Comparison of average prices on Polish market and on European markets in the first half of 2014.



In the first half of 2014, physical capacity flows were subject to a major change. As a result of lower electricity prices in the neighbouring markets, Poland became a net importer of electricity. Imports increased substantially (+107%), with only modest growth in exports (+11%). The situation at specific cross-border profiles did not change significantly – the largest importers remain Germany and Sweden, while exports mostly go to the Czech Republic and Slovakia.

Chart: Monthly imports, exports and cross-border exchange balance in 2013-2014.

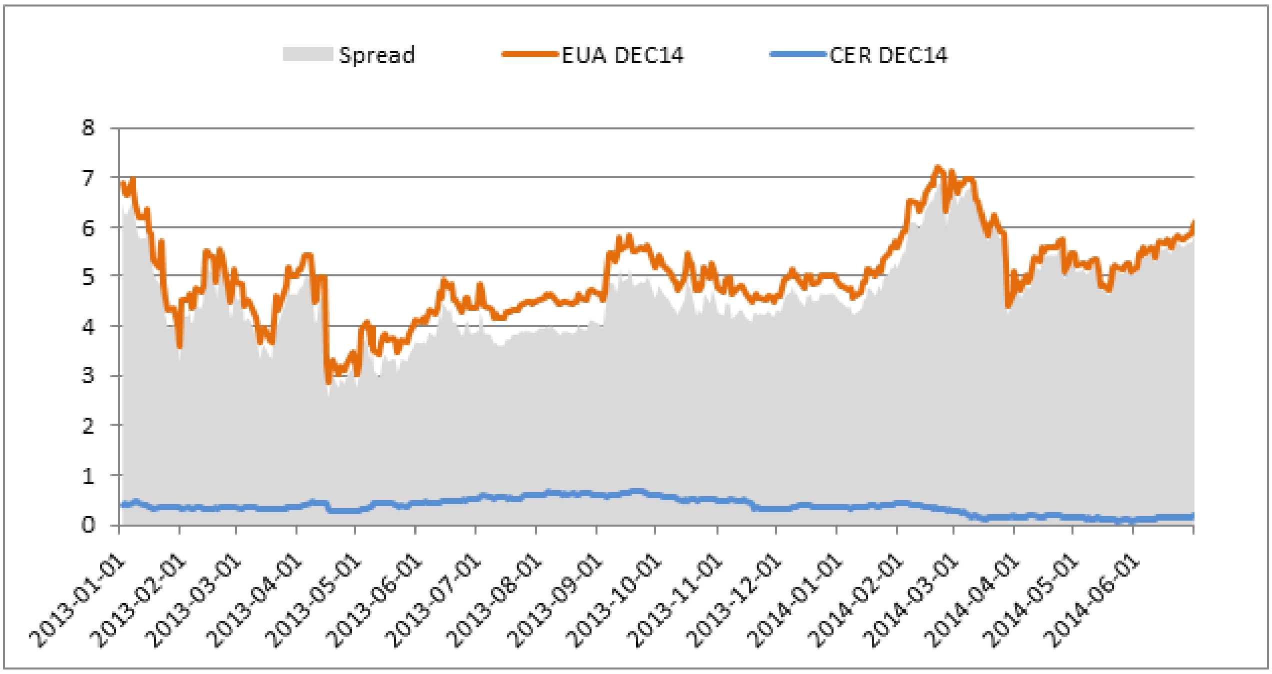


2.1.3 Prices of CO_2 emission rights

Three types of emission rights are available on the market – EUA (European Union Allowances), CER (Certified Emission Reductions) and ERU (Emission Reduction Units) allowing for the emission of one tonne of CO_2. CER-type and ERU-type rights may be redeemed by business operators only to a limited extent, in settlement period 2013-2020 up to 1% of the allocations granted under the National Allocation Plan for years 2008-2012.

The number of CO_2 allowances initially granted to the installations Poland within the National Allocation Plan of CO_2 Allowances is lower than demanded by the Polish industry sector. Business operators are obliged to purchase the difference between the demand resulting from CO_2 emission levels and allowances granted for free under the framework of the so-called European Emissions Trading Scheme ("EU ETS"). The purchasing cost of lacking allowances is therefore a significant factor determining the financial results achieved by PGE.

Chart: Prices of CO_2 emission rights in 2013 and in the first half of 2014, for contract with EUA delivery in December 2014.



The market was in an uptrend from the beginning of 2014 to the end of the first 10-day period of March, followed by a correction in the last two weeks of March which resulted in a decrease in allowance prices. These declines brought prices to the levels from the beginning of 2014. In the second quarter of 2014 market has been in an upward trend.

In the first half of 2014 the spot contracts for allowances were priced in the following ranges:

- EUA 4.35-7.12 EUR/t;
- CER 0.19-0.42 EUR/t;
- ERU 0.07-0.24 EUR/t.

Oversupply of emission rights on the market was the main factor affecting the emission rights prices in the first half of 2014.

On February 6, 2014 the European Parliament approved the regulations necessary for acceleration of backloading implementation. This information contributed to the short-lived increase of allowance prices to the level exceeding 7 EUR/t.

On February 24, 2014 the European Council voted for the backloading.

On March 5, 2014, Polish auctions for allowances sold at European auctions were suspended until 2015, what means reduction of the available allowances in auctions in the whole EU ETS system.

2.1.4 Tariffs

PGE Group companies earn part of their income based on tariffs approved by the President of the Energy Regulatory Office:

I. tariffs for the sale of electricity to households (G tariff group);

II. tariffs of the distribution companies (distribution system operators, DSO);

III. tariffs for heat.

SALES OF ELECTRICITY

In the 6-month period ended June 30, 2014 tariffs for sales of energy to the corporate customers (key and business) and to individuals (other than G tariff customers connected to the distribution network of PGE Dystrybucja S.A.) were not subject to approval of the President of the Energy Regulatory Office.

In the period ended June 30, 2014 sales of electricity to off-takers from the G tariff group, connected to the distribution network of PGE Dystrybucja S.A., was conducted on the basis of electricity Tariff for PGE Obrót S.A. approved by the decision of the President of the Energy Regulatory Office of December 17, 2013 for the period from January 1, 2014 till December 31, 2014. In comparison to the analogical period of 2013 tariffs in G tariff group decreased by approximately 10%.

DISTRIBUTION OF ELECTRICITY

Methodology of and assumptions for tariffs determination were published in the document "Tariffs for the DSO for the year 2014", which was prepared and published by the President of the Energy Regulatory Office (see p. 2.3.4 of this report).

Tariff of PGE Dystrybucja S.A. for 2014 was approved by the President of the Energy Regulatory Office on December 17, 2013 and came into force on January 1, 2014.

Distribution tariffs for 2014 approved by the President of the Energy Regulatory Office, contributed to changes in average payments for customers in particular tariff groups in comparison to year 2013:

- A tariff group – increase by 5.26%;
- B tariff group – increase by 1.10%;
- C+R tariff group – increase by 1.65%;
- G tariff group – increase by 3.37%.

An average price of energy distribution services in comparison to last tariffs binding in 2013 increased by approx. 2.78 %.

During the reporting period the approved tariffs for distribution services were not subject to any changes.

Increase of distribution tariffs takes into account significant increase in fees (quality and transition) transferred from the Transmission System Operator tariff, that increase regulated revenue but do not affect the result of PGE Dystrybucja S.A.

TARIFF FOR HEAT

Pursuant to art. 47 sections 1 and 2 of the Energy Law, energy companies, which hold licences, set tariffs for heat and propose their duration. Submitted tariff is subject to the approval by the President of the Energy Regulatory Office, provided that it is consistent with rules and regulations referred to in art. 44-46 of the Energy Law. Detailed rules for tariffs determination are defined in the Regulation of the Polish Minister of Economy of September 17, 2010 on detailed rules for calculation of tariffs and on settlements with regard to heat supply and in annual information of the ERO President. Conduction of proceedings concerning heat tariffs approval lies within the competence of regional Branches of the Energy Regulatory Office.

In PGE Group, heat producers from PGE GiEK S.A. apply for tariffs which include justified costs of the generators and justified return on capital.

2.1.5 Emission rights granted free of charge for years 2013-2020

The Regulation of the Council of Ministers, that sets the allocation of allowances for particular units of electricity producers in period 2013-2020, was adopted on April 8, 2014. Analogically, allocations of allowances for heat producers were set by the Regulation of the Council of Ministers of March 31, 2014.

PGE GiEK S.A. accounts were credited with free allowances for heating energy for 2014, while free allowances for electricity will be received by the Group by the end of April 2015, after verification of reports from investments submitted to the National Investment Plan.

The following table presents data concerning CO_2 emission from major Group installations in the first half of 2014 (in comparison to the allocations).

Table: Emission of CO_2 from major Group installations in the first half of 2014 in comparison to allocation of CO_2 emission rights for 2014 (in Mg).

Operator	CO_2 emissions in H1 2014	Allocation of CO_2 emission rights for 2014
PGE GiEK Branch Elektrownia Bełchatów	17,602,098	15,535,037
PGE GiEK Branch Elektrownia Turów	3,870,891	6,247,900
PGE GiEK Branch Elektrownia Opole	3,603,139	3,587,594
PGE GiEK Branch Zespół Elektrowni Dolna Odra	2,492,680	2,931,631
PGE GiEK Branch Zespół Elektrociepłowni Bydgoszcz	419,420	708,528
PGE GiEK Branch Elektrociepłownia Gorzów	226,911	297,971
PGE GiEK Branch Elektrociepłownia Lublin-Wrotków	161,775	387,687
PGE GiEK Branch Elektrociepłownia Rzeszów	102,169	140,185
PGE GiEK Branch Elektrociepłownia Kielce	97,586	128,824
PGE GiEK Branch Elektrociepłownia Zgierz	51,835	56,103
TOTAL	**28,628,504**	**30,021,460**

2.1.6 Termination of long-term contracts (LTC)

Due to the termination of LTCs in accordance with the LTC Act, the producers being earlier the parties to such contracts obtained a right to receive compensations for the coverage of so called stranded costs. Stranded costs were capital expenditures resulting from investments in generating assets made by the generator before May 1, 2004 that a generator is not able to recoup from revenues obtained from sales of generated electricity, spare capacity and ancillary services in a competitive environment after early termination of LTC. The LTC Act limits the total amount of funds that may be paid to all generators to cover stranded costs, discounted as at January 1, 2007, to PLN 11.6 billion, including PLN 6,317 million for PGE GiEK S.A.

Table: Key data relating to PGE Group generators subject to the LTC Act.

Generator	LTC maturity	Maximum amount of stranded and additional costs (in PLN million)
PGE GiEK S.A. Branch Elektrownia Opole	2012	1,966
PGE GiEK S.A. Branch Elektrownia Turów	2016	2,571
PGE GiEK S.A. Branch Zespół Elektrowni Dolna Odra	2010	633
PGE GiEK S.A. Branch Elektrociepłownia Gorzów	2009	108
PGE GiEK S.A. Branch Elektrociepłownia Lublin-Wrotków	2010	617
PGE GiEK S.A. Branch Elektrociepłownia Rzeszów	2012	422
TOTAL		**6,317**

In the period provided for by the LTC Act, i.e. till December 31, 2007, PGE S.A. signed LTC termination agreements with generators being parties to the then applicable LTCs. Therefore generators obtained a right to receive funds to cover their stranded costs.

The impact of LTC compensations on results achieved by the PGE Group is described in Note 26.1 to the consolidated financial statements and in p. 4.6 of this report.

2.1.7 Fuel purchase costs

Table: Volume and cost of purchase of fuels from third party suppliers in the first half-year of 2014 and 2013.

Type of fuel	H1 2014		H1 2013	
	Volume (tons 000')	Cost (PLNm)	Volume (tons 000')	Cost (PLNm)
Hard coal	2,910	728	2,585	728
Gas (cubic metres thousand)	108,094	33	227,757	197
Biomass	645	180	531	151
Fuel oil (heavy and light)	18	36	23	50
TOTAL		**977**		**1,126**

In the first half of 2014 the costs of purchasing primary fuels from providers outside the Group amounted to PLN 977 million and were lower by approximately 13% as compared to the first half of 2013.

The following aspects had the biggest impact on the decreased cost of fuel purchase in PGE Capital Group:

- Decreased volumes of use of gas in connection with ceasing production from CCGT in Rzeszów CHP from March 18, 2013 and decreased use in Lublin Wrotków CHP due to lack legal regulations for generation of electricity in cogeneration.
  In accordance with the amended Energy Law, which came into forceon April 30, 2014, cogeneration support scheme was restored and prolonged until the end of 2018. Support for CHP plants which generate electricity and heat in gas-fired installations improves efficiency of these producers and and contributes to the increase in the consumption of this type of fuel.
- Purchase price of gas was 65% lower due to an increase of the share of locally-sourced high-nitrogen gas in total gas consumption during the first half of 2014, as compared with the share of this type of gas in the first half of 2013 (about 97% in 2014 vs. about 46% in 2013);
  An increase of the share of locally-sourced gas results from ceasing and reduction of production in Rzeszów CHP and in Lublin Wrotków CHP along with the similar production level in a unit using locally-sourced gas – Gorzów CHP.
- Purchase prices of hard-coal – lower by 11%, what connected with the higher usage resulted in neutral effect for total purchase cost of hard coal.

In the first half of 2014 approximately 70% of the electricity was produced from internally sourced lignite, whose extraction price is fully controlled by PGE Capital Group.

2.2 Key operational figures of PGE Capital Group

Table: Key operational figures.

Key figures	**Unit**	**H1 2014**	**H1 2013**	**change %**
Lignite extraction	Tons m	24.13	25.08	-4%
Net electricity production	TWh	26.62	28.24	-6%
Heat sales	GJ m	10.06	12.14	-17%
Sales to final customers*	TWh	19.56	17.85	10%
Distribution of electricity**	TWh	15.95	15.60	2%

** sales by PGE Obrót S.A. with additional estimation and with taking into account the sales within PGE Group*
*** with additional estimation*

2.2.1 Balance of energy of PGE Capital Group

SALES OF ELECTRICITY

Table: Sales of electricity outside the PGE Capital Group (in TWh).

Sales volume	**H1 2014**	**H1 2013**	**change %**
SALES IN TWh, including:	**49.14**	**53.27**	**-8%**
Sales to end-users*	19.53	17.84	9%
Sales on the wholesale market, including:	29.05	34.67	-16%
Sales on the domestic wholesale market - power exchange	*27.14*	*26.43*	*3%*
Other sales on the domestic wholesale market	*1.61*	*7.65*	*-79%*
Sales to foreign customers	*0.30*	*0.59*	*-49%*
Sales on the Balancing Market	0.56	0.76	-26%

** after elimination of internal sales within PGE Group*

The decrease of volume of electricity sold by the Group on the wholesale market resulted from ceasing of electricity sales within the contract with Energa - Obrót S.A. which was pursued in 2013.

Increased sales to end users was pursued mainly in large and medium enterprises segment.

Decreased sales of electricity to foreign customers is connected with lower sales of PGE Trading GmbH, resulting mostly from the difference of prices between Polish market and markets of neighbouring countries.

PURCHASES OF ELECTRICITY

Table: Purchases of electricity from outside of the PGE Capital Group (in TWh). Table: Purchases of electricity from outside of the PGE Capital Group (in TWh).

Purchases volume	H1 2014	H1 2013	change %
PURCHASES IN TWh, including:	**25.10**	**27.36**	**-8%**
Purchases on the domestic wholesale market – power exchange	18.30	22.65	-19%
Purchases on the domestic wholesale market, other	2.66	1.92	39%
Purchases from abroad	0.25	0.23	9%
Purchases from Balancing Market	3.89	2.56	52%

In the first half-year of 2013, PGE S.A. purchased larger volumes under an agreement with Energa - Obrót S.A., which terminated in 2013. However in the first half of 2014 the decrease of purchase on the wholesale market was lower than the decrease on the other domestic wholesale market because purchased volumes were used for coverage of increased sales to the final off-takers. An increase in other purchases on the domestic wholesale market results from the purchase by PGE Obrót S.A. of electricity on a local market, which was necessitated by the requirement to procure electricity from renewable sources.

