



***PGE Polska Grupa Energetyczna S.A.  
Consolidated financial statements for 2017***

***ended December 31, 2017  
in accordance with IFRS (in PLN million)***

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## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended December 31, 2017	Year ended December 31, 2016
<b>STATEMENT OF PROFIT OR LOSS</b>			
<b>SALES REVENUES</b>	<u>7.1</u>	<b>23,100</b>	<b>28,092</b>
Cost of goods sold	<u>7.2</u>	(17,615)	(23,174)
<b>GROSS PROFIT ON SALES</b>		<b>5,485</b>	<b>4,918</b>
Distribution and selling expenses	<u>7.2</u>	(1,220)	(1,429)
General and administrative expenses	<u>7.2</u>	(793)	(977)
Other operating income	<u>7.3</u>	403	1,171
Other operating expenses	<u>7.3</u>	(255)	(171)
<b>OPERATING PROFIT</b>		<b>3,620</b>	<b>3,512</b>
Finance income	<u>7.4</u>	191	191
Finance expenses	<u>7.4</u>	(561)	(384)
Share of profit/(loss) of entities accounted for using the equity method	<u>7.5</u>	40	(45)
<b>PROFIT BEFORE TAX</b>		<b>3,290</b>	<b>3,274</b>
Current income tax	<u>8.1</u>	(632)	(414)
Deferred income tax	<u>8.1</u>	9	(294)
<b>NET PROFIT FOR THE REPORTING PERIOD</b>		<b>2,667</b>	<b>2,566</b>
<b>OTHER COMPREHENSIVE INCOME</b>			
<b>Items that may be reclassified to profit or loss in the future:</b>			
Valuation of financial instruments	<u>20.3</u>	(5)	1
Valuation of hedging instruments	<u>20.3</u>	(74)	206
Foreign exchange differences on translation of foreign entities	<u>20.4</u>	(7)	4
Deferred tax	<u>8.1</u>	15	(39)
<b>Items that may not be reclassified to profit or loss in the future:</b>			
Actuarial gains and losses from valuation of provisions for employee benefits	<u>22</u>	(101)	249
Deferred tax	<u>8.1</u>	19	(47)
Share of profit/(loss) of entities accounted for using the equity method	<u>7.5</u>	-	(2)
<b>OTHER COMPREHENSIVE INCOME FOR THE REPORTING PERIOD, NET</b>		<b>(153)</b>	<b>372</b>
<b>TOTAL COMPREHENSIVE INCOME</b>		<b>2,514</b>	<b>2,938</b>
<b>NET PROFIT ATTRIBUTABLE TO:</b>			
- equity holders of the parent company		2,660	2,568
- non-controlling interests		7	(2)
<b>COMPREHENSIVE INCOME ATTRIBUTABLE TO:</b>			
- equity holders of the parent company		2,507	2,940
- non-controlling interests		7	(2)
<b>EARNINGS AND DILUTED EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT COMPANY (IN PLN)</b>	<u>20.7</u>	<b>1.42</b>	<b>1.37</b>

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	As at December 31, 2017	As at December 31, 2016 <i>restated data*</i>	As at January 1, 2016 <i>restated data*</i>
<b>NON-CURRENT ASSETS</b>				
Property, plant and equipment	9	58,620	51,365	47,068
Investment properties	10	47	27	30
Intangible assets	11	1,281	653	904
Financial receivables	25.1.1	158	237	142
Derivatives and other assets at fair value through profit or loss	25.1.2	222	356	43
Available-for-sale financial assets	25.1.3	47	37	15
Shares accounted for using the equity method	12	634	402	8
Other non-current assets	16.1	524	730	1,063
CO <sub>2</sub> emission rights for captive use	15	402	1,157	1,322
Deferred tax assets	13.1	651	268	313
		<b>62,586</b>	<b>55,232</b>	<b>50,908</b>
<b>CURRENT ASSETS</b>				
Inventories	14	1,879	1,596	1,959
CO <sub>2</sub> emission rights for captive use	12	1,040	1,192	850
Income tax receivables		36	19	101
Derivatives	25.1.2	83	9	7
Trade and other financial receivables	25.1.1	3,522	6,325	3,748
Available-for-sale financial assets	25.1.3	5	4	4
Other current assets	16.2	391	416	599
Cash and cash equivalents	17	2,552	2,669	3,104
		<b>9,508</b>	<b>12,230</b>	<b>10,372</b>
<b>ASSETS CLASSIFIED AS HELD FOR SALE</b>				
		<b>12</b>	<b>12</b>	<b>16</b>
<b>TOTAL ASSETS</b>		<b>72,106</b>	<b>67,474</b>	<b>61,296</b>
<b>EQUITY</b>				
Share capital	20.1	19,165	19,165	18,698
Reserve capital	20.2	15,328	13,730	13,009
Hedging reserve	20.3	83	147	(21)
Foreign exchange differences on translation of foreign entities	20.4	(4)	3	(1)
Retained earnings		10,616	9,634	8,636
<b>EQUITY ATTRIBUTED TO EQUITY HOLDERS OF THE PARENT COMPANY</b>		<b>45,188</b>	<b>42,679</b>	<b>40,321</b>
Non-controlling interests	20.6	1,165	96	96
<b>TOTAL EQUITY</b>		<b>46,353</b>	<b>42,775</b>	<b>40,417</b>
<b>NON-CURRENT LIABILITIES</b>				
Non-current provisions	21	5,666	5,004	6,044
Loans, borrowings, bonds and lease	25.1.4	8,422	9,603	5,118
Derivatives	25.1.2	18	30	55
Deferred tax liabilities	13.2	1,250	1,191	852
Deferred income and government grants	23.1	1,038	1,141	1,192
Other financial liabilities	25.1.5	379	33	34
		<b>16,773</b>	<b>17,002</b>	<b>13,295</b>
<b>CURRENT LIABILITIES</b>				
Current provisions	21	2,404	2,181	1,809
Loans, borrowings, bonds and lease	25.1.4	1,623	411	291
Derivatives	25.1.2	106	-	34
Trade and other financial liabilities	25.1.5	3,231	3,556	3,945
Income tax liabilities		196	6	5
Deferred income and government grants	23.2	115	119	112
Other non-financial liabilities	24	1,305	1,424	1,388
		<b>8,980</b>	<b>7,697</b>	<b>7,584</b>
<b>TOTAL LIABILITIES</b>		<b>25,753</b>	<b>24,699</b>	<b>20,879</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>72,106</b>	<b>67,474</b>	<b>61,296</b>

\* restatement of comparative data is described in note 5 of these financial statements.

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Share capital	Reserve capital	Hedging reserve	Foreign exchange differences from translation of foreign entities	Retained earnings	Total	Non-controlling interests	Total Equity
Note	20.1	20.2	20.3	20.4			20.6	
<b>JANUARY 1, 2016</b>	<b>18,698</b>	<b>13,009</b>	<b>(21)</b>	<b>(1)</b>	<b>8,636</b>	<b>40,321</b>	<b>96</b>	<b>40,417</b>
Net profit for the reporting period	-	-	-	-	2,568	2,568	(2)	2,566
Other comprehensive income	-	-	168	4	200	372	-	372
<b>COMPREHENSIVE INCOME</b>	<b>-</b>	<b>-</b>	<b>168</b>	<b>4</b>	<b>2,768</b>	<b>2,940</b>	<b>(2)</b>	<b>2,938</b>
Retained earnings distribution	-	1,301	-	-	(1,301)	-	-	-
Dividend	-	-	-	-	(467)	(467)	(4)	(471)
Increase of share capital	467	(467)	-	-	-	-	-	-
Change in share in subsidiaries not resulting in loss of control	-	-	-	-	-	-	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)
<b>TRANSACTIONS WITH OWNERS</b>	<b>467</b>	<b>721</b>	<b>-</b>	<b>-</b>	<b>(1,770)</b>	<b>(582)</b>	<b>2</b>	<b>(580)</b>
<b>DECEMBER 31, 2016</b>	<b>19,165</b>	<b>13,730</b>	<b>147</b>	<b>3</b>	<b>9,634</b>	<b>42,679</b>	<b>96</b>	<b>42,775</b>
Net profit for the reporting period	-	-	-	-	2,660	2,660	7	2,667
Other comprehensive income	-	-	(64)	(7)	(82)	(153)	-	(153)
<b>COMPREHENSIVE INCOME</b>	<b>-</b>	<b>-</b>	<b>(64)</b>	<b>(7)</b>	<b>2,578</b>	<b>2,507</b>	<b>7</b>	<b>2,514</b>
Retained earnings distribution	-	1,598	-	-	(1,598)	-	-	-
Dividend	-	-	-	-	-	-	(2)	(2)
Purchase of new subsidiaries	-	-	-	-	-	-	1,067	1,067
Acquisition of additional shares in subsidiaries	-	-	-	-	2	2	(3)	(1)
<b>TRANSACTIONS WITH OWNERS</b>	<b>-</b>	<b>1,598</b>	<b>-</b>	<b>-</b>	<b>(1,596)</b>	<b>2</b>	<b>1,062</b>	<b>1,064</b>
<b>DECEMBER 31, 2017</b>	<b>19,165</b>	<b>15,328</b>	<b>83</b>	<b>(4)</b>	<b>10,616</b>	<b>45,188</b>	<b>1,165</b>	<b>46,353</b>



## CONSOLIDATED STATEMENT OF CASH FLOWS

	Note	Year ended December 31, 2017	Year ended December 31, 2016
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Profit before tax		3,290	3,274
Income tax paid		(570)	(327)
<b>Adjustments for:</b>			
Share of profit/(loss) of entities accounted for using the equity method		(40)	45
Depreciation, amortisation, disposal and impairment losses		4,030	3,864
Interest and dividend, net		151	116
(Profit) / loss on investing activities	<u>27.1</u>	132	(131)
Change in receivables	<u>27.1</u>	(434)	(275)
Change in inventories	<u>27.1</u>	115	342
Change in liabilities, excluding loans and borrowings	<u>27.1</u>	343	(169)
Change in other non-financial assets, prepayments and CO <sub>2</sub> emission rights	<u>27.1</u>	874	(96)
Change in provisions	<u>27.1</u>	117	(244)
Other		(74)	(8)
<b>NET CASH FROM OPERATING ACTIVITIES</b>		<b>7,934</b>	<b>6,391</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Proceeds from sale of property, plant and equipment and intangible assets		27	18
Acquisition of property, plant and equipment and intangible assets	<u>27.2</u>	(6,071)	(7,935)
Deposits with maturity over 3 months	<u>27.2</u>	(203)	(2,867)
Termination of deposits with maturity over 3 months	<u>27.2</u>	2,486	566
Purchase of financial assets and increase in stake in Group companies	<u>27.2</u>	(213)	(467)
Purchase of subsidiaries after offsetting acquired cash	<u>27.2</u>	(4,091)	-
Sale of subsidiaries after offsetting sold cash	<u>27.2</u>	272	-
Other		18	29
<b>NET CASH FROM INVESTING ACTIVITIES</b>		<b>(7,775)</b>	<b>(10,656)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from share of non-controlling interests		-	10
Proceeds from loans, borrowings and issue of bonds	<u>27.3</u>	192	4,652
Repayment of loans, borrowings, bonds and finance leasing	<u>27.3</u>	(193)	(203)
Dividends paid	<u>27.3</u>	(1)	(471)
Interest paid	<u>27.3</u>	(300)	(196)
Other		28	38
<b>NET CASH FROM FINANCING ACTIVITIES</b>		<b>(274)</b>	<b>3,830</b>
<b>CHANGE IN CASH AND CASH EQUIVALENTS</b>			
<i>Effect of movements in exchange rates on cash held</i>		(115)	(435)
<b>CASH AND CASH EQUIVALENTS AT THE BEGINNING OF PERIOD</b>	<u>17</u>	<b>2,666</b>	<b>3,101</b>
<b>CASH AND CASH EQUIVALENTS AT THE END OF PERIOD</b>	<u>17</u>	<b>2,551</b>	<b>2,666</b>

## GENERAL INFORMATION, BASIS FOR PREPARATION OF 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 a notarial deed of August 2, 1990, and was 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 Company's registered office is in Warsaw, Mysia 2 Street.

As at January 1, 2017 the composition of the Management Board was as follows:

- Henryk Baranowski – the President of the Management Board,
- Marta Gajęcka – Vice- the 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 Wasilek – the Vice-President of the Management Board,
- Emil Wojtowicz – the Vice-President of the Management Board.

On February 13, 2017, the Supervisory Board dismissed all members of the Management Board as of February 13, 2017. At the same time, on February 14, 2017, the Supervisory Board appointed for the 10th term of the Management Board Henryk Baranowski as President of the Management Board as well as Bolesław Jankowski, Wojciech Kowalczyk, Marek Pastuszko, Paweł Śliwa, Ryszard Wasilek and Emil Wojtowicz as Vice-Presidents of the Management Board.

On June 20, 2017, Bolesław Jankowski resigned effective from July 1, 2017.

As at December 31, 2017 and on the date on which these financial statements were published, the Company's Management Board was as follows:

- Henryk Baranowski – the 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 Wasilek – the Vice-President of the Management Board,
- Emil Wojtowicz – the Vice-President of the Management Board.

#### Ownership structure

The parent's ownership structure was as follows:

	State Treasury	Other shareholders	Total
As at December 31, 2016	57.39%	42.61%	100.00%
As at December 31, 2017	57.39%	42.61%	100.00%

The ownership structure as at particular reporting dates was prepared on the basis of data available to the Company.

According to information known to the Company as of the date on which these financial statements were prepared, the State Treasury was the only shareholder with at least 5% of votes at the general meeting of PGE S.A.

#### 1.2 Information on PGE Group

PGE Group ("PGE Group," "PGE Capita Group" "Group", "CG PGE") includes the parent, PGE Polska Grupa Energetyczna S.A., 58 consolidated subsidiaries, 3 associates and 1 jointly controlled entity. As described in note 33, in the present period the Group acquired significant control over Polimex-Mostostal S.A. and EDF's companies in Poland and consolidated them using the equity method. For additional information about subordinated entities 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, 2017 to December 31, 2017 ("financial statements", "consolidated financial statements") and include comparative data for the period from January 1, 2016 to December 31, 2016.

The financial statements of all subordinated entities were prepared for the same reporting period as the financial statements of the parent company, using consistent accounting principles. Companies acquired in the course of the year were the exception, preparing financial data for the period from the moment when PGE Group obtained control.



PGE Group companies' core activities are as follows:

- production of electricity,
- distribution of electricity,
- wholesale and retail trade in electricity, energy origin rights, CO<sub>2</sub> emission rights and gas,
- production and distribution of heat,
- rendering of other services related to these 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.

## 1.3 Structure of the PGE Group

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

Entity	Entity holding share	Share of the Group entities as at December 31, 2017	Share of the Group entities as at December 31, 2016
<b>SEGMENT: SUPPLY</b>			
1. PGE Polska Grupa Energetyczna S.A. Warsaw	Parent		
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%
6. PGE Paliwa sp. z o.o. (formerly EDF Paliwa sp. z o.o.) Kraków	PGE Energia Ciepła S.A.	100.00%	-
<b>SEGMENT: CONVENTIONAL GENERATION</b>			
7. PGE GiEK S.A. Bełchatów	PGE Polska Grupa Energetyczna S.A.	100.00%	99.98%
8. PGE Energia Ciepła S.A. (formerly EDF Polska S.A.) Warsaw	PGE Polska Grupa Energetyczna S.A.	99.52%	-
9. PGE Toruń S.A. (formerly EDF Toruń S.A.) Toruń	PGE Energia Ciepła S.A.	95.22%	-
10. PGE Gaz Toruń sp. z o.o. (formerly EDF Gaz Toruń sp. z o.o.) Warsaw	PGE Energia Ciepła S.A.	50.04%	-
11. Zespół Elektrociepłowni Wrocławskich KOGENERACJA S.A. Wrocław	PGE Energia Ciepła S.A. Investment III B.V.	17.74% 32.26%	- -
12. Elektrociepłownia Zielona Góra S.A. Zielona Góra	Zespół Elektrociepłowni Wrocławskich KOGENERACJA S.A.	98.40%	-
13. ELBIS sp. z o.o. Rogowiec	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
14. MEGAZEC sp. z o.o. Bydgoszcz	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
15. MegaSerwis sp. z o.o. Bogatynia	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
16. ELMEN sp. z o.o. Rogowiec	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
17. "Przedsiębiorstwo Usługowo-Produkcyjne „ELTUR-SERWIS” sp. z o.o. Bogatynia"	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
18. Przedsiębiorstwo Usługowo-Produkcyjne „TOP SERWIS” sp. z o.o. Bogatynia	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
19. Przedsiębiorstwo Transportowo-Sprzętowe „BETRANS” sp. z o.o. Bełchatów	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
20. Przedsiębiorstwo Wulkanizacji Taśm i Produkcji Wyrobów Gumowych BESTGUM POLSKA sp. z o.o. Rogowiec	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
21. RAMB sp. z o.o. Piaski	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
22. EPORE sp. z o.o. Bogatynia	PGE Górnictwo i Energetyka Konwencjonalna S.A.	85.38%	85.38%

Entity	Entity holding share	Share of the Group entities as at December 31, 2017	Share of the Group entities as at December 31, 2016
23. „Energoserwis – Kleszczów” sp. z o.o. Rogowiec	PGE Górnictwo i Energetyka Konwencjonalna S.A.	51.00%	51.00%
24. Przedsiębiorstwo Energetyki Ciepłej sp. z o.o. Zgierz	PGE Górnictwo i Energetyka Konwencjonalna S.A.	50.98%	50.98%
<b>SEGMENT: RENEWABLES</b>			
25. PGE Energia Odnawialna S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
26. Elektrownia Wiatrowa Baltica-1 sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
27. Elektrownia Wiatrowa Baltica-2 sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
28. Elektrownia Wiatrowa Baltica-3 sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
PGE Energia Natury sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	-	100.00%
29. PGE Energia Natury PEW sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
30. PGE Klaster sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	-
<b>SEGMENT: DISTRIBUTION</b>			
31. PGE Dystrybucja S.A. Lublin	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
<b>SEGMENT: OTHER OPERATIONS</b>			
32. PGE EJ 1 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	70.00%	70.00%
33. PGE Systemy S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
EXATEL S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	-	100.00%
34. PGE Sweden AB (publ) Stockholm	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
35. Investment III B.V. (formerly EDF Investment III B.V.) Amsterdam	PGE Energia Ciepła S.A.	100.00%	-
36. PGE Obsługa Księgowo-Kadrowa sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
37. „Elbest” sp. z o.o. Bełchatów	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
38. Elbest Security sp. z o.o. Bełchatów	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
39. PGE Inwest 2 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
40. PGE Inwest 5 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
41. PGE Centrum sp. z o.o. (formerly PGE Inwest 6 sp. z o.o.) Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
42. PGE Ventures sp. z o.o. (formerly PGE Inwest 7 sp. z o.o.) Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
43. PGE Inwest 8 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
44. PGE Inwest 9 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
45. PGE Inwest 10 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
46. PGE Inwest 11 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
47. PGE Inwest 12 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
48. PGE Inwest 13 S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
49. PGE Inwest 14 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
50. PGE Nowa Energia sp. z o.o. (formerly PGE Inwest 15 sp. z o.o.) Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
51. PGE Inwest 16 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
52. PGE Inwest 17 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%

Entity	Entity holding share	Share of the Group entities as at December 31, 2017	Share of the Group entities as at December 31, 2016
53. PGE Inwest 18 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
54. PGE Inwest 19 sp. z o.o. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	-
55. PGE Towarzystwo Funduszy Inwestycyjnych S.A. Warsaw	PGE Polska Grupa Energetyczna S.A.	100.00%	100.00%
ENERGO-TEL S.A. Warsaw	EXATEL S.A.	-	100.00%
56. BIO-ENERGIA sp. z o.o. Warsaw	PGE Energia Odnawialna S.A.	100.00%	100.00%
57. Przedsiębiorstwo Transportowo-Usługowe „ETRA” sp. z o.o. Białystok	PGE Dystrybucja S.A.	100.00%	100.00%
58. Energetyczne Systemy Pomiarowe sp. z o.o. Białystok	PGE Dystrybucja S.A.	100.00%	100.00%
59. PGE Ekoserwis sp. z o.o. (formerly EDF Ekoserwis sp. z o.o.) Wrocław	PGE Energia Ciepła S.A.	84.15%	-

The table above includes the following changes in the structure of PGE Group companies subject to full consolidation which took place during 2017:

- On February 1, 2017 PGE Polska Grupa Energetyczna S.A. formed PGE Inwest 19 sp. z o.o. The company was registered at the National Court Register on February 24, 2017.
- On March 29, 2017, an agreement was executed to sell 100% of EXATEL S.A. shares. Along with the sale of EXATEL S.A., the Group lost control over its subsidiary ENERGO-TEL S.A.
- The transaction between PGE Polska Grupa Energetyczna S.A. and EDF International SAS and EDF Investment II B.V. concerning the sale of EDF's assets in Poland pursuant to a Conditional Share Sale Agreement of May 19, 2017, was finalised on November 13, 2017. As a result of the transaction, PGE S.A. acquired direct and indirect control over the following companies:
  - EDF Polska S.A. (currently PGE Energia Ciepła S.A.)
  - EDF Investment III B.V. (currently Investment III B.V.)
  - EDF Paliwa sp. z o.o. (currently PGE Paliwa sp. z o.o.)
  - EDF Toruń S.A. (currently PGE Toruń S.A.)
  - EDF Ekoserwis sp. z o.o. (currently PGE Ekoserwis sp. z o.o.)
  - EDF Gaz Toruń sp. z o.o. (currently PGE Gaz Toruń sp. z o.o.)
  - Zespół Elektrociepłowni Wrocławskich KOGENERACJA S.A.
  - Elektrociepłownia Zielona Góra S.A.

The Group's share in capital and voting rights of the above companies as of November 13, 2017, was the same as PGE Group's % stake presented in the table above as at December 31, 2017. Details of the transaction are presented in note 33.3 to these financial statements.
- On November 30, 2017, the merger of PGE Energia Odnawialna S.A. (the acquiring company) and PGE Energia Natury sp. z o.o. (the acquired company) was registered at the National Court Register. The merger had no impact on these financial statements.
- On November 17, 2017, a founding act for PGE Klaster sp. z o.o. was signed. The company was registered at the National Court Register on December 6, 2017.

## 1.4 Accounting for new acquisitions

### Accounting for acquisition of EDF companies in Poland

As described in note 33.3 to these financial statements, the transaction between PGE Polska Grupa Energetyczna S.A. and EDF International SAS and EDF Investment II B.V. concerning the sale of EDF's assets in Poland pursuant to a Conditional Share Sale Agreement of May 19, 2017, was finalised on November 13, 2017.

Pursuant to IFRS 3, PGE Group should finish accounting for the acquisition within 12 months from the acquisition date. Given that control over these companies was acquired in mid-November 2017, these financial statements include a preliminary accounting for the acquired assets and assumed liabilities of these entities. The key adjustments intended to bring this assets and liabilities to fair value as at the acquisition date concerned:

- Adjustment of value of property, plant and equipment and intangible assets at Rybnik Power Plant. Based on financial projections available to the Group, these assets were assigned a zero value as at the acquisition date.
- Measurement of additional provisions.
- Elimination of select deferred revenue items.
- Appropriate adjustment of deferred tax resulting from recognition of above adjustments.

Aside as described above, the adjustments in the value of Rybnik Power Plant as at the date on which these financial statements were prepared, no measurement of the fair value of the acquired tangible and intangible assets was performed. For the purposes of initial recognition, book values from the acquired entities' financial statements were taken.

The following table presents a summary of the recognised assets and liabilities as at the acquisition date.

	Value as at November 13, 2017
Property, plant and equipment and intangible assets	4,710
Other prefixed assets	951
Inventories	398
Cash	186
Other current assets	1,166
<b>Total assets</b>	<b>7,411</b>
Loans and borrowings	2,839
Provisions	478
Other liabilities	1,759
<b>Total liabilities</b>	<b>5,076</b>
<b>Net assets of acquired entities</b>	<b>2,335</b>

The following table presents preliminary accounting for the acquisition and goodwill arising on consolidation.

	Value as at November 13, 2017
Net assets of acquired entities	2,335
Net assets attributable to non-controlling interests	(1,067)
Exclusion of liabilities (subrogation)	2,285
<b>PGE Group's stake in net assets of acquired entities</b>	<b>3,553</b>
Cash transferred	1,992
Subrogation of liabilities	2,285
<b>Total acquisition price</b>	<b>4,277</b>
<b>Goodwill arising on consolidation</b>	<b>724</b>

The goodwill recognised by PGE Group arises from the fact that in accordance with PGE Group's assumptions discounted cash flows from operating activities that will be generated by the acquired assets will be higher than the net asset value of the acquired companies, established in accordance with IFRS 3. The final amount of goodwill should be lower due to a planned measurement of property, plant and equipment and intangible assets.

The goodwill recognised does not constitute goodwill for tax purposes.

### Results of acquired entities

From November 13, 2017, to December 31, 2017, the share of the acquired companies in PGE Group's results was as follows:

- Share in consolidated revenue PLN 837 million (after consolidation exclusions)
- Share in comprehensive income PLN 129 million (after consolidation exclusions)

Throughout 2017, the acquired entities recorded revenue from sale of PLN 6,893 million (without consolidation exclusions) and a loss of PLN 474 million (without consolidation exclusions). The loss resulted largely from the recognition of impairment losses on the generation assets at the Rybnik plant, which did not burden PGE Group's results. Without taking these impairment losses into account, the acquired entities would have posted PLN 593 million in 2017 (without consolidation exclusions).

### Accounting for acquisition of Polimex-Mostostal S.A.

In 2017, PGE S.A. acquired 16.48% of shares and thus gained significant influence over Polimex-Mostostal S.A. The acquired assets were recognised in the current period.

	Value as at December 31, 2016
<b>Purchase price paid for 16.48% stake</b>	<b>81</b>
Fair value of identified net assets	393
PGE's share in these assets	65
<b>Goodwill</b>	<b>16</b>

Because Polimex-Mostostal S.A.'s market capitalisation as at December 31, 2017, was higher than the valuation using the equity method, no indications of impairment were noted.

