

**Management Board's report on  
activities of the Capital Group of  
PGE Polska Grupa Energetyczna S.A.  
for the 3-month and 9-month period**

**ended September 30, 2014**

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## 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 Program of first Polish nuclear power plant 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 CO<sub>2</sub> 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;

### Regulatory environment

- Domestic:
  - Implementation and possible changes to the Poland's energy policy;
  - Changes in scope of services like:
    - 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 ("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 CO<sub>2</sub> 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;

- Matter of implementation of quality tariff in distribution, that will make regulated income dependant on SAIDI and SAIFI ratios;
- 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 EU climate summit decisions from October 2014 particularly: at least 40% CO<sub>2</sub> reduction targets, 27% RES share target, 27% efficiency improvement target; , possibility of granting free CO<sub>2</sub> allowances for energy sector (so called derogations), possible allocation of funds for energy sector modernization;
  - revision of BAT (Best Available Techniques) – uncertainty with regard to future norms of SO<sub>2</sub>, NO<sub>x</sub>, dust and new pollutions (including mercury) emissions from 2020;
  - draft NEC Directive with regard to national limits of emissions of pollution to the atmosphere 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:

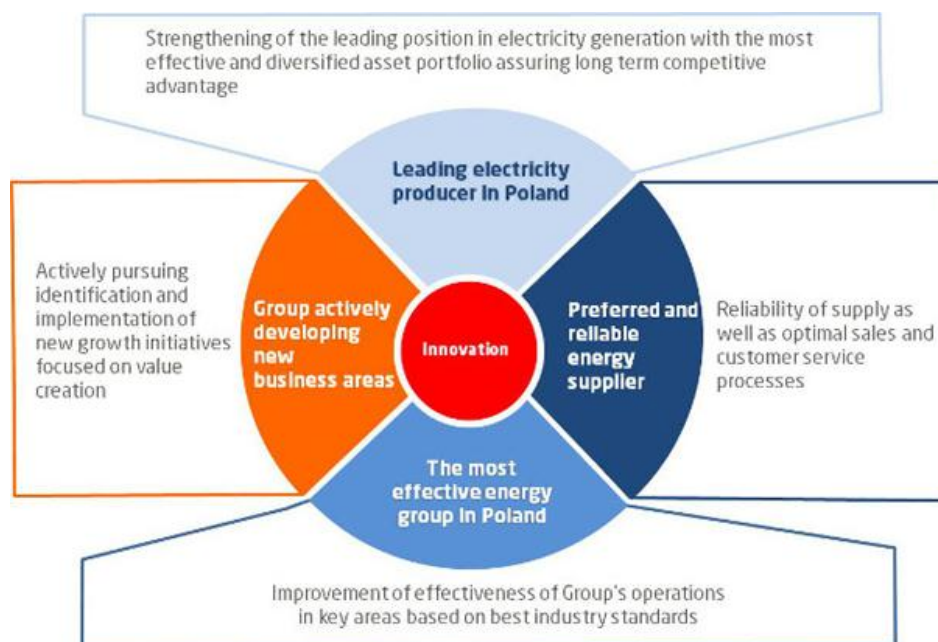
- PGE is the largest vertically integrated power utility in Poland with regard to energy production and installed capacity;
- PGE is leading in the cost efficient, base-load generation technologies in Poland and has the youngest generation asset base.

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 consolidated net profit in 2015-2020 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. Żłoczew 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<sup>1</sup> 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).

#### **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 consolidated net profit as of 2015 on R&D activities with maximization of external financing.

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<sup>1</sup> SAIDI - System Average Interruption Duration Index – minutes lost; unplanned electricity outages (excluding catastrophic events)

## 2 Activity of the PGE Capital Group

### 2.1 Factors and events affecting results

#### 2.1.1 Macroeconomic situation

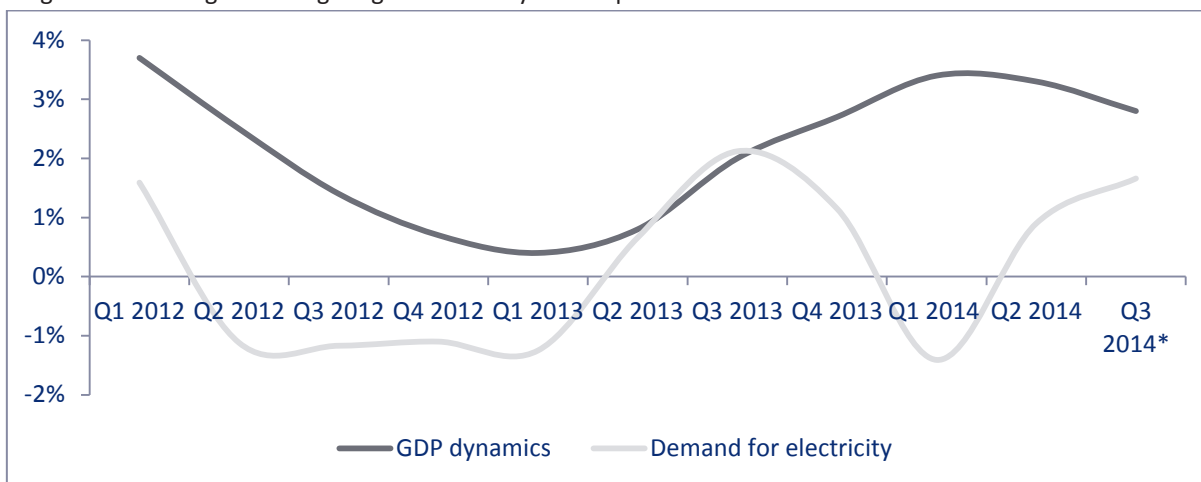
PGE Group's main operating area continues to be Poland, and the domestic macroeconomic backdrop has a substantial impact on Group's results. At the same time, the condition of Poland's economy remains largely tied to the situation across the European Union and in global markets. The Group's financial results are affected by both the situation in specific segments of the economy and the financial markets, which constitute one of the sources of PGE Group's debt financing.

As a rule of thumb, there is a correlation between rising electricity demand and economic growth. Considering PGE Group's position on the Polish power generation market, as well as its substantial share in the electricity sales and distribution market, changes in power and heat demand may have a significant impact on the Group's results.

The latest data on Poland's gross domestic product (GDP) growth show that a stable economic growth will be maintained – GDP increased by 3.3% in the second quarter of 2014 (before seasonal adjustment), and by 3.4% in the first quarter (y/y). As regards the components of GDP, the largest contribution came from positive growth in consumption, which nonetheless remains at a relatively low level, as well as growth in inventories. For the first time since 2010, negative impact came from a decrease in net exports.

In the third quarter of 2014, electricity consumption advanced 1.7% from the same period last year. After the first nine months of 2014, electricity consumption was up 0.3% y/y. A visible increase in domestic consumption during the third quarter was partially tied to a growth trend in peak consumption during the summer season, as observed over the last several years.

Diagram: GDP change vs. change in gross electricity consumption

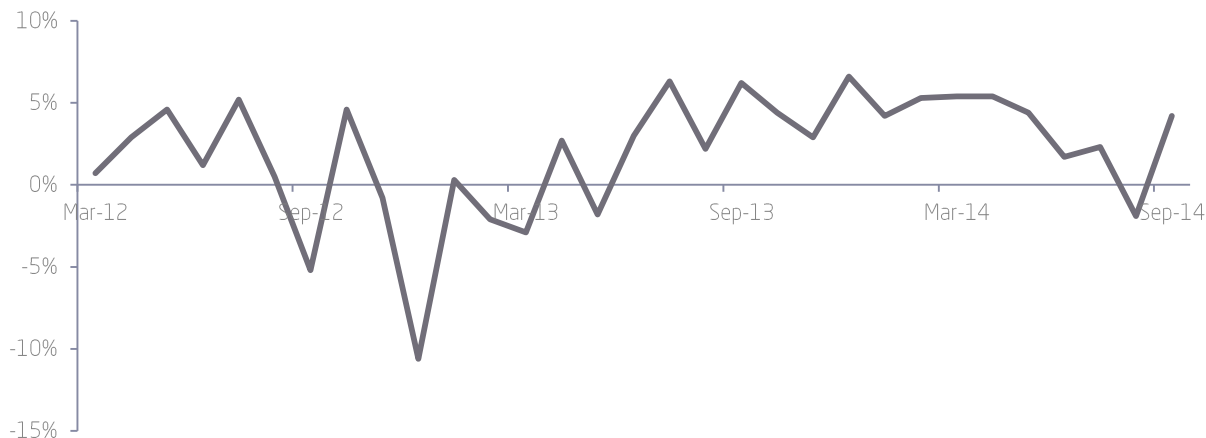


\*Average from GDP forecasts in Q3 2014

Industry accounts for approx. 45% of domestic electricity consumption hence the economic and financial situation in this sector has an impact on PGE Group's business. Total industrial output during the first nine months of 2014 expanded by 3.4% y/y, with positive growth in the crucial industrial-processing sector (4.8% y/y) and negative growth in mining and extraction (-5.4% y/y) and the energy sector (-4.8% y/y). Growth in industrial production in the third quarter alone was lower than in the first half of 2014 (by 1.5% and 4.3%, respectively), and as compared with the third quarter of 2013 (4.9% y/y).



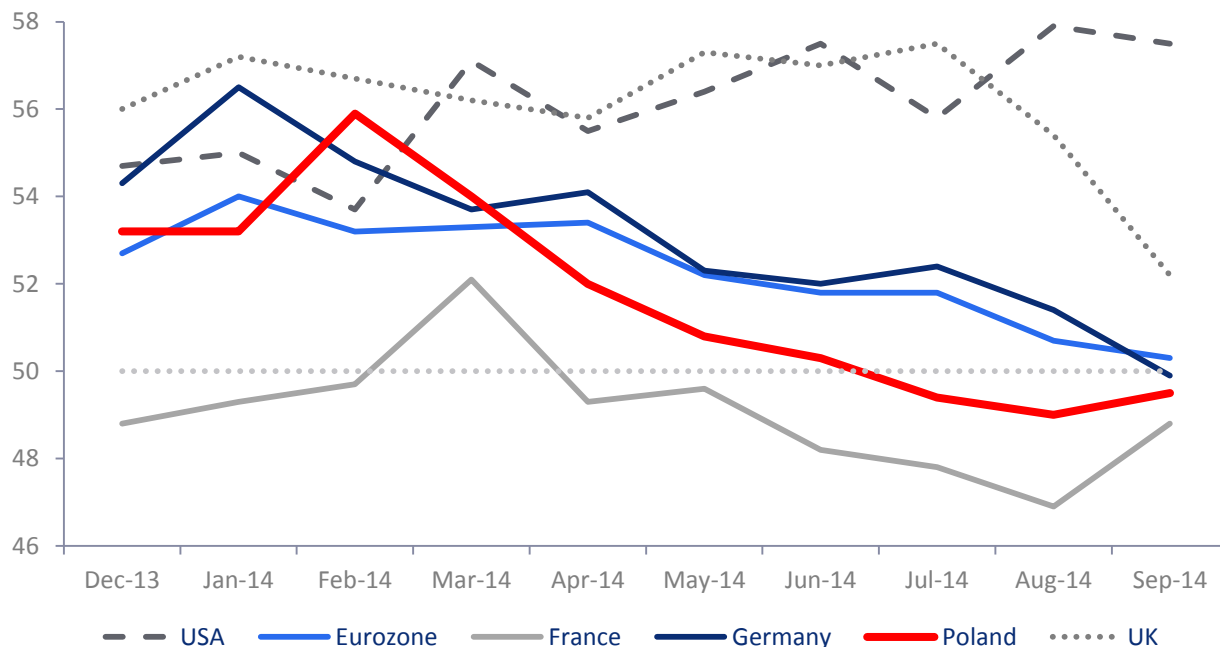
Diagram: Sold industrial production dynamics in Poland (y-o-y)



The slowdown in Polish industry was signalled by PMI. Having reached its three-year maximum of 55.9 in February 2014, this leading indicator began a series of declines, falling to 49.5 by September and remaining below 50 throughout the entire third quarter. The businesses surveyed pointed to decreases in new orders (domestic and export), output levels and procurement volumes.

Weaker industrial performance is being observed nearly everywhere in the European Union. The Eurozone and UK PMIs for the third quarter strongly declined, to 12- and 17-month lows respectively. Deteriorating conditions in industry have been noted in Greece, Austria and Germany, where the indicator dipped below 50 in September and was at the lowest level in 15 months.

Diagram: Manufacturing PMI in particular countries (in points)



Poland's economy has been facing low inflation pressure for quite some time now, which largely determines decisions by the Monetary Policy Council (MPC). Since October 2013, Polish industrial production sold has been growing at a negative rate. In the third quarter of 2014, industrial prices decreased by 1.7% y/y, and by 1.4% y/y after the first nine months of 2014. Similar to the preceding months, the largest decline was noted in the mining and extraction sector. An increase in prices was recorded in the electricity, gas and heat production and distribution sector.

