TAURON POLSKA ENERGIA

Consolidated annual report of TAURON Polska Energia S.A. Capital Group for the year 2016

15 March 2017

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 hereby provide you with the Consolidated Annual Report of TAURON Polska Energia S.A. Capital Group, in which we have included the financial results of TAURON Group and summarised the most important events of 2016.

The first half of the year demonstrated a considerable decline of sentiment in the equity market, mainly triggered by macroeconomic factors and the growth in uncertainty associated with the international situation. The negative sentiment of investors was reflected in results of key indices of the Warsaw Stock Exchange, which has also affected quotations of companies from the energy sector. However, last months of 2016 brought improvement of key economic indicators and a visible recovery in the capital market in Poland, which is a good forecast for the outlook of the Warsaw market in 2017.

Referring to the situation of the energy sector, it should be noted that the previous year was the consecutive period when growth in the domestic electricity consumption was recorded (by approximately 2 percent in relation to 2015), accompanied by the growth in electricity production (by 0.5 percent). High dynamics was observed, in particular, in the growth of energy generated in power plants using renewable sources and in gas-fired power plants.

The financial results of TAURON Group generated in the previous year confirm a stable position of the Company in the Polish power market. The Group's revenue on sales and EBITDA reached the level of PLN 17.6 billion and over PLN 3.3 billion, respectively. These results are slightly lower than those generated in 2015, whereas the decline in EBITDA results mainly from continuing low prices of electricity and coal sales.

In connection with continuing unfavourable market conditions in terms of profitability of coal-fired energy generation, the downturn in prices of green certificates and introduction of new regulations in the area of renewable energy sources, we have performed impairment tests for the loss in value of generation assets. As a result of those tests it became necessary to recognise write-downs at a level of over PLN 700 million, which had an adverse impact on net consolidated profit.

Undoubtedly, the most important event of the past year was the presentation of the new strategy of TAURON Group for the years 2016–2025, which responds to the challenges associated with the future of the power sector. Its underlying assumptions focus on ensuring the Group's financial stability, investment tailored to market needs and financial capacity of the Group as well as on the development of innovation and building relations with a customer. Sales and development of new products and services shall constitute a strong base for the Group's growth. In this area we plan a dynamic development of our offer, which will enable us to retain the existing base of customers buying our products and increase profitability.

The investment directions adopted after 2020 also include a new energy sector, besides regulated energy sector. TAURON will invest in the development of e-mobility, scattered generation of heat and energy, prosumer energy, smart home and smart city solutions as well as services related to energy. In the scope of innovation and research and development activities the strategy assumes raising capital expenditure at a level of 0.4 percent of consolidated revenue value per year.

A significant element of the new strategy is also the efficiency improvement programme assuming that savings at a level of PLN 1.3 billion should be achieved between 2016 and 2018, another important element are strategic initiatives which will generate additional financial effect in 2017–2020 at a level of PLN 1.9 billion.

In the previous year we also implemented a new business model. The method of the Group's functioning and its organisational culture have changed. The new concept is based, inter alia, on process management, customer orientation, removing administrative burdens and better use of knowledge of TAURON Group employees. We will eliminate overlapping activities and internal competition as well as search for synergies which will translate into real savings.

Year 2016 was also a period of enhanced activity in the scope of acquiring alternative sources of TAURON Group financing. One of such activities was the issue of hybrid bonds with the value of EUR 190 million, taken up by the European Investment Bank under the so-called Juncker Plan. It was the first issue of hybrid bonds of this type in Europe and the first one in Poland. The funds to be raised will be allocated for the implementation of investment tasks in the area of Distribution. In the period under discussion we also concluded agreements with a group of bondholders pursuant to which the allowable value of the net debt/EBITDA ratio was increased from 3.0x to 3.5x, which ensures higher financial security of the Group.

Importantly, the adopted direction of TAURON Group's development and activities undertaken by the Management Board were appreciated not only by investors but also by Fitch rating agency which evaluated creditworthiness of the Company and reaffirmed its credit rating at the BBB level and revised the outlook from negative to stable.

The past year showed that TAURON Group operates in a very demanding market where only companies determining the directions of the sector development and offering best solutions to their clients may be successful. Year 2017 carries new challenges, however, I can assure that the Management Board of TAURON Polska Energia S.A. will strive to achieve the best operating and financial results possible on this difficult market.

On behalf of the Management Board, I would like to express our gratitude to our shareholders, Members of the Supervisory Board and employees for their involvement in the process of building TAURON Group's value.

Yours faithfully,

Filip Grzegorczyk

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

Selected figures	in thousands PLN		in thousands EUR	
	2016 period from 01.01.2016 to 31.12.2016	**2015** period from 01.01.2015 to 31.12.2015 *(converted data)*	**2016** period from 01.01.2016 to 31.12.2016	**2015** period from 01.01.2015 to 31.12.2015 *(converted data)*
Selected consolidated figures of TAURON Polska Energia S.A. Capital Group				
Revenues on sales	17 646 489	18 264 440	4 032 838	4 364 471
Operating profit (loss)	801 522	(1 901 216)	183 176	(454 315)
Profit (loss) before tax	508 861	(2 187 771)	116 292	(522 790)
Net profit (loss)	370 137	(1 804 215)	84 589	(431 135)
Net profit (loss) attributable to shareholders of the parent entity	367 468	(1 807 317)	83 979	(431 876)
Net profit (loss) attributable to non-controlling shares	2 669	3 102	610	741
Other total income	277 748	122 076	63 475	29 171
Total aggregate income	647 885	(1 682 139)	148 064	(401 964)
Total aggregate income attributable to shareholders of the parent entity	644 944	(1 685 301)	147 392	(402 720)
Total aggregate income attributable to non-controlling shares	2 941	3 162	672	756
Profit (loss) per share (in PLN/EUR) (basic and diluted)	0,21	(1,03)	0,05	(0,25)
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	3 064 215	3 387 458	700 280	809 467
Net cash flows from investment activity	(3 627 458)	(3 942 122)	(829 000)	(942 010)
Net cash flows from financial activity	590 261	(525 692)	134 895	(125 619)
Increase/(decrease) in net cash and equivalents	27 018	(1 080 356)	6 175	(258 162)
	As of 31.12.2016	**As of 31.12.2015**	**As of 31.12.2016**	**As of 31.12.2015**
Fixed assets	29 148 253	28 124 185	6 588 665	6 599 598
Current assets	4 308 641	3 947 248	973 924	926 258
Total Assets	33 456 894	32 071 433	7 562 589	7 525 856
Share capital	8 762 747	8 762 747	1 980 729	2 056 259
Equity attributable to shareholders of the parent entity	16 649 266	16 018 328	3 763 396	3 758 847
Equity attributable to non-controlling shares	30 052	29 829	6 793	7 000
Total equity	16 679 318	16 048 157	3 770 189	3 765 847
Long-term liabilities	11 968 719	8 583 950	2 705 407	2 014 302
Short-term liabilities	4 808 857	7 439 326	1 086 993	1 745 706
Total liabilities	16 777 576	16 023 276	3 792 400	3 760 008

The above financial data were converted into EUR, cumulatively for the fourth quarter of 2016 and 2015, according to the following principles:

– individual items of the statement of financial standing – according to the average NBP exchange rate announced on 30 December 2016 – PLN/EUR 4.4240 (as at 31 December 2015 – PLN/EUR 4.2615)

– 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 2016 to 31 December 2016 – PLN/EUR 4.3757 (for the period from 01 January 2015 to 31 December 2015 – PLN/EUR 4.1848).

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 2016

TAURON POLSKA ENERGIA S.A.
CAPITAL GROUP

KATOWICE, KS. PIOTRA
ŚCIEGIENNEGO 3

CONSOLIDATED FINANCIAL STATEMENTS FOR THE 2016 FINANCIAL YEAR

WITH
AUDITOR'S OPINION
AND
AUDIT REPORT

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Deloitte.

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AUDITOR'S OPINION

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

Auditor's report

We have audited the attached financial statements of the TAURON Polska Energia S.A. Capital Group (hereinafter: the "Capital Group"), for which TAURON Polska Energia S.A. (hereinafter: the "Parent") with its registered office in Katowice, at ul. ks. Piotra Ściegiennego 3 is the Parent. These consolidated financial statements include: the consolidated statement of financial position prepared as at 31 December 2016, consolidated statement of comprehensive income, consolidated statement of changes in equity, consolidated statement of cash flows for the financial year from 1 January 2016 to 31 December 2016 and notes.

Responsibility of the Company's manager and those charged with governance for the financial statements

The Management Board of the Parent is responsible for the preparation of the consolidated financial statements, based on properly kept accounting records, and their fair presentation in accordance with the International Accounting Standards, International Financial Reporting Standards, related interpretations published as European Commission regulations and applicable laws. It is also obliged to ensure internal control as it determines necessary for the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Under the Accounting Act of 29 September 1994 (Journal of Laws of 2016 item 1047 as amended), hereinafter referred to as the "Accounting Act" the Management Board of the Parent and members of its Supervisory Board are obliged to ensure that the consolidated financial statements meet the requirements of the Accounting Act.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit works.

We conducted our audit in accordance with Section 7 of the Accounting Act and the National Auditing Standards in line with the wording of the International Standards on Auditing adopted by Resolution No. 2783/52/2015 of the National Council of Statutory Auditors of 10 February 2015 as amended. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

Sąd Rejonowy dla m. st. Warszawy KRS 0000446833, NIP: 527-020-07-86, REGON: 010076870

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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 Parent's preparation and fair presentation 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 Parent's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Management Board of Parent, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the attached consolidated financial statements:

- give a true and fair view of the economic and financial position of the Capital Group as at 31 December 2016 and its financial performance for the financial year from 1 January 2016 to 31 December 2016 in accordance with the International Accounting Standards, International Financial Reporting Standards, related interpretations published as European Commission regulations and the adopted accounting principles (policies) of the Parent,
- comply, with respect to their form and content, with the applicable provisions of law and the articles of association of the Capital Group.

Report on other legal and regulatory requirements

Opinion on the report on the activities

We do not express an opinion on the report on the activities of the Capital Group.

It is the responsibility of the Management Board of the Parent to prepare the report on the activities of the Capital Group in accordance with the Accounting Act and other applicable laws. Moreover, the Management Board of the Parent and members of the Supervisory Board are obliged to ensure that the financial statements and the report on the activities meet the requirements of the Accounting Act.

When auditing the consolidated financial statements we were obliged to examine the report on the activities and indicate whether the information contained therein complies with Article 49 of the Accounting Act and the Ordinance of the Minister of Finance of 19 February 2009 on current and periodic information published by issuers of securities and the rules of equal treatment of the information required by the laws of non-member states (Journal of Laws of 2014 item 133 as amended) and is consistent with underlying information disclosed in the attached financial statements. Additionally, it was our responsibility to indicate whether we have detected any material misstatement in the report on the activities based on our knowledge of the Capital Group and its business environment obtained in the course of the audit.

In our opinion, the information contained in the report on the activities of the Capital Group complies with Article 49 of the Accounting Act and the Ordinance of the Minister of Finance of 19 February 2009 on current and periodic information published by issuers of securities and the rules of equal treatment of the information required by the laws of non-member states (Journal of Laws of 2014 item 133 as amended) and is consistent with underlying information disclosed in the attached financial statements. Moreover, based on our knowledge of the Capital

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Group and its business environment obtained in the course of the audit, we have not detected any material misstatements in the report on the activities.

Statement of compliance with corporate governance principles

In relation to our audit of the consolidated financial statements, it was our responsibility to examine the Parent's statement of compliance with corporate governance principles, which constitutes a separate part of the report on the activities of the Capital Group. In our opinion, the Parent's statement provides all information required by the secondary legislation issued under Article 60.2 of the Act on public offering, conditions governing the introduction of financial instruments to organized trading, and public companies of 29 July 2005 (Journal of Laws of 2016 item 1639 as amended) and regulations issued under Article 61 thereof. The information is compliant with the applicable laws and information presented in the consolidated financial statements.

Artur Maziarka
Key certified auditor
conducting the audit
No. 90108

On behalf of Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – entity authorized to audit financial statements entered under number 73 on the list kept by the National Council of Statutory Auditors:

Artur Maziarka – Vice-President of the Management Board of Deloitte Polska Sp. z o.o. – which is the General Partner of Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k.

Warsaw, 13 March 2017

The above audit opinion together with audit report is a translation from the original Polish version. In case of any discrepancies between the Polish and English version, the Polish version shall prevail.

REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS OF THE TAURON POLSKA ENERGIA S.A. CAPITAL GROUP FOR THE 2016 FINANCIAL YEAR

I. GENERAL INFORMATION

1. Details of the audited Parent

The Parent of the Capital Group operates under the business name TAURON Polska Energia S.A. (hereinafter: the "Parent"). The Company's registered office is located in Katowice, Ks. Piotra Ściegiennego 3 Street.

The Parent operates as a joint stock company. The Parent is recorded in the Register of Entrepreneurs kept by the District Court for Katowice-Wschód, VIII Commercial Division of National Court Register under KRS number 0000271562.

The Parent operates based on the provisions of the Code of Commercial Companies.

As of 31 December 2016, the Parent's share capital equaled PLN 8.762.747 thousand and was divided into 1.752.549.394 shares with a face value of PLN 5 each.

Composition of the Management Board of the Parent as at the date of the opinion:
- 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.

Changes in the composition of the Management Board of the Parent during the audited period and until the date of the opinion:
- on 8 January 2016 the Supervisory Boeard dismissed Mrs Anna Striżyk from the posiotion of Vice-President of the Management Board,
- on 29 January 2016 the Supervisory Board appointed Mr. Marek Wadowski to hold the position of the Vice-President of the Management Board,
- on 14 November 2016 the Supevisory Board dismissed Mr. Remigiusz Nowakowski from the position of President of the Management Board and appointed Mr Filip Grzegorczyk to hold this position.

As of 15 December 2016 (the date of the last Shareholders' Meeting) the Parent's shareholders included:
- State Treasury – 30,06% shares,
- KGHM Polska Miedź S.A. – 10,39% shares,
- Nationale Nederlanden Otwarty Fundusz Emerytalny – 5,06% shares,
- other shareholders – 54,49% shares.

During the audited period, the shareholding structure of the Parent's share capital did not undergo any changes.

After the balance-sheet date there were no changes in the Parent's share capital.

As of 31 December 2016, the Parent's equity amounted to PLN 16.530.268 thousand.

2. Structure of the Capital Group

The consolidated financial statements as of 31 December 2016 included the following entities:

a) Parent – TAURON Polska Energia S.A.

We have audited the financial statements of the Parent for the period from 1 January to 31 December 2016. As a result of our audit, on 13 March 2017 we issued an unqualified opinion.

b) Companies subject to full consolidation:

Name and address of the Company	Interest in the share capital (%)	Name of entity that audited the financial statements and type of opinion issued	Balance sheet date of the consolidated entity
TAURON Wytwarzanie S.A	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Ekoenergia Sp. z o.o.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Dystrybucja S.A.	99,72%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Sprzedaż Sp. z o.o.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Czech Energy s.r.o.	100%	COTAX AUDIT s.r.t. – unqualified opinion	31 December 2016
TAURON Sprzedaż GZE Sp. z o.o.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Ciepło Sp. z o.o.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Obsługa Klienta Sp. z o.o.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. w likwidacji	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – qualified opinion	31 December 2016
TAURON Wydobycie S.A.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Sweden Energy AB (publ)	100%	Deloitte AB - audit opinion has not been issued by the date of this report.	31 December 2016
TAURON Dystrybucja Pomiary Sp. z o.o.	99,72%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Dystrybucja Serwis S.A.	99,72%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
TAURON Serwis Sp. z o.o.	95,61%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
Komfort-Zet Sp. z o.o.	99,72%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
Biomasa Grupa TAURON Sp. z o.o.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
Kopalnia Wapienia Czatkowice Sp. z o.o.	100%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016

Name and address of the Company	Interest in the share capital (%)	Name of entity that audited the financial statements and type of opinion issued	Balance sheet date of the consolidated entity
Marselwind Sp. z o.o.	100%	ATAC Audytorzy i Partnerzy spółka z ograniczoną odpowiedzialnością – opinion with emphasis of matter	31 December 2016

c) Companies subject to consolidation using the equity method:

Name and address of the Company	Interest in the share capital (%)	Name of entity that audited the financial statements and type of opinion issued	Balance sheet date of the consolidated entity
Elektrociepłownia Stalowa Wola S.A.	50%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – opinion with emphasis of matter	31 December 2016
Elektrownia Blachownia Nowa Sp. z o.o. w likwidacji	50%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – opinio with emphasis of matter	31 December 2016
Tameh Holding Sp. z o.o.	50%	Not issued	31 March 2017
Tameh Polska Sp. z o.o.	50%	Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – unqualified opinion	31 December 2016
Tameh Czech s.r.o	50%	Deloitte Audit s.r.o. - unqualified opinion	31 December 2016

In the audited financial year, the Parent included in consolidation entities TAURON Serwis Sp. z o.o. and Komfor-Zet Sp. z o.o. Effect of this decision was reflected in the consolidated financial statements.

3. Information about the consolidated financial statements for the prior financial year

The activities of the Capital Group in 2015 resulted in a net loss of PLN 1.804.215 thousand. The consolidated financial statements of the Capital Group for 2015 were audited by a certified auditor. The audit was performed by authorized entity Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. The certified auditor issued an unqualified opinion on those financial statements.

The General Shareholders' Meeting which approved the consolidated financial statements for the 2015 financial year was held on 8 June 2016.

In accordance with applicable laws, the consolidated financial statements for the 2015 financial year were submitted to the National Court Register (KRS) on 13 June 2016.

4. Details of the authorized entity and the key certified auditor acting on its behalf

The entity authorized to audit the financial statements was appointed by the Supervisory Board. The audit of the consolidated financial statements was performed based on the agreement of 15 June 2016 concluded between the Parent and Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. with its registered office in Warsaw, al. Jana Pawła II 22, recorded under number 73 on the list of entities authorized to provide audit services kept by the National Council of Statutory Auditors. On behalf of the authorized entity, the audit of the consolidated financial statements was conducted under the supervision of Arrtur Maziarka, key certified auditor (No. 90108) in the registered office of the Parent from 20 to 24 February 2017 as well as outside the Company's premises until the date of this opinion.

Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. and the key certified auditor conducting audit confirm that they are authorized to carry out audits and meet the requirements of Article 56 of the Act on certified auditors and their self-government, entities authorized to audit financial statements and public supervision (Journal of Laws of 2016 item 1000 as amended) to express an unbiased and independent opinion on the consolidated financial statements of the Capital Group.

5. Availability of data and management's representations

The scope of our audit was not limited.

During the audit, necessary documents and data as well as detailed information and explanations, were provided to the authorized entity and the key certified auditor, as confirmed e.g. in the written representation of the Management Board of the Parent of 13 March 2017.

II. ECONOMIC AND FINANCIAL POSITION OF THE CAPITAL GROUP

Presented below are the main items from the consolidated statement of comprehensive income, consolidated statement of financial position as well as financial ratios describing the financial performance of the Capital Group and its economic and financial position compared to the prior year.

Main financial data from consolidated statement of comprahensive income (PLN '000)	2016	2015
Sales revenue	17.646.489	18.264.440
Operating expenses	(16.829.480)	(20.137.894)
Operating profit (loss)	801.522	(1.901.216)
Net profit (loss)	370.137	(1.804.215)
Main financial data from consolidated statement of financial position (PLN '000)		
Inventory	486.120	433.279
Receivables from clients	1.894.065	1.830.033
Current assets	4.308.641	3.947.248
Total assets	33.456.894	32.071.433
Equity	16.679.318	16.048.157
Short-term liabilities (including short-term provisions and accruals)	4.808.857	7.439.326
Liabilities to suppliers	829.729	790.706
Total liabilities and provisions	16.777.576	16.023.276

Profitability and efficiency ratios	2016	2015
– return on sales	5%	-10%
– net return on equity	2%	-10%
– assets turnover ratio	0,53	0,57
– receivables turnover in days	38	37
– liabilities turnover in days	17	15
– inventory turnover in days	10	9
Liquidity/Net working capital		
– debt ratio	50%	50%
– equity to fixed assets ratio	50%	50%
– net working capital (PLN '000)	(500.216)	(3.492.078)
– current ratio	0,90	0,53
– quick ratio	0,79	0,47

An analysis of the above figures and ratios indicated the following trends in 2016:

- increase of return on sales and net return on equity;
- decrease of assets turnover ratio;
- increase of receivables, liabilities and inventory turnover ratios;
- no change of debt ratio and equity to fixed assets ratio;
- decrease of net working capital deficit;
- increase of liquidity ratios.

III. DETAILED INFORMATION

1. Information about the audited consolidated financial statements

The audited consolidated financial statements were prepared as at 31 December 2016 and include:

- consolidated statement of financial position prepared as of 31 December 2016, with total assets and liabilities plus equity of PLN 33.456.894 thousand,
- consolidated statement of comprehensive income for the period from 1 January 2016 to 31 December 2016, with a net profit of PLN 370.137 thousand and total comprehensive income of PLN 647.885 thousand,
- consolidated statement of changes in equity for the period from 1 January 2016 to 31 December 2016, disclosing an increase in equity of PLN 631.161 thousand,
- consolidated statement of cash flows for the period from 1 January 2016 to 31 December 2016, showing a cash inflow of PLN 27.018 thousand,
- notes, comprising a summary of significant accounting policies and other explanatory information.

The audit covered the period from 1 January 2016 to 31 December 2016 and focused mainly on:

- verification of the correctness and fairness of the consolidated financial statements prepared by the Management Board of the Parent;
- verification of the consolidation documentation;
- evaluation of the correctness of the consolidation methods and procedures applied during consolidation;
- review of opinions and reports on audits of financial statements of subsidiaries and associated companies included in consolidation, prepared by other certified auditors.

2. Consolidation documentation

The Parent presented the consolidation documentation including:

- financial statements of controlled entities, adjusted to the accounting principles (policy) applied during consolidation;
- financial statements of controlled entities translated into the Polish currency;
- consolidation adjustments and eliminations necessary for preparation of the consolidated financial statements;
- calculation of non-controlling interests;
- calculation of exchange differences arising from translation of the financial statements of controlled entities denominated in foreign currencies.

The financial statements of the subsidiaries were consolidated using the full method, i.e. full amounts of all relevant items of the financial statements of the Parent and the subsidiaries included in consolidation were summed up.

The equity method was applied with respect to associated entities. The value of the Parent's interest in the associated company was adjusted by increases or decreases in the equity of the associated company attributable to the Parent, which occurred in the period covered by consolidation, and decreased by dividends due from such companies.

The Parent preparing the consolidated financial statements has not applied any material simplifications and exceptions to the consolidation principles with respect to the controlled entities.

3. Completeness and correctness of drawing up consolidated statement of cash flows, consolidated statement of changes in equity, notes and explanations and the report on the activities of the Capital Group

The Parent confirmed the validity of the going concern basis in preparation of the consolidated financial statements. The notes and explanations to the consolidated financial statements gives a description of measurement principles regarding assets, equity, liabilities, financial performance and principles of preparation of the consolidated financial statements.

The Parent prepared notes in the form of tables to individual items of the consolidated statement of financial position and consolidated statement of comprehensive income as well as narrative descriptions in line with the requirement of IFRS.

The Parent prepared the consolidated cash flow statement and consolidated statement of changes in equity in accordance with the requirements of IFRS.

The Management Board of the Parent prepared and supplemented the consolidated financial statements with a report on the activities of the Capital Group in the 2016 financial year. The report contains information determined by Article 49 of the Accounting Act and the Ordinance of the Minister of Finance Ordinance of 19 February 2009 on current and periodic information published by issuers of securities and the rules of equal treatment of the information required by the laws of non-member states (Journal of Laws of 2014 item 133 as amended). We have audited the report with respect to the disclosed information derived directly from the audited consolidated financial statements.

IV. FINAL NOTES

Management Board's Representations

Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. and the key certified auditor received a representation letter from the Parent's Management Board, in which the Board stated that the Capital Group complied with the laws in force.

Artur Maziarka
Key certified auditor
conducting the audit
No. 90108

On behalf of Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k. – entity authorized to audit financial statements entered under number 73 on the list kept by the National Council of Statutory Auditors:

Artur Maziarka – Vice-President of the Management Board of Deloitte Polska Sp. z o.o. – which is the General Partner of Deloitte Polska Spółka z ograniczoną odpowiedzialnością Sp. k.