## 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 millions (PLNm), 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, 2017	December 31, 2016
USD	3.4813	4.1793
EUR	4.1709	4.4240

## 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, 2017:

Standard	Description of changes	Effective date
IFRS 9 <i>Financial Instruments</i> and subsequent amendments	Changes to the classification and measurement requirements. Changes to hedge accounting. These changes apply to the right of early repayment with negative fees.	January 1 2018 / January 1 2019
IFRS 14 <i>Regulatory Deferral Accounts</i>	Accounting and disclosure principles for regulatory deferral accounts.	Standard in the current version will not be effective in the EU
Amendments to IFRS 10 and IAS 28	Deals with the sale or contribution of assets between an investor and its joint venture or associate.	Postponed indefinitely
IFRS 15 <i>Revenue from Contracts with Customers and clarifications to IFRS 15</i>	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 <i>Leases</i>	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
IFRS 17 <i>Insurance contracts</i>	Defines a new approach to recognising revenue and profit/loss in the period in which insurance services are provided	January 1, 2021
Amendments to IFRS 2	Classification and measurement of share-based payment transactions	January 1, 2018
Amendments to IFRS 4	Application of IFRS 9 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; 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
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 <i>Foreign Currency Transactions and Advance Consideration</i>	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
IFRIC 23 <i>Uncertainty over income tax treatments</i>	This interpretation applies to establishing taxable revenue, tax base, unsettled tax losses, unused tax rebates and tax rates.	January 1, 2019
Amendments to IAS 28	This amendment concerns measurement of non-current investments in associates	January 1, 2019
Annual improvements to IFRS (cycle 2015-2017)	A collection of amendments dealing with: IFRS 3 - measurement of existing stake in a joint operation; IFRS 11 - no measurement of existing stake in a joint operation; IFRS 12 - income tax consequences of dividends; IAS 23 - financing costs when an asset is ready for its intended use.	January 1, 2019
Amendments to IAS 19	Amendments concern defined-benefit plans.	January 1, 2019

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.

## Impact of new regulations on PGE Group's consolidated financial statements

### IFRS 9 Financial Instruments

In July 2014, the IASB published IFRS 9 Financial Instruments (IFRS 9). IFRS 9 covers three aspects related to financial instruments: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted.

The Group plans to use IFRS 9 from the date it enters into force, without restating its comparative data.

In 2017, the Group carried out a detailed analysis of the impact of IFRS 9 on the Group's accounting principles as it relates to the Group's operations or financial results. This assessment is based on currently available information and may be subject to changes based on rational and possible to evidence additional information obtained in the period in which the Group applies IFRS 9 for the first time.

The Group does not expect that implementation of IFRS 9 will have a significant impact on its financial situation and equity, except for the recognition and calculation of the impairment allowance. The Group expects a slight increase in impairment losses, with a negative impact on equity, as discussed below. Moreover the classification of certain financial instruments will change.

The analysis shows that changes will mostly affect the following areas:

- Classification of financial instruments - the existing four categories resulting from IAS 39 Financial Instruments: Recognition and Measurement will be replaced with three categories: financial assets measured at amortised cost, at fair value through profit or loss and at fair value through other comprehensive income. This will result in presentation changes in financial statements but will have no impact on the Group's financial results.
- Rules for estimating and recognition of impairment losses on financial assets (transition from incurred loss model to expected loss model):
  - for trade receivables from significant clients that are subject to a credit risk assessment procedure, the Group will estimate expected credit losses based on a model used to evaluate this risk on the basis of ratings assigned to counterparties; ratings have a likelihood of default assigned, which is adjusted to reflect impact of macroeconomic factors;
  - for receivables from other clients and from related parties, the Group will estimate expected credit losses based on an analysis of the likelihood of credit losses in each ageing structure;
  - for deposits in banks, the Group will estimate expected credit losses based on a model used to evaluate this risk on the basis of ratings assigned to banks by external institutions; ratings have a likelihood of default assigned, which is adjusted to reflect impact of macroeconomic factors;
  - for investments in other equity instruments, measurement will be at fair value; currently the Group does not have significant investments in equity instruments other than shares in subsidiaries and associates.

Impairment of financial assets according to the above-mentioned rules as at December 31, 2017 would have been approx. PLN 4 million higher than those recognised in these financial statements. Equity as at December 31, 2017 would have decreased by about PLN 4 million gross, (with no impact on deferred tax).

Moreover, after analysis, the Group decided not to implement the changes resulting from IFRS 9 referring to hedge accounting from January 1, 2018.

### IFRS 15 Revenue from Contracts with Customers

IFRS 15 Revenue From Contracts with Customers, issued in May 2014 and amended in April 2016, introduces the Five Step Model for recognising revenue from contracts with customers. Revenue in IFRS 15 is recognised in the amount that - according to the entity's expectations - is due in exchange for delivery of the goods or services to the customer.

The new standard will replace all existing requirements concerning revenue recognition in compliance with IFRS. The standard is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted.

The Group analysed the largest contracts with its customers in order to identify those that include provisions which could potentially have an impact on the moment of revenue recognition and the level of revenue in the given reporting period, in particular concerning: contracts for the sale of electricity and gaseous fuel, multi-component contracts, mutually linked contracts and contracts containing the entity's commitment to deliver products or services to the client by another entity (intermediary vs principal), variable remuneration, trade bonuses as well as contractual penalties and bonuses.



The analysis shows that changes will mostly affect the following areas:

- Revenue from connections to distribution network. Currently, revenues from connection fees are recognized at one time when they become due i.e. at the moment of connection. According to PGE Group, the new standard does not change this approach. However connection fees that prior to IFRIC 18 *Transfers of Assets from Customers*, i.e. prior to July 1, 2009, had been recognised as prepayments and settled over time, starting from January 1, 2018 they will be recognised at once as retained earnings. This adjustment reduces the amount of deferred income and increases the amount of retained earnings as at December 31, 2017, by PLN 647 million gross, i.e. without taking into account deferred tax impact. Acting as payers for the transition fee and renewables fee, which are collected from end users by PGE Dystrybucja S.A. and PGE GiEK S.A. and then given to the Transmission System Operator ("TSO"). Both fees constitute a sort of energy quasi-tax, collected from recipients of electricity by PGE Dystrybucja on behalf of the TSO and therefore should not be treated as revenue in accordance with IFRS 15. The recognition of net revenue and expenses related to the transition and renewables fees in the financial statements for 2017 would have decreased operating revenue and expenses by approx. PLN 701 million.
- PGE Obrót S.A. acting as intermediary for gas distribution and transmission services. PGE Obrót has no influence over the key parameters of the services - this is governed by existing regulations concerning terms for the distribution of gas fuel. PGE Obrót is not responsible for failure to perform, or incorrect performance, of framework agreements to provide gas fuel distribution and transmission services. It also does not bear the risk of storing inventories prior to this service being provided to the client. It has no influence over the prices of distribution and transmission services. Given the above, in accordance with IFRS 15, revenue and costs related to distribution and transmission services will be recognised in net values. The recognition of net revenue and expenses related to distribution and transmission services in the financial statements for 2017 would have decreased operating revenue and expenses by approx. PLN 25 million.
- Revenue from compensations received by PGE Dystrybucja S.A. in connection with damages to production assets will be recognised in other operating revenue. Pursuant to IFRS 15, this revenue does not meet the definition of revenue from sales therefore it should not be treated as such. Revenue from compensations that would have been subject to reclassification in the financial statements for 2017 amounts to over PLN 7 million.

#### IFRS 16 Leases

The new standard changes principles for the recognition of contracts which meet the criteria of 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 recognised as a finance lease. Adoption of the standard will have the following effect:

- in the statement of financial position: increase of non-financial non-current assets and financial liabilities,
- in the statement of comprehensive income: decrease of operating expenses (other than depreciation/amortisation), increase of depreciation/amortisation and finance costs.
- increase in net debt and net debt to EBITDA due to proportionally higher increase in financial liabilities than decrease in operating expenses other than depreciation

PGE is currently analysing the potential impact of IFRS 16 on its future financial statements. The analysis is especially focusing on the issue of potential impact of the standard on the receipt of free perpetual usufruct rights to land. In accordance with PGE Group's existing accounting policy, rights to perpetual usufruct of land were not recognised as contracts containing a lease component. Analysis of the standard is not finished yet but its application should not have a major impact on the Group's future financial statements.

#### Other standards

The other standards and amendments should not have a major impact on PGE Group's future financial statements.

### 2.4 Professional judgment of management and estimates

In the process of applying accounting rules with regards to the following issues, management has made judgements and estimates that affect the amounts presented in the 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.

#### Recoverable amount of property, plant and equipment, intangible assets 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. Estimates of recoverable amount of goodwill are 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, 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. The impairment test carried out on PGE Group's selected assets is described in note 3 to these financial statements.

### Depreciation/amortisation period for 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. Capitalised 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 are presented in notes 4.8 and 4.9.

The verification of the economic useful lives of property, plant and equipment and intangible assets conducted in 2017 resulted in an increase in the depreciation and amortisation costs for 2017 by approx. PLN 3 million.

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

The capitalisation 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 2017 caused an increase in costs of PLN 42 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

The 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.

### Measurement 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, 2017	As at December 31, 2016
Expected inflation rate (%)	1.8%	1.30-1.80%
Discount rate (%)	3.4%	3.5%
Expected salary growth rate (%)	0.00-4.29%	0.00-3.57%
Employee turnover (%)	0.27-9.57%	0.24 - 9.41%
Expected medical care costs growth rate (%)	1.8%	1.30-1.80%
Expected Social Fund (ZFS) allowance growth rate (%)	3.5%-5.0%	3.50-8.40%

- The probability of employee attrition has been predicted on the basis of historical data related to 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 the Group'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 3.4% was adopted (December 31, 2016: 3.5%), which corresponds to the profitability of long-term Treasury bonds listed on the Polish capital market.

### Other provisions

As described in note 4.21 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. Aside from the above, the most important provisions are:

- CO<sub>2</sub> 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, PGE Group estimates the probability of occurrence of potential liabilities. If the occurrence of unfavourable future event is probable, PGE Group recognises a provision in the appropriate amount. If the occurrence of unfavourable future event is estimated by PGE Group as not probable but possible, a contingent liability is recognised.

Detailed information on contingent liabilities and legal claims and disputes is presented in note 28 of these financial statements.

### Impairment of receivables

As at the reporting date PGE 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, PGE Group recognises an impairment allowance to the amount of the present value of expected cash flows.

Description of changes in impairment allowances on trade and other receivables is described in note 25.1.1 of these financial statements.

### Electricity sales accrual

Readings 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, 2017 is described in note 25.1.1 of these financial statements.

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

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 transaction 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, 2017, PGE Group acquired EDF's assets in Poland. As a result of initial recognition, goodwill of PLN 724 million was recognised. In addition, PGE Group during the current year began exercising significant influence over Polimex Mostostal S.A. The acquisition resulted in goodwill of PLN 16 million. This goodwill is recognised in the carrying amount of the investment. Details of the transaction are presented in note 1.4 to these financial statements.

### Uncertainty concerning tax settlements

Regulations concerning tax on goods and services, corporate income tax and burdens related to social insurance are subject to changes. These frequent changes result in a lack of reference points, inconsistent interpretations and few precedents that can be applied. The existing regulations also contain uncertainties that result in differing opinions as to legal interpretation of tax regulations both between state organs and between state organs and companies.

Tax settlements and other activity areas are conditioned by regulations (customs or currency controls) and can be subject to controls of respective authorities that are authorised to issue fines and penalties, and all additional tax liabilities resulting from such audits must be paid with high interest. This means that tax risk in Poland is higher than in countries with more stable tax systems.

As a consequence, the amounts presented and disclosed in financial statements may change in the future as a result of a final decision by a tax control organ.

On July 15, 2016, changes were introduced to the Tax Ordinance intended to take into account the provisions of General Anti-Abuse Rule (GAAR). GAAR is intended to prevent the formation and use of artificial legal structures created in order to avoid paying tax in Poland. GAAR defines tax avoidance as an activity performed primarily to obtain a tax benefit contrary under the circumstances to the subject and aim of the tax law. According to GAAR, such an activity does not result in a tax benefit if it is artificial. All proceedings regarding unjustified division of operations, involving intermediaries despite a lack of economic justification, mutually offsetting elements or other similar activities may be treated as a condition for the existence of artificial activities subject to GAAR. These new regulations will require a much greater judgement in assessing the tax effects of transactions.

The GAAR clause is to be applied in relation to transactions executed after its entry into force and to transactions that were executed prior to its entry into force but in the case of which tax benefits were or continue to be obtained after GAAR went into force. The implementation of these regulations will make it possible for Polish tax inspection authorities to question legal arrangements and agreements made by taxpayers such as group restructuring and reorganisation.

The Group recognises and measures current and deferred income tax assets and liabilities using IAS 12 Income tax based on profit (tax loss), tax base, unsettled tax losses, unused tax exemptions and tax rates, taking into account assessment of uncertainties related to tax settlements. If there is uncertainty over where or not and in what scope the tax authority will accept tax accounting for transactions, the Group recognises these settlements taking into account an uncertainty assessment.

### Impact of changes in select estimates on the statement of comprehensive income for 2017

	Impairment losses on property, plant and equipment, intangible assets	Change in actuarial provisions	Change in rehabilitation provision	Change in N:W ratio	Verification economical useful e life
<b>REVENUE FROM SALE</b>	-	-	-	-	-
Cost of goods sold	(957)	(58)	-	(42)	(3)
<b>GROSS PROFIT/(LOSS) ON SALES</b>	<b>(957)</b>	<b>(58)</b>	-	<b>(42)</b>	<b>(3)</b>
Distribution and selling expenses	-	(5)	-	-	-
General and administrative expenses	(37)	(8)	-	-	-
Other operating revenue	2	-	-	-	-
Other operating costs	-	-	(42)	-	-
<b>OPERATING PROFIT / (LOSS)</b>	<b>(992)</b>	<b>(71)</b>	<b>(42)</b>	<b>(42)</b>	<b>(3)</b>
<b>PROFIT/(LOSS) BEFORE TAX</b>	<b>(992)</b>	<b>(71)</b>	<b>(42)</b>	<b>(42)</b>	<b>(3)</b>
<b>Other comprehensive income</b>	-	<b>(101)</b>	-	-	-

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

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

In previous reporting periods, PGE Group recognized substantial impairment allowances of property, plant and equipment of Conventional Generation segment and the Renewables segment. In the current reporting period, the Group analysed impairment indications and identified factors that could result in changes to the asset values in the above segments.

#### Regulatory assumptions

- Entry into force on September 25, 2017, of updated Act on Renewables. The Act on Renewables changed the wording of art. 56, i.e. method for calculating substitute fees so that a unit substitute fee amounts to 125% of the annual average weighted price of property rights resulting from origin certificates (green certificates). Until now, the unit substitute fee was established through a decision of the President of the Energy Regulatory Office. Given the current prices of green certificates, the change in the updated Act on Renewables significantly reduced the substitute fee, which translated into further declines in market prices. This change made pricing terms for the contract executed with Enea S.A. for delivery of green certificates from Szczecin Power Plant in the Conventional Generation segment and wind farms in the Renewables segment substantially worse. It also has significant impact on forecast market prices for property rights. In combination with a persistent market oversupply of green certificates, which results in significant price declines, this reduces expected revenue and margins on generation from renewable sources.
- Adoption by the Parliament on July 20, 2017 of the Water Law The act introduces new rules for water usage. In particular, the law introduces fees (fixed and variable) for using water and introduces higher maximum rates for water consumption and discharge of waste through installations belonging to PGE Group companies. These quasi-fiscal fees are a new expense for PGE Group's generating units.
- Reduction of support for gas-fired generating units after 2018 vs assumptions adopted in 2015. This results from a significant decline in the prices of yellow certificates.
- Lack of support for coal-fired CHP plants under the capacity market due to regulations introduced via the capacity market law of December 8, 2017.
- Proposed legislative changes concerning the law on investment in wind farms of May 20, 2016, indicate that there are positive prospects for wind farm maintenance costs in the Renewables segment.<sup>1</sup> The draft law changes the definition of a structure by re-introducing the definition contained in the Construction Law of July 7, 1994, which in accordance with the draft's justification should clear up interpretation doubts with regard to property tax bases for wind farms, which arose after January 1, 2017. If the Act is changed in the aforementioned scope, wind farms will not be considered entirely as structures, which will translate into lower property tax expenses.

#### Macroeconomic assumptions

The key price assumptions, i.e. prices of electricity, certificates of origin, CO<sub>2</sub> emission rights, hard coal, until 2019 are based on the company's financial plans.

Electricity price forecasts from 2020 are derived from a study prepared by an independent expert. The most probable energy price forecast was adopted, although in the part covered by contracts the prices and settlement terms used in these contracts during their validity were adopted. Electricity price forecasts assume growth in market prices during the forecast period.

The forecast for prices of property rights concerning certificates of origin was drafted by PGE S.A.'s team of in-house experts. Property right prices will be established by a demand-supply balance. It was assumed that auctions should be the dominant support mechanism. The forecast for prices of property rights concerning certificates of origin for renewable energy assume growth until 2021. In later years, prices will be in decline until 2025 (except for 2023) and will remain steady thereafter. For production covered by contracts the prices and settlement terms used in these contracts during their validity were adopted.

The forecast for revenue from the capacity market from 2021 was prepared by PGE S.A.'s in-house team based on results of the British capacity market, among other things.

Revenue from regulatory system services was based on existing bilateral agreements with PSE S.A.

Unit availability was estimated based on repair plans, taking into account statistical failure rates.

As a result of the above changes and other possible changes in macroeconomic factors, PGE Group is forecasting a decrease in cash flows generated in the future and identifying a risk of impairment at some of its conventional and renewable generation assets.

<sup>1</sup> Draft act on amendment of act on renewables and certain other acts of June 16, 2017.

### 3.1 Analysis of impairment of the power generating assets of Conventional segment

Impairment tests were conducted on November 30, 2017, on cash generating unit basis by establishing their recoverable amounts. Determining fair value for very large groups of assets for which there is no active market and there are few comparable transactions is very difficult in practice. In the case of power plants and mines for which a value on the local market should be determined there are no observable fair values. Given the above, the recoverable value of the analysed assets was estimated on the basis of discounted net cash flow method which relied on financial projections prepared for the period from December 2017 to 2030. For conventional power generating units with expected periods of economic useful life in excess of 2030, a residual value was determined for the remaining service time. According to the Company, financial projections longer than five years are justified due to significant and long-term effects of projected changes in the regulatory environment. Using longer projections, recoverable amounts may be determined more reliably.

#### Detailed segment assumptions

Presented below are the key assumptions having impact on estimates of the useful value of CGU:

- classification as CGU of the following:
  - Branch KWB Bełchatów and Branch Elektrownia Bełchatów ("Bełchatów complex").
  - Branch KWB Turów and Branch Elektrownia Turów ("Turów complex").

given the technological and economic links between these branches,

- classification as three separate CGUs Dolna Odra Power Plant, Szczecin Power Plant and Pomorzany Power Plant, which are part of Branch Zespół Elektrowni Dolna Odra
- assumptions concerning electricity production and demand until 2022 were based on a financial plan,
- forecasts for prices of CO<sub>2</sub> emission allowances, assuming dynamic growth in market prices in the years to come (even over a dozen percent year-on-year in constant prices),
- forecasts for hard coal prices, assuming strong growth in market prices in 2018-2019, resulting from lower supply; in 2020 the end of problems with limited supply was foreseen, resulting in a decline in coal prices; up from 2021 prices are expected to stabilise (growth by approx. 1% y/y in fixed prices),
- receipt of a quantity of free-of-charge CO<sub>2</sub> emission allowances for the purposes of electricity generation for 2018-2020 for specific cash generating units in accordance with Poland's application for a transition allocation of free emission allowances for the modernisation of electricity generation activities pursuant to art. 10c sec. 5 of directive 2003/87/EC of the European Parliament and the Council (derogation application), which meets the requirements of Commission Decision of July 13, 2012. As regards heat generation, free-of-charge allowances were taken into account in accordance with the list of quantities of CO<sub>2</sub> emission allowances allocated for heat for 2013-2020 published by the Environment Ministry,
- take into account the allocation of free CO<sub>2</sub> emission allowances in the period 2021-2030 only for system district heating and high-efficiency cogeneration, based on the 2020 level and assuming annual reduction by 2.2%,
- take into account the support system for high-efficiency gas cogeneration in the entire forecast period and the end of the support system for coal high-efficiency cogeneration in 2018,
- take into account work cost optimisation resulting from current work plans, among other things,
- maintain production capacities as a result of replacement-type investments,
- take into account development investments for which construction work has begun,
- adopt WACC for the projection period at 7.56%.

It should also be added that as of December 31, 2017, and at the of date on which these financial statements were prepared, no specific projects and plans existed for the Polish market related to the method and deadline for entry into force of support mechanisms for gas-fired generation sources after 2018. Nonetheless, according to the Company, the adoption of such assumptions is justified given the expected changes in the regulatory framework. The assumptions that are reflected in cash flows constitute a real scenario in terms of method and period, according to the Company. However, it cannot be ruled out that the final shape and period for these solutions will be different from the assumptions.



Presented below are the results of tests on CGUs as at November 30, 2017.

As at November 30, 2017	Assets value before impairment	Impairment loss	Value after impairment
Bełchatów complex	15,514	-	15,514
Opole Power Plant	11,056	-	11,056
Turów complex	2,685	-	2,685
Gorzów CHP	734	-	734
Szczecin Power Plant	473	(473)	-
Rzeszów CHP	367	-	367
Lublin-Wrotków CHP	357	(155)	202
Pomorzaný Power Plant	69	(69)	-
Dolna Odra Power Plant	58	-	58
Kielce CHP	23	-	23
Bydgoszcz CHP	7	-	7
Zgierz CHP	4	-	4
<b>TOTAL</b>	<b>31,347</b>	<b>(697)</b>	<b>30,650</b>

Presented above tested value is the net book value of identifiable assets, less rehabilitation provision as at that date.

As a result of the test, the Group identified a PLN 697 million loss of value of its generation assets. In addition, during 2017 the Group recognised PLN 146 million impairment losses. An impairment loss of PLN 843 million was recognised in operating expenses in the statement of comprehensive income.

### 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. Useful value is to a lesser extent influenced by changes in the cost to purchase hard coal, prices of CO<sub>2</sub> emission allowances and changes in expected rates on the capacity market.

Presented below is the impact of changes in key assumptions on asset impairment as at November 30, 2017.

Parameter	Change	Impact on impairment loss	
		Increase in impairment loss	Decrease in impairment loss
Change in electricity prices throughout the forecast period	1%	-	836
	-1%	836	-
Change in WACC	+ 0,5 p.p.	1,215	-
	- 0,5 p.p.	-	884
Change in CO <sub>2</sub> emission allowance prices during forecast period	1%	196	-
	-1%	-	196
Assumptions regarding the capacity market	capacity market +5%	-	247
	capacity market -5%	247	-
Change in hard coal price throughout forecast period	5%	0.3	-
	-5%	-	0.1

### 3.2 Analysis of impairment of the power generating assets of Renewables segment

Impairment tests were conducted on December 31, 2017, on cash generating unit basis by establishing their recoverable amounts. The recoverable value of the analysed assets was estimated on the basis of discounted net cash flow method which relied on the financial projections prepared for the assumed useful life of the particular CGU in the case of wind farms or for 2018-2037 in the case of other CGUs. According to the Group, financial projects longer than five years are justified because the property, plant and equipment used by the tested entities have significant longer useful lives and also due to significant and long-term effects of projected changes in the regulatory environment.

### Detailed segment assumptions

The key assumptions having impact on estimates of the useful value of CGU presented below are:

- classification as CGU of the following:
  - Pumped-storage power plants
  - Other hydropower plants
  - Wind farms
- production of electricity and property rights was estimated based on historic data and expert estimates prepared for investment purposes, adjusted by the availability of units;
- recognition of cash flows concerning contractual penalties and damages awarded in disputes with Enea S.A. and Energa Obrót S.A. as described in Note 28, in amounts resulting from the contracts or calculated as the difference between the contract prices of property rights and market prices;
- decline in property tax expenses up from 2019;
- maintain production capacities as a result of replacement-type investments,
- adopt WACC for the projection period at 7.56%.

### Impairment of the power generating assets of Renewables segment

Presented below are the results of tests on CGUs as at December 31, 2017.

As at December 31, 2017	Assets value before impairment	Impairment loss	Value after impairment
<b>Renewables segment generating units</b>			
Pumped-storage power plants	747	-	747
Other hydropower plants	304	-	304
Wind farms	2,065	(133)	1,932
- recognition of impairment loss	1,327	(157)	1,170
- reversal of impairment	738	24	762
Goodwill	8	-	8
<b>TOTAL</b>	<b>3,124</b>	<b>(133)</b>	<b>2,991</b>
Unallocated and non-core assets	78	-	78
Property, plant and equipment and intangible assets under construction (including onshore and offshore wind projects)	120	-	120
<b>TOTAL</b>	<b>3,322</b>	<b>(133)</b>	<b>3,189</b>

The tested value presented above is the net book value of identifiable assets.

### 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. Presented below is the estimated impact of changes in key assumptions on changes in impairment losses in the Renewables segment as at December 31, 2017.

Parameter	Change	Impact on impairment loss	
		Increase in impairment loss	Decrease in impairment loss
Change in electricity prices throughout the forecast period	1%	-	16
	-1%	16	-
Change in WACC	+ 0,5 p.p.	43	-
	- 0,5 p.p.	-	42
Change in property right prices throughout forecast period	1%	-	5
	-1%	5	-
No change in property tax from 2018 level		206	-
Adverse resolutions of disputes with Enea S.A. and Energa S.A.		78	-

### 3.3 Distribution segment's property, plant and equipment

As at the reporting date the carrying amount of property, plant and equipment related to the distribution activity amounted to more than PLN 17 billion and represented approx. 28% of 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 Asset Base.

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

## 4. Significant accounting principles

These financial statements are prepared in accordance with the historic cost concept, except for selected categories of financial instruments and CO<sub>2</sub> emission allowance inventories purchased in order to generate the profit on market swings, which are recognised at fair value.

### 4.1 Consolidation rules

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. Companies acquired in the course of the year were the exception, preparing financial data for the period from the moment when PGE Group obtained control.

