

INDEPENDENT AUDITOR'S REPORT ON THE AUDIT OF THE ANNUAL FINANCIAL STATEMENTS

**To the Shareholders Meeting and Supervisory Board of PGE Polska Grupa
Energetyczna S.A.**

The audit report on the annual financial statements

We have audited the accompanying annual financial statements for the year ended 31 December 2017 of PGE Polska Grupa Energetyczna S.A. ('the Company') located in Warsaw at Mysia 2 containing statement of financial position as at 31 December 2017, the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flow for the period from 1 January 2017 to 31 December 2017, general information, basis for preparation of financial statements and other explanatory information ('the accompanying financial statements').

Responsibilities of the Company's Management and members of the Supervisory Board for the financial statements

The Company's Management is responsible for the preparation, based on properly maintained accounting records, and fair presentation of the financial statements in accordance with International Accounting Standards, International Financial Reporting Standards and related interpretations announced in the form of European Commission decrees and other applicable laws, as well as the Company's Statute. The Company's Management is also responsible for such internal control as determined is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In accordance with the Accounting Act of 29 September 1994 (the 'Accounting Act'), the Company's Management and the members of the Company's Supervisory Board are required to ensure that the accompanying financial statements meet the requirements of the Accounting Act.

Auditor's responsibility

Our objective was to express an opinion on whether the accompanying financial statements give a true and fair view¹ of the financial position and results of the operations of the Company in accordance with International Accounting Standards, International Financial Reporting Standards and related interpretations announced in the form of European Commission regulations and adopted accounting policies.

¹ Translation of the following expression in Polish is 'rzetelny i jasny obraz'.

We conducted our audit of the accompanying financial statements in accordance with:

- Act of 11 May 2017 on Statutory Auditors, Audit Firms and Public Oversight ('Act on Statutory Auditors'),
- National Auditing Standards in the wording of the International Auditing Standards adopted by the resolution no. 2783/52/2015 of the National Council of Statutory Auditors of 10 February 2015 with subsequent amendments,
- Regulation (EU) No. 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC ("Regulation 537/2014").

Those regulations require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

The purpose of the audit is to obtain reasonable assurance as to whether the financial statements as a whole were prepared based on properly maintained accounting records and are free from material misstatement due to fraud or error, and to issue an independent auditor's report containing our opinion. Reasonable assurance is a high level of assurance, but it is not guarantee that an audit conducted in accordance with the above mentioned standards will always detect material misstatements. Misstatements may arise as a result of fraud or error and are considered material if it can reasonably be expected that individually or in aggregate, they could influence economic decisions of the users taken on the basis of these financial statements. The risk of not detecting a material misstatement due to fraud is higher than the risk of not recognizing a material misstatement due to an error, as fraud may involve collusion, falsification, deliberate omissions, misleading or circumventing internal control and may affect every area of law and regulation, not just this directly affecting the financial statements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the presentation of the financial statements.

The scope of the audit does not include assurance on the future profitability of the audited Company nor effectiveness of conducting business matters now and in the future by the Company's Management Board.

In accordance with International Auditing Standard 320 section 5 the concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report. Hence, all auditor's assertions and statements contained in the auditor's report, including those on other information or regulatory requirements, are made with the contemplation of the qualitative

and quantitative materiality levels established in accordance with auditing standards and auditor's professional judgement.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion. The opinion is consistent with the additional report to the audit committee issued on the date of this report.

Independence

While conducting our audit, the key certified auditor and the audit firm remained independent of the Company in accordance with the regulations of Act on Statutory Auditors, Regulation 537/2014 and principles of professional ethics adopted by resolutions of the National Council of Statutory Auditors.

Based on our best knowledge and belief, we declare that we have not provided non-audit services, that are prohibited based on article 136 of the Act on Statutory Auditors and article 5, point 1 of Regulation 537/2014, to the Company.

Appointment of the audit firm

We were appointed to audit the Company's financial statements based on the Company's Supervisory Board resolution dated 20th June 2017. We were auditing the financial statements of the Company for the first time for the financial year ended 31 December 2017.

Most significant assessed risks

In the course of our audit we have identified the below described most significant assessed risks of material misstatement (key audit matters), including due to fraud and we designed appropriate audit procedures in response to those risks. Where we considered to be relevant in order to understand the nature of the identified risk and audit procedures performed we have also included key observations arising with respect to those risks.

These matters were addressed in the context of our audit of the accompanying financial statements as a whole, and in forming our opinion thereon. Therefore we do not provide a separate opinion on these matters.