Warsaw, 13 March 2017

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 2016

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(in PLN '000)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended 31 December 2016	Year ended 31 December 2015 (*restated figures*)
Sales revenue	**12**	17 646 489	18 264 440
Cost of sales, of which:	**13**	(15 717 462)	(19 028 962)
Impairment of non-financial non-current assets	***13.3***	*(832 092)*	*(3 594 654)*
Profit (loss) on sale		**1 929 027**	**(764 522)**
Selling and distribution expenses	**13**	(459 191)	(489 963)
Administrative expenses	**13**	(652 827)	(618 969)
Other operating income and expenses	**14**	(15 487)	(27 762)
Operating profit (loss)		**801 522**	**(1 901 216)**
Share in profit/(loss) of joint ventures	**22**	60 040	7 933
Interest expense on debt	**15**	(259 564)	(279 673)
Other finance income and costs	**15**	(93 137)	(14 815)
Profit (loss) before tax		**508 861**	**(2 187 771)**
Income tax expense	**16**	(138 724)	383 556
Net profit (loss)		**370 137**	**(1 804 215)**
Measurement of hedging instruments	**30.5**	127 252	85 932
Foreign exchange differences from translation of foreign entities		9 991	595
Income tax	**16**	(24 178)	(16 327)
Other comprehensive income subject to reclassification to profit or loss		**113 065**	**70 200**
Actuarial gains/(losses)	**34.1**	204 597	64 523
Income tax	**16**	(38 874)	(12 260)
Share in other comprehensive income of joint ventures	**22**	(1 040)	(387)
Other comprehensive income not subject to reclassification to profit or loss		**164 683**	**51 876**
Other comprehensive income, net of tax		**277 748**	**122 076**
Total comprehensive income		**647 885**	**(1 682 139)**
Net profit (loss):			
Attributable to equity holders of the Parent		367 468	(1 807 317)
Attributable to non-controlling interests		2 669	3 102
Total comprehensive income:			
Attributable to equity holders of the Parent		644 944	(1 685 301)
Attributable to non-controlling interests		2 941	3 162
Basic and diluted earnings (loss) per share (in PLN):	**17**	**0.21**	**(1.03)**

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 2016	As at 31 December 2015
ASSETS			
Non-current assets			
Property, plant and equipment	**18**	26 355 189	24 882 817
Goodwill	**19**	40 156	92 059
Energy certificates and emission allowances for surrender	**20.1**	126 260	510 840
Other intangible assets	**21**	1 224 427	1 182 765
Investments in joint ventures	**22**	461 348	418 127
Loans granted to joint ventures	**23**	240 951	221 803
Other financial assets	**24**	227 140	211 215
Other non-financial assets	**25.1**	422 400	550 375
Deferred tax assets	**16.3**	50 382	54 184
		29 148 253	**28 124 185**
Current assets			
Energy certificates and emission allowances for surrender	**20.2**	980 348	805 388
Inventories	**26**	486 120	433 279
Receivables from clients	**27**	1 894 065	1 830 033
Receivables arising from taxes and charges	**28**	263 854	228 345
Other financial assets	**24**	94 753	34 334
Other non-financial assets	**25.2**	185 008	233 059
Cash and cash equivalents	**29**	384 881	364 912
Non-current assets classified as held for sale		19 612	17 898
		4 308 641	**3 947 248**
TOTAL ASSETS		**33 456 894**	**32 071 433**

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 2016	As at 31 December 2015
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**	7 823 339	11 277 247
Revaluation reserve from valuation of hedging instruments	**30.5**	29 660	(73 414)
Foreign exchange differences from translation of foreign entities		9 200	(791)
Retained earnings/(Accumulated losses)	**30.4**	24 320	(3 947 461)
		16 649 266	**16 018 328**
Non-controlling interests		**30 052**	**29 829**
Total equity		**16 679 318**	**16 048 157**
Non-current liabilities			
Debt	**33**	8 759 789	4 924 127
Provisions for employee benefits	**34**	1 373 385	1 735 206
Provisions for disassembly of fixed assets, land restoration and other provisions	**35**	449 310	377 372
Accruals, deferred income and government grants	**38**	554 293	650 364
Deferred tax liabilities	**16.3**	759 568	795 176
Other financial liabilities	**42**	72 374	101 705
		11 968 719	**8 583 950**
Current liabilities			
Debt	**33**	219 740	3 214 520
Liabilities to suppliers	**39**	829 729	790 706
Capital commitments	**40**	1 033 804	766 843
Provisions for employee benefits	**34**	158 228	172 505
Provisions for liabilities due to energy certificates and greenhouse gas emission allowances	**36**	964 821	1 018 134
Other provisions	**37**	366 456	178 044
Accruals, deferred income and government grants	**38**	267 662	254 337
Liabilities arising from taxes and charges	**41**	410 943	429 649
Other financial liabilities	**42**	256 295	340 666
Other non-financial liabilities	**43**	301 179	273 922
		4 808 857	**7 439 326**
Total liabilities		**16 777 576**	**16 023 276**
TOTAL EQUITY AND LIABILITIES		**33 456 894**	**32 071 433**

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 2015		**8 762 747**	**10 393 686**	**(143 019)**	**(1 386)**	**(1 045 580)**	**17 966 448**	**30 116**	**17 996 564**
Dividends	**30.6, 31**	–	–	–	–	(262 882)	**(262 882)**	(2 787)	**(265 669)**
Other transactions with non-controlling shareholders	**30.6**	–	–	–	–	63	**63**	(662)	**(599)**
Distribution of prior year profits		–	883 561	–	–	(883 561)	**–**	–	**–**
Transactions with shareholders		**–**	**883 561**	**–**	**–**	**(1 146 380)**	**(262 819)**	**(3 449)**	**(266 268)**
Net profit (loss)		–	–	–	–	(1 807 317)	**(1 807 317)**	3 102	**(1 804 215)**
Other comprehensive income		–	–	69 605	595	51 816	**122 016**	60	**122 076**
Total comprehensive income		**–**	**–**	**69 605**	**595**	**(1 755 501)**	**(1 685 301)**	**3 162**	**(1 682 139)**
As at 31 December 2015		**8 762 747**	**11 277 247**	**(73 414)**	**(791)**	**(3 947 461)**	**16 018 328**	**29 829**	**16 048 157**
Dividends	**30.6, 31**	–	–	–	–	–	**–**	(3 043)	**(3 043)**
Accounting for acquisition of ZCP Brzeszcze	**32**	–	–	–	–	(14 041)	**(14 041)**	–	**(14 041)**
Other transactions with non-controlling shareholders	**30.6**	–	–	–	–	35	**35**	325	**360**
Coverage of prior years loss	**30.3**	–	(3 453 908)	–	–	3 453 908	**–**	–	**–**
Transactions with shareholders		**–**	**(3 453 908)**	**–**	**–**	**3 439 902**	**(14 006)**	**(2 718)**	**(16 724)**
Net profit (loss)		–	–	–	–	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**

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 2016	Year ended 31 December 2015
Cash flows from operating activities			
Profit (loss) before taxation		**508 861**	**(2 187 771)**
Share in (profit)/loss of joint ventures		(60 040)	(7 933)
Depreciation and amortization		1 668 726	1 832 780
Impairment losses on property, plant and equipment, intangible assets and goodwill	**44.1**	867 109	3 595 895
Interest and commissions		249 719	273 502
Other adjustments of profit before tax		(2 703)	329
Change in working capital	**44.1**	227 335	(7 628)
Income tax paid	**44.1**	(394 792)	(111 716)
Net cash from operating activities		**3 064 215**	**3 387 458**
Cash flows from investing activities			
Purchase of property, plant and equipment and intangible assets	**44.2**	(3 516 296)	(3 973 510)
Public aid refund	**44.2**	(131 077)	–
Purchase of financial assets	**44.2**	(36 621)	(29 067)
Loans granted	**44.2**	(23 575)	(26 100)
Total payments		**(3 707 569)**	**(4 028 677)**
Proceeds from sale of property, plant and equipment and intangible assets		33 260	36 554
Repayment of loans granted		–	14 500
Redemption of debt securities		–	21 732
Dividends received	**44.2**	29 728	4 684
Other proceeds		17 123	9 085
Total proceeds		**80 111**	**86 555**
Net cash used in investing activities		**(3 627 458)**	**(3 942 122)**
Cash flows from financing activities			
Redemption of debt securities	**44.3**	(3 300 000)	(450 000)
Repayment of loans and borrowings	**44.3**	(140 331)	(140 585)
Dividends paid to equity holders of the Parent		–	(262 882)
Interest paid	**44.3**	(255 116)	(276 305)
Other payments		(29 697)	(44 059)
Total payments		**(3 725 144)**	**(1 173 831)**
Issue of debt securities	**44.3**	4 284 607	310 000
Proceeds from contracted loans/borrowings		914	295 000
Subsidies received		29 884	43 139
Total proceeds		**4 315 405**	**648 139**
Net cash from (used in) financing activities		**590 261**	**(525 692)**
Net increase / (decrease) in cash and cash equivalents		**27 018**	**(1 080 356)**
Net foreign exchange difference		1 283	1 169
Cash and cash equivalents at the beginning of the period	**29**	**327 715**	**1 408 071**
Cash and cash equivalents at the end of the period, of which:	**29**	**354 733**	**327 715**
restricted cash	**29**	144 404	206 254

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

INFORMATION ABOUT THE CAPITAL GROUP AND BASIS FOR 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 at 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, Entry No. KRS 0000271562. The Parent has been assigned statistical number REGON 240524697.

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

The core business of the TAURON Group includes the following segments: Mining, Generation, Distribution, Sale and other operations, which has been discussed in more detail in Note 10 to these consolidated financial statements.

The Group's consolidated financial statements cover the year ended 31 December 2016 and present comparative data for the year ended 31 December 2015.

These consolidated financial statements were approved for publication by the Management Board on 13 March 2017.

Composition of the Management Board

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

- 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.

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

As at 31 December 2015, the composition of the Management Board was as follows:

- Remigiusz Nowakowski – President of the Management Board;
- Jarosław Broda – Vice-President of the Management Board;
- Kamil Kamiński – Vice-President of the Management Board;
- Anna Striżyk – Vice-President of the Management Board;
- Piotr Zawistowski – Vice-President of the Management Board.

Changes in the composition of the Management Board in the year ended 31 December 2016 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 2016 (Section 6.11.1).

2. Composition of the TAURON Capital Group and joint ventures

As at 31 December 2016, 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 and in the decision-making body held by TAURON Polska Energia S.A.
1	TAURON Wydobycie S.A.[1]	Jaworzno	Mining	100.00%
2	TAURON Wytwarzanie S.A.	Jaworzno	Generation	100.00%
3	TAURON Ekoenergia Sp. z o.o.	Jelenia Góra	Generation	100.00%
4	Marselwind Sp. z o.o.	Katowice	Generation	100.00%
5	TAURON Ciepło Sp. z o.o.	Katowice	Generation	100.00%
6	TAURON Serwis Sp. z o.o.[2]	Katowice	Generation	95.61%
7	TAURON Dystrybucja S.A.	Kraków	Distribution	99.72%
8	TAURON Dystrybucja Serwis S.A.[3]	Wrocław	Distribution	99.72%
9	TAURON Dystrybucja Pomiary Sp. z o.o.[3]	Tarnów	Distribution	99.72%
10	TAURON Sprzedaż Sp. z o.o.	Kraków	Sales	100.00%
11	TAURON Sprzedaż GZE Sp. z o.o.	Gliwice	Sales	100.00%
12	TAURON Czech Energy s.r.o.	Ostrawa, Czech Republic	Sales	100.00%
13	TAURON Obsługa Klienta Sp. z o.o.	Wrocław	Other	100.00%
14	Kopalnia Wapienia Czatkowice Sp. z o.o.	Krzeszowice	Other	100.00%
15	Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. in liquidation[4]	Warszawa	Other	100.00%
16	TAURON Sweden Energy AB (publ)	Sztokholm, Sweden	Other	100.00%
17	Biomasa Grupa TAURON Sp. z o.o.	Stalowa Wola	Other	100.00%
18	KOMFORT-ZET Sp. z o.o.[3]	Tarnów	Other	99.72%

[1] *On 1 December 2016, the business combination under common control of TAURON Wydobycie S.A. and Nowe Brzeszcze Grupa TAURON Sp. z o.o. was registered, which has been discussed in more detail in Note 32 to these consolidated financial statements.*

[2] *On 2 November 2016, a business combination under common control of TAURON Serwis Sp. z o.o. and TAURON Wytwarzanie Serwis Sp. z o.o. was registered.*

[3] *TAURON Polska Energia S.A. holds indirect interest in TAURON Dystrybucja Serwis S.A., TAURON Dystrybucja Pomiary Sp. z o.o. and KOMFORT-ZET Sp. z o.o. through a subsidiary, TAURON Dystrybucja S.A. Additionally, TAURON Polska Energia S.A. uses the shares of TAURON Dystrybucja Serwis S.A. and TAURON Dystrybucja Pomiary Sp. z o.o.*

[4] *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 annulment of the liqudation of the company.*

As at 31 December 2016, TAURON Polska Energia S.A. held direct and indirect interest in the following key jointly-controlled entities, which are measured in the consolidated financial statements using the equity method:

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	Elektrownia Blachownia Nowa Sp. z o.o. in liquidation[1]	Kędzierzyn Koźle	Generation	50.00%
3	TAMEH HOLDING Sp. z o.o.[2]	Dąbrowa Górnicza	Generation	50.00%
4	TAMEH POLSKA Sp. z o.o.[2]	Dąbrowa Górnicza	Generation	50.00%
5	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. and Elektrownia Blachownia Nowa Sp. z o.o. in liquidation 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 capitals 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 their financial statements in accordance with the International Financial Reporting Standards, as endorsed by the European Union, except KOMFORT-ZET Sp. z o.o., which maintains its accounting records and prepares financial statements in accordance with the Accounting Act, as well as TAURON Czech Energy s.r.o. and TAURON Sweden Energy AB (publ), whose accounting records are kept and financial statements prepared in accordance with the accounting principles adopted 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 of these financial statements, no circumstances posing a risk to the Group companies' ability to continue as a going concern had been identified.

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 covered by 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 judgment and estimates

When applying the accounting policy to the issues mentioned below, professional judgment 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. 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.

Items of the consolidated financial statements exposed to a considerable risk of material adjustment of the carrying amounts of assets and liabilities are presented below. Detailed information regarding assumptions adopted has been presented in notes to these consolidated financial statements, in line with the table below.

(in PLN '000)

Item	Value of item to which the estimate figure applies		Accounting policy description	Details regarding assumptions made and calculation of significant estimates
	As at 31 December 2016	As at 31 December 2015		
Property, plant and equipment	26 355 189	24 882 817	note 9.2 note 9.6	• In the year ended 31 December 2016, having performed impairment tests, the Group recognized an impairment loss on property, plant and equipment of PLN 1 942 937 thousand and derecognized an impairment loss of PLN 1 208 245 thousand. note 18
Goodwill	40 156	92 059	note 9.3 note 9.6	• In the year ended 31 December 2016 as a result of impairment test performed as at 30 June 2016 the Group recognized an impairment loss on goodwill of PLN 51 903 thousand. The impairment tests as at 31 December 2016 did not indicate the need to recognise impairment losses. note 19
Provisions for employee benefits	1 531 613	1 907 711	note 9.18	• Description of actuarial assumptions made and valuation method. note 34
Provision for gas emission obligations	209 736	153 083	note 9.20	• Provision calculation note 36
Provision for obligation to submit energy certificates	755 085	865 051	note 9.20	• Provision calculation note 36
Provision for mine decommissioning costs	146 885	111 675	note 9.19	• Provision calculation note 35
Provision for restoration of land and dismantling and removal of fixed assets	115 302	101 244	note 9.19	• Provision calculation note 35
Provision for onerous contracts	198 844	182 877	note 9.21	• Provision calculation note 35
Accrued revenue from sales of electricity and distribution services in the Sales segment	15 573 358	16 284 291	note 9.26	• Additional assessment of revenue from sales of electricity and distribution services in the Sales segments at the end of the reporting period in the amount of PLN 353 065 thousand. note 12
Deferred tax assets	957 118	936 795	note 9.25	• Realisation of deferred tax assets. note 16.3
Derivative instruments: Assets Liabilities	 56 417 560	 5 684 112 109	note 9.16	• Fair value measurement note 45.3
Receivables from clients	1 894 065	1 830 033	note 9.12	• Impairment loss – as at the end of the reporting period impairment losses on receivables from clients amounted to PLN 205 647 thousand. note 27

7. New standards and interpretations

The Group did not choose an early application of any standards or 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 and are not yet effective**

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

IFRS 9 *Financial Instruments*
Effective in the EU – annual periods beginning on or after 1 January 2018.

Key amendments introduced by IFRS 9 *Financial Instruments*:

- amendments to classification and measurement of financial assets based on the business model for managing the financial assets and their contractual cash flow characteristics. The existing four categories of financial assets

defined in IAS 39 *Financial Instruments: Recognition and Measurement* will be replaced by two categories: amortized cost and fair value;
- a new impairment model based on expected credit losses;
- new hedge accounting model.

Effect on the consolidated financial statements

The amendments to classification and measurement of financial assets will lead to changes in the classification of financial assets in the Group's financial statements, however, this will not have a material impact on the measurement as well as the Group's profit/loss and capitals. An analysis of the financial assets held by the Group as at 31 December 2016 has shown that, provided that the Group maintains similar financial assets when IFRS 9 *Financial Instruments* becomes effective, the new classification will not materially change the measurement and hence the Company's profit/loss and capitals. The instruments which have so far been classified to loans and receivables meet the conditions for classification to assets measured at amortized cost and hence the amendment will not result in any changes in measurement. The Group does not hold any assets held to maturity. Other categories of financial assets measured at fair value in line with IFRS 9 are assets measured at fair value.

The above outcomes of the analysis do not apply to shares held by the Group in entities not quoted in active markets, which cannot be reliably measured and therefore are currently measured at cost less any impairment. Effects of IFRS 9 *Financial Instruments* on the consolidated financial statements with respect to this asset group have not been fully analysed yet.

With respect to expected credit losses, an analysis of receivables from the Sales segment buyers has been carried out. This class of financial instruments constitutes the most important item of the Group's financial assets. These receivables have been classified by client groups demonstrating material differences in terms of credit losses based on historical data. Subsequently, for each group, an allowance recognition coefficient has been determined, including the effects of available information regarding future on historical ratios.

Preliminary analysis performed indicates that application of IFRS 9 will not materially affect the consolidated financial statements.

As at 31 December 2016 the Group held hedging instruments to hedge fluctuations in cash flows related to issued bonds due to interest rate risk. These interest rate swaps are subject to hedge accounting. IFRS 9 *Financial Instruments* coming into effect is not expected to materially affect the consolidated financial statements of the Group with respect to hedge accounting.

IFRS 15 *Revenue from Contracts with Customers*

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

The standard specifies how and when to recognize revenue and requires more detailed disclosures. The Standard replaces IAS 18 *Revenue*, IAS 11 *Construction Contracts* and a number of interpretations concerning revenue recognition.

Effect on the consolidated financial statements

The Group is carrying out an analysis of contracts with clients in five steps, which are necessary from the viewpoint of correct determination of revenue in line with IFRS 15 *Revenue from Contracts with Customers* and include: identifying a contract (or a contract group); indicating individual performance obligations and defining prices; assigning the prices to individual performance obligations and determining the revenue. The new standard requires considerably more detailed disclosure of sales and revenue in financial statements. Evaluation of the effects of IFRS 15 on the consolidated financial statements is still being analysed due to a broad range of the related changes. The new guidance included in IFRS 15 may necessitate system change.

Preliminary analysis of impact of IFRS 15 on the accounting policies applied has shown that the new standard changes the method of accounting for contracts with customers, in particular if services and goods are provided under a single contract, which may be particularly important for the Sales segment, mainly with regard to contracts for sales of electricity and gas, which offer customers additional services or devices included in the sales prices. With respect to the Group, these services shall include providing customers with support of engineers or servicemen in case of power or gas supply failure. Another analysed aspect involves fees for so-called price guarantee in sales contracts, which enable clients to ensure that during a given period, prices paid by them will not change. Pursuant to the new standard, the Group is obliged to separately recognise each identifiable performance obligations, and therefore to allocate transaction price to these obligations. At present, the Group has been analysing its contractual obligations in order to identify individual obligations and allocate transaction prices to them.

Additionally, in the Distribution segment, the Group is analysing contracts that underlie the recognition of revenue from connecting new customers and contracts for distribution and comprehensive services in light of IFRS 15, with regard to separate identification of these services as required by the Standard. To this end the Group analyses its contracts among others in terms of sources of law underlying the provision of these services, legal obligations imposed on the company with regard to the connecting of new customers, service pricing freedom and interrelation of the compensation received for the provision of these services, possibility to include both services into a single agreement and the right of the customer who has concluded the following agreements: the connection agreement and distribution/comprehensive service agreement to resign from the purchasing of these services.

- **Standards, revised standards and interpretations issued by the International Accounting Standards Board which have not been endorsed by the European Union and are not yet effective**

According to the Management Board, the following standard will or may materially impact the accounting policies applied thus far:

IFRS 16 *Leases*

Effective date given in the Standard, not endorsed by the EU – annual periods beginning on or after 1 January 2019.

Under IFRS 16 *Leases*, the lessee recognizes a right-of-use asset and a lease liability. The right-of-use asset is treated similarly to other non-financial assets and depreciated accordingly. The lease liability is initially measured at the present value of the lease payments payable 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 shall use their incremental borrowing rate. Lessors continue to classify leases as operating or finance, with the approach to lessor accounting substantially unchanged from IAS 17 *Leases*. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset. Otherwise, a lease is classified as an operating lease. A lessor recognises 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 recognises 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 benefit from the use of the underlying asset is diminished.

Effect on the consolidated financial statements

A preliminary analysis of the impact of IFRS 16 *Leases* on the accounting principles 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 intends to analyse all its lease agreements to identify leases which require recognition of assets and liabilities in the financial statements. As the effective date of IFRS 16 *Leases* is still distant, and it has not yet been approved by the EU, as at the date of approving these financial statements for publication the Group had not carried out any analyses which would enable determining the impact of the planned changes on the financial statements. The analysis will be conducted at a later time.

(in PLN '000)

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

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*
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 until completion of research on the equity method
Revised IAS 12 *Income Taxes – Recognition of Deferred Tax Assets for Unrealized Losses*	1 January 2017
Revised IAS 7 *Statement of Cash Flows – Disclosure Initiative*. The amendments are intended to clarify IAS 7 to improve information provided to users of financial statements about an entity's financing activities.	1 January 2017
Revised IFRS 2 *Share-based Payments: Classification and Measurement of Share-based Payment Transactions*	1 January 2018
Revised IFRS 4 *Insurance Contracts – application of IFRS 9 Financial Instruments along with IFRS 4 Insurance Contracts*	1 January 2018 or at the date of first-time adoption of IFRS 9
Annual Improvements to IFRS (2014–2016):	
IFRS 12 *Disclosure of Interests in Other Entities*	1 January 2017
IFRS 1 *First-time Adoption of International Financial Reporting Standards*	1 January 2018
IAS 28 *Investments in Associates and Joint Ventures*	1 January 2018
IFRIC 22 *Foreign Currency Transactions and Advance Consideration*	1 January 2018
Revised IAS 40 *Investment Property – Transfers of Investment Property*	1 January 2018

** 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 policies

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 2015, except for the application of amendments to the standards specified below as well as a change in the presentation of gains/losses on trading in emission allowances purchased for resale and generation of profit on market price fluctuations as well as gains/losses on derivative commodity instruments.

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

(in PLN '000)

Standard	Effective in the EU as of (*annual periods beginning on or after this date*)
Revised IAS 19 *Employee Benefits – Defined Benefit Plans: Employee Contributions*	1 February 2015
Annual Improvements to *IFRS (Cycle 2010–2012)*	1 February 2015
Revised IFRS 11 *Joint Arrangements: Accounting for Acquisitions of Interests in Joint Operations.*	1 January 2016
Revised IAS 1 *Presentation of Financial Statements – Disclosure Initiative*	1 January 2016
Revised IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets: Clarification of Acceptable Methods of Depreciation and Amortization*	1 January 2016
Revised IAS 16 *Property, Plant and Equipment* and IAS 41 *Agriculture: Bearer Plants*	1 January 2016
Revised IAS 27 *Separate Financial Statements: Equity Method in Separate Financial Statements*	1 January 2016
Annual Improvements to *IFRS (Cycle 2012–2014)*	1 January 2016
Revised IFRS 10 *Consolidated Financial Statements*, IFRS 12 *Disclosure of Interests in Other Entities* and IAS 28 *Investments in Associates and Joint Ventures Investment Entities: Applying the Consolidation Exception*	1 January 2016

Presentation change

The Group decided to change the presentation of gains/losses on forward and futures transactions – derivative commodity instruments falling within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* as well as gains/losses on trading in emission allowances purchased for resale and generation of profit in the short term due to volatility of market prices, in the financial statements.

Before, gains/losses on derivative commodity instruments were recognized within financing activities. As these gains/losses are linked with operating activities with respect to commodity trading and gains/losses on trading activities are aimed to be recognized in one place in the statement of comprehensive income and volatility of profit is to be reduced in different parts of the statement of comprehensive income, i.e. operating and financing activities, the Management Board decided to introduce a presentation change.

Currently, the aggregate gain/loss on the emission allowances purchased for resale and generation of profit due to volatility of market prices, comprising the aggregate gain/loss on:

- trading in the inventory of greenhouse gas emission allowances classified to the trading portfolio;
- change in fair value measurement of the inventory of greenhouse gas emission allowances classified to the trading portfolio;
- change in measurement and gains/losses on derivative commodity instruments falling within the scope of IAS 39, related to purchases and sales of greenhouse gas emission allowances;

is presented within revenue from sales of goods (gain) or cost of sales (loss).

The cost of fees and charges relating to the aforesaid transactions is also recognized within operating activities.

Additionally, operating revenue or expenses include gain (loss) on change in measurement and on exercising derivative commodity instruments falling within the scope of IAS 39, related to purchases and sales of other commodities.

According to the Management Board, the aforementioned changes concerning aggregate presentation of gains/losses on a specific trading strategy within operating activities will reflect the Company's activities in the field of trading in commodities and the related derivatives in a more accurate manner.

The effect of the presentation change on the consolidated statement of comprehensive income for the year ended 31 December 2015 is presented in the table below. The change has not had any effect on the Group's profit/loss.

(in PLN '000)

	Year ended 31 December 2015 (*approved figures*)	Change in presentation of gains/losses on trading in emission allowances and on commodity derivative instruments	Year ended 31 December 2015 (*restated figures*)
Sales revenue	18 375 224	(110 784)	18 264 440
Cost of sales	(19 140 775)	111 813	(19 028 962)
Profit (loss) on sale	**(765 551)**	**1 029**	**(764 522)**
Selling and distribution expenses	(488 859)	(1 104)	(489 963)
Operating profit (loss)	**(1 901 141)**	**(75)**	**(1 901 216)**
Other finance income and costs	(14 890)	75	(14 815)
Net profit (loss)	**(1 804 215)**	**–**	**(1 804 215)**

9. 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 acquirer 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 — Note 32

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 acquiree 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 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.

(in PLN '000)

9.2. Property, plant and equipment — Note 18

Key fixed assets by segment:

- With respect to 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 sulfur-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.;
- With respect to Distribution: power lines and stations. Power lines are located on the area of 57,000 square meters, with the total length of ca. 267,000 km. The Group holds over 59,000 electrical substations in its assets;
- With respect to 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 9.19);
- 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 charges are calculated at cost of the given 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	17 years
Plant and machinery	13 years
Other tangible fixed assets	5 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 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 for liabilities arising from gas emissions have been presented in Note 9.20.