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, until 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 PGE Group and later Group transformations in the consolidated financial statements

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. The entities that later formed PGE Group were controlled by the State Treasury. This transaction thus, according to the Company, meets the definition of transaction under joint control and is therefore excluded from 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 PGE Group were recognised as transactions concluded between jointly controlled entities, therefore should be accounted within the equity of PGE Group, not affecting the goodwill.

The purchase of companies from third parties is accounted using the acquisition method in line with IFRS 3.

#### Joint ventures and joint operations

Due 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 in a joint venture under the equity method.

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

#### Investments in associates

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 recognised in the statement of financial position at cost increased or decreased to recognise the investor's share in the investee's net assets after the date of acquisition less impairment losses if applicable.

Investments in associates are recognised 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 translation are recognised in profit or loss or, in cases specified in the accounting policies applied, recorded in the value of assets.

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

## 4.3 Operating segments

An operating segment 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 PGE Group, the following segments are distinguished:

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

Segment revenues are revenues, including both sales to external customers and inter-segment 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 inter-segment 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. Revenues are recognised after deducting value added tax (VAT), excise tax and other sales-based taxes as well as discounts. When recognising revenue, the criteria specified below are also taken into account.

### Revenue from sale of goods and products

Revenues from the sale of goods and merchandise are recognised 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 recognised at the time of delivery.

Revenue from the sale of goods and products mainly includes:

- amounts receivable from: wholesale 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.

### Revenue from sale of services

Revenue from services rendered is recognised when the service is performed. Revenue from the provision of unfinished long-term services in the period from contract date to reporting date - after subtracting revenue recognised in previous reporting period - is determined proportionally to the services' status, if this status can be determined reliably.

When the outcome of a contract cannot be estimated reliably, the Group recognises revenue only to the extent of the expenses recognised 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 recognised at once when the service is performed. Fees received prior to July 1, 2009 are recognised 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 and the final adjustment. 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 recognised by the Company are recognised in profit or loss for the reporting period in which the revenues were recognised.

Costs that can only be indirectly attributed to revenues or other economic benefits recognised by entities, are recognised 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 recognised 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 liabilities is recognised for all taxable temporary differences.

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

The carrying amount of a deferred tax asset and deferred tax liability is reviewed at each reporting date. Deferred tax assets 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 utilised 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.

The entity calculates diluted earnings per share by dividing profit or loss attributable to ordinary equity holders of the Company (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, 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 Group also recognises the costs of major overhauls, periodic inspections that meet the definition of component as components of property, plant and equipment.

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 recognised 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.

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

Group	Average remaining amortisation period in years	Most frequently applied total depreciation periods in years
Buildings and structures	15	20 – 67
Machinery and equipment	13	4 – 40
Vehicles	6	4 – 33
Other property, plant and equipment	3	3 – 27

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 recognised 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 recognised PGE Group applies principles described in note 4.11.

Investments relating to fixed assets under construction or assembly are recognised 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 recognise 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.

Capitalised 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 recognised 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 recognised 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 amortisation 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 amortisable amount of an intangible asset with a definite useful life shall be allocated on a systematic basis over its useful life. Amortisation starts when the asset is available for use.

Intangible assets with a definite useful life are amortized over their useful life and analysed for potential impairment, if there are indications of impairment. Amortisation periods and amortisation 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 amortisation period in years	Most frequently applied total amortisation periods in years
Acquired patents and licences	2	3 – 20
Cost of finished development works	3	3 – 20
Other	16	3 – 25

An intangible asset arising from development phase of a project shall be recognised 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 recognised 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 a component of non-financial assets 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 recognised 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
- Financial assets at fair value through profit or loss
- Loans and receivables
- Available-for-sale financial assets

##### Financial assets carried 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 instruments are measured at fair value as at the reporting date. Gain or loss on financial assets classified to the FVP portfolio are recognised in the financial result and are not decreased by amount of interest.

##### Loans and receivables

Loans and receivables are financial assets other than derivatives with identified or identifiable payments, not listed on 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. Loans and receivables are recognised at amortised cost.

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 recognised as other operating expenses or finance costs. Non-current receivables are measured at present (discounted) value.

##### Available-for-sale assets

All other financial assets are available-for-sale financial assets. Financial assets available for sale are recognised 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 recognised in other comprehensive income, except for:

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

Dividends from equity instrument in the AFS portfolio are recognised 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 recognised 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 recognised 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 recognised in hedging reserve in the portion determined to be an effective hedge, while the ineffective portion of the hedge is recognised in profit or loss.

The accumulated changes in fair value of hedging instrument, previously recognised 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 it 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 providing 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<sub>2</sub> emission allowances intended for re-sale).

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

CO<sub>2</sub> emission rights acquired in order to realise 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 CO<sub>2</sub> emission allowances) – using FIFO method;
- CO<sub>2</sub> emission allowances
  - acquired in order to realise profits from fluctuations in market prices - using detailed identification method,
  - purchased for resale to conventional generating units in 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 realisable value. Impairment losses on inventories are recognised in operating expenses. When the realisable value of a specific item of inventory is recovered fully or partially, its carrying amount is adjusted by decreasing revaluation adjustment.

#### 4.16 CO<sub>2</sub> emission rights for captive use

European Union Allowances (EUA) for carbon dioxide emissions intended for captive use of power generating units and CO<sub>2</sub> emission rights are presented in a separate line in the statement of financial position. EUAs received free of charge are recognised in the statement of financial position in nominal value, which is zero. Purchased EUAs are recognised at purchase price. Use of CO<sub>2</sub> emission allowances for captive use is measured based on FIFO method.

#### 4.17 Other assets (including prepayments)

The Group recognises 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 recognised at reliably measured amounts, relate to future periods and will generate future economic benefits.

Other assets include in particular state receivables, advances for deliveries (including advances for property, plant and equipment in progress) and services and dividend 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 contributed, share capital contributions are recognised 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,
- Equity attributable to non-controlling interests

#### 4.21 Provisions

The Group recognises 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 the entity, the Group's employees 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 Group's employees are also 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 recognises 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 recognised 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 recognised in other comprehensive income for post-employment benefits 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 recognised in operating expenses in proportion to the extent of storage filling, whereas the reversal of the discount is recognised 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 recognised in operating expenses or in the initial value of property plant and equipment, respectively. The unwinding of the discount is recognised 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 recognised in the following way:

- for the provisions recognised 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<sub>2</sub> emission allowances

The provision for deficit of CO<sub>2</sub> emission allowances is created by PGE Group entities for the shortfall of CO<sub>2</sub> emission allowances 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 recognised in the statement of comprehensive income as 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 recognised 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 recognised 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's entities create such a fund and make 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 recognised 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 recognised under the principle of prudence and accrual basis of accounting. Deferred income comprises:

- amounts received or due from business partners to be realised in subsequent reporting periods. Deferred income from connection fees that were received before July 1, 2009 is amortised evenly to sales revenues,
- funds 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 amortised to other operating income in line with the depreciation charges on these assets.

Government grants are recognised 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 the Group. 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 recognised as an asset. Lease payments shall be apportioned between reduction of the outstanding liability and the finance charge. Finance costs are recognised as finance costs in the statement of comprehensive income during the lease period.

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 recognised 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 in accounting principles and data presentation

#### New standards and interpretations which became effective on January 1, 2017

The accounting principles applied in preparing these consolidated financial statements are consistent with those applied in preparing the Company's consolidated financial statements for the year ended December 31, 2016, except as stated below. The following amendments to IFRSs are applied in these financial statements as of their effective date however they did not have material impact on the presented and disclosed financial information or they were not applicable to the Group's transactions:

- Amendments to IAS 7 - Disclosure Initiative
- Amendments to IAS 12 - Recognition of deferred tax assets for unrealised losses
- Amendments resulting from IFRS annual improvement cycle 2014-2016 - amendments to IFRS 12 - clarifications regarding the scope of the standard.

The Group decided not to apply early any other standards, interpretations or amendments that were published but are not yet effective.

#### CO<sub>2</sub> emission rights for captive use

In the consolidated statement of financial position for 2016, PGE Group presented CO<sub>2</sub> emission allowances for captive use as short-term. In 2017, the Group changed this presentation method and in these financial statements divides these into short- and long-term. According to the Group's management, this amended presentation will more correctly reflect the nature of this item.

Given the above, PGE Group restated its comparative data presented in the statement of financial position. The restatement is presented in the table below. Information presented in note 15 to these financial statements was also restated accordingly.

Assets classified as held for sale were presented in separate line.



## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	As at January 1, 2016 <i>published data</i>	Change in presentation	As at January 1, 2016 <i>restated data</i>
<b>NON-CURRENT ASSETS, including:</b>			
CO <sub>2</sub> emission rights for captive use	-	1,322	1,322
<b>TOTAL NON-CURRENT ASSETS</b>	<b>49,586</b>	<b>1,322</b>	<b>50,908</b>
<b>CURRENT ASSETS, including:</b>			
CO <sub>2</sub> emission rights for captive use	2,172	(1,322)	850
Assets classified as held for sale	16	(16)	-
<b>TOTAL CURRENT ASSETS</b>	<b>11,710</b>	<b>(1,338)</b>	<b>10,372</b>
<b>ASSETS CLASSIFIED AS HELD FOR SALE</b>	<b>-</b>	<b>16</b>	<b>16</b>
<b>TOTAL ASSETS</b>	<b>61,296</b>	<b>-</b>	<b>61,296</b>
<hr/>			
	As at December 31, 2016 <i>published data</i>	Change in presentation	As at December 31, 2016 <i>restated data</i>
<b>NON-CURRENT ASSETS, including:</b>			
CO <sub>2</sub> emission rights for captive use	-	1,157	1,157
<b>TOTAL NON-CURRENT ASSETS</b>	<b>54,075</b>	<b>1,157</b>	<b>55,232</b>
<b>CURRENT ASSETS, including:</b>			
CO <sub>2</sub> emission rights for captive use	2,349	(1,157)	1,192
Assets classified as held for sale	12	(12)	-
<b>TOTAL CURRENT ASSETS</b>	<b>13,399</b>	<b>(1,169)</b>	<b>12,230</b>
<b>ASSETS CLASSIFIED AS HELD FOR SALE</b>	<b>-</b>	<b>12</b>	<b>12</b>
<b>TOTAL ASSETS</b>	<b>67,474</b>	<b>-</b>	<b>67,474</b>

## EXPLANATORY NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### EXPLANATORY NOTES TO OPERATING SEGMENTS

#### 6. Information on operating segments

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. PGE Group's key concessions 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 its 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 2017, PGE Group's concessions costs amounted to PLN 6 million (PLN 5 million in 2016), exploitation charges and mining usufruct charges amount to PLN 129 million in 2017 and PLN 123 million in 2016.

PGE Group presents information on operating segments in the current and comparative reporting period in accordance with IFRS 8 *Operating Segments*. PGE Group's 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, investment is start-up and setting up e-mobility system.

Organisation and management over 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. An 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. From January 1, 2018 all transactions are on market terms.

When analysing the results of particular business segments the management of 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 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.

In the Renewables segment, electricity is generated from natural resources such as water, wind and sun. Weather conditions are an important factor affecting electricity generation in this segment.

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

## 6.1 Information on business segments

### Information on business segments for the year ended December 31,2017

	Conventional generation	Renewables	Supply	Distribution	Other activity	Consolidation adjustments	Total
<b>STATEMENT OF PROFIT OR LOSS</b>							
Sales revenues from external customers	6,079	597	14,006	2,234	149	35	23,100
Inter-segment sales	6,996	127	1,656	4,158	300	(13,237)	-
<b>TOTAL SEGMENT REVENUE</b>	<b>13,075</b>	<b>724</b>	<b>15,662</b>	<b>6,392</b>	<b>449</b>	<b>(13,202)</b>	<b>23,100</b>
Cost of goods sold	(10,439)	(738)	(13,582)	(4,974)	(428)	12,546	(17,615)
<b>EBIT *)</b>	<b>1,754</b>	<b>(36)</b>	<b>784</b>	<b>1,166</b>	<b>(88)</b>	<b>40</b>	<b>3,620</b>
Net financial income / (expenses)							(370)
Share of profit/(loss) of entities accounted for using the equity method							40
<b>PROFIT BEFORE TAX</b>							<b>3,290</b>
Income tax							(623)
<b>NET PROFIT/(LOSS) FOR THE REPORTING PERIOD</b>							<b>2,667</b>
Depreciation, amortisation, disposal and impairment losses recognised in profit or loss	2,345	400	27	1,167	131	(40)	4,030
<b>EBITDA **)</b>	<b>4,099</b>	<b>364</b>	<b>811</b>	<b>2,333</b>	<b>43</b>	<b>-</b>	<b>7,650</b>
<b>ASSETS AND LIABILITIES</b>							
Segment assets excluding trade receivables	43,096	3,232	1,129	17,084	546	(903)	64,184
Trade receivables	1,459	107	3,009	859	75	(2,350)	3,159
Shares accounted for using the equity method							634
Unallocated assets							4,129
<b>TOTAL ASSETS</b>							<b>72,106</b>
Segment liabilities excluding trade liabilities	8,977	357	1,162	2,044	99	(151)	12,488
Trade liabilities	1,356	41	2,084	324	31	(2,186)	1,650
Unallocated liabilities							11,615
<b>TOTAL LIABILITIES</b>							<b>25,753</b>
<b>OTHER INFORMATION ON BUSINESS SEGMENT</b>							
Capital expenditures	4,899	81	14	1,716	126	(85)	6,751
Acquisition of property, plant and equipment, intangible assets as part of acquisition of new companies***)	5,426	-	2	-	24	-	5,452
Impairment allowances on financial and non-financial assets	919	134	6	10	37	-	1,106
Other non-monetary expenses ****)	1,820	16	829	162	30	2	2,859

\*) EBIT = operating profit (loss)

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

\*\*\*) Including goodwill arising on initial recognition of assets acquired from EDF

\*\*\*\*) Non-monetary expenses include mainly changes in provisions such as: rehabilitation provision, provision for CO<sub>2</sub> emission rights, provision for jubilee awards and employee tariff that are recognised in profit or loss and other comprehensive income.

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

	Conventional generation	Renewables	Supply	Distribution	Other activity	Consolidation adjustments	Total
<b>STATEMENT OF PROFIT OR LOSS</b>							
Sales to external customers	11,303	657	13,711	1,979	406	36	28,092
Inter-segment sales	435	60	2,303	3,939	282	(7,019)	-
<b>TOTAL SEGMENT REVENUE</b>	<b>11,738</b>	<b>717</b>	<b>16,014</b>	<b>5,918</b>	<b>688</b>	<b>(6,983)</b>	<b>28,092</b>
Cost of goods sold	(9,077)	(1,215)	(14,095)	(4,534)	(633)	6,380	<b>(23,174)</b>
<b>EBIT *)</b>	<b>2,691</b>	<b>(770)</b>	<b>473</b>	<b>1,104</b>	<b>(64)</b>	<b>78</b>	<b>3,512</b>
Net financial income / (expenses)							(193)
Share of profit/(loss) of entities accounted for using the equity method							(45)
<b>PROFIT BEFORE TAX</b>							<b>3,274</b>
Income tax							(708)
<b>NET PROFIT/(LOSS) FOR THE REPORTING PERIOD</b>							<b>2,566</b>
Depreciation, amortisation, disposal and impairment losses recognised in profit or loss	1,491	1,135	27	1,126	131	(46)	3,864
<b>EBITDA **)</b>	<b>4,182</b>	<b>365</b>	<b>500</b>	<b>2,230</b>	<b>67</b>	<b>32</b>	<b>7,376</b>
<b>ASSETS AND LIABILITIES</b>							
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 using the equity method							402
Unallocated assets							7,231
<b>TOTAL ASSETS</b>							<b>67,474</b>
Segment liabilities excluding trade liabilities	8,570	349	1,378	1,922	158	105	12,482
Trade payables	602	36	1,194	264	75	(1,195)	976
Unallocated liabilities							11,241
<b>TOTAL LIABILITIES</b>							<b>24,699</b>
<b>OTHER INFORMATION ON BUSINESS SEGMENT</b>							
Capital expenditures	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,IP, goodwill) that are recognised in profit or loss

\*\*\*) Non-monetary expenses include mainly changes in provisions such as: rehabilitation provision, provision for CO<sub>2</sub> emission rights, provision for jubilee awards and employee tariff that are recognised in profit or loss and other comprehensive income.

## 6.2 Information on geographical areas

Geographic distribution of sales revenues for the year ended December 31, 2017 and December 31, 2016 is as follows:

	Year ended December 31, 2017	Year ended December 31, 2016
<b>REVENUES FROM OPERATING ACTIVITIES</b>		
Domestic market	22,722	27,975
EU countries	334	106
Other countries	44	11
<b>TOTAL REVENUES</b>	<b>23,100</b>	<b>28,092</b>

Geographic distribution of assets for the year ended December 31, 2017 and December 31, 2016 is as follows:

	As at December 31, 2017	As at December 31, 2016
<b>OTHER INFORMATION ON AREA</b>		
Domestic market	67,274	59,815
EU countries	67	25
Other countries	2	1
<b>TOTAL SEGMENT ASSETS</b>	<b>67,343</b>	<b>59,841</b>
Domestic market	3,622	7,184
EU countries	507	47
<b>TOTAL UNALLOCATED ASSETS</b>	<b>4,129</b>	<b>7,231</b>
Domestic market	634	402
<b>SHARES ACCOUNTED FOR UNDER THE EQUITY METHOD</b>	<b>634</b>	<b>402</b>
<b>TOTAL</b>		
<b>TOTAL ASSETS</b>	<b>72,106</b>	<b>67,474</b>

## EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Q1 <i>unaudited</i>	Q2 <i>unaudited</i>	Q3 <i>unaudited</i>	Q4 <i>unaudited</i>	Year ended December 31, 2017
Sales revenues	5,741	4,879	6,073	6,407	23,100
Cost of goods sold	(4,149)	(3,723)	(3,759)	(5,984)	(17,615)
<b>GROSS PROFIT/(LOSS) ON SALES</b>	<b>1,592</b>	<b>1,156</b>	<b>2,314</b>	<b>423</b>	<b>5,485</b>
Net other operating income / (expenses)	89	40	7	12	148
<b>EBIT – OPERATING PROFIT / (LOSS)</b>	<b>1,201</b>	<b>731</b>	<b>1,883</b>	<b>(195)</b>	<b>3,620</b>
Net financial income / (expenses)	(63)	(59)	(80)	(168)	(370)
Share of profit/(loss) of entities accounted for using the equity method	9	(8)	10	29	40
<b>PROFIT/(LOSS) BEFORE TAX</b>	<b>1,147</b>	<b>664</b>	<b>1,813</b>	<b>(334)</b>	<b>3,290</b>
Income tax	(184)	(132)	(351)	44	(623)
<b>NET PROFIT/(LOSS) FOR THE REPORTING PERIOD</b>	<b>963</b>	<b>532</b>	<b>1,462</b>	<b>(290)</b>	<b>2,667</b>

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

## 7. Revenues and expenses

### 7.1 Sales revenues

	Q1 <i>unaudited</i>	Q2 <i>unaudited</i>	Q3 <i>unaudited</i>	Q4 <i>unaudited</i>	Year ended December 31, 2017
<b>SALES REVENUES</b>					
<i>Sales of merchandise and finished goods with excise tax duty</i>	5,743	4,949	4,910	6,477	22,079
<i>Excise tax</i>	(125)	(116)	(114)	(128)	(483)
<b>Revenues from sale of merchandise and finished goods, including:</b>	<b>5,618</b>	<b>4,833</b>	<b>4,796</b>	<b>6,349</b>	<b>21,596</b>
Sale of electricity	3,221	2,814	2,910	3,488	12,433
Sale of distribution services	1,574	1,453	1,473	1,581	6,081
Sale of heat	285	129	88	485	987
Sale of energy origin rights	158	87	(7)	169	407
Regulatory system services	147	125	124	155	551
Sale of gas	146	135	92	211	584
Other sales of goods and materials	87	90	116	260	553
<b>Revenue from sale of services</b>	<b>123</b>	<b>46</b>	<b>66</b>	<b>54</b>	<b>289</b>
<b>Revenues from LTC compensations</b>	<b>-</b>	<b>-</b>	<b>1,211</b>	<b>4</b>	<b>1,215</b>
<b>TOTAL REVENUE FROM SALE</b>	<b>5,741</b>	<b>4,879</b>	<b>6,073</b>	<b>6,407</b>	<b>23,100</b>



	Q1 unaudited	Q2 unaudited	Q3 unaudited	Q4 unaudited	Year ended December 31, 2016
<b>SALES REVENUES</b>					
Sales of merchandise and finished goods with excise tax duty	7,001	6,400	6,751	7,393	27,545
Excise tax	(126)	(120)	(122)	(133)	(501)
<b>Revenues from sale of merchandise and finished goods, including::</b>	<b>6,875</b>	<b>6,280</b>	<b>6,629</b>	<b>7,260</b>	<b>27,044</b>
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
Other sales of goods and materials	86	89	95	106	376
<b>Revenue from sale of services</b>	<b>128</b>	<b>130</b>	<b>137</b>	<b>133</b>	<b>528</b>
<b>Revenues from LTC compensations</b>	<b>130</b>	<b>123</b>	<b>131</b>	<b>136</b>	<b>520</b>
<b>TOTAL REVENUE FROM SALE</b>	<b>7,133</b>	<b>6,533</b>	<b>6,897</b>	<b>7,529</b>	<b>28,092</b>

The decrease in revenues from sale of electricity in 2017, as compared to 2016 is mainly due to a lower exchange commitment. The reduction in exchange commitment starting from 2017 resulted in a greater volume of electricity being sold directly between PGE Group companies. These transactions are eliminated at the level of consolidated financial statements.

The issue of compensations from LTCs is described in note 33.1 to these financial statements.

## 7.2 Cost by nature and function

	Q1 unaudited	Q2 unaudited	Q3 unaudited	Q4 unaudited	Year ended December 31, 2017
<b>COSTS BY NATURE</b>					
Depreciation, amortisation , disposal and impairment losses	778	797	808	1,758	4,141
Materials and energy	758	589	634	1,124	3,105
External services	671	642	668	818	2,799
Taxes and charges	863	727	735	866	3,191
Employee benefits expenses	1,098	1,094	1,023	1,260	4,475
Other costs by nature	53	53	75	102	283
<b>TOTAL COST BY NATURE</b>	<b>4,221</b>	<b>3,902</b>	<b>3,943</b>	<b>5,928</b>	<b>17,994</b>
Change in inventories	(18)	2	8	4	(4)
Cost of products and services for the entity's own needs	(190)	(246)	(244)	(321)	(1,001)
Distribution and selling expenses	(304)	(296)	(282)	(338)	(1,220)
General and administrative expenses	(176)	(169)	(156)	(292)	(793)
Value of goods and materials sold	616	530	490	1,003	2,639
<b>COST OF GOODS SOLD</b>	<b>4,149</b>	<b>3,723</b>	<b>3,759</b>	<b>5,984</b>	<b>17,615</b>

The y/y decline in the value of goods and materials sold (mainly purchased electricity) in 2017 resulted mainly from the aforementioned decline in revenue from the sale of electricity.

	Q1 unaudited	Q2 unaudited	Q3 unaudited	Q4 unaudited	Year ended December 31, 2016
<b>COSTS BY NATURE</b>					
Depreciation, amortisation , disposal and impairment losses	731	1,522	782	949	3,984
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 costs by nature	63	65	66	73	267
<b>TOTAL COST BY NATURE</b>	<b>4,155</b>	<b>4,691</b>	<b>3,969</b>	<b>4,384</b>	<b>17,199</b>
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)
Value of goods and materials sold	2,305	2,340	2,304	2,437	9,386
<b>COST OF GOODS SOLD</b>	<b>5,605</b>	<b>6,217</b>	<b>5,517</b>	<b>5,835</b>	<b>23,174</b>

### 7.2.1 Depreciation, amortisation, disposal and impairment losses

The following presents depreciation, amortisation, disposals and impairment losses of property, plant and equipment, intangible assets, investment properties in the statement of comprehensive income.

Year ended December 31, 2017	Depreciation, amortisation, disposal				Impairment losses			
	PPA	IA	IP	TOTAL	PPA	IA	IP	TOTAL
Cost of goods sold	2,894	87	2	2,983	958	2	(3)	957
Distribution and selling expenses	11	5	-	16	-	-	-	-
General and administrative expenses	23	14	-	37	-	37	-	37
<b>Recognised in profit or loss</b>	<b>2,928</b>	<b>106</b>	<b>2</b>	<b>3,036</b>	<b>958</b>	<b>39</b>	<b>(3)</b>	<b>994</b>
Cost of products and services for the entity's own needs	111	-	-	111	-	-	-	-
<b>TOTAL</b>	<b>3,039</b>	<b>106</b>	<b>2</b>	<b>3,147</b>	<b>958</b>	<b>39</b>	<b>(3)</b>	<b>994</b>
Other operating income	-	-	-	-	(2)	-	-	(2)

Year ended December 31, 2016	Depreciation, amortisation, disposal				Impairment losses			
	PPA	IA	IP	TOTAL	PPA	IA	IP	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
<b>Recognised in profit or loss</b>	<b>2,755</b>	<b>103</b>	<b>1</b>	<b>2,859</b>	<b>711</b>	<b>291</b>	<b>3</b>	<b>1,005</b>
Change in inventories	1	-	-	1	-	-	-	-
Cost of products and services for the entity's own needs	119	-	-	119	-	-	-	-
<b>TOTAL</b>	<b>2,875</b>	<b>103</b>	<b>1</b>	<b>2,979</b>	<b>711</b>	<b>291</b>	<b>3</b>	<b>1,005</b>

### 7.2.2 Materials and energy

	Year ended December 31, 2017	Year ended December 31, 2016
Cost of production fuel	2,190	1,994
Renovation materials	513	475
Energy	161	148
Other	241	200
<b>TOTAL MATERIALS AND ENERGY</b>	<b>3,105</b>	<b>2,817</b>

### 7.2.3 External services

	Year ended December 31, 2017	Year ended December 31, 2016
Transmission services	1,900	1,561
External services - repairs and exploitation	282	309
Logistics services	124	85
Telecommunication services	79	232
Rent and lease	44	53
IT services	83	85
Consulting services	54	31
Other	233	213
<b>TOTAL EXTERNAL SERVICES</b>	<b>2,799</b>	<b>2,569</b>

### 7.2.4 Employee benefits expenses and employment structure

	Year ended December 31, 2017	Year ended December 31, 2016
Payroll	3,239	3,154
Social security expenses	635	606
Retirement and pension expenses	17	11
Jubilee awards, coal benefits	105	102
Other post-employment benefits	37	37
Change in provisions for employee benefits	(14)	(146)
Cost of Voluntary Leave Programme	2	16
Other employee benefits	454	457
<b>TOTAL EMPLOYEE BENEFITS EXPENSES, INCLUDING:</b>	<b>4,475</b>	<b>4,237</b>
Included in costs of goods sold	3,443	3,123
Included in distribution and selling costs	264	259
Included in general and administrative expenses	490	504
Cost of products and services for the entity's own needs	278	351

In the item Other costs of employee benefits the Group recognises the costs of employee pension schemes, contributions to Social Fund, cost of healthcare and training.