PRODUCTION OF ELECTRICITY

Table: Generation of electricity by the PGE Capital Group (in TWh).

Generation volume	H1 2014	H1 2013	change %
ENERGY GENERATION IN TWh, including:	**26.62**	**28.24**	**-6%**
Lignite-fired power plants	18.71	20.16	-7%
Including co-combustion of biomass	*0.18*	*0.09*	*100%*
Coal-fired power plants	5.95	5.76	3%
Including co-combustion of biomass	*0.23*	*0.16*	*44%*
Coal-fired CHP plants	0.64	0.67	-4%
Gas-fired CHP plants	0.22	0.76	-71%
Biomass-fired CHP plants	0.24	0.23	4%
Pumped storage power plants	0.28	0.21	33%
Hydroelectric plants	0.24	0.31	-23%
Wind power plants	0.34	0.14	143%

A decrease in production of electricity at lignite-fired power plants results mainly from lower production in PGE GiEK S.A. Branch Elektrownia Turów, as a result of decommissioning of unit no. 10 by the end of 2013. Additionally, shorter operation time of unit no. 14 at PGE GiEK S.A. Branch Elektrownia Bełchatów, due to repair in April 2014, also attributed to the lower production.

An increase in production of electricity at coal-fired power plants results from higher production in PGE GiEK S.A. Branch Elektrownia Opole in the first half of 2014. Lower production in PGE GiEK S.A. Branch Elektrownia Opole in the first half of 2013 was a consequence of breakdown and switching off of unit no. 3 from March to June 2013.

A decrease in production of electricity at coal-fired CHP plants results mainly from lower production of electricity in co-generation with heat in PGE GiEK S.A. Branch ZEC Bydgoszcz due to lack of off-take of the process steam in 2014 by one of the major customers.

A decrease in production at gas-fired CHP plants is a result of ceasing production as of March 18, 2013 in combined cycle units in Rzeszów CHP and Lublin Wrotków CHP due to lack of legal regulations with regard to support of electricity production in co-generation (see p. 2.1.7 of the foregoing report).

Increased production in pumped storage power plants results from the character of work of these units, which were used at higher degree by PSE S.A. in the first half-year of 2014.

A decrease of production in hydroelectric power plants is a result of unfavourable hydrological conditions.

An increase of production in wind power plants is a result of increase of the installed capacity by 173 MW.

2.2.2 Sales of heat

In the first half-year of 2014 the heat sales in PGE Capital Group totalled 10.06 GJ million and were lower by 17% as compared to 2013. Lower sales of heat results mainly from ceased heat input by a key off taker of PGE GiEK S.A. Branch Zespół Elektrociepłowni Bydgoszcz. Lower sales of heat results from lower demand for heat and is dependent on weather conditions in Poland.

2.3 Business segments

Table: Breakdown of the Group's income by business segments in the first half of 2014 and 2013.

in PLN million	Total income H1 2014	Total income H1 2013	% change
Conventional Generation	6,658	6,282	6%
Renewable Energy	387	376	3%
Wholesale Trading	4,765	6,173	-23%
Distribution	2,848	2,786	2%
Retail Sale	6,129	6,486	-6%
Other activity	849	801	6%
TOTAL	**21,636**	**22,904**	**-6%**
Consolidation adjustments	-7,428	-7,803	**-5%**
TOTAL AFTER ADJUSTMENTS	**14,208**	**15,101**	**-6%**

Table: Key figures for each business segment in the first half of 2014 (after eliminations).

in PLN million	EBITDA	EBIT	Capital expenditures	Assets of the segment*
		H1 2014		
Conventional Generation	2,948	2,114	1,578	32,363
Renewable Energy	208	105	155	3,329
Wholesale Trading	287	280	6	1,193
Distribution	1,183	691	452	15,116
Retail Sale	-100	-104	1	3,030
Other activity	73	10	74	1,403
TOTAL	**4,599**	**3,096**	**2,266**	**56,434**
Consolidation adjustments	9	29	-34	-2,054
TOTAL AFTER ADJUSTMENTS	**4,608**	**3,125**	**2,232**	**54,380**

** see Note 10 to the consolidated financial statements*

Table: Key figures for each business segment in the first half of 2013 (after eliminations).

in PLN million	EBITDA	EBIT	Capital expenditures	Purchase of PPE* net, within purchase of new companies	Assets of the segment**
			H1 2013***		
Conventional Generation	1,920	1,071	1,108	0	30,055
Renewable Energy	217	127	62	411	3,004
Wholesale Trading	486	479	5	0	2,534
Distribution	1,136	649	467	0	14,892
Retail Sale	418	414	4	0	2,892
Other activity	59	2	60	0	1,309
TOTAL	**4,236**	**2,742**	**1,706**	**411**	**54,686**
Consolidation adjustments	9	26	-46	312	-3,409
TOTAL AFTER ADJUSTMENTS	**4,245**	**2,768**	**1,660**	**723**	**51,277**

** PPE – property, plant and equipment*

*** see Note 10 to the consolidated financial statements*

**** data restated*

2.3.1 Conventional Generation

Table: Key figures for Conventional Generation.

in PLN million	H1 2014	H1 2013	% change
Sales revenues	6,658	6,282	6%
EBIT	2,114	1,071	97%
EBITDA	2,948	1,920	54%
Capital expenditures	1,578	1,108	42%

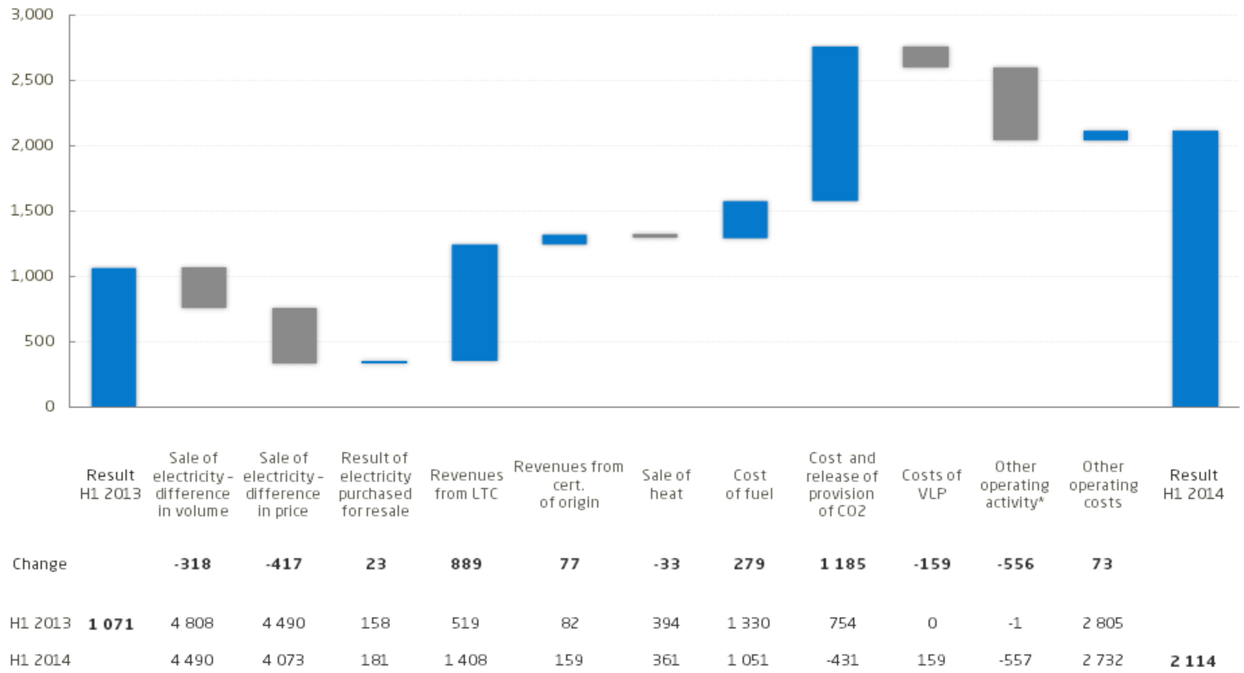
Increase of EBIT by PLN 1,043 million was mainly connected with:

- Higher LTC compensations including: PLN 889 million;
  - revenues from LTC compensations PLN 792 million;
  - adjustment of LTC settlements due to favourable court verdicts PLN 97 million;
- reversal of provision for CO_2 emission rights for 2013 PLN 751 million;
- lower costs of fees for CO_2 emission PLN 432 million;
- lower costs of production fuel used PLN 279 million;
- higher revenues from sales of energy origin certificates PLN 77 million.

Above increases were decreased by:

- lower revenues from sales of electricity from own production PLN (-) 735 million;
- effect of change of discount rate applied to provision for recultivation PLN (-) 601 million;
- higher personnel expenses connected with the implementation of Voluntary Leave Program PLN (-) 159 million;
- lower revenues from sales of heat PLN (-) 33 million.

Chart: Key changes of EBIT in Conventional Generation (in PLN million).



** including change of provision for recultivation due to the change of the discount rate (PLN -601 million)*

CAPITAL EXPENDITURES

Table: Capital expenditures incurred in Conventional Generation segment in the first half of 2014 and 2013, by particular investment tasks.

in PLN million	Capital expenditures		
	H1 2014	H1 2013	% change
Investments in generating capacities, including:	955	416	130%
Development	199	28	611%
Modernization and replacement	756	368	95%
Purchases of finished capital goods	25	14	79%
Vehicles	6	3	100%
Other	331	385	-14%
TOTAL	**1,317**	**818**	**61%**
Activated costs of overburden removal in mines	261	290	-10%
TOTAL with activated costs of overburden removal in mines	**1,578**	**1,108**	**42%**

In the foregoing report presentation of capital expenditures in generating capacities in Conventional Generation segment has changed. Part of expenditures previously shown as development expenditures has been reclassified to capital expenditures for modernization and replacement.

In the first half of 2014 the highest capital expenditures were incurred for the following projects:

- complex reconstruction and modernization of units 7 - 12 in Bełchatów power plant PLN 532 million;
- construction of units 5 and 6 in Opole power plant PLN 127 million;
- change of technology of furnace waste storage in Bełchatów power plant PLN 78 million;
- construction of CCGT gas unit producing electricity and heat in Rzeszów CHP PLN 61 million.

2.3.2 Renewable Energy

Table: Key figures for Renewable Energy.

PLN million	H1 2014	H1 2013	% change
Sales revenues	387	376	3%
EBIT	105	127	-17%
EBITDA	208	217	-4%
Capital expenditures	155	62	150%
Purchase of PPE net, within purchase of new companies	0	411	-

Decrease of EBIT by PLN 22 million mainly resulted from:

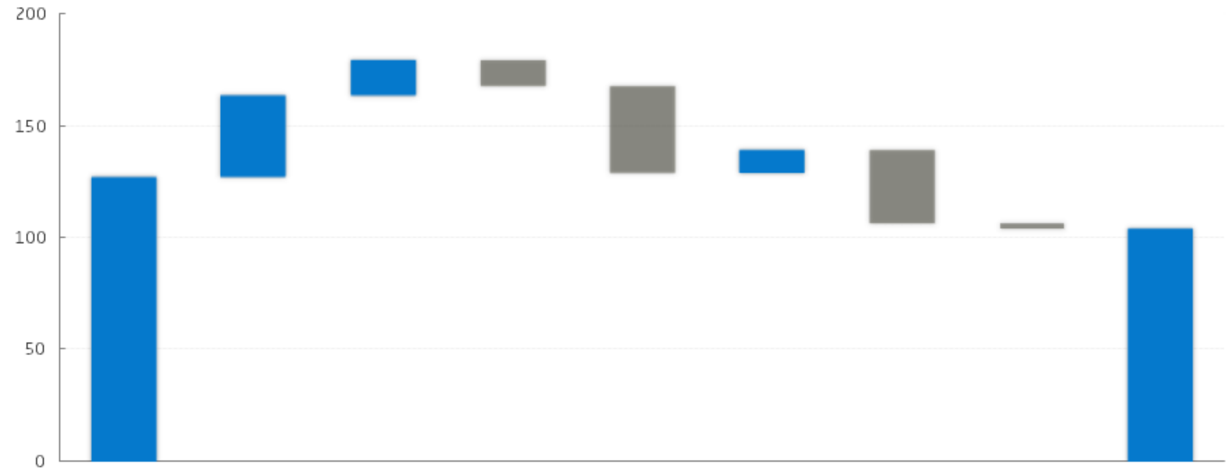
- Lower revenues from sales of electricity and property rights in the hydro power plants PLN (-) 50 million;

Lower result was partly compensated by:

- Higher revenues from sale of electricity and property rights in the wind farms PLN 52 million.

Half-year result of the Renewable Energy segment in 2013 was affected by one-off revaluation of green certificates (as a result of change of settlement price between Renewable Energy and Wholesale Trading segments) what improved the results of Renewable Energy segment by PLN 47 million.

Chart: Key changes of EBIT in Renewable Energy (in PLN million).



	Result H1 2013	Revenues from sale of electricity - wind	Revenues from cert. of origin. - wind	Revenues from sale of electricity - hydro	Revenues from cert. of origin. - hydro	Revenues from regul. serv. and bal. market	Operating expenses of aquired wind farms*	Other	Result H1 2014
Change		36	16	-11	-39	11	-33	-2	
H1 2013	127	28	53	43	72	171	0	-60	
H1 2014		64	69	32	33	182	33	-62	105

**operating expenses of Energia Natury companies reduced by costs of energy used*

CAPITAL EXPENDITURES

Table: Capital expenditures incurred in Renewable Energy segment in the first half of 2014 and 2013.

in PLN million	Capital expenditures		
	H1 2014	H1 2013	% change
Investments in generating capacities, including:	153	57	168%
Development	142	46	209%
Modernization and replacement	11	11	0%
Vehicles	0	2	-
Other	2	3	-33%
TOTAL	**155**	**62**	**150%**
Purchase of PPE net, within purchase of new companies	0	411	-
TOTAL	**155**	**473**	**-67%**

In the first half of 2014 the highest capital expenditures in amount of PLN 114 million were incurred for the construction project of wind farm Wojciechowo with a capacity of 28 MW, for which an occupancy permit was obtained in January 2014 and concession for electricity generation was obtained in March 2014.

The most advanced wind projects for which key decisions were made in the first half of 2014 are as follows:

- Construction of wind farm Karwice with a capacity of 40 MW – an agreement with the general contractor for the construction of the farm was signed in May 2014;
- Construction of wind farm Lotnisko with a capacity of 90 MW - an agreement for delivery of wind turbines was signed in June 2014, a tender for the selection of the building contractor was conducted;
- Construction of wind farm Resko II with a capacity of 76 MW - a tender for the selection of turbines supplier and for the selection of the building contractor were conducted.

Expenditures for the purchase of tangible and intangible fixed assets in the first half of 2013 related to acquisition of wind assets of the Danish company DONG Energy Wind Power A/S.

2.3.3 Wholesale Trading

Table: Key figures for Wholesale Trading.