Growth in price levels for consumer goods and services was 0.2% after the first nine months of 2014, remaining much slower than in 2013 and far from the inflation target set by the National Bank of Poland (NBP). In the third quarter alone, growth

was negative at approx. -0.3% y/y, meaning that Poland experienced deflation for the first time in 40 years. The falling prices are largely driven by declines in price levels for food, clothing and education.

Having to deal with below-target inflation levels over an extended period of time has an impact on the MPC's decisions regarding interest rates. Coupled with macroeconomic readings below expectations, this creates pressure to further ease monetary policy. At its October meeting, the MPC decided to lower the reference rate by 50 basis points, without ruling out further cuts in the future. The reference rate is currently at 2.0%, with the lombard rate at 3.0% and the deposit rate at 1.0%.

Table: Key economic indicators for Poland

<b>Key economic indicators</b>	<b>Q3 2014</b>	<b>Q3 2013</b>
CPI (% change y-o-y) <sup>1</sup>	-0.27	1.07
PPI (% change y-o-y) <sup>1</sup>	-1.70	-1.10
Sold industrial production (% change y-o-y) <sup>1</sup>	1.50	4.88
Sold production – energy <sup>2</sup> (% change y-o-y) <sup>2</sup>	-5.11	2.63
Gross domestic electricity consumption (% change y-o-y) <sup>3</sup>	1.66%	2.11%
Gross domestic electricity consumption (TWh) <sup>3</sup>	38.41	37.78
HSBC Manufacturing PMI (points, half-year average)	49.30	52.30

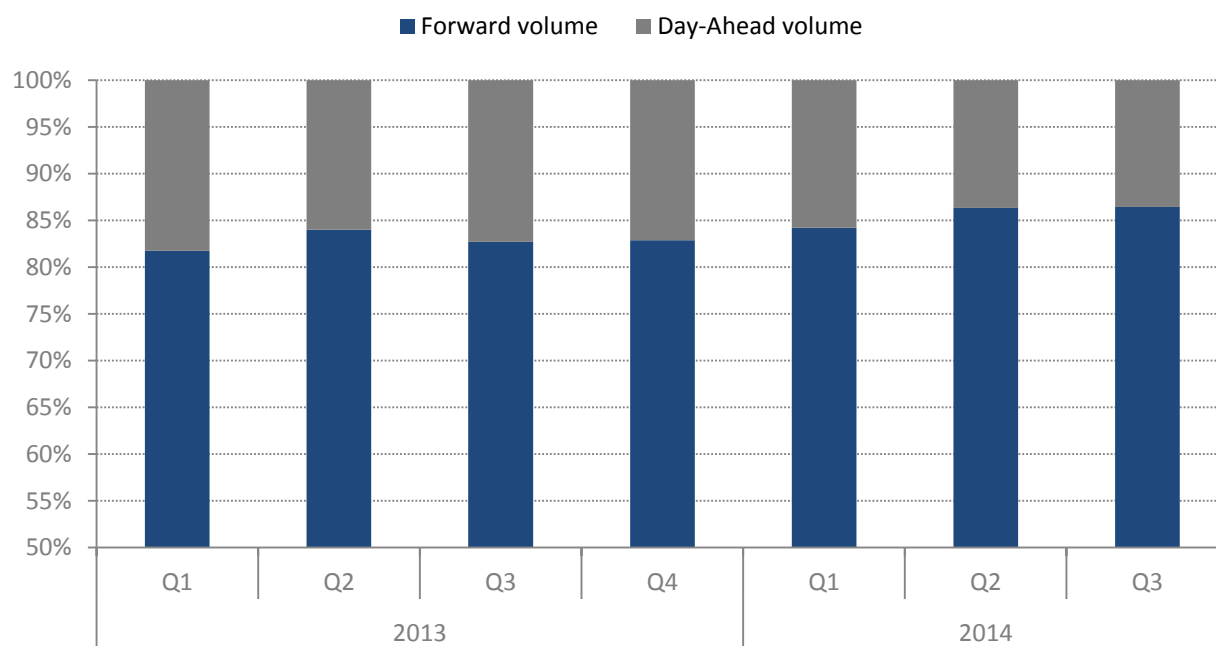
Source: <sup>1</sup> Central Statistical Office of Poland, quarterly averages, <sup>2</sup> Central Statistical Office of Poland - electricity, gas, steam and heated water production and distribution sector, quarterly averages <sup>3</sup> PSE S.A.,

## 2.1.2 Electricity prices

Liquidity on the day-ahead market of Towarowa Giełda Energii S.A. (TGE) over the first three quarters of 2014 increased by 10%, compared with the same period last year. The uptick in liquidity seen on the day-ahead market in the first two quarters of 2014 (+16% on average) significantly slowed down by the third quarter, to just 1%. The main cause of this trend reversal was substantial price volatility, leading some traders to leave the market because of the significant price swings and escalating risk. Overall trading volume on the day-ahead market in three quarters of 2014 was 17.64 TWh.

Trading volumes on the futures market continued to trend up, reaching 34.91 TWh in the third quarter of 2014 (up nearly 35% y/y). Total combined trading volume for the day-ahead market and the futures market was up by more than 32%, reaching 122.99 TWh in three quarters of 2014. This means that TGE trading volumes have exceeded domestic electricity consumption levels, which amounted to a cumulative 116.89 TWh for the period from January to September 2014 (according to Polskie Sieci Elektroenergetyczne S.A.). The excess of electricity trading volumes over domestic consumption suggests an increasing share of 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

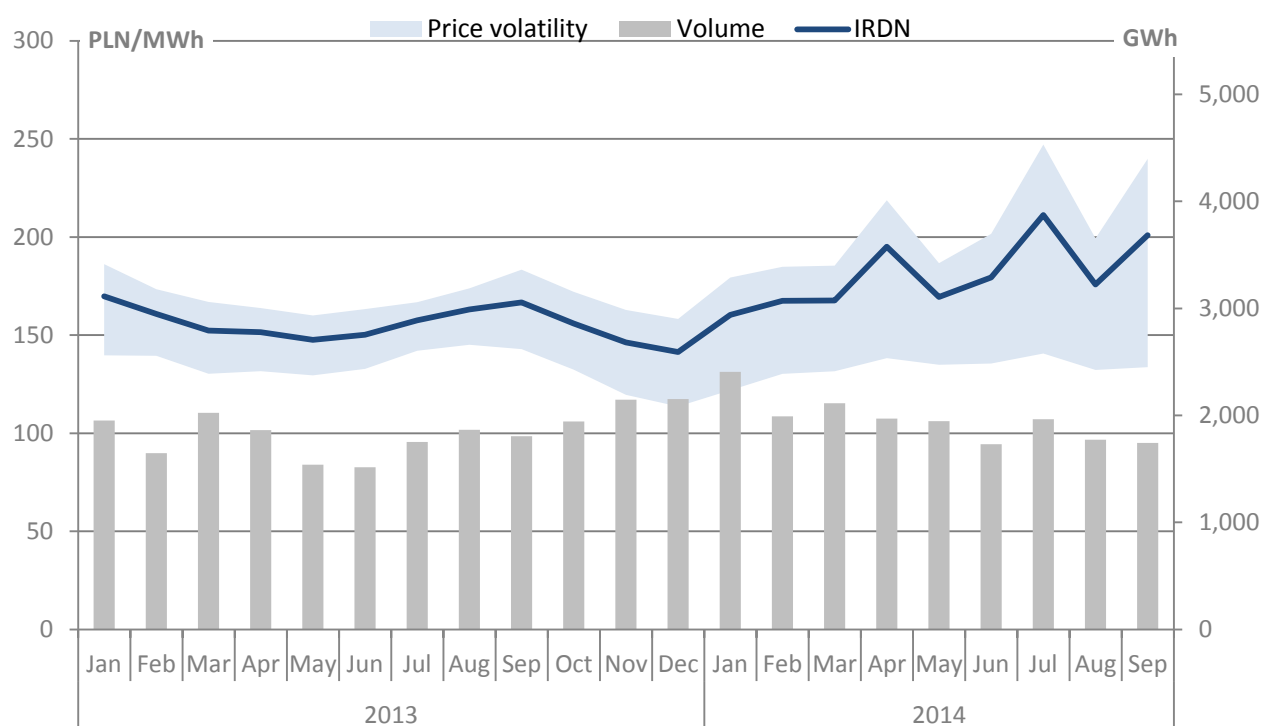
Prices on the day-ahead market in this year's third quarter continued the uptrend commenced in January 2014. The average day-ahead price in the third quarter of 2014 (the IRDN index) was PLN 196.52/MWh, compared with PLN 163.60/MWh in the same period of 2013, denoting a 20% increase. In the first quarter of 2014, prices increased (up by 3% y/y), and the second and third quarters were priced at a higher level (up by 21% and 20% y/y, respectively). In addition, the situation in the third quarter of 2014 was characterised by a 154% y/y uptick in price volatility (on September 18, 2014, the average IRDN price was PLN 370.60/MWh, with singular price swings reaching PLN 1 000/MWh).

Prices on Poland's day-ahead market in 2014 were mostly affected by:

- a change in the fee model for active Production Schedule Units (JGwa) under the Operational Capacity Reserve regulatory system service;
- low capacity reserves in the National Power System (second and third quarter).

The third quarter of 2014 saw an increase in peak prices (the sIRDN index went up by 31% y/y) and a decrease in off-peak prices (the offIRDN index declined 6% y/y), pointing to an increasing amplitude of price swings – the sIRDN index currently constitutes 169% of the offIRDN index, whereas a year ago it was 122%. The strong growth in peak prices results from the necessity to start up new generating units with high variable costs, further aided by the maximising of trade margins by market participants.

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



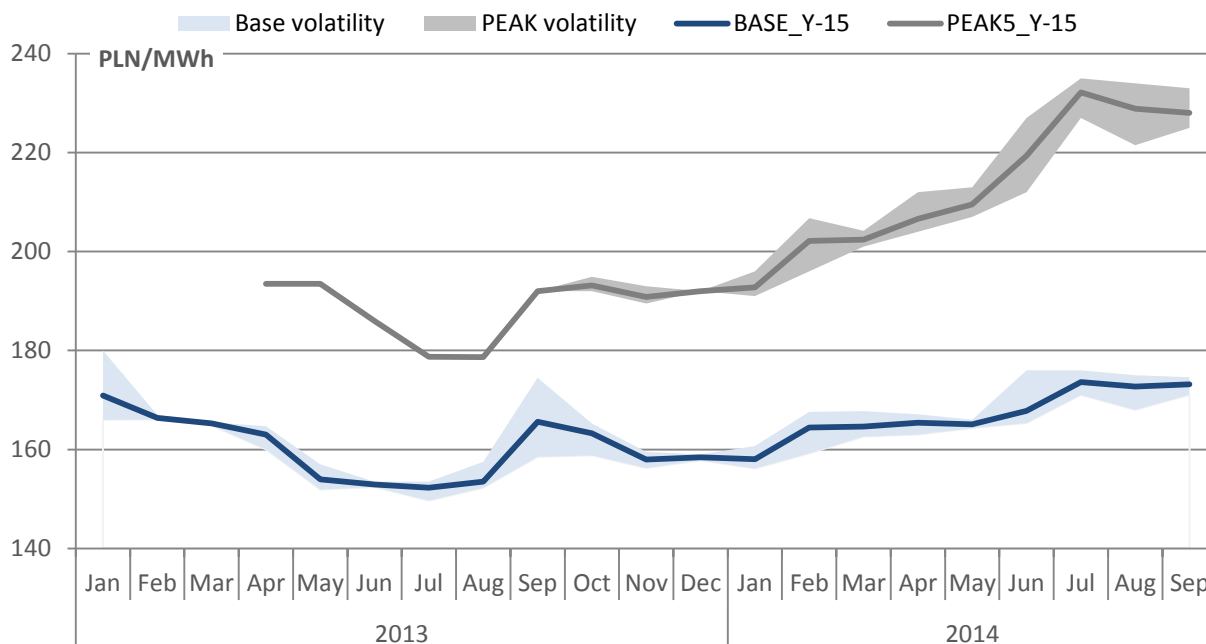
\* arithmetic average price from all power exchange transactions concluded at the session (IRDN) and prices spread (sIRDN, offIRDN)

### Futures market

In the third quarter of 2014, the prices for BASE and PEAK contracts continued to trend up. They were supported by positive information about the Polish economy, particularly the higher growth in GDP and industrial output. In addition, the overall market prices in both the day-ahead market and the futures market were affected by the adopted update of the System Balancing and System Constraint Management section of the Transmission Grid Operation and Maintenance Manual, including an updated operating model for the Operational Capacity Reserve service. The publication by the Transmission System Operator of draft update sheet no. CB/12/2014 of July 28, 2014, providing for amendment in the existing operating model for the Operational Capacity Reserve, had a substantial impact on the market price of the annual peak contract for 2015 (PEAK5\_Y-15), which decreased by 5%.