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.

(in PLN '000)

Average residual useful lives by other intangible asset group:

Asset group	Average remaining amortization period (number of years)
Development expenses	4 years
Software, concessions, patents, licenses and similar items	4 years
Other	10 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 9.17).

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. Shares 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).

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

9.9. Loans granted 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 — Note 25

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.

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 (property rights) 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 9.26.

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. 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.

9.14. Issued capital — Note 30.1

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

9.15. Debt — Note 33

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

(in PLN '000)

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.

9.16. Derivative financial instruments — Note 45.3

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 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 presented 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 9.17). 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 9.17.
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.
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.

9.17. 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.

9.18. Provisions for employee benefits — Note 34

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 bonuses 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 employee 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.

9.19. Provisions for dismantling fixed assets and restoration of land — Note 35

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 ant 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.

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

9.20.1. Provision for the obligation to surrender energy certificates — Note 36.1

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 – such an obligation is considered met.

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.

9.20.2. Provision for greenhouse gas emission liabilities — Note 36.2

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 in 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.

9.21. Other provisions — Note 35.3, 37

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.
- A provision for onerous contracts. At the end of the reporting period, the Group recognized a provision for onerous contracts. It was recognized for a surplus of the expected costs of fulfilment of the obligations under the agreements entered into with a joint venture over the expected benefits.
- 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.

9.22. Accruals and government grants — Note 38

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.

9.23. Liabilities to suppliers, capital commitments and other financial liabilities — Note 39, 40, 42

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

9.24. Receivables / Liabilities due to taxes and charges — Note 28, 41

Settlements due to taxes and charges presented in the statement of financial position comprise:

- Income tax receivables and liabilities;
- VAT and excise duty;
- PIT and social insurance;
- Environmental fees and other regulatory settlements.

9.25. 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.

9.26. 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.

9.26.1. 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 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 recognized 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.

9.26.2. Revenue from sales of electricity, gas fuel 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 being parties 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 of sales related to client migration to an integrated billing system

  Due to the implementation of an integrated billing system, at the end of each reporting period additional assessments are made to comply with technical requirements of the billing system in relation to earlier meter reading dates and changes to the client billing model versus the previous billing systems.
- 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 is also accounted for.

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 energy balance

  The company reconciles the energy 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.

9.26.3. 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 kind of 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 100MW) is subject to similar rules. However, it is the local market operator that is responsible for the settlements.

9.26.4. Revenue from sales of heat in the Generation segment

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

Institutional clients incur charges twice a month: fixed ones for power contracted in advance at rates specified in the tariff in force and floating ones 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 floating charges or just with fixed charges in accordance with concluded contracts. Fixed and variable charges are imposed on consumers once a month, in line with the meter reading schedule, on a specific meter reading date, at rates specified in the tariff in force. Variable charges are imposed periodically, by reference to meter readings on an accrual basis. 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 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.

9.26.5. 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 intragroup market for the Mining segment. Entities operating in the Company's sales network in the Mining segment, i.e. Authorized Coal Sellers and Coal Sellers, play a strategic role in coal sales. Coal sales are performed also under agreements with final buyers, in the form of Intracommunity Delivery of Goods and export, as well as 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.

(in PLN '000)

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.

9.27. 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 selling and distribution as well as 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.

9.28. 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).

Exchange rates applied for the purpose of balance sheet measurement:

Currency	31 December 2016	31 December 2015
USD	4.1793	3.9011
EUR	4.4240	4.2615
CZK	0.1637	0.1577

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.

9.29. Statement of cash flows

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

OPERATING SEGMENTS

10. Information on 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, administrative expenses of the Parent are presented under unallocated expenses. 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.

The Group's financing (including finance income and costs) and income tax are monitored at the Group level and they are not allocated to segments.

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

The Management Board separately monitors operating results of the segments to take decisions on how to allocate the resources, to assess the effects of the allocation and to evaluate 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 2016 to 31 December 2016 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. *Elektrownia Blachownia Nowa Sp. z o.o. in liquidation** *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 desulfurization 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., KOMFORT-ZET Sp. z o.o. and Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. in liquidation are also treated as other operations of the Group.

10.1. Operating segments

Revenue, profit or loss, assets and liabilities of individual operating segments of the Group for the years ended 31 December 2016 and 31 December 2015 have been presented below.

(in PLN '000)

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.*

Year ended 31 December 2015 (*restated figures*)	Mining	Generation	Distribution	Sales	Other	Unallocated items / Eliminations	Total
Revenue							
Sales to external customers	459 304	2 226 869	3 006 443	12 486 908	84 916	–	**18 264 440**
Inter-segment sales	746 640	3 149 411	3 443 831	3 386 447	843 037	(11 569 366)	**–**
Segment revenue	**1 205 944**	**5 376 280**	**6 450 274**	**15 873 355**	**927 953**	**(11 569 366)**	**18 264 440**
Profit/(loss) of the segment	**(104 328)**	**(3 477 076)**	**1 371 577**	**369 529**	**32 596**	**(6 379)**	**(1 814 081)**
Unallocated expenses	–	–	–	–	–	(87 135)	**(87 135)**
EBIT	**(104 328)**	**(3 477 076)**	**1 371 577**	**369 529**	**32 596**	**(93 514)**	**(1 901 216)**
Share in profit/(loss) of joint ventures	–	7 933	–	–	–	–	**7 933**
Net finance income (costs)	–	–	–	–	–	(294 488)	**(294 488)**
Profit/(loss) before income tax	**(104 328)**	**(3 469 143)**	**1 371 577**	**369 529**	**32 596**	**(388 002)**	**(2 187 771)**
Income tax expense	–	–	–	–	–	383 556	**383 556**
Net profit/(loss) for the year	**(104 328)**	**(3 469 143)**	**1 371 577**	**369 529**	**32 596**	**(4 446)**	**(1 804 215)**
Assets and liabilities							
Segment assets	1 657 407	10 370 286	15 974 893	2 709 132	478 618	–	**31 190 336**
Investments in joint ventures	–	418 127	–	–	–	–	**418 127**
Unallocated assets	–	–	–	–	–	462 970	**462 970**
Total assets	**1 657 407**	**10 788 413**	**15 974 893**	**2 709 132**	**478 618**	**462 970**	**32 071 433**
Segment liabilities	537 234	1 735 686	2 505 890	1 654 794	303 352	–	**6 736 956**
Unallocated liabilities	–	–	–	–	–	9 286 320	**9 286 320**
Total liabilities	**537 234**	**1 735 686**	**2 505 890**	**1 654 794**	**303 352**	**9 286 320**	**16 023 276**
EBIT	**(104 328)**	**(3 477 076)**	**1 371 577**	**369 529**	**32 596**	**(93 514)**	**(1 901 216)**
Depreciation/amortization	**(113 473)**	**(647 963)**	**(992 771)**	**(10 876)**	**(67 607)**	**–**	**(1 832 690)**
Impairment	**8**	**(3 583 864)**	**(7 781)**	**–**	**(117)**	**–**	**(3 591 754)**
EBITDA	**9 137**	**754 751**	**2 372 129**	**380 405**	**100 320**	**(93 514)**	**3 523 228**
Other segment information							
Capital expenditure*	211 458	1 934 229	1 924 886	4 604	100 293	–	**4 175 470**

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

10.2. Geographic areas of operations

The majority of the Group's business operations is carried out in Poland. In the years ended 31 December 2016 and 31 December 2015, export sales amounted to PLN 259 166 thousand and PLN 469 756 thousand, respectively.

The aforesaid value of export sales includes sales of emission allowances in the trading portfolio presented less cost of sales in the statement of comprehensive income as the total gain/loss on transactions from this portfolio. Gains/losses on derivative commodity instruments are not taken into account.

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 2016, the Group recognized and reversed impairment losses on property, plant and equipment as a result of impairment tests performed as at 31 December 2016 and 30 June 2016.

As at 31 December 2016, 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;
- a drop in the prices of certificates for energy produced from renewable sources;
- introduction of new RES regulations;
- the continued unfavorable market conditions in the coal power industry;
- an increase in the risk-free rate.

The tests conducted as at 31 December 2016 and 30 June 2016 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 CGU understood as a generation unit or a group of generation units;
- TAURON Ekoenergia Sp. z o.o. – where hydroelectric power stations and wind farms were individually tested for impairment;
- TAURON Ciepło Sp. z o.o. – where generation of heat and electricity was separated from transmission and distribution of heat (former thermal energy companies). Additional tests were carried out for individual generation units.

Key assumptions made for purposes of tests performed as at 31 December 2016:

- the adopted price path for power coal, other coal sizes and gaseous fuels. It is assumed that the price of power coal will increase by ca. 9% in real terms by 2026 and after 2026 insignificant changes in 2026 year prices (fixed) are anticipated;
- the adopted electricity wholesale price path for the years 2017–2026 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. A drop of ca. 5% is assumed by 2020 with a dynamic growth rate by 2026 (16% vs. 2020), an increase of 11% between 2026 and 2040 and 2040 year prices thereafter (fixed);
- estimated changes in the Polish market model aimed to introduce the capacity market or other incentive mechanisms for production capacity have been taken into account;
- emission limits for generating electricity specified in the regulation of the Council of Ministers, adjusted by capital expenditure incurred and the limits for heat generation compliant with the regulation of the Council of Ministers, adjusted by the level of operations, i.e. generation of heat;
- the adopted greenhouse gas emission allowance price path for the years 2017–2026 with the perspective by 2040. It is assumed that the market price will increase by ca. 70% by 2026, followed by a rise of ca. 16% between 2026 and 2040, with 2040 year price level thereafter (fixed);
- green, red and yellow energy production volumes depending on the production capacity, along with the price path for individual energy certificates. A drop of ca. 6% is assumed for renewable energy prices by 2020, followed by a rise by 2026 (13% vs. 2020), an increase of 13% between 2026 and 2040 and 2040 year prices thereafter (fixed);
- limited support periods for green energy have been assumed in accordance with the Act on Renewable Energy Sources (the "RES Act"), 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. At the same time, hydropower plants with installed capacity of more than 5 MW do not qualify for support;

- 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;
- regulated revenue generated by distribution companies, ensuring coverage of reasonable costs and a reasonable level of return on capital. The return on capital is conditional on the Regulatory Asset Value;
- 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 surrender energy certificates as well as an appropriate level of margin;
- sales volumes taking into account GDP growth and increased market competition;
- tariff revenue generated by heat companies, ensuring 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;
- the level of the weighted average cost of capital (WACC) during the projection period, as used in the calculations, ranges from 5.94% to 8.44% in nominal terms before tax.

Key assumptions made for purposes of tests performed as at 30 June 2016:

- the adopted price path for power coal, other coal sizes and gaseous fuels. It is assumed that the price of power coal will decrease by ca. 6% in real terms by 2025 and after 2025 insignificant changes in 2025 year prices (fixed) are anticipated;
- the adopted electricity wholesale price path for the years 2016–2025, 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. A drop of ca. 7% is assumed by 2020 with a dynamic growth rate by 2025 (13% vs. 2020), an increase of 18% between 2025 and 2040 and 2040 year prices thereafter (fixed);
- the adopted greenhouse gas emission allowance price path for the years 2016–2025. It is assumed that the market price will increase by ca. 50% by 2025, followed by a rise of ca. 20% between 2025 and 2040, with 2040 year price level thereafter (fixed);
- green, red and yellow energy production volumes depending on the production capacity, along with the price path for individual energy certificates. A drop of ca. 7% is assumed for renewable energy prices by 2020, followed by a rise by 2025 (11% vs. 2020), an increase of 22% between 2025 and 2040 and 2040 year prices thereafter (fixed);
- the level of the weighted average cost of capital (WACC) during the projection period, as used in the calculations, ranges from 6.34% to 9.63% in nominal terms before tax;
- other assumptions were the same as adopted for tests performed as at 31 December 2016.

In the year ended 31 December 2016, the Group recognized and reversed impairment losses on property, plant and equipment as a result of impairment tests performed:

- as at 31 December 2016: the impairment test revealed that an additional impairment loss of PLN 581 900 thousand should be recognized on a portion of the Generation segment assets. The test also identified the possibility to reverse an impairment loss in this segment in the amount of PLN 505 083 thousand.
- as at 30 June 2016: the impairment test revealed that an additional impairment loss of PLN 1 361 037 thousand should be recognized on a portion of the Generation segment assets. The test also showed that it would be reasonable to reverse an impairment loss in this segment in the amount of PLN 703 162 thousand.

The recoverable amount of this asset group corresponds to the value in use. The impairment losses were charged to the cost of sales.

The impairment loss and its reversal as a result of tests performed as at 31 December 2016 and 30 June 2016 concerned the following cash-generating units:

CGU	Company	Discount rate (before tax) assumed in tests as at: 31 December 2016	30 June 2016	31 December 2015	Recoverable amount As at 31 December 2016	Impairment loss recognized Year ended 31 December 2016	Impairment loss derecognized Year ended 31 December 2016
Elektrownia Jaworzno II	TAURON Wytwarzanie S.A.	7.78%	7.49%	7.69%	235 750	269 823	86 034
Elektrownia Jaworzno III					1 024 583	14 410	433 638
Elektrownia Łaziska					319 744	–	54 124
Elektrownia Łagisza					1 289 344	193 430	–
Elektrownia Siersza					157 356	232 253	156 571
Elektrownia Stalowa Wola					(99 426)	40 216	46 802
Capital projects in progress					–	19 328	–
ZW Bielsko Biała EC 1	TAURON Ciepło Sp. z o.o.	7.63%	7.17%	7.61%	615 489	–	209 433
ZW Bielsko Biała EC 2					(45 965)	7 061	–
ZW Tychy					499 172	382 719	221 643
Hydropower plants	TAURON Ekoenergia Sp. z o.o.	8.44%	8.25%	8.39%	611 273	42 310	–
FW Lipniki		6.71%	6.34%	8.90%	19 112	65 513	–
FW Wicko		6.97%	6.48%	8.17%	69 309	164 121	–
FW Marszewo		7.04%	6.49%	8.14%	228 352	464 839	–
Total CGU						**1 896 023**	**1 208 245**
Common assets	TAURON Wytwarzanie S.A.	7.78%	7.49%	7.69%	(19 511)	46 914	–
Total impairment losses						**1 942 937**	**1 208 245**

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, followed by changes in electricity prices, in hard coal prices and in the weighted average cost of capital. The measurement is also affected by changes in greenhouse gas emission allowances, though to a lesser extent. The estimated changes in impairment losses on Generation assets, considering also the effect of their reversal as at 31 December 2016 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, an additional net loss of ca. PLN 2 666 thousand would be recognized in the Group's profit/loss.

Parameter	Change	Net impact on impairment loss (i.e. reduced by derecognized amounts, in PLN million) Increase of impairment loss (net)	Decrease of impairment loss (net)
Change of electricity prices in the forecast period	+1%	–	237
	-1%	366	–
Change of WACC (net)	+0.1 p.p.	92	–
	-0.1 p.p.	–	44
Change of CO_2 emission allowances prices in the forecast period	+1%	41	–
	-1%	–	41
Change of coal prices in the forecast period	+1%	105	–
	-1%	–	85
No recognition of Capacity Market		2 666	–

11.2. Impairment of goodwill

The test was performed for the net assets increased by goodwill in each operating segment, except Generation, where the test was carried out at each company level. 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 2017 to 2026 (in tests performed on 30 June 2016 for the period from 2016 to 2025) and the estimated residual value. In tests performed on 30 June 2016 for the generation units the projection period covers the whole period of their operation. 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.

(in PLN '000)

The discount rate used for calculation reflects the weighted average cost of capital (WACC), taking into account the risk-free rate determined by reference to the yield on 10-year treasury bonds (3.63%) (in the tests carried out as at 30 June 2016 – 3.27%) 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 the level of 2.5% and it corresponds to the estimated long-term inflation rate.

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

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

Impairment test for the carrying amount of goodwill as at 31 December 2016

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 2016	31 December 2015
Mining	• The adopted price path of power coal and other coal sizes. The actual increase in the price of power coal assumed by 2026 approximates 9%, with slight fluctuations of 2026 prices thereafter (fixed); • The adopted retail price path of electricity based on the wholesale price of black energy including excise costs, cost of energy certificates surrender and a relevant markup; • Maintaining generation capacity of the existing non-current assets as a result of replacement investments.	6.95%	9.05%
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.	6.39%	7.50%

The impairment test performed as at 31 December 2016 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, WACC and greenhouse gas emission allowances as well as the prices of green certificates 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.

Impairment test for the carrying amount of goodwill as at 30 June 2016

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

(in PLN '000)

Goodwill in the segment (company)	Key assumptions	Discount rate (before tax) assumed in tests as at:	
		30 June 2016 (*unaudited*)	31 December 2015
Mining	• The adopted price path of power coal and other coal sizes. The actual decrease in the price of power coal assumed by 2025 approximates 6%, with slight fluctuations of 2025 prices thereafter (fixed); • The adopted retail price path of electricity based on the wholesale price of black energy including excise costs, cost of energy certificates surrender and a relevant markup; • Maintaining generation capacity of the existing non-current assets as a result of replacement investments.	9.57% – 9.63%	9.05%
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.	7.50%	7.50%
Generation (TAURON Ekoenergia Sp. z o.o.)	• Green energy production volumes depending on the production capacity, along with the price path for energy certificates. A drop of approx. 7% in prices of electricity from renewable sources has been assumed by 2020; a growth has been assumed by 2025 (11% in relation to 2020); a rise of ca. 22% is assumed for the years 2025–2040, with 2040 prices thereafter (fixed); • For green energy, limited support periods have been included, in accordance with the provisions of the Act on renewable energy sources determining new mechanisms of supporting generation of electricity from renewable sources. 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. At the same time, hydropower plants with installed capacity exceeding 5 MW have been excluded from the support; • Maintaining generation capacity of the existing non-current assets as a result of replacement investments.	8.25% (for hydropower plants) 6.34% – 8.92% (for windfarms)	8.39% (for hydropower plants) 8.14% – 8.90% (for windfarms)

The impairment test performed as at 30 June 2016 revealed impairment of the carrying amount of goodwill in the Generation segment (TAURON Ekoenergia Sp. z o.o.). As a result, the Group recognized an impairment loss on goodwill of PLN 51 903 thousand. The impairment loss was charged to cost of sales.

CGU	Company	Discount rate (before tax) assumed in tests as at:		Recoverable amount	Impairment loss recognized
		30 June 2016 (*unaudited*)	31 December 2015		
Generation	TAURON Ekoenergia Sp. z o.o.	8.25% (for hydropower plants) 6.34% – 8.92% (for windfarms)	8.39% (for hydropower plants) 8.14% – 8.90% (for windfarms)	1 225 935	51 903

The impairment loss was recognized as a result of a drop in the prices of green certificates as well as introduction of new RES regulations.

The sensitivity analyses for each CGU revealed that changes in electricity prices and in the weighted average cost of capital were the key factors having the most significant effect on the value in use of the tested assets.

(in PLN '000)

EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

12. Sales revenue

	Year ended 31 December 2016	Year ended 31 December 2015 (*restated figures*)
Sale of goods for resale, finished goods and materials without elimination of excise	**11 575 033**	**12 080 940**
Excise	(395 601)	(425 691)
Sale of goods for resale, finished goods and materials, of which:	**11 179 432**	**11 655 249**
Electricity	9 521 948	10 099 333
Heat energy	650 625	613 660
Energy certificates	127 791	272 896
Coal	467 962	439 608
Gas	230 466	117 867
Other goods for resale, finished goods and materials	180 640	111 885
Rendering of services, of which:	**6 409 430**	**6 552 945**
Distribution and trade services	6 051 410	6 184 958
Connection fees	102 657	124 866
Maintenance of road lighting	116 463	116 042
Other services	138 900	127 079
Other revenue	**57 627**	**56 246**
Total sales revenue	**17 646 489**	**18 264 440**

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

Additional assessment of the revenue from the sale of electricity and distribution services has been discussed in Note 9.26 Sales revenue.

As at 31 December 2016, additionally assessed revenue from sale of electricity and distribution services in the Sales segment totaled PLN 353 065 thousand and, when revered estimations from the prior year have been accounted for, the impact on the profit or loss for the period was PLN 104 592 thousand.

13. Cost of goods, products, materials and services sold (cost of sales)

13.1. Expenses by type

	Year ended 31 December 2016	Year ended 31 December 2015 (*restated figures*)
Costs by type		
Depreciation of property, plant and equipment and amortization of intangible assets	(1 668 726)	(1 832 690)
Impairment of property, plant and equipment and intangible assets	(867 109)	(3 598 926)
Materials and energy	(1 537 285)	(1 848 777)
Maitenance and repair services	(265 300)	(382 641)
Distribution services	(1 771 651)	(1 706 894)
Other external services	(759 687)	(674 265)
Cost of obligation to remit the emission allowances	(381 883)	(150 794)
Other taxes and charges	(667 415)	(619 698)
Employee benefits expense	(2 613 984)	(2 560 784)
Allowance for doubtful debts	(22 943)	(29 461)
Other	(106 892)	(130 155)
Total costs by type	**(10 662 875)**	**(13 535 085)**
Change in inventories, prepayments, accruals and deferred income	61 655	(164 328)
Cost of goods produced for internal purposes	471 286	610 506
Selling and distribution expenses	459 191	489 963
Administrative expenses	652 827	618 969
Cost of goods for resale and materials sold	(6 699 546)	(7 048 987)
Cost of sales	**(15 717 462)**	**(19 028 962)**

(in PLN '000)

13.2. Employee benefits expenses

	Year ended 31 December 2016	Year ended 31 December 2015
Wages and salaries	(2 036 168)	(1 952 987)
Social security costs	(399 157)	(380 096)
Jubilee bonuses	84 473	(19 367)
Social Fund	(57 881)	(56 215)
Post-employment benefit expenses, of which:	(85 478)	(31 863)
Provision for retirement, disability and similar benefits	5 368	(11 824)
Coal allowances and special electricity rates and charges	(13 665)	32 287
Social Benefits Fund	(9 754)	16 387
Contributions to employee retirement plans	(67 427)	(68 713)
Voluntary termination scheme	(20 866)	(46 172)
Other employee benefit expenses	(98 907)	(74 084)
Employee benefits expenses, of which:	**(2 613 984)**	**(2 560 784)**
Items included in cost of sales	(1 687 692)	(1 705 021)
Items included in selling and distribution expenses	(203 799)	(226 328)
Movement in stock of finished goods	(89 010)	(5 941)
Items included in administrative expenses	(403 571)	(376 309)
Items included in cost of goods produced for internal purposes	(229 912)	(247 185)

As at 31 December 2016, provisions for post-employment benefits and jubilee bonuses were remeasured. Past service costs were recognized within the Group's operating expenses in relation to:

- Jubilee bonuses – operating expenses were reduced by PLN 84 487 thousand, where PLN 37 027 thousand concerned changes in Collective Labor Agreements, while PLN 47 460 thousand concerned the change in the retirement age;
- post-employment benefit expenses – operating expenses were reduced by PLN 6 603 thousand, where PLN 61 236 thousand related to the reduction of provisions due to changes in Collective Labor Agreements, while PLN 54 633 thousand increased provisions due to the change in the retirement age.

The change in provisions for post-employment benefits and for jubilee bonuses has been discussed in more detail in Note 34.1 to these consolidated financial statements.

13.3. Depreciation and amortization charges and impairment losses

	Year ended 31 December 2016	Year ended 31 December 2015
Items included in cost of sales:	**(2 409 461)**	**(5 337 505)**
Depreciation of property, plant and equipment	(1 532 717)	(1 703 932)
Impairment of property, plant and equipment	(757 974)	(3 437 907)
Amortization of intangible assets	(43 487)	(36 909)
Impairment of intangible assets	(22 215)	(1 749)
Impairment of goodwill	(51 903)	(154 998)
Other	(1 165)	(2 010)
Items included in selling and distribution expenses:	**(33 318)**	**(33 291)**
Depreciation of property, plant and equipment	(17 639)	(16 999)
Amortization of intangible assets	(15 679)	(16 292)
Items included in administrative expenses:	**(75 640)**	**(42 354)**
Depreciation of property, plant and equipment	(27 868)	(25 286)
Impairment of property, plant and equipment	(33 245)	(2 262)
Amortization of intangible assets	(14 308)	(14 806)
Impairment of intangible assets	(219)	–
Items included in cost of goods produced for internal purposes:	**(17 416)**	**(18 466)**
Depreciation of property, plant and equipment	(16 751)	(18 117)
Impairment of property, plant and equipment	(388)	–
Amortization of intangible assets	(277)	(349)
Total depreciation/amortization expense and impairment, of which:	**(2 535 835)**	**(5 431 616)**
Depreciation and amortization	(1 668 726)	(1 832 690)
Impairment	(867 109)	(3 598 926)

(in PLN '000)

In the year ended 31 December 2016, the Group recognized impairment losses on property, plant and equipment as well as goodwill, 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 2016 and 30 June 2016. The total effect on the Group's gross profit/loss for 2016 was PLN 786 595 thousand (surplus 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 2016, the Group companies recognized and derecognized impairment losses on individual assets. The related total charges to operating expenses of the Group amounted to PLN 80 514 thousand. The key items include impairment losses recognized by a Generation segment company on property, plant and equipment in relation to a subsidy obtained under contracts on co-funding of RES units construction of PLN 68 875 thousand, and intangible assets regarding land used for waste storage purposes of PLN 22 734 thousand.

Depreciation and amortization rates

A review of the estimated useful lives of fixed assets and intangible assets, conducted in 2016, 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 2016	Year ended 31 December 2015
Mining	(13 286)	(1 744)
Generation	520	5 567
Distribution	(25 900)	(10 000)

A review of the estimated useful lives in the remaining segments did not have a considerable effect on the amortization and depreciation expense.