Employment at PGE Group (FTE) was as follows:

	As at December 31, 2017	As at December 31, 2016
Conventional energy	25,382	22,788
Renewable energy	510	509
Sales	2,219	2,066
Distribution	10,200	10,239
Other consolidated companies	2,920	2,869
<b>TOTAL EMPLOYMENT</b>	<b>41,231</b>	<b>38,471</b>

The increase in employment in the Conventional Generation and Supply segments is related to the acquisition of assets from EDF in November 2017.

### 7.3 Other operating income and expenses

	Year ended December 31, 2017	Year ended December 31, 2016
<b>OTHER OPERATING INCOME</b>		
Penalties, fines and compensations received	112	137
Adjustment of revenues from LTC compensations	69	148
Reversal of other provisions	48	44
Gain on liquidation/disposal of current assets	43	37
Grants received	38	43
Reversal of impairment allowances	21	24
Profit on disposal of property, plant and equipment / intangible assets	13	11
Property, plant and equipment, intangible assets received free of charge	11	11
Revenue from illegal energy consumption	10	6
Surpluses / asset disclosures	9	4
Compensation for legal proceedings' costs	4	4
Change in rehabilitation provision	-	643
Other	25	59
<b>TOTAL OTHER OPERATING INCOME</b>	<b>403</b>	<b>1,171</b>

The issue of compensations from LTCs is described in note 33.1 to these financial statements.

	Year ended December 31, 2017	Year ended December 31, 2016
<b>OTHER OPERATING EXPENSES</b>		
Donations granted	43	13
Change in rehabilitation provision	42	-
Recognition of impairment losses	37	49
Re-invoicing	27	16
Recognition of impairment losses on other assets	23	1
Recognition of other provisions	21	26
Damage / failure removal	18	19
Write-off of discontinued investments and disposal of current assets	12	5
Compensation	10	5
Disposal of property, plant and equipment, intangible assets related to other activity	7	6
Legal proceedings' costs	6	6
Other	9	25
<b>TOTAL OTHER OPERATING EXPENSES</b>	<b>255</b>	<b>171</b>

#### 7.4 Financial income and financial expenses

	Year ended December 31, 2017	Year ended December 31, 2016
<b>FINANCIAL INCOME FROM FINANCIAL INSTRUMENTS</b>		
Dividends	5	2
Interest	91	55
Revaluation of financial instruments	37	27
Reversal of impairment allowances	2	90
Foreign exchange gains	48	14
<b>FINANCIAL INCOME FROM FINANCIAL INSTRUMENTS</b>	<b>183</b>	<b>188</b>
<b>OTHER FINANCIAL INCOME</b>		
Interest on statutory receivables	2	1
Reversal of provisions	4	1
Other	2	1
<b>OTHER FINANCIAL INCOME</b>	<b>8</b>	<b>3</b>
<b>TOTAL FINANCIAL INCOME</b>	<b>191</b>	<b>191</b>

The Group recognises interest income primarily on cash and receivables. Positive exchange differences were influenced mainly by foreign currency loans.

In the item 'Revaluation' PGE Group presents mainly measurement of hedging transactions in their ineffective part for instruments designated as cash flow hedges and in full as regards other instruments, as well as the measurement of a call option to purchase Polimex-Mostostal S.A. shares.

	Year ended December 31, 2017	Year ended December 31, 2016
<b>FINANCIAL EXPENSES RELATED TO FINANCIAL INSTRUMENTS</b>		
Interest	176	131
Revaluation of financial instruments	14	10
Impairment loss	97	2
Loss on disposal of investment	93	-
Foreign exchange losses	6	33
<b>FINANCIAL EXPENSES RELATED TO FINANCIAL INSTRUMENTS</b>	<b>386</b>	<b>176</b>
<b>OTHER FINANCIAL EXPENSES</b>		
Interest expenses, including unwinding of the discount	172	180
Interest on statutory liabilities	1	1
Provisions created	1	25
Other	1	2
<b>OTHER FINANCIAL EXPENSES</b>	<b>175</b>	<b>208</b>
<b>TOTAL FINANCIAL EXPENSES</b>	<b>561</b>	<b>384</b>

Interest expenses mainly relate to bonds issued and credit and loans taken out. Interest cost (discount unwinding) on non-financial items relates mainly to rehabilitation provisions and employee benefit provisions.

During the reporting period, impairment included mainly the cost of estimated loss of value of bonds issued by Autostrada Wielkopolska S.A. of book value PLN 89 million.

Loss on disposal of investment, amounting to PLN 93 million, mainly due to the sale of EXATEL S.A. shares.

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

	Polska Grupa Górnicza	Polimex Mostostal	ElectroMobility Poland	PEC Bogatynia
<b>SHARE IN VOTES</b>	<b>15.76%</b>	<b>16.48%</b>	<b>25.00%</b>	<b>34.93%</b>
<b>YEAR 2017</b>				
Revenue	8,236	2,068	-	14
Result on continuing operations	86	65	(3)	-
<b>Share of profit of associates and jointly controlled entities</b>	<b>14</b>	<b>11</b>	<b>(1)</b>	<b>-</b>
Elimination of unrealised gains and losses	21	(5)	-	-
<b>SHARE OF PROFIT OF ASSOCIATES AND ENTITIES JOINTLY CONTROLLED</b>	<b>35</b>	<b>6</b>	<b>(1)</b>	<b>-</b>
	Polska Grupa Górnicza	ElectroMobility Poland	PEC Bogatynia	
<b>SHARE IN VOTES</b>	<b>until X.2016 15.66%</b> <b>XI-XII.2016 16.63%</b>	<b>25.00%</b>	<b>34.93%</b>	
<b>YEAR 2016</b>				
Revenue	3,828	-	-	13
Result on continuing operations	(332)	-	-	(1)
<b>Share of profit of associates and jointly controlled entities</b>	<b>(51)</b>	<b>-</b>	<b>-</b>	<b>-</b>
Elimination of unrealised losses	6	-	-	-
<b>SHARE OF PROFIT OF ASSOCIATES AND ENTITIES JOINTLY CONTROLLED</b>	<b>(45)</b>	<b>-</b>	<b>-</b>	<b>-</b>
Other comprehensive income	(11)	-	-	-
<b>SHARE OF ASSOCIATES AND JOINTLY CONTROLLED ENTITIES IN OTHER COMPREHENSIVE INCOME</b>	<b>(2)</b>	<b>-</b>	<b>-</b>	<b>-</b>

Data of associate Polimex Mostostal S.A. consolidated from January 17, 2017.

The Group made a consolidation adjustment related to margin on sale of coal between PGG and the Group and an adjustment of margin on Polimex Mostostal's contracts for the Group.

## 8. Income tax

### 8.1 Tax in the statement of comprehensive income

Main elements of income tax expense for the years ended December 31, 2017 and December 31, 2016 are as follows:

	Year ended December 31, 2017	Year ended December 31, 2016
<b>INCOME TAX RECOGNISED IN STATEMENT OF PROFIT OR LOSS</b>		
Current income tax	632	398
Previous periods current income tax adjustments	-	16
Deferred income tax	(9)	294
<b>INCOME TAX EXPENSE RECOGNISED IN STATEMENT OF PROFIT OR LOSS</b>	<b>623</b>	<b>708</b>
<b>INCOME TAX EXPENSE RECOGNISED IN OTHER COMPREHENSIVE INCOME</b>		
From actuarial gains and losses from valuation of provisions for employee benefits	(19)	47
From valuation of hedging instruments	(15)	39
<b>(TAX BENEFIT) / EXPENSE RECOGNIZED IN OTHER COMPREHENSIVE INCOME (EQUITY)</b>	<b>(34)</b>	<b>86</b>

## 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, 2017	Year ended December 31, 2016
<b>PROFIT BEFORE TAX</b>	<b>3,290</b>	<b>3,274</b>
Income tax according to Polish statutory tax rate of 19%	625	621
<b>ITEMS ADJUSTING INCOME TAX</b>		
Adjustments related to settlement of current income tax of previous years	-	16
Adjustments concerning deferred income tax from prior years	(4)	(36)
Costs not recognised as tax-deductible costs	42	119
Non-taxable income	(42)	(14)
Other	2	2
<b>TAX AT EFFECTIVE TAX RATE</b>	<b>623</b>	<b>708</b>
<b>Income tax (expense) as presented in the consolidated financial statements</b>	<b>623</b>	<b>708</b>
<b>EFFECTIVE TAX RATE</b>	<b>19%</b>	<b>22%</b>



## EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION

### 9. Property, plant and equipment

	As at December 31, 2017	As at December 31, 2016
Land	242	236
Buildings and construction	20,575	19,061
Technical equipment	22,166	19,604
Vehicles	339	341
Other property, plant and equipment	2,952	2,522
Construction in progress	12,346	9,601
<b>CARRYING AMOUNT OF PROPERTY, PLANT AND EQUIPMENT</b>	<b>58,620</b>	<b>51,365</b>

#### Changes in property, plant and equipment by type

	Land	Buildings and construction	Technical equipment	Vehicles	Other property, plant and equipment	Construction in progress	Total
<b>GROSS BOOK VALUE</b>							
<b>AS AT JANUARY 1, 2017</b>	<b>271</b>	<b>33,492</b>	<b>42,152</b>	<b>729</b>	<b>5,271</b>	<b>9,965</b>	<b>91,880</b>
Capital expenditures	-	-	1	2	-	6,599	6,602
Transfer from construction in progress	4	1,994	2,269	54	398	(4,719)	-
Liquidation, disposal	-	(134)	(324)	(25)	(11)	-	(494)
Purchase of new subsidiaries	7	1,239	2,554	5	9	853	4,667
Changes in PGE Group	-	(406)	(505)	(5)	(41)	(33)	(990)
Other	2	(2)	6	(3)	184	94	281
<b>AS AT DECEMBER 31, 2017</b>	<b>284</b>	<b>36,183</b>	<b>46,153</b>	<b>757</b>	<b>5,810</b>	<b>12,759</b>	<b>101,946</b>
<b>ACCUMULATED DEPRECIATION AND IMPAIRMENT LOSSES</b>							
<b>AS AT JANUARY 1, 2017</b>	<b>35</b>	<b>14,431</b>	<b>22,548</b>	<b>388</b>	<b>2,749</b>	<b>364</b>	<b>40,515</b>
Depreciation and net value of liquidation presented in costs by nature	4	1,267	1,555	58	153	2	3,039
Impairment allowances	4	291	601	1	2	57	956
Liquidation, disposal	-	(121)	(289)	(23)	(11)	-	(444)
Changes in PGE Group	-	(246)	(386)	(3)	(35)	-	(670)
Other	(1)	(14)	(42)	(3)	-	(10)	(70)
<b>AS AT DECEMBER 31, 2017</b>	<b>42</b>	<b>15,608</b>	<b>23,987</b>	<b>418</b>	<b>2,858</b>	<b>413</b>	<b>43,326</b>
<b>CARRYING AMOUNT AS AT DECEMBER 31, 2017</b>	<b>242</b>	<b>20,575</b>	<b>22,166</b>	<b>339</b>	<b>2,952</b>	<b>12,346</b>	<b>58,620</b>

	Land	Buildings and construction	Technical equipment	Vehicles	Other property, plant and equipment	Property, plant and equipment in progress	Total
<b>GROSS CARRYING AMOUNT</b>							
<b>AS AT JANUARY 1, 2016</b>	<b>266</b>	<b>31,669</b>	<b>39,261</b>	<b>720</b>	<b>4,991</b>	<b>8,019</b>	<b>84,926</b>
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)
<b>AS AT DECEMBER 31, 2016</b>	<b>271</b>	<b>33,492</b>	<b>42,152</b>	<b>729</b>	<b>5,271</b>	<b>9,965</b>	<b>91,880</b>
<b>DEPRECIATION AND IMPAIRMENT LOSSES</b>							
<b>AS AT JANUARY 1, 2016</b>	<b>23</b>	<b>13,204</b>	<b>21,487</b>	<b>395</b>	<b>2,601</b>	<b>148</b>	<b>37,858</b>
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)
<b>AS AT DECEMBER 31, 2016</b>	<b>35</b>	<b>14,431</b>	<b>22,548</b>	<b>388</b>	<b>2,749</b>	<b>364</b>	<b>40,515</b>
<b>CARRYING AMOUNT AS AT DECEMBER, 2016</b>	<b>236</b>	<b>19,061</b>	<b>19,604</b>	<b>341</b>	<b>2,522</b>	<b>9,601</b>	<b>51,365</b>

### Significant additions and disposals of property, plant and equipment

The largest expenditures were incurred in the Conventional Generation segment (PLN 4,713 million) and the Distribution segment (PLN 1,684 million). The key expenditures items were as follows: construction of units 5-6 at Opole Power Plant (PLN 1,808 million), construction of unit 11 at Turów Power Plant (PLN 967 million), modernisation of units 1-3 at Turów Power Plant (PLN 222 million), construction of thermal processing installation with energy recovery at Rzeszów CHP (PLN 104 million), connection of new customers (PLN 504 million) and the modernisation and expansion of grid, stations and lines (PLN 868 million) in the Distribution segment.

The acquisition of new subsidiaries relates to the acquisition of companies from EDF group. Because the Group has not yet finished work on determining the fair value of property, plant and equipment as at the acquisition date, the values provided in the table above are not final.

During the present period, the Group sold 100% of shares in EXATEL S.A. With the same of EXATEL S.A., the Group also lost control over its subsidiary ENERGO-TEL S.A. As a result of these transactions, the value of the Group's property, plant and equipment and decreased by PLN 320 million.

### Borrowing costs

During the year ended December 31, 2017 PGE Group capitalised in the value of property, plant and equipment and construction in progress borrowings costs of approx. PLN 159 million (PLN 103 million in the comparative period).

### Capitalisation 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 366 million. At the same time, the Group recognised depreciation of capitalised stripping costs of PLN 97 million. Capitalised stripping costs are presented as "other property, plant and equipment".

### Capitalisation of changes in valuation of rehabilitation provision

PGE Group recognises 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, 2017 net value of capitalised rehabilitation provision amounted to PLN 792 million (including PLN 702 million of the provision for rehabilitation of post-exploitation mining properties). In comparative period net value of capitalised rehabilitation provision amounted to PLN 632 million (including PLN 543 million of the provision for rehabilitation of post-exploitation mining properties). Capitalised rehabilitation provision is presented in: "land" and "other property, plant and equipment".

## 10. Investment properties

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.

As a result of the acquisition of new subsidiaries, the value of the Group's investment properties increased as of December 31, 2017.

## 11. Intangible assets

	As at December 31, 2017	As at December 31, 2016
Development costs	2	2
Goodwill	734	9
Software	49	73
Other licences and patents	139	132
Acquired right of perpetual usufruct of land	69	64
Other intangible assets	151	134
Intangible assets not commissioned for use	137	239
<b>CARRYING AMOUNT OF INTANGIBLE ASSETS</b>	<b>1,281</b>	<b>653</b>

## Change in intangible assets

	Development costs	Goodwill	Software	Other licences and patents	Acquired right of perpetual usufruct of land	Other intangible assets	Intangible assets not commissioned for use	Total
<b>GROSS BOOK VALUE</b>								
<b>AS AT JANUARY 1, 2017</b>	<b>18</b>	<b>9</b>	<b>448</b>	<b>274</b>	<b>74</b>	<b>256</b>	<b>246</b>	<b>1,325</b>
Capital expenditures	-	-	-	-	-	-	149	149
Intangible assets not commissioned for use	-	-	18	48	-	14	(80)	-
Liquidation, disposal	-	-	(11)	(19)	-	(7)	-	(37)
Purchase of new subsidiaries	1	724	-	25	13	3	-	766
Changes in PGE Group	-	-	(27)	(26)	(8)	(53)	(3)	(117)
Other	-	1	-	(1)	-	16	(167)	(151)
<b>AS AT DECEMBER 31, 2017</b>	<b>19</b>	<b>734</b>	<b>428</b>	<b>301</b>	<b>79</b>	<b>229</b>	<b>145</b>	<b>1,935</b>
<b>ACCUMULATED AMORTIZATION AND IMPAIRMENT LOSSES</b>								
<b>AS AT JANUARY 1, 2017</b>	<b>16</b>	<b>-</b>	<b>375</b>	<b>142</b>	<b>10</b>	<b>122</b>	<b>7</b>	<b>672</b>
Amortisation	1	-	36	58	1	10	-	106
Impairment allowances	-	-	-	1	-	1	37	39
Liquidation, disposal	-	-	(11)	(19)	-	(7)	-	(37)
Changes in PGE Group	-	-	(21)	(20)	(1)	(53)	-	(95)
Other	-	-	-	-	-	5	(36)	(31)
<b>AS AT DECEMBER 31, 2017</b>	<b>17</b>	<b>-</b>	<b>379</b>	<b>162</b>	<b>10</b>	<b>78</b>	<b>8</b>	<b>654</b>
<b>CARRYING AMOUNT</b>	<b>2</b>	<b>734</b>	<b>49</b>	<b>139</b>	<b>69</b>	<b>151</b>	<b>137</b>	<b>1,281</b>
<b>AS AT DECEMBER 31, 2017</b>	<b>2</b>	<b>734</b>	<b>49</b>	<b>139</b>	<b>69</b>	<b>151</b>	<b>137</b>	<b>1,281</b>
<b>GROSS BOOK VALUE</b>								
<b>AS AT JANUARY 1, 2016</b>	<b>19</b>	<b>286</b>	<b>430</b>	<b>223</b>	<b>71</b>	<b>242</b>	<b>201</b>	<b>1,472</b>
Capital expenditures	-	-	-	-	-	-	135	135
Intangible assets not commissioned for use	-	-	24	53	1	11	(89)	-
Liquidation, disposal	-	-	(6)	(3)	(1)	-	-	(10)
Other	(1)	(277)	-	1	3	3	(1)	(272)
<b>AS AT DECEMBER 31, 2016</b>	<b>18</b>	<b>9</b>	<b>448</b>	<b>274</b>	<b>74</b>	<b>256</b>	<b>246</b>	<b>1,325</b>
<b>ACCUMULATED AMORTIZATION AND IMPAIRMENT LOSSES</b>								
<b>AS AT JANUARY 1, 2016</b>	<b>17</b>	<b>-</b>	<b>337</b>	<b>96</b>	<b>10</b>	<b>107</b>	<b>1</b>	<b>568</b>
Amortisation	1	-	44	48	1	9	-	103
Impairment	-	277	-	-	-	6	8	291
Liquidation, disposal	-	-	(6)	(3)	-	-	-	(9)
Other	(2)	(277)	-	1	(1)	-	(2)	(281)
<b>AS AT DECEMBER 31, 2016</b>	<b>16</b>	<b>-</b>	<b>375</b>	<b>142</b>	<b>10</b>	<b>122</b>	<b>7</b>	<b>672</b>
<b>CARRYING AMOUNT</b>	<b>2</b>	<b>9</b>	<b>73</b>	<b>132</b>	<b>64</b>	<b>134</b>	<b>239</b>	<b>653</b>
<b>AS AT DECEMBER 31, 2016</b>	<b>2</b>	<b>9</b>	<b>73</b>	<b>132</b>	<b>64</b>	<b>134</b>	<b>239</b>	<b>653</b>

### Intangible assets not commissioned for use

The presented amounts of intangible assets not commissioned for use as at December 31, 2017, related mainly to IT implementation programmes at the Group and expenditures related to deposit prospecting and evaluation at the Złoczew field.

The available financial projections do not indicate any impairment of intangible assets not commissioned for use.

### Goodwill

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

In the item Acquisition of new subsidiaries the Group presents PLN 724 million as goodwill arising on initial recognition of the acquired EDF assets.

At reporting period, December 31, 2017, goodwill was allocated to the following segments:

- Conventional Generation - PLN 730 million,
- Renewables - PLN 4 million.

## 12. Investments in associates and jointly controlled entities accounted for under the equity method

	As at December 31, 2017	As at December 31, 2016
Polska Grupa Górnicza Sp. z o.o.	533	391
Polimex Mostostal S.A.	91	-
ElectroMobility Poland S.A.	2	3
PEC Bogatynia Sp. z o.o.	8	8
<b>EQUITY-ACCOUNTED INVESTMENTS</b>	<b>634</b>	<b>402</b>

	Polska Grupa Górnicza	Polimex Mostostal	ElectroMobility Poland	PEC Bogatynia
<b>SHARE IN VOTES</b>	<b>15.76%</b>	<b>16.48%</b>	<b>25.00%</b>	<b>34.93%</b>
<b>As at December 31, 2017</b>				
Current assets	1,876	1,586	7	4
Non-current assets	9,074	654	-	22
Current liabilities	3,409	974	-	3
Non-current liabilities	4,167	810	-	1
<b>NET ASSETS</b>	<b>3,374</b>	<b>456</b>	<b>7</b>	<b>22</b>
<b>Share in net assets</b>	<b>532</b>	<b>75</b>	<b>2</b>	<b>8</b>
Goodwill	1	16	-	-
<b>INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD</b>	<b>533</b>	<b>91</b>	<b>2</b>	<b>8</b>

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

The purchase of shares in Polimex Mostostal S.A. is described in note 33.4 to these financial statements.

### 13. Deferred tax in the statement of financial position

#### 13.1 Deferred tax assets

	As at December 31, 2017	As at December 31, 2016
Difference between tax value and carrying amount of property, plant and equipment	2,403	1,559
Difference between tax value and carrying amount of financial assets	48	16
Difference between tax value and carrying amount of financial liabilities	268	272
Difference between tax value and carrying amount of inventories	17	15
LTC compensations	48	253
Rehabilitation provision	548	472
Provision for purchase of CO <sub>2</sub> emission rights	276	220
Provisions for employee benefits	571	529
Other provisions	122	129
Energy infrastructure acquired free of charge and connection payments received	111	129
Other	38	15
<b>DEFERRED TAX ASSETS</b>	<b>4,450</b>	<b>3,609</b>

#### Change in deferred tax - assets

	Year ended December 31, 2017	Year ended December 31, 2016
<b>AS AT JANUARY 1</b>	<b>3,609</b>	<b>3,703</b>
Change in correspondence to financial result	(113)	(39)
Change in correspondence to other comprehensive income	21	(52)
Purchase of new subsidiaries	971	-
Changes in PGE Group	(30)	-
Other changes	(8)	(3)
<b>AS AT 31 DECEMBER 31</b>	<b>4,450</b>	<b>3,609</b>

#### 13.2 Deferred tax liabilities

	As at December 31, 2017	As at December 31, 2016
Difference between tax value and carrying amount of property, plant and equipment	4,188	2,945
Difference between tax value and carrying amount of energy origin units	46	65
Difference between tax value and carrying amount of financial assets	382	377
CO <sub>2</sub> emission rights	274	439
LTC compensations	34	680
Other	125	26
<b>DEFERRED TAX LIABILITIES</b>	<b>5,049</b>	<b>4,532</b>

#### Change in deferred tax - liabilities

	Year ended December 31, 2017	Year ended December 31, 2016
<b>AS AT JANUARY 1</b>	<b>4,532</b>	<b>4,242</b>
Changes recognized in profit or loss	(122)	255
Change in correspondence to other comprehensive income	(13)	34
Purchase of new subsidiaries	661	-
Other changes	(9)	1
<b>AS AT 31 DECEMBER 31</b>	<b>5,049</b>	<b>4,532</b>

#### AFTER OFF-SET OF THE ASSET AND THE LIABILITY IN PARTICULAR COMPANIES THE GROUP'S DEFERRED TAX IS PRESENTED AS:

Deferred tax assets	651	268
Deferred tax provision	(1,250)	(1,191)

## 14. Inventories

	As at December 31, 2017			As at December 31, 2016		
	Historical cost	Impairment allowance	Carrying amount	Historical cost	Impairment allowance	Carrying amount
Renovation materials	689	(44)	645	664	(33)	631
Hard coal	512	-	512	232	-	232
Mazut	42	-	42	15	-	15
Investment materials	1	-	1	14	-	14
Other materials	58	(13)	45	54	(19)	35
<b>TOTAL MATERIALS</b>	<b>1,302</b>	<b>(57)</b>	<b>1,245</b>	<b>979</b>	<b>(52)</b>	<b>927</b>
Green energy origin rights	419	(143)	276	388	(33)	355
Yellow energy origin rights	178	(1)	177	148	(2)	146
Other energy origin rights	33	(1)	32	66	-	66
<b>TOTAL ENERGY ORIGIN RIGHTS</b>	<b>630</b>	<b>(145)</b>	<b>485</b>	<b>602</b>	<b>(35)</b>	<b>567</b>
Hard coal	71	-	71	-	-	-
CO <sub>2</sub> emission rights	2	-	2	37	(8)	29
Other goods	8	(3)	5	7	(2)	5
<b>TOTAL GOODS</b>	<b>81</b>	<b>(3)</b>	<b>78</b>	<b>44</b>	<b>(10)</b>	<b>34</b>
<b>OTHER INVENTORIES</b>	<b>71</b>	<b>-</b>	<b>71</b>	<b>68</b>	<b>-</b>	<b>68</b>
<b>TOTAL INVENTORIES</b>	<b>2,084</b>	<b>(205)</b>	<b>1,879</b>	<b>1,693</b>	<b>(97)</b>	<b>1,596</b>

	2017	2016
<b>IMPAIRMENT ALLOWANCE OF INVENTORIES AS AT JANUARY 1</b>	<b>(97)</b>	<b>(84)</b>
Purchase of new subsidiaries	(14)	-
Fair value measurement of CO <sub>2</sub> emission rights	8	(46)
Recognition of impairment losses	(127)	(52)
Reversal of impairment loss	20	66
Use of impairment loss	5	16
Other changes	-	3
<b>IMPAIRMENT ALLOWANCE OF INVENTORIES AS AT DECEMBER 31</b>	<b>(205)</b>	<b>(97)</b>

Measurement at net sale prices applied mainly to property rights described in detail in note 28.4 to these financial statements.

