Consolidated annual report of TAURON Polska Energia S.A. Capital Group for the year 2017

13 March 2018

Letter of the President of the Management Board of TAURON Polska Energia S.A.

Ladies and Gentlemen,

On behalf of the Management Board of TAURON Polska Energia S.A. I have the pleasure to introduce to you TAURON Capital Group's Consolidated Annual Report that presents TAURON Group's financial results and highlights of last year.

TAURON Group was implementing its corporate strategy in a favorable economic environment In 2017. The past 12 months brought an improvement of key macroeconomic indicators. Particular attention should be paid to a marked acceleration of Poland's GDP growth rate that topped 4.5 percent. I am looking with optimism at experts' opinions according to which such a strong GDP growth may continue also in 2018.

As a result of the growing economy the domestic electricity consumption and production increased 2 percent in 2017. It is worth emphasizing that a strong growth of electricity generation was achieved based on the power plants using renewable sources and the gas-fired power plants.

To my satisfaction I may say that TAURON Group took advantage of the opportunities presented by the strong growth of the Polish economy. Higher hard coal production output and sales volume as well as rising electricity production, distribution and supply volumes should be noted. As a result we achieved satisfactory financial results and we improved almost all operating and financial indicators in 2017.

TAURON Group generated sales revenue of PLN 17.4 bln in 2017. As a result of our effective actions EBITDA rose 6 percent versus 2016, reaching PLN 3.5 bln. The consolidated net profit reached PLN 1.4 bln in 2017 and it was more than 270 percent higher than in 2016.

TAURON Group's improved financial results were significantly impacted by the steadfastly implemented efficiency improvement program the effects of which, since its launch in 2016, topped one billion PLN. The Management Board of TAURON Polska Energia S.A. places a lot of weight on cost optimization the result of which is the reduction of the costs by 7 percent for the full year. All efficiency improvement actions undertaken brought, in total, a positive financial effect of two billion PLN.

In 2017 TAURON also focused on implementing its CAPEX program worth PLN 3.5 bln during that period. The largest portion of capital expenditures was allocated to the construction of the 910 MW power generation unit at Jaworzno III Power Plant. The construction of this unit progressed in line with the schedule and assumed budget that exceeds PLN 6 bln.

It is worth emphasizing that TAURON, as Poland's largest electricity distributor, is systematically investing in expanding and upgrading its grid infrastructure. The main objective of such actions is to ensure security of electricity supply and such adaptation of the infrastructure so that it could become a platform for creating new services for TAURON Group's customers.

Particular attention should be paid to the fact that in 2017 the Management Board of TAURON Polska Energia S.A. implemented a number of initiatives as a result of which funds required for a further stable expansion of the Group were guaranteed. In July we conducted a 10-year eurobond issue worth EUR 500 mln, and in September we signed an agreement with Bank Gospodarstwa Krajowego that enables a hybrid bond issue worth PLN 400 mln. The diversified mechanism used to finance the operations helped maintain the Group's net debt to EBITDA ratio at a safe level that reached 2.3 at the end of 2017.

Last year we were effectively developing initiatives aimed at increasing TAURON Group's innovations. I am proud of implementing the Strategic Research Agenda which is the first document of this type in the Polish power sector. It precisely describes the directions of expanding innovations in an electric utility. Another important undertaking is carried out jointly with 26 startups and it is to develop solutions aimed at improving the functioning of the existing infrastructure and building new businesses. Furthermore, having the quality of air in mind we began implementing a comprehensive anti-smog program with its main goal being to encourage owners of obsolete heating devices to replace them with ecological heat sources.

It is worth mentioning that in 2017 TAURON shares were, for the fifth time already, included in the prestigious RESPECT index grouping entities listed on the Warsaw Stock Exchange that apply sustainable growth criteria and operate in accordance with the highest corporate governance and investor relations management standards.

Also, the quality of our communications with the capital market was appreciated again – in last year's edition of "The Best Annual Report" competition TAURON was included in the elite *Best of the Best* category and our integrated report was awarded the top prize.

Furthermore, the company was awarded a special prize in the competition for the best investor relations among WIG30 index companies, organized by the Stock Market and Investors Paper "Parkiet" and the Chamber of Brokerage Houses, as well as the *Hero of the capital market 2017* title in the Individual Investors Association's competition.

Last year confirmed TAURON Group's strong position on the energy market which constitutes a solid foundation for further expansion. I believe that, despite many challenges facing TAURON Group, we will accomplish the set operational and financial goals in 2018, and also that we will be effectively implementing the adopted growth strategy so that TAURON Group could be the leader setting the expansion directions for the entire industry.

I am convinced that the business projects and the social dialogue initiatives implemented in 2017 will be contributing to developing TAURON's long term relationships with all stakeholder groups. On behalf of the Management Board of TAURON Polska Energia S.A. I would like to cordially thank our stakeholders, especially the personnel and members of the Supervisory Board, for their commitment to the process of developing and building TAURON Group's value.

Yours respectfully,

Filip Grzegorczyk

President of the Management Board,
TAURON Polska Energia S.A.

Katowice, March 2018

SELECTED FINANCIAL DATA	in thousands PLN		in thousands EUR	
	2017 period from 01.01.2017 to 31.12.2017	2016 period from 01.01.2016 to 31.12.2016	2017 period from 01.01.2017 to 31.12.2017	2016 period from 01.01.2016 to 31.12.2016
Selected consolidated financial data of TAURON Polska Energia S.A. Capital Group				
Revenues on sales	17 416 029	17 646 489	4 103 006	4 032 838
Operating profit (loss)	1 806 271	801 522	425 536	183 176
Profit (loss) before tax	1 757 652	508 861	414 082	116 292
Net profit (loss)	1 382 946	370 137	325 805	84 589
Net profit (loss) attributable to shareholders of the parent entity	1 380 663	367 468	325 267	83 979
Net profit (loss) attributable to non-controlling shares	2 283	2 669	538	610
Other total income	6 366	277 748	1 500	63 475
Total aggregate income	1 389 312	647 885	327 305	148 064
Total aggregate income attributable to shareholders of the parent entity	1 386 996	644 944	326 759	147 392
Total aggregate income attributable to non-controlling shares	2 316	2 941	546	672
Profit (loss) per share (in PLN/EUR) (basic and diluted)	0.79	0.21	0.19	0.05
Weighted average number of shares (in pcs) (basic and diluted)	1 752 549 394	1 752 549 394	1 752 549 394	1 752 549 394
Net cash flows from operating activity	3 558 667	3 064 215	838 379	700 280
Net cash flows from investment activity	(3 871 676)	(3 627 458)	(912 120)	(829 000)
Net cash flows from financial activity	759 629	590 261	178 959	134 895
Increase/(decrease) in net cash and equivalents	446 620	27 018	105 218	6 175
	Status as at 31.12.2017	Status as at 31.12.2016	Status as at 31.12.2017	Status as at 31.12.2016
Fixed assets	31 049 127	29 148 253	7 444 227	6 588 665
Current assets	4 742 894	4 308 641	1 137 139	973 924
Total Assets	35 792 021	33 456 894	8 581 366	7 562 589
Share capital	8 762 747	8 762 747	2 100 925	1 980 729
Equity attributable to shareholders of the parent entity	18 036 446	16 649 266	4 324 354	3 763 396
Equity attributable to non-controlling shares	31 367	30 052	7 520	6 793
Total equity	18 067 813	16 679 318	4 331 874	3 770 189
Long-term liabilities	12 738 005	11 968 719	3 054 018	2 705 407
Short-term liabilities	4 986 203	4 808 857	1 195 474	1 086 993
Total liabilities	17 724 208	16 777 576	4 249 492	3 792 400

The above financial data were converted into EUR, cumulatively for the four quarters of 2017 and 2016, according to the following principles:

– individual items of the statement of financial standing – according to the average NBP exchange rate announced on 29 December 2017 – PLN/EUR 4.1709 (as at 30 December 2016 – PLN/EUR 4.424)

– individual items of the statement of comprehensive income and the statement of cash flows – according to the exchange rate representing the arithmetic means of average NBP exchange rates announced on the last day of each month of the financial period from 01 January 2017 to 31 December 2017 – PLN/EUR 4.2447 (for the period from 01 January 2016 to 31 December 2016 – PLN/EUR 4.3757).

TAURON POLSKA ENERGIA

CAPITAL GROUP TAURON POLSKA ENERGIA S.A.

INDEPENDENT AUDITOR'S OPINION
AND REPORT ON THE AUDIT OF
THE CONSOLIDATED FINANCIAL STATEMENTS OF
THE TAURON POLSKA ENERGIA S.A. CAPITAL GROUP
FOR THE YEAR 2017

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SPRAWOZDANIE NIEZALEŻNEGO BIEGŁEGO REWIDENTA Z BADANIA ROCZNEGO SKONSOLIDOWANEGO SPRAWOZDANIA FINANSOWEGO

Dla Walnego Zgromadzenia oraz dla Rady Nadzorczej TAURON Polska Energia S.A.

Sprawozdanie z badania rocznego skonsolidowanego sprawozdania finansowego

Przeprowadziliśmy badanie załączonego rocznego skonsolidowanego sprawozdania finansowego za rok zakończony dnia 31 grudnia 2017 roku Grupy Kapitałowej TAURON Polska Energia S.A. („Grupa Kapitałowa"), w której jednostką dominującą jest TAURON Polska Energia S.A. („Spółka") z siedzibą w Katowicach, ul. Ściegiennego 3, obejmującego wprowadzenie do skonsolidowanego sprawozdania finansowego, skonsolidowane sprawozdanie z sytuacji finansowej sporządzone na dzień 31 grudnia 2017 roku, skonsolidowane sprawozdanie z całkowitych dochodów, skonsolidowane sprawozdanie ze zmian w kapitale własnym, skonsolidowane sprawozdanie z przepływów pieniężnych za rok obrotowy od dnia 1 stycznia 2017 roku do dnia 31 grudnia 2017 roku oraz dodatkowe informacje i objaśnienia („załączone skonsolidowane sprawozdanie finansowe").

Odpowiedzialność Zarządu Spółki oraz członków Rady Nadzorczej za skonsolidowane sprawozdanie finansowe

Zarząd Spółki jest odpowiedzialny za sporządzenie skonsolidowanego sprawozdania finansowego i za jego rzetelną prezentację zgodnie z Międzynarodowymi Standardami Rachunkowości, Międzynarodowymi Standardami Sprawozdawczości Finansowej oraz związanymi z nimi interpretacjami ogłoszonymi w formie rozporządzeń Komisji Europejskiej oraz innymi obowiązującymi przepisami prawa, a także statutem Spółki. Zarząd Spółki jest również odpowiedzialny za kontrolę wewnętrzną, którą uznaje za niezbędną dla sporządzenia skonsolidowanego sprawozdania finansowego niezawierającego istotnego zniekształcenia spowodowanego oszustwem lub błędem.

Zgodnie z przepisami ustawy z dnia 29 września 1994 roku o rachunkowości („ustawa o rachunkowości"), Zarząd Spółki oraz członkowie Rady Nadzorczej Spółki są zobowiązani do zapewnienia, aby skonsolidowane sprawozdanie finansowe spełniało wymagania przewidziane w ustawie o rachunkowości.

Odpowiedzialność biegłego rewidenta

Naszym zadaniem było wyrażenie opinii o tym, czy załączone skonsolidowane sprawozdanie finansowe przedstawia rzetelny i jasny obraz sytuacji majątkowej i finansowej oraz wyniku finansowego Grupy Kapitałowej zgodnie z Międzynarodowymi Standardami Rachunkowości, Międzynarodowymi Standardami Sprawozdawczości Finansowej oraz związanymi z nimi interpretacjami ogłoszonymi w formie rozporządzeń Komisji Europejskiej i przyjętymi zasadami (polityką) rachunkowości.

Badanie skonsolidowanego sprawozdania finansowego przeprowadziliśmy stosownie do postanowień:

- Ustawy z dnia 11 maja 2017 roku o biegłych rewidentach, firmach audytorskich oraz nadzorze publicznym („ustawa o biegłych rewidentach"),
- Krajowych Standardów Rewizji Finansowej w brzmieniu Międzynarodowych Standardów Badania przyjętych uchwałą nr 2783/52/2015 Krajowej Rady Biegłych Rewidentów z dnia 10 lutego 2015 roku z późn. zm.,
- Rozporządzenia Parlamentu Europejskiego i Rady (UE) nr 537/2014 z dnia 16 kwietnia 2014 roku w sprawie szczegółowych wymogów dotyczących ustawowych badań sprawozdań finansowych jednostek interesu publicznego, uchylającym decyzję Komisji 2005/909/WE („rozporządzenie 537/2014").

Regulacje te wymagają przestrzegania wymogów etycznych oraz zaplanowania i przeprowadzenia badania w taki sposób, aby uzyskać racjonalną pewność, że skonsolidowane sprawozdanie finansowe nie zawiera istotnego zniekształcenia.

Celem badania jest uzyskanie racjonalnej pewności co do tego, czy skonsolidowane sprawozdanie finansowe jako całość nie zawiera istotnego zniekształcenia spowodowanego oszustwem lub błędem, a także wydanie sprawozdania niezależnego biegłego rewidenta zawierającego naszą opinię. Racjonalna pewność jest wysokim poziomem pewności, ale nie gwarantuje, że badanie przeprowadzone zgodnie z powyżej wskazanymi standardami zawsze wykryje istniejące istotne zniekształcenie. Zniekształcenia mogą powstawać na skutek oszustwa lub błędu i są uważane za istotne, jeżeli można racjonalnie oczekiwać, że pojedynczo lub łącznie mogłyby wpłynąć na decyzje gospodarcze użytkowników podjęte na podstawie tego skonsolidowanego sprawozdania finansowego. Ryzyko niewykrycia istotnego zniekształcenia, powstałego na skutek oszustwa jest wyższe niż ryzyko niewykrycia istotnego zniekształcenia powstałego na skutek błędu, ponieważ oszustwo może obejmować zmowy, fałszerstwo, celowe pominięcia, wprowadzanie w błąd lub obejście kontroli wewnętrznej i może dotyczyć każdego obszaru prawa i regulacji, nie tylko tego bezpośrednio wpływającego na skonsolidowane sprawozdanie finansowe.

Badanie polega na przeprowadzeniu procedur służących uzyskaniu dowodów badania kwot i ujawnień w skonsolidowanym sprawozdaniu finansowym. Dobór procedur badania zależy od osądu biegłego rewidenta, w tym od oceny ryzyka istotnego zniekształcenia skonsolidowanego sprawozdania finansowego spowodowanego oszustwem lub błędem. Dokonując oceny tego ryzyka biegły rewident bierze pod uwagę działanie kontroli wewnętrznej, w zakresie dotyczącym sporządzania i rzetelnej prezentacji przez Spółkę skonsolidowanego sprawozdania finansowego, w celu zaprojektowania odpowiednich w danych okolicznościach procedur badania, nie zaś wyrażenia opinii na temat skuteczności kontroli wewnętrznej Spółki. Badanie obejmuje także ocenę odpowiedniości przyjętych zasad (polityki) rachunkowości, racjonalności ustalonych przez Zarząd Spółki wartości szacunkowych, jak również ocenę ogólnej prezentacji skonsolidowanego sprawozdania finansowego.

Zakres badania nie obejmuje zapewnienia co do przyszłej rentowności badanej Grupy Kapitałowej ani efektywności lub skuteczności prowadzenia spraw Grupy Kapitałowej przez Zarząd Spółki obecnie lub w przyszłości.

Zgodnie z Międzynarodowym Standardem Rewizji Finansowej 320 pkt. 5 koncepcja istotności stosowana jest przez biegłego rewidenta zarówno przy planowaniu i przeprowadzaniu badania jak i przy ocenie wpływu rozpoznanych podczas badania zniekształceń oraz nieskorygowanych zniekształceń, jeśli występują, na skonsolidowane sprawozdanie finansowe, a także przy formułowaniu opinii biegłego rewidenta. W związku z powyższym wszystkie stwierdzenia zawarte w sprawozdaniu biegłego rewidenta z badania, w tym stwierdzenia dotyczące innych wymogów prawa i regulacji, wyrażane są z uwzględnieniem jakościowego i wartościowego poziomu istotności ustalonego zgodnie ze standardami badania i osądem biegłego rewidenta.

Wyrażamy przekonanie, że uzyskane przez nas dowody badania stanowią wystarczającą i odpowiednią podstawę do wyrażenia przez nas opinii z badania. Opinia jest spójna z dodatkowym sprawozdaniem dla komitetu audytu wydanym z dniem niniejszego sprawozdania z badania.

Niezależność

W trakcie przeprowadzania badania kluczowy biegły rewident i firma audytorska pozostawali niezależni od jednostek wchodzących w skład Grupy Kapitałowej zgodnie z przepisami ustawy o biegłych rewidentach, Rozporządzenia 537/2014 oraz zasadami etyki zawodowej przyjętymi uchwałami Krajowej Rady Biegłych Rewidentów.

Zgodnie z naszą najlepszą wiedzą i przekonaniem oświadczamy, że nie świadczyliśmy usług niebędących badaniem, które są zabronione przepisami art. 136 ustawy o biegłych rewidentach oraz art. 5 ust. 1 Rozporządzenia 537/2014.

Wybór firmy audytorskiej

Zostaliśmy wybrani do badania skonsolidowanego sprawozdania finansowego Grupy Kapitałowej uchwałą Rady Nadzorczej z dnia 15 marca 2017 roku. Skonsolidowane sprawozdania finansowe Grupy Kapitałowej badamy po raz pierwszy od roku obrotowego zakończonego dnia 31 grudnia 2017 roku.

Najbardziej znaczące rodzaje ryzyka

W trakcie przeprowadzonego badania zidentyfikowaliśmy poniżej opisane najbardziej znaczące rodzaje ryzyka istotnego zniekształcenia (kluczowe sprawy badania), w tym spowodowanego oszustwem oraz opracowaliśmy stosowne procedury badania dotyczące tych rodzajów ryzyka. W przypadkach, w których uznaliśmy za stosowne dla zrozumienia zidentyfikowanego ryzyka oraz wykonanych przez biegłego rewidenta procedur badania, zamieściliśmy również najważniejsze spostrzeżenia związane z tymi rodzajami ryzyka.

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Zagadnienia te zostały uwzględnione w kontekście naszego badania załączonego skonsolidowanego sprawozdania finansowego jako całości oraz przy formułowaniu opinii o tym skonsolidowanym sprawozdaniu finansowym. W związku z powyższym nie wydajemy odrębnej opinii na ich temat.

opis rodzaju ryzyka istotnego zniekształcenia (kluczowe sprawy badania)	*procedury biegłego rewidenta w odpowiedzi na zidentyfikowane ryzyko*
1. Analiza utraty wartości aktywów *Dlaczego zagadnienie jest kluczową sprawą badania* Na dzień 31 grudnia 2017 roku Grupa w ramach istotnych pozycji aktywów wykazywała: aktywa trwałe obejmujące rzeczowe aktywa trwałe, wartość firmy i pozostałe wartości niematerialne (o wartości bilansowej ok. 29 374 mln zł), należności z tytułu pożyczek udzielonych na rzecz wspólnych przedsięwzięć (o wartości bilansowej ok. 570 mln zł), jak również inwestycje we wspólne przedsięwzięcia (o wartości bilansowej ok. 499 mln zł) stanowiące łącznie ok. 85% skonsolidowanej sumy bilansowej Grupy. Zgodnie z MSSF, w wyniku zidentyfikowania przesłanek utraty wartości aktywów środków trwałych, wartości niematerialnych i inwestycji w jednostki stowarzyszone oraz zidentyfikowania obiektywnych zdarzeń wskazujących na możliwą utratę wartości udzielonych pożyczek, co zostało opisane w nocie 11 skonsolidowanego sprawozdania finansowego, przeprowadziła test na	*Podejście do badania* Nasze procedury, w odniesieniu do opisanej kluczowej sprawy badania obejmowały, między innymi: • omówienie procesu oraz identyfikację mechanizmów kontrolnych funkcjonujących w Grupie i związanych z testami na utratę wartości aktywów, jak również zrozumienie stosowanych polityk rachunkowości oraz procedur, w tym środowiska kontroli wewnętrznej, odnoszących się do procesu oceny przesłanek utraty wartości, identyfikacji obiektywnych zdarzeń wskazujących na utratę wartości oraz testów na utratę wartości aktywów; • ocenę przyjętych przez Grupę osądów odnośnie grupowania składników aktywów w ośrodki wypracowujące środki pieniężne; • ocenę, przy wsparciu specjalistów z zakresu wyceny, przyjętych przez Grupę założeń i szacunków służących określeniu wartości odzyskiwalnej aktywów, w tym: - przyjętych przez Grupę kluczowych założeń makroekonomicznych na kolejne lata (w tym: stopy dyskonta, prognozowana stopa wzrostu) poprzez porównanie ich do danych rynkowych oraz dostępnych zewnętrznych danych;

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utratę wartości wskazanych wyżej aktywów. Zagadnienie zostało określone jako kluczowe dla badania skonsolidowanego sprawozdania finansowego Grupy z uwagi na wartość wykazanych powyżej aktywów, która jest istotna dla skonsolidowanego sprawozdania finansowego, jak również z uwagi na element profesjonalnego osądu kierownictwa Grupy oraz złożoność zagadnienia testów na utratę wartości. Przeprowadzenie testów na utratę wartości wymaga przyjęcia przez Zarząd szeregu założeń przyszłych warunków rynkowych i gospodarczych, obejmujących między innymi strategię Grupy TAURON Polska Energia S.A, przyszłe zmiany w zakresie cen surowców, energii elektrycznej, praw majątkowych wynikających ze świadectw pochodzenia energii, praw do emisji CO2 oraz przyszłych przychodów, kosztów i przepływów pieniężnych, średnioważonego kosztu kapitału („WACC"), jak również wpływu potencjalnych i już zatwierdzonych polskich i europejskich zmian regulacyjnych, w tym dotyczących ochrony środowiska i spodziewanych rozwiązań w zakresie rynku mocy oraz przewidywanej sytuacji makroekonomicznej. Wyniki testów na utratę wartości mogłyby się istotnie różnić, gdyby w modelu zastosowano odmienne założenia.	- poprawności arytmetycznej modelu zdyskontowanych przepływów pieniężnych, oraz - założeń przyjętych do ustalenia przepływów pieniężnych oraz wartości rezydualnych po okresie objętym szczegółową strategią; • kierowanie zapytań odnoszących się do statusu realizacji przyjętych założeń, w tym aktualności kluczowych szacunków, do pracowników działu finansowego oraz Zarządu jednostki dominującej; • uzgodnienie danych źródłowych wykorzystywanych w testach na utratę wartości oraz ocenę przesłanek utraty wartości do przyjętych przez jednostkę dominującą prognoz finansowych; • ocenę kompletności ujawnień, zgodnie z Międzynarodowym Standardem Rachunkowości 36 *Utrata wartości aktywów* oraz Międzynarodowym Standardem Rachunkowości 39 *Instrumenty Finansowe*, w skonsolidowanym sprawozdaniu finansowym Grupy w zakresie utraty wartości.

Odniesienie do ujawnienia w skonsolidowanym sprawozdaniu finansowym Grupa zawarła ujawnienie dotyczące analizy przesłanek utraty wartości, szacunków przyjętych do przeprowadzenia testu na utratę wartości, jak również odpisów z tytułu utraty wartości przedmiotowych aktywów w nocie nr 11 informacji dodatkowych do skonsolidowanego sprawozdania finansowego za rok zakończony 31 grudnia 2017 roku.	

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2. Roszczenia, sprawy sądowe i zobowiązania warunkowe	*Podejście do badania*
Dlaczego zagadnienie jest kluczową sprawą badania Grupa występuje jako strona wielu istotnych roszczeń i spraw sądowych. Najbardziej istotne wartościowo zidentyfikowane przez Grupę potencjalne i zgłoszone roszczenia dotyczą rozwiązania umów długoterminowych na zakup energii elektrycznej i praw majątkowych wynikających ze świadectw pochodzenia energii wytwarzanej w odnawialnych źródłach energii. Konieczność utworzenia odpowiednich rezerw oraz ich wysokość, jak również szacunek wartości zobowiązań warunkowych są przedmiotem osądu Zarządu jednostki dominującej. *Odniesienie do ujawnienia w skonsolidowanym sprawozdaniu finansowym* Grupa zawarła ujawnienia dotyczące roszczeń i spraw sądowych w nocie nr 47 informacji dodatkowych do skonsolidowanego sprawozdania finansowego za rok zakończony 31 grudnia 2017 roku.	Nasze procedury, w odniesieniu do opisanej kluczowej sprawy badania obejmowały, między innymi: • monitorowanie zewnętrznych źródeł informacji w celu identyfikacji naruszenia lub potencjalnego naruszenia przez spółki z Grupy przepisów prawa i regulacji; • przegląd przedstawionej do badania dokumentacji dotyczącej spraw sądowych oraz omówienie z Zespołem Prawnej Obsługi Projektów Jednostki Dominującej istotnych spraw sądowych; • analiza kosztów usług prawnych poniesionych w ciągu roku, w celu potwierdzenia kompletności podmiotów świadczących usługi prawne na rzecz Grupy; • uzyskanie pisemnych wyjaśnień od prawników obsługujących spółki z Grupy w zakresie prowadzonych przez nich spraw sądowych i spornych oraz analiza przedstawionych wyjaśnień; • omówienie wybranych spraw sądowych z wewnętrznymi specjalistami z zakresu prawa; • analiza i ocena zobowiązań warunkowych oraz zmian wartości rezerw na roszczenia i sprawy sądowe; • przegląd protokołów posiedzeń organów jednostki dominującej i jej jednostek zależnych oraz protokołów z kontroli organów nadzoru oraz korespondencji z tymi organami; • ocenę kompletności ujawnień w zakresie toczących się istotnych postepowań sądowych i pozasądowych oraz związanych z nimi zobowiązań warunkowych w skonsolidowanym sprawozdaniu finansowym.

3. Zmiana biegłego rewidenta oraz badanie bilansu otwarcia *Dlaczego zagadnienie jest kluczową sprawą badania* Skonsolidowane sprawozdanie finansowe Grupy za rok obrotowy zakończony dnia 31 grudnia 2017 roku było pierwszym sprawozdaniem będącym przedmiotem naszego badania. Zgodnie z zapisami Krajowego Standardu Rewizji Finansowej 510 w brzmieniu Międzynarodowego Standardu Badania 510 „Zlecenie badania po raz pierwszy – stany początkowe", pierwszoroczne badanie sprawozdań finansowych wymaga wykonania wielu dodatkowych czynności audytowych, które w przypadku badania wykonywanego po raz kolejny mają ograniczony zakres. Celem tych dodatkowych procedur audytowych jest zebranie wystarczających i odpowiednich dowodów badania dotyczących tego czy: • stany początkowe zawierają zniekształcenia, które istotnie wpływają na sprawozdania finansowe za bieżący okres oraz • prawidłowe zasady (polityka) rachunkowości zastosowane do stanów początkowych były stosowane w sposób ciągły przy sporządzaniu sprawozdań finansowych za bieżący okres, lub czy zmiany, których w nich dokonano, zostały prawidłowo rozliczone i odpowiednio zaprezentowane zgodnie z	*Podejście do badania* Nasze procedury, w odniesieniu do opisanej kluczowej sprawy badania obejmowały, między innymi: • przeprowadzenie spotkania inicjującego z kluczowym personelem odpowiedzialnym za sprawozdawczość finansową Grupy, jak również spotkań z członkami zespołu audytowego, w tym ze specjalistami planowanymi do zaangażowania w ramach procedur audytowych, • zrozumienie działalności Grupy, jej otoczenia biznesowego oraz kluczowych obszarów ryzyka związanych z prowadzoną działalnością, • zapoznanie się ze środowiskiem kontroli wewnętrznej Grupy obejmujące również przeprowadzenie testów zidentyfikowanych kontroli, • zapoznanie się ze środowiskiem IT, • zrozumienie polityki rachunkowości Grupy oraz ocenę ciągłości jej stosowania, • zrozumienie kluczowych obszarów wymagających szacunku oraz profesjonalnego osądu kierownictwa Grupy, • komunikacja z kluczowym biegłym rewidentem działającym w imieniu poprzedniej firmy audytorskiej obejmująca dyskusję na temat kluczowych zagadnień audytowych oraz przegląd dokumentacji z badania poprzedniego okresu sprawozdawczego, • ocenę głównych zagadnień audytowych z poprzedniego okresu sprawozdawczego oraz ich wpływu na skonsolidowane sprawozdanie finansowe za bieżący rok obrotowy,

mającymi zastosowanie ramowymi założeniami sprawozdawczości finansowej. W związku z powyższym zagadnienie to zostało określone jako kluczowe dla badania skonsolidowanego sprawozdania finansowego Grupy.	• uzyskanie wystarczającej pewności odnośnie bilansu otwarcia poprzez niezależne przeprowadzenie wybranych procedur audytowych w odniesieniu do tego okresu. Nasza strategia badania została omówiona i uzgodniona z Zarządem jednostki dominującej oraz Komitetem Audytu celem zapoznania się z ich oczekiwaniami i dyskusji na temat kluczowych zagadnień sprawozdawczych i audytowych.

Opinia

Naszym zdaniem, załączone skonsolidowane sprawozdanie finansowe:

- przedstawia rzetelny i jasny obraz sytuacji majątkowej i finansowej Grupy Kapitałowej na dzień 31 grudnia 2017 roku oraz jej wyniku finansowego za rok obrotowy od dnia 1 stycznia 2017 roku do dnia 31 grudnia 2017 roku, zgodnie z Międzynarodowymi Standardami Rachunkowości, Międzynarodowymi Standardami Sprawozdawczości Finansowej oraz związanymi z nimi interpretacjami ogłoszonymi w formie rozporządzeń Komisji Europejskiej i przyjętymi zasadami (polityką) rachunkowości,
- jest zgodne co do formy i treści z obowiązującymi Grupę Kapitałową przepisami prawa i statutem Spółki.

Inne sprawy

Skonsolidowane sprawozdanie finansowe za poprzedni rok obrotowy zakończony dnia 31 grudnia 2016 roku było przedmiotem badania przez kluczowego biegłego rewidenta działającego w imieniu innego podmiotu uprawnionego, który w dniu 13 marca 2017 roku wydał opinię bez zastrzeżeń o tym sprawozdaniu finansowym.

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Sprawozdanie na temat innych wymogów prawa i regulacji

Opinia na temat sprawozdania z działalności

Nasza opinia o skonsolidowanym sprawozdaniu finansowym nie obejmuje sprawozdania z działalności Grupy Kapitałowej.

Za sporządzenie sprawozdania z działalności Grupy Kapitałowej zgodnie z przepisami ustawy o rachunkowości oraz innymi obowiązującymi przepisami prawa jest odpowiedzialny Zarząd Spółki. Ponadto Zarząd Spółki oraz członkowie Rady Nadzorczej Spółki są zobowiązani do zapewnienia, aby sprawozdanie z działalności Grupy Kapitałowej spełniało wymagania przewidziane w ustawie o rachunkowości.

Naszym obowiązkiem zgodnie z wymogami ustawy o biegłych rewidentach było wydanie opinii, czy sprawozdanie z działalności Grupy Kapitałowej, za wyjątkiem treści rozdziału „Oświadczenie na temat informacji niefinansowych", zostało sporządzone zgodnie z przepisami prawa oraz, że jest ono zgodne z informacjami zawartymi w załączonym skonsolidowanym sprawozdaniu finansowym.

Naszym obowiązkiem było także złożenie oświadczenia, czy w świetle naszej wiedzy o Grupie Kapitałowej i jej otoczeniu uzyskanej podczas badania skonsolidowanego sprawozdania finansowego stwierdziliśmy w sprawozdaniu z działalności Grupy Kapitałowej istotne zniekształcenia oraz wskazanie, na czym polega każde takie istotne zniekształcenie.

Naszym zdaniem sprawozdanie z działalności Grupy Kapitałowej zostało sporządzone zgodnie z mającymi zastosowanie przepisami i jest zgodne z informacjami zawartymi w załączonym skonsolidowanym sprawozdaniu finansowym. Ponadto, oświadczamy, iż w świetle wiedzy o Grupie Kapitałowej i jej otoczeniu uzyskanej podczas badania skonsolidowanego sprawozdania finansowego, nie stwierdziliśmy w sprawozdaniu z działalności Grupy Kapitałowej istotnych zniekształceń.

Opinia na temat oświadczenia o stosowaniu ładu korporacyjnego

Zarząd Spółki oraz członkowie Rady Nadzorczej Spółki są odpowiedzialni za sporządzenie oświadczenia o stosowaniu ładu korporacyjnego zgodnie z przepisami prawa.

W związku z przeprowadzonym badaniem skonsolidowanego sprawozdania finansowego, naszym obowiązkiem zgodnie z wymogami ustawy o biegłych rewidentach było wydanie opinii, czy emitent obowiązany do złożenia oświadczenia o stosowaniu ładu korporacyjnego, stanowiącego wyodrębnioną część sprawozdania z działalności Grupy Kapitałowej, zawarł w tym oświadczeniu informacje wymagane przepisami prawa oraz w odniesieniu do określonych informacji wskazanych w tych przepisach lub regulaminach stwierdzenie, czy są one zgodne z mającymi zastosowanie przepisami oraz informacjami zawartymi w załączonym skonsolidowanym sprawozdaniu finansowym.

Naszym zdaniem w oświadczeniu o stosowaniu ładu korporacyjnego Spółka zawarła informacje określone w paragrafie 91 ust. 5 punkt 4 lit. a, b, g, j, k oraz lit. l Rozporządzenia Ministra Finansów z dnia 19 lutego 2009 roku w sprawie informacji bieżących i okresowych przekazywanych przez emitentów papierów wartościowych oraz warunków uznawania za równoważne informacji wymaganych przepisami prawa państwa niebędącego państwem członkowskim („Rozporządzenie"). Informacje wskazane w paragrafie 91 ust. 5 punkt 4 lit. c-f, h oraz lit. i tego Rozporządzenia zawarte w oświadczeniu o stosowaniu ładu korporacyjnego są zgodne z mającymi zastosowanie przepisami oraz informacjami zawartymi w załączonym skonsolidowanym sprawozdaniu finansowym.

Informacja o sporządzeniu oświadczenia na temat informacji niefinansowych

Zgodnie z wymogami ustawy o biegłych rewidentach informujemy, że Spółka sporządziła oświadczenie na temat informacji niefinansowych, o którym mowa w art. 49b ust. 1 ustawy o rachunkowości jako wyodrębnioną część sprawozdania z działalności Grupy Kapitałowej.

Nie wykonaliśmy żadnych prac atestacyjnych dotyczących oświadczenia na temat informacji niefinansowych i nie wyrażamy jakiegokolwiek zapewnienia na jego temat.

Warszawa, 12 marca 2018 roku

Kluczowy biegły rewident

Leszek Lerch
Biegły rewident nr 9886

działający w imieniu:
Ernst & Young Audyt Polska
spółka z ograniczoną odpowiedzialnością sp. k.

Rondo ONZ 1
00-124 Warszawa
nr ewid. 130

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

To the General Meeting and Supervisory Board of TAURON Polska Energia S.A.

The audit report on the annual consolidated financial statements

We have audited the accompanying annual financial statements for the year ended 31 December 2017 of TAURON Polska Energia S.A. Group ('the Group'), for which the holding company is TAURON Polska Energia S.A. ('the Company') located in Katowice, at Ściegiennego street 3, containing the statement of financial position as at 31 December 2017, the consolidated statement of comprehensive income, the consolidated statement of changes in equity, the consolidated statement of cash flow for the period from 1 January 2017 to 31 December 2017 and the summary of significant accounting policies and other explanatory notes ('the accompanying consolidated financial statements').

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

The Company's Management is responsible for the preparation and fair presentation of the consolidated 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 Articles of Association. The Company's Management is also responsible for such internal control as determined is necessary to enable the preparation of consolidated 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 consolidated financial statements meet the requirements of the Accounting Act.

Auditor's responsibility

Our objective was to express an opinion on whether the accompanying consolidated financial statements give a true and fair view[1] of the financial position and results of the operations of the Group 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 consolidated 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 consolidated financial statements are free from material misstatement.

The purpose of the audit is to obtain reasonable assurance as to whether the consolidated 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 consolidated 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 consolidated financial statements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

The scope of the audit does not include assurance on the future profitability of the audited Group nor effectiveness of conducting business matters of the Group 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 consolidated 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 entities comprising the Group 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 consolidated financial statements based on the Company's Supervisory Board resolution dated March 15, 2017. We have been auditing the consolidated financial statements of the Company consecutively since the beginning of 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 consolidated financial statements as a whole, and in forming our opinion thereon. Therefore we do not provide a separate opinion on these matters.

description of the nature of the risk of material misstatement (key audit matters)	*audit procedures in response to the identified risk*
1. Impairment of assets analysis *Why the issue is a key audit matter* As at December 31, 2017, the Group presented fixed assets including property, plant and equipment and intangible assets (with a carrying amount of approximately PLN 29 374 million), loans receivable from joint ventures (with a carrying amount of approximately PLN 570 million), as well as investments in joint ventures (with a balance value of approximately PLN 499 million) constituting in total approximately 85% of the Group's consolidated balance sheet total. According to IFRS, based on the analysis of the indicators for impairment of assets (fixed assets, intangible assets, investments in joint ventures), as well as based on identifying objective events indicating a possible loss of value of loans receivable from joint ventures, as described in note 11 to the consolidated financial statements, the Group has performed an impairment test for the above-mentioned assets. The issue was identified as key audit matter in the audit of the consolidated financial statements due to the value of the assets listed above, which is significant for the consolidated financial statements, as well as due to the element of professional judgment of the Group management and the complexity of the impairment tests. Tests of impairment require the Management Board to adopt a number of assumptions regarding future market and economic conditions, such as the strategy of TAURON	*Audit approach* Our procedures, in relation to the key audit matter described, included, among others: • Overview of the process and identification of control mechanisms operating in the Group related to impairment tests of assets, as well as an understanding of the applied accounting policies and procedures, including internal control environment related to the process of assessing impairment indicators and performing of impairment tests, • Assessment of the assumptions made with regard to the grouping of assets into cash-generating units (CGU), • Assessment (with the assistance of valuation specialists) of estimates and assumptions made by the Group in order to determine the assets recoverable amount, including: - the key macroeconomic assumptions adopted by the Group for future years (including: discount rates, projected growth rate) by comparing them to market data and available external data; - arithmetical correctness of the discounted cash flows model, and - assumptions made to determine cash flows and residual values after the period covered by a detailed strategy; • Inquiries to employees of the financial department and the Management Board of the parent entity referring to the status of implementation of the adopted

Polska Energia SA Group, future changes in the prices of raw materials, electricity, property rights arising from certificates of origin of energy, CO_2 emission rights and future revenues, costs and cash flows, weighted average cost of capital ("WACC"), as well as the impact of potential and already approved Polish and European regulatory changes, including environmental protection and the expected shape of the power market, and the anticipated macroeconomic situation. The results of impairment tests could differ materially if the model used different assumptions. *A reference to disclosure in the consolidated financial statements* The Group disclosed information regarding impairment indicators, adopted estimates for the purpose of the impairment test, as well as impairment losses on the assets in note 11 of the notes to the consolidated financial statements for the year ended December 31, 2017.	assumptions, including the validity of key estimates, • Analysis of external sources of information such as industry press and evaluation of potential risk related to the implementation of the assumptions with the support of valuation specialists; • Reconciliation of source data used in impairment test models and assessment of impairment triggers for financial forecasts approved by the Management Board of the parent company; • Assessment of completeness of disclosures in the consolidated financial statements of the Group in terms of impairment in accordance with the International Accounting Standard 36 Impairment of assets and International Accounting Standard 39 Financial Instruments.

2. Claims, lawsuits and contingent liabilities	*Audit approach*
Why the issue is a key audit matter The group is a party to many significant claims and court cases. The most significant are potential and submitted claims identified by the Group relate to the termination of long-term contracts for the purchase of electricity and property rights arising from certificates of origin of energy generated in renewable energy sources. The obligation to create adequate provision and its amount, as well as the estimate of the value of contingent liabilities are the subject of the Parent Company's Management Board's judgment. *A reference to disclosure in the consolidated financial statements* The Group disclosed information regarding claims and court cases in note 47 of the notes to the consolidated financial statements for the year ended December 31, 2017.	Our procedures, in relation to the key audit matter described, included, among others: • Monitoring of external sources of information to identify breaches or potential violations of law and regulations by Group companies; • Review of the documentation regarding court cases presented for the audit purposes and discussion of significant court cases with the Legal Department of the Parent Company; • Analysis of the costs of legal services incurred during the year in order to confirm the completeness of entities providing legal services to the Group; • Obtaining written explanations from lawyers representing companies from the Group with regard to the court and disputable cases conducted by them, and analysis of the provided explanations; • Discussion of the selected court cases with internal specialists in the field of law; • Analysis and assessment of contingent liabilities and changes in the value of provisions for claims and court cases; • Review of minutes of meetings of the legal bodies of the parent company and its subsidiaries as well as control reports of supervisory authorities and correspondence with these authorities. • Assessment of the completeness of disclosures regarding pending major court and out-of-court proceedings and related contingent liabilities in the consolidated financial statements.

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3. Change of the statutory auditor and audit of the opening balances

Why the issue is a key audit matter

The consolidated financial statements of the Group for the financial year ended on December 31, 2017 was the first one being subject to our audit.

In accordance with the provisions of the National Auditing Standard 510, in the wording of International Auditing Standard 510 "Initial Engagements - opening balances", the first-year audit of financial statements requires performing of a number of additional audit procedures that are limited in the case of the audit performed for a consecutive year.

The purpose of these additional audit procedures is to collect sufficient and relevant audit evidence about whether:

• opening balances contain misstatements that materially affect the financial statements for the current period and

• appropriate accounting policy applied to the opening balances was used continuously in the preparation of financial statements for the current period, or whether the changes made were correctly accounted for and properly presented in accordance with the applicable financial reporting framework.

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Audit approach

Our procedures, in relation to the key audit matter described, included, among others:

- the initiating meeting with key personnel responsible for financial reporting of the Group as well as meetings with members of the audit team, including specialists planned to be involved in the audit procedures,
- understanding of the Group's operations, its business environment and key risk areas related to its operations,
- understanding of the Group's internal control environment, including also tests of identified controls,
- understanding of the Group’s IT environment
- understanding of the accounting policy of the Group and assessing the continuity of its application,
- understanding of key areas of estimation and professional judgement of the Group’s management,
- communication with a key certified auditor acting on behalf of the previous audit firm
- including a discussion of key audit issues and a 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 consolidated financial statements for the current financial year,
- obtaining a reasonable assurance of the opening balances by independently carrying out selected audit procedures in relation to this period.

Our audit strategy has been discussed and agreed with the Management Board of the parent company and the Audit Committee in order to know their expectations and discuss key reporting and auditing issues.

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Accordingly, this issue was identified as key audit matter for the audit of the consolidated financial statements of the Group.	

Opinion

In our opinion, accompanying consolidated financial statements:

- give a true and fair view of the financial position of the Group 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,
- are in respect of the form and content in accordance with legal regulations governing the Company and the Company's Articles of Association.

Other matters

The consolidated financial statements for the prior financial year ended December 31, 2016 were subject to an audit by a key certified auditor acting on behalf of another authorised audit firm, who issued an unqualified opinion on these financial statements, dated March 13, 2017.

Report on other legal and regulatory requirements

Opinion on the Directors' Report

Our opinion on the consolidated 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, except for the chapter 'Statement on non-financial information', was prepared in accordance with relevant laws and that it is consistent with the information contained in the accompanying consolidated 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 consolidated 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 consolidated 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 consolidated financial statements.

Information on preparation of the statement on non-financial information

In accordance with the Act on Statutory Auditors, we inform, that the Company has prepared a statement on non-financial information mentioned in article 49b, section 1 of the Accounting Act as a separate element of the Director's Report.

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

Warsaw, 12 March 2018

Key certified auditor

Leszek Lerch
Certified auditor no 9886

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

Rondo ONZ 1
00-124 Warsaw
Reg. No 130

TAURON POLSKA ENERGIA S.A. CAPITAL GROUP

CONSOLIDATED FINANCIAL STATEMENTS
PREPARED ACCORDING TO THE INTERNATIONAL FINANCIAL REPORTING STANDARDS,
AS ENDORSED BY THE EUROPEAN UNION
FOR THE YEAR ENDED 31 DECEMBER 2017

TABLE OF CONTENTS

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME . . . 6
CONSOLIDATED STATEMENT OF FINANCIAL POSITION . . . 7
CONSOLIDATED STATEMENT OF FINANCIAL POSITION – continued . . . 8
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY . . . 9
CONSOLIDATED STATEMENT OF CASH FLOWS . . . 10

INFORMATION ABOUT THE CAPITAL GROUP AND BASIS OF PREPARATION OF THE CONSOLIDATED FINANCIAL STATEMENTS . . . 11

1. General Information about the TAURON Polska Energia S.A. Capital Group and its Parent . . . 11
2. Composition of the TAURON Capital Group and Joint Ventures . . . 11
3. Statement of Compliance . . . 13
4. Going Concern . . . 13
5. Functional and Presentation Currency . . . 13
6. Material Values Based on Professional Judgement and Estimates . . . 13
7. New Standards and Interpretations . . . 14
8. Changes in the Accounting Principles . . . 21
9. Summary of Significant Accounting Policies . . . 21
    9.1. Consolidation principles and the methods of accounting for business acquisitions (including jointly-controlled entities) . . . 21
        9.1.1. Consolidation . . . 21
        9.1.2. Business acquisitions . . . 21
        9.1.3. Acquisition of businesses under common control of the State Treasury . . . 22
    9.2. Property, plant and equipment . . . 22
    9.3. Goodwill . . . 23
    9.4. Energy certificates and gas emission allowances . . . 23
    9.5. Other Intangible Assets . . . 24
    9.6. Impairment of Non-financial Non-current Assets . . . 24
    9.7. Borrowing Costs . . . 24
    9.8. Shares in joint ventures . . . 25
    9.9. Loans to joint ventures . . . 25
    9.10. Other Non-Financial Assets/Liabilities . . . 25
    9.11. Inventories . . . 25
    9.12. Receivables from buyers . . . 25
    9.13. Other financial assets . . . 26
    9.14. Cash and cash equivalents . . . 26
    9.15. Issued capital . . . 26
    9.16. Debt . . . 26
    9.17. Derivative Financial Instruments . . . 26
    9.18. Hedge Accounting . . . 27
    9.19. Provisions for employee benefits . . . 27
    9.20. Provisions for dismantling fixed assets and restoration of land . . . 28
    9.21. Provision for liabilities due to energy certificates and gas emission . . . 28
        9.21.1. Provision for the obligation to surrender energy certificates . . . 28
        9.21.2. Provision for greenhouse gas emission liabilities . . . 29
    9.22. Other provisions . . . 29
    9.23. Deferred income and government grants . . . 29
    9.24. Liabilities to suppliers, Capital commitments and Other financial liabilities . . . 29
    9.25. Receivables / Liabilities arising from taxes and charges . . . 30
    9.26. Current and Deferred Income Tax . . . 30
    9.27. Sales revenue . . . 30
        9.27.1. Revenue from sales of electricity distribution services in the Distribution segment . . . 30
        9.27.2. Revenue from sales of electricity, gas and distribution services in the Sales segment . . . 31

9.27.3. Revenue from wholesale of electricity in the Generation segment . . . 32
9.27.4. Revenue from sales of heat in the Generation segment . . . 32
9.27.5. Revenue from sales of coal in the Mining segment . . . 32
9.28. Operating expenses . . . 33
9.29. Foreign currency transactions translated into the presentation currency of foreign operations . . . 33
9.30. Statement of cash flows . . . 33
9.31. Earnings (loss) per share . . . 33

BUSINESS SEGMENTS . . . 34
10. Operating Segments . . . 34
10.1. Operating Segments . . . 36
10.2. Geographical areas of operations . . . 37

IMPAIRMENT OF NON-FINANCIAL ASSETS . . . 38
11. Impairment of Non-Financial Assets . . . 38
11.1. Impairment of property, plant and equipment . . . 38
11.2. Impairment of goodwill . . . 40

NOTES TO THE CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME . . . 42
12. Sales Revenue . . . 42
13. Cost of Goods, Products, Materials and Services Sold (Cost of Sales) . . . 42
13.1. Costs by type . . . 42
13.2. Costs of employee benefits . . . 43
13.3. Depreciation and amortization charges and impairment losses . . . 44
14. Other Operating Revenue and Expenses . . . 45
15. Finance Income and Costs . . . 45
16. Income Tax . . . 46
16.1. Tax expense in the statement of comprehensive income . . . 46
16.2. Reconciliation of the effective tax rate . . . 46
16.3. Deferred income tax . . . 46
17. Earnings per Share . . . 47

NOTES TO THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION . . . 48
18. Property, Plant and Equipment . . . 48
19. Goodwill . . . 50
20. Energy Certificates and Gas Emission Allowances . . . 50
20.1. Long-term energy certificates and gas emission allowances . . . 50
20.2. Short-term energy certificates and gas emission allowances . . . 50
20.3. Balance of greenhouse gas emission allowances recorded in the Union Registry . . . 51
21. Other Intangible Assets . . . 51
22. Interests in Joint Ventures . . . 52
23. Loans to joint ventures . . . 54
24. Other Financial Assets . . . 56
25. Other Non-Financial Assets . . . 56
25.1. Other non-current non-financial assets . . . 56
25.2. Other current non-financial assets . . . 57
26. Inventories . . . 57
27. Receivables from buyers . . . 58
28. Receivables arising from Taxes and Charges . . . 59
29. Cash and Cash Equivalents . . . 59
30. Equity . . . 59
30.1. Issued capital . . . 59
30.2. Shareholder Rights . . . 60
30.3. Supplementary capital . . . 60
30.4. Retained earnings and dividend limitation . . . 60

30.5. Revaluation reserve – measurement of hedging instruments . . . 60
30.6. Non-controlling interest . . . 60
31. Dividends Paid . . . 61
32. Debt . . . 61
32.1. Loans and borrowings . . . 61
32.2. Bonds issued . . . 63
32.3. Finance lease . . . 66
33. Provisions for Employee Benefits . . . 66
33.1. Provisions for post-employment benefits and jubilee bonuses . . . 66
33.2. Provisions for employment termination benefits . . . 68
34. Provisions for Dismantling Fixed Assets, Restoration of Land and Other . . . 69
34.1. Provision for mine decommissioning costs . . . 69
34.2. Provision for restoration of land and dismantling and removal of fixed assets . . . 70
34.3. Provisions for onerous contracts with a joint venture and for costs . . . 70
35. Provisions for Liabilities due to Gas Emission and Energy Certificates . . . 71
35.1. Provision for Gas Emission Liabilities . . . 72
35.2. Provision for the obligation to surrender energy certificates . . . 72
36. Other Provisions . . . 73
37. Accruals, Deferred Income and Government Grants . . . 75
37.1. Deferred income and government grants . . . 75
37.2. Accrued expenses . . . 75
38. Liabilities to Suppliers . . . 75
39. Capital Commitments . . . 75
40. Liabilities arising from Taxes and Charges . . . 76
41. Other Financial Liabilities . . . 77
42. Other Current Non-Financial Liabilities . . . 77

EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF CASH FLOWS . . . 78
43. Significant Items of the Consolidated Statement of Cash Flows . . . 78
43.1. Cash flows from operating activities . . . 78
43.2. Cash flows from investing activities . . . 79
43.3. Cash flows from financing activities . . . 79

FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT . . . 80
44. Financial Instruments . . . 80
44.1. Carrying amount and fair value of financial instrument classes and categories . . . 80
44.2. Revenue, expenses, gain and loss items included in the statement of comprehensive income by category of financial instruments . . . 81
44.3. Derivative instruments . . . 82
45. Principles and Objectives of Financial Risk Management . . . 83
45.1. Credit risk . . . 84
45.1.1. Credit risk related to receivables from buyers . . . 85
45.1.2. Credit risk related to other financial receivables . . . 85
45.1.3. Credit risk related to cash and cash equivalents . . . 86
45.1.4. Credit risk related to loans granted . . . 86
45.2. Liquidity risk . . . 86
45.3. Market risk . . . 87
45.3.1. Interest rate risk . . . 87
45.3.2. Currency risk . . . 89
45.3.3. Raw material and commodity price risk related to commodity derivative instruments held . . . 91
45.3.4. Unit price risk . . . 92
46. Operational Risk . . . 92

OTHER INFORMATION . . . 94
47. Contingent Liabilities . . . 94
48. Security for Liabilities . . . 98
49. Related-Party Disclosures . . . 100

49.1. Transactions with joint ventures 100
49.2. Transactions with State Treasury companies 100
49.3. Executive compensation 101
50. Operating Leases 102
51. Finance and Capital Management 102
52. Fee of the Certified Auditor or the Entity Authorized to Audit Financial Statements 104
53. Events After the End of the Reporting Period 104

(in PLN '000)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended 31 December 2017	Year ended 31 December 2016
Sales revenue	**12**	17 416 029	17 646 489
Cost of sales, of which:	**13**	(14 503 685)	(15 717 462)
Impairment of non-financial non-current assets	***13.3***	*(40 857)*	*(832 092)*
Profit on sale		**2 912 344**	**1 929 027**
Selling and distribution expenses	**13**	(491 629)	(459 191)
Administrative expenses	**13**	(610 365)	(652 827)
Other operating income and expenses	**14**	(4 079)	(15 487)
Operating profit		**1 806 271**	**801 522**
Share in profit/(loss) of joint ventures	**22**	73 050	60 040
Interest expense on debt	**15**	(209 322)	(259 564)
Other finance income and costs	**15**	87 653	(93 137)
Profit before tax		**1 757 652**	**508 861**
Income tax expense	**16.1**	(374 706)	(138 724)
Net profit		**1 382 946**	**370 137**
Measurement of hedging instruments	**30.5**	(8 159)	127 252
Foreign exchange differences from translation of foreign entities		(2 425)	9 991
Income tax	**16.1**	1 550	(24 178)
Other comprehensive income subject to reclassification to profit or loss		**(9 034)**	**113 065**
Actuarial gains/(losses)	**33.1**	19 653	204 597
Income tax	**16.1**	(3 734)	(38 874)
Share in other comprehensive income of joint ventures	**22**	(519)	(1 040)
Other comprehensive income not subject to reclassification to profit or loss		**15 400**	**164 683**
Other comprehensive income, net of tax		**6 366**	**277 748**
Total comprehensive income		**1 389 312**	**647 885**
Net profit:			
Attributable to equity holders of the Parent		1 380 663	367 468
Attributable to non-controlling interests		2 283	2 669
Total comprehensive income:			
Attributable to equity holders of the Parent		1 386 996	644 944
Attributable to non-controlling interests		2 316	2 941
Basic and diluted earnings per share (in PLN):	**17**	0.79	0.21

Accounting principles (policy) and notes to the consolidated financial statements constitute an integral part hereof.

(in PLN '000)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	As at 31 December 2017	As at 31 December 2016
ASSETS			
Non-current assets			
Property, plant and equipment	**18**	28 079 886	26 355 189
Goodwill	**19**	40 156	40 156
Energy certificates and emission allowances for surrender	**20.1**	303 130	126 260
Other intangible assets	**21**	1 254 077	1 224 427
Investments in joint ventures	**22**	499 204	461 348
Loans granted to joint ventures	**23**	240 767	240 951
Other financial assets	**24**	238 095	227 140
Other non-financial assets	**25.1**	346 846	422 400
Deferred tax assets	**16.3**	46 966	50 382
		31 049 127	**29 148 253**
Current assets			
Energy certificates and emission allowances for surrender	**20.2**	656 703	980 348
Inventories	**26**	295 463	486 120
Receivables from buyers	**27**	2 032 813	1 894 065
Receivables arising from taxes and charges	**28**	244 126	263 854
Loans granted to joint ventures	**23**	329 665	15 116
Other financial assets	**24**	171 910	79 637
Other non-financial assets	**25.2**	87 055	185 008
Cash and cash equivalents	**29**	909 249	384 881
Non-current assets classified as held for sale		15 910	19 612
		4 742 894	**4 308 641**
TOTAL ASSETS		**35 792 021**	**33 456 894**

Accounting principles (policy) and notes to the consolidated financial statements constitute an integral part hereof.

(in PLN '000)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION – continued

	Note	As at 31 December 2017	As at 31 December 2016
EQUITY AND LIABILITIES			
Equity attributable to equity holders of the Parent			
Issued capital	**30.1**	8 762 747	8 762 747
Reserve capital	**30.3**	7 657 086	7 823 339
Revaluation reserve from valuation of hedging instruments	**30.5**	23 051	29 660
Foreign exchange differences from translation of foreign entities		6 776	9 200
Retained earnings/(Accumulated losses)	**30.4**	1 586 786	24 320
		18 036 446	**16 649 266**
Non-controlling interests	**30.6**	**31 367**	**30 052**
Total equity		**18 067 813**	**16 679 318**
Non-current liabilities			
Debt	**32**	9 501 414	8 759 789
Provisions for employee benefits	**33**	1 380 650	1 373 385
Provisions for disassembly of fixed assets, land restoration and other provisions	**34**	351 138	449 310
Accruals, deferred income and government grants	**37**	541 318	554 293
Deferred tax liabilities	**16.3**	871 865	759 568
Other financial liabilities	**41**	91 620	72 374
		12 738 005	**11 968 719**
Current liabilities			
Debt	**32**	351 382	219 740
Liabilities to suppliers	**38**	1 042 427	829 729
Capital commitments	**39**	797 304	1 033 804
Provisions for employee benefits	**33**	134 273	158 228
Provisions for liabilities due to energy certificates and greenhouse gas emission allowances	**35**	953 389	964 821
Other provisions	**36**	353 271	366 456
Accruals, deferred income and government grants	**37**	296 576	267 662
Liabilities arising from taxes and charges	**40**	452 592	410 943
Other financial liabilities	**41**	294 139	256 295
Other non-financial liabilities	**42**	310 850	301 179
		4 986 203	**4 808 857**
Total liabilities		**17 724 208**	**16 777 576**
TOTAL EQUITY AND LIABILITIES		**35 792 021**	**33 456 894**

Accounting principles (policy) and notes to the consolidated financial statements constitute an integral part hereof.

(in PLN '000)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Note	Equity attributable to the equity holders of the Parent						Non-controlling interests	Total equity
		Issued capital	Reserve capital	Revaluation reserve on valuation of hedging instruments	Foreign exchange differences from translation of foreign entities	Retained earnings/ (Accumulated losses)	Total		
As at 1 January 2016		**8 762 747**	**11 277 247**	**(73 414)**	**(791)**	**(3 947 461)**	**16 018 328**	**29 829**	**16 048 157**
Dividend	**30.6, 31**	–	–	–	–	–	**–**	(3 043)	**(3 043)**
Accounting for acquisition of ZCP Brzeszcze		–	–	–	–	(14 041)	**(14 041)**	–	**(14 041)**
Other transactions with non-controlling shareholders	**30.6**	–	–	–	–	35	**35**	325	**360**
Coverage of prior years loss		–	(3 453 908)	–	–	3 453 908	**–**	–	**–**
Transactions with shareholders		**–**	**(3 453 908)**	**–**	**–**	**3 439 902**	**(14 006)**	**(2 718)**	**(16 724)**
Net profit		–	–	–	–	367 468	**367 468**	2 669	**370 137**
Other comprehensive income		–	–	103 074	9 991	164 411	**277 476**	272	**277 748**
Total comprehensive income		**–**	**–**	**103 074**	**9 991**	**531 879**	**644 944**	**2 941**	**647 885**
As at 31 December 2016		**8 762 747**	**7 823 339**	**29 660**	**9 200**	**24 320**	**16 649 266**	**30 052**	**16 679 318**
Dividend	**30.6, 31**	–	–	–	–	–	**–**	(564)	**(564)**
Other transactions with non-controlling shareholders	**30.6**	–	–	–	–	184	**184**	(437)	**(253)**
Coverage of prior years loss	**30.3**	–	(166 253)	–	–	166 253	**–**	–	**–**
Transactions with shareholders		**–**	**(166 253)**	**–**	**–**	**166 437**	**184**	**(1 001)**	**(817)**
Net profit		–	–	–	–	1 380 663	**1 380 663**	2 283	**1 382 946**
Other comprehensive income		–	–	(6 609)	(2 424)	15 366	**6 333**	33	**6 366**
Total comprehensive income		**–**	**–**	**(6 609)**	**(2 424)**	**1 396 029**	**1 386 996**	**2 316**	**1 389 312**
As at 31 December 2017		**8 762 747**	**7 657 086**	**23 051**	**6 776**	**1 586 786**	**18 036 446**	**31 367**	**18 067 813**

Accounting principles (policy) and notes to the consolidated financial statements constitute an integral part hereof.

(in PLN '000)

CONSOLIDATED STATEMENT OF CASH FLOWS

	Note	Year ended 31 December 2017	Year ended 31 December 2016
Cash flows from operating activities			
Profit before taxation		**1 757 652**	**508 861**
Share in (profit)/loss of joint ventures		(73 050)	(60 040)
Depreciation and amortization		1 693 468	1 668 726
Impairment losses on property, plant and equipment and intangible assets		45 604	867 109
Exchange differences		(130 543)	23 549
Interest and commissions		203 653	249 719
Other adjustments of profit before tax		(7 351)	(26 252)
Change in working capital	**43.1**	212 451	227 335
Income tax paid	**43.1**	(143 217)	(394 792)
Net cash from operating activities		**3 558 667**	**3 064 215**
Cash flows from investing activities			
Purchase of property, plant and equipment and intangible assets	**43.2**	(3 561 758)	(3 516 296)
Loans granted	**43.2**	(307 132)	(23 575)
Public aid refund		–	(131 077)
Purchase of investment fund units		(75 000)	(25 000)
Purchase of financial assets		(15 055)	(11 621)
Total payments		**(3 958 945)**	**(3 707 569)**
Proceeds from sale of property, plant and equipment and intangible assets		36 668	33 260
Dividends received	**43.2**	24 636	29 728
Other proceeds		25 965	17 123
Total proceeds		**87 269**	**80 111**
Net cash used in investing activities		**(3 871 676)**	**(3 627 458)**
Cash flows from financing activities			
Redemption of debt securities	**43.3**	(1 650 000)	(3 300 000)
Repayment of loans and borrowings	**43.3**	(154 918)	(140 331)
Interest paid	**43.3**	(184 550)	(255 116)
Other payments		(31 865)	(29 697)
Total payments		**(2 021 333)**	**(3 725 144)**
Issue of debt securities	**43.3**	2 707 462	4 284 607
Proceeds from contracted loans/borrowings		–	914
Subsidies and amends received		73 500	29 884
Total proceeds		**2 780 962**	**4 315 405**
Net cash from financing activities		**759 629**	**590 261**
Net increase / (decrease) in cash and cash equivalents		**446 620**	**27 018**
Net foreign exchange difference		1 820	1 283
Cash and cash equivalents at the beginning of the period	**29**	**354 733**	**327 715**
Cash and cash equivalents at the end of the period, of which:	**29**	**801 353**	**354 733**
restricted cash	**29**	152 952	144 404

Accounting principles (policy) and notes to the consolidated financial statements constitute an integral part hereof.

INFORMATION ABOUT THE CAPITAL GROUP AND BASIS OF PREPARATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

1. General Information about the TAURON Polska Energia S.A. Capital Group and its Parent

The TAURON Polska Energia S.A. Capital Group (the "Group", the "Capital Group", the "TAURON Group") is composed of TAURON Polska Energia S.A. (the "Parent", the "Company") and its subsidiaries. TAURON Polska Energia S.A. is located in Katowice in ul. ks. Piotra Ściegiennego 3. The Company operates as a joint-stock company incorporated by a notarized deed on 6 December 2006. Until 16 November 2007 it had operated under the name Energetyka Południe S.A.

The Parent has been entered in the Register of Entrepreneurs of the National Court Register kept by the District Court for Katowice-Wschód, Business Division of the National Court Register, under number KRS 0000271562.

The duration of the Parent and the companies in the Capital Group is unlimited. The operations are based on appropriate licences granted to individual companies of the Group.

The core business of the TAURON Group includes the following segments: Mining, Generation (encompassing generation of electricity from conventional and renewable sources and generation of heat), Distribution, Sales and other operations, including customer service, which has been discussed in more detail in Note 10 to these consolidated financial statements.

These consolidated financial statements have been prepared for the financial year ended 31 December 2017 and contain comparative information for the year ended 31 December 2016.

These consolidated financial statements were approved for publication by the Management Board on 12 March 2018.

Composition of the Management Board

Management Board as at 31 December 2017:

- Filip Grzegorczyk – President of the Management Board;
- Jarosław Broda – Vice President of the Management Board;
- Kamil Kamiński – Vice President of the Management Board;
- Marek Wadowski – Vice President of the Management Board.

Changes to the composition of the Management Board in the year ended 31 December 2017 have been presented in the Management Board's report on the activities of the TAURON Polska Energia S.A. Capital Group for the year ended 31 December 2017 (Section 6.11.1).

As at the date of approval of these financial statements for publication the composition of the Management Board had not changed.

Management Board as at 31 December 2016:

- Filip Grzegorczyk – President of the Management Board;
- Jarosław Broda – Vice President of the Management Board;
- Kamil Kamiński – Vice President of the Management Board;
- Marek Wadowski – Vice President of the Management Board;
- Piotr Zawistowski – Vice President of the Management Board.

2. Composition of the TAURON Capital Group and Joint Ventures

As at 31 December 2017, TAURON Polska Energia S.A. held direct and indirect interest in the following key subsidiaries:

(in PLN '000)

Item	Company name	Registered office	Operating segment	Interest in the share capital by TAURON Polska Energia S.A.	Interest in the decision-making body held by TAURON Polska Energia S.A.
1	TAURON Wydobycie S.A.	Jaworzno	Mining	100.00%	100.00%
2	TAURON Wytwarzanie S.A.[1]	Jaworzno	Generation	100.00%	100.00%
3	Nowe Jaworzno Grupa TAURON Sp. z o.o.[1]	Jaworzno	Generation	100.00%	100.00%
4	TAURON Ekoenergia Sp. z o.o.	Jelenia Góra	Generation	100.00%	100.00%
5	Marselwind Sp. z o.o.	Katowice	Generation	100.00%	100.00%
6	TAURON Ciepło Sp. z o.o.	Katowice	Generation	100.00%	100.00%
7	TAURON Serwis Sp. z o.o.	Katowice	Generation	95.61%	95.61%
8	TAURON Dystrybucja S.A.	Kraków	Distribution	99.74%	99.75%
9	TAURON Dystrybucja Serwis S.A.	Wrocław	Distribution	100.00%	100.00%
10	TAURON Dystrybucja Pomiary Sp. z o.o.[2]	Tarnów	Distribution	99.74%	99.75%
11	TAURON Sprzedaż Sp. z o.o.	Kraków	Sales	100.00%	100.00%
12	TAURON Sprzedaż GZE Sp. z o.o.	Gliwice	Sales	100.00%	100.00%
13	TAURON Czech Energy s.r.o.	Ostrawa, Czech Republic	Sales	100.00%	100.00%
14	TAURON Obsługa Klienta Sp. z o.o.	Wrocław	Other	100.00%	100.00%
15	Kopalnia Wapienia Czatkowice Sp. z o.o.	Krzeszowice	Other	100.00%	100.00%
16	Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.[3]	Warszawa	Other	100.00%	100.00%
17	TAURON Sweden Energy AB (publ)	Sztokholm, Sweden	Other	100.00%	100.00%
18	Biomasa Grupa TAURON Sp. z o.o.	Stalowa Wola	Other	100.00%	100.00%
19	Wsparcie Grupa TAURON Sp. z o.o.[2, 4]	Tarnów	Other	99.74%	99.75%

[1] *On 3 April 2017 TAURON Wytwarzanie S.A. was spun off and a branch of activity was transferred to Nowe Jaworzno Grupa TAURON Sp. z o.o.*
[2] *TAURON Polska Energia S.A. holds indirect interest in TAURON Dystrybucja Pomiary Sp. z o.o. and Wsparcie Grupa TAURON Sp. z o. o (formerly: KOMFORT-ZET Sp. z o.o.) through its subsidiary, TAURON Dystrybucja S.A. TAURON Polska Energia S.A. uses shares in TAURON Dystrybucja Pomiary Sp. z o.o.*
[3] *On 8 March 2017, the Extraordinary General Shareholders' Meeting of Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. in liquidation adopted a resolution to revoke the liquidation of the company.*
[4] *On 6 September 2017, the name of Komfort-Zet Sp. z o.o. was changed to Wsparcie Grupa TAURON Sp. z o.o.*

As at 31 December 2017, TAURON Polska Energia S.A. held direct and indirect interest in the following key jointly-controlled entities:

Item	Company name	Registered office	Operating segment	Interest in the share capital and in the decision-making body held by TAURON Polska Energia S.A.
1	Elektrociepłownia Stalowa Wola S.A.[1]	Stalowa Wola	Generation	50.00%
2	TAMEH HOLDING Sp. z o.o.[2]	Dąbrowa Górnicza	Generation	50.00%
3	TAMEH POLSKA Sp. z o.o.[2]	Dąbrowa Górnicza	Generation	50.00%
4	TAMEH Czech s.r.o.[2]	Ostrawa, Czech Republic	Generation	50.00%

[1] *TAURON Polska Energia S.A. holds indirect interest in Elektrociepłownia Stalowa Wola S.A. through a subsidiary, TAURON Wytwarzanie S.A.*
[2] *The companies form a capital group. TAURON Polska Energia S.A. holds direct interest in the issued capital and the governing body of TAMEH HOLDING Sp. z o.o., which holds 100% interest in the issued capital and the governing bodies of TAMEH POLSKA Sp. z o.o. and TAMEH Czech s.r.o.*

3. Statement of Compliance

These consolidated financial statements have been prepared in compliance with the requirements of the International Financial Reporting Standards ("IFRS"), as endorsed by the European Union ("EU").

The IFRS consist of standards and interpretations approved by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee.

The Group companies and the Parent keep their accounting records and prepare financial statements in compliance with the International Financial Reporting Standards ("IFRS") as endorsed by the EU, except for TAURON Czech Energy s.r.o. and TAURON Sweden Energy AB (publ), which keep their accounting records and prepare their financial statements in line with accounting policies applicable in the Czech Republic and Sweden, respectively.

The consolidated financial statements contain adjustments which have not been recognized in the accounting records of the Group companies, introduced in order to achieve compliance of the consolidated financial statements with EU-IFRS.

4. Going Concern

These consolidated financial statements have been prepared on the assumption that the Group companies will continue as a going concern in the foreseeable future. As at the date of approval for publication of these consolidated financial statements, no circumstances posing a risk to the Group companies' ability to continue as a going concern had been identified.

The Group identifies and actively manages the liquidity risk understood as the possibility of losing or limiting the ability to pay current expenses, and despite the negative working capital as at the balance sheet date, has the full capacity to pay its liabilities on the date of their payment. As at the balance sheet date, the Group has available financing under the overdraft facility and as part of bond issue programs.

5. Functional and Presentation Currency

The Polish zloty has been used as the presentation currency of these consolidated financial statements and the functional currency of the Parent and the subsidiaries included in these consolidated financial statements, except TAURON Czech Energy s.r.o. and TAURON Sweden Energy AB (publ). The functional currency of TAURON Czech Energy s.r.o. is the Czech koruna ("CZK"), while the functional currency of TAURON Sweden Energy AB (publ) is the euro ("EUR"). Individual items of the financial statements of TAURON Czech Energy s.r.o. and TAURON Sweden Energy AB (publ) are translated to the presentation currency of the TAURON Group using applicable exchange rates.

These consolidated financial statements have been presented in the Polish zloty (PLN) and all figures are in PLN thousand, unless stated otherwise.

6. Material Values Based on Professional Judgement and Estimates

When applying the accounting policy to the issues mentioned below, professional judgement of the management, along with accounting estimates, have been of key importance; they have impacted figures disclosed in the consolidated financial statements and in the explanatory notes. The assumptions underlying the estimates have been based on the Management Board's best knowledge of current and future actions and events in individual areas. In the period covered by these consolidated financial statements, there were no significant changes in estimates or estimation methods applied, which would affect the current or future periods, other than those presented below or described further in these consolidated financial statements.

Presented below are the items of the consolidated financial statements exposed to a considerable risk of material adjustment of the carrying amounts of assets and liabilities.

(in PLN '000)

Item	Significant accounting policies	Note	Estimates and assumptions
Property, plant and equipment	Note 9.2 Note 9.6	Note 18	At the end of each reporting period, the Group verifies whether or not there are objective indications of impairment of items of property, plant and equipment. If there are objective indications of impairment, the Group is obliged to perform impairment tests for items of property, plant and equipment. The Group reviews, at least at the end of each financial year, the useful lives of property, plant and equipment, and depreciation charges may be adjusted effective from the beginning of the reporting period when the review was completed.
Goodwill	Note 9.3 Note 9.6	Note 19	Goodwill is tested for impairment annually and at the end of each reporting period if indications of impairment are identified.
Provisions	Note 9.19 Note 9.20 Note 9.21 Note 9.22	Note 33 Note 34 Note 35 Note 36	The value of provisions is determined based on assumptions made by the Group as well as a methodology and calculation method that is appropriate for a specific provision. To this end, the Group verifies the probability of an outflow of resources embodying economic benefits and estimates reliably the amount necessary to fulfil the obligation. Provisions are recognized if the probability of an outflow of resources embodying economic benefits is higher than 50%.
Accrued revenue from the sale of electricity and distribution services in the Sales segment	Note 9.27	Note 12	At each balance sheet date the Group estimates and recognizes additional estimates from the sale of electricity and distribution services.
Deferred tax assets	Note 9.26	Note 16.3	At the end of each reporting period, the Group verifies whether or not the deferred tax assets may be realized.
Derivative instruments	Note 9.17	Note 44.3	Derivative financial instruments are measured at fair value at the end of each reporting period. Derivative instruments acquired and held for internal purposes are not measured at the end of the reporting period.
Receivables from buyers	Note 9.12	Note 27	At the end of each reporting period, the Group verifies whether or not there are any objective indications of impairment of its receivables from buyers, relying mainly on the assessment of the counterparty credit risk. Where appropriate, impairment losses are recognized on receivables from buyers.

Additionally, the Group's material estimates include contingent liabilities recognized, in particular, in relation to legal proceedings to which the Group companies are parties. Contingent liabilities have been discussed in more detail in Note 47 to these consolidated financial statements.

7. New Standards and Interpretations

The Group did not choose an early application of any standards, amendments to standards or interpretations, which were published, but are not yet mandatorily effective.

- **Standards issued by the International Accounting Standards Board ("IASB") which have been endorsed by the European Union, but are not yet effective**

According to the Management Board, the following new standards may materially impact the accounting policies applied thus far:

IFRS 9 *Financial Instruments*

Effective date in the EU: annual periods beginning on or after 1 January 2018.

Key changes introduced by IFRS 9 *Financial Instruments*:

- **Change in the classification and measurement of financial assets**

Instead of the four classes of financial assets identified by IAS 39 *Financial Instruments: Recognition and Measurement*, IFRS 9 *Financial Instruments* identifies three categories of financial assets:

- financial assets measured at amortized cost,
- financial assets measured at fair value through other comprehensive income (FVTOCI),
- financial assets measured at fair value through profit or loss (FVTPL).

(in PLN '000)

Pursuant to IFRS 9 *Financial Instruments*, financial assets are classified upon initial recognition based on:

- cash flow characteristics (SPPI test; Solely Payments of Principal and Interest),
- a business model underlying the management of financial assets.

- **Introduction of a new impairment testing model based on expected credit losses**

In place of the existing rules for the recognition of credit losses based on the incurred credit losses, IFRS 9 *Financial Instruments* introduces the concept of expected credit losses, resulting in recognition of a loss allowance upon initial recognition of an asset. The requirements regarding impairment of financial assets apply in particular to financial assets measured at amortized cost and at fair value through other comprehensive income.

Impact on the consolidated financial statements as at 1 January 2018

Estimated effect on retained earnings of the application of IFRS 9 *Financial Instruments* as at 1 January 2018:

Categories and classes of financial instruments in line with IAS 39	IAS 39		IFRS 9			Estimated effect of change
				Fair value through:		
	At amortized/ historical cost	At fair value	At amortized cost	Profit/loss	Other comprehensive income	Increase/ (decrease)
1 Financial assets at fair value through profit or loss – held for trading	**–**	**106 292**	**–**	**106 292**	**–**	**–**
Derivative instruments	–	4 934	–	4 934	–	–
Investment fund units	–	101 358	–	101 358	–	–
2 Financial assets available for sale	**141 698**	**2 719**	**–**	**130 657**	**–**	**(13 760)**
Long-term shares*	141 656	–	–	127 896	–	(13 760)
Short-term shares*	42	–	–	42	–	–
Investment fund units	–	2 719	–	2 719	–	–
3 Loans and receivables	**2 734 059**	**–**	**2 473 012**	**177 274**	**–**	**(83 773)**
Receivables from buyers	2 032 813	–	2 049 658	–	–	16 845
Gross value	2 262 490	–	2 262 490	–	–	–
Impairment loss	(229 677)	–	(212 832)	–	–	16 845
Deposits	39 756	–	39 756	–	–	–
Loans granted	580 979	–	329 402	150 959	–	(100 618)
Gross value	580 979	–	340 212	150 959	–	(89 808)
Impairment loss	–	–	(10 810)	–	–	(10 810)
Other financial receivables	80 511	–	54 196	26 315	–	–
4 Hedging derivative instruments	**–**	**28 482**	**–**	**28 482**	**–**	**–**
5 Cash and cash equivalents	**–**	**909 249**	**–**	**909 249**	**–**	**–**
Total estimated effect of the application of IFRS 9 on financial assets						**(97 533)**
1 Financial liabilities measured at amortised cost	**470 239**	**–**	**437 128**	**–**	**–**	**33 111**
Loan granted by European Investment Bank	470 239	–	437 128	–	–	33 111
Total estimated effect of the application of IFRS 9 on financial liabilites						**33 111**
Estimated effect on retained earnings						**(64 422)**
Deferred tax						**12 240**
Estimated effect on retained earnings after deferred tax						**(52 182)**

* *Measurement at historical cost.*

- **Change in the classification and measurement of financial assets**

The categories of financial assets identified in IAS 39 *Financial Instruments: Recognition and Measurement* cannot be directly translated into those identified in IFRS 9 *Financial instruments* and therefore the Group has developed a method of classification of financial assets which sets the terms of SPPI and business model tests. The Group performed business model and SPPI tests for all material items of its financial assets as at 31 December 2017.

The carried out analysis revealed that a considerable portion of financial assets presented in the above table generates cash flows corresponding solely to the repayment of principal and interest and they are maintained under a business model based solely on acquiring cash flows, which translates into classification as financial assets measured at amortized cost.

The subordinated loan and the loans used for the purposes of repayment of debt originated to the joint venture Elektrociepłownia Stalowa Wola S.A., measured at amortized cost in line with IAS 39 *Financial Instruments: Recognition and Measurement*, whose carrying amount as at 31 December 2017 was PLN 240 767 thousand, were categorized into financial assets measured at fair value through profit or loss at PLN 150 959 thousand since the cash flows they generate do not correspond solely to the repayment of principal and interest. The application of IFRS 9 *Financial Instruments in* this respect will reduce the retained earnings of the Group as at 1 January 2018 by PLN 89 808 thousand.

IFRS 9 *Financial Instruments* requires that equity interests in other entities be measured at fair value, also with respect to those shares which – due to limited availability of information – have thus far been measured at cost less impairment losses. Therefore the Group estimated the fair value of the above instruments in line with the adjusted net assets method considering its share in the net assets and adjusting the value by relevant factors affecting the measurement, such as the non-controlling interest discount and the discount for the lack of liquidity of the above instruments. As the key factors affecting the value of the acquired shares had not changed at a given end of the reporting period as compared to initial recognition, in the case of some instruments the Group assumes that the historical cost is a reasonable approximation of fair value. The application of IFRS 9 *Financial Instruments in the* scope of equity share measurement will reduce the retained earnings of the Group as at 1 January 2018 by PLN 13 760 thousand. In accordance with IFRS 9 *Financial Instruments* the above equity instruments will be measured at fair value through profit or loss.

- **Introduction of a new impairment model based on expected credit losses**

The Group has identified the following categories of financial assets for which it has verified the impact of the calculation of expected credit losses in line with IFRS 9 *Financial Instruments* on the consolidated financial statements:

– receivables from buyers and

– originated loans.

As far as the receivables from buyers are concerned, the Group has designated a portfolio of strategic counterparties in the case of which it is expected that the historical performance (lack of material delinquencies) does not provide full information on the expected credit losses to which the Group may be exposed. The risk of insolvency on the part of the strategic counterparties has been assessed based on the ratings assigned to the counterparties using an internal scoring model and appropriately restated to account for the probability of default. The expected credit loss, in line with IFRS 9 *Financial Instruments*, will be calculated based on the estimated potential recovery due to the security lodged. It is expected that the historical performance information concerning the receivables from buyers (other counterparties) may reflect the credit risk that will be faced in future periods. The expected credit losses for such a group of counterparties have been estimated through an analysis of ageing of receivables and percentage ratios assigned to individual ranges and groups (such as receivables claimed at court, receivables from counterparties in bankruptcy) which help estimate the value of receivables from buyers which are not expected to be paid.

Based on carried out analyses, the Group expects that the total value of loss allowance for expected credit losses on receivables from buyers following the application of IFRS 9 *Financial Instruments* will decrease compared to the value estimated in line with the earlier principles, which will consequently increase the retained earnings as at 1 January 2018 by PLN 16 845 thousand.

As far as originated loans are concerned, the Group assesses the risk of insolvency on the part of the borrowers based on the ratings assigned to the counterparties using an internal scoring model, appropriately restated to account for the probability of default. The expected credit loss, in line with IFRS 9 *Financial Instruments*, will be calculated based on the estimated potential recovery due to the security lodged and the time value of money.

It is expected that due to the application of IFRS 9 *Financial Instruments* the total value of loss allowance for expected credit losses on originated loans, measured at amortized cost, will decrease retained earnings of the Group as at 1 January 2018 by PLN 10 810 thousand.

Based on the method of classification of financial assets, the Group has verified the cash flows of owned financial assets and the Group's business models underlying the management of the financial assets.

- **Change in the measurement of liabilities in case of modification of cash flows resulting from the contract**

IFRS 9 *Financial Instruments* also introduces a change in the terms of measurement of liabilities for which there is a modification of cash flows resulting from the contract. The TAURON Group has liabilities under loans granted by European Investment Bank, for which such a modification takes place in the form of a change in the interest rate on a fixed date. The Group estimates that the implementation of IFRS 9 *Financial Instruments* in this respect will increase the retained earnings of the Group as at 1 January 2018 by PLN 33 111 thousand.

- **Hedge Accounting**

As at 31 December 2017 the Group held instruments hedging fluctuations in cash flows related to issued bonds and resulting from the interest rate risk. These interest rate swaps are subject to hedge accounting.

An analysis of risks and rewards related to the adoption of the hedge accounting solutions introduced by IFRS 9 *Financial Instruments* in light of the Group's portfolio of financial instruments revealed that the principles defined in IAS 39 *Financial Instruments: Recognition and Measurement* should still be applied. It is not expected that the application of the provisions of IFRS 9 *Financial Instruments* concerning hedge accounting will have a material impact on the Group's consolidated financial statements as regards its transactions. The Group has been monitoring the work carried out by the International Accounting Standards Board, also with respect to the date of obligatory application of the hedge accounting provisions.

- **Measurement of financial liabilities arising from issued financial guarantees**

The Group conducted an analysis of the influence of IFRS 9 *Financial Instruments* on the measurement of financial liabilities arising from issued financial guarantees. As a result of conducted analysis no material impact of IFRS 9 *Financial Instruments* on the measurement of liabilities in the amount of expected credit losses was identified.

IFRS 15 *Revenue from Contracts with Customers*

Effective date in the EU: annual periods beginning on or after 1 January 2018.

The standard specifies how and when to recognize revenue as well as requires more informative, relevant disclosures. The Standard replaces IAS 18 *Revenue*, IAS 11 *Construction Contracts*, IFRIC 18 *Transfer of Assets from Customers* and a number of interpretations concerning revenue recognition.

The key principles introduced by IFRS 15 *Revenue from Contracts with Customers* are:

- five steps of revenue recognition: identify the contract(s) with a customer; identify the performance obligations in the contract; determine the transaction price; allocate the transaction price to each performance obligation; and recognize revenue when (or as) the entity satisfies a performance obligation;
- revenue is recognized when (or as) the entity satisfies the obligation to transfer an asset. The asset has been transferred as control has passed;
- the transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties.

The new standard requires significantly extended disclosures regarding sales and revenue in order to help users of financial statements to understand the nature, recognition period, amount, risks and uncertainties related to the revenue and cash flows arising from contracts with customers. In particular, a reporting entity is obliged to make quantitative and qualitative disclosures regarding: contracts with customers, key assumptions and estimates made and assets recognized from the costs to obtain or fulfil a contract with a customer.

Impact on the consolidated financial statements as at 1 January 2018

The Group has decided to apply the modified retrospective approach and the practical expedients allowed by IFRS 15 *Revenue from Contracts with Customers*, i.e. with the cumulative effect of initially applying this Standard recognized at the date of initial application.

The Group has conducted a five-step analysis of its contracts with customers, which is necessary for proper measurement of its revenue in accordance with IFRS 15 *Revenue from Contracts with Customers* – from identification of contracts (or contract groups), through selection of liability items and determination of prices, their allocation to individual liability items to revenue recognition.

(in PLN '000)

The estimated impact on retained earnings of the initial adoption of IFRS 15 *Revenue from Contracts with Customers* as at 1 January 2018:

Estimated impact on retained earnings	
Distribution segment	
Write-off of deferred income (connection fees)	195 666
	195 666
Sales segment	
Recognition of assets relating to variable consideration and discounts	7 504
Recognition of assets relating to contract acquisition costs	23 479
	30 983
Total estimated impact of IFRS 15	**226 649**
Deferred tax	(43 063)
Estimated impact on retained earnings, taking account of deferred tax	**183 586**

In the Distribution segment, the Group analysed contracts constituting the basis for recognition of revenue from the connection of new buyers as well as distribution and comprehensive services contracts in light of IFRS 15 *Revenue from Contracts with Customers* so as to identify separate services as required by the standard. The measures taken by the Group included an analysis of the sources of law which form the basis for the provision of the aforesaid services, the legal obligations imposed on it with respect to the connection of new buyers, its discretion to set the prices of services, the relationship and interdependence of the consideration received for the provision of the aforesaid services, the possibility to include both supplies in one contract and the rights of customers being parties to the connection contract and the distribution/comprehensive contract to resign from the purchase of distribution/comprehensive services. Considering this analysis the Group decided that, in accordance with IFRS 15 *Revenue from Contracts with Customers*, the distribution/comprehensive services contracts and the connection contracts are not a single obligation and should not be recognized in aggregate. Therefore the Group will recognize revenues from the connection contracts on a non-recurring basis when the promised service, i.e. connection to the grid, has been performed. Such recognition complies with the Group's accounting policy and will not change its profit/loss.

As far as the recognition of revenue from connection fees for services performed by 1 July 2009 is concerned, the Group decided that, if a retrospective approach is adopted, as at 1 January 2018 PLN 195 666 thousand of deferred income will be transferred to the Group's equity and the revenue will be subsequently reduced due to lack of recognition of the above deferred income in the Group's future profit or loss (with approx. PLN 22 million in the year ended 31 December 2018).

By the date of approval of these consolidated financial statements, as part of measures taken to implement IFRS 15 *Revenue from Contracts with Customers*, the Group also analysed the following, key issues that may affect the profit/loss and the Group's revenues and expenses in the Sales segment.

- Customer acquisition costs – costs to execute new contracts with customers incurred by the companies in the Sales segment on external counterparties and other companies in the Group.

  The Group has analysed whether such costs may be recognized as the costs of obtaining a contract in line with IFRS 15 *Revenue from Contracts with Customers* and capitalized throughout the term of the contract. The analysis revealed that the costs of commission the payment of which depends on a specific contract and which are now charged to profit or loss on a non-recurring basis satisfy the conditions for classification to the costs of obtaining a contract and thus they may be capitalized as of 1 January 2018. The application of IFRS 15 *Revenues from Contracts with Customers* with respect to the costs of obtaining a contract will increase the Group's retained earnings as at 1 January 2018 by PLN 23 479 thousand.

- Multiple-element arrangements – contracts whereby the customer is offered multiple products of the Group which guarantees more favourable terms and conditions than if the products were sold under separate contracts. This applies mainly to combined sales of gas and electricity.

  The analysis revealed that in the case of sales of electricity and gas the Group may apply a simplification whereby separate goods/services, which are generally the same and whose transfer to a customer is conducted in the same manner, are recognized as a single performance obligation. It also revealed that the allocation of the discount between the supply of electricity and gas of the prices set out in the multiple-element arrangements with customers is close to the individual selling prices (determined as the cost plus margin). Therefore the prices set out in the contracts with customers may be applied directly to separate recognition of revenues from the supplies of electricity and gas and no further reallocation of the discount is necessary. As a result the above issues do not impact the Group's equity as at 1 January 2018. In addition, as a result of the carried out analyses, the Group identified that it is an intermediary for the gas transmission service.

- Variable consideration, discounts – a customer who signs a contract or acquires additional goods or services is entitled to a cash discount.

  Following an analysis of the contractual provisions, the Group believes that the discounts given to buyers under the customer schemes in place should be included in the calculation of the transaction price and should reduce the revenue from sales of goods or services. In the opinion of the Group the discounts offered by the companies in the Sales segment are not a separate performance obligation. Therefore the discount offered to the customer is carried forward, i.e. it is recognised as a reduction of revenue over the average outstanding duration of the relevant contract as determined by the Group. The application of IFRS 15 *Revenues from Contracts with Customers* with respect to the variable consideration will increase the Group's retained earnings as at 1 January 2018 by PLN 7 504 thousand.

- Agreements to sell Group's products and services combined with after-sale services – the Group has made an agreement with the buyer to sell products/services with additional after-sale services (e.g. electrician services) and a property insurance contract with a business partner (insurer) whereby the insurer provides the ancillary service directly to the buyer. The fee for the ancillary service has been included in the commercial fee.

  The Group has analysed the contractual provisions to determine whether its obligation is a performance obligation in the form of delivery of specific services in which case the Group would be an ordering party, or in the form of ordering the delivery of the services to a third party in which case the Group would be an intermediary. Having analysed the responsibilities, risks and freedom of prices as regards the services provided by the third party, the Group believes that as far as the above agreements are concerned, it is an intermediary. In view of the above, in accordance with IFRS 15 *Revenues from Contracts with Customers*, the Group is planning to recognize the revenue from the above services, at the amount of consideration net of the fee paid to the third party for the services provided by the party. The above issue does not materially impact the Group's retained earnings as at 1 January 2018.

In the opinion of the Group, as far as the sales of heat in Generation segment is concerned, the customer who is party to a contract cannot derive benefits from individual chargeable elements listed in the contract. This means that individual elements of a contract do not meet the criteria necessary for being treated as separate performance obligations. Therefore every contract with a customer contains one performance obligation in the form of comprehensive heat supply service. The above issue does not impact the Group's retained earnings as at 1 January 2018.

IFRS 16 *Leases*

Effective date in the EU: annual periods beginning on or after 1 January 2019.

Under IFRS 16 *Leases*, the lessee recognizes the right-of-use asset and the lease liability. The right-of-use asset is treated similarly to other non-financial assets and depreciated accordingly. Lease liabilities are initially measured at the present value of the lease payments due over the lease term, discounted at the rate implicit in the lease, if that can be readily determined. If that rate cannot be readily determined, the lessee uses the incremental borrowing rate. Lessors continue to classify leases as operating or finance leases, i.e. in line with IAS 17 *Leases*. A lease is classified by a lessor as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset. Otherwise, the lease is classified as an operating lease. A lessor recognizes finance income over the lease term of a finance lease, based on a pattern reflecting a constant periodic rate of return on the net investment. A lessor recognizes operating lease payments as income on a straight-line basis or another systematic basis if that basis is more representative of the pattern in which better reflects benefits from the use of the underlying asset.

(in PLN '000)

Impact on the consolidated financial statements

A preliminary analysis of the impact of IFRS 16 *Leases* on the accounting policies has shown a change material for the Group, i.e. the need to recognize lease assets and liabilities for leases currently classified as operating leases in the financial statements. The Group analyses all its lease agreements to identify leases which require recognition of assets and liabilities in the financial statements. In addition, the Group identified the key areas in relation to which it analyses the impact of IFRS 16 *Leasing*, including, i.a. the right of transmission easement, perpetual usufruct right to land and lease agreements. As at the date or approval of these consolidated financial statements for publication, the Group is in the process of analysing the impact of planned changes on the consolidated financial statements.

Clarifications to IFRS 15 *Revenue from Contracts with Customers*

Effective date in the EU: annual periods beginning on or after 1 January 2018.

The amendment provides additional clarifications as to some requirements in addition to introducing a new exemption for entities applying IFRS 15 *Revenue from Contracts with Customers* for the first time.

According to the Management Board the following revised standards will not materially impact the accounting policies applied:

Standard	Effective in the EU as of (*annual periods beginning on or after the date provided*)
Revised IFRS 4 *Insurance Contracts*	1 January 2018
Revised IFRS 2 *Share-based Payments: Classification and Measurement of Share-based Payment Transactions*	1 January 2018
Annual *Improvements to IFRS (Cycle 2014–2016)*:	
IFRS 1 *First-time Adoption of International Financial Reporting Standards*	1 January 2018
IAS 28 *Investments in Associates and Joint Ventures*	1 January 2018

- **Standards, amendments to standards and interpretations issued by the International Accounting Standards Board (IASB) which have not been endorsed by the European Union and are not yet effective**

According to the Management Board, the following standards, amendments to standards and interpretations will not materially impact the accounting policies applied thus far:

(in PLN '000)

Standard	Effective date specified in the Standard, not endorsed by the EU (*annual periods beginning on or after the date provided*)
IFRS 14 *Regulatory Deferral Accounts*	1 January 2016*
IFRS 17 *Insurance contracts*	1 January 2021
Revised IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures: Sale or Contribution of Assets between Investor and its Associate or Joint Venture* with subsequent amendments	the effective date has been postponed
IFRIC 22 *Foreign Currency Transactions and Advance Consideration*	1 January 2018
Revised IAS 40 *Investment Property – Transfers of Investment Property*	1 January 2018
Annual *Improvements to IFRS (Cycle 2015–2017)*:	
IAS 12 *Income Taxes*	1 January 2019
IAS 23 *Borrowing Costs*	1 January 2019
IFRS 3 *Business Combinations*	1 January 2019
IFRS 11 *Joint Arrangements*	1 January 2019
IFRIC 23 *Uncertainty over Income Tax Treatments*	1 January 2019
Revised IFRS 9 *Financial Instruments*	1 January 2019
Revised IAS 19 *Employee Benefits*	1 January 2019
Revised IAS 28 *Investments in Associates and Joint Ventures*	1 January 2019

* *The European Commission decided not to launch the process of endorsement of the interim standard for use in the EU until the publication of the final version of IFRS 14.*

Hedge accounting for the financial assets and liabilities portfolio remains beyond the scope of the regulations adopted by the EU.

8. Changes in the Accounting Principles

The accounting principles (policy) adopted for the preparation of these consolidated financial statements are consistent with those used for the preparation of the annual consolidated financial statements of the Group for the year ended 31 December 2016, except for the application of the following amendments to standards.

According to the Management Board, the introduction of the following revised standards has not materially impacted the accounting policies applied thus far.

Standard	Effective in the EU as of (*annual periods beginning on or after the date provided*)
Revised IAS 7 *Statement of Cash Flows*	1 January 2017
Revised IAS 12 *Income Taxes*	1 January 2017
Annual *Improvements to IFRS (Cycle 2014–2016)*:	
IFRS 12 *Disclosure of Interests in Other Entities*	1 January 2017

9. Summary of Significant Accounting Policies

9.1. Consolidation principles and the methods of accounting for business acquisitions (including jointly-controlled entities)

9.1.1. Consolidation

Subsidiaries are entities controlled by the Parent directly or indirectly through its subsidiaries.

Subsidiaries are consolidated using the full method from the date of assuming to the date of losing control. Financial statements of subsidiaries are prepared for the same reporting period as those of the Parent, using consistent accounting principles. Balances and transactions between the Group entities, including unrealized gains and losses (if not indicating impairment) which result from transactions within the Group, are eliminated.

9.1.2. Business acquisitions

Business acquisitions are accounted for using the acquisition method. As at the acquisition date, the acquiring entity recognizes identifiable assets acquired and liabilities assumed, which are measured at fair value.

Goodwill is measured as the excess of the aggregate of the consideration transferred for the acquisition, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree over the net of the acquisition-date fair values of the identifiable assets acquired and the liabilities assumed. The accounting policy applicable to goodwill has been presented in Note 9.3.

9.1.3. Acquisition of businesses under common control of the State Treasury

Combinations of businesses under common control of the State Treasury (i.e. those which have remained under control of the State Treasury before and after the transaction) are accounted for using the pooling of interest method in accordance with the principles described below.

Following the business combination, the continuity of common control is presented in the financial statements, while the fair value remeasurement of the net assets (or recognition of new assets) or measurement of goodwill are not presented therein, as none of the entities combined is actually acquired. The financial statements are prepared as if the combined entities had been combined as of the date when common control began to be exercised.

When accounting for a combination of entities under common control of the State Treasury, the Company relies on the separate financial statements of the acquire which have been brought into line with requirements of IFRS to determine the value of its assets and liabilities. When accounting for a combination of entities under common control of the State Treasury within the TAURON Group, the Company relies on the consolidated financial statements as a source of the value of assets and liabilities of the acquired subsidiary.

The difference between the book value of the net assets recognized as a result of a business combination and the value of shares recognized in the accounting records of the acquirer thus far or consideration paid is recognized in the equity of the acquirer.

The entities acquired in May 2007 were controlled by the State Treasury, which means that the Company and those entities were under common control of the State Treasury at the time of the acquisition. Therefore, in the opinion of the Company, the transaction meets the definition of a transaction under common control, hence it has been excluded from the scope of IFRS 3 *Business combinations.*

9.2. Property, plant and equipment — Note 18

Key fixed assets for the Group by segment:

- Generation:
  - boilers with accessories, turbines with generators, transformers and thermal stations as well as equipment used for purposes of fuel unloading and transportation, pumping stations and sulphur-recovery facilities;
  - thermal stations, equipment used for purposes of fuel unloading and transportation as well as pumping stations and water treatment facilities;
  - wind farms, water turbine sets as well as weirs and dams.
- Distribution: power lines and stations. Power lines are located on the area of 58 thousand square meters, with the total length of ca. 270 thousand km. The Group's assets include over 59 thousand electrical substations;
- Mining: mechanized lining, pit shafts and dip-headings and fixed assets located in the mine walls and the coal processing plant.

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses.

The cost includes:

- acquisition price or manufacturing cost;
- costs directly attributable to the purchase and bringing the asset to a usable condition;
- the expected cost of disassembly and removal of items of property, plant and equipment, and restoration of their current location to its original condition (the accounting policy on provisioning for these costs has been presented in Note 9.20);
- borrowing costs (the accounting policy on capitalizing these costs has been presented in Note 9.7).

All material elements included in an asset but having various useful lives (components) are identified and separated as at the date of acquisition of an item of property, plant and equipment. Components also include costs of overhauls, periodic inspections and costs of replacing their key parts.

The Group recognizes specialized spare parts and service equipment as separate items of property, plant and equipment if their useful life exceeds one year.

Depreciation is calculated by reference to the cost of the asset less its residual value. Depreciation is based on a depreciation plan determining the estimated useful life of each fixed asset. Items of property, plant and equipment (including components) are depreciated on a straight-line basis over the period of their estimated useful lives, except for land and fixed assets under construction, which are not depreciated. Specialized spare parts and service equipment are depreciated over the useful life of the fixed asset they relate to.

Depreciation principles applied to assets used under finance leases are consistent with those applied to depreciation of assets owned by the entity. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset item is fully depreciated over the shorter of the lease term and its useful life.

Average residual useful lives by fixed asset group:

Asset group	Average remaining depreciation period (number of years)
Buildings, premises, civil and water engineering structures	18 years
Plant and machinery	12 years
Other tangible fixed assets	4 years

Items of property, plant and equipment are tested for impairment if there is any indication of impairment. Impairment tests for property, plant and equipment are carried out in line with the accounting policy presented in Note 9.6.

9.3. Goodwill — Note 19

Goodwill is carried at its initial amount (determined in line with the accounting policy presented in Note 9.1.2) less accumulated impairment losses. Goodwill is not amortized but it is tested for impairment on an annual basis or more frequently if any indications of impairment occur.

As at the acquisition date, goodwill acquired is allocated to each cash-generating unit ("CGU") that may derive benefits from synergy effects. An operating segment is the lowest level in the Group with attributable goodwill and with goodwill monitored for internal management purposes in the Group (except the Generation segment). In the Generation segment, however, the lowest level units are cash-generating units related to electricity generation from conventional sources, including in CHP units, in co-firing of biomass and other thermal energy (TAURON Wytwarzanie S.A.), cash-generating units related to generation of electricity from renewable sources (TAURON Ekoenergia Sp. z o.o.) and cash-generating units related to generation, distribution and sale of heat (TAURON Ciepło Sp. z o.o.).

Impairment tests for goodwill are performed in line with the accounting principles presented in Note 9.6.

9.4. Energy certificates and gas emission allowances — Note 20

Energy certificates and gas emission allowances include:

- certificates of energy generated using renewable sources and in gas, methane and other cogeneration and energy efficiency certificates acquired or received for surrendering purposes due to the sale of electricity to end buyers or for resale;
- greenhouse gas emission allowances received or acquired with the intention to fulfil the obligation resulting from emission of greenhouse gases or for resale.

Energy certificates and greenhouse gas emission allowances are classified considering the Group's intention to use them as at the acquisition date (possible subsequent reclassification) as:

- current intangible assets – energy certificates and gas emission allowances designated for internal purposes, where the Group has the intention to surrender them so as to fulfil the obligation for the current or future year, if the Group intends to surrender the allowances in the same year;
- non-current intangible assets – energy certificates and gas emission allowances designated for internal purposes, where they are intended to be used for purposes of the fulfilment of the surrendering obligation for the following years and they are planned to be surrendered within more than one year of the end of the reporting period;
- inventories – energy certificates and gas emission allowances designated for sale.

At initial recognition, the said assets are measured in accordance with the following principles:

	Acquired	Granted/Received free of charge	Release
Energy certificates	Acquisition cost	Fair value as at the receipt date	Weighted average
Greenhouse gas emission allowances	Acquisition cost or fair value*	Nominal value (i.e. zero)	Obtained free of charge in the first place, subsequently acquired ones (according to weighted average)

* *Fair value – Greenhouse gas emission allowances in the trading portfolios.*

The energy certificates and the emission gas allowances are surrendered (in correspondence with settlement of the provision amount) at the date of their being redeemed. The principles applicable to the recognition of provisions relating to the energy certificate surrendering obligation and liabilities arising from gas emissions have been presented in Note 9.21.

9.5. Other Intangible Assets Note 21

Key items of other intangible assets include acquired right to perpetual usufruct of land, software, concessions, patents, licenses and similar items.

Other intangible assets are measured at cost less accumulated amortization and impairment losses.

Other intangible assets, except those which have not been made available for use, are amortized over their estimated useful lives. Amortization is calculated by reference to the initial value less the residual value.

Residual value is included in determining the basis for calculation of depreciation charges, if for a given asset, an active market exists or a third party has committed to buy the asset upon completion of its useful life. For the right to perpetual usufruct of land, the residual value has been determined on the basis of market prices. As the residual value is similar to the carrying amount, the said right has not been amortized.

Average residual useful lives by other intangible asset group:

Asset group	Average remaining amortization period (number of years)
Development expenses	2 years
Software, concessions, patents, licenses and similar items	3 years
Other	9 years

9.6. Impairment of Non-financial Non-current Assets Note 11

Goodwill is tested for impairment every year and each time when indications of impairment have been identified. Other non-financial non-current assets are tested for impairment if there are indications that they may have been impaired.

Impairment tests include estimation of the recoverable amount of an asset or the cash-generating unit (CGU) to which the asset belongs. Information concerning identification of CGU which goodwill is allocated to has been presented in Note 9.3.

The recoverable amount of an asset or CGU is the higher of the fair value less cost to sell and the value in use. If the carrying amount of an asset or CGU exceeds its recoverable amount, impairment occurs and the value of the asset is reduced to the recoverable amount determined.

Impairment losses are allocated to goodwill in the first place and the remaining amount is allocated to individual assets forming the CGU based on the share of the carrying amount of each asset in the carrying amount of the CGU, with the proviso that as a result of such allocation the carrying amount of the asset may not be lower than the highest of the fair value less cost to sell, the value in use and zero.

If the indications of impairment driving the recognition of an impairment loss in a preceding period are no longer present, the impairment loss is reversed or reduced. Impairment losses on goodwill are not reversed.

9.7. Borrowing Costs

Borrowing costs are capitalized as part of the cost of qualifying non-current assets.

Borrowing costs include mainly interest on specific and general borrowings calculated using the effective interest method and financial charges relating to finance lease agreements. The effective portion of the hedge for contracts that satisfy the hedge accounting criteria and are entered into in connection with financing the development of non-current assets is also capitalized (the hedge accounting policy has been presented in Note 9.18).

After the completion of a qualifying asset that has been financed using specific borrowings, specific borrowings and the related costs are not taken into account when determining borrowing costs eligible for capitalization.

General borrowing costs eligible for capitalization are determined by applying the capitalization rate to expenditure incurred for qualifying assets. The capitalization rate is the weighted average rate of all borrowing costs related to borrowings classified as liabilities in a given period, other than specific borrowings.

9.8. Shares in joint ventures — Note 22

Joint arrangements of the Group are classified as joint ventures. Interests in joint ventures where the Group exercises joint control are accounted for using the equity method, whereby the initial value of the investment carried at cost is increased or reduced by a share in profits/losses and in other comprehensive income of the joint venture as from the acquisition date (recognized in profit or loss or in other comprehensive income of the Group, as appropriate).

Interests in joint ventures are tested for impairment if indications of impairment or reversal of impairment losses recognized before are identified.

9.9. Loans to joint ventures — Note 23

Loans granted to a joint venture do not satisfy the criteria to be recognized as a net investment in a joint venture. Initially, loans are recognized at fair value and measured at amortized cost less impairment losses as at the end of the reporting period.

9.10. Other Non-Financial Assets/Liabilities — Note 25, 42

Other non-financial assets of the Group include prepayments as well as advance payments for fixed assets under construction, intangible assets and inventories. Prepayments, as non-monetary items, are not discounted.

Prepayments include in particular costs of production preparation in coal mines, including costs of reinforcing working faces and costs of drilling drifts which are not classified as property, plant and equipment. Such costs are carried at the amount of expenditures incurred by the Group and recognized in profit or loss by reference to the percentage monthly output relative to the volume of commercial coal planned to be produced from each working face.

Other financial liabilities include e.g. overpayments from customers, advance payments towards the connection fee and the excess of liabilities over assets of the Company's Social Benefits Fund.

9.11. Inventories — Note 26

The Group's inventories include mainly the inventory of fuels (being materials, semi-finished products or finished products) as well as energy certificates and greenhouse gas emission allowances designated for sale.

Inventories are measured at the lower of cost and net realizable value. Greenhouse gas emission allowances purchased for resale and generation of profit in the short term due to volatility of market prices are measured at fair value at the end of each reporting period. Release of inventories is measured using the weighted average method.

9.12. Receivables from buyers — Note 27

Receivables from buyers include amounts due which have been billed and those which have been recognized on account of revenue but have not been measured and billed due to the buyer settlement system used. The accounting policy applicable to accrued revenue has been presented in Note 9.27.

Receivables from buyers are measured at the originally billed amounts (including the effect of discounting, if material), less allowances/write-downs.

As at the end of the reporting period, the Group verifies whether there are any objective indications of impairment of its receivables or groups of receivables. Material objective indications of impairment include mainly delays in payment, major financial difficulties encountered by the debtor, institution of court proceedings against the debtor, the debtor being placed into liquidation or bankruptcy, or the occurrence of a material adverse change in the economic, legal or market environment of the debtor.

If the recoverable amount of an asset is lower than its carrying amount, the entity recognizes an allowance/write-down reducing it to the present value of projected cash flows. An allowance/write-down corresponding to the whole amount due is recognized for receivables from debtors placed into liquidation or bankruptcy, those for which court proceedings have been instituted as well as those subject to administrative or court enforcement proceedings. Otherwise, the allowance/write-down is recognized collectively based on the criterion of delinquency – for amounts past due by 6 to 9 months: 50% and for those which have not been paid for more than 9 months: 100%.

Allowances/write-downs on receivables are charged to operating expenses or finance costs, according to the type of receivables.

9.13. Other financial assets — Note 24

Other financial assets the Group includes e.g. units in investment funds, shares, investments, bid bonds, deposits and collateral, derivatives and loans granted to unrelated entities.

9.14. Cash and cash equivalents — Note 29

Cash and cash equivalents include in particular cash at bank and in hand and short-term deposits with original maturity of up to three months.

Cash is recognized at face value. At the end of the reporting period, the face value of cash deposited in bank accounts includes also accrued bank interest or interest calculated by the entity itself.

9.15. Issued capital — Note 30.1

Issued capital is recognized at the amount determined in the articles of association of the Parent and recorded in the court register.

9.16. Debt — Note 32

Debt comprises bank loans, borrowings, debt securities and finance lease liabilities.

Initially, debt is measured at fair value less transaction costs. After initial recognition it is measured at amortized cost using the effective interest method.

Finance leases transferring substantially all the risks and rewards of ownership of a lease object to the Capital Group are recognized in the statement of financial position as at the inception of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments.

Leases whereby the lessor retains substantially all the risks and rewards of ownership of the leased asset are classified as operating leases. Operating lease payments and subsequent lease rents are charged to expenses using the straight-line method over the lease term.

9.17. Derivative Financial Instruments — Note 44.3

Derivative financial instruments falling within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* are classified as financial assets/financial liabilities measured at fair value through profit or loss, except derivatives which are designated as hedging instruments and subject to hedge accounting. Derivative instruments acquired and held for internal purposes as excluded from the scope of IAS 39 *Financial Instruments: Recognition and Measurement* are not measured at the end of the reporting period.

Derivatives classified as "financial assets/financial liabilities measured at fair value through profit or loss" are measured at fair value, taking into account their market value as at the end of the reporting period. Changes in the fair value of these instruments are recognized in profit or loss for the period. Derivatives are disclosed as assets if their value is positive or as liabilities if their value if negative.

As at the end of the reporting period, Interest Rate Swaps (IRS) acquired and held to hedge the interest rate risk relating to bonds issued are subject to hedge accounting (the accounting policy has been discussed in detail in Note 9.18). Other derivative instruments held by the Group as at the end of the reporting period are not subject to hedge accounting.

At the end of the reporting period, the Group held the following derivative instruments:

Classification	Instrument type
Derivatives subject to hedge accounting	Interest Rate Swaps concluded to hedge against risk related to interest rate changes. Subject to hedge accounting; detailed policy presented in Note 9.18.
Derivatives not subject to hedge accounting, classified as "assets/liabilities measured at fair value through profit or loss"	• forward contracts concluded in order to hedge against risk related to foreign exchange rate fluctuations;
	• forwards and futures for purchase and sales of emission allowances, energy and other commodities, concluded and maintained for speculation purposes;
	• Coupon Only Cross Currency Swap (CCIRS) entered into in order to hedge against currency risk.
Derivatives excluded from the scope of IAS 39	Forwards and futures for purchase and sales of non-financial assets, concluded and maintained for own use purposes.

9.18. Hedge Accounting

In order to hedge the interest rate risk the Group uses Interest Rate Swaps (IRS). These instruments hedge cash flows related to bonds issued. Such transactions are subject to hedge accounting.

At the inception of the hedge the hedging relationship is designated and the risk management objective and strategy for undertaking the hedge are documented formally.

A cash flow hedge is accounted for in the following manner:

- the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognized directly in other comprehensive income; and
- the ineffective portion of the gain or loss on the hedging instrument is recognized in profit or loss for the period.

Gain or loss from revaluation of the hedging instrument disclosed in other comprehensive income is recognized directly in profit or loss in the same period during which the hedged item affects profit or loss for the period.

9.19. Provisions for employee benefits — Note 33

In accordance with compensation policies, employees of the Group companies are entitled to the following post-employment benefits:

- retirement and disability benefits – paid on a one-off basis, when an employee retires or is vested with the right to receive disability benefits;
- death benefits;
- cash equivalent resulting from special tariff for energy sector employees;
- in-kind benefits granted in coal or as a cash equivalent;
- benefits from the Company's Social Benefit Fund.

Jubilee bonuses are paid to employees of Group companies after a specified number of years of service.

At the end of the reporting period the present value of provisions for post-employment benefits and provisions for jubilee benefits is calculated by an independent actuary using actuarial methods. The accrued liabilities are equal to discounted future payments, including employee turnover, and pertain to the time remaining until the end of the reporting period. Demographic and staff turnover data are based on historical information.

Actuarial gains and losses on measurement of liabilities arising from post-employment benefits are recognized in whole in other comprehensive income (with the accumulated amount recognized in retained earnings), while actuarial gains and losses on jubilee bonuses are recognized in profit or loss.

Other increases and decreases in provisions are charged to operating expenses in the case of employees, to other operating expenses/revenue in the case of pensioners and individuals entitled to disability allowances and to finance costs in the portion pertaining to interest that constitutes the unwinding of discount.

In accordance with IAS 19 *Employee Benefits* the Group also recognizes provisions for termination benefits under voluntary redundancy schemes. The benefits are measured based on the expected number of employees willing to accept the employment termination offer and the estimated benefit amount.

9.20. Provisions for dismantling fixed assets and restoration of land — Note 34

Provision for mine decommissioning costs

The provision for costs of dismantling fixed assets and restoration of land includes mainly the provision for costs of decommissioning mines for which it is required that the assets be removed and the land restored to its original condition.

The provision is determined based on future decommissioning costs and costs of land restoration estimated by independent experts taking into account the discounting effect and the amount determined in line with separate regulations of the Mine Decommissioning Fund. The provision is estimated based on an analysis prepared using deposit exploitation projections (for mines) and a technical and business analysis.

For coal mines a corresponding entry is made in line with IAS 16 *Property, plant and equipment* as a fixed asset item of a mine and changes in estimates are disclosed in line with IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*, i.e. as adjustments to the provision and capitalized future mine decommissioning costs. The related accounting policy has been presented in Note 9.2. The unwinding of discount is recognized in profit or loss.

Provision for restoration of land and dismantling and removal of fixed assets

Based on estimates of future costs of dismantling prepared by independent experts, taking into account the discounting effect, the Group establishes a provision for estimated costs of dismantling, to include those related to wind farms, but also for removing fixed assets and restoring the land where the fixed assets were located if it has an obligation arising from the acquisition or use of property, plant and equipment items.

9.21. Provision for liabilities due to energy certificates and gas emission

9.21.1. Provision for the obligation to surrender energy certificates — Note 35.2

Pursuant to the Energy Law and regulations of the Minister of Economy energy companies trading in and selling electricity to end buyers are obliged to acquire property rights resulting from energy certificates and to surrender them or to pay a substitution fee. If in a given financial year the volume share of electricity specified in the energy certificates in the total annual sales of electricity to end buyers complies with limits provided for in regulations of the Minister of Economy – it is considered that the obligation has been satisfied.

At the end of each reporting period the Group recognizes a provision for costs of surrendering energy certificates or paying the substitution fee so as to fulfil the obligation.

The provision for the obligation to surrender energy certificates is recognized:

- in the portion corresponding to energy certificates held at the end of the reporting period – at the value of certificates held (the accounting policy applicable to certificates held has been presented in Note 9.4);
- in the portion not covered by energy certificates held at the end of the reporting period – first, at the amount resulting from futures and forwards for the purchase of certificates with the intention to fulfil the obligation for the current year; then at the market value of certificates necessary to fulfil the obligation at the end of the reporting period or at the amount of the substitution fee – in accordance with the Group's intention concerning the method of fulfilling the obligation.

The provision is charged to operating expenses.

The provision is settled and the certificates are surrendered when the President of the Energy Regulatory Office redeems the certificates or when the substitution fee has been paid.

9.21.2. Provision for greenhouse gas emission liabilities — Note 35.1

The provision for liabilities arising from emission of gas covered by the emissions system is recognized only when the actual emission level in a given year exceeds the volume of emission allowances awarded to the Group free of charge, including allocation of free-of-charge emission allowances to facilities belonging to individual Generation companies. The Group companies included in the EU ETS are obliged to surrender emission allowances for each emitted ton of carbon dioxide by 30 April in the following year.

The accounting policy concerning emission allowances received and acquired has been presented in Note 9.4.

The provision is charged to operating expenses (taxes and charges) in the following amount:

- in the portion covered by allowances held at the end of the reporting period:
  - nil – for allowances received free of charge;
  - at cost – for allowances acquired;
- in the portion not covered by allowances held at the end of the reporting period:
  - first, at the amount resulting from futures and forwards for the purchase of emission allowances with the intention to fulfil the obligation for the current year;
  - then at the market value of allowances necessary to fulfil the obligation at the end of the reporting period or in the amount of a possible fine – in accordance with the intention concerning the method of fulfilling the obligation.

Emission allowances are awarded free of charge for the years 2013–2020 based on costs of investments, which is the condition for obtaining allowances.

At the surrendering date, emission allowances classified as current intangible assets are derecognized in correspondence with the provision for gas emission liabilities.

9.22. Other provisions — Note 36

Other provisions include:

- A provision for use of real estate without contract. The Group recognizes provisions for all claims filed by owners of real estate on which distribution systems and heat installations are located in amounts of probable cost of claims due to land owners until the end of the reporting period. The Group does not establish a provision for possible claims of owners of land with unregulated status, which have not been lodged. Recognition and reversal of the provision is charged to other operating revenue or other operating expenses and interest accrued is charged to finance income or finance costs.
- Other provisions relate to court cases, counterparty claims or other claims, possible fines resulting from administrative proceedings carried out by the Energy Regulatory Office and the Office of Competition and Consumer Protection and tax settlements.

9.23. Deferred income and government grants — Note 37

The Group's deferred income and government grants include mainly deferred connection fees as well as grants and subsidies received to acquire property, plant and equipment. Deferred connection fees result from transactions which fall within the scope of IFRIC 18 *Transfers of Assets from Customers* and were received before 1 July 2009. Effective from 1 July 2009, in accordance with IFRIC 18, the said connection fees are recognized within revenue from sales of services.

Grants and subsidies received to acquire property, plant and equipment are recognized at the value of cash received as other operating revenue matching the corresponding depreciation expense related to items of property, plant and equipment.

9.24. Liabilities to suppliers, capital commitments and other financial liabilities — Note 38, 39, 41

Liabilities to suppliers, capital commitments and other financial liabilities are measured at the amount due, as the effect of discounting is immaterial.

9.25. Receivables / Liabilities arising from taxes and charges — Note 28, 40

Settlements arising from taxes and charges presented in the statement of financial position comprise:

- CIT settlements;
- VAT and excise duty settlements;
- PIT and social security settlements;
- Environmental fees and other regulatory settlements.

9.26. Current and Deferred Income Tax — Note 16

Current tax

Income tax recognized in profit or loss for the period includes actual tax charge for the given reporting period for each company from the Tax Capital Group (TCG) as well as other non-TCG companies, determined in line with the provisions of the CIT Act, as well as any previous year tax adjustments.

Deferred tax

The Group recognizes a deferred tax asset and a deferred tax liability arising from temporary differences between the book value of assets and liabilities and their tax value, and a tax loss deductible in the future.

The deferred tax asset is recognized only if its realization is probable, i.e. if it is expected that a taxable profit sufficient to realize the asset will be generated in the future.

Income tax related to items which are recognized in other comprehensive income or directly in equity is recognized in other comprehensive income or in equity, respectively.

The deferred tax asset and deferred tax liability of companies from the Tax Capital Group are netted off due to the fact that the companies file combined tax returns.

9.27. Sales revenue — Note 12

Revenue is recognized at the fair value of the payment, received or due, following reduction by VAT, excise duty, other sales taxes, charges and discounts.

Revenue of the financial year includes also accrued revenue which has not been measured and billed due to the buyer settlement system used.

9.27.1. Revenue from sales of electricity distribution services in the Distribution segment

The Group's revenue from sales of services includes in particular revenue related to distribution operations and settlements of the connection fee.

Electricity distribution services are considered sold upon service provision to the client, as registered by the electricity meter, i.e.:

- for VAT invoices raised by reference to the meter reading – the reading date;
- For VAT invoices raised in a billing period exceeding one month, by reference to the forecast energy consumption – the forecast period; at present one- and two-month periods are settled based on the actual use, while six- and twelve-month periods are settled based on projections;
- For billing periods specified in contracts with buyers exceeding one month, revenue includes revenue which has not been measured and billed. The said revenue is estimated based on the average daily consumption of electricity in prior billing periods and the number of days in the analysed billing period. Additional sales are calculated using the weighted average selling price of the financial year or using prices quoted on the last issued invoice;
- Adjustments to sales revenue are recognized in the period of their identification or in the period to which they relate (only when material).

The Group recognizes revenue relating to fixed assets received free of charge due to rendering services of removing power or heat infrastructure collision in sales revenue. Moreover, since 1 July 2009, the Group has also been recognizing transactions included in the scope of IFRIC 18 *Transfer of Assets from Customers* in this item. Revenue falling within the scope of IFRIC 18 *Transfer of Assets from Customers*, relating to fixed assets received from clients free of charge and used for connecting such clients to the infrastructure and providing them with constant access to supplies of services, or revenue relating to cash received from clients for acquisition or development of the said fixed assets (connection fees) is carried at the estimated fair value or the amount of cash received and recognized as revenue from sales of services in the period when such assets are actually received from clients.

9.27.2. Revenue from sales of electricity, gas and distribution services in the Sales segment

The Group companies operating in the Sales segment generate revenue from sales of electricity and distribution services to retail and wholesale clients (balancing market sales). Revenue from sales is determined on the basis of the billed volume and price, including additional assessments.

Three types of additional assessment of revenue from sales of electricity and distribution services are made in this segment:

- Additional assessment of sales to clients, unbilled as at the end of the reporting period

  Measurement and billing systems showing the electricity volume sold to retail clients are read and invoices are issued mainly in periods not corresponding to reporting periods. Therefore, the Group companies from the Sales segment make appropriate estimates of sales at the end of each reporting period. For clients that are party to complex contracts and sales contracts, the additional assessment is made in the billing systems on the basis of the average daily consumption of electricity between the last actual reading date and the end of the reporting period.

- Additional assessment for buyers using forecast payment billing

  At the end of each reporting period, an additional assessment is made for buyers with 6- or 12-month forecast payment billing periods. It is based on the difference in the number of days between the reading date and the actual number of days in the month. It relies on electricity sales data derived from the billing system and the additional assessment ratio.

- Additional assessment of sales resulting from reconciliation of the energy balance

  The Group companies from the Sales segment reconcile the energy balance by estimating the non-balancing sales or purchase volume at the end of each reporting period. An amount increasing or reducing revenue from sales of electricity, determined as the product of the estimated non-balancing volume and the weighted average purchase price of electricity on the balancing market, is also recognised by the Group.

Revenue from sales of gas fuel and distribution services provided to retail and wholesale buyers (balancing market sales) is classified to the Sales segment. Revenue from sales is determined on the basis of the billed volume and price, including additional assessments.

Revenue from sales of gas fuel and distribution services is estimated using two methods:

- Additional assessment of sales to clients, unbilled as at the end of the reporting period

  Measurement and billing systems showing the gas volume sold to retail clients are read and invoices are issued mainly in periods not corresponding to reporting periods. Therefore, relevant estimates are performed as at the end of the reporting period. For clients who have concluded comprehensive contracts, the additional assessments regarding gas fuel sales are made in the billing systems based on daily average consumption of gas fuel in the period from the last actual reading date until the end of the reporting period. Additional assessments regarding distribution services are made as a difference between the costs of purchasing the gas fuel distribution services and billed revenue from sales of the distribution services.

- Additional assessment of sales resulting from reconciliation of the gas fuel balance

  The company reconciles the gas fuel balance by estimating the non-balancing gas fuel sales or purchase volume at the end of each reporting period. The additional assessment includes the amount increasing or reducing revenue from sales of gas fuel, calculated as the product of the estimated non-balancing volume and the monthly average reference price of high-methane gas published by Operator Gazociągów Przesyłowych GAZ-SYSTEM S.A.

9.27.3. Revenue from wholesale of electricity in the Generation segment

Wholesale of electricity from the generation units managed centrally and as part of trading operations requires the client and the supplier's notification of the volume of electricity declared per each hour to the Transmission System Operator through the centralized computerized Energy Market Information Exchange System, which volume a Generation segment company is obliged to provide under specific contracts as a supplier (sales of energy generated internally or purchased as part of trading operations) or ensure its provision (through energy purchases on the Balancing Market) and the client is obliged to accept. Both the price and volume per each hour is determined on the basis of transactions signed in advance or (in the case of the Polish Power Exchange) recorded electronically. The Transmission System Operator, which somewhat guarantees volume settlements, ensures reliability of data concerning the supplied volume of energy. As billing is based on reports generated by the Transmission System Operator, all electricity wholesale invoices are raised following electricity supply, with a clearly determined volume and value of such energy.

Sales invoices relating to electricity supplied to the Balancing Market are raised on the basis of reports from the centralized system balancing sales in the Polish National Power System. Such settlements are made every decade. The invoicing procedure, including the price setting algorithms and principles as well as the due dates, is set out in the Transmission System Operation and Maintenance Instruction approved by the President of the Energy Regulatory Office.

Wholesale of electricity from generation units which are not managed centrally (local market generation units of less than 100 MW) is subject to similar rules. However, it is the local market operator that is responsible for the settlements.

9.27.4. Revenue from sales of heat in the Generation segment

Heat is sold under heat sale / comprehensive heat supply contracts entered into with institutional clients and consumers.

Institutional clients are charged twice a month: at fixed rates for power contracted in advance and variable rates calculated regularly based on progressive readings. Meters are read between the first and the last reading date. Charges are imposed regularly, on a monthly basis. Seldom, institutional buyers are charged once a month with the total of fixed and variable charges or just with fixed charges in accordance with concluded contracts. Total of fixed and variable charges are imposed on consumers once a month, or seldom, only variable charges are imposed on consumers in accordance with concluded contracts. Variable charges are imposed periodically based on progressive readings. Meters are read between the first and the last reading date. Charges are imposed regularly, on a monthly basis.

Revenue is measured by reference to the tariff in force, the volume of power billed, heat, carrier, lease rate, excess amount and other actual consumption of products, based on rates and prices listed in the current tariffs. It includes mainly charges for contracted power, heat as well as fixed and variable transmission.

Heat is sold by reference to readings on an accrual basis. Therefore, an additional assessment of sales is made for accounting purposes from the reading date to the end of the month so as to determine the monthly sales volume from the first to the last day of the month. Additional assessments of sales are made separately for each reading point. Additional assessment for a given point includes billed sales minus an additional assessment for the previous month, plus an additional assessment for the current month.

9.27.5. Revenue from sales of coal in the Mining segment

Sales of fine coal supplied under sales contracts to power and heat and power stations of the TAURON Group represent the intra-group market for the Mining segment. Entities operating in the sales network of a company from the Mining segment, i.e. Authorized Coal Sellers and Coal Sellers, play a strategic role in coal sales. Coal is also sold under contracts with end buyers, mainly industrial customers, in intra-community supplies and under export contracts, in addition to transactions with retail sales.

Sales are made on a continuous basis in the form of railroad and truck sales, in accordance with the railroad supply schedule and truck sales advice notes. Sales are made when coal is handed over to the carrier, whether in truck or railroad transport.

Revenue from sales of coal is measured on the basis of sales values resulting from the billed volume and price. Revenue from sales of coal is adjusted, in particular, based on discounts, price reductions as well as accepted volume and quality complaints.

(in PLN '000)

9.28. Operating expenses Note 13

Operating expenses include:

- cost of goods, products, materials and services sold (cost of sales), incurred during a given reporting period, including any impairment losses on property, plant and equipment, intangible assets, receivables and inventories, adjusted by cost of manufacturing products for own purposes,
- total sales, general and administrative expenses incurred in the reporting period (disclosed separately in the statement of comprehensive income).

Costs that can be assigned directly to revenue generated by the Group impact the profit or loss for the period which the revenue pertains to.

Costs that can only be indirectly assigned to revenue or other benefits obtained by the Group impact the profit or loss in the portion pertaining to the given reporting period, and match the revenue or other economic benefits.

9.29. Foreign currency transactions translated into the presentation currency of foreign operations

Foreign currency transactions (i.e. those not made in the functional currency) are translated into the functional currency at initial recognition at the exchange rate applicable as at the transaction date.