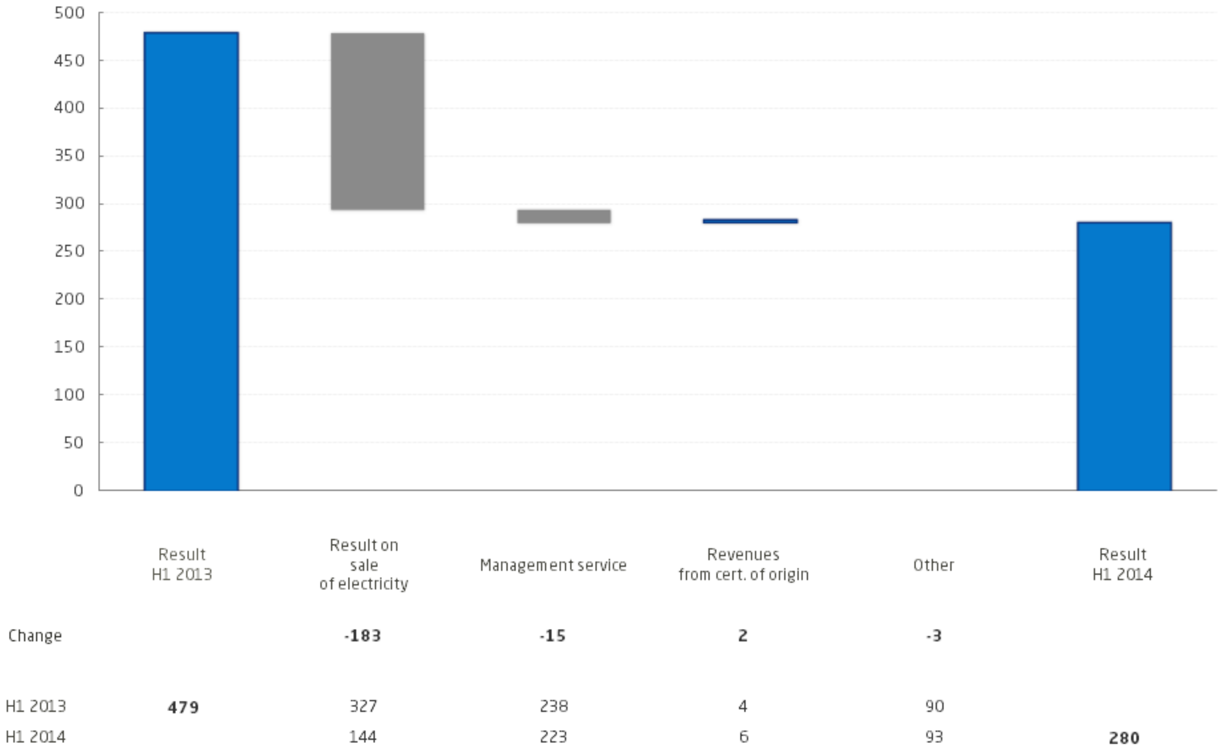
in PLN million	H1 2014	H1 2013	% change
Sales revenues	4,765	6,173	-23%
EBIT	280	479	-42%
EBITDA	287	486	-41%
Capital expenditures	6	5	20%

Decrease of EBIT by PLN 199 million was mainly connected with:

- lower result on electricity sales PLN (-) 183 million;
- lower remuneration with regard to services for PGE GiEK S.A. due to the Agreement on Commercial Management of Generation Capacities PLN (-) 15 million.

In comparison with the same period in 2013, EBIT in the first half of 2014 decreased by PLN 114 million due to changes in power market prices and by PLN 69 million due to lower volumes.

Chart: Key changes of EBIT in Wholesale Trading (in PLN million).



2.3.4 Distribution

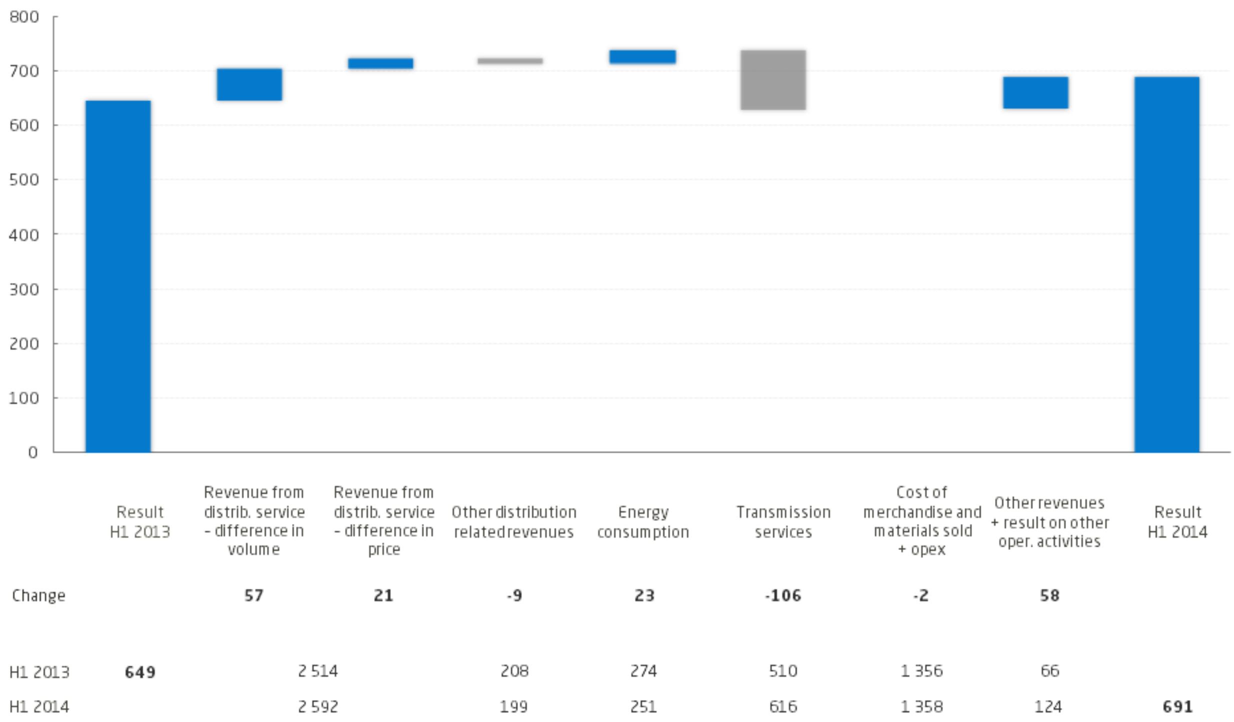
Table: Key figures for Distribution.

in PLN million	**H1 2014**	**H1 2013**	**% change**
Sales revenues	2,848	2,786	2%
EBIT	691	649	6%
EBITDA	1,183	1,136	4%
Capital expenditures	452	467	-3%

Growth of EBIT by PLN 42 million mainly resulted from:

- higher revenues from the distribution services PLN 69 million;
- higher result on other operations (mainly due to higher balance of provisions reversed/created relating to non-contractual use of land) PLN 64 million;
- lower costs of energy used PLN 23 million.

Chart: Key changes of EBIT in Distribution (in PLN million).



CAPITAL EXPENDITURES

Table: Capital expenditures incurred in Distribution segment in the first half of 2014 and 2013.

in PLN million	Capital expenditures		
	H1 2014	H1 2013	% change
MV and LV power networks	110	100	10%
HV/MV and MV/MV power stations	26	50	-48%
HV power lines	16	7	129%
Connection of new off-takers	202	207	-2%
Purchase of transformers and energy counters	47	62	-24%
IT, telemechanics and communication	28	23	22%
Other	23	18	28%
TOTAL	**452**	**467**	**-3%**

The amount of capital expenditures agreed with the ERO President in the Development Plan for a given period, is used as the basis for the appointment of the justified items of regulated revenues; consequently, the amount in question will impact the level of rates in the distribution tariffs subject to approval.

Completed investments lead in the first place to an increase of the Regulatory Asset Base; then, they are reflected in the amount of the return from invested capital and the level of depreciation costs and real estate tax. Return on invested capital is determined for the Distribution System Operator with the use of WACC designated by the ERO President in the given tariff period. The above components are elements of the regulated revenue and in this respect they affect the transmission fees.

In January 2014, PGE Dystrybucja S.A.'s growth plan for 2014-2019 was agreed with the Energy Regulatory Office. The expectation is that the growth plan agreed with the ERO will fully ensure execution of investment activities in the area of connecting new customers and modernization of network assets.

Investment priorities under the approved growth plan are as follows:

- meeting the overall demand for capacity and electricity within PGE Dystrybucja S.A.'s operating area across all voltages;
- implementing plans for supply of electricity to municipalities;
- connecting new receiving installations to the distribution network;
- increasing energy security across the distribution network;
- ensuring the effective distribution of electricity, including reducing energy losses;
- implementing smart metering systems.

2.3.5 Retail Sales

Table: Key figures for Retail Sales.

in PLN million	H1 2014	H1 2013	% change
Sales revenues	6,129	6,486	-6%
EBIT	-104	414	-125%
EBITDA	-100	418	-124%
Capital expenditures	1	4	-75%

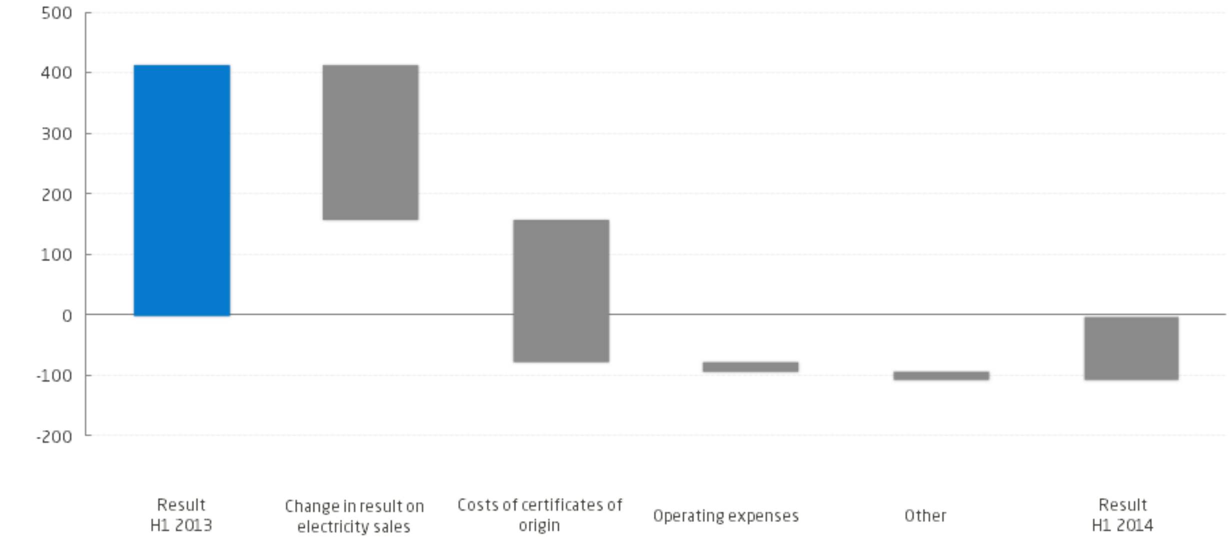
Decrease of EBIT by PLN 518 million was mainly related to:

- lower margin on electricity sales PLN (-) 253 million;
- higher costs of redemption of property rights PLN (-) 235 million.

Lower margin on sale of electricity in the first half of 2014 as compared to the first half of 2013 is mainly due to:

- increasing competition in the corporate customers segment, what directly affects the decline of electricity prices offered to these customers;
- change of sales structure resulting in growth of electricity sales to customers from A and B tariff groups, where margins are lower in comparison to other sales.

Chart: Key changes of EBIT in Retail Sales (in PLN million).



	Result H1 2013	Change in result on electricity sales	Costs of certificates of origin	Operating expenses	Other	Result H1 2014
Change		-253	-235	-15	-15	
H1 2013	414	818	293	138	27	
H1 2014		565	528	153	12	-104

2.3.6 Other Operations

in PLN million	H1 2014	H1 2013	% change
Sales revenues	849	801	6%
EBIT	10	2	400%
EBITDA	73	59	24%
Capital expenditures	74	60	23%

CAPITAL EXPENDITURES

Capital expenditures in Other Operations in the first half of 2014 amounted to PLN 74 million as compared to PLN 60 million in the first half of 2013. Within the above amount, the main capital expenditures in the first half of 2014 were incurred by:

- PGE Systemy S.A. – for IT infrastructure development PLN 21 million;
- Exatel S.A. – for telecommunication infrastructure development PLN 19 million.

Other capital expenditures were mostly related to ancillary services.

2.4 Financial results of PGE Capital Group

Key financial data	Unit	H1 2014 (reviewed)	H1 2013 (reviewed) data restated	% change
Sales revenues	PLN million	14,208	15,101	-6%
EBIT	**PLN million**	**3,125**	**2,768**	**13%**
EBITDA	**PLN million**	**4,608**	**4,245**	**9%**
Net profit attributable to equity holders of the parent company	PLN million	2,497	2,193	14%
LTC compensations, including:	PLN million	1,408	518	172%
Revenues from LTC compensations	*PLN million*	*1,162*	*370*	*214%*
Reversal of provisions for LTC (other operating revenues)	*PLN million*	*246*	*148*	*66%*
Capital expenditures	**PLN million**	**2,232**	**1,660**	**34%**
Net cash from operating activities	PLN million	1,584	3,264	-51%
Net cash from investing activities	PLN million	-5,050	-2,772	-82%
Net cash from financial activities	PLN million	2,093	748	180%
Net earnings per share	PLN	1.34	1.17	15%
EBITDA margin	**%**	**32%**	**28%**	

Key financial data	Unit	As at June 30, 2014 (reviewed)	As at December 31, 2013 (audited)	% change
Working capital	PLN million	7,168	5,223	37%
Net debt/LTM EBITDA*	**x**	**-0.23x**	**-0.39x**	

** LTM EBITDA - Last Twelve Months EBITDA*

Consolidated statement of comprehensive income

In the first half of 2014 total **sales revenues** of the Group amounted to PLN 14,208 million compared to PLN 15,101 million in the first half of 2013, what means decrease by approx. 6%.

Decrease of revenues by PLN 893 million was mainly caused by:

- decreased revenues from sales of electricity PLN (-) 1,847 million;
- decreased revenues from sales of heat PLN (-) 36 million;
- decreased revenues from telecom operations PLN (-) 27 million.

This decrease was partly offset by:

- increase of revenues from LTC compensations PLN 792 million;
- increased revenues from sales of certificates of energy origin PLN 156 million;
- increased revenues from sales of distribution services PLN 82 million.

Cost of goods sold in the first half of 2014 amounted to PLN 10,482 million, what means decrease by approx. 10% in comparison to the first half of 2013.

The decrease of the cost of goods sold by PLN 1,158 million was mainly caused by:

- lower merchandise and materials sold PLN 662 million;
- decreased costs of fees for CO_2 emission PLN 433 million;
- lower costs of production fuel PLN 280 million.

This decrease was partly offset by:

- higher costs of transmission fees PLN (-) 95 million.

Gross profit on sales in the first half of 2014 amounted to PLN 3,726 million compared to PLN 3,461 million in the first half of 2013, what means increase by approx. 8%.

In the first half of 2014 **distribution and selling expenses** of PGE Group amounted to PLN 744 million and were higher by approx. 52% in comparison to the first half of 2013. The increase of selling and distribution expenses was mainly associated with higher costs of redemption of property rights incurred by PGE Obrót S.A.

In the first half of 2014 **general and administrative expenses** amounted to PLN 366 million, reaching a similar level as in the first half of 2013.

Result on other operating activities in the first half of 2014 was positive and amounted to PLN 509 million in comparison to the result of PLN 164 million in the first half of 2013.

Other operating revenues of the Group in the first half of 2014 amounted to PLN 1,289 million, what means increase by approx. 251% in relation to PLN 367 million achieved in the first half of 2013.

Increase of operating revenues by PLN 922 million mainly resulted from:

- reversal of provision for CO_2 emission rights 2013 PLN 751 million;
- adjustment of revenues from LTC compensations PLN 98 million;
- settlement of grant for CCS PLN 67 million.

Other operating expenses of the Group in the first half of 2014 amounted to PLN 780 million compared to PLN 203 million in the first half of 2013, what means increase by approx. 284%.

Increase of operating expenses by PLN 577 million mainly resulted from:

- adjustment of recultivation provision due to change of the discount rate PLN (-) 601 million;
- higher expenses of liquidation of damages and removal of failures PLN (-) 9 million.

In the first half of 2014 result on financial activities was negative and amounted to PLN 7 million, in comparison to negative result in amount of PLN 51 million in the first half of 2013.

The Group's **financial revenues** in the first half of 2014 amounted to PLN 182 million, what means increase by approx. 1% in relation to PLN 180 million achieved in the first half of 2013.