As described in note 25.5 of these financial statements, PLN 45 million of inventories constituted a collateral for the repayment of liabilities or contingent liabilities.

## 15. CO<sub>2</sub> emission rights for captive use

CO<sub>2</sub> emission rights (EUA) are received 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. Pursuant to art. 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<sub>2</sub> emission. The condition under which free of charge CO<sub>2</sub> emission rights can be obtained is presentation of factual-financial statements from realization of tasks included in National Investment Plan.

In September 2017, PGE Group (including PGE Energia Ciepła S.A.) submitted another report on investments included in the National Investment Plan in order to obtain CO<sub>2</sub> EUA allocations for installations that generate electricity, justified with expenditures incurred to implement these investments in the period from July 1, 2016, to June 30, 2017. A formal assessment of the documents submitted began on November 30, 2017.

EUA	2017		2016 <i>restated data</i>	
	Quantity (Mg million)	Value	Quantity (Mg million)	Value
<b>AS AT JANUARY 1</b>	<b>85</b>	<b>2,349</b>	<b>77</b>	<b>2,172</b>
Purchase of new subsidiaries	-	2	-	-
Purchase	12	247	40	937
Granted free of charge	21	-	26	-
Redemption	(56)	(1,156)	(58)	(760)
<b>AS AT THE REPORTING DATE</b>	<b>62</b>	<b>1,442</b>	<b>85</b>	<b>2,349</b>
Long-term	18	402	47	1,157
Short-term	44	1,040	38	1,192

The decline in the value of CO<sub>2</sub> emission allowances held by PGE Group as at December 31, 2017, results from the start of purchases on the derivative market.



## 16. Other current and non-current assets

### 16.1 Other non-current assets

	As at December 31, 2017	As at December 31, 2016
Advances for property, plant and equipment	432	713
Other non-current assets	92	17
<b>TOTAL OTHER ASSETS</b>	<b>524</b>	<b>730</b>

Advances for construction in progress relate mainly to investment projects conducted by the Conventional Generation segment. An increase in other non-current assets results from co-financing by PGE Energia Ciepła S.A. of an investment in district heating networks.

### 16.2 Other current assets

	As at December 31, 2017	As at December 31, 2016 <i>restated data</i>
<b>PREPAYMENTS</b>		
Fees, agency commission	36	34
Social Fund	3	2
Co-financing of investment in development of district heating networks	15	-
Long-term contracts	20	3
Fees for exclusion of land from agricultural production / forestry	-	4
IT services	8	6
Property and tort insurance	21	2
Other prepayments	21	16
<b>OTHER CURRENT ASSETS</b>		
VAT receivables	216	222
Excise tax receivables	18	100
Advances for deliveries	8	6
Other current assets	25	21
<b>TOTAL OTHER ASSETS</b>	<b>391</b>	<b>416</b>

The amount of VAT is related to an estimate of electricity sales, unread on metering equipment as of the reporting date. 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 comprise the following positions:

	As at December 31, 2017	As at December 31, 2016
Cash on hand and cash at bank	1,309	808
Overnight deposits	34	42
Short-term deposits	1,209	1,819
<b>TOTAL</b>	<b>2,552</b>	<b>2,669</b>
Interest accrued on cash, not received at the reporting date	-	(2)
Exchange differences on cash in foreign currencies	(1)	(1)
<b>Cash and cash equivalents presented in the statement of cash flows</b>	<b>2,551</b>	<b>2,666</b>
Undrawn borrowing facilities as at December 31	6,740	6,081
<i>including overdraft facilities</i>	<i>2,174</i>	<i>2,001</i>

A detailed description of credit agreements is presented in note 25.1.4 of these financial statements.

Restricted cash in total amount of PLN 92 million (PLN 72 million in the comparative period) relate to cash deposit securing the settlements of PGE Group entities with Izba Rozliczeniowa Giełd Towarowych S.A. (Warsaw Commodity Clearing House).

## 18. Discontinued operations

During the year ended December 31, 2017 and December 31, 2016 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's entities create such a fund and make periodic contributions to it. The fund does not possess any property, plant and equipment. 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.

	As at December 31, 2017	As at December 31, 2016
Property, plant and equipment contributed to the fund	1	-
Loans granted to employees	89	91
Cash	50	49
Other fund assets	1	-
Fund liabilities	(135)	(138)
<b>BALANCE AFTER COMPENSATION</b>	<b>6</b>	<b>2</b>
<b>Contributions to the Social Fund</b>	<b>138</b>	<b>130</b>

The assets and liabilities of the Social Fund, as recognised in these financial statements, netted off in the financial statements, appropriately in Other current assets or Other current liabilities.

## 20. Equity

The objective of equity management is to ensure a secure and effective financing structure that takes into account operational risk, investment expenditures and the interests of shareholders and debt investors. Equity management takes place at Group level.

In line with commonly applicable practices, the Group monitors its net debt to EBITDA ratio. Net debt is understood as short- and long-term financial debt (interest-bearing credit and loans, bonds and other debt instruments as well as finance lease liabilities), less cash and cash equivalents and short-term deposits. Restricted cash is not include in calculating net debt.

The Group's aim is to maintain its investment grade credit ratings.

	Year ended December 31, 2017	Year ended December 31, 2016
Net debt / EBITDA	0.99x	0.69x
Net debt / share capital ratio	0.16x	0.12x

Taking into account the scale of of the whole PGE Group, net debt ratio was relatively low during 2017: net debt to EBITDA ratio remains lower than 1.

In connection with an on-going investment programme, a gradual increase in financial leverage is expected as a result of which the Group will be more closely analysing the above ratio. The net debt to EBITDA ratio is a central element of the Group's financial forecasts and plans.

### 20.1 Share capital

	As at December 31, 2017	As at December 31, 2016
1,470,576,500 Series A ordinary Shares with a nominal value of PLN 10.25 each	15,073	15,073
259,513,500 Series B ordinary Shares with a nominal value of PLN 10.25 each	2,660	2,660
73,228,888 Series C ordinary Shares with a nominal value of PLN 10.25 each	751	751
66,441,941 Series D ordinary Shares with a nominal value of PLN 10.25 each	681	681
<b>Total share capital</b>	<b>19,165</b>	<b>19,165</b>

All of the Company's shares are paid up.

After the reporting date and until the date of preparation of the foregoing financial statements there were no changes in the value of the Company's share capital.

## Rights of shareholders - State Treasury rights concerning the Company's activities

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 of 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 organised 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 would result in an actual threat to functioning, continuity of operations and integrity of the critical infrastructure. The objection is expressed in the form of an administrative decision.

### 20.2 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 recognised in the Company's separate financial statements until this capital reached at least one-third of share capital. The part of reserve capital which amounts to one third of share capital can only be used to cover losses recognised in the separate financial statements and cannot be distributed for other purposes. The General Meeting decides on the use of reserve and reserve capital.

Reserve capital subject to distribution to shareholders amounted to PLN 8,940 million as at December 31, 2017 and to PLN 7,342 million as at December 31, 2016.

### 20.3 Hedging reserve

	Year ended December 31, 2017	Year ended December 31, 2016
<b>AS AT JANUARY 1</b>	<b>147</b>	<b>(21)</b>
<b>Change in hedging reserve</b>	<b>(79)</b>	<b>207</b>
<b>Valuation of hedging instruments, including:</b>	<b>(74)</b>	<b>206</b>
<i>Deferral of changes in fair value of hedging financial instruments in the part considered as effective hedge</i>	242	313
<i>Accrued interest on derivatives transferred from hedging reserve and recognised in interest expenses</i>	4	1
<i>Currency revaluation of CCIRS transaction transferred from hedging reserve and recognised in the result on foreign exchange differences</i>	(167)	(107)
<i>Ineffective portion of changes in fair value of hedging derivatives recognised in profit or loss</i>	(5)	(1)
<b>Valuation of other financial instruments</b>	<b>(5)</b>	<b>1</b>
<b>Deferred tax</b>	<b>15</b>	<b>(39)</b>
<b>HEDGING RESERVE AFTER DEFERRED TAX</b>	<b>83</b>	<b>147</b>

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

### 20.4 Foreign exchange differences on 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) and Investment III B.V. as part of consolidation procedures.

## 20.5 Retained earnings and limitations on payment of dividend

Retained earnings which are not subject to distribution are amounts that cannot be paid in the form of dividends.

	As at December 31, 2017	As at December 31, 2016
Amounts included in retained earnings not subject to distribution by the parent company		
<ul style="list-style-type: none"> <li>■ Retained earnings of subsidiaries, attributable to equity holders of the parent company, including consolidation adjustments</li> <li>■ Profit/loss recognised by the parent company in retained earnings through other comprehensive income</li> </ul>	6,075 (3)	8,040 (4)
Retained earnings subject to distribution	4,544	1,598
<b>TOTAL RETAINED EARNINGS PRESENTED IN THE STATEMENT OF FINANCIAL POSITION</b>	<b>10,616</b>	<b>9,634</b>

For information regarding limitations to payment of dividends from reserve capital please refer to 20.2 of these financial statements. As at December 31, 2017 there were no other restrictions on dividend payments.

## 20.6 Equity attributable to non-controlling interests

As at December 31, 2017, equity attributable to non-controlling interests related mainly to the non-controlling interests of EDF's assets in Poland, which is described in note 33.3 to these financial statements.

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

	As at December 31, 2017	As at December 31, 2016
<b>AS AT JANUARY 1</b>	<b>96</b>	<b>96</b>
Share of net profit of subsidiaries	7	(2)
Dividends declared by subsidiaries	(2)	(4)
Purchase of new subsidiaries	1,067	-
Share capital increase and share purchase	-	10
Acquisition of non-controlling interests by the Group	(3)	(4)
<b>AS AT 31 DECEMBER 31</b>	<b>1,165</b>	<b>96</b>

## 20.7 Earnings per share

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

	Year ended December 31, 2017	Year ended December 31, 2016
<b>NET PROFIT/(LOSS) ATTRIBUTABLE TO:</b>	<b>2,667</b>	<b>2,566</b>
equity holders of the parent company	2,660	2,568
non-controlling interests	7	(2)
<b>NET PROFIT / (LOSS) ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY USED TO CALCULATE EARNINGS PER SHARE</b>	<b>2,660</b>	<b>2,568</b>
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
<b>WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES USED TO CALCULATE EARNINGS / (LOSS) PER SHARE</b>	<b>1,869,760,829</b>	<b>1,869,760,829</b>
<b>EARNINGS AND DILUTED EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT COMPANY (IN PLN)</b>	<b>1.42</b>	<b>1.37</b>

## 20.8 Dividends paid and recommended for payment

### Dividend from 2017 profit

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

On May 11, 2017 the Company's Management Board decided to change its dividend policy. In light of the need to finance an ambitious growth programme and with a view towards reducing debt growth, the Company's Management Board recommended the suspension of dividends from profit for years 2016, 2017 and 2018.

After this period, the Company's Management Board intends to recommend to the General Meeting dividend payments to shareholders amounting to 40-50% of consolidated net profit attributable to the parent's shareholders, adjusted for impairment of tangible and intangible assets.

## Dividend from 2016 profit

In line with the updated Dividend Policy, on June 27, 2017 the General Meeting of PGE S.A. adopted a resolution to transfer the entire profit generated in 2016 (PLN 1,598 million) to the Company's supplementary capital.

## 21. Provisions

The carrying amount of provisions is as follows:

	As at December 31, 2017		As at December 31, 2016	
	Non-current	Current	Non-current	Current
Employee benefits	2,316	626	2,148	543
Rehabilitation provision	3,082	4	2,666	4
Provision for shortage of CO <sub>2</sub> emission allowances	112	1,341	-	1,154
Provision for energy origin units held for redemption	-	340	-	416
Provision for non-contractual use of the property	72	11	91	12
Other provisions	84	82	99	52
<b>TOTAL PROVISIONS</b>	<b>5,666</b>	<b>2,404</b>	<b>5,004</b>	<b>2,181</b>

## Changes in provisions

	Employee benefits	Rehabilitation provision	Provision for deficit of CO <sub>2</sub> emission rights	Provisions for energy origin rights held for redemption	Provision for non-contractual use of the property	Other	Total
<b>JANUARY 1, 2017</b>	<b>2,691</b>	<b>2,670</b>	<b>1,154</b>	<b>416</b>	<b>103</b>	<b>151</b>	<b>7,185</b>
Actuarial gains and losses	148	-	-	-	-	-	148
Current service costs	65	-	-	-	-	-	65
Past service costs	(8)	-	-	-	-	-	(8)
Interest costs	82	89	-	-	-	-	171
Discount rate and other assumptions adjustment	24	65	-	-	-	-	89
Benefits paid / Provisions used	(737)	-	(1,156)	(864)	(1)	(24)	(2,782)
Provisions reversed	(28)	(2)	-	(12)	(28)	(33)	(103)
Provisions recognised - costs	579	82	1,205	759	8	50	2,683
Provisions recognised - expenditures	-	70	-	-	-	-	70
Purchase of new subsidiaries	143	27	250	41	-	17	478
Changes in PGE Group	(8)	-	-	-	-	-	(8)
Other changes	(9)	85	-	-	1	5	82
<b>DECEMBER 31, 2017</b>	<b>2,942</b>	<b>3,086</b>	<b>1,453</b>	<b>340</b>	<b>83</b>	<b>166</b>	<b>8,070</b>
Change recognised in operating expenses	(679)	(65)	(1,205)	(747)	-	(25)	(2,721)
Change recognised in other operating income/ (expenses)	-	(42)	-	-	18	6	(18)
Change recognised in other financial income/ (expenses)	(82)	(89)	-	-	2	2	(167)
Change recognised in assets	-	(192)	-	-	-	-	(192)
Change recognised in other comprehensive income	(101)	-	-	-	-	-	(101)

	Employee benefits	Rehabilitation provision	Provision for deficit of CO <sub>2</sub> emission rights	Provisions for energy origin rights held for redemption	Provision for non-contractual use of the property	Other	Total
<b>JANUARY 1, 2016</b>	<b>3,013</b>	<b>3,350</b>	<b>760</b>	<b>380</b>	<b>117</b>	<b>233</b>	<b>7,853</b>
Actuarial gains and losses	(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 recognised - costs	577	34	1,154	375	16	67	2,223
Provisions recognised - expenditures	-	92	-	-	-	-	92
Other changes	14	5	-	-	-	(18)	1
<b>DECEMBER 31, 2016</b>	<b>2,691</b>	<b>2,670</b>	<b>1,154</b>	<b>416</b>	<b>103</b>	<b>151</b>	<b>7,185</b>
Change recognised in operating expenses	(536)	(37)	(1,154)	(372)	-	(3)	(2,102)
Change recognised in other operating income/ (expenses)	-	643	-	-	13	5	661
Change recognised in other financial income/ (expenses)	(82)	(99)	-	-	1	(24)	(204)
Change recognised in assets	-	172	-	-	-	-	172
Change recognised in other comprehensive income	249	-	-	-	-	-	249

## 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 PGE Group will be rehabilitated. 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).

PGE Group creates provision for rehabilitation of post-exploitation mining properties. The amount of the provision recognised 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, 2017 amounted to PLN 2,693 million and as at December 31, 2016 to PLN 2,366 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	2,693	881	(889)

### Provision for rehabilitation of ash storages

PGE Group power generating units raise provisions for rehabilitation of ash storages. As at December 31, 2017, this amounted to PLN 175 million (PLN 98 million at the end of the comparative period).

### Provisions for rehabilitation of post-construction grounds of wind farms

Companies that own wind farms create provision for rehabilitation of post-construction grounds of wind farms. The provision amounted to PLN 53 million as of December 31, 2017 (PLN 49 million at December 31, 2016).

### 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 165 million (PLN 157 million as at the end of the comparative period) and refers to some assets of the Conventional Generation and Renewables segments.

The discount rate used for valuation of rehabilitation provisions as at December 31, 2017 amounted to 3.4% (3.5% in the comparative period).

## 21.2 Provision for shortage of CO<sub>2</sub> emission allowances

The provision for deficit of CO<sub>2</sub> emission allowances is created by PGE Group entities for the shortfall of CO<sub>2</sub> emission allowances obtained free of charge. The amount of the provision takes into account purchased EUAs. As described in note 15 of these financial statements PGE Group is entitled to receive CO<sub>2</sub> 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 PGE Group create provision for energy origin rights related to sale realised 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, 2017 amounted to PLN 340 million (PLN 416 million in the comparative period) and was created mainly by PGE Obrót S.A.

## 21.4 Provision for non-contractual use of the property

PGE Group companies recognise a 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 83 million (of which 38 million relate to litigations). In the comparative period the value of the provision amounted to PLN 103 million (of which PLN 43 million related to litigations).

## 21.5 Other provisions

Other provisions comprise mainly provisions raised for claims relating to real estate tax of PLN 81 million (PLN 90 million in the prior year).

## 22. Employee benefits

	As at December 31, 2017		As at December 31, 2016	
	Non-current	Current	Non-current	Current
Post-employment benefits	1,575	129	1,453	117
Jubilee awards	726	99	694	94
Other provisions for employee benefits	15	398	1	332
<b>Total provisions for employee benefits</b>	<b>2,316</b>	<b>626</b>	<b>2,148</b>	<b>543</b>

### 22.1 Post-employment and jubilee awards provision

The amount of actuarial provisions for post-employment benefits recognised in the financial statements results from the valuation prepared by an independent actuary.

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

	As at December 31, 2017		As at December 31, 2016	
	Non-current	Current	Non-current	Current
Retirement, pension and post-mortem benefits	443	79	396	68
Coal subsidy	138	9	138	9
Energy tariff	621	27	566	26
Social Fund	311	11	293	11
Medical benefits	62	3	60	3
<b>Total post-employment benefits</b>	<b>1,575</b>	<b>129</b>	<b>1,453</b>	<b>117</b>
Jubilee awards	726	99	694	94
<b>TOTAL ACTUARIAL PROVISIONS</b>	<b>2,301</b>	<b>228</b>	<b>2,147</b>	<b>211</b>

### 22.2 Other provisions for employee benefits

	As at December 31, 2017		As at December 31, 2016	
	Non-current	Current	Non-current	Current
Provision for Voluntary Leave Program costs	14	23	-	34
Annual bonus and other employee bonuses	-	196	-	153
Unused annual holiday leave	-	139	-	131
Other provisions for employee benefits	1	40	1	14
<b>TOTAL OTHER PROVISIONS FOR EMPLOYEE BENEFITS</b>	<b>15</b>	<b>398</b>	<b>1</b>	<b>332</b>



### Change in provisions for employee benefits

	Retirement, pension and post-mortem benefits	Coal allowance	Energy tariff	Social Fund	Medical benefits	Jubilee awards	Other employee benefits	Total
<b>AS AT JANUARY 1, 2017</b>	<b>464</b>	<b>147</b>	<b>592</b>	<b>304</b>	<b>63</b>	<b>788</b>	<b>333</b>	<b>2,691</b>
Actuarial gains and losses	24	(1)	51	8	-	66	-	148
Discount rate adjustment	4	1	9	4	1	5	-	24
Current service costs	16	1	7	5	1	35	-	65
Past service costs	(4)	-	(7)	3	-	-	-	(8)
Interest costs	16	7	20	11	2	26	-	82
Benefits paid / Provisions used	(17)	(8)	(24)	(11)	(3)	(95)	(579)	(737)
Provisions reversed	-	-	-	-	-	-	(28)	(28)
Provisions recognised	-	-	-	-	-	-	579	579
Purchase of new subsidiaries	20	-	-	-	-	-	123	143
Changes in PGE Group	(1)	-	-	-	-	-	(7)	(8)
Other changes	-	-	-	(2)	1	-	(8)	(9)
<b>AS AT DECEMBER 31, 2017</b>	<b>522</b>	<b>147</b>	<b>648</b>	<b>322</b>	<b>65</b>	<b>825</b>	<b>413</b>	<b>2,942</b>
Change recognised in operating expenses	(12)	(1)	-	(8)	(1)	(106)	(551)	(679)
Change recognised in other financial income/ (expenses)	(16)	(7)	(20)	(11)	(2)	(26)	-	(82)
Change recognised in other comprehensive income	(28)	-	(60)	(12)	(1)	-	-	(101)

  

	Retirement, pension and post-mortem benefits	Coal allowance	Energy tariff	Social Fund	Medical benefits	Jubilee awards	Other employee benefits	Total
<b>AS AT JANUARY 1, 2016</b>	<b>492</b>	<b>160</b>	<b>693</b>	<b>312</b>	<b>64</b>	<b>953</b>	<b>339</b>	<b>3,013</b>
Actuarial gains and losses	(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 recognised	-	-	-	-	-	-	577	577
Other changes	1	-	-	-	-	1	13	15
<b>AS AT DECEMBER 31, 2016</b>	<b>464</b>	<b>147</b>	<b>592</b>	<b>304</b>	<b>63</b>	<b>788</b>	<b>333</b>	<b>2,691</b>
Change recognised in operating expenses	(24)	(5)	(50)	(21)	(3)	98	(531)	(536)
Change recognised in other financial income/ (expenses)	(15)	(7)	(21)	(9)	(2)	(28)	-	(82)
Change recognised in other comprehensive income	53	17	148	27	4	-	-	249

Sensitivity analysis of the value of actuarial provisions as at December 31, 2017, 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	522	43	(35)	(36)	47
Coal subsidy	147	15	(12)	(14)	16
Energy tariff	648	99	(79)	(80)	106
Social Fund	322	45	(37)	(39)	47
Medical benefits	65	7	(7)	(7)	7
Jubilee awards	825	55	(49)	(49)	60
<b>TOTAL</b>	<b>2,529</b>	<b>264</b>	<b>(219)</b>	<b>(225)</b>	<b>283</b>

## 23. Deferred income and governments grants

### 23.1 Non-current deferred income and government grants

	As at December 31, 2017	As at December 31, 2016
<b>GOVERNMENT GRANTS</b>		
Grants received from NFOŚiGW (environmental funds)	255	260
Redemption of loans from environmental funds	37	41
Other government grants	136	153
<b>DEFERRED INCOME</b>		
Subsidies received and connection fees	478	523
Donations and property, plant and equipment granted free of charge	78	86
Lease income	-	25
Other deferred income	54	53
<b>NON-CURRENT GOVERNMENT GRANTS AND DEFERRED INCOME, TOTAL</b>	<b>1,038</b>	<b>1,141</b>

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 governments grants

	As at December 31, 2017	As at December 31, 2016
<b>GOVERNMENT GRANTS</b>		
Grants received from NFOŚiGW (environmental funds)	13	12
Redemption of loans from environmental funds	3	2
Other government grants	10	8
<b>DEFERRED INCOME</b>		
Subsidies received and connection fees	68	79
Donations and property, plant and equipment granted free of charge	9	8
Lease income	-	3
Other deferred income	12	7
<b>CURRENT GOVERNMENT GRANTS AND DEFERRED INCOME, TOTAL</b>	<b>115</b>	<b>119</b>

## 24. Other non-financial liabilities

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

	As at December 31, 2017	As at December 31, 2016
Environmental fees	234	243
VAT liabilities	126	122
Excise tax liabilities	128	129
Payroll liabilities	266	239
Liabilities from social insurances	246	237
Personal income tax	85	80
Liabilities due to Voluntary Leave Programs	12	51
Advances for deliveries	147	143
Tax on share capital increase	-	110
Other	61	70
<b>TOTAL OTHER LIABILITIES</b>	<b>1,305</b>	<b>1,424</b>

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 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.

## 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, 2017		As at December 31, 2016	
	Non-current	Current	Non-current	Current
Trade receivables	-	3,159	-	2,705
Deposits	148	6	136	2,300
LTC compensations	-	10	-	1,241
Debt securities including bonds	-	-	89	-
Bails and security deposits	-	95	2	12
Other financial receivables, included compensation	10	252	10	67
<b>FINANCIAL RECEIVABLES</b>	<b>158</b>	<b>3,522</b>	<b>237</b>	<b>6,325</b>

##### Trade receivables

The main component of trade receivables are receivables recognised by the company PGE Obrót S.A. Receivables from households account for about 10% of the consolidated balance of trade receivables, while receivables from the corporate clients of PGE Obrót S.A. represent about 63% of the consolidated balance of trade receivables. As at December 31, 2017, the share of the three most significant customers of the PGE Group amounted to approximately 7% of the total consolidated balance. Additional information relating to trade receivables is presented in note 26.6.1 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 consists mainly of guarantee fund, compensation and disputed receivables described in note 28.4 of these financial statements.

#### 25.1.2 Derivates and other receivable measured at fair value through profit or loss

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

	As at December 31, 2017			
	Recognised in profit or loss	Recognised in other comprehensive income	Assets	Liabilities
<b>DERIVATIVES AT FAIR VALUE THROUGH PROFIT OR LOSS</b>				
Currency forwards	(32)	-	1	49
Commodity forwards	(4)	-	14	-
Commodity SWAP	5	-	64	7
Contracts for purchase/sale of coal	-	-	9	20
IRS transactions	16	-	-	10
Options	17	-	24	-
<b>HEDGING DERIVATIVES</b>				
CCIRS hedges	(168)	(22)	44	-
IRS hedges	(3)	(48)	98	5
Currency forwards	(23)	(4)	1	33
<b>OTHER ASSETS CARRIED AT FAIR VALUE THROUGH PROFIT OR LOSS</b>				
Investment fund participation units	-	-	50	-
<b>TOTAL</b>	<b>(192)</b>	<b>(74)</b>	<b>305</b>	<b>124</b>
current			83	106
non-current			222	18

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

### Commodity and currency forwards

Commodity and currency forward transactions mainly relate to trade in CO<sub>2</sub> emission rights.