As at the end of the reporting period monetary items are translated at the closing rate (for entities whose functional currency is PLN the closing rate is the average exchange rate published for the currency by the National Bank of Poland as at the date).

The following exchange rates have been applied for the purposes of the balance-sheet valuation:

Currency	31 December 2017	31 December 2016
USD	3.4813	4.1793
EUR	4.1709	4.4240
CZK	0.1632	0.1637

As at the end of the reporting period, exchange differences from translation and settlement are recognized through profit or loss within finance income (or cost), except for those capitalized in assets.

Individual items of the financial statements of foreign operations (TAURON Czech Energy s.r.o. and TAURON Sweden Energy AB (publ)) have been translated to the presentation currency in the following manner:

- assets and liabilities have been translated to the presentation currency at the average exchange rate published by the National Bank of Poland as at the end of the reporting period;
- revenue and expenses have been translated at the average exchange rate of the National Bank of Poland published at the transaction date or the average exchange rate for a given period, if no significant exchange rate fluctuations occurred in the period;
- exchange differences from translation have been recognized in other comprehensive income.

9.30. Statement of cash flows

The statement of cash flows is prepared in line with the indirect method.

9.31. Earnings (loss) per share

Net earnings (loss) per share for each period is calculated by dividing the net profit (loss) for a given reporting period by the weighted average number of shares existing in the reporting period.

BUSINESS SEGMENTS

10. Operating Segments

The Group presents segment information for the current and comparative reporting periods in accordance with IFRS 8 *Operating Segments*.

The Group is organized and managed by segment, in accordance with the type of products and services offered. Each segment constitutes a strategic business entity offering different products and operating on different markets.

The Group applies the same accounting policies to all operating segments. The Group accounts for transactions between segments as if they were made between unrelated parties, i.e. using current market prices.

Revenue from transactions between segments is eliminated in the consolidation process.

After elimination of costs arising from intercompany transactions, general and administrative expenses of the parent are presented under unallocated expenses. General and administrative expenses of the Parent are incurred for the benefit of the entire Group and cannot be directly attributed to a specific operating segment.

Segment assets do not include deferred tax, income tax receivables or financial assets, except for receivables from buyers and other financial receivables, assets relating to gain on measurement of commodity derivative instruments as well as cash and cash equivalents, which represent segment assets.

Segment liabilities do not include deferred tax, income tax liability or financial liabilities, except for liabilities to suppliers, capital commitments and payroll liabilities as well as liabilities relating to loss on measurement of commodity derivative instruments, which represent segment liabilities.

Financing of the Group (together with the financial expenses and revenue) and income tax is monitored at the level of the Group and they are not allocated to segments.

None of the Group's operating segments has been combined with another segment to create the reportable operating segments.

The Management Board monitors operating profit/loss of segments to make decisions concerning the allocation of resources, evaluation of the effects of the allocation and the performance. Evaluation of performance is based on EBITDA and operating profit or loss. EBITDA is defined as EBIT increased by amortization/depreciation and impairment of non-financial assets. EBIT is the profit/loss on continuing operations before tax, finance income and finance costs, i.e. operating profit (loss).

The Group's reporting format for the period from 1 January 2017 to 31 December 2017 and for the comparative period was based on the following operating segments:

Operating segments	Core business	Subsidiaries/ Entities recognized with the equity method
Mining 	*Hard coal mining*	TAURON Wydobycie S.A.
Generation   	*Generation of electricity using conventional sources, including combined heat and power generation, as well as generation of electricity using joint combustion of biomass and other energy acquired thermally. Key fuels include hard coal, biomass, coal gas and coke-oven gas* *Generation of electricity using renewable sources* *Generation, distribution and sales of heat*	TAURON Wytwarzanie S.A. TAURON Ekoenergia Sp. z o.o. TAURON Ciepło Sp. z o.o. TAURON Serwis Sp. z o.o. Marselwind Sp. z o.o. Nowe Jaworzno Grupa TAURON Sp. z o.o. *TAMEH HOLDING Sp. z o.o.** *TAMEH POLSKA Sp. z o.o.** *TAMEH Czech s.r.o.** *Elektrociepłownia Stalowa Wola S.A.**
Distribution 	*Distribution of electricity*	TAURON Dystrybucja S.A. TAURON Dystrybucja Serwis S.A. TAURON Dystrybucja Pomiary Sp. z o.o.
Sales 	*Wholesale trading in electricity, trading in emission allowances and energy certificates and sale of electricity to domestic end users or entities which further resell electricity.*	TAURON Polska Energia S.A. TAURON Sprzedaż Sp. z o.o. TAURON Sprzedaż GZE Sp. z o.o. TAURON Czech Energy s.r.o.

* *Entities recognized with the equity method.*

In addition to the key operating segments listed above, the TAURON Group also conducts operations in quarrying stone (including limestone) for the power industry, metallurgy, construction and highway engineering industry as well as in the area of production of sorbents for use in wet desulphurization installations and fluidized bed combustors (Kopalnia Wapienia Czatkowice Sp. z o.o.). The operations of TAURON Obsługa Klienta Sp. z o.o., TAURON Sweden Energy AB (publ), Biomasa Grupa TAURON Sp. z o.o., Wsparcie Grupa TAURON Sp. z o.o. and Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. are also treated as other operations of the Group.

(in PLN '000)

10.1. Operating Segments

Year ended 31 December 2017

	Mining	Generation	Distribution	Sales	Other	Unallocated items / Eliminations	Total
Revenue							
Sales to external customers	719 373	1 825 644	3 271 933	11 506 781	92 298	–	**17 416 029**
Inter-segment sales	822 052	2 702 836	3 448 010	2 061 106	712 262	(9 746 266)	**–**
Segment revenue	**1 541 425**	**4 528 480**	**6 719 943**	**13 567 887**	**804 560**	**(9 746 266)**	**17 416 029**
Profit/(loss) of the segment	**(211 070)**	**16 595**	**1 210 925**	**832 216**	**35 902**	**801**	**1 885 369**
Unallocated expenses	–	–	–	–	–	(79 098)	**(79 098)**
EBIT	**(211 070)**	**16 595**	**1 210 925**	**832 216**	**35 902**	**(78 297)**	**1 806 271**
Share in profit/(loss) of joint ventures	–	73 050	–	–	–	–	**73 050**
Net finance income (costs)	–	–	–	–	–	(121 669)	**(121 669)**
Profit/(loss) before income tax	**(211 070)**	**89 645**	**1 210 925**	**832 216**	**35 902**	**(199 966)**	**1 757 652**
Income tax expense	–	–	–	–	–	(374 706)	**(374 706)**
Net profit/(loss) for the year	**(211 070)**	**89 645**	**1 210 925**	**832 216**	**35 902**	**(574 672)**	**1 382 946**
Assets and liabilities							
Segment assets	2 085 538	11 303 257	17 409 160	3 041 966	508 825	–	**34 348 746**
Investments in joint ventures	–	499 204	–	–	–	–	**499 204**
Unallocated assets	–	–	–	–	–	944 071	**944 071**
Total assets	**2 085 538**	**11 802 461**	**17 409 160**	**3 041 966**	**508 825**	**944 071**	**35 792 021**
Segment liabilities	849 728	1 858 246	2 339 080	1 362 750	386 693	–	**6 796 497**
Unallocated liabilities	–	–	–	–	–	10 927 711	**10 927 711**
Total liabilities	**849 728**	**1 858 246**	**2 339 080**	**1 362 750**	**386 693**	**10 927 711**	**17 724 208**
EBIT	**(211 070)**	**16 595**	**1 210 925**	**832 216**	**35 902**	**(78 297)**	**1 806 271**
Depreciation/amortization	**(128 036)**	**(401 246)**	**(1 073 621)**	**(8 494)**	**(82 071)**	**–**	**(1 693 468)**
Impairment	**2**	**(46 133)**	**1 861**	**(512)**	**(70)**	**–**	**(44 852)**
EBITDA	**(83 036)**	**463 974**	**2 282 685**	**841 222**	**118 043**	**(78 297)**	**3 544 591**
Other segment information							
Capital expenditure*	165 978	1 516 492	1 693 016	751	97 911	–	**3 474 148**

** Capital expenditure includes expenditures for property, plant and equipment and intangible assets, excluding acquisition of greenhouse gas emission allowances and energy certificates.*

Year ended 31 December 2016

	Mining	Generation	Distribution	Sales	Other	Unallocated items / Eliminations	Total
Revenue							
Sales to external customers	492 231	2 457 280	3 100 495	11 513 348	83 135	–	**17 646 489**
Inter-segment sales	818 912	1 898 821	3 209 721	2 502 842	744 793	(9 175 089)	**–**
Segment revenue	**1 311 143**	**4 356 101**	**6 310 216**	**14 016 190**	**827 928**	**(9 175 089)**	**17 646 489**
Profit/(loss) of the segment	**(205 163)**	**(752 813)**	**1 363 236**	**479 374**	**42 642**	**(20 472)**	**906 804**
Unallocated expenses	–	–	–	–	–	(105 282)	**(105 282)**
EBIT	**(205 163)**	**(752 813)**	**1 363 236**	**479 374**	**42 642**	**(125 754)**	**801 522**
Share in profit/(loss) of joint ventures	–	60 040	–	–	–	–	**60 040**
Net finance income (costs)	–	–	–	–	–	(352 701)	**(352 701)**
Profit/(loss) before income tax	**(205 163)**	**(692 773)**	**1 363 236**	**479 374**	**42 642**	**(478 455)**	**508 861**
Income tax expense	–	–	–	–	–	(138 724)	**(138 724)**
Net profit/(loss) for the year	**(205 163)**	**(692 773)**	**1 363 236**	**479 374**	**42 642**	**(617 179)**	**370 137**
Assets and liabilities							
Segment assets	2 069 263	10 412 940	16 761 938	2 659 458	468 202	–	**32 371 801**
Investments in joint ventures	–	461 348	–	–	–	–	**461 348**
Unallocated assets	–	–	–	–	–	623 745	**623 745**
Total assets	**2 069 263**	**10 874 288**	**16 761 938**	**2 659 458**	**468 202**	**623 745**	**33 456 894**
Segment liabilities	829 974	1 936 334	2 162 907	1 660 156	288 365	–	**6 877 736**
Unallocated liabilities	–	–	–	–	–	9 899 840	**9 899 840**
Total liabilities	**829 974**	**1 936 334**	**2 162 907**	**1 660 156**	**288 365**	**9 899 840**	**16 777 576**
EBIT	**(205 163)**	**(752 813)**	**1 363 236**	**479 374**	**42 642**	**(125 754)**	**801 522**
Depreciation/amortization	**(123 031)**	**(425 742)**	**(1 037 789)**	**(10 631)**	**(71 533)**	**–**	**(1 668 726)**
Impairment	**(2)**	**(872 382)**	**6 213**	**–**	**(395)**	**–**	**(866 566)**
EBITDA	**(82 130)**	**545 311**	**2 394 812**	**490 005**	**114 570**	**(125 754)**	**3 336 814**
Other segment information							
Capital expenditure*	283 169	1 661 215	1 806 054	1 452	64 921	–	**3 816 811**

** Capital expenditure includes expenditures for property, plant and equipment and intangible assets, excluding acquisition of greenhouse gas emission allowances and energy certificates.*

(in PLN '000)

In the years ended 31 December 2017 and 31 December 2016 the Group did not identify individual customers that would generate sales revenue in excess of 10% of total sales revenue of the TAURON Group.

10.2. Geographical areas of operations

The majority of the Group's business operations is carried out in Poland. The table below presents export sales classified by countries.

	Year ended 31 December 2017	Year ended 31 December 2016
Czech Republic	206 434	169 983
Belgium	–	33 699
Slovakia	27 210	1 728
UK	14 279	19 232
Luxembourg	6 412	655
Hungary	1 602	338
Other	939	7 289
Total	**256 876**	**232 924**

Sales to foreign buyers are mainly sale of electricity, which accounted for 97% and 99% of revenue from foreign buyers in the financial years ended 31 December 2017 and 31 December 2016, respectively.

(in PLN '000)

IMPAIRMENT OF NON-FINANCIAL ASSETS

11. Impairment of Non-Financial Assets

11.1. Impairment of property, plant and equipment

In the year ended 31 December 2017, the Group recognized and reversed previously recognised impairment losses on property, plant and equipment as a result of impairment tests performed as at 31 December 2017 and 30 June 2017.

The recoverable amount of the above group of assets corresponds to their value in use. The impairment losses were charged to the cost of sales.

The impairment loss and its reversal as a result from the tests performed in the year ended 31 December 2017 are related to the following cash generating units:

CGU	Company	Discount rate (before tax) assumed in tests as at:			Recoverable amount	Impairment loss recognized	Impairment loss derecognized
		31 December 2017	30 June 2017 *(unaudited)*	31 December 2016	As at 31 December 2017	Year ended 31 December 2017	
Elektrownia Jaworzno II	TAURON Wytwarzanie S.A.	8.39%	8.20%	7.78%	105 454	118 469	–
Elektrownia Jaworzno III					894 229	136 307	85 672
Elektrownia Łaziska					466 037	–	177 229
Elektrownia Łagisza					1 384 014	35 762	178 213
Elektrownia Siersza					69 361	133 211	–
Elektrownia Stalowa Wola					(34 348)	530	–
Capital projects in progress					–	211	–
ZW Bielsko Biała	TAURON Ciepło Sp. z o.o.	7.58%	7.42%	7.63%	531 540	22 490	27 543
ZW Tychy					469 264	37 309	23 628
Hydropower plants	TAURON Ekoenergia Sp. z o.o.	8.64%	8.55%	8.44%	501 188	62 875	40 638
Wind farms		9.54%	7.67% – 9.08%	6.71% – 7.91%	401 128	111 271	95 291
Total CGU						**658 435**	**628 214**
Common assets	TAURON Wytwarzanie S.A.	8.39%	8.20%	7.78%	(8 834)	294	–
Total impairment losses						**658 729**	**628 214**

As at 31 December 2017, impairment tests were performed for property, plant and equipment based on the following indications:

- the market value of the Company's net assets remaining below their carrying amount for a long period;
- global commodity prices and the local power coal market changing following the consolidation in the mining sector;
- amendments to the Act on Renewable Energy Sources and publication of related obligations for the years 2018 and 2019 which affected the prices of renewable energy certificates;
- Act on the capacity market passed and discussion of the functional solutions set out in the proposed capacity market regulations;
- persisting unfavourable market conditions for the conventional power industry;
- an increase in the risk-free rate.

The tests conducted as at 31 December 2017 and 30 June 2017 required estimating the value in use of cash generating units, based on their future cash flows discounted subsequently to the present value using a discount rate.

The impairment tests for property, plant and equipment and intangible assets (non-current assets) were carried out at the level of individual companies, except for:

- TAURON Wytwarzanie S.A., where cash-generating units ("CGU") were identified based on the cost nature and analysis of the applied methods of contracting and allocating generation from particular generation units. Consequently, the test was performed for CGUs understood as generation units or groups of generation units;
- TAURON Ekoenergia Sp. z o.o., where water power plants and wind farms were individually tested for impairment as at 30 June 2017. The test as at 31 December 2017 was carried out with respect to generation of electricity

in water power plants and on shared, integrated CGU for wind farms. Recognition of the shared CGU for wind farms is related to the change in regulations regarding the loss of supplier obliged to wind farms as of 1 January 2018, as well as the change in the approach to contracting energy generated from wind farms, including the total settlement on the balancing market. In connection with the above, in the area of electricity generation from wind sources there has been a change in the scope of the functioning, operation and management of these assets.

- TAURON Ciepło Sp. z o.o., where generation of heat and electricity was separated from transmission and distribution of heat. Additional tests for "generation" activity were carried out for individual generation units.

Key assumptions made for purposes of tests performed as at 31 December 2017:

- There was adopted the price path for power coal, other coal sizes and gaseous fuels. It has been assumed that in the years 2018–2020 the prices of power coal will remain at a similar level to that obtained in current contracts. Next in the years 2021–2040 a real depreciation of 8% is expected with the prices remaining at the 2040 levels (constant);
- There was adopted the electricity wholesale price path for the years 2018–2027 with the perspective by 2040, taking into account such factors as the effect of the balance of the market supply and demand for electricity, costs of fuel as well as costs of acquiring greenhouse gas emission allowances. An increase of ca. 3% is assumed by 2020 comparing to the year 2017, with a 13% growth rate by 2027 (vs. 2020), an increase of 10% between 2027 and 2040 and 2040 year prices thereafter (constant);
- The operating reserve capacity mechanism is to remain in place until the end of 2020, i.e. until the capacity market will have been implemented;
- Planned changes in the Polish market model aimed to introduce the capacity market mechanism have been taken into account (in line with the adopted and notified Capacity Market Act and the draft capacity market regulations). It has been assumed that capacity-related payments will begin as of 2021 and that they will be made until 2035. Auctions will take the form of a single basket solution, broken down by the length of the capacity contract depending on the level of capital expenditure (new, modernized and existing units). The average annual capacity market budget is assumed at ca. PLN 4 billion throughout the period when the mechanism is applied;
- There were adopted the greenhouse gas emission limits for heat generation in line with the regulation of the Council of Ministers, which was adjusted by level of operations, i.e. generation of heat;
- There was adopted the greenhouse emission allowance price path for the years 2018–2027 with the perspective by 2040. It has been assumed that the market price will increase by ca. 173% by 2027 comparing to the year 2017, followed by a rise of ca. 22% between 2027 and 2040, with 2040 year price level thereafter (constant);
- There were taken into consideration green, red and yellow energy production volumes depending on the production capacity, along with the price path for individual energy certificates;
- Limited support periods for green energy have been assumed in accordance with the Act on Renewable Energy Sources, which provides for new support mechanisms for renewable energy. The support period has been limited to 15 years as from the date of the first supply of electricity qualifying for an energy certificate to the distribution network;
- There was adopted the support for CHP in line with the regulations which are currently in force. It is assumed that property rights exist for red, yellow and purple energy and that they will have to be surrendered by 2018. No support for CHP has been assumed thereafter;
- It was assumed, that regulated revenue generated by distribution companies, ensures coverage of reasonable costs and a reasonable level of return on capital. The return on capital is conditional on the Regulatory Asset Value;
- There was adopted the electricity retail price path based on the wholesale price of black energy, taking into account the costs of excise duty, the obligation to cancel energy certificates as well as an appropriate level of margin;
- There was adopted the sales volumes taking into account GDP growth and increased market competition;
- It was assumed, that tariff revenue generated by heat companies, ensures coverage of reasonable costs and a reasonable level of return on capital;
- Maintaining the production capacity of the existing non-current assets as a result of replacement investments;

- There was taken into consideration the level of the weighted average cost of capital (WACC) during the projection period, as used in the calculations, ranges from 7.05% to 10.20% in nominal terms before tax, taking into account the risk-free rate corresponding to the yield of 10-year treasury bonds (at 3.85%) and the risk premium for the energy sector (6%). The growth rate used to extrapolate cash flow projections that go beyond the detailed planning period was adopted at 2.5% and corresponds to the assumed long-term inflation rate. The level of WACC as at 31 December 2017 increased compared to the level as at 31 December 2016, mainly due to the increase in the risk-free rate and the increase in the cost of debt.

A sensitivity analysis performed for each CGU revealed that the value in use of the tested assets was mainly affected by the issue of the capacity market, with other market conditions remaining unchanged, followed by changes in electricity prices and hard coal prices. The impact of changes in the prices of greenhouse gas emission allowances and in the weighted average cost of capital on measurement is less considerable. The estimated changes in impairment losses on Generation assets, considering also the effect of their reversal as at 31 December 2017 as a result of changes in the key assumptions, have been presented below.

If the capacity market mechanism was disregarded in the process of estimation of the value in use of property, plant and equipment, with other market conditions remaining unchanged and internal trading strategy, an additional net loss of ca. PLN 3 961 million would be recognized in the Group's profit/loss.

Parameter	Change	Net impact on impairment loss (in PLN million)	
		Increase of impairment loss (net)	Decrease of impairment loss (net)
Change of electricity prices in the forecast period	+1%	–	245
	-1%	334	–
Change of coal prices in the forecast period	+1%	132	–
	-1%	–	132
Change of gas emission allowances prices in the forecast period	+1%	63	–
	-1%	–	63
Change of WACC (net)	+0.1 p.p.	64	–
	-0.1 p.p.	–	64
Change of the rate on capacity market for 1MW	+1%	–	35
	-1%	35	–
Lack of recognition of payments relating to the Capacity Market		3 961	–

11.2. Impairment of goodwill

The test was performed for the net assets increased by goodwill in each operating segment. The recoverable amount in each company was determined based on the value in use.

The test was performed based on the present value of projected cash flows from operations. The calculations were based on detailed projections for the period from 2018 to 2027 and the estimated residual value. For the Mining segment detailed projections by the date of depletion of the available coal resources were used. Reliance on projections covering a period longer than 5 years results mainly from the fact that investment processes in the power industry are time-consuming. The macroeconomic and sector assumptions serving as the basis for projections are updated as frequently as any indications for their modification are observed on the market. Projections also take into account changes in the regulatory environment known as at the date of the test.

The values determined reflect the past experience and are consistent with information from external sources.

There was taken into calculations the level of the weighted average cost of capital (WACC), which ranged in the projection period between 7.05% – 10.20% in nominal terms before tax having regard the risk free rate determined by reference to the yield on 10-year treasury bonds (3.85%) and the risk premium for operations appropriate for the power industry (6%). The growth rate used for extrapolation of projected cash flows beyond the detailed planning period is at 2.5% and it corresponds to the estimated long-term inflation rate. The level of WACC as at 31 December 2017 increased compared to the level as at 31 December 2016, mainly due to increase in the risk free rate and the increase in the cost of debt.

(in PLN '000)

Impairment test for the carrying amount of goodwill as at 31 December 2017

The key assumptions affecting the estimated value in use and the discount rates applied to individual segments are as follows:

Goodwill in the segment	Key assumptions	Discount rate (before tax) assumed in tests as at:	
		31 December 2017	31 December 2016
Mining	• The adopted price path for power coal and other coal sizes. It has been assumed that in the years 2018–2020 the prices of power coal will remain at a similar level to that obtained in current contracts. Next in the years 2021–2040 a real depreciation of 8% is expected with the prices remaining at the 2040 levels (fixed); • The adopted electricity retail price path based on the wholesale price of black energy, taking into account the costs of excise duty, the obligation to cancel energy certificates as well as an appropriate level of margin; • Maintaining the production capacity of the existing non-current assets as a result of replacement investments.	10.20%	6.95%
Distribution	• Regulated revenue generated by distribution companies, ensuring coverage of reasonable costs and a reasonable level of return on capital. The return level depends on the so-called Regulatory Value of Assets; • Maintaining generation capacity of the existing non-current assets as a result of replacement investments.	7.61%	6.39%

The assumptions were also used to estimate the value in use of other intangible assets.

The impairment test performed as at 31 December 2017 did not reveal impairment of the carrying amount of goodwill in the segments.

A sensitivity analysis performed for each CGU revealed that changes in the key factors, such as electricity prices, hard coal prices, greenhouse gas emission allowances and weighted average costs of capital would have to be material to change the value in use of the tested assets to the extent necessary to recognize impairment losses on goodwill.

(in PLN '000)

NOTES TO THE CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

12. Sales Revenue

	Year ended 31 December 2017	Year ended 31 December 2016
Sale of goods for resale, finished goods and materials without elimination of excise	**10 950 803**	**11 575 033**
Excise	(415 318)	(395 601)
Sale of goods for resale, finished goods and materials	**10 535 485**	**11 179 432**
Electricity	8 795 256	9 521 948
Heat energy	661 038	650 625
Energy certificates	54 700	127 791
Coal	662 305	467 962
Gas	182 636	230 466
Other goods for resale, finished goods and materials	179 550	180 640
Rendering of services	**6 819 034**	**6 409 430**
Distribution and trade services	6 467 258	6 051 410
Connection fees	110 948	102 657
Maintenance of road lighting	115 265	116 463
Other services	125 563	138 900
Other revenue	**61 510**	**57 627**
Total	**17 416 029**	**17 646 489**

Additional assessment of the revenue from sale of electricity and distribution services in the Sales segment

As at 31 December 2017, additionally assessed revenue from sale of electricity and distribution services in the Sales segment totalled PLN 456 972 thousand and, when reversed estimations from the prior year have been accounted for, the impact on the profit or loss for the period was PLN 58 566 thousand.

Additional assessment of the revenue from the sale of electricity and distribution services has been discussed in Note 9.27 of these consolidated financial statements.

13. Cost of Goods, Products, Materials and Services Sold (Cost of Sales)

13.1. Costs by type

	Year ended 31 December 2017	Year ended 31 December 2016
Depreciation of property, plant and equipment and amortization of intangible assets	(1 693 468)	(1 668 726)
Impairment of property, plant and equipment and intangible assets	(45 604)	(867 109)
Materials and energy	(1 392 788)	(1 316 274)
Maitenance and repair services	(251 572)	(265 300)
Distribution services	(2 084 153)	(1 771 651)
Other external services	(900 361)	(759 687)
Cost of obligation to remit the emission allowances	(326 255)	(381 883)
Other taxes and charges	(731 278)	(667 415)
Employee benefits expense	(2 805 162)	(2 613 984)
Allowance for doubtful debts	(25 170)	(22 943)
Other	(98 708)	(106 892)
Total costs by type	**(10 354 519)**	**(10 441 864)**
Change in inventories, prepayments, accruals and deferred income	(102 890)	61 655
Cost of goods produced for internal purposes	488 649	471 286
Selling and distribution expenses	491 629	459 191
Administrative expenses	610 365	652 827
Cost of goods for resale and materials sold	(5 636 919)	(6 920 557)
Cost of sales	**(14 503 685)**	**(15 717 462)**

(in PLN '000)

13.2. Costs of employee benefits

	Year ended 31 December 2017	Year ended 31 December 2016
Wages and salaries	(2 092 398)	(2 036 168)
Social security costs	(407 702)	(399 157)
Jubilee bonuses	(28 932)	84 473
Social Fund	(51 160)	(57 881)
Post-employment benefit expenses, of which:	(93 543)	(85 478)
Provision for retirement, disability and similar benefits	(29 622)	5 368
Coal allowances and special electricity rates and charges	(10 202)	(13 665)
Social Benefits Fund	(6 562)	(9 754)
Contributions to employee retirement plans	(47 157)	(67 427)
Voluntary termination scheme	(22 798)	(20 866)
Other employee benefit expenses	(108 629)	(98 907)
Total	**(2 805 162)**	**(2 613 984)**
Items included in cost of sales	(1 880 817)	(1 687 692)
Items included in selling and distribution expenses	(210 428)	(203 799)
Movement in stock of finished goods	(113 366)	(89 010)
Items included in administrative expenses	(399 783)	(403 571)
Items included in cost of goods produced for internal purposes	(200 768)	(229 912)

The costs of jubilee benefits and provisions for retirement, disability and similar benefits went up versus comparative period mainly as a result of recognition of past service costs resulting primarily from changes in the Company's Labour Agreements in that period. This reduced the costs of jubilee benefits of PLN 84 487 thousand and the costs of provisions for retirement, disability and similar benefits of PLN 20 470 thousand.

The change in provisions for post-employment benefits and for jubilee bonuses has been discussed in more detail in Note 33.1 to these consolidated financial statements.

(in PLN '000)

13.3. Depreciation and amortization charges and impairment losses

	Year ended 31 December 2017	Year ended 31 December 2016
Items included in cost of sales	**(1 650 147)**	**(2 409 461)**
Depreciation of property, plant and equipment	(1 558 790)	(1 532 717)
Impairment of property, plant and equipment	(30 546)	(757 974)
Amortization of intangible assets	(49 144)	(43 487)
Impairment of intangible assets	(10 311)	(22 215)
Impairment of goodwill	–	(51 903)
Other	(1 356)	(1 165)
Items included in selling and distribution expenses	**(35 712)**	**(33 318)**
Depreciation of property, plant and equipment	(16 694)	(17 639)
Amortization of intangible assets	(18 506)	(15 679)
Other	(512)	–
Items included in administrative expenses	**(39 440)**	**(75 640)**
Depreciation of property, plant and equipment	(21 713)	(27 868)
Impairment of property, plant and equipment	802	(33 245)
Amortization of intangible assets	(13 819)	(14 308)
Impairment of intangible assets	(8)	(219)
Other	(4 702)	–
Items included in cost of goods produced for internal purposes	**(13 773)**	**(17 416)**
Depreciation of property, plant and equipment	(13 246)	(16 751)
Impairment of property, plant and equipment	1 155	(388)
Amortization of intangible assets	(1 556)	(277)
Impairment of intangible assets	(126)	–
Total	**(1 739 072)**	**(2 535 835)**
Depreciation and amortization	(1 693 468)	(1 668 726)
Impairment	(45 604)	(867 109)

In the year ended 31 December 2017, the Group recognized impairment losses on property, plant and equipment, in addition to reversing in part the impairment losses recognized before in the Generation segment, which was due to impairment tests performed as at 31 December 2017 and 30 June 2017. The total effect on the Group's accounting profit for 2017 was PLN 30 515 thousand (excess of recognition over reversal). The tests and their results have been discussed in more detail in Note 11 to these consolidated financial statements.

Additionally, in the year ended 31 December 2017 the Group's companies recognized and reversed impairment losses on individual assets and non-current assets classified as held for sale which resulted in the Group's operating expenses being charged with PLN 15 089 thousand.

Review of the estimated useful lives

A review of the estimated useful lives of fixed assets and intangible assets, conducted in 2017, had a material effect on the amortization and depreciation expense in the following operating segments:

Increase/(decrease) in depreciation and amortization costs	Year ended 31 December 2017	Year ended 31 December 2016
Mining	(1 312)	(13 286)
Generation	241	520
Distribution	(13 000)	(25 900)

(in PLN '000)

14. Other Operating Revenue and Expenses

	Year ended 31 December 2017	Year ended 31 December 2016
Penalties, fines, compensations received or receivable	27 161	48 256
Surplus of (recognition)/reversal of actuarial provisions for the existing pensioners and disability pensioners	(1 025)	58 528
Surplus of other provisions (recognized)/derecognized	(35 167)	(115 733)
Subsidies/grants and revenue representing the equivalent of amortization/depreciation charges	29 411	38 434
Surplus of subsidies written-off over provision created for their return	–	29 684
Loss on the disposal of property, plant and equipment / intangible assets and costs of damages to non-current assets	(9 489)	(116)
Write-off for abandoned investments and production as well as liquidated materials	(3 645)	(2 821)
Costs of court proceedings, fines and damages	(10 808)	(24 675)
Other operating income	18 477	22 208
Other operating expenses	(18 994)	(69 252)
Total	**(4 079)**	**(15 487)**

In the year ended 31 December 2017, other provisions recognized by the Group exceeded those reversed by PLN 35 167 thousand, with an increase in a provision recognized by a subsidiary from the Distribution segment for real estate tax in the amount of PLN 27 356 thousand being the most material item.

15. Finance Income and Costs

	Year ended 31 December 2017	Year ended 31 December 2016
Income and costs from financial instruments	**(61 756)**	**(252 206)**
Dividend income	9 136	5 728
Interest income	47 266	35 314
Interest costs	(209 322)	(259 564)
Commission relating to borrowings and debt securities	(19 020)	(18 767)
Gain/loss on derivative instruments	(18 042)	14 138
Foreign exchange gains/losses	127 390	(30 261)
Other	836	1 206
Other finance income and costs	**(59 913)**	**(100 495)**
Interest on employee benefits	(40 764)	(50 101)
Interest on discount of other provisions	(14 328)	(19 106)
Other	(4 821)	(31 288)
Total, including recognized in the statement of comprehensive income:	**(121 669)**	**(352 701)**
Interest expense on debt	(209 322)	(259 564)
Other finance income and costs	87 653	(93 137)

In the year ended 31 December 2017, exchange gains exceeded exchange losses by PLN 127 390 thousand. Exchange gains were mainly related to the Parent's debt in the euro, i.e. loans obtained from a subsidiary, subordinated bonds issued in December 2016 and eurobonds issued in July 2017. Exchange gains exceeded exchange losses by PLN 128 270 thousand.

(in PLN '000)

16. Income Tax

16.1. Tax expense in the statement of comprehensive income

	Year ended 31 December 2017	Year ended 31 December 2016
Current income tax	**(261 178)**	**(229 134)**
Current income tax expense	(256 713)	(223 825)
Adjustments to current income tax from previous years	(4 465)	(5 309)
Deferred tax	**(113 528)**	**90 410**
Income tax expense in profit/(loss)	**(374 706)**	**(138 724)**
Income tax expense relating to other comprehensive income	**(2 184)**	**(63 052)**

16.2. Reconciliation of the effective tax rate

	Year ended 31 December 2017	Year ended 31 December 2016
Profit before taxation	**1 757 652**	**508 861**
Tax at Poland's statutory tax rate of 19%	**(333 954)**	**(96 684)**
Adjustments to income tax from previous years	(4 465)	(5 309)
Tax effects of the following items:	(14 139)	(46 169)
Recognition of non-deductible provisions and write-downs/allowances	(19 382)	(25 072)
National Disabled Persons Rehabilitation Fund (PFRON)	(4 927)	(4 857)
Permanent differences on costs related to tangible assets	2 733	(27 426)
Impairment of goodwill	–	(9 862)
Settlement of a tax loss which was not recognized as a tax asset	–	16 595
Other tax non-deductible costs	(24 624)	(16 658)
Share in profit/loss of joint ventures	13 880	11 408
Other income not included in taxable base	18 181	9 703
Other	(22 148)	9 438
Tax at the effective rate of 21.3% (2016 - 27.3%)	**(374 706)**	**(138 724)**
Income tax (expense) in profit/(loss)	(374 706)	(138 724)

16.3. Deferred income tax

	As at 31 December 2017	As at 31 December 2016
difference between tax base and carrying amount of fixed and intangible assets	1 546 630	1 511 102
difference between tax base and carrying amount of financial assets	37 632	45 981
different timing of recognition of sales revenue for tax purposes	107 511	49 299
difference between tax base and carrying amount of energy certificates	7 964	15 766
other	47 841	44 156
Deferred tax liabilities	**1 747 578**	**1 666 304**
provisions	580 180	638 914
difference between tax base and carrying amount of fixed and intangible assets	167 531	143 403
power infrastructure received free of charge and received connection fees	46 669	51 811
difference between tax base and carrying amount of financial assets and financial liabilities	54 162	50 387
different timing of recognition of cost of sales for tax purposes	41 842	39 940
tax losses	13 386	12 758
other	18 909	19 905
Deferred tax assets	**922 679**	**957 118**
After setting off balances at the level of individual Group companies, deferred tax for the Group is presented as:		
Deferred tax asset	**46 966**	**50 382**
Deferred tax liability	**(871 865)**	**(759 568)**

As at 31 December 2017 and 31 December 2016, the deferred tax assets were set off against the deferred tax liabilities of companies from the Tax Capital Group ("TCG") due to the fact that the said companies had filed a combined tax return under the Tax Capital Group agreement for the years 2015–2017, concluded on 22 September 2014. On 30 October 2017 a decision concerning registration of another Tax Capital Group for the years 2018–2020 was issued, which has been further described in Note 40 hereto.

(in PLN '000)

Based on the forecasts prepared for the TCG, according to which taxable income will be earned in the following years, it has been concluded that there is no risk that the deferred tax asset recognized in these consolidated financial statements will not be realized.

The deferred tax assets applies mainly to the Mining segment. The tax losses in the Segment were incurred before the Company joined the Tax Capital Group, i.e. before 1 January 2015. The Company intends to carry the loss forward over five subsequent years following the validity of the Tax Capital Group.

Change in deferred tax liability

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**1 666 304**	**1 677 787**
Change in the balance:		
corresponding to profit/(loss)	82 807	(27 405)
corresponding to other comprehensive income	(1 550)	–
acquisition of ZCP Brzeszcze	–	15 239
other changes	17	683
Closing balance	**1 747 578**	**1 666 304**

Change in deferred tax asset

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**957 118**	**936 795**
Change in the balance:		
corresponding to profit/(loss)	(30 721)	63 005
corresponding to other comprehensive income	(3 734)	(63 052)
acquisition of ZCP Brzeszcze	–	18 366
other changes	16	2 004
Closing balance	**922 679**	**957 118**

17. Earnings per Share

Earnings per share (in PLN)	Year ended 31 December 2017	Year ended 31 December 2016
Basic and diluted, for profit for the year attributable to equity holders of the Parent	0.79	0.21

Presented below is information about the earnings and shares which served as the basis for calculation of the basic and diluted earnings per share presented in the statement of comprehensive income.

	Year ended 31 December 2017	Year ended 31 December 2016
Net profit for the year attributable to equity holders of the Parent	1 380 663	367 468
Number of ordinary shares	1 752 549 394	1 752 549 394

(in PLN '000)

NOTES TO THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION

18. Property, Plant and Equipment

Year ended 31 December 2017

	Land	Buildings, premises and civil engineering structures	Plant and machinery	Other	Assets under construction	Property, plant and equipment, total
COST						
Opening balance	**121 980**	**21 603 044**	**18 164 046**	**850 102**	**3 261 173**	**44 000 345**
Direct purchase	–	23	–	–	3 137 677	**3 137 700**
Borrowing costs	–	–	–	–	105 346	**105 346**
Transfer of assets under construction	1 086	1 005 444	662 139	82 815	(1 751 484)	**–**
Sale	(154)	(10 012)	(61 733)	(27 922)	–	**(99 821)**
Liquidation	(3)	(41 759)	(117 786)	(7 726)	–	**(167 274)**
Received free of charge	–	7 724	161	–	–	**7 885**
Transfers to/from assets held for sale	(30)	(14 916)	(2 394)	(15)	(11)	**(17 366)**
Overhaul expenses	–	–	–	–	66 910	**66 910**
Items generated internally	–	–	–	–	39 122	**39 122**
Cost of disassembly of wind farms and decommissioning of mines	–	32 152	1 059	–	–	**33 211**
Other movements	(99)	(735)	1 636	(2 109)	(2 645)	**(3 952)**
Foreign exchange differences from translation of foreign entities	–	–	(1)	(1)	–	**(2)**
Closing balance	**122 780**	**22 580 965**	**18 647 127**	**895 144**	**4 856 088**	**47 102 104**
ACCUMULATED DEPRECIATION						
Opening balance	**(433)**	**(7 825 966)**	**(9 268 038)**	**(517 062)**	**(33 657)**	**(17 645 156)**
Depreciation for the period	–	(796 822)	(729 235)	(84 387)	–	**(1 610 444)**
Increase of impairment	(4)	(134 345)	(355 224)	(693)	(3 495)	**(493 761)**
Decrease of impairment	30	155 913	309 848	810	22	**466 623**
Sale	–	5 660	58 996	27 292	–	**91 948**
Liquidation	–	32 724	114 214	7 568	–	**154 506**
Transfers to/from assets held for sale	–	9 536	2 101	15	–	**11 652**
Other movements	–	265	1 016	1 142	(9)	**2 414**
Closing balance	**(407)**	**(8 553 035)**	**(9 866 322)**	**(565 315)**	**(37 139)**	**(19 022 218)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**121 547**	**13 777 078**	**8 896 008**	**333 040**	**3 227 516**	**26 355 189**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**122 373**	**14 027 930**	**8 780 805**	**329 829**	**4 818 949**	**28 079 886**
of which operating segments:						
Mining	**2 774**	**785 380**	**667 412**	**16 301**	**292 435**	**1 764 302**
Generation	**41 256**	**2 322 835**	**3 753 162**	**35 962**	**3 595 630**	**9 748 845**
Distribution	**61 483**	**10 829 553**	**4 244 598**	**261 693**	**918 501**	**16 315 828**
Other segments and other operations	**16 860**	**90 162**	**115 633**	**15 873**	**12 383**	**250 911**

(in PLN '000)

Year ended 31 December 2016

	Land	Buildings, premises and civil engineering structures	Plant and machinery	Other	Assets under construction	Property, plant and equipment, total
COST						
Opening balance	**119 536**	**19 928 399**	**16 910 428**	**804 020**	**2 599 980**	**40 362 363**
Direct purchase	–	–	85	253	3 495 992	**3 496 330**
Borrowing costs	–	–	–	–	94 018	**94 018**
Transfer of assets under construction	1 409	1 587 221	1 373 628	79 288	(3 041 546)	**–**
Sale	(385)	(7 610)	(14 329)	(24 203)	(48)	**(46 575)**
Liquidation	–	(55 360)	(124 965)	(13 342)	–	**(193 667)**
Received free of charge	9	16 912	766	–	–	**17 687**
Transfers to/from assets held for sale	(43)	(11 789)	64	(2 062)	(13)	**(13 843)**
Overhaul expenses	–	–	–	–	60 685	**60 685**
Items generated internally	–	–	–	–	38 332	**38 332**
Acquisition of ZCP Brzeszcze	1 544	165 401	22 429	1 637	14 405	**205 416**
Cost of disassembly of wind farms and decommissioning of mines	–	(31 863)	(1 552)	–	–	**(33 415)**
Other movements	(90)	11 733	(2 520)	4 495	(632)	**12 986**
Foreign exchange differences from translation of foreign entities	–	–	12	16	–	**28**
Closing balance	**121 980**	**21 603 044**	**18 164 046**	**850 102**	**3 261 173**	**44 000 345**
ACCUMULATED DEPRECIATION						
Opening balance	**(466)**	**(6 692 656)**	**(8 304 965)**	**(467 731)**	**(13 728)**	**(15 479 546)**
Depreciation for the period	–	(802 997)	(712 304)	(79 674)	–	**(1 594 975)**
Increase of impairment	(30)	(540 226)	(929 441)	(3 964)	(19 958)	**(1 493 619)**
Decrease of impairment	47	156 917	546 123	835	29	**703 951**
Sale	–	3 952	12 695	22 662	–	**39 309**
Liquidation	–	47 448	121 256	13 050	–	**181 754**
Transfers to/from assets held for sale	16	2 948	(16)	657	–	**3 605**
Other movements	–	(1 352)	(1 379)	(2 890)	–	**(5 621)**
Foreign exchange differences from translation of foreign entities	–	–	(7)	(7)	–	**(14)**
Closing balance	**(433)**	**(7 825 966)**	**(9 268 038)**	**(517 062)**	**(33 657)**	**(17 645 156)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**119 070**	**13 235 743**	**8 605 463**	**336 289**	**2 586 252**	**24 882 817**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**121 547**	**13 777 078**	**8 896 008**	**333 040**	**3 227 516**	**26 355 189**
of which operating segments:						
Mining	**2 774**	**724 056**	**612 225**	**16 706**	**341 810**	**1 697 571**
Generation	**41 303**	**2 394 113**	**3 935 303**	**37 148**	**2 252 690**	**8 660 557**
Distribution	**60 610**	**10 562 543**	**4 222 354**	**260 139**	**620 819**	**15 726 465**
Other segments and other operations	**16 860**	**96 366**	**126 126**	**19 047**	**12 197**	**270 596**

In the year ended 31 December 2017, the Group acquired property, plant and equipment of PLN 3 243 046 thousand (including capitalized borrowing costs). The major purchases were made in connection with investments in the following operating segments:

Operating segment	Year ended 31 December 2017	Year ended 31 December 2016
Distribution	1 637 114	1 717 236
Generation	1 421 493	1 560 458
Mining	153 795	282 420

The average capitalization rate of the borrowing costs in the year ended 31 December 2017 was 3.17% vs. 4.10% in the year ended 31 December 2016.

Key investment projects carried out by the Group in the financial year 2017 have been described in Section 1.5.2. of the Management Board's report on the activities of the TAURON Polska Energia S.A. for the 2017 financial year.

The carrying amounts of property, plant and equipment used under finance lease agreements have been presented in the table below:

	As at 31 December 2017	As at 31 December 2016
Buildings	21 702	34 117
Plant and machinery	32	17 226
Motor vehicles	–	406

(in PLN '000)

Recognition and reversal of impairment losses on property, plant and equipment had the following impact on operating segment performance:

	Year ended 31 December 2017				Year ended 31 December 2016			
	Generation	Distribution	Other	Total	Generation	Distribution	Other	Total
Increase of impairment	(493 181)	(569)	(11)	**(493 761)**	(1 487 766)	(5 853)	–	**(1 493 619)**
Decrease of impairrment	462 787	3 803	33	**466 623**	689 181	14 770	–	**703 951**
Total impact on the profit (loss) for the period	**(30 394)**	**3 234**	**22**	**(27 138)**	**(798 585)**	**8 917**	**–**	**(789 668)**

19. Goodwill

Operating segment	As at 31 December 2017	As at 31 December 2016
Mining	13 973	13 973
Distribution	25 602	25 602
Generation	581	581
Total	**40 156**	**40 156**

20. Energy Certificates and Gas Emission Allowances

20.1. Long-term energy certificates and gas emission allowances

Year ended 31 December 2017

	Energy certificates	Greenhouse gas emission allowances	Total
Opening balance	**110 430**	**15 830**	**126 260**
Direct purchase	87 880	198 635	**286 515**
Reclassification	(102 515)	(7 130)	**(109 645)**
Closing balance	**95 795**	**207 335**	**303 130**

Year ended 31 December 2016

	Energy certificates	Greenhouse gas emission allowances	Total
Opening balance	**232 973**	**277 867**	**510 840**
Direct purchase	110 430	15 830	**126 260**
Reclassification	(232 973)	(277 867)	**(510 840)**
Closing balance	**110 430**	**15 830**	**126 260**

20.2. Short-term energy certificates and gas emission allowances

Year ended 31 December 2017

	Energy certificates	Greenhouse gas emission allowances	Total
Opening balance	**556 501**	**423 847**	**980 348**
Direct purchase	273 404	103 611	**377 015**
Generated internally	52 350	–	**52 350**
Cancellation	(653 561)	(209 652)	**(863 213)**
Reclassification	103 073	7 130	**110 203**
Closing balance	**331 767**	**324 936**	**656 703**

Year ended 31 December 2016

	Energy certificates	Greenhouse gas emission allowances	Total
Opening balance	**652 305**	**153 083**	**805 388**
Direct purchase	283 978	318 127	**602 105**
Generated internally	102 149	–	**102 149**
Cancellation	(709 538)	(325 230)	**(1 034 768)**
Reclassification	227 607	277 867	**505 474**
Closing balance	**556 501**	**423 847**	**980 348**

(in PLN '000)

20.3. Balance of greenhouse gas emission allowances recorded in the Union Registry

Balance emission allowances	Year ended 31 December 2017	Year ended 31 December 2016
Allowances recorded at the beginning of the financial year	**19 482 951**	**23 737 448**
Allowances surrendered:		
in the installations of TAURON Wytwarzanie S.A. (previous year's emissions)	(5 864 561)	(14 736 415)
in the installations of TAURON Ciepło Sp. z o.o. (previous year's emissions)	(1 529 737)	(1 562 047)
in the installations of TAURON Wytwarzanie S.A. (current year's emissions)	–	(7 501 634)
Allocation of free-of-charge allowances	2 150 783	3 627 599
Allowances purchased on the secondary market	16 968 000	24 673 500
Allowances sold on the secondary market	(6 558 000)	(8 755 500)
Allowances recorded at the end of the financial year, of which:	**24 649 436**	**19 482 951**
Allowances intended for surrender for a given year:	(16 454 964)	(7 395 649)
in the installations of TAURON Wytwarzanie S.A.	(14 574 412)	(5 863 776)
in the installations of TAURON Ciepło Sp. z o.o.	(1 880 552)	(1 531 873)

In 2017, the TAURON Group companies obtained emission allowances free of charge under Article 10a of Directive 2009/29/EC of the European Parliament and of the Council of 23 April 2009 (the "Directive") amending Directive 2003/87/EC in the following quantity: 469 945 EUA for heat generation (based on the List of facilities covered by the National Implementation Measures, including the quantity of emission allowances for 2013–2020 – to be awarded for 2017) and greenhouse gas emission allowances subject to derogations under Article 10c of the Directive, following the settlement of capital expenditure incurred from 1 July 2015 to 30 June 2016 in the following quantity: 1 680 838 EUA (based on the List of electricity generation facilities covered by the greenhouse gas emissions trading system, including the quantity of allowances to be granted in 2017). Considering that the derogation allowances are granted between 2013 and 2020 based on capital expenditure incurred, which are a necessary condition to obtain such allowances, in September 2017 the TAURON Group once again settled its capital expenditure incurred in connection with the investment projects included in the National Investment Plan by filing financial and factual reports for the period from 1 July 2016 to 30 June 2017.

21. Other Intangible Assets

Year ended 31 December 2017

	Development expenses	Perpetual usufruct right	Software, concessions, patents, licenses and similar items	Other intangible assets	Intangible assets not made available for use	Intangible assets, total
COST						
Opening balance	**5 434**	**786 283**	**610 578**	**211 873**	**93 060**	**1 707 228**
Direct purchase	–	–	–	–	125 070	**125 070**
Transfer of intangible assets not made available for use	–	1 803	52 171	16 195	(70 169)	**–**
Sale/ Liquidation	(15)	(1 909)	(12 181)	–	–	**(14 105)**
Transfers to/from assets held for sale	–	(12 949)	–	–	–	**(12 949)**
Other movements	984	59	(6 084)	8 480	541	**3 980**
Foreign exchange differences from translation of foreign entities	–	–	(4)	–	–	**(4)**
Closing balance	**6 403**	**773 287**	**644 480**	**236 548**	**148 502**	**1 809 220**
ACCUMULATED AMORTIZATION						
Opening balance	**(5 120)**	**(25 617)**	**(387 075)**	**(64 982)**	**(7)**	**(482 801)**
Amortization for the period	(85)	–	(65 844)	(17 095)	–	**(83 024)**
Increase of impairment	(177)	(9 920)	(690)	(24)	–	**(10 811)**
Decrease of impairment	117	307	10	54	–	**488**
Sale/ Liquidation	15	–	11 805	–	–	**11 820**
Transfers to/from assets held for sale	–	9 859	–	–	–	**9 859**
Other movements	(15)	–	2 154	(2 814)	–	**(675)**
Foreign exchange differences from translation of foreign entities	–	–	1	–	–	**1**
Closing balance	**(5 265)**	**(25 371)**	**(439 639)**	**(84 861)**	**(7)**	**(555 143)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**314**	**760 666**	**223 503**	**146 891**	**93 053**	**1 224 427**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**1 138**	**747 916**	**204 841**	**151 687**	**148 495**	**1 254 077**

(in PLN '000)

Year ended 31 December 2016

	Development expenses	Perpetual usufruct right	Software, concessions, patents, licenses and similar items	Other intangible assets	Intangible assets not made available for use	Intangible assets, total
COST						
Opening balance	**5 690**	**786 504**	**550 892**	**188 004**	**51 885**	**1 582 975**
Direct purchase	–	–	38	–	127 408	**127 446**
Transfer of intangible assets not made available for use	–	184	63 062	22 492	(85 738)	**–**
Sale/ Liquidation	(256)	(2 438)	(4 000)	(89)	(55)	**(6 838)**
Acquisition of ZCP Brzeszcze	–	10 266	95	147	–	**10 508**
Transfers to/from assets held for sale	–	(8 728)	–	–	–	**(8 728)**
Other movements	–	495	449	1 319	(440)	**1 823**
Foreign exchange differences from translation of foreign entities	–	–	42	–	–	**42**
Closing balance	**5 434**	**786 283**	**610 578**	**211 873**	**93 060**	**1 707 228**
ACCUMULATED AMORTIZATION						
Opening balance	**(4 893)**	**(13 064)**	**(332 862)**	**(49 391)**	**–**	**(400 210)**
Amortization for the period	(159)	–	(58 046)	(15 546)	–	**(73 751)**
Increase of impairment	(403)	(23 094)	(1 359)	(138)	(7)	**(25 001)**
Decrease of impairment	79	1 773	1 619	16	–	**3 487**
Sale/Liquidation	256	–	3 920	81	–	**4 257**
Transfers to/from assets held for sale	–	8 768	–	–		**8 768**
Other movements	–	–	(312)	(4)	–	**(316)**
Foreign exchange differences from translation of foreign entities	–	–	(35)	–	–	**(35)**
Closing balance	**(5 120)**	**(25 617)**	**(387 075)**	**(64 982)**	**(7)**	**(482 801)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**797**	**773 440**	**218 030**	**138 613**	**51 885**	**1 182 765**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**314**	**760 666**	**223 503**	**146 891**	**93 053**	**1 224 427**

22. Interests in Joint Ventures

	Elektrociepłownia Stalowa Wola S.A.	TAMEH HOLDING Sp. z o.o.*	As at 31 December 2017
Non-current assets	1 219 954	1 658 016	**2 877 970**
Current assets, including:	3 830	552 456	**556 286**
cash and cash equivalents	*2 673*	*197 401*	***200 074***
Non-current liabilities (-) including:	(538 278)	(670 240)	**(1 208 518)**
debt	*(488 440)*	*(588 368)*	***(1 076 808)***
Current liabilities (-) including:	(726 070)	(460 096)	**(1 186 166)**
debt	*(659 374)*	*(49 415)*	***(708 789)***
Total net assets	(40 564)	1 080 136	**1 039 572**
Share in net assets	(20 282)	540 068	**519 786**
Investment in joint ventures	**–**	**499 204**	499 204
Share in revenue of joint ventures	20	628 145	**628 165**
Share in profit/(loss) of joint ventures	**–**	**72 950**	72 950
Share in other comprehensive income of joint ventures	**–**	**(519)**	(519)

** The data presented concern the TAMEH HOLDING Sp. z o.o. Capital Group. The value of the interest held in TAMEH HOLDING Sp. z o.o. differs from the value of net assets attributable to the Group, because the cost of shares in TAMEH HOLDING Sp. z o.o. was calculated taking into account the fair value of the share contributed to the joint venture by companies from the ArcelorMittal Capital Group.*

(in PLN '000)

	Elektrociepłownia Stalowa Wola S.A.	TAMEH HOLDING Sp. z o.o.*	Elektrownia Blachownia Nowa Sp. z o.o. in liquidation	As at 31 December 2016
Non-current assets	1 126 668	1 479 845	–	**2 606 513**
Current assets, including:	5 739	501 547	37 056	**544 342**
cash and cash equivalents	*3 809*	*196 442*	*37 009*	***237 260***
Non-current liabilities (-) including:	(1 028 954)	(664 603)	–	**(1 693 557)**
debt	*(980 977)*	*(536 585)*	–	***(1 517 562)***
Current liabilities (-) including:	(132 395)	(349 101)	(97)	**(481 593)**
debt	*(65 752)*	*(1 647)*	–	***(67 399)***
Total net assets	(28 942)	967 688	36 959	**975 705**
Share in net assets	(14 471)	483 844	18 479	**487 852**
Investment in joint ventures	**–**	**442 869**	**18 479**	**461 348**
Share in revenue of joint ventures	6 675	559 624	449	**566 748**
Share in profit/(loss) of joint ventures	**–**	**60 022**	**18**	**60 040**
Share in other comprehensive income of joint ventures	**–**	**(1 040)**	**–**	**(1 040)**

* *The data presented concern the TAMEH HOLDING Sp. z o.o. Capital Group.*

Elektrociepłownia Stalowa Wola S.A.

Elektrociepłownia Stalowa Wola S.A. is a special purpose vehicle established in 2010 on the initiative of TAURON Polska Energia S.A. and PGNiG S.A. The entity was registered to carry out an investment project, i.e. construction of a gas and steam unit fuelled with natural gas in Stalowa Wola with the gross maximum electrical capacity of 400 MWe and the net heat capability of 240 MWt.

On 27 October 2016, a conditional agreement was made among the Company, PGNiG S.A. and Elektrociepłownia Stalowa Wola S.A. to set out the key boundary conditions for project restructuring along with a conditional annex to the electricity sales contract. Furthermore, PGNiG S.A. and Elektrociepłownia Stalowa Wola S.A. executed a conditional annex to the gaseous fuel supply contract.

The conditions precedent were satisfied on 31 March 2017, which was followed by the entry into force of the aforesaid agreement and annexes. The issue has been discussed in more detail in Note 34.3 hereto.

TAURON Polska Energia S.A. holds a 50% indirect interest in the issued capital of the company and in its governing body through TAURON Wytwarzanie S.A. Due to the fact that in 2015 the accumulated share in losses of the joint venture and the adjustment to "top-down" transactions between the Group companies and the joint venture exceeded the value of the interest in the joint venture, the Company discontinued to recognize its share in any further losses of the joint venture.

Additionally, the Company has receivables arising from loans extended to Elektrociepłownia Stalowa Wola S.A. with the carrying amount of PLN 570 432 thousand, which has been discussed in more detail in Note 23 to these consolidated financial statements.

TAMEH HOLDING Sp. z o.o. and subsidiaries

In 2014, the TAURON Group entered into an agreement with the ArcelorMittal Group. It is an agreement between entities holding interests in TAMEH HOLDING Sp. z o.o. which governs the investment and operational projects carried out in the industrial power sector. The duration of the agreement is 15 years and may be extended. Following the transactions concluded in 2014, each capital group holds 50% of shares in TAMEH HOLDING Sp. z o.o.

TAMEH HOLDING Sp. z o.o. holds 100% of shares in TAMEH POLSKA Sp. z o.o. composed of: Zakład Wytwarzania Nowa and Elektrownia Blachownia contributed in kind by the TAURON Group and Elektrociepłownia in Kraków contributed in kind by the ArcelorMittal Group. Moreover, TAMEH HOLDING Sp. z o.o. holds 100% of shares in TAMEH Czech s.r.o.

On 29 June 2017, the General Shareholders' Meeting of TAMEH HOLDING Sp. z o.o. decided to allocate PLN 31 000 thousand to pay dividends to the shareholders. The Group's interest in the joint venture TAMEH HOLDING Sp. z o.o. was reduced by the value of the dividend payable to the Group in the amount of PLN 15 500 thousand.

Elektrownia Blachownia Nowa Sp. z o.o. in liquidation

On 5 September 2012, TAURON Wytwarzanie S.A., a subsidiary, and KGHM Polska Miedź S.A. established a special purpose vehicle, Elektrownia Blachownia Nowa Sp. z o.o. The company was set up to perform a comprehensive investment project including preparation, construction and operation of a gas and steam unit with the capacity of ca. 850 MWe on the site of TAURON Wytwarzanie S.A. – Oddział Elektrownia Blachownia.

(in PLN '000)

On 28 July 2016, TAURON Polska Energia S.A., KGHM Polska Miedź S.A. and TAURON Wytwarzanie S.A. signed an agreement pursuant to which they unanimously decided to discontinue the construction of the gas and steam unit in Elektrownia Blachownia Nowa Sp. z o.o. and terminate the shareholders agreement concluded by KGHM Polska Miedź S.A. and TAURON Wytwarzanie S.A. On 11 October 2016, the Extraordinary General Shareholders' Meeting dissolved Elektrownia Blachownia Nowa Sp. z o.o. and placed it into liquidation, in addition to appointing a receiver. The measures employed in connection with the liquidation included completion of sales of the company's assets by the end of the reporting period, document archiving and termination of the contracts which the company was party to. On 7 July 2017, the proceeds from distribution of the assets of Elektrownia Blachownia Nowa Sp. z o.o. in liquidation, amounting to PLN 18 542 thousand, were transferred to the bank account of TAURON Wytwarzanie S.A. After the balance sheet date, in January 2018, there was filed with the district court an application to delete the company from register of entrepreneurs.

23. Loans to joint ventures

Loans to the joint venture Elektrociepłownia Stalowa Wola S.A. as at 31 December 2017 and 31 December 2016:

	Agreement date	Loan amount	As at 31 December 2017		Maturity date	Interest rate	Purpose
			Principal	Interest			
Subordinated loan	20.06.2012	177 000	177 000	35 052	31.12.2032	floating/ WIBOR 3M+mark-up	Project performance: the borrower to obtain external funding
Loan for repayment of debt	14.12.2015	15 850	15 850	1 370	31.12.2027	floating/ WIBOR 3M+mark-up	Repayment of the principal instalment with interest with regard to loans granted to the borrower by European Investment Bank, European Bank for Reconstruction and Development and Bank Polska Kasa Opieki S.A.
	15.12.2016	15 300	11 000	495		floating/ WIBOR 6M+mark-up	
Arrangements to consolidate the borrower's debt	30.06.2017	150 000	150 000	3 259	28.02.2018	floating/ WIBOR 6M+mark-up	Payment of total liabilities under loan agreements entered into by the borrower with the European Investment Bank, the European Bank for Reconstruction and Development and Bank Polska Kasa Opieki S.A. and financing of current operations
	31.10.2017	175 157	175 157	1 249			
Total			**529 007**	**41 425**			
Non-current			203 850	36 917			
Current			325 157	4 508			

	Agreement date	Loan amount	As at 31 December 2016		Maturity date	Interest rate	Purpose
			Principal	Interest			
Subordinated loan	20.06.2012	177 000	177 000	36 381	31.12.2032	floating/ WIBOR 3M+mark-up	Project performance: the borrower to obtain external funding
Loan for repayment of debt	14.12.2015	15 850	15 850	699	31.12.2027	floating/ WIBOR 3M+mark-up	Repayment of the principal instalment with interest with regard to loans granted to the borrower by European Investment Bank, European Bank for Reconstruction and Development and Bank Polska Kasa Opieki S.A.
	15.12.2016	15 300	11 000	21		floating/ WIBOR 6M+mark-up	
Other loans	25.11.2015	2 600	2 600	117	30.06.2017	floating/ WIBOR 6M+mark-up	Financing of current operations
	22.01.2016	5 500	5 500	214		floating/ WIBOR 1M+mark-up	
	22.04.2016	1 200	600	17			
	27.05.2016	3 100	3 100	65			
	31.08.2016	3 800	2 875	28			
Total			**218 525**	**37 542**			
Non-current			203 850	37 101			
Current			14 675	441			

Loans granted by the Company to Elektrociepłownia Stalowa Wola S.A. under agreements dated 30 March 2017 for the purpose of debt repayment totalled PLN 290 742 thousand. With the loans the debtor will be able to make an early payment of liabilities under loan agreements entered into in relation to the construction of a heat and power unit in Stalowa Wola, which has been discussed in more detail in Note 34.3 to these financial statements.

Under agreements concluded on 16 February 2017 and 28 April 2017, the Company extended other loans totalling PLN 5 250 thousand to Elektrociepłownia Stalowa Wola S.A. to finance the current operations of the borrower.

On 30 June 2017, the Company concluded two agreements with Elektrociepłownia Stalowa Wola S.A. consolidating debt under loan agreements entered into for the purpose of refinancing debt totalling PLN 290 742 thousand and other loans for the total amount of PLN 19 925 thousand. Under the debt consolidation agreements, principal amounts and interest accrued by 30 June 2017 were consolidated and comprised:

- The total outstanding principal amount of PLN 145 991 thousand under the refinancing loan agreement dated 30 March 2017 and a portion of the principal amount of PLN 4 009 thousand under the refinancing loan agreement dated 30 March 2017 for PLN 73 518 thousand were included in the debt consolidation agreement of 30 June 2017 for the total amount of PLN 150 000 thousand.
- The debt consolidation agreement dated 30 June 2017 for PLN 170 058 thousand covered:
  - the remaining portion of the principal amount of PLN 69 509 thousand under the refinancing loan agreement dated 30 March 2017 for PLN 73 518 thousand;
  - the total principal amount under the refinancing loan agreement dated 30 March 2017 of PLN 71 233 thousand;
  - the total principal amount under other loan agreements concluded to finance current business operations of the borrower totalling PLN 19 925 thousand;
  - interest accrued on loans granted and included in debt consolidation agreements, calculated for the period from the loan agreement date to 30 June 2017 totalling PLN 3 841 thousand;
  - an additional loan granted to the borrower by the Company under the debt consolidation agreement of PLN 5 550 thousand. The purpose of the loan was in particular to finance current business operations of the borrower.

On 31 October 2017, the Company and Elektrociepłownia Stalowa Wola S.A. signed:

- A new consolidation arrangement totalling PLN 175 157 thousand, effective as of 1 November 2017, whereby the debt of Elektrociepłownia Stalowa Wola S.A. under the consolidation arrangement concluded on 30 June 2017 totalling PLN 170 058 thousand with interest accrued by 31 October 2017 totalling PLN 2 449 thousand was extended until 28 February 2018 and Elektrociepłownia Stalowa Wola S.A. was provided with another loan totalling PLN 2 650 thousand to pay for the current operations of the borrower.
- An annex to the consolidation arrangement of 30 June 2017 totalling PLN 150 000 thousand whereby the maturity of the loans under the arrangement was extended until 28 February 2018.

After the end of the reporting period, on 12 January 2018, the Company and Elektrociepłownia Stalowa Wola S.A. signed an agreement totalling PLN 27 000 thousand to be used for the operations of the borrower. Under the agreement the loan should be repaid with interest accrued based on the WIBOR 1M rate increased by a mark-up, by 28 February 2018. The repayment of the principal, interest and other costs and amounts due to the Company under the agreement is secured by the borrower's blank promissory note and a promissory note agreement up to the maximum amount of PLN 32 400 thousand.

After the end of the reporting period, on 28 February 2018, the Company entered into an agreement with Elektrociepłownia Stalowa Wola S.A. to consolidate the borrower's debt in the total amount of PLN 609 951 thousand, by renewing all the existing liabilities of the borrower arising from loans that had been granted and not repaid by 28 February 2018. The scope of the consolidation agreement includes principal amounts of loans granted whose carrying amount as at 31 December 2017 was PLN 529 007 thousand, the principal amount of a loan of 12 January 2018 of PLN 27 000 thousand as well as interest on the above debt, accrued as at 28 February 2018 in the total amount of PLN 53 944 thousand. Under the consolidation agreement, a portion of the debt of PLN 299 100 thousand is to be repaid within two business days of the borrower's receipt of external funding in relation to the gas and steam unit construction project in Stalowa Wola, while the remaining portion of PLN 310 851 thousand, along with interest accrued as of 1 March 2018, is to be repaid by the borrower by 30 June 2033. The interest rate on the loan is fixed and the repayment is secured by a blank promissory note along with a promissory note agreement up to the maximum amount of PLN 732 000 thousand.

(in PLN '000)

After the end of the reporting period, on 8 March 2018 Elektrociepłownia Stalowa Wola S.A. signed a loan agreement with Bank Gospodarstwa Krajowego and Polskie Górnictwo Naftowe i Gazownictwo S.A. Under the above mentioned agreement Bank Gospodarstwa Krajowego and PGNiG S.A. will grant Elektrociepłownia Stalowa Wola S.A. a loan in the amount of PLN 450 000 thousand each, to be used to refinance the debt of Elektrociepłownia Stalowa Wola S.A. towards the Company and PGNiG S.A. in the total amount of PLN 600 000 thousand and to cover new capital expenditures of PLN 300 000 thousand allowing Elektrociepłownia Stalowa Wola S.A. to complete the project of constructing of a gas and steam unit. The final loan repayment date is 14 June 2030. The loan agreement provides for the funds to be paid out to Elektrociepłownia Stalowa Wola S.A. after the suspending conditions have been met, with one of them being presenting to Bank Gospodarstwa Krajowego of a bank guarantee issued at the Company's instruction and securing the Loan Taker's debt towards Bank Gospodarstwa Krajowego. The bank guarantee will be renewed annually, and its value will not exceed PLN 517 500 thousand.

24. Other Financial Assets

	As at 31 December 2017	As at 31 December 2016
Shares	141 698	131 698
Deposits and term deposits for Mining Decommissioning Fund	39 756	38 472
Derivative instruments	33 416	56 417
Investment fund units	104 077	27 761
Loans granted	10 547	50
Bid bonds, deposits and collateral transferred	61 817	41 818
Initial margins	11 140	–
Other	7 554	10 561
Total	**410 005**	**306 777**
Non-current	238 095	227 140
Current	171 910	79 637

As at 31 December 2017 the shares held by the Group are mainly shares in the following entities:

- SCE Jaworzno III Sp. z o.o., in the amount of PLN 36 283 thousand;
- Przedsiębiorstwo Energetyki Cieplnej Tychy Sp. z o.o., in the amount of PLN 32 483 thousand;
- PGE EJ 1 Sp. z o.o., in the amount of PLN 26 546 thousand;
- Energetyka Cieszyńska Sp. z o.o., in the amount of PLN 15 063 thousand.
- Magenta Grupa TAURON Sp. z o.o. in the amount of PLN 9 500 thousand.

In the year ended 31 December 2017, the Parent acquired units in investment funds in the total amount of PLN 75 000 thousand.

25. Other Non-Financial Assets

25.1. Other non-current non-financial assets

	As at 31 December 2017	As at 31 December 2016
Prepayments for assets under construction and intangible assets including:	163 906	274 301
related to project realization: Construction of 910 MW Power Unit in Jaworzono III Power Plant	*162 589*	*271 667*
Costs of preparing production in hard coal mines	144 061	132 862
Prepayments for debt charges	12 252	6 005
Other prepayments	26 627	9 232
Total	**346 846**	**422 400**

(in PLN '000)

25.2. Other current non-financial assets

	As at 31 December 2017	As at 31 December 2016
Costs settled over time	**79 935**	**78 457**
Costs of preparing production in hard coal mines	52 123	36 175
Property and tort insurance	3 010	10 922
IT, telecom and postal services	15 074	17 994
Prepayments for debt charges	3 917	3 526
Other prepayments	5 811	9 840
Other current non-financial assets	**7 120**	**106 551**
Advance payments for deliveries	4 858	103 601
Surplus of Social Benefit Fund assets over its liabilities	–	338
Other current assets	2 262	2 612
Total	**87 055**	**185 008**

Company's Social Benefit Fund

The Group entities offset the Fund assets with their liabilities to the Fund as the assets are not classified as separate assets of the Group. Presented below is an analysis of the fund.

	As at 31 December 2017	As at 31 December 2016
Loans granted to employees	29 718	30 671
Cash	17 703	17 093
Other Fund assets and liabilities	2 316	2 822
Social Fund liabilities	(49 828)	(50 248)
Net balance	**(91)**	**338**
Transfers made to the Social Fund during the period	(55 624)	(62 180)

26. Inventories

	As at 31 December 2017	As at 31 December 2016
Gross value		
Coal, of which:	189 464	320 201
Raw materials	*33 260*	*98 759*
Semi-finished goods and work-in-progress	*155 180*	*216 831*
Energy certificates	–	783
Gas emission allowances	382	45 912
Other inventories	114 450	115 591
Total	**304 296**	**482 487**
Measurement to fair value		
Emission allowances	8	13 226
Measurement to net realisable value		
Other inventories	(8 841)	(9 593)
Total	**(8 833)**	**3 633**
Fair value		
Gas emission allowances	390	59 138
Net realisable value		
Coal, of which:	189 464	320 201
Raw materials	*33 260*	*98 759*
Semi-finished goods and work-in-progress	*155 180*	*216 831*
Energy certificates	–	783
Other inventories	105 609	105 998
Total	**295 463**	**486 120**

(in PLN '000)

Change in the balance of impairment losses on inventories / Inventory revaluation

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**3 633**	**(10 136)**
Recognition	(4 109)	(5 417)
Reversal	623	2 682
Utilization	4 238	3 278
Fair value measurement of emission allowances	(13 218)	13 226
Closing balance	**(8 833)**	**3 633**

27. Receivables from buyers

	As at 31 December 2017	As at 31 December 2016
Value of items before allowance/write-down		
Receivables from buyers	1 557 864	1 527 921
Receivables from buyers – additional assessment of revenue from sales of electricity and distribution services	499 601	425 705
Receivables claimed at court	205 025	146 086
Total	**2 262 490**	**2 099 712**
Allowance/write-down		
Receivables from buyers	(49 159)	(84 036)
Receivables claimed at court	(180 518)	(121 611)
Total	**(229 677)**	**(205 647)**
Value of item net of allowance (carrying amount)		
Receivables from buyers	1 508 705	1 443 885
Receivables from buyers – additional assessment of revenue from sales of electricity and distribution services	499 601	425 705
Receivables claimed at court	24 507	24 475
Total	**2 032 813**	**1 894 065**

Ageing analysis of receivables from buyers as at 31 December 2017 year

	Not past due	Past due					Total
		<30 days	30–90 days	90–180 days	180–360 days	>360 days	
Value of item before allowance/ write-down	1 794 372	170 594	65 539	17 954	33 717	180 314	**2 262 490**
Allowance/write-down	(1 282)	(1 887)	(32 854)	(6 756)	(30 538)	(156 360)	**(229 677)**
Net Value	**1 793 090**	**168 707**	**32 685**	**11 198**	**3 179**	**23 954**	**2 032 813**

Ageing analysis of receivables from buyers as at 31 December 2016 year

	Not past due	Past due					Total
		<30 days	30–90 days	90–180 days	180–360 days	>360 days	
Value of item before allowance/ write-down	1 661 135	169 403	45 013	19 816	25 657	178 688	**2 099 712**
Allowance/write-down	(5 369)	(12 255)	(3 683)	(6 303)	(22 732)	(155 305)	**(205 647)**
Net Value	**1 655 766**	**157 148**	**41 330**	**13 513**	**2 925**	**23 383**	**1 894 065**

As at the end of the reporting period, the Group did not have any material non-collectible items not covered with the allowance.

Impairment losses on receivables from buyers

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**(205 647)**	**(278 374)**
Recognised	(106 052)	(97 928)
Utilized	9 282	22 861
Reversed	52 296	87 267
Other movements	20 444	60 527
Closing balance	**(229 677)**	**(205 647)**

(in PLN '000)

28. Receivables arising from Taxes and Charges

	As at 31 December 2017	As at 31 December 2016
Corporate Income Tax receivables	2 128	83 468
VAT receivables	211 520	154 181
Excise duty receivables	29 718	24 205
Other	760	2 000
Total	**244 126**	**263 854**

29. Cash and Cash Equivalents

	As at 31 December 2017	As at 31 December 2016
Cash at bank and in hand	703 202	368 274
Short-term deposits (up to 3 months)	205 889	16 450
Other	158	157
Total cash and cash equivalents presented in the statement of financial position, of which:	**909 249**	**384 881**
restricted cash	152 952	144 404
Bank overdraft	(93 503)	(15 156)
Cash pool	(13 676)	(16 095)
Foreign exchange	(717)	1 103
Total cash and cash equivalents presented in the statement of cash flows	**801 353**	**354 733**

As at 31 December 2017 the balance of restricted cash included mainly cash on the accounts for bid bonds of PLN 84 124 thousand and cash on the accounts used for settling electricity trading and emission allowances on the Polish Power Exchange, i.e. Towarowa Giełda Energii S.A., of PLN 61 846 thousand.

30. Equity

30.1. Issued capital

Issued capital as at 31 December 2017

Class/ issue	Type of shares	Number of shares	Nominal value of one share (in PLN)	Value of class/issue at nominal value	Method of payment
AA	bearer shares	1 589 438 762	5	7 947 194	cash/in-kind contribution
BB	registered shares	163 110 632	5	815 553	in-kind contribution
	Total	**1 752 549 394**		**8 762 747**	

As at 31 December 2017, the value of issued capital, the number of shares and the nominal value of shares had not changed as compared to 31 December 2016.

Shareholding structure as at 31 December 2017 ***(to the best of the Company's knowledge)***

Shareholder	Number of shares	Value of shares	Percentage of share capital	Percentage of total vote
State Treasury	526 848 384	2 634 242	30.06%	30.06%
KGHM Polska Miedź S.A.	182 110 566	910 553	10.39%	10.39%
Nationale - Nederlanden Otwarty Fundusz Emerytalny	88 742 929	443 715	5.06%	5.06%
Other shareholders	954 847 515	4 774 237	54.49%	54.49%
Total	**1 752 549 394**	**8 762 747**	**100%**	**100%**

To the best of the Company's knowledge, the shareholding structure as at 31 December 2017 had not changed since 31 December 2016.

(in PLN '000)

30.2. Shareholder Rights

The voting rights of the shareholders holding more than 10% of the total votes in the Company have been limited in such a manner that none of them is entitled to exercise the right to more than 10% of votes at the General Shareholders' Meeting of the Company.

The voting right limitation mentioned above does not apply to the State Treasury and State Treasury owned companies in the period when the State Treasury and State Treasury owned companies hold shares in the Company entitling to more than 25% of the total votes in the Company.

Detailed information concerning the limitations on exercising the voting rights has been presented in Section 6.6 of the Management Board's report on the activities of the TAURON Polska Energia S.A. Capital Group for the 2017 financial year.

30.3. Supplementary capital

On 29 May 2017, the Ordinary General Shareholders' Meeting adopted a resolution to offset the net loss for the 2016 financial year, totalling PLN 166 253 thousand, against the reserve capital.

30.4. Retained earnings and dividend limitation

Prior year profit/loss arising from settlement of business combinations with subsidiaries and actuarial gains and losses related to provisions for post-employment benefits recognized through other comprehensive income are not distributable.

As at 31 December 2017 and as at the date of approval of these financial statements for publication no other dividend restriction occurred.

The Company's Management Board recommends the net profit for the year 2017 in the amount of PLN 854 351 thousand to be allocated the Company's reserve capital.

30.5. Revaluation reserve – measurement of hedging instruments

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**29 660**	**(73 414)**
Remeasurement of hedging instruments	(8 159)	132 108
Remeasurement of hedging instruments charged to profit or loss	–	(4 856)
Deferred income tax	1 550	(24 178)
Closing balance	**23 051**	**29 660**

The revaluation reserve from valuation of hedging instruments results from valuation of Interest Rate Swaps (IRS) hedging the interest rate risk arising from bonds issued, which has been discussed in more detail in Note 44.3 to these consolidated financial statements.

The Company applies hedge accounting to hedging transactions covered by the policy for specific risk management in the area of finance.

As at 31 December 2017 the Company recognized PLN 23 051 thousand of revaluation reserve from valuation of hedging instruments. It represents an asset arising from valuation of interest rate swaps as at the end of the reporting period, totalling PLN 28 482 thousand, adjusted by a portion of valuation relating to interest accrued on bonds as at the end of the reporting period, including deferred tax.

The amount of PLN 1 525 thousand was recognized in profit/loss for the period as a payment under a realized hedge for past interest periods.

30.6. Non-controlling interest

	Year ended 31 December 2017	Year ended 31 December 2016
At the beginning of the period	**30 052**	**29 829**
Dividends for non-controlling interests	(564)	(3 043)
Share in actuarial gains/(losses) related to provisions for post-employment benefits	33	272
Acquisition of non-controlling interests by the Group and mandatory squeeze-out	(437)	325
Share in subsidiaries' net profit or loss	2 283	2 669
At the end of the period	**31 367**	**30 052**

(in PLN '000)

31. Dividends Paid

	Year ended 31 December 2017	Year ended 31 December 2016
Dividends paid by subsidiaries	(595)	(2 787)

On 13 March 2017, the Management Board of TAURON Polska Energia S.A. adopted a resolution to file a motion with the Ordinary General Shareholders' Meeting of TAURON Polska Energia S.A. to offset the Company's net loss for the 2016 financial year of PLN 166 253 thousand against the reserve capital. The Management Board of the Company decided not to put forward a recommendation to the Ordinary General Shareholders' Meeting, concerning the adoption of a decision to use the Company's reserve capital for purposes of payment of dividend for 2016 to the Company's shareholders. On 29 May 2017, the Ordinary General Shareholders' Meeting of the Company adopted a resolution following the recommendation of the Management Board.

On 10 March 2016, the Management Board adopted a resolution to put forward a recommendation to the Ordinary General Shareholders' Meeting, concerning the use of the Company's reserve capital representing amounts transferred from prior year profit for purposes of dividend payment to the Company's shareholders in the amount of PLN 175 255 thousand, which equals to PLN 0.10 per share. On 17 March 2016, the Supervisory Board of the Company approved the recommendation presented by the Management Board. On 8 June 2016, the Ordinary General Shareholders' Meeting did not adopt a resolution to use a portion of the Company's reserve capital representing amounts transferred from prior year profit for purposes of dividend payment to the Company's shareholders.

32. Debt

	As at 31 December 2017	As at 31 December 2016
Loans and borrowings	1 191 388	1 263 553
Bonds issued	8 637 435	7 681 128
Finance lease	23 973	34 848
Total	**9 852 796**	**8 979 529**
Non-current	9 501 414	8 759 789
Current	351 382	219 740

32.1. Loans and borrowings

Loans and borrowings taken out as at 31 December 2017

Currency	Interest rate	Value of loans and borrowings as at the balance sheet date		of which maturing within (*after the balance sheet date*):					
		currency	PLN	less than 3 months	3–12 months	1–2 years	2–3 years	3–5 years	over 5 years
PLN	floating	55 757	55 757	22 297	5 496	7 341	7 341	13 282	–
	fixed	1 036 011	1 036 011	35 187	127 054	162 240	162 240	273 506	275 784
Total PLN		**1 091 768**	**1 091 768**	**57 484**	**132 550**	**169 581**	**169 581**	**286 788**	**275 784**
EUR	floating	22 060	92 009	92 009	–	–	–	–	–
Total EUR		**22 060**	**92 009**	**92 009**	**–**	**–**	**–**	**–**	**–**
USD	floating	418	1 454	1 454	–	–	–	–	–
Total USD		**418**	**1 454**	**1 454**	**–**	**–**	**–**	**–**	**–**
Total			**1 185 231**	**150 947**	**132 550**	**169 581**	**169 581**	**286 788**	**275 784**
Interest increasing carrying amount			6 157						
Total			**1 191 388**						

(in PLN '000)

Loans and borrowings taken out as at 31 December 2016

Currency	Interest rate	Value of loans and borrowings as at the balance sheet date		of which maturing within (*after the balance sheet date*):					
		currency	PLN	less than 3 months	3–12 months	1–2 years	2–3 years	3–5 years	over 5 years
PLN	floating	57 918	57 918	17 791	5 894	7 491	7 341	14 575	4 826
	fixed	1 183 418	1 183 418	20 445	127 044	162 227	162 227	324 455	387 020
Total PLN		**1 241 336**	**1 241 336**	**38 236**	**132 938**	**169 718**	**169 568**	**339 030**	**391 846**
EUR	floating	3 032	13 415	13 415	–	–	–	–	–
Total EUR		**3 032**	**13 415**	**13 415**	**–**	**–**	**–**	**–**	**–**
USD	floating	410	1 716	1 716	–	–	–	–	–
Total USD		**410**	**1 716**	**1 716**	**–**	**–**	**–**	**–**	**–**
Total			**1 256 467**	**53 367**	**132 938**	**169 718**	**169 568**	**339 030**	**391 846**
Interest increasing carrying amount			7 086						
Total			**1 263 553**						

Changes in the balance of loans and borrowings, excluding interest increasing their carrying amount, in the year ended 31 December 2017 and in the comparative period, have been presented below.

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**1 256 467**	**1 403 618**
Movement in bank overdrafts and cash pool loans received	**83 471**	**(8 332)**
Movement in loans (excluding bank overdrafts and cash pool loans):	**(154 707)**	**(138 819)**
Repaid	(154 918)	(140 331)
Taken	–	914
Change in valuation	211	598
Closing balance	**1 185 231**	**1 256 467**

The major liabilities due to loans and borrowings have been presented in the table below:

Loans/ borrowings	Borrowing institution	Purpose	Interest rate	Maturity date	As at 31 December 2017	As at 31 December 2016
Loans	European Investment Bank	Construction of a boiler fired with biomass at Jaworzno III Power Plant and renovation of a steam turbine	Fixed – agreed until 15 June 2016	15.12.2021	84 039	105 039
		Construction and start-up of a co-generation unit at EC Bielsko Biała	Fixed – agreed until 15 June 2016	15.12.2021	120 061	150 056
		Modernization and extension of power grid	Fixed – agreed until 15 December 2017	15.06.2024	266 139	307 362
			Fixed – agreed until 15 March 2018	15.09.2024	128 711	147 091
			Fixed – agreed until 15 March 2018	15.09.2024	160 819	183 783
		Modernization and extension of power grid and improvement of hydropower plants	Fixed – agreed until 15 September 2019	15.03.2027	282 341	297 170
Overdraft facility	Bank Gospodarstwa Krajowego	Financing of transactions involving emission allowance, energy and gas	Floating	31.12.2018	92 048	13 415
Borrowings	Regional Fund for Environmental Protection and Water Management	Construction of renewable power unit at Jaworzno III Power Plant	Floating	15.12.2022	20 000	24 000
		Construction of biomass infeed installation and modernization of fluid bed at Tychy Generation Plant	Floating	15.12.2022	13 881	16 561
Other loans and borrowings					23 349	19 076
Total					**1 191 388**	**1 263 553**

(in PLN '000)

32.2. Bonds issued

Bonds issued as at 31 December 2017

Issuer	Tranche/ Bank	Redemption date	Currrency	Principal at nominal value in currency	As at balance sheet date		of which maturing within (*after the balance sheet date*):		
					Interest accrued	Principal at amortised cost	up to 2 years	2-5 years	Over 5 years
TAURON Polska Energia S.A.	Bank Gospodarstwa Krajowego	20.12.2019	PLN	100 000	107	99 869	99 869	–	–
		20.12.2020	PLN	100 000	107	99 838	–	99 838	–
		20.12.2021	PLN	100 000	107	99 817	–	99 817	–
		20.12.2022	PLN	100 000	107	99 800	–	99 800	–
		20.12.2023	PLN	100 000	107	99 787	–	–	99 787
		20.12.2024	PLN	100 000	107	99 778	–	–	99 778
		20.12.2025	PLN	100 000	107	99 770	–	–	99 770
		20.12.2026	PLN	100 000	107	99 761	–	–	99 761
		20.12.2027	PLN	100 000	107	99 756	–	–	99 756
		20.12.2028	PLN	100 000	107	99 752	–	–	99 752
		20.12.2020	PLN	70 000	74	69 963	–	69 963	–
		20.12.2021	PLN	70 000	74	69 961	–	69 961	–
		20.12.2022	PLN	70 000	74	69 959	–	69 959	–
		20.12.2023	PLN	70 000	74	69 958	–	–	69 958
		20.12.2024	PLN	70 000	74	69 957	–	–	69 957
		20.12.2025	PLN	70 000	74	69 956	–	–	69 956
		20.12.2026	PLN	70 000	74	69 956	–	–	69 956
		20.12.2027	PLN	70 000	74	69 955	–	–	69 955
		20.12.2028	PLN	70 000	74	69 955	–	–	69 955
		20.12.2029	PLN	70 000	74	69 955	–	–	69 955
	Bond Issue Scheme of 24.11.2015	29.12.2020	PLN	1 600 000	389	1 597 188	–	1 597 188	–
	TPEA1119	4.11.2019	PLN	1 750 000	7 609	1 749 277	1 749 277	–	–
	European Investment Bank	16.12.2034	EUR	190 000	1 597	791 355	–	–	791 355
	Eurobonds EURBD050727	5.07.2027	EUR	500 000	24 425	2 069 193	–	–	2 069 193
TAURON Sweden Energy AB (publ)		3.12.2029	EUR	168 000	1 950	695 139	–	–	695 139
Total					**37 780**	**8 599 655**	**1 849 146**	**2 106 526**	**4 643 983**

Bonds issued as at 31 December 2016

Issuer	Tranche/ Bank	Redemption date	Currrency	Principal at nominal value in currency	As at balance sheet date		of which maturing within (*after the balance sheet date*):		
					Interest accrued	Principal at amortised cost	up to 2 years	2-5 years	Over 5 years
TAURON Polska Energia S.A.	Bank Gospodarstwa Krajowego	20.12.2019	PLN	100 000	107	99 805	–	99 805	–
		20.12.2020	PLN	100 000	107	99 786	–	99 786	–
		20.12.2021	PLN	100 000	107	99 773	–	99 773	–
		20.12.2022	PLN	100 000	107	99 763	–	–	99 763
		20.12.2023	PLN	100 000	107	99 754	–	–	99 754
		20.12.2024	PLN	100 000	107	99 749	–	–	99 749
		20.12.2025	PLN	100 000	107	99 744	–	–	99 744
		20.12.2026	PLN	100 000	107	99 738	–	–	99 738
		20.12.2027	PLN	100 000	107	99 734	–	–	99 734
		20.12.2028	PLN	100 000	107	99 733	–	–	99 733
		20.12.2020	PLN	70 000	74	69 976	–	69 976	–
		20.12.2021	PLN	70 000	74	69 976	–	69 976	–
		20.12.2022	PLN	70 000	74	69 976	–	–	69 976
		20.12.2023	PLN	70 000	74	69 976	–	–	69 976
		20.12.2024	PLN	70 000	74	69 975	–	–	69 975
		20.12.2025	PLN	70 000	74	69 975	–	–	69 975
		20.12.2026	PLN	70 000	74	69 975	–	–	69 975
		20.12.2027	PLN	70 000	74	69 975	–	–	69 975
		20.12.2028	PLN	70 000	74	69 975	–	–	69 975
		20.12.2029	PLN	70 000	74	69 975	–	–	69 975
	Bond Issue Scheme of 24.11.2015	29.12.2020	PLN	2 250 000	549	2 244 801	–	2 244 801	–
		25.03.2020	PLN	100 000	790	99 771	–	99 771	–
		9.12.2020	PLN	300 000	560	298 761	–	298 761	–
	TPEA1119	4.11.2019	PLN	1 750 000	7 578	1 749 155	–	1 749 155	–
	European Investment Bank	16.12.2034	EUR	190 000	1 693	839 330	–	–	839 330
TAURON Sweden Energy AB (publ)		3.12.2029	EUR	168 000	2 067	736 930	–	–	736 930
Total					**15 047**	**7 666 081**	**–**	**4 831 804**	**2 834 277**

On 5 July 2017 the Company issued eurobonds with the total par value of EUR 500 000 thousand and the issue price of 99.438 percent of the par value. They are 10-year bonds with fixed interest paid on an annual basis. The bonds have been admitted to trading on the London Stock Exchange. They were rated "BBB" by the Fitch rating agency.

On 20 June 2017 the Company signed annexes to the agency and custody agreement and the underwriting agreement of 24 November 2015 whereby the scheme was extended:

- by one year, i.e. until 31 December 2021 ("1st Extension Period"). During the 1st Extension Period, the scheme's maximum value will be PLN 5 320 000 thousand, and the extension will include the following banks: MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland, Bank Zachodni WBK S.A., CaixaBank S.A. (Spółka Akcyjna) Branch in Poland, Industrial and Commercial Bank of China (Europe) S.A. Branch in Poland, ING Bank Śląski S.A., Powszechna Kasa Oszczędności Bank Polski S.A. and mBank S.A.
- by two years, i.e. until 31 December 2022 ("2nd Extension Period"). During the 2nd Extension Period, the scheme's maximum value will be PLN 2 450 000 thousand, and the extension will include the following banks: MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland and Powszechna Kasa Oszczędności Bank Polski S.A.

After the end of the reporting period, on 9 March 2018 amendments to the agency and custody agreement as well as underwriting agreement were signed, the result of which is an extension by some banks of the period of availability of the funds under the Scheme. This means that the maximum value of the Scheme:

- is PLN 6 070 000 thousand until 31 December 2021 (it had been PLN 5 320 000 thousand before the amendments were signed),
- is PLN 5 820 000 thousand until 31 December 2022 (it had been PLN 2 450 000 thousand before the amendments were signed).

By 31 December 2020 the Scheme's value will not change and will not exceed PLN 6 270 000 thousand.

The amendments were signed with the following banks taking part in the Program: Bank Handlowy in Warsaw S.A., Bank BGŻ BNP Paribas S.A., Bank Zachodni WBK S.A., CaixaBank S.A. (Joint Stock Company) Branch in Poland, Industrial and Commercial Bank of China (Europe) S.A. Branch in Poland, ING Bank Śląski S.A., mBank S.A., MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland and Powszechna Kasa Oszczędności Bank Polski S.A. Due to the extension, the financing margin in the Scheme did not change.

The bonds issued on 16 December 2016, with the par value of EUR 190 000 thousand, were subordinated, unsecured coupon bearer securities, and they were acquired by the European Investment Bank as part of the operations of the European Fund for Strategic Investments, launched by EIB and the European Commission to implement the Juncker Plan. The euro is the currency of the issue. The bonds will mature 18 years of the issue date, with the proviso that in line with the description of hybrid funding the first funding period was defined to last 8 years ("1st Funding Period") during which the Company will not be allowed to repurchase the bonds early and the bonds may not be sold early by EIB to third parties (in both cases, subject to the exceptions set out in the agreement). The bonds bear fixed interest during the 1st Funding Period and during the next 10-year funding period ("2nd Funding Period") interest will be floating and determined by reference to Euribor 6M increased by an agreed margin. Under the agreement, interest on the bonds may be deferred. As the bonds are subordinated, any claims arising therefrom will have priority of satisfaction only before the amounts due to the Company's shareholders in the event of its bankruptcy or liquidation. The bond issue has had a positive effect on the financial stability of the Group as the bonds are not taken into account for purposes of calculation of the debt ratio, which is a covenant in some funding schemes. Additionally, 50% of the bond amount has been classified by the rating agency as equity in the rating model, which has had a beneficial effect on the rating of the TAURON Group. The rating assigned to the bonds by Fitch is BB+.

Other bonds issued by the Parent on the Polish market are dematerialized, unsecured coupon bonds with interest determined by reference to WIBOR 6M increased by a margin agreed separately for each issue. The Polish zloty is the currency of the issue and the repayment.

Bonds issued by TAURON Sweden Energy AB (publ), a subsidiary, are fixed-rate securities with interest payable annually. The euro is the issue currency and repayment currency. As at 31 December 2017, the carrying amount of the bonds with interest in the bond currency was EUR 167 131 thousand (versus EUR 167 043 thousand as at 31 December 2016). The Company granted a corporate guarantee to TAURON Sweden Energy AB (publ) to secure the bonds in question. The guarantee is valid in the entire bond period, i.e. until 3 December 2029, and amounts to EUR 168 000 thousand.

(in PLN '000)

Changes in the balance of bonds, excluding interest which increased the carrying amount

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**7 666 081**	**6 665 528**
Issue*	2 703 643	4 273 379
Redemption	(1 650 000)	(3 300 000)
Change in valuation	(120 069)	27 174
Closing balance	**8 599 655**	**7 666 081**

** Discount and costs of issue have been included.*

In the year ended 31 December 2017, the Company issued (par value) and repurchased the following bonds:

Date of issue/ redemption	Agreement/ Scheme	Description	Year ended 31 December 2017	
			Par value of issue	Redemption
05.07.2017	Eurobonds	Issue of eurobonds with the total par value of EUR 500,000 thousand and the issue price of 99.438% of the par value, maturing on 5 July 2027.	2 107 462	
30.01.2017	Bond Issue Scheme dated 24 November 2015	Issue of bonds with the par value of PLN 100,000 thousand, maturing on 30 January 2020.	100 000	
01.03.2017		Issue of bonds with the par value of PLN 100,000 thousand, maturing on 1 March 2020.	100 000	
31.03.2017		Issue of bonds with the par value of PLN 300,000 thousand, maturing on 30 June 2017.	300 000	
30.06.2017		Issue of bonds with the par value of PLN 100,000 thousand, maturing on 30 July 2017.	100 000	
30.06.2017		Redemption (at maturity) of bonds with the par value of PLN 300,000 thousand, which were issued on 31 March 2017.		(300 000)
30.07.2017		Early redemption of bonds with the par value of PLN 100,000 thousand, which were issued on 30 January 2017.		(100 000)
30.07.2017		Redemption (at maturity) of bonds with the par value of PLN 100,000 thousand, which were issued on 30 June 2017.		(100 000)
01.09.2017		Early redemption of bonds with the par value of PLN 100,000 thousand, which were issued on 1 March 2017.		(100 000)
25.09.2017		Early redemption of bonds with the par value of PLN 100,000 thousand, which were issued on 25 March 2016.		(100 000)
09.12.2017		Early redemption of bonds with the par value of PLN 300,000 thousand, which were issued on 9 December 2016.		(300 000)
29.12.2017		Early partial redemption of bonds with the par value of PLN 650,000 thousand, which were issued on 29 February 2016.		(650 000)
		Total	**2 707 462**	**(1 650 000)**

The Company hedges a portion of interest cash flows related to issued bonds using IRS contracts. The instruments are subject to hedge accounting, which has been discussed in more detail in Note 44.3 to these consolidated financial statements.

The agreements signed by the Company with the banks include legal and financial covenants which are commonly used in such transactions. The key covenant is the net debt/EBITDA ratio (for domestic bond issue programs), which defines the maximum allowable debt level decreased by cash in relation to the generated EBITDA. As at 31 December 2017, none of these covenants had been breached and the contractual provisions were complied with.

(in PLN '000)

32.3. Finance lease

	As at 31 December 2017		As at 31 December 2016	
	Minimum lease payments	Present value of lease payments	Minimum lease payments	Present value of lease payments
Within 1 year	24 145	23 947	12 026	11 301
Within 1 to 5 years	8	8	23 724	23 527
More than 5 years	20	18	22	20
Minimum lease payments, total	**24 173**	**23 973**	**35 772**	**34 848**
Less amounts representing finance charges	(200)	–	(924)	–
Present value of minimum lease payments	**23 973**	**23 973**	**34 848**	**34 848**
Non-current	25	25	23 546	23 546
Current	23 948	23 948	11 302	11 302

As at 31 December 2017, the liabilities arising from the leased building in Katowice of PLN 23 945 thousand (versus PLN 26 974 thousand as at 31 December 2016) were the key item of finance lease liabilities.

33. Provisions for Employee Benefits

	As at 31 December 2017	As at 31 December 2016
Provision for post-employment benefits and jubilee bonuses	1 469 108	1 480 391
Provision for employment termination benefits	45 815	51 222
Total	**1 514 923**	**1 531 613**
Non-current	1 380 650	1 373 385
Current	134 273	158 228

33.1. Provisions for post-employment benefits and jubilee bonuses

Change in provisions for employee benefits for the year ended 31 December 2017

	Provision for retirement, disability and similar benefits	Employee electricity rates	Social Fund	Provision for coal allowances	Jubilee bonuses	Provisions, total
Opening balance	**307 281**	**532 184**	**112 469**	**2 248**	**526 209**	**1 480 391**
Current service costs	16 933	13 878	2 854	–	32 622	**66 287**
Actuarial gains and losses, of which:	1 452	(7 880)	(13 225)	–	4 082	**(15 571)**
arising from changes in financial assumptions	(5 572)	–	–	–	(7 750)	**(13 322)**
arising from changes in demographic assumptions	–	–	(18)	–	(167)	**(185)**
arising from other changes	7 024	(7 880)	(13 207)	–	11 999	**(2 064)**
Benefits paid	(25 382)	(19 663)	(3 750)	–	(58 243)	**(107 038)**
Past service costs	13 442	(2 802)	4 736	–	(8 013)	**7 363**
Interest expense	8 168	15 338	3 237	–	14 021	**40 764**
Other changes	–	(840)	–	(2 248)	–	**(3 088)**
Closing balance	**321 894**	**530 215**	**106 321**	**–**	**510 678**	**1 469 108**
Non-current	293 043	510 172	102 495	–	454 107	**1 359 817**
Current	28 851	20 043	3 826	–	56 571	**109 291**

In the year ended 31 December 2017, the Group increased its provisions for post-employment benefits and jubilee bonuses relating to past service costs by the total of PLN 7 363 thousand, which resulted mainly from changes in Collective Labour Agreements in the following entities:

- an entity from the Mining segment – leading to increase in provisions for retirement, disability and similar benefits and for jubilee bonuses totalling PLN 17 363 thousand;
- entities from the Sales segment – leading to reversal of provisions for jubilee bonuses totalling PLN 4 673 thousand;
- an entity from the Other segment – leading to a reduction in actuarial provisions totalling PLN 3 790 thousand.

(in PLN '000)

Following a change in actuarial assumptions made for purposes of the actuarial valuation as at 31 December 2017, provisions were reduced by PLN 15 571 thousand, which drove an increase in other comprehensive income by PLN 19 653 thousand (provisions for post-employment benefits) and a decrease in the Group's profit/loss by PLN 4 082 thousand (provisions for jubilee bonuses).

Change in provisions for employee benefits for the year ended 31 December 2016

	Provision for retirement, disability and similar benefits	Employee electricity rates	Social Fund	Provision for coal allowances	Jubilee bonuses	Provisions, total
Opening balance	**341 124**	**722 734**	**131 110**	**2 242**	**653 165**	**1 850 375**
Current service costs	17 093	14 003	2 170	–	37 519	**70 785**
Actuarial gains and losses, of which:	(27 145)	(148 051)	(29 401)	–	(40 296)	**(244 893)**
arising from changes in financial assumptions	(6 026)	(54 665)	(15 892)	–	(7 245)	**(83 828)**
arising from changes in demographic assumptions	10 566	(32 751)	(3 966)	–	3 035	**(23 116)**
arising from other changes	(31 685)	(60 635)	(9 543)	–	(36 086)	**(137 949)**
Benefits paid	(22 065)	(22 432)	(3 677)	(2 241)	(74 090)	**(124 505)**
Past service costs	(20 470)	(53 901)	8 677	–	(84 487)	**(150 181)**
Interest expense	9 308	19 831	3 590	–	17 372	**50 101**
Acquisition of ZCP Brzeszcze	9 436	–	–	–	17 026	**26 462**
Other changes	–	–	–	2 247	–	**2 247**
Closing balance	**307 281**	**532 184**	**112 469**	**2 248**	**526 209**	**1 480 391**
Non-current	271 934	512 671	108 116	–	468 963	**1 361 684**
Current	35 347	19 513	4 353	2 248	57 246	**118 707**

Measurement of provisions for employee benefits

Provisions for post-employment benefits and jubilee bonuses have been estimated using actuarial methods. Key actuarial assumptions made as at the end of the reporting period for provision calculation purposes:

	31 December 2017	31 December 2016
Discount rate (%)	3.00%	3.00%
Estimated inflation rate (%)	2.50%	2.50%
Employee rotation rate (%)	1.15% – 8.64%	0.04% – 7.95%
Estimated salary increase rate (%)	1.80% – 2.50%	1.00% – 3.50%
Estimated electricity price increase rate (%)	3.50%	3.50%
Estimated increase rate for contribution to the Social Fund (%)	3.50%	3.50%
Remaining average employment period	9.89 – 20.40	9.27 – 25.00

Sensitivity analysis

As at 31 December 2017 the Group analysed sensitivity of measurement results to changes in the financial discounting rates and changes in the planned increases in the base amounts in the range of -0.5 p.p./+0.5 p.p.

The carrying amounts of individual provisions and provisions calculated based on the changed assumptions have been presented below:

Provision title	Carrying amount as at 31 December 2017	Financial discount rate		Planned base increases	
		-0.5 p.p.	+0.5 p.p.	-0.5 p.p.	+0.5 p.p.
Provision for retirement, disability and similar benefits	321 894	336 386	308 405	308 273	336 395
Employee electricity rates	530 215	572 706	492 594	492 594	572 273
Costs of appropriation to Social Benefits Fund	106 321	114 960	98 643	98 643	114 871
Jubilee bonuses	510 678	527 900	494 316	497 664	524 220
Total		**1 551 952**	**1 393 958**	**1 397 174**	**1 547 759**

(in PLN '000)

The table below presents the carrying amounts of individual provisions and how these carrying amounts would change with different assumptions applied:

Provision title	Carrying amount as at 31 December 2017	Deviations			
		Financial discount rate		Planned base increases	
		-0.5 p.p.	+0.5 p.p.	-0.5 p.p.	+0.5 p.p.
Provision for retirement, disability and similar benefits	321 894	14 492	(13 489)	(13 621)	14 501
Employee electricity rates	530 215	42 491	(37 621)	(37 621)	42 058
Costs of appropriation to Social Benefits Fund	106 321	8 639	(7 678)	(7 678)	8 550
Jubilee bonuses	510 678	17 222	(16 362)	(13 014)	13 542
Total		**82 844**	**(75 150)**	**(71 934)**	**78 651**
effect on profit/loss		17 222	(16 362)	(13 014)	13 542
effect on other comprehensive income		65 622	(58 788)	(58 920)	65 109

The Group classifies provisions as current and non-current based on estimates regarding distribution of payments over time, prepared with the use of actuarial methods.

Provisions for employee benefits by maturity

	Retirement, disability and similar benefits	Employee electricity rates	Social Fund	Jubilee bonuses	Provisions, total
2018	28 851	20 043	3 826	56 571	**109 291**
2019	18 348	21 991	3 933	46 363	**90 635**
2020	23 417	21 482	3 875	41 638	**90 412**
2021	15 462	20 945	3 806	39 303	**79 516**
2022	14 994	20 445	3 747	37 329	**76 515**
Other years	220 822	425 309	87 134	289 474	**1 022 739**
Total	**321 894**	**530 215**	**106 321**	**510 678**	**1 469 108**

33.2. Provisions for employment termination benefits

For the year ended 31 December 2017

	Voluntary redundancy schemes			Total
	Segment Generation	Segment Distribution	Other	
Opening balance	**17 599**	**17 062**	**16 561**	**51 222**
Recognition	24 076	10 025	244	**34 345**
Reversal	(1 940)	(4 982)	–	**(6 922)**
Utilization	(10 168)	(11 563)	(11 099)	**(32 830)**
Closing balance	**29 567**	**10 542**	**5 706**	**45 815**
Non-current	20 833	–	–	**20 833**
Current	8 734	10 542	5 706	**24 982**

For the year ended 31 December 2016

	Voluntary redundancy schemes			Total
	Segment Generation	Segment Distribution	Other	
Opening balance	**23 460**	**25 432**	**8 444**	**57 336**
Recognition	5 383	8 290	14 036	**27 709**
Reversal	(571)	(3 797)	(2 504)	**(6 872)**
Utilization	(10 673)	(12 863)	(3 415)	**(26 951)**
Closing balance	**17 599**	**17 062**	**16 561**	**51 222**
Non-current	11 701	–	–	**11 701**
Current	5 898	17 062	16 561	**39 521**

(in PLN '000)

34. Provisions for Dismantling Fixed Assets, Restoration of Land and Other

For the year ended 31 December 2017

	Provision for mine decommissioning costs	Provision for restoration of land and dismantling and removal of fixed assets	Provision for onerous contracts with a jointly-controlled entity and provision for costs	Provisions, total
Opening balance	**146 885**	**115 302**	**198 844**	**461 031**
Interest cost (discounting)	5 141	3 713	2 330	**11 184**
Discount rate adjustment	39 830	5 012	–	**44 842**
Recognition/(reversal), net	119	64	(201 174)	**(200 991)**
Closing balance	**191 975**	**124 091**	**–**	**316 066**
Non-current	191 975	99 214	–	**291 189**
Current	–	24 877	–	**24 877**
Other provisions, long-term portion				**59 949**
Total				**351 138**

For the year ended 31 December 2016

	Provision for mine decommissioning costs	Provision for restoration of land and dismantling and removal of fixed assets	Provision for onerous contracts with a jointly-controlled entity and provision for costs	Provisions, total
Opening balance	**111 675**	**101 244**	**182 877**	**395 796**
Interest cost (discounting)	4 904	2 700	11 502	**19 106**
Discount rate adjustment	(35 846)	(9 854)	2 257	**(43 443)**
Recognition/(reversal), net	160	21 212	2 208	**23 580**
Acquisition of ZCP Brzeszcze	65 992	–	–	**65 992**
Closing balance	**146 885**	**115 302**	**198 844**	**461 031**
Non-current	146 885	102 984	152 943	**402 812**
Current	–	12 318	45 901	**58 219**
Other provisions, long-term portion				**46 498**
Total				**449 310**

34.1. Provision for mine decommissioning costs

The provision is recognized for mines included in the Group based on estimated costs of liquidating buildings and reclaiming land after completion of the exploitation process. The provision for mine decommissioning costs includes the balance of the Mine Decommissioning Fund ("MDF), which is created under the Geological and Mining Law and the related implementing provisions, by the Group's mining companies as a pre-determined ratio of the tax depreciation charge on fixed assets or, for the exploitation fee, the equivalent of the charge transferred to a separate bank account. Financial assets of the Fund are presented in the statement of financial position under non-current and current financial assets, while the balance of the Fund is recognized under the provision for future costs of mine decommissioning.

The provision balance as at 31 December 2017 was PLN 191 975 thousand. An increase in the provision by PLN 39 830 thousand in the year ended 31 December 2017 was driven by the adoption of lower discount rates (3.00%) for purposes of valuation as at 31 December 2017 than as at 31 December 2016 (3.50%). In the comparative period, following an adoption of increased discount rate used for purposes of valuation of provisions as at 31 December 2016 (up from 2.75%–3.04% to 3.50%), the Group reversed a provision of PLN 35 846 thousand.

The following tables present the amount of appropriation to the Fund, the Fund's assets and the balance of liabilities arising from future costs of mine decommissioning.

(in PLN '000)

Mine Decommissioning Fund financial assets

	Year ended 31 December 2017	Year ended 31 December 2016
Assets as at 1 January	**41 163**	**42 129**
Contributions made	4 441	4 112
Interest	973	730
Use	(4 102)	(6 051)
Other changes	–	243
Assets as at 31 December	**42 475**	**41 163**
Transfers made to the MDF in the period	(4 155)	(4 446)

Provision for mine decommissioning costs

	Year ended 31 December 2017	Year ended 31 December 2016
Mine Decommissioning Fund	46 348	44 442
Surplus of discounted estimated decommissioning costs	145 627	102 443
Total	**191 975**	**146 885**

34.2. Provision for restoration of land and dismantling and removal of fixed assets

The provision for restoration of land and dismantling and removal of fixed assets comprises the following provisions recognized by the Generation segment companies:

- provision for ash pile reclamation costs, which totalled PLN 40 990 thousand as at 31 December 2017 (versus PLN 39 415 thousand as at 31 December 2016);
- provision for windfarm dismantling costs, which totalled PLN 57 887 thousand as at 31 December 2017 (versus PLN 51 088 thousand as at 31 December 2016);
- provision for costs of liquidation of fixed assets – a chimney in Elektrownia Jaworzno as well as cooling towers and a unit in Elektrownia Łagisza, which totalled PLN 25 214 thousand as at 31 December 2017 (versus PLN 24 799 thousand as at 31 December 2016).

34.3. Provisions for onerous contracts with a joint venture and for costs

Changes in provisions in the year ended 31 December 2017 have been presented in the table below.

	Provision for electricity contract	Provision for "take or pay" clause in gas contract	Provision for costs	Provision for onerous contracts with a jointly-controlled entity and provision for costs, total
Opening balance	**133 327**	**54 837**	**10 680**	**198 844**
Unwinding of discount	1 626	475	229	**2 330**
Recognision	–	–	2 250	**2 250**
Reversal	(134 953)	(55 312)	(13 159)	**(203 424)**
Closing balance	**–**	**–**	**–**	**–**

In 2015, the Company recognized provisions for onerous contracts with Elektrociepłownia Stalowa Wola S.A., which as at 31 December 2016 totalled PLN 198 844 thousand.

In the year ended 31 December 2017, the Company reversed in whole the following provisions for onerous contracts with a joint venture:

- a provision resulting from the fact that under a multi-annual electricity sales contract among Elektrociepłownia Stalowa Wola S.A., the Company and PGNiG Energia S.A., the Company was obliged to purchase half of the volume of electricity generated by Elektrociepłownia Stalowa Wola S.A. at a price determined in the "cost plus" formula, which covers the production costs and the financing costs;
- a provision resulting from the fact that the Company was obliged to cover losses which may have been incurred under the take-or-pay clause of the comprehensive gaseous fuel supply contract entered into by PGNiG S.A.

(in PLN '000)

and Elektrociepłownia Stalowa Wola S.A. Pursuant to the said clause, Elektrociepłownia Stalowa Wola S.A. was obliged to pay PGNiG S.A. for uncollected gas;

- a provision for necessary additional costs which the Company may have been required to incur for the operation of Elektrociepłownia Stalowa Wola S.A. due to delays in project completion.

Reversal of the provision for costs relating to the electricity sales contract and the provision for losses which might be incurred under the take-or-pay clause was the result of the fulfilment of the conditions precedent under the conditional arrangement made on 27 October 2016 to determine the key boundary conditions of the restructuring of the "Construction of a gas and steam unit in Stalowa Wola" project. The conditions precedent were discharged on 31 March 2017 when Elektrociepłownia Stalowa Wola paid all its liabilities to the financing institutions, i.e. the European Investment Bank, European Bank for Reconstruction and Development and Bank Polska Kasa Opieki S.A. The funds for repayment of the said bank loans were obtained by Elektrociepłownia Stalowa Wola S.A. under loan agreements entered into with the Company and Polskie Górnictwo Naftowe i Gazownictwo S.A. as the lenders. To this end, the Company granted a loan of PLN 290 742 thousand, which has been discussed in more detail in Note 23 to these consolidated financial statements. Once the conditions precedent were discharged the following documents came into effect:

- an agreement setting out the key boundary Project restructuring conditions among TAURON Polska Energia S.A., Polskie Górnictwo Naftowe i Gazownictwo S.A. and Elektrociepłownia Stalowa Wola S.A.;
- an annex to the electricity sales contract of 11 March 2011 executed by the Company, Polskie Górnictwo Naftowe i Gazownictwo S.A. and Elektrociepłownia Stalowa Wola S.A.;
- an annex to the gaseous fuel supply contract of 11 March 2011 between Polskie Górnictwo Naftowe i Gazownictwo S.A. and Elektrociepłownia Stalowa Wola S.A.

The aforesaid agreement sets out mainly the terms of settlement of liquidated damages, brings the existing price formulas into line with the market ones as well as governing the issue of financial restructuring of the Project. It reflects the will of the Project sponsors, i.e. TAURON Polska Energia S.A. and Polskie Górnictwo Naftowe i Gazownictwo S.A., to continue the construction of the gas and steam unit, modify the gaseous fuel supply contract and the electricity sales contract and change the existing project finance formula to a corporate finance formula. Notwithstanding the above, the sponsors and Elektrociepłownia Stalowa Wola S.A. have continued their efforts to secure new funding for the gas and steam unit construction project in Stalowa-Wola, whose terms and structure would be more favourable than those under the existing agreements.

The annexes to the gaseous fuel supply contract and the electricity sales contract, which entered into force, include in particular the application of market price formulas for the contracts in question. Furthermore, due to delays in the project, the annex to the gaseous fuel supply contract provides for changes in the amount, time limits and methodologies of imposition of liquidated damages. According to the Management Board of the Company, the changes introduced by the aforesaid annexes constituted a basis for reversal of the provision for costs related to the electricity sales contract and the provision for losses which might be incurred under the take-or-pay clause in the first quarter of 2017.

35. Provisions for Liabilities due to Gas Emission and Energy Certificates

Provisions for liabilities due to gas emission and energy certificates concern the current and the preceding year. Therefore, they are only short-term provisions.

For the year ended 31 December 2017

	Provision for gas emission obligations	Provision for obligation to submit energy certificates	Provisions, total
Opening balance	**209 736**	**755 085**	**964 821**
Recognition	324 937	645 009	**969 946**
Reversal	(84)	(10 471)	**(10 555)**
Utilisation	(209 652)	(761 171)	**(970 823)**
Closing balance	**324 937**	**628 452**	**953 389**

(in PLN '000)

For the year ended 31 December 2016

	Provision for gas emission obligations	Provision for obligation to submit energy certificates	Provisions, total
Opening balance	**153 083**	**865 051**	**1 018 134**
Recognition	381 946	754 286	**1 136 232**
Reversal	(63)	(3 884)	**(3 947)**
Utilisation	(325 230)	(860 368)	**(1 185 598)**
Closing balance	**209 736**	**755 085**	**964 821**

35.1. Provision for Gas Emission Liabilities

According to the accounting policy adopted by the Group, the provision for liabilities arising from emission of gas included in the allowance distribution plan is charged to operating expenses if the actual emission level exceeds the volume of emission allowances received free of charge, including allocation of free-of-charge emission allowances to individual facilities of the Generation segment companies, i.e. TAURON Wytwarzanie S.A. and TAURON Ciepło Sp. z o.o. The provision for costs of covering the deficit is established in the amount of allowances acquired or contracted to cover the allowance deficit and in relation to unsecured allowance deficit (if any); the provision is determined based on market prices as at the end of the reporting period.

As at 31 December 2017, the provision for gas emission liabilities amounted to PLN 324 937 thousand and regarded the obligatory surrendering of emission allowances for the year ended 31 December 2017. Provisions were recognized by the companies for current period emission allowances in the amount of:

- TAURON Wytwarzanie S.A.: PLN 286 940 thousand;
- TAURON Ciepło Sp. z o.o.: PLN 37 997 thousand.

In the year ended 31 December 2017 use of the provision in relation to the fulfilment of the remaining obligation for 2016 by TAURON Wytwarzanie S.A. and surrender of emission allowances of PLN 169 335 thousand (the obligation to surrender allowances for 2016 had already been fulfilled in part by that company in December 2016) and use of the provision in connection with the fulfilment of the obligation for 2016 by TAURON Ciepło Sp. z o.o. in the amount of PLN 40 317 thousand.

35.2. Provision for the obligation to surrender energy certificates

As at 31 December 2017, the short-term provision for the obligation to surrender energy certificates for 2017 was estimated at PLN 628 452 thousand, including PLN 331 767 thousand covered by the certificates held as at the end of the reporting period, PLN 155 355 thousand planned to be covered by the payment of the substitution fee and PLN 141 330 thousand by the purchase of property rights.

In the year ended 31 December 2017, the Group fulfilled the obligation to surrender certificates of electricity generated using renewable sources, in CHP units and energy efficiency certificates for 2016. Therefore, a provision of PLN 761 171 thousand was used.

(in PLN '000)

36. Other Provisions

For the year ended 31 December 2017

	Provision for use of real estate without contract	Provision for counterparty claims, court dispute and other provisions	Provisions, total
Opening balance	**92 143**	**262 592**	**354 735**
Interest cost (discounting)	–	3 144	**3 144**
Recognition/(reversal), net	1 141	55 122	**56 263**
Utilisation	(531)	(25 270)	**(25 801)**
Other changes	(723)	725	**2**
Closing balance	**92 030**	**296 313**	**388 343**
Non-current	–	59 949	**59 949**
Current	92 030	236 364	**328 394**
Current portion of provisions for the costs of disassembly of fixed assets and land restoration and other provisions			**24 877**
Total			**353 271**

For the year ended 31 December 2016

	Provision for use of real estate without contract	Provision for counterparty claims, court dispute and other provisions	Provisions, total
Opening balance	**91 909**	**67 711**	**159 620**
Recognition/(reversal), net	902	201 928	**202 830**
Utilisation	(642)	(7 258)	**(7 900)**
Other changes	(26)	211	**185**
Closing balance	**92 143**	**262 592**	**354 735**
Non-current	–	46 498	**46 498**
Current	92 143	216 094	**308 237**
Current portion of provisions for the costs of disassembly of fixed assets and land restoration and other provisions			**58 219**
Total			**366 456**

Provision for use of real estate without contract

The Group companies recognize provisions for all claims filed by the owners of the real estate on which distribution systems and heat installations are located. As at 31 December 2017, the relevant provision amounted to PLN 92 030 thousand and was related to the following segments:

- Generation: PLN 50 930 thousand;
- Distribution: PLN 41 100 thousand.

In 2012, a third party lodged a claim against TAURON Ciepło S.A. (currently: TAURON Ciepło Sp. z o.o.) related to clarification of the legal status of the transmission equipment located on its property. The Company has questioned both the legitimacy of the claims and of the basis for offsetting their amounts against the current liabilities to the company arising from heat supplies. Consequently, the company went to court to recover its current receivables from the debtor. The amount of the potential claims of the aforesaid entity in respect of clarification of the legal status of the company's transmission equipment will be reviewed in the course of the proceedings. With regard to the dispute, in light of the adopted accounting policy, a provision has been recognized for the estimated cost of the above claim. Bearing in mind the pending litigation, in accordance with IAS 37.92, the Group does not disclose all information regarding the above issue as required by IAS 37 *Provisions, Contingent Liabilities and Contingent Assets.*

(in PLN '000)

Provisions for counterparty claims, court disputes and other provisions

Material provisions recognized as other provisions have been discussed below:

Item	Operating segment	Description	As at 31 December 2017	As at 31 December 2016
Provisions for penalties fixed by the contracts	Generation	Considering the risk that the two projects listed below will not be continued (their continuity is required under the subsidy contracts): • Construction of a biomass boiler in Elektrownia Jaworzno III; • Construction of a system of power generation from renewable sources in Stalowa Wola; In 2016 a provision has been recognised for the costs of returning the subsidy totalling PLN 52 297 thousand. The revalued provision as at 31 December 2017 amounted to PLN 55 358 thousand.	55 358	52 297
		Considering the risk that Polski Fundusz Rozwoju S.A. may terminate the agreement, as a result of TAURON Wytwarzanie S.A. withdrawal from the construction of a gas and steam unit in Elektrownia Łagisza in Będzin and the risk of accruing liquidated damages, in 2016 a provision totalling PLN 11 250 thousand was recognised. In the year ended 31 December 2017 as a result of a received debit note the provision was utilised in the amount of PLN 5 625 thousand. The remaining balance of the provision was derecognised.	–	11 250
Provision for a fine to the Energy Regulatory Office	Distribution	The provision was recognized due to the risk of violation of the Energy Law of 10 April 1997 by misleading the President of the Energy Regulatory Office, following their demand for information. In the year ended 31 December 2017, having received the decision of the President of the Energy Regulatory Office, a portion of the provision, totalling PLN 14 436 thousand, was reversed.	6 000	20 436
Provision for increased transmission easement charges	Distribution	The provision was recognized due to the risk of increased periodic charges for transmission easement related to energy infrastructure located within the Forestry Commission areas overseen by the Regional State Forest Directorate in Wrocław, following a the change of designation of the land from forestry to industrial. In the year ended 31 December 2017 the provision was increased by PLN 25 950 thousand.	47 650	21 700
Provision for real estate tax	Mining	Provision for proceedings regarding real property tax on undergrund structures. In the year ended on 31 December 2017, the company from the Mining segment used a provision of PLN 13 816 in connection with the tax authorities' decision determining the amount of tax liabilities for previous years and the company's correction of declarations for previous years.	3 446	23 008
	Distribution	Provision for the business risk regarding tax on real property classified as power grid assets. In the year ended 31 December 2017, the company from the Distribution segment increased the provision by PLN 27 356 thousand.	39 356	12 000
Provision for VAT	Sales	The provision was recognized in connection with pending inspection proceedings instituted by the Director of the Tax Inspection Office in Warsaw in relation to the value added tax. The duration of the proceedings was extended by the Director of the Tax Inspection Office a number of times. Currently, the new deadline for the completion of the inspection proceedings has been set for 28 April 2018. As at 31 December 2017, the provision was PLN 68 694 thousand. An increase in the provision by PLN 4 200 thousand is attributable to interest accrued for the year ended 31 December 2017.	68 694	64 494

(in PLN '000)

37. Accruals, Deferred Income and Government Grants

37.1. Deferred income and government grants

	As at 31 December 2017	As at 31 December 2016
Deferred income	**259 220**	**293 284**
Donations, subsidies received for the purchase or fixed assets received free-of-charge	62 342	71 849
Connection fees	195 666	218 075
Other	1 212	3 360
Government grants	**333 556**	**317 505**
Subsidies obtained from EU funds	235 065	211 981
Forgiven loans from environmental funds	26 258	28 068
Measurement of preferential loans	36 251	37 777
Other	35 982	39 679
Total	**592 776**	**610 789**
Non-current	541 318	553 874
Current	51 458	56 915

37.2. Accrued expenses

	As at 31 December 2017	As at 31 December 2016
Unused holidays	54 679	48 640
Bonuses	108 037	140 930
Environmental protection charges	45 133	3 806
Other	37 269	17 790
Total	**245 118**	**211 166**
Non-current	–	419
Current	245 118	210 747

38. Liabilities to Suppliers

Current liabilities to suppliers as at 31 December 2017 and 31 December 2016 are presented in the table below:

Operating segment	As at 31 December 2017	As at 31 December 2016
Distribution, including:	355 374	294 573
Polskie Sieci Elektroenergetyczne S.A.	*231 973*	*200 732*
Sales	265 660	247 487
Mining	172 758	144 722
Generation	164 980	100 857
Other	83 655	42 090
Total	**1 042 427**	**829 729**

39. Capital Commitments

Short-term capital commitments as at 31 December 2017 and 31 December 2016 are presented in the table below:

Operating segment	As at 31 December 2017	As at 31 December 2016
Distribution	438 492	336 624
Generation	227 084	511 403
Mining	74 682	159 138
Sales and other	57 046	26 639
Total	**797 304**	**1 033 804**

A drop in capital commitments in the Generation segment concerned mainly a decrease related to the construction of unit no. 910 in Jaworzno in the amount of PLN 249 640 thousand, which totalled PLN 208 844 thousand as at 31 December 2017. As at 31 December 2016, capital commitments totalled PLN 458 484 thousand.

(in PLN '000)

A drop in capital commitments in the Mining segment concerned mainly a decrease related to development of a longwall system in Zakład Górniczy Brzeszcze in the amount of PLN 89 080 thousand, which had been paid in whole as at 31 December 2017.

Long-term capital commitments have been presented in the consolidated statement of financial position within other financial liabilities. As at 31 December 2017, the related commitments totalled PLN 10 666. As at 31 December 2016, the related commitments amounted to PLN 299 thousand.

Commitments to incur capital expenditure

As at 31 December 2017 and 31 December 2016, the Group committed to incur expenditure on property, plant and equipment and intangible assets of PLN 3 891 230 thousand and PLN 4 368 685 thousand, respectively, with the key items presented below:

Operating segment	Agreement/investment project	As at 31 December 2017	As at 31 December 2016
Generation	Constructin new capacity in Jaworzno III Power Plant (910 MW)	2 277 479	2 835 269
Distribution	Construction of new electrical connections	594 627	622 415
	Modernization and reconstruction of existing networks	451 907	497 926
Mining	Construction of the "Grzegorz" shaft with the accompanying infrastructure and excavations	235 377	16 484
	Construction of the 800 m drift at Janina Mining Plant	112 065	19 578
	Investment Program in Brzeszcze Mining Plant	25 617	32 731

40. Liabilities arising from Taxes and Charges

	As at 31 December 2017	As at 31 December 2016
Corporate Income Tax	39 290	2 371
Personal Income Tax	54 161	51 084
Excise	43 760	41 549
VAT	110 867	98 114
Social security	190 443	170 039
Environmental charges	1 494	40 964
Other	12 577	6 822
Total	**452 592**	**410 943**

Tax Capital Group

A Tax Capital Group agreement for the years 2015–2017 was concluded on 22 September 2014. Pursuant to the previous agreement, TCG was registered for the period of three fiscal years from 2012 to 2014.

The major companies constituting the Tax Capital Group as from 1 January 2015 are: TAURON Polska Energia S.A., TAURON Wytwarzanie S.A., TAURON Dystrybucja S.A., TAURON Ciepło Sp. z o.o., TAURON Sprzedaż Sp. z o.o., TAURON Sprzedaż GZE Sp. z o.o., TAURON Obsługa Klienta Sp. z o.o., TAURON Ekoenergia Sp. z o.o., TAURON Wydobycie S.A. and Kopalnia Wapienia Czatkowice Sp. z o.o.

As at 31 December 2017, the Tax Capital Group had an income tax liability of PLN 37 629 thousand, constituting the surplus of the tax expense of the Tax Capital Group for 2017 of PLN 253 477 thousand over the income tax withholdings of the Tax Capital Group in 2017 totalling PLN 215 848 thousand.

On 30 October 2017 a relevant decision regarding the registration of the Tax Capital Group for the years 2018–2020 was given. Since 1 January 2018, the composition of the Tax Capital Group in the scope of significant companies has not changed with respect to those listed in the Tax Capital Group agreement for the years 2015–2017.

Regulations concerning VAT, corporate income tax and social insurance charges are frequently amended. The applicable regulations may also contain ambiguous issues, which lead to differences in opinions concerning the legal interpretation of tax legislation both among the tax authorities and between such authorities and enterprises.

Tax reports and other matters (e.g. customs or foreign currency transactions) may be audited by authorities competent to impose substantial penalties and fines, whereas any additional tax liabilities assessed during such audits have to be paid together with interest.

(in PLN '000)

Consequently, the figures presented and disclosed in these consolidated financial statements may change in the future if a final decision is issued by tax inspection authorities.

As of 15 July 2016, changes were introduced to the Tax Ordinance to incorporate the general anti-avoidance rule (GAAR), which is aimed to prevent the creation and use of artificial legal structures with a view to avoiding the payment of taxes in Poland. GAAR defines tax avoidance as an activity which is primarily intended to derive a tax benefit that is, in specific circumstances, in conflict with the scope and the objectives of the applicable tax law. The new regulations will require considerably more judgment in the assessment of the tax consequences of transactions.

GAAR should be applied to transactions made following its entry into force as well as transactions made prior to its implementation for which benefits continued or continue to be derived following the date of GAAR introduction.

41. Other Financial Liabilities

	As at 31 December 2017	As at 31 December 2016
Wages, salaries	203 544	156 867
Bid bonds, deposits and collateral received	86 233	79 415
Insurance contracts	3 246	12 560
Derivative instruments	14 184	560
Margin deposits	7 163	13 106
Other	71 389	66 161
Total	**385 759**	**328 669**
Non-current	91 620	72 374
Current	294 139	256 295

Derivative instruments have been discussed in Note 44.3 to these consolidated financial statements.