Financial expenses of the Group in the first half of 2014 amounted to PLN 189 million, what means decrease by approx. 18% in comparison to PLN 231 million achieved in the first half of 2013.

Lower level of financial expenses by PLN 42 million mainly resulted from:

- lower interest expenses related mainly to discount unwinding PLN 39 million;
- lower expenses due to exchange losses PLN 20 million.

As a result of the factors discussed above, the gross profit of the Group in the first half of 2014 amounted to PLN 3,118 million, compared to PLN 2,717 million in the first half of 2013.

In the first half of 2014 **gross profit margin** of the Group (gross profit to total sales revenues) increased to 22% from 18% in the first half of 2013.

Net profit of the PGE Capital Group in the first half of 2014 amounted to PLN 2,510 million compared to PLN 2,202 million in the first half of 2013.

Net profit attributable to the equity holders of the parent company increased in the first half of 2014 by PLN 304 million, compared to the first half of 2013 and amounted to PLN 2,497 million.

Total comprehensive income of the Group amounted to PLN 2,455 million in the first half of 2014 compared to PLN 2,204 million in the first half of 2013.

Consolidated statement of financial position

Non-current assets of the Group as at June 30, 2014 and as at December 31, 2013 amounted respectively to PLN 49,074 million and PLN 47,738 million.

Increase in value of non-current assets by PLN 1,336 million was mainly caused by:

- Capital expenditures incurred for property, plant and equipment and intangible assets PLN 2,232 million;

  including:

  - PGE GiEK S.A. PLN 1,578 million;
  - PGE Dystrybucja S.A. PLN 452 million;
  - PGE EO S.A. PLN 155 million;
- Increased advances for construction in progress PLN 578 million.

This growth was compensated by:

- depreciation charges on fixed assets and intangible assets PLN (-) 1.483 million;
- provisions created due to impairment and sale of fixed assets and intangible assets PLN (-) 60 million.

Current assets of the Group as at June 30, 2014 and as at December 31, 2013 amounted respectively to PLN 14,384 million and PLN 13,013 million.

The increase of the value of the Group's current assets by PLN 1,371 million was mainly related to:

- increased other loans and financial assets PLN 2,681 million;

  including:

  - deposits over 3 months PLN 2,015 million;
  - LTC receivables PLN 648 million;

- increased other short-term assets PLN 805 million;
- higher inventory PLN 156 million.

Increase in other short-term assets resulted from higher value of advances for hard coal supply and increased VAT receivables.

Increase in inventory results from higher value of certificates of energy origin and CO_2 emission rights held for trading and value of certificates with the simultaneous decrease of exploitation materials.

Current assets were also affected by:

- decreased cash and cash equivalents PLN (-) 1,375 million;
- decrease in greenhouse gases emission rights PLN (-) 442 million;
- decreased trade receivables PLN (-) 435 million.

Changes in cash and cash equivalents were described in the part relating to cash flow statement.

Decrease in greenhouse gases emission rights results from redemption of CO_2 emission rights for 2013.

As at June 30, 2014 and as at December 31, 2013 **total equity of the Group** amounted respectively to PLN 43,914 million and PLN 43,648 million.

Non-controlling interest as at June 30, 2014 and as at December 31, 2013 amounted respectively to PLN 134 million and PLN 266 million.

The increase in total equity by PLN 266 million mainly resulted from recognition of the net profit for the period ended June 30, 2014 in amount of PLN 2,510 million. Total equity of the Group was negatively affected by distribution of the profit for 2013 and allocation of part of the net profit i.e. PLN 2,057 million for dividend payment.

Long-term liabilities as at June 30, 2014 and as at December 31, 2013 amounted respectively to PLN 12,328 million and PLN 9,313 million.

Growth of long-term liabilities by PLN 3,015 million was mainly caused by:

- increase in interest-bearing loans, borrowings, bonds and lease PLN 1,973 million;
- increased long-term provisions PLN 718 million;
- increase of deferred tax liability PLN 402 million.

Increase in interest-bearing loans, borrowings, bonds and lease is mainly connected with issue of Eurobonds in amount of PLN 2,034 million.

Increased long-term provisions result from increased provision for recultivation (result of discount rate change from 4.35% to 3.5%) and actuarial provisions.

Increase of deferred tax liability results from higher difference between tax and carrying value of property, plant and equipment.

Short-term liabilities as at June 30, 2014 and as at December 31, 2013 amounted respectively to PLN 7,216 million and PLN 7,790 million.

Decrease of short-term liabilities by PLN 574 million mainly resulted from:

- lower short-term provisions PLN (-) 1,121 million;
- decrease of other financial liabilities PLN (-) 1,070 million;
- lower income tax liabilities PLN (-) 103 million;
- decreased trade receivables PLN (-) 101 million.

This decrease was compensated by:

- increase in other non-financial liabilities PLN 1,640 million;
- increase in short-term part of interest-bearing loans, borrowings, bonds and lease PLN 165 million;
- higher financial assets at fair value through profit or loss PLN 27 million.

Lower short-term provisions mainly result from reversal and use of provision for purchase of CO_2 emission rights and use of provision for property rights.

Decrease of other financial liabilities was mainly caused by lower LTC liabilities, lower liabilities due to bails and guarantee deposits and lower financial liabilities related to purchase of property, plant and equipment.

Increase in other non-financial liabilities mainly results from increased liability related to dividend along with the lower VAT and excise tax liabilities, lower liabilities related to current employment and lower environmental fees.

Increase in short-term part of interest-bearing loans, borrowings, bonds and lease results from higher degree of use of current account credits by the Group companies.

Consolidated statement of cash flows

Cash and cash equivalents as at June 30, 2014 amounted to PLN 4,575 million and were lower by PLN 1,455 million than at the end of analogical period of 2013. Decrease of Cash and cash equivalents is mainly connected with lower cash flows from operating revenues, expenditures for investment projects of the Group companies along with the advance payments for the construction of new units primarily in PGE GiEK S.A. Branch Elektrownia Opole and advance payment resulting from agreement related to hard coal purchase by PGE GiEK S.A.

The total net cash flow from operating activities for the first half-year ended June 30, 2014 amounted to PLN 1,584 million compared to PLN 3,264 million in the first half-year ended June 30, 2013.

Negative net cash flow from investing activities for the 6-month period ended June 30, 2014 amounted to PLN 5,050 million, compared to negative net cash flow in amount of PLN 2,772 million for the 6-month period ended June 30, 2013.

The level of **cash flow from investing activities** for the 6-month period ended June 30, 2014 was mainly affected by:

- expenses for the purchase of property, plant and equipment and intangible assets PLN (-) 2,988 million;
- deposits over 3 months open PLN (-) 2,091 million.

Positive net cash flow from financial activities for the 6-month period ended June 30, 2014 amounted to PLN 2,093 million compared to positive net cash flow in amount of PLN 748 million z for the 6-month period ended June 30, 2013.

Cash flow from financial activities for the 6-month period ended June 30, 2014 was mainly affected by positive balance of of proceeds/repayments from/of bank loans, borrowings, bonds and finance lease.

2.5 Publication of financial forecasts

PGE Polska Grupa Energetyczna S.A. did not publish financial forecasts.

On July 28, 2014 PGE S.A. published current report no. 37/2014 in which PGE disclosed estimated consolidated EBITDA for the first half of 2014. Consolidated EBITDA for the first half of 2014 was recognised at the estimated level and amounted to PLN 4.6 billion.

2.6 Rating

PGE S.A. holds ratings assigned by two rating agencies: Fitch Ratings Ltd („Fitch") and Moody's Investors Service Limited („Moody's").

On May 23, 2014 Fitch affirmed PGE's long-term foreign and local currency Issuer Default Ratings (IDRs) at BBB+ with a Stable Outlook. Fitch has also assigned a foreign currency senior unsecured rating of 'BBB+' to PGE Sweden AB (publ)'s EUR 2 billion Euro Medium Term Note Programme („EMTN Programme"), which is guaranteed by PGE S.A.

According to a Fitch definition, BBB ratings indicate that expectations of default risk are currently low. The capacity for payment of financial commitments is considered adequate but adverse business or economic conditions are more likely to impair this capacity.

On May 26, 2014 Moody's downgraded PGE's long-term rating from A3 with stable outlook to Baa1 with stable outlook. As a rationale of the rating action Moody's indicated the execution risk associated with PGE's investment plans and the related funding requirements in the context of the weak levels of wholesale power prices and uncertainty around development of energy markets in Poland. Moody's also assigned a rating of (P)Baa1 to PGE Sweden AB (publ)'s EUR 2,000,000,000 billion EMTN Programme.

Baa ratings are investment ratings and belong to medium-grade category that is characterised by moderate credit risk.

Under the EMTN Programme PGE Sweden AB (publ) made two issues of Eurobonds. First issue took place on June 9, 2014. Nominal value of 5-year bonds sold in public offer amounted to EUR 500 million and rating agencies assigned ratings of BBB+ (Fitch) and Baa1 (Moody's). Second issue, amounting to EUR 138 million (private placement) took place on August , 2014. Maturity of these bonds is 15 years and Fitch rated this issue at BBB+.

3 Risks and threats of the PGE Capital Group

The activity of major PGE Capital Group companies, as well as other entities operating in the electrical and power sector, is exposed to a number of external risks and threats connected with market, regulatory and legal environment, as well as internal risks and threats accompanying their operations.

Key risks and threats, to which the PGE Group's activity is exposed, are described below. The order of the presentation of individual risks does not reflect the assessment of their relevance, i.e. the degree of exposure of the PGE Capital Group to the following risks. The following list does not include all the risk factors of PGE Group's activity that may emerge in future.

The PGE Capital Group has continued to develop a comprehensive risk management system so that risks involved in its operations and having a significant impact on the value of the Company are maintained at sustainable levels in relation to assumed business objectives. The risk management procedures cover key segments of the value chain of the PGE Capital Group and are implemented at all levels of management, from lowest-level employees to top management. The PGE Capital Group risks concerning various areas of operations are identified and kept within the assumed limits by reducing negative effects of such risks and by taking preventive or corrective measures. In particular, actions undertaken in respect of specific risks are carried out on the basis of sets of rules and practices. In the case of risks associated with commercial and financial activities, the Group continues to implement adequate risk limits calculated, inter alia, on the basis of statistical measurements and monitors the extent of their application. In addition, the Company's structure comprises two specialised committees supporting and supervising the management of major and specific risks, in particular in the area of commercial, financial and investing activities of the Group.

3.1 Risk factors connected with market environment and general macroeconomic situation in Poland and in the world

3.1.1 Risk connected with macroeconomic situation

The operations of PGE Group are affected mainly by macroeconomic and market factors related to Polish economy, such as dynamics of electricity demand, level and volatility of prices of electricity, CO_2 emission rights, property rights, fuel and availability of materials used for production of electric power and heat and also interest rates, PLN exchange rate, inflation rate, unemployment rate, Polish GDP and industrial production dynamics, changes in directions of the economic and tax policy of the state. Other than factors associated with Polish economy, Group's operations are also affected by macroeconomic conditions in other countries, particularly other Member States of the European Union. Any deterioration of the general economic conditions in Poland or in the world may considerably and negatively impact the operations, performance or financial standing of the Group.

3.1.2 Risk relating to an increasing competition

Given the on-going development of the retail market, increasing activity of energy sellers and growing number of customers who change their energy supplier, the PGE Group is exposed to the risk of losing its existing customers in the retail market and the risk of decreased margin achieved on sale to the existing customers. Moreover, in connection with the increasing production of energy from renewable energy sources and preference of the green energy in the system, there is an increasing pressure on profitability of the conventional energy sources. In addition, from the beginning of 2014 Poland became a net importer of electricity from markets with lower prices. This trend should extend in the coming years as a result of further integration of Europe's electricity market.

3.1.3 Risk of a decrease in demand for electricity and heat

The PGE Group's income is substantially dependant on the consumption of power and heat by the users. In a long run, power consumption is expected to grow. However, there is no guarantee that such a growth will occur and that the rate of growth will achieve an assumed level.

Demand for electricity may decline, in particular, as a result of:

- economic slowdown;
- possible reduction of energy consumption level by off-takers of low economic standing;
- development of new energy saving technologies;
- promotion of the prosumer energy development;
- weather conditions.

Decreasing growth rate of demand for electricity and limited access to interconnectors limiting opportunities for exporting electricity produced by the Group or import of energy may have a significant adverse impact on the activity and financial results of Group companies.

Uncertainty regarding future economic situation in the world's economy, intensified by the financial crisis in European countries and unstable situation in Ukraine, may negatively affect the domestic production, consumption and investments, subsequently leading to decreased demand for electricity and drop of electricity prices.

3.2 Risk factors connected with regulatory and legal environment

3.2.1 Political risk

The activity of the PGE Group in key operating areas, i.e. lignite mining, generation, distribution and sale of electricity and heat, is subject to legislation, government regulation and government policy adopted by Polish authorities and agencies, authorities of the European Union, and other states. Changes in legislation, regulations and/or policies may be influenced by these authorities, what in turn may affect business activity of the Group including, inter alia, the regulation of electricity prices, heat prices and distribution services for off takers, in particular households. It is particularly relevant for investments in the generating segment as they are characterised by high capital expenses and a long implementation period (in case of nuclear power plants it is 10 years and more including the preparation phase).

3.2.2 Risk of instability of legal environment

The PGE Group's activity is subject to numerous Polish and European laws and regulations and international law. The provisions of the laws, regulations, decisions, positions, opinions and actions of relevant authorities important for the Group's activity are subject to changes. In particular, the Energy Law was repeatedly amended, and some of the amendments introduced significant changes with respect to core business areas. Types, directions and scopes of such amendments may have an unpredictable impact on the Group's activity.

Moreover, environment protection regulations become more strict, and adjustment to these changes may be connected with the additional significant expenditures. Non-compliance with regard to environment protection requirements may lead to PGE Group responsibility, including financial sanctions or periodical or even permanent suspension of exploitation of particular installations.

The tax system in Poland is characterised by a substantial instability of regulations, a high level of complexity, potential steep penalties in the event of tax offences or non-compliance, as well as a general attitude of the tax authorities that features the presumption of taxpayers' guilt. Tax settlements may be the subject of audit by relevant authorities, who are authorised to impose penalties and sanctions, together with penalty interest.

3.2.3 Risk associated with amendments to the support schemes for cogeneration sources

In previous years, generators in Group, who provided electricity in combination with heat (cogeneration), benefited from a scheme supporting highly efficient generators. Under the applicable regulations, the scheme supporting highly efficient cogeneration based on certificates of origin (the so-called yellow certificates – for installations fired with gaseous fuels (irrespective of installed capacity) or installation of a total installed capacity below 1 MW, and red certificates – for units fired with fuels other than gas, of a total installed capacity of more than 1 MW) operated until December 31, 2012 (energy produced in 2012 was settled by March 31, 2013). As from December 31, 2012 the support expired. On April 15, 2014, a law amending the Energy Law act, restoring the support scheme for highly efficient co-generation, was published in Journal of Laws (law came into force after 14 days from the publication date). Under the adopted act, the application of the support scheme for electricity and heat generators in the highly efficient co-generation process was prolonged to the end of 2018. Due to the character of the program, the European Commission may consider proposed Polish support scheme for co-generation as unlawful state aid and in consequence the support for co-generation units may be questioned. Therefore there is a risk that the companies will be obliged to return the proceeds received under the support scheme plus interest, what would adversely affect revenues
and returns of co-generation units of the Group who are benefiting from support scheme.

In addition, a lack of legislation effort is still visible as regards developing a framework for long-term support of co-generation, which would allow commencement of new investments in this area.

3.2.4 Risk associated with amendments to the support schemes for renewable energy sources

The Group's units generating electricity from renewable energy sources as they also benefit from the support scheme for renewable energy installations. According to the draft new renewable energy act, which is currently in the legislation process, the present support scheme designed for units generating electricity from renewable sources and stipulated by the Energy Law will be changed. On July 8, 2014, the governmental draft Act on the Renewable Energy Sources was filed with Sejm (lower chamber of Polish Parliament), which directed it for examination by the Extraordinary Committee for energy sector and energy resources .