### Options

On January 20, 2017 PGE S.A. purchased a call option to purchase shares of Polimex-Mostostal S.A. from Towarzystwo Finansowe Silesia Sp. z o.o. The option was valued using the Black-Scholes method. The option exercise dates are: July 30, 2020, July 30, 2021 and July 30, 2022.

### Coal swaps

In the current period, PGE Paliwa sp. z o.o. in order to secure commodity risk related to the price of imported coal executed a number of transactions to hedge this risk using commodity swaps for coal. The number and value of these transactions is correlated to the quantity and value of imported coal. Changes in fair value are recognised in profit or loss.

### Purchase and sale contracts with physical delivery of coal

PGE Paliwa Sp. z o.o. measures all of its sales and purchase contracts with physical delivery of coal at fair value using the trader-broker model. As at the reporting date, the Company held contracts that would be performed in 2018.

### IRS transactions

In the present periods, PGE S.A. executed an IRS transaction to hedge interest rates on a credit facility with a nominal value of PLN 500 million. To recognise this IRS transaction, the Company uses hedge accounting.

In 2016, PGE S.A. executed IRS transactions to hedge interest rates on credit facilities with a total nominal value of PLN 4,630 million. To recognise these IRS transactions, the Company uses hedge accounting.

The impact of hedge accounting is presented in note 20.3 to these financial statements.

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

In 2003, Elektrownia Turów S.A. (currently a branch of PGE Górnictwo i Energetyka Konwencjonalna S.A.) concluded an IRS hedge transactions - swap. This transaction hedges variable interest rates (USD LIBOR 6m) on an investment credit of USD 80 million taken from Nordic Investment Bank to finance investments in Turów power plant. Changes in the fair value of IRS transactions are fully recognised in profit or loss.

### CCIRS hedges

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 - counterparties 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, a relevant part of the CCIRS transaction is treated as a hedge of bonds issued by PGE Sweden AB (publ).

To recognise these CCIRS transactions, the Group uses hedge accounting. The impact of hedge accounting is presented in note 20.3 to 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. 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. As at December 31, 2017, and December 31, 2016, there was no need to recognise an impairment loss on available-for-sale financial assets.

## 25.1.4 Loans, borrowings, bonds and lease

	As at December 31, 2017		As at December 31, 2016	
	Non-current	Current	Non-current	Current
Loans and borrowings	5,788	570	5,839	332
Bonds issued	2,632	1,051	3,764	78
Lease	2	2	-	1
<b>TOTAL LOANS, BORROWINGS, BONDS AND LEASE</b>	<b>8,422</b>	<b>1,623</b>	<b>9,603</b>	<b>411</b>

### Currency position and interest rates

As at December 31, 2017

Currency	Reference rate	Value in currency	Value in PLN	Final maturity date
PLN	Variable	6,351	6,351	Credit, loans - October 2018 - December 2028; bonds - indefinite programme, maturity date for issued tranche - June 2018
	Fixed	356	356	Credit, loans - October 2018 - December 2028
<b>TOTAL PLN</b>		<b>6,707</b>	<b>6,707</b>	
EUR	Variable	111	465	Credit and loans - June 2024
	Fixed	643	2,682	Bonds - June 2019 - August 2029
<b>TOTAL EUR</b>		<b>754</b>	<b>3,147</b>	
USD	Variable	55	191	Credit, loans - May 2019 - September 2020
<b>TOTAL USD</b>		<b>55</b>	<b>191</b>	
<b>TOTAL LOANS, BORROWINGS, BONDS AND LEASE</b>			<b>10,045</b>	

As at December 31, 2016

Currency	Reference rate	Value in currency	Value in PLN	Final maturity date
PLN	Variable	6,381	6,381	Credit, loans - September 2017 - December 2028; bonds - indefinite programme, maturity date for issued tranche - June 2018
	Fixed	121	121	credit, loans - December 2017 - December 2028
<b>TOTAL PLN</b>		<b>6,502</b>	<b>6,502</b>	
EUR	Variable	129	569	Credit and loans - June 2024
	Fixed	642	2,842	Bonds - June 2019 - August 2029
<b>TOTAL EUR</b>		<b>771</b>	<b>3,411</b>	
USD	Variable	24	101	Credit, loans - May 2019
<b>TOTAL USD</b>		<b>24</b>	<b>101</b>	
<b>TOTAL LOANS, BORROWINGS, BONDS AND LEASE</b>			<b>10,014</b>	

### Maturity of loans, borrowings, bonds and lease

	As at December 31, 2017	As at December 31, 2016
Within 1 year	1,623	412
From 1 year to 2 years	2,471	1,374
From 2 year to 3 years	464	2,502
From 3 year to 4 years	1,108	373
From 4 year to 5 years	1,636	1,042
Over 5 years	2,743	4,311
<b>TOTAL LOANS, BORROWINGS, BONDS AND LEASE</b>	<b>10,045</b>	<b>10,014</b>

The following table illustrates changes in interest-bearing debt in the years ended December 31, 2017 and 2016:

	Year ended December 31, 2017	Year ended December 31, 2016
<b>AS AT JANUARY 1</b>	<b>10,014</b>	<b>5,409</b>
<b>CHANGE IN OVERDRAFTS</b>	<b>67</b>	<b>(7)</b>
<b>CHANGE IN LOANS, BORROWINGS, BONDS AND LEASE (excluding overdrafts)</b>	<b>(36)</b>	<b>4,612</b>
Drawn loans, borrowings, leases / issued bonds	125	4,652
Repayment of loans, borrowings, leases / redemption of bonds	(193)	(196)
Accrued interest	226	134
Paid interest	(220)	(113)
Foreign exchange differences	(214)	135
Acquisition of new companies	240	-
<b>AS AT DECEMBER 31</b>	<b>10,045</b>	<b>10,014</b>

### Loans and borrowings

Among loans and borrowings presented above as at December 31, 2017, PGE Group presents mainly the following facilities:

- investment credit facility taken out by PGE Górnictwo i Energetyka Konwencjonalna S.A. from Nordic Investment Bank to finance construction of 858 MW power block in Bełchatów Power Plant of PLN 464 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, 2017, 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. and Bank Polska Kasa Opieki S.A., executed 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, 2017, 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 a maturity date of December 31, 2028. As at December 31, 2017, the Company used all 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 modernisation 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 CHP and Rzeszów CHP. 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, 2017, the Company did not use these credit lines.

As at December 31, 2017, the value of the available overdrafts at significant PGE Group companies was PLN 2,174 million. The repayment date of used overdraft facilities of PGE Group's key companies is February and April 2018. The Group is working on extending the agreements related to overdraft facilities.

### 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 issued bonds in the amount of EUR 138 million, with 15 year maturity.

**25.1.5 Trade and other financial liabilities**

	As at December 31, 2017		As at December 31, 2016	
	Non-current	Current	Non-current	Current
Trade liabilities	-	1,650	-	976
Purchase of property, plant and equipment and intangible assets	-	1,418	12	1,225
Bails and security deposits received	22	87	21	65
Liabilities related to LTC	332	-	-	1,253
Insurance	-	17	-	-
Other	25	59	-	37
<b>TRADE AND OTHER FINANCIAL LIABILITIES</b>	<b>379</b>	<b>3,231</b>	<b>33</b>	<b>3,556</b>

**25.2 Fair value of financial instruments**

The value of financial assets and liabilities measured at amortised 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 amortised cost presented in these financial statements as at December 31, 2017 amounted to EUR 643 million and their estimated fair value amounted to EUR 667 million. The indicators used in the valuation belong to Level 2 of fair value hierarchy.

**Instruments not quoted on active markets, for which 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. These assets are measured at purchase prices less impairment.

**25.3 Fair value hierarchy****Inventories**

During the reporting period the Group held CO<sub>2</sub> emission rights a part of which was purchased in order to benefit from market price swings. This part of the emission allowances is recognised in inventories at fair value less costs of disposal. Fair value is 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).



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

FAIR VALUE HIERARCHY	As at December 31, 2017		As at December 31, 2016	
	Level 1	Level 2	Level 1	Level 2
CO <sub>2</sub> emission rights	-	-	29	-
<b>Inventories</b>	-	-	<b>29</b>	-
Currency forward	-	2	-	1
Commodity forward	-	14	-	8
Commodity SWAP	-	64	-	-
Contracts for purchase/sale of coal	-	9	-	-
CCIRS valuation	-	44	-	231
IRS valuation	-	98	-	125
Options	-	24	-	-
Fund participation units	-	50	-	-
<b>Financial assets</b>	-	<b>305</b>	-	<b>365</b>
Currency forward	-	82	-	-
Commodity forward	-	-	-	-
Commodity SWAP	-	7	-	-
Contracts for purchase/sale of coal	-	20	-	-
IRS valuation	-	15	-	30
<b>Financial liabilities</b>	-	<b>124</b>	-	<b>30</b>

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 were no transfers of financial instruments between the first and second level of fair value hierarchy.

Presented below are the terms of the derivative instruments and other receivables carried at fair value through profit or loss.

	As at December 31, 2017		As at December 31, 2016		Maturity
	Value in financial statements in PLN	Nominal value in currency	Value in financial statements in PLN	nominal value in currency	
Currency forward - EUR			1	17	by January 2018
Commodity forward sale EUA - EUR	-	-	8	9	by March 2020
Commodity forward purchase EUA - EUR				-	by March 2020
CCIRS – EUR to PLN	44	514	231	514	by June 2019
		144		144	by July 2029
IRS – interest rate PLN	98	3,630	125	3,630	by September 2023
		1,000		1,000	by December 2027
Options	24	6	-	-	by July 2022
Investment fund participation units	50	50	-	-	n/a
Commodity forward - EUR	14	219	-	-	by March 2020
		12		-	
Currency forward - EUR	1	6	-	-	by April 2019
Commodity SWAP - USD	64	79	-	-	by December 2018
		1		-	
Currency forward - USD	1	3	-	-	by January 2019
Contracts for purchase - USD	9	100	-	-	by December 2018
Contracts for sale - USD		26		-	
<b>Financial assets</b>	<b>305</b>	-	<b>365</b>		
Currency forward - EUR	(19)	193	-	1	by March 2020
		500		-	by December 2027
IRS – interest rate PLN	(13)	1,000	23	1,000	by June 2018
IRS - interest rate USD	(2)	16	(7)	24	by June 2018
Currency forward - EUR	(30)	137	-	-	by April 2020
Commodity SWAP - USD	(7)	1	-	-	by December 2018
		12		-	
Currency forward - USD		121		-	
Currency forward - EUR	(28)	8		-	by January 2019
Currency forward - USD	(5)	25		-	by November 2018
Contracts for purchase - USD	(20)	45		-	by December

Contracts for sale - USD		53	-	-	2018
<b>Financial liabilities</b>		<b>(124)</b>		<b>(30)</b>	

## 25.4 Statement of comprehensive income

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

Year ended December 31, 2017	Cash	Financial instruments measured at fair value	Hedging derivatives	Available-for- sale financial assets	Loans and receivables	Financial liabilities at amortised cost	TOTAL
Dividends	-	-	-	5	-	-	5
Interest income / (expenses)	67	(4)	(4)	-	16	(160)	(85)
Exchange differences	(4)	-	(166)	-	(2)	214	42
Reversal of impairment / revaluation	-	37	-	-	2	-	39
Recognition of impairment / revaluation	-	(12)	-	-	(92)	(7)	(111)
Loss on disposal of investment	-	-	-	(93)	-	-	(93)
<b>TOTAL PROFIT/ (LOSS)</b>	<b>63</b>	<b>21</b>	<b>(170)</b>	<b>(88)</b>	<b>(76)</b>	<b>47</b>	<b>(203)</b>

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 amortised cost	TOTAL
Dividends	-	-	-	2	-	-	2
Interest income / (expenses)	22	(23)	(61)	-	28	(42)	(76)
Exchange differences	11	-	107	-	3	(140)	(19)
Reversal of impairment / revaluation	-	25	1	-	91	-	117
Recognition of impairment / revaluation	-	(10)	-	-	(2)	-	(12)
<b>TOTAL PROFIT/ (LOSS)</b>	<b>33</b>	<b>(8)</b>	<b>47</b>	<b>2</b>	<b>120</b>	<b>(182)</b>	<b>12</b>

## 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, 2017	As at December 31, 2016
Property, plant and equipment	862	915
Inventories	45	51
Trade receivables	52	34
<b>TOTAL ASSETS AS COLLATERAL FOR REPAYMENT OF LIABILITIES</b>	<b>959</b>	<b>1,000</b>

Property, plant and equipment presented in the table above are collaterals for repayment of drawn investment credits. As at December 31, 2017 and as at December 31, 2016 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.

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

PGE Group companies 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, 2017 it amounted to PLN 92 million (PLN 72 million in the comparative period).

## 26. Objectives and principles of financial risk management

The main goal of financial risk management at 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.

Responsibility for managing PGE Group's financial risk lies with the Management Board of PGE S.A. The Management Board specifies risk appetite, understood as an acceptable level of deterioration of PGE Group's financial results, taking into consideration its current and planned economic and financial situation. The Management Board also decided on the allocation of risk appetite to specific business areas.

The organisation of a function of financial risk management at PGE Group is based on the principle of independence of an entity responsible for measurement and control of risk at PGE Group (Risk Department at PGE Polska Grupa Energetyczna S.A.) vs business entities (risk owners) responsible for taking and managing the risk on an ongoing basis. Risk reports are submitted directly to the Risk Committee, Audit Committee and the Management Board of PGE S.A.

PGE Group has a Risk Committee that exercises oversight of the financial and corporate risk management process at PGE Group. The Risk Committee monitors PGE Group's exposure levels, sets limits for significant financial risks, accepts methodologies in financial risk resulting from trade and finance activities, permits expansions of activities in new business areas and makes key decisions regarding risk management.

Financial risk is managed at Group level, in an integrated manner. This process is implemented and/or supervised by PGE Group's Corporate Centre, which is a centre of competences in this area. Exposures to risk generated by business areas are examined on a comprehensive basis, taking into account interdependencies, the possibility of using natural hedging effects and the overall impact on PGE Group's risk profile and financial situation.

The financial risk management model includes:

- collection and consolidation of data on exposure to particular categories of financial risk;
- calculation of Value-at-Risk and Profit-at-Risk for specific risk factors and overall for all risk factors;
- management of the PGE Group's consolidated exposure in relation to capital at risk and risk limits established based on it (including the identification and implementation of hedging strategies).

In key areas of financial risk, PGE Group has implemented internal regulations for managing these risks.

PGE Group is exposed to a variety of financial risks:

- market risk (commodity risk, interest rate risk, currency risk);
- liquidity risk;
- credit risk.

PGE Group's exposure to specific financial risks depends on the scope of activities in commodity and financial markets.

### 26.1 Market risk

Market risk covers commodity risk, interest rate risk, currency risk.

The main objective of managing market risk at PGE Group is to retain a level of risk resulting from trade and finance activities at an acceptable level and to support business strategy and maximisation of the Group's value for shareholders.

PGE Group's procedures for managing specific market risk categories in trade and finance activities specify the following:

- objective, scope and rules for managing risk;
- responsibility for managing risk;
- management and operational processes within risk management in trade activities on electricity markets and electric product markets and as regards finance activities;
- ways of identifying sources of exposure to risk;
- methods for measuring and monitoring exposures to risk.

PGE Group's market risk management rules also specify ways to set risk appetite, limit exposures to market risk based on Profit-at-Risk and Value-at-Risk and mechanisms for limiting risk when limits are exceeded.

### 26.1.1 Commodity risk

Commodity risk is related to the possibility that financial results deteriorate as a result of changes in commodity prices.

PGE Group companies' exposure to commodity risk relates to the following commodity markets:

- Electricity;
- CO<sub>2</sub> emission rights;
- rights to electricity origin certificates;
- hard coal;
- natural gas;
- biomass and other fuels.

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.

Selected types of commodity risk (including currency) that PGE Group is exposed to:

Risk associated with	Description	Example of exposure source
Risk of changes in electricity prices	<ul style="list-style-type: none"> <li>▪ PGE Group has a natural long position due to its generation assets and a lack of possibility to place its production on the market at a pre-determined price.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Cost to generate electricity,</li> <li>▪ Price of electricity sale contracts to retail clients,</li> <li>▪ Price of transactions to buy/sell energy on the wholesale market,</li> </ul>
Risk of changes in the prices of property rights to electricity origin certificates;	<ul style="list-style-type: none"> <li>▪ PGE Group has a net short position resulting from the obligation to redeem property rights related to the sale of electricity to end users.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Price of transactions to buy/sell property rights on the wholesale market,</li> </ul>
Risk of changes in the prices of CO <sub>2</sub> emission allowances	<ul style="list-style-type: none"> <li>▪ Risk related to changes in the prices of CO<sub>2</sub> emission allowances in EUR and risk of changes in EUR/PLN exchange rate;</li> <li>▪ PGE Group has a short position given its electricity generation at units participating in the EU-ETS scheme.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Use of generation sources not as planned due to their varying emission levels;</li> <li>▪ Uncertainty with regard to volume of free allowances received in EU-ETS scheme;</li> <li>▪ Price of transactions to buy/sell CO<sub>2</sub> emission allowances on the wholesale market.</li> </ul>
Risk of fuel price changes (including hard coal, natural gas, biomass, heating oil)	<ul style="list-style-type: none"> <li>▪ Risk of commodity price changes, including commodities denominated in foreign currency (or indexed to foreign currency) and foreign currency risk;</li> <li>▪ PGE Group has a short position due to its need to purchase fuel on the market.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Price of transactions to buy/sell fuel on the wholesale market.</li> </ul>
Long-term volume risk	<ul style="list-style-type: none"> <li>▪ Risk related to changes in demand for electricity in the National Power System.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Macroeconomic situation, especially in energy-intensive industries;</li> <li>▪ Technological changes, especially in energy efficiency;</li> <li>▪ Climate changes;</li> <li>▪ Regulations, including preferences for specific sectors of the energy industry;</li> <li>▪ Degree of integration with foreign power systems.</li> </ul>
Short-term volume risk	<ul style="list-style-type: none"> <li>▪ Risk related to changes in planned electricity sales volumes as a result of changes in retail demand for electricity</li> </ul>	<ul style="list-style-type: none"> <li>▪ Trends among retail clients concerning changes in energy providers;</li> <li>▪ Regulations, including those pertaining to the opportunity to change energy providers;</li> <li>▪ Short-, mid-term weather changes;</li> <li>▪ Risk associated to the model for planning demand for energy and quality of source data used in planning.</li> </ul>

PGE Group has a strategy for hedging key exposures in trading electricity and related commodities adequately to the level of risk appetite over a mid-term horizon. The level of hedging for an open position is set taking into account risk appetite, results of monitoring the risk of electricity and related product prices, liquidity of specific markets as well as the financial situation of the Group and the Group's strategic objectives.

PGE Group's exposure to commodity price risk (as regards raw materials) reflects the volume of external purchases of each raw material, as presented in the table below:

COMMODITY	Year ended December 31, 2017		Year ended December 31, 2017	
	Tonnage – external purchase (in thousand tonnes)	Purchase costs (PLN million)	Tonnage – external purchase (in thousand tonnes)	Purchase costs (PLN million)
Hard coal	6,211	1,395	5,340	1,141
CO <sub>2</sub> emission rights for captive use	11,447	247	40,681	937
Natural gas [thousand m <sup>3</sup> ]	756,850	527	659,542	454
Biomass	528	99	868	190
Fuel oil	36	51	41	41
<b>TOTAL</b>		<b>2,319</b>		<b>2,763</b>

As described in note 15 to these financial statements, the Group changed rules for purchasing CO<sub>2</sub> emission allowances.

### 26.1.2 Interest rate risk

Interest rate risk is related to the possibility that financial results deteriorate as a result of changes in interest rates.

PGE Group's exposure to interest rate risk results from the fact that PGE Group companies finance their operating and investing activities with financing at variable interest rates, in the form of credits, loans and bonds in domestic and foreign currency, or through investments in financial assets at variable or fixed interest rates.

PGE Group controls interest rate risk through a system of limits relating to the maximum potential loss due to changes in interest rates in related to consolidated exposure to interest rate risk by PGE Group companies. The interest rate risk measure is based on the Value at Risk methodology.

Moreover, PGE Group sets out hedging strategies in relation to consolidated exposure to the Group's interest rate risk through hedging coefficients that are subject to approval by the Risk Committee and Management Board of PGE S.A. The hedging strategy and level of interest rate risk are subject to monitoring and are regularly reported to the Risk Committee.

PGE Group companies executes derivative transactions concerning instruments that are based on interest rate only in order to hedge identified risk exposures. Regulations applicable to PGE Group do not permit derivative transactions based on interest rate for the purposes of speculative transactions that would be intended to generate additional earnings resulting from changes in interest rates while exposing the Company to a risk of potential losses.

Bonds issued in the amount of PLN 1 billion under the Bonds issue program of PLN 5 billion are interest-bearing bonds at a variable rate in PLN. Payments under these bonds are secured using Interest Rate Swaps.

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.

Long-term bank credit of PLN 1.5 billion under the terms of Credit Agreements signed on December 17, 2014, and December 4, 2015, 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. These credit facilities are based on variable interest rates in PLN. Payments under these credit facilities are secured using Interest Rate Swaps.

Bond programmes are described in note 25.1.4, hedging instruments in note 25.1.4 to these financial statements.

PGE Group's exposure to interest rate risk and concentration of this risk by currencies:

PGE Group's exposure to interest rate risk and concentration of this risk by currency:

			As at December 31, 2017	As at December 31, 2016
		Type of interest		
Derivatives - assets exposed to interest rate risk	PLN	Fixed	-	-
		Variable	122	125
	Other currencies	Fixed	-	-
		Variable	133	240
Deposits, cash and debt securities	PLN	Fixed	2,553	5,046
		Variable	4	-
	Other currencies	Fixed	153	59
		Variable	-	89
Derivatives – liabilities, exposed to interest rate risk	PLN	Fixed	-	-
		Variable	(13)	(23)
	Other currencies	Fixed	-	-
		Variable	(111)	(7)
Loans, borrowings, bonds and lease	PLN	Fixed	(356)	(121)
		Variable	(6,351)	(6,381)
	Other currencies	Fixed	(2,682)	(2,842)
		Variable	(655)	(670)
<b>Net exposure</b>	<b>PLN</b>	<b>Fixed</b>	<b>2,197</b>	<b>4,925</b>
		<b>Variable</b>	<b>(6,238)</b>	<b>(6,279)</b>
	<b>Other currencies</b>	<b>Fixed</b>	<b>(2,529)</b>	<b>(2,783)</b>
		<b>Variable</b>	<b>(633)</b>	<b>(348)</b>

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.

### 26.1.3 Currency risk

Currency risk is related to the possibility that financial results deteriorate as a result of changes in currency prices.

The main sources of PGE Group's exposure to currency risk are presented below:

- capital expenditures denominated in or indexed to foreign currencies;
- loans and borrowings 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<sub>2</sub> 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;
- other operating flows denominated in or indexed to foreign currencies.

PGE Group controls currency risk through a system of limits relating to the maximum potential loss due to changes in exchange rates in related to consolidated exposure to currency risk by PGE Group companies. The currency risk measure is based on the Value at Risk methodology.

Moreover, PGE Group sets out hedging strategies for the Group's currency risk using hedging ratios subject to approval by the Company's Risk Committee and Management Board. The hedging strategy and level of currency risk are subject to monitoring and are regularly reported to the Risk Committee.

PGE Group companies conclude derivative transactions concerning instruments that are based on interest rates only in order to hedge identified risk exposures.

Regulations applicable to PGE Group do not permit derivative transactions based on currency for the purposes of speculative transactions that would be intended to generate additional earnings resulting from changes in currencies while exposing the Company to a risk of potential losses.

The following tables present the Group's exposure to currency risk by class of financial instrument:

	Total value in financial statements in PLN	CURRENCY POSITION AT DECEMBER 31, 2017			
		EUR		USD	
		Currency	PLN	Currency	PLN
<b>FINANCIAL ASSETS</b>					
Trade and other financial receivables, including:	3,680	3	13	3	10
<i>Trade receivables</i>	3,159	-	-	3	10
<i>Other receivables</i>	350	3	13	-	-
Cash and cash equivalents	2,552	32	132	6	21
Derivatives, including:	305	720	3,004	23	79
<i>Measured at fair value through profit or loss</i>	89	9	38	23	79
<i>Hedging instruments</i>	44	711	2,966	-	-
<b>FINANCIAL LIABILITIES</b>					
Loans, borrowings, bonds, including:	(10,045)	(753)	(3,306)	(55)	(191)
<i>Interest bearing loans and borrowings</i>	(6,358)	(111)	(464)	(55)	(191)
<i>Bonds issued and debt securities</i>	(3,683)	(642)	(2,842)	-	-
Trade and other financial liabilities measured at amortised cost	(3,610)	(8)	(34)	(22)	(76)
<i>Trade liabilities</i>	(1,650)	(1)	(5)	(22)	(76)
<i>Liabilities due to purchase of property, plant and equipment, intangible assets</i>	(1,418)	(1)	(4)	-	-
<i>Other financial liabilities</i>	(542)	(6)	(25)	-	-
Derivatives, including:	(124)	(338)	(1,405)	(167)	(583)
<i>Measured at fair value through profit or loss</i>	(106)	(338)	(1,405)	(140)	(488)
<i>Hedging instruments</i>	(5)	-	-	(27)	(95)
<b>NET CURRENCY POSITION</b>		<b>(344)</b>	<b>(1,596)</b>	<b>(212)</b>	<b>(740)</b>

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

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.

## 26.2 Liquidity risk

Liquidity risk concerns a situation in which the company is unable to meet its liabilities (current or non-current) when they become due.

The main objective of liquidity risk management at PGE Group is to ensure and maintain the companies' ability to meet their existing and future financial liabilities, taking into account the cost to obtain liquidity.



Liquidity risk management at PGE Group involves planning and monitoring short- and long-term cash flows from operating, investing and financing activities and taking action intended to secure funds for the activities of PGE Group, while limiting the cost of these actions.

Periodic planning and monitoring of liquidity makes it possible to secure funds for any liquidity gaps by allocating funds among PGE Group companies (cash pooling) as well as using external financing, including overdrafts.

