PGE Polska Grupa Energetyczna S.A. Consolidated Financial Statements for the year 2016

ended December 31, 2016

in accordance with IFRS EU (in PLN million)

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for the year 2016 in accordance with IFRS EU (in PLN million)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended December 31, 2016	Year ended December 31, 2015
STATEMENT OF PROFIT OR LOSS			
SALES REVENUES	7.1	**28,092**	**28,542**
Costs of goods sold	7.2	(23,174)	(30,066)
GROSS PROFIT/(LOSS) ON SALES		**4,918**	**(1,524)**
Distribution and selling expenses	7.2	(1,429)	(1,408)
General and administrative expenses	7.2	(977)	(825)
Other operating income	7.3	1,171	431
Other operating expenses	7.3	(171)	(263)
OPERATING PROFIT/(LOSS)		**3,512**	**(3,589)**
Financial income	7.4	191	156
Financial expenses	7.4	(384)	(323)
Share of profit/(loss) of entities accounted for using the equity method	7.5	(45)	-
PROFIT/(LOSS) BEFORE TAX		**3,274**	**(3,756)**
Current income tax	8.1	(414)	(461)
Deferred income tax	8.1	(294)	1,180
NET PROFIT/(LOSS) FOR THE REPORTING PERIOD		**2,566**	**(3,037)**
OTHER COMPREHENSIVE INCOME			
Items, which may be reclassified to profit or loss, including:			
Valuation of financial instruments	20.2	1	-
Valuation of hedging instruments	20.2	206	49
Foreign exchange differences from translation of foreign entities	20.3	4	-
Deferred tax	8.1	(39)	(9)
Items, which will not be reclassified to profit or loss, including:			
Actuarial gains and losses from valuation of provisions for employee benefits	22	249	15
Deferred tax	8.1	(47)	(3)
Share of profit/(loss) of entities accounted for using the equity method	7.5	(2)	-
OTHER COMPREHENSIVE INCOME FOR THE REPORTING PERIOD, NET		**372**	**52**
TOTAL COMPREHENSIVE INCOME		**2,938**	**(2,985)**
NET PROFIT/(LOSS) ATTRIBUTABLE TO:			
– equity holders of the parent company		2,568	(3,032)
– non-controlling interests		(2)	(5)
COMPREHENSIVE INCOME ATTRIBUTABLE TO :			
– equity holders of the parent company		2,940	(2,980)
– non-controlling interests		(2)	(5)
EARNINGS AND DILUTED EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT COMPANY (IN PLN)	20.7	**1.37**	**(1.62)**

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	As at December 31, 2016	As at December 31, 2015
NON-CURRENT ASSETS			
Property, plant and equipment	9	51,365	47,068
Investment property	10	27	30
Intangible assets	11	653	904
Financial receivables	25.1.1	237	142
Derivatives	25.1.2	356	43
Available-for-sale financial assets	25.1.3	37	15
Shares accounted for using the equity method	12	402	8
Other non-current assets	16.1	730	1,063
Deferred tax assets	13.1	268	313
		54,075	**49,586**
CURRENT ASSETS			
Inventories	14	1,596	1,959
CO_2 emission rights for own use	15	2,349	2,172
Income tax receivables		19	101
Derivatives	25.1.2	9	7
Trade and other financial receivables	25.1.1	6,325	3,748
Available-for-sale financial assets	25.1.3	4	4
Other current assets	16.2	416	599
Cash and cash equivalents	17	2,669	3,104
Assets classified as held-for-sale		12	16
		13,399	**11,710**
TOTAL ASSETS		**67,474**	**61,296**
EQUITY			
Share capital	20.1	19,165	18,698
Hedging reserve	20.2	147	(21)
Foreign exchange differences from translation of foreign entities	20.3	3	(1)
Reserve capital	20.4	13,730	13,009
Retained earnings	20.5	9,634	8,636
EQUITY ATTRIBUTED TO EQUITY HOLDERS OF THE PARENT COMPANY		**42,679**	**40,321**
Non-controlling interests	20.6	96	96
TOTAL EQUITY		**42,775**	**40,417**
NON-CURRENT LIABILITIES			
Non-current provisions	21	5,004	6,044
Loans, borrowings, bonds and lease	25.1.4	9,603	5,118
Derivatives	25.1.2	30	55
Deferred tax liabilities	13.2	1,191	852
Deferred income and government grants	23.1	1,141	1,192
Other financial liabilities	25.1.5	33	34
		17,002	**13,295**
CURRENT LIABILITIES			
Current provisions	21	2,181	1,809
Loans, borrowings, bonds and lease	25.1.4	411	291
Derivatives	25.1.2	-	34
Trade and other financial liabilities	25.1.5	3,556	3,945
Income tax liabilities		6	5
Deferred income and government grants	23.2	119	112
Other current non-financial liabilities	24	1,424	1,388
		7,697	**7,584**
TOTAL LIABILITIES		**24,699**	**20,879**
TOTAL EQUITY AND LIABILITIES		**67,474**	**61,296**

for the year 2016 in accordance with IFRS EU (in PLN million)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	EQUITY ATTRIBUTED TO EQUITY HOLDERS OF THE PARENT COMPANY							
	Share capital	Hedging reserve	Foreign exchange differences from translation of foreign entities	Reserve capital	Retained earnings	TOTAL	Non-controlling interests	TOTAL EQUITY
Note	20.1	20.2	20.3	20.4	20.5		20.6	
AS AT JANUARY 1, 2015	**18,698**	**(61)**	**(1)**	**9,231**	**16,901**	**44,768**	**116**	**44,884**
Net loss for the reporting period	-	-	-	-	(3,032)	**(3,032)**	**(5)**	**(3,037)**
Other comprehensive income	-	40	-	-	12	**52**	-	**52**
COMPREHENSIVE INCOME	**-**	**40**	**-**	**-**	**(3,020)**	**(2,980)**	**(5)**	**(2,985)**
Retained earnings distribution	-	-	-	3,778	(3,778)	**-**	-	**-**
Dividend	-	-	-	-	(1,458)	**(1,458)**	(4)	**(1,462)**
Changes within the PGE Group	-	-	-	-	-	**-**	68	**68**
Acquisition of additional shares in subsidiaries	-	-	-	-	(10)	**(10)**	(78)	**(88)**
Other changes	-	-	-	-	1	**1**	(1)	**-**
TRANSACTIONS WITH OWNERS	**-**	**-**	**-**	**3,778**	**(5,245)**	**(1,467)**	**(15)**	**(1,482)**
AS AT DECEMBER 31, 2015	**18,698**	**(21)**	**(1)**	**13,009**	**8,636**	**40,321**	**96**	**40,417**
Net profit for the reporting period	-	-	-	-	2,568	**2,568**	**(2)**	**2,566**
Other comprehensive income	-	168	4	-	200	**372**	-	**372**
COMPREHENSIVE INCOME	**-**	**168**	**4**	**-**	**2,768**	**2,940**	**(2)**	**2,938**
Retained earnings distribution	-	-	-	1,301	(1,301)	-	-	-
Dividend	-	-	-	-	(467)	**(467)**	(4)	**(471)**
Increase of share capital	467	-	-	(467)	-	**-**	10	**10**
Tax related to the increase of the share capital	-	-	-	(110)	-	**(110)**	-	**(110)**
Acquisition of additional shares in subsidiaries	-	-	-	-	(2)	**(2)**	(4)	**(6)**
Other changes	-	-	-	(3)	-	**(3)**	-	**(3)**
TRANSACTIONS WITH OWNERS	**467**	**-**	**-**	**721**	**(1,770)**	**(582)**	**2**	**(580)**
AS AT DECEMBER 31, 2016	**19,165**	**147**	**3**	**13,730**	**9,634**	**42,679**	**96**	**42,775**

for the year 2016 in accordance with IFRS EU (in PLN million)

CONSOLIDATED STATEMENT OF CASH FLOWS

	Note	Year ended December 31, 2016	Year ended December 31, 2015
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit/(loss) before tax		**3,274**	**(3,756)**
Income tax paid		(327)	(616)
Adjustments for:			
Share of profit/ (loss) of entities accounted for using the equity method		45	-
Depreciation, amortization, disposal and impairment losses		3,864	11,817
Interest and dividend, net		116	134
Profit / loss on investment activities	27.1	(131)	(28)
Change in receivables	27.1	(275)	(236)
Change in inventories	27.1	342	224
Change in liabilities, excluding loans and borrowings	27.1	(169)	318
Change in other non-financial assets, prepayments and CO_2 emission rights	27.1	(96)	(860)
Change in provisions	27.1	(244)	(348)
Other		(8)	128
NET CASH FROM OPERATING ACTIVITIES		**6,391**	**6,777**
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from sale of property, plant and equipment and intangible assets		18	39
Acquisition of property, plant and equipment and intangible assets	27.2	(7,935)	(8,606)
Proceeds from sale of financial assets		-	74
Deposits with a maturity over 3 months	27.2	(2,867)	(243)
Termination of deposits over 3 months	27.2	566	233
Acquisition of financial assets and increase in shareholding in the PGE Group companies	27.2	(467)	(97)
Other		29	6
NET CASH FROM INVESTING ACTIVITIES		**(10,656)**	**(8,594)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from sale of non-controlling interests		10	-
Proceeds from loans, borrowings and issue of bonds	27.3	4,652	648
Repayment of loans, borrowings, bonds and finance lease	27.3	(203)	(311)
Dividends paid	27.3	(471)	(1,462)
Interest paid	27.3	(196)	(176)
Other		38	36
NET CASH FROM FINANCING ACTIVITIES		**3,830**	**(1,265)**
CHANGE IN CASH AND CASH EQUIVALENTS		**(435)**	**(3,082)**
Effect of movements in exchange rates on cash held		1	4
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	17	**3,101**	**6,183**
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	17	**2,666**	**3,101**
Restricted cash		107	333

GENERAL INFORMATION, BASIS FOR PREPARATION OF THE FINANCIAL STATEMENTS AND OTHER EXPLANATORY INFORMATION

1. General information

1.1 Information about the parent company

PGE Polska Grupa Energetyczna S.A. („parent company", „the Company", „PGE S.A.") was founded on the basis of the Notary Deed of August 2, 1990 and registered in the District Court in Warsaw, XVI Commercial Department on September 28, 1990. The Company was registered in the National Court Register of the District Court for the capital city of Warsaw, XII Commercial Department, under no. KRS 0000059307. The parent company is seated in Warsaw, 2 Mysia Street.

As at January 1, 2016 the composition of the Company's Management Board was as follows::

- Marek Woszczyk – the President of the Management Board
- Jacek Drozd – the Vice-President of the Management Board,
- Grzegorz Krystek – the Vice-President of the Management Board,
- Dariusz Marzec – the Vice-President of the Management Board.

From January 1, 2016 till December 31, 2016 the following changes occurred in the composition of the Management Board:

- On January 29, 2016 the Supervisory Board recalled Mr. Jacek Drozd and Mr. Dariusz Marzec from the Management Board and delegated its member – Mr. Marek Pastuszko – to temporarily perform the duties of Vice-President of the Management Board for the 3-month period.
- On February 25, 2016 the Supervisory Board cancelled delegation of Mr. Marek Pastuszko to temporarily perform the duties of Member of the Management Board and appointed him to the position of Vice-President of the Management Board.
- On February 26,2016 the Supervisory Board appointed Mr. Emil Wojtowicz to the Management Board as from March 15,2016 entrusting him the position of Vice-President of the Management Board and appointed Mr. Ryszard Wasiłek to the Management Board as from March 7,2016 entrusting him the position of Vice-President of the Management Board.
- On March 2, 2016 Mr. Marek Woszczyk and Mr. Grzegorz Krystek submitted resignations from their positions in the Management Board as from March 30, 2016.
- On March 22, 2016 Mr. Paweł Śliwa submitted his resignation from the Supervisory Board and the Supervisory Board appointed four members of the Management Board as from March 31, 2016: Mr. Henryk Baranowski, entrusting him the position of President of the Management Boad and Ms. Marta Gajęcka, Mr. Bolesław Jankowski and Mr. Paweł Śliwa to the positions of Vice-Presidents of the Management Board.

As at December 31,2016 the composition of the Company's Management Board was as follows:

- Henryk Baranowski – the President of the Management Board,
- Marta Gajęcka – the Vice-President of the Management Board,
- Bolesław Jankowski – the Vice-President of the Management Board,
- Marek Pastuszko – the Vice-President of the Management Board,
- Paweł Śliwa – the Vice-President of the Management Board,
- Ryszard Wasiłek – the Vice-President of the Management Board,
- Emil Wojtowicz – the Vice-President of the Management Board.

After the reporting date, on February 13, 2017, the Supervisory Board recalled all Members of Management Board effective from February 13, 2017. At the same time, the Supervisory Board appointed the following individuals to the 10th term of the Management Board effective from February 14, 2017: Mr. Henryk Baranowski, entrusting him the position of President of the Management Board, Mr. Bolesław Jankowski, Mr. Wojciech Kowalczyk, Mr. Marek Pastuszko, Mr. Paweł Śliwa, Mr. Ryszard Wasiłek and Mr. Emil Wojtowicz to the positions of Vice-Presidents of the Management Board.

As at the date of publication of these financial statements the composition of the Company's Management Board is as follows:

- Henryk Baranowski – the President of the Management Board,
- Bolesław Jankowski – the Vice-President of the Management Board,
- Wojciech Kowalczyk – the Vice-President of the Management Board,
- Marek Pastuszko – the Vice-President of the Management Board,
- Paweł Śliwa – the Vice-President of the Management Board,
- Ryszard Wasiłek – the Vice-President of the Management Board,
- Emil Wojtowicz – the Vice-President of the Management Board.

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

Ownership structure

As at December 31, 2016 the ownership structure of the parent company is as follows:

	State Treasury	Other shareholders	Total
As at December 31, 2015	58.39%	41.61%	100.00%
As at December 31, 2016	57.39%	42.61%	100.00%

Ownership structure for particular reporting dates was presented in accordance with all information obtained and available for the Company.

As of March 30, 2016 the State Treasury transferred 18,697,608 shares, constituting 1% of the share capital of the Company. According to information received from the Ministry of the State Treasury, after the transaction the State Treasury holds 57.39% in the share capital of the Company. According to information available in the Company as at the date of publication of these financial statements the sole shareholder who holds at least 5% of votes at the General Meeting of PGE S.A. is the State Treasury.

1.2 Information about the PGE Group

PGE Polska Grupa Energetyczna S.A. Group („PGE Capital Group", „PGE Group", „Group", „CG PGE") comprises the parent company PGE Polska Grupa Energetyczna S.A., 51 consolidated subsidiaries, 2 associates and 1 jointly controlled entity. As described in note 33.2, in the current period the Group gained significant influence on Polska Grupa Górnicza sp. z o.o. and consolidates this company under the equity method. For additional information about subsidiaries included in the consolidated financial statements please refer to note 1.3.

These consolidated financial statements of the PGE Group comprise financial data for the period from January 1, 2016 to December 31, 2016 („financial statements", „consolidated financial statements") and include comparative data for the period from January 1, 2015 to December 31, 2015.

The financial statements of all affiliated companies were prepared for the same reporting period as the financial statements of the parent company, using consistent accounting principles.

Core operations of the PGE Group companies are as follows:

- production of electricity,
- distrubution of electricity,
- wholesale and retail sale of electricity, energy origin rights, CO_2 emission rights and gas,
- production and distribution of heat,
- rendering of other services related to the above mentioned activities.

Business activities are conducted under appropriate concessions granted to particular Group companies.

Going concern

These consolidated financial statements were prepared under the assumption that the Group companies will continue to operate as a going concern in the foreseeable future. As at the date of the approval of these consolidated financial statements, there is no evidence indicating that the significant Group companies will not be able to continue its business activities as a going concern.

for the year 2016 in accordance with IFRS EU (in PLN million)

1.3 Structure of the PGE Group

During the reporting period, the PGE Group consisted of the enumerated below subsidiaries, consolidated directly and indirectly:

	Entity	Entity holding shares	Share of the Group entities as at December 31, 2016	Share of the Group entities as at December 31, 2015
	SEGMENT: SUPPLY			
1.	PGE Polska Grupa Energetyczna S.A. Warsaw	The parent company		
2.	PGE Dom Maklerski S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
3.	PGE Trading GmbH Berlin	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
4.	PGE Obrót S.A. Rzeszów	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
5.	ENESTA sp. z o.o. Stalowa Wola	PGE Obrót S.A.	87.33%	87.33%
	SEGMENT: CONVENTIONAL GENERATION			
6.	PGE Górnictwo i Energetyka Konwencjonalna S.A. Bełchatów	PGE Polska Grupa Energetyczna S.A.	99.98%	99.96%
7.	ELBIS sp. z o.o. Rogowiec	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
8.	MEGAZEC sp. z o.o. Bydgoszcz	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
9.	MegaSerwis sp. z o.o. Bogatynia	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
10	„ELMEN" sp. z o.o. Rogowiec	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
11	Przedsiębiorstwo Usługowo-Produkcyjne „ELTUR-SERWIS" sp. z o.o. Bogatynia	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
12	Przedsiębiorstwo Usługowo-Produkcyjne „TOP SERWIS" sp. z o.o. Bogatynia	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
13	Przedsiębiorstwo Transportowo-Sprzętowe „BETRANS" sp. z o.o. Bełchatów	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
14	Przedsiębiorstwo Wulkanizacji Taśm i Produkcji Wyrobów Gumowych BESTGUM POLSKA sp. z o.o. Rogowiec	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
15	RAMB sp. z o.o. Piaski	PGE Polska Grupa Energetyczna S.A.	100.00%	-
		PGE Górnictwo i Energetyka Konwencjonalna S.A.	-	100.00%
16	EPORE sp. z o.o. Bogatynia	PGE Górnictwo i Energetyka Konwencjonalna S.A.	85.38%	85.38%
17	„Energoserwis – Kleszczów" sp. z o.o. Rogowiec	PGE Górnictwo i Energetyka Konwencjonalna S.A.	51.00%	51.00%
18	Przedsiębiorstwo Energetyki Cieplnej sp. z o.o. Zgierz	PGE Górnictwo i Energetyka Konwencjonalna S.A.	50.98%	50.98%
	SEGMENT: RENEWABLES			
19	PGE Energia Odnawialna S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
20	Elektrownia Wiatrowa Baltica-1 sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
21	Elektrownia Wiatrowa Baltica-2 sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
22	Elektrownia Wiatrowa Baltica-3 sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
23	PGE Energia Natury sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
	PGE Energia Natury Omikron sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	-	100.00%
24	PGE Energia Natury PEW sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%

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	SEGMENT: DISTRIBUTION			
25	PGE Dystrybucja S.A. Lublin	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
	SEGMENT: OTHER OPERATIONS			
26	PGE EJ 1 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	70.00%	70.00%
27	PGE Systemy S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
28	EXATEL S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
29	PGE Sweden AB (publ) Stockholm	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
30	PGE Obsługa Księgowo-Kadrowa sp. z o.o. Lublin	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
31	„Elbest” sp. z o.o. Bełchatów	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
32	Elbest Security sp. z o.o. Bełchatów	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
33	PGE Inwest 2 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
	PGE Inwest 4 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	-	100.00%
34	PGE Inwest 5 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
35	PGE Inwest 6 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
36	PGE Inwest 7 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
37	PGE Inwest 8 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
38	PGE Inwest 9 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
39	PGE Inwest 10 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
40	PGE Inwest 11 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
41	PGE Inwest 12 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
42	PGE Inwest 13 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
43	PGE Inwest 14 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
44	PGE Inwest 15 sp. z o.o. Warszawa	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
45	PGE Inwest 16 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
46	PGE Inwest 17 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	-
47	PGE Inwest 18 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	-
48	PGE Towarzystwo Funduszy Inwestycyjnych S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	-
49	ENERGO-TEL S.A. Warsaw	EXATEL S.A.	100.00%	100.00%
50	BIO-ENERGIA sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
51	Przedsiębiorstwo Transportowo-Usługowe „ETRA” sp. z o.o. Białystok	PGE Dystrybucja S.A.	100.00%	100.00%
52	Energetyczne Systemy Pomiarowe sp. z o.o. Białystok	PGE Dystrybucja S.A.	100.00%	100.00%

The table above includes the following changes in the structure of the PGE Group companies subject to full consolidation which took place during the year ended December 31, 2016:

- On March 10, 2016 PGE Polska Grupa Energetyczna S.A. and PGE Górnictwo i Energetyka Konwencjonalna S.A. concluded agreement for purchase of 100% shares of subsidiary RAMB sp. z o.o. The transaction had no impact on these financial statements.
- On August 17, 2016 the Extraordinary General Meeting of PGE Energia Natury PEW sp. z o.o. and PGE Energia Natury Omikron sp. z o.o. (subsidiaries of PGE Energia Odnawialna S.A.) adopted resolutions on merger of PGE Energia Natury PEW sp. z o.o. (the Acquiring Company) with PGE Energia Natury Omikron sp. z o.o. (the Acquired Company). The merger of the companies was executed through the transfer to the Acquiring Company of all of the assets of the Acquired Company and subsequent dissolution of the Acquired Company without liquidation. On August 31, 2016 the merger of the companies was registered in the National Court Register and the Acquired Company was deleted from the National Court Register. The merger had no impact on these financial statements.
- On September 15, 2016 PGE Polska Grupa Energetyczna S.A. set up two companies: PGE Inwest 17 sp. z o.o. and PGE Inwest 18 sp. z o.o. The share capital amounts to PLN 10,000 for each company. The companies were registered in the National Court Register: PGE Inwest 17 sp. z o.o. on October 20, 2016 and PGE Inwest 18 sp. z o.o. on October 19, 2016.
- On September 19, 2016 the Extraordinary General Meeting of PGE Inwest 4 sp. z o.o. and RAMB sp. z o.o. (subsidiaries of PGE S.A.) adopted resolutions on merger of PGE Inwest 4 sp. z o.o. (the Acquiring Company) with RAMB sp. z o.o. (the Acquired Company). The merger was registered in the National Court Register on December 16, 2016. The merger had no impact on the consolidated financial statements. After the merger the company changed its name from PGE Inwest 4 sp. z o.o. to RAMB sp. z o.o.
- On December 29, 2016 PGE Polska Grupa Energetyczna S.A. established PGE Towarzystwo Funduszy Inwestycyjnych S.A. The entity was registered in the National Court Register on January 27, 2017.

In addition, on May 31, 2016 PGE S.A. and Polska Grupa Zbrojeniowa S.A. ("PGZ") signed a letter of intent in which they express their willingness to cooperate in order to conclude a sale of shares of Exatel S.A. by PGE to PGZ. Since the conditions resulting from IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* were not met, the shares of Exatel S.A. are recognized and consolidated based on previously existing principles.

After the reporting date the following events took place:

- On Febraury 1, 2017 PGE Polska Grupa Energetyczna S.A. established PGE Invest 19 sp. z o.o. The entity was registered in the National Court Register on February 24, 2017.

1.4 Acquisition of a jointly controlled entity

As described in note 33.2, in the current period the Company acquired shares in Polska Grupa Górnicza sp. z o.o. ("PGG"). Details of the settlement of the aforesaid acquisition is presented in the table below:

	Acquisition price	Share in fair value of net assets	Goodwill
Stage 1 (15.66%)	361	361	-
Stage 2 (0.97%)	83	79	4
Total Stage 1 + Stage 2 (16.63%)	**444**	**440**	**4**

Stage 3 took place on February 1, 2017.

2. Basis for preparation of the financial statements

2.1 Statement of compliance

These financial statements were prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union („EU"). IFRS comprise standards and interpretations approved by the International Accounting Standards Board ("IASB") and International Financial Reporting Interpretation Committee ("IFRIC").

2.2 Presentation and functional currency

The functional currency of the parent company and the presentation currency of these consolidated financial statements is Polish Zloty („PLN"). All amounts are in PLN million, unless indicated otherwise.

For the purpose of translation at the reporting date of items denominated in currency other than PLN the following exchange rates were applied:

	December 31,2016	December 31,2015
USD	4.1793	3.9011
EUR	4.4240	4.2615

for the year 2016 in accordance with IFRS EU (in PLN million)

2.3 New standards and interpretations published, not yet effective

The following standards, changes in already effective standards and interpretations are not endorsed by the European Union or are not effective as at January 1, 2016:

Standard	Description of changes	Effective date
IFRS 9 *Financial Instruments*	Changes to the classification and measurement requirements – replacement of the existing categories of financial instruments with the two following categories: measured at amortized cost and at fair value. Changes to hedge accounting.	January 1, 2018
IFRS 14 *Regulatory Deferral Accounts*	Accounting and disclosure principles for regulatory deferral accounts	Standard in the current version will not be effective in the EU
IFRS 15 *Revenue from Contracts with Customers with explenations to IFRS 15*	The standard applies to all contracts with customers, except for those within the scope of other IFRSs (e.g. lease contracts, insurance contracts and financial instruments). IFRS 15 clarifies principles of revenue recognition.	January 1, 2018
IFRS 16 Leases	The standard eliminates the classification of leases as either operating or finance lease in the lessee's accounts. All contracts which meet the criteria of lease will be recognized as finance lease.	January 1, 2019
Amendments to IAS 12	Clarification of the method of deferred tax asset settlement on unrealized losses.	January 1, 2017
Amendments to IAS 7	The initiative on changes to disclosures.	January 1, 2017
Amendments to IFRS 10 and IAS 28	Deals with the sale or contribution of assets between an investor and its joint venture or associate.	Has not been determined
Amendments to IFRS 2	Classification and measurement of share-based payment transactions	January 1, 2018
Amendments to IFRS 4	Application of IFRS9 Financial instruments jointly with IFRS 4 Insurance contracts	January 1, 2018
Annual improvements to IFRS (cycle 2014-2016)	A collection of amendments dealing with: IFRS 1 – elimination of short-term exemption for entities using IFRS for the first time; IFRS 12 – clarification of the scope of disclosure requirements; IAS 28 – valuation of entities, in which an investment has been made, at fair value through profit or loss or using an individual method.	January 1, 2018/ January 1, 2017
Amendments to IAS 40	Changes to the classification of properties: i.e. transfer from investment property to other groups of assets.	January 1, 2018
IFRIC 22 *Foreign Currency Transactions and Advance Consideration*	Guidelines specifying determination of the date of a transaction and related spot foreign exchange rate to be used in case foreign currency payments are made or received in advance.	January 1, 2018

The PGE Group intends to adopt the above mentioned new standards, amendments to standards and interpretations published by the International Accounting Standards Board but not yet effective at the reporting date, when they become effective.

The influence of new regulations on future financial statements of the PGE Group

IFRS 9 *Financial Instruments*

The standard introduces fundamental changes in respect of classification, presentation and measurement of financial instruments. As part of IFRS 9, new model for calculating impairment will be introduced that will require more timely recognition of expected credit losses and rules for hedge accounting will be updated. These changes are intended to allow the preparers of financial statements to reflect entity's actions more accurately.

Current analysis of the standard mentioned above indicates that possible changes may refer to the following areas:

- rules for calculating and recognition of impairment allowances concerning financial assets (change from incurred loss model to expected loss model),
- classification of financial assets,
- possible simplifications of hedge accounting.

Analysis of the impact of IFRS 9 has not been finished yet, nonetheless according to the PGE Group the standard should not have significant influence on the reported financial results.

IRFS 15 *Revenue from Contracts with Customers*

IFRS 15 is intended to unify and simplify principles of revenue recognition by introducing one model for revenue recognition. In particular, the standard will impact revenue recognition resulting from agreements or package agreements based on which clients are provided with separate services and/or goods.

Analysis of the impact of the standard indicates that changes may concern mainly the following areas:

- revenues from connection to the distribution network. Currently, revenues from connection fees are recognized at one time when they become due i.e. at the moment of connection. The new standard may change principles of revenue recognition from connection to the distribution network and related expenses depending on the final output of dependency analysis between connection agreement and distribution agreement concluded with the same client;
- acting as an intermediary in respect of selected, separate services and goods offered to clients on the basis of electricity or gas sale agreement, or distribution agreement. The change may result in a decrease of sales revenues and related expenses, but it will not affect the reported profit or loss;
- extending the scope of disclosures related to sales reveues.

Apart from the possible impact of changes in recognition of revenues and expenses resulting from connection to distribution network, the implementation of the standard should not significantly influence the Group's financial statements. Analysis of the impact of the standard has not been finished yet.

IFRS 16 Lease

The new standard changes principles for the recognition of contracts which meet the criteria of a lease. The main change is to eliminate the classification of leases as either operating leases or finance leases in the lessee's accounts. All contracts which meet the criteria of a lease will be recognized as a finance lease. Adoption of the standard will have the following effect:

- in the statement of financial position: increase of non-financial non-curent assets and financial liabilities;
- in the statement of comprehensive income: decrease of operating expenses (other than depreciation/amortization), increase of depreciation/amortization and financial expenses.

The PGE Group is in the process of analysis of IFRS 16's impact on the future financial statements.

Other standards and their changes should have no significant impact on future financial statements of the PGE Group.

Amendments to standards and interpretations that entered into force in the period from January 1, 2016 to the date of publication of these consolidated financial statements did not have significant influence on these financial statements.

2.4 Professional judgment of management and estimates

In the process of applying accounting rules with regards to the below issues, management has made judgments and estimates that affect the amounts presented in the consolidated financial statements, including in other explanatory information. The estimates were based on the best knowledge of the Management Board relating to current and future operations and events in particular areas. Detailed information on the assumptions made was presented below or in respective explanatory notes to the consolidated financial statements.

Recoverable amount of property, plant and equipment and goodwill

Changes in the electricity market may have a significant influence on the recoverable amount of power generating property, plant and equipment of particular PGE Group entities. If impairment indicators are identified, the Group estimates the recoverable amount of the respective property, plant and equipment owned. Estimate of recoverable amount of goodwill is performed once a year.

Impairment analysis of property, plant and equipment and goodwill is performed by estimating the recoverable amount of cash generating units. The analysis is based on a number of significant assumptions concerning factors, some of which are outside the control of the Group. Any significant change in these assumptions will impact the result of future impairment tests and as a consequence may lead to significant changes to the financial position and results of the Group.

Performed impairment test is described in note 3 of these financial statements.

Depreciation period of property, plant and equipment and intangible assets

Depreciation rates are calculated on the basis of the estimated economic useful life of an item of property, plant and equipment or intangible assets as well as estimates of its residual value. Capitalized costs of major inspections and overhauls are depreciated throughout the period until the beginning of the next major inspection or overhaul.