The average price for the BASE\_Y-15 instrument in the third quarter of 2014 was PLN 173.38/MWh, denoting an increase of 4% in comparison with the preceding quarter and 9% in comparison with the third quarter of 2013. The average price for the PEAK5\_YH-15 product in the third quarter of 2014 was PLN 230.33/MWh, meaning that it was nearly 8% higher than in the second quarter of 2014 and 27% higher than in the same period last year.

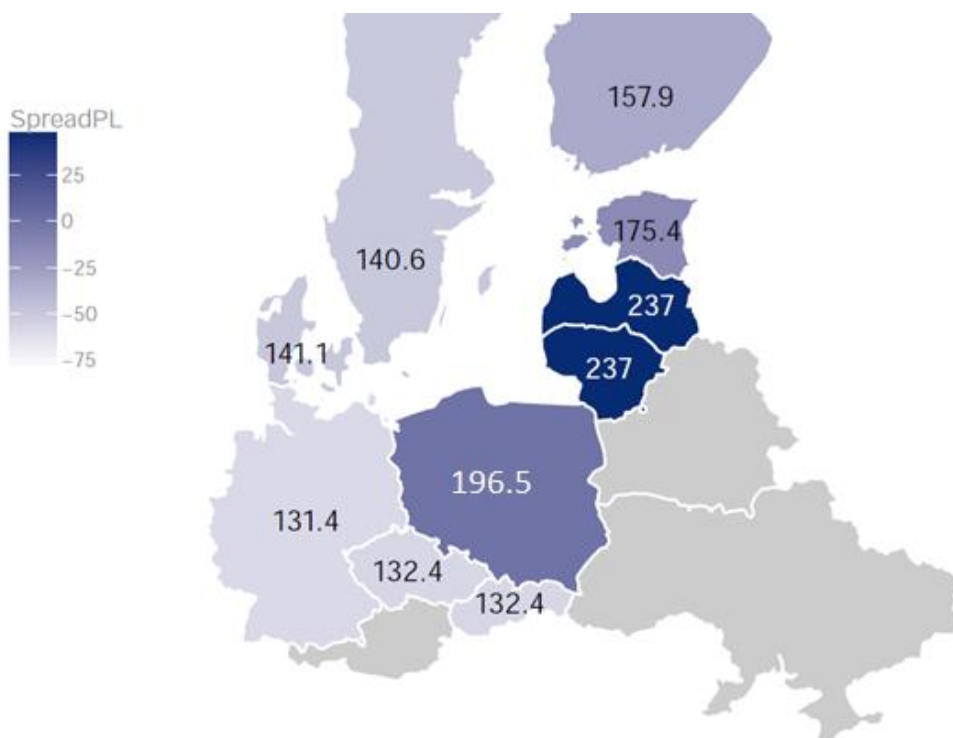
Chart: Average prices and price volatility on the futures market in 2013-2014 (TGE).



**International markets**

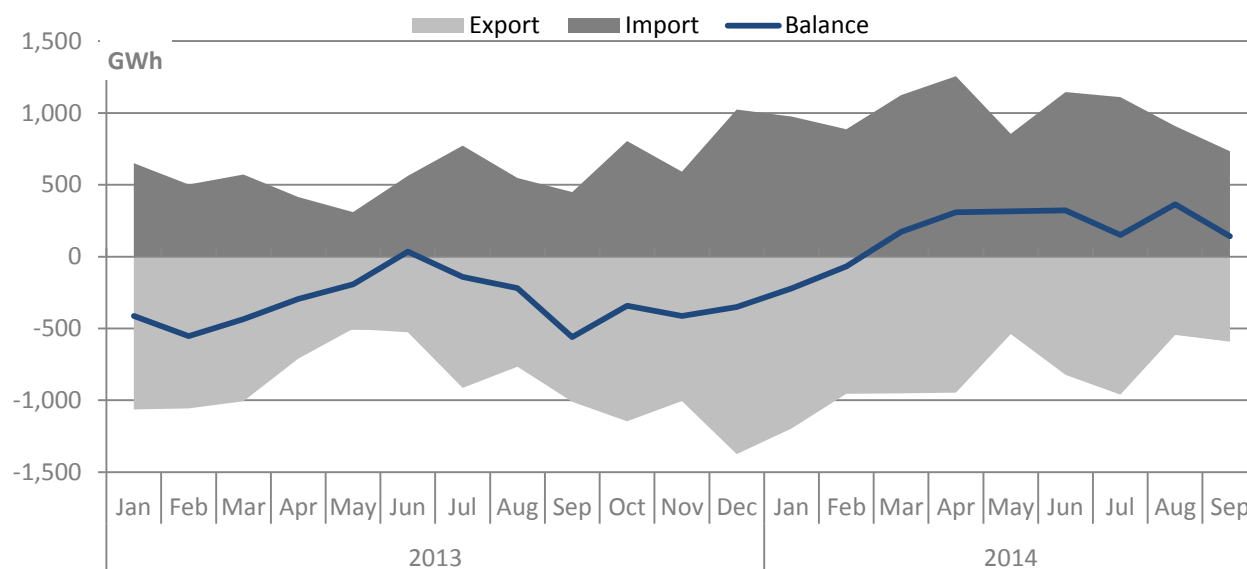
During the third quarter of 2014, prices on the Polish market were higher than those in Sweden, Germany, the Czech Republic and Slovakia. Third quarter of 2014 saw the average price on the German market fall by 20% compared with the same period in 2013 – resulting mainly from higher wind and photovoltaics production. A similar decline in prices was observed in the Scandinavian markets (-18%), driven by hydrological conditions. In Poland, however, the third quarter of 2014 saw higher average prices on the day-ahead market than in the same period last year. The rising average price in Poland, coupled with strong declines in foreign markets, resulted in a situation where the Polish market became the most expensive out of those mentioned above. This led to a change in 2014 to a positive cross-border exchange balance.

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



In the third quarter of 2014, physical flows did not change. Because of the lower power prices in surrounding markets and given the low capacity reserve, the cross-border exchange balance was positive. There was a substantial increase in imports (up by nearly 56% y/y), concurrent with a decline in exports (-22% y/y). As regards cross-border exchange by country, the situation did not change much – Germany and Sweden remained the largest importers, while exports were mainly realised to the Czech Republic and Slovakia.

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

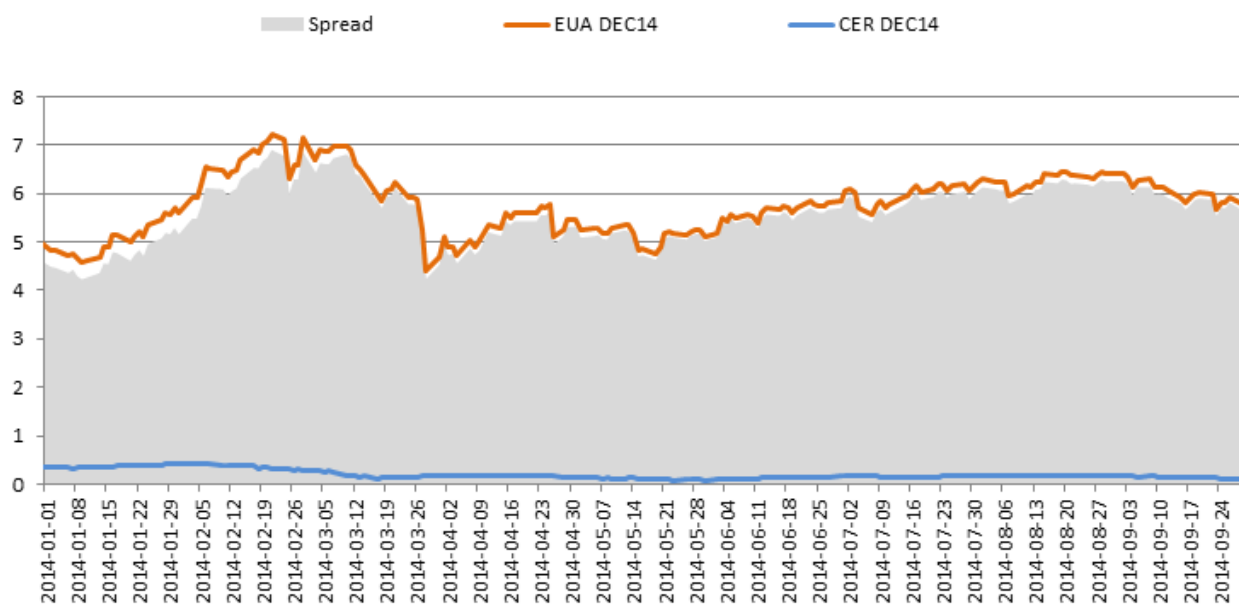


### 2.1.3 Prices of CO<sub>2</sub> emission rights

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<sub>2</sub>. 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<sub>2</sub> allowances initially granted to the installations Poland within the National Allocation Plan of CO<sub>2</sub> Allowances is lower than demanded by the Polish industry sector. Business operators are obliged to purchase the difference between the demand resulting from CO<sub>2</sub> 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<sub>2</sub> emission rights in 2014, for EUA contract with 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 first two months of the third quarter of 2014 allowances market was in an upward trend. September brought a correction of prices what caused a reversal of the trend.

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

- EUA 4.35-7.12 EUR/t;
- CER 0.12-0.42 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 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.

The main factors that might affect pricing trends in the market for CO<sub>2</sub> emission allowances is the planned implementation by the European Commission of the Market Stability Reserve (MSR) within the EU ETS system, aimed at eventually consuming the surplus allowances from the backloading measure. The planned introduction of the MSR may involve the permanent retirement of allowances covered by backloading, i.e. the artificial implementation of the "set aside" design, with the option to artificially shape market prices and regulate EUA surpluses in the EU ETS system. Works on the above design have been on-going for several months, and the first vote on implementation of the MSR is planned for February 2015.

#### 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 three quarters of 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 three quarters of 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 9%.

#### 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.

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. Conduction of proceedings concerning heat tariffs approval lies within the competence of regional Branches of the Energy Regulatory Office.

Average sale price of heat in PGE GiEK S.A. increased by approx. 11% in comparison to the prices from 2013.



### 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<sub>2</sub> emission from major Group installations in the third quarter and the period of three quarters of 2014 (in comparison to the allocations).

Table: Emission of CO<sub>2</sub> from major Group installations in the third quarter and the period of three quarters of 2014 in comparison to allocation of CO<sub>2</sub> emission rights for 2014 (in Mg).

Operator	CO <sub>2</sub> emissions		Allocation of CO <sub>2</sub> emission rights for 2014
	Q3 2014	9M 2014	
PGE GiEK S.A. Bełchatów Power Plant	9,614,217	27,216,315	15,535,037
PGE GiEK S.A. Turów Power Plant	2,500,985	6,371,876	6,247,900
PGE GiEK S.A. Opole Power Plant	1,359,179	4,962,318	3,587,594
PGE GiEK S.A. ZEDO	1,264,391	3,757,071	2,931,631
PGE GiEK S.A. Bydgoszcz CHPs	98,824	518,244	708,528
PGE GiEK S.A. Gorzów CHP	75,555	302,466	297,971
PGE GiEK S.A. Lublin Wrotków CHP	3,187	164,962	387,687
PGE GiEK S.A. Rzeszów CHP	25,321	127,490	140,185
PGE GiEK S.A. Kielce CHP	6,938	104,524	128,824
PGE GiEK S.A. Zgierz CHP	5,733	57,568	56,103
<b>TOTAL</b>	<b>14,954,330</b>	<b>43,582,834</b>	<b>30,021,460</b>

### 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 Turów Power Plant	2016	2,571
PGE GiEK Opole Power Plant	2012	1,966
PGE GiEK ZEDO	2010	633
PGE GiEK Lublin Wrotków CHP	2010	617
PGE GiEK Rzeszów CHP	2012	422
PGE GiEK Gorzów CHP	2009	108
<b>TOTAL</b>		<b>6,317</b>

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. 2.3.8 of this report.

### 2.1.7 Fuel purchase costs

Table: Volume and cost of purchase of fuels from third party suppliers in the third quarter of 2014 and 2013.

Type of fuel	Q3 2014		Q3 2013	
	Volume (tons 000')	Cost (PLNm)	Volume (tons 000')	Cost (PLNm)
Hard coal	1,575	379	1,631	403
Gas (cubic metres thousand)	69,210	27	77,060	42
Biomass	300	87	289	81
Fuel oil (heavy and light)	9	16	10	23
<b>TOTAL</b>		<b>509</b>		<b>549</b>

Table: Volume and cost of purchase of fuels from third party suppliers in period of first three quarters of 2014 and 2013.

Type of fuel	9M 2014		9M 2013	
	Volume (tons 000')	Cost (PLNm)	Volume (tons 000')	Cost (PLNm)
Hard coal	4,485	1,107	4,216	1,131
Gas (cubic metres thousand)	177,304	60	304,817	239
Biomass	945	267	820	232
Fuel oil (heavy and light)	27	52	33	73
<b>TOTAL</b>		<b>1,486</b>		<b>1,675</b>

In the first three quarters of 2014 the costs of purchasing primary fuels from providers outside the Group amounted to PLN 1,486 million and were lower by approximately 11% as compared to the three quarters 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 of legal regulations for generation of electricity in cogeneration.