42. Other Current Non-Financial Liabilities

	As at 31 December 2017	As at 31 December 2016
Payments from customers relating to future periods	**309 298**	**298 606**
Amounts overpaid by customers	253 182	245 544
Prepayments for connection fees	16 741	21 369
Excess of the Company's Social Benefits Fund's liabilities over assets	91	–
Other	39 284	31 693
Other current non-financial liabilities	**1 552**	**2 573**
Total	**310 850**	**301 179**

(in PLN '000)

EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF CASH FLOWS

43. Significant Items of the Consolidated Statement of Cash Flows

43.1. Cash flows from operating activities

Changes in working capital

	Year ended 31 December 2017	Year ended 31 December 2016
Change in receivables	**(171 885)**	**(46 280)**
Change in receivables from buyers in statement of financial position	(138 748)	(64 032)
Change in other financial receivables	(28 132)	871
Change in receivables from disposal of property, plant and equipment and financial assets	(3 636)	529
Other adjustments	(1 369)	16 352
Change in inventories	**188 060**	**(55 731)**
Change in inventories in statement of financial position	190 657	(52 841)
Adjustment related to transfer of invetories to/from property, plant and equipment	(2 597)	(4 347)
Other adjustments	–	1 457
Change in payables excluding loans and borrowings	**233 303**	**156 247**
Change in liabilities to suppliers in statement of financial position	212 698	39 023
Change in payroll, social security and other financial liabilities	33 099	(1 536)
Change in non-financial liabilities in statement of financial position	9 671	27 257
Change in liabilities arising from taxes excluding income tax	4 730	64 280
Adjustment of VAT change related to capital commitments	(29 255)	50 570
Adjustment for the acquisition of an orgnanized part of the enterprise (ZCP Brzeszcze) and including new companies in consolidation	–	(24 610)
Other adjustments	2 360	1 263
Change in other non-current and current assets	**146 301**	**341 335**
Change in other current and non-current non-financial assets in statement of financial position	173 507	176 026
Change in receivables arising from taxes excluding income tax	(61 612)	47 050
Change in non-current and current gas emission allowances	(92 594)	(8 727)
Change in non-current and current energy certificates	239 369	218 347
Change in advance payments for property, plant and equipment and intangible assets	(110 152)	(84 372)
Other adjustments	(2 217)	(6 989)
Change in deferred income, government grants and accruals	**(29 351)**	**(140 063)**
Change in deferred income, government grants and accruals in statement of financial position	15 939	(82 746)
Adjustmet related to property, plant and equipment and intangible assets received free of charge	(9 413)	(18 919)
Adjustment related to subsidies received	(35 877)	(29 220)
Adjustment related to acquisition of orgnanized part of the enterprise (ZCP Brzeszcze)	–	(4 203)
Other adjustments	–	(4 975)
Change in provisions	**(153 977)**	**(28 173)**
Change of short term and long term provisions in statement of financial position	(139 479)	(169 061)
Adjustment related to actuarial gains/losses from provisions for post-employment benefits charged to other comprehensive income	19 653	204 597
Adjustment for the change in provisions for land reclamation and dismantling recognized under other comprehensive income	(33 212)	33 415
Adjustment related to acquisition of orgnanized part of the enterprise (ZCP Brzeszcze)	–	(92 454)
Other adjustments	(939)	(4 670)
Total	**212 451**	**227 335**

Income tax paid

Income taxes paid totalled PLN 143 217 thousand and included PLN 136 824 thousand relating to the Tax Capital Group and resulting from withholding income tax of PLN 215 848 thousand paid in the year ended 31 December 2017 as well as the TCG's receipt of overpaid income tax for the year 2016 in the amount of PLN 79 024 thousand.

(in PLN '000)

43.2. Cash flows from investing activities

Purchase of property, plant and equipment and intangible assets

	Year ended 31 December 2017	Year ended 31 December 2016
Purchase of property, plant and equipment	(3 243 046)	(3 590 348)
Purchase of intangible assets	(125 070)	(127 446)
Change in the balance of VAT – adjusted capital commitments	(196 878)	214 984
Change in the balance of advance payments	110 152	84 372
Costs of overhaul and internal manufacturing	(106 032)	(99 017)
Other	(884)	1 159
Total	**(3 561 758)**	**(3 516 296)**

Loans granted

Payments to grant loans result from the loans disbursed to Elektrociepłownia Stalowa Wola S.A., a jointly-controlled entity, in the total amount of PLN 304 192 thousand, and to PGE EJ 1 Sp. z o.o., in the amount of PLN 2 940 thousand.

Dividends received

Proceeds from dividends received in the amount of PLN 24 636 thousand concern mainly the dividends received by the Company from a jointly-controlled entity, TAMEH HOLDING Sp. z o.o., in the amount of PLN 15 500 thousand.

43.3. Cash flows from financing activities

Redemption of debt securities

Payments on the redemption of debt securities in the year ended 31 December 2017 resulted from the Parent's redemption of a tranche of bonds with the par value of PLN 1 650 000 thousand under a bond issue scheme of November 2015.

Loans and borrowings repaid

Payments to repay loans and borrowings of PLN 154 918 thousand disclosed in the consolidated statement of cash flows result mainly from the Parent's repayment of instalments of a loan obtained from the European Investment Bank in the amount of PLN 147 568 thousand in the year ended 31 December 2017.

Interest paid

	Year ended 31 December 2017	Year ended 31 December 2016
Interest paid in relation to debt securities	(246 790)	(296 949)
Interest paid in relation to loans and borrowings	(42 978)	(53 183)
Interest paid in relation to the finance lease	(727)	(955)
Total	**(290 495)**	**(351 087)**
investment expenditure	(105 945)	(95 971)
financial expenditure	(184 550)	(255 116)

The Group's consolidated statement of cash flows presents incurred borrowing costs which were capitalized in the current period in the value of assets as payments to acquire property, plant and equipment and intangible assets in cash flows from investing activities. In the year ended 31 December 2017, interest constituting borrowing costs which were capitalized in the value of property, plant and equipment and intangible assets amounted to PLN 105 945 thousand.

Issue of debt securities

Proceeds from the issue of debt securities in the year ended 31 December 2017 are related to:

- the issue of tranches of bonds with the total par value of PLN 600 000 thousand under a bond issue scheme of November 2015, which has been discussed in more detail in Note 32.2 to these consolidated financial statements;
- the issue of eurobonds totalling PLN 2 107 462 thousand, which has been discussed in more detail in Note 32.2 to these consolidated financial statements.

(in PLN '000)

FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

44. Financial Instruments

44.1. Carrying amount and fair value of financial instrument classes and categories

Categories and classes of financial assets	Note	As at 31 December 2017		As at 31 December 2016	
		Carrying amount	Fair value	Carrying amount	Fair value
1 Assets at fair value through profit or loss, held for trading		**106 292**		**45 092**	
Derivative instruments	**44.3**	4 934	4 934	19 776	19 776
Investment fund units	**24**	101 358	101 358	25 316	25 316
2 Financial assets available for sale		**144 417**		**134 143**	
Shares (non-current)	**24**	141 656		127 594	
Shares (current)	**24**	42		4 104	
Investment fund units	**24**	2 719	2 719	2 445	2 445
3 Loans and receivables		**2 734 059**		**2 241 033**	
Receivables from buyers	**27**	2 032 813	2 032 813	1 894 065	1 894 065
Deposits	**24**	39 756	39 756	38 472	38 472
Loans granted		580 979	491 171	256 117	153 429
Other financial receivables		80 511	80 511	52 379	52 379
4 Financial assets excluded from the scope of IAS 39		**499 204**		**461 348**	
Investments in joint ventures	**22**	499 204		461 348	
5 Derivative hedging instruments	**44.3**	**28 482**	**28 482**	**36 641**	**36 641**
6 Cash and cash equivalents	**29**	**909 249**	**909 249**	**384 881**	**384 881**
Total, of which in the statement of financial position:		**4 421 703**		**3 303 138**	
Non-current assets		**978 066**		**929 439**	
Investments in joint ventures		499 204		461 348	
Loans granted to joint ventures		240 767		240 951	
Other financial assets		238 095		227 140	
Current assets		**3 443 637**		**2 373 699**	
Receivables from buyers		2 032 813		1 894 065	
Loans granted to joint ventures		329 665		15 116	
Other financial assets		171 910		79 637	
Cash and cash equivalents		909 249		384 881	

Categories and classes of financial liabilities	Note	As at 31 December 2017		As at 31 December 2016	
		Carrying amount	Fair value	Carrying amount	Fair value
1 Financial liabilities at fair value through profit or loss, held for trading		**14 184**		**560**	
Derivative instruments	**44.3**	14 184	14 184	560	560
2 Financial liabilities measured at amortized cost		**12 040 129**		**11 136 323**	
Preferential loans	**32.1**	34 506	34 506	41 748	41 748
Arm's length loans	**32.1**	1 063 379	1 065 694	1 206 649	1 209 558
Bank overdrafts	**32.1**	93 503	93 503	15 156	15 156
Bonds issued	**32.2**	8 637 435	8 695 096	7 681 128	7 719 015
Liabilities to suppliers	**38**	1 042 427	1 042 427	829 729	829 729
Other financial liabilities		154 119	154 119	158 383	158 383
Capital commitments	**39**	807 970	807 970	1 034 103	1 034 103
Salaries and wages		203 544	203 544	156 867	156 867
Insurance contracts		3 246	3 246	12 560	12 560
3 Liabilities under guarantees, factoring and excluded from the scope of IAS 39		**23 973**		**34 848**	
Obligations under finance leases	**32.3**	23 973	23 973	34 848	34 848
Total, of which in the statement of financial position:		**12 078 286**		**11 171 731**	
Non-current liabilities		**9 593 034**		**8 832 163**	
Debt		9 501 414		8 759 789	
Other financial liabilities		91 620		72 374	
Current liabilities		**2 485 252**		**2 339 568**	
Debt		351 382		219 740	
Liabilities to suppliers		1 042 427		829 729	
Capital commitments		797 304		1 033 804	
Other financial liabilities		294 139		256 295	

(in PLN '000)

Derivative financial instruments classified as assets and liabilities measured at fair value through profit or loss and designated as hedging instruments, which are measured at fair value as at the end of the reporting period, were measured in line with the method described in Note 44.3 to these consolidated financial statements. Fair value hierarchy disclosures are also provided in Note 44.3. Measurement of investment fund units has been classified to Level 1 in the fair value hierarchy.

Financial instruments classified to other categories of financial instruments:

- As at 31 December 2017, fixed-rate financial instruments, which included loans obtained from the European Investment Bank, subordinated bonds, eurobonds and bonds issued by a subsidiary, were measured at fair value. The fair value measurement also included subordinated loans and loans for repayment of debt granted to Elektrociepłownia Stalowa Wola S.A., exposed to the variable interest rate. The fair value measurement was carried out based on the present value of future cash flows discounted using an interest rate applicable currently to a given bond or loan, i.e. applying market interest rates. The measurement resulted in Level 2 classification in fair value hierarchy.
- The fair value of other financial instruments (except shares classified as financial assets available for sale and excluded from the scope of IAS 39 *Financial Instruments: Measurement and Recognition*, as described below) as at 31 December 2017 and 31 December 2016 did not significantly differ from their values presented in the financial statements for the respective periods, due to the following reasons:
  - the potential discounting effect relating to short-term instruments is not significant;
  - the instruments are related to arm's length transactions.

  Consequently, the fair value of the instruments in question has been disclosed in the tables above at the carrying amount.
- The Group does not disclose the fair value of shares in companies not quoted on active markets, categorized to financial assets available for sale. They are measured at cost less impairment losses as at the end of the reporting period. Following the adoption of IFRS 9 *Financial Instruments* as from 1 January 2018, the Group estimated the fair value of the above shares as at that date, which has been discussed in more detail in Note 7 to these consolidated financial statements. Interest in joint ventures – financial assets excluded from the scope of IAS 39 *Financial Instruments: Recognition and Measurement* – are measured using the equity method in line with the accounting policies adopted by the Group.

44.2. Revenue, expenses, gain and loss items included in the statement of comprehensive income by category of financial instruments

For the year ended 31 December 2017

	Assets/ liabilities at fair value through profit or loss, held for trading	Financial assets available for sale	Loans and receivables	Financial liabilities at amortized cost	Hedging instruments	Financial assets/ liabilities excluded from the scope of IAS 39	Total
Dividends and shares in profits	–	9 136	–	–	–	–	**9 136**
Interest income / (expense)	20 318	–	26 713	(209 885)	1 525	(727)	**(162 056)**
Currency translation differences	(2 688)	–	1 692	128 386	–	–	**127 390**
Impairment / revaluation	(11 820)	732	(117)	–	–	(229)	**(11 434)**
Commission relating to borrowings and debt securities	–	–	–	(19 020)	–	–	**(19 020)**
Gain/ (loss) on disposal of investments	–	–	(803)	–	–	–	**(803)**
Other	(4 866)	(103)	–	–	–	–	**(4 969)**
Net financial income (costs)	**944**	**9 765**	**27 485**	**(100 519)**	**1 525**	**(956)**	**(61 756)**
Revaluation	(13 514)	–	(25 170)	–	–	–	**(38 684)**
Gain/loss on exercised commodity derivative instruments	8 737	–	–	–	–	–	**8 737**
Net operating income/(costs)	**(4 777)**	**–**	**(25 170)**	**–**	**–**	**–**	**(29 947)**
Remeasurement	–	–	–	–	(8 159)	–	**(8 159)**
Other comprehensive income	**–**	**–**	**–**	**–**	**(8 159)**	**–**	**(8 159)**

(in PLN '000)

For the year ended 31 December 2016

	Assets/ liabilities at fair value through profit or loss, held for trading	Financial assets available for sale	Loans and receivables	Financial liabilities at amortized cost	Hedging instruments	Financial assets/ liabilities excluded from the scope of IAS 39	Total
Dividends and shares in profits	–	5 728	–	–	–	–	**5 728**
Interest income / (expense)	7 412	–	27 902	(177 949)	(80 658)	(957)	**(224 250)**
Currency translation differences	(2 088)	–	183	(28 356)	–	–	**(30 261)**
Impairment / revaluation	14 495	(203)	(603)	–	–	–	**13 689**
Commission relating to borrowings and debt securities	–	–	–	(18 767)	–	–	**(18 767)**
Gain/ (loss) on disposal of investments	–	2 114	(416)	–	–	–	**1 698**
Other	(43)	–	–	–	–	–	**(43)**
Net financial income (costs)	**19 776**	**7 639**	**27 066**	**(225 072)**	**(80 658)**	**(957)**	**(252 206)**
Revaluation	15 982	–	(22 943)	–	–	–	**(6 961)**
Gain/loss on exercised commodity derivative instruments	(34 365)	–	–	–	–	–	**(34 365)**
Net operating income/(costs)	**(18 383)**	**–**	**(22 943)**	**–**	**–**	**–**	**(41 326)**
Remeasurement	–	–	–	–	127 252	–	**127 252**
Other comprehensive income	**–**	**–**	**–**	**–**	**127 252**	**–**	**127 252**

44.3. Derivative instruments

	As at 31 December 2017				As at 31 December 2016			
	Charged to profit or loss	Charged to other comprehensive income	Total		Charged to profit or loss	Charged to other comprehensive income	Total	
			Assets	Liabilities			Assets	Liabilities
CCIRS	(9 299)	–	**–**	**(9 299)**	–	–	**–**	**–**
IRS	23	28 459	**28 482**	**–**	23	36 618	**36 641**	**–**
Commodity forwards/futures	395	–	**4 934**	**(4 539)**	15 999	–	**16 559**	**(560)**
Currency forwards	(346)	–	**–**	**(346)**	3 217	–	**3 217**	**–**
Total			**33 416**	**(14 184)**			**56 417**	**(560)**
Non-current			26 445	(4 958)			35 814	–
Current			6 971	(9 226)			20 603	(560)

The fair value of individual derivative instruments is determined as follows:

Derivative instrument	Methodology of determining fair value hierarchy
IRS	Difference between the discounted interest cash flows based on the floating and fixed interest rates. Reuters' interest rate curve is the input data.
CCIRS	Difference between the discounted interest cash flows of the payable and receivables streams, in two various currencies, denominated in the measurement currency. Reuters' interest rate curve, basis spreads and NBP fixing for relevant currencies are the input data.
Forward currency contracts	Difference between the discounted future cash flows between the future price as at the valuation date and the transaction price multiplied by the par value of the FX contract. Reuter's NBP fixing and the interest rate curve implied from fx swap transaction for a relevant currency is the input data.
Commodity forwards, futures	The fair value of forwards for the purchase and sale of emission allowances, electricity and other commodities is based on prices quoted on an active market or based on cash flows being the difference between the price reference index (forward curve) and the contract price.

(in PLN '000)

The fair value hierarchy for derivative financial instruments was as follows:

	As at 31 December 2017		As at 31 December 2016	
	Level 1	Level 2	Level 1	Level 2
Assets				
Commodity – related derivatives	4 934	–	16 559	–
Derivative instruments – currency	–	–	–	3 217
Derivative instruments – IRS	–	28 482	–	36 641
Total	**4 934**	**28 482**	**16 559**	**39 858**
Liabilities				
Commodity – related derivatives	4 539	–	560	–
Currency derivatives	–	346	–	–
Derivative instruments – CCIRS	–	9 299	–	–
Total	**4 539**	**9 645**	**560**	**–**

Hedging derivative instruments (subject to hedge accounting) – IRS

In the year ended 31 December 2016, based on a decision of the Financial and Credit Risk Management Unit, the Company hedged a portion of its interest rate risk for cash flows relating to the exposure to WIBOR 6M, designated under the dynamic risk management strategy, i.e. interest on debt securities with the nominal value of PLN 2 100 000 thousand, through the entry into interest rate swap (IRS) transactions for a term of 4 to 5 years. The aforementioned transactions are subject to hedge accounting with the exception of the first interest period. This is due to the fact that the floating interest rate in the first interest period was determined in advance, hence the Company could not apply hedge accounting principles to cash flows resulting from the first interest period.

Derivative instruments measured at fair value through profit or loss (FVTPL)

As at 31 December 2017, derivative instruments which did not fall within the scope of hedge accounting and were classified as financial assets or financial liabilities measured at fair value through profit or loss comprised:

- CCIRSs that hedge foreign currency cash flows resulting from the payment of interest on the issued eurobonds;
- commodity derivatives (futures, forward) including emission allowance and other commodity purchase and sale transactions;
- FX forward transactions hedging foreign currency cash flows resulting from the Company's operations.

The CCIRSs have been used with respect to the Company's Coupon Only Cross Currency Swap fixed-fixed transactions concluded in November and December 2017 and involve an exchange of interest payments on the total nominal value of EUR 300 000 thousand. They mature in July 2027. In accordance with the terms and conditions, the Company pays interest accrued based on a fixed interest rate in PLN and receives fixed interest-rate payments in EUR. Hedge accounting principles do not apply to the transaction in question.

45. Principles and Objectives of Financial Risk Management

Risks related to financial instruments which the TAURON Group is exposed to, including a description of the exposure and the risk management method:

(in PLN '000)

Risk exposure	Risk management	Regulation
Credit risk		
Possible loss resulting from the counterparty default on contractual obligations. The credit exposure involves a default risk (the amount that may be lost if a counterparty defaults on its obligations) and a replacement risk (the amount that may be lost if a delivery is not made or a service is not proviced).	Credit risk is managed through the control of the credit exposure at the time when companies in the TAURON Group sign contracts. As a rule, before a contract is signed, every entity is examined in terms of their financial position and is assigned a limit which determines the maximum exposure allowed. The credit exposure in this case is understood as the amount which may be lost, if the counterparty defaults on their obligations at a given time (considering the value of security they have lodged). The credit exposure is calculated at a given day and comprises a default risk and replacement risk. The Group has a decentralized credit risk management system in place, however, the control, mitigation and reporting are managed centrally at a Company-wide level. The TAURON Group's Credit Risk Management Policy sets out the credit risk management procedures for the entire Group with the view to reduce the impact of the risk on the Group's objectives. The value of the credit risk that the TAURON Group is exposed to, is calculated using the Credit Value at Risk method, based on the value of the exposure and the evaluation of the financial condition of individual customers. This is an analytical method which, using a mathematical simulation model, calculates the value exposed to the risk based on the total loss probability distribution.	Credit risk management policy for the TAURON Group
Liquidity risk		
Possible loss or limitation of the ability to make payments on a day-to-day basis due to an inappropriate volume or structure of liquid assets as compared to current liabilities or an insufficient level of the actual net proceeds from operating activities.	The TAURON Group's liquidity is reviewed on an ongoing basis to detect any deviation from plans and the availability of external sources of funds, in the case of which the amount materially exceeds the expected short-term demand, mitigates the liquidity risk. To this end the Company applies the rules of determining the liquidity position both of individual companies and the entire TAURON Group which helps ensure funds that would cover any potential liquidity gaps by allocating funds between companies (cash-pooling) as well as using external financing, including overdraft facilities.	Liquidity management policy for the TAURON Group
Market risk – interest rate and currency risks		
The possibility of an adverse effect on the Group's performance through fluctuations in the fair value of financial instruments or the related future cash flows, driven by changes in interest rates or foreign exchange rates.	The TAURON Group manages the currency and interest rate risks in line with the best market practices. The key objective of such risk management is to minimize the cash flow sensitivity of the TAURON Group to financial risks and to minimize finance cost and costs of hedging with the use of derivative instruments. Wherever possible and commercially viable, the TAURON Group uses derivative instruments, whose nature allows for the application of hedge accounting.	Financial risk management policy for the TAURON Group
Market risk – price risk		
Unplanned volatility of the operating profit/loss of the TAURON Group resulting from fluctuations of prices in the commodity markets and deviations in volumes in individual areas of commercial activities of the TAURON Group.	Effective management is ensured by a commercial risk management system linked in terms of organization and information with the TAURON Group's strategy of hedging trading positions. The policy has introduced an early-warning system and risk-exposure limiting system in various trading areas. The basic operational measure of the market risk at the TAURON Group is the Value at Risk measure which determines the maximum allowed change in the value of the position over a given time period and with a given probability.	Commercial risk management policy for the TAURON Group

45.1. Credit risk

Key classes of financial instruments that give rise to credit risk exposure have been presented in the table below. The maximum credit risk exposure related to financial assets of the TAURON Group equals their carrying amounts.

Classes of financial instruments	As at 31 December 2017	As at 31 December 2016
Receivables from buyers	2 032 813	1 894 065
Cash and cash equivalents	909 249	384 881
Loans granted	580 979	256 117
Deposits	39 756	38 472
Other financial receivables	80 511	52 379

(in PLN '000)

45.1.1. Credit risk related to receivables from buyers

The Group has receivables from two groups of buyers: institutional and individual clients. The percentage share of individual groups in the total amount of receivables from buyers has been presented below:

	As at 31 December 2017	As at 31 December 2016
Institutional clients	70.25%	73.33%
Individual clients	29.75%	26.67%
Total	**100%**	**100%**

No material concentration of credit risk related to the core activity occurs in the Group. Amounts due from PSE S.A. constitute the largest item of receivables from buyers with a share of 4.78% and 4.77% as at 31 December 2017 and 31 December 2016, respectively.

Sales to institutional clients are made only to buyers who have undergone an appropriate verification procedure. As a result, the management believes that there is no additional credit risk that would exceed the allowance for bad debts recognized for trade receivables of the Group.

The ageing analysis of receivables from buyers as well as information on allowances/write-downs on receivables from buyers have been presented in Note 27 to these consolidated financial statements.

45.1.2. Credit risk related to other financial receivables

The Group has receivables from two groups of buyers: institutional and individual clients. The percentage share of each group in the total amount of other financial receivables has been presented below:

	As at 31 December 2017	As at 31 December 2016
Institutional clients	97.61%	93.85%
Individual clients	2.39%	6.15%
Total	**100%**	**100%**

No material concentration of credit risk related to other financial receivables occurs in the Group. Amounts due from Izba Rozliczeniowa Giełd Towarowych S.A. constitute the largest item of other financial receivables with a share of 15.48% and 16.17% as at 31 December 2017 and 31 December 2016, respectively.

The ageing analysis of and allowances/write-downs on other financial receivables have been presented below.

Ageing analysis of other financial receivables as at 31 December 2017 year

	Not past due	Past due					Total
		<30 days	30–90 days	90–180 days	180–360 days	>360 days	
Value of item before allowance/write-down	78 886	2 007	10 055	937	937	66 165	**158 987**
Allowance/write-down	(820)	(108)	(9 734)	(749)	(919)	(66 146)	**(78 476)**
Net Value	**78 066**	**1 899**	**321**	**188**	**18**	**19**	**80 511**

Ageing analysis of other financial receivables as at 31 December 2016 year

	Not past due	Past due					Total
		<30 days	30–90 days	90–180 days	180–360 days	>360 days	
Value of item before allowance/write-down	51 647	439	268	263	527	56 228	**109 372**
Allowance/write-down	(346)	(10)	(14)	(54)	(380)	(56 189)	**(56 993)**
Net Value	**51 301**	**429**	**254**	**209**	**147**	**39**	**52 379**

(in PLN '000)

Allowances/write-downs on other financial receivables

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**(56 993)**	**(2 524)**
Recognised	(13 149)	(2 017)
Utilized	551	473
Reversed	4 087	7 721
Other movements	(12 972)	(60 646)
Closing balance	**(78 476)**	**(56 993)**

45.1.3. Credit risk related to cash and cash equivalents

The Group manages credit risk related to cash by diversifying banks where it deposits its cash surplus. All entities the Group concludes deposit transactions with operate in the financial sector. They include high-rating banks with sufficient equity and stable, strong market position.

As at 31 December 2017, the share of three banks where the Group's largest cash balances were deposited was 78%.

45.1.4. Credit risk related to loans granted

Loans granted include mainly loans to joint ventures. The loans in question had not been overdue as at the end of the reporting period. The key item is a subordinated loan whose carrying amount is PLN 212 052 thousand and whose repayment is secured by a blank promissory note, including a promissory note agreement, as well as loans granted under agreements consolidating the borrower's debt with the total carrying amount of PLN 329 665 thousand, the repayment of which is secured by blank promissory notes and related declarations. On the balance sheet date, the Group performed impairment tests for its assets, including the value of loans granted to a joint venture, which did not reveal the necessity to recognise impairment losses on those loans.

45.2. Liquidity risk

The Group maintains a balance between continuity and flexibility of funding through the use of a variety of funding sources, such as overdraft facilities, bank loans, other loans, bonds and finance leases. Such use of the funding sources enables liquidity risk management and effective mitigation of its negative effects.

In order to minimize the possibility of cash flow disruption and liquidity risk, the TAURON Group, as in previous years, used the cash pooling mechanism. Regardless of funds collected by its individual members, cash pooling is linked to a flexible credit facility in the form of an overdraft. Under the cash pooling agreement, the Company may use external financing in the form of an overdraft of up to PLN 300 000 thousand and an intraday limit of up to PLN 500 000 thousand.

Apart from the overdraft made available under the cash pooling agreement, the Group may use foreign currency overdrafts:

- up to USD 2 000 thousand, with the outstanding amount of USD 418 thousand as at the end of the reporting period;
- up to EUR 45 000 thousand, with the outstanding amount of EUR 22 069 thousand as at the end of the reporting period.

The following tables present the Group's financial liabilities based on non-discounted contractual payments by maturity as at 31 December 2017 and 31 December 2016.

(in PLN '000)

Financial liabilities as at 31 December 2017

Classes of financial instruments	Carrying amount	Non-discounted contractual payments	of which non-discounted contractual payments maturing within (*after the balance sheet date*)					
			less than 3 months	3–12 months	1–2 years	2–3 years	3–5 years	more than 5 years
Financial liabilities other than derivative instruments								
Interest-bearing loans and borrowings and issued bonds	**9 828 823**	**(12 205 838)**	(160 573)	(418 356)	(2 329 557)	(2 195 729)	(991 898)	(6 109 725)
Liabilities to suppliers	**1 042 427**	**(1 042 427)**	(1 038 477)	(3 950)	–	–	–	–
Capital commitments	**807 970**	**(807 970)**	(797 210)	(93)	(10 599)	(68)	–	–
Other financial liabilities	**360 909**	**(360 909)**	(281 066)	(3 849)	(12 503)	(47 138)	(6 050)	(10 303)
Obligations under finance leases	**23 973**	**(24 173)**	(1 475)	(22 670)	(2)	(2)	(4)	(20)
Derivative financial liabilities								
Derivate instruments – commodity	**4 539**	**(4 424)**	–	(4 424)	–	–	–	–
Derivative instruments – currency	**346**	**(346)**	(275)	(71)				
Derivate instruments – CCIRS	**9 299**	**(47 125)**	–	(4 694)	(4 694)	(4 748)	(9 427)	(23 562)
Total	**12 078 286**	**(14 493 212)**	**(2 279 076)**	**(458 107)**	**(2 357 355)**	**(2 247 685)**	**(1 007 379)**	**(6 143 610)**

Financial liabilities as at 31 December 2016

Classes of financial instruments	Carrying amount	Non-discounted contractual payments	of which non-discounted contractual payments maturing within (*after the balance sheet date*)					
			less than 3 months	3–12 months	1–2 years	2–3 years	3–5 years	more than 5 years
Financial liabilities other than derivative instruments								
Interest-bearing loans and borrowings and issued bonds	**8 944 681**	**(11 054 364)**	(69 029)	(405 917)	(452 691)	(2 296 657)	(3 680 323)	(4 149 747)
Liabilities to suppliers	**829 729**	**(829 729)**	(829 693)	(36)	–	–	–	–
Capital commitments	**1 034 103**	**(1 034 103)**	(1 033 711)	(93)	(113)	(113)	(73)	–
Other financial liabilities	**327 810**	**(327 810)**	(245 697)	(10 038)	(14 069)	(4 567)	(40 789)	(12 650)
Obligations under finance leases	**34 848**	**(35 772)**	(5 313)	(6 713)	(23 718)	(2)	(4)	(22)
Derivative financial liabilities								
Derivate instruments – commodity	**560**	**(538)**	–	(538)	–	–	–	–
Total	**11 171 731**	**(13 282 316)**	**(2 183 443)**	**(423 335)**	**(490 591)**	**(2 301 339)**	**(3 721 189)**	**(4 162 419)**

45.3. Market risk

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

- interest rate risk;
- currency risk;
- raw material and commodity price risk related to commodity derivative instruments and price risk related to units held by the Group.

45.3.1. Interest rate risk

The Group's interest rate risk results mainly from debt, concluded IRS contracts, cash and loans granted to joint ventures.

Due to floating-rate items the Group is exposed to cash flow changes resulting from interest rate fluctuations. As a result of fixed-rate items the Group is exposed to changes in the fair value of items measured at amortized cost. The risk of fair value changes resulting from interest rate changes also relates to IRS contracts. The Group is also exposed to the risk of lost benefits related to a decrease in interest rates in the case of fixed-rate debt or to an increase in interest rates in the case of fixed-rate assets, although the changes are not disclosed in the financial statements.

In order to hedge interest rate risk related to floating-rate bonds issued, the Group entered into interest rate swap (IRS) contracts, which has been discussed in more detail in Note 44.3 to these consolidated financial statements.

The carrying amounts of financial instruments of the Group exposed to the interest rate risk have been presented in the tables below. Except the hybrid bonds issued in December 2016 with fixed interest in the first funding period and the eurobonds issued in July 2017, other bonds issued by the Parent bear floating interest. As the Company has adopted a dynamic financial risk management strategy where the hedged item are cash flows relating to the exposure to the floating WIBOR 6M interest rate, the interest rate risk for a portion of interest cash flows has been reduced by the hedging IRS transactions. Thus, a portion of the carrying amount of bonds with interest cash flow fluctuations hedged with interest rate swaps has been presented in the tables below together with valuation of these hedging instruments as fixed-rate items.

(in PLN '000)

Financial instruments by interest rate type as at 31 December 2017

Financial instruments	Fixed interest rate	Floating interest rate	Total
Financial assets			
Deposits	39 756	–	**39 756**
Loans granted	2 954	578 025	**580 979**
Cash and cash equivalents	–	909 249	**909 249**
Derivative instruments – IRS	28 482	–	**28 482**
Financial liabilities			
Bank overdrafts	1	93 502	**93 503**
Preferential loans	–	34 506	**34 506**
Arm's length loans	1 042 110	21 269	**1 063 379**
Bonds issued	5 681 480	2 955 955	**8 637 435**
Obligations under finance leases	27	23 946	**23 973**
Derivative instruments – CCIRS	9 299	–	**9 299**

Financial instruments by interest rate type as at 31 December 2016

Financial instruments	Fixed interest rate	Floating interest rate	Total
Financial assets			
Deposits	–	38 472	**38 472**
Loans granted	–	256 117	**256 117**
Cash and cash equivalents	–	384 881	**384 881**
Derivative instruments – IRS	36 641	–	**36 641**
Financial liabilities			
Bank overdrafts	–	15 156	**15 156**
Preferential loans	–	41 748	**41 748**
Arm's length loans	1 190 501	16 148	**1 206 649**
Bonds issued	3 677 088	4 004 040	**7 681 128**
Obligations under finance leases	141	34 707	**34 848**

Interest rate of floating-rate financial instruments is updated on a regular basis, more frequently than once a year. Interest on fixed-rate financial instruments is fixed throughout the entire term to maturity or until a specified point in time where the interest rates are verified and may be changed – this applies to loans from the European Investment Bank as well as hybrid bonds, which bear fixed interest in the first period and floating interest in the second period, which has been discussed in more detail in Notes 32.1 and 32.2 to these consolidated financial statements.

Sensitivity analysis

The analysis of sensitivity to changes in market risk factors is conducted by means of a scenario analysis. The Group relies on expert scenarios reflecting its judgment concerning the behaviour of individual market risk factors in the future. The scope of the analysis includes only those items which meet the IFRS definition of financial instruments.

The interest rate risk sensitivity analysis is conducted by the Group using the parallel shift in the yield curve by the potential change in reference interest rates within a horizon until the date of the next financial statements. The interest rate risk sensitivity analysis has been carried out based on average reference interest rates in the year. The scale of potential changes in interest rates has been estimated on the basis of implied volatility for interest rate options quoted on the interbank market for currencies which expose the Group to the interest rate risk as at the end of the reporting period.

The Group identifies its exposure to the risk of changes in WIBOR, EURIBOR and LIBOR USD interest rates. As at 31 December 2017, its exposure to the risk of changes in LIBOR USD was immaterial, while the sensitivity analysis performed as at 31 December 2016 did not focus on changes in EURIBOR and LIBOR USD as their effect was considered insignificant. Debt to be repaid in the euro, except an overdraft facility, bears fixed interest. The tables below present sensitivity of the gross profit/loss as well as other comprehensive income (gross) of the Group to reasonably possible changes in interest rates within a horizon until the date of the next financial statements, assuming that all other risk factors remain unchanged.

(in PLN '000)

For the year ended 31 December 2017

Classes of finacial instruments	31 December 2017		Sensitivity analysis for interest rate risk as at 31 December 2017			
			WIBOR		EURIBOR	
	Carrying amount	Value at risk	WIBOR + 43 bp	WIBOR - 43 bp	EURIBOR + 1 bp	EURIBOR - 1 bp
			Profit or loss / other comprehensive income		*Profit or loss*	
Loans granted	580 979	578 025	2 486	(2 486)	–	–
Cash and cash equivalents	909 249	909 249	3 790	(3 790)	1	(1)
Derivatives (assets)	33 416	28 482	21 217	(21 217)	–	–
Bank overdrafts	93 503	93 502	–	–	(9)	9
Preferential loans	34 506	34 506	(148)	148	–	–
Arm's length loans	1 063 379	21 269	(91)	91	–	–
Issued bonds	8 637 435	5 053 775	(21 731)	21 731	–	–
Obligations under finance leases	23 973	23 946	(103)	103	–	–
Derivatives (liabilities)	14 184	9 299	5 995	(5 995)	(146)	146
Total			**11 415**	**(11 415)**	**(154)**	**154**

The exposure to risk as at 31 December 2017 is representative for the Group's exposure to risk during the annual period preceding the aforementioned date, except for material transactions made at the end of 2017. They concern derivative instruments (liabilities), including CCIRS transactions entered into by the Company in November and December 2017, which are sensitive to both changes in WIBOR and EURIBOR rates. CCIRS instruments have been discussed in more detail in Note 44.3 to these consolidated financial statements.

For the year ended 31 December 2016

Classes of finacial instruments	31 December 2016		Sensitivity analysis for interest rate risk as at 31 December 2016	
			WIBOR	
	Carrying amount	Value at risk	WIBOR + 60 bp	WIBOR -60 bp
			Profit or loss / other comprehensive income	
Deposits	38 472	38 472	231	(231)
Loans granted	256 117	256 117	1 537	(1 537)
Cash and cash equivalents	384 881	384 881	1 995	(1 995)
Derivatives (assets)	56 417	36 641	40 992	(40 992)
Preferential loans	41 748	41 748	(250)	250
Arm's length loans	1 206 649	16 148	(97)	97
Issued bonds	7 681 128	6 101 108	(36 607)	36 607
Obligations under finance leases	34 848	34 707	(208)	208
Total			**7 593**	**(7 593)**

The exposure to risk as at 31 December 2016 is representative for the Group's exposure to risk during the annual period preceding the aforementioned date.

45.3.2. Currency risk

The TAURON Group companies are exposed to transaction and translation currency risk. The Group companies are exposed to the risk of EUR/PLN, CZK/PLN, USD/PLN and GBP/PLN exchange rate changes in relation to their operating and financing activities. The Group's exposure to currency risk by financial instrument class in 2017 and in 2016 has been presented below.

(in PLN '000)

Currency position as at 31 December 2017

Classes of financial instruments	Total carrying amount in PLN	EUR		CZK		USD		GBP	
		in currency	in PLN	in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets									
Receivables from buyers	2 032 813	1 016	4 237	46 722	7 625	–	–	–	–
Other financial receivables	80 511	3 321	13 851	20 607	3 363	–	–	–	–
Cash and cash equivalents	909 249	3 321	13 851	64 963	10 602	314	1 093	485	2 280
Derivatives (assets)	33 416	1 169	4 877	–	–	16	57	–	–
Total		**8 827**	**36 816**	**132 292**	**21 590**	**330**	**1 150**	**485**	**2 280**
Financial liabilities									
Bank overdrafts	93 503	22 069	92 048	–	–	418	1 454	–	–
Issued bonds	8 637 435	859 205	3 583 657	–	–	–	–	–	–
Liabilities to suppliers	1 042 427	2 117	8 830	10 208	1 666	3	10	1	5
Other financial liabilities	154 119	1 717	7 162	6	1	–	–	–	–
Derivatives (liabilities)	14 184	1 061	4 425	–	–	33	114	–	–
Total		**886 169**	**3 696 122**	**10 214**	**1 667**	**454**	**1 578**	**1**	**5**
Net currency position		**(877 342)**	**(3 659 306)**	**122 078**	**19 923**	**(124)**	**(428)**	**484**	**2 275**

Currency position as at 31 December 2016

Classes of financial instruments	Total carrying amount in PLN	EUR		CZK		USD		GBP	
		in currency	in PLN	in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets									
Receivables from buyers	1 894 065	937	4 143	42 645	6 981	–	–	–	–
Other financial receivables	52 379	342	1 515	20 605	3 373	–	–	–	–
Cash and cash equivalents	384 881	7 456	32 986	95 406	15 618	306	1 280	499	2 566
Derivatives (assets)	56 417	3 649	16 143	–	–	100	416	–	–
Total		**12 384**	**54 787**	**158 656**	**25 972**	**406**	**1 696**	**499**	**2 566**
Financial liabilities									
Bank overdrafts	15 156	3 032	13 415	–	–	410	1 716	–	–
Issued bonds	7 681 128	357 147	1 580 020	–	–	–	–	–	–
Liabilities to suppliers	829 729	1 839	8 137	10 073	1 649	12	49	–	–
Other financial liabilities	158 383	2 961	13 097	–	–	94	395	2	10
Derivatives (liabilities)	560	122	538	–	–	5	22	–	–
Total		**365 101**	**1 615 207**	**10 073**	**1 649**	**521**	**2 182**	**2**	**10**
Net currency position		**(352 717)**	**(1 560 420)**	**148 583**	**24 323**	**(115)**	**(486)**	**497**	**2 556**

In 2017 and in 2016, in line with its currency risk management strategy, the TAURON Group used forward contracts as hedges against currency risk related to its operations. The Group did not use hedge accounting to hedge currency risk. As at 31 December 2017, liabilities arising from valuation of FX forwards held by the Group amounted to PLN 346 thousand (versus assets of PLN 3 217 thousand as at 31 December 2016).

In the year ended 31 December 2017, the Company entered into CCIRS transactions, whose fair value measurement is exposed to the risk of changes in the EUR/PLN exchange rate. These transactions are not subject to hedge accounting. As at 31 December 2017, the amount from valuation of CCIRS was PLN (9 299) thousand, which has been discussed in more detail in Note 44.3 to these consolidated financial statements.

Sensitivity analysis

The analysis of sensitivity to changes in market risk factors is conducted by means of a scenario analysis. The Group relies on expert scenarios reflecting its judgment concerning the behaviour of individual market risk factors in the future. The scope of the analysis includes only those items which meet the IFRS definition of financial instruments.

The potential changes in foreign exchange rates have been determined within a horizon until the date of the next financial statements and calculated on the basis of annual implied volatility for FX options quoted on the interbank market for a given currency pair as at the end of the reporting period or, in the absence of quoted market prices, on the basis of historical volatility for a period of one year preceding the end of the reporting period.

The Group identifies its exposure to currency risk related to EUR/PLN, CZK/PLN, USD/PLN and GBP/PLN exchange rates. The tables below present sensitivity of the gross profit/loss as well as other comprehensive income (gross) of the Group to reasonably possible changes in foreign exchange rates within a horizon until the date of the next financial statements, assuming that all other risk factors remain unchanged.

(in PLN '000)

For the year ended 31 December 2017

Classes of finacial instruments	31 December 2017		Sensitivity analysis for currency risk as at 31 December 2017							
			EUR/PLN		CZK/PLN		USD/PLN		GBP/PLN	
	Carrying amount	Value at risk	exchange rate EUR/PLN +6.2%	exchange rate EUR/PLN -6.2%	exchange rate CZK/PLN +6.34%	exchange rate CZK/PLN -6.34%	exchange rate USD/PLN +9.76%	exchange rate USD/PLN -9.76%	exchange rate GBP/PLN +9.35%	exchange rate GBP/PLN -9.35%
			Profit or loss / other comprehensive income		*Profit or loss / other comprehensive income*		*Profit or loss / other comprehensive income*		*Profit or loss / other comprehensive income*	
Receivables from buyers	2 032 813	11 862	263	(263)	483	(483)	–	–	–	–
Other financial receivables	80 511	17 214	859	(859)	213	(213)	–	–	–	–
Cash and cash equivalents	909 249	27 826	859	(859)	672	(672)	107	(107)	213	(213)
Derivatives (assets)	33 416	4 934	302	(302)	–	–	6	(6)	–	–
Overdrafts	93 503	93 502	(5 707)	5 707	–	–	(142)	142	–	–
Bonds issued	8 637 435	3 583 657	(222 187)	222 187	–	–	–	–	–	–
Liabilities to suppliers	1 042 427	10 511	(547)	547	(106)	106	–	–	–	–
Other financial liabilities	154 119	7 163	(444)	444	–	–	–	–	–	–
Derivatives (liabilities)	14 184	14 184	19 394	(19 394)	–	–	(11)	11	–	–
Total			**(207 208)**	**207 208**	**1 262**	**(1 262)**	**(40)**	**40**	**213**	**(213)**

The exposure to risk as at 31 December 2017 is representative for the Group's exposure to risk during the annual period preceding the aforementioned date, except for material transactions made in the second half of 2017. These include issued bonds, consisting of eurobonds issued by the Company in July 2017, which has been discussed in more detail in Note 32.2 to these consolidated financial statements, and derivatives (liabilities), consisting of CCIRS transactions entered into by the Company in November and December 2017, which has been discussed in more detail in Note 44.3 to these consolidated financial statements.

For the year ended 31 December 2016

Classes of finacial instruments	31 December 2016		Sensitivity analysis for currency risk as at 31 December 2016							
			EUR/PLN		CZK/PLN		USD/PLN		GBP/PLN	
	Carrying amount	Value at risk	exchange rate EUR/PLN +7.8%	exchange rate EUR/PLN -7.8%	exchange rate CZK/PLN +9.98%	exchange rate CZK/PLN -9.98%	exchange rate USD/PLN +13.8%	exchange rate USD/PLN -13.8%	exchange rate GBP/PLN +11.55%	exchange rate GBP/PLN -11.55%
			Profit or loss / other comprehensive income		*Profit or loss / other comprehensive income*		*Profit or loss / other comprehensive income*		*Profit or loss / other comprehensive income*	
Receivables from buyers	1 894 065	11 124	323	(323)	697	(697)	–	–	–	–
Other financial receivables	52 379	4 888	118	(118)	337	(337)	–	–	–	–
Cash and cash equivalents	384 881	52 450	2 573	(2 573)	1 559	(1 559)	177	(177)	296	(296)
Derivatives (assets)	56 417	19 776	6 624	(6 624)	–	–	57	(57)	–	–
Overdrafts	15 156	15 131	(1 046)	1 046	–	–	(237)	237	–	–
Bonds issued	7 681 128	1 580 020	(123 242)	123 242	–	–	–	–	–	–
Liabilities to suppliers	829 729	9 835	(635)	635	(165)	165	–	–	–	–
Other financial liabilities	158 383	13 502	(1 022)	1 022	–	–	(2)	2	(1)	1
Derivatives (liabilities)	560	560	(42)	42	–	–	(3)	3	–	–
Total			**(116 349)**	**116 349**	**2 428**	**(2 428)**	**(8)**	**8**	**295**	**(295)**

The exposure to risk as at 31 December 2016 is representative for the Group's exposure to risk during the annual period preceding the aforementioned date, except for a transaction made at the end of 2016. It concerned a class of the Company's hybrid bonds issued in December 2016 with the euro as the issue and repayment currency.

45.3.3. Raw material and commodity price risk related to commodity derivative instruments held

As at 31 December 2017, open positions included mainly forwards and futures for emission allowances. As at 31 December 2017, the total carrying amount of all derivative contracts for emission allowances was PLN 453 thousand (the asset item of PLN 4 877 thousand and the liability item of PLN 4 424 thousand). As at 31 December 2016, open positions included mainly forwards and futures for emission allowances as well as a futures contract for gas. The total carrying amount of all derivative contracts for emission allowances was PLN 15 012 thousand (the asset item of PLN 15 550 thousand and the liability item of PLN 538 thousand) and PLN 593 thousand (asset) in the case of the gas derivative transaction.

Sensitivity analysis

The analysis of sensitivity to changes in emissions risk factors is conducted by the Group by means of a scenario analysis. The scenarios reflect the Group's assessment of individual risk factors in the future and are aimed to analyse the effect of changes in risks on the Group's financial performance.

(in PLN '000)

For the year ended 31 December 2017

	Carrying amount as at 31 December 2017			Increase		Decrease	
	price (EUR)	Assets	Liabilities	price (EUR)	Impact on gross profit	price (EUR)	Impact on gross profit
Derivative instruments – commodity (emission allowances)							
EUA Dec18	8.18	4 877	4 424	10.81	(22)	7.14	9
EUA inventory – measurement to fair value	8.14	8	–	10.75	22	7.11	(9)
Total		**4 885**	**4 424**		**–**		**–**

For the year ended 31 December 2016

	Carrying amount as at 31 December 2016			Increase		Decrease	
	price (EUR)	Assets	Liabilities	price (EUR)	Impact on gross profit	price (EUR)	Impact on gross profit
Derivative instruments – commodity (emission allowances)							
EUA Dec17	6.57–6.58	5 410	319	10.18	(10 381)	4.14	6 988
EUA Jan17	6.54	10 140	–	10.14	(21 421)	4.12	14 400
EUA Apr17	6.55	–	219	10.15	(780)	4.13	524
EUA inventory – measurement to fair value	6.54	13 226	–	10.14	32 553	4.12	(21 883)
Total		**28 776**	**538**		**(29)**		**29**

45.3.4. Unit price risk

Units in investment funds which are measured at fair value as at the end of the reporting period are exposed to price risk. As at 31 December 2017 and 31 December 2016 the carrying amount of the said units measured at fair value was PLN 101 358 thousand and PLN 25 316 thousand, respectively.

Sensitivity analysis

For purposes of the analysis of sensitivity to changes in the quoted prices of the units in investment funds held by the Group, the Group relies on a scenario analysis. The potential changes in the quoted prices are determined within a horizon until the date of the next financial statements and calculated by reference to the funds' monthly quoted prices within one year preceding the end of the reporting period.

For the year ended 31 December 2017

Investment fund units	31 December 2017		Sensitivity analysis for price risk as at 31 December 2017			
			Price change		Price change	
	Carrying amount	Value at risk	+1.3%	-1.3%	+0.8%	-0.8%
			Impact on gross profit			
Units in fund investing in money market instruments	5 084	5 084	66	(66)		
Units in fund investing in money market instruments and other debt securities	96 274	96 274			770	(770)
Total	**101 358**	**101 358**	**66**	**(66)**	**770**	**(770)**

For the year ended 31 December 2016

Investment fund units	31 December 2016		Sensitivity analysis for price risk as at 31 December 2016			
			Price change		Price change	
	Carrying amount	Value at risk	+1.0%	-1.0%	+0.7%	-0.7%
			Impact on gross profit			
Units in fund investing in money market instruments	2 519	2 519	25	(25)		
Units in fund investing in money market instruments and other debt securities	22 797	22 797			160	(160)
Total	**25 316**	**25 316**	**25**	**(25)**	**160**	**(160)**

46. Operational Risk

Commercial operational risk is managed at the level of the TAURON Group, which has been discussed in more detail in Section 3.4.4 of the Management Board's report on the activities of the TAURON Polska Energia S.A. Capital Group for the 2017 financial year. The Group manages its commercial risk following the Commercial risk management policy developed and adopted in the TAURON Group, which has introduced an early warning system in addition to a system of limiting the exposure to risk in various commercial areas.

(in PLN '000)

The companies in the TAURON Polska Energia S.A. Capital Group are exposed to adverse effects of risks related to changes in cash flows and financial performance in the domestic currency due to changes in commodity prices. The Group's exposure to commodity price risk is reflected by the volume of the key raw materials and commodities purchased, including coal, gas and energy. The volume and cost of the key raw materials purchased from third-party suppliers have been presented in the table below.

Fuel type	Unit	2017		2016	
		Volume	Purchase cost	Volume	Purchase cost
Coal	tonne	3 234 079	577 465	3 522 216	608 619
Gas	MWh	2 481 078	195 393	2 928 639	241 432
Electricity	MWh	28 645 129	4 672 603	33 138 013	5 602 272
Heat energy	GJ	6 091 071	230 276	6 095 393	232 603
Total			**5 675 737**		**6 684 926**

(in PLN '000)

OTHER INFORMATION

47. Contingent Liabilities

Item	Description
Claims related to termination of long-term contracts	**Claims relating to termination of long-term contracts against subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.** On 18 March 2015 the subsidiary in liquidation terminated long-term contracts concluded in the years 2009–2010 to purchase electricity and property rights from wind farms owned by the companies in the in.ventus group, Polenergia and Wind Invest. The reason for the termination of the contracts by Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. was that the counterparties had breached the contractual provisions by refusing to negotiate in good faith the terms and conditions of the contracts. A case was brought against the Company for the statements made in the notice of termination be declared void. In the case brought by Dobiesław Wind Invest Sp. z o.o. in 2016 the Regional Court in Warsaw dismissed the claim for declaring the termination of the contracts void. The claimant appealed against the ruling. In 2016 the claims against the Company were changed to include claims for compensation for termination of the contracts totalling approx. PLN 40 000 thousand. In October 2017 Dobiesław Wind Invest Sp. z o.o. filed a new lawsuit against Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. for payment of PLN 42 095 thousand of compensation and liquidated damages. After the balance sheet date, in January 2018 the claims brought by Amon Sp. z o.o., Talia Sp. z o.o. and Mogilno III-VI have been amended by extending them with further claims for liquidated damages related to the termination of contracts in the total amount of approximately PLN 69 472 thousand. In light of the current status of the proceedings and the related circumstances, the Group believes that the probability of losing the cases both as regards declaration of ineffectiveness of the termination notices and securing non-monetary claims and the claims for compensation does not exceed 50%. Therefore, no provision for the related costs has been recognized. **Claim relating to termination of long-term contracts against subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and TAURON Polska Energia S.A.** In November 2014 an action was brought against Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and TAURON Polska Energia S.A. by Dobiesław Wind Invest Sp. z o.o. to prevent an imminent danger of loss. It was claimed that the Company should revoke the liquidation of Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. in liquidation. A subsidiary claim was that TAURON Polska Energia S.A. should be obliged to provide security in the amount of PLN 183 391 thousand as a court deposit. On 8 March 2017, pursuant to a decision of the Shareholders' Meeting of Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. the liquidation of the company was revoked. Therefore, in accordance with the order of the Regional Court in Krakow issued on 15 March 2017, the parties to the dispute exchanged pleadings to respond to the change in the company in which the claimant upheld their demands. On 2 August 2017 the Company's representative in the case received pleadings from Dobiesław Wind Invest Sp. z o.o. which changed the claims. The claimant withdrew the initial claim against subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and changed the claim against the Company from a claim for prevention of an imminent danger of loss to a claim for compensation. Dobiesław Wind Invest Sp. z o.o. demands payment of approx. PLN 34 700 thousand with statutory interest as of the date of the claim to the date of payment. Moreover, the claimant seeks a ruling that the Company is liable for future damages of Dobiesław Wind Invest Sp. z o.o., which the latter estimates at approx. PLN 254 000 thousand, (resulting from the Company's alleged torts) and a security of approx. PLN 254 000 thousand in case the court does not establish the Company's liability for future losses. The factual basis of the claim, in accordance with the claimant, is the termination of the long-term contracts to sell electricity and property rights by subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. An analysis of the justification of the statements of the claim shows that they are wholly groundless. At a hearing on 4 October 2017, upon request of TAURON Polska Energia S.A., the Court decided that the new statement of claim against TAURON Polska Energia S.A. would be examined separately. As far as the initial claims against TAURON Polska Energia S.A. and Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. (demand that the liquidation be revoked), the Court referred the case to be examined at a closed-door hearing and dismissed. As the court will have to examine extensive evidence and conduct an analysis of a legal issue which has not been resolved before, it is too early to anticipate the outcome of the proceedings but it is very likely that the decision of the court will be favourable for the defendants.

(in PLN '000)

Item	Description
Claims relating to termination of long-term contracts – continued	**Claims relating to termination of long-term contracts against TAURON Polska Energia S.A.** On 20 July 2017 the Company was served with a summons dated 29 June 2017 of Gorzyca Wind Invest Sp. z o.o. against TAURON Polska Energia S.A. for damages of approx. PLN 39 700 thousand and assessment of liability for future damages resulting from torts, including unfair competition, estimated by the claimant at approx. PLN 465 900 thousand. The case will be heard by a Regional Court in Katowice. On 18 September 2017, the Company responded to the summons, in which it filed, inter alia, to dismiss the action in its entirety as wholly groundless. On 1 December 2017, Gorzyca Wind Invest Sp. z o.o. submitted a reply to the reply to the claim, in which upheld the position contained in the summons and denied the position and argumentation of the Company presented in response to the statement of claim. By the decision of the District Court in Katowice of 8 February 2018, the proceedings brought by Gorzyca Wind Invest Sp. z o.o. against TAURON Polska Energia SA, is entirely carried out in camera, the announcement of the decision ending the proceedings will take place publicly. Another summons, dated 29 June 2017, of Pękanino Wind Invest Sp. z o.o. against TAURON Polska Energia S.A. for damages of approx. PLN 28 500 thousand and assessment of liability for future damages resulting from torts, including unfair competition, estimated by the claimant at PLN 201 600 thousand was delivered on 21 August 2017. On 5 October 2017, the Company filed a reply to the claim in which it filed, inter alia, to dismiss the action in its entirety as wholly grounless. On 1 December 2017, Pękanino Wind Invest Sp. z o.o. filed a reply to the reply to the claim in which claimant upheld the position contained in the summons and denied the position and argumentation of the Company presented in response to the summons. Until the date of approval of these financial statements for publication, the date of the hearing was not set. On 16 October 2017 the Company was served a summons dated 29 June 2017 of Nowy Jarosław Wind Invest Sp. z o.o. against TAURON Polska Energia S.A. for damages of approx. PLN 27 000 thousand and assessment of liability for future damages resulting from torts, including unfair competition, estimated by the claimant at PLN 197 800 thousand. On 28 December 2017 the Company filed a reply to the claim in which it filed, inter alia, to dismiss the action in its entirety as wholly groundless. Until the date of approval of these financial statements for publication, the date of the hearing was not set. The factual basis of all the claims, in accordance with the claimants, is the termination of the long-term contracts to purchase electricity and property rights resulting from energy certificates by subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and the total amount of the future loss incurred by all members of the Wind Invest group estimated by the claimant will be PLN 1 212 900 thousand. As at the date of approval of these financial statements for publication the probability of obtaining a positive settlement in disputes can be assessed positively, i.e. the chances are 70%. **Termination of long-term contracts to purchase property rights by TAURON Sprzedaż Sp. z o.o.** On 28 February 2017, TAURON Sprzedaż Sp. zo.o., a subsidiary, submitted termination notices regarding long-term contracts for the purchase of property rights under green certificates by the subsidiary. The party to the contracts in 2008 are companies from the in.ventus group. The contracts were terminated after the parties were unable to reach an agreement in renegotiation of the contracts in line with the terms and conditions provided for therein. Total net contractual liabilities of TAURON Sprzedaż Sp. z o.o. under the terminated contracts for the years 2017–2023, as at the date of the termination would be approx. net PLN 417 000 thousand. There are no pending court disputes in connection with the termination of the contracts by TAURON Sprzedaż Sp. z o.o. Based on an analysis of the legal circumstances, supported by an analysis performed by independent legal firms, the Group does not see any reason to recognize provisions in connection with the termination of the contracts by TAURON Sprzedaż Sp. z o.o.
Use of real estate without contract	Companies in the Group do not hold legal titles to all land crossed by distribution networks or the land on which heat installations and related devices are sited. The Group may have to incur costs related to non-contractual use of property in the future; the risk of losing assets is close to nil, though. The Group has established a provision for all court disputes regarding the issue. No provision has been recognized for potential, not submitted claims of owners of land with unregulated legal status, since there are no detailed records of such land. As a consequence, potential claim amounts cannot be reliably estimated. In light of the history of claims submitted and the related costs incurred in the previous years, though, the risk of incurring material costs with this regard is low.
Amount	As at the end of the reporting period, a provision was recognized for costs of court disputes in the amount of PLN 92 030 thousand (Note 36).
Claims filed by Huta Łaziska S.A.	Following the Company's business combination with Górnośląski Zakład Elektroenergetyczny S.A. ("GZE"), TAURON Polska Energia S.A. became a party to a court dispute with Huta Łaziska S.A. ("Huta"), against GZE and the State Treasury represented by the President of the Energy Regulatory Office. At present, the case is pending at the Regional Court in Warsaw. Based on a decision of 12 October 2001, the President of the Energy Regulatory Office ordered GZE to resume electricity supplies to Huta (suspended on 11 October 2001 since Huta had not paid its liabilities) on such terms as set out in the agreement of 30 July 2001, in particular at the price of PLN 67/MWh, until final resolution of the dispute, and on 14 November 2001 the dispute was finally resolved pursuant to a decision stating that discontinuation of electricity supplies was not unjustified. Huta appealed against that decision. On 25 July 2006, the Court of Appeals in Warsaw issued a final and binding decision ending the dispute concerning GZE's energy supplies to Huta. The court dismissed Huta's appeal against the decision of the Regional Court in Warsaw dated 19 October 2005, in which the court had dismissed Huta's appeal against the decision of the President of the Energy Regulatory Office. Huta filed a cassation appeal against the decision of the Court of Appeals in Warsaw, which was dismissed by the judgment of the Supreme Court dated 10 May 2007. On 15 November 2001 (following the issue of the above decision by the President of the Energy Regulatory Office on 14 November 2001 and due to the growing indebtedness of Huta to GZE due to power supply) GZE again suspended power supply. Therefore, Huta has sued GZE for damages. Under a suit of 12 March 2007 against GZE and the State Treasury represented by the President of the Energy Regulatory Office (jointly and severally) Huta claimed the payment of PLN 182 060 thousand together with interest from the date of filing the suit to the date of payment, in respect of damages for alleged losses resulting from GZE's failure to comply with the decision of the President of the Energy Regulatory Office dated 12 October 2001. In this case, the courts of the first and second instance passed judgements favourable for GZE; however, in its judgement of 29 November 2011 the Supreme Court overruled the decision of the Court of Appeals and remanded the case for re-examination by that Court. On 5 June 2012, the Court of Appeals overruled the decision of the Regional Court and remanded the case for re-examination by the latter. The case has been heard by the first-instance court since 27 November 2012. Based on a legal analysis of claims the Company believes that they are unjustified and the risk that they must be satisfied is remote. As a result, no provision has been recognized by the Company for any costs associated with those claims.
Amount	Claim regarding payment of damages of PLN 182 060 thousand.

(in PLN '000)

Item	Description
Claim filed by ENEA S.A.	The claim filed by ENEA S.A. ("ENEA") against TAURON Polska Energia S.A. in a case heard by the Regional Court in Katowice since 2016 regards the payment of PLN 17 086 thousand with statutory interest calculated from 31 March 2015 to the payment date. ENEA's claim is based on charges relating to unjust enrichment of the Company associated with possible errors in determination of aggregate measurement and settlement data by ENEA Operator Sp. z o.o. (as the Distribution System Operator), used as the basis for settlements between ENEA and the Company and Polskie Sieci Elektroenergetyczne S.A. arising from non-balancing volumes on the Balancing Market between January and December 2012. In the course of the proceedings, at the request of ENEA, the court decided to extend the suit against seven sellers for which TAURON Polska Energia S.A. acted as an entity in charge of trade balances in the distribution area of ENEA Operator Sp. z o.o. in 2012. The sellers included two subsidiaries of TAURON Polska Energia S.A., i.e.: TAURON Sprzedaż Sp. z o.o. (from which ENEA S.A. demanded PLN 4 934 thousand with statutory interest as of the date of serving a copy of the request to extend the suit until the date of payment) and TAURON Sprzedaż GZE Sp. z o.o. (from which ENEA S.A. demanded PLN 3 480 thousand with statutory interest as of the date of serving a copy of the request to extend the suit until the date of payment). The demand for payment of the above amounts as well as the amounts claimed from the other five sellers was submitted by the petitioner in case the claim against TAURON Polska Energia S.A. is dismissed. The case is pending. By the date of approval of these consolidated financial statements for publication, the hearing had been adjourned ex officio. The Company did not recognize any provision as, in its opinion, the risk of losing the case is below 50%. Provisions were recognized by the subsidiaries of TAURON Polska Energia S.A. in the total amount of PLN 5 237 thousand (TAURON Sprzedaż Sp. z o.o.) and in the total amount of PLN 3 726 thousand (TAURON Sprzedaż GZE Sp. z o.o.). The said provisions cover the principal, interest reviewed as at 31 December 2017 and the cost of the proceedings.
Amount	As at 31 December 2017, the value of the claim against the Company is PLN 17 086 thousand, including statutory interest accrued between 31 March 2015 and the payment date. Should the claim filed against the Company be dismissed, the claim for payment by the Group companies totals PLN 8 414 thousand, including statutory interest accrued between the date of service of a copy of the request filed by ENEA S.A. to extend the suit by a specific Group company and the payment date. As new measurement data were presented by ENEA Operator sp. z o.o. in the course of the proceedings, the values of the claims against the Company and/or the Group companies may be expected to change.
Administrative proceedings instigated by the President of the Energy Regulatory Office (ERO)	In a notice of 5 April 2016, the President of the Energy Regulatory Office informed TAURON Dystrybucja S.A. of the instigation of administrative proceedings to impose a fine for a failure to maintain facilities, installations and equipment in a proper technical condition and for non-compliance with the terms of the electricity distribution licence. In a notice of 30 March 2017, the President of the Energy Regulatory Office informed the Company that the matter would be looked into on 30 April 2017. In subsequent notices of 8 May and 1 June 2017 the President of the Energy Regulatory Office extended the proceedings until 31 May and 30 June 2017, respectively. On 10 July 2017 the Company received a decision of the President of the Energy Regulatory Office to impose an administrative fine totalling PLN 350 thousand. In July 2017 the Company recognized a provision of PLN 351 thousand and on 24 July it filed an appeal with the Court of Competition and Consumer Protection through the President of the Energy Regulatory Office. On 30 January 2018, the Company received the response of the President of the Energy Regulatory Office to the Court of Competition and Consumer Protection to the appeal. At present, the Company is waiting for the next hearing to be scheduled by the Court of Competition and Consumer Protection. On 12 December 2017, the President of the URE initiated administrative proceedings against a company from the Generation segment regarding the imposition of a fine due to the suspicion of producing electricity at Dąbie Hydroelectricity [pl. Elektrownia Wodna Dąbie] and Przewóz Hydroelectricity [pl. Elektrownia Wodna Przewóz] without the permits for special use of Vistula waters for energy purposes required by the provisions of the Act of 20 July 2017 Water law of water. On 12 January 2018, the company sent appropriate explanations about the ongoing proceedings regarding the issue of the water-legal permits in question. The company is of the opinion that the facts that are the basis for the initiation of the proceedings can not constitute a basis for imposing a fine, and therefore the company can not make a reliable valuation of the fine and the company has not created a provision for this. The companies in the Sales segment have been subject to the following proceedings: – proceedings instigated on 31 March 2017 regarding the breach of the obligation to secure energy performance certificates and present them for cancellation to the President of the Energy Regulatory Office in 2013 year. In a notice dated 14 April 2017, the company provided information requested by the President of the Energy Regulatory Office. – proceedings instigated on 30 May 2017, 28 June 2017 and 20 September 2017 regarding a fine for unjustified suspension of energy deliveries to the end users. By decisions dated 6 November and 29 December 2017, the President of the Energy Regulatory Office imposed on the companies from the Sales segment penalties in the total amount of PLN 19 thousand. – proceedings instigated on 26 September 2017 regarding unjustified suspension of energy deliveries by TAURON Sprzedaż Sp. z o.o. with the participation of TAURON Dystrybucja S.A. to the end users. The Companies do not recognize provisions for potential fines that may be imposed in the above proceedings as in the opinion of the Management Board the risk of adverse rulings and fines is low.

(in PLN '000)

Item	Description
Administrative and Explanatory proceedings instigated by the President of the Office for Competition and Consumer Protection (UOKiK)	The President of UOKiK instigated the following procedures against a Sales segment company: – Proceedings instigated on 17 September 2013 against TAURON Sprzedaż Sp. z o.o. with regard to the company's alleged use of practices violating collective consumers' interests. The practices consisted in quoting electricity prices in pricing lists and information materials without VAT, which constituted a breach of the Act of counteracting unfair market practices of 23 August 2007 and therefore constitutes a breach of the Act on competition and consumer protection of 16 February 2007 (Journal of Laws of 2007 No. 50, item 331 as amended; "Act on competition and consumer protection"). The company undertook to discontinue practices that violate the Act on competition and consumer protection. Further, it motioned for proceedings aimed at the issue of a binding decision. On 22 December 2014 the company received a decision of UOKiK closing the evidentiary proceedings. On 14 December 2015 the President of UOKiK demanded that the Company answer whether the practices had been discontinued. The Company responded in February 2016 informing that the practices had been discontinued and requested that the fine be waived. By decision of 22 February 2018, the President of UOKiK stated that the company applied the practice violating collective consumers' interests and its discontinuation as of 1 February 2016. The President of UOKiK did not impose a financial penalty on the company, and the company was obliged to publish a statement with the content specified in the decision. The Company may appeal against the decision to SOKiK [Court of Competition and Customer Protection]. – On 27 January 2015 explanatory proceedings were instigated to provisionally determine if actions taken by TAURON Sprzedaż Sp. z o.o. towards small hydroelectric power stations constitute a breach of the Act on competition and consumer protection. The actions in question include enforcing unfair terms of purchase of electricity generated using renewable sources and conditioning the energy purchase on meeting with the commercial balancing requirement. With a decision of 15 October 2015 the President of UOKiK instigated anti-trust proceedings. On 1 February 2016 UOKiK accepted the company's statement regarding presentation of a specific commitment. On 24 August 2016 the President of UOKiK issued a decision obliging the company to take appropriate measures aimed at preventing the alleged breaches within two months of the date on which the decision of the President of UOKiK becomes final. On 29 September 2016 the Company appealed against the decision to the Court of Competition and Consumer Protection. On 2 December 2016 the President of the Office for Competition and Consumer Protection issued a decision whereby it changed the rationale of the previous decisions. The decision became final on 2 February 2017. A report on its implementation was prepared and sent to UOKiK on 31 March 2017. – On 11 May 2017 explanatory proceedings were instigated against TAURON Sprzedaż Sp. z o.o. to examine the scheme whereby the billing period for the sales of electricity is automatically extended (as set out in the Price List) if the consumer fails to take any action after being presented with a new (renewal) offering. The President of UOKiK requested that the Company presents appropriate explanations. The latest explanations were given on 16 October 2017. – On 21 July 2017 explanatory proceedings were instigated against TAURON Sprzedaż GZE Sp. z o.o. to examine the breach of Article 6b.3 of the Energy Law regarding extra time given in the demands for payment to settle past-due liabilities. The Company intends to take corrective measures and change the wording of the notice sent to the consumers. The final response is being prepared. – On 13 October and 8 November 2017 proceedings were instigated to examine the suspicion that the practices of the companies in the Sales segment violate the collective interests of consumers by making the switching of the electricity supplier more difficult. Under Article 49a of the Act on competition and consumer protection the Companies were requested to respond to the accusation by the President of UOKiK that they made the switching of the supplier more difficult and misled consumers by letting them believe that they may terminate their contract with a different supplier free of charge. The Companies submitted their latest responses on 3 November and 29 December 2017. The companies do not recognize provisions for potential fines that may be imposed in the above proceedings as in the opinion of the Management Board the risk of adverse rulings and fines is low. In relation to the companies from the Sales segment, there are also explanatory proceedings conducted by UOKiK regarding the preliminary determination whether the activities of the companies did not constitute a violation of the provisions of the Act on competition and consumer protection. The companies submit explanations, submit the requested documents and respond to the statements contained in the UOKIK's letters. The management boards of the companies assess, having in mind that the proceedings initiated are of the nature of explanatory proceedings that the probability of unfavorable settlement of cases is low and therefore the Group does not create provisions for these events.
Claim for reimbursement of the expenses incurred to protect a facility against the effects of mining activities	In December 2017 subsidiary TAURON Wydobycie S.A. was served with a claim for the payment of PLN 22 785 thousand, made by Galeria Galena Sp. z o.o. with its registered office in Gliwice, as reimbursement of the expenditures incurred to protect a facility located in Jaworzno against the effects of mining activities. After the balance sheet date, on 7 March 2018, the company submitted a response to the statement of claim to the District Court in Katowice. The company has not recognized any related provision as it believes that at this stage such a provision would be premature, considering legal and practical doubts, which prevent a straightforward prediction of the ruling of the Regional Court in Katowice and the amount of compensation, if any.
Real estate tax	There are different interpretations regarding the approach to real estate tax on electricity generation and transmission facilities and underground excavation equipment Since the tax is imposed by local authorities, there is no unified approach of taxation authorities and in several cases the method of calculation of the tax basis has been questioned. Depending on court decisions and possible amendments to relevant regulations, the status of real estate tax on electricity generation facilities and excavations may change in future. Following the changes introduced in 2017 to the definition of construction facilities in the Investment Act in the scope of wind farms, there is no consistent approach to defining structures at present. This entails the risk of potential disputes with local authorities (municipalities) over the determination of the tax base for real estate tax on wind farms.
Amount	The potential disputed tax on wind farms is approx. PLN 16 000 thousand. In respect of real estate tax and economic risk related disputes, as at 31 December 2017, provisions in the total amount of PLN 42 802 thousand and accruals in the amount of PLN 16 417 thousand relating to tax related to wind farms have been recognised.

(in PLN '000)

48. Security for Liabilities

The Group uses various forms of collateral against its liabilities. Those most frequently used include mortgages, registered pledges, liens on real property and other items of property, plant and equipment and frozen cash in bank accounts.

Carrying amounts of assets pledged as collateral against liabilities of the Group

	As at 31 December 2017	As at 31 December 2016
Real estate	68 251	81 363
Plant and machinery	–	14 059
Other financial receivables	11 139	–
Cash	9	13 740
Total	**79 399**	**109 162**

Other forms of collateral

The Group also uses other forms of collateral to secure payment of liabilities than those listed above, of which the most significant ones as at 31 December 2017 regard the following contracts concluded by the Parent:

Agreement	Collateral form	Collateral amount
Bond Issue Scheme dated 16 December 2010 with subsequent annexes	declaration of submission to enforcement	up to PLN 6 900 000 thousand, valid until 31 December 2018
Long-term Bond Issue Scheme in Bank Gospodarstwa Krajowego	declaration of submission to enforcement	up to PLN 2 550 000 thousand, valid until 20 December 2032
Bond Issue Scheme dated 24 November 2015	declaration of submission to enforcement	up to PLN 7 524 000 thousand, valid until 31 December 2023
Bank guarantee agreement with The Bank of Tokyo-Mitsubishi UFJ, Ltd.	declaration of submission to enforcement	up to PLN 377 383 thousand, valid until 27 October 2018
Hybrid financing contract governing the issue of subordinated bonds dated 6 September 2017	declaration of submission to enforcement	up to PLN 600 000 thousand, valid until 30 June 2034
Framework bank guarantee agreement concluded with CaixaBank S.A. The Company and TAURON Group companies can use the limit for guarantees to secure transactions (the maximum guarantee limit amount was determined at PLN 100 000 thousand).	authorization to debit the bank account maintained by CaixaBank S.A.	up to PLN 100 000 thousand
	declaration of submission to enforcement	up to PLN 120 000 thousand valid until 11 July 2021
Agreement with Bank Zachodni WBK S.A. on bank guarantees for Izba Rozliczeniowa Giełd Towarowych S.A.	authorization to debit the bank account maintained by BZ WBK S.A.	up to PLN 150 000 thousand
Overdraft agreements with PKO Bank Polski S.A. (up to PLN 300 000 thousand and an intraday limit agreement up to PLN 500 000 thousand)	authorizations to debit the bank account maintained by PKO Bank Polski S.A.	up to the total amount of PLN 800 000 thousand
	declaration of submission to enforcement	up to PLN 600 000 thousand, valid until 17 December 2021
	declaration of submission to enforcement	up to PLN 360 000 thousand, valid until 29 December 2021
Overdraft agreement with Bank Gospodarstwa Krajowego (in EUR, up to EUR 45 000 thousand)	authorization to debit the bank account maintained by Bank Gospodarstwa Krajowego	up to PLN 187 690 thousand (EUR 45 000 thousand)
	declaration of submission to enforcement	up to PLN 100 102 thousand (EUR 24 000 thousand) valid until 31 December 2019
	declaration of submission to enforcement	up to PLN 208 545 thousand (EUR 50 000 thousand) valid until 31 December 2020
Overdraft agreement with mBank (in USD, up to USD 2 000 thousand)	declaration of submission to enforcement	up to PLN 10 444 thousand (USD 3 000 thousand) valid until 31 March 2019

(in PLN '000)

Other forms of collateral against liabilities of the Group

As at 31 December 2017, other material forms of collateral regarding liabilities of TAURON Capital Group included:

- Registered pledges and financial pledge on the shares in TAMEH HOLDING Sp. z o.o.

On 15 May 2015 the Parent established a financial pledge and registered pledges of 3 293 403 shares in the issued capital of TAMEH HOLDING Sp. z o.o., with the unit face value of PLN 100 and the total face value of PLN 329 340 thousand, accounting for approx. 50% of shares in the issued capital of the entity for the benefit of RAIFFEISEN BANK INTERNATIONAL AG.

The Company established a first lien registered pledge of shares with the maximum collateral amount of CZK 3 950 000 thousand and a first lien registered pledge of shares with the maximum collateral amount of PLN 840 000 thousand for the benefit of RAIFFEISEN BANK INTERNATIONAL AG. The Company also agreed to establish a financial pledge and registered pledges of new shares acquired or taken up. Moreover, the Company assigned the rights to dividend and other payments.

The agreement to establish registered pledges and a financial pledge was concluded to secure transactions including the agreement for term loans and working capital loans, entered into by TAMEH Czech s.r.o. and TAMEH POLSKA Sp. z o.o. as original borrowers, TAMEH HOLDING Sp. z o.o. as the parent and the guarantor, and RAIFFEISEN BANK INTERNATIONAL AG as the agent and the collateral agent. The registered pledges are valid in the collateral period, i.e. until the total repayment or until release of the pledge by the pledgee. The financial pledge is valid in the entire collateral period or until release by the pledgee, not later than on 31 December 2028.

On 15 September 2016, Annex 1 was executed to the aforementioned agreement, whereby the maximum collateral amount was changed to PLN 1 370 000 thousand.

As at 31 December 2017, the carrying amount of the investment in a joint venture measured using the equity method in the TAMEH HOLDING Sp. z o.o. Capital Group was PLN 499 204 thousand.

- Blank promissory notes

Agreement/transaction secured by blank promissory notes	Capital Group company that has issued a blank promissory note	As at 31 December 2017
Agreements concerning loans granted to TAURON Wytwarzanie S.A. and TAURON Ciepło Sp. z o.o. by Regional Fund for Environmental Protection and Water Management in Katowice. The companies have provided declarations of submission to enforcement as collateral for the loans in question.	TAURON Polska Energia S.A.	70 000
Performance bonds to include co-funding of engagements carried out.	TAURON Dystrybucja S.A.	242 090
Performance bonds under the co-funding agreements concluded with the National Fund for Environmental Protection and Water Management and reimbursement and performance bond under the co-funding agreements concluded with the Regional Fund for Environmental Protection and Water Management.	TAURON Ciepło Sp. z o.o.	228 605
Agreements to connect to a transmission grid, to provide electricity supply services, an agreement with the National Fund for Environmental Protection and Water Management concerning partial cancellation of a loan and an agreement with the National Centre for Research and Development for the funding of a project.	TAURON Wytwarzanie S.A.	76 214

- Collateral under finance lease agreements

Finance lease agreement	Lessee	Carrying amount of the leased asset as at 31 December 2017	Collateral
Real estate in Katowice	TAURON Polska Energia S.A.	21 702	The agreement is collateralized by two blank promissory notes, assignment of receivables and authorization to debit a bank account.

- The Company issued a corporate guarantee to secure the bonds issued by TAURON Sweden Energy AB (publ). The guarantee remains valid until 3 December 2029, i.e. until the date of redemption of bonds, and amounts to EUR 168 000 thousand. The beneficiaries of the guarantee are the bondholders.
- Under the bank guarantee agreement made with Bank Zachodni WBK S.A., the bank issued guarantees to secure stock exchange transactions resulting from the membership in Izba Rozliczeniowa Giełd Towarowych S.A. As at 31 December 2017, the guarantees issued by the bank totalled PLN 50 000 thousand and were valid until 31 March 2018.

(in PLN '000)

- Under the bank guarantee agreement made with CaixaBank S.A. (Joint Stock Company) Branch in Poland, at the request of the Company the bank issued bank guarantees to secure liabilities and transactions of the subsidiaries of TAURON Polska Energia S.A. totalling PLN 13 834 thousand and to secure the transactions performed by the Company:
  - for Operator Gazociągów Przesyłowych GAZ-SYSTEM S.A. – up to PLN 2 661 thousand, valid until 30 November 2018;
  - for Polskie Sieci Elektroenergetyczne S.A. – up to PLN 4 041 thousand, valid until 11 February 2018.

Mining companies from the Capital Group have established a Mine Decommissioning Fund to ensure funds for covering future decommissioning costs.

49. Related-Party Disclosures

49.1. Transactions with joint ventures

The Group has interest in the following joint ventures: Elektrociepłownia Stalowa Wola S.A. and the TAMEH HOLDING Sp. z o.o. Capital Group, which has been discussed in more detail in Note 22 to these consolidated financial statements.

The total amount of transactions with jointly-controlled entities has been presented in the following table.

	Year ended 31 December 2017	Year ended 31 December 2016
Revenue	52 306	111 268
Costs	(36 655)	(46 321)

The key revenue item arises from transactions with the TAMEH HOLDING Sp. z o.o. Capital Group. In the years ended 31 December 2017 and 31 December 2016, transactions with the joint venture amounted to PLN 30 214 thousand and PLN 100 520 thousand, respectively. In the year ended 31 December 2017, revenue was mainly derived from sales of emission allowances of PLN 19 994 thousand. In the year ended 31 December 2016, sales of emission allowances totalling PLN 32 384 thousand and of coal totalling PLN 47 041 thousand were the key revenue items.

The key item of receivables from and liabilities to jointly-controlled entities is a loan granted to Elektrociepłownia Stalowa Wola S.A., which has been discussed in more detail in Note 23 to these consolidated financial statements.

The Company has also pledged collateral for the benefit of joint ventures, in the form of a pledge on the shares in TAMEH HOLDING Sp. z o.o., which has been discussed in more detail in Note 48 to these consolidated financial statements.

In relation to agreements entered into with the joint venture Elektrociepłownia Stalowa Wola S.A., the Company recognized provisions for onerous contracts and for costs. In the year ended 31 December 2017 the Company reversed all these provisions, which has been discussed in more detail in Note 34.3 to these consolidated financial statements.

49.2. Transactions with State Treasury companies

As the State Treasury of the Republic of Poland is the Company's major shareholder, State Treasury companies are treated as related parties.

The total value of transactions with State Treasury companies has been presented in the table below.

Revenue and expense

	Year ended 31 December 2017	Year ended 31 December 2016
Revenue	1 803 577	2 293 142
Costs	(3 007 059)	(2 527 466)

(in PLN '000)

Receivables and liabilities

	As at 31 December 2017	As at 31 December 2016
Receivables	253 834	356 595
Payables	322 002	298 786

As at 31 December 2017, receivables presented in the table above comprised advance payments for purchases of fixed assets of PLN 9 757 thousand. As at 31 December 2016, receivables presented in the table above comprised advance payments of PLN 109 364 thousand, including advance payments for deliveries of coal of PLN 99 607 thousand and advance payments for purchases of fixed assets of PLN 9 757 thousand.

In the year ended 31 December 2017, KGHM Polska Miedź S.A., PSE S.A., Polska Grupa Górnicza Sp. z o.o. and Jastrzębska Spółka Węglowa S.A. were the major customers of the TAURON Polska Energia S.A. Capital Group out of the State Treasury companies. The total sales to these contracting parties accounted for 85% of revenue generated on transactions with State Treasury companies. The largest purchase transactions were concluded by the Group with PSE S.A. and Polska Grupa Górnicza Sp. z o.o. Purchases from these contracting parties accounted for 89% of the value of purchases from State Treasury companies during the year ended 31 December 2017.

In the year ended 31 December 2016, KGHM Polska Miedź S.A., PSE S.A., Jastrzębska Spółka Węglowa S.A. and Polska Grupa Górnicza Sp. z o.o. incorporated on 1 May 2016 were the major customers of the TAURON Polska Energia S.A. Capital Group out of the State Treasury companies. Total sales to these contracting parties accounted for 83% of revenue from transactions with State Treasury companies. The largest purchase transactions were concluded by the Group with PSE S.A., Kompania Węglowa S.A. and Polska Grupa Górnicza Sp. z o.o. Purchases from these contracting parties accounted for 87% of the value of purchases from State Treasury companies during the year ended 31 December 2016.

The Capital Group concludes material transactions on the energy markets through Izba Rozliczeniowa Giełd Towarowych S.A. As it is only responsible for organization of commodities exchange trading, the Group does not classify purchase and sale transactions made through this entity as related-party transactions.

Transactions with State Treasury companies are mainly related to the operating activities of the Group and they are concluded on arm's length terms.

49.3. Executive compensation

The amount of compensation and other benefits paid and/or due to the Management Board, Supervisory Boards and other key executives of the Parent and the subsidiaries in the year ended 31 December 2017 and in the comparative period has been presented in the table below.

	Year ended 31 December 2017		Year ended 31 December 2016	
	Parent	Subsidiaries	Parent	Subsidiaries
Board of Directors	**6 957**	**20 556**	**12 858**	**24 604**
Short-term benefits (with surcharges)	4 545	16 822	6 367	19 051
Employment termination benefits	2 104	3 082	5 806	4 990
Other	308	652	685	563
Supervisory Board	**739**	**684**	**1 159**	**641**
Short-term employee benefits (salaries and surcharges)	739	672	1 159	612
Other	–	12	–	29
Other key management personnel	**13 832**	**41 144**	**13 284**	**39 375**
Short-term employee benefits (salaries and surcharges)	12 151	39 267	10 554	38 242
Jubilee bonuses	–	1 214	–	391
Post-employment benefits	–	–	–	16
Employment termination benefits	776	340	1 911	511
Other	905	323	819	215
Total	**21 528**	**62 384**	**27 301**	**64 620**

In accordance with the adopted accounting policy, the Group recognizes provisions for termination benefits for members of the Management Board and other key executives, which may be paid or due in future reporting periods. The above table presents amounts paid and/or due until 31 December 2017.

50. Operating Leases

Under lease agreements, the Parent uses a real property located in Katowice at ul. ks. Piotra Ściegiennego 3, where its registered office is located. The usable area is 9 931.39 square meters and in 2017, the average monthly rental fee with the service charges was PLN 818 thousand.

Moreover, TAURON Wydobycie S.A. uses mining machines and equipment based on lease agreements. The annual cost of lease in the years 2017 and 2016 reached PLN 24 626 thousand and PLN 34 027 thousand, respectively.

51. Finance and Capital Management

The key tools enabling effective management of financial resources include the central financing model and the TAURON Group's liquidity management policy along with a cash pooling arrangement made by the Group. Additionally, the finance management system is supported by the Group's central financial risk management policy and central insurance policy with the Company acting as a manager directing activities, thus allowing relevant risk exposure limits to be established.

Detailed information regarding finance management has been provided in Section 4.10 of the Management Board's report on the activities of the TAURON Polska Energia S.A Capital Group.

In 2017, the TAURON Group was fully able to pay its liabilities at maturity.

The key objective of the capital management policy developed by the Group is maintaining a good credit rating and safe capital ratios supporting its operations and increasing its shareholder value. The Group manages its capital structure and modifies it in accordance with changes in economic conditions. In order to maintain or adjust the capital structure, the Group may establish a dividend policy for its shareholders, return equity to them, issue new shares or influence external debt level accordingly.

The Group focuses primarily on monitoring the debt ratio, which is defined as net financial debt relative to EBITDA.

Net financial debt is the financial debt of the TAURON Group arising from loans, borrowings and debt securities as well as finance leases, except the liability arising from the issue of subordinated bonds in December 2016 with the par value of EUR 190 000 thousand, less cash and short-term investments maturing within one year. EBITDA is the operating profit or loss of the TAURON Group increased by amortization/depreciation and impairment of non-financial assets. Financial debt means the obligation to pay or refund money (both principal and interest). The value of the ratio is also monitored by the institutions providing financing to the Group and rating agencies and has a measurable impact on the Company's ability to obtain funding and its cost, as well as on evaluation of its credit standing.

As at the end of the reporting period, the debt ratio was 2.3, which is regarded as safe according to the market standards and enables the entity to take on further financial liabilities.

(in PLN '000)

	Year ended 31 December 2017	Year ended 31 December 2016
Loans and borrowings	901 734	1 070 162
Bonds*	7 808 300	6 826 751
Finance lease	25	23 546
Non-current debt liabilities	**8 710 059**	**7 920 459**
Loans and borrowings	289 654	193 391
Bonds*	36 183	13 354
Finance lease	23 948	11 302
Short-term debt liabilities	**349 785**	**218 047**
Total debt	**9 059 844**	**8 138 506**
Cash and cash equivalents	909 249	384 881
Short-term investments maturing within one year	108 370	50 023
Net debt	**8 042 225**	**7 703 602**
EBITDA	**3 544 591**	**3 336 814**
Operating profit (loss)	1 806 271	801 522
Depreciation/amortization	(1 693 468)	(1 668 726)
Impairment	(44 852)	(866 566)
Net debt / EBITDA	**2.3**	**2.3**

** Debt does not include liabilities arising from subordinated bonds.*

Changes in the balance of debt have been presented below.

	Debt liabilities
As at 1 January 2016	**8 138 647**
Proceeds arising from debt taken out	**4 274 293**
financing received	4 285 521
transaction costs	(11 228)
Interest accrued	**350 399**
charged to profit or loss	254 428
capitalized to property, plant and equipment and intangible assets	95 971
Debt related payments	**(3 806 689)**
principal repaid	(3 455 602)
interest paid	(255 116)
interest paid, capitalized to investment projects	(95 971)
Change in the balance of overdraft facility and cash pooling	**(8 332)**
Change in debt measurement	**27 772**
Other non-monetary changes	**3 439**
As at 31 December 2016	**8 979 529**
subordinated bonds	(841 023)
As at 31 December 2016 – debt in the calculation of debt ratio	**8 138 506**
Proceeds arising from debt taken out	**2 703 643**
financing received	2 707 462
transaction costs	(3 819)
Interest accrued	**313 382**
charged to profit or loss	207 434
capitalized to property, plant and equipment and intangible assets	105 948
Debt related payments	**(2 106 885)**
principal repaid	(1 816 388)
interest paid	(184 549)
interest paid, capitalized to investment projects	(105 948)
Change in the balance of overdraft facility and cash pooling	**83 471**
Change in debt measurement	**(119 858)**
Other non-monetary changes	**(486)**
As at 31 December 2017	**9 852 796**
subordinated bonds	(792 952)
As at 31 December 2017 – debt in the calculation of debt ratio	**9 059 844**

52. Fee of the Certified Auditor or the Entity Authorized to Audit Financial Statements

Information concerning the fee of the certified auditor has been presented in the Management Board's report on the activities of the TAURON Polska Energia S.A. Capital Group for the 2017 financial year (Section 4.12).

53. Events After the End of the Reporting Period

Loans to a joint venture

On 12 January 2018 and 28 February 2018, the Company entered into a loan agreement with Elektrociepłownia Stalowa Wola S.A. in the amount of PLN 27 000 thousand and an agreement to consolidate the borrower's debt in the amount of PLN 609 951 thousand, respectively, which has been discussed in more detail in Note 23 to these consolidated financial statements.

Financing a joint venture Elektrociepłownia Stalowa Wola S.A.

After the end of the reporting period, on 8 March 2018 year, a joint venture Elektrociepłownia Stalowa Wola S.A. signed a loan agreement with Bank Gospodarstwa Krajowego and Polskie Górnictwo Naftowe i Gazownictwo S.A., which has been discussed in more detail in Note 23 to these consolidated financial statements.

Signing annexes to agreements concerning the bond issue scheme

After the end of the reporting period, on 9 March 2018 year, a part of the banks extended the availability period of funds under the Bond issue scheme dated 24 November 2015, based on the signed annexes to the agency and custody agreement as well as the underwriting agreement, which has been discussed in more detail in Note 32.2 to these consolidated financial statements.

Management Board of the Company

Katowice, 12 March 2018

Filip Grzegorczyk – President of the Management Board ....

Jarosław Broda – Vice-President of the Management Board ....

Kamil Kamiński – Vice-President of the Management Board ....

Marek Wadowski – Vice-President of the Management Board ....

Oliwia Tokarczyk – Executive Director in Charge of Taxes and Accounting ....

REPORT OF THE MANAGEMENT BOARD
ON OPERATIONS OF
TAURON POLSKA ENERGIA S.A. CAPITAL GROUP
FOR THE FINANCIAL YEAR 2017

MARCH 2018

TABLE OF CONTENTS

1. TAURON CAPITAL GROUP . . . 5
1.1. Basic Information on TAURON Capital Group . . . 5
1.2. Business segments (lines of business) . . . 6
1.3. TAURON Capital Group's organization and structure . . . 7
1.3.1. Units subject to consolidation . . . 7
1.3.2. Changes to TAURON Capital Group's organization . . . 8
1.3.3. Organizational or equity ties . . . 12
1.3.4. Major domestic and foreign investments . . . 14
1.4. Strategy and strategic priorities of TAURON Capital Group . . . 14
1.4.1. TAURON Capital Group's mission, vision and values . . . 15
1.4.2. TAURON Capital Group's 2016–2025 Strategy . . . 15
1.4.3. Key challenges for TAURON Capital Group . . . 19
1.4.4. Opportunities and threats . . . 20
1.4.5. Implementation of the Strategy and priorities of TAURON Capital Group in 2017 . . . 21
1.5. Description of TAURON Capital Group's expansion policy and directions . . . 23
1.5.1. Long term goals and financial assumptions of the Strategy . . . 24
1.5.2. Implementation of strategic investment projects . . . 25
1.5.3. Evaluation of the capability to complete the intended investment projects . . . 28
1.5.4. Building TAURON Capital Group's value . . . 28
1.5.5. Directions for advancing innovations as well as research and development activities . . . 28
1.5.6. Major achievements in the field of research and development . . . 29

2. TAURON CAPITAL GROUP'S OPERATIONS . . . 32
2.1. Factors and non-typical events that have a significant impact on earnings achieved . . . 32
2.1.1. Internal factors and the assessment thereof . . . 32
2.1.2. External factors and the assessment thereof . . . 32
2.1.2.1. Macroeconomic environment . . . 32
2.1.2.2. Market environment . . . 33
2.1.2.3. Regulatory environment . . . 40
2.1.2.4. Competitive environment (landscape) . . . 46
2.2. Material growth impacting factors . . . 50
2.3. TAURON Capital Group's financial results . . . 51
2.3.1. Mining Segment . . . 53
2.3.2. Generation Segment . . . 55
2.3.3. Distribution Segment . . . 58
2.3.4. Supply Segment . . . 60
2.3.5. Other operations . . . 62
2.4. What can be expected in 2018 . . . 63
2.5. Core products, goods and services . . . 64
2.6. Markets and sources of supply . . . 64
2.6.1. Markets . . . 64
2.6.2. Supply sources – fuel . . . 68
2.7. Timeline . . . 69
2.8. Key events and TAURON Capital Group's accomplishments with a significant impact on its operations . . . 70
2.9. Prizes and accolades (honorable mentions) . . . 75
2.10. Information on TAURON Capital Group's employment . . . 77
2.10.1. Policy of Human Resources Management at TAURON Group . . . 77
2.10.2. Development and training . . . 78
2.10.3. Social dialogue . . . 82
2.10.4. Key headcount data . . . 82
2.11. Corporate Social Responsibility (CSR) Policy . . . 84
2.11.1. Energy security . . . 85
2.11.2. Customer orientation . . . 86
2.11.3. Customer satisfaction survey . . . 87
2.11.4. Impact on natural environment . . . 88
2.11.5. Sponsoring activities . . . 92

3. RISK MANAGEMENT AT TAURON CAPITAL GROUP . . . 93
3.1. Risk management objective and principles . . . 93
3.2. Risk management using the “Three Defense Lines Model” . . . 93
3.3. Risk management process and its participants . . . 94
3.4. Architecture of the enterprise risk management system (ERM) . . . 95
3.4.1. Commercial (trading) risk management . . . 97
3.4.2. Financial risk management . . . 98
3.4.3. Credit risk management . . . 99
3.4.4. Operational risk management . . . 99
3.4.5. Project risk management . . . 100
3.5. Description of the most significant risks related to TAURON Capital Group’s operations . . . 101

4. ANALYSIS OF TAURON CAPITAL GROUP’S FINANCIAL POSITION AND ASSETS . . . 105
4.1. Overview of economic and financial data disclosed in the consolidated annual financial statements . . . 105
4.2. Characteristics of the structure of assets and liabilities on the consolidated balance sheet . . . 112
4.3. Material off-balance sheet items . . . 113
4.4. Differences between the financial results reported in the annual report and the forecasts of results for the given year published earlier . . . 114
4.5. Key financial and non-financial ratios . . . 114
4.6. Most significant financial and operating data of TAURON Capital Group for the last 5 years . . . 116
4.7. Proceeds from securities issues . . . 120
4.8. Financial instruments . . . 121
4.8.1. Application of financial instruments in order to eliminate price changes, credit risk, material disruptions of cash flows and loss of financial liquidity . . . 121
4.8.2. Objectives and methods of financial risk management . . . 121
4.9. Current and forecast financial situation (financial outlook) . . . 121
4.10. Assessment of financial resources management . . . 122
4.11. Principles of preparing annual consolidated financial statements . . . 122
4.12. Information on the entity authorized to audit financial statements . . . 123

5. SHARES AND SHAREHOLDERS . . . 124
5.1. Structure of shareholding . . . 124
5.2. Dividend policy . . . 124
5.3. Number and nominal value of the Company’s shares, as well as of the shares in units related to the Company, held by members of the Management Board and the Supervisory Board . . . 125
5.4. Agreements related to potential changes to the shareholding structure . . . 125
5.5. Own shares buybacks . . . 125
5.6. Employee stock award programs . . . 125
5.7. Shares performance on the Warsaw Stock Exchange (WSE) . . . 125
5.8. Investor relations . . . 128

6. STATEMENT ON APPLICATION OF CORPORATE GOVERNANCE . . . 131
6.1. Indication of applied set of corporate governance rules . . . 131
6.2. Indication of abandoned rules of corporate governance . . . 131
6.3. Description of main characteristics of internal control and risk management systems in relation to the process of generating the financial statements and consolidated financial statements . . . 132
6.4. Shareholders holding substantial blocks of shares . . . 134
6.5. Holders of securities providing special control rights . . . 134
6.7. Restrictions on transfer of securities ownership right . . . 136
6.8.1. Management Board . . . 136
6.8.2. Supervisory Board . . . 136
6.9. Description of the procedure of amendment of the Company’s Articles of Association . . . 137
6.10. Procedures of the General Meeting of Shareholders, its fundamental powers and description of shareholders’ rights and the manner of exercising thereof . . . 140
6.11. Composition of the Company’s managing and supervising bodies and their committees, its changes, description of operation . . . 140
6.11.1. Management Board . . . 142
6.11.2. Supervisory Board . . . 144
6.11.3. Audit Committee . . . 150
6.11.4. Nominations and Compensation Committee . . . 151

6.11.5. Strategy Committee . . . 152
6.11.6. Description of activities of the Committees of the Supervisory Board . . . 153
6.12. Description of the policy of diversity applied to the governing bodies of the Company . . . 153

7. COMPENSATION POLICY WITH RESPECT TO THE MANAGEMENT AND SUPERVISORY STAFF . . . 155
7.1. Compensation system for members of the Management Board and key managers . . . 155
7.1.1. General information on the adopted compensation system for members o155f the Management Board . . . 155
7.1.2. General information on the adopted compensation system for key managers . . . 155
7.1.3. Rules, terms and conditions as well level of compensation of members of the Management Board . . . 156
7.1.4. Agreements concluded with managing persons which envisage compensation in case of their resignation or dismissal from the position held, without material reason, or if their dismissal or resignation takes place as a result of the merger of the Company through takeover . . . 158
7.1.5. Non-financial components of compensation allocated to members of the Management Board and key managers . . . 158
7.1.6. Information on changes to the compensation policy over the last financial year . . . 158
7.1.7. Assessment of functioning of the compensation policy in terms of fulfilment of its objectives, in particular, the long-term growth in shareholders' value and stability of the undertaking performance . . . 158
7.2. Compensation system for members of the Supervisory Board . . . 159
7.3. Liabilities arising from pensions and similar benefits for former the Members of the Management Board and the Supervisory Board . . . 160

8. STATEMENT ON NON-FINANCIAL INFORMATION . . . 161
8.1. TAURON Group's Business and Operational Model . . . 161
8.1.1. Assumptions of the Business Model . . . 161
8.1.2. Company management principles . . . 161
8.1.3. TAURON Capital Group management principles . . . 161
8.1.4. TAURON Capital Group's Lines of Business . . . 163
8.1.5. Changes in the principles of managing TAURON Capital Group . . . 164
8.2. Key non-financial performance indicators in operations of TAURON Capital Group . . . 167
8.3. Description of TAURON's policies . . . 168
8.3.1. Social issues . . . 168
8.3.2. Employee issues . . . 168
8.3.3. Natural environment . . . 168
8.3.4. Respect of human rights . . . 169
8.3.5. Countering corruption . . . 169
8.4. Description of the results of application of policies by TAURON . . . 169
8.5. Description of due diligence procedures in operation under the policies applied by TAURON . . . 170
8.6. Description of significant risks related to operations of TAURON that may exert adverse impact on the policies applied by TAURON, as well as description of management of these risks . . . 171

9. OTHER MATERIAL INFORMATION AND EVENTS . . . 175
9.1. Proceedings pending before the court, competent arbitration authority or public administration authority . . . 175
9.2. Information on agreements concluded by TAURON Capital Group's subsidiaries . . . 175
9.2.1. Agreements significant for TAURON Capital Group's operations . . . 175
9.2.2. Transactions with related entities on terms other than at arm's length . . . 177
9.2.3. Signed and terminated credit and loan agreements . . . 177
9.2.4. Loans and sureties granted as well as sureties and guarantees received . . . 179
9.3. Information on other agreements and events . . . 182

APPENDIX A: GLOSSARY OF TERMS AND LIST OF ABBREVIATIONS . . . 186

APPENDIX B: INDEX OF TABLES AND FIGURES . . . 190

1. TAURON CAPITAL GROUP

1.1. Basic Information on TAURON Capital Group

TAURON Polska Energia S.A. Capital Group (TAURON Capital Group) is a vertically integrated energy group located in the south of Poland. TAURON Capital Group conducts its operations in all key segments of the energy market (excluding electricity transmission which is the sole responsibility of the Transmission System Operator (TSO)), i.e. hard coal mining as well as electricity and heat generation, distribution and trading.

Figure no. 1. TAURON Capital Group

TAURON POLSKA ENERGIA S.A.
the holding company in TAURON Capital Group
Supervises corporate functions: management, strategic investment, regulations, human resources, finance, controlling, internal audit, PR, investor relations, procurement

MINING

29% of steam coal resources in Poland

- 3 hard coal mines in 2016
- commercial coal production: 6.4 million Mg, including 72% used within TAURON Capital Group, and 28% sold to external clients
- EBITDA of the segment for 2017: PLN (83) million

GENERATION

One of the largest producer of electricity in Poland

- 8 conventional power plants and CHP plants with electric capacity of 4.6 GW_e and thermal capacity of 2.4 GW_t
- 4 wind farms with the total capacity of 201 MW_e
- 34 hydroelectric power plants with the total capacity of 139 MW_e
- 842 km of heat networks
- 18.4 TWh of gross electricity output, including 0.3 TWh from biomass
- 1.0 TWh of gross electricity production from wind and hydroelectric sources
- 12.2 PJ of heat production
- EBITDA of the segment for 2017: PLN 464 million

DISTRIBUTION

the largest electricity distributor in Poland

- approx. 5.5 million clients
- distribution across the area of 57.1 thousand km^2, i.e. 18.3% of the territory of Poland
- 51.4 TWh of electricity distributed
- EBITDA of the segment for 2017: PLN 2 283 million

SALES

the second largest electricity supplier in Poland

- approx. 5.4 million clients
- 34.9 TWh of electricity retail sales
- EBITDA of the segment for 2017: PLN 841 million

OTHER

- services provided to consumers of electricity and distribution services for companies of TAURON Capital Group
- provision of support services for entities of TAURON Capital Group in the following areas: Accounting, IT and HR
- limestone mining for the needs of power engineering, metallurgical industry, construction and road building
- acquisition, transport and processing of biomass for the needs of professional power sector
- technical service of vehicles
- real estate administration
- financial activities
- EBITDA of the segment for 2017: PLN 118 million

1.2. Business segments (lines of business)

Business operations, in accordance with *TAURON Group's Business and Operational Model* (Business Model) in force, are conducted by units defined as: Corporate Center, seven Lines of Business, i.e. Trading, Mining, Generation, Renewable Energy Sources (RES), Heat, Distribution and Supply as well as Shared Services Centers (CUW). The detailed information on the Business Model was concluded in section 8.1. of this report.

For the needs of reporting TAURON Capital Group's results from operations TAURON Capital Group's operations are split into the following five Segments, hereinafter also referred to as Lines of Business:

Mining segment, comprising mainly hard coal mining, enriching and selling in Poland with such operations conducted by TAURON Wydobycie S.A. (TAURON Wydobycie).

Generation segment, comprising mainly electricity generation using conventional sources, including co-generation, as well as electricity generation from renewable energy sources, including biomass burning and co-firing, and hydroelectric power plants and wind farms. The segment also includes heat generation, distribution and supply. This segment's operations are conducted by TAURON Wytwarzanie S.A. (TAURON Wytwarzanie), TAURON Ciepło sp. z o.o. (TAURON Ciepło) and TAURON EKOENERGIA sp. z o.o. (TAURON EKOENERGIA). The segment also includes TAURON Serwis sp. z o.o. (TAURON Serwis) subsidiary, dealing primarily with the generation equipment's overhauls and Nowe Jaworzno Grupa TAURON Sp. z o.o. (Nowe Jaworzno GT) company responsible for the construction of the new power generation unit at Jaworzno.

Distribution segment, comprising electricity distribution using the distribution grids located in southern Poland. The operations are conducted by TAURON Dystrybucja S.A. (TAURON Dystrybucja). This segment also includes the following subsidiaries: TAURON Dystrybucja Serwis S.A. (TAURON Dystrybucja Serwis) and TAURON Dystrybucja Pomiary sp. z o.o. (TAURON Dystrybucja Pomiary).

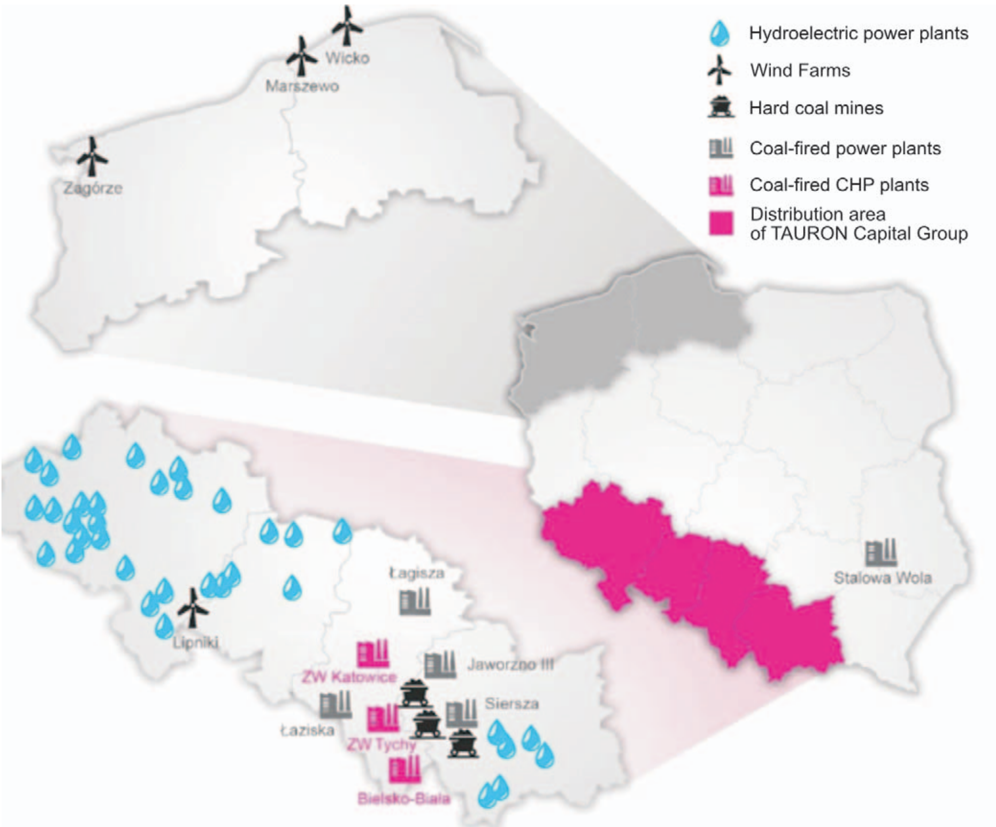
Supply segment, comprising electricity supply to the final consumers and electricity wholesale trading, as well as trading and management of CO_2 emission allowances and property rights arising from certificates of origin as well as fuels. The operations in this segment are conducted by the following subsidiaries: TAURON Polska Energia S.A. (TAURON or the Company), TAURON Sprzedaż sp. z o.o. (TAURON Sprzedaż), TAURON Sprzedaż GZE sp. z o.o. (TAURON Sprzedaż GZE) and TAURON Czech Energy s.r.o. (TAURON Czech Energy).

Other operations, comprising, among others, customer service for TAURON Capital Group's customers, provision of support services for TAURON Capital Group's subsidiaries with respect to accounting, HR and ICT, conducted by TAURON Obsługa Klienta sp. z o.o. (TAURON Obsługa Klienta) subsidiary, as well as operations related to extraction of stone, including limestone, for the needs of power generation, steel, construction and road building industries as well as production of sorbing agents for wet flue gas desulphurization installations and for use in fluidized bed boilers, carried out by Kopalnia Wapienia "Czatkowice" sp. z o.o. (KW Czatkowice) subsidiary. This segment also includes the following subsidiaries: TAURON Sweden Energy AB (publ) (TAURON Sweden Energy), dealing with financial operations, Biomasa Grupa TAURON sp. z o.o., (Biomasa Grupa TAURON), dealing mainly with biomass acquisition, transportation and processing, KOMFORT-ZET sp. z o.o. (KOMFORT-ZET) dealing primarily with real estate administration as well as the technical support of vehicles and Polska Energia – Pierwsza Kompania Handlowa sp. z o.o. (PEPKH).

TAURON Capital Group conducts its operations and generates its revenue mainly from electricity and heat supply and distribution, electricity and heat generation, as well as from hard coal sales.

The below figure presents the location of TAURON Capital Group's key assets as well as the distribution area where TAURON Dystrybucja conducts operations as the Distribution System Operator.

Figure no. 2. Location of TAURON Capital Group's key assets



1.3. TAURON Capital Group's organization and structure

TAURON Polska Energia S.A. parent (holding) company was established on December 6, 2006 as part of the *Program for the Power Generation Sector*. The founders of the Company included: State Treasury represented by the Minister of Treasury, EnergiaPro S.A. with its seat in Wrocław (currently: TAURON Dystrybucja), ENION S.A. with its seat in Cracow (currently: TAURON Dystrybucja) and Elektrownia Stalowa Wola S.A. with its seat in Stalowa Wola (currently: TAURON Wytwarzanie). The Company was registered in the National Court Register on January 8, 2007 under the name: Energetyka Południe S.A. The change of the Company's name to its current one, i.e. TAURON Polska Energia S.A., was registered on November 16, 2007.

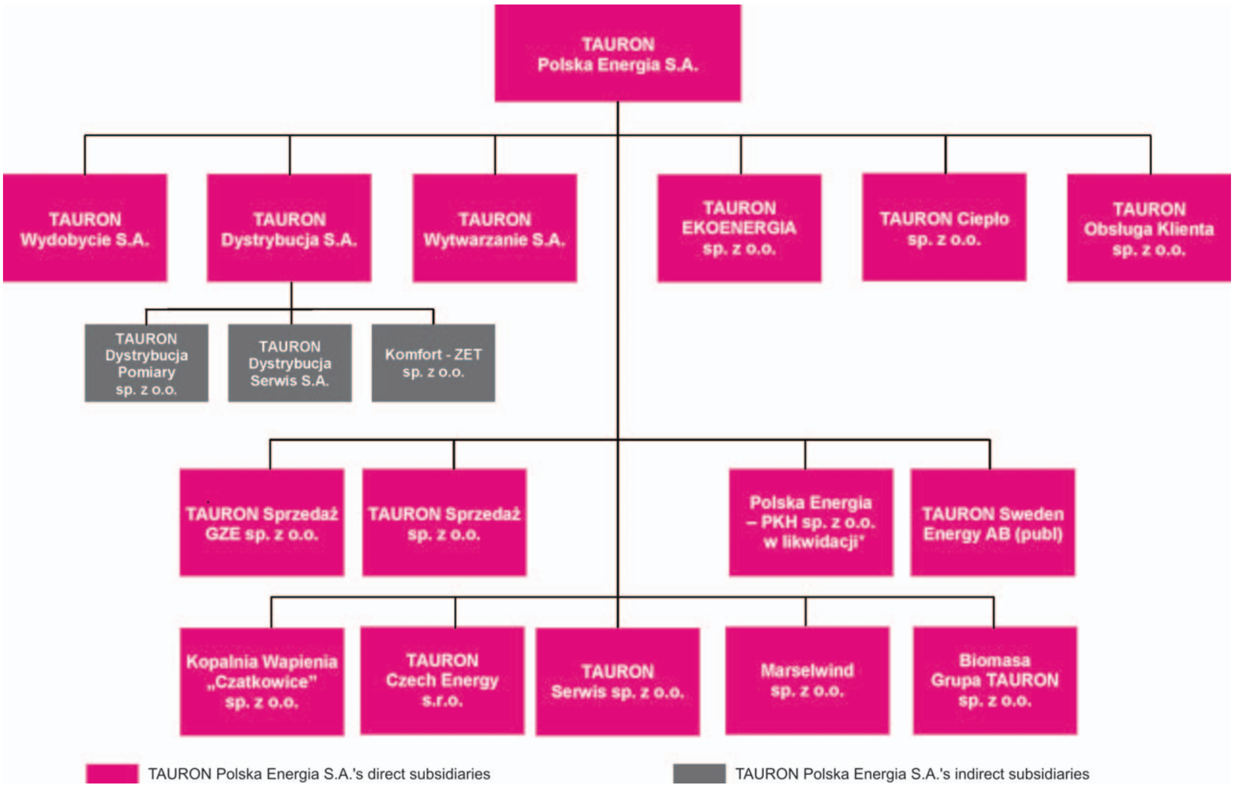
The company does not have any branches (plants).

As of December 31, 2017 TAURON Capital Group's key subsidiaries, besides the TAURON parent company, included 19 subsidiaries subject to consolidation, listed in section 1.3.1. of this report. Furthermore, as of December 31, 2017, the Company held, directly or indirectly, shares in the other 38 subsidiaries.

1.3.1. Units subject to consolidation

The below figure presents TAURON Capital Group's structure, including the subsidiaries subject to consolidation, as of December 31, 2017.

Figure no. 3. TAURON Capital Group's structure, including the subsidiaries subject to consolidation, as of December 31, 2017



TAURON Capital Group also holds stakes in joint ventures: Elektrociepłownia Stalowa Wola S.A. (EC Stalowa Wola) and TAMEH HOLDING sp. z o.o. (TAMEH HOLDING), TAMEH POLSKA sp. z o.o. (TAMEH POLSKA) and TAMEH Czech s.r.o. (TAMEH Czech) that are valued using the equity method in the consolidated financial statements.

Detailed information on subsidiaries subject to consolidation and TAURON's share in their share capital, as well in the parent company, is provided in section 1.3.3. of this report.

1.3.2. Changes to TAURON Capital Group's organization

In 2017 and by the day of drawing up this report the following changes to the organization of TAURON Capital Group had taken place:

Split of TAURON Wytwarzanie by transferring assets to the newly established "Nowe Jaworzno Grupa TAURON sp. z o.o." company

On January 31, 2017 the Extraordinary GM of TAURON Wytwarzanie passed a resolution on the split of TAURON Wytwarzanie subsidiary by way of spinning off under art. 529 § 1 clause 4) of the Commercial Companies Code, i.e. by transferring some assets of TAURON Wytwarzanie in the form of an organized part of the enterprise including the investment process related to the construction of the new 910 MW power generation unit at Jaworzno III Power Plant, carried out by TAURON Wytwarzanie Oddział Elektrownia Jaworzno III in Jaworzno, to the newly established Nowe Jaworzno GT company (in organization) in exchange for 37 000 shares in the Nowe Jaworzno GT company with the nominal value of PLN 50 per share and the total nominal value of PLN 1 850 000 that were taken up by the sole shareholder of the split company – TAURON.

The split process is the result of the implementation of *TAURON Group's 2016–2025 Strategy* according to which the 910 MW unit construction project at Jaworzno III Power Plant will be carried out under a new financing formula, assuming spinning off out of TAURON Wytwarzanie of an organized part of the enterprise and selling a stake therein to external partners.

On April 3, 2017 Nowe Jaworzno GT company was registered in the National Court Register.

Establishing new companies (subsidiaries)

1. On August 1, 2017 Komfort Zarządzanie Aktywami sp. z o.o. (Komfort Zarządzanie Aktywami) company was registered in the National Court Register in organization with its seat in Katowice that had been established on May 25, 2017. Upon registration the company's share capital was PLN 5 000 and was split into 100 shares with the nominal value of PLN 50 per share that were taken up in the following way:
   1) Wsparcie Grupa TAURON (formerly KOMFORT-ZET sp. z o.o.) with its seat in Tarnów took up 99 shares,
   2) TAURON Dystrybucja Pomiary with its seat in Tarnów took up 1 share.

   The company was established in order to concentrate therein minority shares held by TAURON Capital Group's subsidiaries in commercial law companies that are not subsidiaries, joint subsidiaries and associated companies, including companies undergoing liquidation and bankruptcy proceedings, and then sell the company outside of TAURON Capital Group.
2. On August 1, 2017 TAURON established four limited liability companies with their seats in Katowice under the following names:
   1) En-Energia I sp. z o.o. (registered in the National Court Register on September 8, 2017),
   2) En-Energia II sp. z o.o. (registered in the National Court Register on September 30, 2017),
   3) En-Energia III sp. z o.o. (registered in the National Court Register on September 1, 2017),
   4) En-Energia IV sp. z o.o. (registered in the National Court Register on September 14, 2017).

   In each of the above-mentioned companies TAURON took up all of the 100 shares with the nominal value of PLN 50 per share and the total nominal value of PLN 5 000. The above-mentioned companies were established as special purpose vehicles in conjunction with the reorganization projects underway at TAURON Capital Group.

Purchases of shares in other companies

1. In conjunction with the August 9, 2017 conclusion of the agreement between TAURON and TAURON Dystrybucja on the transfer of shares in TAURON Dystrybucja Serwis in order to release TAURON Dystrybucja from the obligation to pay out a dividend to TAURON (datio in solutum), TAURON became the owner of 5 101 003 shares in TAURON Dystrybucja Serwis, used up to now from TAURON Dystrybucja, representing 100% of shares in its share capital.
2. Under the share purchase agreement of November 16, 2017 TAURON Dystrybucja Pomiary acquired from Wsparcie Grupa TAURON 99 shares in Komfort Zarządzanie Aktywami company. This way TAURON Dystrybucja Pomiary became the owner of 100% shares in Komfort Zarządzanie Aktywami and its sole shareholder. The above action was one of the stages of the initiative implemented by TAURON Capital Group, aimed at concentrating in Komfort Zarządzanie Aktywami company the minority stakes and shares held by TAURON Capital Group's subsidiaries in commercial law companies that are not subsidiaries, joint subsidiaries and associated companies, including ones in the course of liquidation and bankruptcy proceedings, and then a sale of the company outside TAURON Capital Group.
3. Furthermore, as part of the initiative described above in section 2, Komfort Zarządzanie Aktywami company acquired from TAURON Capital Group's subsidiaries minority stakes in the below companies:
   1) Huta Batory S.A. in bankruptcy,
   2) Concorde Investissement S.A.,
   3) Opolskie Zakłady Przemysłu Lniarskiego "Linopłyt" S.A. in liquidation in bankruptcy,
   4) LEN S.A. in liquidation,
   5) Przędzalnia Czesankowa "ELANEX" S.A. in liquidation,
   6) Stilna S.A.,
   7) ZMK S.A. in liquidation,
   8) Przedsiębiorstwo Budowlane Katowice S.A. in liquidation,
   9) CFI Holding S.A.

Increase of the subsidiaries' share capital

1. On April 7, 2017 the District Court for Katowice-Wschód, 8th Commercial Department registered in the National Court Register an increase in the share capital of Tauron Wydobycie, passed by the Extraordinary GM of TAURON Wydobycie on March 21, 2017. The subsidiary's share capital was increased from PLN 355 510 780 to PLN 357 110 780, i.e. by PLN 1 600 000, by way of issuance of 160 000 new "K" series registered shares with the nominal value of PLN 10 per share and the total nominal value of PLN 1 600 000. All of the "K" series shares were taken up, by way of a private placement subscription, by the subsidiary's sole shareholder – TAURON, at the price of PLN 1 000 per share, i.e. for the total amount of PLN 160 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 990 per each new share, i.e. in the total amount of PLN 158 400 000, was allocated to the company's spare capital.
2. On June 26, 2017 the District Court for Katowice-Wschód, 8th Commercial Department registered in the National Court Register an increase in the share capital of Nowe Jaworzno GT, passed by the Extraordinary GM of the company on May 16, 2017. The subsidiary's share capital was increased from PLN 1 850 000 to PLN 31 850 000, i.e. by PLN 30 000 000, by way of issuance of 600 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 30 000 000. All of the new shares were taken up by the subsidiary's existing sole shareholder – TAURON. at the price of PLN 5 000 per share, i.e. for the total amount of PLN 3 000 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 2 970 000 000, was allocated to the company's spare capital.

   On July 13, 2017 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of Nowe Jaworzno GT, passed by the Extraordinary GM of Nowe Jaworzno GT on June 29, 2017. The subsidiary's share capital was increased from PLN 31 850 000 to PLN 35 850 000, i.e. by PLN 4 000 000, by way of issuance of 80 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 400 000 000. All of the new shares were taken up by the subsidiary's existing sole shareholder – TAURON. at the price of PLN 5 000 per share, i.e. for the total amount of PLN 400 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 396 000 000, was allocated to the company's spare capital.
3. On June 20, 2017 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of TAURON Ciepło, passed by the Extraordinary GM of TAURON Ciepło on May 11, 2017. The subsidiary's share capital was increased from PLN 1 098 348 500 to PLN 1 104 348 500, i.e. by PLN 6 000 000, by way of issuance of 120 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 6 000 000. All of the new shares were taken up by the subsidiary's existing sole shareholder – TAURON. at the price of PLN 5 000 per share, i.e. for the total amount of PLN 600 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 594 000 000 was allocated to the company's spare capital.
4. On October 13, 2017 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of Marselwind sp. z o.o. (Marselwind) passed by the Extraordinary GM of the company on June 28, 2017. The subsidiary's share capital was increased from PLN 105 000 to PLN 110 000, i.e. by PLN 5 000, by way of issuance of 100 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 5 000. All of the new shares were taken up by TAURON at the price of PLN 5 000 per share, i.e. for the total amount of PLN 200 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 1 950 per each new share, i.e. in the total amount of PLN 195 000 was allocated to the company's spare capital.
5. On January 11, 2018 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of Magenta Grupa TAURON sp. z o.o. (Magenta GT), passed by the Extraordinary GM of the company on October 24, 2017. The subsidiary's share capital was increased from PLN 500 000 to PLN 1 500 000, i.e. by PLN 1 000 000, by way of issuance of 20 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 1 000 000. All of the new shares were taken up by the subsidiary's existing sole shareholder – TAURON at the price of PLN 450 per share, i.e. for the total amount of PLN 9 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 400 per each new share, i.e. in the total amount of PLN 8 000 000 was allocated to the company's spare capital.
6. On March 2, 2018, the District Court for Wrocław-Fabryczna in Wrocław, 9th Commercial Department, registered in the National Court Register an increase in the share capital of TAURON EKOENERGIA passed by the Extraordinary GM on October 24, 2017. The share capital was increased by PLN 10 000 000 by way of issuing 10

000 new shares with the nominal value of PLN 1 000 each and the total nominal value of PLN 10 000 000. All the new shares were taken up by the existing sole shareholder of the company – TAURON at the price of PLN 100 000 per share, i.e. for the total amount of PLN 1 000 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 99 000 per each new share, i.e. in the total amount of PLN 990 000 000 was allocated to the company's spare capital.

7. On December 29, 2017 the District Court for Kraków-Śródmieście in Kraków, 11th Commercial Department, registered in the National Court Register an increase in the share capital of TAURON Dystrybucja subsidiary, passed by the Extraordinary GM of the company on October 26, 2017. The subsidiary's share capital was increased from PLN 511 925 759.22 to PLN 560 611 250.96, i.e. by PLN 48 685 491.74, by way of issuing 2 434 274 587 new ordinary registered shares with the nominal value of PLN 0.02 each, i.e. with the total amount of PLN 48 685 491.74. All of the shares will were taken up by TAURON at the price of PLN 0.4108 per share, i.e. for the total amount of PLN 1 000 000 000.34, where the surplus of the issuing price of each share above its nominal value in the amount of PLN 0,3908 per each such share, i.e. in the total amount of PLN 951 314 508.60 was allocated to the company's spare capital.

   In conjunction with the increase of the share capital TAURON's share in the subsidiary's share capital increased from 99.72% to 99.74%.

8. On January 22, 2018 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of En-Energia II sp. z o.o., passed by the Extraordinary GM of the company on December 15, 2017. The subsidiary's share capital was increased from PLN 5 000 to PLN 5 800, i.e. by PLN 800, by way of issuance of 16 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 800. All of the new shares were taken up by TAURON at the price of PLN 5 000 per share, i.e. for the total amount of PLN 80 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 79 200 was allocated to the company's spare capital.

9. On January 24, 2018 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of En-Energia I sp. z o.o., passed by the Extraordinary GM of the company on December 15, 2017. The subsidiary's share capital was increased from PLN 5 000 to PLN 5 800, i.e. by PLN 800, by way of issuance of 16 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 800. All of the new shares were taken up by TAURON at the price of PLN 5 000 per share, i.e. for the total amount of PLN 80 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 79 200 was allocated to the company's spare capital.

10. On February 26, 2018 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of En-Energia IV sp. z o.o., passed by the Extraordinary GM of the company on December 15, 2017. The subsidiary's share capital was increased from PLN 5 000 to PLN 5 800, i.e. by PLN 800, by way of issuance of 16 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 800. All of the new shares were taken up by TAURON at the price of PLN 5 000 per share, i.e. for the total amount of PLN 80 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 79 200 was allocated to the company's spare capital.

11. On March 8, 2018 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of of En-Energia III sp. z o.o passed by the Extraordinary GM on December 15, 2017. The share capital was increased by from PLN 5 000 to PLN 5 800, i.e. by PLN 800, by way of issuing 10 000 new shares with the nominal value of PLN 1 000 each and the total nominal value of PLN 10 000 000. All of the new shares were taken up by TAURON at the price of PLN 5 000 per share, i.e. for the total amount of PLN 80 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 79 200 was allocated to the company's spare capital.

12. On February 15, 2018 the District Court for Katowice-Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of Komfort Zarządzanie Aktywami passed by the Extraordinary GM of the company on December 8, 2017. The subsidiary's share capital was increased from PLN 5 000 to PLN 52 500, i.e. by PLN 47 500, by way of issuance of 950 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 47 500. All of the new shares were taken up by the existing sole shareholder of the company – TAURON Dystrybucja Pomiary at the price of PLN 100 per share, i.e. for the total amount of PLN 95 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 50 per each new share, i.e. in the total amount of PLN 47 500 was allocated to the company's spare capital.

13. On January 3, 2018 the Extraordinary General Meeting of the Shareholders of ElectroMobility Poland S.A. passed a resolution on increasing the company's share capital from PLN 10 000 000 to PLN 30 000 000, i.e. by PLN 20 000 000, by way of increasing the nominal value of the existing shares from PLN 1 000 per share up to PLN 3 000 per share, as part of which TAURON took up, in proportion to the shares held, the increased nominal value of 2 500 shares held from the total amount of PLN 2 500 000 up to the total amount of PLN 7 500 000, i.e. in the total amount of PLN 5 000 000.

    As of the day of drawing up this information the increase of the share capital was not yet registered in the National Court Register.

Revoking of the liquidation of the PEPKH subsidiary

On March 8, 2017 the Extraordinary GM of the PEPKH subsidiary in liquidation, pursuant to art. 273 of the Commercial Companies Code, passed the resolution on the further existence of the company and revoking its liquidation.

The revoking of the company's liquidation was due to the change of the conditions related to the liquidation proceedings underway, indicating the purposefulness of the further existence of the company.

Conversion of Komfort-ZET sp. z o.o. into Wsparcie Grupa TAURON sp. z o.o.

Conversion of Komfort-ZET sp. z o.o. with its seat in Tarnów into Wsparcie Grupa TAURON sp. z o.o. was registered in the National Court Register on September 6, 2017.