Estimated economic useful lives of assets are subject to verification at least once a year. Depreciation periods applied are presented in notes 4.8 and 4.9 of these financial statements.

The verification of the economic useful lives of property, plant and equipment and intangible assets conducted in 2016 resulted in a decrease in the depreciation and amortization costs for 2016 by approx. PLN 15 million in total, which had the following effects on the costs of particular segments:

- a decrease in the depreciation and amortization costs in the Conventional Generation segment by approx. PLN 14 million,
- a decrease in the depreciation and amortization costs in the Distribution segment by approx. PLN 1 million.

The verification of economic useful lives of assets in other segments did not have significant impact on the depreciation and amortization costs recognized in 2016.

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

Valuation of assets arising from capitalization of stripping costs in the production phase of a surface mine

Capitalization of stripping costs in the production phase is determined based on the excess of annual N:W ratio (ratio of the volume of overburden removed to the volume of coal extracted within a given year) over general N:W calculated for a particular deposit. The general N:W ratio is calculated by comparing the total volume of overburden still to be removed to the total volume of coal still to be extracted from the date of application of IFRIC 20 to the end of the exploitation of lignite from a particular deposit. This ratio is calculated at the end of each year based on the best knowledge of the technical experts employed in the mine and may be subject to change in case of acquisition of new information on the size of the deposit and the way it is located underground. Update of N:W ratio during 2016 caused an increase in costs of PLN 13 million.

Impact of assets arising from capitalization of the stripping costs in the production phase of a surface mine on property, plant and equipment and its depreciation is described in note 9 of these financial statements.

Rehabilitation provision

Rehabilitation provision is calculated using estimates of future costs of rehabilitation together with all information available as at the reporting date. Provision is updated in case of change of estimated time or amounts of expenses necessary to conduct rehabilitation process, or in case of change of discount rate. Estimation of rehabilitation provision requires making technical, geological, environmental, legal and tax assumptions, as well as schedule, scope and the level of rehabilitation costs. Changes in assumptions mentioned above impact the value of rehabilitation provision and capitalized rehabilitation costs recognized in property, plant and equipment, as well as statement of comprehensive income.

Valuation of provisions for employee benefits

Provisions for employee benefits were estimated using actuarial methods.

Key actuarial assumptions related to the calculation of provisions as at the reporting date are as follows:

	As at December 31, 2016	As at December 31, 2015
Expected inflation rate (%)	1.3 - 1.8%	1.59-2.47%
Discount rate (%)	3.5%	3.0%
Expected salary growth rate (%)	0.00 - 3.57 %	0-5.43 %
Employee turnover (%)	0.24 - 9.41%	0.24-12.83 %
Expected medical care costs growth rate (%)	1.3 - 1.8%	1.59 - 2.5%
Expected Social Fund (ZFŚS) allowance rate (%)	3.50 - 8.4%	3.50-5.00%

- The probability of employee attrition has been predicted on the basis of historical data related to the Group's employee turnover ratio and statistical data on employee attrition in the industry.
- Mortality and survival probability have been adopted from the Life Expectancy Tables published by Central Statistical Office of Poland, assuming that the population of Company's employees corresponds, in respect of mortality, to the average in Poland.
- Normal procedure of employees' retirement was assumed, in accordance with detailed rules included in the Law on State Social Insurance Pensions, with the exception of employees who meet the conditions required to early retirement.
- For discounting future benefit payments a discount rate of 3.5% was adopted (December 31, 2015: 3.0%), which corresponds to the profitability of long-term Treasury bonds listed on the Polish capital market.

Other provisions

As described in note 4.21 of these financial statements recognition of provisions requires estimates of the probable outflow of economic benefits and determination of the amount that shall be the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The most important provisions are:

- provision for CO_2 emission rights;
- provision for energy origin units held for redemption.

Sensitivity analysis for changes in assumptions used for calculation of carrying value of provisions, in particular a change in a discount rate, is presented in notes 21 and 22 of these financial statements.

Contingent liabilities

In accordance with IAS 37 with respect to recognition and measurement of provisions and contingent liabilities, the PGE Group estimates the probability of occurrence of potential liabilities. If the occurrence of unfavorable future event is probable, the PGE Group recognizes a provision in the appropriate amount. If the occurrence of unfavorable future event is estimated by the PGE Group as not probable but possible, a contingent liability is recognized. Detailed information on contingent liabilities and legal claims and disputes is presented in note 28 of these financial statements.

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

Compensations resulting from termination of long-term agreements ("LTC")

The Group's estimates of compensation related to early termination of long-term contracts for sale of capacity and electricity resulting in recognition of related revenues and receivables are based on appropriate, in the Group's opinion, interpretation of the Act dated June 29, 2007 on the principles for coverage of costs incurred due to early termination of long-term contracts for sales of capacity and electricity (Official Journal from 2007, No. 130, item 905) ("the LTC Act"), the anticipated outcome of disputes with the President of the Energy Regulatory Office and on a number of significant assumptions to the factors, some of which are outside the control of the Group.

An unfavorable outcome of the dispute with the President of the Energy Regulation Office, described in note 33.1 of these financial statements, with respect to the interpretation of the LTC Act, and changes in assumptions used, including those resulting from mergers within the PGE Group, may significantly impact the estimates and as a consequence may lead to significant changes in the financial position and results of the PGE Group. It is not possible to predict the final outcome of the dispute with the President of the Energy Regulation Office as at the date of preparation of these consolidated financial statements.

During the reporting period the Group revised the estimates of LTC compensations. Detailed information is presented in note 33.1 of these financial statements.

Impairment allowances on receivables

As at the reporting date the Group entities assess whether there is an objective evidence for impairment of a receivable or a group of receivables. If the recoverable amount of an asset is lower than its carrying amount, the PGE Group recognizes an impairment allowance to the amount of the present value of expected cash flows.

Description of changes in impairment allowance on trade and other receivables is presented in note 26.5.1 of these financial statements.

Electricity sales accrual

Reading numbers from meters regarding the volume of electricity provided in retail sales including distribution services and its invoicing is performed mainly in periods different from the reporting periods. Taking into account the above, a retail sale company (PGE Obrót S.A.) and a distribution company (PGE Dystrybucja S.A.) that are part of the PGE Group perform certain revenues estimates at each reporting date that cover the period not covered by the meters reading. The estimates include also a change in the cost of purchase of electricity during the period of the estimates and reconciliation of the energy balance.

The carrying amount of the electricity sales accrual as at December 31, 2016 is described in note 25.1.1 of these financial statements.

Measurement of fair values of acquired assets and liabilities, goodwill calculation

The PGE Group identifies acquired assets and liabilities, measures their fair value and recognizes goodwill or gain on bargain purchase in accordance with IFRS 3 *Business combinations*. Measurement is based on a number of assumptions, which include inter alia: application of appropriate valuation method, management's plans relating to the use of acquired assets, financial projections (including price forecasts influencing main positions of revenues and expenses), changes in laws and regulations and other. On the other hand, the settlement of the tranbbsaction is also influenced by the appropriate determination of the consideration transferred (including contingent part). Assumptions applied may significantly impact fair values of acquired assets and liabilities, and calculation of goodwill or gain on bargain purchase. Goodwill is tested for impairment together with the respective cash generating units.

During the year ended December 31, 2016 the PGE Group acquired shares in a jointly controlled entity: Polska Grupa Górnicza sp. z o.o. This resulted in recognition of goodwill of PLN 4 million. The settlement of the acquisition of shares was described in note 1.4 of these financial statements.

Influence of changes in selected estimates on the statement of comprehensive income for the year 2016

	Impairment of property plant and equipment and intangible assets	Change in actuarial provisions	Change in rehabilitation provision	Change in N:W ratio	Verification of economic useful lives
SALES REVENUES	-	-	-	-	-
Costs of goods sold	**(773)**	**39**	-	**(13)**	**15**
GROSS PROFIT/(LOSS) ON SALES	**(773)**	**39**	-	**(13)**	**15**
Distribution and selling expenses	-	3	-	-	-
General and administrative expenses	(229)	6	-	-	-
Other operating income	-	-	643	-	-
OPERATING PROFIT/(LOSS	**(1,002)**	**48**	**643**	**(13)**	**15**
PROFIT/(LOSS) BEFORE TAX	**(1,002)**	**48**	**643**	**(13)**	**15**
Other comprehensive income	-	**249**	-	-	-

3. The analysis of impairment of property, plant and equipment, intangible assets and goodwill

Property, plant and equipment is the most significant group of assets of the PGE Group. Due to changeable macroeconomic conditions the PGE Group regularly verifies the impairment indicators of its assets. When assessing the market situation the PGE Group uses both its own analytical tools and independent think tanks' support.

3.1 The analysis of impairment of power generating assets of Conventional Generation segment

In the previous reporting periods, the PGE Group recognized substantial impairment allowances of property, plant and equipment of Conventional Generation segment. In the current reporting period, the Group analysed impairment indications in order to verify whether there is a need to recognize further impairment of these assets or to reverse previously recognized impairment allowances.

The most important factors analysed, included:

- analysis of the execution of the financial plan in 2016,
- confirmation of validity of the investment plan,
- analysis of electricity prices included in the contracts concluded for the following years,
- analysis of accuracy of assumptions about the so-called capacity market, cogeneration support after 2018 and allocation of free of charge CO_2 emission rights,
- review of estimated margins on production and sale of electricity in the future periods, in the light of the most recent forecasts of electricity, coal and CO_2 emission rights prices.

The analysis shows that conventional power generating units execute the financial plan as intended. New forecasts of electricity, coal and CO_2 emissions rights prices that are available to the PGE Group do not cause a significant change in the forecasted margins. At the same time, according to the PGE Group the assumptions about the capacity market, cogeneration support and the volume of free of charge CO_2 emissions rights that were adopted in 2015 are also valid on December 31, 2016. In case of heat and power plant Szczecin, the Group is of the opinion that Enea's termination of the contract for the supply of energy origin rights to this entity, as described in note 28.4, is ineffective and therefore the Group will assert in court to resume the contract or to obtain compensation. As a consequence, according to the PGE Group there are no indicators for further impairment of property, plant and equipment of Conventional Generation segment nor for reversal of previously recognized impairment allowances as at the reporting date.

Some of the significant regulatory assumptions adopted in the analysis mentioned above are beyond the control of the PGE Group and their realization in the future is uncertain. This concerns in particular issues related to the final shape of the Polish power market and its notification by the European Commission, cogeneration support after 2018 and allocation of free of charge CO_2 emission rights after 2020. In these areas, the PGE Group relies on its current assumptions as to further changes in regulations which are subject to risk. The change of these regulations in the future, in relation to the current expectations, may affect the valuation of the recoverable amount of power generating assets of Conventional Generation segment.

3.2 The analysis of impairment of the power generating assets of Renewables segment

In the first half of 2016 the PGE Group identified impairment indications that could significantly influence the value of the power generating assets and goodwill of Renewables segment.

In the fourth quarter of 2016, the Group verified the indications once again and found it essential to revise impairment allowances in the area of wind energy.

In the PGE Group's opinion the most important factors influencing the recoverable amount of assets are:

Changes in the market environment

The delayed entry into force of the new support system for the production of electricity from renewable energy sources causes that new units are involved in the current system of support. Although, since the beginning of 2016, the support for large hydropower and biomass co-firing with coal technologies was limited, the delayed entry into force of the provisions of section 4 of the Act on Renewable Energy Sources dated February 20, 2015 contributed to even higher increase of a large surplus of green certificates. Additionally, expected changes of the support system contributed to the intensification of construction works, the consequence of which was a large number of wind power plants that were put into use in 2015 and in 2016. As a result, there have been further declines of prices of energy origin rights and worsening future forecasts.

Changes in the legal environment

On May 20, 2016 act on investments in wind farms was passed. Among other things, it amends the definition of construction in the construction law. Changed definition of construction causes that the tax base of real estate tax will be expanded to wind farms.

Consequently, the PGE Group forecasts a decrease in future cash flows and recognizes the risk of impairment of power generating assets of Renewables segment in the area of wind farms.

The impairment tests of cash-generating units ("CGU") were carried out as at June 30,2016 and then as at December 31, 2016 in order to determine their recoverable amount. The recoverable amount was determined based on estimated value in use of the tested assets calculated using the discounted cash flow method on the basis of financial projections for assumed economic useful life of the particular CGU. According to the PGE Group, adoption of the financial projections longer than five years is reasonable due to the fact that property, plant and equipment used by the Group have significantly longer economic useful lives and due to the significant and long-term impact of projected changes in the regulatory environment.

The impairment allowances of projects concerning wind farms were significantly influenced by the following:

- the Act of May 20, 2016 on investments in wind farms defined the conditions of construction and localization of wind farms located near existing and planned residential buildings. The provisions of the Act concern installations on land exceeding the power of kW 40. The most important changes which were introduced under the power of the Act include:
  - minimum distance between the wind power plant and residential building or mixed-function building is equal to or greater than ten times the heights of the power plant, measured from the ground level to the highest element of the building, including technical elements, escpecially a rotor with blades;
  - permission to build a wind power plant issued before the Act becomes effective remain valid if the occupancy permit is issued within three years from the date of effectiveness of the Act.
- a draft of the Government Order of November, 2016 concerning the maximum quantity and value of electricity obtained from the renewable energy sources that can be sold through auction in 2017. According to the Act of February 20, 2015 on renewable energy sources, the Council of Ministers determines the amount of energy which can be bought through auction in the following year. The decrease in total value of investment projects results from their oversupply in contrast to little demand for renewable energy resulting from the draft of the Government Order.

Due to the minor probability of realization of the projects, the PGE Group decided to raise impairment allowance covering all investment projects related to wind farms located on land, except for Karnice II Project. The amount of the impairment allowance was determined in the same way as for available-for-sale assets, i.e. through comparison of the carrying value to the fair value less costs of disposal.

The assumptions:

The key assumptions influencing the recoverable amount of the CGUs tested were as follows:

- recognition as a single CGU of:
  - pumped-storage power plants
  - other hydropower plants
  - particular wind farms
- the production of electricity and energy origin rights based on historical data and expert estimates made for investment needs and taking into consideration the availability of particular units,
- forecasts of electricity prices for the years 2017-2038 assuming an increasing trend of wholesale market price by 2031 and decrease in prices in the following years (in fixed prices),
- price forecast for renewable energy origin rights assuming first growth and then, since 2019, decrease of prices (with an exception that for the production covered by binding contracts prices resulting from these contracts were assumed),
- increase of property tax,
- maintenance of production capacities at the current level, as a result of replacement investments,
- adoption of weighted average cost of capital after tax (WACC) at the level of 7.56%.

Forecasted electricity and energy origin rights prices are derived from the study prepared by an independent expert. The forecast of energy prices defined as the most likely was considered, with an exception that for the part covered by binding contracts, prices resulting from these contracts during their validity were assumed.

Impairment of the power generating assets of Renewables energy segment

The tests conducted indicate impairment of some of the wind farms, majority of investment projects and goodwill allocated to this CGU.

As at December 31,2016	Assets value before impairment	Impairment loss	Value after impairment
Power generating assets of Renewables segment			
Pumped-storage power plants	808	-	808
Other hydropower plants	322	-	322
Wind farms	2,567	(369)	2,198
Wind investment projects	224	(218)	6
Marine investment projects	61	-	61
Goodwill	285	(277)	8
TOTAL	**4,267**	**(864)**	**3,403**
Unallocated assets and non-core	82	(1)	81
Property, plant and equipment and intangible assets under construction (excluding wind projects)	19	-	19
TOTAL:	**4,368**	**(865)**	**3,503**

Sensitivity analysis

The results of the sensitivity analysis show that changes in estimates regarding weighted average cost of capital as well as sales prices of electricity and energy origin rights have the most significant impact on the recoverable amount of the measured assets. The table below presents the estimated impact of changes in key assumptions on changes in impairment loss of Renewables segment's assets as at December 31, 2016 (data in PLN million).

Parameter	Change	Impact on impairment loss	
		Increase in impairment loss	Decrease in impairment loss
Change in electricity prices throughout the forecast period	+1%	-	16.6
	- 1%	16.6	-
Change in WACC	+ 0.5 p.p.	61.6	-
	- 0.5 p.p.	-	52.2
Change in energy origin rights prices throughout the forecast period	+ 1%	-	8.8
	- 1%	8.8	-

3.3 Property, plant and equipment in Distribution segment

As at the reporting date the carrying amount of property, plant and equipment related to the distribution activity amounted to more than PLN 16 billion and represented approx. 31% of the total consolidated assets. Their recoverable amount depends mainly on tariffs granted by President of the Energy Regulatory Office. Regulated revenue (tariff) which is determined annually provides covering justified costs: operating costs, depreciation and amortisation, taxes, purchase of energy to cover balancing difference and transferred costs. It provides also a return on equity involved in the distribution activity at a justified level. Return on equity and depreciation charges are dependent on the so called Regulatory Value of Assets.

As at the date of preparation of these consolidated financial statements, the PGE Group has not identified the indications for impairment of property, plant and equipment allocated to Distribution segment.

4. Significant accounting principles applied

The financial statements have been prepared under the historical cost convention, which was modified in relation to:

- Property, plant and equipment and intangible assets – property, plant and equipment and intangible assets that were owned by the Group at the date of transition to IFRS were measured at deemed costs as at that date. In addition, for certain property, plant and equipment and intangible assets impairment loss has been recognized.
- Financial instruments – selected categories of financial instruments are measured and presented in the statement of financial position at fair value. Details on the valuation of individual categories of financial instruments are presented in the description of the accounting principles applied.
- Impaired assets – presented in historical cost adjusted by impairment losses.
- Inventories – CO_2 emission rights acquired in order to realize profits from fluctuations in market prices, are measured at fair value less costs of disposal.

4.1 Consolidation principles

These consolidated financial statements of the PGE Group have been prepared on the basis of the financial statements of the parent company, financial statements of its subsidiaries, associates and joint ventures. The financial statements of consolidated entities are prepared for the same reporting period, based on unified accounting principles.

All balances, income and expenses arising between the Group entities and unrealized gains from intra-group transactions, were fully eliminated.

Subsidiaries are consolidated from the date of taking control over them by the Group, till the date of cessation of control. Control by a parent company occurs when this company owns, directly or indirectly through its subsidiaries, more than half of votes in the entity unless it is possible to prove that such ownership does not constitute control. Exercising control occurs when the company, due to its involvement in another entity holds the rights to variable financial results and has the power to influence the amount of financial results by controlling the entity. Exercising control may also occur when the parent company does not own half of votes in a subsidiary.

Accounting for the formation of the PGE Group in the consolidated financial statements

The issues related to the mergers and acquisitions of business units are generally regulated by International Financial Reporting Standard 3 Business Combinations. However, the scope of this standard does not include transactions among business entities under common control. Same as the companies of the PGE Group of that time, the business entities contributed to the Company in May 2007 were controlled by the State Treasury. Thus, in the Company's opinion, the contribution of the companies described above meets the definition of transaction under common control, and thus is excluded from the scope of IFRS 3.

The aforementioned mergers of the entities under common control were accounted for by the pooling of interests method and thus the consolidated financial statements reflect the fact of the common control continuity and does not present the changes in the net asset value to fair value (or recognition of new assets), or valuation of the goodwill.

Further mergers and acquisitions within the PGE Group were recognized as transactions concluded between jointly controlled entities, therefore should be accounted within the equity of the PGE Group, not affecting the goodwill.

The purchase of companies from third parties is accounted using the acquisition method.

Joint ventures and joint operations

In relation to participation in a joint venture (a joint arrangement giving the right to the net assets of the arrangement) a joint venture accounts for its interest i a joint venture under the equity method.

Joint control is the contractually agreed sharing of control in the framework of the contractual arrangement, wich exists only when decisions about relevant activities require the unanimous consent of the parties who share control.

Investments in associates

The associates are entities over which the parent company directly, or through the subsidiary, has significant influence and that are neither controlled nor jointly controlled. Investments in associates are recognized in the statement of financial position at cost increased or decreased to recognize the investor's share in the investee's net assets after the date of acquisition less impairment losses if applicable.

Investments in associates are recognized using the equity method.

4.2 Methods applied to convert positions denominated in foreign currencies

Transactions denominated in foreign currencies are translated into PLN at the rate on the transaction date. As at the reporting date:

- monetary items are translated at the closing NBP rate;
- non-monetary items are valued at historical cost in foreign currency at an exchange rate on the day of the transaction;
- non-monetary items measured at fair value in foreign currency are translated at an exchange rate on the day of fair value measurement.

Foreign exchange differences resulting from transalation are recognized in profit or loss or, in cases specified in the accounting policies applied, recorded in the cost of assets.

Foreign exchange differences resulting from translation of non-monetary items, such as equity instruments measured at fair value through profit or loss, are recognized as a change in fair value. Foreign exchange differences resulting from translation of non-monetary items, such as equity instruments classified as financial assets available for sale, are recognized in other comprehensive income. Foreign exchange differences resulting from translation of assets and liabilities of foreign entities with functional currency other than functional currency of the parent company are recognized in separate position of the equity.

4.3 Operating segments

An operating segments is a component of the Group:

- that engages in business activities from which it may earn revenues and incur expenses,
- whose operating results are regularly reviewed by the entity's chief operating decision maker in the Group to make decisions about resources to be allocated to the segment and assess its performance,
- for which discrete financial information is available.

Due to the types of production processes as well as the current system of regulation within the PGE Group, the following segments are distinguished:

- Conventional Generation,
- Renewables,
- Supply,
- Distribution,
- Other operations that include the activities of the subsidiaries other than listed above, but not material enough to create separate segments.

Segment revenues are the revenues, including both sales to external customers and intersegment transfers within the Group that are presented in profit or loss of the Group and can be directly attributed to the segment together with a relevant portion of revenue that can be allocated on a reasonable basis to the segment. Segment expenses include cost of sales to external customers and the cost of intersegment transfers within the Group, which results from operating activities of the segment and can be directly attributed to the segment together with a relevant portion of entity's expenses that can be allocated on a reasonable basis to the segment. Segment result is a difference between revenues and expenses of the segment.

Segment assets are those operating assets that are used by that segment in its operating activity and that can be directly attributed to the segment or can be allocated on a reasonable basis to the segment. Segment liabilities are those operating liabilities that result from operating activities of the segment and can be directly attributed to the segment or can be allocated on a reasonable basis to the segment. Segment assets and liabilities do not include settlements connected with income tax.

4.4 Revenues

Revenues are measured at the fair value of the consideration received or due. The revenue is recognized after deducting value added tax (VAT), excise tax and other sales-based taxes as well as discounts. When recognizing the revenues, the criteria specified below are also taken into account.

Revenues from sale of goods and merchandise

Revenues from the sale of goods and merchandise are recognized when related risks and rewards have been transferred and when the amount of revenue can be reliably measured and costs incurred can be reliably estimated. In particular, revenues from the sale of electricity are recognized at the time of delivery.

Revenues from sale of goods and merchandise primarily include:

- amounts receivable from: wholesales and retail sales of electricity, sales of heat energy, gas, lignite, certificates of energy origin from renewable energy sources, certificates of production of energy in high efficiency cogeneration plants, greenhouse gas emission rights, distribution and transmission services and other services relevant to core business,
- amounts receivable from sales of materials and merchandise not mentioned above.

Revenues from sale of services

Revenues from services rendered are recognized when the service is performed. When the outcome of a transaction involving the rendering of long-term services can be estimated reliably, revenue associated with the transaction is recognized by reference to the stage of completion of the transaction at the reporting date less revenue recognized in the previous reporting periods.

When the outcome of the transaction involving the rendering of services cannot be estimated reliably, the Group recognizes revenue only to the extent of the expenses recognized that are recoverable.

Connection fees

PGE Dystrybucja S.A. generates revenues from connecting clients to the network, so-called connection fees. According to the interpretation IFRIC 18 *Transfers of Assets from Customers*, starting from July 1, 2009 these revenues are recognized at once when the service is performed. Fees received until July 1, 2009 are recognized as deferred income and settled through the period of 25 years.

Revenues from LTC compensations

Producers of electric energy, who joined the program of early termination of long-term contracts for sale of capacity and electricity, are entitled to receive compensations to cover stranded costs. The compensations are paid in the form of annual advances as four quarterly instalments which are adjusted on yearly basis. At the end of the adjustment period, the final amount of stranded costs will be determined. Due to the above, the producers of electricity of the PGE Group estimate and recognize the revenue from LTC compensations in the amount in which it will be finally approved for the given period, i.e. after annual and final adjustments expected as at the date of the preparation of the consolidated financial statements. Allocation of the final adjustment to the respective reporting period is based on estimated schedule of sales of electricity and system services in the adjustment period, including the final adjustment.

Revenues adjustments in respect of LTC compensations arising from court decisions are presented in other operating activities.

4.5 Cost of goods sold

Cost of goods sold includes:

- production costs incurred in the reporting period adjusted for related changes in inventories (finished goods, semi-finished products and production in progress) and costs related to production of goods for the Group's own use,
- value of electricity, certificates of origin for energy and gas sold, and goods and materials at purchase prices.

Costs that can be directly attributable to revenues recognized by the Company are recognized in profit or loss for the reporting period in which the revenues were recognized.

Costs that can only be indirectly attributed to revenues or other economic benefits recognized by entities, are recognized in the profit or loss in the reporting periods, to which they relate in accordance with accrual basis of accounting, taking into account the principles of measurement of property, plant and equipment and inventories.

4.6 Taxes

Corporate income tax recognized in profit or loss comprises current income tax and deferred income tax, that are actual fiscal charges for the reporting period calculated by the Group entities in accordance with regulations of the Corporate Income Tax Act and the change in deferred tax assets and deferred tax liabilities other than the ones charged or credited directly to equity.

Deferred tax asset or deferred tax liability are calculated on the basis of temporary differences between the carrying amount of a given asset or liability and its tax base and tax loss that is recoverable in the future.

A deferred tax liability is recognized for all taxable temporary differences.

A deferred tax asset is recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible emporary difference can be utilized.

The carrying amount of a deferred tax asset and deferred tax liability is reviewed at each reporting date. The deferred tax asset and deferred tax liabilities are classified as long-term. The Group offsets deferred tax asset and liabilities, at the level of each company of the Group.

The Group reduces the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable profit will be available to allow deferred tax asset to be utilized partially or entirely.

4.7 Earnings per share

Earnings per share for each period is calculated by dividing profit or loss attributable to equity holders of the parent company by the weighted average number of shares outstanding during the reporting period.

An entity calculates diluted earnings per share by dividing profit or loss attributable to ordinary equity holders (after deduction of interest on redeemable convertible preference shares) by the weighted average number of shares outstanding during the period (adjusted by the number of dilutive options or dilutive redeemable convertible preference shares).

4.8 Property, plant and equipment

Property, plant and equipment are assets:

- held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and
- expected to be used for more than one year.

After initial recognition, as an asset, an item of property, plant and equipment is measured at carrying amount, i.e. initial value (or deemed cost for items of property, plant and equipment used before the transition to IFRS) less any accumulated depreciation and any impairment losses. Initial value comprises purchase price including all costs directly attributable to the purchase and bringing the asset into use. The cost comprises estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having it used for purposes other than to produce inventories. As at the date of acquiring or manufacturing of an item of property, plant and equipment, the Group identifies and distinguishes all components being a part of a respective asset that are significant as compared to the acquisition price, cost of manufacture or deemed cost, and depreciates them separately.

The depreciable amount is the cost of an asset less its residual value. Depreciation commences when the asset is available for use. Depreciation is based on a depreciation plan reflecting the future useful life of the asset. The depreciation method used reflects the pattern in which the asset’s future economic benefits are expected to be consumed by the entity. Major inspection and overhauls recognized as a component of property, plant and equipment are depreciated starting from the next month after finishing the inspection/overhaul until the beginning of the next major inspection/overhaul.

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

The following useful lives are adopted for property, plant and equipment:

Group	Average remaining depreciation period in years	The most often applied total amortization period in years
Buildings and structures	16	20 – 60
Machinery and equipment	14	4 – 40
Vehicles	6	4 – 14
Other	3	3 – 10

Depreciation methods, depreciation rates and residual values of property, plant and equipment are verified at least each financial year. Changes identified during verification are accounted for as a change in an accounting estimate and possible adjustments to depreciation amounts are recognized in the year in which the verification took place and in the following periods.

If there is an impairment loss on property, plant and equipment to be recognized the PGE Group applies principles described in note 4.11.

Investments relating to fixed assets under construction or assembly are recognized at cost of acquisition or cost of manufacturing less impairment losses. Property, plant and equipment under construction is not depreciated until the construction is completed and the items are available for use.

Stripping costs

Surface mines from the Group recognize stripping costs incurred during the construction and start of the mine as assets and present them as property, plant and equipment.From the beginning of lignite exploitation those capitalized cost are systematically depreciated using the natural method of depreciation based on the amount of the lignite extracted.

If the conditions of the IFRIC 20 interpretation are met, mines also recognize as a property, plant and equipment so-called deferred stripping cost, i.e. stripping costs incurred during the production phase. The value of the assets arising due to stripping costs in the production phase is determined based on the model that takes into account, inter alia, the estimated value of the overall N-W ratio (the proportion of overburden to lignite) and annual real rate of N-W. An asset arising due to stripping costs is systematically depreciated using the natural method of depreciation based on the amount of lignite extracted from the given deposit.

Costs of rehabilitation of post-exploitation surface mining properties

Surface mines operating in the Group capitalize in the value of the corresponding component of fixed assets estimated costs of rehabilitation of post-exploitation mining properties in the proportion of the volume of the excavation resulting from stripping of overburden at the reporting date to the planned volume of excavation resulting from stripping of overburden at the end of exploitation period.

Capitalized costs of rehabilitation are systematically depreciated using the natural method of depreciation based on the amount of lignite extracted from a particular field.

4.9 Intangible assets

An intangible asset is an identifiable non-monetary asset without physical substance, such as:

- economic rights acquired by the Group entities and recognized in non-current assets, with an economic useful life exceeding one year intended to be used by the Group,
- development costs,
- goodwill excluding internally generated goodwill,
- acquired right of perpetual usufruct of land,
- easements acquired and set free.

The right of perpetual usufruct of land obtained free of charge by an administrative decision is not recognized in the statement of financial position.