In accordance with the amended Energy Law, which came into force on 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 contributes to the increase in the consumption of this type of fuel.

- Purchase price of gas was 57% lower due to an increase of the share of locally-sourced high-nitrogen gas in total gas consumption during the first three quarters of 2014, as compared with the share of this type of gas in the analogical period of 2013 (about 92% in 2014 vs. about 55% 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 (see p. 2.2.1 of this report).

- Purchase prices of hard-coal – lower by 8% and purchase price of fuel oil lower by 13%.

In the first three quarters of 2014 approximately 71% 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	Q3	Q3	change %	9M	9M	change %
		2014	2013		2014	2013	
Lignite extraction	Tons m	12.96	12.89	1%	37.09	37.97	-2%
Net electricity production	TWh	13.80	14.54	-5%	40.42	42.78	-6%
<i>including: production from biomass</i>	<i>TWh</i>	<i>0.31</i>	<i>0.26</i>	<i>19%</i>	<i>0.95</i>	<i>0.73</i>	<i>30%</i>
Heat sales	GJ m	1.32	1.64	-20%	11.38	13.78	-17%
Sales to final customers*	TWh	9.81	9.49	3%	29.37	27.34	7%
Distribution of electricity**	TWh	8.11	7.91	3%	24.06	23.51	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	Q3	Q3	change	9M	9M	change
	2014	2013	%	2014	2013	%
<b>SALES IN TWh, including:</b>	<b>24.83</b>	<b>27.87</b>	<b>-11%</b>	<b>73.97</b>	<b>81.14</b>	<b>-9%</b>
Sales to end-users*	9.81	9.49	3%	29.34	27.33	7%
Sales on the wholesale market, including:	14.74	17.99	-18%	43.79	52.66	-17%
<i>Sales on the domestic wholesale market - power exchange</i>	13.93	13.87	0%	41.07	40.30	2%
<i>Other sales on the domestic wholesale market</i>	0.77	3.95	-81%	2.38	11.60	-79%
<i>Sales to foreign customers</i>	0.04	0.17	-76%	0.34	0.76	-55%
Sales on the Balancing Market	0.28	0.39	-28%	0.84	1.15	-27%

\* 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	Q3	Q3	change	9M	9M	change
	2014	2013	%	2014	2013	%
<b>PURCHASES IN TWh, including:</b>	<b>11.97</b>	<b>14.11</b>	<b>-15%</b>	<b>37.07</b>	<b>41.48</b>	<b>-11%</b>
Purchases on the domestic wholesale market – power exchange	9.19	11.51	-20%	27.49	34.16	-20%
Purchases on the domestic wholesale market, other	1.28	1.34	-4%	3.94	3.26	21%
Purchases from abroad	0.04	0.07	-43%	0.29	0.30	-3%
Purchases from Balancing Market	1.46	1.19	23%	5.35	3.76	42%

In the first three quarters of 2013, PGE S.A. purchased larger volumes under an agreement with Energa - Obrót S.A., which terminated in 2013. In the first three quarters of 2014 the decrease of purchase on the wholesale market –power exchange 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

Generation volume	Q3 2014	Q3 2013	change %	9M 2014	9M 2013	change %
<b>ENERGY GENERATION IN TWh, including:</b>	<b>13.80</b>	<b>14.54</b>	<b>-5%</b>	<b>40.42</b>	<b>42.78</b>	<b>-6%</b>
Lignite-fired power plants	10.44	10.65	-2%	29.15	30.81	-5%
<i>Including co-combustion of biomass</i>	<i>0.10</i>	<i>0.07</i>	<i>43%</i>	<i>0.28</i>	<i>0.16</i>	<i>75%</i>
Coal-fired power plants	2.59	3.13	-17%	8.54	8.89	-4%
<i>Including co-combustion of biomass</i>	<i>0.09</i>	<i>0.08</i>	<i>13%</i>	<i>0.32</i>	<i>0.24</i>	<i>33%</i>
Coal-fired CHP plants	0.14	0.15	-7%	0.78	0.82	-5%
Gas-fired CHP plants	0.18	0.19	-5%	0.40	0.95	-58%
Biomass-fired CHP plants	0.11	0.11	0%	0.35	0.34	3%
Pumped storage power plants	0.11	0.13	-15%	0.39	0.34	15%
Hydroelectric plants	0.10	0.09	11%	0.34	0.40	-15%
Wind power plants	0.13	0.09	44%	0.47	0.23	104%

A decrease in production of electricity at lignite-fired power plants in three quarters of 2014 results mainly from lower production in PGE GiEK S.A. Branch Turów Power Plant, as a result of decommissioning of unit no. 10 by the end of 2013, shorter operation time of units no. 11,12 and 14 at PGE GiEK S.A. Branch Bełchatów Power Plant. Unit no. 14 went through repairs in April 2014, unit no. 11 was being modernized between December 2013 and September 2014, while unit no. 12 has been modernised since May 2014.

A decrease in production of electricity at coal-fired power plants results from lower production in Dolna Odra power plant what is a consequence of decommissioning of unit no. 3 in November 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 until April 30, 2014 (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 three quarters of 2014.

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

An increase of production in wind power plants is a result of increase of the installed capacity by 42 MW and more favourable weather conditions.

### 2.2.2 Sales of heat

In the three quarters of 2014 the heat sales in PGE Capital Group totalled 11.38 GJ million and were lower by 17.4% as compared to analogical period of 2013. Lower sales of heat results from lower demand for heat due to higher average outside temperatures in winter. In addition, ceasing of heat input by a key off taker of PGE GiEK S.A. Branch Bydgoszcz CHPs also affected the heat sales.

## 2.3 Business segments

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

PLN million	Total income		% change
	Q3 2014	Q3 2013	
Conventional Generation	2,909	3,060	-5%
Renewable Energy	169	162	4%
Wholesale Trading	2,288	3,098	-26%
Distribution	1,405	1,367	3%
Retail Sale	3,030	3,218	-6%
Other activity	469	472	-1%
<b>TOTAL</b>	<b>10,270</b>	<b>11,377</b>	<b>-10%</b>
<b>Consolidation adjustments</b>	<b>-3,621</b>	<b>-3,896</b>	<b>7%</b>
<b>TOTAL AFTER ADJUSTMENTS</b>	<b>6,649</b>	<b>7,481</b>	<b>-11%</b>

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

PLN million	EBITDA	EBIT	Capital expenditures	Assets of the segment*
Q3 2014				
Conventional Generation	913	488	1,219	33,033
Renewable Energy	83	28	87	3,574
Wholesale Trading	100	97	3	1,003
Distribution	606	344	318	15,197
Retail Sale	-53	-55	0	2,408
Other activity	45	13	32	1,355
<b>TOTAL</b>	<b>1,694</b>	<b>915</b>	<b>1,659</b>	<b>56,570</b>
<b>Consolidation adjustments</b>	<b>4</b>	<b>15</b>	<b>-32</b>	<b>-1,256</b>
<b>TOTAL AFTER ADJUSTMENTS</b>	<b>1,698</b>	<b>930</b>	<b>1,627</b>	<b>55,314</b>

\* see Note 10 to the consolidated financial statements

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

PLN million	EBITDA	EBIT	Capital expenditures	Purchase of PPE*	Assets of the segment **
				net, within purchase of new companies	
Q3 2013***					
Conventional Generation	1,218	785	764	0	30,719
Renewable Energy	78	26	45	311	3,232
Wholesale Trading	234	229	5	0	1,357
Distribution	603	356	347	0	14,949
Retail Sale	-47	-49	0	0	2,231
Other activity	48	21	36	0	1,338
<b>TOTAL</b>	<b>2,134</b>	<b>1,368</b>	<b>1,197</b>	<b>311</b>	<b>53,826</b>
<b>Consolidation adjustments</b>	<b>-44</b>	<b>-36</b>	<b>-30</b>	<b>60</b>	<b>-1,333</b>
<b>TOTAL AFTER ADJUSTMENTS</b>	<b>2,090</b>	<b>1,332</b>	<b>1,167</b>	<b>371</b>	<b>52,493</b>

\* 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

PLN million	Q3 2014	Q3 2013	% change
Sales revenues	2,909	3,060	-5%
EBIT	488	785	-38%
EBITDA	913	1,218	-25%
Capital expenditures	1,219	764	60%

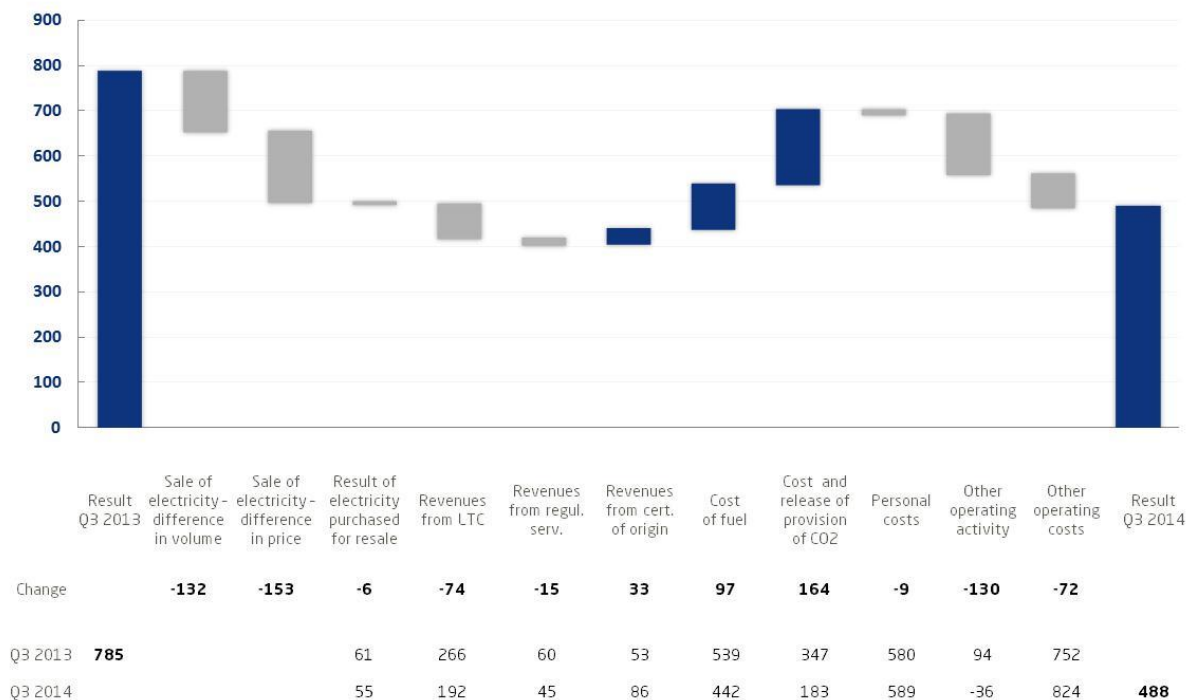
Decrease of EBIT by PLN 297 million was mainly connected with:

- lower revenues from sales of electricity from own production PLN (-) 285 million;
- higher impairment allowances for other assets (other operating activities) PLN (-) 103 million;
- lower LTC compensations PLN (-) 74 million;
- lower revenues from penalties and compensations (other operating activities) PLN (-) 45 million;
- lower revenues from ancillary control services PLN (-) 15 million.

Above declines were partly compensated by:

- lower costs of fees for CO<sub>2</sub> emission PLN 164 million;
- lower costs of production fuel used PLN 97 million;
- higher revenues from sales of produced energy origin certificates PLN 33 million.

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



Other operating expenses include costs by type other than those indicated in the table.



## CAPITAL EXPENDITURES

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

PLN million	Capital expenditures		
	Q3 2014	Q3 2013	% change
Investments in generating capacities, including:	868	263	230%
▪ <i>Development</i>	274	24	1,042%
▪ <i>Modernization and replacement</i>	594	239	149%
Purchases of finished capital goods	13	9	44%
Vehicles	0	1	-
Other	214	314	-32%
<b>TOTAL</b>	<b>1,095</b>	<b>587</b>	<b>87%</b>
Activated costs of overburden removal in mines	124	177	-30%
<b>TOTAL with activated costs of overburden removal in mines</b>	<b>1,219</b>	<b>764</b>	<b>60%</b>

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 third quarter 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 427 million;
- construction of units 5 and 6 in Opole power plant PLN 239 million;
- construction of SO<sub>x</sub> emission reduction installations on units 4-6 in Turów power plant PLN 73 million;
- change of technology of furnace waste storage in Bełchatów power plant PLN 52 million.

On September 30, 2014, a use permit was obtained for a piston engine-based power and heat cogeneration unit at PGE GiEK S.A. Branch Rzeszów CHP, with a capacity of ~ 29 MWe and 26 MWt.