Restoring TAURON EKOENERGIA's share capital to the level from before the company's split

On January 30, 2018 the District Court for Wrocław-Fabryczna in Wrocław, 9th Commercial Department, registered in the National Court Register a change in the share capital of TAURON EKOENERGIA restoring its value to the level from before the company's split by spinning off and transferring to the Marselwind company and the decrease of the share capital of TAURON EKOENERGIA passed by the Extraordinary GM of the company on February 9, 2015. Due to the restoration of the share capital from before the company's split the capital was increased from PLN 444 888 000 to PLN 573 423 000, i.e. by PLN 128 535 000, and the number of shares held by the sole shareholder of the company – TAURON increased from 444 888 shares to 573 423 shares.

Contribution of additional payments to the capital of PEPKH

Acting in accordance with the resolution of the Extraordinary GM PEPKH of March 1, 2018 on imposing on TAURON as a sole shareholder an obligation to make additional payments, on March 7, 2018 TAURON contributed additional payments to the share capital of the above mentioned company in the total amount of PLN 6 000 thou. The resolution of the Extraordinary GM as passed in order to ensure financing for the operations of PEPKH.

1.3.3. Organizational or equity ties

The below table presents a list of material direct or indirect subsidiaries subject to consolidation in which the Company held shares as of December 31, 2017.

Table no. 1. List of material subsidiaries subject to consolidation as of December 31, 2017

No.	Company name	Registered Office	Main subject of operations	TAURON's share in the subsidiary's capital	TAURON's share in the subsidiary's parent company
1.	TAURON Wydobycie	Jaworzno	Hard coal mining	100.00%	100.00%
2.	TAURON Wytwarzanie[1]	Jaworzno	Electricity and heat generation, transmission and distribution	100.00%	100.00%
3.	Nowe Jaworzno GT[1]	Jaworzno	Electricity and heat generation, transmission and distribution, as well as electricity trading	100.00%	100.00%
4.	TAURON EKOENERGIA	Jelenia Góra	Electricity generation	100.00%	100.00%
5.	Marselwind	Katowice	Electricity generation, transmission and trading	100.00%	100.00%
6.	TAURON Ciepło	Katowice	Heat production and distribution	100.00%	100.00%
7.	TAURON Serwis	Katowice	Services	95.61%	95.61%

No.	Company name	Registered Office	Main subject of operations	TAURON's share in the subsidiary's capital	TAURON's share in the subsidiary's parent company
8.	TAURON Dystrybucja	Kraków	Electricity distribution	99.74%	99.75%
9.	TAURON Dystrybucja Serwis	Wrocław	Services	100.00%	100.00%
10.	TAURON Dystrybucja Pomiary[2]	Tarnów	Services	99.74%	99.75%
11.	TAURON Sprzedaż	Kraków	Electricity trading	100.00%	100.00%
12.	TAURON Sprzedaż GZE	Gliwice	Electricity trading	100.00%	100.00%
13.	TAURON Czech Energy	Ostrava, Czech Republic	Electricity trading	100.00%	100.00%
14.	TAURON Obsługa Klienta	Wrocław	Services	100.00%	100.00%
15.	KW Czatkowice	Krzeszowice	Limestone and rock extraction	100.00%	100.00%
16.	PEPKH[3]	Warszawa	Electricity trading	100.00%	100.00%
17.	TAURON Sweden Energy	Stockholm, Sweden	Services	100.00%	100.00%
18.	Biomasa Grupa TAURON	Stalowa Wola	Waste and scrap metal wholesale	100.00%	100.00%
19.	Wsparcie Grupa TAURON[2, 4]	Tarnów	Services	99.74%	99.75%

[1] On April 3, 2017 TAURON Wytwarzanie subsidiary was split and an organzed part of the enterprise was spun off to Nowe Jaworzno GT subsidiary.
[2] Share in TAURON Dystrybucja Pomiary and Wsparcie Grupa TAURON (formerly KOMFORT-ZET sp. z o.o.) is held by TAURON indirectly via TAURON Dystrybucja subsidiary. TAURON is a user of TAURON Dystrybucja Pomiary subsidiary's shares.
[3] On March 8, 2017 the Extraordinary GM of the PEPKH subsidiary in liquidation passed a resolution on revoking the liquidation of this company.
[4] On September 6, 2017 KOMFORT-ZET sp. z o.o. changed its name to "Wsparcie Grupa TAURON sp. z o.o.".

The below table presents a list of material joint subsidiaries subject to consolidation in which the Company held shares as of December 31, 2017.

Table no. 2. List of material joint subsidiaries subject to consolidation as of December 31, 2017

No.	Company name	Registered Office	Main subject of operations	TAURON's share in the capital and subsidiary's parent company
1.	EC Stalowa Wola[1]	Stalowa Wola	Electricity generation	50.00%
2.	TAMEH HOLDING[2]	Dąbrowa Górnicza	Central companies and holding operations	50.00%
3.	TAMEH POLSKA[2]	Dąbrowa Górnicza	Electricity and heat generation, transmission, distribution and trading	50.00%
4.	TAMEH Czech[2]	Ostrawa, Republika Czeska	Production, trading and services	50.00%

[1] Share in EC Stalowa Wola is held by TAURON indirectly via TAURON Wytwarzanie subsidiary.
[2] Subsidiaries form a capital group. TAURON holds a diet share in the capital and the parent company of TAMEH HOLDING subsidiary that holds a 100% share in the capital and the parent company of TAMEH POLSKA and TAMEH Czech.

As of the day of drawing up this report TAURON holds, directly or indirectly, shares in 57 subsidiaries of TAURON Capital Group.

The other most important equity investments in financial assets as of December 31, 2017 include involvement in the following entities:

1. SCE Jaworzno III sp. z o.o. worth PLN 36 283 thousand,
2. Przedsiębiorstwo Energetyki Cieplnej Tychy sp. z o.o. worth PLN 32 483 thousand,
3. PGE EJ 1 sp. z o.o. (PGE EJ 1) worth PLN 26 546 thousand,
4. Energetyka Cieszyńska sp. z o.o. worth PLN 15 063 thousand.

1.3.4. Major domestic and foreign investments

Taking up or purchasing share securities

With respect to purchasing or taking up shares in TAURON Capital Group's subsidiaries major investments made by the Company include:

1. Taking up by TAURON of 717 thousand new shares in the share capital of Nowe Jaworzno GT (three times in 2017, i.e.: upon establishing the company and twice increasing the share capital), for the total amount of PLN 3 400 000 thousand.
2. Taking up by TAURON, by way of a private placement, of 2 434 274 587 new shares in the increased share capital of TAURON Dystrybucja at the price of 0.4108 per share, for the total amount of PLN 1 000 000 thousand.
3. Taking up by TAURON of 10 thousand new shares in the increased share capital of TAURON EKOENERGIA at the price of PLN 100 thousand per share, for the total amount of PLN 1 000 000 thousand.
4. Taking up by TAURON of 120 thousand new shares in the increased share capital of TAURON Ciepło at the price of PLN 5 thousand per share, for the total amount of PLN 600 000 thousand.
5. Taking up by TAURON of 160 thousand new shares in the increased share capital of TAURON Wydobycie at the price of PLN 1 thousand per share, for the total amount of PLN 160 000 thousand.
6. Taking up by TAURON of 20 thousand new shares in the increased share capital of Magenta GT at the price of PLN 450 per share, for the total amount of PLN 9 000 thousand.
7. Taking up by TAURON from TAURON Dystrybucja of 5 101 003 shares in TAURON Dystrybucja Serwis, of the total value of PLN 201 045 thousand, representing 100% shares in the share capital of TAURON Dystrybucja Serwis.

Major investments in financial assets

TAURON Capital Group's major investments in financial assets include:

1. Purchasing by TAURON, being the parent company, of participation units in investment funds for the total amount of PLN 75 000 thousand. As of the balance sheet day the value of participation units in investment funds reached PLN 101 358 thousand.
2. Granting by TAURON, being the parent company, of loans to the EC Stalowa Wola joint subsidiary for the total amount of PLN 304 192 thousand. As of the balance sheet day the amount of loans granted to EC Stalowa Wola reached PLN 570 432 thousand.

Investments in financial assets were finance using own funds and the funds obtained as part of the central financing model functioning at TAURON Capital Group. With respect to the above additionally it should be indicated that to finance the transactions: taking up of shares in the increased share capital of TAURON Dystrybucja and taking up of shares in the increased share capital of TAURON EKOENERGIA the funds coming from TAURON Eurobond issue that had taken place on July 5, 2017 were dedicated. Taking up of shares in the above indicated companies represented accomplishing the main goal of the issue stated in the Eurobond issue prospectus, according to which the funds obtained from the issue were to be used, first of all, to refinance the costs of constructing and purchasing wind farms and to finance the investments of TAURON Capital Group in the Distribution segment.

1.4. Strategy and strategic priorities of TAURON Capital Group

TAURON Group's 2016–2025 Strategy (Strategy), adopted by the Management Board of TAURON on September 2, 2016 and positively evaluated by the Supervisory Board, was implemented in 2017. This Strategy is the response to the challenges stemming from the current and forecast situation on the electricity market and in the power sector. In the process of preparing the Strategy a thorough analysis was conducted of the macroeconomic, market and regulatory environment as well as of the forecasts on the directions of the sector's growth, including translating them into opportunities and risks facing TAURON Capital Group over the next ten years. TAURON Capital Group's ability to finance the current and planned investment projects was reviewed in detail with a view that their completion could be achieved using funds generated from operations and debt financing. The above analyses and market trends were the basis for verifying market and macroeconomic assumptions as well as the CAPEX plan.

1.4.1. TAURON Capital Group's mission, vision and values

Strategy defines the Mission and Vision and defines the key values of TAURON Capital Group:

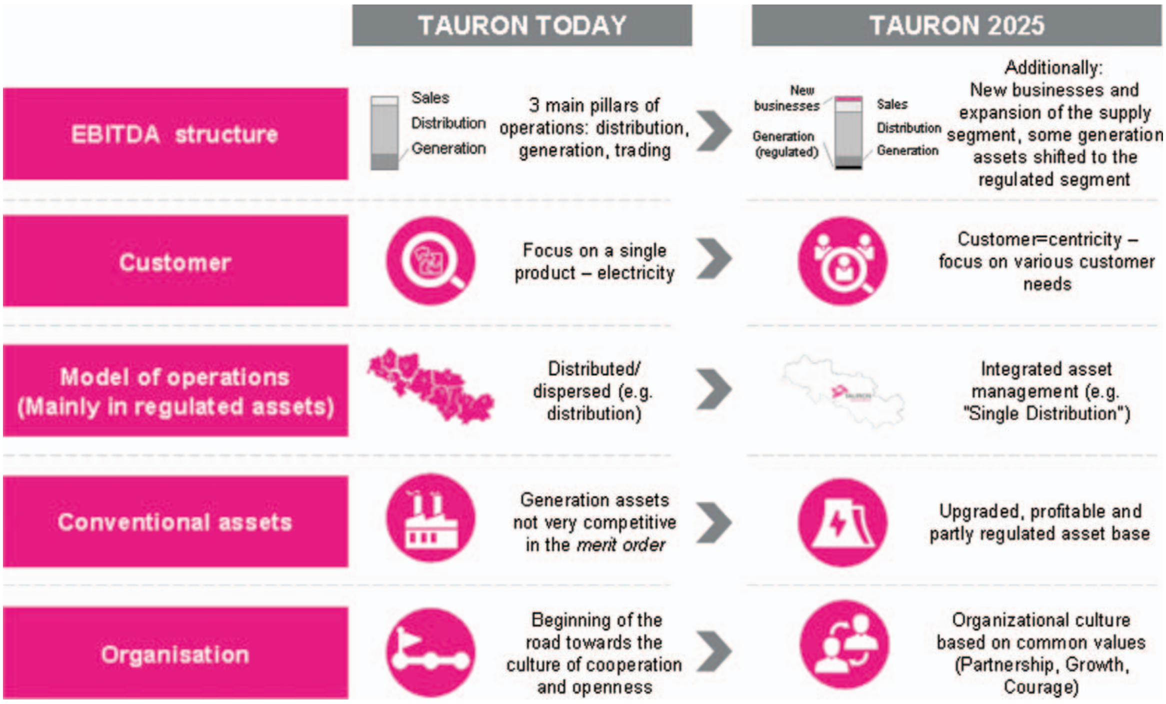
Mission of TAURON Capital Group
"With passion and commitment we are delivering modern solutions that provide energy in the constantly changing world."

Vision of TAURON Capital Group
"We are a company that best meets customer needs in the Polish energy industry."

Mission and vision best describe TAURON Capital Group's strategic intentions. The Supply segment and new products represent the field of operations that TAURON Capital Group is intensely developing. TAURON Capital Group is adjusting its profile in order to ensure full focus on the customer, while appreciating the potential of new products, compatible services, modern contact channels as a way to shape the response to customer needs.

The below figure presents TAURON Capital Group's 2025 Vision.

Figure no. 4. TAURON Capital Group's 2025 Vision



The key values that are to support the implementation of the Strategy include "Partnership", "Development" and "Courage". The values reflect the way in which TAURON Capital Group wants to achieve its goals. What is important as part of the partnership is customer orientation, development of sustainable relationships and engagement. Development means focus on innovations, developing competences, skills and knowledge and seeking ever better solutions meeting customer needs and raising the quality of services. Courage means boldness and openness, determination as well as engagement and passion in achieving common goals.

Combination of such values is to lead to a better understanding of customer expectations, responding to market challenges and developing TAURON Capital Group's organizational culture.

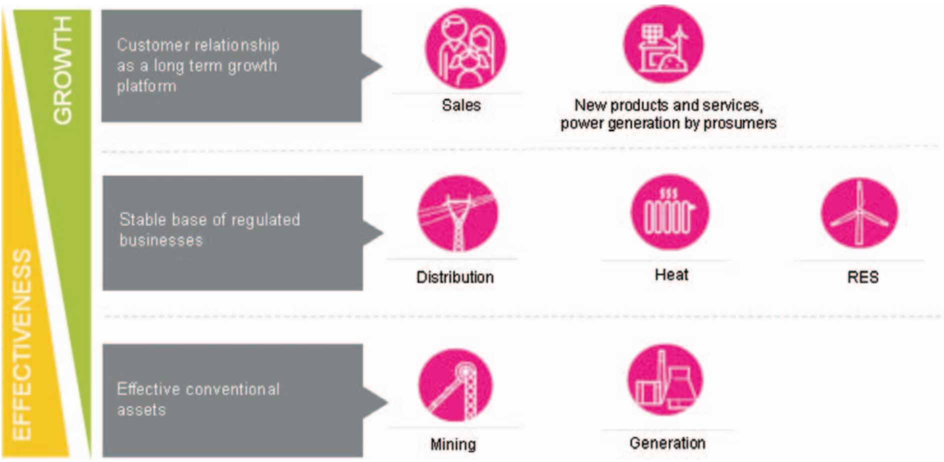
1.4.2. TAURON Capital Group's 2016–2025 Strategy

2016–2025 Strategy adopted presents an optimal expansion path that will ensure financial stability and growth, while at the same time providing support for ensuring stability of the power system. The long term growth will be driven by solutions based on customer relationships. The adopted mission and vision reflect new management philosophy and are in line with the customer-oriented growth concept.

Strategy describes the approach to developing individual segments of TAURON Capital Group's operations, dividing them into ones that TAURON Capital Group is planning to strongly expand, ones that will constitute the foundation of the financial stability and ones where strong emphasis on cost efficiency is required. The above reflects a new management philosophy and emphasizes a turn towards the customer and his/her needs as well as towards developing an innovative, open to new solutions TAURON Capital Group.

The below figure presents the prospects of TAURON Capital Group's segments.

Figure no. 5. Prospects of TAURON Capital Group's segments



Strategy sets the priorities that will transform TAURON Capital Group into an innovative, aligned to the market and customer needs, growing energy company ultimately providing a return on invested capital for its shareholders.

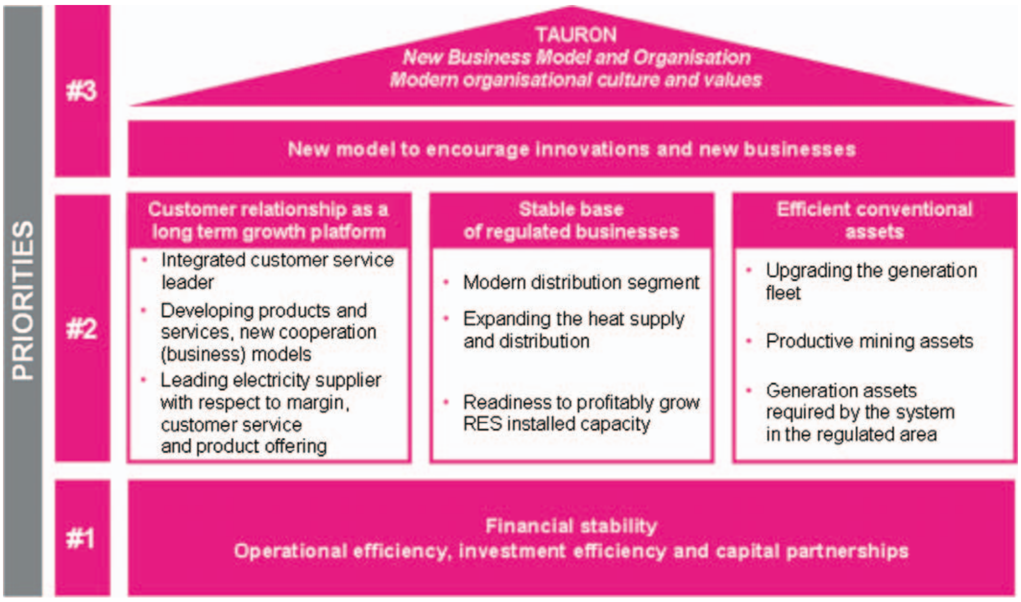
1. Ensuring TAURON Capital Group's financial stability to be achieved through the following actions:
   a) TAURON Group's 2016–2018 Efficiency Improvement Program, adopted in March, 2016 and assuming achieving PLN 1.3 bln in savings in 2016–2018. The above savings include actions resulting in the cumulative EBITDA increase by approximately PLN 1 bln and involving CAPEX reduction by approximately PLN 0.3 bln in 2016–2018.
   b) Strategic Initiatives and CAPEX reduction in 2017–2020 will bring a financial effect of PLN 1.9 bln. It will be achieved as a result of actions leading to the cumulative EBITDA increase by approximately PLN 1.2 bln and the CAPEX reduction by approximately PLN 0.7 bln. These are additional financial outcomes, beside the effects generated by the Efficiency Improvement Program.
   c) Stopping the investment in the CCGT unit at Łagisza Power Plant, resulting in not incurring PLN 1.5 bln in CAPEX. It will be possible to resume the project in case the regulatory and market environment turns favorable.
2. Building a strong capital group.

   Strategy defines a new approach to the value chain where key tasks are set for each Line of Business. Strategy does not assume balanced growth along each link of the value chain. Sales and development of new products and services are to constitute a strong base for the Group's growth. The Group is planning to rapidly develop its offering for the customers in this segment which will allow for retaining the existing base of customers that purchase TAURON products and increasing profitability. Electricity distribution as well as heat generation and distribution segments are to constitute a stable base of the Group's regulated businesses. Mining and conventional generation segments have tasks related first of all to efficiency improvement. The following three pillars of the strong capital group were defined:
   a) Customer relationships based on integrated high quality service with the use of modern sales and customer service channels as well as developing a product and service offering.
   b) Stable base of regulated assets based on the upgraded electricity distribution and heat segments as well as readiness to grow renewable energy sources in case the regulatory environment turns favorable.
   c) Efficient conventional assets, i.e. mining and conventional generation segments, which as a result of improving cost efficiency and productivity will be competitive on the market or, in case of generation assets, they will be shifted to the regulated segment of the power system.

3. Implementing organizational changes supporting the implementation of the Strategy that will transform TAURON Capital Group into a modern and innovative organization:
   a) Implementing a new, process-oriented operational model. Five priority process streams have been identified around which TAURON Capital Group's operations will be concentrated, i.e. Strategy, Finance, Asset Management and Development, Customer and Corporate Management and Support. Such approach will allow for placing a greater emphasis on cross-sectional issues that will determine TAURON Capital Group's competitive advantages in the future.
   b) Expanding research and development as well as innovative activities for which expenditures equal to 0.4% of the consolidated revenue a year are envisaged.
   c) Developing innovative projects based on the Corporate Venture Capital (CVC) type fund dedicated for this purpose or similar solutions.

The below figure presents implementation of priorities based on the pillars of TAURON Capital Group's Strategy.

Figure no. 6. Implementation of priorities based on the pillars of TAURON Capital Group's Strategy



The implementation of the Strategy will allow for increasing EBITDA from PLN 3.5 bln in 2015 to more than PLN 4 bln in 2020 and to more than PLN 5 bln in 2025. Estimated, recurring effect of implementing the Efficiency Improvement Program in the form of an impact on the Group's EBITDA will be approximately PLN 0.4 bln starting from 2018, while the effect of implementing the Strategic Initiatives in the form of an impact on the Group's EBITDA will be approximately PLN 0.3 bln beyond 2020.

As part of rationalizing CAPEX the expenditures planned for 2016–2020 were reduced from PLN 20.2 bln to approx. PLN 18 bln. It is assumed that the commenced and well advanced investment projects will be continued. The detailed analysis revealed that 75 percent of the CAPEX plan until 2020 are tasks that are either a continuation or are related to keeping the commitments made. Such tasks include the investment in the 910 MW unit at Jaworzno III Power Plant as well as the contracted or resulting from regulatory requirements tasks in the distribution segment. Resigning or delaying these tasks would have a negative impact on the Group's value or is impossible due to legal or safety reasons.

In the Mining segment investments at Janina coal mine and the construction of Grzegorz shaft at Sobieski coal mine will be continued and the planned investments at Brzeszcze coal mine will be carried out. CAPEX in this line of business is approximately PLN 1.3 bln until 2020.

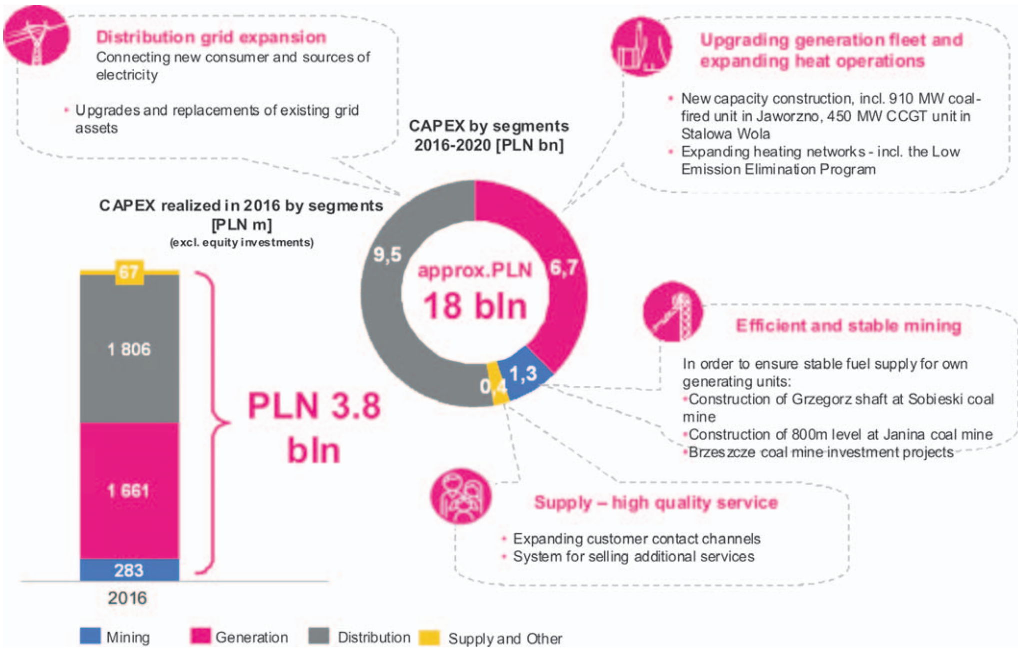
In the Generation segment investments in the construction of the 910 MW unit at Jaworzno III Power Plant and the CCGT unit at Stalowa Wola Combined Heat and Power Plant as well as the investments in the heating networks will be continued. TAURON assumes that the construction of the 910 MW unit at Jaworzno III Power Plant will be carried out under a new financing formula envisaging spinning off of an organized part of the enterprise and selling its shares to third party partners, provided they do not acquire a controlling stake. A change of the way the unit's construction is financed would reduce the net debt/EBITDA ratio, and thus significantly lower the risk of breaching the threshold value of this covenant (3.5x) defined in the financing agreements.

Strategy assumes maintaining financial stability and not breaching the net debt/EBITDA covenant of 3.5x without taking into account selling a minority stake in the construction of the 910 MW unit to third party partners. This means that the planned change of this project's financing formula represents an additional element that would stabilize TAURON Capital Group's financial position. Generation segment's capital expenditures amount to PLN 6.7 bln until 2020.

More than 50 percent of the entire CAPEX, i.e. PLN 9.5 bln by 2020, are investments in the Distribution segment that include connecting new customers and generation sources as well as upgrading and replacing grid assets

The below figure presents capital expenditures by segments in 2016–2020.

Figure no. 7. Capital expenditures by segments in 2016–2020



With respect to innovative as well as research and development activities the Strategy assumes expenditures equal to 0.4% of the consolidated revenue a year.

The overall objective in terms of CAPEX is to align the investment portfolio to the market needs.

In particular the actions to be undertaken will be aimed at:

1. Optimizing the asset structure in all lines of business and achieving compliance with the environmental requirements.
2. Carrying out only those investment projects that guarantee the expected return on capital and are not burdened with material market risks.
3. Using off-balance sheet forms of financing, in particular by engaging third party partners.
4. Reviewing investment projects in the conventional generation segment, provided mechanisms that guarantee revenue are introduced (e.g. capacity market or another form of regulation).
5. Investing in projects in sectors that are related to the power industry (in particular, services) in order to complement the value chain that TAURON is operating in, and also developing a high margin services offering.

Assumed directions of investments beyond 2020 include first of all the regulated segments of the power sector (i.e., among others, electricity distribution, heat generation and distribution, participation in the nuclear power generation and regulated conventional generation) and the new power industry (i.e. e-mobility, distributed heat and electricity generation, power generation by prosumers, Smart Home, Smart City solutions and energy related services). Strategy assumes that in 2020–2025 TAURON Capital Group's estimated investment potential will be more than PLN 6 bln.

1.4.3. Key challenges for TAURON Capital Group

Strategy is TAURON Capital Group's response to the challenges posed by the business environment and the requirements of the energy sector's customers that have been changing fast over the last few years.

Strategy defines four key challenges facing TAURON Capital Group: regulations, market, customer and technologies.

Regulations

Introduction of the dual-product market – capacity market, the European Union's (EU) decarbonization policy and successive regulations aimed at reducing emissions, introduction of the quality based regulation in the distribution segment, changes to the support for RES installations and EU actions aimed at developing a common electricity market.

Market

Changing forecasts of electricity prices, hard coal oversupply and prices, demand for electricity, demand for capacity, growing competition on the retail market, rising level of RES generation along with the withdrawal of the European players and the reduction of the financing for the conventional power generation.

Client

Growing awareness of the customers and the requirements with respect to satisfying their needs as well as comprehensiveness of the offering, increased expectations with respect to customer service quality and availability.

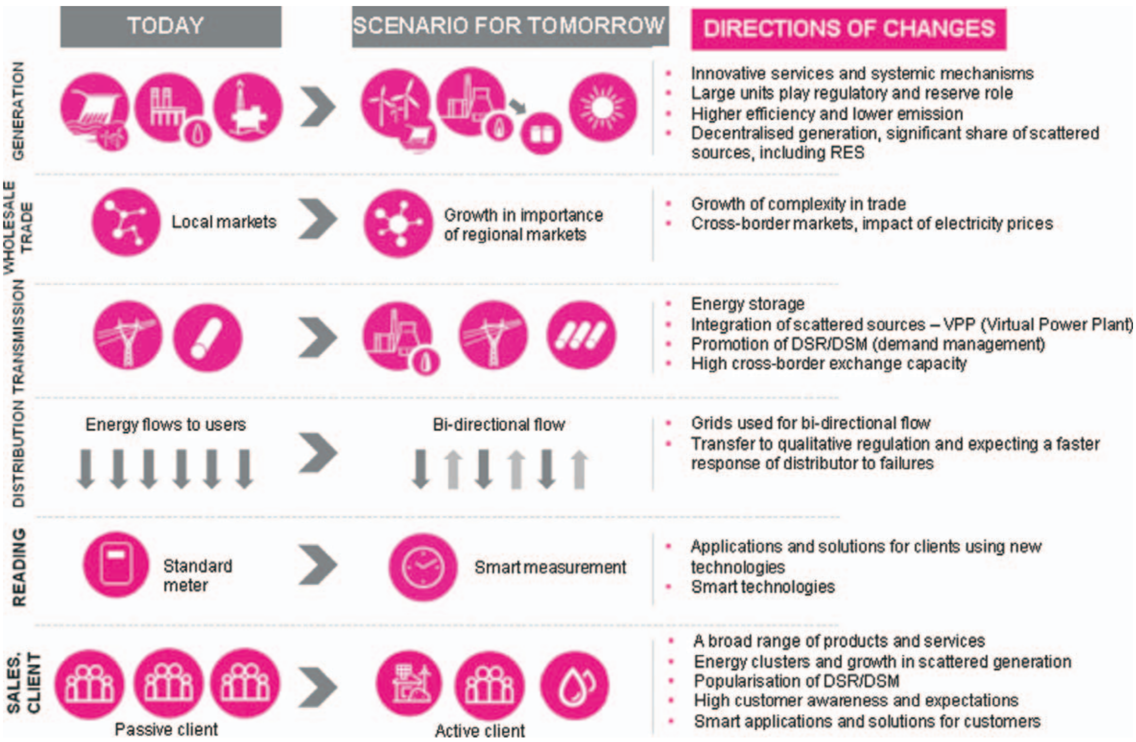
Technologies

Falling prices of renewable and dispersed technologies, rising competitiveness of such sources versus conventional sources, a change of the role of the distribution service due to the expansion of dispersed power generation, advancement of smart technologies, microgeneration and energy storage.

In the long term profound changes of the entire power sector, towards the so-called "power industry of tomorrow", are important. A transformation of the system power sector towards decentralized generation, increased role of transborder connections, energy storage and new energy services, as for example "virtual power plants", demand side management, dispersed generation. This also leads to a change of the role of the distribution segment that must deal with smart technologies, electric vehicle charging infrastructure, distributed generation, including prosumers, bi+directional flows, while at the same time raising the quality and security of supplies.

The below figure presents the key challenges facing TAURON Capital Group.

Figure no. 8. Key challenges facing TAURON Capital Group



1.4.4. Opportunities and threats

The defined key challenges facing TAURON Capital Group create both opportunities as well as threats for TAURON Capital Group's operations.

The below table presents opportunities and threats for TAURON Capital Group's operations.

Table no. 3. Opportunities and threats for TAURON Capital Group's operations

Opportunities	Threats
Regulations	
• Introduction of the dual-product market – additional revenue for maintaining generation capacity. • Support for electromobility (growing electricity consumption). • Introduction of legal regulations supporting the reduction of low emissions (e.g. system district heating, increasing the share of eco-pea coal in the sales). • Expected support for the cogeneration beyond 2018.	• Rising costs of electricity production from conventional assets, growing environmental costs and further tightening of the decarbonization policy. • Negative impact of the EU regulations related to the common energy market. • Lack of stability and predictability of the regulations for the RES sources, including rising costs of maintaining wind farms and hydro-electric power plants as well as uncertain future of the RES sources based on the biomass burning and co-firing technology (RES directive draft). • Lack of support for the cogeneration beyond 2018.
Market	
• Cost effective, own mining assets, competitive on the Polish market, allowing for stabilization and predictability of the fuel cost. • Access to the largest, among Poland's energy companies, customer base. • Entry to the energy related services market segments based on the competences held. • Commercialization of innovative solutions developed as part of research and development operations.	• Declining margins and lower utilization of conventional assets (deteriorating profitability, required outlays for upgrades or the need to shutdown old generating units due to the new high efficiency units entering the system and due to the BAT requirements). • Loss of volume and profitability of the Supply Segment, in particular in the B2B area. • Pressure on electricity prices with the growing transborder exchange volumes. • Rising costs and limited availability of financing. • Increased prices of products and services negatively impacting investment efficiency.
Customer	
• Competitive advantage with respect to customer service quality. • Customer segmentation and offering additional products in line with customer expectations. • Greater customer awareness and expectations towards comprehensive, personalized offering of additional services and products (greater customer product saturation). • Expanding an offering of services for customers based on competences held and trust in TAURON brand. • Growth through concentration on a customer that is not generating large capital investments. • Developing modern and integrated sales and customer service channels. • New competences and business models based on research and development operations. • Maintaining an upward trend in electricity consumption trend by final consumers.	• Potential loss of customers due to an increase in the number of competitors offering customers similar products and due to low electricity supply market entry barriers. • Decreasing customer loyalty – growing number of supplier switchings. • Greater customer awareness and requirements with respect to service quality and product offering. • Power independence of consumers (prosumers, energy (power) islands, clusters). • Energy intensive consumers building their own generation sources, as a result of the drive to reduce electricity costs. • "Carbon leakage" – moving business operations to other countries due to the cost of energy.
Technologies	
• Falling prices of renewable technologies. • Advancement of storage technologies, smart technologies and technologies related to dispersed (distributed) generation. • Additional services for customers related to new technologies (internet of things, dynamic tariffs, virtual power plants). • Advancement of dispersed (distributed) power generation, including prosumers. • Developing and implementing (commercializing) of own innovative solutions that provide a competitive advantage.	• The need to adapt the grid to the growth of dispersed (distributed) power generation (bi-directional flows). • Arrival of new, cost competitive electricity generation technologies in countries neighboring with Poland.

1.4.5. Implementation of the Strategy and priorities of TAURON Capital Group in 2017

2017 was the time when the first effects of the Strategy adopted in September 2016 were achieved. In accordance with the Assumption the most important priority was to ensure financial stability in order to lay down solid foundations for the expansion of TAURON Capital Group. As part of the Strategy actions in the form of Strategic Initiatives were taken and the Efficiency Improvement Program was continued, involving reorganizing core processes throughout TAURON Capital Group and raising asset utilization efficiency. Strategy is implemented by:

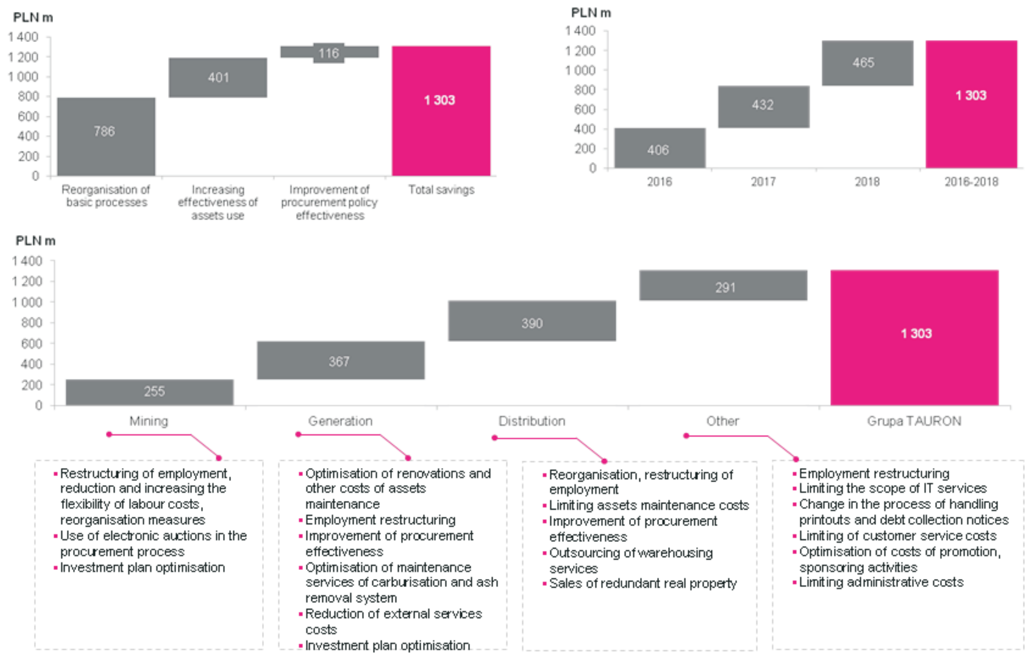
a) Achieving TAURON Capital Group's strategic objectives, which are:

- EBITDA above PLN 4 bln in 2020. The objective is being achieved through actions related to the implementation of the Strategic Initiatives and initiatives carried out as part of the Efficiency Improvement Program the implementation of which in 2017 brought higher returns than planned at the stage of developing the Strategy. In 2017 EBITDA of more than PLN 3.5 bln was achieved, this is a better result than in 2016 when EBITDA of more than PLN 3.3 bln was achieved.
- Maintaining the net debt/EBITDA covenants below 3.5. One of the priorities of the Strategy is to ensure financial stability. Maintaining the covenants is both an effect of actions leading to improved financial results as well as actions aimed at improving investment efficiency. As part of the Strategy the investment portfolio was optimized and modern financing in the form of a hybrid bond issue was obtained. At the end 2017 the net debt/EBITDA ratio reached 2.3x.
- Maintaining a high Customer Satisfaction Index (CSI). TAURON Capital Group is an industry leader in customer service quality. Annual customer satisfaction surveys performed by an external company confirm a high satisfaction level of TAURON Capital Group's customers. The overall result of the September 2017 survey proved maintaining a high 2016 index level of 80 points.
- Power plants generating positive cash flows by 2020. Achievement of this goal will be the result of a number of actions undertaken within TAURON Capital Group, among others: optimizing the costs of the generating units and TAURON Capital Group's trading (commercial) strategy, as well as the impact of the external environment, both the regulatory one, as well as the market one (support for RES and cogeneration, fuel prices, property rights prices, electricity prices).
- Maintaining the customer base. TAURON Capital Group is Poland's distributor and the second largest electricity supplier. Maintaining the customer base represents for TAURON Capital Group a long term growth platform and is implemented by both, actions improving the quality of services, among others an expansion of customer communications channels, as well as a broad product offering. At the end of 2017 TAURON Capital Group provided services for almost 5.4 mln customers of the Supply Segment and more than 5.5 mln customers of the Distribution Segment.
- Unit margin leader among Poland's largest 4 electricity suppliers. Maintaining the leader's position is based both on maintaining a high volume of electricity supplied, as well as the ability to generate a positive financial result. TAURON Capital Group, by concentrating on the customer, is developing a broad, profitable base of products and services offered to our customers. Based on the data for 9 months of 2017 TAURON Capital Group maintained the leading position among Poland's largest 4 utilities.
- New businesses are to represent at least 25% of revenue/margin in 2025. This objective is to be a response to the challenges posed by the competitive environment. Achieving climate improvement targets and building the European energy market will have an impact on the increase of competition in the power sector, therefore actions are undertaken aimed at developing new businesses and we place our bets on innovations.

b) Efficiency Improvement Program, adopted in March, 2016 and assuming achieving PLN 1.3 bln in savings in 2016–2018. The above savings include actions resulting in the cumulative EBITDA increase by approximately PLN 1 bln and involving CAPEX reduction by approximately PLN 0.3 bln in 2016–2018 within three scopes of operations.

   The below figure presents the 2016–2018 Efficiency Improvement Program.

Figure no. 9. 2016–2018 Efficiency Improvement Program

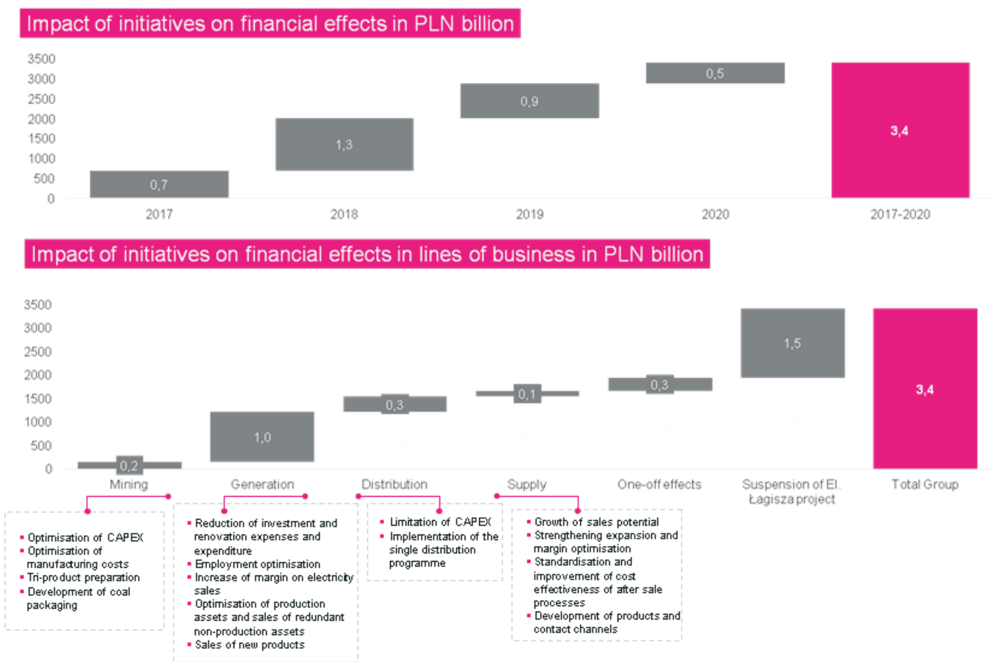


TAURON Capital Group's Efficiency Improvement Program brought, in 2016–2017, savings of PLN 1 091 mln which represents 84% of the planned savings, out of which PLN 640 mln impacted EBITDA, while PLN 451 mln was applicable to CAPEX savings. The largest contribution to the savings achieved came from the Generation Line of Business.

c) Strategic Initiatives and CAPEX rationalization in 2017–2020 assuming financial effects of PLN 3.4 bln, including the cumulative EBITDA increase by approximately PLN 1.2 bln, CAPEX reduction by approximately PLN 0.7 bln and stopping the investment in the new unit at Łagisza Power Plant worth PLN 1.5 bln.

The below figure presents Strategic Initiatives and CAPEX rationalization in 2017–2020.

Figure no. 10. Strategic Initiatives and CAPEX rationalization in 2017–2020



In accordance with the objectives set TAURON Capital Group will be expanding the Supply Line of Business and customer service. In this respect a further introduction of coherent, high customer service standards in each area of the value chain and the growth of modern and integrated sales and customer service channels is planned.

In the Distribution Line of Business the "One Distribution" program based on actions related to unifying the processes and systems as well as implementing an optimal and coherent structure of TAURON Dystrybucja so as to improve operational and investment efficiency of this Line of Business will be continued.

In the Mining and Generation Lines of Businesses tasks related to a further improvement of the cost and investment efficiency will be carried out. The introduction of the detailed regulations related to the capacity market in Poland and the planned auctions related thereto will be important for the generation assets.

In 2017 Strategic Initiatives brought a financial effect of PLN 937 mln, out of which PLN 320 mln impacted EBITDA, while PLN 617 mln was applicable to CAPEX savings (including PLN 428 mln due to stopping the Łagisza investment project). The largest contributions to the savings achieved came from the Generation (PLN 314 mln) and Distribution (PLN 103 mln) Lines of Business.

In 2018 TAURON Capital Group's largest investment projects will be continued in line with the adopted Strategy, including:

1) in the Mining Line of Business: construction of the Grzegorz shaft, 800 m level at Janina Coal Mine and investment projects at Brzeszcze Coal Mine,
2) in the Generation Line of Business: construction of the 910 MW hard coal-fired unit in Jaworzno, the 450 MW CCGT unit in Stalowa Wola,
3) in the Distribution Line of Business: investment tasks related to the grid construction and upgrading.

Furthermore, the Low Emission Elimination Program in the Silesia and Dąbrowa conurbation as well as the project related to implementing heat production at unit no. 10 and construction of peaking and backup boilers at Łagisza Power Plant, as a consequence of planned shutdown of 120 MW units at this site, will be carried out.

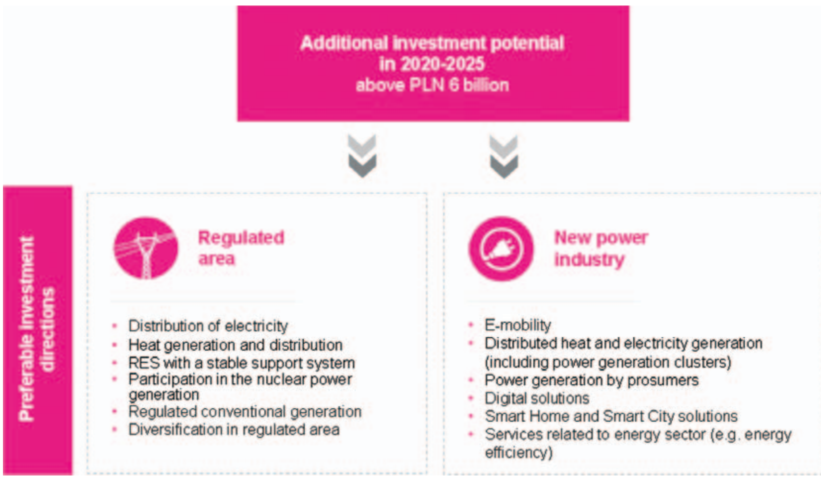
1.5. Description of TAURON Capital Group's expansion policy and directions

Strategy sets the directions of TAURON Capital Group's short and long term expansion. The tasks for TAURON Capital Group's individual Lines of Business were defined in detail until 2020 and the financial effects for such tasks were set. The priority is to maintain stable financial position and lay down solid foundations for growth in a changing environment. This priority is to be achieved through the Efficiency Improvement Program and Strategic Initiatives aimed at the cost and investment optimization. It is planned that by 2020 PLN approximately 18 bln worth of CAPEX will be spent, with more than half on the distribution assets generating TAURON Capital Group's most stable revenue. Strategy sets the priority directions for the innovations as well as research and development activities that will be the basis for developing new products and services in the longer term. In order to achieve this goal TAURON Capital Group adopted a new model for the innovations as well as research and development activities, setting up a dedicated central organization for managing and coordinating such operations and allocating a budget of 0.4% of revenue thereto.

In the longer term Strategy assumes full utilization of the potential of TAURON Capital Group's assets, supporting innovations, organizational culture and, first of all, the broad customer base. Strategy assumes that in 2020–2025 TAURON Capital Group will gain an additional CAPEX potential in the region of approximately PLN 6 bln to be used for projects that will generate value for TAURON Capital Group in the longer term. TAURON Capital Group will be investing in the regulated areas such as electricity distribution as well as heat distribution and generation, RES (on the condition of a stable support system), regulated conventional generation and in the new power sector, e.g. electromobility, dispersed (distributed) electricity and heat generation, smart solutions.

The below figure presents the outlook for CAPEX directions beyond 2020.

Figure no. 11. Outlook for CAPEX directions beyond 2020



TAURON Capital Group's main competitive advantage is the base of 5.5 mln customers. The most important actions in the short and long term will be relatively low capital intensive actions related to an expansion of the product and service offering for the consumers and developing new operations based on TAURON Capital Group's competences. Strategy assumes that in 2025 new businesses will be generating approx. 25% of the total margin or revenue from the Supply Segment's sales.

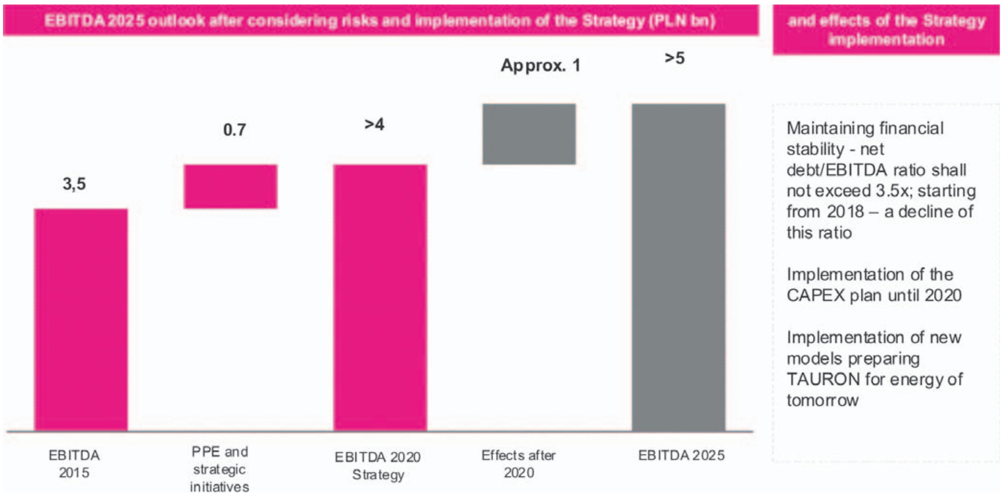
1.5.1. Long term goals and financial assumptions of the Strategy

Actions defined in the Strategy will allow for achieving the set key goals for TAURON Capital Group:

1) EBITDA above PLN 4 bln in 2020
2) Maintaining the net debt/EBITDA covenants below 3.5x
3) Maintaining a high Customer Satisfaction Index (CSI)
4) Power plants generating positive cash flows by 2020
5) Maintaining the customer base
6) Unit margin leader among Poland's largest 4 electricity suppliers
7) New businesses will represent at least 25% of revenue/margin in 2025

The below figure presents the 2025 EBITDA outlook taking into account the risks and the implementation of the Strategy as well as the effects of the implementation of the Strategy.

Figure no. 12. 2025 EBITDA outlook taking into account the risks and the implementation of the Strategy as well as the effects of the implementation of the Strategy



Actions planned for the coming years will allow for stopping the profitability decline. This will be achieved by optimizing operations in the Generation and Mining Segments while at the same time maintaining stability in the Distribution Line of Business.

1.5.2. Implementation of strategic investment projects

Key strategic investment projects underway

The below table presents the activities carried out by TAURON Capital Group in 2017 in connection with the implementation of the key strategic investment projects.

Table no. 4. Key strategic investment projects' work progress

No.	Investment project	Work progress
1.	Construction of a 449 MW_e CCGT unit, including a 240 MW_t heat generation component at Stalowa Wola (Project implemented jointly with the strategic partner – Polskie Górnictwo Naftowe i Gazownictwo S.A. (PGNiG)). **Contractor**: the contract with Abener Energia S.A. was terminated. The Project's completion is envisaged under the EPCM formula (contract manager). EPCM – Energoprojekt Katowice – Energopomiar Gliwice consortium. **Planned project completion date**: 2019 **Work progress**: 86% **Expenditures incurred**: PLN 981.9 mln	The installed machines and devices' maintenance works were conducted on an ongoing basis, works related to the startup of the auxiliary devices were conducted, power supply was provided to the unit's switchgear and negotiations with the suppliers and sub-suppliers of the main devices were conducted. The concept of the project's completion under the contract manager – EPCM formula and the contractors' contracting was prepared. The EPCM service agreement with the Energopomiar Gliwice – Energoprojekt Katowice consortium was concluded. EPCM commenced the performance of the services. In December 2017 ECSW with the EPCM support announced the first proceeding aimed at selecting the critical path contractor – startup group. The proceeding aimed at selecting the Contractor to construct the cooling water's duct was completed. IDS-BUD S.A. was selected, preparations to commence the construction works are underway. The decision was taken on expanding the project's scope by adding the construction of the backup heat source. Preparation works are underway. All liabilities under ECSW's loan agreements towards the financing banks (European Investment Bank, European Bank for Reconstruction and Development, Bank Polska Kasa Opieki S.A.) were totally repaid. Upon the crediting of the financing institutions' bank accounts the suspending conditions were met and at the same time the documents came into force, i.e. the agreement on establishing the basic boundary conditions of the project's restructuring among TAURON, PGNiG and ECSW, the amendment to the electricity sale Agreement among TAURON, PGNiG and ECSW and the amendment to the gas supply agreement between PGNiG and ECSW. Talks aimed at acquiring the financing required to complete the investment project are continued.
2.	Construction of a new 910 MW_e power generation unit for supercritical parameters at Jaworzno III Power Plant (TAURON Wytwarzanie). **Contractor**: RAFAKO S.A. and MOSTOSTAL WARSZAWA S.A. Consortium **Planned project completion date**: 2019 **Work progress**: 54% **Expenditures incurred**: PLN 3 330 mln	Construction works and installing of the steel structures were underway. With respect to the machine room building the basic steel structure of the building including the overhead crane was completed. Installation of the generator's stator was completed. The cooling tower's ultimate height was achieved and the absorber's pump station's roof's steel structure was completed. The project works conducted by the selected contractors selected were underway to construct: ignition oil (auxiliary fuel) installation, compressed air system, office building, power discharge system, water supply system as well as water treatment station and wastewater treatment plant were underway. The Contractor for the construction of the flyovers of pipelines was selected. Tender proceedings to select the Contractor for the construction of the track layout system, telecommunications network and the water and sewage network were continued. An amendment with the RAFAKO S.A. – MOSTOSTAL WARSZAWA S.A. consortium was signed under which the agreement's net price was increased by PLN 71.05 mln (i.e. to PLN 4 470 mln), and the deadline for completing the subject of the agreement was extended by 8 months which means that the new date of handing the unit over for operation is November 2019). The amendment did not impact the investment project's total budget. Furthermore, the unit's process parts were installed. The works performed were related to installing boiler pressure elements, furnace installation, boiler fuel supply and electrostatic precipitator installation. Generator's installation was completed, the installation of the turbine and condenser elements as well as feeding water pumps including the GRP pipelines was continued. Also the contractors for the other systems, i.e.: telecommunications network, the water and sewage network as well as track layout system. Works in the area of auxiliary and accompanying systems were continued: carburization, de-ashing, power discharge system, ignition oil (auxiliary fuel) system, compressed air system, raw water supply system, flyovers (bridges), water treatment station, office building, telecommunications network.

No.	Investment project	Work progress
3.	Construction of the “Grzegorz” shaft including the infrastructure (above the ground and underground) and the accompanying headings (TAURON Wydobycie). **Contractor**: Consortium KOPEX Przedsiębiorstwo Budowy Szybów S.A. FAMUR Pemug Sp. z o.o. (main task – Stage I), LINTER S.A. **Planned project completion date:** 2023 **Work progress**: 20% **Expenditures incurred**: PLN 97.2 mln	Works related to excavating the headings to the “Grzegorz” shaft on the 540 m were continued. Currently the excavated heading’s length reached 930 m. General Contractor of the construction of the shaft, including the above the ground infrastructure, was selected – KOPEX Przedsiębiorstwo Budowy Szybów S.A. and Famur Pemug Sp. z o.o. The construction site was handed over to the General Contractor.
4.	Construction of the 800 m level at Janina Coal Mine (TAURON Wydobycie). **Contractor**: Konsorcjum Mostostal Zabrze GPBP S.A. i SIEMAG TECBERG POLSKA S.A. (Construction of the ultimate above the ground and underground infrastructure including the Janina VI shaft Mine Shaft Elevator), KOPEX S.A. i KOPEX Przedsiębiorstwo Budowy Szybów S.A. (zadanie zakończone – drążenie szybu) Tender proceeding aimed at selecting the contractor for the ultimate above the ground and underground infrastructure including the mine shaft elevator is underway (GWSZ), KOPEX **Planned project completion date:** 2020 **Work progress**: 57% **Expenditures incurred**: PLN 294.1 mln	Works associated with shaft drilling and furnishing as well as the installation of the shaft pipe to the ultimate depth were completed. The works associated with the horizontal heading drilling on the 800 m level are underway. The contractor to complete the construction of the shaft’s above the ground and underground infrastructure, including the mine shaft elevator, was selected.
5.	Brzeszcze CAPEX Program **Contractors:** TRANS-JAN, FAMUR and KOPEX Machinery Consortium, FAMUR and KPRGiBSz Consortium, MAS and Carbospec Consortium, Elektrometal Cieszyn **Planned Program completion date**: 2025 **Work progress**: 26% **Expenditures incurred**: PLN 138,3 mln	Wall 05 was launched. The works related to the alteration of the ventilation excavations are underway. The works related to the construction of the fine coal sales facility, construction of the primary compressors station, construction of the water and ash blending station were conducted. The mine’s upgraded mining rescue station was commissioned and the mine dewatering system was upgraded.
6.	Implementing heat production at unit no. 10 and construction of peaking and backup boilers at Łagisza **Contractor**: proceedings to select General Contractors to carry out individual scopes underway. **Planned Program completion date:** 2019 **Work progress**: 0.5% **Expenditures incurred**: PLN 0.5 mln	The project’s goal is to adapt unit no. 10 at Łagisza Power Plant to produce heat by upgrading the turbine, installing heat-producing heaters at unit no. 10’s turbine, in order to heat heating water using the steam extracted from the turbine’s flow section and upgrading the heating station. Securing of the heat supply during the demand peak and/or during the scheduled or emergency shutdown of unit no. 10 from the operation will be carried out as part of the construction of the peaking and backup boilers. Two of the three main tender proceedings to select contractors to carry out individual tasks have been announced. Planned expenditures to be incurred to carry out the project is approx. PLN 114 mln.
7.	Low Emission Elimination Program (PLNE) on the territory of the Silesia and Dąbrowa conurbation **Contractors**: Contractors selected to carry out individual projects. **Planned Program completion date:** 2023 **Work progress**: 3% **Expenditures incurred**: PLN 2.8 mln	The program is carried out on the territory of the following cities: Będzin, Chorzów, Czeladź, Dąbrowa Górnicza, Katowice, Siemianowice Śląskie, Sosnowiec, Świętochłowice. The scope of the project includes construction and alteration of the district heating networks: transmission ones, housing estate ones and connections, as well as construction of heating nodes to the extent required to connect heat consumers. Connecting of 183 MWt of thermal capacity to the district heating network as well as an increase of heat supply and distribution is planned. The program’s goal is to reduce smog in the Silesia and Dąbrowa conurbation. TAURON Ciepło signed a funding agreement for the amount of approximately PLN 141 mln. The total funds envisaged to carry out the program amount to approximately PLN 250 mln.

Nuclear power plant construction project

On February 15, 2017 PGE EJ 1’s share capital increase was registered in the National Court Register, in line with the resolution passed by the Extraordinary GM of the PGE EJ 1 special purpose vehicle on December 21, 2016. The share capital was increased from PLN 275 859 450 to PLN 310 858 470, i.e. by PLN 34 999 020, by way of issuance of 248 220 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 34 999 020. TAURON took up 24 822 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 3 499 902, paid for by cash in the amount of PLN 3 499 902.

On September 3, 2014 TAURON, ENEA S.A. (ENEA) and KGHM Polska Miedź S.A. (Business Partners) concluded the Partners' Agreement governing the rules of cooperation in the implementation of Poland's first nuclear power plant construction project. On April 15, 2015 the above entities concluded the agreement on the purchase of shares in PGE EJ 1 – a special purpose vehicle responsible for preparing and implementing an investment project involving the construction and operation of a nuclear power plant with the capacity of approximately 3 thousand MWe (Project). Each Business Partner acquired from PGE a 10% stake (30% of shares in total) in the PGE EJ 1 special purpose vehicle. TAURON paid PLN 16 044 000 for the acquired stake. This way one of the commitments under the Partners' Agreement, according to which the parties undertook to jointly, in proportion to the stakes held, finance operations as part of a project milestone, was fulfilled

The Partners' Agreement envisages that the successive decisions related to the project, including the decision on the declaration to further continue participation in a subsequent project stage by the individual parties (including TAURON), will be taken following the completion of the preliminary stage.

In 2017 PGE EJ 1 carried out the scope of the works related to conducting environmental and siting research at Żarnowiec and Lubiatowo-Kopalino sites.

Coal gasification project

On April 20, 2017 TAURON signed a letter of intent with Grupa Azoty S.A., defining general rules of commencing cooperation aimed at implementing the coal gasification project.

The product of the technological process system that the letter of intent is applicable to is primarily the synthesis gas (syngas) with the composition that would allow using it directly to produce hydrogen, ammonia, methanol or other chemicals. The parties came to the conclusion that the current natural gas consumption in the nitrogen fertilizers manufacturing industry could partly be replaced with the synthesis gas (syngas) obtained as a result of coal gasification. This opens new prospects for the mining industry, increasing Poland's security of electricity supply by developing low emission technology.

The project is at the preFeed (Preliminary Front End Engineering Design) and accompanying analyses, including market research, stage. As part of the project Grupa Azoty commissioned works related to documentation, in particular a preliminary selection of licensors and updating of the analyses. The Project's estimated value will reach between EUR 400 mln and EUR 600 mln, depending on the selected technology version.

TAURON has declared its participation in the Project's implementation in accordance with the rules that will be defined by the Parties in separate agreements, including assuming selecting and completing an installation that would ensure maximizing the use of hard coal coming from TAURON Capital Group's coal mines. If TAURON is not able to provide appropriate quantity or parameters of coal required by the installation, it shall be permitted to supplement the supply with coal coming from other suppliers.

The letter of intent expresses the readiness of the parties to commence talks and defines the general cooperation framework and does not cause, at the current stage, any financial or management implications for either Party. The Parties declared an intention to cooperate and expressed the will to sign further agreements, including agreements related to establishing a joint special purpose vehicle (SPV) to carry out the project. Either Party shall have the right to terminate the letter of intent at one month's notice.

413 MW_e CCGT unit construction project including the 266 MW_t, heat production unit at Łagisza Power Plant

In accordance with the Strategy, as part of the priority to ensure TAURON Capital Group's financial stability, the CCGT unit construction project at Łagisza Power Plant was stopped by TAURON Wytwarzanie due to the loss of its business justification. The project continues to maintain the stopped project status and it will be possible to resume it in case the regulatory and market environment turns favorable.

CCGT unit construction project at Elektrownia Blachownia Nowa sp. z o.o.

On December 19, 2017 the Extraordinary GM of Shareholders of Elektrownia Blachownia Nowa sp. z o.o. in liquidation confirmed, through applicable resolutions, the completion of the company's liquidation process. The remaining assets (funds) were split into two equal parts and transferred to KGHM and TAURON Wytwarzanie. It was the consequence of the agreement signed on July 28, 2016 between: TAURON, KGHM and TAURON Wytwarzanie, under which the companies decided in unison to withdraw from implementing the CCGT unit construction project at Elektrownia Blachownia Nowa sp. z o.o., suspended since 2013, and terminate the Partners' Agreement signed between KGHM and TAURON Wytwarzanie, and also to proceed to the liquidation of Elektrownia Blachownia Nowa sp. z o.o.

Capital expenditures

In 2017 TAURON Capital Group's capital expenditures reached PLN 3 474 mln and were approx. 9% lower than the expenditures incurred in 2016 that reached approx. PLN 3 817 mln. This is primarily due to the decreased capex in the following Lines of Business: Generation, Distribution and Mining.

The below table presents selected capital expenditures incurred in 2017, highest by value, by TAURON Capital Group's Lines of Business.

Table no. 5. Capital expenditures, highest by value, incurred in 2017 by TAURON Capital Group's Lines of Business

Item	Capital expenditures (PLN M)
Distribution	
Grid assets' upgrades (refurbishments) and replacements	865
Construction of new connections	610
Generation	
Construction of new capacity at Jaworzno III Power Plant (910 MW)	1 278
CAPEX on upgrades (refurbishments) and replacements as well as components at TAURON Wytwarzanie	77
Investment projects related to the maintenance and development of district heating networks	16
Connecting new facilities	17
Mining	
Brzeszcze Coal Mine's Investment Program	38
Construction of the 800 m level at Janina Coal Mine	41
Construction of the "Grzegorz" shaft, including the infrastructure and the accompanying headings	13

The detailed information on the capital expenditures incurred in the individual Segments of TAURON Capital Group's operations are provided in section 2.3. of this report.

1.5.3. Evaluation of the capability to complete the intended investment projects

TAURON Capital Group's strategic investment projects and the financing thereof are centrally managed at the Company's level. Based on the analyses completed the Company's Management Board assesses that TAURON Capital Group is able to finance the current and future intended investment projects included in the Strategy using funds generated from operations and obtaining debt financing.

1.5.4. Building TAURON Capital Group's value

TAURON Capital Group is conducting operations in all key segments of the energy market, i.e. hard coal mining as well as electricity and heat generation, distribution and trading. Strategy assumes that each Line of Business will be building TAURON Capital Group's value, but in a manner aligned to the market conditions for the given segment. Supply Line of Business as well as the new products and services represent the field of operations that will be intensely expanded by TAURON Capital Group. TAURON Capital Group is changing its profile towards full concentration on the customer. This is achieved by building sustainable relationships with customers, introducing consistent, high customer service standards in each link of the value chain, modern and integrated sales and customer service channels (omnichannel and e-commerce), adapted to today's highest standards. Supply segment and customer service will the main drivers for building TAURON Capital Group's value. Electricity Distribution Line of Business is the most stable line of business in terms of contribution to generating TAURON Capital Group's EBITDA. TAURON Capital Group is planning to maintain a stable role of the Distribution Line of Business and continue the up to now investment policy. Through further upgrades and expansion of its distribution grid TAURON Capital Group will be able to meet the requirements in terms of security and quality of supplies. Generation and Mining Lines of Business will continue to improve the cost and operating efficiency, while a potential expansion of the conventional generation will depend on the market situation or favorable regulations for the conventional generation.

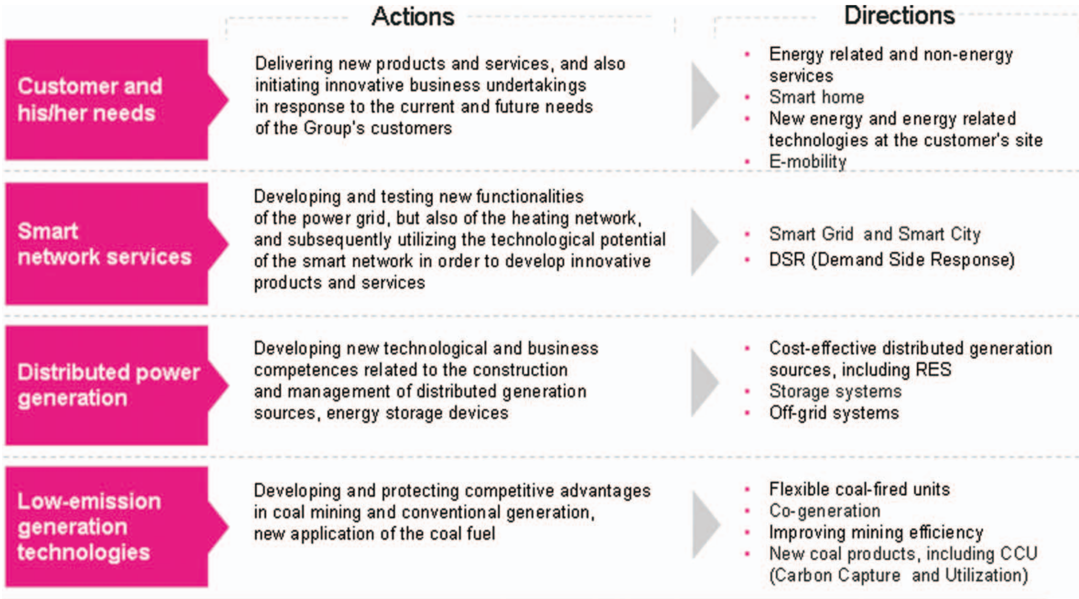
1.5.5. Directions for advancing innovations as well as research and development activities

In its adopted Strategy TAURON Capital Group places its bet on a dynamic expansion of the research and development as well as innovations line of business (R+D+I), viewing it as a way to achieve new revenue in the future. It is assumed that, starting from 2017, minimum 0.4% of consolidated revenue will be spent on R+D+I, as well as on expansion based on, among others, Corporate Venture Capital (CVC) and long term return on the portfolio, and also an annual revision depending on the financial position.

The research and development as well as innovations line of business (R+D+I), in line with the Strategy, introduced portfolio based management of research and development projects in accordance with the priority directions of innovations as well as research and development activities.

The below figure presents the priority directions of innovations as well as research and development activities.

Figure no. 13. Priority directions of innovations as well as research and development activities



The directions of innovations as well as research and development activities were taken into account in the works on developing the Strategic Research Agenda (SRA) conducted in 2017. This document will constitute a conversion of the goals indicated in the Strategy into a "road map" for the R+D+I operations of TAURON Capital Group, accommodating the specifics of the challenges in each of the above four directions and at the same time reaching in the adopted timeframe beyond the timeline of the current Strategy in force.

Additionally, process based management introduced in the R+D+I line of business provided more effective and timely implementation of the R+D portfolio projects by TAURON and TAURON Capital Group's subsidiaries. The change of the line of business operations' organization ensured effective supervision of the Corporate Center over the R+D projects' implementation by TAURON Capital Group's subsidiaries and management of financial and non-financial resources.

1.5.6. Major achievements in the field of research and development

2017 was the first year of the implementation of the Strategy, assuming the R+D+I line of business budget of approx. 0.4% of the consolidated revenue.

Within the dedicated budget a number of research and development projects were launched in all 4 project portfolios, corresponding to the priority directions of the innovations and development activities. At the end of 2017 the R+D project records included 43 projects, including 22 launched and underway, plus 21 at the stage of preparation and acceptance.

The below table presents the most important research and development projects implemented in 2017 by TAURON Capital Group's subsidiaries, co-financed from external sources.

Table no. 6. Selected research and development projects implemented in 2017 by TAURON Capital Group's subsidiaries, co-financed from external sources

No.	Projects/programs/tasks	Co-financing source
1.	• *CO_2-SNG* project, including chemical energy accumulation through production of methane from captured CO_2. • *POLYGEN* project the concept of which is based on the use of the polygeneration processing system in the process of gasifying the locally available fuels (e.g. selected waste fractions).	Knowledge and Innovation Community (Wspólnota Wiedzy i Innowacji) KIC InnoEnergy (KIC InnoEnergy)
2.	• As part of *Power Sector's Research Program* the following projects were launched: • System for assessing propagation and improvement of the quality of electricity in distribution grids. • Developing a platform allowing for aggregating the generation and regulatory potential of the dispersed (distributed) renewable energy sources and energy storage devices as well as the selected categories of controllable consumers. • Integrated Grid Diagnostics System.	National Research and Development Center (Narodowe Centrum Badań i Rozwoju – NCBR)

No.	Projects/programs/tasks	Co-financing source
	• *TENNESSEE* – Development of the industrial design of carbonate fuel cells and ceramic electrolizers enabling integration with the power-to-gas installations. • Flexibility of the existing power generation units with limited capital expenditures. • System for optimizing the operation of conventional generating units aiming to increase their adjustability in order to ensure ongoing stability of the power system and long term conditions for further integration of renewable energy sources. • Platform for managing data from advanced measurement infrastructure. • Dispersed (distributed) power solutions model 2.0 – self-balancing power grid areas. • Applied Research Program under which the project with respect to producing demineralized water to supplement the water and steam circulation using electromembrane methods.	National Research and Development Center (Narodowe Centrum Badań i Rozwoju – NCBR)
3.	• *CERES* project aimed at introducing a number of technology improvements in order to reduce the risk related to the mining waste produced.	European Union's Coal and Steel Research Fund
4.	• *ICP4Life* project related to developing integrated collaboration platform for managing the technology and product services life cycle. • *MOBISTYLE* project related to technology solutions that will allow for positively influencing customer behavior by raising the consumers' awareness and feeling of ownership. • UtilitEE project aimed at implementing a solution that will increase electricity consumption efficiency by actively engaging customers in their behaviors related to electricity consumption with the use of information and communications technologies and DSM mechanisms.	2020 Horizon: Framework Program with respect to scientific research and innovations

8 projects passed NCBiR's verification in 2017 as part of the 1st competition under the Power Sector's Research Program using the funds of the Smart Development Operational Programme, receiving funding in the amount of PLN 21 mln that represented almost 1/3 of the competition's budget. The project that combines the activities of the subsidiaries: TAURON, TAURON Dystrybucja, TAURON EKOENERGIA and TAURON Sprzedaż is *M-GRID 2.0* – "Dispersed (distributed) power solutions model 2.0" – as part of which we will conduct demonstrations of the self-balancing power grid area. The project's goal is to develop the technology to be used to build local power grids the main advantage of which is to reduce transmission losses, improve reliability and flexibility of the system. Knowledge and experience gained with respect to developing and operating microgrids will allow for offering TAURON services to external customers, and also for applying the solution within TAURON Capital Group.

One of the more important research and development projects implemented in 2017 by TAURON Capital Group is the CO_2-SNG project, related to converting CO_2 into synthetic natural gas using the surplus electricity from RES. The project is carried out by an international consortium grouping Polish and French entities, with TAURON Wytwarzanie as the consortium leader. The scope of the project encompasses converting carbon dioxide produced as a result of burning fuels in industrial installations into synthetic natural gas – SNG. This gas will be produced as result of CO_2 reacting with hydrogen coming from the elektrolysis process, powered using cheap electricity coming from RES in the power system's load valleys. The project assumes that this can be the method to store electricity surplus from renewable sources, and at the same time a future-proof solution for utilizing CO_2 produced at TAURON Capital Group's installations. Funding from KIC InnoEnergy was obtained to implement the project. The project constitutes the basis for other projects: POLYGEN and TENNESSEE.

The goal of the POLYGEN project is to develop a technology solution to fill a market niche of environmentally friendly and cost effective thermal waste and alternative fuel processing for small and medium size applications. The project's product will be the development of technology to produce heat, electricity and synthetic natural gas based on gasifying alternative fuels such as municipal waste, dewage sediments or biomass.

The goal of the TENNESSEE project is to improve energy storage process in the chemical form – natural gas substitute, aimed at improving operating parameters of the ultimate installation, mainly based on the higher efficiency of the high temperature electrolysis and the use of carbonate fuel cells to capture CO_2 from flue gases which does not require supplying electricity from the power plant to the capture system. In particular the project will contribute to lowering the energy intensity per a unit of the SNG produced.

An important accomplishment was also the launching of the UtilitEE project co-financed under the Horizon 2020 program under the name of "Transformation of an electricity supplier's business model with a view to energy efficiency based on changing human behaviors and the use of information and communications technologies". The project activities are aimed at implementing a solution that will increase electricity efficiency consumption by actively engaging customers in their behaviors related to electricity consumption with the use of information and communications technologies and DSM mechanisms.

In the Supply Line of Business the key research and development project is "PROmoc – active management of the energy balance and customer preferences in order to optimize the use of the potential for adjusting (controlling) demand for electricity". The project's task is to generate benefits from efficient capacity management for three market participants: customer, utility company contracting electricity and the entity managing the national power system's security.

In 2017 TAURON continued activities with respect to building mechanisms for cooperation between industry and science as well as between industry and startups. In this regard the participation in the works of the Technology and Innovations Highway Institute (Instytut Autostrada Technologii i Innowacji), set up in 2014, that is the new platform for cooperation between industry and Polish universities, took place. In the Pilot Maker program, co-financed by the Polish Agency for Enterprise Development (PARP) as part of the Scale Up competition, 3 startup selection processes were carried out. Since the beginning of 2017 in the entire program TAURON reviewed almost 130 solutions prepared by startups. i.e. 46 in the first selection process, 23 in the second selection process and 60 in the third selection process. 30 startups began cooperating with TAURON on preparing solutions in response to the technological challenges defined by TAURON Capital Group. Currently 26 startups are testing their solutions on TAURON's infrastructure or preparing their solutions for such tests (pilots). The program's leader is techBrainers sp. z o.o., the main partner is TAURON, the other partners are well known companies Kross S.A. and Amplus sp. z o.o.

In 2017 TAURON Capital Group was carrying out works as part of KIC InnoEnergy, in particular the Polish node of InnoEnergy Central Europe sp. z o.o. with its seat in Kraków (one of six in the EU). Within the structures of KIC InnoEnergy TAURON holds the Asscoiated Partner status. One of TAURON's areas of interests are the so-called clean coal technologies. At the same time conducting of tests and coordinating of activities in this area are the main tasks of InnoEnergy Central Europe sp. z o.o., of which TAURON is one of the shareholders. In 2017 the Company's representatives were engaged in the works of KIC InnoEnergy, related to evaluating projects/initiatives proposed to be implemented by other partners operating within the structures of KIC InnoEnergy, both on the national, as well as international level. Additionally, two projects were completed as part of the cooperation with KIC:

1) Smart Home project, encompassing developing a system of integrated devices allowing for an efficient way to remotely manage operation of electric devices and control safety at home.
2) Prointerface project, encompassing developing a system for individually evaluating disruptions of the quality of electricity in the distribution grid along with the power electronic interface for connecting dispersed (distributed) renewable energy sources. In 2017 the first Survey of the Level of Innovations at TAURON Capital Group's subsidiaries that will constitute the basis for monitoring the progress in this area in the subsequent years.

2. TAURON CAPITAL GROUP'S OPERATIONS

2.1. Factors and non-typical events that have a significant impact on earnings achieved

2.1.1. Internal factors and the assessment thereof

TAURON Capital Group's operations and earnings in 2017 were impacted, among others, by the following internal factors:

1) actions with respect to optimizing processes taken by all of TAURON Capital Group's subsidiaries,
2) first effects of the implementation of the Strategy due to implementing the Strategic Initiatives and optimizing capital expenditures,
3) implementation of the Efficiency Improvement Program aimed at reducing TAURON Capital Group's operating expenses in 2016–2018, including the consolidation and restructuring projects, the Voluntary Redundancy Programs for the workforce,
4) decisions with respect to the implementation of the key investment projects, in particular with respect to the construction of new generation capacity and refurbishing the existing generation capacity, the construction of new connections and upgrading (refurbishing) the existing distribution grids, district heating networks, the construction of the underground headings,
5) loyalty building measures aimed at retaining the existing customers and marketing activities with respect to acquiring new customers,
6) centralizing TAURON Capital Group's financial management, supported by the use of such tools as: central model of financing, cash flow (financial liquidity) management policy using the cash pooling mechanism, risk management policy in the financial area, insurance policy,
7) ability to obtain debt financing on international markets,
8) Tax Capital Group's operations, primarily aimed at optimizing the performance of the obligations associated with the payment of the corporate income tax by TAURON Capital Group's key subsidiaries,
9) TAURON's procurement management, in particular, management of fuel purchases for the needs of TAURON Capital Group's generation entities,
10) geological and mining conditions of hard coal extraction.

The impact of the above mentioned factors on the financial result achieved in 2017 is described in section 4 of this report. The effects of this impact are visible both in the short term as well as in the long term outlook.

2.1.2. External factors and the assessment thereof

TAURON Capital Group's operations and earnings in 2017 were impacted by the following external factors:

1) Macroeconomic environment.
2) Market environment.
3) Regulatory environment.
4) Competitive environment (landscape).

2.1.2.1. Macroeconomic environment

TAURON Capital Group's core business operations are conducted on the Polish market and the Company takes advantage of the positive trends occurring thereupon as well as it is affected by the changes thereof. The macroeconomic situation, both in the individual sectors of the economy as well as on the financial markets, is a significant factor impacting the earnings generated by the Company and TAURON Capital Group.

2017 was generally positive for the Polish economy. The Central Statistics Office (GUS) informed in March 2017 that all economic indicators improved. Registered (official) jobless rate reached 8.5% in February 2017. Additionally, Moody's raised Poland's Gross Domestic Product (GDP) growth rate forecast to 3.2% year on year. All this information allowed for strengthening of the Polish currency both versus EUR as well as USD. In March 2017 the USD/PLN exchange rate declined 2.54% to PLN 3.96, while the EUR/PLN exchange rate dropped 1.74% to PLN 4.23. In April 2017 more positive information on the Polish economy surfaced. In March 2017 the manufacturing industry's sold output rose 11.1% year on year. The actual monthly industrial production growth rate reached 17.6%.

In the subsequent months of 2017 more positive information was published. In June 2017 average wages in the enterprises sector rose to PLN 4 508. Also, employment in the enterprises sector went up, leading to the fall of the jobless rate to 7.1%. Furthermore, in Poland, similar to the Eurozone, an increase of the manufacturing industry's PMI was observed reaching 53,1 and 56.8, accordingly.

It should be noted that CPI rose 1,5% in the period under review. In November 2017 the consumer products and services price index increased 2.50% on annual basis and 0.50% on monthly basis. GDP growth rate reached 4.9% year on year in Q3 2017, versus 4% in Q2 2017. According to the Central Statistics Office (GUS) data GDP growth rate for the entire 2017 reached 4.6% versus 3.6% expected earlier which undoubtedly proves the strengthening of the country's economy.

According to the data of Polskie Sieci Elektroenergetyczne S.A. (PSE, TSO) 2017 brought a significant increase (2.13% year on year) of the gross national electricity consumption (KZEE), covered mainly by the rise of production from the domestic power plants (1.98% year on year) – and increased imports (14.41% year on year) that reached 2.23 TWh in 2017.

Due to the increased demand for electricity in the National Power System in 2017 TAURON Wytwarzanie's generating units produced approx. 8,8% more gross electricity than in 2016. Increased electricity output had a direct impact on the volume of consumed coal.

2.1.2.2. Market environment

Electricity

Wholesale electricity prices on the Day Ahead Market (RDN) of the Polish Power Exchange (Towarowa Giełda Energii S.A. – TGE) in 2017 in Poland, in spite of rising commodity and CO_2 emission allowance prices, were on an averaged annualized basis lower than in 2016 and reached 157.84 PLN/MWh (-1,38 PLN/MWh in comparison to 2016). The CRO price on the Balancing Market na Rynku (RB) reached 166.65 PLN/MWh (+2,46 PLN/MWh on an annualized basis).

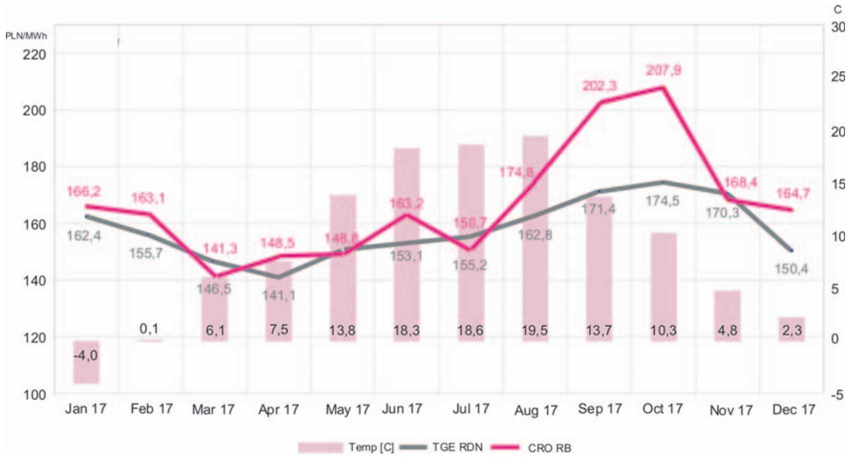
The main reason for a slight price decline on the RDN was a good situation in the National Power System (KSE) and relatively low and very low prices in the 1st half of 2017. The situation improved in the 2nd half of 2017. Rising demand for capacity (year on year increase by 3.99 TWh to 168.4 TWh) in combination with overhaul plans for the centrally dispatched generating units had a significant impact on the increase of CRO prices that were higher, on average, by 8.81 PLN/MWh than the prices on the RDN.

The impact of the rising electricity consumption on the increase of electricity prices was to a certain extent offset by the record volume of electricity produced by the wind sources (14.4 TWh, increase by 2.7 TWh in comparison to 2016). In 2017, in spite of the rising demand, generation output from hard coal fired power plants declined (to 78.7 TWh, i.e. by 1.5 TWh in comparison to 2016). Rising demand was satisfied by increased production at more expensive power plants, for example, the gas-fired ones, the output from which, on an annualized basis, rose 37.8% to 5.8 TWh.

In spite of commissioning approx. 730 MW of new capacity in wind power plants in 2016, a slight increase of the production from RES did not bring the expected output increase in this sub-sector. At the same time a significant, by as much as 4.4%, drop of production from cheap lignite fired power plants was observed in 2017 which had to be offset by the rising production at more expensive power plants, for example, the gas-fired ones, the output from which, on an annualized basis, rose 24.2% to 7.2 TWh. Additionally, KSE was supported by electricity imports in the volume of almost 2.4 TWh.

The below figure presents average monthly electricity prices on the SPOT and RB markets, as well as average temperatures.

Figure no. 14. Average monthly electricity prices on the SPOT and RB markets, as well as average temperatures



The base load contract with the delivery in 2018 was in a clear upward trend on the futures market in 2017. BASE_Y-18 contract prices, after the closing of the BASE_Y-17 contract, began with an up gap in the region of approx. 3 PLN/MWh. However, the gap was quickly closed due to the declining CO_2 prices to the level below 160 PLN/MWh at the end of the first decade of January 2017. In the second half of January 2017 the prices rose and fluctuated in the approx. 160–161 PLN/MWh range. Subsequent months brought stabilization of prices. Only at the end of the summer holidays period rising electricity prices were observed on the energy markets almost all over Europe. The biggest price increases occurred in France, Spain and in Germany (fears of a repeat of the cold 2016/2017 winter and problems with satisfying the demand). In August 2017 the BASE_Q4-17 and BASE_Q1-18 products were particularly high priced, frequently above 50.00 EUR/MWh, i.e. much higher than the reference quarterly product listed on TGE. In September 2017 the average price of the BASE_Y-18 futures contract reached 166.80 PLN/MWh, i.e. it was 3.00 PLN/MWh higher than in August 2017. Forward market electricity prices in October 2017 continued the upward trend commenced in September.

Factors supporting the demand side remained unchanged. A high coal price on the world markets, rising EUA unit prices and a tight situation in the French power system as well as the approaching winter effectively supported reaching new price peaks on the forward products. Additionally, high SPOT price levels also had a clear impact on the wholesale market prices. In October 2017 the average price of the BASE_Y-18 futures contract reached 172.70 PLN/MWh, i.e. it was almost 6.00 PLN/MWh higher than in September. However, the biggest price increase occurred at the beginning of December 2017, when the price of the BASE_Y-18 contract was close to 180 PLN/MWh. The average volume weighted price of the BASE_Y-18 product reached 165.98 PLN/MWh, with the total trading volume reaching 65.2 TWh, i.e. it was more than 10 TWh lower than in 2016.

The below figure presents the BASE Y-18 contracts performance.

Figure no. 15. BASE Y-18 contracts performance

Crude oil and coal

2017 on the crude oil market was characterized by the continuation of the upward trend following the declines that had taken place in 2014–2015. The crude oil prices fluctuated in the 44,35–67.1 USD/bbl range in the period under review.

The beginning of 2017 was characterized by low price volatility. In February crude oil prices fluctuated in the 54.4–57.45 USD/bbl range. At that time investors were analyzing the agreement between the OPEC cartel and Russia, aimed at reducing the crude oil output, and the data on the crude oil production output and inventory levels in the US. It should be noted that a large role in OPEC is played by Saudi Arabia and this country is interested in high oil prices due to the largest IPO in history – the stock market debut of Saudi Armaco.

On March 26, 2017 an OPEC meeting was held in Vienna during which, however, no unequivocal and binding decisions on production levels were taken. Two days later cyclone Debbie hit the northwestern coast of Australia which led to a rise of commodity prices, including also crude oil. In spite of OPEC and Russia's efforts the United States did not join the agreement aimed at reducing oil production, on the contrary, in April 2017 the US observed an increase of its output by almost 0.5 mln bpd, and as a result the worldwide crude oil inventory did not decrease to the expected levels which had a direct impact on the mood on the market.

The second half of 2017 was characterized by a strong anxiety on the market caused by weather related natural disasters and political turmoil. Hurricanes Harvey and Irma had a strong impact on oil prices at the end of August and beginning of September. As a result of the forces of nature a number of US refineries had to stop their operations which led to problems with excessive stockpiles of extracted oil.

Due to increased exports of US oil to other markets the US WTI oil price discount versus the Brent oil widened. Petrol price increased, refining margins rose due to smaller supply of petrol. The strengthening of the crude oil prices in September was due to the “restart” of the US refining industry, but also due to the rising geopolitical tensions. An important factor was also an increase of tension between North Korea and the US and Japan.

Additionally, Kurdistan announced an independence referendum which led to a sharp reaction from Turkey. It threatened to cut off oil supplies from Iraqi oil field in the Kirkuk area to the Ceyhan port in Turkey, which would substantially reduce oil supply.

The situation on the coal market was similar. In Q1 2017 the coal prices were not highly volatile. However, looking at the entire 2017 an upward trend of this commodity should be emphasized. Prices moved in the range between 61.75, and 90.75 USD/Mg. Relative peace on the market was due to investors waiting for the decision of the Chinese National Development and Reform Commission – NDRC, on limiting the number of days in a year when coal may be extracted. Furthermore, safety issues also arose in China – as a result of ad-hoc audits mining was suspended at coal mines that did not meet safety requirements.

On the other hand, due to the beginning of the season characterized by the lower demand for coal, prices on the worldwide market began to drop. Unexpectedly, the aftermath of cyclone Debbie that hit Australia became a factor inhibiting the market declines observed. Particularly strong price hikes during that time were applicable to coke with Australia being one of its main producers, where some mines were closed and the railway infrastructure was destroyed due to difficult conditions as a result of weather related natural disasters. Following the disruptions related to cyclone Debbie coal prices with the delivery in 2018 returned to lower levels. However, Australia was soon hit with flooding rains and finally the price stayed at a relatively high level of 66 USD/Mg.

Additionally, in China, due to overhauls, a very important railway line that connects regions where coal is extracted with the Quindango port was temporarily closed. As a result of these occurrences coal prices with the delivery in 2018 went up by a few dollars – to 68 USD/Mg. Only after a few weeks the situation began to normalize. Finally, the coal at ARA ports with the delivery in 2018 cost 66.50 USD/Mg. In the subsequent months of 2017 temperatures were rising and the precipitation was declining which as a consequence led to the falling water levels. In China the hydroelectric plants’ production fell by as much as 70%, and hydro is the second largest source of energy in this country, following coal. Additionally, continued disruptions on the supply side, as a consequence of cyclone Debbie and flooding rains, led to the rising demand on the market.

Coal prices in September at ARA ports with the delivery in 2018 were in an upward trend that began already in March 2017. In the period under review coal prices with the delivery in 2018 reached the maximum level of 84.25 USD/Mg, i.e. the highest value since 2014. Such increases were caused by the strong demand in the Asia region and speculations related to the possibility of a repeat of last year’s problems of nuclear plants in France and higher coal consumption in Europe. At the end of the month the prices suffered a correction which was due to the lower demand for coal in China, related to the approaching National Days holidays lasting a full week. Also, a transition period for a ban on coal imports from North Korea was introduced which led to increased supply. Finally, at the end of the year coal prices landed at levels not seen since 2013, reaching 90 USD/Mg.

Natural gas

Year 2017 brought price increases on the gas market following the record low prices in 2016. The average price on the Day Ahead Market for gas on the Polish Power Exchange (TGE) reached 84.69 PLN/MWh in 2017 and it was more than PLN 13 higher than in 2016. Contracts with the delivery on the day ahead were particularly high priced in the first two and the last two months of 2017, i.e. during the gas winter season, when the demand for fuel is the highest. Prices in January and in December topped 100 PLN/MWh a number of times. The maximum value was achieved on December 13, 2017 and it reached 105.10 PLN/MWh. High prices in Q1 2017 were the result of increased demand for gas all over Europe, caused by unavailability of some nuclear plants in France (which led to a larger generation from gas-fired sources) and a relatively long cold period.

In Poland the daily average temperatures on a few January days did not exceed -11°C, while temperatures above 0°C began to appear only in mid-February 2017. Due to increased gas consumption an extension of the cold spell may have led to real problems with availability of gas fuel in Europe. Fears of a repeat of the situation that occurred at the end of 2016 / beginning of 2017 were also the reason for high prices at the end of 2017. The distribution of prices on the spot market in 2017 was characteristic for the gas demand distribution (a clear drop of prices during the period of lower demand in the summer).

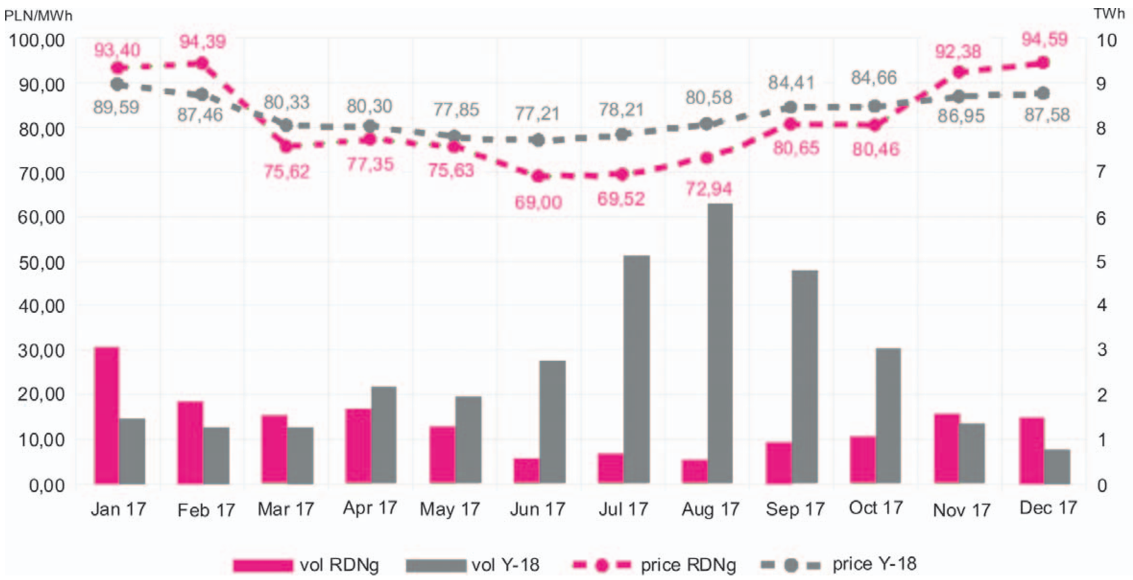
Similar to the markets with a shorter delivery period, on the forward contracts market Q1 and Q3 were characterized by a markedly higher price. The reference one year contract in 2017 was priced within the 76.80–92.27 PLN/MWh range, while upon expiration it was priced at 86.50 PLN/MWh.

The total trading volume on TGE in 2017 reached more than 138.5 TWh. As compared to the previous year an increase by 21% occurred. The forward contracts market had the biggest share in the trading volume, generating a volume at the level close to 115 TWh. On the spot market the total volume of the day ahead contracts and weekend contracts reached more than 19 TWh, which was 0.5 TWh less than in the previous year. A similar slight decline was also observed on the Day Ahead Market for gas where the trading volume reached 4.7 TWh.

The key event for the development of the gas market in Poland was the first historic LNG delivery from the US. A ship carrying liquid gas entered the terminal in Świnoujście on June 7, 2017. While the new rules of maintaining mandatory gas inventory came into force on October 1, 2017. According to these rules importers that want to maintain mandatory gas inventory outside Poland must – in order to ensure their ability to transfer such gas to Poland in case of an energy crisis – reserve the so-called continuous transmission capabilities on the transborder lines (interconnectors). The reserved transmission capabilities are to allow for transmitting the entire inventory to Poland in any conditions within maximum 40 days and additionally they cannot be used for any other purposes, for example commercial (trading) ones.

The below figure presents average monthly SPOT and Y-18 contract prices on TGE in 2017.

Figure no. 16. Average monthly SPOT and Y-18 contract prices on TGE in 2017



CO_2 emission allowances

The CO_2 emission allowances market in 2017 was characterized by high price volatility, caused to a large degree by political factors. During the period under review the prices moved within the 4.29–8.30 EUR/Mg range.

Q1 2017 market should, finally, be deemed as being in the downward trend, in spite of major political events at the EU level, related to the 4th trading period of the European CO_2 Emission Allowances Trading System (EU ETS). The first factor indicating a downward trend were clear declines of electricity contract prices in Germany and France, previously featuring high volatility due to the design problems of the French nuclear plants. Another factor impacting the entire 2017 year was a record high volume offered at the CO_2 emission allowances auctions, Poland's first auction was held on March 29, 2017. It worth noting that the weather conditions in Q1 2017 supported increased utilization of the renewable energy sources. Events that occurred in Q2 2017 resulted in a change of the market mood, and as a consequence a reversal of the downward trend. The main themes attracting the market's attention were:

1. Redemptions of the CO_2 emission allowances – by April 30 every year all industrial installations covered by the EU ETS shall have an obligation to perform the so-called redemptions of the emission allowances the number of which must correspond to the verified emission volume from last year. In case the installation operator does not complete the redemption at the right time, this may lead to an imposition of a financial penalty of 100 EUR/ $MgCO_2$. For comparison it is worth mentioning that the average EUA price quoted on the market during the period of redemptions fluctuated around 5 EUR/Mg.
2. France's presidential elections.

3. Publishing information on the current oversupply volume on the market – by May 15 every year the European Commission undertook to publish data on the oversupply on the market, and this way it will be possible to estimate what oversupply volume will be allocated to the MSR in the subsequent year.
4. G7 meeting – during which one of the leading themes was the ecological policy, and in particular the theme of the so-called "Paris Agreement". The climate agreement signed in Paris in 2015 by 195 states from all over the world constitutes an action plan aimed at limiting the rise of temperatures worldwide. During the G7 summit the US President raised his objections against the above mentioned agreement. Finally the US does not respect this document.

July 2017 for the emission allowances market was a month that continued the upward trend commenced in June. The prices fluctuated between 4.99 EUR/Mg and 5.62 EUR/Mg, while the average price for the period under review reached 5.27 EUR/Mg. Continued price increases on the market were to a large degree a consequence of the weather conditions in Europe. Extended period of high temperature and low precipitation led, first of all, to increased demand for electricity (substantial increase of use of cooling devices) and secondly, a difficult hydrological situation in some EU countries. The above mentioned factors of fundamental nature increased the intensity of the use of the hard coal-fired power plants, and thus contributed to an increase of demand for EUAs. In August the ASE Agency ordered a re-checking of all nuclear reactors located in France in order to finally verify the safety of the installations. This information led to a wave of speculations related to the possibility of a repeat of the 2016 situation. The last month of Q3 2017 featured a substantial price volatility. During only 8 session days the price rose by almost 33%. In the beginning of the month market transactions were made at the level of 5.82 EUR/Mg, while a few days later, the CO_2 emission allowances were contracted at the level of 7.72 EUR/Mg. Such large increases were a consequence of rising fears related to the situation of the French nuclear power plants, as well as the German elections. Furthermore, following the takeover of the EU presidency by Estonia, the works related to the legislation of the EU ETS system's phase 4 were accelerated. October 2017 for the emission allowances market was a month of continued strong growth commenced in the previous month. The EUA prices fluctuated between 6.77 EUR/Mg and 8.05 EUR/Mg, which indicates that in the period under review the prices went up by 18.91%, i.e. by 1.28 EUR/Mg. The price increase was caused mainly by the speculative factors, related to the legislation of the EU ETS system's phase 4, surfacing information on the manner of Great Britain exiting the system, as well as related to the problems of the nuclear power plants in France. Additionally, EUA price increases were impacted by the strong upward trend on the coal market. In November 2017 a working group made up of representatives of three main European institutions completed the works on the EU ETS system's phase 4 that will be in force in 2021–2030. In accordance with the agreements reached the reform defined among others:

1) Market Stabilization Reserve (MSR),
2) Linear Reduction Factor (LRF),
3) quantity of emission allowances available at the CO_2 emission allowances auctions,
4) quantity of free of charge emission allowances granted during the regulation period,
5) modernization and innovation fund.

It is worth noting that the so-called Modernization Fund, and specifically its provisions, prevented the completion of the legislation in October 2017. In its current form the provision on the emission conditions was removed from the provisions setting up the Modernization Fund, however a provision prohibiting the Modernization Fund from subsidizing coal-fired units. In December 2017 the growth trend, developing since Q2, was continued – the prices were moving within the 6.94–8.30 EUR/Mg range.

The below figure presents the impact of the legislative works and the environment on the EUA SPOT product price in 2017.

Figure no. 17. The impact of the legislative works and the environment on the EUA SPOT product price in 2017

Property rights

2017 has brought upon significant changes on the property rights market, mainly related to amendments of legal regulations. Lasting oversupply of PMOZE_A property rights in the market has caused that since June 2017 the average monthly values of the OZEX_A index have been dropping from 37.98 PLN/MWh in January to a historic minimum of 24.38 PLN/MWh in June. In the same period, the surplus on the PMOZE_A register increased by 8.6% to 25.42 TWh. Beginning with July 2017, the prices started to slowly grow back. Compared to 2016, the average weighted price of the OZEX_A index has dropped by nearly 50% to 38.83 PLN/MWh, while the balance on the PMOZE_A register by the end of 2017 was 28.14 TWh that when taking into account the rights blocked for redemption leaves a value of 24.90 TWh at the end of 2017. One should also note the trading volume in “green” certificates in 2017, which amounted to over 10 TWh. So far this was the biggest trade in the history of “green” property rights (higher by as much as 36% than in 2016). According to the *act of 20 July 2017 on amendment of the act on the renewable energy sources*, which came into force on 25 September 2017, the substitution fee in force until September 2017 was 300.03 PLN/MWh, while for the following three months of 2017 this fee dropped to 92.03 PLN/MWh, being 125% of the weighted average price of 2016. The obligation to submit PMOZE_A certificates for redemption increased to 15.40%.

The prices of certificates confirming energy generation from agricultural biogas (called “blue” certificates) for which the obligation rate in 2017 was 0.6% were above the substitution fee that was 300.03 PLN/MWh. From January to May the monthly average prices of the TGEozebio index were dynamically growing, respectively from 301.15 PLN/MWh to as high as 408.08 PLN/MWh. In the following two months this trend has reversed and the prices returned to the substitution fee level. Finally the average weighted value of the index at the end of 2017 was 333.89 PLN/MWh. The total traded volume was 522.5 GWh, and the PMOZE_BIO register balance at the end of 2017 was 309 GWh. Taking into account the certificates blocked for redemption, this value has dropped to 206 GWh.

According to the *act of 10 April 1997, the Energy Law,* amended in 2016, until 30 June of each calendar year the property rights issued to cogeneration units for generation in the previous year may be redeemed. Due to the above, until the end of H1 listings included the property rights for cogeneration both in 2016 and in 2017, while in H2 listings included exclusively the property rights confirming energy generation in 2017.

Until the end of June 2017, the PMEC-2016 (high-efficiency cogeneration) was traded, listed in a narrow price band from 10.76 PLN/MWh in January to 9.27 PLN/MWh in June. However, as of beginning of May 2017, the POLPX started listing PMEC-2017 with opening at 9.68 PLN/MWh. Until the end of 2017, also in case of this instrument the volatility of the KECX index was symbolic and with respect to the monthly values was a mere 0.11 PLN/MWh, while by the end of 2017 the listings ended at 9.79 PLN/MWh. The market prices fluctuated slightly below the substitution fee defined at 10 PLN/MWh.

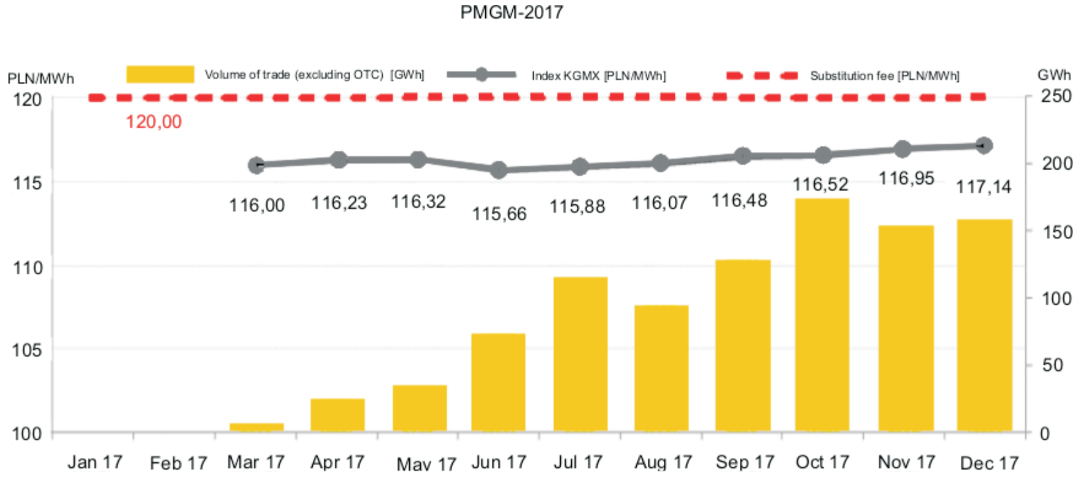
In gas cogeneration the situation was very much alike. By the end of June 2017, the PMGM-2016 instrument was still listed, closing at 112.21 PLN/MWh. This level, like in case of the coal based cogeneration, was determined by the substitution fee, for 2016 set at 125 PLN/MWh. The PMGM-2017 instrument, concerning generation in 2017, was listed already in March 2017, with the average KGMX index at 116.00 PLN/MWh. Until the end of 2017 its value was increasing on month to month basis, reaching 117.14 PLN/MWh in December. The average listings in 2017 for PMGM-2017 instrument were 116.48 PLN/MWh and were just c.a. 3.50 PLN/MWh below the substitution fee, which for 2017 has dropped to 120 PLN/MWh.

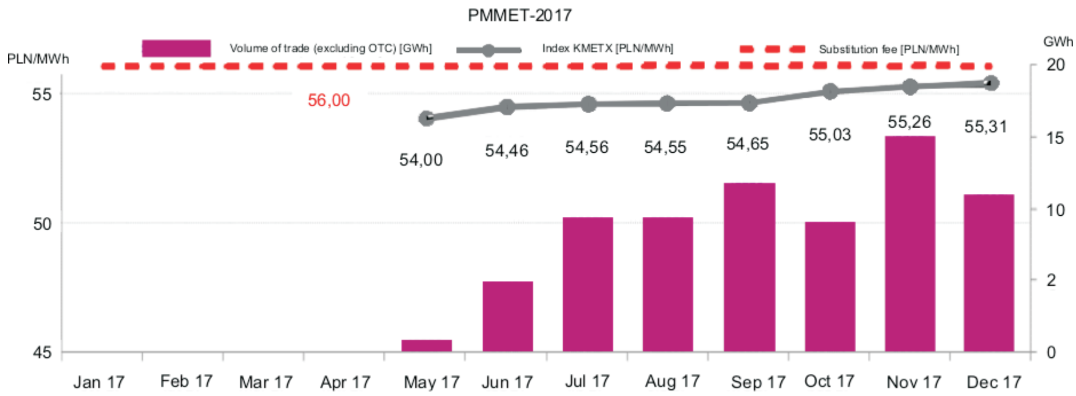
The situation on the market in PMMET property rights confirming energy generation from firing methane was developing similarly to that in case of “yellow” and “red” certificates. Until the end of June 2017 the PMMET-2016 instrument was still listed, with its average value of the KMETX index being 62.19 PLN/MWh. The substitution fee concerning production in 2016 was 63 PLN/MWh, while for 2017 it was lower by 7 PLN/MWh and determined the market prices. The PMMET-2017 instrument for production from the previous year was listed on average at 54.88 PLN/MWh.

The property rights due to the PMEF certificates of energy efficiency (the so-called “white” certificates) continued the downward trend. At the beginning of 2017 the average monthly prices dropped from 1 219,38 PLN/toe in January to the historical lows of 385.86/toe. Finally the weighted average index reached 693.36 PLN/toe and it was as much as 807 PLN/toe lower than the substitution fee set for 2017 at PLN 1 500.00/toe.

The below figure presents the property rights indices, the so-called “green”, “blue”, “red”, “yellow” and “violet” certificates.

Figure no. 18. Property rights indices





2.1.2.3. Regulatory environment

Capacity market law

On December 28, 2017 the President of the Republic of Poland signed the *act of December 8, 2017 on the capacity market*, that came into force on January 18, 2018. This act has a significant impact on the future functioning of the Polish energy sector. The essential goal of the act is to satisfy the deficit of generation capacity due to the foreseen growth of demand for the peak capacity and the simultaneous substantial scope of the planned retirements of generating units from operation. The law defines, among others:

1) rules of providing the service of maintaining readiness to deliver electric capacity and defines the principles of compensation for fulfilling the capacity obligation,
2) organization of the capacity market,
3) rights and obligations of the capacity market participants.

The finally adopted law envisages:

1) permitting foreign capacity market units to take part in the auctions,
2) liquidating price baskets for the new, refurbished and existing units,
3) introducing the possibility of concluding capacity contracts lasting up to 15 or up to 5 years for the new units or up to 5 years for the refurbished or planned units of demand reduction depending on the unit levels of capital expenditures referred to the net achievable capacity,
4) introducing, for the new or refurbished units with emission levels below 450 $kgCO_2$/MWh and cogeneration units feeding the heating systems, the possibility of concluding 2 years longer capacity contracts,
5) taking into account the lack of the possibility to comply with the capacity obligation greater than 40% due to a force majeure occurrence.

Furthermore, it was specified in detail that the period of incurring capital expenditures for the needs of the first main auction shall cover the period from January 1, 2014, and for the needs of the second main auction, from January 1, 2017. For the delivery periods falling in 2021–2023 foreign capacities will be taking part in the capacity market solely by participating in additional auctions. Capacity agreements will not be subject to enforcement until the day the European

Commission's decision on their compliance with the internal market or a decision that this solution does not constitute public aid is issued.

Currently the energy sector is awaiting the publishing of the draft capacity market regulations which is to be published in the coming months and for the executive ordinances. The regulations will describe in detail the course of an auction, including the detailed description of the electricity demand curve. The first capacity auctions are to be held in Q4 2018 and they will be applicable to the 2021–2023 time frame.

BAT conclusions

Best Available Technologies (BAT) mean the most efficient and advanced stage of development and methods of conducting the given operations that indicate the possible use of individual techniques as the base when setting the admissible emissions values and other conditions aimed at preventing arising, and if it is not possible, reducing emissions and impact on the environment as a whole.

BAT conclusions is a document drawn up based on the reference document on the best available technologies, the so-called BREF. BAT conclusions for large combustion plants (LCP) as an executive decision to directive 2010/75/EU on industrial emissions (IED Directive) will be directly applicable. They define the new requirements with respect to admissible emissions values and the monitoring obligation. A consequence of their implementation will be the need to adapt the fuel combustion installations to the requirements defined in the BAT Conclusions by constructing or refurbishing generation sources, flue gases cleaning (scrubbing) installations and in certain cases additionally installing the continuous monitoring systems for the pollutants so far not covered by such an obligation which means the need to bear exceptionally high capital expenditures.

On April 28, 2017 the representatives of the member states in the European Commission passed the new standards tightening the emission standards for the manufacturing industry, i.e. the so-called BAT conclusions for large utility scale combustion facilities. On August 17, 2017 the executive decision of the European Commission (EE) 2017/1442 of July 31, 2017, introducing the conclusions related to the best available technologies (BAT) with respect to large utility scale combustion facilities, was published in the Official Journal of the European Union. Upon publishing the BAT conclusions became a part of the legal order in force in Poland and they will be the basis for issuing the integrated permits.

Apart from more stringent restrictions for the SO_2, NO_x and dust emissions the BAT conclusions introduce emission standards for substances not covered thereby so far, namely for mercury, hydrogen chloride, hydrogen fluoride and ammonia, and also in specific cases order installing continuous monitoring for the pollutants not covered by such an obligation so far. The existing installations have 4 years to adapt to the new requirements and they will have to comply therewith after August 17, 2021. BAT conclusions will be applicable to the facilities and installations burning fuels with the capacity not lower than 50 MW in fuel. They are applicable to both the new facilities that will obtain an integrated permit following the publishing of the conclusions, as well as to the facilities already in operation. New, more stringent requirements related to the permitted values of pollutant emissions will have a significant impact on the future of the European coal-fired power plants.

According to the Ministry of the Environment adapting large industrial installations, including the ones generating electricity and heat, to the tighter SO_2, NO_x and dust emission standards and introduced for the first time binding emission levels for mercury, hydrogen chloride, hydrogen fluoride and ammonia will cost at least PLN 10 bln. Both the costs as well as the schedule of the investment projects aimed at adapting the installations covered by the tightening will be an enormous challenge for the energy sector, especially due to the fact that the refurbishing will have to encompass practically all the power generation units currently in operation. Although the IED Directive provides for an option to obtain temporary derogations from meeting the limit emission values defined based on the BAT conclusions, but such derogation may be granted only if achieving the limit emission values were to lead to unproportionally high costs in relation to the benefits for the environment due to the geographical location of the installations, local environmental conditions or the technical features of the installation.

Further tightening of the emission limits is to take place as a result of subsequent revisions of the conclusions that are to be published every 8 years.

Act on Renewable Energy Sources (RES)

In 2017 works were underway on successive amendments of the *Act on Renewable Energy Sources (RES* law) passed on February 20, 2015. A draft amendment of the law was published and sent for public consultations in June 2017, with its main goal being to ensure the compliance of the provisions of the RES law with the regulations on public aid issued by the European Commission. The amendments presented make the provisions of the Act on RES fully compliant with the requirements defined in the guidelines on public aid related to environment protection and energy goals in 2014–2020, that permit, as compliant with the common market principles, such market instruments as auctions or tender procedures in line with the competition principles that are open for all producers generating electricity from RES competing against one another on equal terms that should substantially ensure that subsidies are reduced to the minimum.

The scope of the amendment defined, among others, a rule on cumulating public aid, new split into auction baskets, additional support rules were proposed in the form Feed-in-tariff (FIT) and Feed-in-premium (FIP) tariffs for electricity generators from renewable sources dedicated for micro and small RES installations that use stable and predictable energy sources (hydroelectricity, biogas, agricultural biogas) with an installed capacity lower than 500 kW – FIT and a capacity not lower than 500 kW and lower than 1 MW – FIP;

On 30 August 2017, the *ordinance of the Minister of Energy of 11 August 2017 on amendment of the quantity share of electricity volume resulting out of the redeemed certificates of origin confirming generation of electricity from renewable sources in 2018–2019* came into force, defining the levels of obligations. These levels are 17.5% and 18.5% respectively, while for the "blue" certificates the share for 2018 and 2019 is 0.5%. The new obligations should result in reduction of certificate surplus on the market, and thus increase of their prices that will be capped by a new substitution fee defined for each year.

On 25 September 2017, the act of *20 July 2017, amending the act on renewable energy sources,* came into force. The key change introduced with this amendment is the discontinuation of the fixed substitution fee in the amount of 300.03 PLN/MWh and relating it to the market prices of certificates of origin of energy from certain RES ("green" and "blue" certificates). This fee is to be equal to 125% annual weighted average price of property rights resulting out of certificates of origin of RES energy, published pursuant to Article 47 (3) 2) of the *act of 20 February 2015 on renewable energy sources*, however not more than 300.03 PLN/MWh.

On 13 December 2017, on power of EU State aid regulations, the European Commission has approved the Polish programme concerning energy from renewable sources. The decision by the European Commission has influenced intensification of work on amendment of the RES act concerning support for RES generators; therefore adoption of another amendment to the RES act is expected in Q1 2018.

In H1 2017, based on the ordinances to the RES act adopted by the Council of Ministers, concerning: the order of conducting the auction sales of electricity from renewable sources in 2017, the maximum volume and value of electricity from renewable sources that may be sold in auctions in 2017 and the reference price of electricity from renewable sources in 2017 and the terms binding the producers who have won auctions in 2017, two RES auctions were conducted for new build and existing producers with installed capacities of up to 1 MW. Subsequent auctions planned to be held in H2 2017 were cancelled by amendment to the previous ordinances.

Amendment to the Water Law Act

The *act of July 20, 2017, the Water Law* was announced on August 23, 2017, however the majority of the new Water law provisions came into force on January 1, 2018.

The act implements into the Polish law, among other, the EU regulations defined in the Water Framework Directive, stating that all water users must incur the costs thereof. The fees shall be applicable to the energy sector, fish growers, farmers and businesses using large quantities of water for their production.

In case of the energy sector the fee for water consumption by hydroelectric power plants is to be borne by the owners of hydroelectric power plants solely for the volume of electricity generated using the reclaimable water and for the intake of non-reclaimable process water.

With respect to the fee for water intake to ensure operation of cooling systems of power plants or combined heat and power plants such fee will be borne solely for the difference between the quantity of water taken for such purposes, and the quantity of water discharged to water streams or to the ground from the cooling systems.

Another fee is the fee for discharging the water from the cooling systems of power plants or combined heat and power plants to water streams or to the ground.

Arrangements concerning the European Union's CO_2 emissions allowance scheme

The beginning of 2017 saw intensification of work on the EU ETS legislation; however, already in 2016 the EU's administration bodies received the preliminary decisions on phase 4 of the EU ETS for consultation. On 15 February 2017, the European Parliament has adopted selected legislative proposals submitted by the ENVI and ITRE committees concerning the shape of the EU ETS in 2021–2030. However, on 28 February 2017 a meeting of environment ministers of the Members States of the European Union was held in Belgian's capital, which adopted the postulates voted at the European Parliament despite objections by nine countries (including Poland), thus demonstrating that EU Member States in majority are for increasing restrictions on greenhouse gas emissions.

Preliminary approval of the resolutions of these institutions has paved the way to further stage of the legislation path adopted in the EU. A working party consisting of representatives of the European Parliament, the European Council and the European Commission (the Trilog) has on 8–9 November 2017 agreed on the compromise text of the draft directive on the reform of the EU ETS in the 4^{th} trading period (2021–2030). The text of the approved reform stipulates, among others:

1) Raising the linear reduction factor (LRF) from the current level of 1.74% to 2.2%.
2) Introduction of the market stability reserve (MSR) mechanism that in principle is to reduce the number of allowances traded in the market to 800 million. In its first years of operation (2019–2023) the mechanism will be absorbing 24% of allowances from the auctioning share and transfer them into reserve. As of 2024, the CO_2 emissions allowances absorption mechanism will be reduced to 12%. Moreover, as of 2023, the allowances held in the MSR in excess of the auctioning share from the previous year will be eliminated.
3) In the fourth trading period the total available auctioning share will constitute 57% with possibility of increase by 3%.
4) Establishment of the Innovation and Modernisation Funds. The Innovation Fund in principle is to support modern low emissions technologies with around 400 million allowances. The Modernisation Fund will support the lowest GDP Member States in modernisation of their energy sectors. The Fund may not be used for supporting energy generation using fossil fuels (with the exception of energy sectors of Romania and Bulgaria).
5) Sectors at risk of carbon leakage shall be allocated 100% of free of charge allowances.

At present, the reform of the fourth trading period of the EU ETS is at the last stage of the approval path provided for by the EU legislative procedure process.

The exchange obligation

The act of 8 December 2017 on the capacity market announced on 3 January 2018 has amended the act of *10 April 1997 – the Energy Law*. In the new wording of the energy Law "energy undertakings dealing with electricity generation are required to sell not less than 30% (previously not less than 15%) of electricity generated in a given year at commodity exchanges in understanding of the *act of 26 October 2000 on commodity exchanges*, or on market organised by a leading undertaking operating a regulated market on the territory of the Republic of Poland (…). The obligation for 2018 shall be fulfilled by energy undertakings dealing with electricity generation with respect to electricity generated as of 1 January 2018.

In December 2017, the total volume of electricity traded in the SPOT and futures markets operated by the POLPX was 13.3 TWh, on year on year basis an increase of 51.2%. In December 2017, the volume of electricity traded in the futures market was 10.8 TWh, meaning an increase by 74.4% comparing to the same period of the previous year, and the trade volume on the SPOT market reached 2.5 TWh, meaning a drop by 3.7% year on year.

However, throughout the entire 2017 the total volume of electricity traded in the SPOT and futures markets was 111.7 TWh, meaning a decrease of 11.8% comparing to the volume in 2016. In 2017 the electricity trading volume on the futures market was 86.4 TWh, meaning a drop of 12.7% comparing to 2016, and the trading volume on the SPOT market reached 27.6 TWh, meaning a drop of 8.6% year on year.

Operating reserve (OR)

In 2017, the OR model did not change functionally. However, the model parameters have changed due to the change of the model calculation baseline. The hourly OR budget was increased from PLN 128 758.72 to PLN 144 070.61 and the CRRM reference hourly price changed from PLN 41.20/MWh to PLN 41.79 /MWh. The hourly required operating reserve volume changed from 3 451.09 MW/h to 3 447.49 MW/h. The COR weighted average price in 2017, determined based on the data published by the Polish Power Grid (PSE) was PLN 33.88/MWh.

Amendment of the act on natural gas stocks

On 2 August 2017, the act of *7 July 2017 came into force amending the act on stocks of crude oil, petroleum products and natural gas, the principles of proceeding in circumstances of a threat to the fuel security of the State and disruption on the petroleum market and certain other acts,* which amended the *act of 16 February 2007 on stocks of crude oil, petroleum products and natural gas, the principles of proceeding in circumstances of a threat to the fuel security of the State and disruption on the petroleum market*, the *act of 10 April 1997 – the Energy Law* and the *act of 22 July 2016 on amendment of the act – the Energy Law and certain other acts*.

The key changes introduced by the above amendment notably include:

1) supplementing the *act of 7 July 2017 came into force amending the act on stocks of crude oil, petroleum products and natural gas, the principles of proceeding in circumstances of a threat to the fuel security of the State and disruption on the petroleum market* with a definition of an entity performing imports of natural gas – the definition considers as an entity performing imports a natural person, legal person or organisational entity not having a legal personality, including an energy undertaking being an owner of a gas transmission system, which performs import of natural gas into the territory of the Republic of Poland for its own needs,

2) unambiguous resolution of doubts concerning the admissible methods of maintaining the mandatory stocks of natural gas by deciding that stocks of gas may be maintained exclusively physically in storage installations connected to the gas transmission or distribution systems,
3) definition of obligations of the operator of a gas storage system and operator of a gas transmission system, aimed at maintaining the mandatory stocks of natural gas at specified level,
4) imposition on the gas transmission system operator of the obligation to notify the President of the Energy Regulatory Office about using the transmission capacities reserved for delivery of total volumes of the mandatory stock of natural gas maintained outside the territory of the Republic of Poland to the domestic transmission or distribution network for other purposes, within 7 of becoming aware of this fact,
5) imposition on energy undertakings performing economic activities of cross-border trade in natural gas and an entity performing imports of natural gas of the obligation to provide the operator of the transmission system with information about the location of storage of mandatory stocks of gas for the purpose of validation of the technical capabilities of delivery of such stock to the gas system,
6) clarification of the rules and procedures in force in the event of activation of the mandatory stock of natural gas for the purpose of balancing the gas system at times of disturbances of gas supply or unforeseen increase of its consumption,
7) clarification of issues relating to imposition of fines on entities that fail to meet the specific statutory obligations,
8) introduction of a transition period during which an undertaking resigns from operations subject to license and then is relieved from the obligations to maintain mandatory stock of natural gas.

Abolishment of tariff obligation

The *act of 30 November 2016 amending the act – the Energy Law and certain other acts* a time schedule was introduced for abolishment of the obligation of gaining approval by the President of the Energy Regulatory Office and application of Tariffs for gas fuels, as of:

1) 1 January 2017, for trade (sales) of gas at a virtual point, sales of LNG and CNG and sales through tenders, auctions or public procurement,
2) 1 October 2017, for final consumers (with exception of household consumers),
3) 1 January 2024, for household consumers.

“Winter Package” and Network Codes

In 2017, at the EU level, work has been conducted focused on elaboration of the final provisions of 11 documents constituting the “Winter Package” proposed by the European Commission on 30 November 2016. The key documents include: Regulation on the Governance of the Energy Union, amendment of the Regulation on the Internal Energy Market, amendment of the Directive on the Internal Energy Market, amendment of the Directive on the Use of Energy from Renewable Sources, amendment of the ACER regulation, amendment of the Energy Efficiency Directive and the Regulation on Risk Preparedness in the Electricity Sector. The documents submitted by the European Commission present the vision of changes that would be implemented in the Union’s energy sector.

The entire “Winter Package” in the proposed shape is intended to guarantee the best possible functioning of non-controllable RES by creating broad opportunities for flow of energy they generate between the Member States. At the same time proposals include transferring a range of – so far national – competences from Member States to the regional and the EU levels. Building an energy union is in principle focused on streamlining the reporting obligations imposed on the Member States and supervision over fulfilment of the goals of the EU climate policy (both the 2030 goals and obligations arising out of the Paris Agreement) with particular attention to decreasing the CO_2 emissions and increasing the use of renewable energy sources.

A lot of stress is placed on growing the internal energy market with particular consideration to the infrastructure interconnecting the energy systems of individual Member States and initiatives to increase the flexibility of operation of the systems with a view to significantly increase the share of renewable energy sources. The Member States are also required to report the progress in improving energy efficiency, including presenting plans for renovation and modernisation of buildings, both public and private.

Initially, the proposals presented by the European Commission provided it with authority to act at the EU level if in the opinion of the European Commission the goals of the energy union or the climate goals could not be achieved due to insufficient contributions by the Member States. Such authority would impose, for example, on the Member States the duty of financial contributions when in the opinion of the European Commission the Union’s goal of RES share would not be pursued collectively. The contributions would be paid into the EU financial platform “contributing” towards development of renewable projects, established at the EU level and managed directly or indirectly by the European Commission. Member States could use as financial contribution their proceeds from greenhouse gas emissions allowances auctions. The European Commission would also be empowered to adopt delegated acts to establish and allow functioning and financing of the aforementioned financial platform. The proposed amendments of the rules governing the functioning of the internal energy market presented the mechanisms limiting the possibilities of use of capacity mechanisms by Member States, by limiting participation in these mechanisms to units with emissions below 550 gr CO_2/kWh, practically unattainable for coal based technologies. The text of the currently amended Renewable Sources Directive presents proposals for limiting the possibility of counting the energy generated from biomass towards achievement of domestic RES goals.

The work on final versions of the texts of regulatory acts constituting the "Winter Package" have been conducted within a "Trilog" of the European Parliament, European Council and the European Commission and at the present stage no agreement has been reached that could gain mutual acceptance.

In 2017, significant part of work was finalised on Network Codes and Guidelines that are the measures used under the EU law for the purpose of construction of Union-wide harmonised market in electricity and gas. The Codes are implemented legally as Regulations of the European Commission that are directly applicable in the Member States without the necessity for their implementation in national legislations. The Codes define common rules for operation and management of energy systems and are intended to eliminate the technical obstacles to further integration of the European electricity and gas markets; they are also intended to foster deregulation and ongoing growth of competition in these markets, as well as to improve service standards and security of supply. The Codes are being developed by ENTSO-E/ENTSO-G and have to comply with the non-binding framework guidelines developed by ACER. Network Codes and Guidelines may be divided into three families:

Market	defines the rules for operation of the electricity balancing market, short term markets – day ahead and intraday, as well as long term markets – forward capacity allocation.
Connection	defines the rules and requirements relating to connection of generators and demand to the electricity networks. It also defines the requirements for high voltage direct current networks and connections.
Operations	defines the requirements and rules for transmission system operators to assure system operation security, effective use of interconnected systems and resources and prevention of propagation or escalation of incidents, to avoid widespread disruptions and blackouts, as well as to allow efficient and quick restoration of electricity systems.

At present all of the eight proceeded Network Codes and Guidelines became effective and the stage of their implementation commences. This process will require further extensive consultations and conducting joint projects, both on the national and the European arenas. Implementation of provisions of the Codes will to a significant extent remodel the principles of operation of the Polish energy market in the upcoming years.

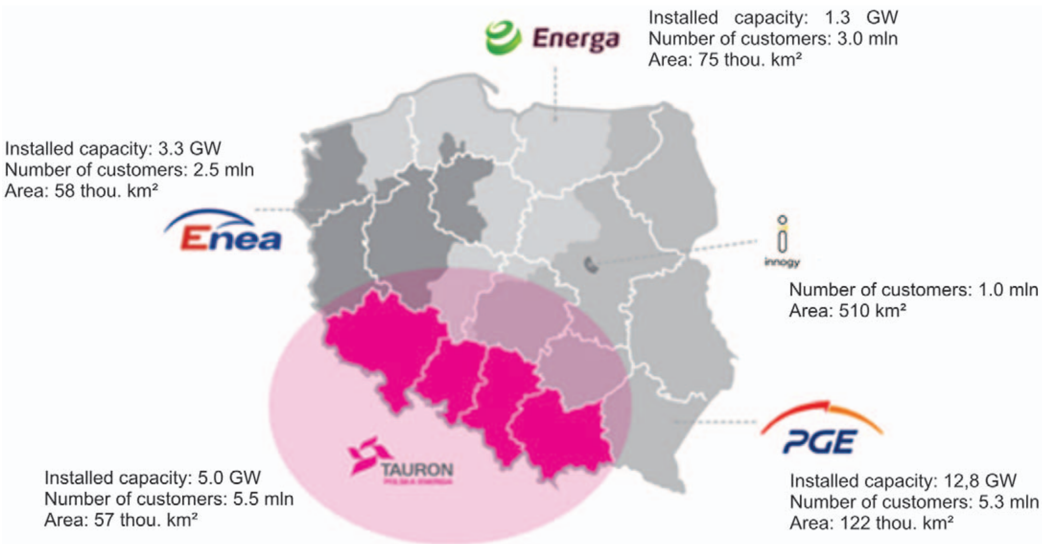
2.1.2.4. Competitive environment (landscape)

Poland's Energy Groups

Apart from TAURON Capital Group currently 3 large, vertically integrated energy groups are operating on the Polish market: PGE, ENEA and ENERGA S.A. (ENERGA).