Taking into account the proposed amendments to the Act on Renewable Energy Sources, the greatest risk for the PGE Capital Group in respect of lost revenues may be caused by the discontinuation of support for hydro power plants with installed capacity of above 5MW and reduced scope of support for biomass co-combustion with conventional fuels to the value of 0.5 of the certificate of origin for each 1MWh of generated power (excluding dedicated multi-fuel combustion plants). If the proposed amendments to the Act on Renewable Energy Sources enter into force, it wil have a significant impact on the profitability of existing installations using renewable energy sources and also on future investment decisions of the PGE Capital Group.

3.2.5 Risk connected with the requirement for licenses

The Group's core activity is subject to a number of licenses, including licenses for the electricity and heat generation, the distribution of electricity and heat, the electricity and heat trading, the fuel gas trading, as well as for the lignite mining. In order to continue business activity, the Group needs to maintain and extend existing licenses. Any withdrawal or limitation of licenses or the imposition of additional conditions under the license may cause that Group companies will not be able to run their activities, their activities will be significantly limited or substantially influenced otherwise.

3.2.6 Risk resulting from the potential violation of antitrust regulations

Distribution company of the PGE Group is a natural monopolist in electricity distribution services on area of it operations. In addition the PGE Group is the main electricity producer in Poland (approximately 38% share in the electricity generation market) and is one of the biggest electricity sellers in Poland. Given its monopolist or dominant position in relevant markets, the PGE Group is subject to limitations in the form of a ban on overusing its dominant position based on antitrust regulations of the Polish law and the law of the European Union. In the case of any violation thereof, antitrust authorities (the President of the Office for Consumer and Competition Protection, European Commission) may order to take up defined actions or enforce sanctions in the form of financial penalties. Constraints arising from the antitrust regulations or the unfavourable interpretation thereof by the public administration bodies may limit the potential of growth of PGE Group.

3.2.7 Risk connected with the programme of CO_2 emissions reduction

As of January 1, 2013 the CO_2 emission rights are not granted through the National Allocation Plan ("NAP") from the pool granted to Poland by the European Commission ("EC") as it took place in the second ETS settlement period (2008-2012). In next, third settlement period (2013-2020), as a rule, allowances –except for are free allowances for industrial producers, heat producers and electricity producers (respectively art. 10a and 10c of the ETS directive) known as derogations - should be purchased on auctions. Size and range of derogations for particular units is determined and proposed by National Implementation Measures ("NIM") pursuant to guidelines of the European Commission. Polish government submitted to the EC documents entitling to receive free CO_2 emission rights. On January 22, 2014, the European Commission accepted the Polish plan assuming the allocation of 404.6 million of CO_2 emission rights to the modernisation of the electricity sector. The plan covers more than 340 investments for a total value of approx. PLN 119 billion. Once the EC decision was published, the Polish government adopted an ordinance on the list of electricity production installations that are covered by the emissions trading scheme for the settlement period 2013-2020, together with allocation of emission allowances for each year. Pursuant to the ordinance, CO_2 emission allowances for 2013 were transferred to the accounts of the relevant companies. PGE Group received approx. 31 million EUAs under free-of-charge allocation of allowances for 2013.

The ETS directive is presently being implemented into the national legislation, i.e. the bill on the trading scheme of greenhouse gas emissions rights was published for public consultations. It introduced a number of changes in the greenhouse gas emission rights scheme in the third settlement period. The changes consist in particular in the introduction of emission rights auctions as a basic method for distribution of rights, the possibility of derogation for the electricity and power sector and introduction of the mechanism of the so-called national implementing measures. In its current version, the act imposes limits on the possibility to transfer excess investment expenditure over the market value of free-of-charge allowances to subsequent reporting periods.

Besides, at the European level, a strong group is lobbying for an increase of the Community CO_2 reduction target, in particular after 2020. In accordance with the 2008 climate package, the European Union and the Member States undertook to reduce their CO_2 emissions by 20% by the year 2020 in relation to the base year (1990). On January 22, 2014, the European Commission published proposals for the 2030 EU climate and energy policy framework, which provided new targets with regard to CO_2 emission reductions and the share of energy generated from renewable sources. According to the assumptions, the binding CO_2 emission rights target is to rise to 40% and the share of the Renewable Energy Sources is to reach a minimum of 27% in final energy balance across the EU. In contrast to the proposed target for renewable energy, which is to be in force only at the level of the entire EU, the 40% CO_2 emission reduction target by the year 2030 proposed by the European Commission will be split into binding targets for individual countries. This may lead to a rise in prices of emission rights, and therefore to a deterioration of profitability, in particular in respect of existing generation assets based on coal combustion. The proposal of the European Commission has not been a formal legislative motion yet, however a draft law on the matter may be presented next year.

Together with the new climate and energy targets, the European Commission put forward amendments to the EU emission trading system (ETS), which had been launched in 2005 as an instrument of the EU countries designed to tackle climatic change. The Commission proposes to set up a stabilization reserve of rights from the year 2021 and to increase the annual reduction in the number of emission rights from 1.74% to 2.2% after 2020. The envisaged amendments to the ETS directive pose a risk of permanent withdrawal of emission rights from the market in order to raise their prices. The proposal constitutes a legislative initiative. Although the measure is to enter into force as of 2021, its effects on the CO_2 prices may be noticeable even before 2020 because of the anticipated fall in the emission rights supply by the market; this may in turn translate into higher prices of emission rights.

3.2.8 Risk of more stringent restrictions with respect to emissions to the environment of substances other than CO_2

Operations conducted by the companies of the Group, including in particular electricity and heat generation, are connected with emissions of not only CO_2, but also NO_X, SO_2, dusts and other substances. In order to minimize their impact on the environment and to protect it, EU and national authorities introduce relevant legislation applying, among others, to the energy and mining sector. Issues of environmental protection and related obligations are stipulated in the so-called "integrated permits" or sectorial permits, and installations which are obliged to obtain the permits must also comply with the requirements of the Best Available Techniques ("BAT") and this means substantial capital expenses. In addition to general conditions relating to pollution emissions, the permits provide for quotas of gas or dust emissions to the air, permissible noise levels, requirements regarding water extraction, quantities of sewage and solid waste and define the general rules for waste generation and handling thereof.

Regulations with respect to environmental protection are subject to very frequent amendments. On 4 August 2014, the President of Poland signed an updated Act on Environmental Protection, which implements into Polish law the Industrial Emissions Directive, concerning limitations on industrial emissions. Adapting (upgrading) installations to the new requirements will necessitate substantial investment expenditures. The stricter emissions standards will be effective from January 1, 2016. On the European forum, revision BREF is in progress in order that will be legally binding after European Commission conclusion on BAT. Around year 2019 the emission norms imposed on energy generators resulting thereof may be subsequently tightened in relation to IED. Today the scale of the norms tightening cannot be determined due to the ongoing works in the European Union.

The European Commission is presently working on the amendment to the so-called framework directive and the Commission's Decision 2000/532/EC of 3 May 2000 establishing the list of hazardous waste. At present, some of the combustion by-products, including in particular slags, bottom ash and boiler combustion ash, are not classified as hazardous waste. Following the amendments they may be considered as such. Their amended status may have significantly adverse financial consequences for the operators concerned because of higher charges for waste storage, higher costs of rehabilitation of combustion by-products landfills and the ban on sales of combustion waste to external parties which, consequently, will compel operators to store all combustion by-products by themselves. In connection with the above, there may be a threat of lack of place for storage of combustion by-products and consequently this situation may threaten maintaining of generation units at stand-by.

More restrictive emission standards may force the PGE Group to incur substantial capital expenses in order to adapt to new requirements. At the same time, some of our facilities, landfill sites or installations may not be able to adapt to newly applicable requirements or will be able to adapt only with a delay causing negative impacts to our activities, financial results and situation or development prospects.

3.3 Risk factors connected with the operating activity of the PGE Capital Group

3.3.1 Risk of disruption of fuel supplies and insufficient stocks of fuel

The generation of electricity and heat by Group power plants and CHP plants depends on fuel supplies, including lignite, hard coal and gas. There is a risk of disruptions in fuel supplies to generating units, mainly for technical reasons (breakdown), natural reasons (calamities, difficult weather conditions), social reasons (strikes), economic and political reasons (limited supply of fuel or transport services and imposing unfavourable conditions of supply and transport) and other reasons. Any break or limitation in fuel supplies may cause a break or significant limitation in electricity or heat generation.

Moreover, the Energy Law obliges every electricity or heat generating enterprise to maintain a stock of fuel in an amount that can guarantee the continuity of electricity and heat supply. The ERO President imposes fines (of up to 15% of income) for the failure to maintain the required level of fuel stocks. The shortage of required level of fuel stocks may also result in the suspension or reduction of electricity or heat generation.

3.3.2 Risk connected with mining site rehabilitation expenses

Lignite mines belonging to PGE Group must rehabilitate sites where they carry out their mining works. The Geological and Mining Act, as well as implementing regulations thereto, obligate mining companies to make contributions to the mine liquidation fund constituting 10% of a maintenance fee. Such funds may be used only to cover costs of mine liquidation, including rehabilitation costs. It may happen that funds and reserves of mining companies allocated to such a purpose will not cover actual rehabilitation expenses that the companies will have to bear in future. This may result in a need to increase amounts payable to the rehabilitation fund, create other reserves, and finance site rehabilitation from external sources.

3.3.3 Risk connected with weather conditions

Weather conditions influence technical and economic conditions of energy and heat generation and distribution and create seasonable demand for energy. Such factors may cause limitations to energy generation, mainly as a result of water in basins that is used for cooling the generating units getting too hot or too low, as well as limitations to transmission capacities of the system. In addition, bad weather conditions, including in particular the force of wind in the case of wind farms and water surface in the case of water power plants, have a significant impact on energy production from renewable sources. While, large rains cause problems with the dehydration of opencast lignite mines. Extreme weather conditions break lines or damage electrical and power devices very often, which results in breaks of and limitations to power supply. It must be added that all the above phenomena are mostly unpredictable and in consequence may cause lowering of PGE Group income and claims by the off-takers for compensations or for discounts. Removal of damages in the grid is also connected with additional expenses relating to reconstruction of the damaged elements.

3.3.4 Risk relating to maintenance, repairs, modernisations and investments

PGE Group companies' activity in lignite mining and energy and heat generation and distribution requires regular maintenance, repairs and modernization of assets. Such actions should ensure that equipment's life is optimum and guarantee necessary availability of key assets, including cost minimisation.

Assets recovery and modernisation investments, as well as investments in new assets, are subject to substantial expenditure. A timely execution of the projects is vital for their profitability. Delays caused by lengthy procedures relating to the acquisition of administrative decisions and possible complaints being filed against them brings a risk of discontinuation of individual investment projects. At the same time, particular stages of works or of new investments may be delayed, for example, by uncertainty relating to the acquisition of sufficient financial resources, difficulties in the acquisition of necessary permits, obstructions in acquirement of land for new investments, protests of environmental organisations, strikes of employees, growth of projected investment costs, limited supply of investment goods and machinery, delays caused by contractors, bankruptcy of contractors or sub-contractors, accidents, unfavourable weather conditions or other unexpected difficulties. Above mentioned circumstances may have significant adverse effect on activity, results, financial standing of the Group or Group's development perspectives.

3.3.5 Risk of unsettled legal status of the real estates

In the case of many properties owned by the PGE Group, in particular those used by distribution system operator, there are doubts as to the legal title to use the properties. In past, there were some cases of investments, mainly ones related to lines, which were carried out in third party properties without express consent of owners of the said properties. Corresponding national legal regulations are not clear and judicature on cases relating to such situations has been changed in recent years. This situation is connected with a risk of claims to be filed against PGE Group companies, like in the case of distribution system operator. We may not exclude further cases of this type and related additional costs or even a need to stop using certain properties.

3.3.6 Risk relating to obtaining and cost of external financing (downgrade or withdrawal of the rating of PGE)

A part of the Group's activities is financed from external sources (bank loans, bonds, etc.). PGE S.A. and Group companies are parties to many financial agreements of the complex legal structure. It is possible that in future it will be difficult to obtain new finance at an amount and terms desired by the Group. This may be caused by still unstable situation in the financial and capital markets in Poland and abroad, poor general economic situation in Poland and abroad, or other reasons that are unpredictable now. Such circumstances may negatively affect the terms of financing, in particular may lead to the growth of costs of such financing (higher interest rates, commissions, etc.). Higher costs of financing may affect the Group's results.

PGE S.A. received positive evaluations from rating agencies confirming its high reliability connected with investment in its debt securities. Nonetheless, rating agencies may at any time downgrade or inform PGE S.A. of their intention to downgrade the rating. The rating agencies may also completely withdraw their ratings which may have the same consequences as a downgrade in PGE's ratings. Any decrease in PGE's rating may increase the costs of external financing, limit access to capital markets and adversely affect the capacity of PGE Group companies to sell their products or contract economic transaction, especially long-term ones. This may in turn decrease the liquidity of PGE S.A. and adversely affect the operating results and financial condition of PGE Group.

3.3.7 Risk associated with the decisions of the President of the Energy Regulatory Office regarding the implementation of LTC Act

The provisions of the LTC Act defining, in particular, terms for the calculation, payment and adjustments of funds to cover stranded costs, calculation and payment of such funds to generators coming within capital groups (including PGE Capital Group), tax consequences of LTC termination and fund payment, as well as other issues, are complicated and there is no defined practice for their application in Poland. Producers that terminated LTC and are authorised to receive funds to cover stranded costs, including PGE Group generation companies, in the case of the negative (annual or final) correction of stranded costs will be obliged to return funds received as result of the implementation of the LTC Act.

3.3.8 Risk of transfer prices

The Company and its subsidiaries have concluded, and continue to conclude, many transactions with the other PGE Group members. These transactions specifically relate to the sale of fuels, electricity, emission allowances, certificates of origin and certain services. Even though the Group carefully follows the arm's length principle in dealings with related parties, and even though they are implementing unified standards regarding the compiling of documentation and procedures in this regard, we cannot preclude potential disputes with the tax authorities in this regard.

3.3.9 Risk of insufficient insurance protection

The activity of the PGE Group is exposed to a number of risks connected with natural calamities, breakdowns and damages. The Group's business activity is also connected with third party liability towards third persons for personal injuries, property damages or so called pure financial loss. The Group maintains insurance policies covering only certain types of damages and there is a risk of insufficient insurance coverage. In addition, there are risks that are not subject to any insurance protection or in the case of which compensations, if any, are not likely to fulfil claims or loss. Consequences of such events will be charged to costs of particular Group companies, what may have a negative impact on their results.

3.3.10 Risk relating to court, arbitration and administrative proceedings and employees' claims

PGE S.A. and PGE Group companies are parties to court, arbitration or administrative proceedings that are important for the Group's activity. The Group takes up actions aiming at the settlement of such cases in favour of PGE Group companies, but there is a risk that they will be resolved unfavourably. There is also a risk that in future other proceedings will be initiated against PGE S.A. and other PGE Group companies, which will be resolved unfavourably for us, which may have an adverse impact on the Group's activity and financial results.

Legal proceedings involving the PGE Capital Group are, among others, related to the exchange ratio that had been fixed for the shares of the PGE Górnictwo i Energetyka S.A. exchanged for the shares of PGE S.A. within the consolidation process that took place in 2010. Former shareholders of PGE Górnictwo i Energetyka S.A. and the purchaser of the debt from former shareholders have filed a petition calling PGE S.A. for a pre-trial settlement with respect of the payment of damages for incorrectly set – as they claim – share exchange ratio. The total value of claims resulting from petitions for pre-trial settlements is approximately PLN 379 million.

PGE S.A. does not accept the above mentioned claims in connection with the calls for pre-trial settlements. The claims are unfounded and unsubstantiated. The value of the shares of companies subject to the consolidation process (mergers) was assessed independently. Plans of the companies merger, including the exchange ratio with respect to shares of the acquired company for the shares of the acquiring company were examined for accuracy and reliability by an expert appointed by the registration court; no irregularities were found. Then, an independent court registered the merger of the companies. Claimants filing motions to the courts did not prove on what grounds, in what way and on the basis of what kind of data or documents the claimed amounts had been calculated.