14. Other operating revenue and expenses

	Year ended 31 December 2016	Year ended 31 December 2015
Penalties, fines, compensations received or receivable	48 256	28 043
Surplus of (recognition)/reversal of actuarial provisions for the existing pensioners and disability pensioners	58 528	45 557
Surplus of other provisions (recognized)/derecognized	(115 733)	(12 616)
Subsidies/grants and revenue representing the equivalent of amortization/depreciation charges on subsidies/grants to fixed assets or fixed assets received free of charge	38 434	39 404
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	(116)	(14 973)
Write-off for abandoned investments and production as well as liquidated materials	(2 821)	(81 540)
Costs of court proceedings, fines and damages	(24 675)	(12 322)
Costs of patricipation in Polish National Foundation	(32 500)	–
Other operating income	22 208	43 878
Other operating expenses	(36 752)	(63 193)
Total other operating income and expenses	**(15 487)**	**(27 762)**

In the year ended 31 December 2016, following the modification of their Collective Labor Agreements, some Group companies reversed their provisions for post-employment benefits for their existing pensioners. Consequently, PLN 58 528 thousand was recognized within other operating revenue.

In the year ended 31 December 2016 the amount of provisions recognized in the Group exceeded the amount of unrecognized ones by PLN 115 733 thousand. The basis for provisions which were recognized or remeasured and had a material effect on the profit/loss of the Group have been presented in Note 37 to these consolidated financial statements.

A decrease in the cost of writing off discontinued investments was driven by a write-off of capitalized costs of work relating to drilling drifts and reinforcing walls of PLN 78 610 thousand in the comparative period, as they were no longer suitable for economic use.

(in PLN '000)

15. Finance income and costs

	Year ended 31 December 2016	Year ended 31 December 2015 (*restated figures*)
Income and costs from financial instruments, of which:	**(252 206)**	**(242 535)**
Interest income	35 314	60 385
Interest costs	(259 564)	(279 673)
Commission relating to borrowings and debt securities	(18 767)	(12 514)
Gain/loss on derivative instruments	14 138	(7 089)
Foreign exchange gains/losses	(30 261)	524
Dividend income	5 728	4 684
Other	1 206	(8 852)
Other finance income and costs, of which:	**(100 495)**	**(51 953)**
Interest on employee benefits	(50 101)	(44 491)
Interest on discount of other provisions	(19 106)	(5 272)
Other	(31 288)	(2 190)
Total finance income and costs, including recognized in the statement of comprehensive income:	**(352 701)**	**(294 488)**
Interest expense on debt	(259 564)	(279 673)
Other finance income and costs	(93 137)	(14 815)

In the year ended 31 December 2016, exchange losses exceeded exchange gains by PLN 30 261 thousand, which was mainly driven by exchange losses on an intra-group loan in the euro.

16. Income tax

16.1. Tax expense in the statement of comprehensive income

	Year ended 31 December 2016	Year ended 31 December 2015
Current income tax	**(229 134)**	**(206 255)**
Current income tax expense	(223 825)	(233 398)
Adjustments to current income tax from previous years	(5 309)	27 143
Deferred tax	**90 410**	**589 811**
Income tax expense in profit/(loss)	**(138 724)**	**383 556**
Income tax expense relating to other comprehensive income	**(63 052)**	**(28 587)**

16.2. Reconciliation of the effective tax rate

	Year ended 31 December 2016	Year ended 31 December 2015
Profit/(loss) before taxation	**508 861**	**(2 187 771)**
Tax at Poland's statutory tax rate of 19%	**(96 684)**	**415 676**
Adjustments to income tax from previous years	(5 309)	27 143
Tax effects of the following items:	(46 169)	(62 376)
Recognition of non-deductible provisions and write-downs/allowances	(25 072)	(9 183)
National Disabled Persons Rehabilitation Fund (PFRON)	(4 857)	(4 551)
Permanent differences on costs related to tangible assets	(27 426)	(5 135)
Impairment of goodwill	(9 862)	(29 450)
Settlement of a tax loss which was not recognized as a tax asset	16 595	–
Other tax non-deductible costs	(16 658)	(19 692)
Share in profit/loss of joint ventures	11 408	1 507
Other income not included in taxable base	9 703	4 128
Other	9 438	3 113
Tax at the effective rate of 27.3% (2015 – 17.5%)	**(138 724)**	**383 556**
Income tax (expense) in profit/(loss)	(138 724)	383 556

(in PLN '000)

16.3. Deferred income tax

	As at 31 December 2016	As at 31 December 2015
difference between tax base and carrying amount of fixed and intangible assets	1 511 102	1 490 408
difference between tax base and carrying amount of financial assets	45 981	29 609
different timing of recognition of sales revenue for tax purposes	49 299	69 064
difference between tax base and carrying amount of energy certificates	15 766	48 817
other	44 156	39 889
Deferred tax liabilities	**1 666 304**	**1 677 787**
provisions	638 914	685 405
difference between tax base and carrying amount of fixed and intangible assets	143 403	6 359
power infrastructure received free of charge and received connection fees	51 811	57 071
difference between tax base and carrying amount of financial assets and financial liabilities	50 387	49 471
valuation of hedging instruments	–	18 139
different timing of recognition of cost of sales for tax purposes	39 940	58 333
tax losses	12 758	12 758
difference between tax base and carrying amount of emission allowances	–	26 985
other	19 905	22 274
Deferred tax assets	**957 118**	**936 795**
After setting off balances at the level of individual Group companies, deferred tax for the Group is presented as:		
Deferred tax asset	**50 382**	**54 184**
Deferred tax liability	**(759 568)**	**(795 176)**

As at 31 December 2016 and 31 December 2015, the deferred tax asset was set off against 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.

Based on the forecasts prepared for the TCG, according to which taxable income will be earned in 2017 and 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.

Change in deferred tax liability

	Year ended 31 December 2016	Year ended 31 December 2015
Opening balance	**1 677 787**	**2 187 951**
Change in the balance:		
corresponding to profit/(loss)	(27 405)	(529 019)
reclassification from disposal group classified as held for sale	–	18 910
acquisition of ZCP Brzeszcze	15 239	–
other changes	683	(55)
Closing balance	**1 666 304**	**1 677 787**

Change in deferred tax asset

	Year ended 31 December 2016	Year ended 31 December 2015
Opening balance	**936 795**	**892 902**
Change in the balance:		
corresponding to profit/(loss)	63 005	60 792
corresponding to other comprehensive income	(63 052)	(28 587)
reclassification from disposal group classified as held for sale	–	11 585
acquisition of ZCP Brzeszcze	18 366	–
other changes	2 004	103
Closing balance	**957 118**	**936 795**

(in PLN '000)

17. Earnings (loss) per share

Earnings (loss) per share (in PLN)	Year ended 31 December 2016	Year ended 31 December 2015
Basic and diluted, for profit (loss) for the year attributable to equity holders of the Parent	0.21	(1.03)

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

	Year ended 31 December 2016	Year ended 31 December 2015
Net profit (loss) for the year attributable to equity holders of the Parent	367 468	(1 807 317)
Number of ordinary shares	1 752 549 394	1 752 549 394

(in PLN '000)

EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION

18. Property, plant and equipment

For the 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, disposal	(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, disposal	–	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 PLN '000)

For the year ended 31 December 2015

	Land	Buildings, premises and civil engineering structures	Plant and machinery	Other	Assets under construction	Property, plant and equipment, total
COST						
Opening balance	**117 142**	**18 195 456**	**14 819 091**	**808 607**	**1 364 263**	**35 304 559**
Direct purchase	–	–	228	401	3 808 063	**3 808 692**
Borrowing costs	–	–	–	–	68 656	**68 656**
Transfer of assets under construction	3 608	1 320 193	1 400 437	102 850	(2 827 088)	**–**
Sale	(1 181)	(5 172)	(8 327)	(17 875)	(586)	**(33 141)**
Liquidation	–	(64 089)	(174 717)	(9 238)	(4)	**(248 048)**
Received free of charge	–	19 830	403	3	–	**20 236**
Transfers to/from assets held for sale	(7)	470 453	793 329	(8 536)	21 192	**1 276 431**
Overhaul expenses	–	–	–	–	139 078	**139 078**
Items generated internally	–	–	–	–	41 899	**41 899**
Cost of disassembly of wind farms and decommissioning of mines	–	(10 039)	(660)	–	–	**(10 699)**
Other movements	(26)	1 767	80 637	(72 202)	(15 493)	**(5 317)**
Foreign exchange differences from translation of foreign entities	–	–	7	10	–	**17**
Closing balance	**119 536**	**19 928 399**	**16 910 428**	**804 020**	**2 599 980**	**40 362 363**
ACCUMULATED DEPRECIATION						
Opening balance	**(458)**	**(5 049 663)**	**(4 957 467)**	**(440 706)**	**(5 323)**	**(10 453 617)**
Depreciation for the period	–	(839 414)	(837 677)	(87 243)	–	**(1 764 334)**
Increase of impairment	(81)	(826 976)	(2 608 593)	(5 036)	(8 421)	**(3 449 107)**
Decrease of impairment	51	8 954	143	770	16	**9 934**
Sale	–	1 890	7 290	16 500	–	**25 680**
Liquidation	–	52 057	169 981	8 821	–	**230 859**
Transfers to/from assets held for sale	22	(39 254)	(43 328)	4 610	–	**(77 950)**
Other movements	–	(250)	(35 310)	34 557	–	**(1 003)**
Foreign exchange differences from translation of foreign entities	–	–	(4)	(4)	–	**(8)**
Closing balance	**(466)**	**(6 692 656)**	**(8 304 965)**	**(467 731)**	**(13 728)**	**(15 479 546)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**116 684**	**13 145 793**	**9 861 624**	**367 901**	**1 358 940**	**24 850 942**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**119 070**	**13 235 743**	**8 605 463**	**336 289**	**2 586 252**	**24 882 817**
of which operating segments:						
Mining	**1 189**	**582 131**	**596 130**	**14 595**	**161 732**	**1 355 777**
Generation	**41 638**	**2 514 623**	**3 977 254**	**38 806**	**1 662 593**	**8 234 914**
Distribution	**59 414**	**10 037 164**	**3 892 698**	**260 861**	**754 370**	**15 004 507**
Other segments and other operations	**16 829**	**101 825**	**139 381**	**22 027**	**7 557**	**287 619**

Property, plant and equipment used based on finance leases	As at 31 December 2016	As at 31 December 2015
Buildings	34 117	33 962
Plant and machinery	17 226	3 715
Motor vehicles	406	870

In the year ended 31 December 2016, the Group purchased property, plant and equipment of PLN 3 590 348 thousand, including capitalized borrowing costs. The major purchases were related to investments in the following operating segments:

Purchase of property, plant and equipment by segment	Year ended 31 December 2016	Year ended 31 December 2015
Distribution	1 717 236	1 858 807
Generation	1 560 458	1 750 548
Mining	282 420	210 574

The average capitalization rate of borrowing costs in the year ended 31 December 2016 was 4.10% vs. 4.33% in the year ended 31 December 2015.

The key investment projects carried out by the Group in the 2016 financial year have been discussed in Section 1.5.2. of the Management Board's report on the activities of the TAURON Polska Energia S.A. Capital Group for the 2016 financial year.

(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 2016				Year ended 31 December 2015			
	Generation	Distribution	Other	Total	Generation	Distribution	Other	Total
Increase of impairment	(1 487 766)	(5 853)	–	**(1 493 619)**	(3 430 917)	(18 173)	(17)	**(3 449 107)**
Decrease of impairrment	689 181	14 770	–	**703 951**	609	9 322	3	**9 934**
Total impact on the profit (loss) for the period	**(798 585)**	**8 917**	**–**	**(789 668)**	**(3 430 308)**	**(8 851)**	**(14)**	**(3 439 173)**

19. Goodwill

	Year ended 31 December 2016	Year ended 31 December 2015
Opening balance	**92 059**	**195 154**
Impairment loss	(51 903)	(154 998)
Reclassification from disposal group classified as held for sale	–	51 903
Closing balance, of which operating segments:	**40 156**	**92 059**
Mining	13 973	13 973
Distribution	25 602	25 602
Generation	581	52 484

In the year ended 31 December 2016, the Group recognized an impairment loss on the carrying amount of goodwill in the Generation segment, totaling PLN 51 903 thousand. The impairment loss was recognized following the performance of impairment tests as at 30 June 2016. The tests performed as at 31 December 2016 did not identify a necessity to recognize an impairment loss on the carrying amount of goodwill. The performed tests have been described in Note 11.2 hereof.

20. Energy certificates and gas emission allowances

20.1. Long-term energy certificates and gas emission allowances

For the 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**

For the year ended 31 December 2015

	Energy certificates	Greenhouse gas emission allowances	Total
Opening balance	**207 397**	**265 103**	**472 500**
Direct purchase	85 240	129 548	**214 788**
Reclassification	(59 664)	(116 784)	**(176 448)**
Closing balance	**232 973**	**277 867**	**510 840**

20.2. Short-term energy certificates and gas emission allowances

For the 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	**602 104**
Generated internally	102 149	–	**102 149**
Cancellation	(709 538)	(325 230)	**(1 034 768)**
Reclassification	227 607	277 867	**505 475**
Closing balance	**556 501**	**423 847**	**980 348**

(in PLN '000)

For the year ended 31 December 2015

	Energy certificates	Greenhouse gas emission allowances	Total
Opening balance	**724 918**	**8 130**	**733 048**
Direct purchase	411 854	33 643	**445 497**
Generated internally	235 484	–	**235 484**
Cancellation	(781 711)	(5 941)	**(787 652)**
Reclassification	61 760	117 251	**179 011**
Closing balance	**652 305**	**153 083**	**805 388**

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

CO_2 emissions allowances	Year ended 31 December 2016	Year ended 31 December 2015
Allowances recorded at the beginning of the financial year	**23 737 448**	**26 878 236**
Allowances surrendered:		
in the installations of TAURON Wytwarzanie S.A. (previous year's emissions)	(14 736 415)	(12 508 585)
in the installations of TAURON Ciepło Sp. z o.o. (previous year's emissions)	(1 562 047)	(1 571 376)
in the installations of TAURON Wytwarzanie S.A. (current year's emissions)	(7 501 634)	–
Allocation of free-of-charge allowances	3 627 599	6 985 193
Allowances purchased on the secondary market	24 673 500	8 745 500
Allowances sold on the secondary market	(8 755 500)	(3 698 500)
Other changes – transferred to TAMEH	–	(1 093 020)
Allowances recorded at the end of the financial year, of which:	**19 482 951**	**23 737 448**
Allowances intended for surrender for a given year:	(7 395 649)	(14 604 360)
in the installations of TAURON Wytwarzanie S.A.	(5 863 776)	(13 040 086)
in the installations of TAURON Ciepło Sp. z o.o.	(1 531 873)	(1 564 274)

The third phase of the EU Emissions Trading System (EU ETS) started on 1 January 2013. For that phase, one EU-wide emission limit has been imposed, which will gradually be reduced by 1.74% a year by 2020. In accordance with Directive 2009/29/EC of the European Parliament and of the Council of 23 April 2009 (the "Directive") amending Directive 2003/87/EC so as to improve and extend the greenhouse gas emission allowance trading scheme of the Community, auctioning has become the key method of obtaining EU emission allowances. It is expected that during the third phase each EU member state will auction over 40% of allowances awarded in 2013–2020. The remaining allowances are allocated free of charge to: energy-intensive sectors (exposed to the risk of carbon leakage), other sectors (in line with the strategy to gradually eliminate free allocation) – pursuant to Article 10a of the Directive, and electric power sectors in selected member states, including Poland, qualifying for derogation under Article 10c ("derogation allowances"). Derogation allowances have been awarded for the years 2013–2020 based on costs of investments, which are a condition for obtaining allowances.

In 2016, the TAURON Group companies obtained emission allowances free of charge under Article 10a of the Directive in the following quantity: 585 344 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 in 2016) and 3 042 255 EUA for electricity generation (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 2016 – allocation for 2015).

In the financial and factual reports filed by the TAURON Group in 2016, which concerned investment task performance covered by National Investment Plan for the settlement period from 1 July 2015 to 30 June 2016, the value of free-of-charge allowances related to modernization of the electricity generation process for 2016, i.e. 1 680 838 EUA were balanced. The Group expects that the allowances will have been obtained by the end of April 2017.

(in PLN '000)

21. Other intangible assets

For the year ended 31 December 2016

	Development expenses	Perpetual usufruct	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, disposal	–	(2 373)	(4)	–	(55)	**(2 432)**
Liquidation	(256)	(65)	(3 996)	(89)	–	**(4 406)**
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, disposal	–	–	3	–	–	**3**
Liquidation	256	–	3 917	81	–	**4 254**
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**

For the year ended 31 December 2015

	Development expenses	Perpetual usufruct	Software, concessions, patents, licenses and similar items	Other intangible assets	Intangible assets not made available for use	Intangible assets, total
COST						
Opening balance	**4 670**	**789 670**	**475 291**	**153 770**	**53 436**	**1 476 837**
Direct purchase	–	–	80	–	117 065	**117 145**
Transfer of intangible assets not made available for use	–	1 123	89 290	33 451	(123 864)	**–**
Sale	–	(2 132)	(8 072)	–	–	**(10 204)**
Liquidation	(256)	(1)	(5 925)	(433)	–	**(6 615)**
Other movements	1 276	(2 156)	200	1 216	5 248	**5 784**
Foreign exchange differences from translation of foreign entities	–	–	28	–	–	**28**
Closing balance	**5 690**	**786 504**	**550 892**	**188 004**	**51 885**	**1 582 975**
ACCUMULATED AMORTIZATION						
Opening balance	**(3 822)**	**(15 297)**	**(289 949)**	**(35 635)**	**–**	**(344 703)**
Amortization for the period	(474)	–	(53 959)	(13 922)	–	**(68 355)**
Increase of impairment	(853)	(383)	(2 845)	(259)	–	**(4 340)**
Decrease of impairment	–	2 616	–	–	–	**2 616**
Sale	–	–	8 072	–	–	**8 072**
Liquidation	256	–	5 916	430	–	**6 602**
Other movements	–	–	(75)	(5)	–	**(80)**
Foreign exchange differences from translation of foreign entities	–	–	(22)	–	–	**(22)**
Closing balance	**(4 893)**	**(13 064)**	**(332 862)**	**(49 391)**	**–**	**(400 210)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**848**	**774 373**	**185 342**	**118 135**	**53 436**	**1 132 134**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**797**	**773 440**	**218 030**	**138 613**	**51 885**	**1 182 765**

(in PLN '000)

In the year ended 31 December 2016 an impairment loss on perpetual usufruct of land of PLN 22 734 thousand was recognized relating to land used for storage of waste coming from power generation in Jaworzno II and Jaworzno III Power Plants.

22. Shares in joint ventures

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

	Elektrociepłownia Stalowa Wola S.A.	Elektrownia Blachownia Nowa Sp. z o.o.	TAMEH HOLDING Sp. z o.o.*	As at 31 December 2015
Non-current assets	1 085 917	–	1 295 743	**2 381 660**
Current assets, including:	12 387	37 008	341 716	**391 111**
cash and cash equivalents	*91*	*36 943*	*14 880*	***51 914***
Non-current liabilities (-) including:	(965 514)	–	(378 507)	**(1 344 021)**
debt	*(963 766)*	–	*(295 503)*	***(1 259 269)***
Current liabilities (-) including:	(125 610)	(85)	(377 432)	**(503 127)**
debt	*(40 149)*	–	*(2 134)*	***(42 283)***
Total net assets	7 180	36 923	881 520	**925 623**
Share in net assets	3 590	18 461	440 760	**462 811**
Investment in joint ventures	**–**	**18 461**	**399 666**	**418 127**
Share in revenue of joint ventures	18	490	545 175	**545 683**
Share in profit/(loss) of joint ventures	**(1 474)**	**(13 644)**	**23 051**	**7 933**
Share in other comprehensive income of joint ventures	**–**	**–**	**(387)**	**(387)**

** 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 in Stalowa Wola fueled with natural gas, with the gross electrical capacity of 400 MWe and the net thermal capacity 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, which has been discussed in more detail in Note 35 to these consolidated financial statements.

The agreement reflects the will of the Company and PGNIG S.A. to continue the construction of the gas and steam unit. According to the Management Board of the Company, the aforesaid documents enable completion of the investment in 2019 (preliminary estimate).

TAURON Polska Energia S.A. holds 50% indirect interest in the issued capital of this 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 due to loans granted to Elektrociepłownia Stalowa Wola S.A. in the amount of PLN 256 067 thousand, which has been discussed in more detail in Note 23, as well as provisions for onerous commercial contracts in the amount of PLN 198 844 thousand, which have been discussed in Note 35.3.

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 named Elektrownia Blachownia Nowa Sp. z o.o., with its registered address in Kędzierzyn Koźle. 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.

TAURON Polska Energia S.A. holds 50% indirect interest in the issued capital of this company and in its governing body through TAURON Wytwarzanie S.A.

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., which denotes expiration of all contractual obligations and discontinuation of all works specified in the agreement. KGHM Polska Miedź S.A. and TAURON Wytwarzanie S.A. unanimously decided to commence the liquidation of the company, in line with its articles of association and laws of general application. 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. As Elektrownia Blachownia Nowa Sp. z o.o. in liquidation holds current assets which may be subject to distribution among the partners in the joint venture to a considerable extent, the Group does not recognize any additional impairment losses on its interest in the company.

TAMEH HOLDING Sp. z o.o. and subsidiaries

In 2014, the TAURON Group entered into an agreement with the ArcelorMittal Group. The shareholders agreement states that TAMEH HOLDING Sp. z o.o. will carry out investment and operational projects related to the industrial power sector. The agreement was concluded for a term of 15 years, which may be further 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 2016, the General Shareholders' Meeting of TAMEH HOLDING Sp. z o.o. decided to allocate PLN 48 000 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 24 000 thousand.

23. Loans granted to joint ventures

Loans granted to the joint venture Elektrociepłownia Stalowa Wola S.A. as at 31 December 2016 and 31 December 2015:

(in PLN '000)

	Agreement date	Contractual loan amount	As at 31 December 2016		As at 31 December 2015		Maturity date	Purpose
			Principal	Interest	Principal	Interest		
Subordinated loan	20 June 2012	177 000	177 000	36 381	177 000	28 922	31.12.2032	Project performance: the borrower to obtain external funding
Loan for repayment of debt	14 December 2015	15 850	15 850	699	15 850	31	31.12.2027	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 December 2016	15 300	11 000	21	–	–		
Other loans	25 November 2015	2 600	2 600	117	2 100	6	30.06.2017	Financing of current operations
	22 January 2016	5 500	5 500	214	–	–		
	22 April 2016	1 200	600	17	–	–		
	27 May 2016	3 100	3 100	65	–	–		
	31 August 2016	3 800	2 875	28	–	–		
Total loans			**218 525**	**37 542**	**194 950**	**28 959**		
Non-current			203 850	37 101	192 850	28 953		
Current			14 675	441	2 100	6		

In the year ended 31 December 2016, the interest income on loans granted amounted to PLN 8 583 thousand.

24. Other financial assets

	As at 31 December 2016	As at 31 December 2015
Shares	127 698	136 488
Deposits	38 472	39 724
Derivative instruments	56 417	5 684
Investment fund units	27 761	2 405
Loans granted	15 166	2 108
Bid bonds, deposits and collateral transferred	41 818	54 106
Other	14 561	5 034
Total	**321 893**	**245 549**
Non-current	227 140	211 215
Current	94 753	34 334

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 32 113 thousand;
- PGE EJ 1 Sp. z o.o., in the amount of PLN 23 046 thousand;
- Energetyka Cieszyńska Sp. z o.o., in the amount of PLN 15 063 thousand.

In the year ended 31 December 2016, the Parent acquired units in investment funds in the total amount of PLN 25 000 thousand. As at 31 December 2016, the carrying amount of these units measured at fair value was PLN 25 316 thousand.

Deposits constitute financial assets of Mine Decommissioning Fund.

25. Other non-financial assets

25.1. Other non-current non-financial assets

	As at 31 December 2016	As at 31 December 2015
Prepayments for assets under construction and intangible assets including:	274 301	358 673
related to project realization: Construction of 910 MW Power Unit in Jaworzono III Power Plant	*271 667*	*337 531*
Costs of preparing production in hard coal mines	132 862	159 159
Other prepayments	15 237	32 543
Total	**422 400**	**550 375**

(in PLN '000)

25.2. Other current non-financial assets

	As at 31 December 2016	As at 31 December 2015
Costs settled over time, including:	**78 457**	**104 251**
Costs of preparing production in hard coal mines	36 175	33 411
Property and tort insurance	10 922	15 888
IT, telecom and postal services	17 994	26 367
Other prepayments	13 366	28 585
Other current non-financial assets, including:	**106 551**	**128 808**
Advance payments for deliveries	103 601	120 342
Surplus of Social Benefit Fund assets over its liabilities	338	3 984
Other current assets	2 612	4 482
Total	**185 008**	**233 059**

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. An analysis of the fund is presented in the following table.

	As at 31 December 2016	As at 31 December 2015
Loans granted to employees	30 671	31 087
Cash	17 093	20 144
Other Fund assets and liabilities	2 822	(382)
Social Fund liabilities	(50 248)	(46 865)
Net balance	**338**	**3 984**
Transfers made to the Social Fund during the period	(62 180)	(60 388)

26. Inventories

	As at 31 December 2016	As at 31 December 2015
Historical cost		
Coal, of which:	320 201	324 635
Raw materials	*98 759*	*163 644*
Semi-finished goods and work-in-progress	*216 831*	*154 555*
Energy certificates	783	1 319
Emission allowances	45 912	3 424
Other inventories	115 591	114 037
Total	**482 487**	**443 415**
Write-downs to net realisable value / Revaluation		
Emission allowances	13 226	–
Other inventories	(9 593)	(10 136)
Total	**3 633**	**(10 136)**
Net realisable value / Fair value		
Coal, of which:	320 201	324 635
Raw materials	*98 759*	*163 644*
Semi-finished goods and work-in-progress	*216 831*	*154 555*
Energy certificates	783	1 319
Emission allowances	59 138	3 424
Other inventories	105 998	103 901
Total	**486 120**	**433 279**

(in PLN '000)

Movement in write-downs to net realizable value / Revaluation

	Year ended 31 December 2016	Year ended 31 December 2015
Opening balance	**(10 136)**	**(21 088)**
Recognition	(5 417)	(3 220)
Reversal	2 682	10 392
Utilization	3 278	3 780
Fair value measurement of emission allowances	13 226	–
Closing balance	**3 633**	**(10 136)**

The inventory of emission allowances purchased for resale and generation of profit in the short term due to volatility of market prices is measured at fair value as at the end of the reporting period. The Group recognized a gain on measurement of PLN 13 226 thousand as at 31 December 2016 following an increase in the prices of emission allowances. The measurement the change of the allowances should be analyzed jointly with the measurement change of forward contracts of allowances.