The below figure presents TAURON Capital Group's competitive environment (landscape) based on the data available, i.e. for 2016.

Figure no. 19. TAURON Capital Group's competitive environment (landscape) (2016 data)



Based on the vertically integrated structure the above entities have a strong position on the domestic market. Furthermore, also foreign energy groups are present on the Polish market.

According to the 2016 data the consolidated energy groups (PGE, TAURON, ENEA, ENERGA) held a 56% market share in the electricity generation subsector. Smaller players, although significant in 2016, included: EDF Polska Centrala sp. z o.o. (EDF) (7%), ENGIE Energia Polska S.A. (ENGIE) (7%) and Zespół Elektrowni Pątnów-Adamów--Konin S.A. (ZE PAK) (5%).

TAURON Capital Group is a fully vertically integrated energy (utility) enterprise that utilizes synergies resulting from the size and scope of the operations conducted.

TAURON Capital Group controls the value chain, from hard coal mining to the delivery of electricity to final consumers. TAURON Capital Group conducts its operations in all key segments of the energy market (excluding electricity transmission), i.e. hard coal mining as well as electricity and heat generation, distribution, supply and trading.

The below figure presents information on EBIT structure by the main segments.

Figure no. 20. EBIT – estimated structure by the main segments in 2016[1]

[1] *In order to make the segments presented comparable the Generation Segment includes also Mining, RES and Heat; Generation Segment includes impairment charges.*
Source: Companies' Annual Reports

Generation

TAURON Capital Group is Poland's second largest electricity generator

TAURON Capital Group's share in the domestic electricity generation market, based on gross electricity production output, reached approx. 10% in 2016, which gave TAURON Capital Group position no. 2 in Poland, behind PGE.

90% of TAURON Capital Group's generation assets are hard coal fired units, 10% of which are modern high efficiency generating units. TAURON Capital Group's total installed capacity reaches almost 5.0 GW. Wind farms' installed capacity represents 3.9%, hydroelectric power plants' installed capacity represents 2.8%, biomass-fired generating units' installed capacity represents 2.3% of TAURON Capital Group's total installed capacity.

Electricity generation market shares changed significantly last year. PGE Group finalized the acquisition of EDF assets and ENEA Group finalized the acquisition of ENGIE assets in 2017. In case of ZE PAK, Adamów Power Plant, a part thereof, was shut down at the beginning of January 2018. The shutdown of the power plant's generating units was due to the European Commission's decision, indicating the need to finish the operation of Adamów Power Plant's generation assets at the beginning of January 2018.

PGE's share in the domestic electricity generation market reached approx. 35% in 2016, with its installed capacity of 12.8 GW. Following the acquisition of EDF's assets (in 2017) PGE's installed capacity rose to almost 16 GW.

ENEA was Poland's third largest electricity generator in 2016, with its market share reaching approx. 8%. ENEA Group's generation assets' capacity rose from 3.3 to 5.8 GW as a result of the 2017 acquisition of Połaniec Power Plant from ENGIE.

Meanwhile ENERGA had the largest, on the Polish market, share of its electricity output coming from RES, reaching more than 30% in 2016. ENERGA Group's total installed capacity reached 1.34 GW.

TAURON Capital Group's generation assets are concentrated in the south of Poland. The hard coal deposits used to fire TAURON Capital Group's power plants and combined heat and power plants are also located in this region. The location of generation assets near the hard coal deposits allows for optimizing the costs related to the transportation of this commodity.

The below table presents information on installed capacity as of December 31, 2016 and on electricity generated in 2016.

Table no. 7. Installed capacity and electricity generation by energy groups in 2016

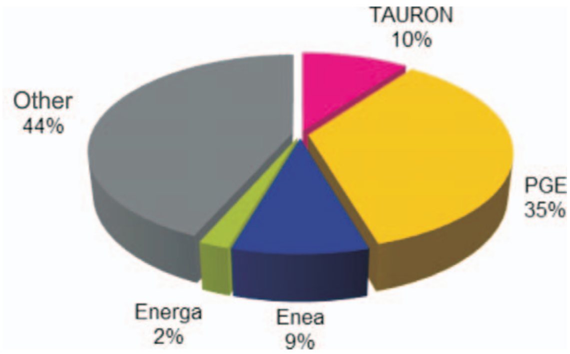
No.	Group	Installed capacity		Generation[1]	
		Value (GW)	Share (%)	Volume (TWh)	Share (%)
1.	PGE	12.75	31	59	35
2.	TAURON	4.96	12	17	10
3.	ENEA	3.30	8	15	9
4.	EDF	3.30	8	12	7
5.	PAK	2.50	6	9	5
6.	Engie	1.90	5	11	7

No.	Group	Installed capacity		Generation[1]	
		Value (GW)	Share (%)	Volume (TWh)	Share (%)
7.	ENERGA	1.34	3	4	2
8.	CEZ	0.60	1	3	2
9.	Other	10.60	26	37	22
	Total	**41.25**	**100**	**167**	**100**

[1] *Volume of gross electricity generated in 2016.*
Source: ARE, information from companies published on their websites, own estimates in case of companies publishing the net production

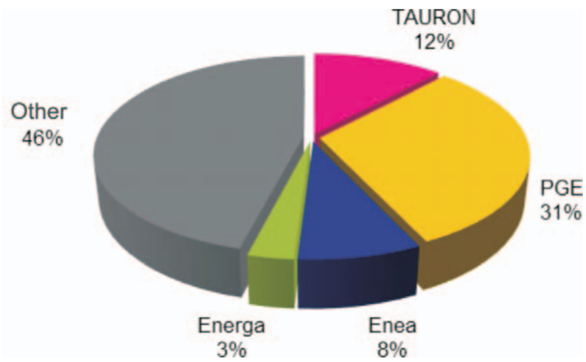
The below figures present information on electricity generated in 2016 and installed capacity as of December 31, 2016.

Figure no. 21. Gross electricity production – estimated market shares in 2016



Source: ARE, information from companies published on their websites

Figure no. 22. Installed capacity – estimated market shares in 2016



Source: ARE, information from companies published on their websites

Distribution

TAURON Capital Group is the Polish market leader in terms of the number of distribution customers and volume of electricity distributed.

TAURON Capital Group is Poland's largest electricity distributor. TAURON Dystrybucja's share in electricity distribution to final consumers reached approx. 38% in 2016 (taking into account top 5 distributors). TAURON Capital Group's distribution grids cover more than 18% of Poland's territory.

TAURON Capital Group is the Polish market leader in terms of the number of distribution customers and volume of electricity distributed.

The below table presents basic information on the share of individual energy groups in terms of electricity distribution based on the 2016 data.

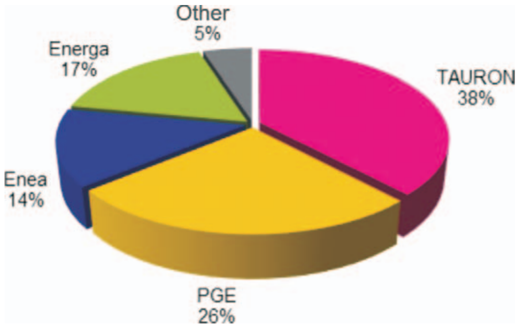
Table no. 8. Electricity distribution to final consumers by energy groups

No.	Group	Distribution	
		Volume (TWh)	Share (%)
1.	TAURON	50	38%
2.	PGE	34	26%
3.	ENERGA	22	17%
4.	ENEA	19	14%
5.	Other	7	5%
	Total	**132**	**100%**

Source: ARE, information from companies published on their websites

The below figure presents basic information on the share of individual energy groups in terms of electricity distribution based on the 2016 data.

Figure no. 23. Electricity distribution – estimated market shares in 2016



Source: ARE, information from companies published on their websites

Based on the data for recent years TAURON Capital Group was number 1 in terms of volume of electricity delivered, with the volume of electricity delivered by the Distribution Segment to the final customers at the level of almost 50 TWh. In 2017 the volume of electricity delivered to the final consumers reached approx. 51,4 TWh. TAURON Capital Group is Poland's largest electricity distributor also in terms of revenue from the distribution operations.

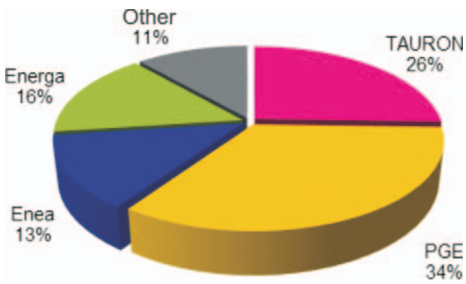
It should be emphasized that TAURON Capital Group's distribution operations, due to the natural quasi monopoly in the designated area, are a source of stable and predictable revenue, representing a material part of the consolidated revenue of the entire TAURON Capital Group. The electricity distribution geographical area on which the Distribution and Supply Segments subsidiaries are historically operating is a strongly industrialized and densely populated area which impacts the demand for electricity both among households, as well as businesses. The number of the Distribution Segment's customers is more than 5.5 mln.

Supply

TAURON Capital Group is Poland's second largest electricity supplier.

The below figure presents basic information on the share of individual energy groups in terms of electricity supply to final consumers based on the 2016 data.

Figure no. 24. Electricity supply to final consumers – estimated market shares in 2016



Source: ARE, information from companies published on their websites

TAURON Capital Group was Poland's second largest electricity supplier behind PGE Capital Group. Electricity retail supply reached 32 TWh in 2016. In 2017 the volume of electricity retail supply reached approx. 34,9 TWh. The number of the Supply Segment's customers is approx. 5.4 mln.

In the electricity supply segment the individual energy groups are geographically tied, first of all, to the areas in which they are performing the DSO function – this is applicable especially to customers classified as households and small enterprises. A broader and more open competition among the groups are limited due to the continued obligation to submit tariffs for households for approval to the President of ERO. The need to apply tariff based prices leads to limited options of positioning prices in the product offerings, and what follows, their attractiveness for customers. These restrictions do not apply to business and institutional customers.

Among the main competitors of TAURON Capital Group in this segment on one hand an upward trend in terms of electricity supply volume is visible, but on the other hand a downward trend in terms of earnings can be observed, which can be the effect of the assumptions adopted in the market strategies of these groups.

The below table presents the main sources of competiveness.

Table no. 9. Sources of competiveness

No.	Line of Business	Initiatives	Sources of competiveness
1.	Mining Generation	1) Reducing the price and fuel supply risk 2) Investments in generating units 3) Operating expenses	1) Own coal resources – security of fuel supply and control over mining costs 2) High efficiency generating units with a competitive unit production cost 3) Improvement of operational efficiency
	RES Heat	1) Operating expenses 2) Investments in district heating networks	1) Improvement of operational efficiency 2) Developing regulated operations
2.	Distribution	1) Operating expenses 2) Investment efficiency 3) Improvement of grid reliability indicators	1) Implementing the ultimate business model 2) Cooperation with the President of ERO with respect to compensation on capex 3) Implemented IT systems, separate processes, clear (transparent) split of responsibilities
3.	Supply	1) Operating expenses 2) Sales margin, developing products tailored to customer needs, growth in new Lines of Business	1) Efficiently allocated operating expenses 2) Brand, current customer base, sales channel held, experience in product and purchasing portfolio management

2.2. Material growth impacting factors

The most material impact on TAURON Capital Group's operations will come, similar as it was in the past, from the following factors:

External factors:

1) macroeconomic situation, particularly in Poland, as well as the economic situation of the area on which TAURON Capital Group is conducting operations and at the EU and global economy level, including changes of interest rates, FX rates, etc., impacting valuation of assets and liabilities listed by the Company in the statement of financial position,
2) political environment, particularly in Poland and at the EU level, including the positions and decisions of the state administration institutions and offices, e.g.: UOKiK, URE (ERO) and the European Commission,
3) changes to the regulations related to the power sector, and also changes in the legal environment, including: tax law, commercial law, environment protection law,
4) introduction of the generation capabilities compensation mechanism (the so-called capacity market) and decisions on the future shape of the OCR (ORM) and cold intervention reserve,
5) support system for electricity generation using high efficiency cogeneration, resulting, on one hand, in the costs of redeeming "red" and "yellow" certificates with the suppliers of electricity to final consumers, on the other hand, in revenue from the sale of "red" and "yellow" certificates with the generators of electricity using cogeneration. The current support system is in force until the end of 2018; no information on its shape beyond 2018,
6) new RES support system, the so-called RES auctions,

7) situation in the power sector, including the activities and actions of the competition on the energy market,
8) number of CO_2 emission allowances allocated for free, and also prices of allowances purchased – in case of a deficit of free allowances,
9) wholesale electricity prices,
10) electricity and coal sales prices and distribution tariffs based on the adopted DSO operations regulation model, as factors impacting the revenues level,
11) prices of certificates of origin of energy from renewable sources and from cogeneration,
12) prices of fuels (energy resources),
13) environment protection requirements,
14) new non-energy products,
15) science (research) and technical progress,
16) demand for electricity and the other energy market products, taking into account changes due to seasonality and weather conditions.

Changes of the above mentioned external factors may constitute premises obliging TAURON Capital Group, in accordance with the International Accounting Standard 36, to conduct asset impairment tests. The results of these tests may have an impact on TAURON Capital Group's financial results in the subsequent reporting periods.

Internal factors:

1) steadfast implementation of the Strategy and achieving the assumed financial and non-financial effects,
2) actions with respect to optimizing processes taken by all of TAURON Capital Group's subsidiaries,
3) decisions with respect to the implementation of the key investment projects,
4) geological and mining conditions of hard coal extraction,
5) potential failures of TAURON Capital Group's equipment, installations and grids.

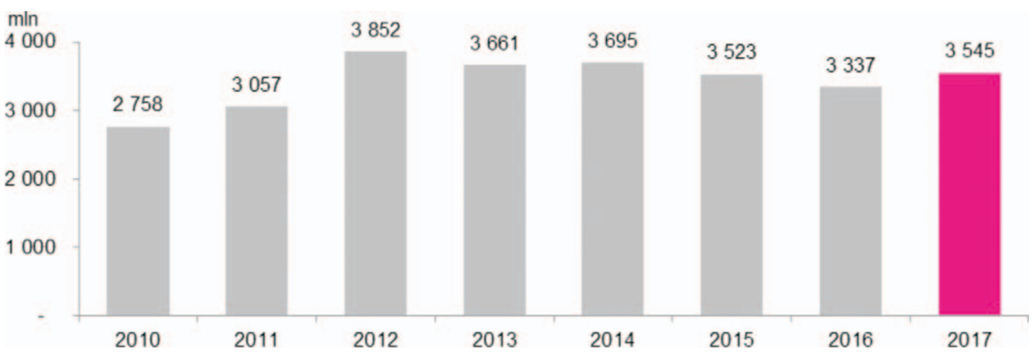
TAURON Capital Group's operations are characterized by seasonality which is applicable, in particular, to heat production, distribution and supply, electricity distribution and supply to individual consumers and hard coal sales to individual consumers for heating purposes. Heat sales depend on weather conditions, in particular, on air temperature, and are higher in the autumn and winter season. Volume of electricity supply to individual consumers depends on the length of day which usually makes electricity supply to this group of consumers lower in the spring and summer season and higher in the autumn and winter season. Hard coal sales to individual consumers is higher in the autumn and winter season. Seasonality of TAURON Capital Group's other lines of business is low.

The impact of the above factors on the financial results achieved in 2017 is described in section 2.3 and in section 4 of this report. The effects of this impact are visible both in the short term, as well as in the long term.

2.3. TAURON Capital Group's financial results

The below figure presents TAURON Capital Group's 2010–2017 EBITDA.

Figure no. 25. TAURON Capital Group's 2010–2017 EBITDA



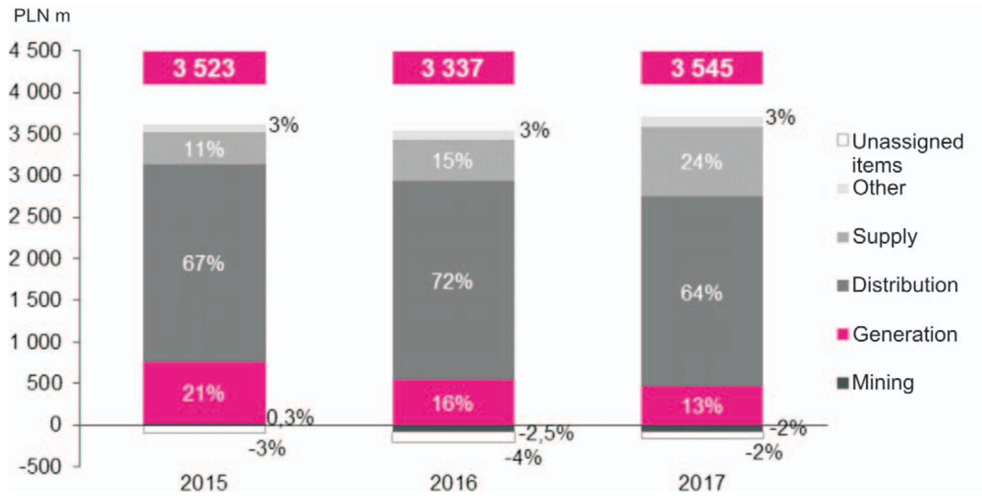
The below table presents TAURON Capital Group's 2015–2017 EBITDA broken down into individual lines of business (segments). Data for the individual segments do not include consolidation exclusions.

Table no. 10. TAURON Capital Group's 2015–2017 EBITDA broken down into individual lines of business (segments)

No.	EBITDA (PLN thous.)	2017	2016	2015	Change in % (2017/2016)	Change (2017–2016)
1.	Mining	(83 036)	(82 130)	9 137	–	(906)
2.	Generation	463 974	545 311	754 751	85%	(81 337)
3.	Distribution	2 282 685	2 394 812	2 372 129	95%	(112 127)
4.	Supply	841 222	490 005	380 405	172%	351 217
5.	Other	118 043	114 570	100 320	103%	3 473
6.	*Unassigned items*	*(78 297)*	*(125 754)*	*(93 514)*	–	*47 457*
	Total EBITDA	**3 544 591**	**3 336 814**	**3 523 228**	**106%**	**207 777**

The below figure presents TAURON Capital Group's 2015–2017 EBITDA structure (composition).

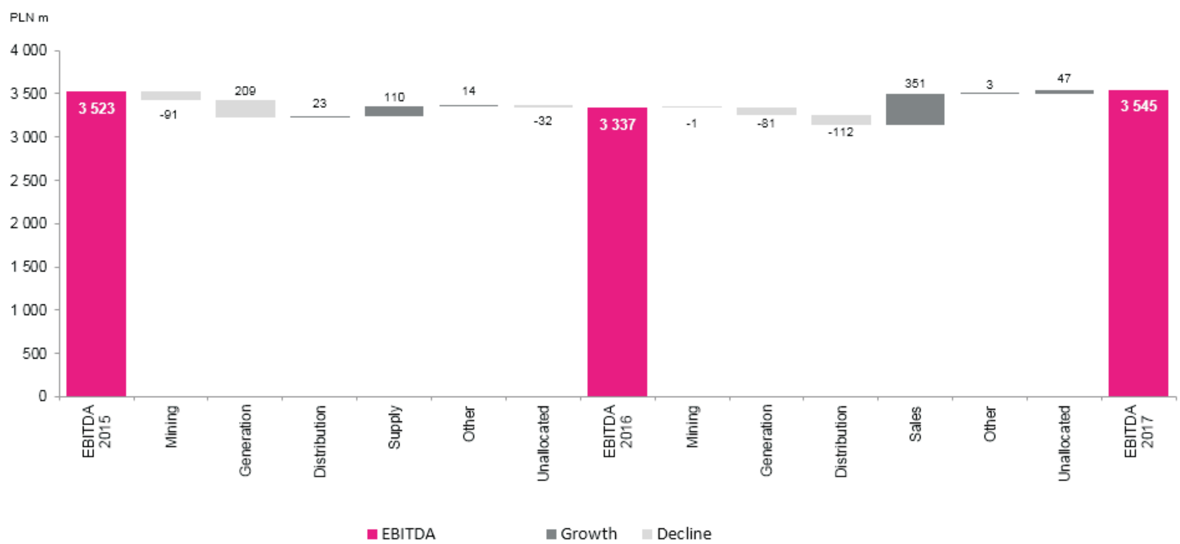
Figure no. 26. TAURON Capital Group's 2015–2017 EBITDA structure (composition)



Distribution, Generation and Supply Segments have the biggest contributions to TAURON Capital Group's EBITDA.

The below figure presents the change in TAURON Capital Group's EBITDA in 2015–2017.

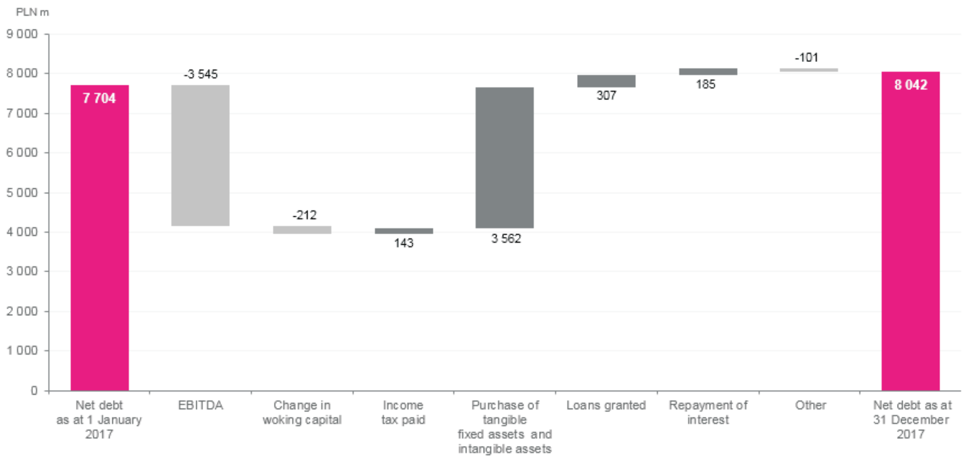
Figure no. 27. Change in TAURON Capital Group's EBITDA in 2015–2017



TAURON Capital Group's 2017 cash flows

The below figure presents TAURON Capital Group's 2017 cash flows.

Figure no. 28. TAURON Capital Group's 2017 cash flows



2.3.1. Mining Segment

The below table presents the Mining Segment's 2015–2017 results.

Table no. 11. Mining Segment's 2015–2017 results

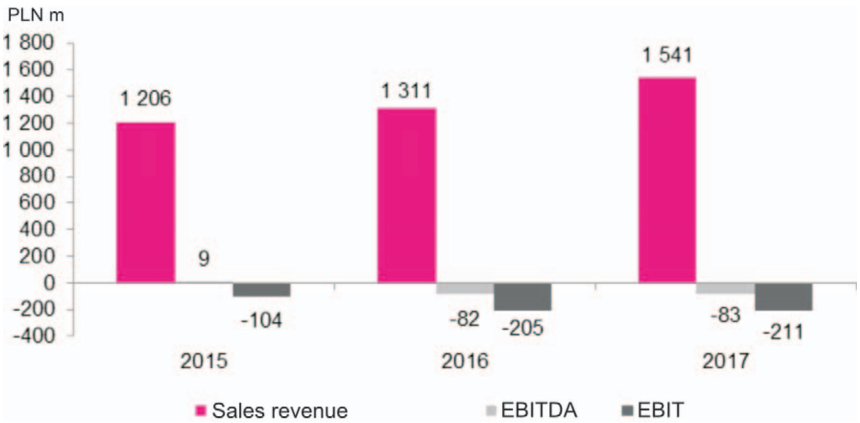
Item (PLN thous.)	2017	2016	2015	Change in % (2017/2016)	Change (2017–2016)
Mining					
Sales revenue	**1 541 425**	**1 311 143**	**1 205 944**	**117.6%**	**230 282**
coal – coarse and medium assortments	*509 348*	*346 251*	*346 778*	*147.1%*	*163 097*
thermal coal	*973 549*	*918 647*	*836 772*	*106.0%*	*54 902*
other revenue	*58 528*	*46 245*	*22 394*	*126.6%*	*12 283*
Operating profit	**(211 070)**	**(205 163)**	**(104 328)**	**–**	**(5 907)**
Depreciation and write-downs	128 034	123 033	113 465	104.1%	5 001
EBITDA	**(83 036)**	**(82 130)**	**9 137**	**–**	**(906)**

Mining Segment's 2017 operating results, EBIT and EBITDA, were at a similar level as the 2016 earnings. This segment's financial results were impacted by the following factors:

1) higher sales volumes of each product assortment by 12% on average,
2) higher average price of products sold by 6.7%,
3) higher unit commercial coal production unit cost due to higher mining services costs, labor costs as a consequence of paying out a one-off bonus, consuming a larger quantity of coal purchased for processing on the market in 2017 and achieving commercial coal production volume slightly higher than in 2016,
4) selling a substantial portion of coal inventory in 2017, which resulted in recognising the coal inventory value as own cost in this period. The coal sales surplus over the realized coal production reached 323 thousand Mg in the reporting period. In the same period of 2016 the situation was opposite and some unsold production (304 thou. Mg) was inventoried and sold in the subsequent periods.

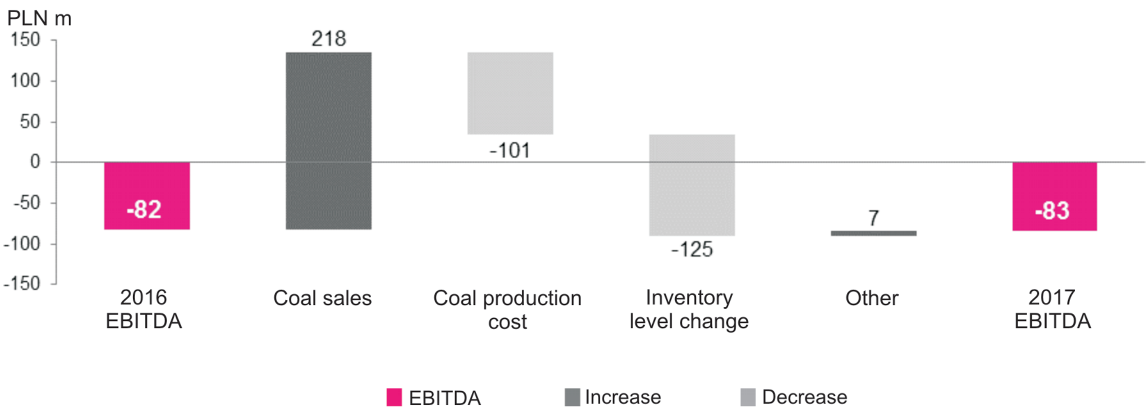
The below figure presents the Mining Segment's 2015–2017 financial data.

Figure no. 29. Mining Segment's 2015–2017 financial data



The below figure presents the Mining Segment's EBITDA, including the material factors affecting the year on year change.

Figure no. 30. Mining Segment's EBITDA



Strategic goals and initiatives

The main goal of the Mining Segment defined in the Strategy is: stable supply of cost competitive and appropriate quality fuel to TAURON Capital Group, as well as development of the product offering and maximizing the margin generated on the sales of the other products.

The goals set out in the Strategy are to be accomplished by implementing the strategic initiatives that include, inter alia: optimizing the costs and capital expenditures, tri-product enrichment at Sobieski Coal Mine and Janina Coal Mine as well as an extension of the line for packaging eco-pea coal.

Major investments

In 2017 the Mining Segment's total capital expenditure reached approximately PLN 166 million, including the following strategic investment projects:

1) PLN 13 PLN m on the construction of the "Grzegorz" shaft, including the construction of the infrastructure and the accompanying headings,
2) PLN 41 mln on the construction of a 800 m level at Janina Coal Mine,
3) PLN 38 PLN m on Brzeszcze Coal Mine's capex program.

Mining Segment's other capital expenditures are spent on coal extraction preparations and operations (mainly the purchase of machines and equipment, drilling of headings, longwall preparation).

Growth outlook

The current situation of the hard coal mining industry in Poland, including the integration of Polska Grupa Górnicza's assets, the logistics problems and the impact of the geological problems brought about the decline of coal extraction output which led to the low coal inventory levels of the coal mines' stock piles and an increase of the commodity's price. The analysts are forecasting stable demand for coal in 2018 which, with low coal extraction output, may lead to an increase of the coal price on the market and as a consequence a potential rise of electricity prices. In 2017 thermal coal prices rose 8% with the main reason being the low supply due to the price declines in 2014–2016 and thus reducing the capex during that period. The low coal supply on the local market may lead to increased coal imports which will also impact the price level. The upcoming period will be difficult and demanding also due to an unfavorable outlook for this fuel in the EU's energy policy.

The challenges for this line of business will include: the evolution of Poland's fuel and energy policy, development directions indicated in the "Program for the hard coal mining sector in Poland", published in January 2018, and also the ordinance on the quality of fuels.

The Strategy assumes that the planned strategic initiatives and the investment projects underway will enable TAURON Capital Group's Mining Segment to strengthen its position and provide coal fuel to TAURON Capital Group's subsidiaries, thus mitigating the risk of the rising prices of this commodity on the external market.

In accordance with the Strategy the main directions of actions to be taken by the Mining Segment include:

1) continuation of the investment projects at Janina Coal Mine and Sobieski Coal Mine,
2) implementation of the capex program at Brzeszcze Coal Mine,
3) optimizing the costs and expenditures in order to maintain TAURON Wydobycie's position as the second most cost-effective coal producer in Poland (following Lubelski Węgiel "Bogdanka" S.A.'s coal mine)",
4) construction of the portfolio of products aligned to internal needs, including the provision of coal supplies for the generation units of TAURON Capital Group at a level of 70–80% of demand;
5) developing a product offering for the customers outside TAURON Capital Group.

The investment projects implemented by TAURON Capital Group in the Mining Segment are aimed at increasing the productivity and lifting the share of coal from own mines in the structure of TAURON Capital Group's purchasing. The effects of actions aimed at improving the efficiency of this segment will be reflected in its financial and operating results in the subsequent periods.

2.3.2. Generation Segment

The below table presents the Generation Segment's 2015–2017 results.

Table no. 12. Generation Segment's 2015–2017 results

Item (PLN thous.)	2017	2016	2015	Change in % (2017/2016)	Change (2017–2016)
Generation					
Sales revenue	**4 528 480**	**4 356 101**	**5 376 280**	**104.0%**	**172 379**
electricity	*3 486 458*	*3 101 505*	*4 021 274*	*112.4%*	*384 953*
heat	*873 929*	*861 029*	*814 045*	*101.5%*	*12 900*
property rights arising from certificates of electricity origin	*114 840*	*335 673*	*480 698*	*34.2%*	*(220 833)*
other revenue	*53 253*	*57 894*	*60 263*	*92.0%*	*(4 641)*
Operating profit	**16 595**	**(752 813)**	**(3 477 076)**	**–**	**769 408**
Depreciation and write-downs	447 379	1 298 124	4 231 827	34.5%	(850 745)
EBITDA	**463 974**	**545 311**	**754 751**	**85.1%**	**(81 337)**

In 2017 the Generation Segment's sales revenue was higher by 4% as compared to 2016 due to higher electricity and heat sales revenue (mainly due to higher sales volumes). Lower revenue from the sales of property rights to the certificates of origin of electricity are the result of the lower sales volume and lower price of PMOZE.

The following factors impacted the results achieved:

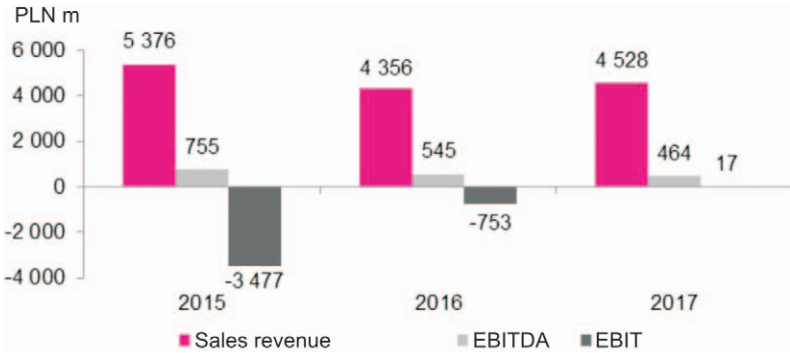
1) lower margin on electricity – mainly due to the lower electricity sales price year on year,
2) lower price and lower sales volume of the RES related property rights – the result of PMOZE oversupply on the market and the reduction of the biomass fired units' production,

3) higher margin on heat – higher heat sales and transmission services volume (the effect of the lower external temperature in the heating season (4.0°C in 2016, 3.6°C in 2017) and a higher rate for the transmission services,
4) lower costs of the CO_2 provision – which is the result of: a larger number of free emission allowances, higher CO_2 emission volume (the result of higher electricity and heat production) and lower prices of forward CO_2 contracting year on year,
5) other – mainly higher costs of the real estate tax on wind farms, the costs of one-off bonuses for the workforce, higher costs of the provision for the Voluntary Redundancy, larger scope of ongoing maintenance and higher costs of electricity related infrastructure damage.

In the year ended on December 31, 2017 TAURON Capital Group booked impairment charges and the dissolving of the previously set up provisions related to the tangible fixed assets as a result of impairment tests for assets conducted as of December 31, 2017 and June 30, 2017. The results of the tests completed proved that for some assets of the Generation Segment an additional write-down in the amount of PLN 658.7 mln should be booked. The tests completed also demonstrated that the reversal of impairment charges in this Segment for the amount of PLN 628.2 mln is justified.

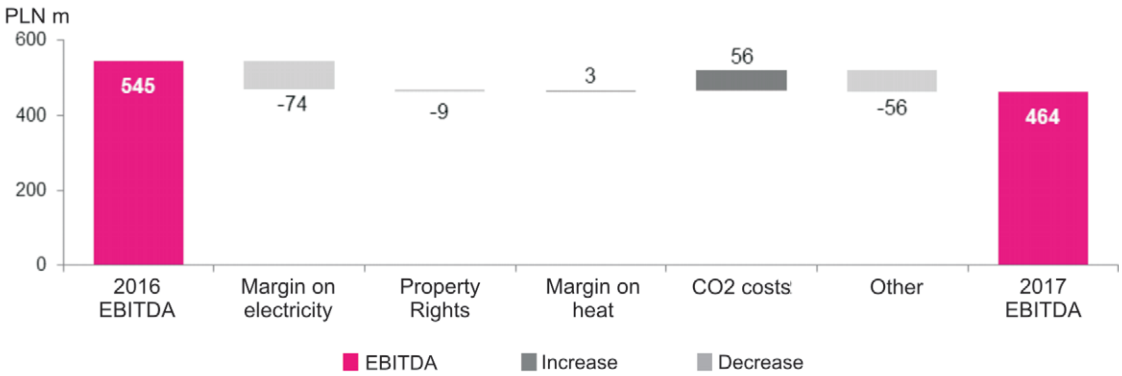
The below figure presents the Generation Segment's 2015–2017 financial data.

Figure no. 31. Generation Segment's 2015–2017 financial data



The below figure presents the Generation Segment's EBITDA, including the material factors impacting the change year on year.

Figure no. 32. Generation Segment's EBITDA



Strategic goals and initiatives

The main goals of the Generation Segment defined in the Strategy include:

1) for TAURON Wytwarzanie subsidiary: halting the decline of the assets' value and modernizing the generation fleet,
2) for TAURON EKOENERGIA subsidiary: raising the profitability of the generation assets held and developing options for a profitable expansion of the line of business,
3) for TAURON Ciepło subsidiary: expanding heat sales and distribution.

The goals set out in the Strategy are to be accomplished by implementing the strategic initiatives that include, inter alia: optimizing the costs and capital expenditures, optimizing employment, optimizing the production assets and selling the redundant non-production assets as well as the investment projects leading to the upgrading of the generation (910 MW unit at Jaworzno Power Plant, 450 MW unit at Stalowa Wola Combined Heat and Power Plant).

The main strategic direction set for the Generation Segment's conventional assets is to achieve economic efficiency pr permanent decommissioning (retirement) from operation. The actions taken in this line of business will focus on, among others, completing the construction of the 910 MW hard coal-fired unit at Jaworzno Power Plant, including the project's implementation jointly with a strategic partner as a result of selling some shares while retaining the controlling stake. The general direction concept related to adapting TAURON Capital Group's generating units to the BAT conclusions will be developed in 2018. The analytical works should provide a recommendation for the best action scenario, i.e. the scope of upgrading (adapting) generating units including the required outlays or the possibilities for potentially obtaining derogations with respect to the limit emission values.

With respect to RES, options are being prepared for expanding RES installations assuming a favorable support system is put in place and a profitable model for the operation thereof is developed.

With respect to the heat generation, distribution and trading, material actions include an expansion of the heat generation, distribution and trading, and in particular the implementation of the Low Emission Liquidation Program, seeking solutions in the multi-fuel co-generation area and increasing the level of utilizing the existing infrastructure.

Major investments

In 2017 the Generation Segment's total capital expenditure reached PLN 1 516 million, including the following strategic investment projects:

1) PLN 1 278 mln on the construction of the coal-fired 910 MW unit at Jaworzno III Power Plant,
2) PLN 16 mln on investment projects related to expanding and maintaining the district heating networks,
3) PLN 17 mln on connecting new facilities.

Moreover, approx. PLN 77 million was spent on replacements and repairs (maintenance) by TAURON Wytwarzanie. Apart from the above capex an investment project in Stalowa Wola with the participation of the strategic partner, PGNiG, is underway. TAURON and PGNiG hold a 50% stake each in the special purpose vehicle implementing the project that includes the construction of the 449 MW_e CCGT unit, including the 240 MW_t heat generation component. In January 2016, the contract with the general contractor Abener Energia S.A was terminated. In March 2017, thanks to the repayment of the existing institutions financing the project, the signed amendments to the gas and electricity agreements as well as the agreement on the project's restructuring came into force. The agreement was reached and the decision was taken on the construction of the backup heat source. Talks with the financing institutions on obtaining new, more favorable financing are being finalized. As a result of completing a number of analyses, among others due to the project's advancement level the contract manager formula (EPCM) was chosen. Energopomiar Gliwice – Energoprojekt Katowice consortium was selected to implement the EPCM project. The project's completion is scheduled for 2019. Expected capital expenditures on the project (excluding the financial costs) are to reach approx. PLN 411 mln (with approx. PLN 165 mln planned to be spent in 2018). PLN 984 mln had been spent by the end of 2017.

Growth outlook

The available forecasts and analyses for the upcoming year assume an increase of domestic electricity production, including also production from RES and rising wholesale market contract prices of: electricity, certificates and EUAs. In the near future the generation sector will also have to deal with an unfavorable situation on the labor market. Due to the noticeable generational gap problem there is a shortage of specialists on the market which impacts the operations of electricity and heat producers.

Analysts are forecasting an increase of RES generation capacity and its key role in electricity production on the market (mainly wind farms), which poses a challenge for the gird and the stability of electricity supply. A strong interest in the RES line of business, supported by the EU policy, may have an impact on investments, including acquisition opportunities in the RES segment.

A growing share of intermittent generation sources and decreasing volumes of production from the conventional generating units (due to, inter alia, age and low efficiency) have a significant impact on Poland's security of electricity supply. In the coming years the key issue will continue to be ensuring the security of the operation of KSE, this why the capacity market was introduced in Poland which should allow for obtaining an additional revenue source for the generating units for the required capex and asset refurbishments.

On the heat market Poland's policy, aimed at improving the air quality, may lead to a material increase of investments and an expansion of this line of business.

2.3.3. Distribution Segment

The below table presents the Distribution Segment's 2015–2017 results.

Table no. 13. Distribution Segment's 2015–2017 results

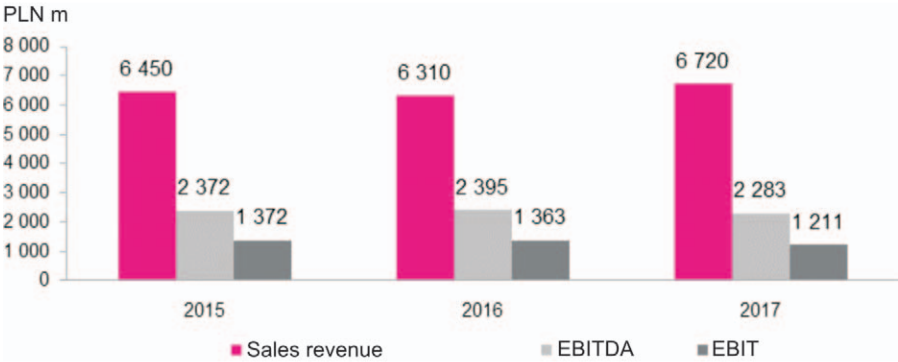
Item (PLN thous.)	2017	2016	2015	Change in % (2017/2016)	Change (2017–2016)
Distribution					
Sales revenue	**6 719 943**	**6 310 216**	**6 450 274**	**106.5%**	**409 727**
distribution services	*6 311 594*	*5 892 510*	*6 022 144*	*107.1%*	*419 084*
connection fees	*114 112*	*103 636*	*125 698*	*110.1%*	*10 476*
maintenance of street lighting	*115 265*	*116 462*	*116 042*	*99.0%*	*(1 197)*
other revenue	*178 972*	*197 608*	*186 389*	*90.6%*	*(18 636)*
Operating profit	**1 210 925**	**1 363 236**	**1 371 577**	**88.8%**	**(152 311)**
Depreciation and write-downs	1 071 760	1 031 576	1 000 552	103.9%	40 184
EBITDA	**2 282 685**	**2 394 812**	**2 372 129**	**95.3%**	**(112 127)**

In 2017, as compared to 2016, the Distribution Segment reported a 6.5% revenue increase and a change of results on the EBIT and EBITDA level by (11,2)% and (4,7)%, respectively. The following reasons impacted the results:

1) increase of the average rate of the distribution service sales to the final consumers in each tariff group, mainly as a result of an increase of the transition fee and RES fee rates,
2) rising supplies to consumers in each group, in particular, among consumers in A and B groups, as a result of favorable economic conditions, rising production, and reducing own generation,
3) rising transmission services purchase costs as a result of a higher transition fee and the RES fee (not existing in 2016),
4) declining costs of purchasing electricity to cover the balancing difference achieved due to the reduction of the purchase volume,
5) lower grid losses indicator year on year as recorded in the books, among others due to conducting the "Program of actions aimed at reducing electricity losses",
6) increase of revenue from fees for above-standard passive energy off-take where the main parameter of the positive deviation versus last year is an increase of the electricity price on the competitive market,
7) drop of the revenue due to fixing collisions, mainly as a result of shifting the performance of tasks to 2018,
8) incurring costs due to the implementation of the Grid Reliability Improvement Program in 2017 and the costs of the one-off bonus,
9) actuarial provision – a one-off event in December 2016 involving dissolving of the actuarial provision associated with the harmonisation of the Company Collective Bargaining Agreement in the companies of the Distribution Segment,
10) increase of the costs of taxes and fees as a result of the investment projects underway, rising value of the grid assets and the higher provision due to the easement of the transmission lines located on the territory of the State Forest Company (Lasy Państwowe).

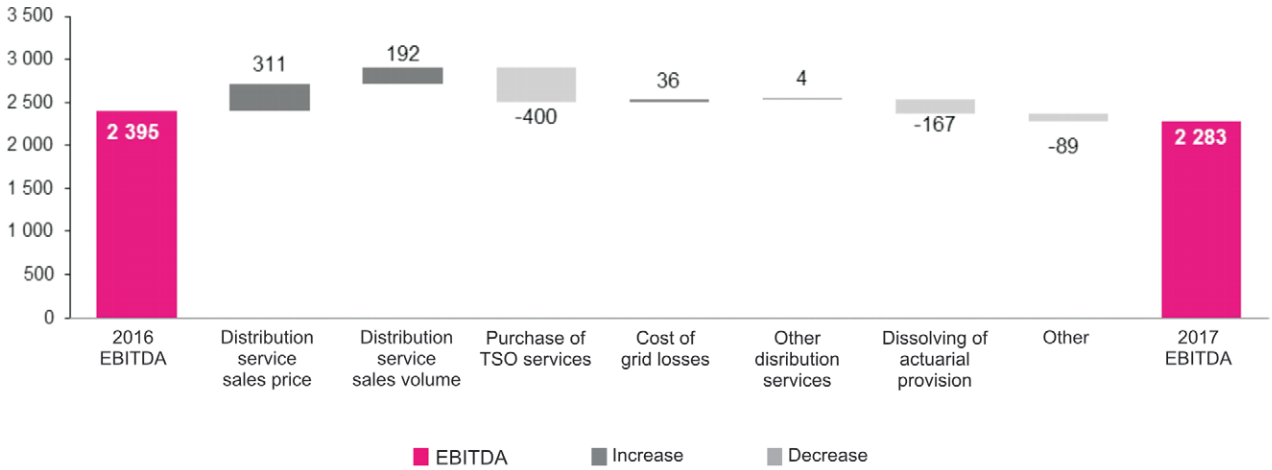
The below figure presents the Distribution Segment's 2015–2017 financial data.

Figure no. 33. Distribution Segment's 2015–2017 financial data



The below figure presents the Distribution Segment's EBITDA, including the material factors impacting the year on year change.

Figure no. 34. Distribution Segment's EBITDA



Strategic goals and initiatives

The main goal of the Distribution Segment defined in the Strategy is to maintain the leading position on the Polish market in terms of the security and efficiency of the grid's operation.

The assumed goal is to be accomplished by implementing the strategic initiatives: "Single Distribution" program comprising projects optimizing the operational processes in the company; actions leading to the improvement of customer satisfaction and simultaneously the improvement of the company's image; electrical mobility program and storage systems. The Distribution Segment is implementing material investment projects related to the upgrading and replacing of the grid.

Major investments

In 2017 the Distribution Segment's total capital expenditures reached PLN 1 693 million. The main capex directions of investment included:

1) PLN 610 mln on investments related to connecting new consumers
2) PLN 865 mln on investments related to the upgrading and replacing of the grid

Moreover, in 2017 expenditures were spent on implementing the following Strategic Investment Projects: *The Grid Assets Management System (*approx. PLN 16 million), *The Construction of the Grid Management Centre in Kraków* (approx. 31 million). Expenditures in the total amount of approx PLN 150 million were also spent on: communications and IT, buildings and structures, means of transportation, modernisation of street lighting.

Growth outlook

The Distribution Segment must align its capex to URE's requirements related to the quality based regulation. Actions oriented towards ensuring the reliability of electricity supply and simplifying the procedures related to connecting new consumers will be continued. The investment projects implemented must allow for adapting the company's distribution assets to the growing volume of electricity generated by the renewable sources, and also for preparing the grid to interwork with the infrastructure for charging electric vehicles. The company's expansion in terms of smart grids and meters will allow for introducing additional functionalities, both on the distributor's as well as the customer's side. The segment's expansion will be significantly impacted by the competences with respect to obtaining aid funds, both for improving the security, as well as the conducted research and development works.

It should be noted that these challenges will be dealt with on the regulated market which makes the Segment's actions dependent on the new elements of the DSO regulatory policy introduced by the President of URE and the risks associated therewith, i.e. an updated approach to the weighted average cost of capital, the companies' efficiency improvement correction factors with respect to the operating expenses and the balancing differences level, continuing the quality based regulation. A significant change for the Segment is the introduction of the so-called anti-smog tariff. President of URE approved TAURON Dystrybucja's new tariff in force until December 31, 2018. The tariff change involves setting up a separate tariff group, with a reduced rate for the consumers consuming electricity for household needs in order to stimulate such consumers to consume greater volume of electricity at night, i.e. from 22^{00} to 6^{00}.

2.3.4. Supply Segment

The below table presents the Supply Segment's 2015–2017 results.

Table no. 14. Supply Segment's 2015–2017 results

Item (PLN thous.)	2017	2016	2015	Change in % (2017/2016)	Change (2017–2016)
Supply					
Sales revenue	**13 567 887**	**14 016 190**	**15 873 355**	**96.8%**	**(448 303)**
electricity, including	*8 740 196*	*8 814 692*	*10 357 041*	*99.2%*	*(74 496)*
revenue from retail sales of electricity	*7 554 291*	*7 145 644*	*8 111 002*	*105.7%*	*408 647*
greenhouse gas emission allowances	*336 566*	*363 500*	*94 086*	*92.6%*	*(26 934)*
fuel	*1 024 912*	*1 583 672*	*1 972 403*	*64.7%*	*(558 759)*
distribution service (transferred)	*3 400 487*	*3 183 232*	*3 377 473*	*106.8%*	*217 255*
other revenue, including commercial services	*65 725*	*71 094*	*72 353*	*92.4%*	*(5 369)*
Operating profit	**832 216**	**479 374**	**369 529**	**173.6%**	**352 842**
Depreciation and write-downs	9 006	10 631	10 876	84.7%	(1 625)
EBITDA	**841 222**	**490 005**	**380 405**	**171.1%**	**351 217**

Sales revenue was 3.2% lower In 2017 versus 2016, mainly due to the decline of fuel and electricity sales. The lower electricity sales revenue is due to the lower wholesale electricity sales as a result of lower electricity sales volume (by 2.1 TWh), while revenue from retail electricity sales went up by 5.7% due to a rise in the sales volume (by 2.9 TWh). The result of the higher retail sales volume is a higher distribution service sales revenue. Fuel sales revenue decline is due to a change of the coal supply organization model and lower natural gas sales revenue (lower sales volume).

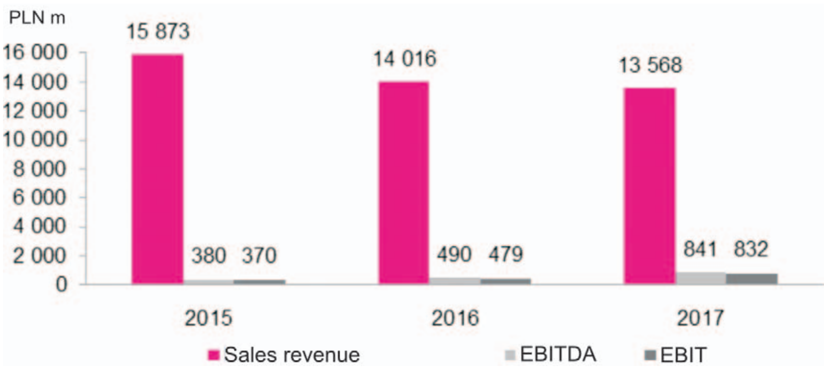
2017 EBIT and EBITDA were higher than in 2016 due, among others, to dissolving of the ECSW related provision and the termination of the long term PMOZE purchase contracts in H1 2017. The results were mainly affected by the following factors:

1) Electricity volume and prices – a negative impact on the result is due to the lower electricity sales price with retail electricity sales volume rising at the same time. The stronger sales price decline rate versus the purchase price decline rate is due, among others, to the falling sales prices to business customers because of lower PMOZE market prices. The sales prices drop was also affected by the reduction of the G tariff at TAURON Sprzedaż by 5% year on year.
2) Property rights prices – a positive impact on the result due to taking advantage of the favorable market situation, mainly related to the "green" certificates (purchase of PMOZE at lower prices) and a change of the regulations related to the calculation of the property rights related to energy efficiency at the same time,
3) Property rights redemption obligation – a negative impact on the result due to an increase of the obligation level year on year: for PMOZE in H1 2017 from 15.00% to 15.40% and in H2 2017 from 14.35% to 15.40%, for PMMET from 1.5% to 1.8%, for PMGM from 6.00% to 7.00% and the introduction of the obligation for PMOZE-BIO in H1 2017: 0.60% (in H1 2016 there was no such obligation), and in H2 2017: a change from 0.65% to 0.60%,

4) Dissolving of the provision for the agreements related to the joint venture (ECSW) led to an improvement of the Supply Segment's result by PLN 203 mln due to the coming into force of the Agreement concluded between TAURON i PGNiG on the gas and electricity agreement and the amendments to the long term gas and electricity sale agreements related to the CCGT unit construction project at Stalowa Wola,
5) Other commercial products – margins reached on the other commercial products (primarily the declining margin on the natural gas sales due to the lower sales volume),
6) Other – higher result on the other operations recorded and higher costs of sales.

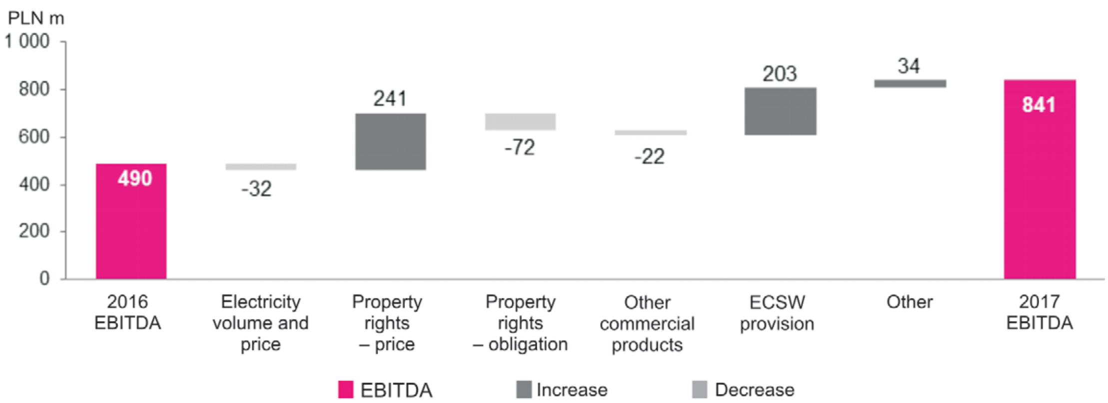
The below figure presents the Supply Segment's 2015–2017 financial data.

Figure no. 35. Supply Segment's 2015–2017 financial data



The below figure presents the Supply Segment's EBITDA, including the material factors impacting the year on year change.

Figure no. 36. Supply Segment's EBITDA



Strategic goals and initiatives

The main goal for the Supply Segment defined in the Strategy is: to achieve the leading position customer relationships based on high quality of service and product leadership.

The goals set in the Strategy are to accomplished by implementing the strategic initiatives, including, inter alia: increasing the sales potential by transforming service channels into integrated customer contact channels focused on sales and product advice, increasing the value of product and service sales to mass customers by developing the product offering and sales techniques, developing products and building communication channels for specialized products and the partnership offering addressed to the mass customer segment, as well as to the business customers, strengthening of expansion and optimizing the sales margins in the business segments.

Major investments

The Supply Segment's total capital expenditures reached PLN 1 million in 2017.

Growth outlook

Growing competition in the electricity supply segment as well as the demanding situation on the wholesale electricity market leads to the decline of sales volumes and margin erosion. Actions taken by the competition and rising customer expectations are impacting product offering development and maintaining of the highest customer service standards. Growing customer awareness leads to increased requirements, both in terms of the products offered, as well as the customer service speed and quality. TAURON Capital Group is systematically expanding its product offering in this respect, aligning it to the individual and business customers, and it is expanding communications channels, both with respect to digital platforms as well as direct contacts. The upgrading and expanding of the traditional customer service network meets the expectations of that part of the public that is not ready for IT based electronic solutions.

TAURON's competitors are also offering a broad range of products on the market that are often very similar (photovoltaics, air conditioning, professional (handyman), etc.). With price offerings at a similar level customer competition will take place at the level of innovative product and service proposals, win particular with respect to customer communications platforms and customer service quality.

2.3.5. Other operations

The below table presents the Other Operations Segment's 2015–2017 results.

Table no. 15. Other Operations Segment's 2015–2017 results

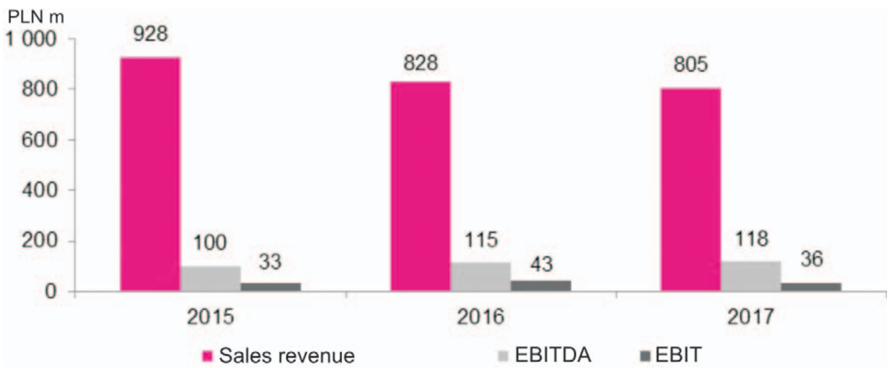
Item (PLN thous.)	2017	2016	2015	Change in % (2017/2016)	Change (2017–2016)
Other					
Sales revenue	**804 560**	**827 928**	**927 953**	**97,2%**	**(23 368)**
customer service, accounting and IT services	*544 860*	*558 046*	*581 050*	*97,6%*	*(13 186)*
electricity and property rights arising from certificates of electricity origin	*15 013*	*12 827*	*73 927*	*117,0%*	*2 186*
biomass	*74 248*	*111 087*	*171 326*	*66,8%*	*(36 839)*
aggregates	*101 343*	*90 491*	*89 102*	*112,0%*	*10 852*
other revenue	*69 096*	*55 477*	*12 548*	*124,5%*	*13 619*
Operating profit	**35 902**	**42 642**	**32 596**	**84,2%**	**(6 740)**
Depreciation and write-downs	82 141	71 928	67 724	114,2%	10 213
EBITDA	**118 043**	**114 570**	**100 320**	**103,0%**	**3 473**

The Other Operations Segment's revenue was approx. 3% lower in 2017 versus 2016 and the main reasons should be attributed to the loss of biomass sales revenue.

The biggest contribution to this segment's results comes from the customer service, accounting and IT services representing 79% of the segment's EBITDA, 20% margin on aggregates represents 20%, support services provided for TAURON Capital Group's subsidiaries represent 4% and 1% is the margin on biomass. This segment's result is also affected by the negative margin on electricity and property rights sales.

The below figure presents the Other Operations Segment companies' 2015–2017 financial data.

Figure no. 37. Other Operations Segment companies' 2015–2017 financial data



Major investments

The Other Operations Segment companies' total capital expenditures reached PLN 98 million. They include mainly expenditures on the IT systems.

Growth outlook

The Other Operations Segment companies' cost efficiency has a direct impact of the competitiveness of the Segments for which they are providing their services. The operations with respect to customer service, and in particular professional and efficient customer service, as well as tailoring of the IT tools to the business needs, developing both the traditional, as well as electronic customer service channels will have a material impact on the expansion of the Supply and Distribution Segments.

The current market trends clearly show customer service migrating to the alternative channels, aligned with the growing customer expectations and diversity. It is necessary to take actions related to stationary (in person) customer service as well to expand telephone and electronic customer service channels. The efficiency, quality and innovations included in the solutions offered will to a large degree impact on the earnings of the entire TAURON Capital Group.

2.4. What can be expected in 2018

2017 was the year of growth, both for the world economy, as well as for the Polish economy. According to the World Bank's forecasts the world economy will accelerate in 2018 even more than in 2017, and the estimated 2018 GDP growth rate worldwide will reach 3.1%.

With respect to the Polish economy analysts are predicting the 2018 GDP growth rate to continue at the level of approx. 4%[1], the unemployment rate to drop to approx. 6% and the inflation to increase (the annual average inflation rate at the level of approx. 2.3%)[2]. Poland's economy growth rate is to a large extent determined by internall consumption, however foreign investment is also the key factor. Investors TFI and BZ WBK analysts are expecting strong consumption (impacted, among others, by the declining unemployment and rising wages) in 2018, and also investments to increase, including private sector investments. Good economic situation in the eurozone will provide a strong support for the expansion of the Polish manufacturing industry and fuel Poland's exports.

Poland's power sector can expect big challenges related to the industry regulations in 2018. The detailed capacity market regulations (ordinances, regulations) as well as the first certification process and, as a consequence, the first auctions. This will allow for developing detailed plans with respect to the future of many generating units in Poland.

In 2018, in accordance with the public announcements, works on Poland's fuel and energy policy that will set the long term expansion (growth) directions and also works on the new support system for the cogeneration will be conducted. Also, probably the decision on the future of the nuclear energy in Poland will be taken. The above material issues will impact the developing of the detailed expansion (growth) directions for Poland's energy sector. The construction of the Baltic Pipe gas pipeline, with respect to which the final investment decision should be taken by the end of the year, while the completion of its construction is expected at the end of 2022, will have a real impact on the situation of Poland's energy sector and energy security.

For KSE 2018 will be the year of commissioning or launching the full operation in the system of new conventional units with the total capacity of more than 3 GW. Also, numerous projects implemented based on the first RES auction should be commissioned (the volume contracted for 2018 reached close to 70 GWh).

Following the 2017 acquisitions on the power market (the acquisition of EDF assets by PGE Group and ENGIE assets by ENEA Group) these assets will be integrated and the impact of this concentration on the market will be visible, first of all in the generation segment.

The capacity market, and also RES auctions, should stimulate appetite for investments in new capacity. On the other hand, in case of the distribution grids the rising umber of dispersed RES sources and microinstallations pose challenges in terms of ensuring the reliability of electricity supplies which will require capital expenditures on grid upgrades and replacements.

As consumption is rising the domestic electricity production is expected to increase, including electricity generated from RES. Wholesale coal prices and EUA prices can be expected to rise, and, as a consequence, also electricity and property rights prices.

[1] *2018 GDP growth rate forecasts: World Bank 4%, OECD 3,5%, government's budget assumptions 3.8%, European Commission 4.2%, NBP 4%.*

[2] *NBP's forecasts.*

2.5. Core products, goods and services

The below table presents TAURON Capital Group's 2015–2017 production and sales volumes.

Table no. 16. 2015–2017 production and sales volumes

No.	Volumes of production and sales	Unit	2017	2016	2015	Change in % (2017/2016)
1.	Commercial coal production	*M Mg*	**6.45**	6.37	4.91	101%
2.	Net production of electric energy	*TWh*	**18.41**	16.80	18.56	110%
	including production from RES	*TWh*	**1.30**	1.32	1.63	98%
3.	Heat production	*PJ*	**12.20**	11.52	11.51	106%
4.	Distribution of electricity	*TWh*	**51.37**	49.68	49.20	103%
5.	Retail sales of electricity (in total, by Areas: Sales and Generation)	*TWh*	**34.94**	32.04	35.94	109%
6.	Number of customers – Distribution	*thou.*	**5 533**	5 474	5 418	101%

2.6. Markets and sources of supply

2.6.1. Markets

Mining Segment

The core operations of the Mining Segment is carried out by TAURON Wydobycie subsidiary and comprises extraction and production of coal offered for sale on the market in coarse, medium coal assortments and as steam coal dust as well as methane being the accompanying mineral from the Breszcze deposit. TAURON Group is operating three coal mines: Sobieski Coal Mine, Janina Coal Mine and Brzeszcze Coal Mine.

Depending on the coal assortment, coal has the following trade parameters:

1) calorific value from 19 MJ/kg to 31 MJ/kg,
2) ash content from 4.3% to 45.2%,
3) sulphur content from 0.23% to 1.68%.

Production of commercial coal in 2017 was slightly higher than in 2016 as a result of increased Brzeszcze Coal Mine's extraction capacity, favorable coal faces distribution at Janina Coal Mine in the January – September 2017 timeframe and adverse mining and geological conditions in Q4 2017.

TAURON Wydobycie conducts the sales of coal in two directions:

1) sales of fine coal and coal sludge to power plants and co-generation plants, mostly within TAURON Capital Group
2) sales of coarse, medium and small amount of fine coal assortments through the nationwide organized sales network, primarily on the domestic market.

TAURON Wydobycie is selling coal mainly in southern and central Poland, in particular in the following regions (provinces): Silesia, Małopolska, Podkarpacie, Świętokrzyskie and Lower Silesia, to enterprises and individual consumers.

In 2017 hard coal sales reached approx. 6.8 mln Mg, including 4.9 mln Mg (approx. 72%) to TAURON Capital Group's Generation Segment companies. It means a 12% increase as compared to 2016 and is due to higher coal production and higher demand for coal on the market.

Generation Segment

Generation Segment's core operations within TAURON Capital Group comprises generation of electricity and heat using:

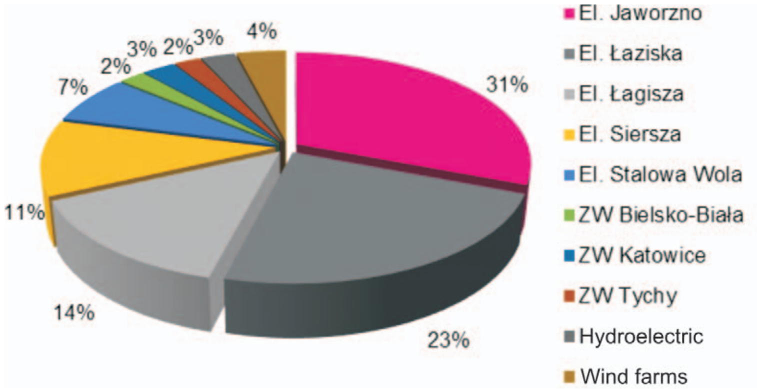
1) coal-fired and biomass burning power plants and combined heat and power plants,
2) hydroelectric power plants,
3) wind farms.

Moreover, the Generation Segment's operations include trading, distribution and transmission of heat.

The total installed electric capacity of generation units of the Generation Segment reached 5.0 GW_e of electric capacity and 2.4 GW_t of heat capacity at the end of 2017.

The below figure presents the structure of installed electric capacity of the Generation Segment as of December 31, 2017 (no material changes versus 2016).

Figure no. 38. Structure of installed electric capacity of the Generation Segment as of December 31, 2017



In 2017 the Generation Segment produced 18.4 TWh of electricity (including 1.3 TWh from RES), i.e. 10% more in relation to 2016 when the production of electricity reached 16.8 TWh (including 1.3 TWh from RES). Higher electricity production is a result of the adopted commercial (trading) strategy, taking into account the changing market conditions and favorable wind and hydrological conditions.

Sales of electricity from own production plus energy purchased for trading purposes reached 19.6 TWh in 2017, which means an increase by 26% in relation to 2016.

In 2017 the electricity produced by the Generation Segment was sold on the domestic market, first of all to TAURON Capital Group's Supply Segment (80%), as well as TGE (power exchange obligation) and to the external consumers. The share of electricity sold on the balancing market was materially lower in 2017 versus 2016.

Heat sales of the Generation Segment reached 16.4 PJ in 2017 and it was higher by 4% in relation to the corresponding period of 2016. The share of heat generated using own sources in the total heat sales reached 62% in 2017. TAURON Wytwarzanie subsidiary's power plants are selling heat in Upper Silesia and Zagłębie, and also in parts of the Podkarpackie region – Stalowa Wola and Nisko supplied by the Stalowa Wola Power Plant and Małopolska region – a part of Trzebinia supplied by the Siersza Power Plant.

Heat is sold mainly via the heat distributors: TAURON Ciepło, Spółka Ciepłowniczo-Energetyczna Jaworzno III sp. z o.o., Przedsiębiorstwo Energetyki Cieplnej Tychy and others, and on the Podkarpackie market – Przedsiębiorstwo Energetyki Cieplnej in Stalowa Wola and ENESTA. Small volumes of heat are sold directly to the consumers located in the vicinity of the generation companies.

On the other hand, TAURON Ciepło's heat sales market, mainly for heating purposes, production of hot water for domestic use, process water, includes diverse consumers: housing cooperatives and communities, private single- and multi-family houses, offices and institutions, shopping centers and industrial plants.

Moreover, due to electricity generation from RES and in co-generation, the Generation Segment acquires certificates of origin, which are subsequently purchased by the Supply Segment companies and submitted to the President of ERO for redemption.

Distribution Segment

TAURON Dystrybucja, as a utility conducting operations with respect to electricity distribution and being at the same time, pursuant to the decision of the President of ERO, a DSO, is operating under the natural monopoly conditions. The regulated market on which the company is operating includes the operations of 5 large distribution system operators that are subject to the full regulatory model. Each DSO is operating on the territory defined in the license. Following changes to the law, also more than a hundred of small distribution system operators are operating on this market serving small portions of the market, with respect to which the President of ERO is applying a simplified regulatory model. Their operations are local, based on the technical infrastructure held. One of the larger entities holding a license for distribution operations nationwide is PKP Energetyka.

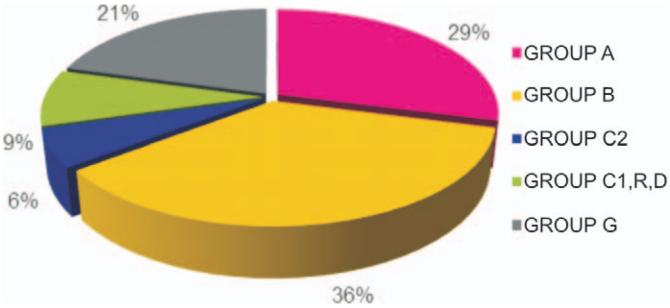
TAURON Capital Group's Distribution Segment serves approx. 5 533 thou. final consumers. It covers with its operations the area of about 57 thousand km^2, located mainly in the Lower Silesia, Małopolska, Opole and Silesia regions and, in addition, in the Łódź, Podkarpacie and Świętokrzyskie regions. The operational functions are performed by 11 branches located in: Bielsko-Biała, Będzin, Częstochowa, Gliwice, Jelenia Góra, Kraków, Legnica, Opole, Tarnów, Wałbrzych and Wrocław.

In 2017 the sales volume of electricity distribution services reached 51.37 TWh, i.e. it increased in relation to 2016 by approximately 1.69 TWh, i.e. 3.4%.

Sales to the tariff covered consumers on individual voltage levels represent 95.6%: high voltage (A group), medium voltage (B group) and low voltage (C,G,R), of the supply of the distribution services volume. The total electricity volume supplied to the tariff covered consumers connected to the TAURON Dystrybucja grid in 2017, as part of the sales of distribution services, reached 49 TWh (estimated) and it was higher as compared to 2016 by approximately 1.6 GWh, i.e. by 3.38%.

The below figure presents electricity distribution by tariff groups in 2017 (the structure in relation to 2016 did not change).

Figure no. 39. Electricity distribution by tariff groups in 2017 Distribution of electricity according to tariff groups in 2016 (MWh)



Sales of the distribution services are carried out on the basis of comprehensive agreements as well as agreements on the provision of distribution services concluded with consumers. The first type of agreement covers both electricity supply by the companies of the Supply Segment as well as the supply of this energy by the company acting as a DSO. The second type of agreement regulates only supplies of electricity by the company acting as a DSO. In case of this type of agreements, the purchase of electricity is governed by separate electricity supply agreements, concluded by a consumer with the supplier selected thereby.

The share of the distribution services sales under the comprehensive agreements in the total value of the distribution services sales to the final consumers in 2017 reached approximately 53% whereas the volume of supplies in the total volume of supplies to the final consumers reached approximately 35%.

Supply Segment

Supply Segment comprises operations with respect to the wholesale trading of electricity, natural gas and other products of the energy market as well as operations with respect to retail electricity and natural gas sales.

TAURON's wholesale trading operations comprise mainly wholesale of electricity, trading and management of CO_2 emission allowances, property rights arising from the energy certificates of origin and trading in natural gas primarily for the needs of securing the purchase and sale positions of TAURON Capital Group's entities.

The Company's operations are conducted on the wholesale markets both in Poland and abroad, also on the SPOT market and the forward market. The Company is an active participant of TGE and the OTC platform conducted by a London energy broker – Tradition Financial Services.

With respect to gas trading TAURON is expanding its presence on the foreign markets. The agreements signed by the Company with the German transmission system operators: GASCADE Gastransport and ONTRAS Gastransport GmbH as well as Czech NET4GAS s.r.o. enabling purchasing in Germany and selling on the Czech market.

TAURON is a participant of the European transmission capacity trading platform PRISMA European Capacity Platform GmbH, where it is purchasing inter-system (interconnector) transmission capacities. With respect to booking transmission capacity on the Polish market the Company is operating as a participant of the GSA GAZ-SYSTEM Aukcje auction platform. Gas trading on the Czech and Slovak markets and the inter-system (interconnector) gas exchange between Poland and the Czech Republic is performed through the TAURON Czech Energy subsidiary.

On the other hand retail sales operations, conducted by the TAURON Sprzedaż and TAURON Sprzedaż GZE subsidiaries, include electricity and gas sales to the final customers, including also the key accounts.

The Supply Segment was operating in a market environment In 2017 where the level of competitiveness in individual segments did not change significantly as compared to the previous years. In 2017 households market (individual customers) continued to be covered by the obligation to have electricity sales prices approved by the President of ERO.

According to the ERO data, from mid-2007 until December 2017, i.e. since the beginning of the liberalisation process of the energy market, approximately 547 thousand of households and approximately 199 thousand of institutional entities that switched their electricity supplier were recorded.

In the institutions and business entities (business customer) market segment, where competition is strong and companies have already been taking advantage of the liberalisation of electricity prices for several years, the progress of the liberalisation has resulted in the increasing awareness of business customers expecting competitive solutions. The enhanced sales activities of energy companies exert ever increasing price pressure. New entities competing for customers have also appeared, and the transparency of energy market mechanisms is already a necessity when operating on this market, as business customers are more and more willing to switch their supplier. The household segment is considered to offer a a strong potential as the number of supplier switchings in this segment represents a small percentage.

In 2017 over 98 thousand consumers of electricity switched their suppliers (including approximately 14 thousand institutional customers and approximately 84 thousand households). In 2017 the growth rate of changes in case of households reached 18.1%, and in case of institutional entities – 8%.

In 2017 the retail sales of electricity realized by the Supply Segment to approx. 5.4 million customers reached approx. 34.9 TWh, i.e. 109% of the 2016 level when the sales reached approx. 32.0 TWh. Increased sales volume is visible primarily in the Business Customer Segment, which is due to both acquiring new customers (e.g. Polenergia Obrót S.A., ANIMEX FOODS Spółka z o.o.), as well much higher electricity consumption by some customer already served by the Company (e.g. KGHM, Katowicki Holding Węglowy S.A., Arcellor Mittal Poland S.A. or ISD Huta Częstochowa).

The customer segmentation applied by TAURON Capital Group (strategic, business and mass customers), depending on the volume of electricity consumed, is aimed at tailoring the product offering, sales channels and marketing communications to the expectations of the specific customer segment.

The below table presents categories of TAURON Capital Group’s final customers, resulting from the market segmentation used and the specific nature of their business:

Table no. 17. Categories of TAURON Capital Group’s final customers

No.	Group of customers	Description of customers
1.	Strategic customers	Customers with the annual potential energy consumption at a level not lower than 40 GWh or strategic business partners of TAURON Capital Group, i.e. mainly entities representing the sector of heavy industry, among others: metallurgical industry, chemical industry, mining industry, automotive industry.
2.	Business customers	Customers with the annual potential energy consumption at a level above 250 MWh (other than consumers), or purchasing energy based on the provisions of the *Act of 29 January 2004 on Public procurement law*, i.e. entities representing other sectors of industry, producers of equipment, consumers from food industry, public sector, construction sector and public utilities sector.
3.	Mass customers – small and medium-sized enterprises	Customers dealing with sales, services, banking, catering and small entrepreneurs.
4.	Mass customers – households	Households.

The below table presents information on the volume of electricity sold by TAURON Capital Group’s subsidiaries operating with respect to electricity supply to customers, as well as the number of customers, broken down into individual customer segments, in 2017.

Table no. 18. Volume of retail electricity sold by the Supply Segment and the number of customers in 2017

No.	Customer type	Electricity volume sold (TWh)	Number of customers (thou.)
1.	Strategic customers	7.7	1
2.	Business customers	12.7	185
3.	Mass customers, including:	11.4	5 175
	households	*9.5*	*4 836*
4.	Sales to TAURON Dystrybucja to cover balancing differences	2.9	0.001
5.	Other (exports, own needs)	0.2	–
	Supply Segment	**34.9**	**5 361**

The process of the progressing liberalisation and the customers' rising awareness with respect to mechanisms functioning on the energy market associated therewith is reflected by the degree of loyalty in individual customer segments. This situation results in activities aimed at protecting own customer base against actions undertaken by the competition, through the introduction of loyal customer agreements. Customers from the business segment of TAURON Capital Group are most advanced in this process, where approx. 97% of the volume of the agreements concluded are the results of individually negotiated commercial terms.

In 2017 the sales offering of the TAURON Sprzedaż subsidiary for the business segment covered two media – electricity and gas fuel. Due to the customers' awareness of the energy market mechanisms and the acquired skills of using those mechanisms, TAURON Sprzedaż focused its activities on the protection of its customer base. In particular, activities oriented towards customer loyalty building were continued. It was recognised that particular emphasis would be placed building an offering that would meet customer expectations. Customers were offered a selection of a number of products taking into account their needs and the specific nature of their electricity consumption, including ecological, exchange and technical products.

While expanding the offering in the developing gas fuel sales area, the TAURON Gaz Giełda (TAURON Gas Exchange) product sales were continued, based on market prices determined in relation to quotations of TGE RTT indices. Moreover, in order to intensify electricity and gas contracting, the TAURON Multipakiet (TAURON Multipackage) product was retained in the offering, which provides simultaneous contracting of customers with respect to both media during a single round of business negotiations.

In 2017 the process of migration of mass segment customers (individual customers and small and medium-sized enterprises) from the tariff to the product area was continued. At the end of 2017 TAURON Capital Group sold electricity to approximately 38% of customers in this segment under agreements with a guarantee of commercial terms and conditions for a specific period (loyalty agreements), and 62% of customers bought energy at tariff prices.

The key element of the commercial offering for mass customers in 2017 were the combined products called Elektryk (Electrician) and Serwisant (Service Provider), based on the assistance functionality, used by over 1 million customers. As part of the sales campaigns TAURON Sprzedaż continued sales of gas to mass market customers in 2017.

These products will also constitute the basis of the offering in 2018. Furthermore, in 2017 the range of products addressed to the customers of TAURON Sprzedaż was expanded by the specialist products.

2.6.2. Supply sources – fuel

Coal (domestic market)

TAURON Capital Group purchases coal solely on the domestic market, in 2017 coal purchases were continued by TAURON for the needs of TAURON Wytwarzanie and TAURON Ciepło subsidiaries.

In 2017 the majority of TAURON Capital Group's demand for fuel to produce electricity and heat (approx. 56,5%) was satisfied with hard coal from own coal mines.

The remaining part of the demand was covered from external sources, where Polska Grupa Górnicza sp. z o.o. that took over the mines of Katowicki Holding Węglowy S.A., had the highest share (approx. 36.2% of the demand)

Gas (domestic and foreign market)

TAURON Capital Group purchases fuel gas solely on the domestic and foreign market, via exchanges. The company is an active participant of the gas market managed by TGE, carries out transactions on the SPOT market, as well as on the RTT forward market products.

The Company is also involved in the proprietary trading activity on an international gas exchange POWERNEXT Pegas. The Company is present in the hub: GASPOOL, New Connect Germany i Tittle Transfer Facility. Presence in the New

Connect Germany hub (German market) also allows for, apart from the trading activities, physical gas deliveries to the Czech Republic.

Furthermore, the Company is a participant of the Intercontinental Exchange (ICE) on the National Balancing Point (NBP) hub. It is also systematically increasing the volume of transaction concluded by the Company on the OTC market.

Operating on the gas market the Company is securing gas supplies TAURON Capital Group's entities.

2.7. Timeline

The below figure presents the timeline of selected highlights associated with the operations of TAURON Capital Group that took place in 2017.

Figure no. 40. Timeline

TAURON CAPITAL GROUP'S 2017 HIGHLIGHTS

JANUARY – FEBRUARY

- Split of TAURON Wytwarzanie by spinning off and transferring assets covering the construction of the 910 MW unit in Jaworzno to the newly formed company Nowe Jaworzno GT.
- Adoption of the *Rules of compensating members of the subsidiaries' corporate bodies.*
- Launch of a new website for customers.
- Conclusion with Banco Santander S.A. of the agreement on the provision of clearing services on EEX, EPEXSPOT, ICE, POWERNEXT with respect to processing transactions related to electricity, gas, CO_2 emission allowances and other commodity products.
- Launch by TAURON Dystrybucja of Poland's first HAN TAURON AMIplus service enabling monitoring electricity consumption in real time
- Commissioning by TAURON EKOENERGIA of a photovoltaic installation with the total system capacity of 3.36 kW.

MARCH – APRIL

- Implementation by TAURON Capital Group's subsidiaries of the process management based on the Business Model adopted in 2016
- Publishing of TAURON's and TAURON Capital Group's 2016 earnings
- Appointment of members of the Management Board of TAURON for the 5th common term.
- Selection of certified auditor.
- Launch of the TAURON Capital Group's Ambassador with its goal to build a positive image of TAURON Capital Group in the academic community and recruit top students.
- Signing by TAURON EKOENERGIA of an agrement on setting up Karkonoski Klaster Energii with Związek Gmin Karkonoskich, Karkonoskie Centrum Gospodarki Odpadami, Green Energy Power, POLTEGOR-INSTYTUT Instytut Górnictwa Odkrywkowego i Instytut Niskich Temperatur i Badań Strukturalnych.
- Adoption of *TAURON Capital Group's Corporate Responsibility Code*.

MAY – JUNE

- Conclusion by TAURON Wydobycie with a consortium of companies of the general contractor agreement on the investment project related to the stage 1 "Grzegorz" shaft construction works including the construction of the above the ground infrastructure.
- Launch of the projects qualified to the sector based "PBSE" Program as part of operation 1.2 "Sector based R+D programs".
- Publishing of TAURON's and TAURON Capital Group's Q1 2017 earnings.
- Ordinary GM of TAURON.
- Appointment of Members of TAURON's Supervisory Board for the 5th common term.
- Passing of amendments to the Company's Articles of Association by the Ordinary GM of TAURON.
- Concluding with the investment funds managed by Polski Fundusz Rozwoju S.A. of an agreement on potential cooperation in the 910 MWe unit construction project at Jaworzno III Power Plant.
- Concluding by TAURON Wytwarzanie with Polski Fundusz Rozwoju S.A. of an agreement on terminating the investment agreement between these entities on the implementation of the 413 MWe CCGT unit construction project pat Elektrownia Łagisza in Będzin.
- Intention to conduct a eurobond issue, extension of the bond issue program and establishing of the eurobond parameters.
- Commencement by TAURON Capital Group of the pilot stage for Startups as part of the Pilot Maker program.

JULY – AUGUST

- TAURON eurobond issue o with the nominal value of EUR 500 mln.
- Granting by Fitch rating agency of a rating for the eurobonds issued by TAURON.
- Adoption of the *Strategic Research Agenda of TAURON Group*.
- Adoption of *TAURON Group's Environmental Policy*.
- Adoption of *TAURON Group's 2017–2025 CAPEX Strategy.*
- Approval of TAURON Group's 2017–2020 Investment Portfolio.
- Adoption of *TAURON Group's 2017–2025 Sustainable Growth Strategy*.
- Publishing of TAURON's and TAURON Capital Group's H1 2017 earnings
- Publishing of TAURON Capital Group's 2016 multimedia Integrated Annual Report on TAURON Capital Group's operations.
- Implementation of a package improving customer service policy.
- Commencement by TAURON Ciepło of the PLNE program for the Silesia and Dąbrowa conurbation and conclusion by TAURON Ciepło and WFOŚiGW of agreements on financing projects under the above mentioned program.
- Launching and conducting of the subordinate bond (hybrid) issue.

SEPTEMBER – OCTOBER

- Launch of the program to implement the GDPR regulations at TAURON Groups.
- TAURON units' win in a RES auction
- Establishing the Tax Capital Group for 2018-2020.
- Launch of the project with respect to developing and implementing a new IT infrastructure in order to improve customer service.
- Introducing for use by TAURON Capital Group's subsidiaries of a new compensation policy for members of the supervising and managing authorities.
- Adoption of the *2018–2025 TAURON Brand Strategy*.
- Inclusion of TAURON in the *The Best of The Best* group and receipt of the top prize for the integrated report in the *The Best Annual Report* competition.
- Change of the name of "KOMFORT-ZET sp. z o. o." subsidiary to "Wsparcie Grupa TAURON sp. z o.o."

NOVEMBER – DECEMBER

- Publishing of TAURON's and TAURON Capital Group's Q3 2017 earnings
- Adoption of *TAURON Group's 2018-2025 Sponsoring Strategy.*
- Launch of the Project aimed at developing a detailed strategic research agenda for TAURON Capital Group with respect to 3 of 4 project portfolios.
- Adoption of a model for the operations of Shared Services Centers at TAURON Obsługa Klienta.
- Pilot implementation of an application automating actions in the customer service process.
- Adoption of policies related to social, personnel, human rights respect and corruption counteraction related issues.
- Introduction of the *PRO Client Social Policy at TAURON Group.*
- Commencement by TAURON Wytwarzanie of the 460 MW turbine refurbishment project at Łagisza Power Plant in order to launch heat production at Łagisza Power Plant.
- Conclusion by TAURON Wydobycie of the agreement on the construction of the above the ground infrastructure at Janina VI shaft at Janina Coal Mine.
- Affirming by Fitch rating agency and ihc of TAURON's Outlook and granting of the rating for the hybrid bond issue worth PLN 400 mln.
- Extending until February 28, 2018 of the validity term of the agreement on cooperation in the 910 MWe unit construction project at Jaworzno III Power Plant with the investment funds managed by Polski Fundusz Rozwoju S.A.

2.8. Key events and TAURON Capital Group's accomplishments with a significant impact on its operations

The more important events and accomplishments that had a significant impact on TAURON Capital Group's operations that occurred in 2017, as well as until the day of drawing up this report are listed below. Additionally the above events should include concluding agreements significant for TAURON Capital Group's operations, described in detail in section 9.2.1. of this report.

Key business events in 2017

Eurobond issue by TAURON

On June 14, 2017 TAURON, in agreement with a consortium of investment banks, commenced activities aimed at conducting a eurobond issue of a nominal value not higher than EUR 500 mln that included in particular conducting meetings with investors in Europe. Conducting of a eurobond issue was dependent on market conditions, and the issue size, the final issue price and the interest rate of the eurobonds were determined following the meetings with investors in Europe.

The Company's intention was to file for admission of the eurobonds to trading on the regulated market of the London Stock Exchange, as well as to use the proceeds from the eurobonds issue to cover TAURON Capital Group's expenses.

On June 28, 2017 the following parameters of the eurobonds were set:

1) Total nominal value: EUR 500 mln,
2) Maturity: 10 years,
3) Interest periods: annual,
4) Coupon: 2.375. per annum,
5) Yield as of issue date: 2.439% per annum (i.e. mid-swap + 1.63%),
6) Issue price: 99.438% of the nominal value.

The condition for the bond issue was the signature of the documentation of the transaction and the fulfillment of the conditions indicated therein.

On July 5, 2017 the Company issued eurobonds with the above indicated parameters that were admitted to trading on the regulated market of the London Stock Exchange on July 10, 2017.

On the same day Fitch rating agency granted the "BBB" rating for unsecured and unsubordinated debt in the form of the Company's 10-year eurobonds with the total nominal value of EUR 500 mln. The rating reflects the Company's leading position in the regulated and stable distribution segment that generates a significant part of TAURON Capital Group's EBITDA (72% in 2016).

The Company disclosed information on the above events in the following regulatory filings (current reports): no. 28/2017 of June 14, 2017, no. 30/2017 of June 28, 2017, no. 31/2017 of July 5, 2017 and no. 32/2017 of July 5, 2017.

TAURON ratings and outlooks affirmed; rating assigned to the hybrid bonds program

On December 21, 2017 Fitch rating agency ("Fitch") affirmed long-term foreign and local currency IDRs of TAURON at 'BBB' with a stable outlook and assigned local currency rating of 'BB+' and national rating of 'BBB+(pol) to the PLN 400 million hybrid bonds program.

Full list of rating actions includes:

1) long-term foreign and local currency IDRs affirmed at 'BBB'; stable outlook,
2) short-term foreign and local currency IDRs affirmed at 'F3',
3) existing hybrid bonds affirmed at 'BB+',
4) national long-term rating affirmed at 'A+(pol)'; stable outlook,
5) national senior unsecured rating affirmed at 'A+(pol)',
6) foreign currency senior unsecured rating of Eurobonds affirmed at 'BBB',
7) ratings assigned to PLN400 million hybrid bonds program: local currency rating of 'BB+' and national rating of 'BBB+(pol).

Information on the above event was published in the regulatory filing (current report): no. 41/2017 of December 21, 2017.

Termination of the long term agreements on the purchase of the property rights by a subsidiary

On February 28, 2017 TAURON Sprzedaż filed a statement on the termination of the long term agreements on the purchase of the property rights arising from the certificates of origin of electricity from renewable energy sources (the so-called "green" certificates). Parties to the agreements concluded in 2008 are the below listed counterparties that own facilities generating electricity from renewable sources:

1) in.ventus limited liability company EW Dobrzyń limited partnership,
2) in.ventus limited liability company Ino 1 limited partnership,
3) in.ventus limited liability company EW Gołdap limited partnership.

The agreements were terminated effective immediately as a result of the parties failing to achieve an agreement while trying to renegotiate the contracts under the procedure provided for in the agreements. The financial implication of the termination of the agreements will be TAURON Sprzedaż avoiding a loss equal to the difference between the contractual prices and the market price of the "green" certificates. An estimated net value of the above mentioned loss due to the performance of the agreements until the end of the originally assumed agreements' term (i.e. until 2023), based on the current market prices of the "green" certificates is approximately PLN 343 mln. Estimated total net value of the contractual obligations of TAURON Sprzedaż in 2017–2023 is approximately PLN 417 mln. The above figure was calculated based on the pricing formulas assumed in the agreements for the period running from the day of drawing up this report until the end of the originally assumed agreements' term (i.e. until 2023).

The above event was described in detail in the regulatory filing (current report) no. 6/2017 of February 28, 2017.

Signing of the letter of intent on the coal gasification project

On April 20, 2017 a Letter of intent was signed between TAURON and Grupa Azoty S.A. defining the general rules of commencing cooperation aimed at implementing the coal gasification project.

The parties signed the Letter of intent due to the fact that among various coal conversion methods of key importance in the medium and long term are those that are offering efficient utilization of coal resources, in line also with the direction of the European Union's policy. This is due, among others, to the need to reduce the ecological burden (footprint) of the power generation and chemical processes, including to significantly reduce the CO_2 emissions.

The detailed information on the above event is provided in section 1.5.2. of this report.

The Company disclosed information on the signature of the letter of intent in the regulatory filing (current report) no. 12/2017 of April 20, 2017.

Important corporate events in 2017

Dismissal and appointment of members of the Company's Management Board

On March 15, 2017 the Company's Supervisory Board dismissed, effective as of the end of day on March 15, 2017, all members of the Company's Management Board of the 4th common term of office, i.e.: Filip Grzegorczyk – President of the Management

Board, Jarosław Broda – Vice-President of the Management Board for Asset Management and Development, Kamil Kamiński – Vice-President of the Management Board for Corporate Governance, Marek Wadowski – Vice-President of the Management Board for Finance, Piotr Zawistowski – Vice-President of the Management Board for Customer and Trade.

At the same time the Supervisory Board on March 15, 2017 appointed as of March 16, 2017 the following persons to TAURON's Management Board of the 5th common three-year term of office: Filip Grzegorczyk, as the President of the Management Board, Jarosław Broda, as Vice-President of the Management Board for Asset Management and Development, Kamil Kamiński as Vice-President of the Management Board for Corporate Governance, Marek Wadowski as Vice-President of the Management Board for Finance.

On March 15, 2017 Piotr Zawistowski up to then performing the function of Vice-President of the Management Board for Customer and Trade provided the Supervisory Board with the information on the resignation from applying for being selected to be a member of TAURON's Management Board of the 5th common term of office. Due to the change made to the Company's Organizational Regulations the Supervisory Board made, as of April 14, 2017, a change of the existing position held by Kamil Kamiński to Vice-President of the Management Board for Customer and Corporate Support.

The Company disclosed information on the change to the composition of the Management Board in the regulatory filing (current report) no. 10/2017 of March 15, 2017.

Changes to the Supervisory Board's composition

On May 25, 2017 the Company received Jacek Rawecki a statement on the resignation, as of May 26, 2017, from the function of a member of the Company's Supervisory Board. Jacek Rawecki did not provide the reason for the submitted resignation.

On May 29, 2017 the Minister of Energy, acting pursuant to § 23, clause 1, sections 1) and 3) of the Company's Articles of Association, appointed the following persons to be members of the Company's Supervisory Board of the 5th common term of office as of May 29, 2017:

1. Beata Chłodzińska,
2. Teresa Famulska,
3. Barbara Łasak-Jarszak,
4. Jan Płudowski,
5. Agnieszka Woźniak.

On May 29, 2017 the Ordinary GM of the Company, acting pursuant to § 22, clause 1 of the Company's Articles of Association, appointed the following persons to be members of the Company's Supervisory Board of the 5th common term of office:

1. Radosław Domagalski-Łabędzki,
2. Paweł Pampuszko,
3. Jacek Szyke.

The Company disclosed information on the above events in the regulatory filings (current reports): no. 19/2017 of May 25, 2017 and no. 22/2017 of May 29, 2017. The information on appointed members of the Supervisory Board was disclosed in the regulatory filing (current report) no. 27/2017 of June 5, 2017.

Decision of TAURON's Management Board on the motion filed to the Ordinary GM of the Company to cover the Company's net loss for the financial year 2016 from the Company's spare (supplementary) capital and not recommend the use of the spare (supplementary) capital for the dividend payout

On March 13, 2017 TAURON's Management Board of the Company adopted the resolution on filing a motion to the Ordinary GM of the Company to cover the Company's net loss in the financial year 2016 in the amount of PLN 166 252 898.52 from the Company's spare (supplementary) capital.

At the same time, in reference to the information on the adoption of the 2016–2025 dividend policy, provided in the regulatory filing (current report) no. 35/2016 of September 2, 2016, the Company's Management Board decided not to recommend to the Ordinary GM of the Company taking of the decision on the use of the Company's spare (supplementary) capital for the payout of the dividend for 2016 to the Company's shareholders.

The above decision was dictated by the needs related to the implementation of the investment program worth approx. PLN 18 bln by 2020 and ensuring TAURON Capital Group's financial stability, including in particular maintaining the net debt/EBITDA ratio defined in TAURON's financial agreements at the level not higher than 3.5x.

Additionally, in accordance with the information published by the company in the regulatory filing (current report) no. 41/2016 of November 14, 2016 the planned stopping of the dividend payout until 2019 was one of the factors enabling the Fitch rating agency to maintain TAURON's long term rating at investment grade level and to change the outlook from negative to stable.

The Company disclosed information on the above decision in the regulatory filing (current report) no. 8/2017 of March 13, 2017.

Shareholder's request to include particular items on the agenda of the General Meeting of the Company

On May 5, 2017 the State Treasury of the Republic of Poland, as a shareholder representing more than one twentieth of TAURON's share capital, submitted a request to include on the agenda of the Ordinary General Meeting of the Company convened on May 29, 2017 additional items related to a change of the resolution no. 5 of the Extraordinary GM of December 15, 2016 on the principles of setting the compensation of the members of the Management Board and a change to the Company's Articles of Association the scope of which was indicated in detail in the content of the regulatory filing (current report) no. 16/2017 of May 5, 2017.

State Treasury indicated as a justification for the proposed changes the need to align the principles of setting the compensation of the members of the Management Board and the content of the Company's Articles of Association to the requirements of the *Act of December 16, 2016 on the state assets management principles*.

The introduction of the amendment to the Company's Articles of Association was aimed at implementing a more transparent split of competences of the Company's corporate authorities, transparent asset management principles, investment decision making principles, manner of appointing members of the supervisory and management authorities and setting their compensation, as well as standards related to actions taken by the management boards of companies, among others in such areas as: consulting, marketing, sponsoring or meals and entertainment expenses.

The draft resolutions received from the State Treasury to be the subject of discussions at the Ordinary GM of the Company and the proposed changes to the Company's Articles of Association were published on May 19, 2017. Meanwhile on May 25, 2017 the State Treasury filed a change to the draft resolution on the change of § 20 of TAURON's Articles of Association and withdrew the draft resolution on the change of § 35 of TAURON's Articles of Association.

The Company disclosed information on the above events in the regulatory filings (current reports) no. 16/2017 of May 5, 2017, 17/2017 and 18/2017 of May 19, 2017 and 20/2017 and 21/2017 of May 25, 2017.

Ordinary General Meeting of TAURON

On May 29, 2017 the Ordinary GM of the Company was held which adopted resolutions concerning, inter alia: the approval of the Consolidated financial statements of TAURON Capital Group and the Report of the Management Board on the operations of TAURON Capital Group for the financial year 2016, the Financial statements of TAURON and the Report of the Management Board on the operations of TAURON for the financial year 2016, covering of net loss for the financial year 2016 from the spare (supplementary) capital, acknowledgement of the fulfillment of duties by members of the Company's Management Board and Supervisory Board, determining the number of members of the Company's Supervisory Board and appointing of members of the Supervisory Board, changing resolution no. 5 of the Ordinary GM of December 15, 2016, as well as amending the Company's Articles of Association.

It was decided to cover the net loss of the Company for the financial year 2016 in the amount of PLN 166 252 898,52 from the Company's spare (supplementary) capital.

The Company disclosed information on convening the Ordinary GM and on the content of the draft resolutions in the regulatory filings (current reports) no. 13/2017 and no. 14/2017 of April 27, 2017. The Company disclosed information on the adopted resolutions and the decisions of the Ordinary GM concerning: covering of the net loss, amendments to the Company's Articles of Association and appointment of the Supervisory Board members in the regulatory filings (current reports): no. 22/2017, no. 23/2017, no. 24/2017 of May 29, 2017.

Amendments to TAURON's Articles of Association

On May 29, 2017 the Ordinary GM of the Company adopted the resolutions on the amendments to the Company's Articles of Association.

As part of the passed amendments to the Company's Articles of Association the majority of the provisions of the *Act of December 16, 2016 on the state assets management principles* were implemented directly in the Company's Articles of Association. Also the competences of the Supervisory Board were extended and it shall express its consent for the conclusion of agreements on legal, marketing services, public relations and social communications services and consulting services related to management if the envisaged total net compensation for the services provided exceeds PLN 500 000, on annualized basis, with respect to donations granted or other agreements of similar effect with the value exceeding PLN 20 000 or 0.1. of the total assets, determined based on the last approved financial statements and relieving of debt exceeding PLN 50 000 or 0,1% of the total assets. Furthermore, the competences of the Supervisory Board were extended by including: tasks related to determining the manner of exercising the voting rights at TAURON Capital Group's subsidiaries' GMs on issues regarding setting up companies, amending the Articles of Association or the Agreement, transformations or liquidations, raising or reducing share capital, divesting and leasing out the company's enterprises or its organized part and establishing a limited property right thereupon, redeeming shares, setting the compensation of members of management boards or supervisory boards, claims for redressing damage inflicted upon formation of the company or exercising management or supervision, with respect to issues mentioned in art. 17 of the *Act of December 16, 2016 on the state assets management principles*. Also the principles of divesting fixed asset components were defined and procedures for selecting members of the management board following the qualification proceeding by the Supervisory Board the goal of which will be to verify and evaluate the candidates' qualifications were introduced, as well as the requirements for candidates for members of management authorities were defined.

On July 12, 2017 the District Court for Katowice-Wschód, the 8th Commercial Department of the National Court Register, entered into the Register of Entrepreneurs of the National Court Register the amendments to the Company's Articles of Association, adopted by the Ordinary GM of the Company by way of resolutions no. 39-45 of May 29, 2017 on amendments to the Company's Articles of Association.

On July 17, 2017 the Supervisory Board of TAURON, acting pursuant to § 20, clause 1, section 13 of the Company's Articles of Association, adopted a consolidated text of the Articles of Association of TAURON that includes the amendment to the Articles of Association entered into the National Court Register by the District Court for Katowice-Wschód in Katowice, the 8th Commercial Division.

The information on the above events was provided in the regulatory filings (current reports): no. 24/2017 of May 29, 2017, 33/2017 of July 12, 2017 and 34/2017 of July 17, 2017.

Other important events in 2017

Appointment of certified auditor

On March 15 2017 the Company's Supervisory Board appointed Ernst & Young Audyt Polska Limited Liability Company Limited Joint-Stock Partnership as the entity authorized to examine TAURON's standalone and consolidated financial statements for the financial year 2017 and review TAURON's standalone and consolidated interim financial statements for the period ending on June 30, 2017. To date the services provided by Ernst & Young for the Company included examinations of the Company's standalone and consolidated financial statements for the years: 2008–2012, as well as reviews of the Company's standalone and consolidated interim financial statements for the periods ending on 30 June in the individual years from 2010 to 2012. The Company also used advisory and training services provided by Ernst & Young to the extent that in no way limited the impartiality and independence of the auditor. The certified auditor was appointed in accordance with the regulations in force, following a non-public order award procedure conducted by way of offer and acceptance. The agreement with Ernst & Young will be concluded by the Management Board of the Company for a period required to perform the contracted services

The Company disclosed information on the above event in the regulatory filing (current report) no. 9/2017 of March 15, 2017.

Submission of the lawsuits in connection with the termination by PEPKH of long-term contracts for the purchase of power and property rights

1. On July 20, 2017 TAURON received the lawsuit of June 29, 2017 of Gorzyca Wind Invest sp. z o.o. with its seat in Warsaw against TAURON for payment of damages in the amount of PLN 39.7 mln and determination of liability for damages that may arise in the future due to torts, including unfair competition acts, estimated by the plaintiff to be worth PLN 465.9 mln. The case is pending before the Regional Court in Katowice. The factual basis for the lawsuit, according to the plaintiff, is the termination by PEPKH – TAURON's subsidiary, of the long term contracts for the purchase of electricity and property rights arising from certificates of origin, and the total amount of the future damages suffered by all of Wind Invest's subsidiaries will reach, according to the plaintiff, PLN 1 212.9 mln. TAURON disclosed information on the termination of the above mentioned agreements in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

   The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

2. On August 2, 2017 a submission was made to TAURON's power of attorney appointed in the lawsuit conducted before the Regional Court in Cracow, file reference no. IX GC 983/14, filed by Dobiesław Wind Invest sp. z o.o. with its registered office in Warsaw against TAURON and its subsidiary, i.e. PEPKH (to prevent the imminent danger of damage to Dobiesław Wind Invest sp. z o.o., by obligating TAURON and PEPKH and to revoke the liquidation of PEPKH), of a pleading of Dobiesław Wind Invest sp. z o.o. containing a change to the lawsuit.

   The plaintiff changed the lawsuit's claim in such a manner that it had withdrawn its original legal action against PEPKH, while it changed the legal action against TAURON from the claim to prevent the imminent danger of damage into the claim for the payment of compensation.

   Dobiesław Wind Invest sp. z o.o. was demanding: 1) payment of PLN 34.7 mln including statutory interest accrued from the day the claim was filed until the payment date, 2) determination that TAURON is liable towards Dobiesław Wind Invest sp. z o.o. for damages that may arise in the future, estimated by the plaintiff at PLN 254 mln (and stemming from TAURON's alleged torts), 3) that injunctive relief be granted against TAURON for the amount of PLN 254 mln in case the court does not find TAURON liable for the damages that may arise in the future.

   The factual basis for the lawsuit, according to the plaintiff, is the termination by TAURON's subsidiary – PEPKH with its registered office in Warsaw of the long-term contracts for the purchase of electricity and property rights arising from certificates of origin, as described by TAURON in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

   The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

3. On August 21, 2017 TAURON received the lawsuit of June 30, 2017 of Pękanino Wind Invest sp. z o. o. with its seat in Warsaw against the Issuer for payment of damages in the amount of PLN 28.5 mln and determination of liability for damages that may arise in the future due to torts, including unfair competition acts, estimated by the plaintiff to be worth PLN 201.6 mln.

   The case is pending before the Regional Court in Katowice. The factual basis for the lawsuit, according to the plaintiff, is the termination by PEPKH – the Issuer's subsidiary, of the long term contracts for the purchase of electricity and property rights arising from certificates of origin. The Issuer disclosed information on the termination of the above mentioned agreements in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

   The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

4. On October 16, 2017 TAURON received the lawsuit of June 30, 2017 of Nowy Jarosław Wind Invest sp. z o. o. with its seat in Warsaw against the Issuer for payment of damages in the amount of PLN 27 mln and determination of liability for damages that may arise in the future due to torts, including unfair competition acts, estimated by the plaintiff to be worth PLN 197.8 mln. This is the last of four announced lawsuits by Grupa Wind Invest companies in this case.

   The case is pending before the Regional Court in Katowice. The factual basis for the lawsuit, according to the plaintiff, is the termination by TAURON's subsidiary, i.e. PEPKH, of the long term contracts for the purchase of electricity and property rights arising from certificates of origin. TAURON disclosed information on the termination of the above mentioned agreements in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

   The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

   The Company disclosed information on the above events in the regulatory filings (current reports): no. 35/2017 of July 20, 2017, no. 37/2017 of August 3, 2017, no. 38/2017 of August 21, 2017 and no. 39/2017 of October 16, 2017.

Important events after December 31, 2017

Selection of certified auditor

On February 26, 2018 TAURON's Supervisory Board selected the audit company Ernst & Young Audyt Polska Limited Liability Company Limited Joint-Stock Partnership ("Ernst & Young") to conduct an audit of the standalone and consolidated financial statements of TAURON for the financial year 2018 and a review of the interim standalone and consolidated financial statements of TAURON for the six months ending on June 30, 2018.

The selection of Ernst & Young to conduct an audit of the standalone and consolidated financial statements of the Company took place in conjunction with the need to bring the agreement concluded with Ernst & Young on auditing the financial statements for the financial year 2017 in line with the requirements of the regulations of art. 66 clause 5 of the law of September 29, 1994 on accounting in the version given thereto by the law of May 11, 2017 on certified auditors, audit companies and public supervision, including with respect to the period for which the first audit agreement should be concluded (i.e. for a period not shorter than 2 years). An amendment to the agreement with Ernst & Young will be concluded for the period required to complete the entrusted activities.

The detailed information was provided in the regulatory filings (current reports): no. 3/2018 of February 26, 2018.

2.9. Prizes and accolades (honorable mentions)

In 2017 TAURON and TAURON Capital Group's subsidiaries received the following awards and accolades.

Figure no. 41. Prizes and accolades (honorable mentions)

PRIZES AND HONORABLE MENTIONS AWARDED TO TAURON AND TAURON CAPITAL GROUP'S SUBSIDIARIES IN 2017

JANUARY

Awarding of the *Laurel of Skills and Competence 2016* prize to the Opole branch of TAURON Dystrybucja by Opole Chamber of Commerce for supporting the economic development of Opole Silesia particularly taking into account the economic zones, efficient and fast fixing of failures, efficient cooperation with institutions, local governments, entreprenesurs and many other entities associated with the region's operations, and also efficient completion of investment processes on the territory of the Opole region, positive participation in the life of Opole counties and municipalities and the attitude of a socially responsible enterprise.

MARCH

- Awarding of a special prize to TAURON in the competition for the best investor relations among WIG30 index companies, organized by the Stock Market and Investors Paper "Parkiet" and the Chamber of Brokerage Houses.
- Honorable mention for 12 initiatives conducted by TAURON Capital Group in the field of sustainable growth in the report "Responsible business in Poland. Best practice" authored by Forum Odpowiedzialnego Biznesu.

APRIL

- Awarding of the *2016 Transparent Company of the Year"* title to TAURON by the Stock Market and Investors Paper "Parkiet" for business transparency and quality of the market communications.
- Awarding of the prize to TAURON in the "Leaders of the Energy World" competition for the energy industry's first startup accelerator program PilotMaker.
- Awarding of the "Leader" title to TAURON during the Techno Biznes 2017 Gala for implementing the "Innovation Zone" application, allowing the company's personnel to submit solutions improving the entire organization's operations.

JUNE

- Awarding the Hero of the capital market 2017 title to TAURON in the Individual Investors Association's competition. Individual investors appreciated TAURON's high standards in the investor relations area and applying of the best practices in the communications addressed thereto.
- Awarding the "Platinium MegaWatt" trophy to TAURON by TGE for being most active on the electricity market among electric utilities in 2016.
- Awarding the "Platinium MegaWatt" trophy to TAURON Sprzedaż by TGE for being most active on the Property Rights market among electric utilities in 2016.

SEPTEMBER

Awarding of the *Ceramic Bat 2017* prize to KW Czatkowice by the board of the BAT FESTIVAL for all contributions to the Cracow county, including many years of contributions to environment protection and actions aimed at popularizing culture and national heritage.

OCTOBER

- Including TAURON in *The Best of the Best* group and awarding the top prize for the integrated annual report in the "The Best Annual Report" competition organized by the Institute of Accounting and Taxes. Thus the Company confirmed its position among companies that can boast the highest reporting standards.
- Awarding TAURON the *Golden Laurel of "Super Business"* prize by business section of the "Super Express" daily in the "Corporate Social Responsibility". TAURON was appreciated for the "Houses of Positive Energy" – competition organized for orphanages and educational care facilities.
- Awarding TAURON Dystrybucja the honorable mention in the *New Impulse 2017* competition by the 16th Congress of Nowy Przemysł / Grupa PTWP S.A. for effective introduction of smart solutions in electricity distribution.
- Awarding TAURON the Wprost Innovator 2017 prize in the energy sector category for participating in the Pilot Maker program, one of the most advance accelerator programs on the Polish market dedicated to implementing solutions developed by startUPs at large enterprises.

NOVEMEBER

- Awarding TAURON Dystrybucja the *White Tiger Laurel* by the Energy Promotion Agency during the 10th Energetykon 2017 "Energy-Climate-Economy-Society" Conference for the design to build Poland's first digital power station in which fully electronic communications will be applied.
- Awarding TAURON Sprzedaż the *Eagle of Wprost 2017 Business Leader* title by the publisher of the "Wprost" weekly in the "Companies with the highest net profit" category in Małopolska region.

DECEMBER

- TAURON's inclusion, for the fifth time in a row, in the RESPECT Index – a group of listed companies managed in responsible and sustainable manner included in this index.
- Awarding TAURON Ciepło a certificate in the *Personnel Friendly Employer* competition by the National Commission of NSZZ "Solidarność" (competition under the patronage of the President of the Republic of Poland Andrzej Duda. The certification committee took into account labor law compliance, concluding of collective bargaining agreements, employing personnel for an idefinite period of time, unionization and counteracting mobbing.
- Awarding TAURON Wydobycie the Miners Families Foundation Medal "A Friend of the Miners Families Foundation Medal". The medal is awarded to an institution that provides financial support for the Foundation, is its active donor and promotor.
- Awarding ZG Janina TAURON Wydobycie the 1st position in the Miners Professional Solidarity competition by the Miners Families Foundation. The metric is the amount of the contributions collected during a year for the Miners Families Foundation in relation to a company's headcount.

JANUARY – FEBRUARY 2018 (prizes for 2017)

- Awarding TAURON Dystrybucja the *Top Event 2017* prize by Evential sp. z o.o. for the "Light Alchemy" organized in 2017 in Katowice – unique Nationwide multimedia show, combining Visual arts: three dimensional mapping, lights, laser and pyrotechnical displays, music, singing and dance live and diverse elements of the form theatre.
- Awarding TAURON Wydobycie the *Solid Company 2017* prize by the Board of the Economic and Consumers Program certifying a company's credibility and integrity. TAURON Wydobycie is a laureate of the "Bronze Solidarity Tophy", as it has passed the verification process for the seventh time already.

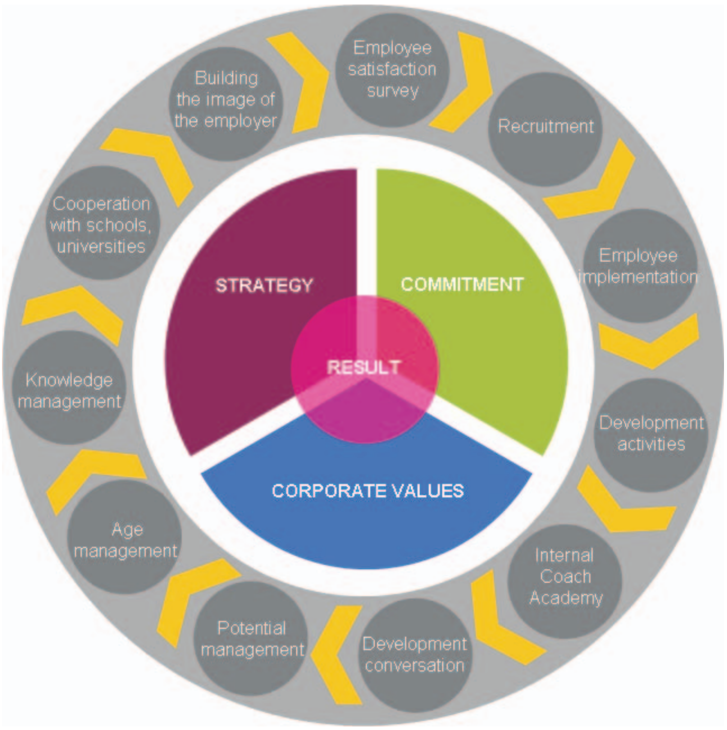
2.10. Information on TAURON Capital Group's employment

2.10.1. Policy of Human Resources Management at TAURON Group

Adoption by TAURON Capital Group of the management by process style of management in 2017 led to updating of the applicable in all companies *Human Resources Management Policy at TAURON Group*, which together with the core values of Partnership, Development and Courage constitute the signposts for management and employees in meeting new challenges and efficiency increasing activities. TAURON Capital Group strives to develop, motivate and win employees capable of attaining the assumed objectives. The overriding purpose is to support the management in effective implementation of changes and promoting new initiatives. TAURON Capital Group seeks to establish conditions fostering development of knowledge and skills, and creating a work environment of cooperation and partnership, where innovativeness and all optimizing initiatives will be the basis for taking actions.

The below figure presents the assumptions of the *Policy of Human Resources Management at TAURON Group*.

Figure no. 42. Assumptions of the Policy of Human Resources Management at TAURON Group



Interdisciplinary teams in the HR area of TAURON Group

Good practice

Partnership attitudes as one of the core corporate values are being instilled already when developing systemic solutions. Challenges facing the HR function are undertaken in adherence to a principle of establishing workgroups consisting of HR staff from companies of the TAURON Capital Group. Team members are appointed by the HR Management Council of TAURON Capital Group, consisting of top HR manager of the Group. This proven style of HR project management results in standardizing and optimizing HR management processes, improving at the same time task completion quality with consideration of the specific requirements in each of the Group companies. Such participative approach is reflected in effectiveness of solutions and building a consistent image of the HR function.

2.10.2. Development and training

Employees of TAURON Capital Group's subsidiaries are participating various forms of development activities:

The below figure presents the forms of development activities of employees of TAURON Capital Group's subsidiaries.

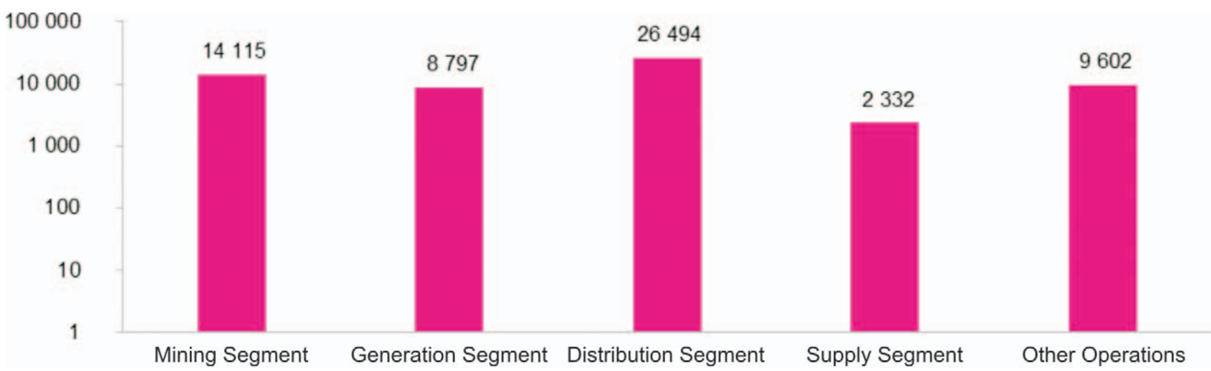
Figure no. 43. Forms of development activities of employees of TAURON Capital Group's subsidiaries

The below figure presents TAURON Capital Group's key 2017 training statistics.

Figure no. 44. TAURON Capital Group's key 2017 training statistics

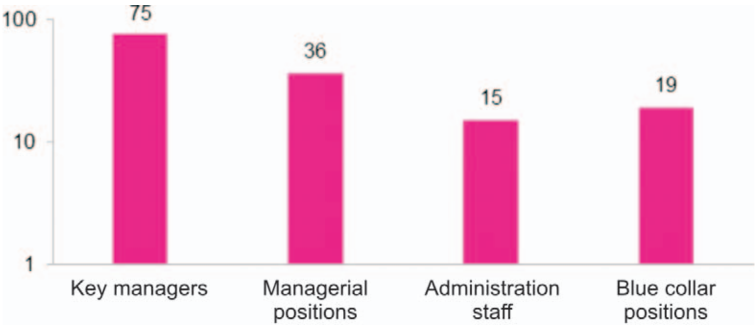
The below figure presents the total number of training days broken down into Segments of operations (lines of business).

Figure no. 45. Total number of training days broken down into Segments of operations (lines of business)



The below figure presents the average number of training hours per employee, broken down into job (work position) groups.

Figure no. 46. The average number of training hours per employee, broken down into job (work position) groups



HR initiatives organized by TAURON Group

Initiative

Employee satisfaction poll (survey) at TAURON Capital Group. The Employee satisfaction poll at TAURON Capital Group took place between end of April and beginning of May 2017. The questionnaire ensured full anonymity and for the first time in history of the TAURON Capital Group was performed in all companies of the Group. Purpose of the poll was to acquire staff opinions as to the most important issues related with their working environs, including values of the company, communicating with superiors and within the company, team atmosphere and cooperation, work safety and hygiene and availability of training and development opportunities.

46% of TAURON Capital Group employees participated in the poll (3769 used hardcopy questionnaires and 7751 filled-in the electronic forms). Of the participants, 84% declared high levels of commitment to their work, 80% stated satisfaction with employee relationships and 70% expressed satisfaction with working conditions at TAURON Capital Group.

Initiative

TAURON Group's Competence Model. *TAURON Group's Competence Model* was developed in mid 2017 as a result of interaction between representatives of individual group companies, coming from a variety of business areas and the HR function. The model reflects strategy, mission, vision and key values, i.e.: Partnership, Development, Courage, and also involves business challenges facing TAURON Capital Group. The model assumes continuing staff development and supporting the attaining of results within TAURON Capital Group. Each employee has awareness of what competences and behaviors are expected of him/her; thus enabling not just performance of assigned tasks, but also developing of own professional capacities. The model affects a multitude of human resources management processes, including recruitment, adaptation, development and employee assessment. Also, individual companies held workshops devoted to the Model, addressed both to managers and employees.

Initiative

Cooperation with universities. TAURON Capital Group cooperated with almost 50 educational establishments (universities, secondary and vocational schools) all over the country. As part of the cooperation, pupils, students and graduates may apply for internship and training at TAURON Capital Group. 693 persons worked as interns in 2017. Through the cooperation partnership relations with the academic community are built – the scientific (academic) staff (faculty) and students. TAURON as a leader can influence education and gaining professional competence amount future adepts in the industry. Best students and graduates were searched for both at universities, through cooperation with university Career Offices and through participation in the largest national fair – Absolvent Talent Days. Furthermore, TAURON Group's Ambassador program was launched in 2017 with its goal to expand cooperation with universities, build a positive image of TAURON Capital Group and recruit top students from the business needs point of view. The program is announced for the given academic year, and the target group includes students in the 2nd to 5th year of their studies.

Initiative

The "Join Us" internship program at TAURON. TAURON launched an internship (traineeship) program in 2017, the purpose of which is to prepare most talented students at Polish universities to enter the job market. Participants are offered a versatile professional development program in state-of-the-art energy industry. Trainees are acquainted with the Company's structure, determinants and rules. The program heavily focuses on forming appropriate attitudes to the tasks assigned, attention to quality and timeliness of performing assigned tasks, valid cooperation with other persons and units within the Company, developing own initiative, acquiring teamwork skills. The program is addressed to 4th and 5th year university students.

Initiative

TAURON Group Open University. TAURON Group Open University is a cycle of lectures conducted since 2014 by the most outstanding experts specialising in various disciplines of science, politics, business, culture and personal development. Through participation in the lectures we want to provide Employees with access to current knowledge and information. In addition, this initiative allows to create a platform for the exchange of ideas and experience among employees from various companies and, consequently, to provide even better support for the implementation of TAURON Capital Group's strategic objectives.

UNIWERSYTET OTWARTY GRUPY TAURON

TAURON Group Open University was launched in order to offer the following opportunities to employees:

1) lifelong learning through exploring new issues and acquiring new skills,
2) active participation in the reality surrounding us through learning new phenomena and the skill to face them,
3) comprehensive, broadly understood development,
4) learning and using the latest technologies,
5) development of own personality, values and pro-social attitudes,
6) exploring various areas of science, life, culture and arts.

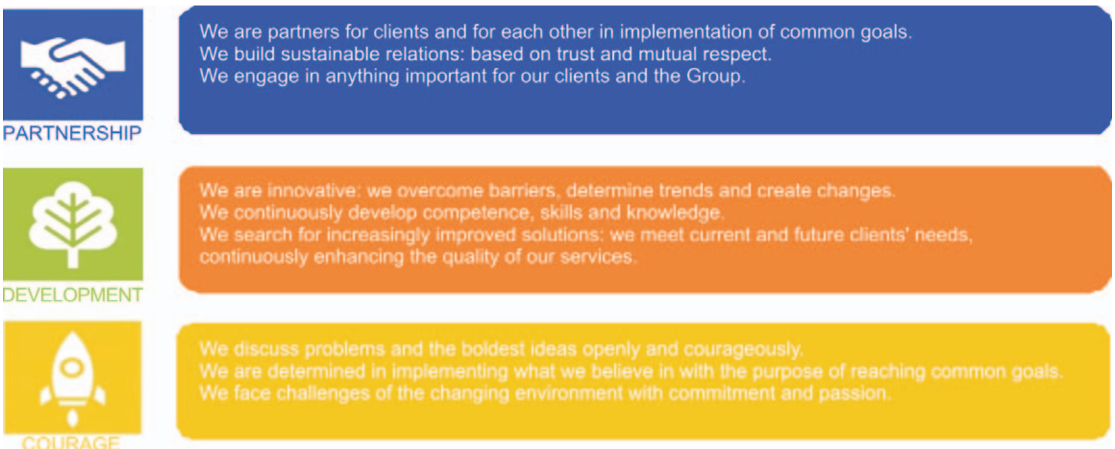
So far, 17 lectures have been provided, attended by over 3 000 employees of all TAURON Capital Group's subsidiaries. 6 lectures were organized in 2017, attended by almost 1 000 employees in total.

Initiative

Values: Partnership, Development, Courage – their implementation within the TAURON Capital Group companies. 2017 was devoted to implementing our core values: Partnership, Development and Courage ("PRO") at TAURON Capital Group's subsidiaries. Workshops introducing staff to the PRO Values program were held throughout the Group. 100% of the lines of business underwent training. Promoting these values within the Group companies proceeded along varying pathways. PRO Values were discussed and refreshed at TAURON Wydobycie and TAURON Wytwarzanie in course of occupational safety and hygiene training courses. TAURON EKOENERGIA organized the "We are PRO" competition, the purpose of which was to promote values by awarding those employees who promote corporate values through their attitude and everyday actions, thus becoming Value Ambassadors within the TAURON Capital Group. Questionnaire based voting led to election of one Ambassador for each of the core values. In turn, TAURON Obsługa Klienta organized workshops at which the importance of PRO Values at work was discussed. A number of involving discussions emerged, during which employees were to respond to issues such as: Why corporations need values? How are values to be understood? What attitudes and behavior support Partnership, Development and Courage?

The PRO Values are a symbol of, and determine TAURON Capital Group's organizational culture; hence it is importance for each employee to be guided by such values in performing his/her everyday duties.

TAURON PRO



Initiative

E-learning platform. Employees of selected companies of TAURON Capital Group's subsidiaries may use the e-learning platform containing many training courses. They include both specialised training and training courses developing interpersonal skills. In 2017 mandatory training courses were launched for the workforce with respect to "Recruitment and adaptation (induction) of employees – step by step", "Responsible Business Code" and "Counteracting mobbing and discrimination at TAURON Group". In total all users of the platform realized more than 32 000 training courses in 2017.

Initiative

Developing managers. The Managers Development Program comprises a comprehensive growth initiative the purpose of which is to support management level staff in both their business as well as personal efficiency, and to consciously develop model leadership attitudes within the entire TAURON Capital Group. Core values of TAURON Capital Group, i.e. Partnership, Development and Courage, guide individual actions within the program and constitute its second foundation. Developed competence enables the participants to become even more efficient leaders, whereas values determine the areas and objectives where their efficiency attains best results. The Program has been prepared and implemented based on globally proven solutions and expertise of coaches and experts involved in the Program. The development process is practical in nature and at the same time delivers inspiration and nurtures uniqueness. More than 70 key managers at TAURON Capital Group participate in the Program.

Initiative

International Family Day festivities at TAURON Capital Group. 2017 marked the fourth year in which TAURON participated in public festivities associated with the International Family Day, the purpose of which is to strengthen family ties through sincere discussion and by building and strengthening identity of the young generation. All TAURON Capital Group companies participated in the 2017 festivities. On the agreed day, employees were allowed to work 2 hours less on full pay, and free time was to be devoted to their families and friends. The companies also organized competitions promoting leitmotif of the campaign, which this year read "Cooking within the family circle". The festivities continued at TAURON, TAURON Dystrybucja and TAURON Ciepło where visits of children, and even grandchildren, at parent workplaces were organized. Visits were accompanied by entertainment and attractions.

Initiative

The Innovativeness Marathon at TAURON Dystrybucja. November 2017 witnessed the first Innovativeness Marathon organized at TAURON Dystrybucja. Twelve teams of 6 students, each, worked on a project inspired by the slogan: "Energy of the Future: Internet of Things, Big Data and electro-mobility in power grids of the future". Participants came from the AGH University of Science and Technology in Kraków, and from the Silesian, Częstochowa and Wrocław Technology Universities. First 3 days of the Marathon gave participants an opportunity to familiarize with needs of TAURON Dystrybucja clients and principles of working in the service design thinking formula based on workshop based activities using creative techniques. Acquired knowledge was used during the next two days to create innovative solutions for TAURON Dystrybucja. The competition was won by the "Electron" team from the Silesian Technical University in Gliwice, which presented the idea of an algorithm defining optimal locations for electric power loading stations for electric vehicles, taking into account characteristics and loads of the existing power grid.

Initiative

Skills development for employees of TAURON Obsługa Klienta. In implementing its objective to provide high quality services and developing employee skills, TAURON Obsługa Klienta being the Shared Services Center in 2017 organized a number of training course and workshops on communication and cooperation, integration of staff and building team relationships, course oriented towards agility at work, workshops on mediation based operating styles, courses on improving security at the Customer Service Centers (POK), effective communication techniques, cooperation under changing requirements and a set of workshops devoted to leadership skills. Over 1200 employees participated in these initiatives

Initiative

Management by Objectives training for management staff. In 2017 TAURON held a series of workshop course dedicated to management staff, devoted to the Management by Objectives methods, particularly principles of setting and cascading objectives based on the SMART model. The goal of the workshops was to make the participants familiar with the principles of evaluating attaining of objectives and giving constructive return information. Also, tools used to support employees in attaining their objectives and tools for assessment of subordinates were presented. More than 60% of the Company's management staff participated in the two-day workshops.

Initiative

Policies combating Mobbing and Discrimination at the TAURON Group. The *Policy of combating Mobbing and Discrimination at the TAURON Group* was developed in the second half of 2017. The policy document applies throughout the entire TAURON Capital Group. The policy defines principles for counteracting mobbing and discrimination at the workplace and in relation to performing duties, ensures implementation of labor law provisions and includes internal regulations enforced by the employer. Intervening activities and actions aimed at alleviating abusing mobbing or discrimination behaviors against employees were presented, as well as consequences awaiting perpetrators.

2.10.3. Social dialogue

The Management Board of TAURON conducts a constructive and open dialogue with the workforce (social party), mainly aimed at maintaining high quality and effectiveness of mutual cooperation. During regular meetings and consultations, the workforce representatives are informed about issues associated with:

1) TAURON Capital Group's economic and financial situation of TAURON Capital Group,
2) TAURON Group's 2016–2018 Efficiency Improvement Program and Strategic Initiatives,
3) Voluntary Redundancy Programs underway at TAURON Capital Group's subsidiaries,
4) issues related to employee affairs at TAURON Capital Group.