As at the date of initial recognition, an intangible asset is measured at acquisition cost or production cost with respect to development costs. After initial recognition, an intangible asset shall be carried at its cost less any accumulated amortization and any accumulated impairment losses. The cost of an internally generated intangible asset, except for development costs, are not capitalized and are recorded in profit or loss for the period when the related cost was incurred.

The Group assesses whether the useful life of intangible assets is definite or indefinite. If the useful life is definite, the Group estimates the length of useful period, the volume of production or other measures as the basis to define the useful life. An intangible asset is regarded as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the Group.

The amortizable amount of an intangible asset with a definite useful life shall be allocated on a systematic basis over its useful life. Amortization starts when the asset is available for use.

Intangible assets with a definite useful life are amortized over their useful life and analyzed for potential impairment, if there are indications of impairment. Amortization periods and amortization methods of intangible assets with a definite useful life are verified at least each financial year. Changes in the expected useful lives and in the expected pattern of consumption of the future economic benefits embodied in the asset are treated as change of estimate.

Intangible assets with an indefinite useful life and those not being used are subject to impairment testing each year. The following useful lives are adopted for intangible assets:

Group	Average remaining amortization period in years	The most often applied total amortization period in years
Acquired patents and licenses	3	3 – 8
Costs of finished developed works	2	3 – 15
Other	16	3 – 25

An intangible asset arising from development phase of a project shall be recognized if, and only if, the Group can demonstrate all of the following:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale,
- its intention to complete the intangible asset and use or sell it,
- its ability to use or sell the intangible asset,
- how the intangible asset will generate probable future economic benefits,
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset,
- its ability to reliably measure the expenditure attributable to the intangible asset during its development.

4.10 Borrowing costs

Borrowing costs are interest and other costs that the Group incurs in connection with the borrowing of funds. Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognized as an expense. Exchange differences arising from foreign currency borrowings the Group capitalizes to the extent that they are regarded as an adjustment to interest costs.

4.11 Impairment of non-financial assets

The Group assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, or if there is a need to perform an annual impairment testing, the Group estimates the recoverable amount of the asset or cash-generating unit.

Recoverable amount is defined as the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use. Recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. If the carrying amount is higher than the recoverable amount, an impairment loss is recorded. When estimating the value in use of an asset, future cash flows are discounted to the present value using a discount rate before tax, which represents current market estimate of time value of money and risk relevant to an asset. Impairment losses applicable to assets used in continuing operations are recognized in costs relating to the function of impaired assets.

4.12 Financial assets

Financial assets are classified in the following categories:

- Held-to-maturity investments (HTM),
- Financial assets at fair value through profit or loss (FVP),
- Loans and receivables,
- Available-for-sale financial assets (AFS).

Financial assets at fair value through profit or loss

A financial asset at fair value through profit or loss is a financial asset that meets either of the following conditions:

- It is classified as held-for-sale. A financial asset is classified as held-for-sale if it is:
  - acquired or incurred principally for the purpose of selling in the near term,
  - part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking, or
  - a derivative, except for a derivative that is a designated and effective hedging instrument.
- Upon initial recognition it is designated by the entity as at fair value through profit or loss. Any financial asset within the scope of this standard may be designated when initially recognized as a financial asset at fair value through profit or loss except for investments in equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured.

These assets are measured at fair value as at the reporting date. Gains and losses on financial assets classified as FVP are recognized in profit or loss and are not reduced by the amount of accrued interest.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are classified as current assets, if their maturity does not exceed 12 months from the reporting date. Loans and receivables with maturity exceeding 12 months are classified as non-current assets. If the time value of money is significant over the period, the assets are measured at discounted value.

Trade receivables are measured at least at each reporting date in the amount due, i.e. at the nominal value increased by applicable penalty interest, in accordance with the principle of prudence, i.e. less applicable impairment allowances. Impairment allowances on receivables are recognized as other operating expenses or financial expenses. Non-current receivables are measured at present (discounted) value.

Available-for-sale financial assets

All other financial assets (except for shares in subsidiaries) are accounted for as available-for-sale financial assets. Financial assets available for sale are recognized at fair value as at each reporting date. Fair value of an instrument which does not have a quoted market price is estimated with regards to another instrument of similar characteristics or based on future cash flows relevant to an investment asset (measurement using discounted cash flow method).

Positive and negative differences between fair value of available-for-sale financial assets (if their price is determinable on a regulated active market or if the fair value may be estimated by some other reliable method) and cost, net of deferred tax are recognized in other comprehensive income, except for:

- impairment losses,
- exchange gains and losses arising on monetary assets,
- interest recognized using the effective interest rate method.

Dividends from equity instrument in the AFS portfolio are recognized in profit or loss on the date that the entity's right to receive payment is established.

4.13 Derivatives and hedging instruments

The Group uses derivatives in order to hedge against interest rate risk and exchange rate risk. The most frequently used derivatives are forward contracts and interest rate swaps (IRS). Such derivatives are measured at fair value. Depending on whether the valuation of a derivative is positive or negative, it is recognized as a financial asset or financial liability, respectively.

The gain or loss resulting from the change in fair value of a derivative not qualifying for hedge accounting, is recognized directly in profit or loss.

The fair value of currency forward contracts is estimated with reference to current forward rates for contracts of similar maturity. Fair value of interest rate swaps is estimated with reference to the market value of similar financial instruments.

4.14 Hedge accounting

Changes in fair value of derivative financial instruments designated as cash flow hedges CCIRS (Cross Currency Interest Rate Swap) and IRS (Interest Rate Swap) are recognized in hedging reserve in the portion determined to be an effective hedge, while the ineffective portion of the hedge is recognized in the profit or loss.

The accumulated changes in fair value of hedging instrument, previously recognized in hedging reserve are transferred to profit or loss in the period or periods in which the hedged item affects profit or loss. Alternatively, if the hedge of a planned transaction results in the recognition of non-financial assets or non-financial liabilities, the Group excludes the amount from equity and includes in the initial cost or other carrying amount of a non-financial asset or liability.

4.15 Inventories

Inventories are assets held for sale in the ordinary course of business, in the process of production for such sale, or in the form of materials or supplies to be consumed in the production process or in rendering of services.

Inventories comprise:

- materials,
- finished goods,
- work in progress,
- energy origin rights – purchased rights of origin for energy produced from renewable energy sources, rights of origin for energy relating to energy generated in cogeneration and rights to energy efficiency certificates,
- merchandise (especially CO_2 emission rights purchased for resale).

Inventories are measured at the lower of cost and net realizable value.

CO_2 emission rights acquired in order to realize profits from fluctuations in market prices are measured at fair value less costs of disposal.

Cost of usage of inventories is determined as follows:

- Materials and merchandise (except for the CO_2 emission rights) – using FIFO method;
- CO_2 emission rights:
  - acquired in order to realize profits from fluctuations in market prices - using detailed identification method,
  - purchased for resale to conventional generating units in the PGE Group - according to the FIFO method.
- Energy origin rights - using detailed identification method.

As at reporting date, the cost of inventories cannot be higher than net realizable value. Impairment allowances on inventories are recognized in operating expenses. When the realizable value of a specific item of inventory is recovered fully or partially, its carrying amount is adjusted by decreasing revaluation adjustment.

4.16 CO_2 emission rights for own use

European Union Allowances (EUA) for carbon dioxide emissions intended for captive use of power generating units and CO_2 emission rights are presented in a separate line in the statement of financial position. EUA received free of charge are recognized in the statement of financial position in nominal value, which is zero. Purchased EUA are recognized at purchase price. Use of CO_2 emission rights for captive use is measured based on FIFO method.

4.17 Other assets (including prepayments)

The Group recognizes an asset as a prepayment under the following conditions:

- an expense was incurred in the past in relation to operating activity,
- it can be reliably measured,
- it refers to future reporting periods.

Prepayments are recognized at reliably measured amounts, relate to future periods and will generate future economic benefits.

Other assets include in particular state receivables, advances for deliveries and services (including advances for construction in progress) and dividends receivables.

4.18 Cash and cash equivalents

Cash comprises cash on hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

4.19 Non-current assets classified as held for sale

Non-current assets classified as held for sale are those which comply simultaneously with the following criteria:

- the appropriate level of management (General Shareholders Meeting, Supervisory Board, Management Board) is committed to a plan to sell the asset,
- the assets are available for immediate sale in their present condition,
- an active program to locate a buyer has been initiated,
- the sale transaction is highly probable and can be settled within 12 months following the decision,
- the selling price is reasonable in relation to its current fair value,
- it is unlikely that significant changes to the sales plan of these assets will be made.

Non-current assets (or disposal groups) classified as held for sale are not subject to depreciation. Non-current assets or group of assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. In the consolidated statement of financial position assets (or disposal groups) classified as held for sale are presented in separate line of current assets.

4.20 Equity

Equity is stated at nominal value, classified by nature, in accordance with legal regulations and the Company's Articles of Association.

Share capital, reserve capital and other capital reserves in the consolidated financial statements are the ones of the parent company. Hedging reserve, foreign exchange differences from translation on foreign entities and retained earnings include both the amounts deriving from the financial statements of the parent company and the relevant portion of the subsidiaries' equity, established in accordance with the consolidation principles. Declared, but not yet contributed, share capital contributions are recognized as outstanding share capital contributions as negative value.

In the consolidated statement of financial position equity is divided into:

- Equity attributable to equity holders of the parent company,
- Non-controlling interests.

4.21 Provisions

The Group recognizes provisions when there is present obligation (legal or constructive) that arises from past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

When the effect of the time value of money is significant, the amount of a provision is the present value of the expenditures expected to be required to settle the obligation. The discount rate is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The discount rate does not reflect risks for which future cash flow estimates have been adjusted.

Post-employment and jubilee awards provision

Depending on an entity, employees of the Group companies are entitled to the following post-employment benefits:

- retirement and pension benefits – paid once when the employee retires or becomes a pensioner,
- post-mortem severance,
- cash equivalent related to energy tariff for employees of power industry,
- coal allowance given in nature or paid as a cash equivalent,
- benefits from the Social Fund,
- medical benefits.

The employees of the Group are entitled to receive jubilee awards that are paid after an employee has worked for a specified period of time. The amount of awards paid depends on the period of service and the average remuneration of the employee..

The Group recognizes a provision for future obligations relevant to past service costs and jubilee awards for the purpose of assigning costs to the periods in which they are incurred. The provision raised is recognized as an operating expense in the amount corresponding with accrued future employees' benefits. The present value of these obligations is measured by an independent actuary.

Actuarial gains and losses arising from the change of actuarial assumptions (including change in discount rate) and ex post actuarial adjustments are recognized in other comprehensive income for past service costs and in operating expenses of the current period for jubilee awards.

Rehabilitation provision

The mining companies which belong to the Group raise provisions for costs of rehabilitation of post-exploitation mining properties. The value of the provision is based on the estimated cost of rehabilitation and development works related to final excavations. This cost is divided into the part attributable to stripping cost and the part attributable to mined lignite. The provision is created:

- for the part attributable to mined lignite: in the proportion of the extracted lignite as at the reporting date to the total planned volume of extraction over the period of the lignite deposit exploitation,
- for the part attributable to the stripping cost: in the proportion of the volume of the excavation resulting from stripping of overburden as at the reporting date to the planned excavation volume resulting from stripping of overburden at the end of exploitation period.

In case of rehabilitation of ash storages (production waste from electricity production) the cost of provision is recognized in operating expenses in proportion to the extent of storage filling, whereas the reversal of the discount is recognized in the financial expenses.

Provision for rehabilitation of grounds after wind farms is created when the farm is brought into use in the present value of estimated costs of dismantling and removal of remaining devices, constructions and buildings and also cost of bringing grounds to condition as close to its state prior the commissioning the farm as possible.

Estimates concerning expected costs of rehabilitation are subject to revaluation at least once in a 5-year-period. However, once a year the amount of provision is verified according to actual assumptions in terms of inflation rate, discount rate and the volume of lignite extraction or the extent of storage filling, respectively.

The increase in the provision concerning the given year is recognized in operating expenses or in the initial value of property plant and equipment, respectively. The unwinding of the discount is recognized in financial expenses. Changes in the valuation of provisions resulting from the change of assumptions (e.g. macroeconomic factors, way of conducting the rehabilitation, date, etc.), are recognized in the following way:

- for the provisions recognized as the part of the cost of property, plant and equipment: they are added to or deducted from the costs of the asset to which they relate, however the amount deducted from the cost of the asset should not exceed its carrying amount;
- as other operating expenses or other operating income - in other cases.

Provision for deficit of CO_2 emission rights

The provision for deficit of CO_2 emission rights is created by the PGE Group entities for the shortfall of CO_2 emission rights obtained free of charge. The provision is measured at the best estimate of the expenditure to be incurred to fulfil the existing obligations as at reporting date, taking into account recorded EUA obtained free of charge and EAU purchased.

Provisions are recognized in operating expenses (as costs of goods sold in cost by function and taxes and charges in cost by nature).

Provisions for energy origin rights held for redemption

The provision is created based on the requirement of the percentage share of the renewable energy and the energy generated in cogeneration units in the total sales of electricity to end users and the volume of sales to a end users. To the extent of owned energy origin rights held for redemption the provision is recognized at the value of those rights. The provision for the energy origin rights missing is measured at a reliably estimated amount of future obligation of redemption. When making the estimate, the Group takes into account substitution fees and prices. The provision is recognized in distribution and selling expenses.

4.22 Liabilities

Liabilities are the Group's present obligations, arising from past events, settlement of which will cause an outflow of resources embodying economic benefits from the Group. The Group divides liabilities into the following categories

- financial liabilities at fair value through profit or loss,
- other financial liabilities measured at subsequent reporting dates at amortized cost,
- non-financial liabilities.

When the effect of the time value of money is significant, liabilities are presented at discounted value.

4.23 The Social Fund and Other Special Funds

The Social Fund Act of March 4, 1994 states that a Social Fund is created by employers employing over 20 employees (calculated using full time equivalents). The Group creates such fund and makes periodic contributions to it. The objective of the fund is to subsidize the social activity for employees of the Group, loans granted to its employees and other social expenses. Contributions to the Social Fund are recognized as an expense in the period in which they are incurred.

The assets and liabilities of the Social Fund are netted off in the financial statements. In addition, as described in note 22, the Group creates provision for the post-employment benefits from the Social Fund.

4.24 Deferred income and government grants

Deferred income is recognized under the principle of prudence and accrual basis of accounting. Deferred income comprises:

- amounts received or due from business partners to be realized in subsequent reporting periods. Deferred income form connection fees that were received before July 1, 2009 is amortised evenly to sales revenues,
- grants obtained to finance acquisition or production of property, plant and equipment and intangible assets,
- property, plant and equipment and intangible assets acquired free of charge. Deferred income is amortized to other operating income in line with the depreciation charges on these assets.

Government grants are recognized if there is a reasonable assurance that the grant will be received and all the related conditions will be met. Government grants related to assets are amortized to other operating income proportionally to the depreciation charges on these assets.

4.25 Lease

Classification of the lease is made at the lease inception, based on the economic substance of the lease agreement.

A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. At the commencement of a finance lease, the leased asset and the leased liability are recorded at the lower of the fair value of the leased asset or the present value of the minimum lease payments. Any initial direct costs of the lessee are added to the amount recognized as an asset. Lease payments shall be apportioned between reduction of the outstanding liability and the finance charge. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. The finance charge as recognized as financial expenses in the statement of comprehensive income throughout the lease term.

An operating lease is a lease under which the lessor retains significant part of the risks and rewards incidental to ownership of the asset. Lease payments under an operating lease are recognized as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

4.26 Statement of cash flows

The statement of cash flows is prepared using the indirect method..

5. Changes of accounting principles and data presentation

New standards and interpretations which became effective on January 1, 2016

- Amendments to IAS 19 Employee benefits;
- Changes resulting from annual improvements of IFRS 2010-2012;
- Amendments to IFRS 11 Settlement of acquisition of an interest in a joint operation;
- Amendments to IAS 16 and IAS 38 Explanation of allowed depreciation methods;
- Amendments to IAS 16 and IAS 41 Agriculture: bearer plants;
- Amendments to IAS 27 Equity method in separate financial statements;
- Changes resulting from annual improvements of IFRS 2012-2014;
- Amendments to IAS 1 Disclosures;
- Amendments to IFRS 10, IFRS 12 and IAS 28 Clarification of the provisions on recognition of investment units in the consolidation.

The above amendments had no influence on the applied accounting policy and did not require amendments to the financial statements.

EXPLANATORY NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

EXPLANATORY NOTES TO THE OPERATING SEGMENTS

6. Information on operating segments

The PGE Group companies conduct their business activities based on relevant concessions, including primarily concession on: production, trading and distribution of electricity, generation, transmission and distribution of heat, granted by the President of Energy Regulatory Office and concessions for the extraction of lignite deposits, granted by the Minister of the Environment. Concessions, as a rule, are being issued for the period between 10 and 50 years. Main concessions in the PGE Group expire in the years 2020-2038.

Relevant assets are assigned to the held concessions on lignite mining and generation and distribution of electricity and heat, which was presented in detailed information on operating segments. For holding concessions concerning electricity and heat the Group incurs annual charges dependent on the level of turnover, whereas for conducting licensed extraction of lignite the exploitation charges as well as fees for the use of mining are borne. The exploitation charges depend on the current rate and the volume of the extraction. In 2016, PGE Group's concessions costs amounted to PLN 5 milion (PLN 5 million in 2015), exploitation charges and minig usufruct charges amount to PLN 123 million in 2016 and PLN 126 million in 2015.

PGE Group presents information on operating segments in the current and comparative reporting period in accordance with IFRS 8 *Operating Segments*. The PGE Group' segment reporting is based on the following business segments:

- Conventional Generation comprises exploration and mining of lignite and production of electricity in the Group's power plants and heat and power plants as well as ancillary services,
- Renewables comprise generation of electricity in pumped-storage power plants and from renewable sources,
- Supply includes sales and purchases of electricity and gas on the wholesale market, trading in emissions certificates and energy origin rights, sales and purchases of fuel, as well as sales of electricity and rendering services to end users,
- Distribution comprises management over local distribution networks and transmission of electricity,
- Other operations comprise services rendered by the subsidiaries for the Group, e.g. fund raising, IT, telecommunication, accounting and HR, and transport services. Additionally, the other operations segment comprises the activities of a subsidiary whose main business is preparation and implementation of a nuclear power plant construction project.

Organization and management over the PGE Group is based on segment reporting separated by nature of the products and services provided. Each segment represents a strategic business unit, offering different products and serving different markets. Assignment of particular entities to operating segments is described in note 1.3 of these financial statements. As a rule, inter-segment transactions are disclosed as if they were concluded with third parties – under market conditions. The exception to this rule were new bonds issued by subsidiaries belonging the tax group with interest rates below market rates and settlements of tax losses within the tax group.

When analysing the results of particular business segments the management of the PGE Group draws attention primarily to EBITDA reached.

Seasonality of business segments

Main factors affecting the demand for electricity and heat are: weather conditions – air temperature, wind force, rainfall, socio-economic factors – number of energy consumers, energy carriers prices, growth of GDP and technological factors – advances in technology, product manufacturing technology. Each of these factors has an impact on technical and economic conditions of production, distribution and transmission of energy carriers, thus influence the results obtained by the PGE Group.

The level of electricity sales is variable throughout a year and depends especially on weather conditions- air temperature, length of the day. Growth in electricity demand is particularly evident in winter periods, while lower demands are observed during the summer months. Moreover, seasonal changes are evident among selected groups of end users. Seasonality effects are more significant for households than for the industrial sector.

Sales of heat depend in particular on air temperature and are higher in winter and lower in summer.

for the year 2016 in accordance with IFRS EU (in PLN million)

6.1 Information on business segments

Information on business segments for the period ended December 31,2016

	Conventional Generation	Renewables	Suppy	Distribution	Other operations	Consolidation adjustments	Total
STATEMENT OF PROFIT OR LOSS							
Sales revenues from external customers	11,303	657	13,711	1,979	406	36	28,092
Sales revenues from inter-segment transactions	435	60	2,303	3,939	282	(7,019)	-
TOTAL SEGMENT REVENUES	**11,738**	**717**	**16,014**	**5,918**	**688**	**(6,983)**	**28,092**
Costs of goods sold	(9,077)	(1,215)	(14,095)	(4,534)	(633)	6,380	**(23,174)**
EBIT *)	**2,691**	**(770)**	**473**	**1,104**	**(64)**	**78**	**3,512**
Financial income / (expenses), net							(193)
Share of profit/(loss) of entities under the equity method							(45)
PROFIT/(LOSS) BEFORE TAX							**3,274**
Income tax							(708)
NET PROFIT/(LOSS) FOR THE REPORTING PERIOD							**2,566**
Depreciation, amortization, disposal and impairment losses recognized in profit or loss	1,491	1,135	27	1,126	131	(46)	3,864
EBITDA **)	**4,182**	**365**	**500**	**2,230**	**67**	**32**	**7,376**
ASSETS AND LIABILITIES							
Segment assets excluding trade receivables	35,862	3,566	970	16,549	961	(772)	57,136
Trade receivables	481	105	2,499	833	106	(1,319)	2,705
Shares accounted for under the equity method							402
Unallocated assets							7,231
TOTAL ASSETS							**67,474**
Segment liabilities excluding trade liabilities	8,570	349	1,378	1,922	158	105	12,482
Trade liabilities	602	36	1,194	264	75	(1,195)	976
Unallocated liabilities							11,241
TOTAL LIABILITIES							**24,699**
OTHER INFORMATION ON BUSINESS SEGMENT							
Capital expenditure	6,179	144	23	1,721	170	(85)	8,152
Impairment allowances on financial and non-financial assets	104	865	(108)	11	1	(1)	872
Other non-monetary expenses ***)	768	5	396	26	33	-	1,228

*) EBIT = operating profit (loss)

**) EBITDA = EBIT + depreciation, amortization, disposal and impairment losses (PPE, IA, goodwill) that are recognized in profit or loss

***) Non-monetary expenses include mainly changes in provisions such as: rehabilitation provision, provision for CO_2 emission rights, provision for jubilee awards and employee tariff that are recognized in profit or loss and other comprehensive income.

for the year 2016 in accordance with IFRS EU (in PLN million)

Information on business segments for the period ended December 31, 2015

restated	Conventional Generation	Renewables	Supply	Distribution	Other operations	Consolidation adjustments	Total
STATEMENT OF PROFIT OR LOSS							
Sales revenues from external customers	12,164	709	13,308	1,935	409	17	28,542
Sales revenues from inter-segment transactions	551	52	2,475	4,148	273	(7,499)	-
TOTAL SEGMENT REVENUES	**12,715**	**761**	**15,783**	**6,083**	**682**	**(7,482)**	**28,542**
Costs of goods sold	(17,706)	(586)	(13,719)	(4,397)	(611)	6,953	**(30,066)**
EBIT *)	**(5,732)**	**107**	**585**	**1,387**	**(51)**	**115**	**(3,589)**
Financial income / (expenses), net							(167)
Share of profit/(loss) of entities under the equity method							-
PROFIT/(LOSS) BEFORE TAX							**(3,756)**
Income tax							719
NET PROFIT/(LOSS) FOR THE REPORTING PERIOD							**(3,037)**
Depreciation, amortization, disposal and impairment losses recognized in profit or loss	10,430	284	25	1,074	117	(113)	11,817
EBITDA **)	**4,698**	**391**	**610**	**2,461**	**66**	**2**	**8,228**
ASSETS AND LIABILITIES							
Segment assets excluding trade receivables	31,974	4,687	1,168	15,945	917	(896)	53,795
Trade receivables	445	80	2,594	765	116	(1,452)	2,548
Shares accounted for under the equity method							8
Unallocated assets							4,945
TOTAL ASSETS							**61,296**
Segment liabilities excluding trade liabilities	9,361	436	1,668	2,076	209	(345)	13,405
Trade liabilities	711	39	1,330	260	82	(1,303)	1,119
Unallocated liabilities							6,355
TOTAL LIABILITIES							**20,879**
OTHER INFORMATION ON BUSINESS SEGMENT							
Capital expenditure	6,495	931	31	1,841	216	(64)	9,450
Impairment allowances on financial and non-financial assets	8,997	49	10	19	2	(13)	9,064
Other non-monetary expenses ***)	975	6	1,040	119	30	6	2,176

*) EBIT = operating profit (loss)
**) EBITDA = EBIT + depreciation, amortization, disposal and impairment losses (PPE, IA, goodwill) that are recognized in profit or loss
***) Non-monetary expenses include mainly changes in provisions such as: rehabilitation provision, provision for CO_2 emission rights, provision for jubilee awards and employee tariff that are recognized in profit or loss and other comprehensive income.

for the year 2016 in accordance with IFRS EU (in PLN million)

6.2 Information on geographical areas

The geographic distribution of sales revenues for the year ended December 31, 2016 and December 31, 2015 is as follows:

	Year ended December 31, 2016	Year ended December 31, 2015
REVENUES FROM OPERATING ACTIVITIES		
Domestic market	27,975	28,421
EU countries	106	110
Other countries	11	11
TOTAL REVENUES	**28,092**	**28,542**

The geographical distribution of assets as at December 31, 2016 and December 31, 2015 is as follows:

	Year ended December 31, 2016	Year ended December 31, 2015 *restated*
OTHER INFORMATION ON THE AREA		
Domestic market	59,815	56,312
EU countries	25	29
Other countries	1	2
SEGMENT ASSETS, TOTAL	**59,841**	**56,343**
Domestic market	7,184	4,902
EU countries	47	43
UNALLOCATED ASSETS, TOTAL	**7,231**	**4,945**
Domestic market	402	8
SHARES ACCOUNTED FOR UNDER THE EQUITY METHOD, TOTAL	**402**	**8**
TOTAL ASSETS	**67,474**	**61,296**

In order to correct presentation of the data the Group conducted reclassifications between specific positions for the year 2015.

EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2016
Sales revenues	7,133	6,533	6,897	7,529	**28,092**
Costs of goods sold	(5,605)	(6,217)	(5,517)	(5,835)	**(23,174)**
GROSS PROFIT / (LOSS) ON SALES	**1,528**	**316**	**1,380**	**1,694**	**4,918**
Other operating income / (expenses), net	157	77	28	738	**1,000**
EBIT – OPERATING PROFIT / (LOSS)	**1,123**	**(171)**	**895**	**1,665**	**3,512**
Financial income / (expenses), net	(48)	(107)	(47)	9	**(193)**
Share of profit/loss of entities accounted for under equity method	-	(42)	(19)	16	**(45)**
PROFIT / (LOSS) BEFORE TAX	**1,075**	**(320)**	**829**	**1,690**	**3,274**
Income tax	(206)	(6)	(173)	(323)	**(708)**
NET PROFIT / (LOSS) FOR THE REPORTING PERIOD	**869**	**(326)**	**656**	**1,367**	**2,566**

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2015
Sales revenues	7,553	6,692	6,915	7,382	**28,542**
Costs of goods sold	(5,548)	(13,925)	(5,140)	(5,453)	**(30,066)**
GROSS PROFIT / (LOSS) ON SALES	**2,005**	**(7,233)**	**1,775**	**1,929**	**(1,524)**
Other operating income / (expenses), net	14	174	40	(60)	**168**
EBIT – OPERATING PROFIT / (LOSS	**1,416**	**(7,590)**	**1,312**	**1,273**	**(3,589)**
Financial income / (expenses), net	(54)	(7)	(49)	(57)	**(167)**
PROFIT / (LOSS) BEFORE TAX	**1,362**	**(7,597)**	**1,263**	**1,216**	**(3,756)**
Income tax	(264)	1,440	(234)	(223)	**719**
NET PROFIT / (LOSS) FOR THE REPORTING PERIOD	**1,098**	**(6,157)**	**1,029**	**993**	**(3,037)**

In order to correct presentation of the data for the quarterly periods the Group conducted reclassifications between specific positions.

7. Revenues and expenses

7.1 Sales revenues

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2016
SALES REVENUES					
Sales of merchandise and finished goods with excise tax	*7,001*	*6,400*	*6,751*	*7,393*	***27,545***
Excise tax	*(126)*	*(120)*	*(122)*	*(133)*	***(501)***
Revenues from sale of merchandise and finished goods, including:	**6,875**	**6,280**	**6,629**	**7,260**	**27,044**
Sale of electricity	4,678	4,608	4,847	5,039	**19,172**
Sale of distribution services	1,433	1,332	1,365	1,464	**5,594**
Sale of heat	283	119	81	249	**732**
Sale of energy origin rights	185	(39)	59	156	**361**
Regulatory system services	137	113	123	140	**513**
Sale of gas	73	58	59	106	**296**
Others sale of merchandise and materials	86	89	95	106	**376**
Revenues from sale of services	**128**	**130**	**137**	**133**	**528**
Revenues from LTC compensations	**130**	**123**	**131**	**136**	**520**
TOTAL SALES REVENUES	**7,133**	**6,533**	**6,897**	**7,529**	**28,092**

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2015
SALES REVENUES					
Sales of merchandise and finished goods with excise tax	*7,375*	*6,549*	*6,779*	*7,269*	***27,972***
Excise tax	*(117)*	*(130)*	*(130)*	*(134)*	***(511)***
Revenues from sale of merchandise and finished goods, including	**7,258**	**6,419**	**6,649**	**7,135**	**27,461**
Sale of electricity	*4,988*	*4,540*	*4,844*	*4,874*	**19,246**
Sale of distribution services	*1,455*	*1,358*	*1,395*	*1,475*	**5,683**
Sale of heat	*271*	*132*	*90*	*231*	**724**
Sale of energy origin rights	*207*	*122*	*56*	*215*	**600**
Regulatory system services	*127*	*117*	*117*	*138*	**499**
Sale of gas	*101*	*35*	*35*	*77*	**248**
Others sale of merchandise and materials	*109*	*115*	*112*	*125*	**461**
Revenues from sale of services	**133**	**134**	**124**	**144**	**535**
Revenues from LTC compensations	**162**	**139**	**142**	**103**	**546**
TOTAL SALES REVENUES	**7,553**	**6,692**	**6,915**	**7,382**	**28,542**

The decrease in revenues from sale of electricity in 2016, as compared to 2015 is mainly due to lower volumes on the wholesale market and lower average selling price of electricity sold.

The decrease in revenues from sale of energy origin rights is primarily caused by decline in prices of green certficates.