27. Receivables from buyers

Current receivables from buyers as at 31 December 2016 and 31 December 2015 have been presented in the table below.

	As at 31 December 2016	As at 31 December 2015
Value of items before allowance/write-down		
Receivables from clients	1 527 921	1 581 863
Receivables from clients – additional assessment of revenue from sales of electricity and distribution services	425 705	298 805
Receivables claimed at court	146 086	227 739
Total	**2 099 712**	**2 108 407**
Allowance/write-down		
Receivables from clients	(84 036)	(74 828)
Receivables claimed at court	(121 611)	(203 546)
Total	**(205 647)**	**(278 374)**
Value of item net of allowance (carrying amount)		
Receivables from clients	1 443 885	1 507 035
Receivables from clients – additional assessment of revenue from sales of electricity and distribution services	425 705	298 805
Receivables claimed at court	24 475	24 193
Total	**1 894 065**	**1 830 033**

Information on allowances/write-downs on receivables from buyers and other financial receivables has been presented in Note 46.1.1 to these consolidated financial statements.

28. Receivables due to taxes and charges

	As at 31 December 2016	As at 31 December 2015
Corporate Income Tax receivables	83 468	909
VAT receivables	154 181	205 713
Excise duty receivables	24 205	20 314
Other	2 000	1 409
Total	**263 854**	**228 345**

As at 31 December 2016, the Group had the following income tax assets and liabilities:

- income tax receivables of PLN 83 468 thousand, where PLN 83 153 thousand relates to settlements of the Tax Capital Group;
- income tax liability of PLN 2 371 thousand not included in the settlements of the Tax Capital Group.

Tax Capital Group

A Tax Capital Group ("TCG") agreement for the years 2015–2017 was concluded on 22 September 2014. The Tax Capital Group was registered by the Head of the First Śląski Tax Office in Sosnowiec under a tax identification number

(in PLN '000)

NIP 2050004308 pursuant to a decision of 20 November 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.

In the year ended 31 December 2016, the income tax charge of the Tax Capital Group was PLN 217 201 thousand. At the same time, the Tax Capital Group made advance payments relating to income tax of PLN 300 053 thousand and reported receivables arising from tax overpaid by a subsidiary before joining the Tax Capital Group in the amount of PLN 301 thousand.

29. Cash and cash equivalents

	As at 31 December 2016	As at 31 December 2015
Cash at bank and in hand	368 274	353 428
Short-term deposits (up to 3 months)	16 450	10 722
Other	157	762
Total cash and cash equivalents presented in the statement of financial position, of which:	**384 881**	**364 912**
restricted cash	144 404	206 254
Bank overdraft	(15 156)	(10 206)
Cash pool	(16 095)	(29 377)
Foreign exchange	1 103	2 386
Total cash and cash equivalents presented in the statement of cash flows	**354 733**	**327 715**

The difference between the balance of cash presented in the statement of financial position and the one in the statement of cash flows results from overdrafts, cash pool loans granted by entities not subject to consolidation due to the overall immateriality and exchange gains and losses on measurement of cash on foreign currency accounts.

As at 31 December 2016, the balance of restricted cash included mainly cash on the accounts for bid bonds of PLN 79 227 thousand and cash on the accounts used for the settlement of electricity and emission allowances traded on the Polish Power Exchange, i.e. Towarowa Giełda Energii S.A., of PLN 49 000 thousand.

30. Issued capital and other capitals

30.1. Issued capital

Issued capital as at 31 December 2016

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 2016, the value of issued capital, the number of shares and the nominal value of shares had not changed as compared to 31 December 2015.

Shareholding structure as at 31 December 2016 (*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**	**100.00%**	**100.00%**

(in PLN '000)

To the best of the Company's knowledge, the shareholding structure as at 31 December 2016 had not changed as compared to 31 December 2015.

30.2. Shareholders' 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 2016 financial year.

30.3. Reserve capital

On 8 June 2016, the Ordinary General Shareholders' Meeting adopted a resolution to offset the net loss for the 2015 financial year, totaling PLN 3 453 908 thousand, against the reserve capital.

30.4. Retained earnings and accumulated losses and restrictions on dividend payment

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 2016 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 loss for the year 2016 in the amount of PLN 166 253 thousand to be covered from the Company's reserve capital.

30.5. Revaluation reserve from valuation of hedging instruments

	Year ended 31 December 2016	Year ended 31 December 2015
Opening balance	**(73 414)**	**(143 019)**
Remeasurement of hedging instruments	132 108	85 466
Remeasurement of hedging instruments charged to profit or loss	(4 856)	466
Deferred income tax	(24 178)	(16 327)
Closing balance	**29 660**	**(73 414)**

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 45.3 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 2016, the Company recognized PLN 29 660 thousand of revaluation reserve from valuation of hedging instruments. It represents receivables arising from valuation of interest rate swaps as at the end of the reporting period, totaling PLN 36 641 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 profit/loss for the period was charged with PLN 80 658 thousand, where PLN 85 514 thousand was the amount paid in respect of hedges used in relation to closed interest periods and PLN (4 856) thousand resulted from a change in valuation of instruments related to interest on bonds accrued as at the end of the reporting period. The aforementioned costs of IRS hedging transactions adjusted finance costs arising from interest on bonds issued in the statement of comprehensive income.

(in PLN '000)

30.6. Non-controlling interest

	Year ended 31 December 2016	Year ended 31 December 2015
At the beginning of the period	**29 829**	**30 116**
Dividends for non-controlling interests	(3 043)	(2 787)
Share in actuarial gains/(losses) related to provisions for post-employment benefits	272	60
Acquisition of non-controlling interests by the Group and mandatory squeeze-out	325	(662)
Share in subsidiaries' net profit or loss	2 669	3 102
At the end of the period	**30 052**	**29 829**

31. Dividends paid

	Year ended 31 December 2016	Year ended 31 December 2015
Dividends paid in the period		
Dividends paid by subsidiaries	(2 787)	(2 630)
Dividends paid by the Parent	–	(262 882)
Total dividends paid	**(2 787)**	**(265 512)**

Dividend per share paid out by the parent for individual years was the following:

	Year ended 31 December 2016	Year ended 31 December 2015
Dividend paid per share (PLN)	–	0.15

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.

On 23 April 2015, the Ordinary General Shareholders' Meeting adopted a resolution to pay dividend to the shareholders of the Company of PLN 262 882 thousand from the net profit of the Company generated in the 2014 financial year, i.e. PLN 0.15 per share. The dividend was paid in August 2015.

32. Acquisition under common control

Acquisition of an organized part of the enterprise of Zakład Górniczy Brzeszcze

On 31 December 2015, Nowe Brzeszcze Grupa TAURON Sp. z o.o and Spółka Restrukturyzacji Kopalń S.A. ("SRK") entered into an agreement for sale of a designated part of Zakład Górniczy Brzeszcze as an organized part of the enterprise ("ZCP Brzeszcze"). The aforesaid agreement was entered into in performance of the preliminary agreement of 19 October 2015 and under Article 8a.4 of the Act on Hard Coal Mining of 7 September 2007. Under the sale agreement, the date of the provision of the object of sale and making the acquired ZCP Brzeszcze available for use to Nowe Brzeszcze Grupa TAURON Sp. z o.o was 1 January 2016, as of which date the risks and rewards relating to the object of sale were transferred onto Nowe Brzeszcze Grupa TAURON Sp. z o.o.

The ZCP Brzeszcze selling price agreed by the parties and payable to SRK is PLN 1.00. Due to the fact that KWK Brzeszcze incurred losses at the time of its operation as part of SRK, under an agreement of 29 May 2015 between the Minister of Economy and SRK, funds from the government budget were allocated to SRK for purposes of offsetting current production losses of the mining company in 2015 ("Public Aid"). At the same time, in accordance with the aid refund agreement, Nowe Brzeszcze Grupa TAURON Sp. z o.o. committed to return the Public Aid, including interest accrued as of each date of disbursement of the Public Aid by its provider to SRK. Thus, the acquisition price comprises the agreed price of PLN 1.00 and the Public Aid amount to be refunded, including interest due as at 31 December 2015, i.e. PLN 130 218 thousand. In the year ended 31 December 2016, Nowe Brzeszcze Grupa

(in PLN '000)

TAURON Sp. z o.o. refunded the aforementioned Public Aid amount along with interest accrued by the repayment date. The expenditure relating to the Public Aid refund has been presented under investing activities in the consolidated statement of cash flows.

As the transaction involving the acquisition of ZCP Brzeszcze is carried out under common control of the State Treasury, Nowe Brzeszcze Grupa TAURON Sp. z o.o. accounted for the business combination using the pooling of interest method, as provided for by the accounting policies adopted by the Group, on the assumption that comparative data could not be presented.

Presented below is the balance sheet as at the date of the acquisition of the designated part of Zakład Górniczy Brzeszcze by Nowe Brzeszcze Grupa TAURON Sp. z o.o.

	As at 1 January 2016		As at 1 January 2016
Non-current assets		**Equity**	**(14 041)**
Property, plant and equipment and intangible assets	215 924	**Provisions and liabilities**	
Deferred tax assets	3 127	Provision for mine decommissioning	65 992
	219 051	Provisions for employee benefits	26 462
		Accruals (provision for unused annual leave)	4 203
Current assets		Obligations under leases	3 132
Inventories	1 349	Liabilities arising from public aid refund	130 218
Other financial assets	25	Other financial liabilities	4 459
	1 374		**234 466**
Total assets	**220 425**	**Total equity and liabilities**	**220 425**

As Zakład Górniczy Brzeszcze did not prepare its financial statements in conformity with IFRS, for purposes of accounting for the transaction, the Group prepared the balance sheet of ZCP Brzeszcze in accordance with its own accounting policies. To this end, the following procedures were performed:

- fixed assets were measured by an independent property appraiser. In the absence of an active market, the major part of such assets were measured at amortized replacement cost.
- The following provisions were recognized:
  - a mine decommissioning provision – estimated on the basis of third-party expert calculations;
  - an actuarial provision – estimated using actuarial methods on the basis of agreements setting out the terms of calculation and payment of retirement and disability benefits and jubilee bonuses at Kompania Węglowa S.A.;
  - a provision for unused annual leave – estimated by an actuary.

Following the acquisition of ZCP Brzeszcze, no trade receivables or liabilities relating to that part of the enterprise were transferred onto Nowe Brzeszcze Grupa TAURON Sp. z o.o. As regards inventories, only materials of PLN 1 349 thousand were transferred.

Business combination under common control of Nowe Brzeszcze Grupa TAURON Sp. z o.o. and TAURON Wydobycie S.A.

On 1 December 2016, the business combination under common control of TAURON Wydobycie S.A. (acquirer) and Nowe Brzeszcze Grupa TAURON Sp. z o.o. (acquiree) was registered. The business combination under common control was effected in accordance with Article 492.1.1 of the Code of Commercial Companies as an acquisition, through the transfer of all the assets, equity and liabilities of Nowe Brzeszcze Grupa TAURON Sp. z o.o. onto TAURON Wydobycie S.A. The business combination has not affected these consolidated financial statements.

33. Debt

	As at 31 December 2016	As at 31 December 2015
Loans and borrowings	1 263 553	1 411 776
Bonds issued	7 681 128	6 680 433
Finance lease	34 848	46 438
Total	**8 979 529**	**8 138 647**
Non-current	8 759 789	4 924 127
Current	219 740	3 214 520

(in PLN '000)

33.1. Loans and borrowings

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 loans and borrowings			**1 263 553**						

Loans and borrowings taken out as at 31 December 2015

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	77 350	77 350	29 993	6 864	7 333	7 308	14 316	11 536
	fixed	1 316 062	1 316 062	20 444	112 297	147 478	162 214	324 429	549 200
Total PLN		**1 393 412**	**1 393 412**	**50 437**	**119 161**	**154 811**	**169 522**	**338 745**	**560 736**
EUR	floating	2 025	8 630	8 630	–	–	–	–	–
Total EUR		**2 025**	**8 630**	**8 630**	**–**	**–**	**–**	**–**	**–**
USD	floating	404	1 576	1 576	–	–	–	–	–
Total USD		**404**	**1 576**	**1 576**	**–**	**–**	**–**	**–**	**–**
Total			**1 403 618**	**60 643**	**119 161**	**154 811**	**169 522**	**338 745**	**560 736**
Interest increasing carrying amount			8 158						
Total loans and borrowings			**1 411 776**						

Changes in the balance of loans and borrowings, excluding interest increasing their carrying amounts, in the year ended 31 December 2016 and in the year ended 31 December 2015, have been presented below.

	Year ended 31 December 2016	Year ended 31 December 2015
Opening balance	**1 403 618**	**1 225 612**
Movement in bank overdrafts and cash pool loans	**(8 332)**	**23 184**
Movement in loans (excluding bank overdrafts and cash pool loans):	**(138 819)**	**154 822**
Repaid	(140 331)	(140 585)
Taken out*	914	294 705
Change in valuation	598	702
Closing balance	**1 256 467**	**1 403 618**

** Costs of granting the loan have been included.*

(in PLN '000)

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 2016	As at 31 December 2015
Loans	European Investment Bank	Construction of a boiler fired with biomass at Jaworzno III Power Plant and renovation of a steam turbine	Fixed	15.12.2021	105 039	126 218
		Construction and start-up of a co-generation unit at EC Bielsko Biała	Fixed	15.12.2021	150 056	180 303
		Modernization and extension of power grid	Fixed – agreed until 15 December 2017	15.06.2024	307 362	348 325
			Fixed – agreed until 15 March 2018	15.09.2024	147 091	165 467
			Fixed – agreed until 15 March 2018	15.09.2024	183 783	206 746
		Modernization and extension of power grid and improvement of hydropower plants	Fixed – agreed until 15 September 2019	15.03.2027	297 170	297 132
Borrowings	Regional Fund for Environmental Protection and Water Management	Construction of renewable power unit at Jaworzno III Power Plant	Floating	15.12.2022	24 000	28 000
		Construction of biomass infeed installation and modernization of fluid bed at Tychy Generation Plant	Floating	15.12.2022	16 561	19 216
Other loans and borrowings					32 491	40 369
Total					**1 263 553**	**1 411 776**

33.2. Bonds issued

Bonds issued as at 31 December 2016

Issuer	Tranche/ Bank	Redemption date	Currrency	As at balance sheet date		of which maturing within (after the balance sheet date):				
				Interest accrued	Principal at amortised cost	up to 3 months	3–12 months	1–2 years	2–5 years	Over 5 years
TAURON Polska Energia S.A.	Bank Gospodarstwa Krajowego	20 December 2019	PLN	107	99 805	–	–	–	99 805	–
		20 December 2020	PLN	107	99 786	–	–	–	99 786	–
		20 December 2021	PLN	107	99 773	–	–	–	99 773	–
		20 December 2022	PLN	107	99 763	–	–	–	–	99 763
		20 December 2023	PLN	107	99 754	–	–	–	–	99 754
		20 December 2024	PLN	107	99 749	–	–	–	–	99 749
		20 December 2025	PLN	107	99 744	–	–	–	–	99 744
		20 December 2026	PLN	107	99 738	–	–	–	–	99 738
		20 December 2027	PLN	107	99 734	–	–	–	–	99 734
		20 December 2028	PLN	107	99 733	–	–	–	–	99 733
		20 December 2020	PLN	74	69 976	–	–	–	69 976	–
		20 December 2021	PLN	74	69 976	–	–	–	69 976	–
		20 December 2022	PLN	74	69 976	–	–	–	–	69 976
		20 December 2023	PLN	74	69 976	–	–	–	–	69 976
		20 December 2024	PLN	74	69 975	–	–	–	–	69 975
		20 December 2025	PLN	74	69 975	–	–	–	–	69 975
		20 December 2026	PLN	74	69 975	–	–	–	–	69 975
		20 December 2027	PLN	74	69 975	–	–	–	–	69 975
		20 December 2028	PLN	74	69 975	–	–	–	–	69 975
		20 December 2029	PLN	74	69 975	–	–	–	–	69 975
	Bond Issue Scheme of 24.11.2015	29 December 2020	PLN	549	2 244 801	–	–	–	2 244 801	–
		25 March 2020	PLN	790	99 771	–	–	–	99 771	–
		9 December 2020	PLN	560	298 761	–	–	–	298 761	–
	TPEA1119	4 November 2019	PLN	7 578	1 749 155	–	–	–	1 749 155	–
	European Investment Bank	16 December 2034	EUR	1 693	839 330	–	–	–	–	839 330
TAURON Sweden Energy AB (publ)		3 December 2029	EUR	2 067	736 930	–	–	–	–	736 930
Total debentures				**15 047**	**7 666 081**	**–**	**–**	**–**	**4 831 804**	**2 834 277**

(in PLN '000)

Bonds issued as at 31 December 2015

Issuer	Tranche/ Bank	Redemption date	Currrency	As at balance sheet date		of which maturing within (after the balance sheet date):				
				Interest accrued	Principal at amortised cost	up to 3 months	3–12 months	1–2 years	2–5 years	Over 5 years
TAURON Polska Energia S.A.	C	12 December 2016	PLN	4 389	2 998 938	2 249 203	749 735	–	–	–
	Bank Gospodarstwa Krajowego	20 December 2019	PLN	106	99 836	–	–	–	99 836	–
		20 December 2020	PLN	106	99 823	–	–	–	99 823	–
		20 December 2021	PLN	106	99 815	–	–	–	–	99 815
		20 December 2022	PLN	106	99 808	–	–	–	–	99 808
		20 December 2023	PLN	106	99 802	–	–	–	–	99 802
		20 December 2024	PLN	106	99 800	–	–	–	–	99 800
		20 December 2025	PLN	106	99 796	–	–	–	–	99 796
		20 December 2026	PLN	106	99 792	–	–	–	–	99 792
		20 December 2027	PLN	106	99 790	–	–	–	–	99 790
		20 December 2028	PLN	97	99 790	–	–	–	–	99 790
		20 December 2020	PLN	12	70 000	–	–	–	70 000	–
		20 December 2021	PLN	12	70 000	–	–	–	–	70 000
		20 December 2022	PLN	12	70 000	–	–	–	–	70 000
	TPEA1119	4 November 2019	PLN	7 508	1 749 043	–	–	–	1 749 043	–
TAURON Sweden Energy AB (publ)		3 December 2029	EUR	1 921	709 495	–	–	–	–	709 495
Total debentures				**14 905**	**6 665 528**	**2 249 203**	**749 735**	**–**	**2 018 702**	**1 647 888**

Changes in the balance of bonds, excluding interest which increased the carrying amount, in the year ended 31 December 2016 and in the comparative period, have been presented below.

	Year ended 31 December 2016	Year ended 31 December 2015
Opening balance	**6 665 528**	**6 803 298**
Issue*	4 273 379	309 789
Redemption	(3 300 000)	(450 000)
Change in valuation	27 174	2 441
Closing balance	**7 666 081**	**6 665 528**

** Costs of issue have been included.*

In the year ended 31 December 2016, the Parent issued (par value) and repurchased the following bonds:

Date of issue/ redemption	Agreement/ Scheme	Description	Year ended 31 December 2016	
			Par value of issue	Redemption
8.01.2016	Agreement with Bank Gospodarstwa Krajowego	Issue of three bond tranches with the par value of PLN 70 000 thousand each, maturing on 20 December 2023, 2024 and 2025, respectively.	210 000	
29.02.2016	Bond Issue Scheme dated 16 December 2010	Early repurchase of C tranche bonds with the par value of PLN 2 250 000 thousand, issued on 12 December 2011.		(2 250 000)
29.02.2016	Bond Issue Scheme dated 24 November 2015	Issue of bonds with the par value of PLN 2 250 000 thousand, maturing on 29 December 2020.	2 250 000	
25.03.2016		Issue of bonds with the par value of PLN 100 000 thousand, maturing on 25 March 2020.	100 000	
30.03.2016		Issue of bonds with the par value of PLN 300 000 thousand, maturing on 30 March 2020.	300 000	
30.09.2016		Early repurchase of a tranche of PLN 300 000 thousand, issued in March 2016.		(300 000)
9.12.2016		Issue of bonds with the par value of PLN 300 000 thousand, maturing on 9 December 2020.	300 000	
9.12.2016	Agreement with Bank Gospodarstwa Krajowego	Issue of four bond tranches with the par value of PLN 70 000 thousand each, maturing on 20 December 2026, 2027, 2028 and 2029, respectively.	280 000	
12.12.2016	Bond Issue Scheme dated 16 December 2010	Repurchase of C tranche bonds with the par value of PLN 750 000 thousand, issued on 12 December 2011, at maturity.		(750 000)
16.12.2016	Agreement with European Investment Bank	Issue of bonds with the par value of EUR 190 000 thousand, maturing on 16 December 2034.	844 607	
		Total	**4 284 607**	**(3 300 000)**

The major issues and repurchases have been discussed below:

- Under the bond issue scheme of 16 December 2010, the debt balance as at 1 January 2016 was PLN 3 000 000 thousand. On 29 February 2016, the Company repurchased 22 500 out of 30 000 Tranche C bonds issued on 12 December 2011, for purposes of redemption. The remaining 7 500 Tranche C bonds were not repurchased early. In accordance with the terms of issue, they were repurchased on 12 December 2016. The aforesaid bonds were repurchased at the issue price of PLN 100 thousand. Thus, the total par value of bonds which were repurchased and redeemed by the Company was PLN 2 250 000 thousand. This amount was increased by interest due between the beginning of the interest period of the repurchase and the repurchase date. The bonds were repurchased for redemption under bilateral agreements concluded by the Company with Tranche C bond holders, mainly to prolong the date of the Company's repayment of debt incurred in the form of bonds. The funds necessary to refinance the bonds were secured as part of a new bond issue scheme of 24 November 2015.
- Under the new bond issue scheme of 24 November 2015, the Company issued 22 500 bonds with the total par value of PLN 2 250 000 thousand on 29 February 2016. The bonds will mature on 29 December 2020. The bonds were issued as unsecured, dematerialized coupon securities. They were purchased at the issue price equal to the par value of PLN 100 thousand. The interest on issued bonds was determined by reference to WIBOR 6M increased by a fixed margin. The bonds will be repurchased at the issue price at maturity, while interest will be paid in arrears at the end of each interest period to bond holders determined at the record date. The bonds were purchased by financial institutions being parties to the bond issue scheme agreements, i.e. Bank BGŻ BNP Paribas S.A., Bank Handlowy w Warszawie S.A., Bank of Tokyo-Mitsubishi UFJ (Holland) BV, Bank of Tokyo-Mitsubishi UFJ (Polska) S.A., 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., mBank S.A. and Powszechna Kasa Oszczędności Bank Polski S.A. As part of the aforesaid scheme lower value issues took place as well. They have been presented in the table above.
- On 14 December 2016, the Company entered into agreements with the European Investment Bank ("EIB") serving as the basis for the issue of hybrid bonds of EUR 190 000 thousand. The purpose of the issue is to finance the expenditures of an entity from the Distribution segment, planned for 2016–2020 in relation to the development and modernization of electric energy grid infrastructure.

  The bonds were issued on 16 December 2016 as subordinated, unsecured coupon bearer securities, and they were acquired by EIB 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 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 Capital 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.

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 the repayment currency. As at 31 December 2016, the carrying amount of the bonds in the bond currency, increased by accrued interest, was EUR 167 043 thousand (versus EUR 166 941 thousand as at 31 December 2015). 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.

The Company hedges a portion of interest cash flows related to bonds issued using IRS contracts. The instruments are subject to hedge accounting, which has been discussed in more detail in Note 45.3 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. As at 31 December 2016, none of these covenants were breached and the contractual provisions were complied with.

(in PLN '000)

33.3. Finance lease

	As at 31 December 2016		As at 31 December 2015	
	Minimum lease payments	Present value of lease payments	Minimum lease payments	Present value of lease payments
Within 1 year	12 026	11 301	13 909	12 715
Within 1 to 5 years	23 724	23 527	34 691	33 701
More than 5 years	22	20	24	22
Minimum lease payments, total	**35 772**	**34 848**	**48 624**	**46 438**
Less amounts representing finance charges	(924)	–	(2 186)	–
Present value of minimum lease payments, of which:	**34 848**	**34 848**	**46 438**	**46 438**
Non-current	23 546	23 546	33 723	33 723
Current	11 302	11 302	12 715	12 715

Key finance lease items as at 31 December 2016:

- liability due to lease of buildings in Katowice in the amount of PLN 26 974 thousand (versus PLN 30 169 thousand as at 31 December 2015);
- liability due to lease of technical equipment and machines as well as real property of PLN 6 642 thousand (versus PLN 15 785 thousand as at 31 December 2015).