Liquidity risk management in the long term allows PGE Group to define its borrowing capacity and supports decisions regarding the financing of long-term investments.

PGE Group has a central financing model in which, as a rule, agreements relating to external financing are executed by PGE S.A. PGE Group subsidiaries use various sources of intra-group financing such as loans, bonds, bank account consolidation agreements and real cash pooling agreements.

PGE Group uses various financing sources, such as overdrafts, term loans and investment loans, issue of domestic bonds and eurobonds.

The following table presents maturities of the Group's financial liabilities at reporting dates by maturity based on contractual non-discounted payments

	Carrying amount	Total payments	Under 3 months	From 3 to 12 months	From 1 year to 5 years	Over 5 years
<b>As at December 31, 2017</b>						
Loans and borrowings	6,358	7,103	90	499	3,871	2,643
Bonds issued	3,683	3,949	-	1,064	2,189	696
Trade and other financial liabilities	3,610	3,610	3,189	40	48	333
Finance lease liabilities and lease agreement with purchase option	4	4	1	1	2	-
Derivatives	124	125	15	81	33	(4)
<b>TOTAL</b>	<b>13,779</b>	<b>14,791</b>	<b>3,295</b>	<b>1,685</b>	<b>6,143</b>	<b>3,668</b>

	Carrying amount	Total payments	Under 3 months	From 3 to 12 months	From 1 year to 5 years	Over 5 years
<b>As at December 31, 2016</b>						
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	-
Finance lease liabilities and lease agreement with purchase option	1	1	-	1	-	-
Derivatives	30	30	-	20	10	-
<b>TOTAL</b>	<b>13,633</b>	<b>14,713</b>	<b>2,332</b>	<b>1,671</b>	<b>5,497</b>	<b>5,213</b>

### 26.3 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).

PGE Group companies 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<sub>2</sub> emission rights, purchases of fuels etc. This 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 PGE Group related to trade receivables. The three most significant customers accounted for ca. 7% of the trade receivables balance.

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

	Year ended December 31, 2017	Year ended December 31, 2016
Trade and other financial receivables	3,680	6,562
Cash and cash equivalents	2,552	2,669
Derivatives - assets	305	365
<b>MAXIMUM EXPOSURE TO CREDIT RISK</b>	<b>6,537</b>	<b>9,596</b>

### 26.3.1 Trade receivables Other loans and financial receivables

The terms of payments for trade receivables are usually 2-3 weeks. In 2017 the PGE Group received payments for receivables on average after 49 days (debtors turnover ratio in the main companies of the PGE Group ranged between 12 and 61 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.

PGE Group reduces and controls credit risk related to commercial transactions in accordance with harmonised credit risk management rules implemented at all key PGE Group companies. In the case of trade transactions which due to high value may generate substantial loss in case of failure of business partner to comply with the agreement, the assessment of contractor is carried out before the transaction is conducted, taking into account contractor’s financial analysis, its credit history and other factors. Based on the assessment, an internal rating is recognised or PGE Group uses a rating determined by an independent reputable agency. A limit for the contractor is set based on the rating. Entering into contracts that would increase exposure above the limit, requires in principle the collateral in line with PGE Group's rules pertaining to credit risk management. The level of used limit is regularly monitored and reported to the Risk Committee and if it is substantially exceeded, units responsible for contractor’s risk are obliged to undertake measures to eliminate them. 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 credit bureaus and debt collection companies.

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

	December 31, 2017		December 31, 2016	
	Receivables balance	% share	Receivables balance	% share
Poland	3,070	97%	2,691	99%
Netherlands	59	2%	-	-
Other	30	1%	14	1%
<b>TOTAL</b>	<b>3,159</b>	<b>100%</b>	<b>2,705</b>	<b>100%</b>

### Ageing of receivables and impairment

As at December 31, 2017 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, 2017	Trade and other receivables	Other financial receivables	Bonds
<b>Impairment as of January 1</b>	<b>(170)</b>	<b>(195)</b>	<b>(297)</b>
Impairment allowance used	13	5	-
Reversal of impairment allowance	5	9	-
Recognition of impairment losses	(14)	(22)	(89)
Acquisition of companies	(16)	-	-
Sale of companies	7	-	-
Other changes	5	-	-
<b>Impairment as of December 31</b>	<b>(170)</b>	<b>(203)</b>	<b>(386)</b>
<b>Value before impairment allowance</b>	<b>3,329</b>	<b>724</b>	<b>386</b>
<b>Net value (carrying amount)</b>	<b>3,159</b>	<b>521</b>	<b>-</b>

Impairment of trade receivables concerns the supply and distribution segments. The total amount of trade receivables impairment at these companies as at December 31, 2017, was PLN 141 million (PLN 147 million in 2016).

Impairment losses recognised on bonds of PLN 89 million relate to Autostrada Wielkopolska S.A.

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, 2016	Trade and other receivables	Other financial receivables	Bonds
<b>Impairment as of January 1</b>	<b>(212)</b>	<b>(181)</b>	<b>(386)</b>
Impairment allowance used	46	12	-
Reversal of impairment allowance	4	11	89
Recognition of impairment allowance	(16)	(25)	-
Other changes	8	(12)	-
<b>Impairment as of December 31</b>	<b>(170)</b>	<b>(195)</b>	<b>(297)</b>
<b>Value before impairment allowance</b>	<b>2,875</b>	<b>3,963</b>	<b>386</b>
<b>Net value (carrying amount)</b>	<b>2,705</b>	<b>3,768</b>	<b>89</b>

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

	DECEMBER 31, 2017			DECEMBER 31, 2016		
	Gross	Impairment allowance	Carrying amount	Gross	Impairment allowance	Carrying amount
<b>Receivables before due date</b>	<b>3,776</b>	<b>(449)</b>	<b>3,327</b>	<b>6,638</b>	<b>(360)</b>	<b>6,278</b>
<i>Past due &lt;30 days</i>	242	(9)	233	197	(2)	195
<i>Past due 30-90 days</i>	51	(2)	49	40	(1)	39
<i>Past due 90-180 days</i>	28	(7)	21	14	(8)	6
<i>Past due 180-360 days</i>	20	(15)	5	62	(19)	43
<i>Past due &gt;360 days</i>	322	(277)	45	273	(272)	1
<b>Receivables past due, total</b>	<b>663</b>	<b>(310)</b>	<b>353</b>	<b>586</b>	<b>(302)</b>	<b>284</b>
<b>Trade and other financial receivables</b>	<b>4,439</b>	<b>(759)</b>	<b>3,680</b>	<b>7,224</b>	<b>(662)</b>	<b>6,562</b>

As at December 31, 2017, more than 55% 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.

#### 26.3.2 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 with which 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 high investment level ratings, adequate indicator of solvency and equity as well as strong, stable market position. The share of three major banks in which PGE Group allocated the most significant cash balances as at December 31, 2017, accounted for approximately 72% (80% in the comparative period).

#### 26.3.3 Derivatives

All entities with which PGE Group concludes derivative 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, PGE Group was party to the derivative transactions, described in detail in note 25.1.2 to these financial statements.

#### 26.3.4 Guarantees and sureties issued

Guarantees and sureties issued by PGE Group companies are presented in note 28 to these financial statements.

## 26.4 Market (financial) risk - sensitivity analysis

PGE Group is exposed mainly to currency risk related to foreign exchange rates between EUR/PLN, USD/PLN and to interest rate risk related to referential interest rates of PLN, EUR, USD. PGE Group uses a script analysis method for the purpose of analysing 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 analyse the influence of changes in market risk factors on consolidated financial results. 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, 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 income or expenses or as revaluation of financial instruments measured at fair value.

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

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, 2017 and December 31, 2016, without taking the discount into account. The book value of derivatives constitutes their fair value measurement.

### 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, 2017			
			EUR/PLN		USD/PLN	
			Impact on financial result / Equity		Impact on financial result / Equity	
			+10%	-10%	+10%	-10%
Trade and other financial receivables	3,680	23	1	(1)	1	(1)
Cash and cash equivalents	2,552	153	13	(13)	2	(2)
Derivatives measured at fair value through profit or loss	89	117	13	(13)	2	(2)
<i>Hedging derivatives</i>	44	2,966	274	(274)	-	-
Interest bearing loans and borrowings	(6,358)	(655)	(46)	46	(19)	19
Bonds issued	(3,683)	(2,282)	(268)	268	-	-
Trade and other financial liabilities	(3,610)	(109)	(3)	3	(8)	8
Derivatives measured at fair value through profit or loss	(106)	(1,893)	(141)	141	(49)	49
<b>IMPACT ON FINANCIAL RESULT</b>			<b>(157)</b>	<b>157</b>	<b>(71)</b>	<b>71</b>
Hedging instruments	39	2,871	22	(22)	(10)	10
<b>IMPACT ON REVALUATION RESERVE</b>			<b>22</b>	<b>(22)</b>	<b>(10)</b>	<b>10</b>

SENSITIVITY ANALYSIS FOR CURRENCY RISK AS AT DECEMBER 31, 2016						
FINANCIAL INSTRUMENTS BY CLASS	Carrying amount in PLN	Value at risk	EUR/PLN		USD/PLN	
			Impact on financial result / equity		Impact on financial result / equity	
			+10%	-10%	+10%	-10%
Trade 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 hedges	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 payables	(3,589)	(65)	(7)	7	-	-
Derivatives - liabilities	(30)	(7)	-	-	(1)	1
<b>Impact on financial result</b>			<b>(27)</b>	<b>27</b>	<b>(11)</b>	<b>11</b>
CCIRS hedges	231	3,222	31	(31)	-	-
<b>Impact on revaluation reserve</b>			<b>31</b>	<b>(31)</b>	-	-

### 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, 2017								
FINANCIAL ASSETS AND LIABILITIES	Carrying amount in PLN	Value at risk	WIBOR		EURIBOR		LIBOR USD	
			Impact on financial result / equity		Impact on financial result / equity		Impact on financial result / equity	
			+50bp	-50bp	+25bp	-25bp	+25bp	-25bp
Derivatives measured at fair value through profit or loss - assets	305	111	<1	<(1)	<1	<(1)	<1	<(1)
Interest bearing loans and borrowings	(6,358)	(6,002)	(27)	27	(1)	1	<(1)	<1
Bonds issued	(3,683)	(1,000)	(5)	5	-	-	-	-
Lease	(4)	(4)	-	-	-	-	-	-
Derivatives measured at fair value through profit or loss - liabilities	(114)	(27)	-	-	-	-	-	-
<b>Impact on financial result</b>			<b>(32)</b>	<b>32</b>	<b>(1)</b>	<b>1</b>	-	-
CCIRS hedges	44	44	46	(48)	(27)	27	-	-
IRS hedges - assets	98	98	109	(113)	-	-	-	-
IRS hedges - liabilities	(5)	(5)	(12)	16	-	-	-	-
<b>Impact on revaluation reserve</b>			<b>143</b>	<b>(145)</b>	<b>(27)</b>	<b>27</b>	-	-

SENSITIVITY ANALYSIS FOR INTEREST RATE RISK AS AT DECEMBER 31, 2016								
FINANCIAL ASSETS AND LIABILITIES	Carrying amount in PLN	Value at risk	WIBOR		EURIBOR		LIBOR USD	
			Impact on financial result / equity		Impact on financial result / equity		Impact on financial result / equity	
			+50bp	-50bp	+25bp	-25bp	+25bp	-25bp
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	-	-	-	-
Lease	(1)	(1)	-	-	-	-	-	-
Derivatives measured at fair value through profit or loss - liabilities	(30)	(30)	5	(5)	-	-	<1	<(1)
<b>Impact on financial result</b>			<b>(10)</b>	<b>10</b>	<b>(1)</b>	<b>1</b>	-	-
CCIRS hedges	231	231	60	(62)	(37)	37	-	-
IRS hedges	125	125	128	(133)	-	-	-	-
<b>Impact on revaluation reserve</b>			<b>188</b>	<b>(195)</b>	<b>(37)</b>	<b>37</b>	-	-

### Sensitivity analysis for commodity price risk

The Group identifies exposure to commodity price risk, including commodities to produce electricity and heat using the Group's generating assets.

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

COMMODITY	AS AT DECEMBER 31, 2017			AS AT DECEMBER 31, 2016		
	Purchase cost	Impact on financial result		Purchase cost	Impact on financial result	
		+10%	-10%		+10%	-10%
Hard coal	1,395	140	(140)	1,141	114	(114)
CO <sub>2</sub> emission allowances for captive use	247	25	(25)	937	94	(94)
Natural gas [m3 000s]	527	53	(53)	454	45	(45)
Biomass	99	10	(10)	190	19	(19)
Fuel oil	51	5	(5)	41	4	(4)
<b>TOTAL</b>	<b>2,319</b>	<b>233</b>	<b>(233)</b>	<b>2,763</b>	<b>276</b>	<b>(276)</b>

### 26.5 Hedge accounting

In connection with loans received from PGE Sweden AB (publ), PGE S.A. concluded CCIRS transactions, hedging the exchange rate. In these transactions, banks - counterparties 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, a relevant part of the CCIRS transaction is treated as a hedge of bonds issued by PGE Sweden AB (publ).

PGE S.A. secures cash flow risk resulting from exchange rates related to forward contracts to purchase CO<sub>2</sub> emission allowances, the price of which is expressed in EUR.

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. In these transactions, banks - counterparties 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.

To recognise these CCIRS transactions, PGE Group uses hedge accounting. The impact of hedge accounting on the revaluation reserve is presented in note 20.3 to these financial statements.

## 27. Statement of cash flows

### 27.1 Cash flows from operating activities

#### (Profit) / loss on investing activities

	Year ended December 31, 2017	Year ended December 31, 2016
(Profit) / loss on sale of property, plant and equipment	(13)	(11)
(Profit) / loss on disposal of financial non-current assets	93	-
Change in impairment of shares and other financial assets	90	(84)
Matching cost measurement of derivatives	(76)	(62)
Other	38	26
<b>(PROFIT) / LOSS ON INVESTING ACTIVITIES, TOTAL</b>	<b>132</b>	<b>(131)</b>

#### Change in receivables

	Year ended December 31, 2017	Year ended December 31, 2016
Change in trade receivables and other financial receivables	2,882	(2,672)
Adjustment for changes in purchased bonds	(88)	89
Adjustment for deposits	(2,282)	2,311
Netting of LTC receivables/liabilities	(1,241)	-
Adjustment for acquisition of subsidiaries	321	-
Other	(26)	(3)
<b>TOTAL CHANGE IN RECEIVABLES</b>	<b>(434)</b>	<b>(275)</b>

**Change in inventories**

	Year ended December 31, 2017	Year ended December 31, 2016
Change in inventories	(283)	363
Adjustment for transfer of investment materials to property, plant and equipment	(2)	(12)
Adjustment for property rights from trial startup	-	(9)
Adjustment for acquisition of subsidiaries	398	-
Other	2	-
<b>TOTAL CHANGE IN INVENTORIES</b>	<b>115</b>	<b>342</b>

**Change in liabilities, excluding loans and borrowings**

	Year ended December 31, 2017	Year ended December 31, 2016
Change in trade and other financial payables	21	(390)
Change in other non-financial liabilities	(119)	36
Adjustment for change in investment liabilities	(101)	298
Adjustment for changes in tax liabilities due to share capital increase	110	(110)
Netting of LTC receivables/liabilities	1,241	-
Adjustment for acquisition of subsidiaries	(829)	-
Other	20	(3)
<b>TOTAL CHANGE IN LIABILITIES</b>	<b>343</b>	<b>(169)</b>

**Change in other non-financial assets, prepayments and CO<sub>2</sub> emission allowances**

	Year ended December 31, 2017	Year ended December 31, 2016
Change in other assets	231	516
Change in CO <sub>2</sub> emission allowances	907	(177)
Change in deferred income	(107)	(44)
Change in advances for construction in progress	(285)	(329)
Change in balance concerning financing/investing activities	(15)	(45)
Adjustment for acquisition of subsidiaries	144	-
Other	(1)	(17)
<b>CHANGE IN OTHER NON-FINANCIAL ASSETS, PREPAYMENTS AND CO<sub>2</sub> EMISSION RIGHTS, TOTAL</b>	<b>874</b>	<b>(96)</b>

**Change in provisions**

	Year ended December 31, 2017	Year ended December 31, 2016
Change in provisions	885	(668)
Change in actuarial provisions recognised in other comprehensive income	(101)	249
Change in rehabilitation provision recognised in assets	(192)	174
Adjustment for acquisition of subsidiaries	(478)	-
Other	3	1
<b>TOTAL CHANGE IN PROVISIONS</b>	<b>117</b>	<b>(244)</b>

**27.2 Cash flows from investing activities****Purchase of property, plant and equipment and intangible assets**

In 2017, the most significant capital expenditures were incurred by Conventional Generation segment (PLN 4,200 million, of which PLN 1,605 million is related to construction of units 5 and 6 at Opole Power Plant, PLN 830 million is related to construction of unit 11 at Turów Power Plant, PLN 184 million on modernisation of units 1-3 at Turów Power Plant, PLN 174 million on change in combustion waste storage technology and related installations at Bełchatów Power Plant) and the Distribution segment (PLN 1,619 million, most of which concerns connection of new clients as well as modernisation and expansion of power grid, stations).

In 2016, the Conventional Generation segment incurred PLN 5,788 million in expenditures and the Distribution segment PLN 1,730 million.

**Purchase of financial assets and increase in stake in Group companies**

Expenditures incurred in 2017 amounting to PLN 213 million related to the investment in Polska Grupa Górnicza (PLN 126 million) and in Polimex-Mostostal S.A. (described in notes 33.2 and 33.4 to these financial statements, respectively).

In 2016, the amount of PLN 467 million concerns mainly investments in Polska Grupa Górnicza (PLN 444 million) and prepayments for BOŚ's shares and acquisition of shares in an associate ElectroMobility.



### Recognition and release of deposits with maturity over 3 months

In 2017, PGE S.A. released deposits with a maturity over 3 months at the total amount of PLN 2,340 million. In 2016, 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.

### Purchase of subsidiaries after offsetting acquired cash

The Group recognised expenditures on the acquisition of EDF's companies in Poland. Funds paid PLN 1,992 million, subrogation of liabilities PLN 2,285 million, adjusted by acquired cash PLN 186 million. Details are presented in note 1.4 of these financial statements.

### Sale of subsidiaries after offsetting sold cash

On March 29, 2017 an agreement to sell 100% of EXATEL S.A. shares was executed. Along with the sale of EXATEL S.A., the Group lost control over its subsidiary ENERGO-TEL S.A. The sale price amounting to PLN 369 million was adjusted by cash handed over.

## 27.3 Cash flows from financing activities

### Proceeds from loans

In 2017, companies in the Conventional Generation segment received credits and loans from environmental funds worth a total of approx. PLN 116 million. PGE Paliwa sp. z o.o. increased its credit line debt by PLN 67 million. 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 leasing

This position includes mainly repayment of loans from environmental funds obtained by Conventional Generation segment in the total amount of approximately PLN 193 million and PLN 203 in the preceding reporting period.

### Dividends paid

As described in note 20.8 to these financial statements, according to an updated dividend policy, the Group postponed the payment of dividends from profit for 2016, 2017 and 2018.

In 2016, PGE S.A.'s General Meeting resolved to distribute PLN 467 million from the net profit of 2015 as a dividend. The remaining amount of PLN 4 million is related to dividends paid to non-controlling shareholders.

### Interest paid

In 2017, this item included mainly interest on loans and credit of PLN 143 million, interest on bonds of PLN 77 million and interest on CCIRS and IRS of PLN 75 million.

In 2016, the Group paid interest mainly on: loans and credit (PLN 34 million), bonds (PLN 79 million) and financial instruments (CCIRS and IRS, PLN 83 million).

## OTHER EXPLANATORY NOTES

### 28. Contingent liabilities and receivables. Legal claims

#### 28.1 Contingent liabilities

	As at December 31, 2017	As at December 31, 2016
Contingent return of grants from environmental funds	753	469
Legal claims	188	73
Bank guarantee liabilities	223	-
Contingent return of CO <sub>2</sub> emission rights received free of charge	-	115
Contractual fines and penalties	12	12
Employees' claims	2	1
Other contingent liabilities	74	61
<b>Total contingent liabilities</b>	<b>1,252</b>	<b>731</b>

#### Contingent return of grants from environmental funds

The liabilities represent the value of possible future reimbursements of funds received by 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.

#### Legal claims

##### Dispute with WorleyParsons

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 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 was 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. Through a letter of March 24, 2017, WorleyParsons expanded its claim from PLN 59 million to PLN 104 million (i.e. by PLN 45 million). The Court-ordered deadline for responding to the letter from WorleyParsons expanding the lawsuit is March 31, 2018. The Group does not accept the claim and regards its possible admission by the court as unlikely.

##### Claims related to property right sale contracts executed by Energa-Obrót S.A.

In October 2017, PGE Energia Odnawialna S.A. and PGE Energia Natury sp. z o. o. (currently acquired by PGE Energia Odnawialna S.A.) received lawsuits in which Energa-Obrót S.A. demanded the annulment of legal relations that were to arise as a result of the execution of agreements to sell property rights resulting from electricity origin certificates from FW Kieselice in 2009, FW Koniecwałd (Malbork) and FW Galicja (a wind farm owned by PGE Energia Natury sp. z o.o.). The demands in all of Energa-Obrót S.A.'s lawsuits were based on the accusation that implementing agreements (agreement to sell specific property rights) were executed in circumvention of the Public Procurement Law. Alternatively, if framework agreements are considered as agreements on award of a public procurement, Energa-Obrót S.A. claimed absolute invalidity of such agreements due to them being executed in a way that violated the Public Procurement Law. In November 2017, these PGE companies submitted their responses to the lawsuits, stating that Energa-Obrót S.A.'s accusations are groundless. Proceedings in these cases are in progress.

In addition, through motions of September 2017, Energa-Obrót S.A. summoned PGE Energia Odnawialna S.A. and PGE Energia Natury sp. z o.o. (currently acquired by PGE Energia Odnawialna S.A.) to amicably resolve disputes regarding payment of a claim totalling PLN 71 million for undue considerations paid based on invalid agreements from 2009. No agreement was reached at hearings that took place in November and December 2017. In connection with this, a PLN 71 million claim is recognised as a contingent liability in these financial statements. The Group does not accept the claims and regards their possible admission by the court as unlikely.

Citing invalidity of the agreements from 2009, Energa-Obrót S.A. refused to purchase property rights generated in connection with the generation of renewable electricity at wind farms FW Kieselice, FW Koniecwałd (Malbork) and FW Galicja, which constituted a breach of contractual terms and resulted in contractual penalty claims that were recognised as revenue in the current period, amounting to PLN 16 million. In light of the refusal to pay contractual penalties, PGE Energia Odnawialna S.A. intends to seek their payment in court.

Estimated volume of the green certificates covered by the aforementioned contracts with Energa-Obrót S.A. amounts to 836 000 MWh. This volume was calculated based on the volume of production in the period from July 2017 (FW Koniecwałd/Malbork) or from August 2017 (other farms) to the end of the expected support periods for each of the farms.

### Bank guarantee liabilities

These liabilities for the most part present bank guarantees provided as collateral for stock market transactions resulting from membership in the Stock Exchange Clearinghouse. As at December 31, 2017, the total amount of bank guarantees was PLN 215 million.

### 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 Elekrowni 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 33 million, which was described above, as well as PLN 31 million related to risk of additional costs related to PGE Group's debt financing programmes.

## 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 recognises 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, PGE Group held PLN 10 million in contingent receivables related to non-balancing of purchase and sale of energy on the domestic market. In the preceding year, as at December 31, 2016, this was a contingent liability and amounted to PLN 19 million.

## 28.4 Other legal claims and disputes

### 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 a 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.

A similar claim was raised by Pozwy sp. z o.o., an entity that purchased claims from former PGE Elekrownia Opole S.A. shareholders. Pozwy sp. z o.o. has filed a claim at the District Court in Warsaw against PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE S.A. and PwC Polska sp. z o.o. ("Defendants"), demanding from the Defendants, in solidum, or jointly damages for Pozwy sp. z o.o. totalling over PLN 260 million with interest for allegedly incorrect (in its opinion) determination of exchange ratio for PGE Elekrownia Opole S.A. shares for PGE Górnictwo i Energetyka Konwencjonalna S.A. shares in a merger of these companies. This lawsuit was delivered to PGE S.A. on March 9, 2017, and the deadline for responding to it was set by the court as July 9, 2017. On July 8, 2017, PGE S.A. and PGE GiEK S.A. submitted a response to the claim and the lawsuit is currently being proceeded in the first instance.

PGE Group companies do not recognise the claims being raised by Socrates Investment S.A., Pozwy sp. z o.o. and other shareholders requesting conciliatory settlements. According to PGE S.A., these claims are groundless and the entire 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. PGE Group has not recognised a provision for this claim.

### Claims for annulment of General Meeting resolutions

On April 1, 2014, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of the resolutions 1, 2 and 4 of the Company's Extraordinary General Meeting held on February 6, 2014. The Company filed a response to the claim. 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 reply to the appeal. On March 24, 2017, a hearing was held at the Appellate Court in Warsaw. The court discontinued the proceedings due to the lawsuit being withdrawn without relinquishing the claim.

On August 21, 2015, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of resolution 5 of the Company's Ordinary General Meeting held on June 24, 2015. The Company filed a response to the claim. On April 26, 2016, the District Court in Warsaw issued a judgment dismissing the shareholder's claim. On April 3, 2017, the shareholder appealed. Through a ruling of April 18, 2017, the District Court rejected the appeal due to the appeal deadline having been exceeded. The ruling became final on May 6, 2017.

On September 17, 2014, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of resolution 4 of the Company's Ordinary General Meeting held on June 6, 2014. The Company filed a response to the claim. 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 reply to the appeal. Through a ruling of March 2, 2017, the Appeals Court in Warsaw dismissed the shareholder's appeal. The shareholder filed a cassation claim dated June 10, 2017. On August 3, 2017, the Company filed a response to the cassation claim. In a ruling of January 10, 2018, the Supreme Court rejected the shareholder's cassation claim.

On October 23, 2015, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of resolution 1 of the Company's Extraordinary General Meeting held on September 14, 2015. The Company filed a response to the claim. A hearing before the District Court in Warsaw was held on April 24, 2017. In a ruling of May 8, 2017, the court dismissed the shareholder's claim. On July 3, 2017, the shareholder appealed. On August 27, 2017, the District Court ruled to dismiss the shareholder's appeal. The ruling became final on September 13, 2017.