## 2.3.2 Renewable Energy

Table: Key figures for Renewable Energy

PLN million	Q3 2014	Q3 2013	% change
Sales revenues	169	162	4%
EBIT	28	26	8%
EBITDA	83	78	6%
Capital expenditures	87	45	93%
Purchase of PPE net, within purchase of new companies	0	311	-

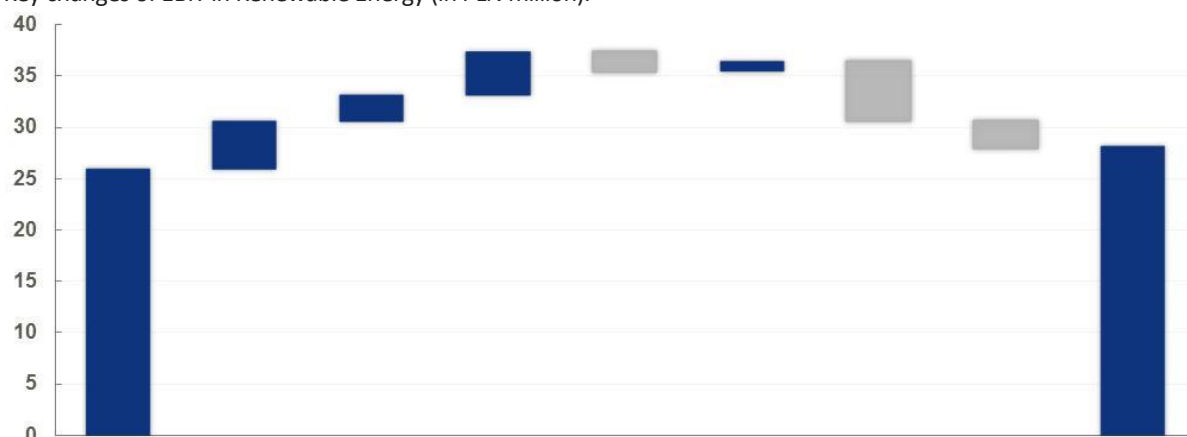
Increase of EBIT by PLN 2 million mainly resulted from:

- Higher revenues from sale of electricity PLN 9 million.

EBIT was negatively affected by:

- Higher operational expenses of wind farms acquired in the second half of 2013 (amortisation and depreciation, property tax, repairs and maintenance costs) PLN (-) 6 million.

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



	Result Q3 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	Fixed costs	Other	Result Q3 2014
Change		5	3	4	-2	1	-6	-3	
Q3 2013	26	18	23	11	17	86	88	-44	
Q3 2014		23	26	15	15	87	94	-41	28

## CAPITAL EXPENDITURES

Table: Capital expenditures incurred in Renewable Energy segment in the third quarter of 2014 and 2013.

PLN million	Capital expenditures		
	Q3 2014	Q3 2013	% change
Investments in generating capacities, including:	86	44	95%
▪ <i>Development</i>	74	30	147%
▪ <i>Modernization and replacement</i>	12	14	-14%
Other	1	1	0%
<b>TOTAL</b>	<b>87</b>	<b>45</b>	<b>93%</b>
Purchase of PPE net, within purchase of new companies	0	311	-
<b>TOTAL</b>	<b>87</b>	<b>356</b>	<b>-76%</b>

In the third quarter of 2014 the highest capital expenditures were incurred for the construction project of wind farm Karwice with a capacity of 40 MW (PLN 68 million).

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

- Construction of wind farm Kisielice II with a capacity of 12 MW – tender for General Contractor was announced in July 2014;
- Construction of wind farm Lotnisko with a capacity of 90 MW – agreement for construction works was signed in August 2014 and building site was relayed to the contractor;
- Construction of wind farm Resko II with a capacity of 76 MW – an investment supervision contract was signed in September 2014, while contract for delivery of wind turbines was concluded in October.

Expenditures for the purchase of tangible and intangible fixed assets in the third quarter of 2013 related to acquisition of wind assets of Iberdrola Renewables Polska sp. z o.o.

### 2.3.3 Wholesale Trading

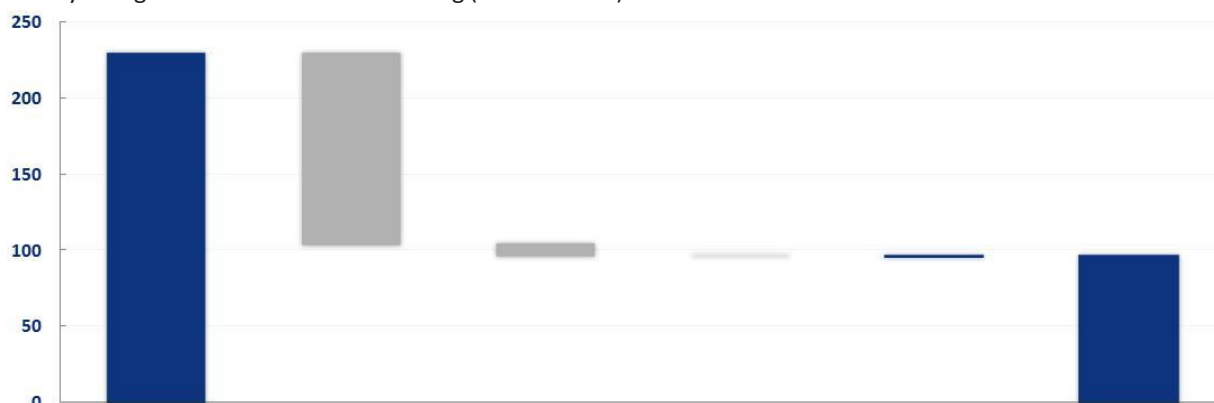
Table: Key figures for Wholesale Trading

PLN million	Q3 2014	Q3 2013	% change
Sales revenues	2,288	3,098	-26%
EBIT	97	229	-58%
EBITDA	100	234	-57%
Capital expenditures	3	5	-40%

Decrease of EBIT by PLN 132 million was mainly connected with:

- lower result on electricity sales PLN (-) 125 million;
- lower remuneration with regard to services for PGE GiEK S.A. due to the Agreement on Commercial Management of Generation Capacities PLN (-) 6 million.

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



	Result Q3 2013	Result on sale of electricity	Management service	Revenues from cert. of origin	Other	Result Q3 2014
Change		<b>-125</b>	<b>-6</b>	<b>-1</b>	<b>0</b>	
Q3 2013	<b>229</b>	156	120	2	49	
Q3 2014		31	114	1	49	<b>97</b>

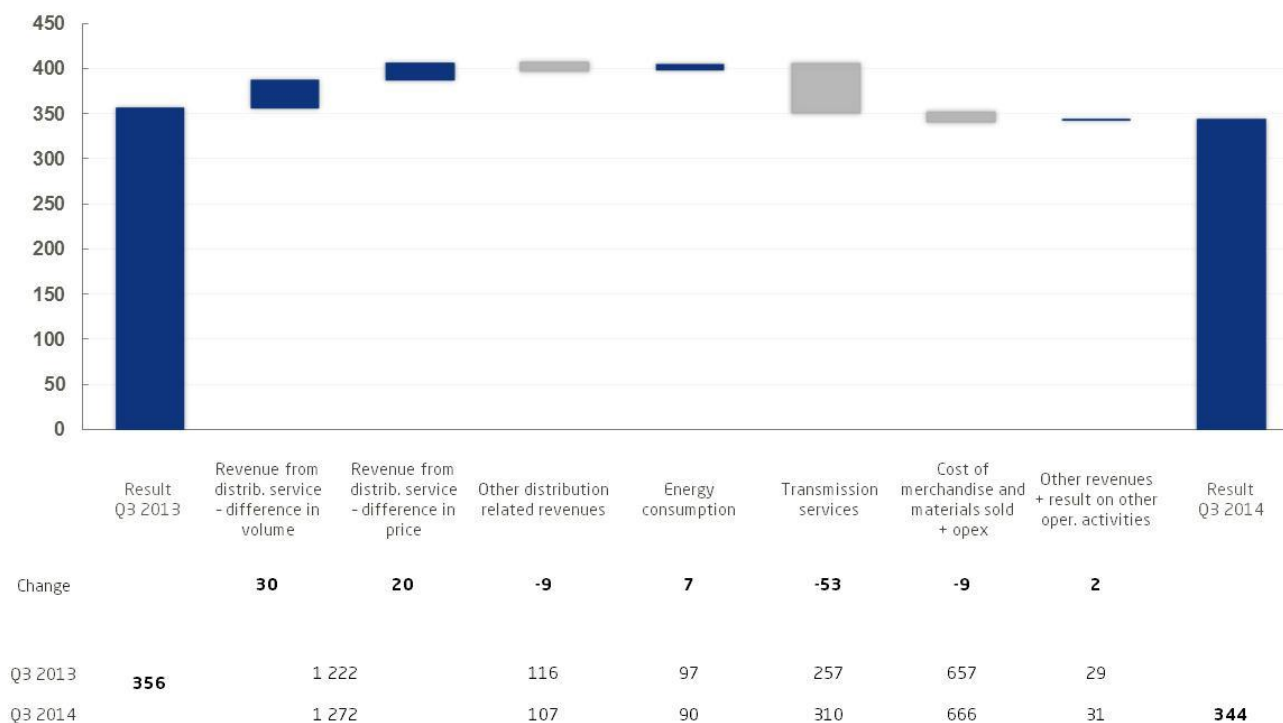
## 2.3.4 Distribution

Table: Key figures for Distribution

PLN million	Q3 2014	Q3 2013	% change
Sales revenues	1,405	1,367	3%
EBIT	344	356	-3%
EBITDA	606	603	0%
Capital expenditures	318	347	-8%

Sales revenues increased due to components carried through tariff (mainly transmission fees and transition charge paid to Polskie Sieci Elektroenergetyczne S.A.). Decline of EBIT is a consequence of lower return on regulatory assets base due to lower cost of capital set by the ERO President for distribution enterprises.

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



## CAPITAL EXPENDITURES

Table: Capital expenditures incurred in Distribution segment in the third quarter of 2014 and 2013.

PLN million	Capital expenditures		
	Q3 2014	Q3 2013	% change
MV and LV power networks	92	58	59%
HV/MV and MV/MV power stations	16	53	-70%
HV power lines	7	5	40%
Connection of new off-takers	126	150	-16%
Purchase of transformers and energy counters	45	54	-17%
IT, telemechanics and communication	15	19	-21%
Other	17	8	113%
<b>TOTAL</b>	<b>318</b>	<b>347</b>	<b>-8%</b>

In the third quarter of 2014 the highest capital expenditures were incurred for connection of new off-takers (PLN 126 million) and modernisation and development of MV and LV power networks (PLN 92 million).

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

PLN million	Q3 2014	Q3 2013	% change
Sales revenues	3,030	3,218	-6%
EBIT	-55	-49	-12%
EBITDA	-53	-47	-13%
Capital expenditures	0	0	-

Decrease of EBIT by PLN 6 million was mainly related to:

- lower margin on electricity sales PLN (-) 80 million.

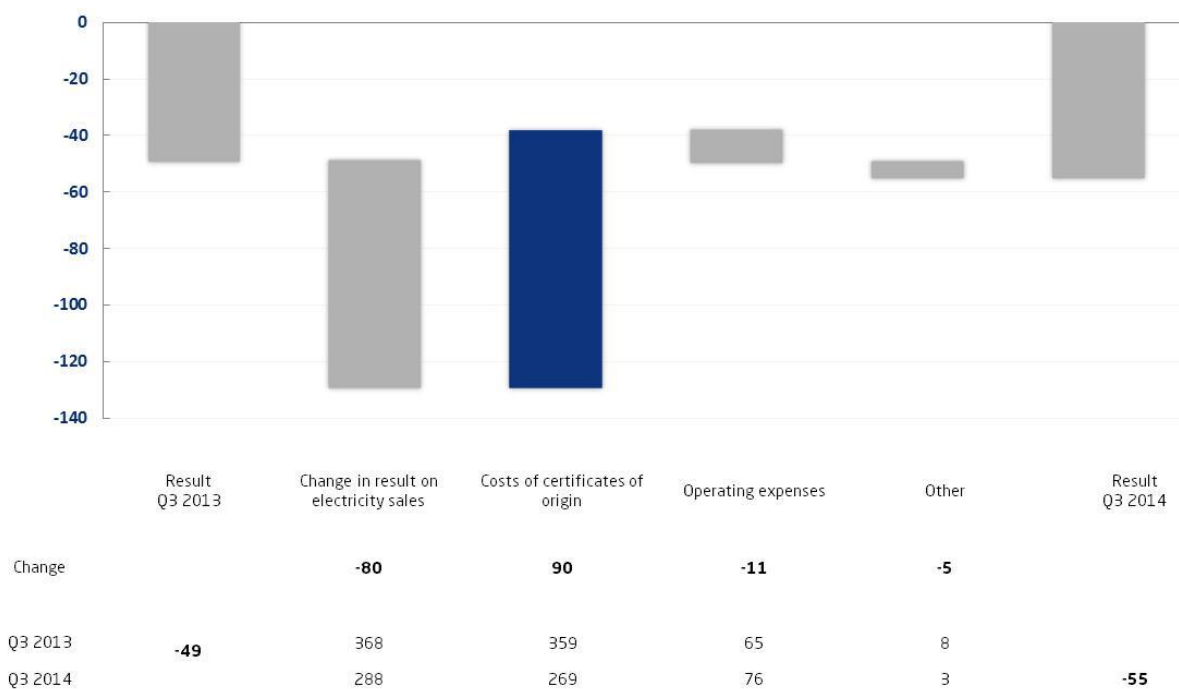
EBIT was also affected by:

- lower costs of redemption of property rights PLN 90 million.