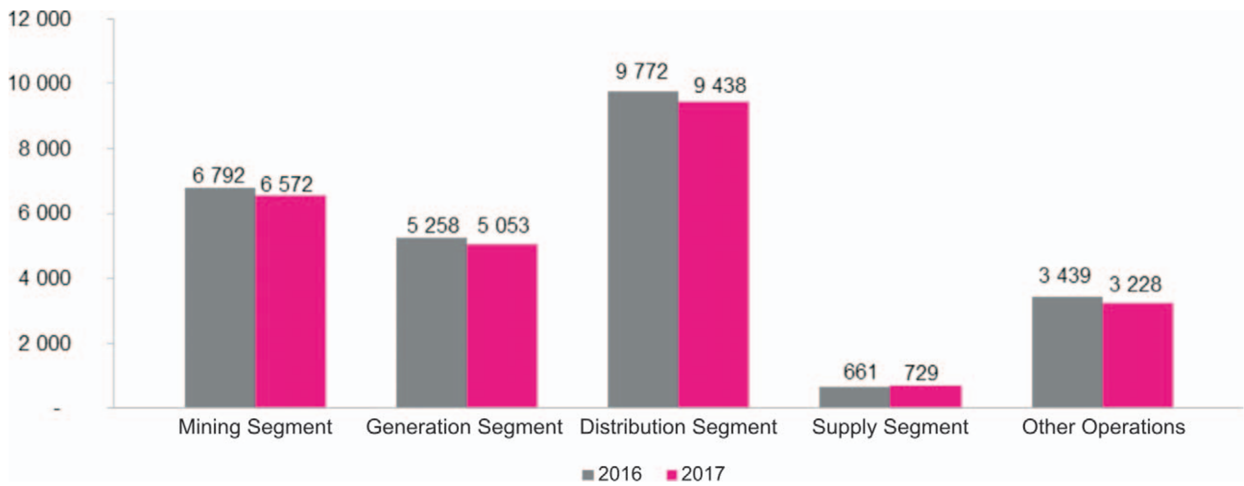
As part of the conducted social dialogue the Management Board of TAURON provided many answers to the correspondence from the trade union organisations and the Ministry of Energy. In parallel, ongoing communication is maintained at TAURON Capital Group's subsidiaries between Management Boards and trade union organisations operating at the given employer. TAURON takes an active part in meetings at the national level with the representatives of the government, employees and employers (within the activities of the Tri-party Team for the Energy Sector).

2.10.4. Key headcount data

TAURON Capital Group's average headcount reached 25 020 FTEs in 2017 which means a decrease versus the headcount in 2016, when the average employment was 25 992 FTEs.

The below figure presents TAURON Capital Group's average headcount in FTEs (rounded up to the full FTE) per line of business (Segment) in 2016 and in 2017.

Figure no. 47. TAURON Capital Group's average headcount in 2016 and in 2017[1] (FTEs)



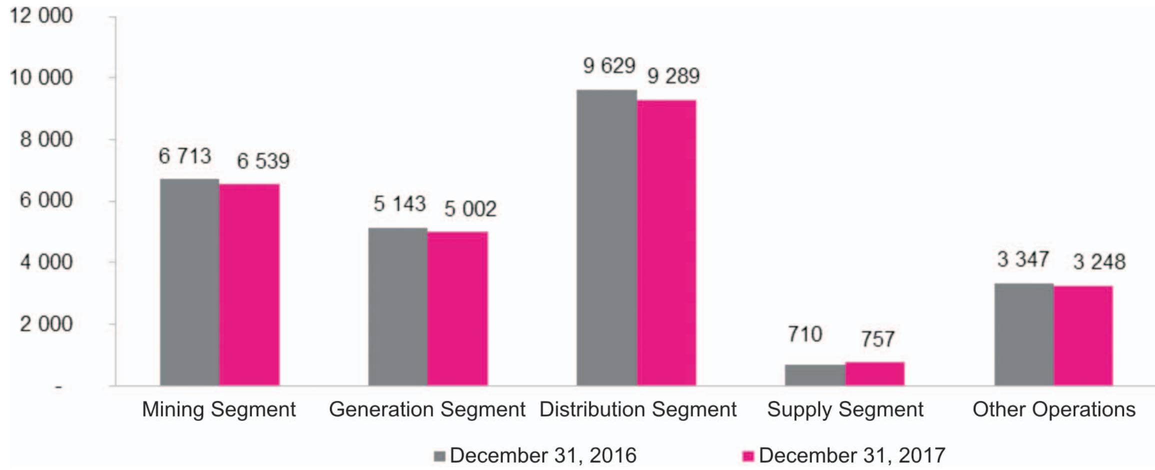
[1] *Average headcount includes Nowe Jaworzno GT subsidiary that was covered by the consolidated reporting in H1 2017.*

Changes to the average headcount at individual Lines of Business (Segments) in 2017 in relation to the average headcount in 2016 arise, inter alia, from the *Voluntary Redundancy Programs in the* Distribution, Generation Segments and the Other Operations line of business underway, as well as employees leaving TAURON Capital Group.

24 835 persons were employed by TAURON Capital Group's subsidiaries as of December 31, 2017. The headcount decreased by 707 persons as compared to the headcount as of December 31, 2016 that reached 25 542 persons.

The below figure presents TAURON Capital Group's headcount in persons as of December 31, 2016 and December 31, 2017.

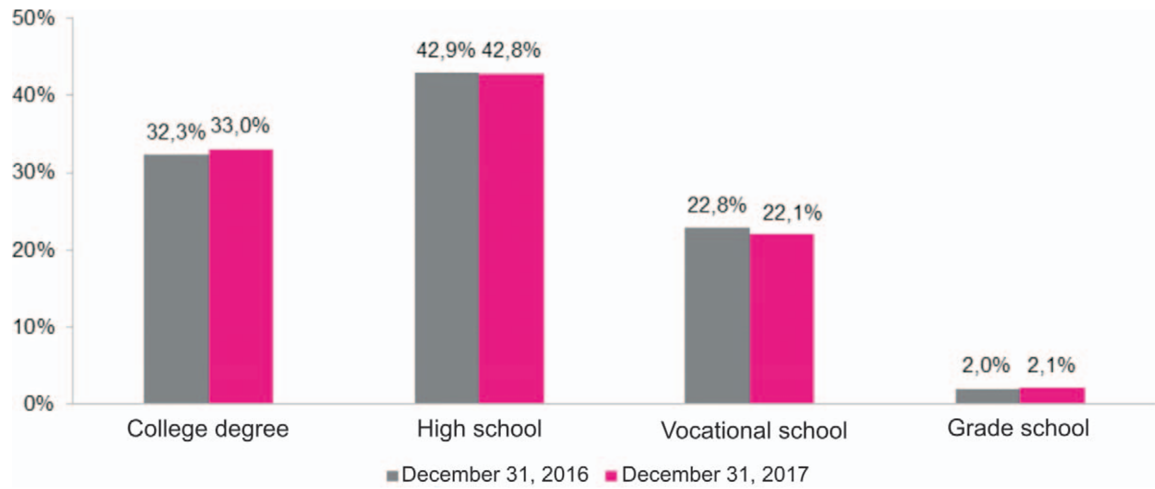
Figure no. 48. TAURON Capital Group's headcount as of December 31, 2016 and December 31, 2017[1] (persons)



[1] *Headcount in persons includes Nowe Jaworzno GT subsidiary that was included in the consolidated reporting in H1 2017*

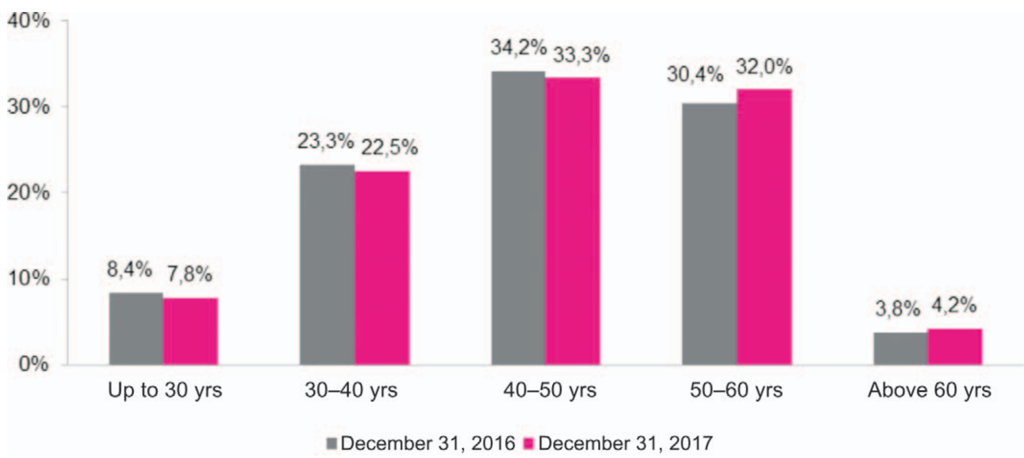
The below figure presents the structure of employment at TAURON Capital Group by education level as of December 31, 2016 and December 31, 2017.

Figure no. 49. Structure of employment at TAURON Capital Group as of December 31, 2016 and December 31, 2017 (by education level)



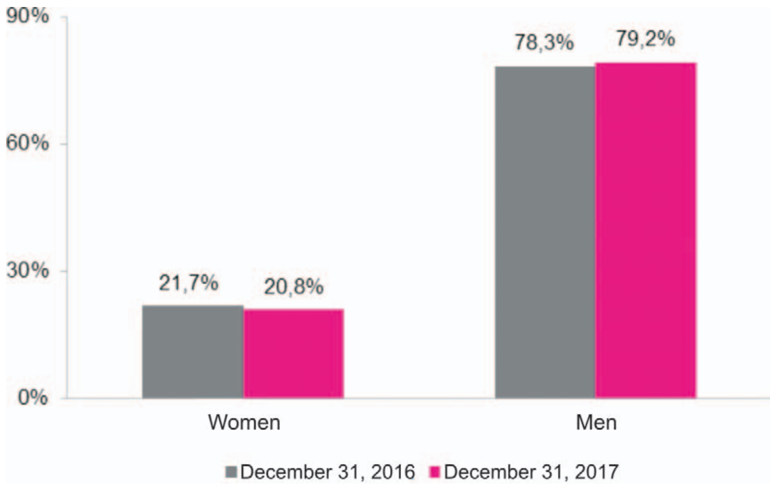
The below figure presents the structure of employment at TAURON Capital Group by age as of December 31, 2016 and December 31, 2017.

Figure no. 50. Structure of employment at TAURON Capital Group as of December 31, 2016 and December 31, 2017 (by age)



The below figure presents the structure of employment at TAURON Capital Group by gender as of December 31, 2016 and December 31, 2017.

Figure no. 51. Structure of employment at TAURON Capital Group as of December 31, 2016 and December 31, 2017 (by gender)



2.11. Corporate Social Responsibility (CSR) Policy

TAURON Group's 2017–2025 Sustainable Development Strategy

Undertakings commenced in 2016 were continued in 2017 in order to strengthen TAURON Capital Group's position as a leading, innovative and modern enterprise that is steadfastly implementing its Strategy and Business Model.

On August 1, 2017 TAURON's Management Board adopted the updated *TAURON Group's 2017–2025 Sustainable Development Strategy* (Sustainable Development Strategy) that was developed based on *TAURON Group's 2016–2025 Strategy*, taking into account feedback of the stakeholders, and also the current challenges facing the energy sector. Sustainable Development Strategy constitutes the framework of actions with respect to TAURON Capital Group's Corporate Social Responsibility.

Sustainable Development Strategy is based on 5 directions. Two of them are of leading nature as they are related to the operations on the market – "Orientation towards the customer and his/her needs" and "Reliability and quality of the supply of products and services for customers". The other three are the supporting directions and they include "Labor safety, ethical culture and employee engagement", "Environment protection" and "Social and business partnership". For each direction obligations (18 in total) that TAURON is intending to fulfill by the end of 2025 were defined. For each obligation key initiatives were formulated that support their implementation and they were assigned to the individual organizational units (business units) of TAURON Capital Group.

Reporting non-financial data

Sustainable Development Strategy is directly associated with all of TAURON Capital Group's lines of business. It streamlines both the approach to the CSR as well as the methodology for assessing the effectiveness of measures undertaken based on Global Reporting Initiative (GRI) indicators.

In 2017 TAURON Capital Group published its integrated report for the second time. Apart from the financial data the document presented the complete view of the company's operations, including its impact on the economy, society and environment.

The integrated formula provided a clear way to show the relationships and dependencies between the financial and non-financial aspects of the operations of all of TAURON Capital Group's subsidiaries and thus constituted a comprehensive and transparent document, presenting the company's operations, its Business Model, Strategy, most important changes, opportunities and risks, and also the results from the point of view of all stakeholder groups. Combining the financial data with the non-financial aspects of the company was also aimed at showing the potential reached due to the synergies between the core operations and the non-business activities.

The report was prepared in accordance with the highest reporting standards – GRI G.4, and it was subjected to external verification by an independent auditor. The Company was also audited in connection with joining the RESPECT Index – the index comprising companies listed on the stock exchange, operating in accordance with the rules of sustainable development. In 2017, TAURON achieved, for the fifth time, a positive result and was included in this most prestigious ranking of socially responsible companies.

Key CSR projects

One of the directions of the Sustainable Development Strategy is the social and business partnership. The resulting goals are implemented, among others, through the activities of TAURON Foundation which allows for even more effective implementation of CSR goals with respect to taking care of safety of local communities and actions for public benefit.

TAURON Capital Group, operating in the south of Poland, holds the leading position in electricity distribution and its supply on the territory of the Lower Silesia, Opole, Silesia and Małopolska regions. Because of that the range of actions conducted for the benefit of the communities in which TAURON Capital Group's subsidiaries are operating, is very broad. Many projects are supported which are important for the inhabitants of the Upper and Lower Silesia, Opole, Małopolska and Podkarpacie regions. Among others, TAURON is cooperating with the Mountain Voluntary Emergency Service (GOPR), with the goal to improve safety in the mountains.

In 2017 TAURON continued also its cooperation, commenced in 2014, with the SIEMACHA Association – one of the leading NGOs in the country focusing on the implementation of projects in the area of education, sports and therapy, providing systemic assistance to children and teenagers. As part of this cooperation TAURON's patronage covered sports activities of the association, gaining the title of *TAURON – SIEMACHA's sports partner*. In 2017 such projects were supported as *Football Children's Day with TAURON* and *Juliada.*

Activities carried out by TAURON Capital Group's subsidiaries are also worth mentioning. In 2017 the campaign, implemented by TAURON Sprzedaż, called: *TAURON does not go door to door to sell electricity or gas* was continued. Its stage focused on raising awareness of customers on the energy market, in particular, in order to protect them against practices of unfair salesmen. On the other hand, TAURON Dystrybucja has been conducting, since 2013, an educational program for children and teenagers called *TAURON fuses. Switch on for the kid's benefit.* Its main goal is to improve safety by popularizing the rules of safe electricity use.

In 2017 TAURON Foundation, the Company and TAURON Dystrybucja implemented the thirteenth edition of the Houses of Positive Energy campaign, addressed to 24-hour custody and caretaking facilities, aimed at improving the living conditions of children from orphanages and educating, motivating them to act, opening prospects and enabling to set themselves apart in a positive manner. Since refreshing the campaign's formula, i.e. since 2011, 523 orphanages have taken part in the campaign. Young persons taking part in the campaign are competing for a financial prize every year in order to fulfill their youth passions, dreams and wishes.

In 2017 the Foundation also accomplished its goals, in particular, through supporting private individuals and legal entities, institutions and organisations in their activities consistent with the Foundation's goals, transferring by way of donations PLN 3 074 896.41.

TAURON is a signatory of the declaration signed on June 17, 2009 during the national conference as part of the cycle *Responsible Energy*, comprising the principles of sustainable development in the energy sector in Poland.

In 2013, the Company joined a group of signatories of the *Business declaration for the sustainable development*, consequently undertaking to get involved in the implementation of strategic goals of the *Vision of sustainable development for the Polish business 2050*.

Since 2014, TAURON has also been a member of the Responsible Business Forum.

2.11.1. Energy security

Ensuring energy security to customers is the first of the obligations included in the Sustainable Development Strategy. As an essential element of Poland's energy system, TAURON optimizes processes in individual lines of its business operations: generation, distribution and supply of electricity and heat, in order to ensure stable power supplies with high quality parameters to customers. In order to ensure continuity of power supply, TAURON not only implements new investment projects but also conducts ongoing maintenance works and upgrades of its infrastructure held as well as actively searches for new solutions.

In 2017 TAURON Dystrybucja upgraded almost 1 300 km of existing grids and 36 main power supply points. The Company also built 2 500 km of new lines including the connections. Also 4 new main power supply points were built. Investment projects are also conducted by TAURON Ciepło. In 2017 the total capacity under the agreements with customers on new connections to the heating network reached 47.2 MW.

On August 30, 2017 an agreement on financing the Low Emission Elimination Program (Program Likwidacji Niskiej Emisji – PLNE) in 8 cities of the Silesia and Dąbrowa metropolitan area covered by the low emission, i.e.: Będzin, Chorzów, Czeladź, Dąbrowa Górnicza, Katowice, Siemianowice Śląskie, Sosnowiec, Świętochłowice, was signed. TAURON Ciepło is planning to connect, under PLNE, by the end of 2022, approximately 1300 buildings which represents approximately 183 MW of heat capacity in total. Ultimately, as a result of the construction and refurbishment of the heating networks under PLNE, 100 km of modern heating networks (pre-insulated) will be built.

Under PLNE, by the end of 2017 TAURON Ciepło concluded, additionally, agreements with customers on connecting building to the heating networks with the total capacity of 14 MW.

At the same time, in order to guarantee stable supplies, TAURON Dystrybucja conducts ongoing measures minimizing the risk of failure as well as shortening the response time necessary to find the place of failure and to remedy it. It is fostered, inter alia, by the implementation of the modern system of Grid Assets Management or the increase of the grid automation level. For several years, rules of prioritisation of investment needs have been applicable in TAURON. They are aimed at addressing the expenditure to places that have the strongest impact on the improvement of electricity supplies and effectiveness of the distribution grid performance, including the enhancement of the qualitative electricity indicators.

Moreover, taking care for comfort and security of persons having contact with electricity and the equipment supplied by it, TAURON Dystrybucja has been carrying out the educational and information campaign called *TAURON Fuses* addressed to children and teenagers. In 2017 a multimedia educational platform was developed and launched, providing teachers, pupils and parents with access to educational materials. Some of them are adapted to the needs of disabled pupils. The Company is also the initiator and co-organizer of other social campaigns enhancing the level of energy supply reliability (e.g. “Stop the illegal electricity intake” campaign).

Innovative technological solutions represent an important element of the energy supply process. Accordingly, TAURON Capital Group puts strong emphasis on activities in the area of research and development, resulting not only in innovative solutions with respect to, inter alia, reducing the emission of hazardous substances from combustion processes but also innovative products and services for individual customers (e.g. Electricity with an electrician 24 h, offering “Your 300”, Preferential 0 percent interest rate for those buying boilers from TAURON).

Since 2016 the Zone of Innovation has been operating in TAURON Capital Group’s intranet, within which competitions for employees are organised. Its objective is to promote innovative organizational culture and encourage employees to submit innovative solutions optimizing daily work. After the announcement of the competition results, the proposals are archived and available in the Zone of Innovation to all users. The first competition launched in the Zone of Innovation was related to safety at work place. In 2017 all projects that won prizes in the “Safe at work” competition were implemented. They included, e.g. representing a compendium of Occupational Health and Safety, safety boards and books at TAURON Wydobycie’s Janina Coal Mine and the boards promoting the slogan “Always in good form!”, presenting simple exercises dedicated to office workers, placed at all TAURON Capital Group’s subsidiaries’ sites nest to network printers. The Research and Development Team was also conducting Works on further initiatives aimed at engaging the workforce to be innovative.

2.11.2. Customer orientation

At the time of intense changes in the market environment, progressing digitization and mobility of the society also a visible change of customer expectations is taking place who are becoming more active and aware, expect a broad and comprehensive offering and modern service channels. Meeting the needs of almost 5.3 mln customers, and also orientation towards their needs is reflected in the Sustainable Development Strategy in which customer related issues represent the two leading directions: “Reliability and quality of the supply of products and services for customers” and “Orientation towards the customer and his/her needs”.

Efforts aimed at accomplishing the assumed obligations in this respect are based on many measures in each of the value chain areas, inter alia, through grid modernisation, searching for solutions enhancing customer satisfaction, ensuring security of customer interests, care for vulnerable customers and disadvantaged groups as well as through continuous education in the area of effective use electricity and its safe utilisation.

TAURON analyses market trends on an on-going basis as well as conducts cyclical customer satisfaction surveys concerning the services and products offered. Owing to such activities the Company endeavors to meet customers’ expectations, satisfying their current and future needs, to the largest extent possible. At the same time, complaint handling procedures are improved, allowing for prompt and efficient response in situations reported by customers.

All measures constituting the customer service process are conducted in compliance with the highest ethical standards.

Seeking not to limit the relations with customers only to the provision of products and services, as well as having the awareness of many threats which may potentially affect a customer in various aspects of electricity purchase or use, TAURON conducts educational campaigns addressed to electricity users.

The educational and informational functions are fulfilled, inter alia, by the action "Energy for the senior", implemented by the Team of Customer Rights Ombudsman operating within the customer area in TAURON. The initiative is addressed to the elderly who are most exposed to activities of unfair energy vendors (salesmen). Its aim is to educate customers how to move across the energy market. The action is based on the inter-sectoral cooperation of business, public administration represented by consumer rights ombudsmen and non-governmental organisations, i.e. universities of third age, senior clubs as well as associations of retired and pensioners. Within the workshops, both lectures for a broad group of audience and intimate educational meetings are organized.

2.11.3. Customer satisfaction survey

One of key tools of customer satisfaction evaluation at TAURON Capital Group is the CSI survey (poll). This survey is conducted on a regular basis, once a year, at the turn of the 2nd and 3rd quarter, by an independent research agency. The said survey is conducted on a random basis for the selected group of TAURON customers and for a group of customers of other energy companies, such as: ENEA, ENERGA and PGE.

In accordance with the adopted plan the CSI poll, representing one of key tools of customer satisfaction evaluation at TAURON Capital Group, was conducted in June – August 2017 by an independent research agency – TNS Polska S.A.

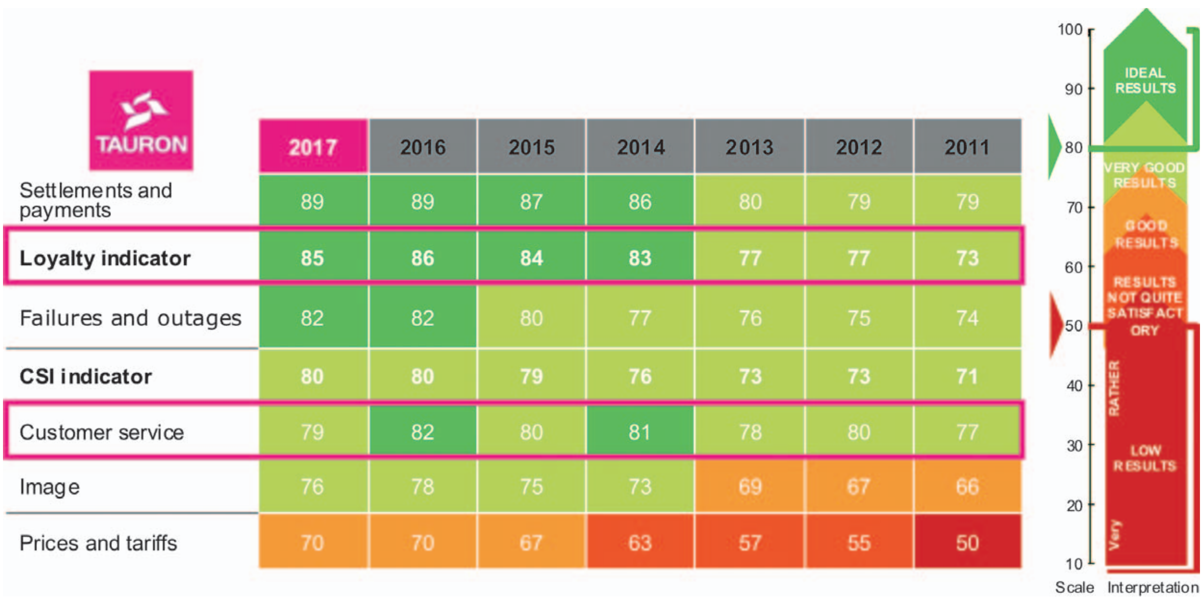
The survey covered randomly selected customers of the Household segment (1 000 customers), Small enterprises (200 customers) and Corporations and large enterprises (300 customers) and a group of customers of other energy companies, such as: ENEA, ENERGA and PGE.

As a result of conducted surveys the CSI was determined to be at the following level:

1) Households – 80 points,
2) Small enterprises – 71 points,
3) Corporations and large enterprises – 77 points.

The below figure presents results of surveys conducted in the Household segment, achieved by TAURON in the period from 2011 to 2017, and the level of the CIS indicator reached in 2017, as compared to other energy groups

Figure no. 52. Results of the survey covering households in 2011–2017

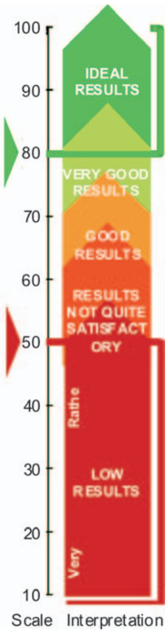


	2017	2016	2015	2014	2013	2012	2011
Settlements and payments	89	89	87	86	80	79	79
Loyalty indicator	85	86	84	83	77	77	73
Failures and outages	82	82	80	77	76	75	74
CSI indicator	80	80	79	76	73	73	71
Customer service	79	82	80	81	78	80	77
Image	76	78	75	73	69	67	66
Prices and tariffs	70	70	67	63	57	55	50

The below figure presents the results of the TAURON survey as compared to other Energy Groups in 2017.

Figure no. 53. Results of the TAURON survey as compared to other Energy Groups in 2017

	TAURON	COMPETITION TOTAL	Energa	Enea	PGE	innogy
Settlements and payments	89	86	85	88	87	83
Loyalty indicator	**85**	**81**	**79**	**81**	**84**	**69**
Failures and outages	82	80	81	80	81	76
CSI indicator	**80**	**76**	**74**	**77**	**79**	**69**
Customer service	79	76	73	75	80	63
Image	76	72	71	72	74	61
Prices and tariffs	70	66	67	66	68	55



2.11.4. Impact on natural environment

Environmental protection in the energy sector is the area controlled and regulated by the EU and national legal regulations as well as the local law, therefore, it is strongly associated with the business operations of TAURON Capital Group, in particular, in the context of contemporary challenges related to minimizing the environmental impact throughout the value chain: from mining, through generation and distribution, up to the supply of electricity and heat to final consumers. Considering the sustainable development rules, TAURON Capital Group's subsidiaries are optimizing the processes of management of the resources used (water, raw materials and materials) and are also conducting an active policy of waste management (both process related waste as well as the other waste arising as a result of the operations conducted).

The pro-ecological education conducted by the individual TAURON Capital Group's subsidiaries, addressed both to children and youth as well as to adults, also plays an important role in the area of environmental protection.

TAURON Capital Group's subsidiaries are actively engaging in many information and educational programs concerning environmental protection and energy saving and conservation which are addressed both to employees, local communities and to customers. Such actions include the educational campaign to combat low emission called "Breathe with Air", launched in 2016 and continued in 2017.

A confirmation of the above actions was the adoption in July 2017 of *TAURON Group's Environmental Policy*, in which it was stated that TAURON Capital Group accepts responsibility for taking care of natural environment and the consequences of the use of its resources for the benefit of the current and future generations, recognizing as important the social obligation to ensure environment protection both in its operations, as well as among its customer partners.

The most important actions with respect to environment protection

TAURON Capital Group's subsidiaries are conducting responsible environmental protection policy and apply due diligence to ensure that both the operations conducted as well as the implemented investment projects are compliant with the requirements and include technological advancements with respect to environment protection.

The most important actions with respect to environment protection conducted by TAURON Capital Group in 2017 included:

1) continuation of the construction of the 910 MW unit capacity at Jaworzno III Power Plant, whose commissioning will significantly influence the reduction of emissions of NO_x, SO_2, CO_2 and particulate matter (TAURON Wytwarzanie),
2) Projects started: Revamping of the mechanical sewage treatment plant with chemicals support at the Jaworzno III Power Plant – Power Plant II (TAURON Wytwarzanie), modernization of the electrofilter of unit no. 5 at Jaworzno III Power Plant in order to reduce dust emission (TAURON Wytwarzanie),

3) Projects started at Łaziska Power Plant: revamping of the hydrochloric acid, sodium hydroxide, iron sulphate unloading station to enable unloading of truck takers and commencing with project on protecting the mazut unit area against penetration of hazardous substances into the environment (TAURON Wytwarzanie),
4) General overhaul of electrofilter No. 1 and partial upgrade of lighting system to LED technology within the general overhaul of Power Unit No. 1 at Siersza Power Plant (TAURON Wytwarzanie),
5) Low Emissions Elimination Program implementation (TAURON Ciepło),
6) Revamping of hydroelectric power stations to reduce oils leakage and contamination of natural environment risks caused by installation failures (TAURON EKOENERGIA),
7) Launching of project associated with construction of a fish ladder at the Marszowice Hydroelectric power station (TAURON EKOENERGIA),
8) Construction and reconstruction of the sanitary and rainwater sewerage system for ZG Sobieski with up-connection to the municipal grid (TAURON Wydobycie),
9) Revamping of transformer stations to protect the water environment (transformer stations equipped with trays) and elimination of intrusive sources of noise (TAURON Dystrybucja),
10) Launching of the project associated with heat recuperation at the limestone milling unit (KW Czatkowice),
11) Launching of the project associated with automatic road sprinkling using process water supply (KW Czatkowice),
12) Thermal revamping of vehicle service station and control room building (KW Czatkowice),
13) Revamping of the heating system – laying of external gas supply network by Polska Spółka Gazownictwa sp. z o.o. (PSG) (KW Czatkowice),
14) Reconstruction of the Dumping Station with construction of dust removal system for reducing random emissions (KW Czatkowice),
15) Pro-ecological initiatives – educational campaign developing ecological awareness of young people: “Clean up of the Pilchowski Reservoir”, where 159 students of partner schools within operating area of TAURON EKOENERGIA together with teachers and employees of TAURON EKOENERGIA completed the 19th campaign of cleaning shores of the Pilchowski Reservoir. Over 400 120-liter bags of refuse were collected (TAURON EKOENERGIA),
16) Continuing of the long-lasing “Our Stork” campaign, i.e. construction of successive stork nest poles and performing necessary maintenance of existing nest poles (TAURON Dystrybucja).

The exemplified above actions are aimed at ensuring the compliance of TAURON Capital Group operations with regulations applicable in protection of the environment, with consideration of local circumstances, specific nature of our business, striving at the same time to improve efficiencies.

Minimizing the negative impacts on the environment

Minimizing of the negative impacts on the environment is effectively implemented the specifics of the sector, technology advancements and access to the environmentally friendly technologies.

TAURON Capital Group is monitoring on an ongoing basis the main aspects of the direct and indirect impact on the environment of its operations.

The effects of implementing the capex plan over many years, related to adapting TAURON Wytwarzanie’s conventional sources to comply with the tightened emission requirements allowed, in 2017, for the operations of the generation units at values well below the NO_X, SO_2, dust emission standards currently in force and in many cases close to the values of the future environmental requirements.

The below table presents the estimated levels of NO_X, SO_2, dust and CO_2 emissions from fuel combustion for electricity generation purpose for selected TAURON Capital Group’s subsidiaries in 2017.

Table no. 19. Annual levels of NO_X, SO_2, dust and CO_2 emissions from fuel combustion for electricity generation purpose for 2017

No.	Subsidiary name	SO_2 emission (Mg)	NO_X emission (Mg)	Dust emission (Mg)	CO_2 Emissions (Mg)
1.	TAURON Wytwarzanie, including:	13 385	13 701	733	14 654 964
	Oddział Jaworzno III	3 423	5 438	143	6 919 502
	Oddział Łaziska	3 430	3 302	182	3 879 920
	Oddział Łagisza	2 343	2 294	161	1 869 428

No.	Subsidiary name	SO_2 emission (Mg)	NO_X emission (Mg)	Dust emission (Mg)	CO_2 Emissions (Mg)
	Oddział Siersza	2 686	1 706	177	1 538 045
	Oddział Stalowa Wola	1 503	961	70	448 069
2.	TAURON Ciepło, including:	3 522	1 610	217	1 913 711
	ZW Bielsko-Biała	979	278	29	500 989
	ZW Kamienna Góra[3]	52	17	6	17 208[3]
	ZW Katowice	1 572	660	84	877 950
	ZW Tychy	591	543	18	422 857
	CC Olkusz	143	39	10	40 239
	CC Zawiercie	127	43	9	36 079
	Other (local heating plants)[3]	58	30	61	18 38
3.	KW Czatkowice	3	6	14	5 909
	Total	**16 910**	**15 317**	**964**	**16 574 584**

[1] *Total emission of dust from fuel combustion.*
[2] *CO_2 emission within the meaning of EU ETS – according to Annual Reports on CO_2 Emission (status in January 2017, the level of emission prior to verification).*
[3] *Installations not covered by EU ETS. Estimated value, prior to verification at the end of the 1st quarter of 2017.*

TAURON Capital Group accepts responsibility for taking care of natural environment and the consequences of the use of its resources. In 2017 TAURON Capital Group's subsidiaries accrued fees in the total amount of approximately PLN 38.6 million, i.e. approximately 8% more than in 2016.

The below table presents the level of fees for the use of the environment for business purposes due for 2017 at selected TAURON Capital Group's subsidiaries.

Table no. 20. The level of fees for the use of the environment for business purposes due for 2017

No.	Subsidiary name	Fees for use of the environment for business purposes due for 2017 (PLN thous.)
1.	TAURON Wytwarzanie	21 012
2.	TAURON Wydobycie	13 372
3.	TAURON Ciepło	4 074
4.	TAURON Dystrybucja	100[2]
5.	KW Czatkowice	50
6.	TAURON Dystrybucja Serwis	12[2]
7.	TAURON Obsługa Klienta	1.9
8.	TAURON EKOENERGIA[1]	< 0.8
9.	TAURON Sprzedaż	1.6
	Total	**38 623.5**

[1] *Total amount below PLN 800 a year is not subject to the statutory exemption from paying fees for the use of the environment for business purposes.*
[2] *Estimate data, the annual settlement has not been closed.*

Sustainable development

TAURON Capital Group is taking actions aimed at improving energy efficiency in order to reduce or not increase the consumption of fuels and monitoring climate impact.

In 2017 within TAURON Capital Group a number of investment projects were submitted, associated with the improvement of energy efficiency in the Distribution and Mining lines of business, whose direct environmental effect is the reduction of CO_2 emission. This effect was partly confirmed through the allocation of the so-called "white" certificates as a result of the tender, resolved in July 2017, carried out by the President of ERO based on the rules in force before, i.e. 2016 rules. The remaining part of the effect will only be confirmed in 2018 through the allocation of the property rights certificates according to the new principles of the amended energy efficiency law.

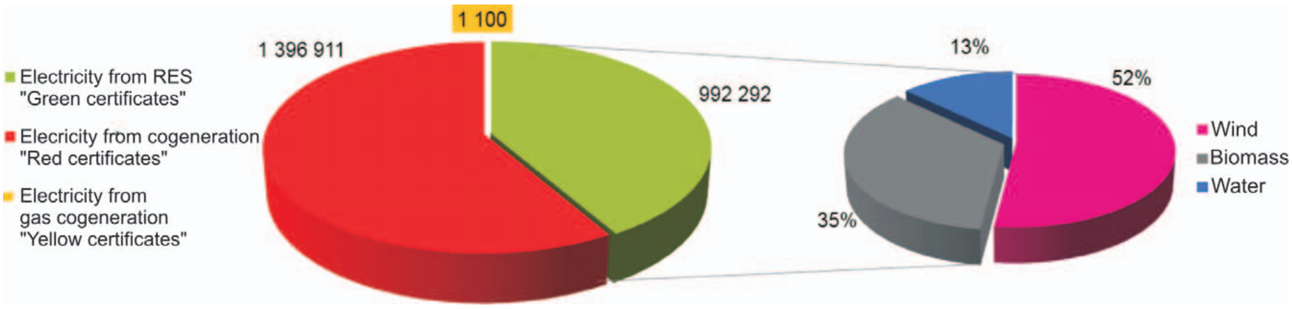
Furthermore, in 2017 an energy efficiency audit was completed for all of TAURON Capital Group's Lines of Business in order to identify optimization areas.

Although the core production of TAURON Capital Group is based on the traditional energy relying on solid fossil fuel, TAURON Capital Group, in its basic volume of production, includes high efficiency generation of electricity and heat in the co-generation system and supplements its offering with electricity generated from renewable sources or in generation based on gas which is reflected in the quantity of property rights to the certificates of origin of electricity generated:

– 992 292 MWh, so-called “green” certificates,
– 1 396 911 MWh, so-called “red” certificates,
– 1 100 MWh, so-called “yellow” certificates.

The below figure presents the structure of the property rights to the certificates of origin obtained by TAURON Capital Group in 2017.

Figure no. 54. Structure of the property rights to the certificates of origin (MWh)



Management of by-products

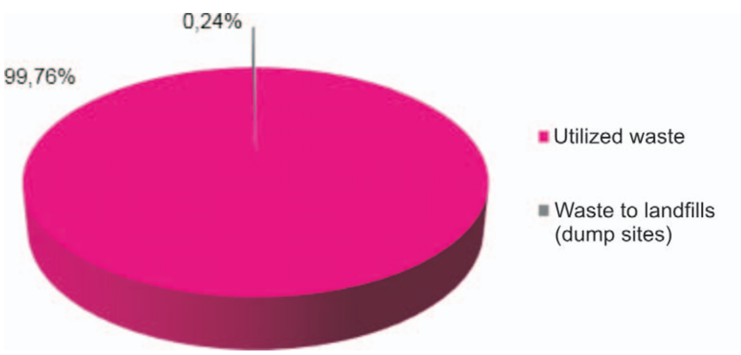
TAURON Capital Group, caring for the natural environment, minimises the quantity of waste deposited in the environment through their introduction to the market, to be used as substitutes for natural materials.

Waste generated by TAURON Capital Group is mainly used in the construction, road building and mining sector. The waste is broadly used by cement and concrete plants. It was also used as the material for reclamation of unfavourably transformed areas.

In 2017 TAURON Capital Group’s conventional power generation segment generated approximately 2.2 million Mg of furnace waste, including 99.76% that was managed on the market and only 0.24% was deposited directly at the dumping sites.

The below figure presents the structure of energy waste management.

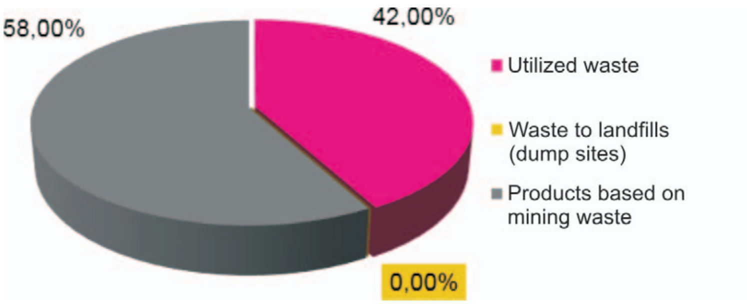
Figure no. 55. Structure of energy waste management



In 2017 hard coal mining at TAURON Capital Group generated 1.1 million Mg of mining waste and 1.4 Mg of full value aggregate products. The products obtained were used in various industries, among others in the construction and mining. waste comprised aggregate and sludge originating from coal processing and preparation. 100% of the waste generated was used for the business purposes.

The below figure presents the structure of mining waste management.

Figure no. 56. Structure of mining waste management



TAURON Capital Group is seeking to implement the model of closed circuit (circular) economy. It is planned that the maximum of generated process waste is used within TAURON Capital Group, consequently reducing the consumption of natural resources and the product's carbon footprint.

2.11.5. Sponsoring activities

In 2017 TAURON introduced significant changes to its internal regulations related to the sponsoring activities. New *Rules of conducting sponsoring activities by TAURON Group* taking into account the *Best practice with respect to conducting the sponsoring activities by companies with the State Treasury shareholding. TAURON Group's 2018–2025 sponsoring strategy* was adopted. The sponsoring activities were conducted based on the *Plan of conducting the sponsoring activities by TAURON Group in 2017*, adopted by the Management Board and granted a positive opinion by the Supervisory Board.

The main objective of TAURON Capital Group's sponsoring activities is to support its business and communications goals in reference to *TAURON Group's 2016–2025.*

The sponsoring activity was carried out based on negotiated agreements, according to standardized provisions. Moreover, this activity was monitored, analysed and reported on an on-going basis, through detailed reports on the implementation of sponsoring agreements, surveys and analyses conducted in quarterly and annual cycles by specialized external entities and the supervision of companies of TAURON Capital Group.

In accordance with the implemented procedures, the assessment of effectiveness of the activities conducted was carried out, through opinion surveys, measurement of the value and size of brand exposure in media, in the context of the activities conducted, measurement of implementation of sales targets, with reporting of the obtained results. As a result of the promotion effectiveness measurement, an independent research entity initially estimated the advertising equivalent in relation to activities completed in 2017. Comparing the summarised value obtained in this way to the sum of all expenditure arising from sponsoring agreements the ROI ratio at a level of approximately PLN 7.2. was obtained. It means that each zloty (PLN) spent for that purpose generated promotional benefits to TAURON Capital Group whose preliminary value is independently estimated at approximately PLN 7.2. The ongoing verification of the aforementioned value should not significantly change the value of this ratio.

The confirmation of the financial effectiveness of the activities conducted is the high positioning of TAURON brand in an independent research report, *Sponsoring Monitor 2017*, which is the only source of this type of information on the Polish market. According to this report, TAURON is ranked seventh in the TOP 10 list of sponsors and it is the most recognized (noticeable) sponsor versus its direct competitors. More than 200 brands were classified In the ranking, which is the result of opinion polls. In spite of relatively lower outlays on sponsoring versus some of its direct competitors, TAURON achieved a better result, being ranked 3 positions higher than the next group and finding itself among the very top group of the most recognized (noticeable) sponsors. Because of a relatively low level of TAURON Capital Group's sponsoring expenditures its position in this ranking can be regarded as truly very high. Taking into account an indicative value of Poland's sponsoring market according to the *Sponsoring Insight* data and the data from the above mentioned ranking it can be extrapolated that the effect achieved gives TAURON Capital Group a 9–11% market share – which in comparison to other power sector entities is a result that puts TAURON in a position of the leader of efficiency and effectiveness of the funds invested in these activities.

In 2017 sponsoring activities were carried out by TAURON and TAURON Sprzedaż. Both companies implemented 24 projects with 16 customers in total. The preliminary data related to accomplished advertising equivalents referring to activities ended in 2017 indicate that the best results were achieved by activities under projects related to professional sports, i.e. KS Vive TAURON Kielce, Lang Team (among others Tour de Pologne) and Polish Ski Association. Among projects underway such activities as sponsoring of TAURON Arena Kraków were characterized by a strong potential.

3. RISK MANAGEMENT AT TAURON CAPITAL GROUP

3.1. Risk management objective and principles

Risk at TAURON Capital Group is understood as an uncertain occurrence or a group of occurrences that, in case of materializing, will have an impact on achieving by TAURON Capital Group of its defined strategic goals, both negatively (threat), as well as positively (opportunity).

In line with its Strategy the Company is implementing the process of managing the risk related to the operations of TAURON Capital Group. The primary goals of risk management include ensuring the broadly understood security of TAURON Capital Group's operations. In particular, risk management is to ensure increased predictability of TAURON Capital Group achieving its strategic goals, including sustainable financial generation of its financial results.

TAURON Capital Group's risk management:

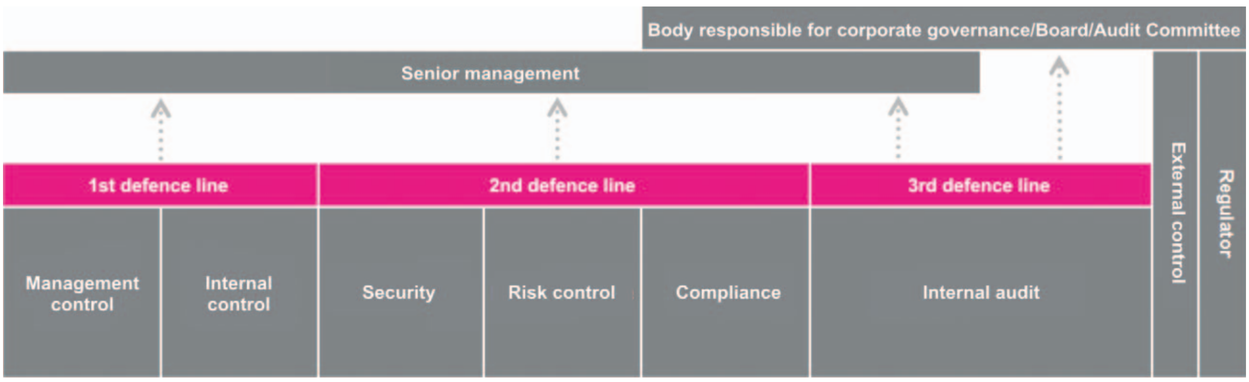
1) covers all elements of the value chain,
2) provides centralized risk measurement, monitoring and control function, and also ability to evaluate the full risk profile in the organization and coherent risk management principles,
3) ensures independence of the risk taking function from its control and monitoring,
4) ensures a clear split of competences and responsibilities, in particular by introducing the risk ownership function,
5) is an active process, focused on an appropriately early identification of threats, allowing for taking preventive measures,
6) is a systematic and continuously improved process which allows for aligning it on an ongoing basis to TAURON Capital Group's specifics and organizational structure, as well as to the changing environment,
7) places a strong emphasis on developing awareness, training and encouraging personnel to use the knowledge of risks in daily activities,
8) co-creates at TAURON Capital Group the internal audit system, constituting, along with the compliance and security management functions, an element of the three line defense.

3.2. Risk management using the "Three Defense Lines Model"

In order to ensure security of the functioning of the organization the "Three Defense Lines Model" is implemented by TAURON Capital Group, comprising internal control (audit), independent control (audit) within the second defense line and institutional control (audit). In particular, the risk management function co-creates a system of internal control (audit) at TAURON Capital Group, constituting an element of the second defense line, next to the function of ensuring the compliance and security management

The below figure presents the "Three Defense Lines Model".

Figure no. 57. Three Defense Lines Model

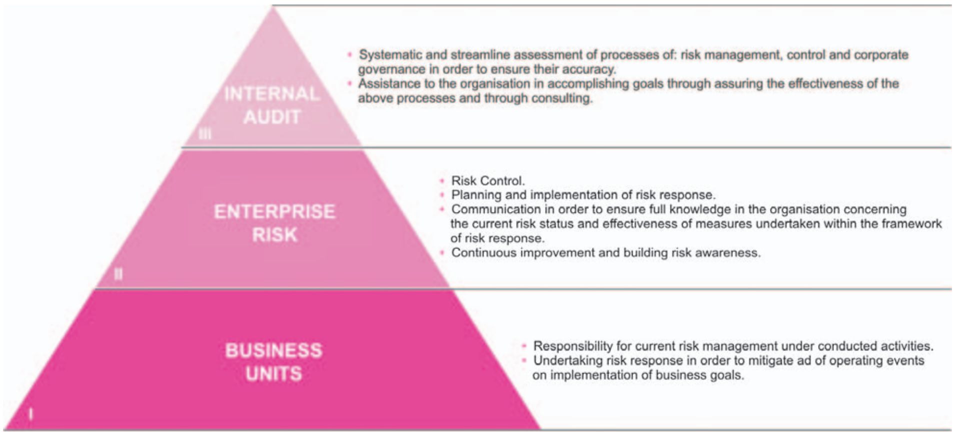


Functions of the individual defense lines:

First Line of Defence is:	Business units obliged to perform ongoing control embedded in the tasks implemented and the functional control.
Second Line of Defence is:	a) function of risk management implemented in accordance with the adopted *Corporate risk management strategy at TAURON Group* and detailed policies related to main risk categories, b) function of ensuring compliance understood as adjustment of the organisation to the applicable legal regulations, c) function of ensuring information security and technical safety.
Third Line of Defence is:	internal audit responsible for creating the internal control system and adequate functioning of the three defense lines model.

The below figure presents risk management as a function of the second defense line.

Figure no. 58. Risk management as a function of the second defense line

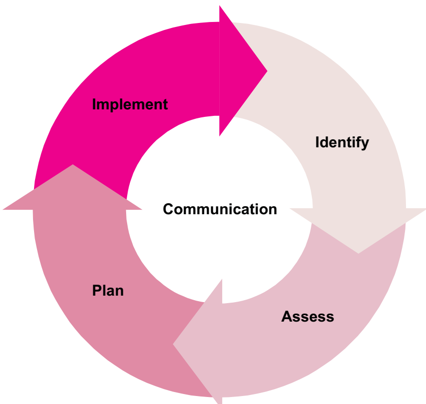


3.3. Risk management process and its participants

The process of enterprise risk management ensures the comprehensive and consistent risk management rules linked with each other in terms of methodology and information. The process of enterprise risk management means continuous measures comprising risk identification, risk assessment, planning of risk response, implementation of the adopted risk response and communication between risk management process participants.

The below figure presents the risk management process.

Figure no. 59. Risk management process



Risk identification – consisting in determining the potential events that may affect the implementation of business goals of TAURON Capital Group.

Risk assessment – consisting in determining of potential financial and non-financial effects of risk materialisation influencing the implementation of specific goals.

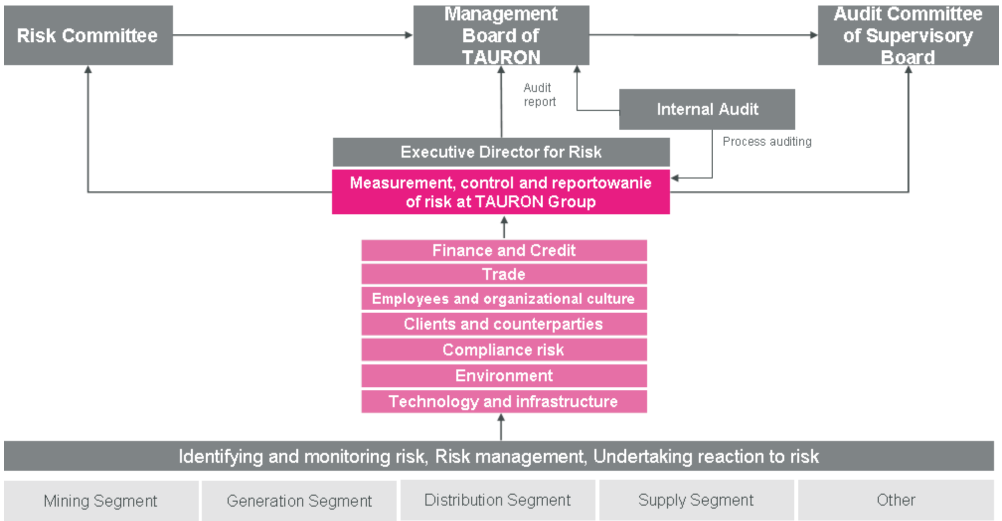
Planning – consisting in preparation of the dedicated response to the risk identified in order to achieve the desirable goals.

Implementation of risk response – consisting in practical implementation of the responses to identified risk prepared in the planning process.

Communication – consisting in continuous information flow among participants of the process which should ensure full knowledge concerning the current risk status and effectiveness of activities conducted within the response to risk. The periodical risk reporting is also an element of this process

The below figure presents the risk management process.

Figure no. 60. Diagram of the management risk communication



3.4. Architecture of the enterprise risk management system (ERM[3])

The enterprise risk management system (ERM), implemented at TAURON Capital Group's level, constitutes a set of rules, standards and tools allowing for implementing the primary goal of risk management which is, broadly understood, ensuring safety (security) of TAURON Capital Group's operations. This system is governed by the document entitled *Corporate risk management strategy at TAURON Group* that defines TAURON Capital Group's corporate risk management rules and its goal is to ensure the consistency of managing the individual risk categories that were detailed in separate regulations, aligned with the specifics of the individual threat groups.

The below figure presents the ERM system.

Figure no. 61. ERM system

[3] *Enterprise Risk Management*

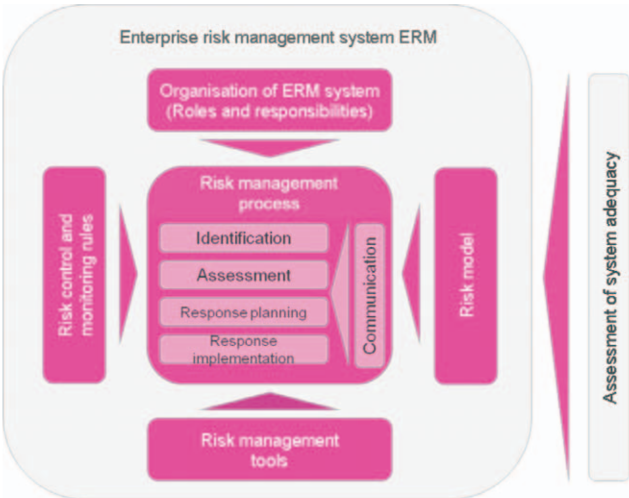
The detailed description of the rules and tools for managing the individual risk categories is provided further on in this section.

The risk management process described in detail in section 3.3 is the center (core) of the system. Moreover, the architecture of the ERM system comprises elements to ensure effective functioning of the process, including:

1) risk management tools,
2) risk models,
3) control and monitoring rules,
4) organisation of the ERM system

The below figure presents the architecture of the ERM system.

Figure no. 62. Architecture of the ERM System



Risk management tools comprise elements allowing for effective implementation of individual stages of the process, such as risk identification questionnaire, risk card, risk register, risk model, risk map, risk tolerance

Within the framework of **ERM system organisation**, roles and responsibilities of risk management process at TAURON Capital Group were defined. Participants of the process include, in particular: TAURON Supervisory Board, Audit Committee of TAURON Supervisory Board, Management Board of TAURON, Risk Committee, Executive Director for Risk at TAURON, Executive Director for Audit at TAURON, management boards of subsidiaries, Risk Owners, Risk Management Coordinators and Executors of risk response.

The below figure presents the organizational structure and documentation of the risk management process.

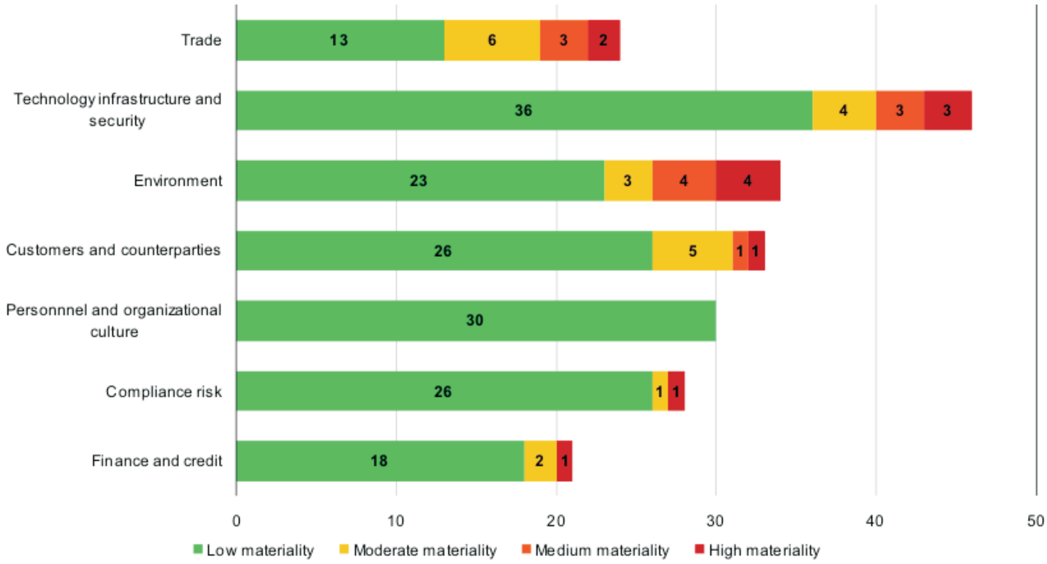
Figure no. 63. Organisational structure and documentation of the risk management process

<table>
<tr><td colspan="7">Supervisory Board
Audit Committee</td></tr>
<tr><td colspan="7">Management Board</td></tr>
<tr><td>Management</td><td colspan="5">Risk Committee
Team for Commercial Risk Management
Team for Financial and Credit Risk Management</td><td>Internal audit</td></tr>
<tr><td rowspan="5">Organisational Regulations/ Bylaws</td><td colspan="5">Strategy of enterprise risk management in TAURON Group</td><td rowspan="2">Internal Audit regulations</td></tr>
<tr><td>Policy of commercial risk management in TAURON Group</td><td>Policy of operating risk management in TAURON Group</td><td>Policy of risk management in projects in TAURON Group</td><td>Policy of credit risk management in TAURON Group</td><td>Policy of management of risk specific in financial area in TAURON Group</td></tr>
<tr><td>Market Risk Team</td><td colspan="2">Corporate Risk Team</td><td>Credit Risk Team</td><td>Executive Director for Finance</td><td>Internal Audit Team</td></tr>
<tr><td colspan="5">Executive Director for Risk</td><td>Executive Director for Internal Audit</td></tr>
<tr><td colspan="5">Reporting to Supervisory Board, Management Board of TAURON, Members of Risk Committees</td><td>Reporting to the President of the Board</td></tr>
</table>

Risk model defines a consistent risk classification, enabling a consistent and comprehensive capturing of risk across TAURON Capital Group. Each risk identified is assigned to specific categories and sub-categories.

The below figure presents the main risk categories defined by TAURON Capital Group, including the number of key threats:

Figure no. 64. Number of risks monitored, broken down into categories



As part of the implementation of the **risk control and monitoring rules** the Management Board of TAURON approves risk tolerance, taking into consideration the specific nature and scope of operations of TAURON Capital Group. The level of the tolerance defines the value of the maximum permitted risk exposure at TAURON Capital Group and the rules of measurement of individual risks in the organisation ensure the consistency of risk measurement with the applied tolerance definition. The risk tolerance constitutes basis for allocation of its level to the global limits dedicated to a single risk or many key risks. Subsequently global limits are allocated to operating limits within the key risk management.

A supplementary tool used for risk monitoring and control comprises the Early Warning System based on the catalogue of Key Risk Indicators – KRI and Early Warning Indicators – EWI. The system functioning based on the KRI and EWI indicators enables an appropriately early identification of threats by measuring the causes of the individual threats. At the same time this system Allows for an appropriately early ta king of remedy actions, before the individual threats actually materialize.

3.4.1. Commercial (trading) risk management

TAURON Capital Group's commercial (trading) risk management is understood as reducing unplanned volatility of its operating result, due to price fluctuations on the commodity markets and volume deviations in the individual areas of TAURON Capital Group's commercial (trading) operations. The commercial (trading) risk, due to the specifics of the operations conducted, constitutes one of TAURON Capital Group's key risks. TAURON Capital Group is made up of subsidiaries operating both in the Mining and the Generation Lines of Business as well as in the Supply Line of Business. Due to the opposing positions in these Lines of Business the risk is, to a certain degree, naturally diversified. However since these Lines of Business do not fully offset each other, and due to the diverse nature of the exposures, TAURON Capital Group is displaying sensitivity to the volatility of the prices of electricity, gas and related products.

In order to efficiently manage this group of risks the commercial (trading) risk management system was established, tied on the organizational and information level to TAURON Capital Group's process used to develop a commercial (trading) position hedging strategy. In particular *TAURON Group's commercial (trading) risk management policy* introduces an early warning system and a system used to limit risk exposure in the individual commercial areas. The basic operating measure of TAURON Capital Group's market risk is Value at Risk, defining the maximum admissible change of the position's value over the given time horizon and at a specific probability level. Value at Risk represents a dynamic risk measure which in contrast to static measures allows for determining potential negative effects before their factual occurrence. Due to the limitations of the statistical measures the commercial (trading) risk management system also uses a number of supplementary risk measures enabling a safe operation of the commercial (trading) areas.

The organizational structure of the commercial (trading) risk management system envisages a strict split of competences as part of which risk management is decentralized, where the supervision and risk control are performed centrally at TAURON's level. In particular an element of the organizational structure of the commercial risk management system is the split of TAURON Capital Group's trading operations into: Front Office, Middle Office and Back Office. The goal of such a split of tasks is to guarantee the independence of the operating functions carried out by the Front Office from the risk control carried out by the Risk Area, and it ensures an appropriate level of operational flexibility. For the needs of of the risk management process such placement of responsibility is assumed in order to ensure an optimal approach to the given type of threat, especially taking advantage of the economy of scale and the synergy effect. Such approach ensures efficiency of the commercial processes conducted and appropriate supervision over one of the main business processes conducted by TAURON Capital Group.

The below figure presents a breakdown of TAURON Capital Group's trading operations.

Figure no. 65. Breakdown of TAURON Capital Group's trading operations

PARTICIPANT	ROLES AND RESPONSIBILITIES OF PARTICIPANTS
Front Office	• Concludes transactions on markets of commodities and related products • Manages portfolio within TAURON Capital Group • Operationally manages trade risk within defined risk limits
Middle Office	• Identifies, aggregates and measures exposure to trade risk • Ensures independent risk assessment and measurement of generated result • Conducts monitoring of trade operations in terms of their compliance with adopted policy, procedures and market conditions • Supervises structure of portfolios in terms of its adjustment to commercial activity
Back Office	• Is responsible for confirmation, settlement and invoicing of trade transactions • Is responsible for archiving data related to trade transactions

3.4.2. Financial risk management

As part of financial risk management TAURON Capital Group is managing the FX risk and interest rate risk, based on the rules and standards in line with the best practices in this respect. The main goal of managing these risks is to minimize the sensitivity of TAURON Capital Group's cash flows to the financial risk factors and to minimize the financial costs and the hedging costs as part of a transaction with the use of derivative instruments. In cases when it is possible and economically justified TAURON Capital Group uses the derivative instruments the characteristic of which allows for applying the hedging accounting.

With respect to the financial risks TAURON Capital Group also identifies and actively manages the liquidity risk understood as a potential loss or limitation of the ability to pay current expenses, due to an inadequate value or structure of liquid assets in relation to short term obligations or an insufficient level of the actual net inflows from the operations. TAURON Capital Group's liquidity position is monitored on an ongoing basis for any potential deviations from the assumed plans and the availability of external sources of financing the amount of which substantially exceeds the expected short term demand, mitigates the risk of losing liquidity. For this purpose TAURON applies specific rules of determining the liquidity position, both of the individual subsidiaries, as well of entire TAURON Capital Group, which allows for securing funds to cover a potential liquidity gap, both by allocating funds among subsidiaries (cash pool mechanism), as well as with the use of external financing, including overdrafts.

Risk associated with financing is identified at three levels:

1) Risk of failure to raise new financing, understood as a lack of possibility to acquire new funding, which would result in suspension of the investment process or the lack of possibility to re-finance the current debt,
2) Risk of cost increase understood as the growth in financing margin,
3) Risk of termination of financing in case of breach of covenants and the necessity to repay current financing.

Within the mitigation of risk associated with financing TAURON Capital Group Company conducts a policy of funding acquisition at least 24 months in advance in relation to the planned date of its use. It means that TAURON Capital Group should hold signed programs of guaranteed financing or hedge this financing through collection of funds on TAURON Capital Group's accounts. Such a policy is mainly aimed at ensuring a higher comfort in acquisition of external financing and reducing the risk of incurring new liabilities under unfavourable market conditions. At the same time, the Company diversifies financing sources by active measures with respect to the acquisition of various debt instruments, also outside the Polish market.

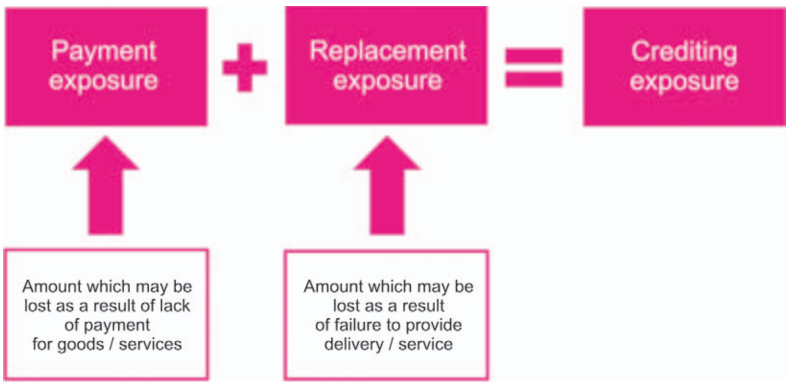
3.4.3. Credit risk management

Credit risk is understood as a possibility to incur a loss due to trade partners (counterparties) failing to fulfill their contractual obligations (default). TAURON Capital Group is using a decentralized credit risk management system, however the control, limiting and reporting of this risk category is carried out centrally, on the parent Company level. *TAURON Group's Credit Risk Management Policy* in place defines credit risk management principles on TAURON Capital Group's level, aimed at effectively minimizing the impact of this risk on achieving TAURON Capital Group's goals.

Credit risk management is carried out by controlling the credit exposure generated upon the conclusion of contracts by TAURON Capital Group's subsidiaries. The general rule is that prior to concluding a contract every entity is subjected to an examination of its financial standing and receives a credit limit which caps the maximum exposure due to the given trade. Credit exposure is, in this context, understood as an amount that may be lost if a counterparty fails to fulfill its obligations (defaults) within a certain time (taking into account the value of collaterals contributed thereby). Credit exposure is calculated as of the current day and is split into exposure due to payment (payment exposure) and replacement exposure.

The below figure presents credit exposure components.

Figure no. 66. Credit exposure components



Based on the exposure value and the evaluation of the financial standing of specific customers the credit risk value that TAURON Capital Group is exposed to is calculated using the Credit Value at Risk method. It is an analytical method that, based on the mathematical Monte Carlo simulation model, calculates the exposure value based on the total loss probability distribution.

3.4.4. Operational risk management

Operational risk is understood as a possibility to incur a loss due to inappropriate or unreliable internal procedures, human and system errors or as a consequence of external events. It also includes legal risk, reputational risk and non-compliance risk. Operational risk, due to the specific nature of the threats and the ability to manage them, constitutes a separate group of risks affecting TAURON Capital Group's operations. This risk is a complex issue, occurs in every process and type of operations, it is multi-dimensional and applies to various types of activities and operations. In particular, the exposure to the operational risk factors is related to the size and complexity of the organizational structure, the number and complexity of IT systems and to the number of business processes conducted. The operational risk is characterized by the lack of the ability to totally eliminate its sources, and the analysis of its factors and parameters (among others, frequency and severity), and also the evaluation thereof requires the use of complex measurement and analysis methods.

In order to effectively manage the operational risk TAURON Capital Group is using appropriate tools, presented on the below diagram. In particular, they include the operational risk profile, operational events database, global operational risk limit and the related system of operational limits and also the early warning system operating on a large scale.

The below figure presents risk management system tools.

Figure no. 67. Risk management system tools

Global operational risk limit is the basic tool for the operational risk control and represents the allocation of risk tolerance adopted by TAURON Capital Group. The global operational risk limit can be subsequently allocated to TAURON Capital Group's individual lines of business, the operational risk sub-categories as well as to the specific operational risks.

Operational risk profile is aimed at identifying areas, processes or activities with an excessive exposure to threats stemming from specific operational risk factors. Operational risk profile is expressed in particular in the structural dimension that includes types of operational events, TAURON Capital Group's organizational structure and processes, in the scale dimension that includes estimated potential losses, taking into account especially historical values of actual losses, as well as the tools used to mitigate the threats. For the needs of measuring the operational risk and defining the operational risk Profile the individual types of the operational risk are broken down (due to the nature of the occurrence thereof) into continuous and one-off risks.

Early warning system is defined in order to monitor the operational risk level for each identified threat. Early Warning Indicators (EWI) are selected from the Key Risk Indicators (KRI) set as the ones that are subject to continuous control with respect to the caution thresholds set for them, i.e. acceptance, mitigation and escalation thresholds.

Operational events database is created for the needs of identifying new risk factors, and in parallel in order to define the risk profile for TAURON Capital Group. It allows for keeping the records of cases that are characterized by a potential or actual loss for the organization. The goal of maintaining the operational events database is to determine the frequency and severity of the individual operational risk factors, as well as the areas and processes they occur in.

Risk identification questionnaire is a document in the form of a table form that constitutes a tool supporting the performance of the risk management process with respect to risk identification, specifying the detailed information that should be collected in this process.

3.4.5. Project risk management

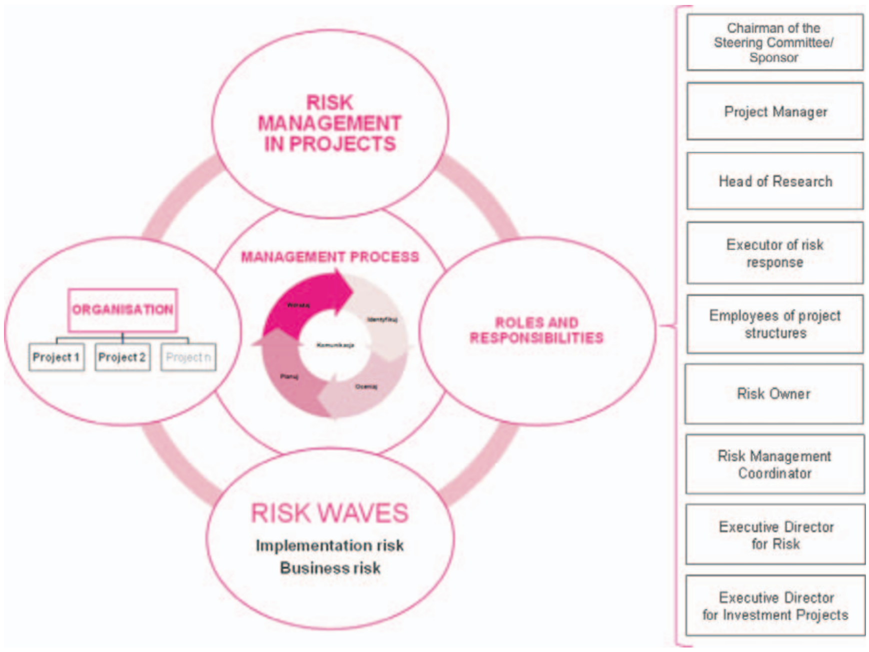
TAURON Capital Group is conducting a number of investment projects in many lines of its business operations. These projects, due to their scale and often very complicated nature of implementation, represent a source of threats that may have an impact on the schedule, budget or quality of the final products. Systematic use of the provisions of *TAURON Group's Project Risk Management Policy* is aimed at mitigating these risks, supporting at the same time the accomplishment of the organization's strategic goals. This regulation, in particular, defines the basic principles of project risk management, ensuring coherence, comprehensive approach and unequivocal understanding in this area. The goal of the actions taken is to achieve the required probability of the project's completion while complying with the defined schedule, budget and quality of the products received. The overall objective is to obtain the expected benefits from the project's completion and to achieve TAURON Capital Group's strategic goals.

Project risk management is also applicable to managing the risk stemming from the projects and having an impact on the organization. The process of managing the risk stemming from the projects includes identification, valuation of such risks, defining and monitoring early warning indicators as well as planning and implementing actions related to managing such risks. In case of risks having an impact on the organization the risk valuation is made as the absolute value of the impact including indicating the impact period broken down into individual accounting periods, in reference to the assumed EBITDA or the assumptions made in the organization for the long term projections. In case of the most important risks having an impact on the organization the Plans of reactions to the risk and back-up

Plans are developed. The evaluation of project risks and risks stemming from the projects for the organization is taken into account when making the key decisions related to launching and implementing such projects.

The below figure presents the project risk management model.

Figure no. 68. Project risk management model



3.5. Description of the most significant risks related to TAURON Capital Group's operations

The below table presents the most significant risks identified for TAURON Capital Group.

Table no. 21. Most significant risks identified for TAURON Capital Group

No.	Risk name	Risk description	Risk trend	Risk response
Finance and credit				
1.	Interest rate and FX rate risk	Risk related to an unfavorable impact of interest rates and FX rates on TAURON Capital Group's financial results.	→	• Ongoing monitoring of risk exposure in order to minimize negative impact of changes to the market factors, • Transfer of risk through the use of derivative instruments
2.	Liquidity / financing risk	Risk related to the manner of financing operations, due to the enterprise's capital structure.	→	• Diversification of the sources of financing including arranging guaranteed financing programs and securing alternative sources of financing. • Implementing the central financing policy. • Analyzing the market and the availability of the sources of financing. • Monitoring the schedules and the date of announcing the financing program.
3.	Credit risk	Risk related to a potential occurrence of overdue accounts payable or a conclusion of a contract with a counterparty that will turn out to be insolvent.	→	• Regular monitoring of the counterparties' financial standing. • Periodic customer scoring, credit rating of each customer prior to submitting an offer/concluding a contract. • Use of protection mechanisms (hedging) in commercial agreements.
Trade				
4.	Market risk	Risk related to an unfavorable change of prices on the electricity market and on the related products markets, having a negative impact on TAURON Capital Group's financial results.	↗	• Monitoring and updating the hedging strategy. • Ongoing monitoring of exposure to the above mentioned risk in order to minimize negative impact of changes to the market factors. • Limits (caps) on trade positions within risk mandates.

No.	Risk name	Risk description	Risk trend	Risk response
Workforce and organizational culture				
5.	Social dispute risk	Risk related to collective disputes, strikes, social conflicts being the consequence of a lack of the personnel's satisfaction with the economic and social situation.	→	• Conducting social consultations with respect to the planned changes. • Conducting a policy of dialogue with the workforce. • Preparing and implementing motivational solutions for the personnel. • Standardizing the tasks and requirements towards the personnel. • Developing organizational culture based on values. • Conducting active internal communications on personnel matters.
6.	Human resources risk	Risk related to the temporary or permanent loss of specialized staff and difficulties in its restoration.	↘	• Taking measures aimed at developing a model that would enhance workforce motivation • Developing competences by training the personnel.
7.	Occupational Health and Safety Risk	Risk related to accidents at work resulting from non-compliance with the Occupational Health and Safety as well as Fire Protection regulations	→	• Implementing manuals and rules defining safe organization of work. • Stimulating workforce development by conducting periodic Occupational Health and Safety and additional specialist training. • Analyzing and updating, based on needs, the evaluation of the professional risk at individual work stations (positions). • Maintaining a high standard of equipping the personnel with protection means and enforcing the appropriate use thereof. • Performing measurements of harmful factors in the work environment.
Customers and contractors				
8.	Customer service risk	Risk related to non-compliance with the customer service standards.	→	• Monitoring and analyzing external customer satisfaction indicators and indicators related to complaints. • Taking additional measures, e.g. with respect to internal regulations, defining standards of conduct as a result of the analysis of indicators. • Developing key account managers' competences and skills. • Continued raising of customer service standards.
9.	Risk related to performance of agreements by subcontractors	Risk related to improper performance by subcontractors of the works commissioned, termination of the agreement and delays, changes to the budget, scope related thereto	↘	• Concluding agreements with subcontractors in accordance with TAURON Capital Group's standards. • Analyzing the performance of the subject of the agreement, examining the quality of services provided by subcontractors. • Evaluating the financial standing and credibility of the subcontractors.
10.	Purchasing process risk	Risk related to the volatility of the situation on the supplies/services market, volatility of demand for the given type of product/supply/service on the market, decline of the availability of supplies/services of appropriate quality, leading to the purchase order value increase risk.	→	• Preparing a plan of purchase orders and updating thereof. • Aggregating purchases of selected product groups. • Consolidating purchase orders. • Concluding long term agreements. • Taking into account the price risk related to commodity prices/FX rate fluctuations in contracts with contractors
11.	Volume and margin risk	Unfavorable changes or terminations of commercial agreements by customers, leading to the declining revenue from operations; loss and lack of acquiring new customers.	↗	• Conducting marketing campaigns, acquiring new customers. • Taking actions focused on retaining the existing customers and recovering the lost ones. • Ongoing updating of the offering, launching sales of multi-package type products.

No.	Risk name	Risk description	Risk trend	Risk response
Compliance risk				
12.	Internal fraud risk	Appropriation or temporary use of the company's assets, destruction of TAURON Capital Group's property, abuse of work position to derive various types of personal gain by forcing specific behavior of customers while performing work related activities.	↘	• Strict adherence to internal procedures aimed at achieving protection against abuse (security procedures, reviews of authorizations). • Conducting compliance type activities. • Promoting best practices, improving procedures, training. • Enforcing and promoting the provisions of *TAURON Group's Code of Responsible Business in* force.
13.	External fraud risk	Third party actions aimed at, among others, theft, robbery, physical burglary, computer hacking, information theft, forgery.	↘	• Monitoring potential and actual security incidents. • Anti-virus protection of workstations. • Physical protection of facilities. • Conducting security tests.
14.	Risk of unethical behaviors	Risk related to the occurrence of behaviors not in line with the generally accepted by the society social coexistence rules, moral standards and lobbing.	↘	• Functioning of the whistleblowing system in the organization. • Lack of organizational culture based on TAURON Capital Group's values and principles. • Training, building awareness through meetings, TAURONET, press materials. • Functioning of Ethics Committees in the organization operating based on the adopted regulations.
15.	Legal risk	Risk related to non-compliance with the legal regulations, misinterpretation of the new provisions and regulations, court disputes (litigations), requirements imposed by URE/UOKiK/KNF/GIODO, etc.	→	• Continuous monitoring of the legal environment and changes to the legal regulations. • Implementing the required changes to internal regulations. • Appointing working groups tasked with preparing and implementing the required changes stemming from the legal environment. • Continuous cooperation with the authorities overseeing the energy market and the capital market. • Training for the personnel on the changes being introduced.
16.	Risk of breaching contractual provisions (default)	Risk related to the possibility of being in default in performing the obligations under agreements concluded with counterparties.	→	• Optimizing the sales and service processes. • Updating and adapting agreement samples to the changes to the law. • Monitoring complaints and proceedings of URE/UOKiK.
Environment				
17.	Reputational risk	Current and future impact on the company's revenue and capital due to the negative public opinion backlash.	→	• Continuous monitoring of the Company's external and internal threats. • Media monitoring, developing contacts and relationships with the media within TAURON Capital Group. • Preparing procedures for the Company's communications with the external and internal environment (stakeholders).
18.	Regulatory risk	Unfavorable impact of the domestic and European level legislation due to the need to pass or adapt to the legal regulations and to incur the required financial costs in order to comply therewith.	↗	• Continuous monitoring of the legal environment and changes to the regulations. • Analyzing draft legal acts and planning the required adaptation steps. • Implementing the required changes into internal regulations. • Cooperation with the regulator.
19.	License risk	No ability to conduct operations as a result of a prolonged process of obtaining a license or amending the licenses held. Unfavorable legal changes with respect to licensed operations.	→	• Ongoing control of the correct performance of licensing obligations. • Monitoring changes to the legal acts with respect to licensing obligations. • Legal support for the license extension and obtaining process.

No.	Risk name	Risk description	Risk trend	Risk response
Technology and infrastructure				
20.	Environmental risk	Potential negative impact of the operations on the environment and of non-alignment to and non-compliance with the environmental requirements of the domestic and community law.	→	• Ongoing supervision over compliance with the conditions of the environmental decisions. • Maintaining the required efficiency of the devices reducing the emission of pollutants. • Frequent evaluation of the compliance of actions with the legal requirements with respect to environment protection. • Implementing investment projects in environment protection in order to minimize the adverse impact of the mining and processing operations conducted.
21.	Weather risk	Impact of weather conditions on the operations of the enterprise, both with respect to technological aspects as well as the commercial ones.	→	• Upgrading (refurbishing) hydroelectric structures aimed at optimizing the utilization of water resources. • Preparing plans of overhauls, inspections and maintenance activities with flexible provisions on deadlines for completing the works. • Continuous monitoring of wind conditions and icing on the wind farms' blades. • Continuous technical oversight over the operation of individual wind farms, conducted by the companies operating the farms. • Monitoring and analyzing new technological solutions that reduce the impact of adverse weather conditions on the volume of electricity generated. • Increase in acquisitions and takeovers.
22.	Company asset failure risk	Impact of failures of machines and devices, overhauls, upgrades (refurbishments), maintenance and management of production and non-production assets on achieving the company's goals.	→	• Optimizing capital expenditures on asset replacements, ongoing monitoring of the condition of machines, devices and installations. • Raising professional qualifications and work culture of the personnel by organizing courses and training. • Responding to an emergency situation by the technical personnel and automatic process safety interlocks. • Insuring assets against fortuitous events (excluding underground assets). • Introducing IT tools with respect to improving the monitoring and managing failure indicators (ratios).
23.	IT risk	Risks related to the IT infrastructure security, failures of the IT infrastructure	↗	• Developing and maintaining plans aimed at ensuring continuity of IT infrastructure's operation. • Periodic identifying and categorizing IT resources based on the service restoration targets. • Use of IT solutions with appropriate technical parameters, providing an acceptable level of reliability and efficiency of operation (including also UPS devices, GSM modem, mobile phones). • Planning and conducting training on IT continuity. • Storing and protecting the back-up data.
24.	Asset security and protection risk	Risk related to compromising the integrity of machines/devices and to the security of information, including its improper processing and unauthorized disclosure.	↘	• Monitoring the implementation of the developed plans to protect the facilities that are subject to mandatory protection. • Maintaining and updating contingency procedures/plans. • Implementing/updating and oversight over compliance with the information security rules in force. • Regular personnel training with respect to security procedures in force.
25.	Geological risk	Impact of geological factors on the mining operations.	↗	• Making test drillings for the better intelligence on the positioning of coal deposits. • Continuing to take preventive measures in areas under threat in order to improve the geological and mining conditions and to provide protection against natural threats (including, among others, long-drilled blasting hole shooting in order to break the rock mass)

4. ANALYSIS OF TAURON CAPITAL GROUP'S FINANCIAL POSITION AND ASSETS

4.1. Overview of economic and financial data disclosed in the consolidated annual financial statements

Consolidated statement of financial position

The below table presents the annual consolidated statement of financial position – **assets**.

Table no. 22. Annual consolidated statement of financial position – assets (material items)[1]

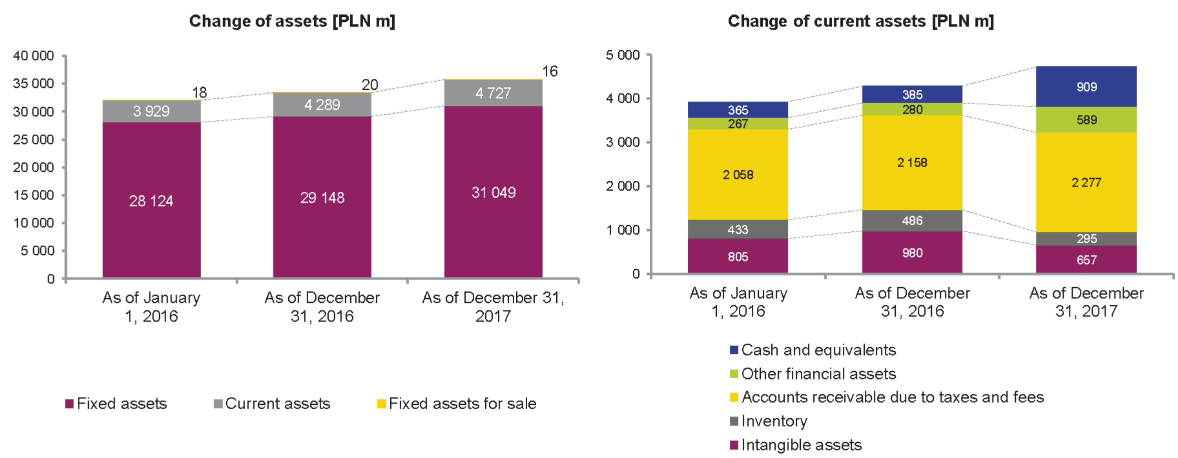
Statement of financial standing (PLN thous.)	As of December 31, 2017	As of December 31, 2016	As of 1 January 2016	Change in % (2017/2016)
ASSETS				
Fixed assets	**31 049 127**	**29 148 253**	**28 124 185**	**107%**
Tangible fixed assets	28 079 886	26 355 189	24 882 817	107%
Current assets	**4 742 894**	**4 308 641**	**3 947 248**	**110%**
Cash and equivalents	909 249	384 881	364 912	236%
Fixed assets and assets of TAURON Capital Group for disposal, classified as held for sale	15 910	19 612	17 898	81%
TOTAL ASSETS	**35 792 021**	**33 456 894**	**32 071 433**	**107%**

[1] *Due to the limited comparability of earlier periods, data is presented in a three-year horizon. Data comprising earlier periods are presented in section no. 4.6 of this report.*

As of 31 December 2017 the statement of the financial position of TAURON Capital Group indicates the balance sheet total higher by approx. 7%.

The below figure presents the change in the level of assets and current assets.

Figure no. 69. Change in the level of assets and current assets



In the year ended on December 31, 2017 TAURON Capital Group, having taken into account the following premises:

1) long-term maintaining of the market value of Company's net assets at a level below the balance sheet carrying amount,
2) changes to the commodity prices on the worldwide markets and a change of the situation on the domestic thermal coal market following the consolidation of the mining sector,
3) amendments to the RES law and publishing of the RES obligations for 2018 and 2019, that impacted the prices of the certificates of origin for electricity generated from renewable sources,
4) passing of the capacity market law and proceeding with the functional solutions described in the draft capacity market regulations,
5) continuing unfavourable market conditions in terms of profitability of coal-based power industry,
6) increase in risk-free rate,

recognized (booked) impairment write-offs and the reversal of previously booked write-downs related to tangible fixed assets as a result of impairment tests, conducted as of December 31, 2017 and June 30, 2017. Results of the conducted tests indicated that a part of assets of the Generation Segment should be covered by an additional write-down in the amount of PLN 658.7 mln. The conducted test has also confirmed the legitimacy to reverse the write-downs in this Segment in the amount of PLN 628.2 million.

The sensitivity analysis for individual units generating cash flows indicated that the factors most significantly influencing the useful value of the assets tested are related to:

1) capacity market with the other market conditions unchanged,
2) changes in electricity prices,
3) changes in hard coal prices.

The change in the prices of CO_2 emission allowances and changes of the average weighted cost of capital have a lower impact on the valuation.

The value of tangible fixed assets increased by PLN 1 906 million (6.5%), which is the resultant of the following events:

1) increase in the value of tangible fixed assets as a result of investments in tangible fixed assets underway at TAURON Capital Group's subsidiaries (mainly at TAURON Dystrybucja, TAURON Wytwarzanie, Nowe Jaworzno GT and TAURON Ciepło) and intangible assets (mainly TAURON Dystrybucja),
2) purchase of property rights to the certificates of origin of electricity and greenhouse gases emission allowances in connection with the requirement to fulfil the legal obligation of their redemption.

The following factors had an impact on the increase in the value of current assets by approximately PLN 434 mln (10.1%):

1) increase of the level of cash and equivalents by PLN 524 mln which was more extensively described in the section on the cash flow account,
2) increase of the value of loans granted for joint ventures by approx. PLN 315 mln, due to the agreement signed between TAURON and ECSW,
3) increase of the value of accounts receivable from the consumers by PLN 139 mln,
4) increase in the value of other financial assets by PLN 92 mln mainly due to the purchase of investment fund units in 2017,
5) decline of the value of certificates of origin of electricity and greenhouse gas emission allowances to be redeemed by PLN 324 mln as a result of the fulfilment of the obligation to redeem certificates of origin of electricity and CO_2 emission allowances and an increase of their level in conjunction with the production and acquisition of the property rights due to the current year's obligation,
6) decrease of the inventory value by PLN 191 mln, mainly due to the sale of TAURON Wydobycie's coal inventory and the consumption of coal by the Generation Segment's companies,
7) decrease of the value of the other non-financial assets by PLN 98 mln, mainly due to recognizing in 2016 of advance payments towards the supplies by TAURON Capital Group's subsidiaries.

The below table presents the annual consolidated statement of financial position – **liabilities**.

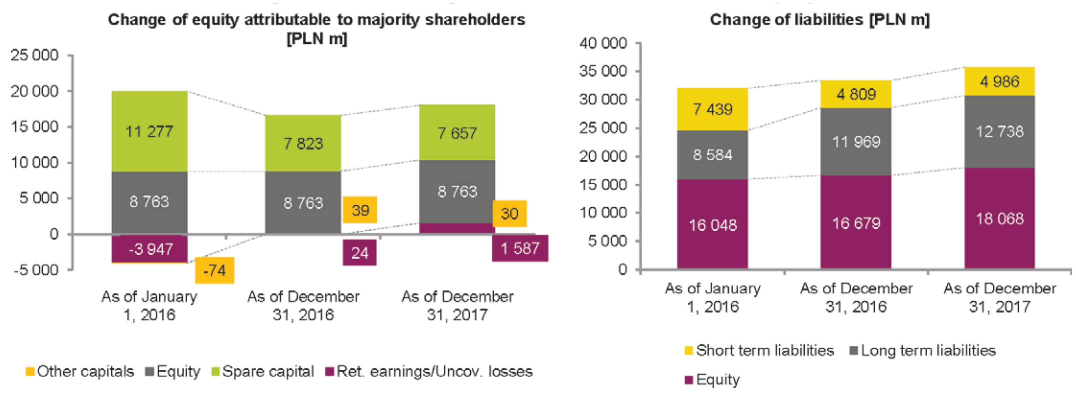
Table no. 23. Annual consolidated statement of financial position – liabilities (material items)[1]

Statement of financial standing (PLN thous.)	As of 31 December 2017	As of 31 December 2016	As of 1 January 2016	Change in % (2017/2016)
LIABILITIES				
Equity attributable to shareholders of the parent entity	**18 036 446**	**16 649 266**	**16 018 328**	**108%**
Non-controlling shares	31 367	30 052	29 829	104%
Long-term liabilities	**12 738 005**	**11 968 719**	**8 583 950**	**106%**
Loans, credits and debt securities	9 501 414	8 759 789	4 924 127	108%
Short-term liabilities	**4 986 203**	**4 808 857**	**7 439 326**	**104%**
Current portion of credits, loans and debt securities	351 382	219 740	3 214 520	160%
TOTAL LIABILITIES	**35 792 021**	**33 456 894**	**32 071 433**	**107%**

[1] *Due to the limited comparability of earlier periods, data are presented in a three-year horizon. Data comprising earlier periods are presented in section no. 4.6 of this report.*

The below figure presents the change in the level of liabilities and equity

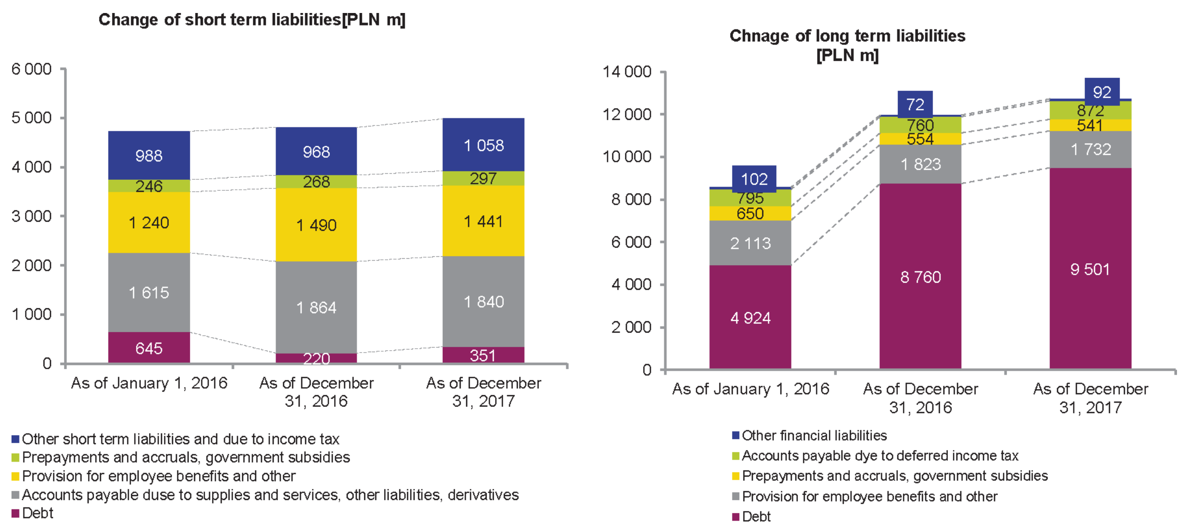
Figure no. 70. Change in the level of liabilities and equity



Similar to the previous years, in 2017 the dominating source of assets financing was equity whose share in the total liabilities reached 50.5%.

The below figure presents the change in the level of liabilities.

Figure no. 71. Change in the status of liabilities



The following factors had an impact on the increase in the value of TAURON Capital Group's long-term liabilities by PLN 769 PLN m (6%):

1) increase of the liabilities due to debt by 8% as a result of issue of eurobonds on July 5, 2017 with the total nominal value of EUR 500 million and the issuing price of 99.438% of the nominal value and the maturity of 10 years,
2) increase of the liabilities due to the deferred income tax by PLN 112 mln which is the effect of setting up a liability due to a different moment of recognizing for tax purposes of the revenue from products and services sales,
3) decrease of the value of provisions due to the costs of dismantling the fixed assets and recultivation of the land and other by PLN 98 mln which is related to dissolving the provision for the costs related to the electricity sale agreement and the provision for the covering of the potential losses in conjunction with the enforcement of the "take or pay" contractual clause, as a result of the fuilfilment of the suspending conditions stemming from the contingent agreement signed on October 27, 2016 on establishing the basic boundary conditions of the restructuring of the "Construction of the CCGT unit at Stalowa Wola" project. Meanwhile as a result of updating of the provision for the liquidation of coal mines in conjunction with the change of the discount rate this balance sheet item increased.

The value of short-term liabilities of TAURON Capital Group increased by PLN 177 million (4%), which resulted from the following factors:

1) increase due to debt by PLN 132 mln,
2) increase of accounts payable towards suppliers by PLN 213 mln and decrease of the value of capex obligations by PLN 237 mln,

3) slight drop, by approx. 1%, of the value of provisions, which is the resultant of using the provision set up in 2016 on the account of fulfilling of the obligation to present the certificates of electricity origin for redemption, due to the regulations of the *act of April 10, 1997 Energy law*, and the CO_2 emission allowances, and setting up of the provision on the account of fulfilling of the 2017 obligations.

Consolidated statement of comprehensive income

The below table presents the annual consolidated statement of comprehensive income. Due to the changes in the Segments and in order to maintain the comparability, the results are presented for three years.

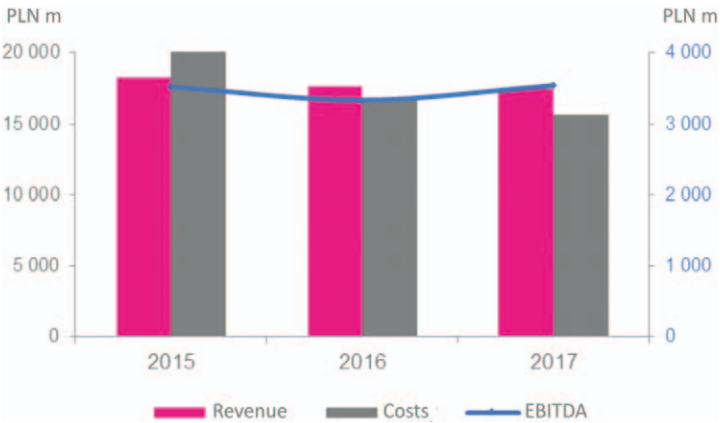
Table no. 24. Annual statement of comprehensive income for 2015–2017[1]

Statement of comprehensive income (PLN thous.)	2017	2016	2015	Change in % 2017/2016)
Sales revenue	**17 416 029**	**17 646 489**	**18 264 440**	**99%**
Own cost of sales (including sales costs and overheads)	(15 605 679)	(16 829 480)	(20 137 894)	93%
Other operating revenues and costs	(4 079)	(15 487)	(27 762)	26%
Operating profit (loss)	**1 806 271**	**801 522**	**(1 901 216)**	**225%**
Operating profit margin (%)	*10,4%*	*4,5%*	*(10,4)%*	*228%*
Financial revenue	190 968	65 279	73 185	293%
Financial expenses	(312 637)	(417 980)	(367 673)	75%
Share in the profit (loss) of joint venture	73 050	60 040	7 933	122%
Gross profit (loss)	**1 757 652**	**508 861**	**(2 187 771)**	**345%**
Gross profit margin (%)	*10,1%*	*2,9%*	*(12,0)%*	*350%*
Income tax	(374 706)	(138 724)	383 556	270%
Net profit (loss) for financial year	**1 382 946**	**370 137**	**(1 804 215)**	**374%**
Net profit margin (%)	*7,9%*	*2,1%*	*(9,9)%*	*381%*
Other comprehensive income for financial year, post tax	6 366	277 748	122 076	2%
Total income for financial year	**1 389 312**	**647 885**	**(1 682 139)**	**214%**
Profit attributable to:				
Shareholders of the parent entity	**1 380 663**	**367 468**	**(1 807 317)**	**376%**
Non-controlling shares	2 283	2 669	3 102	86%
EBIT and EBITDA				
EBIT	**1 806 271**	**801 522**	**(1 901 216)**	**225%**
EBITDA	**3 544 591**	**3 336 814**	**3 523 228**	**106%**

[1] *Due to the limited comparability of earlier periods, data are presented in a three-year horizon. Data comprising earlier periods are presented in section no. 4.6 of this report.*

The below figure presents TAURON Capital Group's 2015–2017 financial results.

Figure no. 72. TAURON Capital Group's 2015–2017 financial results

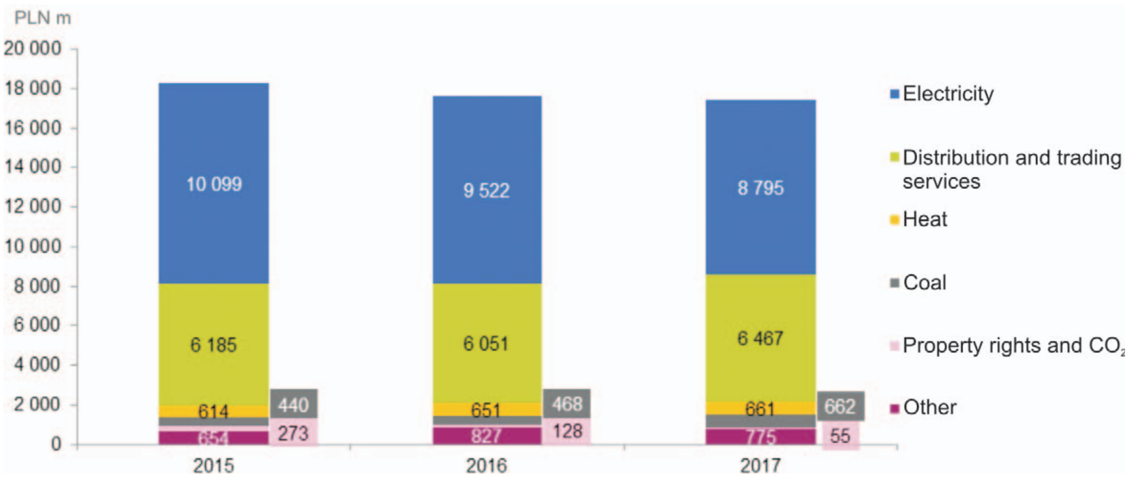


In the reporting period ended on December 31, 2017, TAURON Capital Group generated sales revenue lower by 1.3% as compared to the values achieved in 2016, due to the following factors:

1) lower revenue from electricity sales – higher electricity retail sales volume and lower wholesale volume, with lower electricity sales prices,
2) higher revenue from heat sales – higher heat sales and transmission services volume and higher rate for the transmission services,
3) lower revenue from electricity origin property rights sales, mainly due to a substantial decline of PMOZE market prices,
4) higher revenue from distribution services sales, due to an increase of the distribution service sales volume (by 4%) and the rate for the distribution services delivered to the final consumers,
5) higher revenue from coal sales due to an increase of coal sales volume (by 34%) – greater demand from the consumers and higher coal sales price.

The below figure presents the structure of TAURON Capital Group's revenue in 2015–2017.

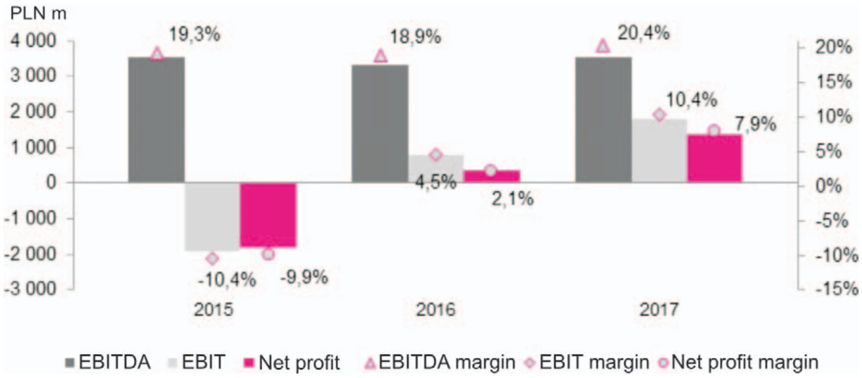
Figure no. 73. Structure of TAURON Capital Group's revenue in 2015–2017[1]



[1] *The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Operational Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

The below figure presents TAURON Capital Group's financial results and the level of margins realized.

Figure no. 74. TAURON Capital Group's financial results and the level of margins realized in 2015–2017[1]



[1] *The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Operational Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

In 2017 TAURON Capital Group's costs of operations reached PLN 15.6 bln, which meant that they were 7.3% lower than the costs incurred in 2016.

On of the reasons for the cost decline was the booking, in 2016, of the write-downs due to the loss of the carrying amount of the Generation Segment's generating units.

The impairment tests, conducted as of December 31, 2017 and June 30, 2017, for the tangible fixed assets, taking into account the premises related to the assets' net market value, changes of the commodity prices on the worldwide markets, changes of the thermal coal prices on the domestic market, changes of the RES law and publishing of the RES obligations fo 2018 and 2019, as well as passing of the capacity market law, proved the legitimacy of booking the impairment charges and of reversing the earlier booked write-downs related to the tangible fixed assets in the amount of PLN 0.03 bln:

- net value of the booked write-downs (i.e. the excess of the reversed write-downs versus the booked write-downs) related to the wind farms and hydroelectric power plants: PLN 0.04 bln,
- net value of the reversed write-downs (i.e. the excess of the reversed write-downs versus the booked write-downs) related the generation assets in the electricity and heat generation line of business: PLN 0.01 bln.

Apart from the aforementioned one-off events the level of TAURON Capital Group's costs in 2017 was impacted by the following factors:

1) decline of the costs of purchasing electricity, mainly due to the lower volume of electricity (wholesale) sold,
2) increase of the costs of the distribution service, mainly due to the increase of the volume of electricity transferred,
3) increase of the costs of maintenance of devices, overhaul services and the other services,
4) increase of the costs of taxes, mainly the real estate tax,
5) increase of the labor costs as a result of setting up a provision related to the one-off bonus in conjunction with the agreement signed with the workforce (social party),
6) decline of the cost of the redeemed property rights due to the reduction of their price,
7) sale of the inventory coal due to the rising demand (increase of the coal sales by 34%).

EBITDA margin achieved in 2017 was 20,4% and it was 7.6% higher than in 2016. As a result of the write-downs booked, the value of which in 2016 was much higher than the write-downs in 2017, EBIT margin and net profit margin were significantly higher in the reporting period than a year ago, reaching 10.4% and 7.9%, respectively. Should the effects of the impairment charges be disregarded, EBIT margin and net profit margin would reach in 2017, respectively, 10.5% and 8.1%, and in 2016, respectively, 9.0% and 5.8%.

In accordance with the presented consolidated statement of comprehensive income, the total comprehensive income of TAURON Capital Group for 2017, taking into account the net profit increased or decreased by the change in the value of hedging instruments, FX differences arising from the conversion of the foreign entity and the other revenue after tax, reached PLN 1 389.3 mln in 2017, versus PLN 647.9 million generated in 2016, while the net profit attributable to the shareholders of the parent entity reached PLN 1 380.7 mln versus PLN 367.5 million posted in 2016.

Statement of cash flows

The below table presents the statement of cash flows

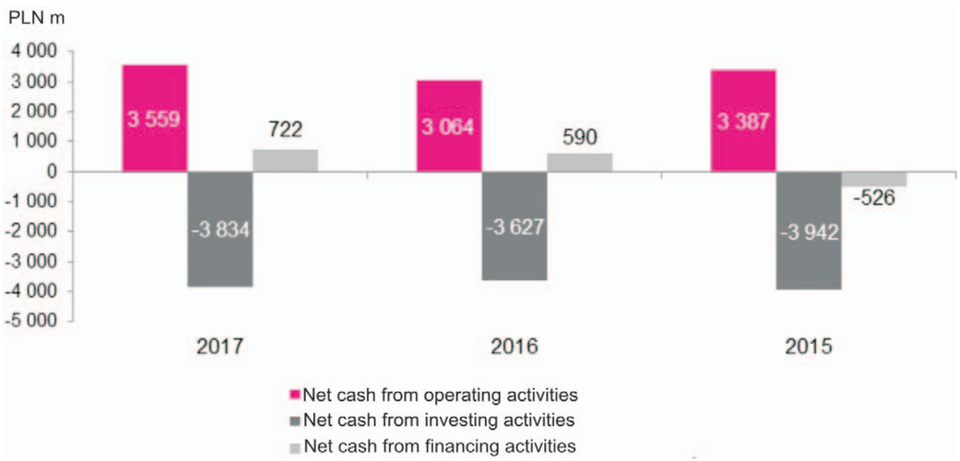
Table no. 25. Statement of cash flows (significant items) in 2015–2017[1]

Statement of Cash Flows (PLN thous.)	Year ended 31.12.2017	Year ended 31.12.2016	Year ended 31.12.2015	Change in % (2017/2016)
Cash flows from operating activities				
Gross profit/(loss)	1 757 652	508 861	(2 187 771)	345%
Adjustments	1 801 015	2 555 354	5 575 229	70%
Net cash from operating activities	**3 558 667**	**3 064 215**	**3 387 458**	**116%**
Cash flows from investing activities				
Purchase of tangible fixed assets and intangible assets	(3 561 758)	(3 516 296)	(3 973 510)	101%
Net cash from investing activities	**(3 871 676)**	**(3 627 458)**	**(3 942 122)**	**106%**
Cash flows from financing activities				
Cash inflows due to loans/credits	(1)	914	295 000	–
Repayment of loans/credits	(154 918)	(140 331)	(140 585)	110%
Issue of debt securities	2 707 462	4 284 607	310 000	63%
Redemption of debt securities	(1 650 000)	(3 300 000)	(450 000)	50%
Net cash from financing activities	**759 629**	**590 261**	**(525 692)**	**122%**
Increase/(decrease) in net cash and equivalents	**446 620**	**27 018**	**(1 080 356)**	**1 653%**
Cash opening balance	**354 733**	**327 715**	**1 408 071**	**108%**
Cash closing balance	**801 353**	**354 733**	**327 715**	**226%**

[1] *Due to the limited comparability of earlier periods, data are presented in a three-year horizon. Data comprising earlier periods are presented in section no. 4.6 of this report.*

The below figure presents the 2017–2015 cash flows.

Figure no. 75. 2017–2015 cash flows



The realized positive value of cash flows from operating activities in 2017 was higher than the cash flow realized in the previous year by PLN 494 million. The following factors had the biggest impact on the change in this item of the cash flow account:

1) reduction of the inventory level as a result of higher coal sales, which is related to increased demand for the extracted coal PLN +244 mln,
2) income tax payment lower by PLN 252 mln, which is due to advance payments made by the Tax Capital Group in 2017 on the account of the 2017 income tax, in the amount of PLN 216 million, while in 2016 the Tax

Capital Group made advance payments on the account of the income tax in the amount of PLN 301 million and paid the 2015 income tax in the amount of PLN 89 million. In addition, TAURON Capital Group received in the reporting period the refund of the overpaid 2016 income tax in the amount of PLN 79 million,

3) negative change of accounts receivable and accounts payable in the amount of PLN 49 million,
4) incurring of a lower expenditure in the total amount of PLN 38 million to purchase the certificates of origin and a lower substitution fee in the 2017 reporting period than in 2016.

The biggest impact on cash flows from investing activities came from the expenditures to purchase tangible fixed assets, which in the reporting period were higher by 1% than the expenditures incurred in 2016. The larges expenditures were incurred by the Generation and Distribution Segments.

The positive value of cash flows from financing activities is due to the bond issues completed in 2017 worth PLN 2 707 mln in total, including the EUR 500 mln eurobond issue. At the same time TAURON Capital Group redeemed the bonds issued and repaid credits and loans in the total amount of PLN 1 805 mln.

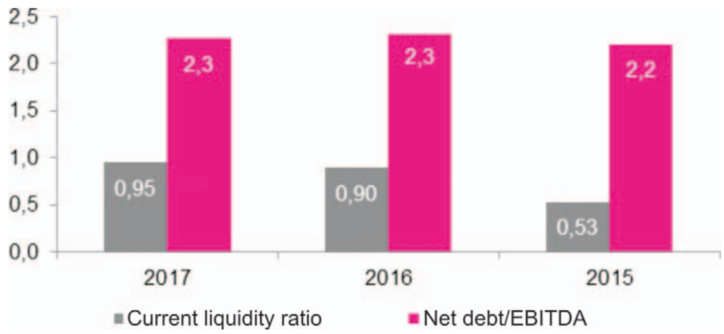
On the other hand in 2016 TAURON Capital Group issued bonds with the total nominal value of PLN 4 285 mln, redeemed the bonds issued in the previous years with the total nominal value of PLN 3 330 mln and repaid credits and loans taken in the previous years in the total amount of PLN 140 mln.

The value of financial expenses due to paid interest on financial liabilities amounted to PLN 185 million in 2017 and it was lower by 28% year on year.

TAURON Capital Group is continuing its expansion process and keeps strengthening its market position. It should be noted that the balance of cash flows from operating activities is positive, consequently enabling TAURON Capital Group to autonomously finance its ongoing operations. The current liquidity ratio and the net debt to EBITDA ratio remain at a safe level.

The below figure presents the current liquidity ratio and the net debt to EBITDA ratio in 2017–2015.

Figure no. 76. The current liquidity ratio and the net debt to EBITDA ratio in 2017–2015



4.2. Characteristics of the structure of assets and liabilities on the consolidated balance sheet

Structure of the annual consolidated statement of financial position

The below table shows the structure of the annual consolidated statement of financial position.

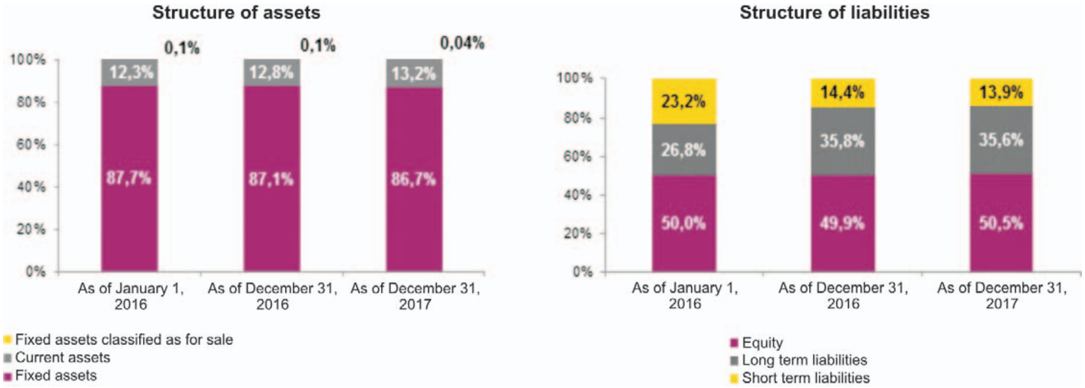
Table no. 26. Structure of the annual consolidated statement of financial position

Consolidated statement of financial position	As of 31 December 2017	As of 31 December 2016	As of 1 January 2016
ASSETS			
Fixed assets	**86,7%**	**87,1%**	**87,7%**
Current assets	**13,3%**	**12,9%**	**12,3%**
TOTAL ASSETS	**100,0%**	**100,0%**	**100,0%**
LIABILITIES			
Equity attributable to shareholders of the parent entity	50,4%	49,8%	49,9%
Non-controlling stakes	0,1%	0,1%	0,1%
Total equity	**50,5%**	**49,9%**	**50,0%**

Consolidated statement of financial position	As of 31 December 2017	As of 31 December 2016	As of 1 January 2016
Long-term liabilities	35,6%	35,8%	26,8%
Short-term liabilities	13,9%	14,4%	23,2%
Total liabilities	**49,5%**	**50,1%**	**50,0%**
TOTAL LIABILITIES	**100,0%**	**100,0%**	**100,0%**
Financial liabilities	9 059 844	8 138 506	8 138 647
Net financial liabilities	8 042 225	7 703 602	7 763 963

The below figure presents the structure of assets and liabilities.

Figure no. 77. Structure of assets and liabilities



As of December 31, 2017, similar as in 2016, the value of fixed assets represents the largest share in the structure of assets. In the structure of fixed assets, the tangible fixed assets of the following Segments represent the largest share: Distribution (57.9%), Generation (31.7%) and Mining (6.2%).

As of December 31, 2017, equity and financial liabilities represent the largest share in the structure of liabilities.

The level of debt of TAURON Capital Group remains at a safe level, which is indicated by the value of the leverage ratio, as compared to the European benchmarks for the sector, and the positive cash flows from operating activities.

4.3. Material off-balance sheet items

As of December 31, 2017, material contingent liabilities of TAURON Capital Group were related to:

1) lawsuits against PEPKH, TAURON as well as PEPKH and TAURON associated with the termination of long-term contracts by PEPKH,
2) termination of long-term contracts on purchasing property rights by TAURON Sprzedaż,
3) potential claims not reported by owners of land with unregulated status due to the lack of detailed records of unregulated land and the resulting inability to reliably estimate the amount of potential claims, and as a consequence, lack of a possibility to create provisions,
4) proceedings initiated on September 17, 2013 by the President of UOKiK against TAURON Sprzedaż in connection with the suspected use of practices violating the collective interests of consumers, by providing electricity prices in price lists and information materials without including the value added tax, which constitutes the infringement of the *Act of 23 August 2007 on prevention of unfair market practices*,
5) anti-monopoly proceedings initiated by the President of UOKiK pursuant to the decision of October 15, 2015, in connection with suspected use of measures by TAURON Sprzedaż in relation to small hydroelectric power plants, consisting in imposing unfair purchase terms by the entrepreneur in relation to electricity generated in renewable energy sources and making the purchase of this energy dependent on the need to settle the obligation of trade balancing, which may constitute the infringement of the provisions of the *Act of 16 February 2007 on the protection of competition and consumers,*
6) proceedings initiated on October 13, 2017 in conjunction with the suspected applying by TAURON Sprzedaż and TAURON Sprzedaż GZE of a practice violating the collective interests of consumers involving hindering a switch of an electricity supplier,

7) clarification proceedings conducted by the President of UOKiK against TAURON Sprzedaż and TAURON Sprzedaż GZE,
8) administrative proceedings initiated by the President of ERO against TAURON Dystrybucja concerning imposing of a fine due to the failure to maintain facilities, equipment and installations in due technical condition and the violation of the terms defined in the license,
9) administrative proceedings initiated by the President of ERO against TAURON Sprzedaż and TAURON Sprzedaż GZE with respect to the following matters: non-compliance with the obligation to obtain and present for redemption to the President of ERO of the energy efficiency certificates and imposing of a fine for a violation involving unjustified halting of the supply of electricity to the final consumers,
10) court dispute between TAURON as a legal successor of Górnośląski Zakład Elektroenergetyczny S.A (GZE) and Huta Łaziska S.A. as a result of the failure of Huta Łaziska S.A. to fulfil the obligation to pay the accounts payable for electricity supplies, which consequently caused the halting of electricity supplies to Huta Łaziska S.A. by GZE in 2001; the claim for the payment of damages is PLN 182 060 thou. plus interest,
11) lawsuit brought by ENEA against TAURON as well as TAURON Sprzedaż and TAURON Sprzedaż GZE (as third party respondents (defendants)) due to alleged unjustified benefit gained by the Company in connection with the settlements of imbalancing on the Balancing Market, made with PSE (TSO) in the period from January to December 2012; the claim for payment by TAURON amounts to PLN 17 086 thousand, in case the lawsuit against TAURON is dismissed, the claim for payment by TAURON Sprzedaż and TAURON Sprzedaż GZE amounts to PLN 8 414 thou. including interest,
12) registered pledge and financial lien on TAMEH HOLDING shares, established by TAURON in favour of RAIFFEISEN BANK INTERNATIONAL AG in order to hedge transactions comprising the agreement for term and working capital loans, concluded between TAMEH Czech and TAMEH POLSKA, TAMEH HOLDING as well as RAIFFEISEN BANK INTERNATIONAL AG,
13) value of the real estate tax imposed on devices used for generation and transmission of electricity as well as equipment of underground mining headings,
14) claim against TAURON Wydobycie related to the refund of the expenditures incurred to protect a facility against the impact of mining operations in the amount of PLN 22 785 thou.

The detailed information concerning off-balance sheet items is included in notes 47 and 48 of the Consolidated financial statements for the year ended on December 31, 2017.

4.4. Differences between the financial results reported in the annual report and the forecasts of results for the given year published earlier

The Management Board of the Company did not publish any forecasts of the earnings of TAURON Capital Group for 2017. This decision was due to the considerable volatility of the market and a substantial number of factors affecting its predictability.

4.5. Key financial and non-financial ratios

Financial ratios

The below table presents key financial ratios of TAURON Capital Group.

Table no. 27. TAURON Capital Group's key financial ratios[1]

Ratios	Definition	2017	2016	2015
PROFITABILITY				
EBIT Margin	Operating profit / Sales revenue	**10.4%**	4.5%	(10.4)%
EBITDA Margin	EBITDA/ Sales revenue	**20.4%**	18.9%	19.3%
Net Profitability	Net profit/ Sales revenue	**7.9%**	2.1%	(9.9)%
Return on Equity (ROE)	Net profit/ Equity at the end of the period	**7.7%**	2.2%	(11.2)%
LIQUIDITY				
Current liquidity ratio	Current assets (excluding assets held for trade) / Short-term liabilities	**0.95**	0.90	0.53
DEBT				
Total debt ratio	Total obligations/ total liabilities	**0.50**	0.50	0.50
Net financial debt/ EBITDA	(Financial liabilities - Cash)/ EBITDA	**2.3x**	2.3x	2.2x
OTHER RATIOS				
Earnings per share (EPS)	Net result attributable to shareholders of the parent entity / Number of ordinary shares	**0.79**	0.21	(1.03)

[1] *Due to the limited comparability of earlier periods, data are presented in a three-year horizon. Data comprising earlier periods are presented in section no. 4.6 of this report.*

In 2017 the net profitability ratio of TAURON Capital Group was higher than last year, as a result of recognising of the balance of impairment charges related to the generation assets of the Generation Segment in 2016 in the amount higher than in 2017. Due to the differences in the values of the write-downs these ratios are not comparable. Disregarding the write-downs, the 2017 net profitability ratio reached 8.1% in 2017 and 5.8% in 2016.

The current liquidity ratio reached, as of December 31, 2017, a value slightly higher than that as of December 31, 2016, which confirms a stable financial position of TAURON Capital Group.

The total debt ratio and the net debt/EBITDA ratio reflect the share of liabilities in TAURON Capital Group's financing. The current level of this ratio enables TAURON Capital Group to acquire external financing required to implement the investment projects planned. The levels of both ratios confirm a stable financial position of TAURON Capital Group, and a slight rise of the net debt was offset by the increase of EBITDA which allowed for maintaining the ratio at the same level as at the end of 2016.

EPS ratio (calculated in relation to net profit attributable to shareholders of the parent entity) is higher in 2017 than in 2016 due to recognizing the balance of the impairment charge related to the tangible fixed assets in the amount higher than the amount recognized in 2017.

Non-financial ratios (indicators)

The non-financial ratios (indicators) in TAURON Capital Group are closely associated with the specific nature of its operations, its resources and the adopted Strategy, including:

1) assessment of investment opportunities,
2) methods of human resources management,
3) risk optimization,
4) customer satisfaction surveys (polls),
5) centralizing of governance (management) functions at TAURON Capital Group, limiting the non-core operations,
6) development of organizational structures and management procedures.
7) Process management and implementation of the PRO values (Partnership – Development – Courage).

The description of the monitoring of the implementation (performance) of the above mentioned indicators (ratios) is provided in the individual sections of the report, while the summary of the key non-financial efficiency indicators (ratios) associated with the operations of TAURON Capital Group is provided in section 8.2. of this report.

4.6. Most significant financial and operating data of TAURON Capital Group for the last 5 years

The below table presents the most significant financial data and operating data of TAURON Capital Group for the last 5 years, i.e. for the 2017–2013 period.

Table no. 28. Financial and operating data for 2017–2013[1]

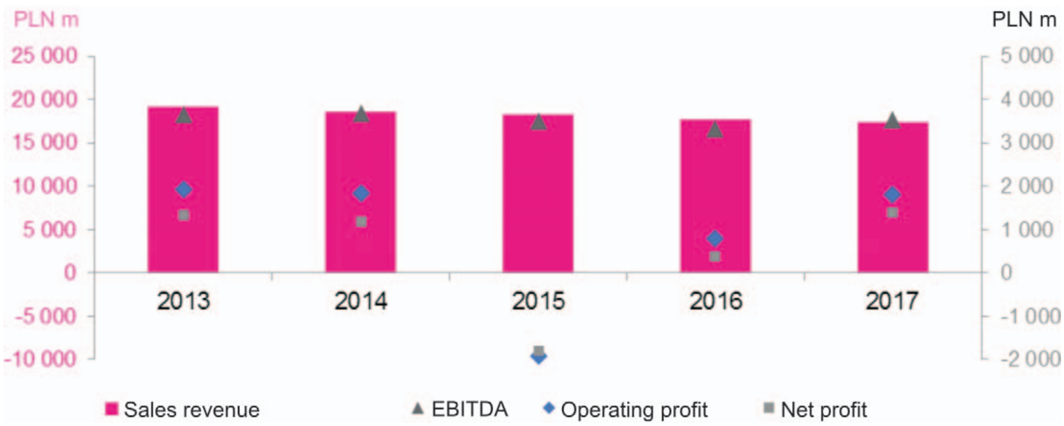
Key information	Unit	2017	2016	2015	2014	2013	% change (2017/2016)
Statement of comprehensive income							
Sales revenue	*PLN m*	**17 416**	17 646	18 264	18 577	19 131	99%
Operating profit	*PLN m*	**1 806**	802	(1 901)	1 830	1 934	225%
Financial revenue (total)	*PLN m*	**264**	125	81	86	99	211%
Financial expenses (total)	*PLN m*	**(313)**	(418)	(368)	(418)	(347)	75%
Gross profit	*PLN m*	**1 758**	509	(2 188)	1 498	1 684	345%
Income Tax	*PLN m*	**(375)**	(139)	384	(313)	(337)	270%
Net profit	*PLN m*	**1 383**	370	(1 804)	1 186	1 346	374%
attributable to shareholders of the parent entity	*PLN m*	**1 381**	367	(1 807)	1 181	1 308	376%
attributable to non-controlling shares	*PLN m*	**2**	3	3	5	38	86%
EBITDA	*PLN m*	**3 545**	3 337	3 523	3 695	3 661	106%
Statement of financial position							
Fixed assets	*PLN m*	**31 049**	29 148	28 124	28 163	27 567	107%
Current assets	*PLN m*	**4 743**	4 309	3 947	6 396	4 789	110%
Total equity	*PLN m*	**18 068**	16 679	16 048	17 997	17 793	108%
Total liabilities	*PLN m*	**17 724**	16 778	16 023	16 563	14 562	106%
Long-term liabilities	*PLN m*	**12 738**	11 969	8 584	11 744	9 304	106%
Short-term liabilities	*PLN m*	**4 986**	4 809	7 439	4 819	5 258	104%
Net financial debt**	*PLN m*	**8 042**	7 704	7 764	6 665	5 227	104%
Net financial debt[2]	*PLN m*	**8 944**	7 730	7 764	6 665	5 227	116%
Capital expenditures	*PLN m*	**3 474**	3 817	4 175	3 090	3 780	91%
Cash flow account							
Net cash from operating activities	*PLN m*	**3 559**	3 064	3 387	2 618	4 079	116%
Net cash from investing activities	*PLN m*	**(3 834)**	(3 627)	(3 942)	(3 387)	(4 180)	106%
Net cash from financing activities	*PLN m*	**722**	590	(526)	1 636	(249)	122%
Cash closing balance	*PLN m*	**801**	355	328	1 408	541	226%
Ratios							
EBIT Margin	%	**10,4**	4,5	(10,4)	9,9	10,1	228%
EBITDA Margin	%	**20,4**	18,9	19,3	19,9	19,1	108%
Net financial debt/ EBITDA	*number*	**2,27**	2,31	2,20	1,80	1,43	98%
Net earnings per share	*PLN/ share*	**0,79**	0,21	(1,03)	0,67	0,75	377%
Dividend per share	*PLN/ share*	**–**	–	0,15	0,19	0,20	–

Key information	Unit	2017	2016	2015	2014	2013	% change (2017/2016)
Operating data							
Commercial coal production	*mln Mg*	**6,45**	6,37	4,91	5,40	5,45	101%
Gross electricity production	*TWh*	**18,41**	16,80	18,56	17,35	21,72	110%
Electricity production from RES	*TWh*	**1,30**	1,32	1,63	1,82	1,39	98%
Heat production	*PJ*	**12,20**	11,52	11,51	13,41	15,62	106%
Retail sales of electricity	*TWh*	**34,91**	32,04	35,94	36,43	41,30	109%
Distribution of electricity	*TWh*	**51,37**	49,68	49,20	47,90	47,90	103%
Number of customers (Distribution)	*mln*	**5,53**	5,47	5,42	5,38	5,33	101%

[1] *The values presented do not reflect the values compliant with the IFRS and are not directly comparable due to the changes in organisation of Segments after 2012.*
[2] *Excluding the issue of hybrid bonds.*

The below figure presents the financial data of TAURON Capital Group for 2013–2017.

Figure no. 78. Financial data of TAURON Capital Group for 2013–2017



The below table presents TAURON Capital Group's EBITDA, broken down into Segments (Lines of Business) for 2017–2013.

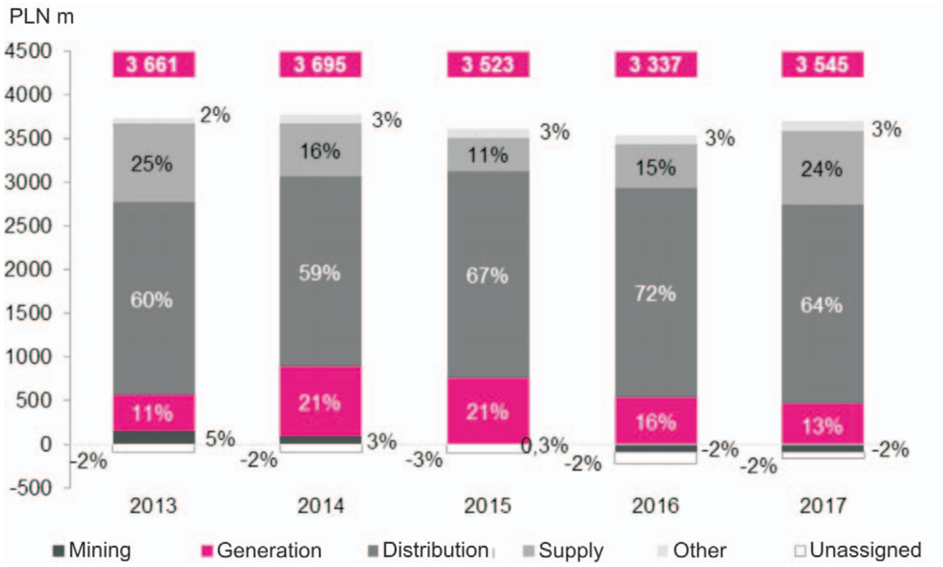
Table no. 29. TAURON Capital Group's EBITDA, broken down into Segments (Lines of Business)[1]

No.	EBITDA (PLN m)	2017	2016	2015	2014	2013	Rate of change (2017/2016)	Change (2017–2016)
1.	Mining	**(83)**	(82)	9	98	166	–	(1)
2.	Generation	**464**	545	755	793	400	85%	(81)
3.	Distribution	**2 283**	2 395	2 372	2 172	2 208	95%	(112)
4.	Sales	**841**	490	380	608	899	172%	351
5.	Other	**118**	115	100	106	63	103%	3
6.	*Unallocated items*	***(78)***	*(126)*	*(94)*	*(83)*	*(75)*	*62%*	*47*
	Total EBITDA	**3 545**	**3 337**	**3 523**	**3 695**	**3 661**	**95%**	**208**

[1] *The values presented do not reflect the values compliant with the IFRS and are not directly comparable due to the changes in organisation of Segments.*

The below figure presents the structure of TAURON Capital Group's EBITDA in 2013–2017.