<i>description of the nature of the risk of material misstatement (key audit matter)</i>	<i>audit procedures in response to the identified risk</i>
First year audit <i>Why a matter was determined to be a key audit matter</i>	<i>Audit approach</i> Our audit procedures covered, among others, the following: <ul style="list-style-type: none">• conducting the initiating meeting with key personnel responsible for financial

<p>The financial statements for the financial year ended 31 December 2017 were the first report being subject to our audit.</p> <p>Bearing in mind the size and scope of the Company's operations, the key was to understand the complexity of the organizational structure of the Company and its impact on the processes within the Company.</p> <p>During the audit, we performed a number of additional procedures necessary to gaining an initial understanding of the Group and its accompanying processes, specific risks related to the business, control mechanisms implemented by the Company and adopted policies affecting the financial reporting of the Company.</p> <p>These procedures allowed us to assess the risk of the audit, identify the risk of material misstatement, including inherent audit risks and control risks, determine materiality levels and the scope of audit procedures.</p> <p>In addition, as part of the first-year auditing, the purpose of our additional procedures was to determine whether opening balances contain distortions that materially affect the financial statements for the current period and whether the accounting policies applied to the opening balance were applied continuously in the preparation of financial statements for the current period, or whether the changes made therein were correctly accounted for and properly presented in accordance with the applicable financial reporting assumptions.</p>	<p>reporting of the Company as well as meetings with members of the audit team, including specialists planned to be involved in the audit procedures;</p> <ul style="list-style-type: none">• Gaining an understanding of the control environment and testing of selected controls in relation to individual processes,• understanding of the Company's accounting policy and significant values included in financial statements based on professional judgment and estimates,• communication with a predecessor auditor, including discussion of key audit matters and review of audit documentation from the previous reporting period,• assessment of the main audit issues from the previous reporting period and their impact on the financial statements for the current financial year and the opening balances. <p>The results of our procedures as well as the revised audit strategy based on them have been communicated to the Management Board of the Company and the Audit Committee.</p>
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<p>Impairment of investments in subsidiaries and long-term financial receivables</p> <p><i>Why a matter was determined to be a key audit matter</i></p> <p>In the financial statements prepared as at 31 December 2017, the Company presented long-term financial assets in the amount of PLN 44,492 million net of impairment losses of PLN 253 million recognized in the current period and reversals of prior period losses of PLN 1,289 million. Determination of the existence of impairment indicators and asset recoverable amount, including changes thereto, requires a number of estimates and judgments from the Company's management, taking into account, among others, changing market and legal conditions impacting the companies operating cash flows.</p> <p>We have identified the issue of impairment of investments in subsidiaries and long-term financial receivables as a key audit matter due to the significant value of financial fixed assets, and due to the complex professional judgment of the Management Board regarding estimation of the recoverable amount of investments in subsidiaries and impairment of long-term financial receivables. Estimation of the recoverable amount of investments in subsidiaries requires the adoption of long-term assumptions regarding operating cash flows of subsidiaries of PGE Polska Grupa Energetyczna SA, including prices of electricity, carbon dioxide emission rights, cost of post-mining land reclamation, as well as parameters of the support to be given to renewable energy. In the case of long-term financial receivables, it is required to assess whether there are objective events</p>	<p><i>Audit approach</i></p> <p>Our audit procedures, with the support of valuation specialists, regarding the investments in subsidiaries and long-term financial receivables covered, among others, the following:</p> <ul style="list-style-type: none"> • assessment of the Company's judgement in the area of impairment indicators of investments in subsidiaries and estimates of recoverable amount of relevant assets, • analysis of forecasts of future cash flows and key assumptions of these forecasts prepared by the Management Board, including price parameters, volumes, operating costs, discount rates and inflation indicators, forecasted growth rates and the discounted cash flow model prepared by the Company by (i) comparing them to the market data and publically available external data; (ii) assessment of the models of discounted cash flows for their mathematical accuracy, (iii) inquiry of the financial department employees and the Management Board of the Company regarding the status of the implementation of the adopted assumptions, including the validity of key estimates; • analysis of potential risks related to the implementation of assumptions by reference to public information or industry knowledge; • reconciliation of the source data of the impairment test models and assessment of impairment indicators to the current financial forecasts of the companies and the realization of budgets; • assessment of the adequacy of disclosures, in accordance with the International Accounting Standard 36 <i>Impairment of Assets</i>, in the Company's financial statements regarding impairment
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<p>indicating impairment of a financial asset, and if there is a decrease in impairment loss, can it be objectively linked to an event occurring after the impairment was recognized.</p> <p><i>Reference to related disclosures in the financial statements</i></p> <p>Disclosures regarding the recoverable amount of property, plant and equipment are presented in note 2.4 "Professional judgment of management and estimates and in note 9.1 „Analysis of the value of non-current financial assets” of the financial statements for the year ended 31 December 2017.</p>	<p>In the case of long-term financial receivables, we assessed the Management Board's judgment regarding the existence of objective events having an impact on the impairment of long-term receivables, including the analysis of publicly available information on these financial assets.</p>
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Opinion