Lower margin on sale of electricity realised in the third quarter of 2014 as compared to the third quarter 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;
- contracts based on the electricity prices from 2013.

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



### 2.3.6 Other Operations

PLN million	Q3 2014	Q3 2013	% change
Sales revenues	469	472	-1%
EBIT	13	21	-38%
EBITDA	45	48	-6%
Capital expenditures	32	36	-11%

EBIT lower by PLN 8 million was mainly related to:

- a lower result at PGE EJ1 sp. z o.o., mainly caused by an increase in the company's operating costs in connection with its development, and the recognition in the third quarter of 2013 of work delay penalties – which did not occur in 2014 – in other operating revenue (a one-off event), PLN (-) 10 million;
- lower result of companies rendering ancillary services (construction works, repairs, modernisations) to companies from other segments of PGE Capital Group and to external contractors.

Decline of EBIT was partly compensated by:

- an improved result at PGE Systemy S.A., stemming from higher revenue on new service commissioning (Local IT Support – provided by staff employed in construction of the IT shared service centre (CUW IT), as well as support services for the accounting, consolidation and reporting processes) PLN 13 million;
- better result of Exatel S.A. due to savings in personnel expenses connected mainly with employment restructuring PLN 3 million.

### CAPITAL EXPENDITURES

Capital expenditures in Other Operations in the third quarter of 2014 amounted to PLN 32 million as compared to PLN 36 million in the third quarter of 2013. Within the above amount, the main capital expenditures in the third quarter of 2014 were incurred by:

- PGE Systemy S.A. – for IT infrastructure development PLN 10 million;
- PGE EJ1 sp z o.o. – for nuclear project development PLN 8 million;
- Exatel S.A. – for telecommunication infrastructure development PLN 7 million.

Other capital expenditures were mostly related to ancillary services.



## 2.1 Financial results of PGE Capital Group

Key financial data	Unit	Q3 2014	Q3 2013**	% change	9M 2014	9M 2013**	% change
Sales revenues	PLN million	6,649	7,481	-11%	20,857	22,582	-8%
<b>EBIT</b>	<b>PLN million</b>	<b>930</b>	<b>1,332</b>	<b>-30%</b>	<b>4,055</b>	<b>4,100</b>	<b>-1%</b>
<b>EBITDA</b>	<b>PLN million</b>	<b>1,698</b>	<b>2,090</b>	<b>-19%</b>	<b>6,305</b>	<b>6,336</b>	<b>0%</b>
Net profit attributable to equity holders of the parent company	PLN million	387	1,111	-65%	2,884	3,304	-13%
LTC compensations:	PLN million	192	266	-28%	1,600	784	104%
<i>Revenues from LTC compensations</i>	<i>PLN million</i>	<i>192</i>	<i>162</i>	<i>19%</i>	<i>1,354</i>	<i>532</i>	<i>155%</i>
<i>Reversal of provisions for LTC (other operating revenues)</i>	<i>PLN million</i>	<i>0</i>	<i>104</i>	<i>-</i>	<i>246</i>	<i>252</i>	<i>-2%</i>
<b>Capital expenditures</b>	<b>PLN million</b>	<b>1,627</b>	<b>1,167</b>	<b>39%</b>	<b>3,859</b>	<b>2,827</b>	<b>37%</b>
Net cash from operating activities	PLN million	2,849	2,533	12%	4,433	5,797	-24%
Net cash from investing activities	PLN million	415	-1,534	-	-4,635	-4,306	-8%
Net cash from financial activities	PLN million	-1,904	-1,896	0%	189	-1,148	-
Net earnings per share	PLN	0.20	0.59	-66%	1.54	1.76	-12%
<b>EBITDA margin</b>	<b>%</b>	<b>26%</b>	<b>28%</b>		<b>30%</b>	<b>28%</b>	

Key financial data	Unit	As at September 30, 2014	As at December 31, 2013*	% change
Working capital	PLN million	7,489	5,223	43%
<b>Net debt/LTM EBITDA ***</b>	<b>x</b>	<b>-0.13x</b>	<b>-0.39x</b>	

\* data restated

\*\* audited

\*\*\* LTM EBITDA - Last Twelve Months EBITDA

## Consolidated statement of comprehensive income

In the third quarter of 2014 total **sales revenues** of the Group amounted to PLN 6,649 million compared to PLN 7,481 million in the third quarter of 2013, what means decrease by approx. 11%.

Decrease of revenues by PLN 832 million was mainly caused by:

- decreased revenues from sales of electricity PLN (-) 951 million;
- decreased revenues from ancillary control services PLN (-) 24 million;
- decreased revenues from sales of heat PLN (-) 6 million.

This decrease was partly offset by:

- increased revenues from sales of certificates of energy origin PLN 74 million;
- increased revenues from sales of distribution services PLN 52 million;
- increase of revenues from LTC compensations PLN 30 million.

**Cost of goods sold** in the third quarter of 2014 amounted to PLN 5,123 million, what means decrease by approx. 9% in comparison to the third quarter of 2013.

The decrease of the cost of goods sold by PLN 526 million was mainly caused by:

- lower merchandise and materials sold (including energy purchased for resale) PLN 433 million;
- decreased costs of fees for CO<sub>2</sub> emission PLN 164 million;
- lower costs of production fuel PLN 99 million.

Cost of goods sold was also affected by:

- higher costs of transmission fees PLN (-) 50 million.

**Gross profit on sales** in the third quarter of 2014 amounted to PLN 1,526 million compared to PLN 1,832 million in the third quarter of 2013, what means decrease by approx. 17%.

In the third quarter of 2014 **distribution and selling expenses** of PGE Group amounted to PLN 383 million and were lower by approx. 17% in comparison to the third quarter of 2013. The decreased selling and distribution expenses were mainly associated with lower costs of redemption of property rights incurred by PGE Obrót S.A.

In the third quarter of 2014 **general and administrative expenses** amounted to PLN 192 million, i.e growth by approximately 5% in comparison to the third quarter of 2013.

Result on other operating activities in the third quarter of 2014 was negative and amounted to PLN (-) 21 million in comparison to positive result of PLN 142 million in the third quarter of 2013.

**Other operating revenues** of the Group in the third quarter of 2014 amounted to PLN 85 million, what means decrease by approx. 59% in relation to PLN 205 million achieved in the comparative period. In the third quarter of 2013, in connection with the favourable court verdicts, an impairment on revenues from LTC compensations was reversed (PLN 104 million). Lower level of other operating revenues in the third quarter of 2014 results also from compensations, penalties and fines received lower by PLN (-) 51 million.

**Other operating expenses** of the Group in the third quarter of 2014 amounted to PLN 106 million compared to PLN 63 million in the third quarter of 2013, what means increase by approx. 68%. A reversal of impairment of Opole II project in amount of PLN 56 million, that was raised in the first half of 2013, was recognised in the third quarter of 2013. In the third quarter of 2014 impairment losses on other assets were raised in amount of PLN 32 million. As a result of above events, other operating expenses increased by PLN (+) 88 million.

In the third quarter of 2014 result on financial activities was negative and amounted to PLN (-) 433 million, in comparison to positive result in amount of PLN 33 million in the third quarter of 2013.

The Group's **financial revenues** in the third quarter of 2014 amounted to PLN 106 million what means increase by approx. 86% in relation to PLN 57 million achieved in the third quarter of 2013.

Increased financial revenues mainly result from revenues from foreign exchange translations higher by PLN 49 million.

**Financial expenses** of the Group in the third quarter of 2014 amounted to PLN 539 million, what means increase by PLN 515 million in comparison to value achieved in the third quarter of 2013.

Higher level of financial expenses mainly resulted from:

- |  |                  |
|--|------------------|
| ▪ recognition of estimated loss of value of bonds issued by Autostrada Wielkopolska S.A. | PLN 386 million; |
| ▪ higher expenses due to exchange losses   | PLN 93 million;  |
| ▪ higher interest expenses   | PLN 26 million;  |
| ▪ recognition of revaluation of CCIRS and IRS hedge transactions.                        | PLN 24 million.  |

Detailed description of CCIRS and IRS transactions is presented in note 22.2 of the consolidated financial statements.

As a result of the factors discussed above, the gross profit of the Group in the third quarter of 2014 amounted to PLN 497 million, compared to PLN 1,364 million in the third quarter of 2013.

In the third quarter of 2014 **gross profit margin** of the Group (gross profit to total sales revenues) decreased to 7% from 18% in the third quarter of 2013.

**Net profit** of the PGE Capital Group in the third quarter of 2014 amounted to PLN 390 million compared to PLN 1,122 million in the third quarter of 2013.

**Net profit attributable to the equity holders of the parent company** in the third quarter of 2014 decreased by PLN 724 million, in comparison to the third quarter of 2013 and amounted to PLN 387 million.

**Total comprehensive income** of the Group amounted to PLN 357 million in the third quarter of 2014, compared to PLN 1,121 million in the third quarter of 2013.

## Consolidated statement of financial position

**Non-current assets** of the Group as at September 30, 2014 and as at December 31, 2013 amounted respectively to PLN 49,592 million and PLN 47,738 million.

Increase in value of non-current assets by PLN 1,854 million was mainly caused by:

- |   |                    |
|---|--------------------|
| ▪ Capital expenditures incurred for property, plant and equipment and intangible assets | PLN 3,859 million; |
| including:  |                    |
| ▪ Conventional Generation   | PLN 2,797 million; |
| ▪ Distribution  | PLN 770 million;   |
| ▪ Renewables  | PLN 242 million;   |
| ▪ Increased advances for construction in progress                                       | PLN 594 million;   |
| ▪ Higher deferred tax assets  | PLN 102 million.   |

Non-current assets were also affected by:

- |  |                        |
|--|------------------------|
| ▪ depreciation charges on fixed assets and intangible assets               | PLN (-) 2,250 million; |
| ▪ impairment loss on value of bonds issued by Autostrada Wielkopolska S.A. | PLN (-) 386 million.   |

**Current assets** of the Group as at September 30, 2014 and as at December 31, 2013 amounted respectively to PLN 13,347 million and PLN 13,013 million.

The increase of the value of the current assets by PLN 334 million was mainly related to:

- increased other short-term assets PLN 532 million;
- higher inventories PLN 370 million;
- increased LTC receivables PLN 190 million.

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

Increase in inventories results from higher value of certificates of energy origin, CO<sub>2</sub> emission rights held for trading and materials and production in progress.

This growth was offset by:

- decreased trade receivables PLN (-) 538 million;
- decrease in greenhouse gases emission rights PLN (-) 185 million;
- decrease in short-term financial assets at fair value through profit or loss PLN (-) 29 million;

including:

- commodity forward PLN (-) 37 million;
- FX forward PLN 8 million.

Decrease in greenhouse gases emission rights results from redemption of CO<sub>2</sub> emission rights for 2013.

As at September 30, 2014 and as at December 31, 2013 **total equity of the Group** amounted respectively to PLN 44,267 million and PLN 43,648 million.

**Non-controlling interest** as at September 30, 2014 and as at December 31, 2013 amounted respectively to PLN 131 million and PLN 266 million.

The increase in total equity by PLN 619 million mainly resulted from recognition of the net profit for the period ended September 30, 2014 in amount of PLN 2,900 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 2,061 million for dividend payment.

**Long-term liabilities** as at September 30, 2014 and as at December 31, 2013 amounted respectively to PLN 12,814 million and PLN 9,313 million.

Growth of long-term liabilities by PLN 3,501 million was mainly caused by:

- increase in interest-bearing loans, borrowings, bonds and lease PLN 2,590 million;
- increased long-term provisions PLN 751 million;
- increase of deferred tax liability PLN 233 million.

Increase in interest-bearing loans, borrowings, bonds and lease is mainly connected with issue of Eurobonds in amount of PLN 2,612 million.

Increased long-term provisions result from increased provision for reclamation of land (result of discount rate change from 4.35% to 3.5%) and actuarial provisions along with decrease of provisions for non-contractual use of the property.

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

**Short-term liabilities** as at September 30, 2014 and as at December 31, 2013 amounted respectively to PLN 5,858 million and PLN 7,790 million.

Decrease of short-term liabilities by PLN 1,932 million mainly resulted from:

- decrease of other financial liabilities PLN (-) 697 million;

- lower short-term provisions PLN (-) 614 million;
- decrease in short-term part of interest-bearing loans, borrowings, bonds and lease PLN (-) 310 million;
- decrease in other non-financial liabilities PLN (-) 308 million;
- decreased trade receivables PLN (-) 121 million.

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

Lower short-term provisions mainly result from reversal and use of provision for purchase of CO<sub>2</sub> emission rights. This decline was partly compensated by provision raised for property rights.