In the said cases, the PGE Polska Grupa Energetyczna S.A. refused to enter into pre-trial settlements. However, former shareholders and purchasers of debts from former shareholders may start legal actions to claim the payment of amounts that were claimed previously in the proceedings involving petitions for pre-trial settlements.

Another proceeding concerns claims raised by the city of Görlitz, connected with damages resulting from a flooding incident that took place on 7-10 August 2010. On November 30, 2012, PGE GiEK S.A. submitted a claim to establish the non-existence of liability for the damages caused by the above flooding event. However, if the claim raised by PGE GiEK S.A. is dismissed, there is a risk that the city of Görlitz will submit a claim for damages. In addition, PGE GiEK S.A. has received a payment demand for EUR 3.6 million, issued in writ-of-payment proceedings of January 16, 2014, which the company has appealed.

Over 100 company and inter-company trade unions are present in the PGE S.A. and PGE Group companies and more than 24 thousand employees are members thereof. Pursuant to the current provisions of law, trade unions influence the legislative process. They are also able to exert pressure on employers in a number of ways, including in the form of collective labour disputes. PGE Group companies are parties to a number of corporate and sector collective bargaining agreements. Furthermore, management boards of many Group companies have entered into social agreements with trade unions which confer considerable power upon employees and trade unions. The necessity to consult or co-ordinate certain actions with the trade unions may delay, or even render impossible, such actions and may lead to collective disputes, involving strikes or other labour protests. Furthermore, should any significant redundancy program be required in the PGE Group in the future, the obligation to make high severance payments to employees may delay or limit our ability to carry out such redundancy program or may increase its cost.

Risks relating to court, arbitration and administrative proceedings and employees' claim that are essential for the Group's activity are described in Note 21.4 to the consolidated financial statements.

3.3.11 Risk of asset impairment

Possibility of low energy prices in the long-term perspective may lead to to situation when impairment losses with respect to generation assets of the Group may need to be recognised. Description of impairments of assets in the first half of 2014 is presented in Note 12 to the consolidated financial statements.

3.4 Financial and market risks

During regular business activity, Group's operations, financial results and cash flows are exposed to various types of market and financial risks, including price risk, interest rate risk, foreign currency risk, liquidity risk and credit risk. Each risk could have a negative impact on business activities, financial standing and performance of operations.

3.4.1 Commodity price risk

Due to the nature of their operations the companies in the PGE Capital Group are exposed to cash flow and financial results volatility caused by changes in prices of the following risk items:

- Electricity;
- Hard coal;
- Natural gas;
- Biomass;
- CO_2 emission rights;
- Property rights to certificates of origin for electricity generated from renewable energy sources ("green certificates"), from cogeneration ("red/yellow certificates") or other property rights such as white and violet certificates.

The most significant risk factor concerns changes in the price of electricity. Electricity prices are affected by fundamental factors such as supply, demand and the prices of fuel and CO_2 emission allowances. Market risk factors are subject to continuous monitoring and analysis as part of the market risk management process. Sales of the electricity produced by PGE Group companies, as well as purchases for the end customers of PGE Group, are executed via futures contracts in order to secure predictable and stable financial results and in consideration of the futures market's limited liquidity. In limiting market risk, PGE Group uses natural hedging to the widest possible extent. The present stage of growth and the liquidity of the Polish power market allow securing the production and demand of PGE Group companies in futures contracts only to a limited degree. This results from a lack of reliable, long-term pricing indicators and a liquid market for financial instruments, particularly non-deliverable forwards. On top of this, pricing benchmarks from European and global markets are of limited use. These considerations also apply to certificates of origin and hard coal.

3.4.2 Interest rate risk

The companies of the PGE Group are exposed to interest rate risk since their operating and investing activities are financed from debt borrowed at a variable interest rate or through investments in financial assets remunerated at a floating or fixed interest rate. On the other hand, financing activities through debt borrowed at a fixed interest rate is associated with the risk of lost profits when interest rates fall.

The rates of floating rate financial instruments are updated in periods of time shorter than one year. Interests earned on financial instruments with a fixed interest rate are constant throughout the period preceding their maturity.

The Group is exposed to the risk of changes in the fair value of SWAP derivatives resulting from changes in interest rates.

3.4.3 Foreign exchange risk

The PGE Group companies are affected by two types of exposure to foreign exchange risk:

EXPOSURE TO TRANSACTION RISK

It stems from the fact that a part of the cash flows from the core business of the companies is denominated or indexed to foreign exchange rates. Furthermore, transaction risk is created as a result of using foreign currencies to capital investments and to finance operations. Due to changes in foreign exchange rates, the foreign exchange risk translates into the variability of future cash flows denominated/indexed in foreign currencies.

TRANSLATION EXPOSURE

It arises from converting balance sheet items denominated in foreign currencies into the currency of the financial statements of the Group, i.e. the Polish zloty. Similarly to the transaction exposure, a lack of assurance as to the level of future exchange rates to be applied in the conversion of data in the financial statements on the balance sheet day leads to uncertainty as to the value of the items in Polish zloty on the balance sheet day and related revenues and/or financial costs due to exchange rate differences shown in the total income statement.

Major elements which constitute sources of exposure to foreign exchange risk of the Group (both in transaction and translation aspect) are presented below:

- Capital expenses denominated/indexed to foreign exchange rates;
- Debt of the companies belonging to the Group and denominated in foreign currencies;
- Electricity sale transactions in exports denominated in foreign currencies;
- Electricity purchase transactions denominated in foreign currencies and electricity purchase transactions where part of the purchase price is indexed to the exchange rate;
- Fees for the purchase transmission capacity denominated/indexed to foreign exchange rates;
- Sale/ purchase of CO_2 emission rights denominated/indexed to foreign exchange rates;
- Hard-coal transactions denominated/indexed to foreign exchange rates;
- Expenses related to the current use of capital goods denominated/indexed to foreign exchange rates;
- Invested financial assets denominated in foreign currencies.

3.4.4 Liquidity risk

PGE Group companies run active cash investment policy. This means that they monitor their financial surplus, forecast future cash flows and carry out their investment strategy on the basis thereof.

A central financing process was introduced at the Group. As the Group's central entity, PGE S.A. is responsible for providing financing to Group entities for investment and on-going operating activities by raising external finance and re-distributing these funds within the Group. PGE Group companies are individually responsible for maintaining current liquidity, which is mainly done through intra-group instruments or overdraft facilities.

3.4.5 Credit Risk

The credit risk is related with potential credit defaults particularly such as a counterparty's insolvency, incomplete repayment or significant delay in the repayment of a debt or other default on contractual terms.

Companies of the PGE Group are exposed to credit risk arising in the following areas:

- Core business of the companies – sources of credit risk include transactions for the purchase or sale of electricity and other energy products and the uncertainty relating to fulfilment of the agreement by the contractor, both their financial liabilities towards PGE Group and non-financial liabilities for supply or off-take of the subject-matter of the agreement, what in case of uncompleted transaction creates necessity for concluding a substitute contract on current market conditions;
- Investing activities undertaken by the companies – the credit risk is generated by transactions within investment projects where successful completion is subject to the financial standing of the Group's suppliers;
- Financial operations of the companies, inter alia Investing the companies' available funds – the credit risk arises if available funds are invested by the companies of the PGE Group in financial instruments involving credit risk, i.e. financial instruments other than issued by the State Treasury.
- The following classes of financial instruments are vulnerable to credit risk exposure and have distinct credit risk characteristics:
    - Current and long-term deposits;
    - Acquired bonds, bills of exchange and other bonds;
    - Trade receivables;
    - Loans granted;
    - Other financial receivables;
    - Cash and cash equivalents;
    - Derivatives;
    - Granted guarantees.

The maximum exposure to credit risk related to financial assets of the Group is equal to the carrying values of these items.

The primary objective of credit risk management is to approve and control the credit risk at a level which is defined based on major business targets with respect to traded electricity and related products. The credit risk management of a counterparty in PGE S.A. and units belonging to the PGE Capital Group, which are exposed to losses to the largest extent because of a counterparty's credit risk, bases on policies and procedures adopted to this respect. In order to reduce a counterparty's credit risk, trading operations with customers (with regard to transactions exceeding materiality threshold) are subject to credit limits assigned on the basis of credit ratings. The standing of the counterparties that were issued credit limits is subject to periodic verification, taking into consideration the available quantitative and qualitative data. Customers displaying a weak financial standing may be required to provide a security. Securities with a high recovery rate are preferred. Payments from contractors and credit risk exposure in combination with credit limits and established collaterals are monitored on a regular basis. Recovery procedures and processes are applied in order to minimise losses related to untimely payments from a counterparty.

4 Other significant events of the reporting period and subsequent events

4.1 Changes in the Supervisory Board

On February 28, 2014, Ms. Małgorzata Dec, a Chairperson of the Supervisory Board, resigned from her position of the Chairman of the Supervisory Board and Member of the Supervisory Board.

On the same day the Extraordinary General Meeting adopted resolutions on determination of number of Supervisory Board members at 9 and on appointment of the following persons to the Supervisory Board:

Name and surname of the member of the Supervisory Board	Position
Barbara Dybek	Chairman of the Supervisory Board, appointed on February 28, 2014
Jarosław Gołębiewski	Supervisory Board Member, appointed on February 28, 2014
Małgorzata Molas	Supervisory Board Member, appointed on February 28, 2014
Krzysztof Trochimiuk	Supervisory Board Member, appointed on February 28, 2014
Piotr Machnikowski	Supervisory Board Member, appointed on February 28, 2014

As at the publication date of this report, the composition of the Supervisory Board is as follows:

Name and surname of the member of the Supervisory Board	Position
Barbara Dybek	Chairman of the Supervisory Board
Piotr Machnikowski	Vice-Chairman of the Supervisory Board - independent
Anna Kowalik	Secretary of the Supervisory Board
Małgorzata Mika – Bryska	Member of the Supervisory Board
Czesław Grzesiak	Supervisory Board Member - independent
Jarosław Gołębiewski	Member of the Supervisory Board
Małgorzata Molas	Member of the Supervisory Board
Krzysztof Trochimiuk	Member of the Supervisory Board
Jacek Barylski	Member of the Supervisory Board

In accordance with the Supervisory Board resolutions of March 12, 2014 the composition of the Committees of the Supervisory Board were also changed.

In accordance with the Supervisory Board resolution no 170/IX/2014, the Audit Committee consists of:

Name and surname	Position
Jarosław Gołębiewski	Chairman of the Committee
Barbara Dybek	Committee Member
Krzysztof Trochimiuk	Committee Member
Anna Kowalik	Committee Member

In accordance with the Supervisory Board resolution no 171/IX/2014, the Corporate Governance Committee consists of:

Name and surname	Position
Piotr Machnikowski*	Chairman of the Committee
Małgorzata Mika – Bryska	Committee Member
Jacek Barylski	Committee Member
Czesław Grzesiak	Committee Member

** on May 5, 2014 Mr Piotr Machnikowski was appointed a position of the Chairman of the Corporate Governance Committee*

In accordance with the Supervisory Board resolution no 172/IX/2014, the Strategy and Development Committee consists of:

Name and surname	Position
Małgorzata Mika – Bryska	Chairman of the Committee
Jarosław Gołębiewski	Committee Member
Czesław Grzesiak	Committee Member
Małgorzata Molas	Committee Member

In accordance with the Supervisory Board resolution no 173/IX/2014, the Appointment and Remuneration Committee consists of:

Name and surname	Position
Jacek Barylski	Chairman of the Committee
Czesław Grzesiak	Committee Member
Krzysztof Trochimiuk	Committee Member
Anna Kowalik	Committee Member

4.2 Establishment of Eurobonds program

On May 22, 2014 PGE Polska Grupa Energetyczna S.A. along with PGE Sweden AB (publ), 100% subsidiary of PGE, signed a documentation establishing Euro Medium Term Note Programme („Programme"). Under the Programme PGE Sweden may issue Eurobonds up to EUR 2,000,000,000 with a minimum maturity of 1 year.

On June 9, 2014 PGE Sweden AB (publ) issued Eurobonds with aggregate value of EUR 500 million ad maturity of 5 years. Afterwards, on June 10, 2014 PGE Sweden AB (publ) concluded with PGE S.A. three loan agreements with a total value of EUR 514 million. According to the repayment schedule loans were granted for 5 years. Value of the loans granted amounted to PLN 2,140 million as at the balance sheet date.

After the reporting period, on August 1, 2014 PGE Sweden AB (publ) issued bonds amounting to EUR 138 million maturity of 15 years.

4.3 Activities related to nuclear energy

Environmental and site characterization

On February 7, 2013 PGE EJ 1 sp. z o.o. signed an agreement with syndicate of WorleyParsons companies ("Contractor"). The subject-matter of the agreement is the environmental research, site characterisation and services connected with obtaining permits and rights which are necessary in the investment process. In March 2013 the Contractor received authorisation for commencement of the works with the indications for Choczewo and Żarnowiec localisations.

In the second quarter of 2014, the Contractor:

- Continued research and characterisation of the existing environmental conditions at both sites;
- Completed work on mobilising the necessary on-site resources for the purposes of field work under Phase I;

- Continued planning the field works under Phase I;
- Submitted applications for approval of geological work programmes for Phase I field work at both sites;
- Continued work on planning hydrological surveying at both sites;
- Completed construction of a meteorological tower at the Żarnowiec site;
- Submitted, and received approval for, the requirements matrix, proposed scope of the site characterisation report and a chapter in the preliminary safety report;
- Commenced work on a transition report concerning the existing environmental conditions at both sites;
- Continued drafting the project data sheet, together with a requirement matrix and the proposed scope of the environmental impact assessment report;
- Continued to draft a major disadvantage analysis for the Żarnowiec site as regards disassembly of the existing infrastructure and reclamation.

Selection of Owner's Engineer

On February 17, 2014, final tenders in the procurement procedure to provide owner's engineer services were opened. The tenders were submitted by:

- Exelon Generation Company, LLC;
- Consortium: URS Polska sp. z o.o., Tractebel Engineering S.A.;
- Consortium: Mott MacDonald Limited, AF-Consult Ltd.;
- AMEC Nuclear UK Ltd.

The tender committee finished analyses and evaluation of the offers. Company received appropriate corporate approvals necessary to announce information about the result of the tender and on July 7, 2014 company announced the selection of the offer of AMEC Nuclear UK Ltd.

Conclusion of the agreement with the selected Owner's Engineer is planned for the third quarter of 2014.

Grid analyses

Pursuant to a memorandum signed on November 28, 2012 between PSE S.A. and PGE Energia Jądrowa S.A., the parties' on-going cooperation resulted in the preparation of a procurement procedure to select a contractor for variant-based grid analyses, which was concluded on May 2013. An agreement with a consortium comprising PSE Innowacje sp. z o.o., Lublin University of Technology, Warsaw University of Technology - Electrical Power Engineering Institute and Biuro Studiów i Projektów Energetycznych Energoprojekt-Kraków S.A. was executed on July 9, 2013.

In accordance with the agreement, work under phase one has now been completed, which included analysis of National Power System requirements with regard to the safe and reliable withdrawal of capacity from a nuclear power plant connected to the Żarnowiec power station (Żarnowiec and Choczewo sites). The works were handed over on March 19, 2014. The analyses covered three variants of nuclear technology. The analysed technologies were selected so as to cover the full nuclear reactor capacity spectrum. The analyses resulted in the specification of essential investments aimed at strengthening the transmission system, together with a cost estimate.

Selection of technology, integrated proceeding

In 2012 a decision was taken on application of integrated tender proceeding, which covers key supplies and services for the nuclear project.

Currently the first phase of the proceeding – initial dialogue – is being executed. The completion of this phase of the proceeding will allow for elaboration of a full summary and the management boards of PGE S.A. and PGE EJ 1 sp. o.o. will be able to decide on the final shape, scope, approach and formula of integrated proceeding. The second phase of the procedure will be a competitive tender.