Figure no. 79. Structure of TAURON Capital Group's EBITDA in 2013–2017



Key information for 2013–2017 by Segments

The below figures present the financial data for 2013–2017 by Segments.

Figure no. 80. Data of the Mining Segment for 2013–2017

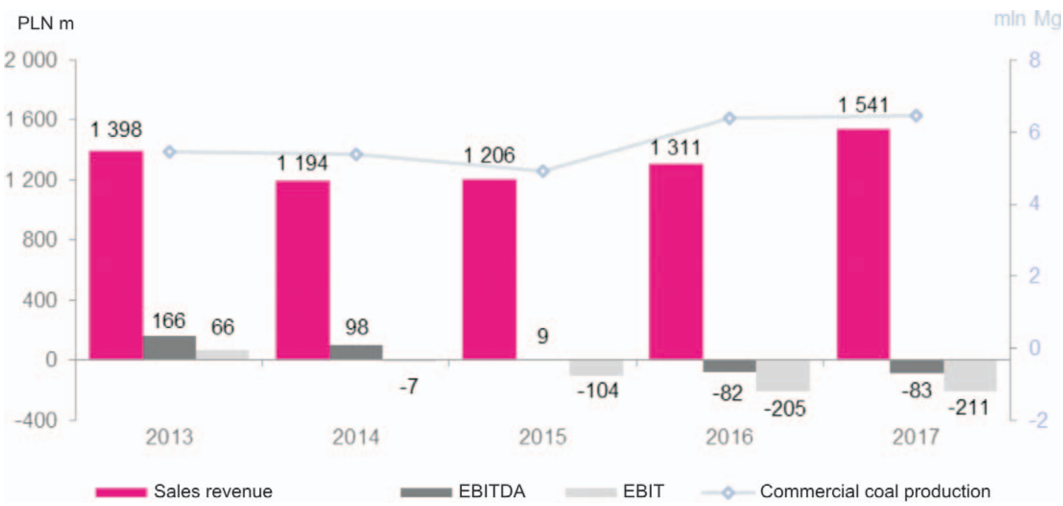


Figure no. 81. Data of the Generation Segment for 2013–2017

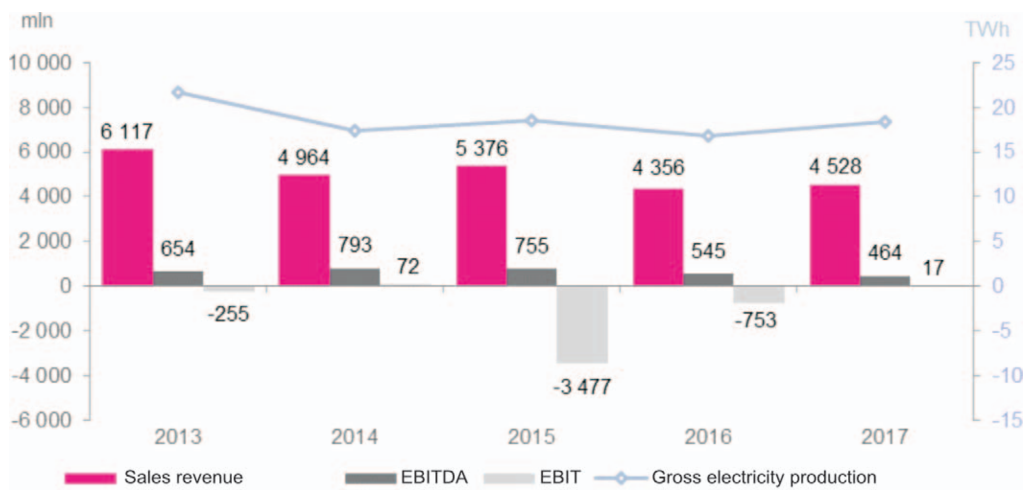


Figure no. 82. Data of the Distribution Segment for 2013–2017

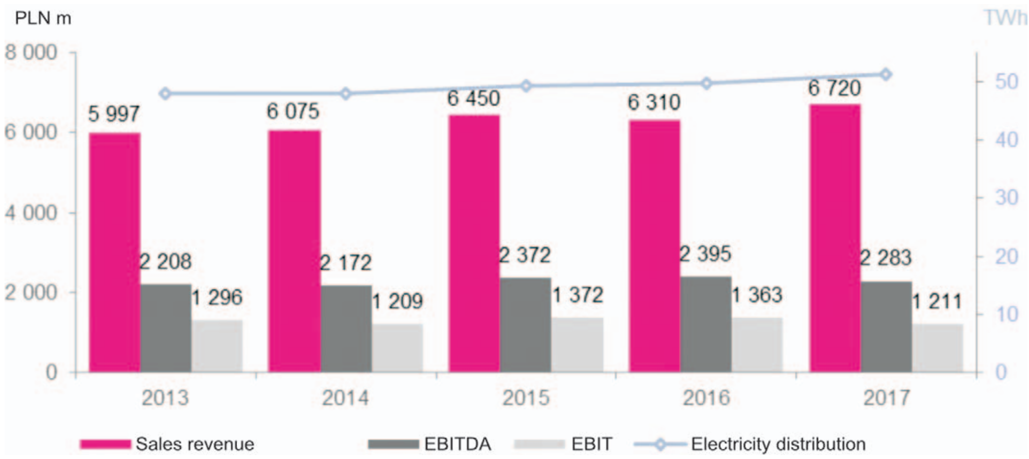


Figure no. 83. Data of the Supply Segment for 2013–2017

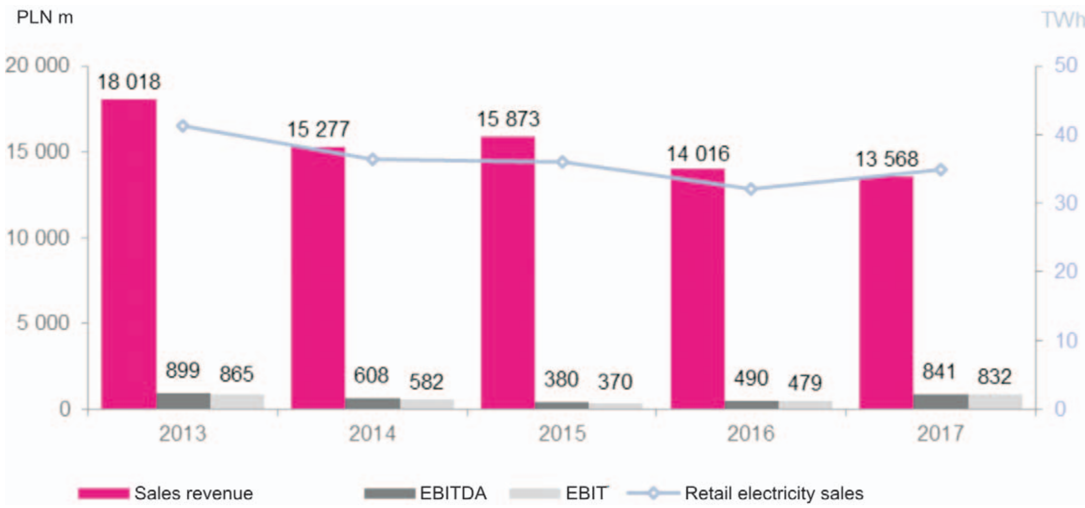
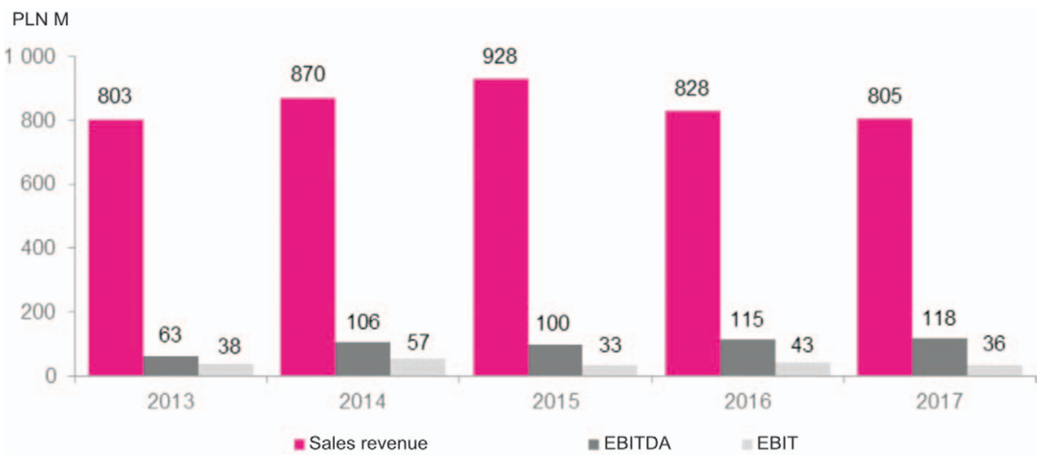


Figure no. 84. Data of the Other Operations for 2013–2017



4.7. Proceeds from securities issues

Under the bond issue programme concluded on 24 November 2015 between the Company and the consortium of banks In 2017 TAURON conducted bond issues and redemptions under the existing program (tj. the bond issue program concluded with the consortium of banks on November 24, 2015), and also completed the eurobond issue.

Eurobond issue

On July 5, 2017 TAURON issued eurobonds with the nominal value of EUR 500 mln. Eurobonds are unsecured, senior, coupon bearing securities. Eurobonds' maturity date is 10 years from the date of issue. The interest rate is based on a fixed rate of 2.375% per annum. The yield as of the date of issuance was 2.439% per annum with the issue price equal to 99.438% of the nominal value. In accordance with the eurobond issue prospectus the proceeds from the issue were to be used to refinance the costs of the construction and acquisition of wind farms by one of TAURON Capital Group's subsidiaries, financing of TAURON Capital Group's investment projects in the distribution segment and for general corporate purposes. Eurobonds were granted BBB rating by Fitch rating agency. Fulfilling this obligation in Q4 2017 TAURON completed the redistribution of the funds obtained from the bond issue by recapitalizing the following subsidiaries: TAURON EKOENERGIA and TAURON Dystrybucja, as a result of which TAURON EKOENERGIA made a repayment of a substantial portion of the debt related to the construction and acquisition of wind farms and TAURON Dystrybucja received funds to cover the expenditures related to the investment projects implemented by this subsidiary.

Eurobonds were admitted to trading on the regulated market of the London Stock Exchange.

Information on the eurobond issue was disclosed in detail in the regulatory filings (current reports) described in section 2.8. of this report.

Bond issues and redemptions in 2017

The bonds issue program signed on 24 November 2015 between TAURON and a consortium of banks led to issue in 2017 by TAURON of bonds having the total part value of PLN 600 Mln, according to the following specification:

1) Bonds issue on 30 January 2017 with total par value of PLN 100 Mln – redeemed on 30 July 2017,
2) Bonds issue on 01 March 2017 with total par value of PLN 100 Mln – redeemed on 01 September 2017,
3) Bonds issue on 31 March 2017 with total par value of PLN 300 Mln – redeemed on 30 June 2017,
4) Bonds issue on 30 June 2017 with total par value of PLN 100 Mln – redeemed on 30 July 2017

Funds received from the above bonds issue were used as stated in issue documents, i.e. to cover investment outlays of the TAURON Capital Group and for general corporate purposes.

Also, TAURON redeemed early the following bonds issued within the bonds issue program signed on 24 November 2015:

1) Redemption of PLN 100 Mln par value of bonds on 25 September 2017,
2) Redemption of PLN 300 Mln par value of bonds on 09 December 2017,
3) Redemption of PLN 650 Mln par value of bonds on 29 December 2017.

The below table presents the summary of issued and non-redeemed bonds as of December 31, 2017.

Table no. 30. Summary of issued and non-redeemed bonds as of December 31, 2017

No.	Value of bonds issues (thou.)	Type and level of interest rate	Redemption term of the last series	Balance as of 31 December 2016 (thou.)
1.	1 750 000 PLN	WIBOR 6M + fixed margin	04.11.2019	1 750 000 PLN
2.	1 700 000 PLN	WIBOR 6M + fixed margin	20.12.2029	1 700 000 PLN
3.	1 600 000 PLN	WIBOR 6M + fixed margin	29.12.2020	1 600 000 PLN
4.	190 000 EUR	Fixed interest rate	16.12.2034	190 000 EUR
5.	500 000 EUR	Fixed interest rate	05.07.2027	500 000 EUR

4.8. Financial instruments

4.8.1. Application of financial instruments in order to eliminate price changes, credit risk, material disruptions of cash flows and loss of financial liquidity

The financial risk at TAURON Capital Group is managed by TAURON. The centralizing of the financial risk management function is aimed at optimizing the process, including minimizing TAURON Capital Group's costs in the above mentioned respect. As part of financial risk management in 2017 TAURON Capital Group continued to hedge the risk of volatility in cash flows resulting from its debt based on WIBOR reference rate. Moreover, in 2017 TAURON Capital Group hedged the currency exposure arising from the trading operations (mainly due to the purchase of CO_2 emission allowances) by concluding forward contracts. In 2017 TAURON Capital Group was also implementing the strategy of hedging its foreign currency exposure generated by interest payments on the financing obtained in EUR by concluding forward contracts and CIRS transactions. The goal of these transactions was to hedge against the risk of cash flow volatility resulting from currency rate fluctuations.

The below table presents active forward derivative transactions as of December 31, 2017 (due to the adopted centralized model of financial risk management, the data refers only to TAURON).

Table no. 31. Information on forward transactions and derivatives as of December 31, 2017

No.	Type of transaction concluded	Total denomination of the specific type of transaction (thou.)	Currency			Maturity date of the specific type of transaction		Valuation of transaction of the specific type as of December 31, 2017 (thou.)
			PLN	EUR	other	up to one year	above one year	
1.	IRS	2 100 000	X				X	24 482
2.	CIRS	1 262 120	X				X	- 9 299
2.	Forward	6 610		X		X		- 346

With respect to hedging the risk arising from price volatility and the credit risk TAURON Capital Group did not use financial instruments.

On the other hand, as part of liquidity loss risk management debt instruments referred to in section 4.10 are used.

4.8.2. Objectives and methods of financial risk management

The objectives and methods of financial risk management at TAURON Capital Group are presented in section 3.4.2 of this report.

4.9. Current and forecast financial situation (financial outlook)

Considering the current market situation, it is expected that the results of TAURON Capital Group in the coming years will be affected by both internal factors as well as external factors.

The results of the **Mining Segment** in the coming years will, to a large degree, be dependent on the work progress in the implementation of the investment projects and the technical and organizational changes introduced. The effects of actions aimed at increasing the efficiency of this segment will be reflected in its financial and operating results in the subsequent periods. However it should be indicated that achieving a positive profitability of the segment already in 2018 will be a challenge.

It is expected that the financial situation in the **Generation Segment** in the next few years will not improve in relation to the current situation, due to the macroeconomic and sector related conditions under which electricity producers will be operating. In a longer term the new generation units, currently under construction, demonstrating better production parameters, will have an impact on the improvement of the current status. It is also expected that the changes of the Polish market model being prepared, aimed at implementing the capacity market mechanism, in accordance with the passed and notified capacity market law and the draft capacity market regulations draft, will bring additional revenue that will allow for refurbishing the generating units and extending their lifecycle. The operations related to electricity generation from RES is subject to statutory regulation which, to a large extent, determine the profitability. The segment's cost efficiency improvement measures undertaken will have an impact on the improvement of the results of the entire line of business.

In the **Distribution Segment**, the estimated level of remuneration on the invested capital and the cost efficiency improvement measures undertaken will play a key role impacting the level of the operating result. It is expected that the estimated level of operating profit in the coming years will be lower than the result reached in 2017. New elements of the regulatory policy and the associated risks will have a significant impact on results in the years to come, i.e. the updated approach to the average weighted cost of capital, enterprise efficiency improvement correction factors with respect to operating expenses and the level of the balancing difference, continuation of the quality based regulation.

Supply Segment – in the coming years the need to incur higher costs has to be taken into account, in connection with conducting expansion activities and measures aimed at minimizing the number of customers leaving as well as recovery of customers lost in the previous years under the circumstances of the increased activities of the competition.

Other Segment is mainly responsible for providing shared services as well as for the implementation and finalization of the projects used mainly to provide services to the Distribution and Supply Lines of Business with respect to contacts and settlements with customers assuring the highest quality. In addition, services for TAURON Capital Group's subsidiaries are provided, inter alia, with respect to financial and accounting as well as IT services. These activities enable achieving synergy effects across TAURON Capital Group and improve cost efficiency.

4.10. Assessment of financial resources management

TAURON Capital Group has a centralized financial management function in place and thus effective management of finance of entire TAURON Capital Group is possible. The main tools enabling effective management include: the implemented central financing model and the appropriate internal corporate regulations as well as the cash pooling implemented by TAURON Capital Group. Additionally, the financial management system is supported by the central policy of managing the financial risk at TAURON Capital Group and the central Insurance policy of TAURON Capital Group. In these areas TAURO plays the role of the management body and decision maker with respect to the directions of measures undertaken, enabling determining the relevant limits of risk exposure.

In accordance with the adopted central model of financing TAURON is responsible for acquiring the financing for TAURON Capital Group's subsidiaries. Funds acquired both internally (from TAURON Capital Group's subsidiaries generating financial surpluses), as well as externally (from the financial market) are subsequently transferred to TAURON Capital Group's subsidiaries, reporting the requirement for financing (for this purpose, besides cash pooling, the intra-group bond issue program is implemented).

Such model of acquiring the funding sources enables, first of all, decreasing of the cost of capital, increasing the possibility to obtain financing, reduces the number and form of hedges established on assets of TAURON Capital Group and covenants required by financial institutions, as well as reduces the administrative costs. The central model of financing also enables acquiring financing sources unavailable for individual subsidiaries, such as, for example, issue of eurobonds.

Another key element influencing the efficiency of financial management is the policy of financial liquidity management. Through implementation of relevant forecasting standards it becomes possible to establish the precise liquidity position allowing for optimizing the moment of fund raising as well as the maturity term and types of deposit instruments as well as the appropriate level of the liquidity reserve. The above factors lead to both, cost reduction as well as liquidity safety improvement. The current liquidity management is supported by the implemented cash pooling mechanism. Its overriding goal is to provide for current financial liquidity at TAURON Capital Group, while at the same time limiting the costs of short term external financing and maximizing the financial revenue due to investing cash surpluses. Owing to the cash pooling structure TAURON Capital Group's subsidiaries facing short term deficits of funds, may use funds of the subsidiaries generating financial surpluses, without the need to acquire external financing.

Moreover, a unified program of bank guarantees was implemented at TAURON Capital Group. Under the agreements concluded by TAURON with banks it is possible to issue guarantees to secure the liabilities of TAURON Capital Group's subsidiaries companies within the centralized limit. The above mentioned measure reduced the cost of guarantees acquired, made their acquisition independent of the individual subsidiaries' financial standing and limited the total number of actions required to obtain a guarantee.

In 2017 TAURON Capital Group demonstrated full capacity to pay its accounts payable with the payment deadlines thereof.

4.11. Principles of preparing annual consolidated financial statements

Consolidated financial statements have been drawn up in accordance with the IFRS approved by the EU.

The IFRS comprise standards and interpretations approved by the International Accounting Standards Board as well as the International Financial Reporting Interpretation Committee.

TAURON Capital Group's subsidiaries and the parent entity keep their accounting books and prepare their financial statements in accordance with the IFRS, excluding TAURON Czech Energy and TAURON Sweden Energy that are keeping their books and preparing their financial statements in accordance with the accounting principles applicable, respectively, in the Czech Republic and in Sweden.

The consolidated financial statements contain adjustments which are not included in the ledgers of TAURON Capital Group's entities, introduced in order to bring the consolidated statements into compliance with IFRS.

The consolidated financial statements have been prepared with the assumption of the continuation of business operations by TAURON Capital Group's subsidiaries in the foreseeable future. As of the date of approval of the consolidated financial statements for publication, no circumstances have been detected, indicating any risk for business continuity by TAURON Capital Group's subsidiaries.

The accounting principles (policy) adopted for drawing up of the consolidated financial statements are presented in note 9 of the Consolidated financial statements for the year ended on December 31, 2017.

4.12. Information on the entity authorized to audit financial statements

On April 27, 2017 TAURON concluded the agreement with Ernst & Young Audyt Polska Limited Liability Company Limited Joint-Stock Partnership on conducting an audit of:

1) financial statements of the Company for 2017, prepared in accordance with the requirements of the IFRS,
2) financial statements of selected subsidiaries of TAURON Capital Group for 2017, prepared in accordance with the IFRS,
3) consolidated financial statements for 2017, prepared in accordance with the requirements of the IFRS.

The Agreement also covers conducting a review of the interim, half year financial statements of the Company and the consolidated financial statements of TAURON Capital Group, prepared in accordance with the IFRS requirements for the period ending on June 30, 2017.

The above audit company was also selected, on February 26, 2018 by TAURON's Supervisory Board to audit the standalone and consolidated financial statements of TAURON for the financial year 2018 and the review of the interim standalone and consolidated financial statements of TAURON for the period ending on June 30, 2018. The detailed information on the conclusion of the amendment to the agreement with the above audit company is provided in section 2.8. of this report.

The audit of the standalone and consolidated financial statements of TAURON for the financial year 2016, the financial statements of selected TAURON Capital Group's subsidiaries for the financial year 2016 and the review of the interim standalone and consolidated financial statements of TAURON for the period ending on June 30, 2016 were conducted by Deloitte Polska Limited Liability Company Limited Joint-Stock Partnership.

The compensation of the certified auditors for the services provided for TAURON Capital Group's subsidiaries is shown in the below table.

Table no. 32. Compensation of the certified auditors for the services provided for TAURON Capital Group's subsidiaries

No.		Year ended on December 31, 2017 (PLN thous.)	Year ended on December 31, 2016 (PLN thous.)
1.	Mandatory audit, including:	1 018	752
	consolidated financial statements	*124*	*25*
	standalone financial statements of the parent entity	*54*	*80*
	standalone financial statements of the subsidiaries	*840*	*647*
2.	Other certifying services provided to TAURON Capital Group, including reviews of financial statements	565	438
3.	Tax advisory services	0	0
4.	Other services (including training) provided for TAURON Capital Group	3	244
	Total	**1 586**	**1 434**

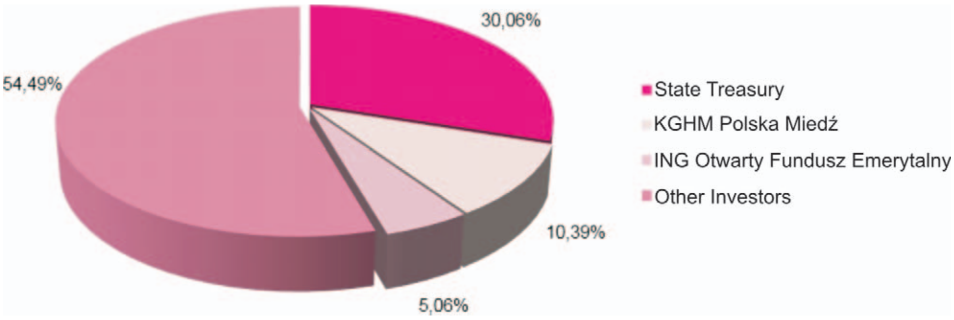
5. SHARES AND SHAREHOLDERS

5.1. Structure of shareholding

As of December 31, 2017 and as of the day of drawing up this report the Company's share capital was, in accordance with an entry in the National Court Register, PLN 8 762 746 970 and was split into 1 752 549 394 shares with a nominal value of PLN 5 per share, including 1 589 438 762 ordinary AA series bearer shares and 163 110 632 registered BB series shares.

The below figure presents the structure of shareholding as of December 31, 2017 and as of the day of drawing up this report.

Figure no. 85. Structure of shareholding as of December 31, 2017 and as of the day of drawing up this report



5.2. Dividend policy

As part of its Strategy adopted on September 2, 2016 the Company adopted its dividend policy. In the long term TAURON is planning to pay out a dividend of minimum 40 percent of the consolidated net profit. The Company's intention is to provide a dividend yield that would be competitive versus the yield offered by long term debt instruments issued on the Polish market by investment grade rated companies. The final recommendation on the dividend will be impacted by additional factors, including in particular

1) TAURON Capital Group's liquidity position,
2) Market situation,
3) Implementation of the investment policy,
4) Cost and ability to obtain financing,
5) Legal requirements and provisions of the financing agreements, in particular related to not breaching the defined level of the leverage ratio,
6) Ensuring investment grade rating.

The forecasts that are the basis for the Strategy indicate that 2020 will be the first year in which the dividend payout will be possible.

The below table presents the dividends paid out in 2010–2014.

Table no. 33. Dividends paid out in 2010–2014

Dividends paid out in 2010–2014						
No.	Financial year for which the dividend was paid out	Dividend amount paid out (PLN)	Net profit %	Dividend per share (PLN)	Dividend record date	Payment date
1.	2010	262 882 409,10	31%	0.15	30.06.2011	20.07.2011
2.	2011	543 290 312,14	44%	0.31	02.07.2012	20.07.2012
3.	2012	350 509 878,80	24%	0.20	03.06.2013	18.06.2013
4.	2013	332 984 384,86	25%	0.19	14.08.2014	04.09.2014
5.	2014	262 882 409,10	23%	0.15	22.07.2015	12.08.2015

5.3. Number and nominal value of the Company's shares, as well as of the shares in units related to the Company, held by members of the Management Board and the Supervisory Board

As of December 31, 2017 and as of the day of drawing up this report members of the Management Board and members of the Supervisory Board did not have any TAURON shares, nor they held any shares in units related to the Company.

5.4. Agreements related to potential changes to the shareholding structure

Management Board has no information on the existence of agreements (including also the ones concluded past the balance sheet date), as a result of which changes in the proportions of shares held by the existing shareholders and bondholders may occur in the future.

5.5. Own shares buybacks

In 2017 and as of the day of drawing up this report the Company did not own any of its shares.

5.6. Employee stock award programs

In 2017 no employee stock award programs were implemented by the Company.

5.7. Shares performance on the Warsaw Stock Exchange (WSE)

TAURON shares have been listed on the Main Market of the Warsaw Stock Exchange since June 30, 2010. In 2017 TAURON share price fluctuated between PLN 2.76 and PLN 4.12 (at closing prices). During the last session of 2016 the share price was PLN 2.85, while a year later the price reached PLN 3.05. This means that the rate of return on the investment in TAURON shares was 7 percent in 2017.

Performance of shares listed on WSE in 2017 was impacted by favorable, both global as well as local factors. Investors were convinced that the government's economic policy allowed for a further strong GDP growth, while PLN was one of the strongest currencies on the market. Also energy sector companies became more attractive for investors, which led to a 15% rise of the WIG-Energia index.

Apart from very good economic conditions and the growing demand for electricity TAURON share price last year was also positively impacted by activities with respect to obtaining financing aimed at ensuring TAURON Capital Group's financial stability, in particular the July 2017 issue of 10-year Eurobonds worth EUR 500 mln.

As of December 31, 2017 TAURON shares were included in the following stock exchange indices:

1. **WIG** – index that includes all companies listed on WSE's Main Market that meet basic criteria for inclusion in indices. TAURON's share in WIG: 0.96%.
2. **WIG-Poland** – national index that groups solely shares of domestic companies listed on WSE's Main Market that meet basic criteria for inclusion in indices. TAURON's share in WIG-Poland index: 1.11%.
3. **WIG20** – index calculated on the basis of the value of the portfolio of shares of 20 largest and most liquid companies listed on WSE's Main Market. TAURON's share in WIG20 index: 1.46%.
4. **WIG30** – index that includes 30 of the largest and most liquid companies listed on WSE's Main Market. TAURON's share in WIG30 index: 1.35%.
5. **WIG-Energia** – sector based index that comprises companies included in WIG index and are also qualified to the energy sector. TAURON's share in WIG-Energia: 15.98%.
6. **Respect Index** – index that groups in its portfolio companies that operate in accordance with the highest corporate social responsibility standards. TAURON's share in RESPECT Index: 2.65%.
7. **MSCI Emerging Markets Europe**– index that includes key companies in 15 developed countries in Europe. TAURON's share in MSCI Emerging Markets Europe Index: 0.02%.
8. **MSCI Poland Index** – index that includes more than 20 key companies listed on WSE. TAURON's share in MSCI Poland Standard Index: 1.26%.

The below table presents key data on the Company's shares in 2011–2017.

Table no. 34. Key data on TAURON shares in 2011–2017

No.		2011	2012	2013	2014	2015	2016	2017
1.	Share price high (PLN)	6.81	5.61	5.39	5.69	5.29	3.19	4.12
2.	Share price low (PLN)	4.65	4.08	3.85	4.04	2.37	2.31	2.75
3.	Last share price (PLN)	5.35	4.75	4.37	5.05	2.88	2.85	3.05
4.	Capitalization at the end of the period (PLN m)	9 376	8 325	7 659	8 850	5 047	4 995	5 345
5.	Capitalization at the end of the period (%)	2.1	1.59	1.29	1.5	0.98	0.9	0.8
6.	Book value (PLN m)	15 922.47	16 839.41	17 675.34	18 106.79	18 837	16 348.99	17 880
7.	P/E	8.1	5.5	5.5	7.8	4.2	x	3.02
8.	P/BV	0.59	0.49	0.43	0.49	0.27	0.31	0.31
9.	Rate of return ytd[1] (%)	-16.73	-5.03	-3.64	20.07	-40.78	-1.04	7.02
10.	Dividend yield (%)	2.8	6.5	4.6	3.8	5.2	–	–
11.	Trading volume (PLN m)	5 574.82	3 198.94	3 103.56	3 134.81	3 062.52	3 199.02	2 737.33
12.	Trading volume share (%)	2.21	1.7	1.41	1.53	1.5	1.69	1.16
13.	Average volume per session	3 721 539	2 667 725	2 793 020	2 489 329	3 190 195	4 662 087	3 261 765
14.	Average number of transactions per session	1 373	960	1 022	1 106	1 431	1 465	1 323

Source: WSE Statistical Bulletin

[1] *Rate of return calculated taking into account the investor's income from the dividend and assuming that the additional income realized is re-invested. Methodology in accordance with WSE Statistical Bulletin.*

The below graphs present historical TAURON share price performance and trading volumes, including against WIG20 and WIG-Energia indices.

Figure no. 86. TAURON share price and trading volumes in 2017

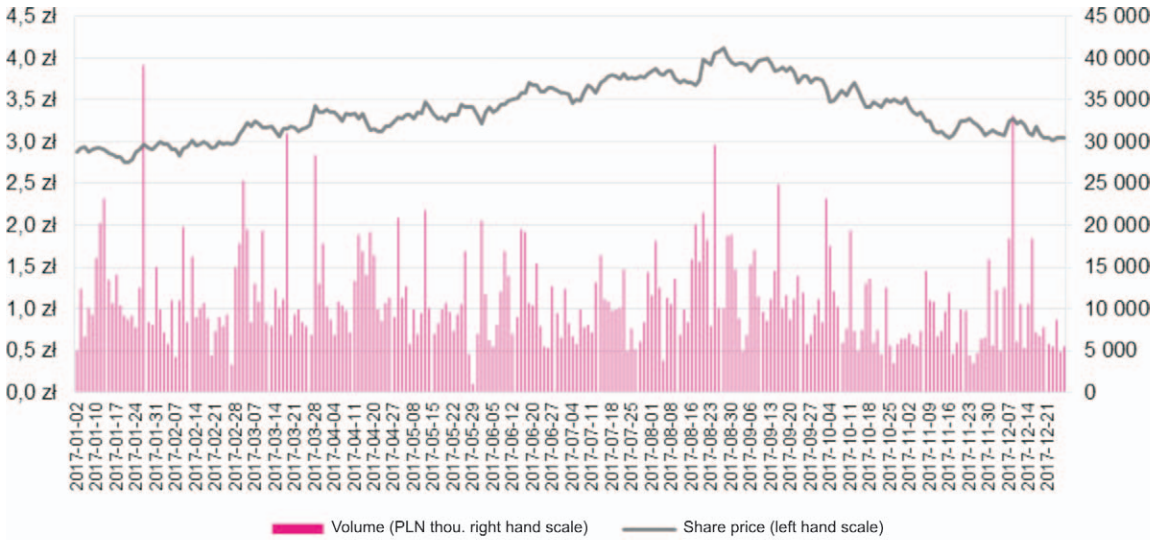


Figure no. 87. TAURON share price and trading volumes since the market debut until December 31, 2017

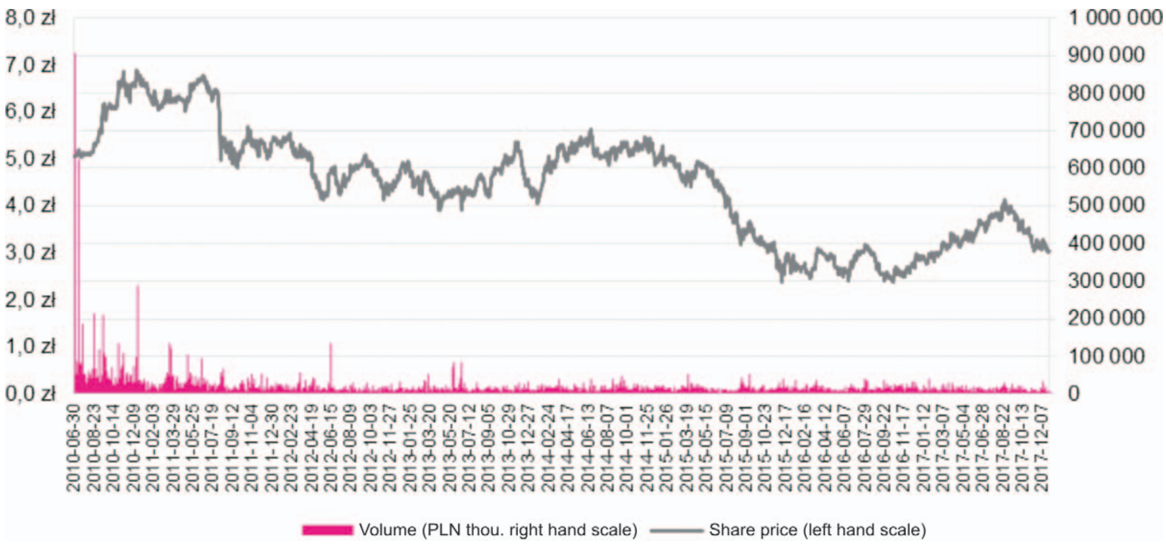
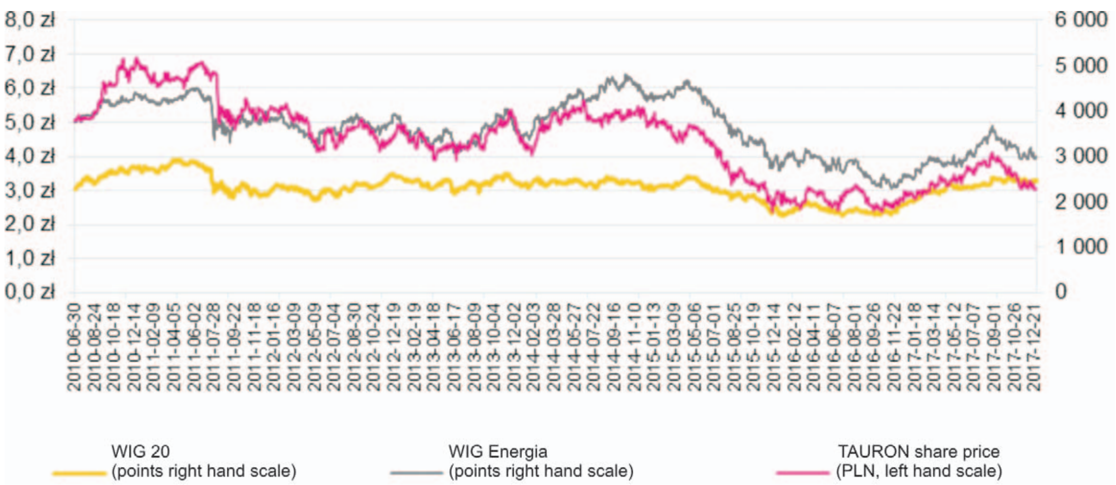


Figure no. 88. TAURON share price versus WIG20 and WIG-Energia indices since the market debut until December 31, 2017



Recommendations for the shares of TAURON Polska Energia S.A.

In 2017 analysts from brokerage houses and investment banks issued 11 recommendations for TAURON shares in total, including:

1) three "Buy" recommendations,
2) four "Hold" recommendations,
3) four "Sell" recommendations.

The below table presents a list of recommendations issue in 2017.

Table no. 35. Recommendations issued in 2017

Lp.	Data wydania rekomendacji	Recommending institution	Recommendation/target price
1.	15.11.2017	Societe Generale	Buy / PLN 4.50
2.	21.03.2017	Societe Generale	Buy / PLN 4.00
3.	10.01.2017	Pekao Investment Banking	Buy / PLN 4.00
4.	20.11.2017	DM BZ WBK	Hold / PLN 3.40
5.	14.09.2017	Exane BNP Paribas	Hold / PLN 4.00

Lp.	Data wydania rekomendacji	Recommending institution	Recommendation/target price
6.	27.06.2017	mBank	Hold / PLN 3.67
7.	20.03.2017	Raiffeisen Centrobank	Hold / PLN 3.50
8.	08.08.2017	DM PKO BP	Sell / PLN 3.40
9.	26.01.2017	DM BOŚ	Sell / PLN 2.50
10.	08.02.2017	DM Banku Handlowego (Citi)	Sell / PLN 2.50
11.	07.07.2017	DM Banku Handlowego (Citi)	Sell / PLN 2.50

5.8. Investor relations

Accurate and regular communications is one of the key priorities of TAURON with respect to conducting the dialogue with investors. It is provided both in the form of mandatory activities required by law (e.g. by disclosing information in the current and periodic regulatory filings) but also using many additional tools addressed directly to institutional and individual investors. The Company organises itself as well as participates in many investor conferences and roadshows organised by entities operating on the capital market, both in Poland and abroad.

During meetings with investors, the Strategy, the investment projects underway, the financial situation of TAURON Capital Group is presented as well as information on the current standing and outlook of the energy sector.

In connection with the publishing of periodical reports the Company organized conferences for investors and analysts during which members of the Management Board discussed financial results and presented the most important events in the reported periods. The conferences were broadcast on the Internet in Polish and in English. A possibility listening via telephone was also provided. This way all interested investors were able to receive the information at the same time. Separate meetings devoted to discussion of financial results are also regularly arranged for representatives of key media, so that information concerning the standing of TAURON Capital Group could reach all investors via diverse channels.

Besides meetings accompanying the publication of periodical reports, in 2017 members of the Management Board and representatives of the Investor Relations Team took part in 16 conferences and roadshows, during which approximately 100 meetings with managers and capital market analysts were held. Representatives of TAURON met institutional investors not only in Poland, but also in the US, Great Britain, Austria, Germany, Holland, France and Czech Republic.

In connection with the growing role of Internet channels and social media, much emphasis was put on their development with respect to the communications with investors. Via the YouTube service broadcasts of events important for investors are provided: earnings conferences, GMs, Investor Days and comments of the President of the Management Board on the financial results. On the other hand, on Facebook, announcements of significant events are published by the Company, including links to websites where the broadcasts may be followed or participation in an investor chat is possible. TAURON also launched a corporate profile on Twitter where entries related to investor relations appear. Being aware of the fact that the website is a significant source of information for investors, in particular, the *Investor Relations* tab; the Company takes cares of its content and validity of the content provided therein. *Investor Relations* section contains a lot of useful information on the current events, financial results or GMs. It also provides presentations and video broadcasts of conferences summarising the financial results.

In 2017, similar to 2016, TAURON participated in events addressed to individual investors. The company was, inter alia, a partner of the “WallStreet” conference in Karpacz, as well as winter and summer sports competitions of the capital market “Capital Market Games”. As party of the regular communications with this sizeable group of investors, 4 chats with a representative of the Management Board took place in 2017, in which approximately 100 investors took part each time.

Activities with respect to investor relations are appreciated by participants of the capital market and investors. In 2017 the Company was awarded successive prizes for the high quality of investor relations.

In March 2017, the Company was awarded a special prize in the competition for the best investor relations among WIG30 index companies, organized by the Stock Market and Investors Paper “Parkiet” and the Chamber of Brokerage Houses.

In June 2017 TAURON was awarded the “Hero of the capital market 2017” title in the company category. The winner in the competition organized by the Individual Investors Association was selected based on the vote of the investors who appreciated TAURON’s high standards in the field of investor relations and applying the best practice with respect to the communications address to the individual investors.

In the past year TAURON was among the laureates of the “2016 Transparent Company of the Year” ranking for business transparency and quality of the market communications. The ranking, organized by the Stock Market and Investors Paper “Parkiet” and the Institute of Accounting and Taxes (Instytut Rachunkowości i Podatków), was based on a survey in which three most important market communications area were evaluated, i.e. financial statements and reporting, investor relations and corporate governance rules.

TAURON is also regularly awarded prizes in the top annual report competitions. The Company finished first in the previous three editions of “The Best Annual Report” competition organized by the Institute of Accounting and Taxes (Instytut Rachunkowości i Podatków), qualifying, in 2017, to the elite “The Best of the Best” category. In last year’s edition of the competition TAURON was also awarded the top prize for the integrated annual report.

Company is maintaining high quality of reporting to meet the expectations of the broadest possible group of recipients of its communications – customers, shareholders, analysts, as well as media representatives. This is why in 2017 the team working on the design of the integrated annual report focused on the compliance of its structure and content with the international integrated reporting standards. The result of these works is a modern, multimedia online report online presenting the most important information on TAURON Capital Group.

TAURON has been included in the RESPECT Index since 2013, and in December 2017, for the fifth time, the Company found itself in the group of stock market listed entities lthat apply the highest sustainable growth standards.

2017 investor relations highlights and activities are presented in the below table.

Table no. 36. Highlights and activities performed as part of investor relations in 2017

No.	Date	Event
1.	15.03.2017	Full year 2016 stand-alone and consolidated earnings reports published
2.	16.03.2017	Management Board’s meeting with analysts and fund managers to present FY 2016 earnings, Warsaw
3.	16.03.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
4.	21–22.03.2017	Participation in DM PKO BP CEE Capital Markets Conference, London
5.	27–28.03.2017	Participation in Raiffeisen Centrobank Investor Conference, Austria, Zürs
6.	10.05.2017	Q1 2017 earnings report published
7.	11.05.2017	Management Board’s meeting with analysts and fund managers to present Q1 2017 earnings, Warsaw
8.	11.05.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
9.	25.05.2017	Meetings with fund managers following Q1 2017 earnings, DM Banku Handlowego (Citi), Warsaw
10.	29.05.2017	TAURON’s Ordinary GM
11.	20.06.2017	Eurobond Roadshow, Germany
12.	21.06.2017	Eurobond Roadshow, Netherlands
13.	22.06.2017	Eurobond Roadshow, Great Britain
14.	23.06.2017	Eurobond Roadshow, France
15.	26.06.2017	Eurobond Roadshow, Warsaw
16.	17.08.2017	H1 2017 earnings report published
17.	18.08.2017	Management Board’s meeting with analysts and fund managers to present H1 2017 earnings, Warsaw
18.	18.08.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
19.	24.08.2017	Meetings with fund managers following H1 2017 earnings, Societe Generale, Warsaw
20.	11–12.09.2017	Participation in 14th Annual Emerging Europe Investment Conference, Pekao Investment Banking, Warsaw
21.	26–27.09.2017	Participation in Mining&Energy Conference, DM PKO BP, Katowice
22.	11–12.10.2017	Participation in Erste Group Investor Conference, Austria, Stegersbach
23.	08.11.2017	Q3 2017 earnings report published
24.	09.11.2017	Management Board’s meeting with analysts and fund managers to present Q3 2017 earnings, Warsaw

No.	Date	Event
25.	09.11.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
26.	15.11.2017	Meetings with fund managers following Q3 2017 earnings, DM mBanku, Warsaw
27.	20–21.11.2017	Participation in Poland Investment Forum NY, JP Morgan, New York
28.	01.12.2017	Participation in BZ WBK Energy & Mining Conference, Warsaw
29.	05.12.2017	Participation in Wood's Winter Conference in Prague, Prague

6. STATEMENT ON APPLICATION OF CORPORATE GOVERNANCE

Pursuant to § 91(5)(4) of the Regulation of the Minister of Finance of 19 February 2009 *on current and periodical information submitted by issuers of securities and conditions to acknowledge as equivalent information required by legal regulations of a country not being a member state* (Journal of Laws no.33 item 259 as amended), and the *Best Practice of GPW Listed Companies 2016* (Best Practice 2016), the Company's Management Board submits the statement on application of corporate governance in 2017.

6.1. Indication of applied set of corporate governance rules

In 2017 the Company was subject to the corporate governance rules, described in the document *Best Practice of GPW Listed Companies* (Best Practice 2016), adopted by the Supervisory Board of the GPW Board no. 27/1414/2015 of 13 October 13, 2015, which came into force on January 1, 2016.

The text of the Best Practice 2016 the Company is subject to is published on the GPW website at the address: www.gpw.dobre-praktyki.pl.

6.2. Indication of abandoned rules of corporate governance

In 2017 the Company did not apply the following detailed rules provided in Best Practice 2016:

1) IV.Z.2. concerning ensuring of publicly available real-time broadcasts of general meetings, due to the lack of the relevant provisions of the Articles of Association enabling the aforementioned broadcast. In order to enable the application of the rule, the Company Management Board requested the Ordinary GM of the Company to adopt the relevant amendment to the Company Articles of Association ensuring publicly available real-time broadcast of general meetings. However, the Ordinary GM of the Company convened on 8 June 2016 did not adopt the amendment to the Company Articles of Association proposed by the Company Management Board in this respect,
2) VI.Z.1. concerning the construction of incentive schemes in a way necessary, among others, to tie the level of compensation of members of the Company's management board and key managers to the actual long-term financial standing of the Company and long-term shareholder value creation as well as the Company's stability. This rule was not applied due to the compensation and bonus system applicable in TAURON in relation to members of the Management Board of the Company and its key managers stipulates that the level of compensation will be tied to the financial situation of the Company within the annual perspective, in conjunction with the implementation of strategic objectives,
3) VI.Z.2. stating that in order to tie the compensation of members of the management board and key managers to the Company's long-term business and financial goals, the period between the allocation of options or other instruments linked to the Company's shares under the incentive scheme and their exercisability should be no less than two years. 2 years This rule was not applied due to the compensation and bonus system applicable in TAURON in relation to Members of the Management Board of the Company and its key managers does not provide that compensation should be tied to instruments linked with the Company shares.

In 2017 the following rules did not apply to the Company:

1) I.Z.1.10. concerning placing financial projections on the Company website – if the company has decided to publish them – published at least in the last 5 years, including information about the degree of their implementation – due to the fact that financial forecasts are not published,
2) III.Z.6. stating that where the Company has no separate internal audit function in its organisation, the audit committee (or the supervisory board if it performs the functions of the audit committee) should review on an annual basis whether such function needs to be separated – due to the fact that the Company has a separate Internal Audit Department in its organisational structure.

Furthermore, the Management Board of the Company, adopting the detailed rules of Best Practice 2016 designated as: I.Z.1.3, I.Z.1.15, I.Z.1.16, II.Z.1, II.Z.6, II.Z.10.1, II.Z.10.2, II.Z.10.3, II.Z.10.4, V.Z.5, V.Z.6, VI.Z.4., indicated the manner of applying them. The detailed description of the manner of applying the above rules is provided in the *Information on the status of applying by the Company of the recommendations and rules provided in Best Practice 2016,* constituting an appendix to the above mentioned report on not applying the detailed rules provided in Best Practice 2016 and provided on the Company's website.

In 2017 the Company developed and introduced into use the document *Diversity Policy at TAURON Group*, that was described in detail in section 6.12. of this report. Before that the Company had not had a single document describing the applied policy of diversity in relation to the authorities of the Company and its key managers, referred to in the rule designated as I.Z.1.15. of Best Practice 2016, in the report published on February 1, 2016 concerning the abandoned detailed rules of corporate governance contained in Best Practice 2016, the Company indicated the method of applying the diversity policy. It was indicated at then that the rules on diversity management were introduced for application under many documents constituting internal legal acts.

Information concerning abandonment of recommendations provided in Best Practice 2016 for application

In 2017 the Company did not apply only the recommendation provided in Best Practice 2016, designated as IV.R.2 concerning ensuring a possibility to shareholders to participate in the GM using electronic communication means, due to the lack of such shareholders' expectation. This decision is expressed by the failure of the Company GM on 8 June 2016 to adopt the relevant amendments to the Company Articles of Association ensuring publicly available real-time broadcast of general meetings.

The other recommendations provided in Best Practice 2016 were applied by the Company in 2017.

6.3. Description of main characteristics of internal control and risk management systems in relation to the process of generating the financial statements and consolidated financial statements

The internal audit and risk management system with respect to the process of drawing up the financial statements and consolidated financial statements is implemented on three levels:

Level I

General principles of management at the Company and TAURON Capital Group. TAURON Capital Group's subsidiaries operate based on organizational regulations and possess defined organizational structures based on internal documents adopted for the entire Group. These define the business units responsible for preparing financial statements and consolidated financial statements. Such units have the duty to perform regular control of the tasks vested and functional control of their activities. Business Model of the TAURON Capital Group resulted in implementation of Process Documentation of Megaprocess 3.4 Accounting, containing procedures associated with financial reporting of the Company and the TAURON Capital Group. Process documents define responsibilities of business units within the reporting processes.

Level II

Risk management. TAURON Capital Group implemented a Risk Area managed by the Executive Director for Risk Management, whose role is to oversee and establish the risk management process for the entire TAURON Capital Group. These functions are implemented within the Company by Corporate, Market and Credit Risk Management Teams. The purpose of risk management is to improve the predictability of attaining strategic objectives by the TAURON Capital Group, including stable creation of the financial result through early identification of threats allowing preventive activities to commence. Risk management standards applicable at the TAURON Capital Group have been defined in the *Strategy for corporate risk management at the TAURON Group* and in policies for managing specific risks. The ERM system encompasses all spheres of TAURON Capital Group business and business processes within the Group, including the process of preparing financial statements. Risks associated with his process are managed, monitored and reported within the ERM system. Standardization aims to ensure coherence in managing the individual risk categories, defining general principles, standards and tools of system architecture. Oversight of the ERM system at the TAURON Capital Group is performed by the Risk Committee.

Level III

Internal Audit. Internal Audit Department is functioning in the Company. The goal of the Internal Audit is planning and implementing audit tasks, including performance of commissioned ad-hoc inspections, and also activities of advisory and opinion (feedback) providing nature. Methods and rules of implementing the Internal Audit function are defined by the Process Documentation of the Megaprocess 1.5 Audit along with the related document *Regulations of Internal Audit at TAURON Group.* The introduction of Megaprocess 1.5 Audit was a consequence of the adoption of the Business Mode by the Management Board of TAURON. In implementing the internal audit function the Company shall be acting in compliance with the *TAURON Group's Corporate Social Responsibility Code* and the International Standards for the Professional Practice of Internal Auditing.

Key aspects with respect to internal control and risk management in reference to the process of preparing financial statements and consolidated financial statements include:

Supervision over application of consistent accounting rules by TAURON Capital Group's subsidiaries when developing reporting packages for the purpose of preparing TAURON Capital Group's consolidated financial statements

In order to ensure consistent accounting principles based on International Financial Reporting Standards (IFRS) approved by the European Union the Accounting Policy of TAURON Polska Energia S.A. Capital Group (Accounting Policy) was developed and implemented in TAURON Capital Group. This document shall be accordingly updated in case there are changes to the regulations. The rules defined in the Accounting Policy shall be applicable to TAURON's stand-alone financial statements and TAURON Capital Group's consolidated financial statements. TAURON Capital Group's subsidiaries shall be obligated to apply the Accounting Policy when preparing the reporting packages that provide the basis for preparing TAURON Capital Group's consolidated financial statements.

Furthermore, TAURON Capital Group developed and implemented an intra-group regulation that comprehensively regulates issues related to the rules and deadlines for preparing the reporting packages for the purpose of consolidated financial statements. The reporting packages shall be validated by the holding company's Consolidation and Reporting Office and by an independent certified auditor during an audit or review of TAURON Capital Group's consolidated financial statements.

Procedures used to authorize and provide opinions on the Company's financial statements and TAURON Capital Group's consolidated financial statements

The Company has implemented financial statements' authorization procedures. Quarterly, half year and full year financial statements of the Company and TAURON Capital Group's consolidated financial statements shall be approved by the Company's Management Board before being published. Full year financial statements of TAURON and TAURON Capital Group's consolidated financial statements shall be additionally presented for evaluation to the Company's Supervisory Board before being published. Vice President of the Management Board for economic and financial affairs (Chief Financial Officer) shall oversee the preparation of financial statements, while the Management Boards of the subsidiaries included in the consolidation shall be responsible for preparing the reporting packages for TAURON Capital Group's consolidated financial statements.

Supervisory Board's structure includes the Audit Committee of the Supervisory Board of TAURON Polska Energia S.A., whose membership, competence and description of activities are provided in clause 6.11.3 of this report

IT systems as well as financial and accounting processes

TAURON Capital Group's subsidiaries maintain accounting books (ledgers) which constitute the basis for preparing financial statements using ERP financial and accounting computer systems, enabling system audits of the correctness of the document flow and classifying of the business events. Consolidated financial statements are prepared using an IT tool used to consolidate financial statements, providing system control with respect to the coherence (integrity) and timeliness of preparing the consolidation data.

TAURON Capital Group's subsidiaries have implemented IT and organizational solutions that provide control of access to the financial and accounting system and ensure adequate protection and archiving of the accounting books. Access to IT systems is restricted based on applicable access rights assigned to authorized personnel. Control mechanisms are applied in the process of granting and changing access rights to the financial and accounting systems. Granted rights are also subject to periodic verification.

Due to the integration of the accounting functions and the transfer of TAURON Capital Group's material subsidiaries' financial and accounting services to CUW-R (Shared Cervices Center – Accounting) TAURON Capital Group's financial and accounting processes were gradually unified. The subsidiaries adjusted their own procedures to the flow of the financial and accounting processes, taking into account the specifics of the individual segments.

TAURON Capital Group's Business Model clearly distributes responsibilities with respect to the financial and accounting processes between the Company (indicated as the Corporate Centre) and the subsidiaries and CUW R, indicating that the Corporate Centre is the owner of processes associated with accounting and reporting of TAURON Capital Group. With respect to the tasks of the Corporate Centre, strategic functions associated with the development of the model of operations and standards of TAURON Capital Group were indicated in the area of accounting and supervision of the implementation of standards in the accounting area in the subsidiaries and CUW R. Moreover, it was indicated that the Company as the Corporate Centre is responsible for drawing up the Company's financial statements and the consolidated financial statements of TAURON Capital Group. A clear split of responsibilities and strong emphasis on the fulfillment of the supervisory functions by the Corporate Centre in relation to CUW R and the subsidiaries is, inter alia, aimed at improving the process of preparing the financial statements.

Subjecting the Company's financial statements and TAURON Capital Group's consolidated financial statements to an audit and reviews by an independent certified auditor

Full year financial statements of the Company and full year consolidated financial statements of TAURON Capital Group are subject to an audit by an independent certified auditor. Half year financial statements of the Company and half year consolidated financial statements of TAURON Capital Group are subject to a review by a certified auditor. In 2017 the Company selected an entity authorized to audit and review the financial statements of the material subsidiaries of TAURON Capital Group and the consolidated financial statements. The agreement with the entity authorized to audit financial statements was concluded to conduct an audit and review of the 2017 financial statements. Due to the selection by TAURON's Supervisory Board on February 26, 2018 of an audit company to conduct an audit of the Company's and TAURON Capital Group's 2018 financial statements and a review of the Company's and TAURON Capital Group's 2018 financial statements for the period ended on June 30, 2018 it is planned that an amendment to the agreement with the audit company will be signed.

Due to the coming into force of the *law of May 11, 2017 on certified auditors, audit companies and public supervision*, the Audit Committee TAURON's Supervisory Board adopted the following regulations on October 16, 2017:

1) *Policy of selecting an audit company to conduct an audit and review of the financial statements and consolidated financial statements of TAURON Polska Energia S.A.,*
2) *Procedure of selecting an audit company to conduct an audit and review of the financial statements and consolidated financial statements of TAURON Polska Energia S.A., and*
3) *Policy of providing at TAURON Group, by an audit company conducting of an audit of the annual financial statements and consolidated financial statements of TAURON Polska Energia S.A., entities related to this audit company and a member of the audit company's network, of the permitted services that are not an audit.*

The above regulations in a clear manner define the principles and rules of the process of selecting an audit company to audit the Company's financial statements, as well as the principles of providing permitted services for the benefit of TAURON Capital Group's, in order to ensure independence of an audit company and certified auditors towards the Company and guarantee for the Company the provision of audit services of high subject matter quality, while meeting the required deadlines that the Company must comply with.

Principle of changing the Company and TAURON Capital Group's audit company

The principle of changing the Company's and TAURON Capital Group's audit company was changed in 2017. The following rule was established in the *Policy of selecting an audit company to conduct an audit and review of the financial statements and consolidated financial statements of TAURON Polska Energia SA*, adopted by the Audit Committee of the Company's Supervisory Board on October 16, 2017:

1) maximum period of continuous orders for audits to be conducted by the same audit company or an entity related to that audit company or any member of the network operating in the European Union countries that such audit companies are members of, shall not exceed 5 years,
2) after a 5-year duration of the order neither the audit company, nor any member of its network operating within the European Union shall conduct an audit of the Company for the subsequent 4 years,
3) a key certified auditor shall not conduct an audit of the Company for a period longer than 5 years,
4) a key certified auditor may again conduct an audit of the Company after at least 3 years have elapsed from the completion of the last audit.

Before that the principle adopted by the Supervisory Board of the Company on August 27, 2010 had been in force according to which the rule was adopted concerning changing of the entity authorised to audit the financial statements of the Company and TAURON Capital Group at least once every five 5 financial years. The entity authorized to audit the financial statements of the Company and TAURON Capital Group was able to perform these activities again after the elapse of two financial years.

6.4. Shareholders holding substantial blocks of shares

The below table presents shareholders holding, as of December 31, 2017 and as of the day of drawing up this report, directly or indirectly substantial blocks of the Company's shares.

Table no. 37. Shareholders holding, directly or indirectly, substantial blocks of shares

No.	Shareholders	Number of shares held	Percentage interest in share capital	Number of votes held	Percentage share in the total number of votes
1.	State Treasury	526 848 384	30.06%	526 848 384	30.06%
2.	KGHM Polska Miedź S.A.	182 110 566	10.39%	182 110 566	10.39%
3.	Nationale-Nederlanden Otwarty Fundusz Emerytalny	88 742 929	5.06%	88 742 929	5.06%

Since the day of publishing the previous periodical report, i.e. since November 8, 2017, until the day of publishing this report the Company did not receive any notifications from its shareholders on any changes in the ownership structure of substantial blocks of TAURON shares.

6.5. Holders of securities providing special control rights

The Company did not issue securities that would provide special control rights with respect to the Company.

6.6. Restrictions on exercising the voting right

Restrictions on exercising the right to vote are provided in § 10 of the Company's Articles of Association which are available on the Company's website http://www.tauron.pl/.

The above restrictions on exercising the voting right are formulated in the following way:

1. The voting right of shareholders holding over 10% of total votes in the company shall be limited so that none of them can exercise more than 10% of the total votes in the company at the General Meeting of Shareholders.
2. The restriction on exercising the voting right mentioned in clause 1 above shall not apply to the State Treasury and entities controlled thereby in the period during which the State Treasury, together with entities controlled thereby, hold a number of the company's shares that entitle them to exercise at least 25% of the total votes in the company.
3. Votes of shareholders who have a parent/subsidiary relationship in the understanding of § 10 of the Articles of Association (Shareholder Cluster) shall be aggregated; in case the aggregate number of their votes exceeds 10% of total votes in the company it shall be subject to reduction. Rules of votes' aggregation and reduction are defined in clauses 6 and 7 below.
4. A shareholder, in the understanding of § 10 of the Articles of Associations, shall be any party (entity), including its parent and subsidiary company, entitled directly or indirectly to a voting right at the General Meeting of Shareholders on the basis of any legal title; it shall also be applicable to a party (entity) that does not hold the company's shares, and in particular to a user, lien holder, party (entity) entitled on the basis of a depositary receipt under regulations of the Act of July 29, 2005 on financial instruments trading, as well as a party (entity) entitled to take part in the General Meeting of Shareholders in spite of disposing of its shares after the date of establishing (registering) the right to take part in the General Meeting of Shareholders.
5. A parent company and subsidiary company, for the purposes of § 10 of the Articles of Association, shall be understood, accordingly, as a party (entity):
   1) having the status of a controlling undertaking, controlled undertaking or, at the same time, both the status of a controlling undertaking and controlled undertaking in the understanding of the *Act of February 16, 2007 on the protection of competition and consumers*, or
   2) having the status of a parent company, higher level parent company, subsidiary company, lower level subsidiary company, co-controlled company or one that has both the status of a parent company (including a higher level parent company) and the status of a subsidiary (including a lower level subsidiary company and a co-controlled company) in the understanding of the *Act of September 29, 1994 on accounting*, or
   3) which has (parent company) or one which is under controlling influence (subsidiary company) in the understanding of the *Act of September 22, 2006 on transparency of financial relationships between public bodies and public undertakings and on financial transparency of some undertakings*, or
   4) whose votes due to the company's shares owned directly or indirectly are subject to aggregation with votes of another party (entity) or other parties (entities) on conditions defined in the *Act of July 29, 2005 on a public offering and conditions of introducing financial instruments to an organized trading system and on public companies* in connection with holding, disposing of or acquiring large blocks of the company's shares.
6. Aggregation of votes is based on totaling the number of votes held by individual shareholders that are members of the Shareholders' Cluster.
7. Reduction of votes involves decreasing the total number of votes in the company that shareholders that are members of the Shareholders' Cluster, are entitled to exercise at the General Meeting of Shareholders to the level of 10% of total votes in the company. Reduction of votes shall take place in accordance with the following rules:
   1) number of votes of a shareholder who holds the largest number of votes in the company among all shareholders that are members of the Shareholders' Cluster shall be reduced by a number of votes equal to a surplus above 10% of total votes in the company held by all shareholders that are members of the Shareholders' Cluster,
   2) if, despite the above mentioned reduction, the total number of votes that shareholders that are members of the Shareholders' Cluster are entitled to exceeds 10% of the total votes in the company, a further reduction of votes held by other shareholders that are members of the Shareholders' Cluster shall be made. The further reduction of individual shareholders' votes shall take place in an order established on the basis of the number of votes that individual shareholders that are members of the Shareholders' Cluster hold (from the highest to the lowest one). The further reduction shall take place until the total number of votes held by shareholders that are members of the Shareholders' Cluster does not exceed 10% of the total votes in the Company,
   3) in any case a shareholder whose voting rights have been reduced shall have the right to exercise at least one vote,
   4) restriction on exercising the voting right shall also apply to a shareholder absent at the General Meeting of Shareholders.
8. Each shareholder who is going to take part in the General Meeting of Shareholders, in person or through a proxy, shall be obliged to, without a separate notice mentioned in clause 9 below, notify the Management Board or the Chairperson of the General Meeting of Shareholders that she/he holds, directly or indirectly, more than 10% of the total votes in the company.

9. Notwithstanding the provisions of clause 8 above, in order to establish the basis for aggregating and reducing the votes, a Company's shareholder, Management Board, Supervisory Board and individual members of such bodies shall have the right to demand that a shareholder of the Company provide information whether she/he is a party (entity) having the status of a parent or subsidiary company towards another shareholder in the understanding of § 10 of the Articles of Association. The entitlement mentioned in the preceding sentence shall also include the right to demand the revealing of the number of votes that the company's shareholder holds on its own or jointly with other shareholders of the Company.
10. A party (entity) that has failed to fulfill or has fulfilled the information obligation mentioned in clauses 8 and 9 above improperly, shall, until the failure to fulfill the information obligation has been remedied, be able to exercise its voting right with respect to one share only; exercising voting rights with respect to other shares by such party (entity) shall be null and void.

6.7. Restrictions on transfer of securities ownership right

As of December 31, 2017 and as of the day of drawing up this report TAURON's Articles of Association do not envisage limitations on the transfer of the Company's securities ownership right.

However, in accordance with the *law of July 24, 2015 on the control of some investments an* entity intending to purchase or achieve a material shareholding or purchase the dominating control over TAURON, which is an entity subject to protection, shall, each time, be obligated to submit a notification to the control body – Minister of Energy of its intention to do so, unless such obligation rests on other entities.

6.8. Rules on appointing and dismissing managing and supervising persons and their powers

6.8.1. Management Board

Rules on appointing and dismissing members of the Management Board

Management Board of the company shall be composed of one to six persons, including the President and Vice Presidents. Members of the Management Board shall be appointed and dismissed by the Supervisory Board for a common term of office lasting 3 years, except for the 1st term that lasted 2 years.

Each of the Management Board members can be dismissed or suspended in office by the Supervisory Board or the GM.

In order to recruit a person with whom an agreement on performing the management board level function at the Company, Supervisory Board announces the competition and conducts a qualification procedure for the position of the President or Vice President aimed at verifying and assessing the candidates' qualifications and selecting the best candidate. A candidate for a member of the Management Board must meet the requirements set forth in §16 clauses 3 and 4 of the Company's Articles of Association. The announcement of the qualification process is published on the Company's web site and in the Public Information Bulletin of the Ministry of Energy. The Company notifies the shareholders of the results of the qualification procedure.

Management Board's competence

Management Board shall conduct the company's affairs and represent the company in all court and out of court proceedings. Any matters related to conducting the Company's affairs, not assigned, based on the legal regulations or the provisions of the Articles of Association, to the scope of competence of the General Meeting of Shareholders or Supervisory Board, shall be within the scope of competence of the Management Board.

In accordance with the Articles of Association, all issues which go beyond the regular scope of the Company's activities shall require a resolution of the Management Board, in particular, the following issues listed in the below table:

Table no. 38. Management Board's competence

Matters that require a resolution of the Management Board
as of December 31, 2017 and as of the day of drawing up this report
1. Management Board bylaws, 2. company's organizational regulations, 3. establishment and liquidation of branches, 4. appointment of a proxy, 5. taking on credits and loans, 6. approving annual material and financial plans of the company and of the Capital Group as well as the Capital Group's Corporate Strategy, 7. assuming contingent liabilities in the understanding of the Act of September 29, 1994 on accounting, including granting guaranties and sureties by the company as well as issuing bills of exchange, subject to § 20 clause 2 item 4 and 5 of the company's Articles of Association, 8. making donations, cancelling interest or releasing from debt, subject to § 43 clause 3 items 1 and 2 of the company's Articles of Association,

Matters that require a resolution of the Management Board
as of December 31, 2017 and as of the day of drawing up this report

9. purchase of real estate, perpetual usufruct or shares in real estate or in perpetual usufruct, subject to § 20 clause 2 item 1 of the company's Articles of Association,
10. purchase of fixed assets excluding real estate, perpetual usufruct or share in real estate or perpetual usufruct with the value equal to or exceeding the PLN equivalent of EUR 10,000, subject to the provisions of § 20 clause 2 item 2 of the Company's Articles of Association,
11. disposal (control) of fixed assets including real estate, perpetual usufruct or share in real estate or perpetual usufruct with the value equal to or exceeding the PLN equivalent of EUR 10,000, subject to the provisions of § 20 clause 2 item 3 of the company's Articles of Association,
12. defining the way the voting right will be exercised at the General Meeting of Shareholders or the Meeting of Shareholders of companies in which the company holds shares, on matters within the scope of competence of the General Meeting of Shareholders or the Meeting of Shareholders of such companies, subject to the provisions of § 20 clause 3 item 9 of the company's Articles of Association,
13. rules of conducting sponsoring activities,
14. adoption of the annual plan of sponsoring activities,
15. matters which the Management Board refers to the Supervisory Board or the General Meeting of Shareholders for review.

6.8.2. Supervisory Board

Rules on appointing and dismissing members of the Supervisory Board

Supervisory Board shall be composed of five to nine persons, appointed for a common term of office lasting three years, except for the first term that lasted 1 year. In accordance with the Company's Articles of Association members of the Supervisory Board shall be appointed and dismissed by the General Meeting of Shareholders, subject to the following:

1) during the time when the State Treasury, together with the State Treasury controlled entities in the understanding of § 10 clause 5 of the Articles of Association, hold a number of the company's shares that entitle them to exercise at least 25% of the total votes in the company, the State Treasury, represented by the minister competent to handle the State Treasury's affairs, shall be entitled to appoint and dismiss members of the Supervisory Board in the number equal to half of the maximum number of members of the Supervisory Board defined in the Articles of Association (in case such number is not integral it shall be rounded down to an integral number, for example 4.5 shall be rounded down to 4) and increased by 1, provided that the State Treasury:
   a) shall be obliged to vote at the General Meeting of Shareholders on establishing the number of members in the Supervisory Board that would correspond to the maximum number of members of the Supervisory Board defined in the Articles of Association in case such a motion is submitted to the Management Board by a shareholder or shareholders who hold a number of votes that entitle them to exercise at least 5% of the total number of votes in the Company,
   b) shall be excluded from the voting at the General Meeting of Shareholders on appointing and dismissing other members of the Supervisory Board, including independent members of the Supervisory Board; this shall not, however, apply to the case when the Supervisory Board cannot act due to its membership being smaller than required by the Articles of Association, and the shareholders present at the General Meeting of Shareholders, other than the State Treasury, do not supplement the membership of the Supervisory Board in accordance with the distribution of seats in the Supervisory Board defined in this section;
2) during the time when the State Treasury, together with the State Treasury controlled entities in the understanding of § 10 clause 5 of the Articles of Association, hold a number of the company's shares that entitle them to exercise less than 25% of the total number of votes in the company, the State Treasury, represented by the minister competent to handle the State Treasury's affairs, shall be entitled to appoint and dismiss one member of the Supervisory Board.
3) appointing and dismissing members of the Supervisory Board by the State Treasury pursuant to the above mentioned clause 1) or 2) shall take place by means of a statement submitted to the Company.

In accordance with the Best Practice at least two members of the Supervisory Board shall meet the criteria of independence. Phrase an "independent member of the Supervisory Board" shall denote an independent member of the Supervisory Board in the understanding of Appendix II to the *European Commission's Recommendation of February 15, 2005 related to the role of non-executive directors or members of a supervisory board of publicly listed companies and a supervisory board's committee* (2005/162/EC).

Members of the Supervisory Board shall submit to the Company, prior to their appointment as members of the Supervisory Board, a written statement on compliance with the independence criteria. In case a situation occurs where the independence criteria are not complied with a member of the Supervisory Board shall be obligated to forthwith inform the company thereof. The company shall inform shareholders of the up to date number of independent members of the Supervisory Board.

Supervisory Board's competence

Supervisory Board shall continuously oversee the Company's activities in all areas of its operations.

According to the Company's Articles of Association the Supervisory Board's tasks and competences shall include in particular the matters listed in the below table.

Table no. 39. Supervisory Board's competence

Matters that require a resolution of the Supervisory Board
as of December 31, 2017 and as of the day of drawing up this report
Competences related to providing opinions
1. evaluate the Management Board's report on the company's operations (Directors' Report) as well as the financial statements for the last financial year with respect to their compliance with books, documents as well as with the actual status. This shall also apply to the Capital Group's consolidated financial statements, provided they are prepared,
2. evaluate the Management Board's recommendations on profit distribution or loss coverage,
3. submit a written report to the General Meeting of Shareholders on the outcome of activities covered in clauses 1 and 2,
4. prepare once a year and submit to the General Meeting: a) evaluation of the company situation, including the assessment of the internal control, risk management systems, compliance and internal audit functions, including all significant control mechanisms, in particular, those related to financial reporting and operations, b) b) report on activities of the Supervisory Board comprising at least information concerning: – the composition of the Supervisory Board and its committees, – fulfilment of independence criteria by Members of the Supervisory Board, – number of meetings of the Supervisory Board and its committees, – self-assessment of the Supervisory Board c) assessment of the method of fulfilment of information obligations by the Company, in relation to the application of corporate governance principles defined in the Regulations of the Exchange and provisions related to current and periodical information submitted by issuers of securities, d) assessment of rationality of sponsoring, charitable policy, or other similar policy pursued by the Company, or information concerning the lack of such policy,
5. prepare, along with the report on the results of the Company's annual financial statements' evaluation, the Supervisory Board's opinion on the financial viability of the company's capital investments in other commercial law entities made in the given financial year,
6. provide opinions on the Capital Group's Corporate Strategy,
7. provide opinions on the rules of conducting sponsoring activities,
8. provide opinions on the annual plan of conducting sponsoring activities as well as on the annual report on its implementation,
9. provide opinions on the reports prepared, by the Management Board, on entertainment expenses, expenditures on legal services, marketing services, public relations and social communications service as well as advisory services related to management,
10. provide opinions on the changes of the rules of divesting fixed assets, defined in § 381 of the Company's Articles of Association.
Competences that include
1. selecting a certified auditor to carry out an audit of the company's financial statements and the Capital Group's consolidated financial statements,
2. defining the scope and deadlines for submitting the company's and the Capital Group's annual material and financial plan by the Management Board,
3. adopting the consolidated text of the company's Articles of Association, prepared by the company's Management Board,
4. approving the Management Board's bylaws,
5. approving the organizational regulations of the company's enterprise,
6. purchasing real estate, perpetual usufruct or shares in real estate or in perpetual usufruct with the value exceeding the PLN equivalent of EUR 5,000,000, except for real estate, perpetual usufruct or shares in real estate or in perpetual usufruct purchased from the Capital Group's subsidiaries,
7. purchasing fixed assets, excluding real estate, perpetual usufruct or share in real estate or perpetual usufruct, bonds issued by the Capital Group's subsidiaries and other fixed assets purchased from the Capital Group's subsidiaries of the value exceeding the PLN equivalent of EUR 5,000,000,
8. disposing of fixed assets, including real estate, perpetual usufruct or share in real estate or perpetual usufruct, of the value equal to or exceeding the PLN equivalent of EUR 5,000,000, except for real estate, perpetual usufruct or shares in real estate or in perpetual usufruct, and also other fixed assets that as a result of disposing will be sold or encumbered in favor of the Capital Group's subsidiaries,
9. assuming contingent liabilities, including granting guaranties and sureties by the company with the value exceeding the PLN equivalent of EUR 5,000,000,
10. issuing bills of exchange of the value exceeding the PLN equivalent of EUR 5,000,000,
11. making an advance payment on account of the expected dividend,
12. taking over or purchasing shares in other companies than the Capital Group's subsidiaries with the value exceeding the PLN equivalent of EUR 5,000,000, except for situations when taking over shares in such companies takes place in exchange for the company's liabilities as a part of composition or bankruptcy proceedings,

Matters that require a resolution of the Supervisory Board

as of December 31, 2017 and as of the day of drawing up this report

13. selling shares with the value exceeding the PLN equivalent of EUR 5,000,000 along with defining the conditions and procedure to be applied in their sale, except for:
    a) selling shares which are traded on the regulated market,
    b) selling shares that the company holds in the amount not exceeding a 10% interest in the share capital of particular companies,
    c) selling shares in favor of the Capital Group's subsidiaries,
14. concluding a material agreement with a shareholder holding at least 5% of the total number of votes in the Company or a related company, with a proviso, that this obligation shall not cover typical transactions and concluded at arm's length as part of the business operations conducted by the Company with entities that are members of TAURON Capital Group,
15. concluding an agreement on legal services, marketing services, public relations and social communications services as well as advisory services related to management, if the amount of total net compensation for the services provided exceeds PLN 500 000, on a yearly basis,
16. amending an agreement on legal services, marketing services, public relations and social communications services as well as advisory services related to management, increasing the compensation above the amount mentioned in the above clause j,
17. concluding an agreement on legal services, marketing services, public relations and social communications services as well as advisory services related to management, under which the maximum compensation amount is not envisaged,
18. concluding a donation agrement or another agreement with similar consequences of the value exceeding PLN 20 000 or 0.1% of the total assets in the understanding of the *law of September 29, 1994 on accounting*, determined on the basis of the last approved financial statements,
19. relieving from debt długu or from another agreement with similar consequences of the value exceeding PLN 50 000 or 0.1% of the total assets in the understanding of the *law of September 29, 1994 on accounting*, determined on the basis of the last approved financial statements,
20. granting a permission to establish the company's branches abroad,
21. defining the way of exercising the voting right at the General Meeting of Shareholders or at the Meeting of Shareholders of companies in which the company holds more than 50% of shares, with respect to the following matters:
    a) selling and leasing out the company's enterprise or its organized part as well as establishing a limited proprietary right on them if their value exceeds the PLN equivalent of EUR 5 000 000,
    b) dissolving and liquidating the company.
22. defining the manner of exercising the voting right by a representative of TAURON during the GMs of companies (subsidiaries) with respect to which the Company is a dominating entrepreneur in the understating of art. 4 section 3 of the *law of February 16, 2007 on competition and consumer protection*, with respect to the following issues:
    a) company setting up another company,
    b) change to the Articles of Association or the shareholders agreement and the subject of the company's operations,
    c) merging, transforming, splitting, dissolving and liquidating the company,
    d) increasing or decreasing the company's share capital,
    e) selling and leasing out the company's enterprises or its organized part and establishing a limited property right thereupon,
    f) redeeming (retiring) of shares,
    g) setting the compensation of members of Management Boards and Supervisory Boards,
    h) provision on claims for remedying damage inflicted when setting up the company or performing management or supervision,
    i) matters mentioned in art. 17 *of the law of December 16, 2016 on the principles of managing state property,* subject to § 15 clause 4 of the Company's Articles of Association,
23. approving compensation policy for the capital group.

Competences related to the Management Board

1. appoint and dismiss members of the Management Board,
2. establish the rules of compensation and the amounts of compensation for the members of the Management Board, subject to § 18 of the Company's Articles of Association,
3. suspend members of the Management Board from office for important reasons,
4. delegate members of the Supervisory Board to temporarily perform duties of the members of the Management Board who cannot perform their duties and establish their compensation subject to the provision that the total compensation of the delegated person as a Member of the Supervisory Board's as well as on account of being delegated to temporarily perform duties of a Member of the Management Board shall not exceed the compensation established for the Member of the Management Board to replace whom the Member of the Supervisory Board was delegated,
5. conduct a recruitment process for the position of a Member of the Management Board,
6. conduct a competition in order to select a person with whom an agreement to perform the management board functions in the Company shall be concluded and conclude such agreement to perform the management board functions in the Company,
7. grant a permission to Members of the Management Board to take positions in governing bodies of other companies.

Other competences of the Company's Supervisory Board

1. prepare reports on overseeing the implementation of investment projects by the Management Board, including fixed asset purchases, and in particular provide opinions on the correctness and effectiveness of expenditures related thereto,
2. approve the Management Board's annual report on the supervision over the implementation of investment projects,
3. pass regulations describing in detail the Supervisory Board's procedures.

6.9. Description of the procedure of amendment of the Company's Articles of Association

Amendments to the Company's Articles of Association in accordance with the provisions of the Ksh, in particular: amendments to the Company's Articles of Association take place by means of resolution of the GM, at the majority of two thirds of the votes, and then requires issuing a decision by a proper court on entering the change into the register of entrepreneurs. The consolidated text of the Company's Articles of Association, including amendments passed by the General Meeting, shall be adopted by the Supervisory Board by means of a resolution.

In accordance with the Company's Articles of Association, a material amendment to the subject of activities requires two thirds of votes under the presence of persons representing at least a half of the share capital.

Ordinary GM on May 29, 2016 adopted the resolutions concerning amendments to the Company's Articles of Association; the relevant information s provided in section 2.8. of this report.

6.10. Procedures of the General Meeting of Shareholders, its fundamental powers and description of shareholders' rights and the manner of exercising thereof

The Company's General Meeting of Shareholders' procedures and its empowerments are defined in the company's Articles of Association and in the Regulations of the General Meeting of Shareholders of TAURON Polska Energia S.A. which are available on the Company's website http://www.tauron.pl/.

Procedures of the General Meeting of Shareholders

General Meeting of Shareholders shall be convened by a notice published on the company's website and in a manner defined for providing current information by public companies. In case the General Meeting is convened by an entity or a body other than the Management Board on the basis of regulations of the Code of Commercial Companies, as convening a General Meeting of Shareholders requires the Management Board's cooperation, the Management Board shall be obligated to perform any activities required by law in order to convene, organize and conduct General Meetings of Shareholders that take place either at the Company's seat or in Warsaw.

General Meeting of Shareholders shall be opened by the Chairperson of the Supervisory Board, and in case he/she is absent the following persons shall be entitled to open the General Meeting of Shareholders in the given order: Vice Chairperson of the Supervisory Board, President of the Management Board, a person designated by the Management Board or the shareholder who registered at the General Meeting of Shareholders such number of shares that provide the right to exercise the highest number of votes. Then, the chairperson of the General Meeting of Shareholders shall be elected from among persons entitled to participate in the General Meeting of Shareholders.

General Meeting of Shareholders shall pass resolutions irrespective of the number of shares represented at the Meeting, unless regulations of the Code of Commercial Companies, as well as provisions of the company's Articles of Association state otherwise. General Meeting of Shareholders may order a break in the meeting by the majority of two thirds of votes. The breaks shall not exceed 30 days in total.

A break in the GM session may take place only in exceptional situations indicated on a case-by-case basis in the justification to the resolution, prepared based on reasons presented by a shareholder requesting the announcement pf the break.

The GM resolution concerning a break shall clearly indicate the date of resumption of the session, however, such a date must not create a barrier for participation of the majority of shareholders in resumed meeting, including minority shareholders.

Competence of the General Meeting of Shareholders

In accordance with the Company's Articles of Association the matters listed in the below table shall require a resolution of the General Meeting of Shareholders.

Table no. 40. Competence of the General Meeting of Shareholders

Matters that require a resolution of the General Meeting of Shareholders
as of December 31, 2017 and as of the day of drawing up this report
1. reviewing and approving the financial statements of the Company and the consolidated financial statements of TAURON Capital Group for the previous financial year for the previous financial year as well as the Management Board's report on the Company's operations (Directors' Report) and the Management Board's report on the operations of TAURON Capital Group
2. granting the acknowledgement of the fulfillment of duties to the members of the Company's corporate bodies,
3. profit distribution and coverage of loss,
4. appointing and dismissing members of the Supervisory Board,
5. suspending members of the Management Board in performance of their duties,
6. establishing the amount of compensation for members of the Supervisory Board, subject to § 29 clause 4 of the company's Articles of Association,
7. establishing the principles of determining compensation and the amount of compensation of members of the Management Board taking into account the provisions of the *law of June 9, 2016 on the principles of determining compensation of persons managing some companies*,
8. selling and leasing out the company's enterprise or its organized part as well as establishing a limited proprietary right on them,

Matters that require a resolution of the General Meeting of Shareholders	
as of December 31, 2017 and as of the day of drawing up this report	
9.	concluding a credit, loan, surety agreement or any other similar agreement by the company with a member of the Management Board, Supervisory Board, proxy, liquidator or for the benefit of any such person. Concluding a credit, loan, surety or any other similar agreement by a subsidiary with a member of the Management Board, Supervisory Board, proxy, liquidator or for the benefit of any such person,
10.	increasing and decreasing the company's share capital,
11.	issuing convertible bonds or senior bonds as well as registered securities or bearer securities entitling their holder to subscribe or acquire the shares,
12.	purchasing of treasury shares in cases required by the regulations of the Code of Commercial Companies,
13.	mandatory redemption of shares (squeeze-out) in accordance with the provisions of art. 418 of the Code of Commercial Companies,
14.	setting up, using and liquidating reserve capitals,
15.	using supplementary capital,
16.	provisions related to claims to repair damage caused while establishing the company or serving on the management board or performing supervision,
17.	merger, transformation and division of the company,
18.	redemptions (retirements) of shares,
19.	amendment to the Articles of Association and change of the subject of the Company's operations,
20.	dissolving and liquidating the company.

In accordance with the provisions of the CCC the decision on issue and repurchase of shares in included within the competence of the General Meeting.

Description of shareholders' rights and the manner of exercising thereof

Description of the Company's shareholders' rights related to the General Meeting of Shareholders in accordance with the Company's Articles of Association, Code of Commercial Companies and the *Regulations of the General Meeting of Shareholders of TAURON Polska Energia S.A.* is presented in the below table.

Table no. 41. Description of the shareholders' rights related to the General Meeting of Shareholders

No.	Shareholders' rights	Description of shareholders' rights
1.	Convene a General Meeting of Shareholders	Shareholders representing at least one twentieth of the share capital, may request convening of an Extraordinary General Meeting of Shareholders. Such request should include a concise justification. It may be submitted to the Management Board in writing or in an electronic form, to the company's e-mail address, provided by the company on its website under the "Investor Relations" tab. Shareholders representing at least a half of the share capital or at least a half of all votes in the company may convene an Extraordinary General Meeting of Shareholders and appoint a chairperson of such General Meeting.
2.	Include matters (items) in the agenda of the General Meeting of Shareholders	Shareholders representing at least one twentieth of the share capital, may request that certain matters (items) be included in the agenda of the forthcoming General Meeting of Shareholders. Such request, including a justification or a draft resolution related to the proposed item of the agenda, should be submitted to the Management Board not later than 21 days prior to the set date of the General Meeting of Shareholders in electronic form to the company's e-mail address or in writing to the company's address.
3.	Become acquainted with the list of shareholders	Shareholders may become acquainted with the shareholders' list at the company's Management Board's seat for three weekdays preceding directly the General Meeting of Shareholders. Shareholders may also request that the list of shareholders be sent to them free of charge by electronic mail, providing the address to which the list should be sent.
4.	Participate in the General Meeting of Shareholders	Only persons who are Shareholders sixteen days before the date of the General Meeting of Shareholders (date of registering to participate in the General Meeting of Shareholders) shall have the right to take part in the General Meeting of Shareholders. In order to participate in the General Meeting shareholders should submit a request to issue a name bearing affidavit on the right to take part in the General Meeting of Shareholders to an investment (brokerage) company running their securities account. Such request should be submitted not earlier than following the announcement on convening of the General Meeting of Shareholders and not later than on the first weekday following the day of registering the participation in the General Meeting of Shareholders.
5.	Represent a shareholder by a proxy	Shareholders may take part in the General Meeting of Shareholders as well as exercise the voting right in person or through a proxy. Shares' co-owners may take part in the General Meeting of Shareholders and exercise the voting right only through a joint representative (proxy). A proxy may represent more than one shareholder and vote differently based on shares of each shareholder.
6.	Elect the Chairperson of the General Meeting of Shareholders	Shareholders shall elect the Chairperson of the General Meeting of Shareholders from among the persons entitled to take part in the General Meeting of Shareholders. Each of the participants of the General Meeting of Shareholders shall have the right to propose one candidate for the post of the Chairperson. Chairperson shall be elected by a secret ballot, by an absolute majority of votes. In case there is just one candidate for the Chairperson, election can take place by acclamation.
7.	Elect the Returning Committee	Each shareholder may propose no more than three candidates for members of the Returning Committee to be elected by the General Meeting of Shareholders, and vote for three candidates maximum.

No.	Shareholders' rights	Description of shareholders' rights
8.	Submit a draft resolution	During the General Meeting of Shareholders a shareholder shall have the right, until the discussion on a certain item of the agenda is closed, to submit a proposal of changes to the content of a draft resolution proposed for adoption by the General Meeting of Shareholders, as part of the given item of the agenda, or put forward his/her own draft of such resolution. Proposals of changes or draft resolutions, including justifications, may be submitted in writing to the Chairperson or verbally to be recorded in the minutes of the meeting.
9.	Raise an objection	Shareholders who voted against a resolution and, after the General Meeting of Shareholders has adopted it, want to raise their objection, should, immediately after the results of the voting have been announced, raise their objection and request it be included in the minutes of the meetings before proceeding to the next item of the agenda. In case such objection is raised later, which however shall not take place later than by the time the General Meeting of Shareholders is closed, the shareholders shall indicate against which resolution passed by the General Meeting they are raising their objection. Shareholders raising their objection against a resolution of the General Meeting may request their concise justification of the objection be recorded in the minutes of the meeting.

6.11. Composition of the Company's managing and supervising bodies and their committees, its changes, description of operation

6.11.1. Management Board

The current, fifth term of office of the Management Board began its run on March 16, 2017, i.e. on the day of appointing the Management Board of the Company for the fifth common term of office. In accordance with the Company's Articles of Association the common term of office shall last 3 years.

Composition of the Management Board as of December 31, 2017 and as of the day of drawing up this report

1. Filip Grzegorczyk – President of the Management Board,
2. Jarosław Broda – Vice-President of the Management Board for Asset Management and Development,
3. Kamil Kamiński – Vice-President of the Management Board for Customer and Corporate Support,
4. Marek Wadowski – Vice-President of the Management Board for Finance.

Changes to the Management Board's composition in 2017 and in the period up to the day of drawing up this report

As of January 1, 2017 the Management Board was composed of the following members: Filip Grzegorczyk (President of the Management Board), Jarosław Broda (Vice-President of the Management Board), Kamil Kamiński (Vice-President of the Management Board), Marek Wadowski (Vice-President of the Management Board) and Piotr Zawistowski (Vice-President of the Management Board).

On March 15, 2017 the Company's Supervisory Board dismissed, effective as of the end of day on March 15, 2017, all members of the Company's Management Board. On the same day Piotr Zawistowski up to then performing the function of Vice-President of the Management Board for Customer and Trade provided the Supervisory Board with the information on the resignation from applying for being selected to be a member of TAURON's Management Board of the 5th common term of office. The other members of the Management Board were appointed as of March 16, 2017 to the Company's Management Board of the 5th common term of office.

There were no other changes to the composition of the Management Board by the day of publishing this report

Experience and competences of members of the Management Board

Filip Grzegorczyk – President of the Management Board

A graduate of the Faculty of Law and Administration and the Faculty of International and Political Studies of the Jagiellonian University in Cracow where the obtained a PhD degree in the EU law, and then a post-PhD degree in the business law.

He also completed the Summer Advanced Course program in the European Law at the University of London, King's College, Centre of European Law as well as the International Business and Trade Summer School program at Catholic University of America – Columbus School of Law and the Ecole de droit français Université d'Orléans. He holds the position of Professor at the University of Economics in Cracow, where he is a lecturer at the Faculties of Management and Economics and International Relations.

He has broad professional experience in the energy and fuel sector. In 2011–2013 he was associated with Kompania Węglowa as a management board proxy for energy sector development at Kompania Węglowa S.A. In 2007–2008 he was a member of the Management Board of TAURON. From November 2015 he served as the Undersecretary of State at the Ministry of State Treasury. He speaks fluent English and French.

He has been holding the position of the President of the Management Board of TAURON Polska Energia S.A. since November 15, 2016. He is currently overseeing the following areas of the operations: strategic management and regulatory solutions, relationships with the environment (stakeholders), legal support and investor relations, risk management, legal and internal audit, security and compliance as well as human resources development and social dialogue policy.

Jarosław Broda – Vice-President of the Management Board

A graduate of the Warsaw School of Economics, a holder of a postgraduate diploma in project management from the Kozmiński University.

He has experience in the area of consolidation and operation of the energy sector, privatization of state-owned utility groups, developing processes associated with the restructuring and strategy building as well as energy entities' expansion projects.

Since the beginning of his professional career he has been associated with the energy sector's entities, holding senior executive and managerial positions. He gained his professional experience working at the Ministry of State Treasury as well as at TAURON and GDF Suez Energia Polska. Recently associated with GDF Suez Energia Polska – Katowice and GDF Suez (Branch Energy Europe) where he was responsible for market analyses and developing the company's expansion strategy, regulatory management and M&A projects. He was also involved in developing the sales and marketing expansion strategy in Europe. Since mid-2015 he was responsible for developing the commercial strategy and the contract for difference related to the nuclear project in Great Britain.

He has been holding the position of the Vice-President of the Management Board of TAURON Polska Energia S.A. since December 8, 2015. He is currently overseeing the following areas of the operations: asset management, research and innovation, investment projects and programs as well as occupational health and safety.

Kamil Kamiński – Vice-President of the Management Board

A graduate of the Faculty of Management and Social Communications of the Jagiellonian University. A holder of the MBA Executive diploma (Stockholm University School of Business/ Cracow University of Economics) and the Post-MBA Diploma in Strategic Financial Management (Rotterdam School of Management, Erasmus University/ GFKM).

He has experience in the area of building company value, mergers and acquisitions, business integration and strategy operationalization as well as management of comprehensive projects in the public and private sectors. He was involved in complex transformation and restructuring processes of enterprises in the energy and fuel as well as transportations logistics sectors.

He gained his professional experience acting in the capacity of the President or Vice-President of the Management Board and holding senior managerial positions. From the beginning of 2014 he was associated with Węglokoks Capital Group where, within the structures of Węglokoks Energia, he participated in the consolidation of electricity and heat generation assets of Kompania Węglowa and Węglokoks. At that time he was the head of the Management Committee. Previous professional experience includes, among others, work at the Research and Development Centre of the Refining Industry (OBR) in Płock or Jan Paweł II International Cracow-Balice Airport. He also managed the operations of John Menzies PLC in Poland. For many years he cooperated with Lotos Group where he supported the development of the aviation fuel segment which resulted in the *joint venture* with Air BP Ltd. and the establishment of Lotos Air BP.

He has been holding the position of the Vice-President of the Management Board of TAURON Polska Energia S.A. since December 8, 2015. He is currently overseeing the following areas of the operations: corporate management, human resources, marketing strategy and customer relations, IT systems functioning and management, personal data protection as well as procurement and administration.

Marek Wadowski – Vice President of the Management Board

A graduate of the Faculty of Economics of the University of Economics in Katowice. He also completed post graduate studies at École Supérieure de Commerce Toulouse where he obtained Mastère Spécialisé en Banque et Ingéniere Financière diploma and the Executive MBA studies at the Kozminski University in Warsaw.

He has professional experience in the field of financial, controlling and accounting process management in industry (power sector, mining, steel industry), as well as in financing of investment projects and international commercial transactions. He was involved in the implementation of the *due diligence* projects and valuations of many enterprises (using income-based, equity and comparison valuation methods).

From the beginning of his professional career he was associated with the energy, mining and steel sector entities, acting in the capacity of the President or the Vice-President of the Management Board and holding senior managerial positions. He gained his professional experience working at BRE Corporate Finance S.A., Huta Cynku Miasteczko Śląskie S.A. and at Jastrzębska Spółka Węglowa S.A. Capital Group's subsidiaries. From 2008, acting in the capacity of the Vice-President of the Management Board in charge of the financial division at Jastrzębska Spółka Węglowa S.A. Capital Group's subsidiaries, he was responsible, inter alia, for structuring commercial transactions, implementing the foreign exchange risk hedging policy, financial costs reduction, liquidity management, acquiring funds from the consortium of banks in the form of a bond issue program. He was also involved in the IPO of JSW S.A. (implementation of the International Accounting Standards, modification of the management information system, preparing the IPO prospectus, talks with investors). He held the position of the President of the Management Board at Towarzystwo Finansowe Silesia where he was involved in the bond issue program for Kompania Węglowa and was dealing with the acquisition of debt financing from the consortium of banks.

He has been holding the position of the Vice-President of the Management Board of TAURON Polska Energia S.A. since January 29, 2016. He is currently overseeing the following areas of the operations: finance and insurance policy, controlling and planning, analyses, accounting and tax policy. Additionally, until the Vice-President of the Management Board for Commercial Affairs is appointed, he also oversees the following areas: electricity and property rights trading, fuel trading, portfolio management and electricity tradinginance, controlling, business analyses, accounting and taxes, risk and IT.

The description of the experience and competences of the members of the Management Board is published on the Company's website http://www.tauron.pl/.

Description of the operations

Management Board of the company shall act on the basis of the Code of Commercial Companies and other legal regulations, provisions of the company's Articles of Association and provisions of the *Bylaws of the Management Board of TAURON Polska Energia Spółka Akcyjna with its seat in Katowice* which are available on the company's website http://www.tauron.pl/. When performing their duties members of the Management Board shall be acting in accordance with the principles included in Best Practice 2016.

2 members of the Management Board or one member of the Management Board together with a proxy shall be entitled to make valid statements on behalf of the Company. In case the Management Board includes one person, one member of the Management Board or a proxy shall be entitled to make valid statements on behalf of the Company.

Meetings of the Management Board shall be convened by the President of the Management Board or a Vice President of the Management Board designated thereby. Meetings of the Management Board shall also be convened on the motion of the majority of Vice Presidents of the Management Board as well as on the motion of the Chairperson of the Supervisory Board. The meetings shall be held at the company's seat on the date set by the person that convened the meeting. In justified cases the Management Board's meetings may be held outside the company's seat. The President of the Management Board or a Vice President of the Management Board designated thereby shall chair the meetings of the Management Board.

Management Board shall vote in an open ballot. The result of the ballot shall be recorded in the minutes of the meeting. President of the Management Board shall order a secret ballot at the request of any Vice President of the Management Board.

Resolutions of the Management Board shall be passed by an absolute majority of votes in the presence of 3/5 of the members of the Management Board. In case of an equal number of votes the President of the Management Board shall have a casting vote. Management Board may pass resolutions by voting in writing or using means of direct remote communications. Voting in accordance with the above procedures shall be ordered by the President of the Management Board or a Vice President of the Management Board designated thereby, including setting the deadline for casting votes by members of the Management Board. Submission of a dissenting opinion shall be allowed. Such dissenting opinion shall be recorded in the minutes of the meeting, including the justification thereof. Decisions of the Management Board related to ongoing issues that do not require passing of a resolution shall be recorded solely in the minutes of the meeting.

In case there are fewer members of the Management Board than the foreseen number of divisions (areas of responsibility), members of the Management Board may combine performing duties related to managing two divisions or introduce a different split of competences that would not be in conflict with the assignment of competences made by the Supervisory Board.

The internal divisi on, among members of the Management Board, of the tasks and responsibilities for the individual areas of the Company's operations (Divisions) defined in the *Organizational Regulations of TAURON Polska Energia S.A.* and including the independent work positions (jobs) as well as organizational units reporting to the individual Members of the Management Board and supervised thereby, shall be defined by the above Organizational Regulations, while the diagram showing the above mentioned division is published on the Company's website.

The structure of the divisions reporting to the individual Members of the Management Board is defined on the diagram (flowchart) of the Company's organizational structure, described in section 8.1.2. of this report.

6.11.2. Supervisory Board

The current, fifth term of office of the Supervisory Board, began on May 29, 2017, i.e. on the day of holding the Ordinary GM of the Company approving the financial statements for the last full financial year of the tenure of the members of the Supervisory Board of the fourth term, i.e. for the financial year 2016. In accordance with the Company's Articles of Association it shall be a common term of office and it shall last for 3 years.

The composition of the Supervisory Board as of December 31, 2017 and as of the date of drawing up this report

1. Beata Chłodzińska – Chair of the Supervisory Board,
2. Teresa Famulska – Deputy Chair of the Supervisory Board,
3. Jacek Szyke – Secretary of the Supervisory Board,
4. Radosław Domagalski-Łabędzki – Member of the Supervisory Board,
5. Katarzyna Łasak-Jarszak – Member of the Supervisory Board,
6. Paweł Pampuszko – Member of the Supervisory Board,
7. Jan Płudowski – Member of the Supervisory Board,
8. Agnieszka Woźniak – Member of the Supervisory Board.

Changes to the Supervisory Board's membership in 2017

As of January 1, 2017 the Supervisory Board was composed of the folowing members: Beata Chłodzińska (Chair of the Supervisory Board), Anna Mańk (Vice-Chair of the Supervisory Board), Jacek Szyke (Secretary of the Supervisory Board), Stanisław Bortkiewicz (Member of the Supervisory Board), Leszek Koziorowski (Member of the Supervisory Board), Jan Płudowski (Member of the Supervisory Board), Jacek Rawecki (Member of the Supervisory Board), Stefan Świątkowski (Member of the Supervisory Board) and Agnieszka Woźniak (Member of the Supervisory Board).

On May 25, 2017 Jacek Rawecki submitted a statement on the resignation, as of May 26, 2017, from the function of a member of the Company's Supervisory Board.

On May 29, 2017 the State Treasury, acting within its personal powers defined in § 23, clause 1, sections 1) and 3) of the Company's Articles of Association, appointed the following persons to be the members of the Company's Supervisory Board of the 5th common term of office: Beata Chłodzińska, Teresa Famulska, Barbara Katarzynę Łasak-Jarszak, Jan Płudowski i Agnieszka Woźniak.

On May 29, 2017 the Ordinary GM of the Company appointed the following persons to be the members of the Company's Supervisory Board of the 5th common term of office: Radosław Domagalski-Łabędzki, Paweł Pampuszko and Jacek Szyke.

There were no other changes to the composition of the Supervisory Board by the day of publishing this report.

Information on the independence of members of the Supervisory Board as of December 31, 2017

The independence requirements defined in the Best Practice and Appendix II to the *European Commission's Recommendation of February 15, 2005 related to the role of non-executive directors or members of a supervisory board of publicly listed companies and a supervisory board's committee* (2005/162/EC) are met by the following members of the Supervisory Board:

1) Teresa Famulska,
2) Barbara Łasak-Jarszak,
3) Paweł Pampuszko,
4) Jan Płudowski,
5) Jacek Szyke.

The other members of the Supervisory Board do not meet the independence requirements defined in the Best Practice.

As of the day of drawing up this report a member of the Supervisory Board, Beata Chłodzińska, met the independence requirements defined in the Best Practice.

Experience and competences of the members of the Supervisory Board

Beata Chłodzińska – Chair of the Supervisory Board

A graduate of the Faculty of Law and Administration of the Warsaw University. She is a licensed legal counsel.

In 2001–2016 she was associated with the Ministry of State Treasury where she was providing legal services, most recently as the Deputy Director at the Legal and Litigation Department. She is currently working at PKN Orlen S.A. in the legal area.

She gained professional experience associated with supervising the operations of the State Treasury owned companies by, among others, holding seats on the supervisory boards of the following companies: Polska Agencja Prasowa S.A. with its seat in Warsaw, Centrum Techniki Okrętowej S.A. with its seat in Gdańsk, Chemia Polska sp. z o.o. with its seat in Warsaw, Międzynarodowa Korporacja Gwarancyjna sp. z o.o. with its seat in Warsaw.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since August 12, 2015. In the Supervisory Board of the 5th common term of office she is the Chair of the Supervisory Board, the Head of the Nominations and Compensation Committee of the Supervisory Board, as well as a member of the Audit Committee of the Supervisory Board and a member of the Strategy Committee of the Supervisory Board.

Teresa Famulska – Deputy Chair of the Supervisory Board

A graduate of the University of Economics in Katowice, a Professor of economics appointed by the President of the Republic of Poland at the request of the Board of the Faculty of Finance and Insurance of the University of Economics in Katowice.

She has been associated with the University of Economics in Katowice since 1981. She is currently the Head of the Public Finance Department holding the full Professor's position. In 1998–2013 she was working at the School of Banking and Finance, recently as a dean, holding the full Professor's position.

An author of approximately 150 domestic and foreign publications in the field of finance, mainly public finance (including taxes and tax systems) and corporate finance. Apart from academic work she is continuously involved in business practice, participating, among others, in several dozen science and research projects. She conducts numerous lectures and training courses for the finance and management personnel of enterprises and for the tax authorities staff as part of the post-graduate studies and in cooperation with, among others, the Polish Economic Society (Polskie Towarzystwo Ekonomiczne) and the Accountants Association in Poland (Stowarzyszenie Księgowych w Polsce). Since 2007 she has been working at the State Examination Commission on Tax Advisory Services, where she has been the Head of the Commision since 2010. Since 2007 a member of the Financial Ediucation Committee of the Polish Academy of Science, where she was a member of the Board of the Committee in 2011–2015. Furthermore, she is a member of the Main Board of the Polish Finance and Banking Association (Zarząd Główny Polskiego Stowarzyszenia Finansów i Bankowości), International Fiscal Association, Center for Information and Organization of Public Finance and Tax Law Research of Central and Eastern European Countries (Centrum Informacji i Organizacji Badań Finansów Publicznych i Prawa Podatkowego Krajów Europy Środkowej i Wschodniej) and Polish Economic Society (Polskie Towarzystwo Ekonomiczne).

She was awarded the following orders and accolades: Silver Cross of Merit (Srebrny Krzyż Zasługi), Silver Medal for Long-term Service (Srebrny Medal za Długoletnią Służbę), Medal of the Commission of National Education (Medal Komisji Edukacji Narodowej), awards of the Minister of National Education and of the President of the University of Economics in Katowice.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2015. In the Supervisory Board of the 5th common term of office she is the Vice-Chair of the Supervisory Board and the Head of the Audit Committee of the Supervisory Board

Jacek Szyke – Secretary of the Supervisory Board

A graduate of Faculty of Economics of Łódź University and of the Faculty of Electric Engineering of the Technical University in Poznań where he also obtained a PhD in technical science.

He has yearslong professional experience associated with the utility scale power industry where he climbed up all levels of the career ladder, starting with an intern, through foreman, Head of the Safety and Instrumentation and & Control Department (Zakład Energetyczny Kalisz and Łódź), Engineer On Duty Responsible for the Operation (Elektrociepłownia Łódź), up to the position of the Chief Engineer (Zakład Energetyczny Łódź and Płock) and General Manager (Zakład Energetyczny Płock and Elektrociepłownia Siekierki). He also worked as the Contract Manager in Libya. The owner and President of the JES ENERGY consulting company.

State orders awarded: Golden Cross of Merit (Złoty Krzyż Zasługi), Knight's Order (Krzyż Kawalerski). Industry orders awarded: Distinguished for the following sectors: Power, Construction, Communications, Firefighting, Culture and Heat industry.

The author of more than 100 articles, publications and books, including: “Wspomnienia o tradycji i zwyczajach pracy w energetyce” (Memories of traditions and customs related to working in the power utilities sector), “O energetyce z sentymentem” (About electric utilities sector with a sentiment), “Historia Polskiej Elektroenergetyki” (History of Poland's Power Industry), “Złota Księga Elektroenergetyki” (Golden Book of Power Industry), “Grupa TAURON – monografia” (TAURON Group – monograph).

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since September 14, 2010. In the Supervisory Board of the 5th common term of office he is the Secretary of the Supervisory Board and the Head of the Strategy Committee of the Supervisory Board as well as a member of the Audit Committee of the Supervisory Board.

Radosław Domagalski-Łabędzki – Member of the Supervisory Board

A graduate of Łódź University (master's degree in law). Completed Executive MBA studies at Rutgers University in New Jersey. Visiting fellow at the German Munster and Mannheim Universities.

A manager with a broad practical experience in managing complex international business projects. He prepared and effectively implemented an expansion strategy in Asia for one of Poland's largest capital groups.

In 2006–2013 the President of the Management Board of Magellan Trading Shanghai Co. Ltd in China. Prior to that he worked as a lawyer at GSP Group Sp. z o.o. in Łódź, and also at American Enterprise Institute in Washington – one of the largest American think-thanks.

Between December 2015 and October 2016 the Undersecretary of State at the Ministry of Development, responsible, among others, for promoting the Polish economy, a member of the Financial Supervision Commission (Komisja Nadzoru Finansowego).

Since October 2016 until March 10, 2018 he was the President of the Management Board of KGHM Polska Miedź S.A.

Co-founder of the Polish-Chinese Chamber of Industry and Commerce in Shanghai. An author of many business publications.

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2017. In the Supervisory Board of the 5th common term of office he is a member of the Audit Committee of the Supervisory Board.

Barbara Katarzyna Łasak-Jarszak – Member of the Supervisory Board

A graduate of the Faculty of Law and Administration of the Warsaw University.

Between January 1997 and February 2017 she was working at the Legal Department of the Ministry of State Treasury. Between April 1998 and February 2017 she headed an organizational unit of the Legal Department providing legal services for the Ministry. Since March 1 2017 the Head of the State Property and Finance Division of the State Treasury Department of the Chancellery of the Prime Minister where she is dealing with. among others, with the issues related to the new principles of managing the state owned property.

In 1999–2001 a member of the Disciplinary Commission of the Ministry of State Treasury. In 1999–2005 deputy public finance auditor for the Minister of State Treasury.

He has yearslong professional experience of holding seats on supervisory boards of State Treasury owned companies, including: ZPP “Lenora” sp. z o.o., Koneckie Zakłady Odlewnicze S.A., Uzdrowisko Busko-Zdrój S.A., ŚWWG Polmos S.A., Stocznia Gdynia S.A., Archimedes S.A., PSO “Maskpol” S.A., ZG “Dom Słowa Polskiego” S.A. in liquidation, Fundusz Rozwoju Spółek S.A., Zakłady Mięsne Nisko S.A.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2017. In the Supervisory Board of the 5th common term of office she is a member of the Nominations and Compensation Committee of the Supervisory Board.

Paweł Pampuszko – Member of the Supervisory Board

A graduate of the Faculty of Law and Administration of the University of Silesia in Katowice, a lawyer entered on the list of lawyers maintained by the Solicitors Regulation Authority (Izba Adwokacka) in Katowice.

During his yearslong professional career he gained significant experience with respect to negotiating contracts as part of major industrial and business undertakings, and also preparing and conducting significant court disputes where it was necessary to become familiar with non-legal specialist issues and close cooperation with specialists in other fields. He was also actively involved in identifying and eliminating deficiencies in the operations of the corporations’ authorities.

He gained professional experience related to providing legal services for business entities by working in 2005–2009, among others, at Kancelaria Biura Prawne Babula i Wspólnicy sp. k., Kancelaria Adwokatów i Radców Prawnych Ślązak, Zapiór & Partnerzy, SILEGE S.C. and Woszym Technologies sp.j. In 2009–2011 he was running his own legal practice. Since 2011 till now he has been a founding partner at law firm Kuś-Zielińska, Pampuszko i Wspólnicy – Adwokaci i Radcy Prawni sp.j.

He was a member of supervisory authorities in the non-government organizations and corporations: CHK S.A. and Medicina Pro Humana Foundation.

He is an author of publications on medical law.

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2017. In the Supervisory Board of the 5th common term of office he is a member of the Strategy Committee of the Supervisory Board.

Jan Płudowski – Member of the Supervisory Board

A graduate of the Faculty of Electric Engineering of the Silesian University of Technology in Gliwice. He also completed post-graduate studies at the Faculty of Electric Engineering of the Gdańsk University of Technology, at the University of Economics (formerly K. Adamiecki Academy of Economics) in Katowice in the field of corporate finance management and at the Faculty of Management and Services Economics of the University of Szczecin in the field of marketing and corporate management.

Professionally associated with the power sector, he gained professional experience by climbing up all levels of the career ladder. He was working, among others, as the Regional Chief Power Engineer (PKP Śląska Dyrekcja Okręgowa Kolei Państwowych (Polish State Railways’ Silesian Regional Board) in Katowice), Director of Zakład Energetyki Kolejowej (Railways’ Power Unit) in Katowice and the Head of the Power Management Department (PKP Dyrekcja Energetyki Kolejowej (Polish State Railways’ Power Unit Board) in Warsaw), Director of the Cash Flow Office (“PKP Energetyka” sp. z o.o. in Warsaw). He is currently holding the position of the Project Coordinator Director at “PKP Energetyka” S.A. in Warsaw.

In 2007–2008 he was a member of the Supervisory Board of Spółka Energetyczna Jastrzębie S.A.

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since December 30, 2016. In the Supervisory Board of the 5th common term of office he is a member of the Audit Committee of the Supervisory Board and a member of the Strategy Committee of the Supervisory Board.

Agnieszka Woźniak – Member of the Supervisory Board

A graduate of the Faculty of Law and Administration of the UMCS University in Lublin. A lawyer by education.

In 2001–2015 she worked at the Ministry of Economy where she climbed up all levels of the career ladder, starting from a referendary, through the positions of a specialist, chief specialist, head of division, deputy director and director. Since 2005 an appointed civil servant. She has been associated with the Ministry of Energy since it was formed, i.e. since November 2015, where she is currently holding the position of the Director of the Minister's Office.

She has yearslong experience in personnel management. She was dealing with matters related to audits, organizational affairs of the office, public procurement, personnel issues. She was also holding the position of the Plenipotentiary of the General Director for the Integrated Management System.

She has experience related to supervising the operations of State Treasury owned companies. Between January 2009 and June 2014 a member of the Supervisory Board of Węglokoks S.A. with its seat in Katowice.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since December 16, 2016. In the Supervisory Board of the 5th common term of office she is a member of the Nominations and Compensation Committee of the Supervisory Board and a member of the Strategy Committee of the Supervisory Board.

The detailed description of the experience and competences of the members of the Supervisory Board is published on the Company's website http://www.tauron.pl/.

Description of the operations

Detailed description of the Supervisory Board's operations is provided in the Code of Commercial Companies, the company's Articles of Association which are available on the company's website http://www.tauron.pl/ and in the *Regulations of the Supervisory Board of TAURON Polska Energia S.A. with its seat in Katowice*.

The main form of the Supervisory Board overseeing the Company's operations shall be the meetings of the Supervisory Board. Supervisory Board shall perform its obligations collectively. Meetings of the Supervisory Board shall be convened by the Chairperson of the Supervisory Board or Vice Chairperson of the Supervisory Board by presenting a detailed agenda:

1) in accordance with the decisions taken by the Supervisory Board,
2) of his/her own initiative,
3) at a written request of each member of the Supervisory Board,
4) at a written request of the Management Board.

Meetings of the Supervisory Board shall be held at the Company's seat. In justified cases a meeting may be convened at a different venue.

In order to convene a meeting all members of the Supervisory Board must be invited in writing at least 7 days before the date of the Supervisory Board's meeting. For important reasons the Chairperson of the Supervisory Board may shorten this period to 2 days, defining the way the invitations should be distributed. Notifications of the Supervisory Board's meeting shall be sent by fax or electronic mail and confirmed by phone. In the notification of the Supervisory Board's meeting the Chairperson shall define the date of the meeting, venue of the meeting and the detailed draft agenda. Supervisory Board shall meet on as needed basis, however not less frequently than once every 2 months. Supervisory Board may hold meetings without convening a formal meeting if all members of the Supervisory Board are present and nobody objects against the fact of holding the meeting or against the agenda.

A change of the proposed agenda may occur when all members of the Supervisory Board are present at the meeting and no one raises an objection against the agenda. An issue not included in the agenda should be included in the agenda of the next meeting.

Participation in a meeting of the Supervisory Board shall be a Supervisory Board member's duty. A member of the Supervisory Board shall provide information on the reason for his/her absence in writing. Excusing an absence of a member of the Supervisory Board shall require a resolution of the Supervisory Board. Members of the company's Management Board may take part in the Supervisory Board's meetings unless the Supervisory Board raises an objection. Participation of the Management Board's members in the Supervisory Board meetings shall be mandatory if they have been invited by the Chairperson of the Supervisory Board. Other persons may also take part in the meetings if they have been invited in the above mentioned way.

Supervisory Board may seek opinions of legal counsels who provide regular legal advice for the company, as well as, in justified cases, it may appoint and invite to meetings of the Supervisory Board appropriate experts in order to seek their opinion and make the right decision. In the above mentioned cases the Supervisory Board shall pass a resolution on commissioning the selected expert (auditing, consulting company) to carry out the work, obligating the Company's Management Board to conclude an applicable agreement.

Meetings of the Supervisory Board shall be chaired by the Chairperson of the Supervisory Board, and in case of his/her absence by the Vice Chairperson. For important reasons, with the consent of the majority of members of the Supervisory Board present at the meeting, the chairperson chairing the meeting shall be obligated to subject to a vote a motion to interrupt the meeting and set the date of resuming the meeting of the Supervisory Board. Supervisory Board shall make decisions in the form of resolutions. Supervisory Board's resolutions shall be passed mainly at its meetings. Supervisory Board shall pass resolutions if at least half of its members are present at the meeting and all its members have been invited in the appropriate way defined in the Regulations. Subject to the mandatory legal regulations in force, including the Code of Commercial Companies and the provisions of the company's Articles of Association, the Supervisory Board shall pass resolutions by an absolute majority of votes of the persons present at the meeting where the absolute majority of votes shall be understood as more votes cast "for" than "against" and "abstain". Resolutions shall not be passed on matters not included in the agenda unless all members of the Supervisory Board are present and nobody raises an objection. This shall not apply to resolutions on excusing a Supervisory Board's member's absence at the meeting. Resolutions shall be voted on in an open ballot. A secret ballot shall be ordered:

1) at the request of at least one member of the Supervisory Board,
2) in personnel related matters.

In accordance with the company's Articles of Association the Supervisory Board may pass resolutions in writing or using means of direct remote communications. Passing a resolution in such way shall require a prior notification of all members of the Supervisory Board of the content of the draft resolution. Passing resolutions this way shall not apply to appointing the Chairperson, the Vice Chairperson and the Secretary of the Supervisory Board, appointing or suspending from office a member of the Management Board and dismissing these persons, as well as other matters that require a secret ballot vote. When voting on a resolution in the aforementioned way a member of the Supervisory Board shall indicate his/her vote, i.e. "for", "against" or "abstain". In case a member of the Supervisory Board fails to indicate his/her vote by the time defined by the Chairperson the resolution shall not be passed. A resolution with a note that it has been passed in writing or by voting using means of direct remote communications shall be signed by the Chairperson of the Supervisory Board. Resolutions passed this way shall be presented at the forthcoming meeting of the Supervisory Board along with the result of the voting.

Members of the Supervisory Board shall be allowed to take part in the meeting and vote on resolutions during such meeting using means of direct remote communications, i.e. a conference call or a video conference, subject to a proviso that at least half of its members are present at the meeting's venue indicated in the notification of the meeting and a secure communications link is technically possible.

Members of the Supervisory Board shall take part in meetings and exercise their rights and responsibilities in person, and while performing their duties they shall be obliged to act with due diligence. Members of the Supervisory Board shall be obliged to keep confidential information related to the company's activities that they have acquired in connection with holding their seat or on another occasion. Supervisory Board shall perform its activities collectively.

Supervisory Board may, for important reasons, delegate its individual members to perform certain supervision actions on their own for a defined period of time. Supervisory Board may delegate its members, for a period not longer than three months, to temporarily perform duties of members of the Management Board who have been dismissed, submitted their resignation or if for other reasons they cannot perform their functions. The above mentioned delegation shall require obtaining a consent of the member of the Supervisory Board who is to be delegated.

The detailed description of the activities of the Supervisory Board in the last financial year is provided in the Report on the Activities of the Supervisory Board, submitted on annual basis to the General Meeting of Shareholders and then published on the company's website http://www.tauron.pl/.

Supervisory Board may appoint from among its members permanent or temporary (ad-hoc) working groups, committees to perform specific actions. Supervisory Board's standing committees shall be:

1) Audit Committee of the Supervisory Board of TAURON Polska Energia S.A. (Audit Committee),
2) Nominations and Compensation Committee of the Supervisory Board of TAURON Polska Energia S.A. (Nominations and Compensation Committee),
3) Strategy Committee of the Supervisory Board of TAURON Polska Energia S.A. (Strategy Committee).

Membership, tasks and rules of operation of the above mentioned committees shall be defined in the regulations thereof passed by the Supervisory Board.

6.11.3. Audit Committee

Due to the changes to the membership of the Supervisory Board of the Company introduced in 2017, the Supervisory Board also made changes to the membership of the Audit Committee.

Members of the Audit Committee as of December 31, 2017 and as of the day of drawing up this report

1. Teresa Famulska – Head of the Audit Committee,
2. Beata Chłodzińska – Member of the Audit Committee,
3. Radosław Domagalski-Łabędzki – Member of the Audit Committee,
4. Jan Płudowski – Member of the Audit Committee,
5. Jacek Szyke – Member of the Audit Committee.

Changes to the Audit Committee's membership

As of January 1, 2017 the Audit Committee was composed of the following members: Beata Chłodzińska (Head of the Audit Committee), Jacek Rawecki and Jacek Szyke.

On January 30, 2017 the Supervisory Board appointed the following members of the Audit Committee: Stanisław Bortkiewicz and Jan Płudowski. On the same day the Audit Committee elected, from among its members, Stanisław Bortkiewicz as the Head of the Audit Committee.

On May 25, 2017 Jacek Rawecki submitted a statement on the resignation, as of May 26, 2017, from the function of a member of the Company's Supervisory Board. Consequently, his membership in the Audit Committee also expired.

On May 29, 2017, due to the end of the 4th term of the Supervisory Board mandates of members of the Supervisory Board expired and consequently their membership in the Audit Committee expired.

On June 20, 2017, due to the appointment, as of May 29, 2017, of members of the Supervisory Board of the 5th term, the Supervisory Board appointed the Audit Committee with the following members: Beata Chłodzińska, Radosław Domagalski-Łabędzki, Teresa Famulska, Jan Płudowski and Jacek Szyke. On the same day the Audit Committee, during the first meeting of the 5th term, elected Teresa Famulska as the Head of the Audit Committee.

No other changes to the membership of the Audit Committee had been made as of the day of disclosing this report.

Information on the independence of members of the Audit Committee as of December 31, 2017

The membership (composition) of the Audit Committee is in compliance with the requirements defined in the *law of May 11, 2017 on certified auditors, audit companies and public supervision*. The evaluation of independence and the statutory requirements with respect to the knowledge and skills of the individual members of the Audit Committee was made by the Supervisory Board Rada based on the relevant statements submitted by the members of the Audit Committee. Three members of the Audit Committee comply with the statutory requirements related to independence, including the Head of the Audit Committee who also has knowledge and skills in the field of accounting and auditing financial statements. Two members of the Audit Committee: Jacek Szyke and Jan Płudowski, knowledge and skills in the field of energy, i.e. the Company's industry.

The independence requirements defined for the members of the Audit Committee by the above law are met by the following members of the Audit Committee:

1) Teresa Famulska,
2) Jan Płudowski,
3) Jacek Szyke.

The other members of the Audit Committee do not meet the independence requirements defined by the above law.

As of the day of drawing up this report a member of the Supervisory Board, Beata Chłodzińska, met the independence requirements defined by the above law.

Tasks and competence of the Audit Committee

The tasks and competence of the Audit Committee with the coming into force on June 21, 2017 of the law of May 11, 2017 on certified auditors, audit companies and public supervision, have been verified and aligned with the current legal regulations in force and adopted by the Supervisory Board at the motion of the Audit Committee in the form of the new Regulations of of the Audit Committee of the Supervisory Board of TAURON Polska Energia S.A.

The tasks and competence of the Audit Committee as of the day of drawing up this report are presented in the below table.

Table no. 42. Competence of the Audit Committee

Competence of the Audit Committee
as of December 31, 2017 and as of the day of drawing up this report

1. monitoring:
   1) the Company's financial reporting process,
   2) the effectiveness of internal control, risk management, compliance and internal audit systems, including with respect to the financial reporting,
   3) monitoring of performing of financial revisions, in particular performing of an audit by an audit company, taking into account any conclusions (motions) and arrangements of the Audit Supervision Committee stemming from an audit (inspection) performed at an audit company,
2. controlling and monitoring of independence and impartiality of the chartered accountant (certified auditor) and the entity entitled to examine financial statements, including rendering by them services other than financial audit, monitoring the independence of a certified auditor and audit company, in particular in case other services than an audit are provided for the benefit of the Company,
3. performing the evaluation of independence of the certified auditor and expressing consent for performing by him of permitted services not constituting the audit within the Company,
4. developing the policy foe selecting the auditing company to perform the audit,
5. developing a policy of performing by the auditing company performing the audit, entities related with the auditing company and members of the auditing company's corporate network of permitted services no constituting the audit,
6. defining the procedure for selecting the auditing company by the Company,
7. presenting to the Supervisory Board of recommendation for selection of the auditing company responsible for performing the statutory audit or review of financial statements, as required under Art. 130 Paras 2 and 3 of the *Act of 11 May 2017 on certified auditors, auditing companies and public oversight* and in Art. 16.2 *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*, in line with policies referred to above in items 4 and 5,
8. informing the Supervisory Board of audit results and explaining as to who did the audit contribute to trustworthiness of financial reporting in the Company, and also what was the role of the Audit Committee in course of the audit,
9. presenting recommendations aimed at ensuring reliability of the financial reporting process within the Company,
10. performing other activities vested with audit committees pursuant to *Act of 11 May 2017 on certified auditors, auditing companies and public oversight, 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 and Act of 29 September 1994 – the Accounting Act*.

The detailed description of the activities of the Audit Committee in the last financial year is provided in the report on the activities of the Supervisory Board submitted on annual basis to the General Meeting of Shareholders and published on the Company's website http://www.tauron.pl/.

6.11.4. Nominations and Compensation Committee

Due to the changes to the membership of the Supervisory Board of the Company introduced in 2017, the Supervisory Board also made changes to the membership of the Nominations and Compensation Committee

Members of the Nominations and Compensation Committee as of December 31, 2017 and as of the day of drawing up this report

1. Beata Chłodzińska – Head of the Nominations and Compensation Committee,
2. Barbara Łasak-Jarszak – Member of the Nominations and Compensation Committee,
3. Agnieszka Woźniak – Member of the Nominations and Compensation Committee.

Changes to the Nominations and Compensation Committee's membership

As of January 1, 2017 the Nominations and Compensation Committee was composed of the following members: Beata Chłodzińska (Head), Leszek Koziorowski i Agnieszka Woźniak.

On May 29, 2017, due to the end of the 4th term of the Supervisory Board mandates of members of the Supervisory Board expired and consequently their membership in the Nominations and Compensation Committee expired.

On June 20, 2017, due to the appointment, as of May 29, 2017, of members of the Supervisory Board of the 5th term, the Supervisory Board appointed the Nominations and Compensation Committee with the following members: Beata Chłodzińska, Barbara Łasak-Jarszak and Agnieszka Woźniak. On the same day the Nominations and Compensation Committee, during the first meeting of the 5th term, elected Beata Chłodzińska as the Head of Nominations and Compensation Committee.

No other changes to the membership of the Nominations and Compensation Committee had been made as of the day of disclosing this report.

Tasks and competence of the Nominations and Compensation Committee

The tasks and competence of the Nominations and Compensation Committee did not change in 2017.

The tasks and competence of the Nominations and Compensation Committee as of December 31, 2017 and as of the day of drawing up this report are presented in the below table

Table no. 43. Competence of the Nominations and Compensation Committee

Competence of the Nominations and Compensation Committee	
as of December 31, 2017 and as of the day of drawing up this report	
1.	recommending to the Supervisory Board a recruitment procedure for the positions of members of the company's Management Board,
2.	evaluating candidates for members of the Management Board and providing the Supervisory Board with opinions in this respect,
3.	recommending to the Supervisory Board a form and content of agreements to be concluded with members of the Management Board,
4.	recommending to the Supervisory Board a compensation and bonus system for members of the Management Board,
5.	recommending to the Supervisory Board the need to suspend a member of the Management Board for important reasons,
6.	recommending to the Supervisory Board the need to delegate a member of the Supervisory Board to temporarily perform the duties of members of the Management Board who cannot perform their duties, along with a compensation proposal.

The detailed description of the activities of the Nominations and Compensation Committee in the last financial year is provided in the Report on the activities of the Supervisory Board submitted on annual basis to the General Meeting of Shareholders and published on the Company's website http://www.tauron.pl/.

6.11.5. Strategy Committee

Due to the changes to the membership of the Supervisory Board of the Company introduced in 2017, the Supervisory Board also made changes to the membership of the Strategy Committee

Members of the Strategy Committee as of December 31, 2017 and as of the day of drawing up this report

1. Jacek Szyke – Head of the Strategy Committee,
2. Beata Chłodzińska – Member of the Strategy Committee,
3. Paweł Pampuszko – Member of the Strategy Committee,
4. Jan Płudowski – Member of the Strategy Committee,
5. Agnieszka Woźniak – Member of the Strategy Committee.

Changes to the Strategy Committee's membership

As of January 1, 2017 the Strategy Committee was composed of the following members: Jacek Szyke (Head), Beata Chłodzińska, Anna Mańk i Stefan Świątkowski.

On March 15, 2017 the Supervisory Board passed a resolution on appointing as members of the Strategy Committee: Stanisław Bortkiewicz and Jan Płudowski.