34. Provisions for employee benefits

	As at 31 December 2016	As at 31 December 2015
Provision for post-employment benefits and jubilee bonuses	1 480 391	1 850 375
Provision for employment termination benefits	51 222	57 336
Total	**1 531 613**	**1 907 711**
Non-current	1 373 385	1 735 206
Current	158 228	172 505

34.1. Provisions for post-employment benefits and jubilee bonuses

Change in provisions for employee benefits in 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**

(in PLN '000)

Change in provisions for employee benefits in the year ended 31 December 2015

	Provision for retirement, disability and similar benefits	Employee electricity rates	Social Fund	Provision for coal allowances	Jubilee bonuses	Provisions, total
Opening balance	**357 017**	**769 975**	**170 242**	**67 661**	**679 510**	**2 044 405**
Current service costs	14 533	8 144	2 960	983	39 023	**65 643**
Actuarial gains and losses, of which:	(11 222)	(47 439)	(6 084)	222	(8 683)	**(73 206)**
arising from changes in financial assumptions	(29 065)	(63 451)	(12 090)	–	(39 657)	**(144 263)**
arising from changes in demographic assumptions	2 439	15 946	3 749	–	6 687	**28 821**
arising from other changes	15 404	66	2 257	222	24 287	**42 236**
Benefits paid	(24 011)	(22 784)	(3 943)	(1 321)	(61 515)	**(113 574)**
Past service costs	(3 115)	(2 321)	(35 561)	(68 432)	(10 197)	**(119 626)**
Interest expense	7 922	17 159	3 496	887	15 027	**44 491**
Other changes	–	–	–	2 242	–	**2 242**
Closing balance	**341 124**	**722 734**	**131 110**	**2 242**	**653 165**	**1 850 375**
Non-current	318 390	699 207	126 824	–	581 372	**1 725 793**
Current	22 734	23 527	4 286	2 242	71 793	**124 582**

In the year ended 31 December 2016, the Group reduced its provisions for post-employment benefits and jubilee bonuses relating to past service costs by the total of PLN 150 181 thousand, which increased the Group's profit/loss. Past service costs resulted mainly from:

- modification of the Collective Labor Agreements in companies mainly from the Distribution segment – reversal of provisions totaling PLN 156 792 thousand;
- changes in the retirement age – increase in provisions by PLN 7 174 thousand.

Following a change in actuarial assumptions made for purposes of the actuarial valuation as at 31 December 2016, provisions were reduced by PLN 244 893 thousand, which drove an increase in other comprehensive income by PLN 204 597 thousand (provisions for post-employment benefits) and in the Group's profit/loss by PLN 40 296 thousand (provisions for jubilee bonuses).

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 2016	31 December 2015
Discount rate (%)	3.00%	2.75%
Estimated inflation rate (%)	2.50%	2.35%
Employee rotation rate (%)	0.04% – 7.95%	1.14% – 9.10%
Estimated salary increase rate (%)	1.00% – 3.50%	0.23% – 2.43%
Estimated electricity price increase rate (%)	3.50%	4.30%
Estimated increase rate for contribution to the Social Fund (%)	3.50%	4.50%
Remaining average employment period	9.27 – 25.00	9.80 – 14.90

Sensitivity analysis

As at 31 December 2016, the Group analyzed sensitivity of measurement results to changes in the financial discount 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 2016	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	307 281	321 730	293 961	294 146	321 401
Employee electricity rates	532 184	575 395	493 934	493 934	574 953
Costs of appropriation to Social Benefits Fund	112 469	123 616	106 232	106 294	123 453
Jubilee bonuses	526 209	544 509	509 054	512 185	541 052
Total		**1 565 250**	**1 403 181**	**1 406 559**	**1 560 859**

(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	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	307 281	14 449	(13 320)	(13 135)	14 120
Employee electricity rates	532 184	43 211	(38 250)	(38 250)	42 769
Costs of appropriation to Social Benefits Fund	112 469	11 147	(6 237)	(6 175)	10 984
Jubilee bonuses	526 209	18 300	(17 155)	(14 024)	14 843
Total, including:		**87 107**	**(74 962)**	**(71 584)**	**82 716**
effect on profit/loss		18 300	(17 155)	(14 024)	14 843
effect on other comprehensive income		68 807	(57 807)	(57 560)	67 873

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	Coal allowances	Jubilee bonuses	Provisions, total
2017	35 347	19 513	4 353	2 248	57 246	**118 707**
2018	14 346	21 557	4 421	–	48 304	**88 628**
2019	14 675	21 067	4 321	–	44 081	**84 144**
2020	14 167	20 606	4 227	–	39 598	**78 598**
2021	13 702	20 130	4 134	–	37 973	**75 939**
Other years	215 044	429 311	91 013	–	299 007	**1 034 375**
Total	**307 281**	**532 184**	**112 469**	**2 248**	**526 209**	**1 480 391**

34.2. Provisions for employment termination benefits

For the year ended 31 December 2016

	Voluntary redundancy schemes in operating segments		Other	Total
	Generation	Distribution		
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**

For the year ended 31 December 2015

	Voluntary redundancy schemes in operating segments			Other	Total
	Mining	Generation	Distribution		
Opening balance	**–**	**38 867**	**22 236**	**1 769**	**62 872**
Recognition	4 750	9 864	24 898	8 444	**47 956**
Reversal	(4 750)	(419)	(3 563)	–	**(8 732)**
Utilization	–	(24 852)	(18 139)	(1 769)	**(44 760)**
Closing balance	**–**	**23 460**	**25 432**	**8 444**	**57 336**
Non-current	–	9 413	–	–	**9 413**
Current	–	14 047	25 432	8 444	**47 923**

(in PLN '000)

In the year ended 31 December 2016, the TAURON Group continued the Voluntary Redundancy Schemes introduced in previous years and implemented new schemes.

35. Provisions for dismantling fixed assets, restoration of land and other

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	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**

For the year ended 31 December 2015

	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	Provisions, total
Opening balance	**120 704**	**42 774**	**–**	**163 478**
Interest cost (discounting)	2 996	961	–	**3 957**
Discount rate adjustment	(13 308)	(675)	–	**(13 983)**
Recognition/(reversal), net	1 283	(1 205)	182 877	**182 955**
Reclassification to liabilities of a disposal group classified as held for sale	–	59 389	–	**59 389**
Closing balance	**111 675**	**101 244**	**182 877**	**395 796**
Non-current	111 675	100 339	163 449	**375 463**
Current	–	905	19 428	**20 333**
Other provisions, long-term portion				**1 909**
Total				**377 372**

35.1. Provision for mine decommissioning costs

The provision is recognized for mines included in the Group based on estimated costs of facility decommissioning and reclaiming land after completion of the exploitation process. More details on the calculation of the provision have been presented in Note 9.19 to these consolidated financial statements.

The provision for mine decommissioning costs includes the balance of the Mine Decommissioning Fund, 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.

In the year ended 31 December 2016, the provision increased by PLN 65 992 thousand following the acquisition of an organized part of the enterprise of Zakład Górniczy Brzeszcze, which has been discussed in more detail in Note 32 to these consolidated financial statements.

A decrease in the provision by PLN 35 846 thousand in the year ended 31 December 2016 was driven by the adoption of higher discount rates (3.50%) for purposes of valuation as at 31 December 2016 than as at 31 December 2015 (2.75%–3.04%). In the comparative period, following an increase in the discount rate used for purposes of valuation of provisions as at 31 December 2015 (up from 2.25%–2.50% to 2.75%–3.04%), the Group derecognized a provision of PLN 13 308 thousand.

(in PLN '000)

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.

Mine Decommissioning Fund financial assets

	Year ended 31 December 2016	Year ended 31 December 2015
Assets as at 1 January	**42 129**	**38 232**
Contributions made	4 112	4 463
Interest	730	809
Use	(6 051)	(1 375)
Other changes	243	–
Assets as at 31 December	**41 163**	**42 129**
Transfers made to the MDF in the period	(4 446)	(4 113)

Provision for mine decommissioning costs

	Year ended 31 December 2016	Year ended 31 December 2015
Mine Decommissioning Fund	44 442	43 731
Surplus of discounted estimated decommissioning costs	102 443	67 944
Total	**146 885**	**111 675**

35.2. 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 totaled PLN 39 415 thousand as at 31 December 2016 (versus PLN 41 855 thousand as at 31 December 2015).
- Provision for wind farm dismantling costs, which totaled PLN 51 088 thousand as at 31 December 2016 (versus PLN 59 389 thousand as at 31 December 2015).
- In 2016, a provision was recognized for the costs of removal of fixed assets in the amount of PLN 24 799 thousand related to the decommissioning of a chimney in Elektrownia Jaworzno as well as cooling towers and a unit in Elektrownia Łagisza.

35.3. Provision for onerous contracts with a joint venture

As the schedule had not been met and the material technical terms of the contract signed with the general contractor on the gas and steam unit construction project in Stalowa Wola, determining the safety and failure-free operation as well as the future efficiency and costs of operation of the unit, had been breached, Elektrociepłownia Stalowa Wola S.A. terminated the contract with the general contractor on 29 January 2016 and officially took over the construction site on 22 February 2016. The inventory of works performed by the general contractor was completed. Acceptance of the post-inventory documentation is in progress. Asset maintenance works are performed on an ongoing basis to prevent degradation.

In view of the foregoing, in the year ended 31 December 2015, the Company recognized provisions for onerous contracts with a joint venture, Elektrociepłownia Stalowa Wola S.A., totaling PLN 182 877 thousand.

In the year ended 31 December 2016, the Company remeasured the provisions for onerous contracts with a joint venture due to the unwinding of discount as at the end of the reporting period, which increased the provisions by PLN 11 502 thousand in total, and recognized additional provisions of PLN 4 465 thousand (net).

As at the end of the reporting period, the balance of provisions for onerous contracts amounted to PLN 198 844 thousand and included:

- a provision of PLN 133 327 thousand 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 is obliged to purchase half of the volume of electricity at a price determined in the "cost plus" formula, which covers the production costs and the financing costs. The provision was estimated taking account of the difference between the planned market prices of electricity and the costs resulting from the "cost plus" formula;

(in PLN '000)

- a provision of PLN 54 837 thousand resulting from the fact that the Company may be obliged to cover losses which may be incurred under the take or pay clause of the comprehensive gaseous fuel supply contract entered into by PGNiG S.A. and Elektrociepłownia Stalowa Wola S.A. In accordance with the aforesaid clause, Elektrociepłownia Stalowa Wola S.A. is obliged to make a payment to PGNiG S.A. for uncollected gas or resell it on the market. The provision was estimated on the assumption that the gas volume for 2016–2018 was the same as the one specified in the contract. The short-term portion of the provision is PLN 38 608 thousand;
- a provision for costs of PLN 10 680 thousand (PLN 7 293 thousand of which is the short-term portion). The Company may be required to incur additional costs necessary for the operation of Elektrociepłownia Stalowa Wola S.A. due to delays in project completion.

The provisions for the costs of fulfilment of the gas contract and for additional costs of operation have been recognized in proportion to the Company's interest in the joint venture.

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 aforesaid agreements and annexes will enter into force once the conditions precedent have been satisfied, i.e. the binding financing agreements have been amended or the amounts due to the last institution which currently provides funding to Elektrociepłownia Stalowa Wola S.A. have been paid. With a view to enforcing the standstill agreement entered into by the Company, Elektrociepłownia Stalowa Wola S.A., PGNiG S.A., the European Investment Bank, the European Bank for Reconstruction and Development and Bank Polska Kasa Opieki S.A. aimed to ensure that the financing institutions will refrain from accelerating the loans granted to the company and satisfying their claims through the use of the related collateral, at the request of the Company The Bank of Tokyo-Mitsubishi UFJ, Ltd. issued three bank guarantees for the financing institutions, totaling PLN 314 486 thousand.

The agreements and annexes reflect the will of the Company and PGNIG S.A. to continue the construction of the gas and steam unit. According to the Management Board of the Company, the aforesaid documents enable completion of the investment in 2019 (preliminary estimate). As the aforesaid agreements are conditional, the Management Board decided not to modify the key assumptions constituting the basis for provision calculation.

36. Provisions for liabilities due to gas emission and energy certificates

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

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	743 312	**1 125 258**
Reversal	(63)	(3 884)	**(3 947)**
Utilisation	(325 230)	(849 394)	**(1 174 624)**
Closing balance	**209 736**	**755 085**	**964 821**

For the year ended 31 December 2015

	Provision for gas emission obligations	Provision for obligation to submit energy certificates	Provisions, total
Opening balance	**8 130**	**914 926**	**923 056**
Recognition	153 084	863 210	**1 016 294**
Reversal	(2 290)	(2 202)	**(4 492)**
Utilisation	(5 841)	(910 883)	**(916 724)**
Closing balance	**153 083**	**865 051**	**1 018 134**

36.1. Provision for the obligation to surrender energy certificates

As at 31 December 2016, the Group recognized a short-term provision for the obligation to surrender energy certificates in the amount of PLN 755 085 thousand, out of which the amount of PLN 556 223 thousand was covered by certificates held as at the end of the reporting period, the amount of PLN 145 727 thousand was planned to be paid in the form of a substitution fee and the amount of PLN 53 135 thousand through the purchase of property rights.

(in PLN '000)

In the year ended 31 December 2016, the Group fulfilled the obligation to surrender certificates of electricity generated using renewable sources, in CHP units and energy efficiency certificates for 2015. Therefore, a provision of PLN 849 394 thousand was used.

36.2. 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 recognized at the amount of allowances acquired or contracted for that purpose and at market prices at the end of the reporting period for the unsecured allowance deficit (if any).

As at 31 December 2016, the provision for gas emission liabilities amounted to PLN 209 736 thousand and regarded the obligatory surrendering of emission allowances for the year ended 31 December 2016. As at 31 December 2016, the provision was recognized both for facilities owned by TAURON Wytwarzanie S.A. and by TAURON Ciepło Sp. z o.o.

In the year ended 31 December 2016, the Group fulfilled the surrendering obligation for 2015 and in part for 2016. A change in the balance of the provision in the year ended 31 December 2016 arises from:

- remeasurement of the provision for the obligation for 2015: TAURON Wytwarzanie S.A. recognized an additional provision of PLN 21 937 thousand and TAURON Ciepło Sp. z o.o. reversed a provision of PLN 63 thousand;
- recognition of the provision for the obligation for 2016: TAURON Wytwarzanie S.A. recognized a provision of PLN 319 620 thousand and TAURON Ciepło Sp. z o.o. a provision of PLN 40 389 thousand;
- use of the provision due to the fulfilment of the obligation for 2015 and surrender of emission allowances in the amount of PLN 174 957 thousand;
- use of the provision due to the fulfilment of the obligation for 2016 and surrender of emission allowances in the amount of PLN 150 273 thousand in December 2016.

As at 31 December 2016, 19 482 951 emission allowances were registered in the Group's accounts with the Union Registry, out of which 7 395 649 allowances were planned to be surrendered in fulfillment of the remaining obligation for 2016.

37. Other provisions

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 current other provisions			**366 456**

(in PLN '000)

For the year ended 31 December 2015

	Provision for use of real estate without contract	Provision for counterparty claims, court dispute and other provisions	Provisions, total
Opening balance	**93 818**	**66 341**	**160 159**
Recognition/(reversal), net	3 587	5 840	**9 427**
Utilisation	(5 496)	(6 240)	**(11 736)**
Other movements	–	1 771	**1 771**
Foreign exchange differences from translation of foreign entities	–	(1)	**(1)**
Closing balance	**91 909**	**67 711**	**159 620**
Non-current	–	1 909	**1 909**
Current	91 909	65 802	**157 711**
Current portion of provision for the costs of disassembly of fixed assets and land restoration and other provisions			**20 333**
Total current other provisions			**178 044**

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 facilities are located. As at 31 December 2016, the relevant provision amounted to PLN 92 143 thousand and was related to the following segments:

- Generation: PLN 50 196 thousand;
- Distribution: PLN 41 947 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 for counterparty claims, court disputes and other provisions

Material provisions recognized as other provisions have been discussed below:

(in PLN '000)

Item	Operating segment	Description	As at 31 December 2016	Effect on gross profit/loss for 2016
Provision 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 – Elektrownia II; • Construction of a system of power generation from renewable sources in Stalowa Wola, a provision has been recognised for the costs of returning the subsidy totalling PLN 52,297 thousand. 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, a provision totalling PLN 11,250 has been recognised.	63 547	(63 547)
Provision for a fine to the Energy Regulatory Office	Distribution	The provision concerning the risks of the violation of the Energy Law of 10 April 1997 by providing misleading information to the President of the Energy Regulatory Office.	20 436	(20 436)
Provision for increased transmission easement charges	Distribution	The provision concerns a 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 change in the nature of the land from forestry to business.	21 700	(21 700)
Proceedings before the Office of Competition and Consumer Protection	Distribution	A provision for fines imposed by the President of the Office of Competition and Consumer Protection for the abuse by ENION S.A. (now TAURON Dystrybucja S.A.) of its dominant position on the electricity distribution market. As at 31 December 2016, the provision was recognized for fines related to proceedings before the Court of Competition and Consumer Protection which had not been closed as at that date. The balance of the provision had not changed as compared to 31 December 2015.	7 302	–
Provision for real estate tax	Mining	Provisions for proceedings related to real estate tax on underground mining excavations.	23 008	(20 860)
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 period of the inspection proceedings was prolonged by the Director of the Tax Inspection Office a few times and the new deadline has been set at 28 April 2017.	64 494	(64 494)

38. Accruals, deffered income and government grants

38.1. Deferred income and government grants

	As at 31 December 2016	As at 31 December 2015
Deferred income, of which:	**293 284**	**325 861**
Donations, subsidies received for the purchase or fixed assets received free-of-charge	71 849	83 308
Connection fees	218 075	240 485
Other	3 360	2 068
Government grants, of which:	**317 505**	**382 660**
Subsidies obtained from EU funds	211 981	286 222
Forgiven loans from environmental funds	28 068	11 801
Measurement of preferential loans	37 777	39 401
Other	39 679	45 236
Total	**610 789**	**708 521**
Non-current	553 874	650 364
Current	56 915	58 157

(in PLN '000)

38.2. Accruals

	As at 31 December 2016	As at 31 December 2015
Unused holidays	48 640	37 468
Bonuses	140 930	140 946
Environmental protection charges	3 806	4 449
Other	17 790	13 317
Total	**211 166**	**196 180**
Non-current	419	–
Current	210 747	196 180

39. Liabilities to suppliers

Current liabilities to suppliers as at 31 December 2016 and 31 December 2015 are presented in the table below:

Liabilities to suppliers in operating segments	As at 31 December 2016	As at 31 December 2015
Distribution	294 573	281 839
including from Polskie Sieci Elektroenergetyczne S.A.	*200 732*	*176 859*
Sales	247 487	245 424
Mining	144 722	83 111
Generation	100 857	130 606
Other	42 090	49 726
Total	**829 729**	**790 706**

40. Capital commitments

Short-term capital commitments as at 31 December 2016 and 31 December 2015 are presented in the table below:

Capital commitments in operating segments	As at 31 December 2016	As at 31 December 2015
Generation	511 403	290 916
Distribution	336 624	420 735
Mining	159 138	30 603
Sales and other	26 639	24 589
Total	**1 033 804**	**766 843**

An increase in capital commitments in the Generation segment concerned mainly a rise in commitments relating to construction of unit 910 in Jaworzno, which totaled PLN 458 484 thousand as at 31 December 2016 versus PLN 124 690 thousand as at 31 December 2015.

A rise in capital commitments in the Mining segment concerned mainly a commitment relating to development of a longwall system in Zakład Górniczy Brzeszcze in the amount of PLN 89 080 thousand. No such commitment was recognized as at 31 December 2015.

Long-term capital commitments have been presented in the consolidated statement of financial position within other financial liabilities. As at 31 December 2016 and 31 December 2015, the related commitments totaled PLN 299 thousand (Distribution) and PLN 916 thousand (Distribution: PLN 416 thousand, Sales: PLN 500 thousand), respectively.

Commitments to incur capital expenditure

As at 31 December 2016 and 31 December 2015, the Group committed to incur expenditure on property, plant and equipment and intangible assets of PLN 4 368 685 thousand and PLN 5 597 990 thousand, respectively, with the key items presented below:

(in PLN '000)

Operating segment	Agreement/investment project	As at 31 December 2016	As at 31 December 2015
Generation	Construction of a power-generating unit with the capacity of 910 MW for supercritical parameters in Jaworzno III Power Plant	2 579 313	3 773 520
	Commissioning of a part of external coal handling system and an ash removal system for a power-generating unit with the capacity of 910 MW for supercritical parameters in Jaworzno III Power Plant	229 150	144 325
	Constructing new cogeneration capacity in Tychy Heat and Power Plant	10 000	98 970
Distribution	Redevelopment of the double track overhead line Przybków-Kąty Wrocławskie-Klecina	31 446	73 140
	Implementation of Smart City Wrocław, an intelligent measurement system	18 880	91 126
	Construction of Grid Management Centre in Kraków and in Wrocław	30 951	55 176
Mining	Construction of the "Grzegorz" shaft with the accompanying infrastructure and excavations	16 484	22 105
	Construction of the 800 m drift at Janina Mining Plant	19 578	37 986
	Investment Program in Brzeszcze Mining Plant	32 731	–

41. Liabilities due to taxes and charges

	As at 31 December 2016	As at 31 December 2015
Corporate Income Tax	2 371	85 357
Personal Income Tax	51 084	46 841
Excise	41 549	42 467
VAT	98 114	46 787
Social security	170 039	156 635
Environmental charges	40 964	46 889
Other	6 822	4 673
Total	**410 943**	**429 649**

A decrease in corporate income tax liabilities was driven by the fact that as at 31 December 2016, the Tax Capital Group had receivables of PLN 83 153 thousand arising from income tax, which has been discussed in more detail in Note 28 to these consolidated financial statements. As at 31 December 2015, the Tax Capital Group had an income tax liability in the amount of PLN 82 944 thousand.

42. Other financial liabilities

	As at 31 December 2016	As at 31 December 2015
Wages, salaries and related charges	174 212	172 660
Bid bonds, deposits and collateral received	79 415	120 890
Insurance contracts	12 560	16 149
Derivative instruments	560	112 109
Other	61 922	20 563
Total	**328 669**	**442 371**
Non-current	72 374	101 705
Current	256 295	340 666

Derivative instruments have been discussed in Note 45.3 to these consolidated financial statements.

43. Other current non-financial liabilities

	As at 31 December 2016	As at 31 December 2015
Payments from customers relating to future periods, of which:	**298 606**	**273 168**
Prepayments for connection fees	21 369	25 366
Amounts overpaid by customers	245 544	240 700
Other	31 693	7 102
Other current non-financial liabilities	**2 573**	**754**
Total	**301 179**	**273 922**

(in PLN '000)

EXPLANATORY NOTES TO THE CONSOLIDATED STATEMENT OF CASH FLOWS

44. Significant items of the consolidated statement of cash flows

44.1. Cash flows from operating activities

Impairment losses on property, plant and equipment, intangible assets and goodwill

Impairment losses of PLN 867 109 thousand, which adjust the Group's profit/loss before tax, have been discussed in more detail in Note 11 to these consolidated financial statements.

Changes in working capital

	Year ended 31 December 2016	Year ended 31 December 2015
Change in receivables	**(46 280)**	**118 806**
Change in receivables from clients in statement of financial position	(64 032)	87 065
Adjustment related to acquisition of orgnanized part of the enterprise (ZCP Brzeszcze) and inclusion of new companies in consolidation	12 496	13 200
Other adjustments	5 256	18 541
Change in inventories	**(55 731)**	**90 497**
Change in inventories in statement of financial position	(52 841)	94 317
Adjustment related to transfer of invetories to/from property, plant and equipment	(4 347)	(4 502)
Other adjustments	1 457	682
Change in payables excluding loans and borrowings	**156 247**	**(180 636)**
Change in liabilities to suppliers in statement of financial position	39 023	(126 038)
Change in payroll, social security and other financial liabilities	(1 536)	(74 211)
Change in non-financial liabilities in statement of financial position	27 257	(3 649)
Change in liabilities due to taxes excluding income tax	64 280	2 174
Adjustment related to acquisition of orgnanized part of the enterprise (ZCP Brzeszcze) and inclusion of new companies in consolidation	(24 610)	(9 395)
Adjustment of VAT change related to capital commitments	50 570	33 574
Other adjustments	1 263	(3 091)
Change in other non-current and current assets	**341 335**	**(104 176)**
Change in other current and non-current non-financial assets	176 026	95 543
Change in receivables due to taxes excluding income tax	47 050	(94 481)
Change in non-current and current emission allowances	(8 727)	(157 717)
Change in non-current and current energy certificates	218 347	47 037
Change in advance payments for property, plant and equipment and intangible assets	(84 372)	(49 172)
Reclassification to/from assets held for sale	–	39 758
Other adjustments	(6 989)	14 856
Change in deferred income, government grants and accruals	**(140 063)**	**(73 962)**
Change in deferred income, government grants and accruals	(82 746)	(2 891)
Adjustmet related to property, plant and equipment and intangible assets received free of charge	(18 919)	(21 348)
Adjustment related to subsidies received	(29 220)	(41 941)
Other adjustments	(9 178)	(7 782)
Change in provisions	**(28 173)**	**141 843**
Change of short term and long term provisions in statement of financial position	(169 061)	127 291
Adjustment related to actuarial gains/losses from provisions for post-employment benefits charged to other comprehensive income	204 597	64 523
Adjustment related to acquisition of orgnanized part of the enterprise (ZCP Brzeszcze)	(92 454)	–
Adjustment related to change of provisions for disassembly of fixed assets and land restoration booked in correspondence with property, plant and equipment	33 415	10 699
Reclassification to/from assets held for sale	–	(59 375)
Other adjustments	(4 670)	(1 295)
Total	**227 335**	**(7 628)**

Income tax paid

Income tax paid in the amount of PLN 394 792 thousand results mainly from the Tax Capital Group's payment of advance income tax for 2016 totaling PLN 300 054 thousand in the year ended 31 December 2016 and advance income tax for the fourth quarter of 2015 totaling PLN 88 784 thousand.

(in PLN '000)

44.2. Cash flows from investing activities

Purchase of property, plant and equipment and intangible assets

	Year ended 31 December 2016	Year ended 31 December 2015
Purchase of property, plant and equipment	(3 590 348)	(3 877 348)
Purchase of intangible assets	(127 446)	(117 145)
Change in the balance of VAT – adjusted capital commitments	214 984	138 635
Change in the balance of advance payments	84 372	49 172
Costs of overhaul and internal manufacturing	(99 017)	(180 912)
Other	1 159	14 088
Total	**(3 516 296)**	**(3 973 510)**

Public aid refund

Payments to refund public aid of PLN 131 077 thousand are related to the refund made by Nowe Brzeszcze Grupa TAURON Sp. z o.o. under the public aid refund agreement, which has been discussed in more detail in Note 32 to these consolidated financial statements.

Acquisition of financial assets

Payments to acquire financial assets in the year ended 31 December 2016 in the amount of PLN 36 621 thousand include mainly the Parent's purchase of units of PLN 25 000 thousand.