Revenues from LTC compensations are described in note 33.1 of these financial statements.

for the year 2016 in accordance with IFRS EU (in PLN million)

7.2 Cost by nature and function

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	**Year ended December 31, 2016**
COST BY NATURE					
Depreciation, amortization and disposal	722	724	749	784	**2,979**
Impairment losses	9	798	33	165	**1,005**
Materials and energy	840	655	588	734	**2,817**
External services	593	617	638	721	**2,569**
Taxes and charges	811	773	873	868	**3,325**
Employee benefits expenses	1,117	1,059	1,022	1,039	**4,237**
Other cost by nature	63	65	66	73	**267**
TOTAL COST BY NATURE	**4,155**	**4,691**	**3,969**	**4,384**	**17,199**
Change in inventories	(29)	19	8	4	**2**
Cost of products and services for the entity's own needs	(264)	(269)	(251)	(223)	**(1,007)**
Distribution and selling expenses	(379)	(348)	(350)	(352)	**(1,429)**
General and administrative expenses	(183)	(216)	(163)	(415)	**(977)**
Cost of merchandise and materials sold	2,305	2,340	2,304	2,437	**9,386**
COST OF GOODS SOLD	**5,605**	**6,217**	**5,517**	**5,835**	**23,174**

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	**Year ended December 31, 2015**
COST BY NATURE					
Depreciation, amortization and disposal	812	807	694	635	**2,948**
Impairment losses	24	8,867	41	107	**9,039**
Materials and energy	917	730	709	897	**3,253**
External services	582	618	629	724	**2,553**
Taxes and charges	762	694	721	726	**2,903**
Employee benefits expenses	1,121	1,033	1,019	1,036	**4,209**
Other cost by nature	59	68	78	75	**280**
TOTAL COST BY NATURE	**4,277**	**12,817**	**3,891**	**4,200**	**25,185**
Change in inventories	(44)	-	-	32	**(12)**
Cost of products and services for the entity's own needs	(307)	(372)	(378)	(435)	**(1,492)**
Distribution and selling expenses	(395)	(337)	(322)	(354)	**(1,408)**
General and administrative expenses	(208)	(194)	(181)	(242)	**(825)**
Cost of merchandise and materials sold	2,225	2,011	2,130	2,252	**8,618**
COST OF GOODS SOLD	**5,548**	**13,925**	**5,140**	**5,453**	**30,066**

In order to correct presentation of the data for the quarterly periods the Group conducted reclassifications between specific positions.

for the year 2016 in accordance with IFRS EU (in PLN million)

7.2.1 Depreciation, amortization, disposal and impairment losses

Recognition of depreciation, amortization, disposal and impairment losses of property, plant and equipment, intangible assets and investment property in the financial statement of comprehensive income is presented below:

Year ended December 31, 2016	Depreciation, amortization and disposal				Impairment losses			
	Property, plant and equipment	Intangible assets	Investment property	TOTAL	Property, plant and equipment	Intangible assets	Investment property	TOTAL
Cost of goods sold	2,691	84	1	**2,776**	489	284	3	**776**
Distribution and selling expenses	12	5	-	**17**	-	-	-	**-**
General and administrative expenses	52	14	-	**66**	222	7	-	**229**
TOTAL DEPRECIATION, AMORTIZATION AND IMPAIRMENT LOSSES REFLECTED IN FINANCIAL RESULT	**2,755**	**103**	**1**	**2,859**	**711**	**291**	**3**	**1,005**
Change in inventories	1	-	-	**1**	-	-	-	**-**
Cost of products and services for the entity's own needs	119	-	-	**119**	-	-	-	**-**
TOTAL DEPRECIATION, AMORTIZATION AND IMPAIRMENT LOSSES	**2,875**	**103**	**1**	**2,979**	**711**	**291**	**3**	**1,005**

As described in note 3.2 of these financial statements, impairment allowances were raised mainly due to impairment losses of power generating assets of Renewables segment. In previous period, impairment allowances referred primarily to Conventional Generation segment.

Year ended December 31, 2015	Depreciation, amortization and disposal				Impairment losses			
	Property, plant and equipment	Intangible assets	Investment property	TOTAL	Property, plant and equipment	Intangible assets	Investment property	TOTAL
Cost of goods sold	2,631	74	2	**2,707**	9,013	16	-	**9,029**
Distribution and selling expenses	23	4	-	**27**	8	-	-	**8**
General and administrative expenses	33	11	-	**44**	2	-	-	**2**
TOTAL DEPRECIATION, AMORTIZATION AND IMPAIRMENT LOSSES REFLECTED IN FINANCIAL RESULT	**2,687**	**89**	**2**	**2,778**	**9,023**	**16**	**-**	**9,039**
Change in inventories	(12)	-	-	**(12)**	-	-	-	**-**
Cost of products and services for the entity's own needs	182	-	-	**182**	-	-	-	**-**
TOTAL DEPRECIATION, AMORTIZATION AND IMPAIRMENT LOSSES	**2,857**	**89**	**2**	**2,948**	**9,023**	**16**	**-**	**9,039**

7.2.2 Materials and energy

	Year ended December 31, 2016	Year ended December 31, 2015
Cost of production fuel	1,994	2,372
Renovation materials	475	474
Energy	148	156
Other	200	251
TOTAL MATERIALS AND ENERGY	**2,817**	**3,253**

for the year 2016 in accordance with IFRS EU (in PLN million)

7.2.3 External services

	Year ended December 31, 2016	Year ended December 31, 2015
Transmission services	1,561	1,483
External services – repairs and exploitation	309	311
Logistics services	85	84
Telecommunication services	232	231
Rent and lease	53	56
IT services	85	89
Consulting services	31	45
Other	213	254
TOTAL EXTERNAL SERVICES	**2,569**	**2,553**

7.2.4 Employee benefits expenses and employment structure

	Year ended December 31, 2016	Year ended December 31, 2015
Payroll	3,154	3,173
Social security expenses	606	612
Retirement and pension expenses	11	16
Jubilee awards, coal benefits	102	100
Other post-employment benefits	37	30
Change in provisions for employee benefits	(146)	(173)
Cost of the Voluntary Leave Program	16	(20)
Other employee benefits	457	471
TOTAL EMPLOYEE BENEFITS EXPENSES	**4,237**	**4,209**
Included in costs of goods sold	3,123	2,984
Included in distribution and selling expenses	259	233
Included in general and administrative expenses	504	512
Included in cost of products and services for the entity's own needs	351	480

Employment in the PGE Group (FTE) was as follows:

	Year ended December 31, 2016	Year ended December 31, 2015
Conventional Generation	22,788	23,198
Renewables	509	519
Supply	2,066	2,002
Distribution	10,239	10,298
Other consolidated units	2,869	2,860
TOTAL EMPLOYMENT	**38,471**	**38,877**

for the year 2016 in accordance with IFRS EU (in PLN million)

7.3 Other operating income and expenses

	Year ended December 31, 2016	Year ended December 31, 2015
OTHER OPERATING INCOME		
Change in rehabilitation provision	643	93
Adjustment of revenues from LTC compensations	148	-
Penalties, fines and compensations received	137	67
Reversal of other provisions	44	74
Grants received	43	25
Gain on liquidation/disposal of current assets	37	49
Reversal of impairment allowances on receivables	24	31
Profit on disposal of property, plant and equipment / intangible assets	11	20
Property, plant and equipment, intangible assets received free of charge	11	9
Tax refund	6	1
Revenues from illegal energy consumption	6	7
Surpluses / recognition of assets	4	18
Compensation for legal proceedings' costs	4	9
Other	53	28
TOTAL OTHER OPERATING INCOME	**1,171**	**431**

Revenues from LTC compensations are described in note 33.1 of these financial statements.

Change in measurements of revenues from LTC compensations relates mainly to surface mines and is described in note 21.1 of these financial statements.

	Year ended December 31, 2016	Year ended December 31, 2015
OTHER OPERATING EXPENSES		
Recognition of impairment allowances on receivables	49	56
Recognition of other provisions	26	56
Liquidation of damages / breakdowns	19	20
Reinvoices	16	24
Donations granted	13	18
Liquidation of property, plant and equipment and intangible assets associated with other operations	6	4
Legal proceedings' costs	6	8
Impairment of discounted investments and liquidation of current assets	5	12
Compensations	5	7
Impairment allowances on other assets	1	5
Other	25	53
TOTAL OTHER OPERATING EXPENSES	**171**	**263**

for the year 2016 in accordance with IFRS EU (in PLN million)

7.4 Financial income and expenses

	Year ended December 31, 2016	Year ended December 31, 2015
FINANCIAL INCOME FROM FINANCIAL INSTRUMNETS		
Dividends	2	1
Interest	55	103
Revaluation of financial instruments, including:	117	33
Reversal of impairment allowances	*90*	*2*
Other derivatives	*27*	*20*
CO_2 emission rights	*-*	*11*
Gain on disposal of investments	-	15
Foreign exchange gains	14	-
FINANCIAL INCOME ON FINANCIAL INSTRUMENTS	**188**	**152**
OTHER FINANCIAL INCOME		
Interest on statutory receivables	1	1
Reversal of provisions	1	1
Other	1	2
OTHER FINANCIAL INCOME	**3**	**4**
TOTAL FINANCIAL INCOME	**191**	**156**

The Group recognizes interest income primarily on cash.

The increase of Revaluation of financial instruments is mainly due to partly reversed impairment allowance of bonds issued by Autostrada Wielkopolska S.A. in the total amount of PLN 89 million.

Revaluation of other derivatives the Group includes an ineffective portion of CCIRS hedging transactions valuation designated as hedging instruments in the cash-flow hedge accounting and total valuation of other derivatives.

	Year ended December 31, 2016	Year ended December 31, 2015
FINANCIAL EXPENSES FROM FINANCIAL INSTRUMNETS		
Interest	131	123
Revaluation of financial instruments	10	-
CO_2 emission rights	*5*	*-*
Other derivatives	*5*	*-*
Impairment loss	2	5
Foreign exchange losses	33	30
FINANCIAL EXPENSES FROM FINANCIAL INSTRUMENTS	**176**	**158**
OTHER FINANCIAL EXPENSES		
Interest expenses, including unwinding of the discount	180	156
Interest on statutory liabilities	1	1
Provisions created	25	5
Other	2	3
OTHER FINANCIAL EXPENSES	**208**	**165**
TOTAL FINANCIAL EXPENSES	**384**	**323**

Interest expense relates mainly to issued bonds, loans and borrowings. Interest expense (unwinding of the discount) on non-financial items relates mainly to rehabilitation provision and provisions for employee benefits.

for the year 2016 in accordance with IFRS EU (in PLN million)

7.4.1 Valuation of transaction related to trading in CO_2 emission rights

As described in note 7.4 of these financial statements, income and expenses recognized under the heading "revaluation of the financial instruments" comprise result on transactions related to the CO_2 emission rights (so-called trading portfolio). The following table illustrated the effects of particular items related to the CO_2 emission rights on the financial income and expenses.

	Year ended December 31, 2016	Year ended December 31, 2015
Income		
Valuation of commodity forward	41	4
Profit on sale of CO_2 emission rights outside of PGE Group	1	52
Profit on realization of currency forward	-	4
INCOME RELATED TO TRADING IN CO_2 EMISSION RIGHTS, TOTAL	**42**	**60**
Expenses		
Valuation of currency forward	(1)	(7)
Revaluation of trading portfolio	(46)	(42)
EXPENSES RELATED TO TRADING IN CO_2 EMISSION RIGHTS, TOTAL	**(47)**	**(49)**
Financial income / (Expenses) related to trading in CO_2 emission rights	**(5)**	**11**

7.5 Share of profit of associates and entities jointly controlled entities accounted for under the equity method

	Polska Grupa Górnicza	ElectroMobility Poland	PEC Bogatynia
SHARE IN VOTES	Until October 2016 15.66% November – December 2016 16.63%	25.00%	34.93%
PERIOD ENDED DECEMBER 31, 2016			
Revenues	3.828	-	13
Result from continuing operations	(332)	-	(1)
Share of profit of associates and jointly controlled entities	**(51)**	-	-
Elimination of unrealized losses	6	-	-
SHARE OF PROFIT OF ASSOCIATES AND ENTITIES JOINTLY CONTROLLED	**(45)**	-	-
Other comprehensive income	(11)	-	-
SHARE OF ASSOCIATES AND JOINTLY CONTROLLED ENTITIES IN OTHER COMPREHENSIVE INCOME	**(2)**	-	-

Data of jointly controlled entity Polska Grupa Górnicza sp. z o.o. has been consolidated since April 29, 2016 and the data of ElectroMobility S.A. since December 7, 2016.

PGE Group made an consolidation adjustment related to the margin of coal sale between Polska Grupa Górnicza and the Group.

Purchase of shares in Polska Grupa Górnicza sp. z o.o. is described in more details in note 33.2 of these financial statements.

for the year 2016 in accordance with IFRS EU (in PLN million)

8. Income tax

8.1 Tax in the statement of comprehensive income

Main elements of income tax expense for the years ended December 31, 2016 and December 31, 2015 are as follows:

	Year ended December 31, 2016	Year ended December 31, 2015
INCOME TAX RECOGNISED IN THE STATEMENT OF PROFIT OR LOSS		
Current income tax	398	467
Previous periods current income tax adjustments	16	(6)
Deferred income tax	294	(1,180)
INCOME TAX EXPENSE PRESENTED IN THE STATEMENT OF PROFIT OR LOSS	**708**	**(719)**
INCOME TAX PRESENTED IN OTHER COMPREHENSIVE INCOME		
From actuarial gains and losses from valuation of provisions for employee benefits	47	3
From valuation of hedging instruments	39	9
(TAX BENEFIT) / EXPENSE RECOGNIZED IN OTHER COMPREHENSIVE INCOME (EQUITY)	**86**	**12**

A substantial change in the deferred tax in 2015 is related to the creation of impairment allowances on property, plant and equipment.

8.2 Effective tax rate

A reconciliation of the calculation of income tax on profit before tax at the statutory tax rate and income tax calculated according to the effective tax rate of the Group is as follows:

	Year ended December 31, 2016	Year ended December 31, 2015
GROSS PROFIT / (LOSS)	**3,274**	**(3,756)**
Income tax according to Polish statutory tax rate of 19%	621	(714)
Previous periods current income tax adjustments	16	(6)
Previous periods deferred income tax adjustments	(36)	(17)
Costs not recognized as tax-deductible costs	119	61
Non-taxable income	(14)	(26)
Other	2	(17)
TAX AT EFFECTIVE TAX RATE (Income tax (expense) as presented in the consolidated statements)	**708**	**(719)**
EFFECTIVE TAX RATE	**22%**	**19%**

Other differences presented in the comparative period concern mainly adjustments of deferred tax estimates made by the PGE Group subsidiaries.

for the year 2016 in accordance with IFRS EU (in PLN million)

EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION

9. Property, plant and equipment

	As at December 31, 2016	As at December 31, 2015
Land	236	243
Buildings and construction	19,061	18,465
Technical equipment	19,604	17,774
Vehicles	341	325
Other property, plant and equipment	2,522	2,390
Construction in progress	9,601	7,871
CARRYING AMOUNT OF PROPERTY, PLANT AND EQUIPMENT	**51,365**	**47,068**

Changes in property, plant and equipment by type

	Land	Buildings and construction	Technical equipment	Vehicles	Other property, plant and equipment	Construction in progress	Total
GROSS BOOK VALUE							
AS AT JANUARY 1, 2016	**266**	**31,669**	**39,261**	**720**	**4,991**	**8,019**	**84,926**
Capital expenditures	-	-	-	-	-	8,016	**8,016**
Transfer from construction in progress	16	2,003	3,546	59	476	(6,100)	**-**
Liquidation, disposal	(1)	(119)	(640)	(17)	(7)	(1)	**(785)**
Other	(10)	(61)	(15)	(33)	(189)	31	**(277)**
AS AT DECEMBER 31, 2016	**271**	**33,492**	**42,152**	**729**	**5,271**	**9,965**	**91,880**
ACCUMULATED DEPRIACIATION AND IMPAIRMENT LOSSES							
AS AT JANUARY 1, 2016	**23**	**13,204**	**21,487**	**395**	**2,601**	**148**	**37,858**
Depreciation and net value of liquidation presented in costs by nature	5	1,203	1,445	57	164	1	**2,875**
Impairment allowances	9	195	293	1	2	211	**711**
Liquidation, disposal	-	(107)	(592)	(17)	(7)	-	**(723)**
Other	(2)	(64)	(85)	(48)	(11)	4	**(206)**
AS AT DECEMBER 31, 2016	**35**	**14,431**	**22,548**	**388**	**2,749**	**364**	**40,515**
CARRYING AMOUNT AS AT DECEMBER 31, 2016	**236**	**19,061**	**19,604**	**341**	**2,522**	**9,601**	**51,365**

	Land	Buildings and construction	Technical equipment	Vehicles	Other property, plant and equipment	Construction in progress	Total
GROSS BOOK VALUE							
AS AT JANUARY 1, 2015	**293**	**29,865**	**36,457**	**658**	**4,198**	**4,800**	**76,271**
Capital expenditures	-	1	7	3	2	9,205	**9,218**
Transfer from construction in progress	14	1,880	3,200	82	810	(5,986)	**-**
Liquidation, disposal	(2)	(130)	(442)	(21)	(11)	(4)	**(610)**
Changes in the PGE Group	-	(2)	(1)	(1)	-	-	**(4)**
Other	(39)	55	40	(1)	(8)	4	**51**
AS AT DECEMBER 31, 2015	**266**	**31,669**	**39,261**	**720**	**4,991**	**8,019**	**84,926**
ACCUMULATED DEPRECIATION AND IMPAIRMENT LOSSES							
AS AT JANUARY 1, 2015	**25**	**10,282**	**14,368**	**356**	**1,400**	**102**	**26,533**
Depreciation and net value of liquidation presented in costs by nature	6	1,169	1,471	56	152	3	**2,857**
Impairment allowances	-	1,859	6,077	4	1,037	46	**9,023**
Liquidation, disposal	(1)	(106)	(439)	(19)	(11)	(3)	**(579)**
Changes in the PGE Group	-	(1)	(1)	(1)	-	-	**(3)**
Other	(7)	1	11	(1)	23	-	**27**
AS AT DECEMBER 31, 2015	**23**	**13,204**	**21,487**	**395**	**2,601**	**148**	**37,858**
CARRYING AMOUNT AS AT DECEMBER 31, 2016	**243**	**18.465**	**17.774**	**325**	**2.390**	**7.871**	**47.068**

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

Significant additions and disposals of property, plant and equipment

The most significant capital expenditures were incurred by the Conventional Generation segment (PLN 6,171 million), Distribution segment (PLN 1,696 million). The main investment projects were: construction of power units 5-6 at the Elektrownia Opole (Power Plant Opole) (PLN 3,467 million), reconstruction and refurbishment of power units 7-12 at the Elektrownia Bełchatów (Power Plant Bełchatów) (PLN 518 million), construction of power unit 11 at the Elektrownia Turów (PLN 498 million), construction of gas and steam unit at the Elektrociepłownia Gorzów (PLN 215 million), connection of new customers (PLN 572 million) and modernization and development of electric power networks, stations and lines (PLN 788 million) in the Distribution segment.

No significant property, plant and equipment sale transactions occurred during the reporting period.

Borrowing costs

During the year ended December 31, 2016 the PGE Group capitalized in the value of property, plant and equipment and construction in progress borrowings costs of approx. PLN 103 million (PLN 67 million in the comparative period).

Capitalization of stripping costs

In the current period, in accordance with the requirements of IFRIC 20, the Group capitalized expenditures regarding stripping costs in the production phase of PLN 447 million. At the same time, the Group recognized depreciation of capitalized stripping costs of PLN 73 million. Capitalized stripping costs are presented as "other property, plant and equipment".

Capitalization of changes in valuation of rehabilitation provision

The PGE Group recognizes in the property, plant and equipment changes in the value of rehabilitation provision assigned to stripping of overburden, provision for rehabilitation of post-construction grounds of wind farms and provision for liquidation of property, plant and equipment. As at December 31, 2016 net value of capitalized rehabilitation provision amounted to PLN 632 million (including PLN 543 million of the provision for rehabilitation of post-exploitation mining properties). In comparative period net value of capitalized rehabilitation provision amounted to PLN 900 million (including PLN 779 million of the provision for rehabilitation of post-exploitation mining properties). Capitalized rehabilitation provision is presented in: “land” and “other property, plant and equipment”.

10. Investment property

Investment property in the PGE Group companies comprises mainly buildings located in the entity’s locations, leased fully or partially to third parties. Fair value of investment property is not significantly different than valuation determined under the historical cost convention in light of the materiality related to the consolidated financial statements.

11. Intangible assets

	As at December 31, 2016	As at December 31, 2015
Development costs	2	2
Goodwill	9	286
Software	73	93
Other licenses and patents	132	127
Purchase of right of perpetual usufruct of land	64	61
Other intangible assets	134	135
Intangible assets not-commissioned to use	239	200
CARRYING AMOUNT OF INTANGIBLE ASSETS	**653**	**904**

for the year 2016 in accordance with IFRS EU (in PLN million)

Changes in intangible assets

	Development costs	Goodwill	Software	Other licenses and patents	Purchase of right of perpetual usufruct of land	Other intangible assets	Intangible assets not-commissioned to use	Total
GROSS BOOK VALUE								
AS AT JANUARY 1, 2016	**19**	**286**	**430**	**223**	**71**	**242**	**201**	**1,472**
Capital expenditures	-	-	-	-	-	-	135	135
Transfer of non-commissioned intangible assets	-	-	24	53	1	11	(89)	-
Liquidation, disposal	-	-	(6)	(3)	(1)	-	-	(10)
Other	(1)	(277)	-	1	3	3	(1)	(272)
AS AT DECEMBER 31, 2016	**18**	**9**	**448**	**274**	**74**	**256**	**246**	**1,325**
ACCUMULATED AMORTIZATION AND IMPAIRMENT LOSSES								
AS AT JANUARY 1, 2016	**17**	**-**	**337**	**96**	**10**	**107**	**1**	**568**
Amortization	1	-	44	48	1	9	-	103
Impairment allowances	-	277	-	-	-	6	8	291
Liquidation, disposal	-	-	(6)	(3)	-	-	-	(9)
Other	(2)	(277)	-	1	(1)	-	(2)	(281)
AS AT DECEMBER 31, 2016	**16**	**-**	**375**	**142**	**10**	**122**	**7**	**672**
CARRYING AMOUNT AS AT DECEMBER 31, 2016	**2**	**9**	**73**	**132**	**64**	**134**	**239**	**653**

	Development costs	Goodwill	Software	Other licenses and patents	Purchase of right of perpetual usufruct of land	Other intangible assets	Intangible assets not-commissioned to use	Total
GROSS BOOK VALUE								
AS AT JANUARY 1, 2015	**19**	**286**	**382**	**149**	**64**	**228**	**121**	**1,249**
Capital expenditures	-	-	1	-	-	-	231	232
Transfer of non-commissioned intangible assets	-	-	69	72	1	9	(151)	-
Liquidation, disposal	(1)	-	(21)	-	-	-	(1)	(23)
Other	1	-	(1)	2	6	5	1	14
AS AT DECEMBER 31, 2015	**19**	**286**	**430**	**223**	**71**	**242**	**201**	**1,472**
ACCUMULATED AMORTIZATION AND IMPAIRMENT LOSSES								
AS AT JANUARY 1, 2015	**16**	**-**	**319**	**55**	**8**	**85**	**3**	**486**
Amortization	1	-	39	40	1	8	-	89
Impairment allowances	-	-	-	-	-	16	-	16
Liquidation, disposal	(1)	-	(21)	-	-	-	-	(22)
Other	1	-	-	1	1	(2)	(2)	(1)
AS AT DECEMBER 31, 2015	**17**	**-**	**337**	**96**	**10**	**107**	**1**	**568**
CARRYING AMOUNT AS AT DECEMBER 31, 2015	**2**	**286**	**93**	**127**	**61**	**135**	**200**	**904**

Goodwill

Evaluation of recoverable amount of goodwill has been described in note 3 of these consolidated financial statements.

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

12. Shares in associates accounted for under the equity method

	As at December 31,2016	As at December 31,2015
Polska Grupa Górnicza Sp. z o.o.	391	-
ElectroMobility Poland S.A.	3	-
PEC Bogatynia Sp. z o.o.	8	8
INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD	**402**	**8**

	Polska Grupa Górnicza	ElectroMobility Poland	PEC Bogatynia
SHARE IN VOTES	**16.63%**	**25.00%**	**34.93%**
AS AT DECEMBER 31,2016			
Current assets	1,008	10	3
Non-current assets	6,277	-	22
Current liabilities	2,516	-	2
Non-current liabilities	2,442	-	-
NET ASSETS	**2,327**	**10**	**23**
Share in net assets	**387**	**3**	**8**
Goodwill	4	-	-
INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD	**391**	**3**	**8**

Purchase of shares in Polska Grupa Górnicza sp. z o.o. is described in more detail in note 33.2 of these financial statements.

13. Deferred tax in the statement of financial position

13.1 Deferred tax asset

	As at December 31, 2016	As at December 31, 2015
Difference between tax value and carrying amount of property, plant and equipment	1,559	1,520
Difference between tax value and carrying amount of financial assets	16	31
Difference between tax value and carrying amount of liabilities	272	271
Difference between tax value and carrying amount of inventories	15	21
LTC compensations	253	231
Rehabilitation provision	472	605
Provision for CO_2 emission rights	220	144
Provisions for employee benefits	529	591
Other provisions	129	128
Energy infrastructure acquired free of charge and connection payments received	129	141
Other	15	20
DEFERRED TAX ASSET	**3,609**	**3,703**

Change of deferred tax – assets

	Year ended December 31, 2016	Year ended December 31, 2015
AS AT JANUARY 1	**3,703**	**2,711**
Changes recognized in profit or loss	(39)	1,012
Changes recognized in other comprehensive income	(52)	(16)
Other changes	(3)	(4)
AS AT DECEMBER 31	**3,609**	**3,703**

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13.2 Deferred tax liability

	As at December 31, 2016	As at December 31, 2015
Difference between tax value and carrying amount of property, plant and equipment	2,945	2,681
Difference between tax value and carrying amount of energy origin units	65	107
Difference between tax value and carrying amount of financial assets	377	357
CO_2 emission rights	439	403
LTC compensations	680	671
Other	26	23
DEFERRED TAX LIABILITY	**4,532**	**4,242**

Change of deferred tax – liabilities

	Year ended December 31, 2016	Year ended December 31, 2015
AS AT JANUARY 1	**4,242**	**4,418**
Changes recognized in profit or loss	255	(172)
Changes recognized in other comprehensive income	34	(4)
Other changes	1	-
AS AT DECEMBER 31	**4,532**	**4,242**

AFTER OFF-SET OF THE ASSET AND THE LIABILITY IN PARTICULAR COMPANIES THE GROUP'S DEFFERED TAX IS PRESENTED AS:		
Deferred tax asset	268	313
Deferred tax liability	(1,191)	(852)

14. Inventories

	As at December 31, 2016			As at December 31, 2015		
	Historical cost	Revaluation adjustments	Carrying amount	Historical cost	Revaluation adjustments	Carrying amount
Materials, including	**979**	**(52)**	**927**	**1,067**	**(103)**	**964**
Renovation materials	664	(33)	631	643	(80)	563
Coal	232	-	232	307	-	307
Mazut	15	-	15	14	-	14
Investment materials	14	-	14	16	-	16
Other materials	54	(19)	35	87	(23)	64
Energy origin rights, including:	**602**	**(35)**	**567**	**831**	**(17)**	**814**
Green energy origin rights	388	(33)	355	681	(14)	667
Yellow energy origins rights	148	(2)	146	113	(2)	111
Other energy origin rights	66	-	66	37	(1)	36
Merchandise, including:	**44**	**(10)**	**34**	**66**	**36**	**102**
CO_2 emission rights	37	(8)	29	60	38	98
Other merchandise	7	(2)	5	6	(2)	4
Other inventories	**68**	**-**	**68**	**79**	**-**	**79**
TOTAL INVENTORIES	**1,693**	**(97)**	**1,596**	**2,043**	**(84)**	**1,959**

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

	Year ended December 31, 2016	Year ended December 31, 2015
REVALUATION ADJUSTMENT FOR INVENTORIES AS AT JANUARY 1	**(84)**	**(63)**
Fair value of CO_2 emission rights	(46)	(42)
Impairment allowance raised	(52)	(55)
Impairment allowance reversed	66	58
Impairment allowance used	16	19
Other	3	(1)
REVALUATION ADJUSTMENT FOR INVENTORIES AS AT DECEMBER 31	**(97)**	**(84)**

CO_2 emission rights recognized in the inventories include the rights classified as held-for-sale. These rights are presented at fair value. Change in valuation of these rights in the reporting period should be analyzed together with the revaluation of forward contracts (as presented in note 7.4.1 of these consolidated financial statements).

Creation of impairment allowances related mainly to spare parts and materials as a result of their amortization or obsolescence.

As described in note 25.5 of these consolidated financial statements, PLN 51 million of inventories constituted a collateral for the repayment of liabilities or contingent liabilities.

15. CO_2 emission rights for captive use

CO_2 emission rights (EUA) receive power generating units belonging to the PGE Group, which are covered with the Act dated June 12, 2015 on a scheme for greenhouse gas emission allowance trading. Starting from 2013, only part of emission rights for production of heat will be granted unconditionally, while for production of electricity there is, as a rule, lack of free of charge EUA. Only on the basis of article 10c of Directive 2003/87/EC of the European Parliament and of the Council establishing a scheme for greenhouse gas emission allowance trading within the Community, the derogation is possible providing the realization of investment tasks included in National Investment Plan, which allow to reduce CO_2 emission. The condition under which free of charge CO_2 emission rights can be obtained is presentation of factual-financial statements from realization of tasks included in National Investment Plan.

In the current period entities of the PGE Group received free of charge CO_2 emission rights in the amount of about 25 million for units generating electricity, and about 1 million for the installations other than generating electricity.

In September 2016 PGE Capital Group submitted subsequent reports on the implementation of the investments in order to obtain new units for CO_2 emission. They will be issued at the beginning of 2017.

The schedule for CO_2 emission rights disposal relating heat energy is different – at the beginning of 2017 EUA emission rights will be issued in order to cover the emission of CO_2 for 2017.