At the same time, work is on-going (with the intermediation of the Polish government) on obtaining the European Commission's approval for exclusion of the integrated procedure from the law on public tenders. In the near future, PGE EJ 1 Sp. z o.o. plans to draft the final version of the integrated procedure regulations and boundary conditions for all elements within the scope of the procedure. Also on-going are analyses concerning state support mechanisms, which may be crucial in terms of securing financing for the project.

Participation in legislative work

On January 28, 2014, Poland's cabinet adopted the Polish Nuclear Power Programme (PPEJ), as drafted by the Minister of the Economy. The PPEJ is a government document specifying the roles and scope of responsibilities of the institutions responsible for developing Poland's nuclear power programme, as well as issues surrounding nuclear safety and protection from radiation. The PPEJ also contains economic justification for the development of nuclear power in Poland, financing options and the means of managing spent nuclear fuel and radioactive waste. As per the document, the entity in charge of the investment to build Poland's first nuclear power plants is PGE Polska Grupa Energetyczna S.A. Operational management of the initial nuclear power plants will be assumed by a subsidiary/subsidiaries of PGE.

During the first half of 2014, legislative work was carried out at the Polish parliament (the Sejm) on a bill to amend the Nuclear Law and certain other acts. PGE EJ 1 Sp. z o.o. participated in consultations with regard to the above bill as carried out by the Polish government at public and inter-ministerial level. The bill was drafted in order to transpose into national regulations Council Directive 2011/70/EURATOM of July 19, 2011, establishing a Community framework for the responsible and safe management of spent fuel and radioactive waste (the Directive). The Directive imposes the obligation on Member States to establish national legislative, regulatory and organisational frameworks ensuring a high level of safety in the management of spent nuclear fuel and radioactive waste. The Directive reaffirms the ultimate responsibility of Member States to manage the spent fuel and radioactive waste generated in them. The Directive was adopted by the Sejm on April 4, 2014 and subsequently submitted to the Senate. The President of Republic of Poland signed this bill on May 8, 2014.

Educational and information activities

In the first half of 2014, communications activities concentrated primarily on dialogue with local communities concerning the presence of the environmental study contractor at potential nuclear power plant sites.

To this end, an exhibition of the planned site characterisation and environmental studies was organised with WorleyParsons in all three municipalities.

Local Information Points (LPIs), operating in the municipalities where the potential sites are located, are carrying out informational initiatives for residents and tourists and are organising educational trips for children and youth.

Business partnership

On January 28, 2014, Poland's cabinet adopted the Polish nuclear power programme. Its adoption of the Programme was one of the conditions precedent for the conclusion of a partners' agreement between PGE S.A., KGHM Polska Miedź S.A., Tauron Polska Energia S.A. and ENEA S.A. (later jointly "Parties") A second condition precedent is the acquisition of the legally required approval of the President of the Polish Office for Competition and Consumer Protection (UOKiK) regarding the proposed concentration.

The Partners' Agreement was initialled on September 23, 2013 as a result of works concerning implementation of a draft purchase agreement with regard to shares in special purpose company for construction and operating of the nuclear power plant. In this way parties jointly declared that the initialled document constitutes a draft of a future Partner's Agreement, which will be signed if necessary corporate approvals are obtained by all parties.

The Partner's Agreement will obligate its Parties to conclude the purchase agreement with regard to shares in PGE EJ 1 sp. z o.o. – a special purpose company for construction and operating of the nuclear power plant. According to the Partners' Agreement, PGE shall sell for the benefit of other parties 30% of the share capital of PGE EJ 1 sp. z o.o. As a consequence:

- PGE S.A. will hold 70% in the share capital of PGE EJ 1 sp. z o.o.
- KGHM Polska Miedź S.A. will hold 10% in the share capital of PGE EJ 1 sp. z o.o.

- Tauron Polska Energia S.A. will hold 10% in the share capital of PGE EJ 1 sp. z o.o.
- ENEA S.A. will hold 10% in the share capital of PGE EJ 1 sp. z o.o.

On August 1, 2014, the Parties filed a request for concentration approval from Poland's Office for Competition and Consumer Protection (UOKiK) concerning PGE S.A.'s planned sale of shares in PGE EJ 1 sp. z o.o. to KGHM Polska Miedź S.A., Tauron Polska Energia S.A. and Enea S.A.

4.4 Legal aspects

Information about the petition for annulment of the resolutions of the Extraordinary General Meeting of PGE S.A. of February 6, 2014.

On April 1, 2014 the Company received a copy of petition filed by one of the shareholders with the Regional Court in Warsaw. The shareholder files for annulment of resolutions no 1, 2 and 4 of the Extraordinary General Meeting of February 6, 2014.

The Company filed a reply to the petition.

4.5 Description of material agreements

Conclusion of an agreement for establishment by PKO BP of a guarantee limit for PGE GiEK. Fulfilment of material agreement criteria.

On January 20, 2014 PGE S.A. and PGE GiEK S.A. concluded an agreement with Powszechna Kasa Oszczędności Bank Polski S.A. („PKO BP"). Subject matter of the Agreement is the establishment by PKO BP of a guarantee limit for PGE GiEK S.A. to a maximum value of PLN 2,548,607,358. The beneficiary of the guarantee will be the general contractor of works associated with the construction of power units No. 5 and 6 in Opole Power Plant.

The Agreement provides for the award on behalf of PGE GiEK S.A.:

- guarantee of payment to a maximum value of PLN 1,300,309,875 (PGE GiEK was obliged to submit to the general contractor of units 5 and 6 at the Opole power plant guarantees of payment representing 15% of the total price of the construction of units - a guarantee from PKO BP fulfilled 75% of the obligation, the remaining amount of the payment guarantee has been provided through arrangements with other banks);
- guarantee of payment for construction works up to 100% of the guarantee line.

The Agreement is valid for a period of 67 months from the date of its conclusion.

The agreement provides securities in form of:

- a guarantee by PGE to 120% of the current amount of the guarantee;
- a statement of execution by PGE GiEK S.A. (up to 120% of the guarantee limit) and a statement of execution by PGE, as a guarantor (up to 120% of the current amount of the guarantee);
- a statement of execution by PGE S.A., as a guarantor (up to 120% of the current amount of the guarantee).

The agreement does not provide for contractual penalties.

During the 12 months preceding the conclusion of the above agreement, PGE S.A. and its subsidiaries concluded a number of agreements with PKO BP, that jointly met the criteria of a material agreement. The aggregate value of the mentioned agreements amounted to approximately PLN 3.1 billion. The agreements were considered as material, since their aggregate value exceeded value of 10% of PGE's equity.

Conclusion of agreements for guarantee lines and guarantees for Opole II Project

On January 20, 2014 three agreements between PGE GiEK S.A., PGE S.A. and each of the banks mentioned below (jointly "Banks" and separately as "Bank") were concluded:

- Powszechna Kasa Oszczędności Bank Polski S.A. with its seat in Warsaw;
- Bank Polska Kasa Opieki S.A. with its seat in Warsaw;
- BNP Paribas Bank Polska S.A. with its seat in Warsaw.

The agreements provide three guarantee limits for the aggregate amount of PLN 3,398,143,144, under which PGE GiEK S.A. is entitled to order bank guarantees of payments. The beneficiary of the guarantees will be the general contractor of works associated with the construction of power units No. 5 and 6 in Opole Power Plant.

Table: Guarantee lines for the Opole II Project.

Bank	Date of the agreement (yyyy-mm-dd)	Agreement maturity date (yyyy-mm-dd)	Available guarantee limit in PLN as at the agreement date	Available guarantee limit in PLN as at June 30, 2014
Powszechna Kasa Oszczędności Bank Polski S.A.	2014-01-20	2019-08-20	2,548,607,358	2,392,570,173.00
Bank Polska Kasa Opieki S.A.	2014-01-20	2019-08-20	424,767,893	398,761,695.50
BNP Paribas Bank Polska S.A	2014-01-20	2019-08-20	424,767,893	398,761,695.50
TOTAL			**3,398,143,144**	**3,190,093,564.00**

The agreement provides for security in form of a guarantee by PGE to 120% of the current amount of the guarantee by the Banks.

In connection with the establishing on January 29, 2014 of three guarantees by the Banks for the general contractor for the total amount of PLN 1,733,746,500, PGE S.A. issued guarantees on the terms presented below.

Table: Guarantees issued for the Opole II Project.

Guarantor	Type of security	Security for	Beneficiary of the guarantee	Guarantee issued for the liability of	Issue date	Guarantee period		Total value of the guaranteed instrument as at June 30, 2014 in PLN	Value of the guarantee as at June 30, 2014 in PLN
						from	to		
PGE S.A.	Guarantee	bank guarantee of payment	Bank Polska Kasa Opieki S.A.	PGE GiEK S.A.	2014-01-22	2014-01-29	2020-03-31	216.718.312.5	260.061.975
PGE S.A.	Guarantee	bank guarantee of payment	Powszechna Kasa Oszczędności Bank Polski S.A.	PGE GiEK S.A.	2014-01-22	2014-01-29	2020-03-31	1.300.309.875.0	1.560.371.850
PGE S.A.	Guarantee	bank guarantee of payment	BNP Paribas Bank Polska S.A.	PGE GiEK S.A.	2014-01-22	2014-01-29	2020-03-31	216.718.312.5	260.061.975
								1.733.746.500.0	**2.080.495.800**

Conclusion of agreement for designing and construction of a power unit in PGE GiEK S.A. Branch Elektrownia Turów

On July 10, 2014 PGE Górnictwo i Energetyka Konwencjonalna S.A. („PGE GiEK S.A.") concluded an agreement („Agreement") with syndicate of companies: Mitsubishi Hitachi Power Systems Europe GmbH (leader), Budimex S.A. and Tecnicas Reunidas S.A. (later referred to as the „Contractor").

Subject matter of the Agreement is designing and turn-key construction of 450 MWe supercrititcal power unit with steam dust boiler in PGE GiEK S.A. Branch Elektrownia Turów. New unit will be CCS Ready.

The construction of the new unit will be finished within 56 months from the date of the Notice To Proceed ("NTP") issued by PGE GiEK S.A. The net value of the Agreement amounts to PLN 3,250,000,000 PLN, while gross value of the Agreement as at the Agreement signing date amounts to PLN 3,997,500,000.

The aggregate amount of the contractual penalties to be paid by the Contractor due to delay and due to breach of specific technical parameters amounts to 25% of the Agreement's net value, wherein the maximum total amount of contractual penalties payable by the Contractor for the delay is 10% of the Agreement's net value while the maximum total amount of contractual penalties payable by the Contractor for breach of specific technical parameters is 15% of the Agreement's net value. PGE GiEK S.A. entitlement to receiving the contractual penalty from the Contractor, as a rule precludes PGE GiEK S.A. from seeking compensation exceeding maximum value of contractual penalty. However, the Agreement allows PGE GiEK S.A. to seek compensation claims on general basis, shall certain conditions stipulated in the Agreement be fulfilled.

After signing of the Agreement, parties amended the Agreement with Annex 1 providing for risks limitation for the parties (time for issue of NTP prolonged to December 31, 2014) connected with the potential complaint to the District Court by other bidders participating in the tender.

4.6 Decisions of the President of the Energy Regulatory Office related to realisation of LTC Act

Some generating entities, currently branches of PGE GiEK S.A., became entitled to receive funds to cover stranded costs (so-called "LTC compensation") pursuant to the Act of June 29, 2007 on the Rules of Coverage of Costs Occurring at Production Plants as a Consequence of Early Termination of Long-Term Power and Electricity Sales Contracts (Journal of Laws No. 130, item 905, of 2007) (the "LTC Act"). The LTC Act is ambiguous in many points and raise important questions of interpretation. The calculation of the estimated results of each entity and resulting compensations, annual adjustments of stranded costs and final adjustments as well as resulting revenues recognized in the statement of comprehensive income was performed by the Group with the best of its knowledge in this area and with support of external experts.

In the previous years entitled producers from PGE Group received decisions on annual adjustments of stranded costs and costs related to natural gas fired entities for 2008-2012. The majority of these decisions were disadvantageous for the particular entities and the Group believes that they were issued in violation of the Long-Term Contracts Act. As a consequence, since 2009, a number of proceedings have been pending before the Regional Court in Warsaw - Competition and Consumer Protection Court ("CCP Court") and before the Court of Appeal concerning appeals by PGE Group producers against the Decision of the President of the Energy Regulatory Office. These proceedings are currently at various levels of advancement.

In the first half of 2014 new, favourable for the Group, final and binding verdicts were issued in cases regarding the appeals against the decisions of the President of the Energy Regulatory Office concerning annual adjustments of stranded costs: for PGE GiEK S.A. Branch Elektrociepłownia Rzeszów for year 2009, PGE GiEK S.A. Branch Elektrownia Opole for year 2009 and for PGE GiEK S.A. for year 2010. Claim value in the above cases amounted to PLN 680 million.

On August 11, 2014 PGE GiEK S.A. received administrative decision of the ERO President concerning the annual adjustment of the stranded costs for the year 2013. According to the decision of ERO President annual adjustment of the stranded costs generated in branches Elektrownia Turów and Elektrownia Opole for the year 2013 amounts to app. PLN (+)438 million. PGE does not dispute this amount.

On August 14, 2014 the Court of Competition and Consumer Protection (the "CCCP") issued verdict which in part allowed the appeal of PGE GiEK S.A. and changed the decision of the President of Energy Regulatory Office from July 2011 regarding the settlement value of annual adjustment of the stranded costs for 2010 for PGE GiEK S.A. Branch Elektrownia Opole. According to the CCCP verdict value of annual adjustment of the stranded costs for 2010 for PGE GiEK S.A. Branch Elektrownia Opole plus interest was determined at approx. (-) PLN 50 million.

Impact on the financial statements for the first half of 2014

In the financial statements for the period ended June 30, 2014 the Group recognised the LTC compensations in amount of PLN 1,162 million in sales revenues. Within this amount, approx. PLN 911 million is a result of re-calculation of the LTC compensations model what was caused by change of assumptions applied for calculation of the so called final adjustment (primarily change of the discount rate). Change in assumptions stems from the information about the ERO President decision regarding the final adjustment for one of the generators subject to the compensations scheme.

Moreover, verdicts of the Court of Appeal in cases of PGE GiEK S.A. Branch Elektrownia Opole, PGE GiEK S.A. Branch Elektrociepłownia Rzeszów and PGE GiEK S.A. resulted in an adjustment of LTC compensations settlements in amount of PLN 246 million in the financial statements for the period ended June 30, 2014. Value of adjustment was recognized in other operating revenues in the statement of the comprehensive income.

Claim value in all cases related to years 2008 – 2012 amounts to PLN 1,660 million, including claim value in cases with favourable verdicts of the Court of Appeal and favourable final and binding verdict of the CCP Court - PLN 1,422 million.

The decision of the ERO President regarding annual adjustment of LTC compensations for year 2013 and the verdict of CCP Court of August 14, 2014 will not affect the reported revenues and profits of the PGE Capital Group in 2014.

4.7 Description of the organization of the PGE Capital Group

Companies comprising the main business segments of PGE Group as at June 30, 2014:

Segment		Company
CONVENTIONAL GENERATION	1.	PGE Górnictwo i Energetyka Konwencjonalna S.A.
	2.	Przedsiębiorstwo Energetyki Cieplnej sp. z o.o.
RENEWABLE ENERGY	3.	PGE Energia Odnawialna S.A.
	4.	Bio-Energia S.A.
	5.	Pelplin sp. z o.o.
	6.	Żuromin sp. z o.o.
	7.	Elektrownia Wiatrowa Baltica-1 sp. z o.o.
	8.	Elektrownia Wiatrowa Baltica-2 sp. z o.o.
	9.	Elektrownia Wiatrowa Baltica-3 sp. z o.o.
	10.	Eolica Wojciechowo sp. z o.o.
	11.	PGE Energia Natury S.A.
	12.	PGE Energia Natury sp. z o.o.
	13.	PGE Energia Natury Karnice sp. z o.o.
	14.	PGE Energia Natury Bukowo sp. z o.o.
	15.	PGE Energia Natury Omikron sp. z o.o.
	16.	PGE Energia Natury Kappa sp. z o.o.
	17.	PGE Energia Natury PEW sp. z o.o.
	18.	PGE Energia Natury Olecko sp. z o.o.
WHOLESALE TRADING	19.	PGE Polska Grupa Energetyczna S.A.
	20.	PGE Dom Maklerski S.A.
	21.	PGE Trading GmbH
DISTRIBUTION	22.	PGE Dystrybucja S.A.
RETAIL SALES	23.	PGE Obrót S.A.