Loans granted

Payments to grant loans result from the loans disbursed by the Parent to Elektrociepłownia Stalowa Wola S.A., a jointly-controlled entity, in the total amount of PLN 23 575 thousand under agreements entered into in November 2015 and in the year ended 31 December 2016, which has been discussed in more detail in Note 23 to these consolidated financial statements.

Dividends received

Proceeds from dividends received in the amount of PLN 29 728 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 24 000 thousand.

44.3. Cash flows from financing activities

Repurchase of debt securities

Payments to repurchase debt securities result from the Company's repurchase of Tranche C bonds in the total amount of PLN 3 000 000 thousand in the year ended 31 December 2016 and the early repurchase (on 30 September 2016) of a Tranche of PLN 300 000 thousand issued in March 2016.

Loans and borrowings repaid

Payments to repay loans and borrowings of PLN 140 331 thousand disclosed in the consolidated statement of cash flows result mainly from the Parent's repayment of installments of a loan obtained from the European Investment Bank in the amount of PLN 132 818 thousand in the year ended 31 December 2016.

Interest paid

	Year ended 31 December 2016	Year ended 31 December 2015
Interest paid in relation to debt securities	(296 949)	(286 692)
Interest paid in relation to loans and borrowings	(53 183)	(57 536)
Interest paid in relation to the finance lease	(955)	(1 237)
Total, of which:	**(351 087)**	**(345 465)**
financing cash outflows	(255 116)	(276 305)
investing cash outflows	(95 971)	(69 160)

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.

Issue of debt securities

Proceeds from the issue of debt securities in the year ended 31 December 2016 are related to:

- the Company's issue of bonds with the total par value of PLN 2 950 000 thousand under a bond issue scheme of November 2015, which has been discussed in more detail in Note 33.2 to these consolidated financial statements;
- the Company's issue of bond tranches under the agreement with Bank Gospodarstwa Krajowego in the total amount of PLN 490 000 thousand;
- the Company's issue of subordinated hybrid bonds of PLN 844 607 thousand.

(in PLN '000)

FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

45. Financial instruments

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

Categories and classes of financial assets	Note	As at 31 December 2016		As at 31 December 2015	
		Carrying amount	Fair value	Carrying amount	Fair value
1 Assets at fair value through profit or loss, held for trading		**45 092**		**5 684**	
Derivative instruments	**45.3**	19 776	19 776	5 684	5 684
Investment fund units	**24**	25 316	25 316	–	–
2 Financial assets available for sale		**130 143**		**140 783**	
Shares (non-current)	**24**	123 594		132 383	
Shares (current)	**24**	4 104		4 105	
Investment fund units	**24**	2 445	2 445	2 405	2 405
Bonds, T-bills and other debt securities		–	–	1 890	1 890
3 Loans and receivables		**2 245 033**		**2 150 918**	
Receivables from clients	**27**	1 894 065	1 894 065	1 830 033	1 830 033
Deposits	**24**	38 472	38 472	39 724	39 724
Loans granted		256 117	256 117	223 911	223 911
Other financial receivables		56 379	56 379	57 250	57 250
4 Financial assets excluded from the scope of IAS 39		**461 348**		**418 127**	
Investments in joint ventures	**22**	461 348		418 127	
5 Derivative hedging instruments	**45.3**	**36 641**	**36 641**	**–**	**–**
6 Cash and cash equivalents	**29**	**384 881**	**384 881**	**364 912**	**364 912**
Total financial assets, of which in the statement of financial position:		**3 303 138**		**3 080 424**	
Non-current assets		**929 439**		**851 145**	
Investments in joint ventures		461 348		418 127	
Loans granted to joint ventures		240 951		221 803	
Other financial assets		227 140		211 215	
Current assets		**2 373 699**		**2 229 279**	
Receivables from clients		1 894 065		1 830 033	
Other financial assets		94 753		34 334	
Cash and cash equivalents		384 881		364 912	

(in PLN '000)

Categories and classes of financial liabilities	Note	As at 31 December 2016		As at 31 December 2015	
		Carrying amount	Fair value	Carrying amount	Fair value
1 Financial liabilities at fair value through profit or loss, held for trading		**560**		**16 642**	
Derivative instruments	**45.3**	560	560	16 642	16 642
2 Financial liabilities measured at amortized cost		**11 136 323**		**9 980 020**	
Preferential loans	**33.1**	41 748	41 748	47 999	47 999
Arm's length loans	**33.1**	1 206 649	1 209 558	1 353 571	1 375 724
Bank overdrafts	**33.1**	15 156	15 156	10 206	10 206
Bonds issued	**33.2**	7 681 128	7 719 015	6 680 433	6 683 707
Liabilities to suppliers	**39**	829 729	829 729	790 706	790 706
Other financial liabilities	**42**	158 383	158 383	157 240	157 240
Capital commitments	**40**	1 034 103	1 034 103	767 759	767 759
Salaries and wages		156 867	156 867	155 957	155 957
Insurance contracts	**42**	12 560	12 560	16 149	16 149
3 Liabilities under guarantees, factoring and excluded from the scope of IAS 39		**34 848**		**46 438**	
Obligations under finance leases	**33.3**	34 848	34 848	46 438	46 438
4 Derivative hedging instruments	**45.3**	**–**	**–**	**95 467**	**95 467**
Total financial liabilities, of which in the statement of financial position:		**11 171 731**		**10 138 567**	
Non-current liabilities		**8 832 163**		**5 025 832**	
Debt		8 759 789		4 924 127	
Other financial liabilities		72 374		101 705	
Current liabilities		**2 339 568**		**5 112 735**	
Debt		219 740		3 214 520	
Liabilities to suppliers		829 729		790 706	
Capital commitments		1 033 804		766 843	
Other financial liabilities		256 295		340 666	

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 45.3 to these consolidated financial statements. Disclosures regarding the fair value hierarchy have also been presented in Note 45.3. Measurement of units in investment funds has been classified to Level 1 in the fair value hierarchy.

Financial instruments classified to other categories of financial instruments:

- As at 31 December 2016, fixed-rate financial instruments, which included loans obtained from the European Investment Bank and bonds issued by a subsidiary, were measured at fair value. 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. by applying market interest rates. The measurement resulted in Level 2 classification in the fair value hierarchy. The fair value of bonds issued in December 2016 with the par value of EUR 190 000 thousand, bearing fixed interest in the first financing period, did not differ considerably from the carrying amount as the issue date was close to the end of the reporting period.
- The fair value of other financial instruments (except shares classified as financial assets available for sale and excluded from the scope of IAS 39, as discussed below) as at 31 December 2016 and 31 December 2015 did not significantly differ from their values presented in the financial statements for the respective periods, for 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. The Group is unable to reliably estimate the fair value of shares held in companies which are not quoted on active markets. They are measured at cost less impairment losses as at the end of the reporting period. Similarly, interest in joint ventures – financial assets excluded from the scope of IAS 39 – are measured using the equity method in line with the accounting policies adopted by the Group.

(in PLN '000)

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

For the year ended 31 December 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**

For the year ended 31 December 2015 (*restated data*)

	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	–	4 684	–	–	–	–	**4 684**
Interest income / (expense)	15 651	–	44 734	(189 057)	(89 380)	(1 236)	**(219 288)**
Currency translation differences	1 887	–	(24)	(2 152)	–	813	**524**
Impairment / revaluation	2 148	189	(9 798)	–	–	–	**(7 461)**
Commission relating to borrowings and debt securities	–	–	–	(12 514)	–	–	**(12 514)**
Gain/ (loss) on disposal of investments	3	754	–	–	–	–	**757**
Other	(9 237)	–	–	–	–	–	**(9 237)**
Net financial income (costs)	**10 452**	**5 627**	**34 912**	**(203 723)**	**(89 380)**	**(423)**	**(242 535)**
Revaluation	267	–	(29 461)	–	–	–	**(29 194)**
Gain/loss on exercised commodity derivative instruments	762	–	–	–	–	–	**762**
Net operating income/(costs)	**1 029**	**–**	**(29 461)**	**–**	**–**	**–**	**(28 432)**
Remeasurement	–	–	–	–	85 932	–	**85 932**
Other comprehensive income	**–**	**–**	**–**	**–**	**85 932**	**–**	**85 932**

(in PLN '000)

45.3. Derivative instruments

	As at 31 December 2016				As at 31 December 2015			
	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	–	–	**–**	**–**	(11 368)	–	**3 055**	**(14 423)**
IRS	23	36 618	**36 641**	**–**	(4 833)	(90 634)	**–**	**(95 467)**
Commodity forwards/futures	15 999	–	**16 559**	**(560)**	17	–	**2 225**	**(2 208)**
Currency forwards	3 217	–	**3 217**	**–**	393	–	**404**	**(11)**
Total derivative instruments, including:			**56 417**	**(560)**			**5 684**	**(112 109)**
Non-current			35 814	–			16	(15 156)
Current			20 603	(560)			5 668	(96 953)

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

Derivative instrument	Methodology of determining fair value hierarchy
IRS	Based on discounted future cash flows accounting for the difference between the forward price (calculated based on zero-coupon interest rate curve) and the transaction price.
Forward currency contracts	Based on discounted future cash flows accounting for the difference between the forward price (calculated based on NBP fixing and the interest rate curve implied by fx swap transactions) and the transaction price.
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.

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

	As at 31 December 2016		As at 31 December 2015	
	Level 1	Level 2	Level 1	Level 2
Assets				
Commodity-related derivatives	16 559	–	2 225	–
Derivate instruments – CCIRS	–	–	–	3 055
Derivative instruments – IRS	–	36 641	–	–
Derivative instruments – currency	–	3 217	–	404
Liabilities				
Commodity-related derivatives	560	–	2 208	–
Currency derivatives	–	–	–	11
Derivate instruments – CCIRS	–	–	–	14 423
Derivate instruments – IRS	–	–	–	95 467

Hedging derivative instruments (subject to hedge accounting) – IRS

Pursuant to a decision of the Financial Risk Management Committee of 30 January 2012, the Company hedged the interest rate risk arising from bonds issued under the Bond Issue Scheme (Tranche A and Tranche C), by entering into an interest rate swap (IRS) transaction for a term of 5 years. The aforementioned transaction was concluded due to fluctuations in the projected future cash flows from interest payments resulting from the issue of bonds in PLN with a floating interest rate based on WIBOR 6M. The Company hedged 80% of such cash flows. The Tranche A transaction was settled at maturity of the instrument, i.e. in December 2015. On 29 February 2016, the Company repurchased and redeemed a portion of Tranche C bonds with the par value of PLN 2 250 000 thousand, which had been hedged using IRS, and at the same time issued bonds with the same par value under an agreement entered into in November 2015, which has been discussed in more detail in Note 33.2 to these consolidated financial statements. In accordance with the dynamic interest rate risk hedging strategy adopted by the Company, whereby cash flows related to the exposure to the WIBOR 6M interest rate risk are the hedged instrument, the Company maintained the hedging relationship for the IRS transactions concluded in March 2012 with respect to the newly issued bonds. As the effectiveness of the hedge was considered high, the transactions were covered by hedge accounting. On 5 July

2016, a portion of the IRS transactions concluded in March 2012 was settled earlier. The amount paid by the Company on that basis was PLN 7 697 thousand. On 12 December 2016, the remaining portion of the IRS transactions concluded in March 2012 was settled at maturity.

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 par 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)

In the first quarter of 2016, the Company closed a transaction involving a coupon cross currency swap (CCIRS), which was not subject to hedge accounting. Following the settlement of the aforesaid transaction in February 2016, the Company received PLN 5 400 thousand. The transaction involved a swap of interest payments on the nominal amount of EUR 168 000 thousand and its original maturity was 15 years. In accordance with the contract, the Company paid interest accrued based on a floating interest rate in PLN and received fixed-rate payments in EUR.

As at 31 December 2016, 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:

- commodity derivatives (futures, forward,) including emission allowance and other commodity purchase and sale transactions;
- FX forward transactions hedging foreign currency cash flows resulting from operations.

46. 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:

Risk exposure	Risk management	Regulation
	Credit risk	
The possibility to incur a loss due to counterparty default on contractual obligations. The credit exposure means the amount that may be lost if a counterparty defaults on its obligations within the agreed time limit (taking into account any security provided by the counterparty).	The credit risk is managed with a view to minimizing the probability of the counterparty default as well as the effect of the credit risk on the achievement of the objectives of the TAURON Group. The credit risk is managed by way of steering the credit risk exposure generated at the time of the entry into contracts by each TAURON Group company. The Group has a decentralized risk management system, but credit risk control, credit risk limits and reporting are managed centrally at the Company's level. The value of the credit risk which the TAURON Group is exposed to is monitored using the Value at Risk method. The Group manages the counterparty credit risk mainly through the application of the following mechanisms and techniques: • evaluation of counterparty's financial standing and assignment of credit limits; • the requirement to provide specific collateral, imposed on clients with a poor financial standing; • standardization of contractual clauses relating to the credit risk and of collateral; • ongoing monitoring of payments and an early collection system; • regular measurement of the credit risk arising from trading operations; • credit risk diversification through a reduction of a high credit exposure both to a single counterparty and a counterparty's related parties.	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 liquidity situation of the TAURON Group is monitored on an ongoing basis for any differences versus the plans, while availability of external sources of funding, whose value exceeds the expected demand in the short term substantially, mitigates the liquidity risk. The Liquidity management policy for the TAURON Group implemented by the Group lays down the principles applicable to determination of the liquidity position of each company and the TAURON Group as a whole, which enables it to secure funds that may be necessary for purposes of closing a liquidity gap if it is identified, both through the allocation of funds among the companies (cash pool mechanism) and through the use of external funding, including overdrafts.	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 key objective of financial risk management is to minimize the sensitivity of the TAURON Group's cash flows to financial risks and to minimize finance costs as well as the costs of hedging with the use of derivative instruments. The policy adopted by the Group has also introduced hedge accounting principles, including a definition of the types of cash flow hedges and the accounting treatment of hedging instruments and hedged items in accordance with the International Financial Reporting Standards. In line with the policy, wherever possible and commercially viable, the TAURON Group uses derivative instruments in the case of which hedge accounting may be applied.	Specific risk management policy in the area of finance for the TAURON Group
	Market risk – price risk	
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 market prices. At the end of the reporting period, the Group identifies the raw material and commodity price risk for its commodity derivative instruments as well as the price risk for its units in investment funds.	The policy has introduced an early warning system as well as a system of limits related to the exposure to risk in each commercial area. Value at Risk is the key operational measure of the market risk used by the TAURON Group. The Company concludes derivative contracts, with underlying instruments being commodities and raw materials. The Group's exposure to the price risk inherent in commodity derivative instruments is related to a risk of changes in the fair value of the said instruments, driven by fluctuations in the prices of the underlying raw materials/commodities. In most cases the Group hedges the risk by entering into offsetting transactions. This way the Group hedges the price risk related to commodity derivative instruments. The risk is limited to open long and short positions concerning a given commodity or raw material.	Commercial risk management policy for the TAURON Group

(in PLN '000)

46.1. 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 exposures related to financial assets of the TAURON Group equals their carrying amounts.

Classes of financial instruments	As at 31 December 2016	As at 31 December 2015
Receivables from clients	1 894 065	1 830 033
Cash and cash equivalents	384 881	364 912
Loans granted	256 117	223 911
Deposits	38 472	39 724
Other financial receivables	56 379	57 250

46.1.1. Credit risk related to receivables from buyers and other financial receivables

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 and other financial receivables has been presented below:

	As at 31 December 2016	As at 31 December 2015
Institutional clients	73.20%	75.39%
Individual clients	26.80%	24.61%
Total	**100%**	**100%**

No material concentration of credit risk related to the core activity occurs in the Group. Amounts due from PSE S.A. represent the key item of receivables, while the share in the balance of receivables from buyers and other financial receivables was 4.64% as at 31 December 2016 and 6.97% as at 31 December 2015.

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 and allowances/write-downs on receivables from buyers and other financial receivables have been presented below.

Allowances/write-downs on receivables from buyers and other financial receivables

	Year ended 31 December 2016	Year ended 31 December 2015
Allowance/write-down at the beginning of period	**(280 898)**	**(282 848)**
Recognised	(99 945)	(106 039)
Utilized	23 334	18 438
Reversed	94 988	89 435
Other movements	(119)	116
Allowance/write-down at the end of period	**(262 640)**	**(280 898)**
Value of item before allowance	2 213 084	2 168 181
Value of item net of allowance (carrying amount)	1 950 444	1 887 283

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

Ageing analysis of receivables from buyers and other financial receivables as at 31 December 2016

	Not past due	Past due					Total
		<30 days	30–90 days	90–180 days	180–360 days	>360 days	
Before allowance/write-down	1 716 782	169 842	45 281	20 079	26 184	234 916	**2 213 084**
Allowance/write-down	(5 715)	(12 265)	(3 697)	(6 357)	(23 112)	(211 494)	**(262 640)**
After allowance/write-down	**1 711 067**	**157 577**	**41 584**	**13 722**	**3 072**	**23 422**	**1 950 444**

(in PLN '000)

Ageing analysis of receivables from buyers and other financial receivables as at 31 December 2015

	Not past due	Past due					Total
		<30 days	30–90 days	90–180 days	180–360 days	>360 days	
Before allowance/write-down	1 643 946	173 145	36 604	22 435	40 656	251 395	**2 168 181**
Allowance/write-down	(1 753)	(3 298)	(3 060)	(8 037)	(29 922)	(234 828)	**(280 898)**
After allowance/write-down	**1 642 193**	**169 847**	**33 544**	**14 398**	**10 734**	**16 567**	**1 887 283**

46.1.2. 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 2016, the share of three banks where the Group's largest cash balances were deposited was 68%.

46.1.3. Credit risk related to loans granted

Loans granted to joint ventures have been recognized under loans granted by the Group. The loans in question had not been overdue as at the end of the reporting period or before. According to the Group, credit risk due to originated loans was insignificant as at the balance sheet date. The key item was a subordinated loan of PLN 213 381 thousand, secured with a blank promissory note and a promissory note agreement.

46.2. 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 possible 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 pool 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 an overdraft made available under the cash pool agreement, the Group is entitled to use foreign currency overdrafts:

- up to USD 2 000 thousand, with the outstanding amount of USD 410 thousand as at the end of the reporting period;
- up to EUR 25 000 thousand, with the outstanding amount of EUR 3 032 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 2016 and 31 December 2015.

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)**

(in PLN '000)

Financial liabilities as at 31 December 2015

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	**8 092 209**	**(9 236 101)**	(2 335 274)	(1 046 480)	(316 908)	(324 752)	(2 596 757)	(2 615 930)
Liabilities to suppliers	**790 706**	**(790 706)**	(790 655)	(29)	(22)	–	–	–
Capital commitments	**767 759**	**(767 759)**	(766 749)	(93)	(613)	(113)	(191)	–
Other financial liabilities	**329 346**	**(329 346)**	(231 380)	(12 332)	(9 184)	(40 662)	(35 647)	(141)
Obligations under finance leases	**46 438**	**(48 625)**	(4 799)	(9 110)	(10 958)	(23 730)	(4)	(24)
Derivative financial liabilities:								
Derivate instruments – IRS	**95 467**	**(96 559)**	–	(96 559)	–	–	–	–
Derivate instruments – CCIRS	**14 423**	**(68 165)**	–	2 749	2 662	988	(4 350)	(70 214)
Derivate instruments – commodity	**2 208**	**(985)**	–	(251)	(734)	–	–	–
Total	**10 138 556**	**(11 338 246)**	**(4 128 857)**	**(1 162 105)**	**(335 757)**	**(388 269)**	**(2 636 949)**	**(2 686 309)**

** Negative values indicate a cash outflow. Estimations of future payments to be made in selected periods may be positive for some derivatives, i.e. they may indicate a cash inflow, but the value resulting from measurement of such instruments during the entire term to maturity is negative (liability).*

As at 31 December 2016, the Group had a contingent liability relating to guarantees issued by The Bank of Tokyo-Mitsubishi UFJ, Ltd. at the request of the Company, totaling PLN 314 486 thousand, where the institutions financing Elektrociepłownia Stalowa Wola S.A. are the beneficiaries. All these bank guarantees are valid from 30 October 2016 to 14 April 2017. The said guarantees constitute contingent liabilities and do not considerably affect the liquidity risk of the Group.

46.3. 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 risk of price change related to units held.

46.3.1. Interest rate risk

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

Due to floating interest rate items the Group is exposed to cash flow changes resulting from interest rate fluctuations. As a result of fixed interest 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 45.3.

The carrying amounts of financial instruments of the Group exposed to the interest rate risk have been presented in the tables below. Except hybrid bonds issued in December 2016, bearing fixed interest rate in the first financing period, other bonds issued by the Parent bear floating interest. As the Company has adopted a dynamic financial risk management strategy where the hedged item is 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 Interest Rate Swap 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 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 (CCIRS)	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**

Financial instruments by interest rate type as at 31 December 2015

Financial instruments	Fixed interest rate	Floating interest rate	Total
Financial assets			
Deposits	–	39 724	**39 724**
Loans granted	–	223 911	**223 911**
Cash and cash equivalents	–	364 912	**364 912**
Derivative instruments (CCIRS)	–	3 055	**3 055**
Financial liabilities			
Bank overdrafts	–	10 206	**10 206**
Preferential loans	–	47 999	**47 999**
Arm's length loans	1 324 191	29 380	**1 353 571**
Bonds issued	3 714 744	2 965 689	**6 680 433**
Derivative instruments (IRS)	95 467	–	**95 467**
Obligations under finance leases	–	46 438	**46 438**
Derivative instruments (CCIRS)	–	14 423	**14 423**

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 of the contract until 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 33.1 and 33.2.

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 behavior 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.

In the interest rate risk sensitivity analysis, the effect of changes in risk factors has been determined for interest income/expense related to financial instruments measured at amortized cost and for the fair value of floating-rate financial instruments measured at fair value 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 2016 and 31 December 2015, its exposure to changes in EURIBOR and LIBOR USD rates was immaterial. 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 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.

For the year ended 31 December 2015

Classes of finacial instruments	31 December 2015		Sensitivity analysis for interest rate risk as at 31 December 2015	
			WIBOR	
	Carrying amount	Value at risk	WIBOR + 66 bp	WIBOR -66 bp
			Profit or loss / other comprehensive income	
Deposits	39 724	39 724	262	(262)
Loans granted	223 911	223 911	1 478	(1 478)
Cash and cash equivalents	364 912	364 912	2 152	(2 152)
Derivatives (assets)	5 684	3 055	(3 360)	3 360
Preferential loans	47 999	47 999	(317)	317
Arm's length loans	1 353 571	29 380	(194)	194
Issued bonds	6 680 433	5 969 017	(39 396)	39 396
Obligations under finance leases	46 438	46 438	(306)	306
Derivatives (liabilities)	112 109	109 890	(24 358)	24 358
Total			**(64 039)**	**64 039**

The exposure to risk as at 31 December 2015 is representative for the Group's exposure to risk during the annual period preceding the aforementioned date.

46.3.2. 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 2016 and in 2015 has been presented below.

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 clients and other financial receivables	1 950 444	1 279	5 658	63 250	10 354	–	–	–	–
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 and other financial liabilities	988 112	4 800	21 234	10 073	1 649	106	444	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 PLN '000)

Currency position as at 31 December 2015

Classes of financial instruments	Total carrying amount in PLN	EUR		CZK		USD	
		in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets							
Receivables from clients and other financial receivables	1 887 283	1 586	6 759	57 819	9 118	96	376
Cash and cash equivalents	364 912	8 184	34 876	16 988	2 679	338	1 317
Derivatives (assets)	5 684	334	1 425	–	–	205	800
Total		**10 104**	**43 060**	**74 807**	**11 797**	**639**	**2 493**
Financial liabilities							
Bank overdrafts	10 206	2 025	8 630	–	–	404	1 576
Issued bonds	6 680 433	166 941	711 417	–	–	–	–
Liabilities to suppliers and other financial liabilities	947 946	3 173	13 523	13 139	2 072	1	4
Derivatives (liabilities)	112 109	242	1 032	70	11	301	1 176
Total		**172 381**	**734 602**	**13 209**	**2 083**	**706**	**2 756**
Net currency position		**(162 277)**	**(691 542)**	**61 598**	**9 714**	**(67)**	**(263)**

In 2016 and in 2015, 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 the end of the reporting period, the Group presented an asset from valuation of FX forward contracts in the amount of PLN 3 217 thousand.

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 behavior 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.

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 clients and other financial receivables	1 950 444	16 012	441	(441)	1 034	(1 034)	–	–	–	–
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 and other financial liabilities	988 112	23 337	(1 657)	1 657	(165)	165	(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 hybrid bonds issued by the Company in December 2016 with the euro as the issue and repayment currency, which has been discussed in more detail in Note 33.2 to these consolidated financial statements.

(in PLN '000)

For the year ended 31 December 2015

Classes of finacial instruments	31 December 2015		Sensitivity analysis for currency risk as at 31 December 2015					
			EUR/PLN		CZK/PLN		USD/PLN	
	Carrying amount	Value at risk	exchange rate EUR/PLN +7.15%	exchange rate EUR/PLN -7.15%	exchange rate CZK/PLN +8.22%	exchange rate CZK/PLN -8.22%	exchange rate USD/PLN +11.43%	exchange rate USD/PLN -11.43%
			Profit or loss / other comprehensive income		*Profit or loss / other comprehensive income*		*Profit or loss / other comprehensive income*	
Receivables from clients and other financial receivables	1 887 283	16 253	483	(483)	749	(749)	43	(43)
Cash and cash equivalents	364 912	38 872	2 494	(2 494)	220	(220)	151	(151)
Derivatives (assets)	5 684	5 684	3 078	(3 078)	–	–	91	(91)
Overdrafts	10 206	10 206	(617)	617	–	–	(180)	180
Bonds issued	6 680 433	711 417	(50 866)	50 866	–	–	–	–
Liabilities to suppliers and other financial liabilities	947 946	15 599	(966)	966	(170)	170	–	–
Derivatives (liabilities)	112 109	16 642	21 587	(21 587)	(1)	1	(135)	135
Total			**(24 807)**	**24 807**	**798**	**(798)**	**(30)**	**30**

The exposure to risk as at 31 December 2015 is representative for the Group's exposure to risk during the annual period preceding the aforementioned date.