	As at December 31,2016		As at December 31,2015	
EUA	Amount (Mg million)	Value	Amount (Mg million)	Value
AS AT JANUARY 1	**77**	**2,172**	**68**	**1,552**
Purchase	40	937	38	1,301
Granted free of charge	26	-	30	-
Redemption	(58)	(760)	(59)	(681)
AS AT DECEMBER 31	**85**	**2,349**	**77**	**2,172**

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

16. Other current and non-current assets

16.1 Other non-current assets

	As at December 31, 2016	As at December 31, 2015
Advances for construction in progress	713	1,042
Other non-current assets	17	21
OTHER ASSETS, TOTAL	**730**	**1,063**

Advances for construction in progress relate mainly to investment projects conducted by the Conventional Generation segment.

16.2 Other current assets

	As at December 31, 2016	As at December 31, 2015
PREPAYMENTS		
Fees, agency commission	34	41
IT services	6	7
Fees for the exclusion of land from agricultural production / forestry	4	4
Property and tort insurance	2	3
Other prepayments	21	19
OTHER CURRENT ASSETS		
VAT receivables	222	388
Excise tax receivables	100	90
Advances for deliveries	6	34
Other current assets	21	13
OTHER ASSETS, TOTAL	**416**	**599**

Fees and commissions include agency commissions and bank loan commissions. Other prepayments include costs of energy infrastructure collisions and long-term contracts.

The increased VAT receivables result from the investment purchases in the Conventional Generation and Renewables segments.

The amount of excise tax receivables regards the exemption from excise tax of electricity generated from renewable energy sources on the basis of a document confirming the redemption of the certificate of origin.

17. Cash and cash equivalents

Short-term deposits are made for different periods, from one day up to one month, depending on the Group's needs for cash, and are deposited at individually agreed interest rates.

The balance of cash and cash equivalents comprises the following positions:

	As at December 31, 2016	As at December 31, 2015
Cash on hand and cash at bank	808	1,304
Overnight deposits	42	57
Short-term deposits	1,819	1,743
TOTAL	**2,669**	**3,104**
Interest accrued on cash, not received at the reporting date	(2)	(1)
Exchange differences on cash in foreign currencies	(1)	(2)
Cash and cash equivalents presented in the statement of cash flows	**2,666**	**3,101**
including restricted cash	*107*	*333*
Undrawn borrowing facilities as at December 31	6,081	5,257
including overdraft facilities	*2,001*	*2,254*

For detailed description of credit agreements please refer to note 25.1.4 of these financial statements.

for the year 2016 in accordance with IFRS EU (in PLN million)

Restricted cash disclosed in the consolidated statement of cash flows relate primarily to:

- cash received as a guarantee of proper execution of the contract and cash received as a tender deposit;
- cash deposit securing the settlements of subsidiaries of the PGE Group with Izba Rozliczeniowa Giełd Towarowych S.A. (Warsaw Commodity Clearing House)

18. Discontinued operations

During the year ended December 31, 2016 and December 31, 2015 the parent company and key subsidiaries did not discontinue any significant operations. However, there are some activities carried out in the PGE Group under which assets that are not closely related to core business are disposed.

19. Assets and liabilities of the Social Fund

The Social Fund is created by employers employing over 20 full time employees. The Group entities create such a fund and contribute periodical allowances. The fund does not possess any property, plant and equipment. The goal of the fund is to subsidize the social activity for employees of the Group, loans granted to its employees and other social expenses.

	As at December 31, 2016	As at December 31, 2015
Loans granted to employees	91	96
Cash	49	48
Social Fund liabilities	(138)	(141)
BALANCE AFTER COMPENSATION	**2**	**3**
Contributions to the Social Fund	**130**	**128**

The assets and liabilities of the Social Fund are netted off in these financial statements.

20. Equity

The purpose of capital management is to maintain safe and effective financing structure, which take into account the operational risk, investment expenditures and interests of shareholders and debt investors. The capital management takes place at the Group level.

According to common practice, the Group monitors the net debt/EBITDA ratio. Net debt comprises current and non-current financial debt (bank credits and loans bearing interest, bonds issued, other debt securities and lease liabilities) reduced by cash and cash equivalents as well as short-term deposits. Restricted cash is not included in the calculation of net debt.

The Group assumes that the maximum level of net debt to EBITDA ratio which allows to maintain credit ratings on investment level amounts to 3.0x.

	Year ended December 31, 2016	Year ended December 31, 2015
Debt / EBITDA ratio	0.70x	0.32x
Net debt / share capital ratio	0.12x	0.07x

Taking into accout the scale of of the whole PGE Group, net debt ratio was relatively low during 2016: net debt to EBITDA ratio remains lower than 1.

Due to continuation of investment program, gradual increase of financial leverage is planned, whereby the Group will intensify analysis of the ratio described above. Net debt to EBITDA ratio is the key element of Group's forecasts and financial strategies.

20.1 Share capital

	As at December 31, 2016
1,470,576,500 Series A ordinary Shares with a nominal value of PLN 10.25 each	15,073
259,513,500 Series B ordinary Shares with a nominal value of PLN 10.25 each	2,660
73,228,888 Series C ordinary Shares with a nominal value of PLN 10.25 each	751
66,441,941 Series D ordinary Shares with a nominal value of PLN 10.25 each	681
TOTAL SHARE CAPITAL	**19,165**

for the year 2016 in accordance with IFRS EU (in PLN million)

	As at December 31, 2015
1,470,576,500 Series A ordinary Shares with a nominal value of PLN 10 each	14,706
259,513,500 Series B ordinary Shares with a nominal value of PLN 10 each	2,595
73,228,888 Series C ordinary Shares with a nominal value of PLN 10 each	732
66,441,941 Series D ordinary Shares with a nominal value of PLN 10 each	665
TOTAL SHARE CAPITAL	**18,698**

All shares of the Company are paid up.

On September 5, 2016 the Extraordinary General Meeting of PGE S.A. adopted resolution on increase of the Company's share capital by PLN 467,440,207.25 from the Company's reserve capital, through increasing the nominal value of shares from PLN 10.00 to PLN 10.25. The capital increase was registered in the National Court Register on November 25, 2016.

Raising the nominal value of the shares is an event that generates tax revenue on shareholders' side. On September 5, 2016 the Extraordinary General Meeting of PGE S.A. adopted resolution on allocation of part of the reserve capital to cover the flat-rate income tax related to the increase of the share capital from the Company's own funds, so the tax burden will be borne by the Company. PGE S.A. received tax interpretations in response to questions on the proper application of the provisions relating to corporate income tax and personal income tax. The analysis of received interpretations leads to the conclusion that the amount of tax which the Company is supposed to pay to the Tax Office due to the increase of the share capital amounts to PLN 110 million. As at December 31, 2016 that amount decreased the equity of the Group and is recognized in non-financial liabilities. Tax liability was paid on January 9, 2017.

After the reporting date until the date of preparation of these financial statements, there have been no changes to the Company''s share capital.

Rights of the shareholders – Rights of the State Treasury regarding the Company's operations

The Company is a part of the PGE Polska Grupa Energetyczna S.A. Group, to which State Treasury holds special rights as long as it remains a shareholder.

Special rights of the State Treasury that are applicable to the PGE Group entities derive from the Act of March 18, 2010 on special rights of the Minister of Energy and their performance in certain companies and groups operating in the electricity, oil and gaseous fuels sectors (Official Journal from 2016, item 2012). The aforesaid Act specifies the particular rights entitled to the Minister of Energy related to companies and groups operating in the electricity, oil and gaseous fuels sectors whose property was disclosed within the register of buildings, installations, equipment and services included in critical infrastructure.

Based on this act the Minister of Energy has the right to object to any resolution or legal action of the Management Board that relates to the ability to dispose a part of Company's property, which may result in threat to functioning, continuity of operations and integrity of critical infrastructure. The objection can also be expressed against any resolution adopted that relates to:

- liquidation of the Company,
- changes of the use or discontinuance of exploitation of the Company's asset, which is a component of critical infrastructure,
- change in the scope of activities of the Company,
- sale or lease of the enterprise or its organized part or establishment of legal restrictions,
- approval of operational and financial plan, investment plan, or long-term strategic plan,
- movement of the Company's seat abroad,

if the enforcement of such a resolution resulted in an actual threat to the operation continuity or integrity of the critical infrastructure. The objection is expressed in the form of an administrative decision.

The Act of September 14, 2016 on change of Act on functioning of hard coal mining and some other acts changed also the Act of March 18, 2010 on special rights of the Minister of Energy and their performance in certain companies and groups operating in the electricity, oil and gaseous fuels sectors. The name of the Act was changed into the Act on special rights of the Minister of Energy and their performance in certain companies and groups operating in the electricity, oil and gaseous fuels sectors. Additionally previous rights of Minister of the State Treasury arising from this Act were attributed to the Minister of Energy.

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20.2 Hedging reserve

	Year ended December 31, 2016	Year ended December 31, 2015
AS AT JANUARY 1	**(21)**	**(61)**
Change of hedging reserve	**207**	**49**
Valuation of hedging instruments, ncluding:	**206**	**49**
Deferral of changes in fair value of hedging instruments recognized as an effective hedge	*313*	*51*
Accrued interest on derivatives transferred from hedging reserve and recognized in interest expense	*1*	*1*
Currency revaluation of CCIRS transaction transferred from hedging reserve and recognized in the result on foreign exchange differences	*(107)*	*1*
Ineffective portion of change in fair value of hedging derivatives recognized in profit or loss	*(1)*	*(4)*
Valuation of other financial instruments	**1**	**-**
Deferred tax	**(39)**	**(9)**
HEDGING RESERVE INCLUDING DEFERRED TAX	**147**	**(21)**

Hedging reserve includes mainly valuation of heging instruments to which cash flow hedge accounting is applied.

20.3 Foreign exchange differences from translation of foreign entities

Foreign exchange differences from translation of subsidiaries comprise the effect of translation into PLN of the financial statements of foreign companies belonging to the Group, i.e. PGE Trading GmbH and PGE Sweden AB (publ) as part of consolidation procedures.

20.4 Reserve capital

Reserve capital results from statutory allocation of profits generated in previous reporting periods, from surplus of profit distribution in excess of the value of statutory allocations, as well as from merger of PGE S.A. with its subsidiaries.

According to regulations of the Commercial Code, joint stock companies are obliged to create reserve capital to cover potential losses. At least 8% of the profit for the reporting year recognized in the parent company's separate financial statements is transferred to reserve capital, until this capital amounts to at least one third of the share capital. The part of reserve capital which amounts to one third of share capital can only be used to cover losses recognized in the separate financial statements and cannot be distributed for other purposes. The General Shareholders' Meeting decides on the use of the reserve capital.

Reserve capital subject to distribution to shareholders amounted to PLN 7,342 million as at December 31, 2016 and to PLN 6,776 million as at December 31, 2015.

20.5 Retained earnings and limitations to payment of a dividend

Non-distributable retained earnings concern amounts which cannot be paid in the form of dividends.

	As at December 31, 2016	As at December 31, 2015
Amounts included in retained earnings not subject to distribution by the parent company		
▪ Retained earnings of subsidiaries, attributable to equity holders of the parent company, including consolidation adjustments	8,040	6,872
▪ Profit/loss recognized by the parent company in retained earnings through other comprehensive income	(4)	(4)
Retained earnings of the parent company subject to distribution	1,598	1,768
TOTAL RETAINED EARNINGS PRESENTED IN THE STATEMENT OF FINANCIAL POSITION	**9,634**	**8,636**

For information regarding limitations to payment of dividends from reserve capital please refer to 20.4 of these financial statements. As at December 31, 2016 there were no other limitations to payment of dividends.

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20.6 Equity attributed to non-controlling interests

As at December 31, 2016 and December 31, 2015 non-controlling interests related mainly to non-controlling shareholders of PGE EJ 1 sp. z o.o.

The below table presents changes in non-controlling interests in the reporting periods.

	As at December 31, 2016	As at December 31, 2015
AS AT JANUARY 1	**96**	**116**
Share in net profit of subsidiaries	(2)	(5)
Dividends declared by subsidiaries	(4)	(4)
Change in ownership interests while retaining control	-	68
Increase of equity, shares acquisition	10	-
Acquisition of non-controlling interests by the Group	(4)	(78)
Other changes	-	(1)
AS AT 31 DECEMBER 31	**96**	**96**

Acquisition of non-controlling interests during the year ended December 31, 2016 and December 31, 2015 relates mainly to the acquisition of shares of PGE Górnictwo i Energetyka Konwencjonalna S.A. by PGE S.A.

Change in ownership interests while retaining control that took place in the year ended December 31, 2015 concerns sales of 30% of PGE EJ1 sp. z o.o. shares owned by PGE S.A.

20.7 Earnings per share

During current and comparative reporting periods there was no dilutive effect on earnings per share.

	Year ended December 31, 2016	Year ended December 31, 2015
NET PROFIT / (LOSS), ATTRIBUTED TO	**2,566**	**(3,037)**
shareholders of the parent company	2,568	(3,032)
non-controlling interests	(2)	(5)
NET PROFIT / (LOSS) ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY USED TO CALCULATE EARNINGS PER SHARE	**2,568**	**(3,032)**
Number of ordinary shares at the beginning of the reporting period	1,869,760,829	1,869,760,829
Number of ordinary shares at the end of the reporting period	1,869,760,829	1,869,760,829
WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES USED TO CALCULATE EARNINGS PER SHARE	**1,869,760,829**	**1,869,760,829**
EARNINGS/ DILUTED EARNINGS PER SHARE ATTRIBUTABE TO EQUITY HOLDERS OF THE PARENT COMPANY (IN PLN)	**1.37**	**(1.62)**

20.8 Dividends paid and dividends declared

	Dividend paid or declared from the profit for the year ended		
	December 31, 2016	December 31, 2015	December 31, 2014
CASH DIVIDENDS FROM ORDINARY SHARES			
Dividend paid from retained earnings	-	467	1,458
Cash dividends per share (in PLN)	**-**	**0.25**	**0.78**

Dividend from the profit for the year 2016

During the reporting period and until the date of preparation of these financial statements PGE S.A. made no advance payments of dividends.

Until the date of preparation of these financial statement suggested distribution of the Company's profit for 2016 has not been approved. The Company's dividend policy provides for payments of dividends amounting to 40-50% of the consolidated net profit adjusted by impairment of non-current assets.

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Dividend from the profit for the year 2015

On June 28, 2016 the General Shareholders' Meeting of PGE S.A. resolved to distribute PLN 467 million from the net profit of 2015 as a dividend (that comprises dividend of PLN 0.25 per share). The dividend was paid on October 14, 2016.

Dividend from the profit for the year 2014

On June 24, 2015, the General Shareholders' Meeting of PGE S.A. resolved to distribute PLN 1,458 million from the net profit of 2014 as a dividend (that comprises dividend of PLN 0.78 per share). The dividend was paid on October 15, 2015.

21. Provisions

The carrying amount of provisions is as follows:

	As at December 31, 2016		As at December 31, 2015	
	Non-current	Current	Non-current	Current
Employee benefits	2,148	543	2,496	517
Rehabilitation provision	2,666	4	3,348	2
Provision for deficit of CO_2 emission rights	-	1,154	-	760
Provision for energy origin units held for redemption	-	416	-	380
Provision for non-contractual use of the property	91	12	97	20
Other provisions	99	52	103	130
TOTAL PROVISIONS	**5,004**	**2,181**	**6,044**	**1,809**

Changes in provisions

	Employee benefits	Rehabilitation provision	Provision for deficit of CO_2 emission rights	Provision for energy origin units held for redemption	Provision for non-contractual use of the property	Other provisions	Total
JANUARY 1, 2016	**3,013**	**3,350**	**760**	**380**	**117**	**233**	**7,853**
Actuarial gains and losses excluding discount rate adjustment	(175)	-	-	-	-	-	(175)
Current service costs	74	-	-	-	-	-	74
Past service costs	(23)	-	-	-	-	-	(23)
Interest costs	82	99	-	-	-	-	181
Discount rate and other assumptions adjustment	(121)	(460)	-	-	-	-	(581)
Benefits paid / provisions used	(691)	(1)	(760)	(336)	-	(104)	(1,892)
Provisions reversed	(59)	(449)	-	(3)	(30)	(27)	(568)
Provisions raised in correspondence with costs	577	34	1,154	375	16	67	2,223
Provisions raised in correspondence with property, plant and equipment	-	92	-	-	-	-	92
Other changes	14	5	-	-	-	(18)	1
DECEMBER 31, 2016	**2,691**	**2,670**	**1,154**	**416**	**103**	**151**	**7,185**
Change recognized in operating costs	(536)	(37)	(1,154)	(372)	-	(3)	(2,102)
Change recognized in other operating income/ (expenses)	-	643	-	-	13	5	661
Change recognized in other financial income/ (expenses)	(82)	(99)	-	-	1	(24)	(204)
Change recognized in assets	-	172	-	-	-	-	172
Change recognized in other comprehensive income	249	-	-	-	-	-	249

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restated*	Employee benefits	Rehabilitation provision	Provision for deficit of CO_2 emission rights	Provisions for energy origin units held for redemption	Provision for non-contractual use of property	Other provisions	Total
JANUARY 1, 2015	**3,243**	**3,299**	**676**	**555**	**92**	**304**	**8,169**
Actuarial gains and losses excluding discount rate adjustment	50	-	-	-	-	-	50
Current service costs	82	-	-	-	-	-	82
Past service costs	(55)	-	-	-	-	-	(55)
Interest costs	70	86	-	-	-	-	156
Discount rate and other assumptions adjustment	(122)	(224)	-	-	-	-	(346)
Benefits paid / Provisions used	(725)	(1)	(680)	(1,159)	(1)	(74)	(2,640)
Provisions reversed	(116)	(4)	(1)	(2)	(19)	(82)	(224)
Provisions raised in correspondence with costs	560	56	765	986	45	85	2,497
Provisions raised in correspondence with property, plant and equipment	-	122					122
Changes in the PGE Group	(3)	-	-	-	-	-	(3)
Other changes	29	16	-	-	-	-	45
DECEMBER 31, 2015	**3,013**	**3,350**	**760**	**380**	**117**	**233**	**7,853**
Change recognized in operating costs	(442)	(27)	(764)	(984)	-	(41)	(2,258)
Change recognized in other operating income/ (expenses)	2	93	-	-	(26)	42	111
Change recognized in other financial income/ (expenses)	(70)	(86)	-	-	-	(4)	(160)
Change recognized in assets	-	(32)	-	-	-	-	(32)
Change recognized in other comprehensive income	15	-	-	-	-	-	15

* restatement of comparative figures refers to reclassifications between particular positions

21.1 Rehabilitation provision

Provision for rehabilitation of post-exploitation mining properties

After the completion of the lignite mining, the area of the surface mines belonging to the PGE Group will be rehabilitated. Some changes have been introduced in new technical plans for rehabilitation that concern extension of the period over which the rehabilitation will be carried out. According to the current plans, costs will be incurred in the years 2023 - 2069 (in case of PGE Górnictwo i Energetyka Konwencjonalna S.A. Branch Bełchatów Lignite Mine) and in the years 2045-2087 (in case of PGE Górnictwo i Energetyka Konwencjonalna S.A. Branch Turów Lignite Mine).

The PGE Group creates provision for rehabilitation of post-exploitation mining properties. The amount of the provision recognized in the financial statements includes also the value of Mine Liquidation Fund created in accordance with the Geological and Mining Law Act. The value of the provision as at December 31, 2016 amounted to PLN 2,366 million and as at December 31, 2015 to PLN 3,051 million.

Estimated influence of changes in discount rate on the value of rehabilitation provision:

	Carrying amount	Discount rate	
		-1 p.p.	+1 p.p.
Provision for rehabilitation of post-exploitation mining properties	2,366	943	(659)

Provision for rehabilitation of ash storages

The PGE Group power generating units raise provisions for rehabilitation of ash storages. As at December 31, 2016 and as at December 31, 2015 the provision amounted to PLN 98 million.

Provisions for rehabilitation of post-construction grounds of wind farms

The companies which own wind farms create provision for rehabilitation of post-construction grounds of wind farms. As at December 31, 2016 and as at December 31, 2015 the provision amounted to PLN 49 million.

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Liquidation of property, plant and equipment

The obligation to liquidate assets and rehabilitate the area results from „The integrated permission for running electric energy and heat energy producing installation" in which the restitution of the area was specified. As at the reporting date, the value of the provision amounts to PLN 157 million (PLN 152 million as at the end of the comparative period) and refers to some assets of the Conventional Generation and Renewables segments.

Discount ratio used for valuation of rehabilitation provisions as at December 31, 2016 amounted to 3.5% (3.0% in the comparative period).

21.2 Provision for deficit of CO_2 emission rights

As a general rule, the PGE Group entities recognize provision for the shortfall of CO_2 emission rights granted free of charge. In estimating the value of the provision the Group takes into accpunt EUA purchased. As described in note 15 of these financial statements the PGE Group is entitled to receive CO_2 emissions rights granted free of charge in connection to expenditures concerning investments included in National Investment Plan. The calculation of the provision includes also these rights.

21.3 Provision for energy origin rights held for redemption

Companies within the PGE Group create provision for energy origin rights related to sale realized during the reporting period or in prior reporting periods, in the amount of non-depreciated part until the reporting date. The total value of provision as at December 31, 2016 amounted to PLN 416 million (PLN 380 million in the comparative period) and was created mainly by PGE Obrót S.A.

21.4 Provision for non-contractual use of property

Entities of the PGE Group recognize provision for damages related to a non-contractual use of property. This issue mainly relates to distribution company, which owns distribution networks. As at the reporting date the provision amounted to approximately PLN 103 million (of which 43 million relate to litigations). In the comparative period the value of the provision amounted to PLN 117 million (of which PLN 46 million related to litigations).

21.5 Other provisions

Other provisions comprise mainly provisions raised for claims relating to real estate tax of PLN 90 million (PLN 88 million in the prior year).

22. Employee benefits

	As at December 31, 2016		As at December 31, 2015	
	Non-current	Current	Non-current	Current
Post-employment benefits	1,453	117	1,624	97
Jubilee awards	694	94	861	92
Other provisions for employee benefits	1	332	11	328
TOTAL PROVISIONS FOR EMPLOYEE BENEFITS	**2,148**	**543**	**2,496**	**517**

22.1 Post-employment benefits and jubilee awards

The amount of the actuarial provisions recognized in the financial statements results from the valuation prepared by an independent actuary.

The carrying amount of the provisions for the post-employment benefits and jubilee awards:

	As at December 31, 2016		As at December 31, 2015	
	Non-current	Current	Non-current	Current
Retirement, pension and post-mortem benefits	396	68	443	49
Coal allowance	138	9	151	9
Energy tariff	566	26	669	24
Social Fund	293	11	300	12
Medical care	60	3	61	3
TOTAL POST-EMPLOYMENT BENEFITS	**1,453**	**117**	**1,624**	**97**
Jubilee awards	694	94	861	92
TOTAL ACTUARIAL PROVISIONS	**2,147**	**211**	**2,485**	**189**

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22.2 Other provisions for employee benefits

	As at December 31, 2016		As at December 31, 2015	
	Non-current	Current	Non-current	Current
Provision for Voluntary Leave Program costs	-	34	11	59
Annual bonus and other employee bonuses	-	153	-	139
Unused annual holiday leave	-	131	-	127
Other provisions for employee benefits	1	14	-	3
TOTAL OTHER PROVISIONS FOR EMPLOYEE BENEFITS	**1**	**332**	**11**	**328**

Change in provisions for employee benefits

	Retirement, pension and post-mortem benefits	Coal allowance	Energy tariff	Social Fund	Medical care	Jubilee awards	Other employee benefits	Total
AS AT JANUARY 1, 2016	**492**	**160**	**693**	**312**	**64**	**953**	**339**	**3,013**
Actuarial gains and losses excluding discount rate adjustment	(33)	(9)	(105)	(7)	(1)	(21)	-	**(176)**
Discount rate adjustment	(20)	(8)	(43)	(20)	(3)	(27)	-	**(121)**
Current service costs	17	1	9	4	1	42	-	**74**
Past service costs	6	4	41	17	2	(93)	-	**(23)**
Interest costs	15	7	21	9	2	28	-	**82**
Benefits paid / provisions used	(14)	(8)	(24)	(11)	(2)	(95)	(537)	**(691)**
Provisions reversed	-	-	-	-	-	-	(59)	**(59)**
Provisions raised	-	-	-	-	-	-	577	**577**
Other changes	1	-	-	-	-	1	13	**15**
AS AT DECEMBER 31, 2016	**464**	**147**	**592**	**304**	**63**	**788**	**333**	**2,691**
Change recognized in operating costs	(24)	(5)	(50)	(21)	(3)	98	(531)	(536)
Change recognized in other financial income/ (expenses)	(15)	(7)	(21)	(9)	(2)	(28)	-	(82)
Change recognized in other comprehensive income	53	17	148	27	4	-	-	249

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	Retirement, pension and post-mortem benefits	Coal allowance	Energy tariff	Social Fund	Medical care	Jubilee awards	Other employee benefits	Total
AS AT JANUARY 1, 2015	**525**	**152**	**695**	**301**	**58**	**1,042**	**470**	**3,243**
Actuarial gains and losses excluding discount rate adjustment	(11)	22	44	11	11	(27)	-	**50**
Discount rate adjustment	(20)	(7)	(44)	(18)	(3)	(30)	-	**(122)**
Current service costs	18	1	9	4	1	49	-	**82**
Past service costs	(19)	(4)	(5)	(6)	(2)	(19)	-	**(55)**
Interest costs	13	4	18	8	1	26	-	**70**
Benefits paid / provisions used	(16)	(8)	(23)	(10)	(2)	(93)	(573)	**(725)**
Provisions reversed	-	-	-	-	-	-	(116)	**(116)**
Provisions raised	-	-	-	-	-	-	560	**560**
Changes in the PGE Group	-	-	(1)	-	-	(1)	(1)	**(3)**
Other changes	2	-	-	22	-	6	(1)	**29**
AS AT DECEMBER 31, 2015	**492**	**160**	**693**	**312**	**64**	**953**	**339**	**3,013**
Change recognized in operating costs	(1)	3	(3)	(20)	1	22	(444)	(442)
Change recognized in other operating income/ (expenses)	-	-	-	-	-	-	2	2
Change recognized in other financial income/ (expenses)	(13)	(4)	(18)	(8)	(1)	(26)	-	(70)
Change recognized in other comprehensive income	31	(15)	-	7	(8)	-	-	15

Sensitivity analysis of the value of actuarial provisions as at December 31, 2016 for changes in key assumptions:

	Carrying amount	Discount rate		Expected average growth rate of the basis of calculation	
		-1 p.p.	+ 1 p.p.	-1 p.p.	+ 1 p.p.
Retirement, pension and post-mortem benefits	464	25	(50)	(50)	30
Coal allowance	147	16	(13)	(7)	17
Energy tariff	592	75	(87)	(61)	88
Social Fund	304	36	(41)	(43)	36
Medical care	63	7	(6)	(7)	8
Jubilee awards	788	21	(78)	(79)	30
TOTAL	**2,358**	**180**	**(275)**	**(247)**	**209**

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23. Deferred income and governments grants

23.1 Non-current deferred income and government grants

	As at December 31, 2016	As at December 31, 2015
GOVERNMENT GRANTS		
Grants received from NFOŚiGW (environmental funds)	260	267
Redemption of loans from environmental funds	41	46
Other government grants	153	141
DEFERRED INCOME		
Subsidies received and connection fees	523	567
Donations and property, plant and equipment granted free of charge	86	95
Lease income	25	26
Other deferred income	53	50
NON-CURRENT GOVERNMENT GRANTS AND DEFERRED INCOME, TOTAL	**1,141**	**1,192**

Subsidies received and connection fees presented in deferred income (current also) comprise mainly connection fees for connection to power received until July 1, 2009, so before the interpretation of IFRIC 18 Transfers of Assets from Customers became effective.

23.2 Current deferred income and government grants

	As at December 31, 2016	As at December 31, 2015
GOVERNMENT GRANTS		
Grants received from NFOŚiGW (environmental funds)	12	12
Redemption of loans from environmental funds	2	2
Other government grants	8	9
DEFERRED INCOME		
Subsidies received and connection fees	79	68
Donations and property, plant and equipment granted free of charge	8	8
Lease income	3	3
Other deferred income	7	10
CURRENT GOVERNMENT GRANTS AND DEFERRED INCOME, TOTAL	**119**	**112**

24. Other non-financial liabilities

The main components of other non-financial liabilities as at the respective reporting dates are as follows:

	As at December 31, 2016	As at December 31, 2015
Environmental fees	243	273
VAT liabilities	122	110
Excise tax liabilities	129	128
Payroll liabilities	239	247
Liabilities from social insurances	237	234
Personal income tax	80	81
Liabilities due to Voluntary Leave Programs	51	106
Advances for deliveries	143	142
Income tax related to the increase in the share capital	110	-
Other	70	67
OTHER LIABILITIES, TOTAL	**1,424**	**1,388**

Income tax related to the increase in the share capital was described in note 20.1 of these financial statements. The tax was paid on January 9, 2017.

Environmental fees relate mainly to charges for the use of water and gas emission in conventional power plants as well as exploitation charges paid by the coal mines.

The "Other" position comprises mainly payments to the Employment Pension Program, the Social Fund and the State Fund for Rehabilitation of Persons with Disabilities.

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EXPLANATORY NOTES TO FINANCIAL INSTRUMENTS

25. Financial instruments

25.1 Description of significant items within particular classes of financial instruments

25.1.1 Financial receivables

	As at December 31, 2016		As at December 31, 2015	
	Non-current	Current	Non-current	Current
Trade receivables	-	2,705	-	2,548
Deposits	136	2,300	124	1
LTC compensations	-	1,241	-	1,075
Debt securities including bonds	89	-	-	-
Bails and security deposits	2	12	1	37
Collateral – balancing market	-	-	-	18
Other financial receivables	10	67	17	69
FINANCIAL RECEIVABLES	**237**	**6,325**	**142**	**3,748**

Trade receivables

The main component of trade receivables are receivables recognized by the company PGE Obrót S.A. Receivables from households account for about 20% of the consolidated balance of trade receivables, while receivables from corporate clients of PGE Obrót S.A. represent about 58% of the consolidated balance of trade receivables. On December 31, 2016 the share of the three most significant customers of the PGE Group amounted to approximately 10% of the total consolidated balance. Additional information relating to trade receivables is presented in note 26.5.1 of these financial statements.