In our opinion, accompanying financial statements:

- give a true and fair view of the financial position of the Company as at 31 December 2017 and its financial performance for the year from 1 January 2017 to 31 December 2017 in accordance with International Accounting Standards, International Financial Reporting Standards and related interpretations announced in the form of regulations of the European Commission and other applicable laws and the adopted accounting policies,
- have been prepared based on properly, in accordance with chapter 2 of Accounting Act, maintained accounting records,
- are in respect of the form and content in accordance with legal regulations governing the Company and the Company's Statute.

Other matters

The financial statements for the prior financial year ended 31 December 2016 were subject to an audit by a key certified auditor acting on behalf of another authorized audit firm, who issued an unqualified opinion on these financial statements, dated 7 March 2017.

Report on other legal and regulatory requirements

Opinion on the Directors' Report

Our opinion on the financial statements does not include the Directors' Report.

The Company's Management is responsible for preparation of the Directors' Report in accordance with the Accounting Act and other applicable laws. In addition, the Company's Management and members of the Company's Supervisory Board are required to ensure that the Directors' Report meets the requirements of the Accounting Act.

Our responsibility in accordance with the Act on Statutory Auditors was to issue an opinion on whether the Director's Report was prepared in accordance with relevant laws and that it is consistent with the information contained in the accompanying financial statements.

Our responsibility was also to make a statement, on whether based on our knowledge about the Company and its environment obtained during the audit of the financial statements we have identified in the Director's Report any material misstatements and to indicate the nature of each of material misstatement.

In our opinion the Directors' Report was prepared in accordance with the relevant regulations and reconciles with the information derived from the accompanying financial statements. Moreover, based on our knowledge of the Company and its environment obtained during the audit of the financial statements, we have not identified material misstatements in the Directors' Report.

Opinion on the corporate governance application representation

The Company's Management and members of the Company's Supervisory Board are responsible for preparation of the representation on application of corporate governance in accordance with the applicable laws.

In connection with the conducted audit of the financial statements, our responsibility in accordance with the Act on Statutory Auditors was to issue an opinion on whether the issuer, obliged to present a representation on application of corporate governance, constituting a separate part of the Director's Report, included in the representation information required by applicable laws and whether the related information is in accordance with applicable regulations and with the information included in the accompanying financial statements.

In our opinion, in the representation on application of corporate governance, the Company has included information stipulated in paragraph 91, section 5, point 4, letter a, b, g, j, k and l of the Regulation of the Minister of Finance of 19 February 2009 on current and periodic information provided by issuers of securities and conditions of deeming information required by the regulations of a non-member country equal ('Regulation'). Information stipulated in paragraph 91, section 5, point 4 letter c-f, h and i of the Regulation included in the representation on application of corporate governance is in accordance with applicable laws and information included in the accompanying financial statements.

Information on preparation of the statement on non-financial information

In accordance with the requirements of the Act on Statutory Auditors, we inform that the Company has published information on the preparation of a separate report on non-financial information, referred to in art. 49b par. 9 of the Accounting Act and that the Company has prepared such a separate report.

We have not performed any attestation services in respect to the separate report on non-financial information and do not express any assurance in this respect.

Other information, including compliance with obligations arising from the law

In addition, we have concluded that the presented in note 25 statement of financial position and statement of comprehensive income, prepared separately for each type of business activity in the transmission or distribution of electricity, transmission, distribution or storage of gas, fuel gas trading, natural gas liquefaction or regasification of liquefied natural gas comply, in all material respects, with the requirements referred to in Article 44 of the Act dated 10 April 1997 Energy Law ("Energy Law").

The scope of regulatory financial information contained in the explanatory note 25 is specified in art. 44 of the Energy Law. Our audit did not include an assessment on whether the information required to be disclosed by the law are sufficient to ensure equal treatment of customers and elimination of cross-subsidy between business activities.

Warsaw, 6th March 2018

Key Certified Auditor

/s/

Artur Żwak
certified auditor
No. 9894

on behalf of
Ernst & Young Audyt Polska spółka
z ograniczoną odpowiedzialnością sp. k.
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