On May 29, 2017, due to the end of the 4th term of the Supervisory Board mandates of members of the Supervisory Board expired and consequently their membership in the Strategy Committee expired.

On June 20, 2017, due to the appointment, as of May 29, 2017, of members of the Supervisory Board of the 5th term, the Supervisory Board appointed the Strategy Committee with the following members: Jacek Szyke, Beata Chłodzińska, Paweł Pampuszko, Jan Płudowski i Agnieszka Woźniak. On the same day the Strategy Committee, during the first meeting of the 5th term, elected Jacek Szyke as the head of the Strategy Committee.

No other changes to the membership of the Strategy Committee had been made as of the day of disclosing this report.

Tasks and competence of the Strategy Committee

The tasks and competence of the Strategy Committee did not change in 2017. The tasks and competence of the Strategy Committee as of December 31, 2017 and as of the day of drawing up this report are presented in the below table.

Table no. 44. Competence of the Strategy Committee

Competence of the Strategy Committee	
as of December 31, 2017 and as of the day of drawing up this report	
1.	evaluating the Company's and TAURON Capital Group's Strategy and presenting the results of such evaluation to the Supervisory Board,
2.	recommending to the Supervisory Board the scope and deadlines for submitting the long term strategic plans by the Management Board,
3.	evaluating the impact of planned and currently undertaken strategic investment projects on the Company's assets,
4.	monitoring the implementation of strategic investment tasks,
5.	evaluating activities related to the use of material Company's assets,
6.	providing opinions on strategic documents submitted to the Supervisory Board by the Management Board.

The detailed description of the activities of the Strategy Committee in the last financial year is provided in the report on the activities of the Supervisory Board submitted on annual basis to the General Meeting of Shareholders and published on the Company's website http://www.tauron.pl/.

6.11.6. Description of activities of the Committees of the Supervisory Board

The detailed description of the operations of the Committees of the Supervisory Board is provided in the Regulations of individual Committees of the Supervisory Board of TAURON Polska Energia S.A.

The Committees of the Supervisory Board are advisory and opinion-making bodies acting collectively as a part of the Supervisory Board and perform support and advisory functions towards the Supervisory Board. The tasks of the Committees of the Supervisory Board are carried out by submitting motions, recommendations, opinions and statements on the scope of its tasks to the Supervisory Board, by means of resolutions. The Committees of the Supervisory Board are independent of the Management Board of the Company. The Management Board may not issue binding orders to the Committees of the Supervisory Board concerning performing their tasks.

The Audt Committee and the Nominations and Compensation Committee of the Supervisory Board are composed of three to five members, while the Strategy Committee is composed of three to seven members. The activities of the individual Committees are managed by their Chairpersons (Heads).

Meetings of the Committees are convened by the Chairperson of the specific Committee on his/her own initiative or upon the motion of a member of the Committee or Chairperson of the Supervisory Board and they are held on as needed basis. In case of the Audit Committee the meetings are convened at least on a quarterly basis. The Chairpersons of the Committees may invite members of the Supervisory Board, who are not members of the specific Committee, members of the Management Board and employees of the Company as well as other persons working or cooperating with the Company to the meetings of the Committees. The Chairperson of the specific Committee or a person appointed by him/her submits motions, recommendations and reports to the Supervisory Board.

The Committees of the Supervisory Board pass resolutions if at least a half of their members were present at the meeting and all their members have been duly invited. The resolutions of the Committees of the Supervisory Board are adopted by an absolute majority of votes present at the meeting, where the absolute majority of votes is understood as more votes given "for" than "against" and "abstain". The Committees of the Supervisory Board may pass resolutions in writing or by using means of direct remote communication.

Members of the Committees of the Supervisory Board may also participate in meetings and vote of the adopted resolutions by using means of direct remote communication, i.e. tele- or videoconferences.

The Company's Management Board shall be informed about recommendations and assessments submitted to the Supervisory Board by the given Committee of the Supervisory Board. Every year, the Committees of the Supervisory Board provide public record information, through the Company, on their memberships, the number of meetings held and participation in the meetings during the year as well as on their main activities. In addition, the Audit Committee performs an assessment of the independence of the certified auditor and expresses its consent for the provision thereby of the permitted services that are not an audit of the Company.

The Company's Management Board provides the possibility to use the services of external advisers by the Committees to the extent required for performing the obligations of the Committees.

6.12. Description of the policy of diversity applied to the governing bodies of the Company

Diversity and openness are an integral part of both, TAURON Capital Group's business operations, as well its management policy. All of TAURON Capital Group's subsidiaries apply the policy of equal treatment and strive to ensure diversity in terms of gender, educational background, age and professional experience in relation to all employees and key managers.

With respect to the members of the corporate bodies of TAURON, i.e. the Management Board and the Supervisory Board, persons acting as Members of the Management Board are selected by the Supervisory Board, while Members of the Supervisory Board are selected by the Minister of Energy. In 2017, acting within its statutory powers, the State Treasury appointed 5 Members of the Supervisory Board and the Ordinary GM of TAURON on May 29, 2017 elected 3 Members of the Management Board. Information concerning qualifications and professional experience of persons appointed to the Management Board and the Supervisory Board is published in the relevant regulatory filings (current reports) as well as on the Company's website.

Members of the Management Board are appointed by the Supervisory Board after conducting a qualification procedure designed for verifying and assessing their qualifications and selected the best candidates. Announcement of qualification process is published on the Company's web page and in the Public Information Bulletin of the Ministry of Energy. The competition is open for any person meeting requirements set forth in the Company's By-laws and formal requirements specified in the announcement. Candidates are required to possess university level education, at least five years of employment and minimum three years of experience as managers, and have to meet requirements set forth in other legislation. No special requirements are placed on features such as sex, type of education, age and professional expertise, to the Supervisory Board is capable of assessing candidates to the Management Board with consideration of their overall capabilities and diversity requirements.

The *Diversity Policy of the TAURON Group* was implemented in 2017, the purpose of which is to strengthen awareness and organizational culture open to diversity. Implementation of the Diversity Policy enables employees to full realize their individual potential in the job environment.

Also, actions have been undertaken to prevent any discrimination by structuring the appropriate atmosphere and culture at the workplace based on key PRO corporate values – Partnership, Development and Courage, confirmed through the *Policy of combating Mobbing and Discrimination at the TAURON Group*.

7. COMPENSATION POLICY WITH RESPECT TO THE MANAGEMENT AND SUPERVISORY STAFF

7.1. Compensation system for members of the Management Board and key managers

7.1.1. General information on the adopted compensation system for members of the Management Board

In 2017 the principles of compensation of members of the Company's Management Board defined in the Resolution of the Extraordinary GM of TAURON of December 15, 2016 *on the principles for determining compensation of members of the Management Board* (Principles for determining compensation) were in force at the Company, as subsequently amended and detailed by the Supervisory Board of the Company pursuant to the resolution of December 19, 2016 *on the principles for determining compensation of members of the Management Board TAURON Polska Energia S.A.* as subsequently amended. The above principles for determining compensation are in line with the provisions of the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies*.

The adopted principles for determining compensation define the compensation system for members of the Management Board in connection with outstanding tasks aimed at the implementation of the adopted Strategy, directions of expansion and financial plans. The overriding objective of the adopted compensation system is to ensure an incentive-based compensation of the senior management staff and to create basis for their development.

Overall objectives of the compensation policy are:

1) ensuring a consistent and motivational compensation system for members of the Management Board,
2) linking the compensation rules with monitoring of the implementation of adopted strategic plans and implementation of the financial plans,
3) setting the level of compensation for the Management Board members in connection with the implementation of the management tasks set,
4) increasing the Company's value through the development of the senior management staff,
5) improving the compensation systems leading to the implementation of the Company's strategy and expansion directions.

Model of compensation for members of the Management Board is based on a two-component system for determining compensation, composed of a fixed part constituting the monthly base wage and a variable part constituting the supplementary compensation for the Company's financial year, dependent on achieving specific management objectives.

System of compensation for members of the Management Board assumes linking the variable part of the compensation with the outstanding management goals stemming from the provisions of the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies* and set, based upon these provisions, by the GM the Supervisory Board of the Company. The goal of adopting in the system of compensation, of the dependence of the compensation's variable part on achieving the management goals set is, in particular, to implement the adopted Strategy, the directions of the Company's expansion and financial plans, it also shapes a new organizational culture of the Company.

Taking into account the applicable regulations, the level of compensation for members of the Management Board is defined by the Supervisory Board, within the brackets determined by the Company's GM.

Members of the Management Board of the Company are neither covered by the bonus program based on the capital of the Company, nor do they receive any compensation or awards due to fulfilment of their functions in governing bodies of TAURON Capital Group's subsidiaries.

In 2017 the Supervisory Board updated the *Policy of compensation for Members of the supervision and management authorities (bodies) including the description of the principles for the determination thereof at TAURON Polska Energia S.A.,* in force since February 24, 2011.

7.1.2. General information on the adopted compensation system for key managers

The rules concerning compensation and bonus system for key managers and other employees are defined in the *Regulations on Compensation of Employees of TAURON Polska Energia S.A.,* adopted for application by the Management Board of the Company.

In 2017 the *Principles of Compensation at TAURON Group* were developed representing the guidelines for TAURON Capital Group's subsidiaries with respect to the personnel compensation systems, particularly taking into account the bonus system for key managers based on the management by objectives system consistent throughout TAURON Capital Group, representing a combination of the planning process, efficiency measurement process and evaluation process.

The compensation and bonus system for key managers stipulates that the level of compensation should be tied to the financial situation of TAURON Capital Group in an annual perspective, in connection with the implementation of strategic goals.

The overriding assumption of the compensation system in force is to ensure the optimum and motivating compensation level, depending on the value and type of work on a given position as well as the quality of work and effects achieved by employees.

The structure of the compensation consists of the following elements:

1) fixed part – constituting the base salary determined in accordance with the table of grade categories applicable in the Company and monthly rates of personal grade. The allocated level of basic salary reflects the value and type of work as well as the quality of employee's work, defined through the assessment of employee's competence level
2) variable part – which depends on performance results, defined through the level of accomplishment of targets and tasks within the MBO bonus system,
3) benefits – which are defined in the internal regulations of the Company

The MBO bonusing system based on market principles of awarding bonuses ensures focusing activities of key management staff on attaining objectives defined within the Strategy, as well as individual strategic objectives and development directions of individual companies within the TAURON Capital Group. This system also ensures cascading of objectives defined by the Company's Management Board at the TAURON Capital Group level and at the Company level, down to concrete, parametric tasks vested with employees of lower structural levels. The MBO bonusing system has been tied with the management by process style of operations at the TAURON Capital Group, *inter alia* by aligning the objectives with Megaprocesses defined within the TAURON Capital Group. Therefore, the introduced culture of Management by Objectives reflects the specific features of each function implemented in the Company and allows use of dialogue mechanisms between the superior and subordinate during the process of setting and assessing objectives, leading to attaining overall efficiency throughout the entire organization.

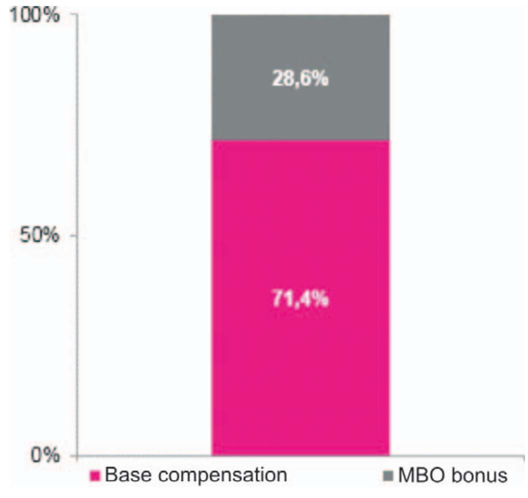
At the same time, this took enables precise correlating of KPIs defined for members of the Management Board with objectives defined for the given year for key managers of the Company. Initial assessment of accomplished objectives takes place after end of the first 6 months and after end of the year, members of the Management Board conduct final assessment of KPI performance by key managers.

Moreover, in March 2017 the bonus system for the trading area aimed at motivating to generate higher revenue for TAURON Capital Group. The trading bonus covered key managers in the trading area, however the bonus system sets an additional bonus for them only once they have topped annual trade plans.

Employees of the Company do not receive any compensation or awards on account of functions fulfilled in governing bodies of TAURON Capital Group's subsidiaries.

The below figure presents the structure of compensation for key manager positions.

Figure no. 89. Structure of compensation for key manager positions



7.1.3. Rules, terms and conditions as well level of compensation of members of the Management Board

The total amount of compensation understood as the value of salaries, awards and benefits received in cash, in kind or in any other form, due or paid by the Company to the Management Board members in 2017 reached the gross amount of PLN 4 534 thousand.

The compensation of members of the Company's Management Board in 2017, broken down into components, is presented in the below table.

Table no. 45. Compensation of members of the Company's Management Board in 2017 broken down into components

No.	Name	Period of holding the position in 2017	Compensation[1] (PLN '000)	Bonus[1] (PLN '000)	Other benefits[1] (PLN '000)	Total (PLN '000)
1.	Filip Grzegorczyk[2]	01.01.2017 – 31.12.2017	793	–	24	817
2.	Jarosław Broda[3]	01.01.2017 – 31.12.2017	803	226	79	1 108
3.	Kamil Kamiński[3]	01.01.2017 – 31.12.2017	792	181	77	1 050
4.	Marek Wadowski[3]	01.01.2017 – 31.12.2017	863	181	36	1 080
5.	Piotr Zawistowski	01.01.2017 – 15.03.2017	186	226	69	481
	Total		**3 437**	**812**	**285**	**4 534**

[1] *Excluding markups (surcharges).*
[2] *Compensation in accordance with the agreement on the provision of management services in force.*
[3] *From January 1, 2017 till March 15, 2017 the compensation in accordance with the labor agreement, while from March 16, 2017 till December 31, 2017 the compensation in accordance with the agreement on the provision of management services.*

Members of the Management Board did not receive compensation or bonuses for performing functions in the corporate bodies of TAURON Capital Group's subsidiaries in 2017.

From January 1, 2017 till March 15, 2017 members of the Management Board received the compensation in accordance with the labor agreement (except for the President of the Management Board who received the compensation in accordance with the agreement on the provision of management services). From March 16, 2017 all members of the Management Board appointed for the 5th term received the compensation in accordance with the agreement on the provision of management services, prepared in accordance with the *law of June 9, 2016 on the principles of determining the compensation of persons managing certain companies.*

Model of compensation for members of the Management Board, defined in the agreements on the provision of management services is based on a two-component system for determining compensation, composed of a fixed part (monthly base wage) and a variable part (supplementary compensation for the Company's financial year), dependent on fulfiling specific result-based criteria, i.e. achieving management objectives.

System of compensation for members of the Management Board assumes linking the variable part of the compensation with the outstanding management goals stemming from the provisions of the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies* and set, based upon these provisions, by the GM the Supervisory Board of the Company. The goal of adopting in the system of compensation, of the dependence of the compensation's variable part on achieving the management goals set is, in particular, to implement the adopted Strategy, the directions of the Company's expansion and financial plans, it also shapes a new organizational culture of the Company.

The variable part of the compensation represents up to 60% of the fixed part of the compensation for the financial year, assuming the management goals set by the Supervisory Board for the given financial year have been achieved.

The Supervisory Board determines the percentage level of the variable part of the compensation for each of the following management goals:

1) achieving EBITDA at the level approved in the material and financial plan for a given financial year,
2) achieving the Net debt/EBITDA ratio at the level approved in the material and financial plan for a given financial year,
3) implementation of the "2016–2018 Efficiency Improvement Program" and achieving the total effect at the level approved in the material and financial plan for a given financial year,
4) implementation of the non-financial management goals objectives.

The variable part of the compensation for achieving the financial management goals is allocated based on the data derived from the audited consolidated financial statements of the Company for the given financial year.

The variable part of the compensation for achieving the non-financial management goals is allocated based on the achievement of specific objectives in the given financial year, based on the assessment of their performance by the Supervisory Board.

7.1.4. Agreements concluded with managing persons which envisage compensation in case of their resignation or dismissal from the position held, without material reason, or if their dismissal or resignation takes place as a result of the merger of the Company through takeover

According to the agreements on the provision of management services concluded with the members of the Management Board on March 15, 2017 envisage, in case of termination or dissolution of the agreement by the Company for reasons other than defined therein, a payout of the severance payment at a level of three-fold fixed part of the compensation, under the condition of fulfilment of the function by them over a period of at least 12 months prior to the termination of the agreement.

Furthermore, due to the access of members of the Management Board to confidential information the disclosure of which could expose the Company and TAURON Capital Group's subsidiaries to losses, the aforementioned agreements on the provision of management services include non-competition provisions applicable after the expiry of the term of office. Under the aforementioned agreements members of the Management Board undertook to refrain from conducting competitive activities in the specified period in return for compensation.

Members of the Company's Management Board did not hold positions of members of Management Boards of subsidiaries (companies included) in TAURON Capital Group prior to being appointed as members of the Company's Management Board.

7.1.5. Non-financial components of compensation allocated to members of the Management Board and key managers

Non-financial components of the compensation of members of the Management Board

Members of the Management Board, in accordance with the agreements on provision of management services, are entitled to:

1) refinancing by the Company of the cost of training up to the net amount of PLN 15 000 in a calendar year,
2) use a company car,
3) use the technical devices required to perform the obligations under the concluded agreement.

Non-financial components of the compensation of key managers

Staff members employed at key positions by the Company are entitled to use the following benefits and non-financial components of the compensation offered by the Company:

1) participate in the Employee Pension Scheme operated by the employer (under the condition of being employed in the Company or one of the subsidiaries of TAURON Capital Group over a period of at least one year),
2) use the medical package financed from the Company funds,
3) use a company car allocated for sole disposal,
4) use company accommodation in case if the availability of the employee is required due to the nature of his/her work and scope of responsibilities.

7.1.6. Information on changes to the compensation policy over the last financial year

On May 29, 2017 the Ordinary GM amended resolution no. 5 of the Extraordinary GM of TAURON of December 15, 2016 *on the principles for determining compensation of members of the Management Board,* by adding an extra management goal to be achieved by members of the Management Board by December 31, 2017, making the payment of the variable part of the compensation contingent, covering the performance of the obligations mentioned in art. 17–20, art. 22 and art. 23 *of the law of December 16, 2016 on the state assets management principles.*

With a view to implement the principles to determine compensation passed by the GM in December 2016 r., on March 15, 2017 agreements on the provision of management services were concluded with the members of the Management Board appointed for the common 5th term in office. The agreement on the provision of management services with the President of the Management Board had been concluded earlier, meanwhile labor contracts had been concluded earlier with the other members of the Management Board.

7.1.7. Assessment of functioning of the compensation policy in terms of fulfilment of its objectives, in particular, the long-term growth in shareholders' value and stability of the undertaking performance

The applied compensation system for members of the Management Board is compliant with the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies*. The incentive-based and consistent system is provided, linked with the monitoring of annual financial plans and the adopted Strategy and development (expansion) directions

The form, structure and level of compensation correspond to market conditions and are oriented towards enabling the recruitment and maintaining of individuals fulfilling the criteria required for running the Company in the manner taking into account shareholders' interests (building the Company's value for shareholders), as well as prevent conflicts of interest from arising among members of the Management Board and shareholders. At the same time, they are constructed in the manner which is transparent for investors, so that their trust towards the Company is built and they are able to express their opinions using the applicable procedures.

Information policy on the form, structure and level of compensation of members of the Management Board and the Supervisory Board is conducted by the Company in communication with the Supervisory Board in a manner that is in compliance wth the regulations in force and best market practice.

The disbursement of variable components of compensation is linked with the pre-defined, measurable management goals. The set management goals should foster long-term stability of the Company.

The indicators (criteria) determining obtaining and level of variable components of the compensation are defined in accordance with the SMART principle, thus, they also display such features as: precision, measurability, achievability, materiality and defining in time.

The compensation and bonus system for both Members of the Management Board of the Company as well as the key managers in force at TAURON supports the implementation of strategic goals and determines the compensation depending on the financial situation of the Company and TAURON Capital Group in an annual perspective.

7.2. Compensation system for members of the Supervisory Board

In 2017 the system of compensation for members of the Supervisory Board of the Company defined in the Resolution of the Extraordinary GM of TAURON of December 15, 2016 *on the principles for determining compensation for members of the Supervisory Board of TAURON Polska Energia S.A.* was in force, adopted as the implementation of the provisions of the *Act of 9 June 2016 concerning principles for determining compensation of persons managing certain companies* (Journal of Laws of 2016, item 1202).

In accordance with the aforementioned Resolution of the Extraordinary GM a monthly compensation of Supervisory Board members is determined as a product of the average monthly compensation in the enterprise sector, excluding payment of profit distribution bonuses in the fourth quarter of the preceding year, announced by the President of the Central Statistics Office and the multiplier:

1) for the chairperson of the Supervisory Board – 1.7
2) for other members of the Supervisory Board – 1.5

Members of the Supervisory Board are entitled to receive the compensation irrespective of the frequency of formally convened meetings.

The compensation does not apply for a month in which a member of the Supervisory Board was not present at any of the formally convened meetings, for unjustified reasons. The decision on excusing or failure to excuse the absence of a member of the Supervisory Board at its meeting is taken by the Supervisory Board by means of a resolution.

The compensation is calculated on a pro rata basis, in relation to the number of days when the function was fulfilled in case if the appointment or dismissal occurred during the calendar month.

The Company covers costs incurred in connection with the fulfilment of functions assigned to members of the Supervisory Board, in particular: costs of return transfer between the place of residence and the venue of the Supervisory Board meeting or meeting of the Supervisory Board Committee, costs of individual supervision and costs of accommodation and board.

Compensation of supervising personnel

The compensation of members of the Company's Supervisory Board in 2017 is presented in the below table.

Table no. 46. Compensation of members of the company's Supervisory Board in 2017

No.	Name	Period of holding the position in 2017	Compensation (PLN '000)
1.	Beata Chłodzińska	01.01.2017 – 31.12.2017	89
2.	Teresa Famulska	29.05.2017 – 31.12.2017	47
3.	Jacek Szyke	01.01.2017 – 31.12.2017	79
4.	Radosław Domagalski-Łabędzki	29.05.2017 – 31.12.2017	47
5.	Barbara Łasak-Jarszak	29.05.2017 – 31.12.2017	47

No.	Name	Period of holding the position in 2017	Compensation (PLN '000)
6.	Paweł Pampuszko	29.05.2017 – 31.12.2017	47
7.	Jan Płudowski	01.01.2017 – 31.12.2017	79
8.	Agnieszka Woźniak	01.01.2017 – 31.12.2017	79
9.	Jacek Rawecki	01.01.2017 – 26.05.2017	32
10.	Leszek Koziorowski	01.01.2017 – 29.05.2017	33
11.	Stefan Świątkowski	01.01.2017 – 29.05.2017	33
12.	Anna Mańk	01.01.2017 – 29.05.2017	33
13.	Stanisław Bortkiewicz	01.01.2017 – 29.05.2017	33
	Total		**677**

7.3. Liabilities arising from pensions and similar benefits for former the Members of the Management Board and the Supervisory Board

The Company does not have any liabilities towards former the Members of the Management Board and the Supervisory Board arising from pensions and similar benefits.

At the same time, it is indicated that due to the Company's liabilities towards former members of TAURON Management Board, in 2017 the total amount of PLN 2 258 thousand was paid due to bonuses for the accomplishment of KPIs in 2016 and compensations for compliance with the non-competition clause.

8. STATEMENT ON NON-FINANCIAL INFORMATION

8.1. TAURON Group's Business and Operational Model

TAURON Capital Group comprises selected companies managed jointly as a uniform economic body consisting of independent commercial law companies, led by TAURON as the parent entity.

In 2017 the *Business Model of TAURON Group* adopted by the Management Board of the Company on May 4, 2016 was in force. In order for TAURON Capital Group to effectively carry out the tasks the above document was updated by the Management Board of TAURON. A document called *Business and Operational Model of TAURON Group* (Business Model) adopted on January 23, 2018 defines TAURON Capital Group's management model, defines the high-level architecture of processes and contains guidelines concerning key performance indicators of units constituting TAURON Capital Group.

8.1.1. Assumptions of the Business Model

The key assumptions of the Business Model include building of TAURON Capital Group value, focusing on customers, transparent distribution of duties and responsibilities, effective information exchange, use of employees' knowledge, volatility of the Business Model, organisational integrity of TAURON Capital Group.

8.1.2. Company management principles

In accordance with the provisions of the *By-laws of the Management Board of TAURON Polska Energia Spółka Akcyjna with its seat in Katowice*, the Management Board conducts the affairs of the Company and represents it in all judicial and extra-judicial proceedings. All issues connected with managing the Company, which are not restricted by legal regulations and provisions of the Company's Articles of Association to the competence of the General Meeting or the Supervisory Board lie within the competence of the Company's Management Board. Cooperation of two members of the Management Board or one member of the Management Board together with a proxy is required for submitting statements on behalf of the Company.

Issues covered within the competence of the Management Board as a collective body are described in detail in section 6.8.1. of this report.

In accordance with the *Organisational Regulations of TAURON Polska Energia S.A.* (Organisational Regulations), the Company is managed directly by the Management Board of the Company as well as through proxies, Executive Directors, Managing Directors or power of attorneys.

The Company implements its tasks through:

1) separate organizational units (business units):
   - Divisions comprising independent positions and business units reporting to individual members of the Management Board and supervised by them,
   - Teams, constituting business units reporting directly to Executive Directors or Managing Directors. The activities of the team are managed by the Team Leader (Manager),
2) independent positions:
   - Managing Director manages and leads the work of subordinated Executive Directors and Teams,
   - Executive Director manages and leads the work of subordinated Teams,
   - Other independent positions which may be entrusted to Power of Attorneys, Coordinators, Consultants or Specialists,
3) temporary organisations – Project Teams established with the aim to implement tasks and projects of the Company.

8.1.3. TAURON Capital Group management principles

The main regulatory act of TAURON Group is the *Code of TAURON Group* adopted by the Management Board of the Company which regulates its operations, ensuring the implementation of the goals through tailored solutions in the area of management of TAURON Capital Group's entities, including, in particular, setting the operating objectives of companies, enabling the achievement of effects assumed in the new Strategy.

Regulations implemented in 2016 together with the Business Model led to introduction of the management by processes structure within the entire TAURON Capital Group, consisting in establishing of process subordination running horizontally within all companies of the Group. Members of the Management Board are responsible for the allocated to them process streams which are subsequently divided into Megaprocesses. Megaprocesses are owned by named managing and executive directors at TAURON. Process documentation (maps, diagrams and process sheets) defines and describes decision authorities and actions to be undertaken by individual organizational units within companies of the TAURON Capital Group. Owners of Megaprocesses decompose these into lower level processes and appoint their owners. Each process has its owner and process metrics defined by the higher level process owner. Process documentation defines the decision dependences and authorities for repeatable processes.

Management by processes model has been implemented to benefit from operating synergies between companies of the TAURON Capital Group, share and use best practices, standardize and automate processes, and to ensure coherence of actions taken within Group companies to support implementation of Group Strategy.

The essence of management by processes lies in unending search for and implementation of efficiencies along with clear and transparent division of authorities and responsibilities. Processes are modified to improve their efficiencies. Process documentation is published in the Intranet and available to all employees.

Authorities and process dependences described in process documentation supplement authorities set forth in the organizational structure of individual companies and support operations of TAURON Capital Group companies as a single organism.

Within TAURON Capital Group the Standing Committees of TAURON Capital Group are operating, including:

1) Investment Committee,
2) Risk Committee.

The aforementioned Committees were established in order to enable performing of operations in accordance with the principles of operating consistency, in compliance with the law and interests of TAURON Capital Group and its stakeholders.

The below figure presents process streams cutting across TAURON Capital Group's Lines of Business.

Figure no. 90. Process streams

Business Model identifies 23 mega processes cutting across all units of TAURON Capital Group.

The below figure presents the structure of TAURON Capital Group's processes (mega processes).

Figure no. 91. Structure of TAURON Capital Group's processes (megaprocesses)

Management processes	
1.1 Strategy	1.5 Audit
1.2 Controlling	1.6 Asset management
1.3 Corporate communication	1.7 Research and innovation
1.4 Risk management	

Operating processes	
2.1 Mining	2.4 Distribution of electricity and heat
2.2 Production of electricity and heat	2.5 Sales and Customer Service
2.3 Trade	

Support processes	
3.1 Corporate management	3.7 IT support
3.2 Mergers and acquisitions	3.8 Legal service
3.3 Finance management	3.9 Purchases
3.4 Accounting	3.10 Ensuring security
3.5 Tax management	3.11 Project implementation
3.6 Human capital management	

8.1.4. TAURON Capital Group's Lines of Business

In accordance with the Business Model in force activities are underway aimed at fully implementing the distribution of roles and responsibilities base on assigning the process competences, among:

Corporate Centre – superior business unit responsible for management of TAURON Capital Group's operations and taking the most important decisions affecting TAURON Capital Group, Lines of Business, Shared Services Centers and TAURON Capital Group's subsidiaries.

Lines of Business – seven lines of TAURON Capital Group's core operations, defined in accordance with the links of the electricity and heat production value chain, i.e.: Trading, Mining, Generation, Renewable Energy Sources (RES), Heat, Distribution and Supply.

Shared Services Centers – units responsible for the provision of specific support services (e.g. Accounting, IT, HR and payroll, insurance, customer service) in favour of other entities of TAURON Capital Group.

TAURON Capital Group's business operations are conducted based on seven Lines of Business defined in accordance with the links of the electricity and heat production value chain: Mining, Generation, Renewable Energy Sources (RES), Heat, Trading, Distribution and Supply.

The below figure presents the structure of TAURON Capital Group's Lines of Business.

Figure no. 92. Structure of TAURON Capital Group's Lines of Business

TAURON Capital Group's Shared Services Centers (CUW)

Centralizing of the support services is aimed at relieving the Corporate Centre and Lines of Business from execution of processes which are not directly associated with the conducted business operations (so-called support processes) as well as at reducing costs of the implementation of such processes due to the economy of scale and increase of the operational efficiency. Within the formal structure of TAURON Capital Group, CUWs were placed in TAURON Obsługa Klienta, TAURON Ubezpieczenia sp. z o.o. and Wsparcie Grupa TAURON subsidiaries.

8.1.5. Changes in the principles of managing TAURON Capital Group

Changes in the principles of managing the Company

Three amendments were introduced in 2017 in the Organizational By-laws at TAURON aimed to optimize management processes, i.e.:

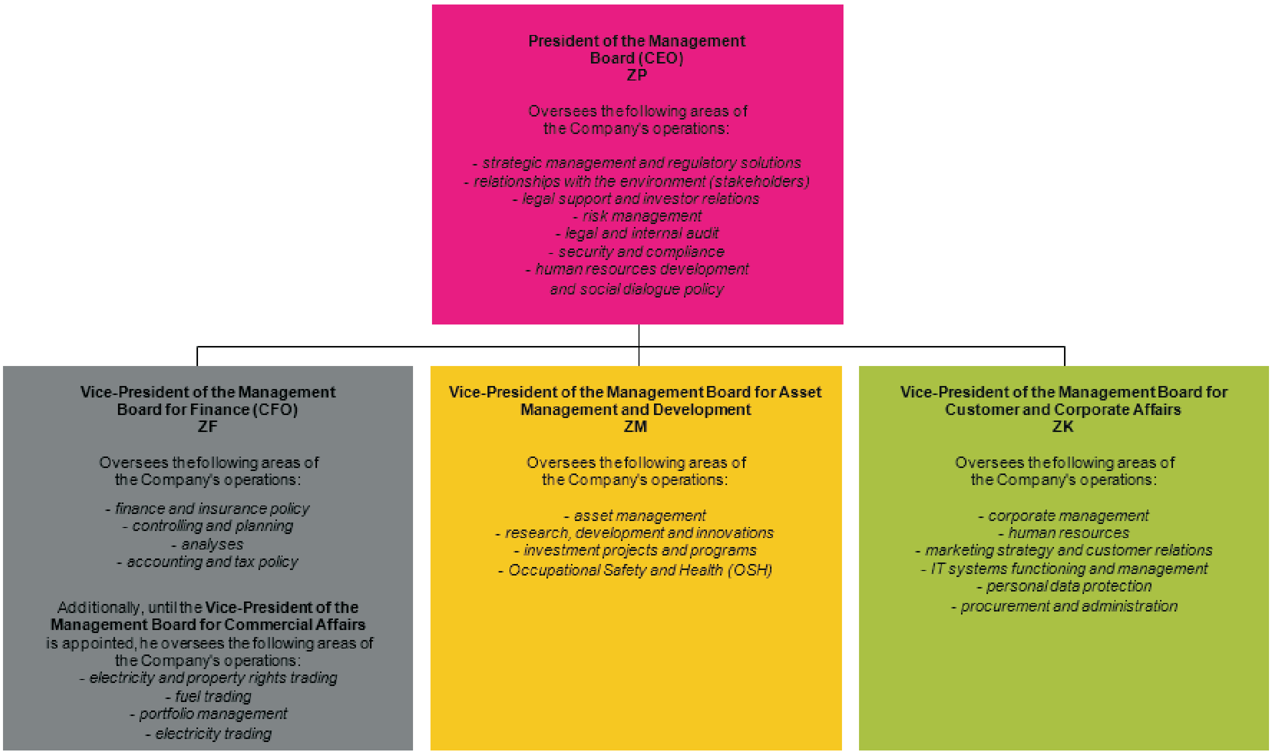
1. The following key amendments to the Organizational By-laws were enforced on 14 April 2017:
    1) Vice-President of the Management Board for Finance was vested with oversight of the development of forecasting s and tools necessary for analyzing the wholesale and retail markets by subordinating to him the activities of the Executive Director for Business Analyses,
    2) The following positions were changed: Vice-President of the Management Board for Corporate Management to Vice-President of the Management Board for Clients and Corporate Support, and Vice-President of the Management Board for Clients and Trade to Vice-President of the Management Board for Trade,
    3) The Vice-President of the Management Board for Clients and Corporate Support was vested with oversight of representing client interest inside and outside the organization by subordinating to him the Executive Director for Client Affairs,
    4) The sphere of project analysis and assessment was subordinated to the Executive Director for Investment Projects at the Division of the Vice-President of the Management Board for Asset Management and Development,
2. The following key amendments to the Organizational By-laws were enforced on 17 July 2017:
    1) The sphere of the Executive Director for External Relations at the Division of the President of the Management Board was integrated with the sphere of Executive Director for Strategy and Regulations by creating a single sphere of Executive Director for Strategic Management. Integration of both these spheres of activities was justified in light of the operational synergies existing in several planes of operations, particularly in light of the correlation between external communications and building relationships, including relationships with public administration and international authorities as well as with professional industrial organizations,
    2) The sphere of investor relations previously subordinated in the Division of the President of the Management Board to the Executive Director for External Relations was transferred to the Executive Director for Legal Issues. The purpose of this change wad to concentrate in the legal area all tasks related with ensuring adherence by the Company to principles of corporate governance and information duties of a securities issuer.
3. The following key amendments to the Organizational By-laws were enforced on 25 October 2017:
    1) The President of the Management Board was vested with:
        a) oversight over functioning of the risk management system of the TAURON Capital Group by subordinating to him the activities sphere of the Executive Director for Risk Management, who was subordinated previously to the Vice-president of the Management Board for Finance,
        b) creating and overseeing the Company's and TAURON Capital Group system of legal compliance by subordinating the sphere of the Attorney for Compliance to the Executive Director for Security and Compliance,
        c) coordinating and overseeing security activities, including IT security, technical infrastructure security, protection of confidential information and physical security by subordinating to him the sphere of the Executive Director for Security and Compliance, who was previously subordinated to the Vice-president of the Management Board for Clients and Corporate Support.
    2) Vice-president of the Management Board for Clients and Corporate Support was vested with:
        a) overseeing the formulation of the IT area functioning and management model by subordinating to him the sphere of the Executive Director for IT, who was previously subordinated to the Vice-president of the Management Board for Finance,

b) overseeing the formulation of strategy as well as standard and guidelines for protection of personal data in the Company and in the TAURON Capital Group, now subordinated to the Executive Director for IT.

At the time, due to the vacancy on position of Vice-president of the Management Board for Trade, these functions were temporarily vested as from 14 April 2017 to the Vice-president of the Management Board for Assets Management and Development, and as from 25 October 2017 temporarily to the Vice-president of the Management Board for Finance.

The below figure presents the diagram of the split of responsibilities of members of the Management Board.

Figure no. 93. Diagram of the split of responsibilities of members of the Management Board



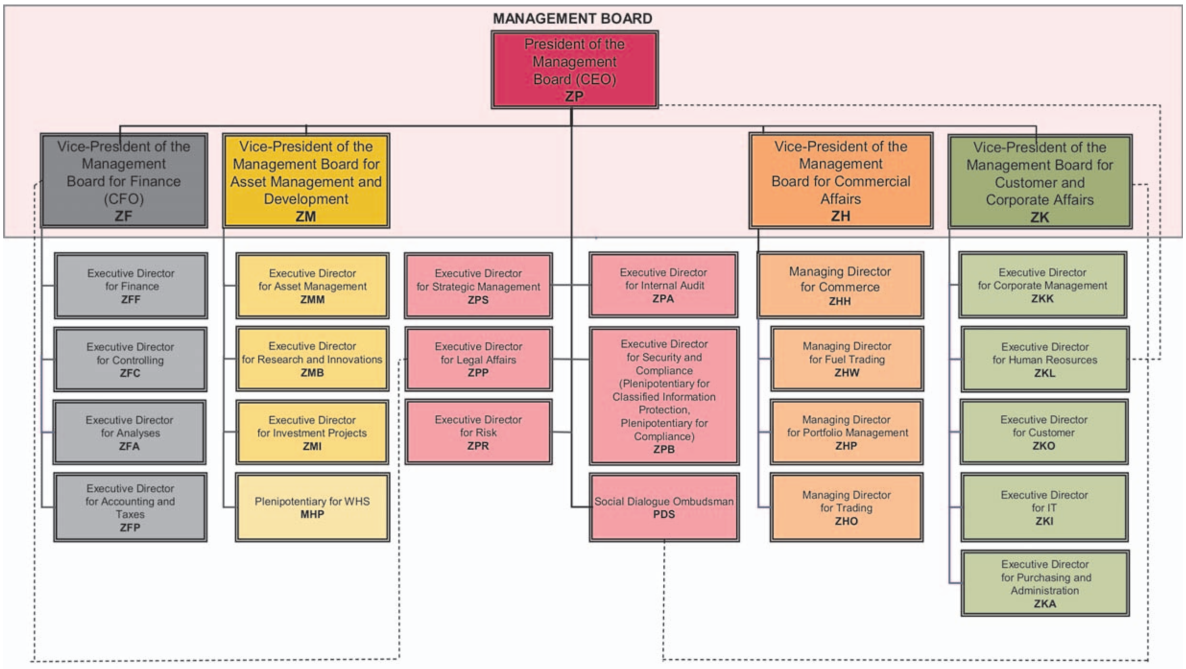
Introducing the above changes to the Organizational By-laws the required modifications of the scopes of the individual business units in the Company's structure were made.

In the general part of the Organizational By-laws provisions on establishing additional reporting lines and principles of proceeding in case of conflicting instructions were modified. Furthermore, the power to issue intra corporate regulatory acts was also granted to the Vice President of the Management Board empowered by the Management Board.

Changes to the organisational structure of the Company were aimed at optimizing the operations of the Company and TAURON Capital Group. Areas assigned to the individual divisions managed by members of the Management Board of the Company were revised.

The below figure presents the divisions assigned to the individual members of the Management Board, down to the level of business units and independent work positions reporting directly to members of the Management Board, as of the day of drawing up this report.

Figure no. 94. TAURON's organizational diagram (flowchart) as of the day of drawing up this report



Changes in the principles of managing the TAURON Capital Group

Activities undertaken in implementing the management by processes structure resulted in updating of the Business Model. Scope of authorities and functions attributed to individual Megaprocesses were specified in further detail and supplemented to fully reflect the performed activities in the documents and to ensure possibly high effectiveness. Most important changes include allocation of activities in occupational safety, hygiene and environmental protection to the assets management Megaprocess, transfer of activities related with market forecasting from the trade Megaprocess to the controlling Megaprocess and including public aid activities into the controlling Megaprocess. Some other minor modifications and changes were made in line with the Business Model Structure.

Owners of the Megaprocesses were defined in course of 2017 implementation processes of the Business Model and the Megaprocesses devolved to lower level processes being implemented in their entirety in all companies of the TAURON Capital Group. Full documentation of processes active within TAURON was prepared and published.

Process documentation (maps, diagrams and sheets) were developed, implemented and published in H2 2017 in key companies of the TAURON Capital Group, i.e. at TAURON Wydobycie S.A., TAURON Wytwarzanie S.A., TAURON EKOENERGIA sp. z o.o., TAURON Ciepło sp. z o.o., TAURON Dystrybucja S.A., TAURON Sprzedaż sp. z o.o. and TAURON Obsługa Klienta sp. z o.o.

Process design activities led to identification and elimination of much inefficiency and products of processes not generating added value, as well as added were actions necessary and required for effective implementation of objectives and assumptions resulting from the Strategy. These activities were supported through workshops and training courses for employees participating in process modeling and creating process documentation.

New statutes and company deeds were adopted in 2017 within the TAURON Capital Group companies, implementing principles of management set forth in the *Act of 16 December 2016 on principles of managing State-owned assets*. Provisions defining scope of authorities of corporate bodies that were described in process documents were removed forth the deeds. This served to avoid overlaps and prolonging of decision processes in the scope that has been allocated in process documents to other units and persons.

Implementation of the Business Model redefined, redesigned all repeatable processes unifying descriptions that were published in implemented through process documentation. Implemented process documents and tool as well as acquired within the TAURON Capital Group competences in process management and process optimization throughout the Group have become a starting point for attaining further efficiencies and operating effectiveness.

Activities associated with design and implementing of key processes in remaining operating companies of the TAURON Capital Group shall be continued in 2018.

8.2. Key non-financial performance indicators in operations of TAURON Capital Group

Being among the biggest energy sector holdings in Central and Eastern Europe, with operations along the entire energy value chain, the TAURON Capital Group is aware of the influence it has on its broad surroundings – natural environment, stakeholders (employees, customers, shareholders, local communities, suppliers, representatives of authorities and institutions), the micro- and macroeconomic situation and the industry it operates in. While studying its social influence and impacts on the economy, lives of employees, customers, natural environment and communities, the TAURON Capital group is continuously monitoring the non-financial indicators of its operations and presents the results annually in its integrated report.

The integrated formula allows a clear presentation of relations and dependencies between the financial and non-financial aspects of the operations of all companies of the TAURON Capital Group. This makes it a comprehensive and transparent document presenting the company operations, its business model, strategy, key changes, opportunities and risks as well as results from the point of view of all stakeholder groups. Combining the financial data with the non-financial aspects of the TAURON Capital Group is also intended to demonstrate the potential achieved through synergy of the core business with non-business operations, based on the Strategy.

Within the 5 directions set by the Strategy, 18 commitments were made, and due to the need to monitor the extent of their achievement, each commitment was assigned a metric and initiatives.

The key non-financial performance metrics of the TAURON Capital Group include, in line with the Sustainable Development Strategy, the system average interruption frequency index (SAIDI), number of innovative R&D initiatives submitted in employee competitions, the level and monitoring of the Customer Satisfaction Index (CSI), the complaints index as well as offering match indicator.

Striving for the customer relations not to be limited only to providing products and services, while being aware of the numerous threats that may be encountered by customers in various aspects of using or purchasing electricity, TAURON is conducting educational campaigns targeted at electricity consumers, while the performance indicator of these activities is, e.g., the number of delivered initiatives such as “Energy for Seniors”.

The non-financial indicators also concern TAURON Capital Group’s impact on natural environment. Having in mind the sustainable development principles, the companies of the TAURON Capital Group are optimising their resource management processes (water, raw materials and materials) and are executing active waste management policies (with respect to process and communal waste). Important role in environment protection is also played by the pro-environmental education conducted by individual companies of the TAURON Capital Group, addressed to children as well as to adults.

The non-financial performance metrics of environmental operations of the companies of the TAURON Capital Group also include the number and reach of information and education programmes about environment protection addressed to the customers, employees and the local communities.

The non-financial performance metrics of the TAURON Capital Group operations in employee dimension are, for example, indices of injuries, vocational diseases, days lost and absences, as well as fatal work accidents according to regions and gender, as well as the average number of training hours per year per employee according to gender and job category.

The non-financial performance indicators included in the integrated report of the TAURON Capital Group also presented the dual benefits indicators (dual indicators), i.e. non-financial indicators that are clearly related to financial indicators. An example here is energy consumption dynamics. Reduction of electricity consumption is good for the environment (first benefit) and at the same time reduces costs and improves the results of an entity.

The use of non-financial performance indicators allows the TAURON Capital Group a more comprehensive company mapping in the annual integrated reports, presenting processes and events taking place, as well as including in the analyses the factors impacting its success in a longer time horizon.

Non-financial indicators presented in the annual report of the TAURON Capital Group comprehensively present the social impact, characterise the way in which TAURON intends to remedy its negative impact on the natural and social environment and the ways it contributed to its improvement.

8.3. Description of TAURON's policies

For the purpose of implementation in the national legislation of the Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014, amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups (Non-financial Information Disclosure Directive), the Polish act of 29 September 1994 on accounting (the Accounting Law) was amended.

According to Article 49 b (2) and (3) of the Accounting Law, the scope of information contained in a non-financial report was extended with the description of policies applied with respect to social, employee, natural environment, respect for human rights and corruption countering issues, as well as with description of due diligence procedures applied under these policies and their results.

To assure compliance of the operations of the TAURON Capital Group with the new regulatory requirements, the Management Board of TAURON has in 2017 adopted for use throughout the TAURON Group the following regulations:

1) Customer Oriented Social Policy of the TAURON Group (the Customer Oriented Social Policy),
2) Diversity Policy of the TAURON Group (the Diversity Policy),
3) Environmental Policy of the TAURON Group (the Environmental Policy),
4) Human Rights Respect Policy of the TAURON Group along with Code of Conduct of Business Partners of the TAURON Group Companies (the Human Rights Respect Policy or the Code of Conduct of Business Partners),
5) Work Health and Safety Policy of the TAURON Group (the WHS Policy),
6) Anticorruption Policy of the TAURON Group (the Anticorruption Policy).

Each of the above documents comprehensively presents its subject matter along with an exhaustive description of measures taken by TAURON Capital Group's subsidiaries to achieve the targets adopted in the relevant areas.

8.3.1. Social issues

The responsibilities taken on by the TAURON Capital Group in the area of social issues are governed by the adopted Customer Oriented Social Policy (PRO), aimed at assuring appropriate organisational and business conditions required for achievement of the strategic goals of the TAURON Capital Group concerning its customer and market environment relations. The Customer Oriented Social Policy defines the measures taken by TAURON under a customer dialogue, stresses the importance of building lasting relations both with the customers and the market environment.

8.3.2. Employee issues

Diversity and openness constitute an integral part of both the business operations of the TAURON Capital Group as well as of its *Human Resources Management Policy of the TAURON Group*. The companies of the TAURON Capital Group observe the equal treatment policy and strive to assure diversity with respect to gender, education type, age and professional experience with respect to all employees, and in particular Company authorities and its key managers.

Streamlining of the above measures is supported by the Diversity Policy implemented at the TAURON Capital Group with the key objective of strengthening organisational awareness and culture welcoming diversity.

In employee related matters the TAURON Capital Group also takes measures to prevent discrimination by creating appropriate working atmosphere and culture based on corporate values (Partnership, Development and Courage), as confirmed by implementation of the *Counter Mobbing and Counter Discrimination Policy at the TAURON Group*.

8.3.3. Natural environment

TAURON Capital Group takes on responsibility for caring for the natural environment and the consequences of using its resources. Considering it an important social responsibility, since many years TAURON has been commencing a range of measures aimed at minimising the negative impact of its operations on natural environment.

All companies of TAURON Capital Group have adopted the Environmental Policy that defines the approach to environmental management, including the general direction of environmental operations of the organisation and the principles it follows in environment related matters. The environmental policy is the benchmark for assessing the operation of all companies in the area of environment protection and environmental management; it also documents the values and the vision followed by TAURON Capital Group in its influence on the natural environment.

8.3.4. Respect of human rights

The principles followed by the TAURON Capital Group in the context of respect for human rights and measures taken to prevent their violation as well as support for a climate of dignity and mutual respect are expressed in the Human Rights Respect Policy. This document defines the rules for actions and conduct with respect to human rights that are dedicated to all stakeholders of the TAURON Capital Group, in particular the employees, trading partners and business partners, and include: prohibition of mobbing and discrimination, observing employment and remuneration conditions, work health and safety (WHS).

Due to the nature of operations of the TAURON Capital Group, the area of respect for human rights gives prominent place to aspects relating to work safety assurance. For this reason a separate document was developed that defines the values, rules of conduct and principles of actions concerning the WHS. The goal of the WHS Policy is to achieve the four fundamental goals of work health and safety, being:

1) Assuring optimal working conditions to everyone employed by and working for the TAURON Capital Group.
2) Raising the qualifications of employees of the TAURON Capital Group aimed at building knowledge, commitment and competences of all employees in the area of improvement of their safety and safety of co-workers and persons present at their places of work.
3) Implementing and improving an effective WHS management system, closely related to ongoing operations of the TAURON Capital Group.
4) Eliminating of work related accidents to everyone employed by and working for the TAURON Capital Group and other persons present at the premises of business operations of the companies of the TAURON Capital Group.

Provisions contained in the WHS Policy bind all employees of the TAURON Capital Group as well as all contractors and suppliers of products and services, and any other persons present at the premises of the TAURON Capital Group. The WHS reporting procedures at the TAURON Capital Group are compliant with the Labour Law regulations governing the operation of work place accidents register and informing external authorities about work related accidents and vocational diseases.

Without a business based on respect for human rights there is no possibility to collaborate with the market at the top level. The TAURON Capital Group also expects its business partners to observe the rules and respect human rights of their own employees and to abstain from any forms of breach. As a consequence of supporting the responsible and ethical business conduct, the Code of Conduct of Business Partners was implemented.

8.3.5. Countering corruption

The goal of the Anticorruption Policy in force is to define uniform rules and standards of conduct that allow identifying, countering and mitigating the risk of occurrence of corrupt practices and other kinds of fraud at the companies of the TAURON Capital Group. TAURON has a zero tolerance policy towards corruption and other fraud with respect to all aspects of business and non-business operations of the TAURON Capital Group.

The Anticorruption Policy defines acts of corruption and other practices contrary to the legal regulations in force, internal regulations and corporate regulations of the TAURON Capital Group or ethics. The document defines the obligations relating to countering corruption, potential areas of corruption risk as well as the warning signals the employees should be paying attention to in their daily work. According to the provisions of the Anticorruption Policy, the TAURON Capital Group operates appropriate communication channels allowing the employees to immediately and securely (including anonymous) report potential cases of breach.

8.4. Description of the results of application of policies by TAURON

The basic premise of the Customer Oriented Social Policy is an ongoing survey of general customer satisfaction. At the TAURON Capital Group, one of the key tools for their satisfaction evaluation is the Customer Satisfaction Index (CSI). The survey is performed every Q2/Q3 by an independent research agency. It includes a randomly selected group of customers of TAURON and a group of customers of other energy utilities, such as: ENEA, ENERGA and PGE.

The effects of application of the Customer Oriented Social Policy also include educational initiatives oriented at disadvantaged groups, primarily energy sensitive customers and seniors. The range of topics of these initiatives includes the commercial dangers on the energy market, consumer rights, ways to overcome difficulties with paying the electricity bills, assistance in understanding the bill, etc. In this way TAURON is helping the disadvantaged groups in informed and safe use of the energy market. Educational activities take the form of:

1) information campaigns (e.g. Strangers? Do not answer the door!, i.e. *TAURON is not knocking on doors to sell electricity or gas*),

2) organising educational meetings addressed to senior citizens “Energy for Seniors” (in 2017, five meetings were held – in Limanowa, Nowy Targ, Cieszyn, Wałbrzych and in Bytom),
3) organisation of educational workshops addressed to social assistance workers: “Customer on the horizon” (in 2017, four meetings were held – in Siemianowice Śląskie, Wałbrzych, Kraków and in Wrocław).

The results of implementation of the assumptions of the Customer Oriented Social Policy also include simplification of the marketing communication of products and services as well as providing the customers with an option to pay their distribution service fees and connection charges using electronic payments. Moreover, the partners TAURON collaborates with in the offerings (suppliers of specialised equipment) and in expanding the sales channels (at present, sales through real estate agencies – over 10 partners in total) are selected according to the procedures for establishing collaboration.

Presently the TAURON Capital Group is working on operationalisation of the principles of the implemented employee related policies. The measures taken are targeted at creating a culture based on corporate values of Partnership, Development and Courage that support dialogue, openness, mutual tolerance and teamwork.

Moreover, in 2017 an e-learning training was launched on countering mobbing and discrimination at the TAURON Capital Group, which supports the procedures of reporting incidents that may indicate occurrence of mobbing or discrimination.

The result of application of the Environmental Policy by the TAURON Capital Group is a gradual reduction of both the direct and indirect influence on the environment and conducting relevant communication assuring understanding of the operations of the TAURON Capital Group that may be impacting the environment.

The TAURON Capital Group observes all the internationally recognised human rights and supports their protection, while at the same time preventing situations where these rights would be directly or indirectly violated. The Human Rights Respect Policy is binding on all employees, and with the implementation of the Code of Conduct of Business Partners – also on TAURON’s business partners. Currently the process of operationalisation of the document is under way. Due to the above it is not possible to comprehensively present the results of application of the above policy at present.

The WHS Policy streamlines the rules on the WHS that the TAURON Capital Group has been observing long before the development of this document. The expected result of operationalisation of the WHS Policy is a continuing improvement of work health and safety standards that is to result in, among others, elimination of work related accidents and minimisation of occurrence of vocational diseases and potentially accident prone incidents.

Each and every employee of the TAURON Capital Group is required to study the content of the Anticorruption Policy, respect it unconditionally and sign a statement on having studied its content. Introduction of the Anticorruption Policy at the TAURON Capital Group contributes towards continued improvement of awareness concerning identification of corrupt practices and promotion of honesty and transparent conduct.

8.5. Description of due diligence procedures in operation under the policies applied by TAURON

One of the key metrics of due diligence used in the Customer Oriented Social Policy are the cyclically determined Key Performance Indicators (KPIs) concerning, for example, the number of complaints submitted to the TAURON Capital Group. In its operations TAURON pays particular attention to the procedures aimed at raising customer awareness, thus preventive measures are developed and implemented after post-collection reconnection of electricity supply, i.e. the customers are informed about the need to prepare their premises for renewed electricity supply so as to prevent occurrence of hazards to people and property.

TAURON is planning further delivery of information campaigns, trainings and other initiatives facilitating understanding of the Customer Oriented Social Policy by the employees and developing customer oriented attitudes with:

1) e-learning on products and services offered, increasing the level of knowledge about the customers, primarily addressed to all employees of the TAURON Capital Group,
2) an educational programme building customer oriented awareness for all employees of the TAURON Capital Group,
3) development of a knowledge base available to all employees of the TAURON Capital Group (it will provide the employees with the knowledge on current customer oriented initiatives and with the content deepening the knowledge and awareness of employees about customer focus, consumer rights, good practices in customer relations and building positive customer experience in contacts with the TAURON brand).

With respect to employee issues under the policies applied at the TAURON Capital Group, regulations are in force on remuneration and labour law, as well as a standardised *Human Resources Management Policy at the TAURON Group* and *Rules of Remuneration at the TAURON Group*.

Moreover, respecting the freedom of association, the TAURON Capital Group has a Social Council and dozens of trade union organisations.

The general direction of environmental measures at the TAURON Capital Group includes minimising the negative impact on the environment taking into account the specifics of the sector, technical progress and access to environmentally friendly technologies, achieved by:

1) assuring compliance of operation of all companies of the TAURON Capital Group with the environment protection regulations, taking into account the local conditions and specifics of business operations,
2) collaborating with all parties to and participants in the processes,
3) monitoring and exchange of "industry good environmental practices",
4) ongoing monitoring of the main aspects of direct and indirect environmental impact of operations.

The TAURON Capital Group strives to respect human rights and to understand the values of local communities by holding open dialogues with those affected by the company operations. When making business decisions, TAURON analyses the extent of their potential impact on the local communities of the region and seeks to balance its impact on the environment, which is reflected in its *Human Rights Respect Policy*, with its provisions also defining the path for reporting violation of its rules.

Under the due diligence procedures in operation under the human rights respect policies, changes were introduced to the template TOR and detailed TOR documents that constitute attachments to the *Rules for Awarding Contracts at the TAURON Group*, resulting in the requirement on every business partner of the companies of the TAURON Capital Group to submit the statement on having reviewed the Code of Conduct of Business Partners.

Under the due diligence procedures aimed at improving the WHS standards, the TAURON Capital Group measures and benchmarks its results with respect to the WHS both internally and externally, and uses the best identified practices. Moreover it seeks to develop its own best practices in the WHS and conducts internal and external audits with participation of the management staff, employees and their representatives, WHS services and contractors. TAURON also works on initiatives raising the awareness of the WHS among employees, including information and training activities, as well as campaigns oriented at increasing the employee engagement in shaping the work health and safety system at the TAURON Capital Group.

The TAURON Capital Group encourages its employees and third parties to come forward with any information on breaches of the Anticorruption Policy and other violations using the dedicated communications channels. The employees and third parties may submit their doubts or request the assistance of the Compliance Officer in case of doubt as to whether a justified suspicion arises in specific situation of breach of provisions of the Anticorruption Policy or other legal regulations, internal company regulations or corporate regulations of the TAURON Capital Group or of ethical standards. All submissions are treated with confidence and studied with due diligence.

TAURON is taking measures to raise employee knowledge and awareness of combating corruption. In 2017, TAURON has organised workshops for the members of the management staff on topics of corruption. Similar trainings particularly dedicated to the staff from procurement and investments areas took place also at the other companies of the TAURON Capital Group. In 2018, TAURON is planning to deliver information initiatives, trainings and other measures facilitating correct understanding of the Anticorruption Policy by the employees and following its principles in their daily work.

8.6. Description of significant risks related to operations of TAURON that may exert adverse impact on the policies applied by TAURON, as well as description of management of these risks

Under the risk management process employed by the TAURON Capital Group, risks related to operations of the companies were identified that could exert adverse impact on the social, employee, natural environment, respect for human rights and anticorruption issues as well as on policies employed by TAURON.

According to regulations in force, for every identified risk its Risk Owner is appointed and made responsible for this risk management, risk records are developed containing descriptions of mitigation measures conducted, risk measurement parameters and early warning indicators are defined and in particular cases separate risk response and backup plans are developed. These risks are included in the risk model that defines the categories of risks present in the operations of TAURON.

The key risks include: social risk, human capital management risk, WHS risk, internal communication risk, environmental risk, procurement process risk, legal risk and compliance risk.

The below table below characterises the risks related to the operations of TAURON that could exert adverse impact on the policies employed by TAURON.

Table no. 47. Risks related to the operations of TAURON that could exert adverse impact on the policies employed by TAURON

No.	Risk name	Risk description	Risk response
1.	Social risk	The risk includes failing to meet customer service standards, to deliver on sales agreements, external communications and marketing activities and the personal data protection related risk. Risk materialisation could result in loss of reputation and customer trust, customer disputes, non-achievement of goals including sales targets and possible penalties for legal noncompliance concerning personal data protection.	• Adoption and execution of Customer Oriented Social Policy. • Holding a dialogue with customers, including customer satisfaction surveys, tailoring the product offering to their needs, looking after high customer service levels. • Building relations with the customers and market environment. • Responsibility for the product including quality and security of supply, tailoring the product offering to customer needs. • Customer personal data privacy and security protection. • Implementing tools supporting execution of customer focused social policy. • Standardisation of customer agreement templates and their adaptation to legislation changes and optimisation of sales and service processes. • Delivery of promotional activities in line with the adopted *TAURON brand strategy* and *TAURON Group sponsoring strategy for 2018–2025*, taking into account respect for human rights and conducting responsible marketing.
2.	Human capital management risk	Risk relating to employee issues including diversity, inclusion, employment conditions and respect of right of association, capital management, career paths and recruitment management, training system, work health and safety management. Risk materialisation results in employee complaints, collective disputes, strikes, loss of specialised staff and problems with its restoration.	• Adoption and execution of the Employee Recruitment, Selection and Adaptation Policy. • Adoption and execution Counter Mobbing and Counter Discrimination Policy. • Looking after development of employee competences, including through participation in trainings. • Holding consultations with social organisations within the TAURON Capital Group. • Execution of the staffing policy based on the Competence Model and Rules of Compensation, and Rules of Work. • Adoption and implementation of the Diversity Policy. • Adoption and implementation the Human Rights Respect Policy.
3.	Work Health and Safety (WHS) risk	Risk relating to ensuring health and safety at work. Risk materialisation result is employee injury, health loss or excessive employee exposure to hazards.	• Prioritisation of employee, customer, contractor and stakeholder safety in the business activities performed. • Adoption and execution of the *Work Health and Safety Policy of the TAURON Group*. • Assuring optimal working conditions. • Raising employee qualifications with respect to work safety improvements. • Conducting trainings, implementation and improvement of WHS management system.
4.	Internal communication risk	Risk relating to assuring optimal and effective communication within the TAURON Group and transmission of honest information to employees of the TAURON Capital Group while observing confidentiality of sensitive information. Risk materialisation result is a loss of trust in the employer, increased social unrests, loss of reputation and negative impact on the TAURON brand.	• Building relations with the social side at the TAURON Capital Group and close cooperation with the Social Dialogue Spokesperson. • Use and development of available communications tools to provide significant information to the employees of the TAURON Capital Group. • When providing significant information – organisation of fact to face meetings of the management staff with the employees. • Ongoing monitoring of situation and events at companies of the TAURON Capital Group that could result in social unrests. • Regular meetings with the representatives of companies dealing with internal communication to exchange information. • Developing the Communication Strategy for the TAURON Group.

No.	Risk name	Risk description	Risk response
5.	Environmental risk	Risk relating to impact of business operations on natural environment and the use of its resources, pollution control and prevention, protection of water sources and waste management. Risk materialisation result is a degradation of natural environment and penalties for failing to meet environmental requirements, the need to remedy them, to limit production, possibility of benefiting from subsidy programmes and loss of image of the TAURON Capital Group.	• Adoption and implementation of *Environmental Policy of the TAURON Group.* • Conducting business operations impacting the natural environment according to sustainable development principles. • Identification of areas of environmental impact and assuring the operation of the TAURON Capital Group in compliance with the environment protection laws. • Continuing development of knowledge and environmental responsibility culture among the employees, customers and business partners of the TAURON Capital Group. • Seeking solutions aimed at implementing circular economy principles at the TAURON Capital Group and actively seeking technical and organisational solutions that minimise the negative impact of operations on the environment. • Improvement of energy efficiency and efficient water management. • Offering products / services that take into account the aspect of limiting the negative environmental impact. • Promoting conservation of nature and relevant collaboration with local government and central government administration bodies.
6.	Procurement process risk	Risk relating to the exercised procurement procedures, taking into account prevention of violation of human rights by business partners, countering corruption and fraud in procurement processes and observing ethical and moral standards in their progress. Risk materialisation result are non-optimal purchase contracts, need to annul tendering procedures, loss of image of the TAURON Capital Group and credibility to stakeholders.	• Adoption and implementation of the Code of Conduct of Business Partners of the TAURON Group. • Adoption and execution of the *Anticorruption Policy of the TAURON Group.* • Adoption and execution of the *Human Rights Respect Policy.* • Standardisation of conducting procurement processes and their transparency. • Building lasting business partner relationships based on trust and mutual respect. • Expecting the business partners to observe the legal regulations, ethics standards and fair trading practices, including work health and safety, prevention of discrimination and unequal treatment, respecting employee human rights and dignity, transparent HR policy, environment protection, fair competition, fraud prevention and combating, as well as information security and protection. • Use of standard template agreements and standard clauses in contracts providing for respect for human rights by the business partners of the TAURON Capital Group.
7.	Legal risk	Risk relating to non-observance of legal regulations, misinterpretation of new rules and regulations, requirements imposed by the regulator and the supervisory bodies.	• Ongoing monitoring of the legal environment and amendments to legal regulations, including in scope of social issues, respect for human rights, countering corruption, environment protection and employee issues. • Implementation of the required amendments to the in-house regulations. • Appointing working parties tasked with developing and implementing the required changes resulting from the legal environment. • Ongoing cooperation with the bodies supervising the energy market and the capital market. • Training the employees in legal regulations and in-house regulations.

No.	Risk name	Risk description	Risk response
8.	Compliance risk	Compliance risk includes the risk of internal fraud, external fraud and non-ethical conduct. Risk relating to misappropriation or improper use of Company assets, their devastation, abuse of official position for personal gains, acts by third parties aimed at theft, burglary, counterfeiting and related to occurrence of conduct violating generally accepted social coexistence standards, moral standards and mobbing.	• Adoption and implementation of *Code of Conduct of Business Partners of the TAURON Group*. • Adoption and execution of the *Anticorruption Policy of the TAURON Group.* • Adoption and execution of the *Human Rights Respect Policy.* • Adoption and execution of the *Counter Mobbing and Counter Discrimination Policy.* • Adoption and implementation of the *Diversity Policy*. • Use of internal procedures aimed at fraud prevention (security procedures, reviews of authorisations), their testing and improvement. • Promoting best practices, improvement of procedures, conducting trainings and observing the Code of Business Ethics of the TAURON Group and operation of a fraud reporting system. • Building an organisational culture based on values and principles of the TAURON Group.

9. OTHER MATERIAL INFORMATION AND EVENTS

9.1. Proceedings pending before the court, competent arbitration authority or public administration authority

During the reporting period no proceedings were pending before any court, competent arbitration authority or public administration authority, related to the Company, the standalone or aggregate value of which would represent at least 10% of TAURON's equity.

Furthermore, during the reporting period no proceedings were pending before any court, competent arbitration authority or public authority body, related to the subsidiaries of TAURON Group, the standalone or aggregate value of which would represent at least 10% of TAURON's equity.

9.2. Information on agreements concluded by TAURON Capital Group's subsidiaries

9.2.1. Agreements significant for TAURON Capital Group's operations

In the financial year 2017 and until the day of drawing up this report TAURON Capital Group's subsidiaries concluded the following agreements significant for the operations of TAURON Capital Group:

Concluding of the amendment to the agreement with the RAFAKO S.A. – MOSTOSTAL WARSZAWA S.A. consortium on the construction of a power generation unit at Jaworzno III Power Plant

On March 1, 2017 the Management Board of TAURON's subsidiary – TAURON Wytwarzanie (Ordering Party) signed with the RAFAKO S.A. – MOSTOSTAL WARSZAWA S.A. consortium (Contractor) an amendment to the agreement on the construction of a 910 MWe power generation unit for super critical parameters at Jaworzno III Power Plant – Elektrownia II, currently carried out by the Ordering Party's spun off branch – Oddział Jaworzno 910 MW in Jaworzno, with respect to: steam boiler, turbine set, main building, electric part and the unit's instrumentation and control (I&C).

Under the amendment the agreement's net price was increased by PLN 71.05 mln, i.e. to PLN 4 470 mln, and the deadline for completing the subject of the agreement was extended by 8 months, i.e. until the 67th month from the date of concluding the agreement at the latest which means that the new assumed date of handing over the unit for operation is November 2019.

The decision to sign by TAURON Wytwarzanie of the above mentioned amendment was taken on February 28, 2017. On the same day also the Management Board of TAURON issued a positive opinion on the conclusion of the amendment on the above mentioned terms.

Amendments to the agreement were due to the need to change the unit's facilities' foundations to the deep foundations, and also due to the parties to the agreement agreeing on additional works beneficial to the Ordering Party for technical and economic reasons (erecting the foundation for the fifth electrofilter (EF) zone and extending the EF switchgear building). The additional works will allow the Ordering Party to achieve savings during the planned outage of the unit in 2021 in order to partly adapt the unit to comply with the future BAT conclusions requirements. The Ordering Party partly accepted the Contractor's claims related to the above circumstances and the change necessity protocols as justified. The claims due the change of the design standards – EUROKODY, were not accepted as justified by the Ordering Party.

Due to the above the warranties granted by the Contractor were extended:

1) by 6 months with respect to the Unit's availability for the direct shipments carried out by RAFAKO S.A., boiler maximum continuous rating, unit's technical minimum and flue gas water content behind FGD, vibration level for a structure,
2) by 12 months with respect to the unit's design and construction.

The Contractor will also ensure an appropriate extension of the agreement's performance bond.

Signing of the amendment changed the terms of the agreement with the Contractor, however it had no impact on the change of the entire investment project's budget.

The Company provided information on the amendment to the above mentioned agreement in the regulatory filings (current reports): no. 5/2017 of February 28, 2017 and no. 7/2017 of March 1, 2017.

Coming into force of the agreement and amendments on the terms of further implementation of the "CCGT unit's construction at Stalowa Wola" project

On March 31, 2017, in reference to the earlier concluded agreements and amendments on the terms of further implementation of the "CCGT unit's construction at Stalowa Wola" project (Project), as described in the regulatory filing (current report) no. 36/2016 of October 27, 2016 ECSW issued an instruction to make the payment to the institutions so far providing the financing for ECSW, i.e. European Investment Bank, European Bank for Reconstruction and Development, Bank Polska Kasa Opieki S.A. (Financing Institutions) of PLN 581.4 mln as the repayment of all of ECSW's liabilities towards the Financing Institutions. Upon the crediting of the Financing Institutions' bank accounts the suspending conditions were met and at the same time the documents described in the above mentioned report (filing) came into force, i.e.:

1) agreement on establishing the basic boundary conditions of the Project's restructuring among TAURON, PGNiG and ECSW,
2) amendment to the electricity sale Agreement of March 11, 2011 (Electricity Sale Agreement) among TAURON, PGNiG and ECSW,
3) amendment to the gas supply Agreement of March 11, 2011 (Gas Agreement) between PGNiG and ECSW.

The agreement governs, first of all, the conditions of settling the liquidated damages, making the so far used pricing formulas market based and the Project's financial restructuring issues and it constitutes a reflection of the will of the Project's sponsors, i.e.: TAURON and PGNiG (Sponsors) with respect to the continuation of the CCGT unit's construction, making changes to the Gas Agreement and the Electricity Sale Agreement and changing Project's financing formula from project finance to corporate finance.

Changes to the Gas Agreement and the Electricity Sale Agreement envisage in particular making the pricing formulas used in these agreements market based. Furthermore, due to the delay in the Project's implementation, the amendment to the Gas Agreement envisages a change with respect to amounts, deadlines and methodology used to assess liquidated damages.

ECSW acquired the funds for the bank loans' repayment under loan agreements according to which each of the Sponsors granted ECSW a PLN 290.7 mln loan.

In accordance with the provisions of the standstill agreement mentioned in the regulatory filing (current report) no. 36/2016 the Financing Institutions were obligated to return the bank guarantees received from the Sponsors for the total amount of approx. PLN 629m, where the total amount of bank guarantees provided by TAURON was PLN 314.5 mln.

Irrespective of the above the Sponsors, along with ECSW, are continuing joint works aimed at acquiring new financing for the CCGT unit's construction project at Stalowa Wola the terms and the structure of which would be more favorable than the existing agreements.

The Company disclosed information on the above event in the regulatory filing (current report) no. 11/2017 of March 31, 2017.

The bank guarantees for PLN 314.5 mln issued at TAURON's instruction in order to guarantee the banks' liabilities under the loans granted to ECSW mentioned in the above regulatory filing (current report) expired in April 2017.

Signing of the agreement on potential cooperation in the implementation of the construction of a 910 MW power generation unit project at Jaworzno III Power Plant and the termination of the investment agreement related to the CCGT unit at Łagisza Power Plant

In reference to the Strategy that assumes an implementation of the construction of a 910 MW power generation unit project at Jaworzno (Project) under the new financing formula, envisaging spinning off of an organized part of an enterprise including the above mentioned investment project into a new special purpose vehicle, and then external partners joining the company, on June 1, 2017 TAURON signed the Agreement on the preliminary terms of potential cooperation as part of the Project with Fundusz Inwestycji Infrastrukturalnych – Kapitałowy Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych and Fundusz Inwestycji Infrastrukturalnych – Dłużny Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych (Funds), managed by Towarzystwo Funduszy Inwestycyjnych BGK S.A. A part of the investment portfolio of the above mentioned Funds is managed by Polski Fundusz Rozwoju S.A.

Under the Agreement the Funds expressed a preliminary interest in investing in the Project PLN 880 mln in total, by way of the Funds taking up new shares in the Nowe Jaworzno GT special purpose vehicle, that is currently TAURON's wholly owned company currently implementing the Project. The Funds' share in the share capital of Nowe Jaworzno GT cannot be higher than 50% minus one share. The other shares in Nowe Jaworzno GT will be held by the Company or by the Company and an additional Investor (Investors), where the Company will own at least 50% plus one share in Nowe Jaworzno GT. The Agreement expresses the will of the parties to conduct, in good faith, negotiations aimed at defining the rules of potential cooperation in implementing the Project. The joining of the Project by the Funds will be dependent on the results of the detailed analysis of the Project by the Funds, the parties agreeing and fulfilling the conditions defined in the documentation of the transaction and the Funds obtaining the required investment consents to take part in the Project. The Agreement shall be valid until December 31, 2017.

At the same time on June 1, 2017 an agreement was signed between TAURON Wytwarzanie and PFR under which the investment agreement concluded between the above mentioned entities aimed at the joint implementation of the project "Construction of a 413 MWe CCGT unit at TAURON Wytwarzanie Spółka Akcyjna Oddział Elektrownia Łagisza in Będzin" was terminated. The Company provided information on the conclusion of the investment agreement in the regulatory filing (current report) no. 17/2015 of July 13, 2015. The termination of the investment agreement is in line with the assumptions of the Strategy envisaging stopping of the investment in the CCGT unit at Łagisza Power Plant which translates into the reduction of capital expenditures for this purpose by approximately PLN 1.5 bln.

In reference to the term (expiration date) of the above mentioned Agreement, on December 29, 2017 TAURON signed an amendment under which the Agreement on potential cooperation in the implementation of the 910 MW power generation unit construction project in Jaworzno was extended until February 28, 2018.

The other provisions of the above mentioned Agreement were not changed.

On February 28, 2018 TAURON informed of the will, expressed by the parties to the Agreement, to continue activities aimed at signing agreements that will define the terms of the Funds' equity investment in the Special Purpose Vehicle.

The intention of the parties is to have the Funds join the Special Purpose Vehicle and participate in the successive recapitalizations of the Special Purpose Vehicle, by taking up the newly created shares in exchange for financial contributions up to the total maximum amount of PLN 880 mln.

The Funds' share in the Special Purpose Vehicle's share capital, as of the day the Unit is commissioned, should reach approx. 14%, while TAURON's share should reach at least 50% + 1 share. Joining the Special Purpose Vehicle by the Funds will be contingent on the fulfillment of the conditions that will be defined in the agreements.

The Company disclosed information on the above events in the regulatory filings (current reports): no. 25/2017 of June 1, 2017, no. 43/2017 of December 29, 2017 and no. 4/2018 of February 28, 2018.

Extension of the bond issue program

On June 20, 2017 amendments were signed to the agreements related to the bond issue program (Program), i.e. agency and custody agreement and underwriting agreement of the conclusion of which the Company provided information in the regulatory filing (current report) no. 49/2015 of November 20, 2015. Under the above amendments the following extension of the Program was made:

a) one year, i.e. until December 31, 2021 ("Extension Period I"). Program amount in Extension Period I will be PLN 5.32 bln maximum, and the following banks joined the extension: MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland, Bank Zachodni WBK S.A., CaixaBank S.A. (Joint Stock Company) Branch in Poland, Industrial and Commercial Bank of China (Europe) S.A. Branch in Poland, ING Bank Śląski S.A., Powszechna Kasa Oszczędności Bank Polski S.A. and mBank S.A.,
b) by two years, i.e. until December 31, 2022 ("Extension Period II"). Program amount in Extension Period II will be PLN 2.45 bln maximum, and the following banks joined the extension: MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland and Powszechna Kasa Oszczędności Bank Polski S.A.

Until December 31, 2020 the Program amount will not change and will be PLN 6.27 bln maximum. The margin of the financing under the Program did not change due to the extension made.

On the other hand on March 9, 2018 amendments to the agency and custody agreement as well as the underwriting agreement were signed, the result of which is an extension by some banks of the period of availability of the funds under the Program.

This means that the maximum value of the Program:

a) is PLN 6.27 bln until December 31, 2020 (this amount did not change as a result of signing the amendments),
b) is PLN 6.07 bln until December 31, 2021 (it had been PLN 5.32 bln before the amendments were signed),
c) is PLN 5.82 bln until December 31, 2022 (it had been PLN 2.45 bln before the amendments were signed).

The amendments were signed with the following banks taking part in the Program: Bank Handlowy in Warsaw S.A., Bank BGŻ BNP Paribas S.A., Bank Zachodni WBK S.A., CaixaBank S.A. (Joint Stock Company) Branch in Poland, Industrial and Commercial Bank of China (Europe) S.A. Branch in Poland, ING Bank Śląski S.A., mBank S.A., MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland and Powszechna Kasa Oszczędności Bank Polski S.A.

The information on the above events was disclosed by the Company in the regulatory filings (current reports) no. 29/2017 of June 20, 2017 and no. 6/2018 of March 9. 2018.

Conclusion of the coal purchase agreement with Polska Grupa Górnicza S.A.

On January 18, 2018 a coal purchase agreement was signed between TAURON and Polska Grupa Górnicza S.A. with the subject of the agreement being the purchase of thermal coal for the production needs of TAURON Capital Group's power generating units. The estimated value of coal supplies in the 2018–2021 time frame, based on the coal price agreed for 2018, will reach the net amount of approximately PLN 2.15 bln. The coal price was agreed for the first year of the agreement's term, while in the subsequent years the coal price will be indexed based on the formula included in the agreement, taking into account changes of the market conditions. The above agreement was concluded for an indefinite period of time and it provides for liquidated damages in the amount of 10 percent of the value of unrealized deliveries in the given year.

The information on the above event was disclosed by the Company in the regulatory filing (current report) no. 1/2018 of January 18, 2018.

Financing for EC Stalowa Wola subsidiary

On March 8, 2018 in reference to the current report no. 11/2017 of March 31, 2017 with respect to the information on actions related to obtaining new financing for the CCGT unit construction project at Stalowa Wola, EC Stalowa Wola (Loan Taker), i.e. entity in which the TAURON holds indirectly, via its TAURON Wytwarzanie S.A. subsidiary, a 50% stake in the share capital; signed a loan agreement with BGK and PGNiG.

Under the above mentioned agreement BGK and PGNiG will grant the Loan Taker a loan in the amount of PLN 450 mln each, to be used to refinance the Loan Taker's debt towards the Issuer and PGNiG (PLN 600 mln) and to cover the Loan Taker's further capital expenditures (PLN 300 mln). The agreement was concluded for the period lasting until June 14, 2030.

As of March 8, 2018 the Loan Taker's current loan liabilities towards the Issuer were approximately PLN 610 mln.

The loan agreement provides for the funds to be paid out to the Loan Taker after the suspending conditions have been met, with one of them being presenting to BGK of a bank guarantee issued at the Issuer's instruction and securing the Loan Taker's debt towards BGK. The bank guarantee will be renewed annually, and its value will not exceed PLN 517.5 mln.

The information on the above event was disclosed by the Company in the regulatory filing (current report) no. 5/2018 of March 8, 2018.

9.2.2. Transactions with related entities on terms other than at arm's length

All transactions with related entities are concluded at arm's length.

The detailed information on the transactions with related entities is provided in note 49 of the consolidated financial statements for the year ended on December 31, 2017.

9.2.3. Signed and terminated credit and loan agreements

Working capital credits and short term loans

In accordance with the financing model adopted by TAURON Capital Group, only TAURON may act as a party to working capital credits and short-term loans raised with external institutions.

TAURON Capital Group is using a true cash pooling structure, implemented under the cash management agreement concluded with PKO BP (the former agreement expired on December 17, 2017, while the new agreement came into force on December 18, 2017, valid until December 17, 2020). The cash pooling structure is based on daily limits granted to individual participants by the agent managing the service, i.e. TAURON. As a result of implementing the cash pooling mechanism, cash transfers are performed between accounts of participants of the service and the agent's account. Within the cash pooling structure TAURON uses at PKO BP:

1) overdraft limit in the amount of PLN 300,000 thousand, based on the overdraft agreement concluded with the bank in October 2017, with the repayment date falling on December 29, 2017 (the former overdraft limit agreement of December 2014 expired on December 29, 2017), and
2) intraday limit in the amount of PLN 500,000 thousand, effective until December 17, 2020 (the effective date was extended under the amendment to the bank account concluded in October 2017). The intraday limit is a daily limit which must be fully repaid by the end of each day on which it was used).

As part of financing its ongoing operations following agreements were also in force:

1) overdraft agreement with BGK, up to the amount of EUR 45,000 thousand with the repayment date of December 31, 2017. The overdrawn amount is used for financing of the transactions of purchase/ sale/ exchange of CO_2 emission allowances, trading in electricity and gas made on the European exchanges, (accordingly, under amendments no. 1 and no. 2 to the overdraft agreement, concluded in May and December 2017, its amount was raised from EUR 25 000 thou. to EUR 45 000 thou. and the effective date was extended until December 31, 2018).

2) overdraft agreement concluded with mBank for the amount not exceeding of USD 2,000 thousand, to be used for financing the ongoing operations, in particular, for financing the collateral margin and commodity products transactions. The repayment deadline of the loan, pursuant to the amendment of January 12, 2017, falls on March 31, 2018.

The use of above described foreign currency loans is aimed at mitigating the FX risk related to the trade transactions concluded.

The below table presents a detailed summary of working capital loan and credit agreements effective as of December 31, 2017.

Table no. 48. Summary of TAURON Capital Group's working capital loan and credit agreements as of December 31, 2017

No.	Type of agreement	Interest rate	Amount of credit/loan (thou.)	Period of financing	Balance as of December 31, 2017 (thou.)
1.	Overdraft facility	LIBOR 1M + fixed margin	2 000 USD	16.04.2015 – 30.03.2018	417 USD
2.	Overdraft facility	EURIBOR 1M + fixed margin	45 000 EUR	09.05.2017 – 31.12.2018	22 060 EUR
3.	Overdraft facility	WIBOR O/N + fixed margin	300 000 PLN	30.12.2017 – 29.12.2020	0 PLN
4.	Intraday limit	None	500 000 PLN	18.12.2017 – 17.12.2020	0 PLN

Investment credits and loans

The below table presents a detailed summary of investment credit and loan agreements effective at TAURON Capital Group as of December 31, 2017.

Table no. 49. Summary of TAURON Capital Group's investment credit and loan agreements as of December 31, 2017

No.	Parties to the agreement	Type of agreement and interest rate	Amount of credit/loan (thou.)	Repayment date	Balance as of December 31, 2017 (thou.)
1.	TAURON – EBI	fixed margin	210 000 PLN	15.12.2021	84 000 PLN
2.	TAURON – EBI	fixed margin	300 000 PLN	15.12.2021	120 000 PLN
3.	TAURON – EBI	fixed margin	450 000 PLN	15.06.2024	265 909 PLN
4.	TAURON – EBI	fixed margin	200 000 PLN	15.09.2024	127 273 PLN
5.	TAURON – EBI	fixed margin	250 000 PLN	15.09.2024	159 091 PLN
6.	TAURON – EBI	fixed margin	295 000 PLN	15.03.2027	280 250 PLN
7.	TAURON Wytwarzanie – WFOŚiGW	base rate + fixed margin	40 000 PLN	15.12.2022	20 000 PLN
8.	TAURON Ciepło – WFOŚiGW	floating	30 000 PLN	15.12.2022	15 000 PLN
10.	KW Czatkowice – WFOŚiGW	floating	914 PLN	31.05.2021	627 PLN

In 2017 TAURON Capital Group's subsidiaries did not terminate any credit and loan agreements.

9.2.4. Loans and sureties granted as well as sureties and guarantees received

Loans granted

Besides its subsidiaries included in the consolidation, In 2017 TAURON granted financing to its co-subsidiary, EC Stalowa Wola, in the form of loans to be used for the current operations of EC Stalowa Wola and the repayment of loan installments of this subsidiary towards the European Investment Bank, European Bank for Reconstruction and Development and Pekao S.A. Furthermore, the agreement consolidating ECSW's debt due to the loans granted to the company before was signed in 2017.

Moreover, on November 8, 2017 the Company concluded, with PGE EJ 1 sp. z o.o., an agreement on a PLN 2 940 thou. loan for the period of 3 years from the date of concluding the agreement, i.e. until November 6, 2020.

The below table presents a summary of loans granted and effective as of December 31, 2017.

Table no. 50. Summary of loans granted by TAURON, effective as of December 31, 2017

No.	Type of agreement/Beneficiary	Interest rate type	Loan amount under the agreement (thou.)	Effective term	Balance as of December 31, 2017 (thou.)
1.	Loan EC Stalowa Wola	WIBOR 3M + fixed margin	177 000 PLN	20.06.2012 – 31.12.2032	177 000 PLN
2.	Loan EC Stalowa Wola	WIBOR 3M + fixed margin	15 850 PLN	14.12.2015 – 31.12.2027	15 850 PLN
3.	Loan EC Stalowa Wola	WIBOR 6M + fixed margin	15 300 PLN	15.12.2016 – 31.12.2027	11 000 PLN
4.	Loan EC Stalowa Wola	WIBOR 6M + fixed margin	150 000 PLN	30.06.2017 – 28.02.2018	150 000 PLN
5.	Loan EC Stalowa Wola	WIBOR 6M + fixed margin	175 157 PLN	01.11.2017 – 28.02.2018	175 157 PLN
6.	Loan PGE EJ 1	Fixed	2 940 PLN	08.11.2017 – 06.11.2020	2 940 PLN

Sureties and guarantees granted

TAURON Capital Group's principles of granting collaterals are based on TAURON Capital Group's regulation in force.

The below table presents a summary of collaterals granted by TAURON effective as of December 31, 2017.

Table no. 51. Summary of collaterals granted by TAURON, effective as of December 31, 2017

No.	Beneficiary	Agreement/Collateral	Entity whose liabilities constitute the subject of collateral	Amount (thou.)	Effective date
1.	WFOŚiGW	Bills of exchange with a promissory note	TAURON Wytwarzanie	40 000 PLN	15.12.2022
2.	WFOŚiGW	Bills of exchange with a promissory note	TAURON Ciepło	30 000 PLN	15.12.2022
3.	WFOŚiGW	Surety agreement	KW Czatkowice	914 PLN	15.06.2021
4.	PSG	Surety agreement	TAURON Sprzedaż	15 000 PLN	31.03.2018
5.	PSE	Surety agreement	TAURON Wytwarzanie	5 000 PLN	04.08.2019
6.	GAZ-SYSTEM	Surety agreement	EC Stalowa Wola	1 667 PLN	30.07.2020
7.	Doradcy Funduszu (Fund (Advisors)	Surety agreement	Nowe Jaworzno GT	2 350 PLN	28.09.2025
8.	Businesses and consumers that concluded an agreement TAURON Ekoenergia based on the electricity trading license granted by the President of ERO	Corporate guarantee	TAURON EKOENERGIA	16 400 PLN	31.12.2030
9.	NCBiR	Bills of exchange with a promissory note	TAURON	1 869 PLN	31.03.2026
10.	NCBiR	Bills of exchange with a promissory note	TAURON	2 375 PLN	31.07.2024
11.	Bondholders	Corporate guarantee	TAURON Sweden Energy	168 000 EUR	03.12.2029

The following framework (master) agreements, under which bank guarantees were issued, were in force in 2017:

1) Framework (master) agreement of June 8, 2015 on a limit on bank guarantees, concluded with BZ WBK, with the effective date of June 7, 2018 and an extension option by another 12 months. The limit amount of PLN 150 000 thou. to be used by TAURON and its subsidiaries in favor of the beneficiary – Izba Rozliczeniowa Giełd Towarowych S.A. (IRGIT).
2) Framework (master) Agreement of July 12, 2016 on a limit on bank guarantees, concluded with CaixaBank S.A. (Joint Stock Company) Branch in Poland (CaixaBank), under which a limit was granted for the period of 36 months, i.e. until July 11, 2019. The maximum effective term of the bank guarantees issued within the limit shall not exceed July 11, 2020. The limit to be used by TAURON and its subsidiaries in conjunction with their operations.

Within the bank guarantee limit obtained from BZ WBK in 2017 TAURON was ordering issuing of bank guarantees for the benefit of IRGIT as a security for the transactions made on TGE, with the effective term of less than one year.

The below table presents a summary of bank guaranties granted under the agreements effective as of December 31, 2017.

Table no. 52. Summary of bank guaranties granted under the agreements effective as of December 31, 2017

No.	Bank	Company	Beneficiary	Type of guarantee	Amount (thou.)	Launch date	Effective date
1.	BZ WBK	TAURON	IRGIT	payment	30 000 PLN	11.08.2016	31.03.2018
2.	BZ WBK	TAURON	IRGIT	payment	20 000 PLN	14.12.2016	31.03.2018
3.	CaixaBank	TAURON	PSE	performance bond	4 041 PLN	01.01.2017	11.02.2018
4.	CaixaBank	TAURON	GAZ-SYSTEM	performance bond	2 661 PLN	01.12.2017	30.11.2018
5.	CaixaBank	KW Czatkowice	PGE	performance bond	147 PLN	09.09.2016	31.01.2018
6.	CaixaBank	TAURON Dystrybucja Serwis	Strabag Infrastruktura Południe	performance bond	116 PLN	09.09.2016	15.06.2019
7.	CaixaBank	TAURON Wydobycie	Polskie Koleje Państwowe	performance bond	103 PLN	01.01.2017	31.12.2018
8.	CaixaBank	TAURON Ciepło	Elektrobudowa	payment	12 300 PLN	02.01.2017	31.12.2018
9.	CaixaBank	KW Czatkowice	PGE Paliwa (formerly EDF Paliwa)	performance bond	187 PLN	12.01.2017	30.01.2018
10.	CaixaBank	KW Czatkowice	PGE Paliwa (formerly EDF Paliwa)	performance bond	412 PLN	01.07.2017	30.01.2018[1]
11.	CaixaBank	TAURON Dystrybucja	Gmina Sosnowiec	performance bond	53 PLN	06.10.2017	06.10.2018
12.	CaixaBank	KW Czatkowice	PGE Górnictwo i Energetyka Konwencjonalna	performance bond	515 PLN	24.10.2017	30.01.2020

[1] *As of January 1, 2018 by way of amendment no. 1 to the guarantee the guarantee value was increased to PLN 761 thou. and the term was extended to January 31, 2019.*

Sureties and guarantees received

The below table presents a summary of collaterals received by TAURON effective as of December 31, 2017.

Table no. 53. Summary of collaterals received by TAURON, effective as of December 31, 2017

No.	Entity whose liabilities constitute the subject of collateral	Entity issuing collateral	Type of collateral	Amount in currency (thou.)	Effective date
1.	Polenergia Obrót S.A.	PKO BP	Bank guarantee	750 EUR	28.02.2019
2.	Ezpada s.r.o.	Ezpada A.G.	Corporate guarantee	1 000 EUR	28.02.2018
3.	Interenergia S.A.	NDI S.A.	Corporate guarantee	10 000 PLN	06.11.2019

9.3. Information on other agreements and events

Concluding of the agreement with TAURON Wydobycie on coal sales

On February 1, 2017 a multi-year agreement on coal sales for electricity generation purposes was concluded between TAURON and TAURON Wydobycie the subject of which was the purchase of coal by the Company for the needs of the generation units of TAURON Wytwarzanie and TAURON Ciepło. The agreement was concluded for the period until 31 December 31, 2019.

New coal trading model within TAURON Capital Group

On April 1, 2017 a new coal trading model within TAURON Capital Group, i.e. between TAURON Wydobycie and TAURON Wytwarzanie and TAURON Ciepło came into force. In accordance with the new model coal sales by TAURON Wydobycie to TAURON Wytwarzanie and TAURON Ciepło take place directly, bypassing TAURON as an intermediary. TAURON provides an agency service for the above mentioned entities. In accordance with the agreements concluded between TAURON and TAURON Wytwarzanie and TAURON Ciepło on the provision of services (agency agreements), TAURON was granted the power of attorney, among others, to:

1) agree and negotiate coal purchase terms,
2) draw up draft agreements,
3) conclude, make changes (amend) and terminate on behalf of TAURON Wytwarzanie and TAURON Ciepło agreements concluded with TAURON Wydobycie related to coal sales,
4) perform on behalf of TAURON Wytwarzanie and TAURON Ciepło actions related to the performance of the agreements,
5) draw up for TAURON Wytwarzanie and TAURON Ciepło monthly reports on the size of shipments, quality parameters, volumes of coal products transferred (for the needs of the excise tax related record keeping).

The above described model change led, among others, to the reduction of the number of invoices issued between TAURON Wydobycie and TAURON Wytwarzanie and TAURON Ciepło and to an improvement of the profitability ratio of the companies included within the Tax Capital Group.

Allocations of free CO_2 emission allowances and free allowances for heat production

In accordance with Directive 2003/87/EC of the European Parliament and of the Council of October 13, 2003 establishing a scheme for greenhouse gas emission allowances trading within the Community and amending the Council's Directive 96/61/EC, TAURON Capital Group is entitled to obtain free emission allowances pursuant to Article 10c of the above mentioned Directive ("derogation allowances"),

In order to obtain free allowances for electricity generation for 2016 TAURON Capital Group, on September 29, 2016, submitted to the National Emissions Balancing and Management Center (Krajowy Ośrodek Bilansowania i Zarządzania Emisjami) reports on works and expenditures related to the settlement of capital expenditures incurred to carry out investment tasks included in the National Investment Plan for the reporting period: July 1, 2015 – June 30, 2016.

Based on the reports submitted on April 21, 2017 the accounts of TAURON Capital Group's installations were credited with free CO_2 emission allowances in the number stemming from the incurred investment expenditures, i.e. 1 680 838 EUAs.

Additionally, in February 2017 the accounts of TAURON Capital Group's installations were credited with free allowances for heat production for 2017 in the total number of 469 945 EUAs.

Determining of the level of substitution fees by the ERO President

The binding *Act of April 10, 1997 the Energy Law* defines the rules of the support system for high efficiency coal co-generation and gas co-generation in the years 2014–2018. The Act defines the obligation to purchase and redeem certificates of electricity origin (the so-called "yellow" certificates – for gas co-generation, the so-called "red" certificates – for coal co-generation) or pay the substitution fee by electricity suppliers to the final consumers. For the "red" certificates the redemption obligation is 23.3% of the volume of electricity sold. In case of the "yellow" certificates this obligation shall increase from 3.9% in 2014 to 8% in 2018, in 2016 it was 6.0%, which is to contribute to the expansion of the co-generation sources operating on the gas fuel,

In accordance with the said Act the ERO President set and announced in Q2 2016 the following substitution fees in force in 2017:

1) for "red" certificates: PLN 10/MWh in 2017 (PLN 11/MWh in 2016),
2) for "yellow" certificates: PLN 120/MWh in 2017 (PLN 125/MWh in 2016),
3) for "violet" certificates: PLN 56/MWh in 2017 (PLN 63/MWh in 2016).

The substitution fees for the subsequent years shall be defined by the ERO President according to the following rules:

1) in case of coal-fired co-generation the substitution fee which in the system of certificates represents the benchmark for their prices, may not have a value lower than 5% and higher than 40% of the average electricity sales price on the competitive market in the preceding year,
2) in case of gas-fired co-generation the substitution fee may not be lower than 15% and higher than 110% of the average electricity sales price on the competitive market.

It will be possible to redeem the certificates originating from production in co-generation in individual years only within the settlement for the given year, i.e. until June of the subsequent year, which is a significant difference in relation to the previously used mechanisms when the possibility of "banking" the certificates from the previous years led to the disruption of the relationship between supply and demand and instability of the prices of certificates.

For certificates of origin obtained for electricity generation from renewable energy sources the unit substitution fee was set in the *Act of February 20, 2015 on renewable energy sources* at a fixed level of PLN 300.03/MWh in force for the entire duration of the support period.

The value of the announced unit substitution fees has a direct impact on TAURON Capital Group's results. The costs of electricity for consumers purchasing electricity for own use are additionally burdened with the costs of purchasing and submitting for redemption to the ERO President of the relevant certificates and should be classified as justified costs in the process of updating the electricity tariff.

TAURON units' win in a RES auction

On June 30, 2017 Ordinary Auction no. AZ/2/2017 was held for installations with total installed electric capacity not greater than 1 MW at which CO_2 emission is not greater than 100 kg/MWh with the factor of utilizing the installed electric capacity greater than 3 504 MWh/MW/year. As part of the preparation TAURON Capital Group selected for participation in the RES auction three hydroelectric power plants owned by TAURON EKOENERGIA: EW Brzeg, EW Kraszewice and EW Wrocław II. All the bids submitted by TAURON won the auctions and thus these power plants guaranteed for themselves the sale of electricity until the end of the support period (i.e. 2020 for EW Kraszewice and EW Wrocław II, and 2026 for EW Brzeg), at the bid price much higher than the prices obtained under the existing support system.

Signing of the hybrid financing agreements with BGK

On September 6, 2017 the Company and Bank Gospodarstwa Krajowego (BGK) signed the documentation of the subordinate bond issue program, constituting the basis for conducting a hybrid bond issue worth up to PLN 400 000 thousand.

The Company may carry out the hybrid bond issue in several series, and the period of the availability of funds was set as up to June 30, 2019. The financing period is 12 years from the issue date, however in accordance with the characteristic of the hybrid financing the first period of financing was defined as 7 years (the so-called *non-call period)*, during which an early redemption of the hybrid bonds by TAURON will not be possible BGK will not be able to sell them to third parties (in both cases subject to the exceptions defined in the documentation). The agreement also provides for an option to defer payment of interest on the hybrid bonds, until the hybrid bonds' redemption day as a maximum. Due ot the subordinate nature of the hybrid bonds, in case of TAURON's bankruptcy or liquidation the obligations under the hybrid bonds will have a priority of being satisfied only ahead of TAURON's shareholders' liabilities. A potential hybrid bond issue will have a positive impact on TAURON's financial stability because the bonds are excluded from calculating the leverage ratio (net debt/EBITDA ratio) which constitutes a covenant in some of TAURON's financing programs. Furthermore, 50% of the hybrid bonds amount will be classified by Fitch rating agency as equity in the rating model, which will have a positive impact on TAURON's rating. The hybrid bonds were granted BB+ rating by Fitch rating agency. In 2017 the Company did not conduct a bond issue under the above mentioned program, and the hybrid financing, due to its cost, is treated as an option in case of potential implementation of new investment projects and represents a financial security for the Group.

Tax Capital Group (Podatkowa Grupa Kapitałowa – PGK)

Due to the elapse, on December 31, 2017, of the three-year period of PGK's operation, on September 26, 2017 selected TAURON Capital Group's subsidiaries concluded the PGK agreement in the form of a notary authenticated deed. On October 30, 2017 the Head of the First Silesian Tax Office in Sosnowiec issued a decision on PGK's registration for the period of subsequent tax years 3, i.e. from January 1, 2018 until December 31, 2020. The new PGK includes the following subsidiaries: TAURON, TAURON Wytwarzanie, TAURON Dystrybucja, TAURON Sprzedaż, TAURON Sprzedaż GZE, TAURON Ciepło, TAURON Wydobycie, TAURON EKOENERGIA, TAURON Obsługa Klienta, TAURON Serwis, KW Czatkowice, Biomasa GT, TAURON Dystrybucja Serwis, Marselwind, Magenta GT, TAURON Ubezpieczenia sp. z o.o., En-Energia I sp. z o.o., En-Energia II sp. z o.o., En-Energia III sp. z o.o. and En-Energia IV sp. z o.o. Setting up of a new PGK will allow for taking advantage of the tax settlements synergy effect, i.e. deducting the tax loss of the subsidiaries that are members of the PGK from the income of the other subsidiaries. At the same time it will allow for continuing a unified system of settlements and for ensuring consistent interpretation of the tax regulations at the PGK level.

Revoking of the license for trading of natural gas abroad

As of September 30, 2017, at TAURON's request the President of the Energy Regulatory Office (ERO-URE), by way of the decision no. DRG.DRG-1.4112.38.2017.KL, revoked TAURON'S license for trading of natural gas abroad.

The revoking of the license involves obtaining an exemption from the need to maintain mandatory natural gas inventory (stock), beginning as of October 1, 2017, in connection with the coming into force of the amendment to the *law of February 16, 2007 on the inventory (stock) of oil products and natural gas.*

At the same time, taking into account the nature of its operations related to supplying TAURON Capital Group's subsidiaries with gas and the active participation in wholesale trading, TAURON has an option to purchase gas on the domestic market under its license for trading gas fuels. Gas contracting is conducted directly on the Polish Power Exchange (Towarowa Giełda Energii S.A.), both by way of futures market contracts, as well as SPOT market transactions. Furthermore, the Company contracts gas purchases and sales on the OTC market, based on commercial agreements concluded. Therefore, it should be pointed out that purchasing of gas fuel for the wholesale trading purpose as well as the security of supply and securing of the gas needs of TAURON Capital Group's subsidiaries are not in jeopardy.

Management Board of the Company

Katowice, March 12, 2018

Filip Grzegorczyk	– President of the Management Board	....
Jarosław Broda	– Vice-President of the Management Board	....
Kamil Kamiński	– Vice-President of the Management Board	....
Marek Wadowski	– Vice-President of the Management Board	....

Appendix A: GLOSSARY OF TERMS AND LIST OF ABBREVIATIONS

The glossary of trade terms and the list of abbreviations and acronyms most commonly used in this report is presented below.

Table no. 54. Explanation of abbreviations and acronyms and trade terms used in the report

No.	Abbreviation and trade term	Full name/explanation
1.	ARE	Agencja Rynku Energii S.A. with its seat in Warsaw
2.	BGK	Bank Gospodarstwa Krajowego with its seat in Warsaw
3.	Biomasa Grupa TAURON	Biomasa Grupa TAURON sp. z o.o. with its seat in Stalowa Wola
4.	BZ WBK	Bank Zachodni WBK S.A. with its seat ine Wrocław
5.	B2B	B2B (business-to-business) an acronym denoting transactions between two or more business entities
6.	CC	Central heating plant (Centralna Ciepłownia) in Olkusz lub Zawiercie
7.	Cash pooling	Cash pooling used by the Company – the consolidation of balances of bank accounts through physical transferring of cash from the accounts of TAURON Capital Group's subsidiaries in the bank in which cash pooling is operated to the bank account of the Pool Leader whose function is performed by the Company. At the end of each working day, cash is transferred from the bank accounts of TAURON Capital Group's subsidiaries which show positive balance to the bank account of the pool leader. At the beginning of each working day the bank accounts of TAURON Capital Group's subsidiaries are credited from the bank account of the pool leader with the amount required to maintain the financial liquidity of the TAURON Capital Group's subsidiary on the given working day.
8.	Color certificates	Property rights resulting from the certificates of origin of electricity generated in the way subject to support, the so-called colored certificates: 1) green – certificates of origin of electricity from RES, 2) violet – certificates of origin of electricity generated in co-generation fired using methane released and captured during underground mining works in active, in liquidation or liquidated hard coal mines, or using gas obtained from biomass processing, 3) red – certificates of origin of electricity from co-generation (CHP certificates – Combined Heat and Power), 4) yellow – certificates of origin of electricity generated in co-generation from gas-fired sources or with the total installed capacity below 1 MW, 5) blue – certificates of origin of electricity generated from agricultural biogas. White – energy efficiency certificates (mechanism stimulating and forcing pro-savings behaviors.
9.	CIRS	Transaction involving a swap between counterparties of interest payments assessed on amounts denominated in various currencies and determined according to various interest rates
10.	CSI	Customer Satisfaction Index – index used in marketing to determine the level of customer satisfaction with the products or services offered by a company
11.	CSR	Corporate Social Responsibility
12.	CUW	Shared Services Center (Centrum Usług Wspólnych), np. CUW R – accounting services
13.	DM	Brokerage House (Dom Maklerski)
14.	Good Practices 2016	Good Practices of WSE Listed Companies 2016, in force as of January 1, 2016
15.	EIB	European Investment Bank with its seat in Luxembourg
16.	EBIT	Earnings Before Interest and Taxes
17.	EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
18.	EC Stalowa Wola/ECSW	Elektrociepłownia (Combined Heat and Power Plant – CHP) Stalowa Wola S.A. with its seat in Stalowa Wola
19.	ENEA	ENEA S.A. with its seat in Poznań
20.	ENERGA	ENERGA S.A. with its seat in Gdańsk
21.	ERM	Enterprise Risk Management system

No.	Abbreviation and trade term	Full name/explanation
22.	EU ETS	European Union CO_2 Emission Allowances Trading System
23.	EUA	European Union Allowance – an allowance to introduce the carbon dioxide (CO_2) equivalent to the air, within the meaning of Article 2 section 4 of the *Act of July 17, 2009 on the management system of emissions of greenhouse gases and other substances*, which is used for settlements of emission level within the system and which can be managed under the rules provided in the *Act of April 28, 2011 on the system of greenhouse gases emission allowances trading (Journal of Laws No. 122, item 695)*
24.	EUR	Euro – a common European currency introduced in some EU member states
25.	GAZ-SYSTEM	Transmission Pipelines Operator GAZ-SYSTEM S.A. with its seat in Warsaw
26.	GPW	Warsaw Stock Exchange (Giełda Papierów Wartościowych w Warszawie S.A.) with its seat in Warsaw
27.	GRI	Global Reporting Initiative
28.	TAURON Capital Group	TAURON Capital Group Polska Energia S.A.
29.	GZE	Górnośląski Zakład Elektroenergetyczny
30.	IRGIT	Izba Rozliczeniowa Giełd Towarowych S.A. with its seat in Warsaw
31.	IRS	Interest Rate Swap, one of basic derivatives that is the subject of trading on the interbank market
32.	KGHM	KGHM Polska Miedź S.A. with its seat in Lubin
33.	KIC InnoEnergy	Knowledge and Innovations Community KIC InnoEnergy with its seat in Kraków
34.	Komfort Zarządzanie Aktywami	Komfort Zarządzanie Aktywami sp. z o.o. with its seat in Katowice
35.	Audit Committee	Audit Committee of the Supervisory Board of TAURON Polska Energia S.A.
36.	Nominations and Compensation Committee	Nominations and Compensation Committee of the Supervisory Board of TAURON Polska Energia S.A.
37.	Strategy Committee	Strategy Committee of the Supervisory Board of TAURON Polska Energia S.A.
38.	KPI	Key Performance Indicators, financial and non-financial indicators used as ways to measure progress of achieving goals of an organization
39.	KSE	National Power System (Krajowy System Elektroenergetyczny)
40.	Ksh	Commercial companies code
41.	KW Czatkowice	Kopalnia Wapienia (Limestone Mine) “Czatkowice” sp. z o.o. with its seat in Krzeszowice
42.	KZEE	National electricity consumption
43.	Model Biznesowy	Document entitled *TAURON Group’s Business and Operational Model* (which is an update of *TAURON Group’s Business Model* adopted by the Management Board on May 4, 2016)
44.	mBank	mBank S.A. with its seat in Warsaw
45.	Magenta GT	Magenta Grupa TAURON sp. z o.o. with its seat in Katowice
46.	Marselwind	Marselwind sp. z o.o. with its seat in Katowice
47.	Mg	Mega gram – million grams (1 000 000 g) i.e. a ton
48.	MSR	CO2 Emission Allowances Market Stability Reserve
49.	ISSR	International Financial Reporting Standards
50.	Nowe Jaworzno GT	Nowe Jaworzno Grupa TAURON sp. z o.o. with its seat in Jaworzno
51.	Line of Business	Seven areas of TAURON Capital Group’s core operations set up by the Company: Trading, Mining, Generation, RES, Heat, Distribution and Supply
52.	OPEC	Organization of the Petroleum Exporting Countries with its seat in Vienna
53.	ORM	Operational Capacity Reserve (OCR)
54.	OSD	Distribution System Operator (DSO)

No.	Abbreviation and trade term	Full name/explanation
55.	OSP	Transmission System Operator (TSO)
56.	OTC (OTC market)	Over The Counter Market
57.	OZE	Renewable Energy Sources (RES)
58.	OZEX_A	Green certificates index price
59.	Efficiency Improvement Program	TAURON Group's 2016–2018 Efficiency Improvement Program
60.	PEPKH	Polska Energia – Pierwsza Kompania Handlowa sp. z o.o. with its seat in Warsaw
61.	PGE	PGE Polska Grupa Energetyczna S.A. with its seat in Warsaw
62.	PGE EJ 1	PGE EJ 1 sp. z o.o. with its seat in Warsaw
63.	PGNiG	Polskie Górnictwo Naftowe i Gazownictwo S.A. with its seat in Warsaw
64.	PKB	Gross Domestic Product (GDP)
65.	PKO BP	Powszechna Kasa Oszczędności Bank Polski S.A. with its seat in Warszawie
66.	PLN	Polish zoty currency symbol – zł
67.	PMEC	Property rights for certificates of origin confirming generation of electricity in the other co-generation sources
68.	PMEF	Property rights for energy efficiency certificates
69.	PMGM	Property rights for certificates of origin confirming generation of electricity in co-generation, from gas-fired sources or sources with the total installed capacity below 1 MW
70.	PMMET	Property rights for certificates of origin confirming generation of electricity in co-generation fired using methane released and captured during underground mining works in active, in liquidation or liquidated hard coal mines, or using gas obtained from biomass processing
71.	PMOZE	Property rights for certificates of origin confirming generation of electricity in RES before March 1, 2009
72.	PMOZE_A	Property rights for certificates of origin confirming generation of electricity in RES after March 1, 2009
73.	PMOZE-BIO	Property rights for certificates of origin confirming generation of electricity from agricultural biogas from July 1, 2016
74.	PSE	Polskie Sieci Elektroenergetyczne S.A. with its seat in Konstancin-Jeziorna
75.	PSG	Polska Spółka Gazownictwa sp. z o.o. with its seat in Warsaw
76.	RB	Balancing Market (Rynek Bilansujący)
77.	RDN	Day Ahead Market (Rynek Dnia Następnego)
78.	RESPECT Index	Stock market index grouping stock market companies operating in accordance with the sustainable growth principles
79.	RTT	Futures Commodity Market (Rynek Terminowy Towarowy)
80.	Segment	TAURON Capital Group's segments of operations used in the statutory reporting process. TAURON Capital Group's results from operations are allocated to the following five Segments (also called Line of Business or Areas in this report): Mining, Generation, Distribution, Supply and Other.
81.	SPOT (SPOT market)	With respect to electricity, it is the place where trade transactions for electricity are concluded for which the period of delivery falls, at the latest, three days after the date of the transaction's conclusion (usually it is one day before the date of delivery). Operation of the SPOT market for electricity is strongly tied to the operation of the balancing market run by the TSO
82.	Company/TAURON	TAURON Polska Energia S.A. with its seat in Katowicach
83.	Strategy	Document entitled *TAURON Group's 2016–2025 Strategy* adopted by the Management Board on September 2, 2016

No.	Abbreviation and trade term	Full name/explanation
84.	Sustainable development strategy	Document entitled *TAURON Group's 2017–2025* Sustainable development strategy adopted by the Management Board on August 1, 2017, which is an update of the document entitled *TAURON Group's 2016–2018 Sustainable development strategy with an outlook until 2020*.
85.	TAMEH Czech	TAMEH Czech s.r.o. with its seat in Ostrava, Czech Republic
86.	TAMEH HOLDING	TAMEH HOLDING sp. z o.o. with its seat in Dąbrowa Górnicza
87.	TAMEH POLSKA	TAMEH POLSKA sp. z o.o. with its seat in Dąbrowa Górnicza
88.	TAURON/Company	TAURON Polska Energia S.A. with its seat in Katowice
89.	TAURON Ciepło	TAURON Ciepło sp. z o.o. with its seat in Katowice
90.	TAURON Czech Energy	TAURON Czech Energy s.r.o. with its seat in Ostrava, Czech Republic
91.	TAURON Dystrybucja	TAURON Dystrybucja S.A. with its seat in Kraków
92.	TAURON Dystrybucja Pomiary	TAURON Dystrybucja Pomiary sp. z o.o. with its seat in Tarnów
93.	TAURON Dystrybucja Serwis	TAURON Dystrybucja Serwis S.A. with its seat in Wrocław
94.	TAURON EKOENERGIA	TAURON EKOENERGIA sp. z o.o. with its seat in Jelena Góra
95.	TAURON Obsługa Klienta	TAURON Obsługa Klienta sp. z o.o. with its seat in Wrocław
96.	TAURON Serwis	TAURON Serwis sp. z o.o. with its seat in Katowice
97.	TAURON Sprzedaż	TAURON Sprzedaż sp. z o.o. with its seat in Kraków
98.	TAURON Sprzedaż GZE	TAURON Sprzedaż GZE sp. z o.o. with its seat in Gliwice
99.	TAURON Sweden Energy	TAURON Sweden Energy AB (publ) with its seat in Stockholm, Sweden
100.	TAURON Ubezpieczenia	TAURON Ubezpieczenia sp. z o.o. with its seat in Katowice
101.	TAURON Wydobycie	TAURON Wydobycie S.A. with its seat in Jaworzno
102.	TAURON Wytwarzanie	TAURON Wytwarzanie S.A. with its seat in Jaworzno
103.	TAURON Wytwarzanie Serwis	TAURON Wytwarzanie Serwis sp. z o.o. with its seat in Jaworzno
104.	TGE	Towarowa Giełda Energii S.A. with its seat in Warsaw
105.	EU	European Union
106.	UOKiK	Office of Competition and Consumer Protection (Urząd Ochrony Konkurencji i Konsumentów)
107.	USD	United States Dollar – US dollar's international acronym
108.	ERO (URE)	Energy Regulatory Office (Urząd Regulacji Energetyki)
109.	WFOŚiGW	Regional Environment Protection and Water Management Fund (Wojewódzki Fundusz Ochrony Środowiska i Gospodarki Wodnej) in Katowice or in Kraków
110.	Wsparcie Grupa TAURON	Wsparcie Grupa TAURON sp. z o.o. with its seat in Tarnów (formerly KOMFORT-ZET sp. z o.o.)
111.	WZ/ZW	General Meeting (GM) / Shareholders' Meeting
112.	ZG	Coal Mine (Zakład Górniczy) (Sobieski, Janina or Brzeszcze)
113.	ZW	Generation Plants (Zakłady Wytwarzania) in Bielsko-Biała, Kamienna Góra, Katowice or Tychy

Appendix B: INDEX OF TABLES AND FIGURES

The list of tables and figures presented in this report is provided below.

Index of tables

Table no. 1. List of material subsidiaries subject to consolidation as of December 31, 2017 . . . 12
Table no. 2. List of material joint subsidiaries subject to consolidation as of December 31, 2017 . . . 13
Table no. 3. Opportunities and threats for TAURON Capital Group's operations . . . 20
Table no. 4. Key strategic investment projects' work progress . . . 25
Table no. 5. Capital expenditures, highest by value, incurred in 2017 by TAURON Capital Group's Lines of Business . . . 28
Table no. 6. Selected research and development projects implemented in 2017 by TAURON Capital Group's subsidiaries, co-financed from external sources . . . 29
Table no. 7. Installed capacity and electricity generation by energy groups in 2016 . . . 47
Table no. 8. Electricity distribution to final consumers by energy groups . . . 49
Table no. 9. Sources of competiveness . . . 50
Table no. 10. TAURON Capital Group's 2015–2017 EBITDA broken down into individual lines of business (segments) . . . 52
Table no. 11. Mining Segment's 2015–2017 results . . . 53
Table no. 12. Generation Segment's 2015–2017 results . . . 55
Table no. 13. Distribution Segment's 2015–2017 results . . . 58
Table no. 14. Supply Segment's 2015–2017 results . . . 60
Table no. 15. Other Operations Segment's 2015–2017 results . . . 62
Table no. 16. 2015–2017 production and sales volumes . . . 64
Table no. 17. Categories of TAURON Capital Group's final customers . . . 67
Table no. 18. Volume of retail electricity sold by the Supply Segment and the number of customers in 2017 . . . 68
Table no. 19. Annual levels of NO_X, SO_2, dust and CO_2 emissions from fuel combustion for electricity generation purpose for 2017 . . . 89
Table no. 20. The level of fees for the use of the environment for business purposes due for 2017 . . . 90
Table no. 21. Most significant risks identified for TAURON Capital Group . . . 101
Table no. 22. Annual consolidated statement of financial position – assets (material items) . . . 105
Table no. 23. Annual consolidated statement of financial position – liabilities (material items) . . . 106
Table no. 24. Annual statement of comprehensive income for 2015–2017 . . . 108
Table no. 25. Statement of cash flows (significant items) in 2015–2017 . . . 111
Table no. 26. Structure of the annual consolidated statement of financial position . . . 112
Table no. 27. TAURON Capital Group's key financial ratios . . . 114
Table no. 28. Financial and operating data for 2017–2013 . . . 116
Table no. 29. TAURON Capital Group's EBITDA, broken down into Segments (Lines of Business) . . . 117
Table no. 30. Summary of issued and non-redeemed bonds as of December 31, 2017 . . . 120
Table no. 31. Information on forward transactions and derivatives as of December 31, 2017 . . . 121
Table no. 32. Compensation of the certified auditors for the services provided for TAURON Capital Group's subsidiaries . . . 123
Table no. 33. Dividends paid out in 2010–2014 . . . 124
Table no. 34. Key data on TAURON shares in 2011–2017 . . . 126
Table no. 35. Recommendations issued in 2017 . . . 127
Table no. 36. Highlights and activities performed as part of investor relations in 2017 . . . 129
Table no. 37. Shareholders holding, directly or indirectly, substantial blocks of shares . . . 134
Table no. 38. Management Board's competence . . . 136
Table no. 39. Supervisory Board's competence . . . 138
Table no. 40. Competence of the General Meeting of Shareholders . . . 140
Table no. 41. Description of the shareholders' rights related to the General Meeting of Shareholders . . . 141
Table no. 42. Competence of the Audit Committee . . . 151
Table no. 43. Competence of the Nominations and Compensation Committee . . . 152
Table no. 44. Competence of the Strategy Committee . . . 153
Table no. 45. Compensation of members of the Company's Management Board in 2017 broken down into components . . . 157
Table no. 46. Compensation of members of the company's Supervisory Board in 2017 . . . 159
Table no. 47. Risks related to the operations of TAURON that could exert adverse impact on the policies employed by TAURON . . . 172

Table no. 48. Summary of TAURON Capital Group's working capital loan and credit agreements as of December 31, 2017 . . . 179
Table no. 49. Summary of TAURON Capital Group's investment credit and loan agreements as of December 31, 2017 . . . 179
Table no. 50. Summary of loans granted by TAURON, effective as of December 31, 2017 . . . 180
Table no. 51. Summary of collaterals granted by TAURON, effective as of December 31, 2017 . . . 180
Table no. 52. Summary of bank guaranties granted under the agreements effective as of December 31, 2017 . 181
Table no. 53. Summary of collaterals received by TAURON, effective as of December 31, 2017 . . . 182
Table no. 54. Explanation of abbreviations and acronyms and trade terms used in the report . . . 186

Index of figures

Figure no. 1. TAURON Capital Group . . . 5
Figure no. 2. Location of TAURON Capital Group's key assets . . . 7
Figure no. 3. TAURON Capital Group's structure, including the subsidiaries subject to consolidation, as of December 31, 2017 . . . 8
Figure no. 4. TAURON Capital Group's 2025 Vision . . . 15
Figure no. 5. Prospects of TAURON Capital Group's segments . . . 16
Figure no. 6. Implementation of priorities based on the pillars of TAURON Capital Group's Strategy . . . 17
Figure no. 7. Capital expenditures by segments in 2016–2020 . . . 18
Figure no. 8. Key challenges facing TAURON Capital Group . . . 19
Figure no. 9. 2016–2018 Efficiency Improvement Program . . . 22
Figure no. 10. Strategic Initiatives and CAPEX rationalization in 2017–2020 . . . 22
Figure no. 11. Outlook for CAPEX directions beyond 2020 . . . 23
Figure no. 12. 2025 EBITDA outlook taking into account the risks and the implementation of the Strategy as well as the effects of the implementation of the Strategy . . . 24
Figure no. 13. Priority directions of innovations as well as research and development activities . . . 29
Figure no. 14. Average monthly electricity prices on the SPOT and RB markets, as well as average temperatures . . 33
Figure no. 15. BASE Y-18 contracts performance . . . 34
Figure no. 16. Average monthly SPOT and Y-18 contract prices on TGE in 2017 . . . 36
Figure no. 17. The impact of the legislative works and the environment on the EUA SPOT product price in 2017 . . . 38
Figure no. 18. Property rights indices . . . 39
Figure no. 19. TAURON Capital Group's competitive environment (landscape) (2016 data) . . . 46
Figure no. 20. EBIT – estimated structure by the main segments in 20161 . . . 46
Figure no. 21. Gross electricity production – estimated market shares in 2016 . . . 48
Figure no. 22. Installed capacity – estimated market shares in 2016 . . . 48
Figure no. 23. Electricity distribution – estimated market shares in 2016 . . . 49
Figure no. 24. Electricity supply to final consumers – estimated market shares in 2016 . . . 49
Figure no. 25. TAURON Capital Group's 2010–2017 EBITDA . . . 51
Figure no. 26. TAURON Capital Group's 2015–2017 EBITDA structure (composition) . . . 52
Figure no. 27. Change in TAURON Capital Group's EBITDA in 2015–2017 . . . 52
Figure no. 28. TAURON Capital Group's 2017 cash flows . . . 53
Figure no. 29. Mining Segment's 2015–2017 financial data . . . 54
Figure no. 30. Mining Segment's EBITDA . . . 54
Figure no. 31. Generation Segment's 2015–2017 financial data . . . 56
Figure no. 32. Generation Segment's EBITDA . . . 56
Figure no. 33. Distribution Segment's 2015–2017 financial data . . . 59
Figure no. 34. Distribution Segment's EBITDA . . . 59
Figure no. 35. Supply Segment's 2015–2017 financial data . . . 61
Figure no. 36. Supply Segment's EBITDA . . . 61
Figure no. 37. Other Operations Segment companies' 2015–2017 financial data . . . 62
Figure no. 38. Structure of installed electric capacity of the Generation Segment as of December 31, 2017 . . . 65
Figure no. 39. Electricity distribution by tariff groups in 2017 bDistribution of electricity according to tariff groups in 2016 (MWh) . . . 66
Figure no. 40. Timeline . . . 69
Figure no. 41. Prizes and accolades (honorable mentions) . . . 75
Figure no. 42. Assumptions of the Policy of Human Resources Management at TAURON Group . . . 77
Figure no. 43. Forms of development activities of employees of TAURON Capital Group's subsidiaries . . . 78
Figure no. 44. TAURON Capital Group's key 2017 training statistics . . . 78
Figure no. 45. Total number of training days broken down into Segments of operations (lines of business) . . . 78

Figure no. 46. The average number of training hours per employee, broken down into job (work position) groups . . . 79
Figure no. 47. TAURON Capital Group's average headcount in 2016 and in 2017 (FTEs) . . . 82
Figure no. 48. TAURON Capital Group's headcount as of December 31, 2016 and December 31, 2017 (persons) . . . 83
Figure no. 49. Structure of employment at TAURON Capital Group as of December 31, 2016 and December 31, 2017 (by education level) . . . 83
Figure no. 50. Structure of employment at TAURON Capital Group as of December 31, 2016 and December 31, 2017 (by age) . . . 83
Figure no. 51. Structure of employment at TAURON Capital Group as of December 31, 2016 and December 31, 2017 (by gender) . . . 84
Figure no. 52. Results of the survey covering households in 2011–2017 . . . 87
Figure no. 53. Results of the TAURON survey as compared to other Energy Groups in 2017 . . . 88
Figure no. 54. Structure of the property rights to the certificates of origin (MWh) . . . 91
Figure no. 55. Structure of energy waste management . . . 91
Figure no. 56. Structure of mining waste management . . . 92
Figure no. 57. Three Defense Lines Model . . . 93
Figure no. 58. Risk management as a function of the second defense line . . . 94
Figure no. 59. Risk management process . . . 94
Figure no. 60. Diagram of the management risk communication . . . 95
Figure no. 61. ERM system . . . 95
Figure no. 62. Architecture of the ERM System . . . 96
Figure no. 63. Organisational structure and documentation of the risk management process . . . 96
Figure no. 64. Number of risks monitored, broken down into categories . . . 97
Figure no. 65. Breakdown of TAURON Capital Group's trading operations . . . 98
Figure no. 66. Credit exposure components . . . 99
Figure no. 67. Risk management system tools . . . 100
Figure no. 68. Project risk management model . . . 101
Figure no. 69. Change in the level of assets and current assets . . . 105
Figure no. 70. Change in the level of liabilities and equity . . . 107
Figure no. 71. Change in the status of liabilities . . . 107
Figure no. 72. TAURON Capital Group's 2015–2017 financial results . . . 109
Figure no. 73. Structure of TAURON Capital Group's revenue in 2015–2017 . . . 109
Figure no. 74. TAURON Capital Group's financial results and the level of margins realized in 2015–2017 . . . 110
Figure no. 75. 2017–2015 cash flows . . . 111
Figure no. 76. The current liquidity ratio and the net debt to EBITDA ratio in 2017–2015 . . . 112
Figure no. 77. Structure of assets and liabilities . . . 113
Figure no. 78. Financial data of TAURON Capital Group for 2013–2017 . . . 117
Figure no. 79. Structure of TAURON Capital Group's EBITDA in 2013–2017 . . . 118
Figure no. 80. Data of the Mining Segment for 2013–2017 . . . 118
Figure no. 81. Data of the Generation Segment for 2013–2017 . . . 118
Figure no. 82. Data of the Distribution Segment for 2013–2017 . . . 119
Figure no. 83. Data of the Supply Segment for 2013–2017 . . . 119
Figure no. 84. Data of the Other Operations for 2013–2017 . . . 119
Figure no. 85. Structure of shareholding as of December 31, 2017 and as of the day of drawing up this report . 124
Figure no. 86. TAURON share price and trading volumes in 2017 . . . 126
Figure no. 87. TAURON share price and trading volumes since the market debut until December 31, 2017 . . . 127
Figure no. 88. TAURON share price versus WIG20 and WIG-Energia indices since the market debut until December 31, 2017 . . . 127
Figure no. 89. Structure of compensation for key manager positions . . . 156
Figure no. 90. Process streams . . . 162
Figure no. 91. Structure of TAURON Capital Group's processes (megaprocesses) . . . 163
Figure no. 92. Structure of TAURON Capital Group's Lines of Business . . . 163
Figure no. 93. Diagram of the split of responsibilities of members of the Management Board . . . 165
Figure no. 94. TAURON's organizational diagram (flowchart) as of the day of drawing up this report . . . 166

STATEMENTS OF THE MANAGEMENT BOARD OF TAURON POLSKA ENERGIA S.A.

TAURON POLSKA ENERGIA

RESPONSIBILITY STATEMENT

of the Management Board of TAURON Polska Energia S.A.
on the compliance of the Consolidated financial statements
of TAURON Capital Group
and the Management Board's report on the operations
of TAURON Capital Group

I, the undersigned, represent that, to the best of my knowledge, the consolidated financial statements of TAURON Capital Group and comparable figures were prepared in accordance with the applicable set of accounting standards and give a true and fair view of the assets, liabilities, financial position and profit or loss of TAURON Capital Group.

I also certify that the Management Board's report on the operations of TAURON Capital Group includes a fair review of the development and performance of the business and the position of TAURON Capital Group, together with a description of the principal risks and uncertainties that TAURON Capital Group faces.

Management Board Members:

Filip Grzegorczyk	– President of the Management Board	....
Jarosław Broda	– Vice-President of the Management Board	....
Kamil Kamiński	– Vice-President of the Management Board	....
Marek Wadowski	– Vice-President of the Management Board	....

12 March 2018
date

TAURON POLSKA ENERGIA

S T A T E M E N T

of the Management Board of TAURON Polska Energia S.A.
on the appointment of the entity authorized to audit financial statements
(Consolidated financial statements of TAURON Capital Group)

I, the undersigned, represent that the entity authorized to audit financial statements and examining the financial statements of TAURON Capital Group was appointed in accordance with legal regulations, and this entity and auditors examining the statements have met conditions for developing an impartial and independent report on the review of the audited financial statements in accordance with applicable regulations and professional standards.

Management Board Members:

Filip Grzegorczyk	– President of the Management Board	....
Jarosław Broda	– Vice-President of the Management Board	....
Kamil Kamiński	– Vice-President of the Management Board	....
Marek Wadowski	– Vice-President of the Management Board	....

12 March 2018

date