Trade receivables comprise also electricity sales accrual.

LTC compensations

LTC compensations are described in detail in note 33.1 of these financial statements.

Other financial receivables

The value of other financial receivables consist mainly of disputed receivables described in note 28.4 of these financial statements.

25.1.2 Derivatives

All derivatives are recognized in the Company's financial statements at fair value.

	As at December 31, 2016			
	Recognized in profit or loss	Recognized in other comprehensive income	Assets	Liabilities
DERIVATIVES AT FAIR VALUE THROUGH PROFIT OR LOSS				
Currency forward	(5)	-	1	-
Commodity forward	(5)	-	8	-
IRS transactions	2	-	-	30
HEDGING DERIVATIVES				
CCIRS hedging transactions	48	80	231	-
IRS hedging transactions	(1)	126	125	-
TOTAL DERIVATIVES	**39**	**206**	**365**	**30**
current			9	-
non-current			356	30

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	As at December 31, 2015			
	Recognized in profit or loss	Recognized in other comprehensive income	Assets	Liabilities
DERIVATIVES AT FAIR VALUE THROUGH PROFIT OR LOSS				
Currency forward	(4)	-	7	1
Commodity forward	4	-	-	33
IRS transactions	8	-	-	55
HEDGING DERIVATIVES				
CCIRS hedging transactions	(63)	52	43	-
TOTAL DERIVATIVES	**(55)**	**52**	**50**	**89**
current			7	34
non-current			43	55

Commodity and currency forwards

Commodity and currency forwards relate mainly to CO_2 emission rights trade.

IRS transactions

In the current reporting period PGE S.A. concluded 6 IRS transactions, hedging the interest rate on loans taken with a total nominal value of PLN 4,630 million. The Company applies hedge accounting to the above IRS transactions. The impact of hedge accounting was described in note 20.2 of these financial statements.

In 2014 PGE S.A. concluded 2 IRS transactions, hedging the interest rate on bonds issued with a nominal value of PLN 1 billion. Payments arising from IRS transactions are correlated with interest payments on bonds. Changes in fair value of IRS transaction are fully recognized in profit or loss.

In 2003, Elektrownia Turów S.A. (currently a branch of PGE Górnictwo i Energetyka Konwencjonalna S.A.) concluded IRS hedge transactions. These transactions are aimed to hedge variable interest rates (USD LIBOR 6m) on investment credits of USD 30, 40 and 80 million taken from Nordic Investment Bank to finance investments in Turów power plant. Changes in fair value of IRS transaction are fully recognized in profit or loss.

CCIRS hedging transaction

In connection with loans received from PGE Sweden AB (publ), PGE S.A. concluded CCIRS transactions, hedging both the exchange rate and interest rate. In these transactions, banks-contractors pay PGE S.A. interest based on a fixed rate in EUR and PGE S.A. pays interest based on a fixed rate in PLN. In the consolidated financial statements the relevant part of CCIRS transactions is recognized as a hedge of bonds issued by PGE Sweden AB (publ).

The Group applies hedge accounting to the above CCIRS transactions. The impact of hedge accounting is presented in note 20.2 of these financial statements.

25.1.3 Available-for-sale financial assets

The most significant positions of available-for-sale financial assets are shares in entities not quoted on active markets. The PGE Group is not able to estimate reliably the fair value of shares not-quoted on an active markets, therefore they are measured at cost less impairment losses.

25.1.4 Loans, borrowings, bonds and lease

	As at December 31, 2016		As at December 31, 2015	
	Non-current	Current	Non-current	Current
Loans and borrowings	5,839	332	1,459	214
Bonds issued	3,764	78	3,658	76
Lease	-	1	1	1
TOTAL LOANS, BORROWINGS, BONDS AND LEASE	**9,603**	**411**	**5,118**	**291**

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Currency position and interest

As at December 31, 2016

Currency	Reference rate	Value in currency	Value in PLN	Final maturity date
PLN	Variable	6,381	6,381	September 2017 - December 2028; bonds - indefinite program, maturity date of the tranche issued – June 2018
	Fixed	121	121	December 2017 - December 2028
TOTAL PLN		**6,502**	**6,502**	
EUR	Variable	129	569	June 2024
	Fixed	642	2.842	June 2019 – August 2029
TOTAL EUR		**771**	**3,411**	
USD	Variable	24	101	May 2019
TOTAL USD		**24**	**101**	
TOTAL LOANS, BORROWINGS AND BONDS			**10,014**	

As at December 31, 2015

Currency	Reference rate	Value in currency	Value in PLN	Final maturity date
PLN	Variable	1,759	1,759	January 2016 - December 2027; bonds - indefinite program, maturity date of the tranche issued - June 2018
	Fixed	156	156	October 2016 - September 2020
TOTAL PLN		**1,915**	**1,915**	
EUR	Variable	140	597	June 2024
	Fixed	642	2,734	June 2019 – August 2029
TOTAL EUR		**782**	**3,331**	
USD	Variable	35	137	August 2016 – May 2019
TOTAL USD		**35**	**137**	
CHF	Variable	6	26	December 2016
TOTAL CHF		**6**	**26**	
TOTAL LOANS, BORROWINGS AND BONDS			**5,409**	

Loans, borrowings and bonds maturity

	As at December 31, 2016	As at December 31, 2015
Within 1 year	412	291
From 1 to 2 years	1,374	288
From 2 to 3 years	2,502	1,225
From 3 to 4 years	373	2,262
From 4 to 5 years	1,042	202
Above 5 years	4,311	1,141
TOTAL LOANS, BORROWINGS AND BONDS ISSUED AS AT DECEMBER 31	**10,014**	**5,409**

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The following table presents changes in interest bearing debt in the years ended December 31, 2016 and 2015:

	Year ended December 31, 2016	Year ended December 31, 2015
AS AT JANUARY 1	**5,409**	**5,045**
CHANGE IN OVERDRAFTS	**(7)**	**(135)**
CHANGE IN LOANS, BORROWINGS, BONDS AND LEASE (excluding overdrafts)	**4,612**	**499**
Drawn loans, borrowings, leases / issued bonds	4,652	648
Repayment of loans, borrowings, leases / redemption of bonds	(196)	(176)
Accrued interest	134	99
Paid interest	(113)	(95)
Foreign exchange differences	135	23
AS AT DECEMBER 31	**10,014**	**5,409**

Loans and borrowings

Among loans and borrowings presented above as at December 31, 2016, the PGE Group presents mainly the following facilities:

- investment credit facility taken out by PGE Górnictwo i Energetyka Konwencjonalna S.A. from Nordycki Bank Inwestycyjny (Nordic Investment Bank) to finance construction of 858 MW power blovk in Bełchatów Power Plant of PLN 569 million;
- investment credit facilities taken out by PGE Górnictwo i Energetyka Konwencjonalna S.A. from Nordycki Bank Inwestycyjny (Nordic Investment Bank) and UBS Investment Bank AG to finance the modernization of power blocks no. 1-6 in Turów Power Plant in the total amount of PLN 101 million;
- investment credit facility taken out by PGE S.A. from Bank Gospodarstwa Krajowego S.A. of PLN 1 billion with a maturity date of December 31, 2027. As at December 31, 2016, the Group used all available credit.
- long-term loan agreement with a syndicate of banks composed of: BNP Paribas S.A., Société Générale S.A., Bank Handlowy w Warszawie S.A., ING Bank Śląski S.A., Bank Zachodni WBK S.A., mBank S.A., Powszechna Kasa Oszczędności Bank Polski S.A., Bank Polska Kasa Opieki S.A. concluded on September 7, 2015. Subject matter of the agreement is granting a loan in two parts, i.e. term loan facility and revolving loan facility. As at December 31, 2016 PGE S.A. used the whole term loan facility of PLN 3,630 million which falls on September 30, 2023.
  The revolving loan facility of up to PLN 1,870 million and falling on April 30, 2019 is available, but not used by PGE S.A.
- loan agreement signed by PGE S.A. on December 4, 2015 of PLN 500 million with Bank Gospodarstwa Krajowego S.A. with the maturity date of December 31, 2028. As at December 31, 2016, PGE S.A. used the whole available credit.

Additionally, on October 27, 2015, PGE S.A. concluded two loan agreements with the European Investment Bank for the total amount of nearly PLN 2 billion. The amount of PLN 1.5 billion, obtained on the basis of the first of the two agreements, will be used for projects relating to the modernization and development of distribution grid. The funds from the second agreement, i.e. the remaining PLN 490 million, will be used to finance and refinance the construction of cogeneration units Gorzów Heat and Power Plant and Rzeszów Heat and Power Plant. The European Investment Bank loans will be available for disbursement over a period of up to 22 months from the date of signing of the agreements. The funds shall be repaid within 15 years from the date of the last tranche. As at December 31, 2016 the aforesaid loans were not used.

Additionally, the value of overdraft facilities at the disposal of the significant PGE Group's companies amounted to PLN 2,001 million as at December 31, 2016. The repayment date of used overdraft facilities of the main PGE Group's companies is February-April 2018.

Bonds issued

The Group has the ability to finance its own operations through two bond issue programs:

- The bond issue program for the amount of PLN 5 billion directed towards investors from the Polish capital market. On June 27, 2013, the first non-public issuance of 5-year bonds under this program took place, the coupon bearer bonds with a variable interest rate. The nominal value of the issue was PLN 1 billion and the maturity of the bonds is June 27, 2018. On August 29, 2013, the bonds were floated in the Alternative Trading System organized by BondSpot S.A. and Giełda Papierów Wartościowych w Warszawie S.A. (Warsaw Stock Exchange).
- The medium term Eurobonds Issue Program of EUR 2 billion established on May 22, 2014 by PGE S.A. together with PGE Sweden AB (publ), a 100% subsidiary of PGE S.A. Under the Program, PGE Sweden AB (publ) may issue eurobonds up to the amount of 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 and a five year maturity and on August, 1 2014 it has issued bonds in the amount of EUR 138 million and fifteen year maturity.

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25.1.5 Trade and other financial liabilities

	As at December 31, 2016		As at December 31, 2015	
	Non-current	Current	Non-current	Current
Trade liabilities	-	976	-	1,119
Purchase of property, plant and equipment and intangible assets	12	1,225	25	1,608
Bails and security deposits received	21	65	9	81
Liabilities related to LTC	-	1,253	-	1,131
Insurances	-	-	-	-
Other	-	37	-	6
TRADE AND OTHER FINANCIAL LIABILITIES	**33**	**3,556**	**34**	**3,945**

25.2 Fair value of financial instruments

The value of financial assets and liabilities measured at amortized cost is a rational approximation of their fair value, except for bonds issued by PGE Sweden AB (publ).

Bonds issued by PGE Sweden AB (publ) are based on a fixed interest rate. Their amortized cost presented in these financial statements as at December 31, 2016 amounted to EUR 642 million and their estimated fair value amounted to EUR 679 million. The indicators used in the valuation belong to Level 2 of fair value hierarchy.

Instruments not quoted on active markets, for which the fair value cannot be estimated reliably

Basic assets of the Group classified as available-for-sale financial assets are shares in entities not quoted on active markets. For shares in entities that are not quoted on the stock exchange, there is no active market nor possibility to use measurement techniques that will give reliable values. Due to the above, the Group is not able to establish reasonable fair value estimates. Such assets are measured at cost less impairment losses.

25.3 Fair value hierarchy

Inventories

The Group possesses CO_2 emission rights, some of which are acquired in order to realize profits from fluctuations in market prices. This part of the emission rights is recognized in inventories at fair value less costs of disposal, cost of usage of inventories is measured by detailed identification. Fair value is determined based on the market quotations (Level 1).

Derivatives

The Group measures derivatives at fair value using valuation models for financial instruments based on publicly available exchange rates, interest rates, discount curves in particular currencies (applicable also for commodities which prices are denominated in these currencies) derived from active markets. The fair value of derivatives is determined based on discounted future cash flows from transactions, calculated based on the difference between the forward rate and transaction price. Forward exchange rates are not modelled as separate risk factor, but are derived from the spot rate and appropriate forward interest rate for foreign currencies in relation to PLN.

In the category of financial assets at fair value through profit or loss, the Group presents derivatives related to greenhouse gases emission rights – currency and commodity forwards and IRS hedging transactions changing variable interest rate in PLN to fixed interest rate in PLN (Level 2).

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In addition, the Group presents CCIRS derivative that hedges foreign exchange rate and interest rate (Level 2).

	As at December 31, 2016		As at December 31, 2015	
FAIR VALUE HIERARCHY	**Level 1**	**Level 2**	**Level 1**	**Level 2**
CO_2 emission rights	29	-	98	-
Inventories	**29**	**-**	**98**	**-**
Currency forward	-	1	-	7
Commodity forward	-	8	-	-
CCIRS valuation	-	231	-	43
IRS valuation	-	125	-	-
Financial assets	**-**	**365**	**-**	**50**
Currency forward	-	-	-	1
Commodity forward	-	-	-	33
IRS valuation	-	30	-	55
Financial liabilities	**-**	**30**	**-**	**89**

Inventories are described in note 14 of these financial statements, whereas derivatives are presented in note 25.1.2 of these financial statements. During the current and comparative reporting periods, there have been no transfers of financial instruments between the first and the second level of fair value hierarchy.

The table below presents terms of particular derivatives.

	As at December 31, 2016		As at December 31, 2015		
	Carrying amount in PLN	**Nominal value in currency**	**Carrying amount in PLN**	**Nominal value in currency**	**Maturity**
Currency forward - EUR	1	17	7	66	to January 2018
Commidity forward sale EUA - EUR	8	9	-	-	to December 2017
Commodity forward purchase EUA - EUR		-	-	-	To December 2017
CCIRS – EUR to PLN	231	514	43	514	to June 2019
		144		144	to July 2029
IRS - rate % PLN	125	3,630	-	-	to September 2023
		1,000	-	-	to December 2027
Financial assets	**365**		**50**		
Currency forward - EUR		1	(1)	6	to January 2018
Commodity forward sale - EUA - EUR	-	-	(33)	25	to December 2017
Commodity forward purchase - EUA - EUR		-		10	to December 2017
IRS - rate % PLN	(23)	1,000	(43)	1,000	to June 2018
IRS - rate % USD	(7)	-	(12)	3	to August 2016
		24		32	to May 2019
Financial liabilities	**(30)**		**(89)**		

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25.4 Statement of comprehensive income

The table below presents the combined effect of the various categories of the financial instruments on the financial income and expenses.

Year ended December 31, 2016	Cash	Financial instruments measured at fair value	Hedging derivatives	Available-for-sale financial assets	Loans and receivables	Financial liabilities at amortized cost	TOTAL
Dividends	-	-	-	2	-	-	**2**
Interest income/(expenses)	22	(23)	(61)	-	28	(42)	**(76)**
Exchange gains/ (losses)	11	-	107	-	3	(140)	**(19)**
Reversal of impairment allowances/ Revaluation of financial instruments	-	25	1	-	91	-	**117**
Creation of impairment allowances/ Revaluation of financial instruments	-	(10)	-	-	(2)	-	**(12)**
TOTAL PROFIT / (LOSS)	**33**	**(8)**	**47**	**2**	**120**	**(182)**	**12**

Year ended December 31, 2015	Cash	Financial instruments measured at fair value	Hedging derivatives	Available-for-sale financial assets	Loans and receivables	Financial liabilities at amortized cost	TOTAL
Dividends	-	-	-	1	-	-	**1**
Interest income/(expenses)	74	(24)	(62)	-	26	(34)	**(20)**
Exchange gains/ (losses)	-	-	(1)	-	(2)	(27)	**(30)**
Reversal of impairment allowances	-	32	-	-	1	-	**33**
Creation of impairment allowances	-	-	-	-	(5)	-	**(5)**
Gain on disposal of investments	-			15	-	-	**15**
TOTAL PROFIT / (LOSS)	**74**	**8**	**(63)**	**16**	**20**	**(61)**	**(6)**

25.5 Collaterals for repayment of receivables and liabilities

The Group uses many financial instruments and combinations thereof as collaterals for repayment of loans. The most frequently used are agreements for transfer of receivables, bills and execution statements. Additionally, the Group uses powers of attorney to bank accounts and assignments of receivables.

As at the reporting date, the following assets were used as collateral for repayment of liabilities or contingent liabilities:

	As at December 31, 2016	As at December 31, 2015
Property, plant and equipment	915	845
Inventories	51	65
Trade receivables	34	28
TOTAL ASSETS BEING THE COLLATERAL FOR REPAYMENT OF LIABILITIES	**1,000**	**938**

Property, plant and equipment presented in the table above are collaterals for repayment of drawn investment credits. As at December 31, 2016 and as at December 31, 2015 the most significant item is a collateral mortgage on the power unit 858 MW constructed in PGE Górnictwo i Energetyka Konwencjonalna S.A. Branch Bełchatów Power Plant.

The collaterals on inventories comprise mainly pledges related to loans received from environmental funds.

The companies from the PGE Group are obliged to maintain a specified cash balance on its accounts held with PKO BP and Nordea Bank AB according to the rules of Izba Rozliczeniowa Giełd Towarowych S.A. (Warsaw Commodity Clearing House) and to participate in a guarantee fund. Cash from the two titles mentioned above is accounted for as restricted cash. As at December 31, 2016 it amounted to PLN 72 mln (PLN 285 mln in the comparative period).

26. Objectives and principles of financial risk management

The PGE Group is exposed to different kinds of financial risks. Types and significance of those risks depend on the range of activities on the commodity and financial markets. In particular these are:

- liquidity risk
- market risk, including: interest rate risk, currency risk, price risk;
- credit risk.

The supreme goal of financial risk management in the PGE Group is to support the process of creating value for shareholders and to implement business strategies of the Group through maintaining the financial risk at the level acceptable for the Group management. This goal is attained through reducing the effect of risk factors changes on the range of cash flows and financial result fluctuations arising out of the PGE Group's exposure to financial risk. The financial risk management activities are integrated from the perspective of the PGE Group as a whole. This means that the process of risk management takes into account the sources of exposure to the risk generated by individual areas of business, co-relationships between them and their aggregate influence on the risk profile and the financial situation of the PGE Group.

Financial risk management model includes:

- collection and consolidation of data on exposure to particular categories of financial risk,
- calculation and analysis of the aggregate measures of financial risk and global risk measurement,
- management of the PGE Group's consolidated exposure in relation to capital at risk and risk limits established on its basis (including the identification and implementation of hedging strategies).

Management Board of PGE S.A. bears the responsibility for the infrastructure of financial risk management. The Management Board of PGE S.A. determines the risk appetite which is an acceptable level of worsening of the financial result of the PGE Group, taking into account its current and projected economic and financial situation. The Management Board decides also on the allocation of the risk appetite to particular areas of business activity. In the PGE Group, there is the Risk Committee that supervises the process of risk management as well as the scope and level of the Group's exposure to significant risks (including financial risks) in the relation to applicable limits and risk appetite. The Risk Committee makes key decisions in the area of risk management concerning, among others, setting risk limits as part of the risk appetite, as well as the approval of applied methods and instruments in the area of commercial and hedging operations.

The organization of a function of financial risk management is based on the principle of independence of an entity responsible for measurement and control of risk vs business entities (risk owners) responsible for taking and managing the risk on an ongoing basis. The independence of the risk control function from business entities assuming the risk is guaranteed by way of locating the risk unit in a separate division of the PGE Group's Corporate Center and independent reporting lines to the Risk Committee and the Management Board of PGE S.A.

In the key areas for financial risks, the PGE Group has implemented internal rules for managing these risks.

The rules for financial risk management support a business decision making process and attainment of assumed strategic goals with the concurrent risk optimization.

The risk owners execute transactions exclusively in the scope of agreed area of operations and approved products, markets and types of instruments/transactions. Each decision regarding the extension of operations into a new area is preceded with an independent assessment of, among others, a risk unit, in respect of the generated risk profile, impact on risk exposure of the PGE Group and requirements to be met to ensure risk control and must be approved by the Risk Committee.

Interest rate and foreign currency risks management in the PGE Group assumes that the transfer of market risk generated by the companies from the PGE Group is transferred to the parent entity, i.e. PGE S.A., by way of intergroup transactions. Financial risk management process involves natural hedge mechanisms and hedging instruments, including derivatives which are concluded in the scope determined by the PGE Group's internal regulations.

26.1 Liquidity risk

The main task in the process of management of liquidity risk in the PGE Group is to plan and to report on a regular basis the liquidity of PGE S.A. and its subsidiaries. The PGE Group monitors the risk of losing the liquidity using forecasts of cash flows from operating, investing and financing activities. The purpose of the PGE Group is to maintain balance between continuity and flexibility of financing through the use of various sources of financing, such as: overdraft facilities, term and investment loans, national bonds and Eurobonds. Moreover, the parent entity conducts the on-going monitoring of meeting covenants stipulated in the agreements for financing and their forecasts in subsequent periods.

The above activities allow to determine the PGE Group's debt raising capacity and ensure the capacity to repay debt on a long-term basis. They also affect the determination of its investment abilities.

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In the PGE Group a central financing model applies, which provides that principally the external financing is executed by PGE S.A. The subsidiaries in the PGE Group use various sources of intra-group financing, such as: loans, bonds or agreements for consolidation of bank accounts and cash management agreements in the group of accounts (real cash pooling).

The below table presents maturity of the Group's financial liabilities in accordance with the maturity date, based on contractual non-discounted payments.

AS AT DECEMBER 31, 2016	Carrying amount	Total payments	Less than 3 months	Between 3 and 12 months	Between 1 and 5 years	More than 5 years
Loans and borrowings	6,171	6,887	69	278	2,084	4,456
Bonds issued	3,842	4,206	-	79	3,370	757
Trade and other financial liabilities	3,589	3,589	2,263	1,293	33	-
Liabilities from finance lease and lease agreements with a purchase option	1	1	-	1	-	-
Derivatives measured at fair value through profit or loss	30	30	-	20	10	-
TOTAL	13,633	14,713	2,332	1,671	5,497	5,213

AS AT DECEMBER 31, 2015	Carrying amount	Total payments	Less than 3 months	Between 3 and 12 months	Between 1 and 5 years	More than 5 years
Loans and borrowings	1,673	1,847	36	194	877	740
Bonds issued	3,734	4,166	-	77	3,342	747
Trade and other financial liabilities	3,979	3,979	2,780	1,165	34	-
Liabilities from finance lease and lease agreements with a purchase option	2	2	-	1	1	-
Derivatives measured at fair value through profit or loss	89	92	1	57	34	-
TOTAL	9,477	10,086	2,817	1,494	4,288	1,487

26.2 Interest rate risk

The companies belonging to the PGE Group are exposed to interest rate risk as a result of financing their operating and investment activities with interest bearing indebtedness at variable interest rates or through investments in financial assets at variable or fixed interest rates. On the other hand, financing business activity with indebtedness at a fixed interest rate is related to the opportunity cost risk in case of interest rates' decline.

The PGE Group is exposed to interest rate risk related to investment in debt instruments, liabilities from loans granted, and changes in fair value of derivatives swaps resulting from changes in interest rates.

Bonds issued in amount PLN 1 billion under the Bond Issue Program in amound of PLN 5 billion are interest bearing bonds at a variable rate in PLN. Payments relating to those bonds are hedged by IRS transactions. Bonds issued under the medium term Eurobonds Issue Program, are interest bearing bonds at a fixed rate in EUR. Payments relating to these bonds are hedged by CCIRS transactions. Bonds issuance programs are described in note 25.1.4 and hedging instruments are described in note 25.1.2 of these financial statements.

Incured financing in the form of long-term bank credit of PLN 1 billion under the terms of Credit Agreement signed on December 17, 2014 with Bank Gospodarstwa Krajowego and syndicated loan (term loan facility tranche) of PLN 3.63 billion under the terms of Credit Agreement signed on September 7, 2015, constitute financial instruments at a variable interest rate in PLN. Payments related to bank credits are hedged with IRS hedge instruments, described in note 25.1.2.

The PGE Group entities enter into interest-rate based derivative transactions exclusively in the purpose to hedge identified exposure to risk. Thus, the PGE Group entities are not permitted, as regards interest-rate based derivative transactions, to enter into speculative transactions, i.e. those that increase the interest rate risk exposure in comparison with the level resulting from the identified sources of exposure and that aim to obtain additional gains from risk factor changes.

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The PGE Group's exposure to interest rate risk and risk concentration, by currencies:

		Type of interest rate	As at December 31, 2016	As at December 31, 2015
Derivatives – assets, exposed to interest rate risk	PLN	Fixed	-	-
		Variable	125	-
	Other currencies	Fixed	-	-
		Variable	240	50
Deposits, cash and debt securities	PLN	Fixed	5,046	2,948
		Variable	-	-
	Other currencies	Fixed	59	281
		Variable	89	-
Derivatives – liabilities, exposed to interest rate risk	PLN	Fixed	-	-
		Variable	(23)	(43)
	Other currencies	Fixed	-	-
		Variable	(7)	(46)
Loans, borrowings, bonds and lease	PLN	Fixed	(121)	(156)
		Variable	(6,381)	(1,759)
	Other currencies	Fixed	(2,842)	(2,734)
		Variable	(670)	(760)
Net exposure	**PLN**	**Fixed**	**4,925**	**2,792**
		Variable	**(6,279)**	**(1,802)**
	Other currencies	**Fixed**	**(2,783)**	**(2,453)**
		Variable	**(348)**	**(756)**

Interest rates on variable interest rate financial instruments are updated in periods shorter than one year. Interest rates on fixed interest rate financial instruments are fixed throughout the whole period until maturity of these instruments.

26.3 Currency risk

The PGE Group entities are exposed to currency transaction risk and currency translation risk. The main sources of exposure to currency risk are presented below:

- capital expenditures denominated in or indexed to foreign currencies;
- indebtedness denominated in foreign currencies;
- sales of electricity denominated in foreign currencies (export);
- fees denominated in or indexed to foreign currency relevant to purchase of transmission capacities;
- sales and purchases of CO_2 emission rights and gas as well as purchases of hard coal denominated in or indexed to foreign currencies;
- expenses related to current use of production goods denominated in or indexed to foreign currencies;
- financial assets with deposit characteristics denominated in foreign currencies.

The PGE Group entities enter into currency based derivative transactions exclusively in the purpose to hedge identified exposure to risk. Thus, the PGE Group entities are not permitted, as regards currency based derivative transactions, to enter into speculative transactions, i.e. those that increase the currency risk exposure in comparison with their level resulting from identified sources of exposure and that aim to obtain additional gains from risk factor changes.

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The table below presents the Group's exposure to currency risk with regards to particular classes of financial instruments:

	Total carrying amount in PLN	CURRENCY POSITION AS AT DECEMBER 31, 2016			
		EUR		USD	
		Currency	PLN	Currency	PLN
FINANCIAL ASSETS					
Trade and other financial receivables, including:	6,562	39	173	-	-
Bonds acquired, bills	*89*	*20*	*89*	-	-
Trade receivables	*2,705*	*19*	*84*	-	-
Cash and cash equivalents	2,669	13	59	-	-
Derivatives, including:	365	743	3,288	-	-
Measured at fair value through profit or loss	*9*	*15*	*66*	-	-
CCIRS hedging instruments	*231*	*728*	*3,222*	-	-
FINANCIAL LIABILITIES					
Loans, borrowings, bonds, including:	(10,014)	(771)	(3,411)	(24)	(101)
Interest bearing loans and borrowings	*(6,171)*	*(129)*	*(569)*	*(24)*	*(101)*
Bonds issued and other debt securities	*(3,842)*	*(642)*	*(2,842)*	-	-
Trade and other financial liabilities measured at amortized cost, including:	(3,589)	(16)	(65)	-	-
Trade liabilities	*(976)*	*(8)*	*(33)*	-	-
Liabilities due to purchase of property, plant and equipment	*(1,237)*	*>(1)*	*(2)*	-	-
Other financial liabilities	*(123)*	*(7)*	*(30)*		
Derivatives, including:	(30)	-	-	(2)	(7)
Measured at fair value through profit or loss	*(30)*	-	-	*(2)*	*(7)*
NET CURRENCY POSITION		**8**	**44**	**(26)**	**(108)**

The carrying amount of derivative instruments is their fair value. The value of currency risk exposure for forward derivatives is their nominal value at currency. The value of currency risk exposure for CCIRS derivatives is the currency value of discounted cash flows of currency leg.

	Total carrying amount in PLN	CURRENCY POSITION AS AT DECEMBER 31, 2015					
		EUR		USD		CHF	
restated		Currency	PLN	Currency	PLN	Currency	PLN
FINANCIAL ASSETS							
Trade receivables	2,548	36	151	-	-	-	-
Cash and cash equivalents	3,104	67	280	-	-	-	-
Derivatives, including:	50	694	2,958	-	-	-	-
Measured at fair value through profit or loss	*7*	*(35)*	*(149)*	-	-	-	-
CCIRS hedging instruments	*43*	*729*	*3,107*	-	-	-	-
FINANCIAL LIABILITIES							
Interest bearing loans and borrowings	(1,673)	(140)	(597)	(35)	(137)	(6)	(26)
Bonds issued and other debt securities	(3,734)	(642)	(2,734)	-	-	-	-
Trade and other financial liabilities measured at amortized cost, including:	(3,979)	(50)	(213)	-	-	-	-
Trade liabilities	*(1,119)*	*(42)*	*(178)*	-	-	-	-
Liabilities due to purchase of property, plant and equipment	*(1,633)*	*(8)*	*(35)*	-	-	-	-
Derivatives, including:	(89)	(9)	(37)	(3)	(12)	-	-
Measured at fair value through profit or loss	*(89)*	*(9)*	*(37)*	*(3)*	*(12)*	-	-
NET CURRENCY POSITION		**(44)**	**(192)**	**(38)**	**(149)**	**(6)**	**(26)**

The carrying amount of derivative instruments is their fair value. The value of currency risk exposure for forward derivatives is their nominal value at currency. The value of currency risk exposure for CCIRS derivatives is the currency value of discounted cash flows of currency leg.

26.4 Price risk

Due to the type of PGE Group company's business activities, they are exposed to change of cash flows and financial results due to price changes of the following risk factors:

- electricity;
- hard coal, gas, biomass and other fuels;
- CO_2 emission rights;
- energy origin rights.