Decrease in short-term part of interest-bearing loans, borrowings, bonds and lease results from use of current account credit limits by the Group companies.

Decrease in other non-financial liabilities mainly results from lower environmental fees, liabilities related to current employment and VAT and excise tax liabilities.

This decline was compensated by:

- increase of financial liabilities at fair value through profit or loss PLN 104 million.
  - including:
    - CCIRS valuation PLN 58 million;
    - IRS valuation PLN 45 million.

## Consolidated statement of cash flows

**The total net cash flow from operating activities** for the third quarter of 2014 amounted to PLN 2,849 million compared to PLN 2,533 million in the third quarter of 2013.

**Positive net cash flow from investing activities** for the third quarter of 2014 amounted to PLN 415 million in comparison to negative net cash flow of PLN 1,534 million in the analogical period of 2013.

The level of **cash flow from investing activities** in the third quarter of 2014 was mainly affected by:

- termination of deposits over 3 months PLN 2,024 million;
- expenses for the purchase of property, plant and equipment and intangible assets PLN (-) 1,627 million.

**Negative net cash flow from financial activities** in the third quarter of 2014 amounted to PLN 1,904 million in comparison to negative net cash flow of PLN 1,896 million in the third quarter of 2013.

**Cash flow from financial activities** in the third quarter of 2014 as well as in the third quarter of 2013 was mainly affected by the dividend paid to the shareholders.

## 2.2 Publication of financial forecasts

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

## 2.3 Other significant events of the reporting period and subsequent events

### 2.3.1 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 Gołębiowski	Supervisory Board Member, appointed on February 28, 2014
Piotr Machnikowski	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

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
Jacek Barylski	Member of the Supervisory Board
Jarosław Gołębiowski	Member of the Supervisory Board
Czesław Grzesiak	Member of the Supervisory Board - independent
Anna Kowalik	Secretary of the Supervisory Board
Piotr Machnikowski	Vice-Chairman of the Supervisory Board - independent
Małgorzata Mika – Bryska	Member of the Supervisory Board
Małgorzata Molas	Member of the Supervisory Board
Krzysztof Trochimiuk	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 Gołębiowski	Chairman of the Committee
Barbara Dybek	Committee Member
Anna Kowalik	Committee Member
Krzysztof Trochimiuk	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
Jacek Barylski	Committee Member
Czesław Grzesiak	Committee Member
Małgorzata Mika – Bryska	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 Gołębiowski	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
Anna Kowalik	Committee Member
Krzysztof Trochimiuk	Committee Member

### 2.3.2 Creation of Tax Capital Group

On September 18, 2014, an agreement concerning a tax group, named "PGK PGE 2015," was executed for a 25-year period. The PGK PGE 2015 tax group comprises PGE S.A. together with: PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE Dystrybucja S.A., PGE Obrót S.A., PGE Energia Odnawialna S.A., PGE Systemy S.A., PGE Energia Natury S.A., PGE Dom Maklerski S.A., ELBIS sp. z o.o., ELBEST sp. z o.o., ELTUR-SERWIS sp. z o.o., Betrans sp. z o.o., MegaSerwis sp. z o.o., MEGAZEC sp. z o.o., BESTGUM POLSKA sp. z o.o., ELMEN sp. z o.o., TOP SERWIS sp. z o.o. and 15 companies named PGE Inwest, PGE Inwest 2,3,...,15 that were not operational at the time the agreement was signed.

The Polish Corporate Income Tax Act treats tax groups as separate income tax payers. This means that companies within PGK PGE 2015 are not treated as separate entities for corporate income tax purposes, with PGK PGE 2015 being treated as one whole entity instead. PGK PGE 2015's tax base will constitute the group's aggregate income, calculated as the excess of the income of the companies that make up the group over their losses. PGK PGE 2015 is considered to be a separate entity only for the purposes of corporate income tax. This should not be equated with a separate legal entity. This also does not transfer over to other taxes, with particular emphasis on the fact that each of the companies within PGK PGE 2015 will continue to be a separate payer of VAT and tax on civil-law transactions, as well as withholding agent with respect to personal income tax.

The agreement will be effective after January 1, 2015. PGK PGE 2015 was registered by tax authorities on October 30, 2014.

Until December 31, 2014, PGE S.A. remains a member of a tax group established in 2011, which also includes PGE Systemy S.A. and PGE Obrót S.A.

### 2.3.3 Establishment of Eurobonds program

On May 22, 2014 PGE S.A. along with PGE Sweden AB (publ), 100% subsidiary of PGE S.A., established a Euro Medium Term Note Programme. Under the Programme PGE Sweden AB (publ) may issue Eurobonds up to EUR 2 billion with a minimum maturity of 1 year.

On June 9, 2014 PGE Sweden AB (publ) issued Eurobonds in the total amount of EUR 500 million with a five-year maturity. Then, on June 10, 2014 PGE Sweden AB (publ) concluded 3 loan agreements with PGE S.A. of EUR 514 million. The loans were granted for the period of 5 years.

On August 1, 2014 PGE Sweden AB (publ) issued Eurobonds in the total amount of EUR 138 million with a fifteen-year maturity. Then, on September 2, 2014 PGE Sweden AB (publ) concluded 2 loan agreements with PGE S.A. of EUR 144 million for the period of 15 years.

The total value of bonds issued as at the reporting date amounts to PLN 2,662 million (including PLN 2,612 million of long-term liabilities).

### 2.3.4 Activities related to nuclear energy

#### Business partnership

On January 28, 2014, the Council of Ministers adopted a resolution regarding the Polish Nuclear Power Program. Adoption of the Program was one of the conditions required by the shareholders agreement between PGE S.A., KGHM Polska Miedź S.A., Tauron Polska Energia S.A. and ENEA S.A. (further together as "Parties"). The second of the conditions was to obtain a favorable response from the President of the OCCP regarding the intention of the concentration.

On September 3, 2014 PGE S.A., TAURON Polska Energia S.A., ENEA S.A. and KGHM Polska Miedź S.A. concluded a Partners' Agreement. In accordance with the Partners' Agreement TAURON Polska Energia S.A., ENEA S.A. and KGHM Polska Miedź S.A., as Business Partners, will acquire from PGE, under a separate agreement, a total of 30% of shares (each Business Partner will acquire 10% of shares) in special purpose company - PGE EJ 1 sp. z o.o., which is responsible for preparation and execution of investment of construction and operating of the first nuclear power plant in Poland with a capacity of approx. 3,000 MWe (the "Project").

The Shareholders agreement was initialed on September 23, 2013, as a result of the work related to the development of a draft agreement for the acquisition of shares in the target company responsible for the construction and operation of the nuclear power plant. In accordance, the Parties stated that the initialed document was a draft of the future shareholders agreement, which would be signed after obtaining necessary corporate approvals of all Parties. As a result of the sale of 30% of shares in PGE EJ 1 sp. z o.o. to Business Partners:

- PGE S.A. will possess 70% of the share capital of PGE EJ1 sp. z o.o.,
- KGHM Polska Miedź S.A. will possess 10% of the share capital of PGE EJ1 sp. z o.o.,
- Tauron Polska Energia S.A. will possess 10% of the share capital of PGE EJ1 sp. z o.o.,
- ENEA S.A. will possess 10% of the share capital of PGE EJ1 sp. z o.o.

According to assumptions, PGE Group will be the leader of the Project and PGE EJ 1 sp. z o.o. will be a future operator of the power plant.

According to the Partners' Agreement, the parties jointly undertake to finance operations in years 2014-2016 under the initial phase of the Project (the "Initial Phase"), proportionally to their shareholdings. The Initial Phase is to determine such elements as potential partners, including strategic partner, technology providers, EPC contractor (Engineering, Procurement, Construction), a provider of nuclear fuel and obtaining financing for the Project, as well as organizational and competence preparation of PGE EJ 1 sp. z o.o. to the future role of nuclear power plant operator, responsible for its safe and efficient operation (the "Integrated Proceeding"). PGE's financial commitment in the Initial Phase will not exceed amount of approx. PLN 700 million.



The Parties of the Partners' Agreement anticipate that further decision on the Project, including decision on declaration of further participation of particular Parties in the next stage of the Project, will be made after the completion of the Initial Phase, directly before the settlement of the Integrated Proceeding.

Request for concentration was filed with the President of the Polish Office of Competition and Consumer Protection by the parties of the Partners' Agreement on August 1, 2014 and on October 7, 2014 the President of the Polish Office of Competition and Consumer Protection issued unconditional concentration approval for creation by the Applicants of a joint enterprise under the name PGE EJ 1 sp. z o.o. Obtaining of concentration approval is the condition precedent for conclusion of agreement for the acquisition of shares in PGE EJ 1 sp. z o.o., that was specified in the Partners' Agreement.

It is assumed that the agreement for sale of shares in PGE EJ 1 sp. z o.o. shall take place in the fourth quarter of 2014.

## **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 third quarter of 2014, the Contractor:

- Continued research and characterisation of the existing environmental conditions at both sites;
- Continued work on a transition report concerning the existing environmental conditions at both sites;
- Continued process of obtaining of geological works projects for Phase I of field works at both sites;
- Continued drafting the project data sheet ("KIP"), 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;
- Commenced meteorological monitoring in Żarnowiec;
- Commenced hydrological monitoring at both sites.

## **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.

On September 11, 2014 an agreement with AMEC Nuclear UK Ltd was concluded and preparations for co-operation with the advisor began. Issuance of first authorisations to the Owner's Engineer is planned for fourth quarter of 2014.

## 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.

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.

## Educational and information activities

In 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.

Nationwide and local public-opinion polls are performed cyclically, intended to monitor the level of support for the nuclear power plant project and the expectations relating to communications activities.

## Safety

In December 2013, a tender procedure was announced for a contractor to implement security architecture, including the Information Security Management System and business continuity procedures (in compliance with ISO 27001). There was one tender submitted, and the procedure was closed without making a selection. In June 2014, the tender procedure was again announced. As a result, a contractor for the above architecture was selected – Ernst & Young sp. z .o.o. Business Advisory sp. k. On October 1, 2014, an agreement for performance of works was signed with the above contractor, providing for their completion within 16 months from the agreement date, spread out over four phases. Works being performed under phase 1 of the agreement are expected to be completed by the end of the fourth quarter of 2014.

### 2.3.5 Legal aspects

#### Information regarding Shanghai Electric Group Company Limited's complaint

PGE Górnictwo i Energetyka Konwencjonalna S.A. carried out a public tender procedure for the "Construction of a new power unit at Turów power plant" and selected the most favourable tender from a consortium comprising: Mitsubishi Hitachi Power Systems Europe GmbH (consortium leader), Budimex S.A. and Tecnicas Reunidas SA. Following the appeals of two contractors: Shanghai Electric Group Company Limited and Doosan Heavy Industries & Construction Co. Ltd, the National Appeals Chamber (KIO) on May 23, 2014 issued a ruling that dismissed both of the appeals..

On July 18, 2014, PGE Górnictwo i Energetyka Konwencjonalna S.A. received a copy of a complaint concerning KIO's ruling of May 23, 2014, addressed to the District Court in Łódź, 10th Commercial Division, made by the complainant – Shanghai Electric Group Company Limited – with the intermediation of the President of the KIO.

On October 24, 2014, the court issued a ruling that dismissed the complaint made by Shanghai Electric Group Company Limited.

## Claims for annulment of the resolutions of the General Shareholders Meetings

On April 1, 2014 and on September 17, 2014 PGE S.A. received a copies of lawsuits filed to the District Court of Warsaw by one of the shareholders. In the lawsuits, the shareholder is seeking for annulment of the resolutions 1, 2 and 4 of the Extraordinary General Shareholders Meeting of the Company held on February 6, 2014 and for annulment of the resolution 4 of the Ordinary General Shareholders Meeting of the Company held on June 6, 2014. The Company filed responses to the claims.

### 2.3.6 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);
- 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 September 30, 2014
Powszechna Kasa Oszczędności Bank Polski S.A.	2014-01-20	2019-08-20	2,548,607,358	2,343,418,460
Bank Polska Kasa Opieki S.A.	2014-01-20	2019-08-20	424,767,893	390,569,743
BNP Paribas Bank Polska S.A.	2014-01-20	2019-08-20	424,767,893	390,569,743
<b>TOTAL</b>			<b>3,398,143,144</b>	<b>3,124,557,946</b>

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

Guarant or	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 September 30, 2014 in PLN	Value of the guarantee as at September 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	212.266.165.0	254.719.397
PGE S.A.	Guarantee	bank guarantee of payment	Powszechna Kasa Oszczędności i Bank Polski S.A.	PGE GiEK S.A.	2014-01-22	2014-01-29	2020-03-31	1.273.596.987.0	1.528.316.385
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	212.266.165.0	254.719.397
<b>Total</b>								<b>1.698.129.316.0</b>	<b>2.037.755.180</b>

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

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”) (see p. 2.3.5 of this report).

Subject matter of the Agreement is designing and turn-key construction of 450 MWe supercritical 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.