4.7.1 Changes in organisation of the Capital Group

4.7.1.1 Changes in organisation of the Capital Group in the first half of 2014

The changes, which occurred in the Group's structure during the first half of 2014, are presented in Note 3 to consolidated financial statements and described below.

Shares in subsidiaries and associates

In the first half of 2014 PGE S.A. changed its equity interest in the following entities:

- On February 14, 2014, the Extraordinary General Meeting of PGE Dom Maklerski S.A. adopted a resolution on an increase of the company's share capital from PLN 16,500,000 to PLN 36,500,000, i.e. by PLN 20,000,000, through the issue of 20,000 new registered shares with a nominal value and issue price of PLN 1,000 each. All of the shares in the increased capital were acquired by PGE Polska Grupa Energetyczna S.A. in exchange for a cash contribution. On April 16, 2014, the share capital increase was registered with the National Court Register.
- On March 19, 2014, an agreement was executed in Sundsvall, Sweden, between Bolagsrätt Sundsvall AB and PGE Polska Grupa Energetyczna S.A. concerning the sale of shares in Stockholm-based Goldcup 5812 AB (publ.). Pursuant to the share sale agreement, PGE Polska Grupa Energetyczna S.A. purchased 500,000 shares in Goldcup 5812 AB

(publ.), constituting 100% of its share capital. PGE Polska Grupa Energetyczna S.A. paid for the shares on April 8, 2014. Currently, Goldcup 5812 AB (publ.) is operating as PGE Sweden AB (publ).

- On April 10, 2014, the Extraordinary General Meeting of PGE EJ 1 Sp. z o.o. adopted a resolution concerning a mandatory cash contribution by the sole shareholder, PGE Polska Grupa Energetyczna S.A., in the amount of PLN 15,000,000, which constitutes 20.55% of the nominal value of the shares held by PGE Polska Grupa Energetyczna S.A. The contribution was made on April 11, 2014.
- On May 16, 2014 the Extraordinary General Meeting of PGE Sweden AB (publ) adopted a resolution on an increase of the company's share capital from SEK 500,000 to SEK 191,000,000, i.e. by SEK 190,500,000, through the issue of 190,500,000 new shares with a nominal value and issue price of SEK 1 each. All of the shares in the increased capital were acquired by PGE Polska Grupa Energetyczna S.A. in exchange for a cash contribution. On June 10, 2014, the share capital increase was registered with the Swedish Companies Register.

In period January 1, 2014 – June 30, 2014 PGE Polska Grupa Energetyczna S.A. purchased from minority shareholders – on ground of share sale agreements - a total of 4,238,381 shares of PGE GiEK S.A. (constituting 0.61% in the share capital of PGE GiEK S.A.). As at June 30, 2014 PGE Polska Grupa Energetyczna S.A. directly held 94.23% and indirectly through PGE Obrót S.A. 4.95% of shares in the share capital of PGE GiEK S.A. (share including treasury shares held by PGE GiEK S.A.)

In the first half of 2014 PGE Group companies changed their capital exposure in the following entities:

Transformation of companies in Renewable Energy segment

On January 10, 2014 Extraordinary Assembly of Partners of EPW Energia Olecko sp. z o.o. (PGE held 81% of shares and ENERGA Wytwarzanie sp. z o.o. held 19% of shares in the share capital) adopted a resolution on the division of the EPW Energia Olecko sp. z o.o. (division by separation) by transferring a part of assets of EPW Energia Olecko sp. z o.o., constituting the organized part of the enterprise operating as a branch under the name EPW Energia Olecko sp. z o.o. branch in Kętrzyn, to the existing company, i.e. EPW 1 sp. z o.o. with a seat in a Pruszcz Gdański (subsidiary of ENERGA Wytwarzanie sp. z o.o. belonging to the Energa S.A. Capital Group). In connection with the division by separation, the share capital of the company was decreased by an amount of PLN 380,000, i.e. from PLN 2,000,000 to PLN 1,620,000, and the number of shares was reduced by 380 shares, with a nominal value of PLN 1,000 each, attributable to ENERGA Wytwarzanie sp. z o.o., that are subject to conversion for 250 new shares of EPW 1 sp. z o.o. in the increased share capital of that company.

On February 7, 2014 the decrease of the share capital of EPW Energia Olecko sp. z o.o. was registered by the court and the information about division by separation was entered into the register.

On February 11, 2014 the court registered the increase of the share capital of EPW 1 sp. z o.o., the company which acquires part of the assets of EPW Energia Olecko sp. z o.o., thus completing the process of division of EPW Energia Olecko sp. z o.o. As a result of above separation, PGE S.A. became the sole partner in EPW Energia Olecko Sp. z o.o.

On March 25, 2014 the name of company EPW Energia Olecko sp. z o.o. was changed to PGE Energia Natury Olecko sp. z o.o.

On January 10, 2014 the Extraordinary Assembly of Partners of EPW Energia sp. z o.o. (PGE held 32.7% of shares and ENERGA Wytwarzanie sp. z o.o. held 67.3% of shares in the share capital) adopted a resolution on the division of the EPW Energia sp. z o.o. (division by separation) by transferring two parts of its assets constituting the organized part of the enterprise as:

- branches under the name: EPW Energia sp. z o.o. Branch „Kisielice/Malbork" Wracławek and EPW Energia sp. z o.o. Branch „Galicja" Orzechowce to PGE Energia Natury sp. z o.o.
- branch under the name: EPW Energia sp. z o.o. Oddział „Pipeline" Pruszcz Gdański to EPW Parsówek sp. z o.o. with seat in Pruszcz Gdański (a subsidiary of ENERGA Wytwarzanie sp. z o.o. belonging to the Energa S.A. Capital Group).

In connection with the division, the company's share capital was reduced by the amount of PLN 337,174,000, i.e. from PLN 894,376,000 to PLN 557,202,000 and the number of shares has been reduced by 337,174 shares with a nominal value of PLN 1000 per share, attributable in amount of 44,713 shares to partner ENERGA Wytwarzanie sp. z o.o., which can be exchanged for 18,000 shares of EPW Parsówek sp. z o.o. and in the number of 292,461 shares for PGE S.A., that are subject to conversion for 331,921 shares of PGE Energia Natury sp. z o.o.

In connection with the above, Extraordinary Assemblies of Partners of EPW Parsówek sp. z o.o. and PGE Energia Natury sp. z o.o. were held on January 10, 2014 with regard to the increase of the share capital of these companies respectively by PLN 18,000,000 and by PLN 331,921,000. The new shares in the increased share capital of PGE Energia Natury sp. z o.o. were allotted to PGE S.A. and new shares of EPW Parsówek sp. z o.o were allotted to ENERGA Wytwarzanie sp. z o.o.

On February 4, 2014 the court registered the increase of the share capital of the company acquiring one part of the assets of EPW Energia sp. z o.o., i.e. EPW Parsówek sp. z o.o.

On February 10, 2014 the court registered the decrease in the share capital of EPW Energia sp. z o.o. and entered into the register information regarding the division by separation.

On February 28, 2014 the court registered the increase of the share capital of the company that acquired second part of assets of EPW Energia sp. z o.o., i.e. of PGE Energia Natury sp. z o.o. Entry of the increase of the share capital into the National Court Register completed the division process of EPW Energia sp. z o.o. As a result of the above division, ENERGA Wytwarzanie sp. z o.o. became the sole partner in EPW Energia sp. z o.o.

Other changes

On October 14, 2013, the Extraordinary Assembly of Partners of Niezależny Operator Międzystrefowy Sp. z o.o. adopted a resolution on a share capital decrease through a voluntary redemption in exchange for remuneration paid to the sole partner, i.e. EXATEL S.A. The share capital was decreased from PLN 30,000,000 to PLN 22,500,000, i.e. by PLN 7,500,000, through the redemption of 7,500 shares with a nominal value of PLN 100 each. On March 6, 2014, the share capital decrease was registered with the National Court Register.

On April 15, 2014, an agreement was executed between PGE Obrót S.A. and Przedsiębiorstwo Energetyczne "ESV" S.A., based in Siechnice, concerning the sale of 600 shares in Energetyka Wisłosan Sp. z o.o., held by PGE Obrót S.A., which constituted 19.65% of the company's share capital. On April 25, 2014, Przedsiębiorstwo Energetyczne "ESV" S.A. made payment for the shares, and ownership of the shares was transferred.

During the period from January 1, 2014 to June 30, 2014, PGE Górnictwo i Energetyka Konwencjonalna S.A., through a squeeze-out of shares pursuant to art. 418^1 § 4 of the Polish Commercial Companies Code, purchased a total of 623,402 treasury shares from minority shareholders, constituting 0.09% of PGE GiEK S.A.'s share capital.

In the first half of 2014 PGE Capital Group did not discontinue any of its substantial operations.

4.7.1.2 Changes in Group structure after the end of the reporting period

On March 5, 2014, the Extraordinary General Meeting of ELBIS Sp. z o.o. adopted a resolution on a share capital decrease through a voluntary redemption for a fee, issued to the sole shareholder, i.e. PGE GiEK S.A. The share capital will be decreased from PLN 46,070,000 to PLN 6,449,800, i.e. by PLN 39,620,200. The change in share capital will be carried out via a reduction in the nominal value from PLN 1,000 to PLN 140, i.e. by PLN 860 per share. The reduction of nominal value covers all 46,070 shares held by PGE GiEK S.A. On August 21, 2014 the decrease of the share capital was registered with the National Court Register.

On July 15, 2014 PGE Polska Grupa Energetyczna S.A. set up 14 special purpose companies in form of limited companies with the following names: PGE Inwest 2 sp. z o.o., PGE Inwest 3 sp. z o.o., PGE Inwest 4 sp. z o.o., PGE Inwest 5 sp. z o.o., PGE Inwest 6 sp. z o.o., PGE Inwest 7 sp. z o.o., PGE Inwest 8 sp. z o.o., PGE Inwest 9 sp. z o.o., PGE Inwest 10 sp. z o.o., PGE Inwest 11 sp. z o.o., PGE Inwest 12 sp. z o.o., PGE Inwest 13 sp. z o.o., PGE Inwest 14 sp. z o.o. and PGE Inwest 15 sp. z o.o., with a share capital of PLN 10,000 each. PGE Inwest 2 sp. z o.o., PGE Inwest 5 sp. z o.o. and PGE Inwest 12 sp. z o.o. were registered in the National Court Register on August 19, 2014 and PGE Inwest 15 sp. z o.o. was registered on August 21, 2014.

On August 22, 2014 Zakład Obsługi Energetyki sp. z o.o. was sold. As a result PGE Capital Group earned profit in amount of more than PLN 5 million.

5 Shareholders holding directly or indirectly by subsidiaries at least 5% of the total votes at Company's General Meeting as at the date of the half-year report

According to the information held by the Company*, the sole shareholder holding at least 5% of the total number of votes is the State Treasury, which holds 1,091,681,706 shares of the Company, what constitutes 58.39% of the share capital of the Company and entitles to exercise the same amount of the votes at the General Meeting of the Company.

Table: Shareholders holding directly or indirectly by subsidiaries at least 5% of the total votes at the General Meeting o PGE Polska Grupa Energetyczna S.A.

Shareholder	Number of shares	Number of votes	% in total votes on General Meeting
State Treasury	1,091,681,706	1,091,681,706	58.39%
Others	778,079,123	778,079,123	41.61%
TOTAL	**1,869,760,829**	**1,869,760,829**	**100.00%**

** According to the notification from the Minister of State Treasury of July 8, 2014, about which PGE S.A. informed in current report no 35/2014 dated July 9, 2014*

6 Number of shares or rights to shares of the Company held by Company's managers and supervisors, as of the date of submission of the half-year report

According to the best knowledge of the Management Board of PGE S.A., as of the date of submission of this consolidated half-year report and as of the date of publishing of the consolidated report for the first quarter of 2014 Company's managers and supervisors held following number of shares:

Shareholder	Number of shares as of publication date of the quarterly report for Q1 2014 (i.e. May 14, 2014)	Change in number of owned shares	Number of shares as of submission date of this report	Nominal value of shares as of submission date of this report (PLN)
Management Board	**350**	**no change**	**350**	**3,500**
Grzegorz Krystek	350	no change	350	3,500
Supervisory Board	**873**	**no change**	**873**	**8,730**
Krzysztof Trochimiuk	873	no change	873	8,730

Other members of the Management Board and of the Supervisory Board did not hold shares.

7 Information on issue, redemption and repayment of debt securities and other securities

Information on issue, redemption and repayment of debt securities and other securities were described in Note 22 to the consolidated financial statements and p. 4.7.1. of the foregoing report.

8 Information on granting by the Company or its subsidiary of loan securities or guarantees – jointly to a single entity or its subsidiary, if the total value of the existing securities or guarantees is equivalent to at least 10% of Company's equity

In connection with the establishment of the EMTN Programme (see p. 4.2. of the foregoing report), on May 22, 2014 a Deed of Guarantee was concluded for issue of guarantee by PGE for the liabilities of PGE Sweden AB (publ). Guarantee amounts to EUR 2.5 billion and refers to liabilities of PGE Sweden AB (publ) arising from the issue of the Eurobonds under the EMTN Programme up to EUR 2.0 billion. Guarantee will be valid until December 31, 2041. Financial terms of the guarantee will depend on the terms of Eurobonds issued by PGE Sweden AB (publ) and the remuneration for the guarantee will be reflected in the interest rates applied to loans granted to PGE S.A.

9 Information concerning proceedings in front of court, body appropriate for arbitration proceedings or in front of public administration authorities

As at June 30, 2014 PGE S.A. and its subsidiaries were not a party of any proceedings concerning payables or debts whose total value would constitute at least 10% of the Company's equity, except for applications filed by generators from PGE Group to confirm excise tax overpayment and tax return together with interest for the years 2006-2008 and the first two months of 2009. Total overpaid tax to be returned to the PGE Group companies may amount to approximately PLN 3.4 billion, excluding interest (the generators are entitled to interest on overpaid excise tax, accrued from the date of payment of the overstated tax). PGE Group entities are convinced of the merits of the claim, however taking into account the current practice of the tax authorities and court verdicts, refund of overpaid tax should be considered unlikely. Significant proceedings pending in front of courts, competent arbitration authority or public administration authority are described in Note 21.4 to the consolidated financial statements.

10 Statements of the Management Board

10.1 Statement on the reliable preparation of the financial statements

To the best knowledge of the Management Board of PGE Polska Grupa Energetyczna S.A., the half-year consolidated and stand-alone financial statements and comparable data were prepared in accordance with the governing accounting principles, present a fair, true and reliable view of the material and financial situation of PGE S.A. and PGE Capital Group and its financial result.

The report of the Management Board on the activities of PGE Capital Group presents a true view of the development, achievements and situation of the Capital Group.

10.2 Statement on the entity authorised to audit the financial statements

The Management Board of PGE Polska Grupa Energetyczna S.A. declares that the entity authorised to audit the financial statements, that reviews the interim consolidated and stand-alone financial statements, has been appointed in accordance with provisions of the law. The entity and the statutory auditors fulfilled all the requirements for issuing an unbiased and independent report on the review, in accordance with the governing provisions and professional standards.

Warsaw, August 26, 2014

Signatures of Members of the Management Board of PGE Polska Grupa Energetyczna S.A.

Marek Woszczyk

President of the Management Board

Jacek Drozd	*Grzegorz Krystek*	*Dariusz Marzec*
Vice-President of the Management Board	*Vice-President of the Management Board*	*Vice-President of the Management Board*