The PGE Group owns lignite mines that deliver production fuel to two power plants operating within the PGE Group. Due to this fact, the Group's exposure to price risk in this area is not significant.

The main objective of market risk management is to shape the optimal relations of the profit generated to the level of risk incurred and acceptable by the Group within its commercial activities. The defined objective is realized by reducing potential changes of financial result and the level of cash flows resulting from market prices fluctuations of electricity and related products.

The PGE Group has implemented the internal rules for market risk management including above others the determination of the global risk appetite, risk limits measured "at risk" as well as the management of consolidated exposure to the price risk of commodities and mechanisms hedging the risk levels in excess of the acceptable level, with the leading role of PGE S.A. in this process. This allows to create hedging strategies in the area of electricity and related products taking into account the risk borne by the PGE Group in relation to the expected return on assets.

The market risk management policies stipulate uniform assumptions for the organization of that process in the context of commercial strategies and medium-term planning, including among others:

- division of responsibility of individual units;
- specification of accepted products, markets and strategies of operation;
- rules for the calculation of open contract position for particular scopes of commercial activity;
- level of accepted risk with the principles of allocation and management of the capital at risk;
- applicable risk limits;
- risk quantification methodology (including, inter alia, nominal measures, VaR, PaR, scenario analyses, stress tests);
- data and reporting circulation in the risk management process (specifically in the area of application of limits and implementation of hedging strategies).

The management of the consolidated exposure to the market risk in the area of commercial operations of the PGE Group and material risk factors includes the global measurement of the market risk, calculation of aggregated risk measures based on, among others, a concept of value at risk (including VaR and PaR), maintaining the level of risk borne within acceptable limits as well as hedging of the risk exceeding that level and regular reporting of the global exposure level with respect to the risk limits.

The PGE Group executes strategies to secure the key exposures in the area of trading in electricity and related products equivalent to the risk appetite at medium-term (up to 5 years, with the assumption of availability of required markets liquidity). The level of securing the position is determined taking into account the results of measurement of the risk of electricity and related products prices. The results of the risk measurement show the level of potential deviations from the expected achievable results in particular years. The PGE Group assesses the results of the price risk measurement in the context of its risk appetite and the possibilities of hedging the risk of prices of electricity and related products, taking into account liquidity of individual markets. Furthermore, while setting out the target hedge ratios, the PGE Group considers its financial situation, including in particular the assumed goals resulting from the strategy adopted by the Group.

The Group's exposure to price risk of commodities (in relation to raw materials) reflects the volume of external purchases of particular resources which is presented in the table below:

	Year ended December 31, 2016		Year ended December 31, 2015	
COMMODITY	**Tonnage – external purchase (in thousand tonnes)**	**Purchase costs (PLN million)**	**Tonnage – external purchase (in thousand tonnes)**	**Purchase costs (PLN million)**
Hard coal	5,340	1,141	5,588	1,315
CO_2 emission rights for own use	40,681	937	37,879	1,301
Gas [thousand m3]	659,542	454	575,198	484
Biomass	868	190	1,215	333
Fuel oil	41	41	30	38
TOTAL		**2,763**		**3,471**

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26.5 Credit risk

Credit risk is connected with a potential credit event that can occur, such as insolvency of a customer, partial payment of a receivable, significant delay in receivable payment or other breaches of contract conditions (in particular the lack of delivery and acceptance of the goods as agreed in the contract and the possible non-payment for damages and contractual penalties).

The PGE Group entities are exposed to credit risk arising in the following areas:

- basic activities of entities – the credit risk results from, among others, purchases and sales of electricity and heat, purchases and sales of energy origin rights and CO_2 emission rights, purchases of fuels etc. It relates primarily to the possibility of a default by the other party of the transaction, if fair value of the transaction is positive from the point of view of the Group;
- investment activities of entities – the credit risk results from transactions resulting from investment projects which depend on the financial situation of the Group's suppliers;
- investing free cash of entities – the credit risk results from investing free cash of the PGE Group entities in securities bearing credit risk, i.e. financial instruments other than those issued by the State Treasury.

There are significant concentrations of credit risk within the PGE Group related to:

- trade receivables from key customers. The three most significant customers accounted for ca. 10% of the trade receivables balance;
- LTC compensations.

Maximum credit risk exposure resulting from PGE Group's financial assets is equal to the carrying value of these items.

	Year ended December 31, 2016	Year ended December 31, 2015
Trade and other financial receivables	6,562	3,890
Cash and cash equivalents	2,669	3,104
Derivatives – assets	365	50
MAXIMUM CREDIT RISK EXPOSURE	**9,596**	**7,044**

26.5.1 Trade receivables. Other loans and financial receivables

The terms of payments for trade receivables are usually 2-3 weeks. In 2016 the PGE Group received payments for receivables on average after 37 days (debtors turnover ratio in the main companies of the PGE Group ranged between 7 and 56 days). Trade receivables relate mainly to receivables for energy sold and distribution services. According to the management, due to current control over trade receivables, there is no additional credit risk that would exceed the level reflected by allowances for receivables.

The Group reduces and controls credit risk related to commercial transactions. In case of high-value commercial transactions, which may generate significant losses as a result of default of a contracting party, the assessment of the contractor is carried out before the transaction is concluded taking into account financial analysis, past experiences and other factors. Based on the above assessment, the internal rating is awarded or the PGE Group uses ratings given by the independent renowned agencies. Credit limit is determined on the basis of the rating. As a general rule, entering into contracts, which would increase an exposition over the approved limits, requires a collateral consistent with accepted principles of credit risk management. The level of limits used is regularly monitored, and in case of exceeding the limit the units responsible for counterpart risk management are obliged to take action to eliminate them. The PGE Group regularly monitors payments of receivables and uses system of early vindication, taking into consideration deadlines arising from the energy law and high level of repayment of receivables with short term of expire. It also works with business intelligence agencies and debt collection companies.

Credit risk relating to trade receivables by geographical regions is presented in the table below:

	December 31, 2016		December 31, 2015	
	Receivables balance	Share %	Receivables balance	Share %
Poland	2,691	99%	2,520	99%
Other	14	1%	28	1%
TOTAL	**2,705**	**100%**	**2,548**	**100%**

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Ageing of receivables and impairment allowances

As at December 31, 2016 part of financial assets was covered by impairment allowances. The change in allowances accounts for these classes of financial instruments is presented in the table below:

Year ended December 31, 2016	Trade receivables	Other financial receivables	Bonds
Impairment allowance as at January 1	**(212)**	**(181)**	**(386)**
Impairment allowance used	46	12	-
Impairment allowance reversed	4	11	89
Impairment allowance raised	(16)	(25)	-
Other changes	8	(12)	-
Impairment allowance as at December 31	**(170)**	**(195)**	**(297)**
Value before the impairment allowance	**2,875**	**3,963**	**386**
Net value (carrying amount)	**2,705**	**3,768**	**89**

The majority of impairment allowances on trade receivables concern companies from supply and distribution segment. Total impairment allowances on trade receivables recognized in these companies as at December 31, 2016 amounted to PLN 147 million (PLN 171 million in 2015).

PGE S.A. possesses bonds issued by Autostarda Wielkopolska S.A., which in previous years were fully covered with an impairment allowance. Due to revaluation of recoverable amount, the Company partly reversed the impairment allowance of PLN 89 million.

There are no significant receivables in the Group that would be substantially past due and not covered by an impairment allowance, except for disputed claims from ENEA S.A. described in detail in note 28.4 of these financial statements.

Year ended December 31, 2015	Trade receivables	Other financial receivables	Bonds
Impairment allowance as at January 1	**(243)**	**(163)**	**(415)**
Impairment allowance used	33	-	29
Impairment allowance reversed	7	15	-
Impairment allowance raised	(16)	(33)	-
Other changes	7	-	-
Impairment allowance as at December 31	**(212)**	**(181)**	**(386)**
Value before the impairment allowance	**2,760**	**1,523**	**386**
Net value (carrying amount)	**2,548**	**1,342**	**-**

The analysis of ageing structure of trade receivables and other loans and receivables taking into account impairment allowances is presented below:

	December 31, 2016			December 31, 2015		
	Gross amount	Impairment allowances	Carrying amount	Gross amount	Impairment allowance	Carrying amount
Receivables before due date	**6,638**	**(360)**	**6,278**	**4,096**	**(447)**	**3,649**
Past due <30 days	*197*	*(2)*	***195***	*196*	*(3)*	***193***
Past due 30-90 days	*40*	*(1)*	***39***	*41*	*(2)*	***39***
Past due 90-180 days	*14*	*(8)*	***6***	*15*	*(8)*	***7***
Past due 180-360 days	*62*	*(19)*	***43***	*34*	*(32)*	***2***
Past due >360 days	*273*	*(272)*	***1***	*287*	*(287)*	*-*
Receivables past due, total	**586**	**(302)**	**284**	**573**	**(332)**	**241**
Trade and other financial receivables	**7,224**	**(662)**	**6,562**	**4,669**	**(779)**	**3,890**

As at December 31, 2016, more than 66% of overdue trade receivables and other loans and receivables that were not covered by an impairment allowances related to sale of energy to end-users.

26.5.2 Deposits, cash and cash equivalents

The Group manages credit risk related to cash and cash equivalents by diversification of banks in which surpluses of cash are allocated. All entities, that the PGE Group concludes deposit transactions with, operate in the financial sector. These can only be banks registered in Poland or divisions of foreign banks with at least investment ratings, adequate indicators of solvency and equity as well as strong, stable market position. The share of three major banks in which the PGE Group allocated the most significant cash balances as at December 31, 2016 accounted for approximately 80%.

26.5.3 Derivatives

All entities, that the PGE Group concludes derivatives transactions with, operate in the financial sector. These are banks with investment ratings, adequate equity and strong, stable market position. As at the reporting date, the PGE Group was a party to the derivative transactions, described in detail in note 25.1.2 of these consolidated financial statements.

26.5.4 Guarantees and sureties granted

Guarantees and sureties granted by the PGE Group entities are presented in note 28 of these consolidated financial statements.

26.6 Market (financial) risk – sensitivity analysis

The PGE Group identifies the following types of market risk to which it is exposed:

- interest rate risk,
- currency risk,
- commodity price risk.

Currently, the PGE Group is exposed mainly to currency risk related to foreign exchange rates between EUR/PLN, USD/PLN and CHF/PLN and to interest rate risk related to referential interest rates of PLN, EUR, USD and CHF. The PGE Group uses a script analysis method for the purpose of analyzing sensitivity to changes of market risk factors i.e.the Group uses experts' scripts reflecting the subjective opinion in relation to future fluctuations of individual market risk factors.

The scenario analysis presented in this point is intended to analyze the influence of changes in market risk factors on the financial results of the Group. Only those items that can be defined as financial instruments are subject to the analysis of interest and currency risk.

In sensitivity analysis related to interest rate risk, the PGE Group applies parallel shift of interest rate curve related to a potential possible change of referential interest rates during the following year.

In case of sensitivity analysis of interest rates' fluctuations, the effect of risk factors' changes could be recorded in the consolidated statement of comprehensive income as interest income or expenses or as revaluation of financial instruments measured at fair value.

The tables below present sensitivity analysis related to all types of financial market risks to which the Group is exposed as at the reporting date, indicating potential influence of changes of individual risk factors on profit before tax by class of assets and liabilities.

The currency risk exposure for derivative forward instruments is their nominal value together with accrued interest to the reporting date, translated into Polish zloty at the closing rate as at December 31, 2016 and December 31, 2015, without taking the discount into account. In turn, the carrying amount of these derivative instruments is their fair value.

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Sensitivity analysis for currency risk

The table below presents sensitivity of financial instruments to reasonably possible changes in foreign currency exchange rates, under the assumption of stability of other risk factors.

FINANCIAL INSTRUMENTS BY CLASS	Carrying amount in PLN	Amount exposed to risk	SENSITIVITY ANALYSIS FOR CURRENCY RISK AS AT DECEMBER 31, 2016			
			EUR/PLN Impact on financial result/Equity		USD/PLN Impact on financial result/Equity	
			+10%	-10%	+10%	-10%
Trade receivables and other financial receivables	6,562	172	17	(17)	-	-
Cash and cash equivalents	2,669	59	6	(6)	-	-
Derivatives – assets	9	66	7	(7)	-	-
CCIRS hedging instruments	231	3,222	291	(291)	-	-
Interest bearing loans and borrowings	(6,171)	(670)	(57)	57	(10)	10
Bonds issued	(3,842)	(2,842)	(284)	284	-	-
Trade and other financial liabilities	(3,589)	(65)	(7)	7	-	-
Derivatives – liabilities	(30)	(7)	-	-	(1)	1
IMPACT ON PROFIT OR LOSS			**(27)**	**27**	**(11)**	**11**
CCIRS hedging instruments	231	3,222	31	(31)	-	-
IMPACT ON HEDGING RESERVE			**31**	**(31)**	**-**	**-**

FINANCIAL INSTRUMENTS BY CLASS	Carrying amount in PLN	Amount exposed to risk	SENSITIVITY ANALYSIS FOR CURRENCY RISK AS AT DECEMBER 31, 2015					
			EUR/PLN Impact on financial result/Equity		USD/PLN Impact on financial result/Equity		CHF/PLN Impact on financial result/Equity	
			+10%	-10%	+10%	-10%	+10%	-10%
Trade receivables	2,548	151	15	(15)	-	-	-	-
Cash and cash equivalents	3,104	280	28	(28)	-	-	-	-
Derivatives – assets	50	2,958	265	(265)	-	-	-	-
Interest bearing loans and borrowings	(1,673)	(760)	(60)	60	(14)	14	(3)	3
Bonds issued	(3,734)	(2,734)	(273)	273	-	-	-	-
Trade and other financial liabilities	(3,979)	(213)	(21)	21	-	-	-	-
Derivatives – liabilities	(89)	(49)	(4)	4	(1)	1	-	-
IMPACT ON PROFIT OR LOSS			**(50)**	**50**	**(15)**	**15**	**(3)**	**3**
CCIRS hedging instruments	43	3,107	30	(30)	-	-	-	-
IMPACT ON HEDGING RESERVE			**30**	**(30)**	**-**	**-**	**-**	**-**

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Sensitivity analysis for interest rate risk

The Group identifies exposure to interest rate risk related to WIBOR, EURIBOR and LIBOR. The table below presents the sensitivity of financial instruments to reasonably possible changes in interest rates, under assumption of stability of other risk factors.

SENSITIVITY ANALYSIS FOR INTEREST RATE RISK AS AT DECEMBER 31, 2016								
FINANCIAL ASSETS AND LIABILITIES	Carrying amount in PLN	Amount exposed to risk	WIBOR Impact on financial result/Equity		EURIBOR Impact on financial result/Equity		LIBOR USD Impact on financial result/Equity	
			+50bp	-50bp	+25bp	-25bp	+25bp	-25 bp
Trade and other receivables	6,562	88	-	-	<1	<(1)	-	-
Derivatives measured at fair value through profit or loss – assets	365	9	-	-	-	-	-	-
Interest bearing loans and borrowings	(6,171)	(6,050)	(10)	10	(1)	1	-	-
Bonds issued	(3,842)	(1,000)	(5)	5	-	-	-	-
Leasing	(1)	(1)	-	-	-	-	-	-
Derivatives measured at fair value through profit or loss – liabilities	(30)	(30)	5	(5)	-	-	<1	<(1)
IMPACT ON FINANCIAL RESULT			**(10)**	**10**	**(1)**	**1**	**-**	**-**
CCIRS hedging instruments	231	231	60	(62)	(37)	37	-	-
IRS hedging instruments	125	125	128	(133)				
IMPACT ON HEDGING RESERVE			**188**	**(195)**	**(37)**	**37**	**-**	**-**

Value of derivatives exposed to interest rate risk is fair value of those instruments (carrying amount). Sensitivity analysis for CCIRS and IRS derivatives was carried out using the valuation change due to the shift of interest rate curves for particular currency.

SENSITIVITY ANALYSIS FOR INTEREST RATE RISK AS AT DECEMBER 31, 2015								
FINANCIAL ASSETS AND LIABILITIES	Carrying amount in PLN	Amount exposed to risk	WIBOR Impact on financial result/Equity		EURIBOR Impact on financial result/Equity		LIBOR USD Impact on financial result/Equity	
			+50bp	-50bp	+25bp	-25bp	+25bp	-25bp
Derivatives measured at fair value through profit or loss – assets	50	7	<1	<(1)	-	-	-	-
Interest bearing loans and borrowings	(1,673)	(1,519)	(4)	4	(1)	1	-	-
Bonds issued	(3,734)	(1,000)	(5)	5	-	-	-	-
Derivatives measured at fair value through profit or loss – liabilities	(89)	(89)	12	(13)	-	-	(1)	1
IMPACT ON FINANCIAL RESULT			**3**	**(4)**	**(1)**	**1**	**(1)**	**1**
CCIRS hedging instruments	43	43	73	(76)	(43)	44	-	-
IMPACT ON HEDGING RESERVE			**73**	**(76)**	**(43)**	**44**	**-**	**-**

Value of derivatives exposed to interest rate risk is fair value of those instruments (carrying amount). Sensitivity analysis for CCIRS and IRS derivatives was carried out using the valuation change due to the shift of interest rate curves for particular currency.

Sensitivity analysis for commodity price risk

The Group identifies exposure to commodity price risk.

The table below presents the sensitivity analysis to changes of the purchase cost of selected commodities by 10%:

COMMODITY	AS AT DECEMBER 31, 2016			AS AT DECEMBER 31, 2015		
	Purchase cost	Impact on profit or loss		Purchase cost	Impact on profit or loss	
		+10%	-10%		+10%	-10%
Hard coal	1,141	114	(114)	1,315	132	(132)
CO_2 emission rights for own use	937	94	(94)	1,301	130	(130)
Gas [thousand m^3]	454	45	(45)	484	48	(48)
Biomass	190	19	(19)	333	33	(33)
Fuel oil	41	4	(4)	38	4	(4)
TOTAL	**2,763**	**276**	**(276)**	**3,471**	**347**	**(347)**

26.7 Hedge accounting

Due to the loan received from PGE Sweden AB (publ), PGE S.A. concluded CCIRS transactions, that hedge the exchange rate. In these transactions, banks - contractors pay PGE S.A. interest based on a fixed rate in EUR and PGE S.A. pays interest based on a fixed rate in PLN. In the consolidated financial statements the relevant portion of the CCIRS transaction is considered as a hedge of bonds issued by PGE Sweden AB (publ).

Hedge accounting is also applied to the IRS transactions hedging interest rate due to the financial liabilities under credit agreements such as the Credit Agreement with a syndicate of banks signed on September 7, 2015 and Credit Agreement with Bank Gospodarstwa Krajowego signed on December 17, 2014. Within the concluded IRS transactions, banks-contractors pay PGE S.A. interest based on a variable rate in PLN and PGE S.A. pays interest based on a fixed rate in PLN.

The PGE Group applies hedge accounting to the CCIRS and IRS transactions described above. The impact of hedge accounting on the hedging reserve is presented in note 20.2 of these financial statements.

EXPLANATORY NOTES TO THE STATEMENT OF CASH FLOWS

27. Statement of cash flows

27.1 Cash flows from operating activities

Profit/loss on investment activities

	Year ended December 31, 2016	Year ended December 31, 2015
Profit / (loss) on disposal of property, plant and equipment	(11)	(20)
Profit / (loss) on disposal of financial non-current assets	-	(15)
Change in impairment of shares and other financial assets	(84)	-
Valuation of securities	(1)	(12)
Valuation of derivatives	(62)	(5)
Other	27	24
PROFIT/ LOSS ON INVESTMENT ACTIVITIES, TOTAL	**(131)**	**(28)**

Change in receivables

	Year ended December 31, 2016	Year ended December 31, 2015
Change in non-current financial receivables	(95)	(17)
Change in trade and other financial receivables	(2,577)	(233)
Change in bonds acquired	89	-
Change in deposits	2,311	11
Other	(3)	3
CHANGE IN RECEIVABLES, TOTAL	**(275)**	**(236)**

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Change in inventories

	Year ended December 31, 2016	Year ended December 31, 2015
Change in inventories	363	216
Transfer of investment materials to property, plant and equipment	(12)	-
Property rights from the shake-down	(9)	8
CHANGE IN INVENTORIES, TOTAL	**342**	**224**

Change in liabilities, excluding loans and borrowings

	Year ended December 31, 2016	Year ended December 31, 2015
Change in trade and other financial liabilities	(390)	831
Change in other non-financial liabilities	36	21
Change in investment liabilities	298	(536)
Change in tax liabilities related to the increase of the share capital	(110)	-
Other	(3)	2
CHANGE IN LIABILITIES, TOTAL	**(169)**	**318**

Change in other non-financial assets, prepayments and CO_2 emission rights

	Year ended December 31, 2016	Year ended December 31, 2015
Change in other non-current assets	333	165
Change in other current assets	183	(219)
Change in CO_2 emission rights	(177)	(620)
Change in non-current deferred income	(51)	34
Change in current deferred income	7	(30)
Change in advances for construction in progress	(329)	(130)
Change in balance concerning financing/investing activities	(45)	(51)
Other	(17)	(9)
CHANGE IN OTHER NON-FINANCIAL ASSETS, PREPAYMENTS AND CO_2 EMISSION RIGHTS, TOTAL	**(96)**	**(860)**

Change in provisions

	Year ended December 31, 2016	Year ended December 31, 2015
Change in non-current provisions	(1.040)	(55)
Change in current provisions	372	(261)
Change in actuarial provisions recognized in other comprehensive income	249	15
Change in rehabilitation provision recognized in assets	174	(30)
Other	1	(17)
CHANGE IN PROVISIONS, TOTAL	**(244)**	**(348)**

27.2 Cash flows from investing activities

Acquisition of property, plant and equipment and intangible assets

The most significant capital expenditures were incurred by Conventional Generation segment (PLN 5,788 million, of which PLN 3,173 million is related to expenditures on the construction of power units no. 5 and 6 in Opole Power Plant and PLN 663 million is related to expenditures on reconstruction and refurbishment of power units in Bełchatów Power Plant, PLN 434 million related to expenditures on construction of gas and steam units in Gorzów Heat and Power Plant) and by Distribution segment (PLN 1,730 million related mainly to connection of new customers and modernization and development of electric power networks).

Acquisition of financial assets and increase in shareholding in the PGE Group companies

The amount of PLN 467 million concerns mainly investments in Polska Grupa Górnicza (PLN 444 million) described in note 33.2 of these consolidated financial statement, prepayments for BOŚ's shares and acquisition of shares in an associate ElectroMobility.

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Deposits with maturity over 3 months

In the current reporting period PGE S.A. concluded deposits with maturity over 3 months in the total amount of PLN 2,290 million. Additionally, companies belonging to Conventional Generation segment are obliged to hold cash of the Mine Liquidation Fund, which is collected and deposited as required by the Geological and Mining Law Act.

27.3 Cash flows from financing activities

Proceeds from loans

In 2016 the Group has used all of the credits available within the agreements signed in previous years by PGE S.A. with Bank Gospodarstwa Krajowego and Syndicate of Banks in the total amount of PLN 4,630 million.

Repayment of loans, borrowings, bonds and finance lease

This position includes mainly repayment of loans from environmental funds obtained by Conventional Generation segment in the total amount of approximately PLN 203 million.

Dividends paid

On June 28, 2016 the General Shareholders' Meeting of PGE S.A. resolved to distribute PLN 467 million from the net profit of 2015 as a dividend (which comprises PLN 0.25 per share). The dividend was paid on October 14, 2016. The remaining amount of PLN 4 million is related to dividends paid to non-controlling shareholders.

Interests paid

This position includes interest on loans and borrowing of PLN 34 million, interest on bonds of PLN 79 million and interest on financial instruments (CCIRS and IRS) of PLN 83 million.

OTHER EXPLANATORY NOTES

28. Contingent liabilities and receivables. Legal claims

28.1 Contingent liabilities

	As at December 31, 2016	As at December 31, 2015
Contingent return of grants from environmental funds	469	433
Contingent return of CO_2 emission rights received free of charge	115	-
Legal claims	73	67
Employees' claims	1	-
Contractual fines and penalties	12	12
Bank guarantees	-	1
Other contingent liabilities	61	47
TOTAL CONTINGENT LIABILITIES	**731**	**560**

Contingent return of grants from environmental funds

The liabilities represent the value of possible future reimbursements of funds received by the PGE Group companies from environmental funds for the particular investments. The funds will be reimbursed, if investments for which they were granted, will not bring the expected environmental effect.

Contingent return of CO_2 emission rights received free of charge

The contingent liability results from the risk of a return of the equivalent of CO_2 emission rights (including interest) balanced in 2013 and 2014 by capital expenditure that may not obtain the approval of compliance indicators.

Legal claims

The contingent liability is mainly related to the dispute with WorleyParsons. WorleyParsons made a claim for payment of PLN 59 million due to the claimant in the claimant's opinion, and for the return of the amount that in the claimant's opinion was unduly collected by PGE EJ 1 sp. z o.o. from a bank guarantee. PGE EJ 1 sp. z o.o. filed a response to the lawsuit. Moreover, the value of the claims mentioned in the WorleyParsons' lawsuit of PLN 54 million has been included in a request for payment of PLN 92 million related to termination of the agreement, that was filed by WorleyParsons on March 13, 2015. It is anticipated that WorleyParsons may take a separate legal action for the amount of PLN 38 million. The company does not accept the claim and regards its possible admission by the court as unlikely.

Claims related to contractual fines and penalties

The contingent liability comprises mainly accrued contractual fines relating to the delay in realization of the investment issued by the Mayor of the City and Municipality of Gryfino to Zespół Elektrowni Dolna Odra S.A. (currently PGE Górnictwo i Energetyka Konwencjonalna S.A.). The Group committed to the Municipality of Gryfino to accomplish two investments with the total value of not less than almost PLN 8 million until the end of 2018. Failure to realize investments included in the agreement will result in claims relating to contractual fines and penalties by the Municipality of Gryfino.

Other contingent liabilities

Other contingent liabilities comprise the value of potential claim from WorleyParsons of PLN 38 million, which was described above and not balanced transacions for purchase and sale of electricity on the domestic market at the total amount of PLN 20 million.

28.2 Other significant issues related to contingent liabilities

Non-contractual use of property

As described in note 21.4 of these financial statements the PGE Group recognizes provision for disputes under court proceedings, concerning non-contractual use of properties for distribution activities. In addition, in the PGE Group, there are disputes at an earlier stage of proceedings and it cannot be excluded that the number and value of similar disputes will grow in the future.

Contractual liabilities related to purchase of fuels

According to the concluded agreements on the purchase of fuels (mainly coal and gas), the PGE Group companies are obliged to collect the minimum volume of fuels and not to exceed the maximum level of collection of gas fuel in particular hours and months. A failure to collect a minimum volume of fuels specified in the contracts, may result in a necessity to pay some extra fee (in case of gas fuel, the volume not collected by power plants but paid up, may be collected within the next three contractual years).

In the PGE Group's opinion, the terms and conditions of fuel deliveries to its power generating units as described above do not differ from terms and conditions of fuel deliveries to other power generating units on the Polish market.

28.3 Contingent receivables

As at the reporting date, the PGE Group do not have any significant contingent receivables.

28.4 Other legal claims and disputes

The issue of compensation for conversion of shares

Former shareholders of PGE Górnictwo i Energetyka S.A. are presenting to the courts motions to summon PGE S.A. to a conciliation hearing concerning payment of compensation for incorrect (in their opinion) determination of the exchange ratio of shares of PGE Górnictwo i Energetyka S.A. into shares of PGE S.A. during consolidation process that took place in 2010. The total value of claims resulting from summons to a conciliation hearing directed by the former shareholders of PGE Górnictwo i Energetyka S.A. amounts to over PLN 10 million.

Regardless of the above, on November 12, 2014 Socrates Investment S.A. (an entity which purchased claims from former PGE Górnictwo i Energetyka S.A. shareholders) filed a lawsuit to impose a compensation in the total amount of over PLN 493 million (plus interest) for damages incurred in respect of incorrect (in their opinion) determination of the exchange ratio of shares in the merger of PGE Górnictwo i Energetyka S.A. and PGE S.A.

The Company filed a response to the lawsuit. Currently the proceedings before the court of first instance are in progress.

Additionally, Pozwy sp. z o.o. (an entity which purchased claims from former PGE Elektrownia Opole S.A.'s shareholders) filed a similar claim for the amount of over PLN 229 million in the letter dated October 31, 2016 in which they notify about the acquisition of debt and demand payment from PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE S.A. and PwC Polska sp. z o.o. The claim concerns compensation for the allegedly incorrect determination of the exchange ratio of shares of PGE Elektrownia Opole S.A. into shares of PGE Górnictwo i Energetyka Konwencjonalna S.A. in the process of merging these companies. In January 2017, the Company received from Pozwy sp. o.o. two additional notices of acquisition of debt and demands for payment of compensation due to titles mentioned above for the total amount of PLN 27 million.

The PGE Group entities do not recognize the claims of Socrates Investment S.A., Pozwy sp. z o.o. and other shareholders who call for trial settlements. These claims are unfounded. In PGE S.A.'s opinion the consolidation process was conducted fairly and properly. The value of the shares, which were subject to the process of consolidation (merger), was established by an independent company PwC Polska sp. z o.o. Additionally, merger plans of the companies mentioned above, including the exchange ratios were examined for accuracy and reliability by an expert appointed by the registration court; no irregularities were found. Then, the court registered the mergers of the companies mentioned above.

For the reported claims, the PGE Group has not created any provision.

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

On April 1, 2014 PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of the shareholders. In the lawsuit, 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. The Company filed responses to the claims. On June 22, 2015, the District Court in Warsaw issued a judgment dismissing the shareholder's claim in its entirety. The shareholder appealed and the Company filed a response to the appeal.

On August 21, 2015 PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of the shareholders. In the lawsuits, the shareholder is seeking for annulment of the resolution 5 of the Ordinary General Shareholders' Meeting of the Company held on June 24, 2015. The Company filed a response to the lawsuit. The District Court in Warsaw dismissed the shareholder's claim in its judgment issued on April 26, 2016.

On September 17, 2014 PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of the shareholders. In the lawsuits, the shareholder is seeking for annulment of the resolution 4 of the Extraordinary General Shareholders' Meeting of the Company held on June 6, 2014. The Company filed a response to the lawsuit. On August 13, 2015, the District Court in Warsaw issued a judgment dismissing the shareholder's claim in its entirety. The shareholder appealed and the Company filed a response to the appeal. On March 2, 2017 the Appeals Court in Warsaw dismissed the appeal.