On May 20, 2016, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of resolution 1 of the Company's Extraordinary General Meeting held on March 1, 2016. The Company filed a response to the claim. The proceedings were discontinued through a ruling of March 14, 2017 after the withdrawal of the claim prior to the first hearing.

On September 12, 2016, PGE S.A. received a copy of lawsuit filed to the District Court in Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of the resolution 1 of the Company's Ordinary General Meeting held on June 28, 2016. The Company filed a response to the claim. The proceedings were discontinued through a ruling of March 14, 2017 after the withdrawal of the claim prior to the first hearing.

On December 30, 2016, PGE S.A. received a copy of lawsuit filed to the District Court in Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of resolution 1 of the Company's Extraordinary General Meeting held on September 5, 2016. The Company filed a response to the claim. The proceedings were discontinued through a ruling of March 16, 2017 after the withdrawal of the claim prior to the first hearing.

On March 15, 2017, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking for annulment of resolution 4 of the Company's Extraordinary General Meeting held on September 5, 2016. The Company filed a response to the claim. Having examined the shareholder's claim at a closed-door hearing on October 11, 2017, the District Court in Warsaw ruled to refer the case for mediation. PGE S.A. decided not to agree to mediation. On March 1, 2018 a hearing was held -the date of the judgment was postponed until March 15, 2018.

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

In October 2016 and November 2016, PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE Energia Odnawialna S.A. and PGE Energia Naturity PEW sp. z o.o. received from Enea S.A. a notice of termination of long-term contracts for the purchase of renewable energy origin rights, so called "green certificates." In its justification, Enea S.A. stated that these companies severely breached contractual provisions by failing to re-negotiate contract provisions in accordance with the adaptation clause, as requested by Enea S.A. in July 2015 in connection with an alleged change in legal regulations having impact on the performance of these contracts.

In the opinion of PGE Group, the notices of termination sent by Enea S.A. were submitted in violation of contractual terms. The companies took appropriate steps to enforce their rights. In light of Enea S.A.'s refusal to perform the long-term contracts by purchasing property rights resulting from certificates of origin received by PGE Group companies in connection with the generation of renewable electricity, PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Energia Naturity PEW sp. z o.o. demanded payment of contractual penalties by Enea S.A., while PGE Energia Odnawialna S.A. demanded the payment of compensation for damages. In light of a refusal to pay these debts, the Companies intend to seek their payment in court. In a lawsuit filed by PGE Energia Naturity PEW sp. z o.o., the District Court in Poznań, 9th Commercial Department, fully accepted the lawsuit's demand and issued a payment order in writ-of-payment proceedings. Following an appeal submitted by Enea S.A. the payment order legally had no power. The proceedings are in progress. The next hearing is scheduled for April 2018.

Due to the fact that according to PGE Group the declarations on termination of the agreements presented by Enea S.A. were submitted in breach of contractual terms, as at the reporting date the Group recognised contractual penalty receivables of PLN 128 million. As the same time, property rights inventories that were initially measured at values resulting from the agreements were revalued to market prices. According to PGE Group companies, based on available legal analysis, a favourable resolution in the above disputes is more probable than a negative resolution.

Estimated volume of the green certificates covered by the contracts with Enea S.A. amounts to approximately 2 662 000 MWh. The above amount was calculated for the period from the date the contracts were terminated to the end of the expected initial term of the contracts.

Additionally, PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE Energia Odnawialna S.A. and PGE Energia Natury PEW sp. z o.o. filed lawsuits against Enea S.A. for the payment of receivables totalling PLN 47 million for invoices issued to Enea S.A. concerning sale of property rights under the contracts. Enea S.A. refused to pay these receivables, claiming that they were successfully offset against its debts towards the Group's companies concerning compensation for alleged damages arising from the failure to re-negotiate the contracts. According to the Group companies, these setoffs are invalid because Enea S.A.'s receivables never materialised and there are no grounds to accept Enea S.A.'s claim that the companies breached any sort of contractual terms. The proceedings are in progress. The next hearings are scheduled for April 2018.

## 29. Future investment commitments

As at December 31, 2017, PGE Group committed to incur capital expenditures on property, plant and equipment of approximately PLN 5,891 million. These amounts relate mainly to construction of new power units, modernisation of Group's assets and purchase of machinery and equipment.

	As at December 31, 2017	As at December 31, 2016 <i>restated data*</i>
Conventional energy	4,755	7,647
Distribution	897	796
Renewable energy	67	38
Sales	1	2
Other activity	171	201
<b>TOTAL FUTURE INVESTMENT COMMITMENTS</b>	<b>5,891</b>	<b>8,684</b>

\*Data as at December 31, 2016, does not include the option scope of an advisory agreement executed by PGE EJ1 sp. z o.o.

The most significant future investment commitments concern:

- Conventional Generation:
  - Branch Opole Power Plant – construction of power units no. 5 and 6 – approximately PLN 1,290 million,
  - Branch Turów Power Plant – construction of new power unit – approximately PLN 2,282 million,
  - Branch Turów Power Plant – modernisation of power units no. 1-3 – approximately PLN 442 million,
  - Branch Rzeszów Heat and Power Plant – construction of Thermal Processing Installation with Energy Recovery – approximately PLN 173 million,
- Distribution – investment commitments related to network distribution assets with the total value of approximately PLN 897 million,
- Other activity, 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 159 million (basic scope) An optional scope includes the amount of approx. PLN 1,121 million.

### 30. Lease

#### 30.1 Operating lease liabilities – the Group as a lessee

As at December 31, 2017, and December 31, 2016, the future minimum lease payments related to irrevocable lease agreements amounted to as follows:

	As at December 31, 2017	As at December 31, 2016
Within 1 year	9	9
1-5 years	37	37
Over 5 years	134	147
<b>TOTAL FUTURE LIABILITIES</b>	<b>180</b>	<b>193</b>

PGE Group entities incur costs related to fees for perpetual usufruct of land. The value of these costs for the year ended December 31, 2017, amounted to PLN 18 million and PLN 18 million in the comparative period.

#### 30.2 Operating lease receivables – the Group as a lessor

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 Power System. 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.

As at December 31, 2017, and December 31, 2016, the future minimum lease payments related to irrevocable lease agreements amounted to as follows:

	As at December 31, 2017	As at December 31, 2016
Within 1 year	252	249
1-5 years	-	252
<b>TOTAL FUTURE RECEIVABLES</b>	<b>252</b>	<b>501</b>

#### 30.3 Finance lease liabilities and lease contracts with buy option

As at the reporting date the present value of the minimum current lease payments amounted to approximately PLN 2 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 identified receivables from short- and long-term finance lease agreements of PLN 1 million and PLN 3 million, respectively. During the reporting period, the Group did not identify significant receivables.

### 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 the 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 the point of view of business entities, 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 must also be mentioned Among these there are social security charges.

Basic tax rates were as follows in 2017: corporate income tax rate – 19%, basic value added tax rate – 23%, reduced: 8%, 5%, 0%, furthermore some goods and products are subject to a VAT tax exemption.

The tax system in Poland is characterized by a significant changeability of tax regulations, their high complexity, high potential fees for commitment of a tax crime or violation. Tax settlements and other activity areas are conditioned by regulations (customs or currency controls) and 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

An agreement for a tax group named PGK PGE 2015, for which PGE S.A. is the representative, was signed on September 18, 2014, for a period of 25 years.

Companies included in the tax group must meet a number of requirements covering: appropriate level of equity, parent's stake in PGK companies of at least 95% (75% from 2018), lack of capital ties between subsidiaries, no tax arrears, share in total revenue of at least 3% (counted for the entire tax group, 2% from 2018 on), and execution of transactions with related parties from outside the tax group only on market terms. Violating these requirements would mean the dissolution of the tax group and loss of its taxpayer status. When the tax group is dissolved, each of its member companies becomes an individual payer of corporate income tax.

### Changes in corporate income tax in effect from January 1, 2018

As a result of changes in legislation, starting from 2018 taxpayer revenue is divided into two sources: economic (operating) activities and capital gains. This means that each source of revenue will be settled separately and that companies may not offset losses incurred in one source using revenue from the other source. The capital gains source includes: dividends, income obtained as a result of mergers of de-mergers, in-kind contributions, share disposals, disposal of debt claims, income from property rights (authors' rights, licences) and income from securities.

According to existing estimates, the introduction of two income sources should not substantially affect the PGE Group's tax burden.

### VAT split payment mechanism

Starting from July 1, 2018, a VAT split payment mechanism will be introduced. This solution is intended to seal off the tax system by separating VAT amounts from bank transfers being made by buyers of products and services and directing these to sellers' dedicated VAT accounts. Funds collected in these VAT accounts may only be used for VAT settlements concerning invoices received and VAT settlements with the tax office. Using split VAT payments will not be the buyer's right but rather an obligation.

Funds collected at the VAT account will constitute restricted cash. Given the above, the introduction of a split payment mechanism might increase net debt and increase net debt to EBITDA. At the date on which these financial statements were prepared, there was no set practice as to how cash in VAT accounts will be taken into account when calculating debt ratios that are presented to financing institutions. PGE Group intends to effectively use the funds received from counterparties in VAT accounts to pay its liabilities that contain VAT. The level of funds in these VAT accounts will depend mainly on how many of PGE Group's counterparties decide to use this mechanism and the relation between receivables and liabilities payment dates. According to the Group's estimates, the average level of cash in VAT accounts might be in the range of PLN 100-200 million.

### Excise tax

In connection with an incorrect implementation of EU regulations in the Polish legal system, PGE GiEK S.A. in 2009 initiated proceedings regarding reimbursement of improperly paid excise tax for the period January 2006 - February 2009. The irregularity consisted of taxing electricity at the first stage of sale, i.e. by producers, whereas sales to end users should have been taxed.

Examining the company's complaints with regard to the restitution claims against decisions issued by tax authorities refusing to confirm overpayment of excise tax, administrative courts ruled that the company did not bear the economic burden of the improperly calculated excise tax (which in the context of the resolution by the Supreme Administrative Court of June 22, 2011, file no. I GPS 1/11, precludes the return of overpaid amounts). According to the Supreme Administrative Court, the claims that the company sought, especially using economic analyses, are of an offsetting nature and therefore may be sought only in civil courts. Given the above, PGE GiEK S.A. decided to withdraw from the proceedings as regards restitution claims. Currently, the issue of overpaid excise tax is in civil courts and the intention is to reach a settlement with the State Treasury as regards restitution claims.

Given the significant uncertainty over the final ruling in this issue, the Group does not recognise in its financial statements any effects related to potential compensation in civil courts in connection with the improperly paid excise tax.

### Real estate tax

Considering pending disputes, PGE Group established at the reporting date the provision for property tax in the amount of PLN 81 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.

In addition, on July 15, 2016, the Act on investments in wind farms entered into force. The act defined a "wind farm" as foundation, mast and technical equipment (technical equipment include rotor with blades, gondola, control system). The act introduced amendments to the Construction Law and thus on the amount of property tax because the act on local taxes and fees refers to this act. By the end of 2016 (based on rulings on the basis of the amended Construction Law) it was commonly accepted that property tax is only applicable to the construction parts of wind farms, i.e. foundation and tower, whereas the wind farm's technical equipment is exempt from property tax. The tax consequences related to the act went into force on January 1, 2017.

The changes in the act caused the necessity to tax the entire wind farm, which increased tax property expenses by more than PLN 39 million in the year. According to PGE Group, there are legal arguments that indicate that the updated Construction Law did not lead to a change in the tax object or that the value of the tax object should be established again. In the course of 2017, the Group received two negative interpretations concerning wind farm tax according to rules in effect from January 1, 2017. Proceedings regarding these interpretations are on-going in first and second instance courts.

Given the fact that advanced work on amendment of these provisions is on-going, which would result in the return to the wind farm taxation methods in effect prior to January 1, 2017, the Group suspends the process of filing tax corrections for 2017 until these amendments enter into force.

### 32. Information on related parties

PGE Group's transactions with related entities are concluded based on 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, 2017	Year ended December 31, 2016
Sales to associates and jointly controlled entities	14	88
Purchases from associates and jointly controlled entities	1,854	571
	As at December 31, 2017	As at December 31, 2016
Trade receivables from associates and jointly controlled entities	9	41
Trade liabilities to associates and jointly controlled entities	180	16

The increase in turnover and balances results from the inclusion of Polska Grupa Górnicza sp. z o.o. and Polimex-Mostostal S.A. in these financial statements.

#### 32.2 State Treasury-controlled companies

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. 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, 2017	Year ended December 31, 2016
Sales to related parties	2,164	2,137
Purchases from related parties	3,987	3,579
	As at December 31, 2017	As at December 31, 2016
Trade receivables from related parties	280	313
Trade liabilities to related parties	629	418

The largest transactions with State Treasury companies involve Polskie Sieci Elektroenergetyczne S.A., PGNiG S.A., Energa Group companies, Enea Group companies, Grupa Azoty Zakłady Azotowe Puławy S.A., PKN Orlen S.A. and certain Polish coal mines.

Moreover, 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 recognised as transactions with related parties.

On March 29, 2017 an agreement to sell 100% of EXATEL S.A. shares was executed. The sale amounted to PLN 369 million and is not included in the above lists.



### 32.3 Management remuneration

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

<i>PLN 000s</i>	Year ended December 31, 2017	Year ended December 31, 2016
Short-term employee benefits (salaries and salary related costs)	31,433	32,508
Post-employment benefits	2,427	9,446
<b>TOTAL REMUNERATION OF KEY MANAGEMENT PERSONNEL</b>	<b>33,860</b>	<b>41,954</b>
Remuneration of key management personnel of entities of non-core operations	15,858	15,395
<b>TOTAL REMUNERATION OF KEY MANAGEMENT PERSONNEL</b>	<b>49,718</b>	<b>57,349</b>

<i>PLN 000s</i>	Year ended December 31, 2017	Year ended December 31, 2016
Management Board of the parent company	7,454	11,669
<i>Post-employment benefits</i>	168	3,066
Supervisory Board of the parent company	760	510
Management Boards – subsidiaries	23,192	27,448
Supervisory Boards – subsidiaries	2,454	2,327
<b>TOTAL</b>	<b>33,860</b>	<b>41,954</b>
Remuneration of key management personnel of entities of non-core operations	15,858	15,395
<b>TOTAL REMUNERATION OF KEY MANAGEMENT PERSONNEL</b>	<b>49,718</b>	<b>57,349</b>

Until June 30, 2017, members of the management boards of PGE Group companies were employed based on civil contracts and employment contracts. From the end of June 2017, PGE Group companies (direct and indirect subsidiaries) apply a rule according to which management board members are employed on the basis of management services contracts.

The above remuneration is included in other costs by nature disclosed in note 7.2 Costs by nature and function.

### 33. Significant events during and after the reporting period

#### 33.1 Termination of long term contracts

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.

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

Power generating unit	Effective term of LTC	Maximum stranded and extra costs (PLN million)
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	until 2010	617
Rzeszów CHP	until 2012	422
Gorzów CHP	until 2009	108
<b>TOTAL PGE GiEK S.A. branches</b>		<b>6,317</b>
Elektrociepłownia Zielona Góra S.A.	until 2024	778

#### Decisions of the President of the Energy Regulatory Office related to realisation of the LTC Act for PGE GiEK S.A.

In December 2016, the adjustment period for producers covered by the compensation system at PGE GiEK S.A. ended.

The process of determining the amount of annual correction of stranded costs for 2016 was finished through a decision of the URE President of July 31, 2017, while the process of determining the final correction of stranded costs - through a decision by the URE President of August 25, 2017. Given a lack of contested issues in these processes, the URE President's decisions ended the participation of PGE GiEK S.A.'s generation units in the compensation system:

- annual correction of stranded costs for 2016 is positive and amounted to (+) PLN 276 million
- final correction of stranded costs is positive and amounted to (+) PLN 937.8 million

The above amounts were paid to the account of PGE GiEK S.A. in September and December 2017.

The amount of funds collected throughout the entire correction period reached PLN 9,035 million, including stranded costs of PLN 8,749 million and gas costs of PLN 286 million.

Throughout the correction period, numerous court cases took place related to disputes resulting from URE President's decision. As at the date on which these financial statements were prepared, all of these court proceedings were finished.

During the period from 2009 to December 31, 2017:

- At the initiative of PGE GiEK S.A. 19 court proceedings were initiated, including: concerning unfavourable decisions regarding the amount of annual corrections of stranded costs - 14 cases, regarding unfavourable decisions regarding annual corrections of gas costs - 5 cases,
- 7 cases finished with a positive ruling for PGE GiEK; 5 cases finished with a positive ruling for the URE President; 7 cases was partially favourable to PGE GiEK.

On August 28, 2017, PGE GiEK S.A. withdrew its appeal from the Appeals Court and thus withdrew from seeking compensation from the State Treasury - URE President in connection with the URE President's decision for PGE GiEK S.A. on the annual corrections of stranded costs and gas costs.

### Compensation due for Elektrociepłownia Zielona Góra S.A.

Given the acquisition of control over Elektrociepłownia Zielona Góra S.A., compensation due for this company is recognised in financial statements from November 13, 2017 (i.e. from the acquisition date).

### Impact on financial statements for the year 2017

In accordance with the adopted accounting rules, the amount of final correction forecast for PGE GiEK S.A. was settled in 2008-2016. A decision issued in 2017 on the final correction differed from the forecasts. This was connected mainly with the URE President taking into account a CJEU ruling of September 15, 2016, which pointed to a dynamic approach to the aspect of group in LTC settlements. Therefore the decision took into account an extension of the correction period for all generating units. In addition, the URE President in the final correction applied a liquid approach, taking into account the funds collected in the form of advances and annual corrections, which was also favourable to PGE GiEK SA.

Moreover, court rulings that took place until December 31, 2017, resulted in a correction of LTC compensation settlements in the financial statements by PLN 69 million. The amount of corrections was recognised in the statement of comprehensive income after offsetting, in the item other operating income.

In the financial statements for the year 2017, PGE Group recognised the following LTC revenue:

	PGE GiEK S.A.	Elektrociepłownia Zielona Góra S.A.	Total
Revenue from sale	1,211	4	1,215
Other operating income	69	-	69
<b>TOTAL</b>	<b>1,280</b>	<b>4</b>	<b>1,284</b>

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

On March 31, 2017, PGE GiEK S.A. executed another agreement on financial investment in Polska Grupa Górnicza sp. z o.o. ("PGG," currently Polska Grupa Górnicza S.A.) ("Investment") ("Investment Agreement").

The parties of the Agreement are: PGE Górnictwo i Energetyka Konwencjonalna S.A., ENERGA Kogeneracja sp. z o.o., PGNiG TERMIKA S.A., Węglkokoks S.A., Towarzystwo Finansowe „Silesia” Sp. z o.o., Fundusz Inwestycji Polskich Przedsiębiorstw FIZAN (jointly referred later to as the „Investors”) and PGG. Under the Investment Agreement, PGG will purchase certain mining assets from Katowicki Holding Węglowy S.A. pursuant to a preliminary agreement executed on April 1, 2017.

The Investment Agreement regulates the manner in which the Investment will be implemented, operational rules for PGG and its organs as well as rules for the Investor's exit from the Investment. The Investment Agreement includes a recapitalisation of PGG in three stages by PGE GiEK, Enea S.A., ENERGA Kogeneracja sp. z o.o., PGNiG TERMIKA S.A. and Towarzystwo Finansowe Silesia sp. z o.o. by a total of PLN 1 billion.

As part of the PGG recapitalisation, PGE GiEK S.A. committed to purchase new PGG shares with a total nominal value of PLN 100 million in exchange for a cash contribution of PLN 100 million, in three stages:

- as part of the first stage, PGE GiEK S.A. purchased new PGG shares in exchange for a PLN 50 million cash contribution. The first-stage recapitalisation took place on April 6, 2017,
- as part of the second stage, PGE GiEK S.A. purchased new PGG shares in exchange for a PLN 20 million cash contribution. The second-stage recapitalisation took place on June 23, 2017,
- as part of the third stage, PGE GiEK S.A. purchased new PGG shares in exchange for a PLN 30 million cash contribution. The third-stage recapitalisation took place on February 13, 2018,

After the acquisition of the above shares in the third stage, PGE GiEK S.A. will hold a 15.3% stake in PGG, compared to 15.8% as of December 31, 2017.

### 33.3 Purchase of EDF's assets in Poland

On May 11, 2017, PGE S.A. and EDF International SAS and EDF Investment II B.V. (together "EDF") signed a put option agreement concerning the sale of EDF's assets in Poland. Under the put option agreement, EDF obtain the option to call for PGE S.A. to sign a share sale agreement concerning the following assets once certain conditions are met, including EDF securing corporate approvals for the sale transaction.

On May 19, 2017, as a result of EDF exercising its put option under the put option agreement, EDF and PGE signed a conditional sale agreement.

The sale agreement concerned in particular:

- purchase of 99.52% of shares in EDF Polska S.A.,
- purchase of 100% of shares in EDF Investment III B.V.,
- indirect purchase of 50% and 1 share of ZEW Kogeneracja S.A. (shares held by EDF Polska S.A. and EDF Investment III B.V.) and purchase of shares in EDF Polska S.A. subsidiaries engaged in support activities.

Once all of the conditions precedent were met, the transaction was conducted on November 13, 2017.

As a result of the agreement, PGE S.A. purchase a number of generating assets, including: 8 CHP plants, i.e. Kraków, Gdańsk, Gdynia, Toruń, Wrocław, Zielona Góra, Czechnica i Zawidawie, district heating distribution networks in Toruń, Zielona Góra, Siechnice and Zawidawie as well as the Rybnik power plant.

The final value of the transaction was approx. PLN 4.27 billion. PGE's overall expenditures related to the transactions included:

- value of equity of approx. PLN 2.45 billion, establishing using the Locked-Box formula as of December 31, 2016,
- intra-group debt as of November 13, 2017, of approx. PLN 1.68 billion and approx. USD 10 million,
- cost of interest on equity accrued on a pro rata basis counting from January 1, 2017 to the transaction date of PLN 93.27 million on account of the purchased companies having generated economic gains within the scope of the transaction after the price had been set, i.e. December 31, 2016,
- interest payable, as of the transaction closure date, on intra-group debt (and other fees) amounting to PLN 18.21 million and PLN 0.05 million, respectively.

In connection with the closure of the Transaction and the indirect purchase of shares in Zespół Elektrociepłowni Wrocławskich KOGENERACJA S.A. ("KOGENERACJA"), resulting in PGE exceeding the 33% threshold of votes in KOGENERACJA, on February 1, 2018, PGE S.A. announced a tender offer to subscribe for the sale of 2 383 999 dematerialised ordinary bearer shares issued by KOGENERACJA at PLN 81.80 per share, which entitled to 16.00% votes at KOGENERACJA's general meeting. PGE Energia Ciepła S.A. is the buyer. After the tender offer, the buyer together with subsidiary Investment III B.V. intends to hold a total of 66% of votes at KOGENERACJA's general meeting, which corresponds to 9,834,000 shares of KOGENERACJA.

Initial recognition of the acquisition of EDF's assets was done for the purposes of these financial statements. Details are presented in note 1.4 to these financial statements.

### 33.4 Equity investment in Polimex-Mostostal S.A.

On January 18, 2017, PGE S.A. executed agreements concerning an equity investment in Polimex-Mostostal S.A. ("Polimex"):

- investment agreement with ENEA S.A., Energa S.A., PGNiG Technologie S.A. ( jointly referred 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. 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. obliging the parties, subject to fulfilment of conditions precedent, to conduct a sale transaction of 6,000,001 Polimex shares by SPV Operator to Investors, whereas PGE obligated to acquire 1,500,001 Polimex 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.

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

On January 20, 2017, due to the fulfilment 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 fulfilment of conditions precedent, the Company acquired 1,500,001 Polimex shares from SPV Operator for approx. PLN 5.6 million.

On March 21, 2017, Investors announced a tender offer to subscribe for the sale of Polimex shares in a number that would result in the 66% threshold of total votes being exceeded, as a result of which PGE S.A. would be able to purchase up to 42 102 shares of Polimex for PLN 4.90 per share. On March 28, 2017, Investors adjusted the price proposed in the tender offer from PLN 4.90 to PLN 4.91 per one Polimex share. The share purchase was cleared by the National Depository for Securities on April 28, 2017. As a result of the Tender Offer, PGE S.A. purchased 24 shares for PLN 117.84 and holds a total of 39 000 025 shares constituting 16.48% of Polimex's share capital and entitling to 16.48% of votes at Polimex's general meeting.

The investment agreement gives Investors influence over Polimex's financial and operational policy. These entitlements are exercised by the Supervisory Board. As per the agreement, the Supervisory Board will consist of up to 7 members, 4 of which will be appointed by Investors. Moreover, Investors signed an agreement concerning the investment in Polimex. The aim of this agreement is to ensure increased control over Polimex for Investors, who hold a majority share of votes at Polimex's general meeting (65.93%). The agreement stipulates that joint positions will be agreed on through voting on key decisions of the general meeting and supervisory board, including the appointment of Polimex's management board.

Given the Investors' above-mentioned entitlements, which constitute significant influence, the stake in Polimex has been classified as an associate.

As at December 31, 2017, the Group completed work on the allocation of the purchase price of Polimex in accordance with IFRS 3. Details are presented in note 1.4 to these financial statements.

### **33.5 Events after the reporting period**

As at the date on which these financial statements were approved, no significant events took place after the end of the reporting period the impact or disclosure of which is not included in these financial statements.

### 34. Approval of financial statements

These consolidated financial statements were approved for publication by the Management Board on March 6, 2018.

Warsaw, March 6, 2018

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

**President of the  
Management Board      Henryk Baranowski**

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**Vice-President of the  
Management Board      Wojciech Kowalczyk**

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**Vice-President of the  
Management Board      Marek Pastuszko**

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**Vice-President of the  
Management Board      Paweł Śliwa**

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**Vice-President of the  
Management Board      Ryszard Wasilek**

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**Vice-President of the  
Management Board      Emil Wojtowicz**

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Signature of person responsible for drafting these financial statements

Michał Skiba - Director, Reporting and Tax Department