### **2.3.7 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 three quarters of 2014:

- Final sentences, favourable for the Group, were made in the proceedings concerning appeals against the President of ERO decisions regarding the annual adjustment of stranded costs for PGE GiEK S.A. Branch Rzeszów CHP for the year 2009, PGE GiEK S.A. Branch Opole Power Plant for the year 2009 and PGE GiEK S.A. for the year 2010. The amount of dispute in these cases was PLN 680 million.
- A favourable verdict of the Court of Appeal was issued in case of annual adjustments costs related to natural gas fired entities for PGE GiEK S.A. Branch Lublin Wrotków CHP for the year 2009. Claim value in the above case is PLN 7 million.
- CCP Court issued a sentence which considered part of the appeal of PGE GiEK S.A. and changed the decision of the President of ERO from July 2011 regarding the amount of the annual adjustment of the stranded costs due to PGE GiEK S.A. Branch Opole Power Plant for the year 2010. Based on the CCP Court sentence, the annual adjustment of the stranded costs due to PGE GiEK S.A. Branch Opole Power Plant for the year 2010 amounted to approximately PLN (-) 50 million including interests.
- On August 11, 2014, PGE GiEK S.A. received an administrative decision from the President of ERO regarding the amount of the annual adjustment of the stranded costs for the year 2013. In accordance with the decision of the President of ERO, the annual adjustment of stranded costs incurred in the manufacturing units: Branch Turów Power Plant and Branch Opole Power Plant for the year 2013 amounted to approximately PLN (+) 438 million. The Group considers this amount as undisputable.

On October 8, 2014, the Supreme Court examined a cassation appeal from the President of ERO against a ruling by the Court of Appeal regarding the amount of annual corrections in stranded costs for PGE GiEK S.A. – Branch ZEDO for 2009. The Supreme Court has not yet issued a final decision regarding the appeal and has submitted an inquiry to the Court of Justice of the European Union.

## Impact on the financial statements for the period ended September 30, 2014

In the financial statements for the period ended September 30, 2014, the Group recognized LTC revenue in sales revenue in the amount of PLN 1,354 million. In this value, the amount of approximately PLN 911 million relates mainly to the revaluation of the LTC compensation model, which was caused by the change in assumptions used to calculate the final adjustment (including in particular the change in the discount rate). The rationale for the introduced changes in assumptions was the information regarding the decision of the President of ERO concerning the final adjustment submitted to one of the producers which is covered by the compensation system.

In addition, the final judgments of the Court of Appeal on PGE GiEK S.A. Branch Opole Power Plant, GiEK S.A. Branch Rzeszów CHP and PGE GiEK S.A. caused an LTC compensation adjustment of approximately PLN 246 million recorded in the financial statements for the period ended September 30, 2014. The adjustment value is recognized in the statement of comprehensive income under other operating income.

The amount of disputes in all matters relating to the years 2008 – 2012 amount to PLN 1,660 million, including the amount of disputes favourably resolved for PGE Group by the Court of Appeal and a favourable final judgment regarding CCP Court in the amount of PLN 1,429 million.

## 2.4 Description of the organization of the PGE Capital Group

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

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

## 2.4.1 Changes in organisation of the Capital Group

### 2.4.1.1 Changes in organisation of the Capital Group in the third quarter of 2014

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

#### Shares in subsidiaries and associates

In the first three quarters 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 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 S.A. concerning the sale of shares in Stockholm-based Goldcup 5812 AB (publ.). Pursuant to the share sale agreement, PGE S.A. purchased 500,000 shares in Goldcup 5812 AB (publ.), constituting 100% of its share capital. PGE 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 S.A., in the amount of PLN 15,000,000, which constitutes 20.55% of the nominal value of the shares held by PGE 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 S.A. in exchange for a cash contribution. On June 10, 2014, the share capital increase was registered with the Swedish Companies Register.
- On June 23, 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 36,500,000 to PLN 37,000,000 i.e. by PLN 500,000 through the issue of 500 new registered shares with a nominal value of PLN 1,000 each and issue price of PLN 120,000 each. All of the shares in the increased capital were acquired by PGE S.A. in exchange for a cash contribution. On September 2, 2014 the share capital increase was registered with the National Court Register.
- On July 9, 2014 Exatel S.A. and Telestrada S.A. seated in Warsaw concluded a conditional agreement for sale of 100% of shares of Niezależny Operator Międzysztrefowy sp. z o.o. with its seat in Warsaw. On September 26, 2014 General Meeting of Exatel S.A. gave its approval for sale of 100% of the company. On September 29, 2014 Telestrada S.A. paid for the shares and ownership of shares was transferred on this date.
- On August 18, 2014 the Extraordinary General Meeting of PGE Sweden AB (publ) adopted a resolution on an increase of the company's share capital from SEK 191,000,000 to SEK 245,000,000 SEK, i.e. by SEK 54,000,000, through the issue of 54,000,000 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 S.A. in exchange for a cash contribution. On August 26, 2014, the share capital increase was registered with the Swedish Companies Register.
- On August 29, 2014, PGE S.A. executed share sale agreements pursuant to which it purchased 100% of shares in the following subsidiaries:
  - 1) ELBEST sp. z o.o.,
  - 2) PTS Betrains sp. z o.o.,
  - 3) ELBIS sp. z o.o.,
  - 4) BESTGUM POLSKA sp. z o.o.,
  - 5) MegaSerwis sp. z o.o.,
  - 6) TOP SERWIS sp. z o.o.,
  - 7) ELTUR-SERWIS sp. z o.o.,
  - 8) MEGAZEC sp. z o.o.,
  - 9) ELMEN sp. z o.o.

As of August 31, 2014 ownership of shares of above mentioned companies was transferred to PGE S.A., in accordance with the share sale agreements.

- On September 10, 2014 PGE S.A. concluded donation agreements with PGE Obrót S.A. with its seat in Rzeszów. Subject matter of the donation agreements is 874,905,583 ordinary bearer shares of PGE Dystrybucja S.A. with its seat in Lublin, with a nominal value of PLN 10 each (aggregate nominal value of the shares acquired by PGE S.A. amounts to PLN 8,749,055,830) and 34,473,704 registered shares of PGE Górnictwo i Energetyka Konwencjonalna S.A. with its seat in Bełchatów, with a nominal value of PLN 10 each (aggregate nominal value of the shares acquired by PGE S.A. amounts to PLN 344,737,040). Above shares represent respectively 89.91% of the share capital of PGE Dystrybucja S.A. and 4.95% of the share capital of of PGE Górnictwo i Energetyka Konwencjonalna S.A. and entitle to perform respectively 874,905,583 votes at the general meeting of PGE Dystrybucja S.A., representing 89.92% at the general meeting of PGE Dystrybucja S.A. and 344,737,040 votes, representing 4.95% at the general meeting of PGE GiEK S.A. As a consequence of the donations PGE S.A. became the sole shareholder of PGE Dystrybucja S.A., holding a total of 972,942,416 shares constituting 99.99% in the share capital and 100% at the general meeting of PGE Dystrybucja S.A. (PGE Dystrybucja S.A. holds 131,873 treasury shares constituting 0.01% in the share capital - a resolution of the Extraordinary General Meeting of PGE Dystrybucja of September 5, 2014 on redemption of treasury shares concerns these shares). Moreover, PGE S.A. currently holds 99.21% in the share capital of PGE GiEK S.A. As a result of donations PGE Obrót S.A. lost its status of shareholder of PGE Dystrybucja S.A. and PGE GiEK S.A.
- On September 11, 2014 the Extraordinary General Meeting of PGE Energia Odnawialna S.A. adopted a resolution on merger of PGE Energia Odnawialna S.A. (the acquiring company) with Żuromin sp. z o.o. (the acquired company), through transfer of all assets of the acquired company to the acquiring company without the exchange of acquired company's shares for the shares of the acquiring company, by course of art. 514 of Code of Commercial Companies. PGE Energia Odnawialna S.A. held 100% in the share capital of Żuromin sp. z o.o. On September 30, 2014 the merger of the companies was registered in the National Court Register.
- On July 15, 2014 roku PGE S.A. set up 14 special purpose companies in form of limited companies with the following names (date of the registration of the company is presented in brackets) i.e.: PGE Inwest 2 sp. z o.o. (August 19, 2014); PGE Inwest 3 sp. z o.o. (August 25, 2014); PGE Inwest 4 sp. z o.o. (August 25, 2014); PGE Inwest 5 sp. z o.o. (August 19, 2014); PGE Inwest 6 sp. z o.o. (August 27, 2014); PGE Inwest 7 sp. z o.o. (September 5, 2014); PGE Inwest 8 sp. z o.o. (September 12, 2014); PGE Inwest 9 sp. z o.o. (August 26, 2014); PGE Inwest 10 sp. z o.o. (August 26, 2014); PGE Inwest 11 sp. z o.o. (September 12, 2014); PGE Inwest 12 sp. z o.o. (August 19, 2014); PGE Inwest 13 sp. z o.o. (August 25, 2014); PGE Inwest 14 sp. z o.o. (September 12, 2014); PGE Inwest 15 sp. z o.o. (August 21, 2014) with a share capital of PLN 10,000 each.

In period January 1, 2014 – September 30, 2014 PGE S.A. purchased from minority shareholders – on ground of share sale agreements - a total of 4,413,347 shares of PGE GiEK S.A. (constituting 0.6337% in the share capital of PGE GiEK S.A.). As at September 30, 2014 PGE S.A. directly held 99.2% of shares in the share capital of PGE GiEK S.A. (share including treasury shares held by PGE GiEK S.A.).



In the three quarters 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” Wraclawek 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 1,000 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.

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 August 21, 2014 PGE Dystrybucja S.A. and TECHNITEL POLSKA S.A. seated in Łódź concluded an agreement for sale of 2,639 shares of Zakład Obsługi Energetyki sp. z o.o. with its seat in Zgierz, held by PGE Dystrybucja S.A., representing 100% of the company's share capital. On August 22, 2014, TECHNITEL POLSKA S.A. paid for the shares and ownership of shares was transferred on this date.

During the period from January 1, 2014 to September 30, 2014, PGE GiEK S.A., through a squeeze-out of shares pursuant to art. 418<sup>1</sup> § 4 of the Polish Commercial Companies Code, purchased a total of 637,561 treasury shares from minority shareholders, constituting 0.0915% of PGE GiEK S.A.'s share capital.

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

#### **2.4.1.2 Changes in Group structure after the end of the reporting period**

On September 12, 2014 the Extraordinary General Meeting of PGE Energia Natury S.A. adopted a resolution on an increase of the share capital from PLN 6,000,000 to PLN 51,300,000 i.e. by PLN 45,300,000, through the issue of 45,300 new registered shares with a nominal value and issue price of PLN 1,000 each. All shares in the company's increased share capital were acquired by PGE S.A. in exchange for a non-cash contribution in the form of 100% of shares in the following companies: PGE Energia Natury Bukowo sp. z o.o., PGE Energia Natury Karnice sp. z o.o. and PGE Energia Natury Olecko sp. z o.o. On October 8, 2014 the increase of the share capital was registered in the National Court Register.

On October 8, 2014 PGE S.A. set up a limited company with the following name: PGE Inwest 16 sp. z o.o. On October 29, 2014 the company was registered in the National Court Register.

On October 15, 2014 the Extraordinary General Meeting of PGE GiEK S.A. adopted a resolution on squeeze-out of shares held by minority shareholders PGE S.A., pursuant to art. 418 of Code of Commercial Companies. The squeeze-out included 2,772,703 shares held by minority shareholders, representing 0.3981% in the share capital of PGE GiEK S.A.

On November 6, 2014 PGE S.A. and Polskie Towarzystwo Przesyłu i Rozdziału Energii Elektrycznej with its seat in Poznań concluded an agreement for sale of 1,300 shares of Exatel S.A. held by Polskie Towarzystwo Przesyłu i Rozdziału Energii Elektrycznej, representing 0.02% of the company's share capital. The ownership of shares was transferred to PGE S.A. on November 6, 2014. As a result of the transaction PGE S.A. became the sole shareholder of the company.

### 3 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 quarterly 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 of PGE 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%
<b>TOTAL</b>	<b>1,869,760,829</b>	<b>1,869,760,829</b>	<b>100.00%</b>

\* 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

### 4 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 quarterly report

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

Shareholder	Number of shares as of publication date of the H1 2014 report (i.e. August 27, 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)
<b>Management Board</b>	<b>350</b>	<b>No change</b>	<b>350</b>	<b>3,500</b>
Grzegorz Krystek	350	No change	350	3,500
<b>Supervisory Board</b>	<b>873</b>	<b>No change</b>	<b>873</b>	<b>8,730</b>
Krzysztof Trochimiuk	873	No change	873	8,730

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

## **5 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. 2.4.1. of the foregoing report.

## **6 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. 2.3.3 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.

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

As at September 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.

Warsaw, November 12, 2014

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

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*Marek Woszczyk*

*President of the Management Board*

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*Jacek Drozd*

*Vice-President of the  
Management Board*

*Grzegorz Krystek*

*Vice-President of the  
Management Board*

*Dariusz Marzec*

*Vice-President of the  
Management Board*