On October 23, 2015 PGE S.A. received a copy of a lawsuit filed to the District Court in Warsaw by one of the shareholders. In the lawsuit, the shareholder is seeking for annulment of the resolution 1 of the Extraordinary General Shareholders' Meeting of the Company held on September 14, 2015. The Company filed a response to the lawsuit.

On May 20, 2016 PGE S.A. received a copy of a lawsuit filed to the District Court in Warsaw by one of the shareholders. In the lawsuit, the shareholder is seeking for annulment of the resolution 1 of the Extraordinary General Shareholders' Meeting of the Company held on March 1, 2016. The Company filed a response to the lawsuit.

On September 12, 2016 PGE S.A. received a copy of a lawsuit filed to the District Court in Warsaw by one of the shareholders. In the lawsuit, the shareholder is seeking for annulment of the resolution 1 of the Ordinary General Shareholders' Meeting of the Company held on June 28, 2016. The Company filed a response to the lawsuit.

On December 30, 2016 PGE S.A. received a copy of a lawsuit filed to the District Court in Warsaw by one of the shareholders. In the lawsuit, the shareholder is seeking for annulment of the resolution 1 of the Extraordinary General Shareholders' Meeting of the Company held on September 5, 2016. The Company filed a response to the lawsuit.

Termination of long-term contracts for purchase of energy origin rights by Enea S.A.

On October 28, 2016 and October 31, 2016 PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE Energia Odnawialna S.A. and PGE Energia Natury PEW sp. z o.o. received from Enea S.A. termination of long-term contracts for purchase of renewable energy origin rights, so called "green certificates".

In the opinion of the PGE Group, notices of termination of contracts presented by Enea S.A. were filled in with a violation of terms of the agreements. The companies took appropriate steps to enforce their rights. In particular, in the opinion of the Management Board of PGE GiEK S.A. the termination of the contract by Enea S.A. is ineffective and against the earlier agreement between the parties (a letter of intent) and on that ground PGE GiEK S.A. will demand compensation for termination of the long-term contract.

Estimated volume of the green certificates, covered by the contracts with Enea S.A., amounts to approximately 3,115 thousand MWh. The above amount was calculated for the period from December 2016 (i.e. the month from which Enea S.A. stopped purchasing of green certificates - after taking into account the notice period) until the initial maturity dates of the contracts.

Additionally, PGE Górnictwo i Energetyka Konwencjonalna S.A. is a part to the dispute with ENEA S.A. in connection to damage resulting from inadequate (according to ENEA) execution of agreement for sales of energy origin rights by not participating in renegotiations of the agreement within a contract procedure. In PGE GiEK S.A.'s opinion, there is no reasonable basis to acknowledge ENEA S.A.'s viewpoint that inadequate execution of any contractual obligations by PGE GiEK S.A. occured. Therefore, the Company does not accept the claim in principle, nor the amount. ENEA S.A. disagrees with the opinion of PGE GiEK S.A. and thus it deducted the amount of its claim from its liabilities to PGE GiEK S.A. As at the date of preparation of these financial statements the dispute is in mediation proceedings. The disputed amount is PLN 42 million.

for the year 2016 in accordance with IFRS EU (in PLN million)

29. Future investment commitments

As at December 31, 2016 the PGE Group committed to incur capital expenditures on property, plant and equipment of approximately PLN 9,789 million. These amounts relate mainly to construction of new power units, modernization of Group's assets and purchase of machinery and equipment.

	As at December 31, 2016	As at December 31, 2015
Conventional Generation	7,647	11,603
Distribution	796	850
Renewables	38	116
Supply	2	3
Other operations	1,306	1,323
TOTAL FUTURE INVESTMENT COMMITMENTS	**9,789**	**13,895**

The most significant future investment commitments concern:

- Conventional Generation:
  - Branch Opole Power Plant – construction of power units no. 5 and 6 – approximately PLN 2,726 million,
  - Branch Turów Power Plant – construction of new power unit – approximately PLN 3,252 million,
  - Branch Turów Power Plant – modernization of power units no. 1-3 – approximately PLN 588 million,
  - Branch Rzeszów Heat and Power Plant – construction of Thermal Processing Installation with Energy Recycling – approximately PLN 275 million,
- Distribution – investment commitments related to network distribution assets with the total value of approximately PLN 796 million,

- Other operations, PGE EJ1 sp. z o.o. – agreement for owners engineer in the investment process related to construction of the first Polish nuclear power plant – approximately PLN 1,288 million (of wich 183 million PLN is the basic range and the remaining amount of the agreement is the extend optional).

30. Lease

30.1 Operating lease liabilities – the Group as a lessee

As at the reporting date and in the comparative period the future minimum lease payments related to irrevocable lease agreements amounted to PLN 193 million.

The PGE Group entities incur costs related to fees for perpetual usufruct of land. The value of these costs for the year ended December 31, 2016 amounted to PLN 18 million and PLN 17 million in the comparative period.

30.2 Operating lease receivables – the Group as a lessor

The PGE Group companies have signed agreements with Polskie Sieci Elektroenergetyczne S.A. on rendering intervention services related to administration and use of production units by the system operator in order to balance active and passive power on an intervention basis in the National Electroenergetic System (NES). This aims at ensuring proper and safe operation of the system. The above mentioned agreements, although not having a legal form of a lease, give the right to use the assets for a series of payments.

30.3 Liabilities from finance lease and lease agreements with a purchase option

As at the reporting date the present value of the minimum current lease payments amounted to approximately PLN 1 million, while in the corresponding period the present value of the minimum current and non-current lease payments amounted to approximately PLN 1 million.

30.4 Receivables from finance lease and lease agreement with a purchase option

At the reporting date, and in the comparative period the Group did not identify significant receivables from finance lease agreements.

Consolidated financial statements of the PGE Polska Grupa Energetyczna S.A. Group for the year 2016 in accordance with IFRS EU (in PLN million)

31. Tax settlements

Tax obligations and rights are specified in the Constitution of the Republic of Poland, tax regulations and rectified international agreements. According to the tax ordinance, tax is defined as public, unpaid, obligatory and non-returnable cash liability toward the State Treasury, provincial or other regional authorities resulting from tax regulation. Taking into account the subject criterion, current taxes in Poland can be divided into five groups: taxation of incomes, taxation of turnover, taxation of assets, taxation of activities and other, not classified elsewhere.

From economic units point of view, the most important is the taxation of incomes (corporate income tax), taxation of turnover (value added tax, excise tax) followed by taxation of assets (real estate tax and vehicle tax). Other payments classified as quasi – taxes cannot be omitted. Among these there are social security charges.

Basic tax rates were as follows in 2016: corporate income tax rate – 19%, basic value added tax rate – 23%, lowered: 8%, 5%, 0%, furthermore some goods and products are subject to the tax exemption.

The tax system in Poland is characterized by a significant changeability of tax regulations, their high complexity, high potential fees foreseen in case of commitment of a tax crime or violation. Tax settlements and other activity areas subject to regulations (customs or currency controls) can be subject to controls of respective authorities that are entitled to issue fines and penalties with penalty interest. Controls may cover tax settlements for the period of 5 years after the end of calendar year in which the tax was due.

Tax Group

On September 18, 2014 an agreement concerning a tax group, named “TG PGE 2015” was executed for a 25-year period. PGE S.A. is the representing company of this group.

The companies forming a tax group are obligated to meet a number of requirements including: the appropriate level of equity, the parent company’s share in companies included in the group at least at the level of 95%, no equity relationships between subsidiaries, no tax arrears and share of profits in revenues at least at the level of 3% (calculated for the whole TG) as well as concluding transactions with entities not belonging to TG solely on market terms. The violation of these requirements will affect in termination of the tax group and the loss of status of the taxpayer. Since the termination, each of the companies included in the tax group becomes an independent taxpayer for CIT tax purpose.

Real estate tax

Considering pending disputes the PGE Group established at the reporting date the provision for property tax in the amount of PLN 90 million. The provision relates mainly to tax proceedings with regard to property tax in selected power plants. The dispute is related to the subject of taxation and concerns mainly a decision whether installations in buildings and detached technical machinery should be taxed as autonomous constructions. Tax proceedings are currently at various stages of tax authorities proceedings, i.e. in front of first instance authorities (village mayor, mayor), local government board of appeals and administrative courts.

32. Information on related parties

The PGE Group’s transactions with related entities are being concluded using market prices for provided goods, products and services or are based on the cost of manufacturing.

32.1 Associates and jointly controlled entities

The total value of transactions with such entities is presented in the table below.

	Year ended December 31, 2016	Year ended December 31, 2015
Sales to associates and jointly controlled entities	88	7
Purchases from associates and jointly controlled entities	571	-

	Year ended December 31, 2016	Year ended December 31, 2015
Trade receivables from associates and jointly controlled entities	41	1
Trade liabilities to associates and jointly controlled entities	16	-

The increase in turnover and balances results from the inclusion of Polska Grupa Górnicza sp. z o.o. in these financial statements. This entity is treated as a jointly controlled entity.

32.2 Subsidiaries of the State Treasury

The State Treasury is the dominant shareholder of PGE Polska Grupa Energetyczna S.A. and as a result in accordance with IAS 24 *Related Party Disclosures*, State Treasury companies are treated as related entities. The PGE Group entities identify in detail transactions with approximately 40 of the biggest State Treasury subsidiaries.

The total value of transactions with such entities is presented in the table below:

	Year ended December 31, 2016	Year ended December 31, 2015
Sales to related parties	2,137	2,509
Purchases from related parties	3,579	3,539

	Year ended December 31, 2016	Year ended December 31, 2015
Trade receivables from related parties	313	383
Trade liabilities to related parties	418	387

The largest transactions with State Treasury companies involve Polskie Sieci Elektroenergetyczne S.A., Enea S.A., ENERGA-OBRÓT S.A., PKN Orlen S.A. and purchases of coal from Polish mines.

Moreover, the PGE Group concludes significant transactions on the energy market via Towarowa Giełda Energii S.A. (Polish Power Exchange). Due to the fact that this entity only deals with the organization of trading, purchases and sales transacted through this entity are not recognized as transactions with related parties.

32.3 Management personnel remuneration

The key management includes the Management Boards and Supervisory Boards of the parent company and significant Group entities.

PLN thousand	Year ended December 31, 2016	Year ended December 31, 2015
Short-term employee benefits (salaries and salary related costs)	32,508	30,877
Post-employment and termination benefits	9,446	4,542
TOTAL REMUNERATION OF KEY MANAGEMENT PERSONNEL	**41,954**	**35,419**
Remuneration of key management personnel of entities of non-core operations	15,395	13,720
TOTAL REMUNERATION OF MANAGEMENT PERSONNEL	**57,349**	**49,139**

PLN thousand	Year ended December 31, 2016	Year ended December 31, 2015
Management Board of the parent company, including:	11,669	6,217
Post-employment benefits	*3,066*	*(46)*
Supervisory Board of the parent company	510	407
Management Boards – subsidiaries	27,448	27,394
Supervisory Boards – subsidiaries	2,327	1,401
TOTAL	**41,954**	**35,419**
Remuneration of key management personnel of entities of non-core operations	15,395	13,720
TOTAL REMUNERATION OF MANAGEMENT PERSONNEL	**57,349**	**49,139**

Increase of the remuneration of management personnel is mainly caused by higher post-employment benefits (terminations, non-competition clauses).

The Members of the Management Boards of some of the Group companies are employed on the basis of civil law contracts for management (so called management contracts). The above remuneration is included in other costs by nature disclosed in note 7.2 Costs by nature and function.

33. Significant events of the reporting period and subsequent events

33.1 Termination of long term contracts LTC

Due to the termination of long-term contracts for sale of capacity and electricity ("LTC"), pursuant to the LTC Act, power generating units who once served as parties to such contracts have acquired the right to compensations for the coverage of the so-called stranded costs. Stranded costs are the expenses of the power generating units, borne until May 1, 2004 for property, plant and equipment related to the production of electricity, uncovered by revenue from the sales of the electricity produced, capacity reserves and system services on the competitive market, after the premature termination of the long-term contract. The LTC Act limits the total resources which can be paid out to all power generating units to cover stranded costs discounted as of January 1, 2007 to the sum of PLN 11.6 billion, with PLN 6.3 billion attributable to PGE.

Basic data for Group power generating units assumed with the LTC Act.

Power generating unit	Effective term of the Act	Maximum stranded and extra costs (in PLN mln)
Turów Power Plant	Until 2016	2,571
Opole Power Plant	Until 2012	1,966
Dolna Odra Power Plant Complex	Until 2010	633
Lublin Wrotków CHP Plant	Until 2010	617
Rzeszów Heat and Power Plant	Until 2012	422
Gorzów Heat and Power Plant	Until 2009	108
TOTAL		**6,317**

Within the term stipulated by the LTC Act, i.e. until December 31, 2007, PGE S.A. signed contracts terminating its long-term capacity and electricity sales contracts with power generating units who once served as parties to the then effective LTC. Therefore, the power generating units have gained the right to receive funds to cover stranded costs.

Decisions of the President of the Energy Regulatory Office related to realisation of the 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 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.

Until the date of preparation of these financial statements, producers from the PGE Group received decisions on annual adjustments of stranded costs and costs generated in gas-fired units for the years 2008-2015. In part, these decisions were unfavourable for the particular units, and, in the opinion of the Group, were issued in violation of the LTC Act. In consequence, since 2009, a number of proceedings have been pending before the District Court in Warsaw - Competition and Consumer Protection Court ("CCP Court") and before the Court of Appeals, regarding appeals of power generating units from the PGE Group against the Decision of the President of the Energy Regulatory Office ("ERO President"). The value of disputes in all matters relating to the years 2008 – 2012 amounts to PLN 1,660 million, including the value of disputes favourably resolved for the PGE Group by the Court of Appeals and a favourable final judgment by the CCP Court of PLN 1,489 million. As at the date of preparation of these financial statements, majority of the proceedings are conducted before the Supreme Court.

During 2016 the following events took place regarding annual adjustments of stranded costs and costs generated in gas-fired units for the years 2008-2015:

- On April 7, 2016 the court case was conducted before the Supreme Court, during which a cassation appeal of the ERO President was examined concerning the determination of annual adjustment of costs arising in gas-fired units at PGE GiEK S.A. Branch Lublin - Wrotków Heat and Power Plant for 2009. The Supreme Court overruled the contested judgment of the Court of Appeals in Warsaw in its entirety and dismissed the appeal of PGE GiEK S.A. The claimed amount in this case was nearly PLN 7 million. As a consequence of the verdict, the company paid that amount to the account of Zarządca Rozliczeń S.A.
- On April 7, 2016 the Supreme Court refused to accept for examination the cassation submitted by PGE GiEK S.A appeal concerning the determination of annual adjustment of costs arising in gas-fired units at PGE GiEK S.A. Branch Lublin – Wrotków Heat and Power Plant and Branch Rzeszów Heat and Power Plant for 2010. The ruling ends the proceedings, meaning that rulings by the CCP Court and the Court of Appeals are binding. The claimed amount in this case was PLN 4 million.

On April 14, 2016 the court case was conducted before the Court of Appeals concerning the determining of annual adjustment of stranded costs due to GiEK S.A. Branch Opole Power Plant for 2010. The court allowed the appeal of the PGE Group and at the same time dismissed the appeal of the ERO President. The above means that the court changed the contested decision as requested by the appeal of the PGE Group. The judgement is binding. The ERO President did not file a cassation appeal. The claimed amount in this case was approx. PLN 142 million. Zarządca Rozliczeń S.A. transferred that amount to the PGE GIEK S.A.'s account.

- On May 12, 2016 the court case was conducted before the Court of Appeals concerning the determination of annual adjustment of costs arising in gas-fired units at Branch Rzeszów Heat and Power Plant for 2012. The Court of Appeals issued a judgment in which changed the verdict of the CCP Court in its entirety and dismissed the company's appeal. The claimed amount in this case is approx. PLN 7 million.
- On May 12, 2016 the Supreme Court refused to accept for examination the cassation appeal of PGE GIEK S.A. concerning determination of annual adjustment of costs arising in gas-fired units at Branch Rzeszów Heat and Power Plant for 2009 and 2011. The claimed amount in both cases is to approx. PLN 10 million.
- On August 8, 2016 PGE GiEK S.A. received administrative decision of the ERO President regarding the annual adjustment of the stranded costs for the year 2015. The amount of the annual adjustment of stranded costs in power generating units: Branch Turów Power Plant and Brach Opole Power Plant for 2015 is approx. PLN (+) 326 million. The company does not dispute this amount. The advances collected in 2015 amounted to PLN 251 million.
- On September 14, 2016, the PGE Group appealed against the ruling of the District Court in Warsaw regarding the compensation claimed by the company from the State Treasury – the ERO President for lost benefits incurred by the Group due unfavourable decisions of the ERO President regarding stranded costs for 2008. The claimed amount in this case is PLN 57 million.
- On September 15, 2016, the Court of Justice of the European Union issued a ruling regarding prejudicial questions concerning the group in the meaning of the LTC Act.

  The above question concerned two issues:

  - whether national courts are competent to examine issues related to LTCs?

  The Court ruled that the national bodies and courts are not authorised to verify whether national laws that are considered to be an authorised state aid are in compliance with the assumptions listed in the Announcement of the Commission relating to the methodology for analysing state aid linked to stranded costs;

  - whether entities in a group should be defined based on the group structure reflected in Annex 7 to the LTC Act or based on the current structure in each year covered by the programme?

  The Court ruled that when determining annual adjustments of compensations for stranded costs to be paid to a power generating untit belonging to a group, the companies should take into account the group's structure and consequently the group's financial results at the time when the adjustment is made, and not the group structure reflected in Annex 7 to the LTC Act.
- In connection with the above, a cassation hearing before the Supreme Court took place on November 10, 2016 regarding the cassation appeal of the ERO President against judgment of the Court of Appeals in respect of calculation of the annual adjustment of stranded costs at the Branch Dolna Odra Power Plant Complex for 2009. The Supreme Court overruled the judgement of the Court of Appeals in its entirety and changed the judgement of the CCP Court by replacing the annual adjustment for 2009 in the amount of PLN (+) 117 million with the amount of PLN (+) 51 million. As a result of this judgement, PGE GiEK S.A. paid PLN 66 milion to the account of Zarządca Rozliczeń S.A. on November 30, 2016.
- On December 8, 2016 conciliatory meeting was held, involving PGE GiEK S.A. as a petitioner and the ERO President as a defendant. The meeting concerned the payment of PLN 107 million as a compensation for PGE GiEK S.A. for lost benefits resulting from unfavorable decisions for the year 2009. Agreement has not been reached.

Additionally, starting from January 1, 2017 until the date of preparation of these financial statements, the following events took place related to adjustments of stranded costs and costs generated in gas-fired units for the years 2008-2015:

- On January 10, 2017 the Supreme Court:
  - refused to accept for examination the cassation appeal of PGE GiEK S.A. against the judgement of the Court of Appeals concerning the determination of annual adjustment of stranded costs for Branch Dolna Odra Power Plant Complex for 2008.
  - overruled judgement of the Court of Appeals in Warsaw regarding the determination of annual adjustment of stranded costs for Branch Gorzów Heat and Power Plant for 2009. The case was submitted for reexamination by the Court of Appeals.
- On January 26, 2017 the Supreme Court issued an alter decision concerning:
  - the annual adjustment of stranded costs for Branch Lublin Wrotków Heat and Power Plant for 2008 in which it determined its value at approx. PLN (+) 9 million. As a result, PGE GiEK S.A. will return to Zarządca Rozliczeń S.A. the amount of approx. PLN 1 million.

- the annual adjustment for stranded costs for Branch Rzeszów Heat and Power Plant for 2009, in which it determined its value at PLN 0. As a result, PGE GiEK S.A. will return to Zarządca Rozliczeń S.A. the amount of approx. PLN 7 million.

Effect on the financial statements for the period ended December 31, 2016

In the financial statements for the period ended December 31, 2016, the PGE Group recognized revenues from LTC compensations of PLN 520 million in sales revenues.

The verdict of the Court of Appeals concerning the determination of annual adjustment of stranded costs for GiEK S.A. Branch Opole Power Plant for 2010 resulted in an adjustment of LTC settlements of approx. PLN (+) 173 million that was recognized in the financial statements for the period ended December 31, 2016.

Moreover, refusal to accept for examination the cassation appeal of PGE GIEK S.A. concerning annual adjustment of costs arising in gas-fired units at PGE GiEK S.A. Branch Lublin-Wrotków Heat and Power Plant and Branch Rzeszów Heat and Power Plant for 2010 and unfavourable ruling of the Supreme Court in case of the annual adjustment of costs arising in gas-fired units at PGE GiEK S.A. Branch Lublin - Wrotków Heat and Power Plant for 2009 caused an adjustment of LTC settlements of PLN (-) 25 million that was recognized in the financial statements for the period ended December 31, 2016.

The above adjustments are presented in net amount in the statement of comprehensive income in other operating revenues.

In the period from 2008 till December 31, 2016 the PGE Group recognised revenues from LTC compensations in total amount of PLN 7,755 million

33.2 Agreement on financial investment in Polska Grupa Górnicza sp. z o.o.

On April 28, 2016, PGE Górnictwo i Energetyka Konwencjonalna S.A. signed the Investment Agreement determining the conditions of the financial investment ("Investment") in Polska Grupa Górnicza sp. z o.o. („Agreement"). The parties of the Agreement are: PGE Górnictwo i Energetyka Konwencjonalna S.A., ENERGA Kogeneracja sp. z o.o., PGNiG TERMIKA S.A., Węglokoks S.A., Towarzystwo Finansowe „Silesia" Sp. z o.o., Fundusz Inwestycji Polskich Przedsiębiorstw FIZAN (jointly referred later to as the „Investors") and Polska Grupa Górnicza Sp. z o.o. („PGG"). PGG operates on the basis of selected mining assets, acquired from Kompania Węglowa S.A. ("KW") (including 11 hard coal mines, 4 operational units and support, managing and supervisory functions of KW headquarters transferred therewith).

The Agreement specifies the Investment conditions, including inter alia, conditions of PGG recapitalisation by the Investors, operating rules of PGG and corporate governance rules, including method of Investors' supervision over PGG.

Recapitalisation of PGG in total amount of PLN 2,417 million, was divided into 3 tranches, within which PGE GiEK S.A. will pay a total of PLN 500 million, including:

- PLN 361 million within the first tranche. The result was acquisition of 15.7% in the share capital of PGG by PGE GiEK S.A. on April 29, 2016;
- PLN 83 million within the second tranche. The result was acquisition of further shares increasing the share of PGE GiEK S.A. in the share capital up to 16.6% on November 3, 2016;
- PLN 56 million within the third tranche. As a result of the third payment, PGE GiEK's share in the share capital of PGG increased up to 17.1% on February 1, 2017).

The particular tranches were released, on the condition, inter alia, that terms of PGG bonds issue are not breached.

PGG operates on the basis of the business plan, which aims at optimisation of coal production costs and achieving defined profitability levels. The business plan assumes that in 2017 PGG will generate positive cash flows for the Investors. The Agreement foresees several mechanisms allowing for on-going monitoring of the financial standing of PGG, including execution of the business plan and taking further optimization measures, among others, in case of adverse changes in market conditions. The Agreement assumes that each shareholder of PGG is entitled to appoint, recall and suspend one member of the Supervisory Board (individual rights). Moreover, key decisions of the General Sheraholeders' Meeting of PGG regarding the capital management and restructuring require the Investors' approval.

Moreover, on June 17, 2016 PGE Górnictwo i Energetyka Konwencjonalna S.A., ENERGA Kogeneracja sp. z o.o., PGNiG TERMIKA S.A. and Fundusz Inwestycji Polskich Przedsiębiorstw Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych (jointly referred to as „New Investors") signed an agreement concerning PGG. The purpose of this agreement is to provide increased control over PGG leading to higher probability of investment success in PGG, as well as increased impact on potential modifications to PGG's business plan that would meet the expectations of New Investors and new market challenges.

On June 29, 2016 the Office of Competition and Consumer Protection issued consent for concentration that involves taking of joint control over PGG by the New Investors.

Taking into account rights entitled to PGE Górnictwo i Energetyka Konwencjonalna S.A. mentioned above, the investment in PGG is treated as a jointly controlled entity and accounted for using the equity method in these consolidated financial statements.

33.3 Submission of an initial offer with partners for EDF assets in Poland

On September 16, 2016 PGE Polska Grupa Energetyczna S.A., together with Energa S.A., Enea S.A., and PGNiG Termika S.A. ("Business Partners") jointly submitted to EDF an initial, non-binding offer for purchase of conventional generation and heat and power plant assets.

Due to the fact that initial offer was applicable until December 2016, PGE Polska Grupa Energetyczna S.A., together with Energa S.A., Enea S.A. and PGNiG Termika S.A. submitted on November 30, 2016 a conditional offer concerning a purchase of EDF's assets to maintain a willingness of further participation in the sale process.

On January 27, 2017 PGE Polska Grupa Energetyczna S.A. together with ENEA S.A., Energa S.A. and PGNiG Termika S.A. signed a Memorandum of Understanding with EDF concerning conducting negotiations to purchase EDF's assets located in Poland and related due diligence procedures.

33.4 Overburden slide at an internal heap in the Turów lignite mine

In the night from September 26 to 27, 2016 a landslide process began at an internal heap in the Turów lignite mine. The mine temporarily limited coal mining activities what resulted in slight reduction of generation capacity of the Turów power plant. This limitation meant that the amount of surplus sales contracts above production capacities in Turów Power Plant were transferred to other free generating capacity in the PGE Capital Group. Production of electricity from PGE Group entities resulted from a new level of distribution contracting for individual generating units and was realized with accordance with the needs of the National Power System.

A rescue operation intended to secure equipment and infrastructure was completed on October 5, 2016, and the situation around the landslide stabilised. Coal supply to the power plant was continuous, drawing from a coal reserve, which stores fuel inventories, and thanks to the launch of additional mining walls. From October 7, 2016, an overburden removal operation is taking place, removing overburden that is covering lignite deposits. As a consequence of the slide a stacker and part of transportation system and associated infrastructure were destroyed. Due to the above in 2016, the Company recognized costs at the amount of PLN 19 million which comprised impairment losses of damaged assets and net value of liquidated property, plant and equipment.

Current geological-engineering situation around landslide is stable. Till the end of 2016 full supply of coal to adjacent Turów Power Plant was restored, with reception of ash provided and a limited amount of overburden. Numerous design works have been conducted in order to adapt the transporting system of the internal heap and pit mining to the occured situation. The additional expenses related to securing the landslip and recovering the full technical efficiency amounted to PLN 23 million in 2016. Total compensation received in 2016 amounted to PLN 49 million.

Supply of fuel to the Turów Power Plant proceeds without any limitations and the working of power units in Turów Power Plant goes according to the plan and requirements of domestic energy system.

Estimated, as at December 31, 2016 and as at the date of publication of these consolidated financial statements, value of costs and capital expenditures for the years 2017-2019 essential to restore damaged and lost assets due to the landslip amounts to approx. PLN 142 million. The amount comprises mainly expenses related to reconstruction of stacker, construction and reconstruction of conveyor belts and grading of internal heap.

33.5 Capital investment in Polimex-Mostostal S.A.

On January 18, 2017 PGE S.A. signed the following agreements concerning capital investment in Polimex-Mostostal S.A. („Polimex"):

- investment agreement with ENEA S.A., Energa S.A., PGNiG Technologie S.A. (jointly refered as to "Investors") and Polimex, on the basis of which, subject to conditions precedent specified in the agreement, Investors are obligated to make an investment in Polimex. The investment includes taking up 150,000,000 of series T ordinary shares with a nominal value of PLN 2 each and an issue price of PLN 2 each ("New Shares") issued by Polimex as the increase of share capital of Polimex by up to PLN 300 million ("Investment Agreement"). Under the terms of the Agreement PGE committed to purchase 37,500,000 New Shares at the total issue price amounting to PLN 75 million;
- agreement between Investors, defining the terms of cooperation together with mutual rights and responsibilities of Investors relating to the investment carried out on the basis of Investment Agreement;
- agreement between Investors and SPV Operator Sp. z o.o. ("SPV Operator") obliging the parties, subject to fulfillment of conditions precedent, to conduct a sale transaction of 6,000,001 Polimex shares by SPV Operator to Investors, whereas PGE obligated to acquire a number of 1,500,001 aforesaid shares;
- agreement between Investors and TFS whereby TFS granted Investors, for remuneration, a possibility to acquire Polimex shares provided that TFS realizes conversion right in respect of convertible bonds issued by Polimex. Moreover, TFS has committed not to converse possessed convertible bonds of series A issued by Polimex without prior written request made by Investors.

for the year 2016 in accordance with IFRS EU (in PLN million)

On January 20, 2017, due to the fulfillment of conditions precedent specified in the Investment Agreement, PGE accepted the offer made by Polimex's Management Board to acquire 37,500,000 series T ordinary shares issued by Polimex with a nominal value of PLN 2 each and an issue price of PLN 2 each and the total issue price of PLN 75 million.

Additionally, on the terms of agreement with SPV Operator and due to the fulfillment of conditions precedent, the Company acquired 1,500,001 Polimex shares from SPV Operator.

On January 18, 2017, the President of the Office for Competition and Consumer Protection issued a permission for Investors to take joint control over Polimex.

Due to rights entitled to PGE S.A. under the terms of the aforesaid investments, in the next financial statements Polimex will be treated as a jointly controlled entity, and the investment in Polimex will be recognized under the equity method.

34. Approval of the financial statements

These consolidated financial statements were authorized for issue by the Management Board on March 7, 2017.

Warsaw, March 7, 2017

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

President of the Management Board	**Henryk Baranowski**
Vice-President of the Management Board	**Bolesław Jankowski**
Vice-President of the Management Board	**Wojciech Kowalczyk**
Vice-President of the Management Board	**Marek Pastuszko**
Vice-President of the Management Board	**Paweł Śliwa**
Vice-President of the Management Board	**Ryszard Wasiłek**
Vice-President of the Management Board	**Emil Wojtowicz**

Signature of the person responsible for preparation of the financial statements

Michał Skiba - Director of Financial Reporting and Tax Department