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

As at 31 December 2016, open positions included forwards and futures for emission allowances and a futures contract for gas. As at 31 December 2016, the total carrying amount of all derivative instruments related to emission allowances was PLN 15 012 thousand (the asset item of PLN 15 550 thousand and the liability item of PLN 538 thousand) and of the derivative contract for gas: PLN 593 thousand (the asset item) and as at 31 December 2015, the total carrying amount of all derivative instruments related to emission allowances was PLN 433 thousand (the asset item of PLN 1 425 thousand and the liability item of PLN 992 thousand) and of the derivative contract for gas: PLN 40 thousand (the liability item).

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 analyze the effect of changes in risks on the Group's financial performance.

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 Jan 17	6.54	10 140	–	10.14	(21 421)	4.12	14 400
EUA Apr 17	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**

For the year ended 31 December 2015

	Carrying amount as at 31 December 2015			Increase		Decrease	
	price (EUR)	Assets	Liabilities	price (EUR)	Impact on profit (loss)	price (EUR)	Impact on profit (loss)
Derivative instruments – commodity (emission allowances)	8.25–8.29	1 425	992	8.53–8.57	(122)	4.83–4.85	1 490

(in PLN '000)

46.3.4. Unit price risk

As at 31 December 2016, the Group held units in investment funds with the carrying amount of PLN 25 316 thousand. As they are measured at fair value at the end of the reporting period, they are exposed to the price risk.

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 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			
UniKorona Pieniężny/UniFundusze FIO	2 519	2 519	25	(25)		
UniWIBID Plus/UniFundusze SFIO	22 797	22 797			160	(160)
Total	**25 316**	**25 316**	**25**	**(25)**	**160**	**(160)**

47. Operational risk

Commercial operational risk is managed at the level of the TAURON Group, which has been discussed in more detail in Section 3 of the Management Board's Report on the Activities of the TAURON Polska Energia S.A. Capital Group for the 2016 financial year. The Company manages its commercial risk following the Commercial risk management policy developed and adopted in the TAURON Group, which introduces an early warning system and a system of limiting risk exposure in each trade area.

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

Fuel type	Unit	2016		2015	
		Volume	Purchase cost	Volume	Purchase cost
Coal	tonne	3 522 216	608 619	4 821 241	947 360
Gas	MWh	2 928 639	241 432	1 235 889	122 189
Electricity	MWh	33 138 013	5 602 272	33 993 308	5 703 158
Heat energy	GJ	6 095 393	232 603	6 028 877	227 926
Total			**6 684 926**		**7 000 633**

(in PLN '000)

OTHER INFORMATION

48. Contingent liabilities

Item	Description
Use of real estate without contract	Entities of the Group do not hold legal titles to all plots of land where distribution networks, heating installation and the related devices are located. 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 their detailed records do not exist. 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 92 143 thousand (Note 37).
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 Energy Regulatory Office (ERO). At present, the case is pending at District Court in Warsaw. Based on a decision of 12 October 2001, the President of the Energy Regulatory Office (ERO) ordered GZE to resume electricity supplies to Huta (suspended on 11 October 2001 since Huta had failed to pay 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 judgement of the Court of Appeals in Warsaw, which was dismissed by the judgement of the Supreme Court dated 10 May 2007. On 15 November 2001 (following the above decision issued by the President of ERO 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 Huta has 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 ERO 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 judgement 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 judgement of the Regional Court and remanded the case for re-examination by the latter. The first hearing before the first instance court was held on 27 November 2012. In May 2015, a court expert prepared an opinion on correctness of settlements between the parties to the dispute. On 30 June 2015, TAURON Polska Energia S.A. lodged complaints against the opinion in question. Complaints against the opinion were also filed by Huta and the State Treasury. In its decision dated 16 September 2015 the court admitted an additional court expert's opinion concerning charges levelled by the parties as evidence. After the issue of the decision, the Company tried to change the proceeding concept adopted by the Court stating that taking evidence from a court expert opinion is unacceptable. Finally, the Court commissioned an additional opinion to be prepared by the court expert. On 5 September 2016, the additional opinion by the court expert was delivered to the Company. The Company filed charges against the said opinion on 12 and 19 September 2016. Charges were also brought by the State Treasury and Huta. The next hearing is to be held on 24 March 2017 in order to continue the questioning of the court expert with respect to the aforesaid opinions, which began during the hearing conducted on 21 December 2016. 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.
Litigation related to termination of long-term contracts	On 18 March 2015 Polska Energia – Pierwsza Kompania Handlowa Sp. z o.o. in liquidation terminated long-term agreements regarding purchase of power and property rights from windfarms. Court proceedings were instigated against the Company to consider the termination notices invalid. In 2016 the claims against the company were changed through the incorporation of claims for damages related to termination of the agreements in the total amount of ca. PLN 40 074 thousand. Since the court proceedings regarding the above issues are pending, the final amount of possible financial effects on the Company and the Group cannot be reliably estimated. In light of the current status of the proceedings and the related circumstances, the Group believes that the probability of losing the cases both in terms of the termination notes being declared invalid and of securing both non-monetary claims and the claims for damages does not exceed 50%. Therefore, no provision for the related costs has been recognized.

(in PLN '000)

Item	Description
Claim filed by ENEA S.A.	The claim filed by ENEA S.A. ("ENEA") to the District Court in Katowice regards the payment of PLN 17 086 thousand with statutory interest calculated from 31 March 2015 until the payment date for unjust enrichment of the Company arising from settlement of balances on the Balancing Market performed with Polskie Sieci Elektroenergetyczne S.A. in the period from January to December 2012. The claim was delivered to the Company on 11 January 2016. As stated by ENEA, the improper settlement was caused by inconsistency in measurement data collected by ENEA Operator Sp. z o.o. (as the Distribution System Operator, DSO) and made available to the Balancing Market participants (PSE S.A., ENEA S.A. and the Company) for the settlement purposes. The error resulted in PSE S.A. assigning to ENEA S.A. (as the official seller in the distribution area of ENEA Operator Sp. z o.o.) the amount of consumed power that should have been assigned to the Company (as the entity in charge of trade balances of power sellers operating in the distribution area of ENEA Operator Sp. z o.o.). The dispute concerns the fact that pursuant to the Power Transmission Grid Traffic and Operation Instruction (IRiESP) binding all participants of the Balancing Market, settlements regarding trade balances for a given period may be adjusted within 2 months, 4 months and 15 months after the settlement period. According to IRiESP, after 15 months the settlements become final. ENEA Operator Sp. z o.o. informed TAURON Polska Energia S.A. about the necessity to adjust measurement data and the entire settlement after the permitted adjustment period. Therefore, settlements between PSE S.A. and ENEA S.A. and between PSE S.A. and the Company have not been adjusted. TAURON Polska Energia S.A. responded to the claim with a series of charges. The Court obliged ENEA to reply to the response, which was done on 5 April 2016. On 20 June 2016, TAURON Polska Energia S.A. filed a petition for inviting ENEA Operator Sp. z o.o. to take part in the litigation. The Court also admitted evidence from the witnesses' testimonies. On 4 July 2016 TAURON Polska Energia S.A. filed a process document with the court. The last hearing was conducted on 6 March 2017. During that hearing the Court following the motion filed by ENEA S.A. (expressed in its pleading of 8 December 2016) ruled to summon before the Court (in accordance with Article 194.1 of the Code of Civil Procedure) seven sellers for which TARON 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 case is pending. The hearing was deferred with the deadline ex officio. No provision has been recognized as the Company believes that the risk of losing the case is below 50%.
Amount	The claim regards the payment of PLN 17 086 thousand.
Registered pledges and a financial pledge on shares of TAMEH HOLDING Sp. z o.o	On 15 May 2015 TAURON Polska Energia S.A. 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, constituting ca. 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. Moreover, the Company assigned the rights to dividend and other payments. Agreement on establishing 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. 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 a release by the pledgee, not later than on 31 December 2028. On 15 September 2016, Annex 1 was executed to the aforesaid agreement, whereby the maximum amount of the collateral was changed to PLN 1 370 000 thousand.
Amount	As at 31 December 2016 the carrying amount of investments in joint venture recognized using the equity method in the TAMEH HOLDING Sp. z o.o. capital group was PLN 442 869 thousand.
Bank guarantees issued at the request of TAURON Polska Energia S.A. to secure the payment of liabilities of a joint venture	Following the entry into agreements setting out the terms of further implementation of the gas and steam unit construction project in Elektrociepłownia Stalowa Wola S.A. on 27 October 2016, and with a view to enforcing the standstill agreement entered into by the Company, Elektrociepłownia Stalowa Wola S.A., PGNiG S.A., the European Investment Bank, the European Bank for Reconstruction and Development and Bank Polska Kasa Opieki S.A. aimed to ensure that the financing institutions will refrain from accelerating the loans granted to the company and satisfying their claims through the use of the related collateral, at the request of the Company The Bank of Tokyo-Mitsubishi UFJ, Ltd. issued three bank guarantees for: – the European Investment Bank – in the amount of PLN 156 000 thousand; – the European Bank for Reconstruction and Development – in the amount of PLN 83 494 thousand; – Bank Polska Kasa Opieki S.A. – in the amount of PLN 74 992 thousand. All these bank guarantees are valid from 30 October 2016 to 14 April 2017. A notarized declaration of voluntary submission to enforcement is a security under the Agreement.
Amount	The total value of guarantees issued PLN 314 486 thousand.

(in PLN '000)

Item	Description
Administrative proceedings instigated by the President of the Office for Competition and Consumer Protection (UOKiK)	President of UOKiK instigated the following procedures against the Sales segment companies: – 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 committed to discontinue practices violating 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 requested the company to demonstrate whether the practices have been discontinued. The company responded to the request in February 2016 informing that the practices have been discontinued and motioned for a decision not to charge a fine. No such decision had been issued by the date of the financial statements. – Under a decision of 19 December 2014 anti-trust proceedings were instigated regarding the alleged abuse of the dominant position by TAURON Sprzedaż Sp. z o.o. and TAURON Sprzedaż GZE Sp. z o.o. on the reserve electricity distribution market. In 2015 the companies applied for a decision requesting the entities to discontinue activities violating the Act on competition and consumer protection and to take steps preventing the alleged violations. In July 2015 the President of the Office for Competition and Consumer Protection, issued a decision requesting the entities to take appropriate steps to prevent the alleged infringements within four months from the date when the decision becomes final and binding. The entities were obliged to report on fulfilling the obligations within 6 months from the date the decision becomes final and binding. On 22 February 2016 the companies informed the office that the obligation had been fulfilled and filed the required reports. – 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. By a decision of 15 October 2015 the President of UOKiK instigated anti-trust proceedings. On 1 February 2016 UOKiK accepted the company's decision regarding presentation of a specific commitment. On 24 August 2016, the President of UOKiK issued a decision obliging the company to fulfil the obligation to take steps to prevent the alleged violations through the employment of specific measures within two months of the said decision becoming final. On 29 September 2016, the company filed an appeal against the decision with the Court of Competition and Consumer Protection. On 2 December 2016, the President of the Office of Competition and Consumer Protection issued a decision amending the statement of reasons supporting the previous decision. The companies do not recognize provisions for fines related to the above proceedings, since their management boards believe the risk of losing the cases and paying the fines is low.
Explanatory proceedings instigated by the President of UOKiK	Explanatory proceedings have been instigated against companies from the Sales segment to preliminarily determine whether their actions have been in breach of the Act on competition and consumer protection. The companies provided requested documents and explanations and responded to statements included in the letters of UOKiK. The companies' Management believe that, considering the explanatory nature of the proceedings instigated, the probability of an unfavorable outcome of the above-mentioned cases is low; hence no provision has been recognized for these events.
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 license. The company does not recognize a provision for potential fines related to the aforesaid proceedings, as the Management Board is of the opinion that the risk of an unfavorable ruling and imposition of a fine is low.

49. Contingent assets and liabilities related to tax returns

Tax returns may be inspected within five years, starting from the end of the year when the tax was paid. As a result of such inspections the Group's tax settlements may be increased by additional tax liabilities. According to the Group, as at 31 December 2016 appropriate provisions had been recognized for identified and measurable tax risk.

As at the date of the consolidated financial statements, the following proceedings regarding settlements under public law were pending in the Capital Group companies:

(in PLN '000)

Item	Description
Excise duty	In view of the differences between the Polish and EU regulations concerning excise duty on electricity, following the judgment of the European Court of Justice ("ECJ") in Luksemburg of 12 February 2009 power and heat and power plants from the TAURON Capital Group filed tax return correction and applications to acknowledge excise tax excess payment for the years 2006–2008 and for January and February 2009. In the judgment in question ECJ conceded that Polish regulations determining the timing of recognition for excise tax purposes were not adjusted to the requirements of the Energy Directive neither before nor after the transition period. Proceedings concerning individual companies from the TAURON Capital Group (TAURON Wytwarzanie S.A. and TAURON Ciepło Sp. z o.o.) have been carried out before competent tax authorities and Administrative Courts. As the final outcome of this dispute is highly unpredictable, the Group has not recognized any effects of possible reimbursement of excise duty overpayment or claims and possible claims of electricity buyers in these consolidated financial statements. On 5 January 2017 and 23 January 2017 unfavorable decisions were issued by the Regional Administrative Court in Gliwice with respect to another application for ascertainment of overpayment for the period from July to December 2007. The Company will decide on the further course of the proceedings.
Amount	The overpaid amounts claimed by the Group approximate PLN 908 500 thousand.
Income tax – an increase in tax-deductible costs by the amount of component repair cost	In accordance with the tax ruling, companies in the Tax Capital Group ("TCG") (TAURON Wytwarzanie S.A. and TAURON Ekoenergia Sp. z o.o.) expensed costs incurred on component repairs over time. At the same time the Company, representing the TCG, appealed against the tax ruling, as in its opinion the repairs in question should be expensed when incurred, on one-off basis, irrespective of the way they are accounted for in the accounting records. Such position was confirmed by the Regional Administrative Court in Gliwice in its decision dated 18 September 2014. On 30 December 2014 the Company filed an application to acknowledge tax excess payment and a tax return correction for 2013, where the component repairs were recognized in tax-deductible expense on one-off basis. At the same time, an impairment loss for income tax receivable has been recognized with relation to the excess payment. In 2015, TCG received an overpayment refund of PLN 22 250 thousand. The impairment loss has been reversed, thus reducing the tax expense for 2015. Following a cassation appeal filed by the Minister of Finance the case was dismissed by the Supreme Administrative Court on 24 January 2017, which supported the position taken by the Company.
Amount	The refunded overpayment of PLN 22 250 thousand.
Real estate tax	There are different interpretations regarding the approach to real estate tax on electricity generation and transmission facilities and on equipment used in underground excavations. Since the tax is imposed on the local self-government level, there is no unified approach and in several cases, the tax base calculation has been questioned. Depending on court decisions and possible amendments to relevant regulations, the status of real estate tax on electricity generation and transmission facilities, as well as on underground excavations, may change in future.
Amount	As at the end of the reporting period, provisions were recognized for costs of disputes regarding real estate tax and for the related business risk (totaling PLN 35 008 thousand).

50. Collateral against liabilities

The Group uses various forms of collateral against 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.

The carrying amounts of assets pledged as collateral for the payment of liabilities at the end of each reporting period have been presented in the table below.

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

	As at 31 December 2016	As at 31 December 2015
Real estate	81 363	82 250
Plant and machinery	14 059	614
Cash	13 740	22 067
Total	**109 162**	**104 931**

Other forms of collateral

The Group also uses other forms of collateral to secure payment of liabilities, of which the most significant ones as at 31 December 2016 concerned the following contracts concluded by the Parent:

(in PLN '000)

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 – as regards Tranche C (repaid), Tranche D and Tranche E (not disbursed)
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
Framework bank guarantee agreement with PKO Bank Polski S.A. The bank guarantee limit securing transactions may be used by the Company and the TAURON Group companies (limit amounted to PLN 100 000 thousand).	authorization to debit the bank account maintained by PKO Bank Polski S.A.	up to PLN 125 000 thousand
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
overdraft agreement with Bank Gospodarstwa Krajowego (in EUR, up to EUR 25 000 thousand)	authorization to debit the bank account maintained by Bank Gospodarstwa Krajowego	up to PLN 110 600 thousand (EUR 25 000 thousand)
	declaration of submission to enforcement	up to PLN 221 200 thousand (EUR 50 000 thousand) valid until 31 December 2019
overdraft agreement with mBank (in USD, up to USD 2 000 thousand)	declaration of submission to enforcement	up to PLN 12 538 thousand (USD 3 000 thousand) valid until 31 March 2019

Other forms of collateral against liabilities of the Group

As at 31 December 2016, other significant collateral for the liabilities of the TAURON Group included:

- Blank promissory notes

Agreement/transaction secured by blank promissory notes	Capital Group company that has issued a blank promissory note	As at 31 December 2016
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.	170 888
Performance bonds related to co-funding agreements concluded with the National Fund for Environmental Protection and Water Management	TAURON Ciepło Sp. z o.o.	87 251
Agreements for connecting to the industrial network, agreements for power transmission services and agreements for partial loan cancelling concluded with the National Fund for Environmental Protection and Water Management	TAURON Wytwarzanie S.A.	66 844

(in PLN '000)

- Collateral under finance lease agreements

Finance lease agreement	Lessee	Carrying amount of the leased asset as at 31 December 2016	Collateral
Leaseback agreement concerning real estate, plant and machinery	TAURON Ciepło Sp. z o.o.	22 857	Blank promissory note for PLN 92 215 thousand. This agreement is additionally secured by the assignment of receivables, assignment of rights under insurance policies, mortgage on real estate, plant and machinery and authorization to debit bank accounts.
Finance lease agreement concerning real estate in Katowice	TAURON Polska Energia S.A.	25 318	The agreement is collateralized by two blank promissory notes, assignment of receivables and authorization to debit a bank account.

- The Company granted a corporate guarantee to TAURON Sweden Energy AB (publ), a subsidiary, to secure bonds issued by the entity in December 2014. The guarantee is valid in the entire bond period, i.e. until 3 December 2029, and amounts to EUR 168 000 thousand.
- 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 the Commodity Clearing House. As at 31 December 2016, the guarantees issued by the bank totaled PLN 100 000 thousand and were valid until January 2017.
- Under the bank guarantee agreement made with CaixaBank S.A. (Spółka Akcyjna) Branch in Poland ("CaixaBank S.A."), 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. totaling PLN 263 thousand and to secure the transactions performed by the Company for GAZ-SYSTEM S.A. up to PLN 3 664 thousand, valid until 30 November 2017.
- Under the framework agreement for bank guarantees entered into with PKO Bank Polski S.A., at the request of the Company the bank issued bank guarantees securing liabilities of TAURON Polska Energia S.A. subsidiaries totaling PLN 1 691 thousand.
- Collateral for transactions on the Polish Power Exchange.

  In the year ended 31 December 2016, emission allowances held by the Group were frozen in the National Registry of Allowances in order to collateralize transactions concluded at Polish Power Exchange. The alienation agreements expired during 2016.

Mining companies from the Capital Group have established a Mine Decommissioning Fund to ensure funds for covering future decommissioning costs. Detailed information is provided in Note 35.1.

51. Related-party disclosures

51.1. Transactions with joint ventures

The Group has the following joint ventures: Elektrociepłownia Stalowa Wola S.A., Elektrownia Blachownia Nowa Sp. z o.o. in liquidation and TAMEH HOLDING Sp. z o.o. with subsidiaries, which have 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 2016	Year ended 31 December 2015
Revenue	117 451	58 013
Costs	(46 321)	(36 002)

The key income item arises from transactions with the TAMEH HOLDING Sp. z o.o. Capital Group, a joint venture. In the year ended 31 December 2016 and 31 December 2015, transactions with the joint venture amounted to PLN 106 703 thousand and PLN 48 483 thousand, respectively.

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 PLN '000)

In relation to agreements entered into with a joint venture, Elektrociepłownia Stalowa Wola S.A., in the year ended 31 December 2015, the Company recognized provisions for onerous contracts totaling PLN 182 877 thousand. In the year ended 31 December 2016, the Company remeasured the provisions due to the unwinding of discount as at the end of the reporting period by the total amount of PLN 11 502 thousand and recognized additional provisions of PLN 4 465 thousand net, which has been discussed in more detail in Note 35 to these consolidated financial statements.

51.2. Transactions with State Treasury companies

The State Treasury of the Republic of Poland is the Group's major shareholder; therefore 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 expenses

	Year ended 31 December 2016	Year ended 31 December 2015
Revenue	2 293 142	2 558 894
Costs	(2 527 466)	(3 018 993)

Receivables and liabilities

	As at 31 December 2016	As at 31 December 2015
Receivables	356 595	367 207
Payables	298 786	270 429

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. As at 31 December 2015, receivables comprised advance payments totaling PLN 128 650 thousand, including advance payments for deliveries of coal of PLN 124 996 thousand and advance payments for purchases of fixed assets of PLN 3 649 thousand.

In the year ended 31 December 2016, the Polish National Foundation was established by 17 founders being key State Treasury companies. The Company is among the founders. As a result of its declaration to make contributions to the initial capital of the Polish National Foundation and the commitment to make annual contributions to be used for purposes of its statutory activities for a period of 10 years, the Company recognized a liability and other operating expenses of PLN 32 500 thousand.

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.

In the year ended 31 December 2015, KGHM Polska Miedź S.A., PSE S.A., PKP Energetyka S.A., Jastrzębska Spółka Węglowa S.A. and Kompania Węglowa S.A. 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 79% of revenue from transactions with State Treasury companies. The largest purchase transactions were concluded by the Group with PSE S.A. and Kompania Węglowa S.A. Purchases from these contracting parties accounted for 80% of the value of purchases from State Treasury companies during the year ended 31 December 2015.

The Capital Group enters into material transactions in the energy market through Izba Rozliczeniowa Giełd Towarowych S.A. As such entities are 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.

(in PLN '000)

51.3. 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 2016 and in the comparative period has been presented in the table below.

	Year ended 31 December 2016		Year ended 31 December 2015	
	Parent	Subsidiaries	Parent	Subsidiaries
Board of Directors	**12 858**	**24 604**	**11 225**	**22 152**
Short-term employee benefits (salaries and surcharges)	6 367	19 051	7 333	19 640
Post-employment benefits	–	–	–	599
Employment termination benefits	5 806	4 990	2 820	1 544
Other	685	563	1 072	369
Supervisory Board	**1 159**	**641**	**1 118**	**990**
Short-term employee benefits (salaries and surcharges)	1 159	612	1 118	927
Other	–	29	–	63
Other key management personnel	**13 284**	**39 375**	**14 588**	**40 541**
Short-term employee benefits (salaries and surcharges)	10 554	38 242	12 392	38 580
Jubilee bonuses	–	391	–	1 001
Post-employment benefits	–	16	507	607
Employment termination benefits	1 911	511	627	125
Other	819	215	1 062	228
Total	**27 301**	**64 620**	**26 931**	**63 683**

As regards termination benefits paid to members of the Management Board, as presented in the table above, the amount of PLN 4 585 thousand was accounted for as the use of a provision recognized as at 31 December 2015 by the Parent and the amount of PLN 1 435 thousand as the use of provisions recognized as at 31 December 2015 by the subsidiaries.

Additionally, in the year ended 31 December 2016, the Group companies recognized provisions for termination benefits payable to members of the Management Board, in the amount of PLN 2 592 thousand. The aforesaid benefits have not become due yet. The table does not present the aforesaid costs of recognition of provisions which have not been paid.

52. 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 9 588.83 square meters and in 2016, the average monthly rental fee with the service charges was PLN 510 thousand.

Moreover, TAURON Wydobycie S.A. uses mining machines and equipment based on lease agreements. The annual cost of lease in the years 2016 and 2015 reached PLN 34 027 thousand and PLN 28 987 thousand, respectively.

53. 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 specific 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 2016, 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.

(in PLN '000)

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 Company 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.

	Year ended 31 December 2016	Year ended 31 December 2015 (*restated figures*)
Loans and borrowings	1 070 162	1 223 814
Bonds*	6 826 751	3 666 590
Finance lease	23 546	33 723
Non-current debt liabilities	**7 920 459**	**4 924 127**
Loans and borrowings	193 391	187 962
Bonds*	13 354	3 013 843
Finance lease	11 302	12 715
Short-term debt liabilities	**218 047**	**3 214 520**
Total debt	**8 138 506**	**8 138 647**
Cash and cash equivalents	384 881	364 912
Short-term investments maturing within one year	50 023	9 772
Net debt	**7 703 602**	**7 763 963**
EBITDA	**3 336 814**	**3 523 228**
Operating profit (loss)	801 522	(1 901 216)
Depreciation/amortization	(1 668 726)	(1 832 690)
Impairment	(866 566)	(3 591 754)
Net debt / EBITDA	**2.3**	**2.2**

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

(in PLN '000)

Change in the balance of debt has been presented below.

	Debt liabilities
As at 1 January 2015	**8 113 766**
Proceeds arising from debt taken out	**604 494**
financing received	605 000
transaction costs	(506)
Interest accrued	**344 378**
charged to profit or loss	275 218
capitalized to property, plant and equipment and intangible assets	69 160
Debt related payments	**(950 476)**
principal repaid	(605 011)
interest paid	(276 305)
interest paid, capitalized to investment projects	(69 160)
Change in the balance of overdraft facility and cash pooling	**23 184**
Change in debt measurement	**3 143**
Other non-monetary changes	**158**
As at 31 December 2015	**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**

54. 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 2016 financial year (Section 4.12).

55. Events after the end of the reporting period

Termination of agreements by TAURON Sprzedaż Sp. z o.o., a subsidiary

On 28 February 2017, TAURON Sprzedaż Sp. zo.o., a subsidiary, submitted termination notices regarding long-term agreements for purchase of property rights resulting from green certificates. The agreements have been terminated with immediate effect, since the parties thereto failed to reach an agreement under contract renegotiation procedures provided for therein. The financial effect of the termination for TAURON Sprzedaż Sp. z o.o. is avoiding the loss calculated as a difference between contractual and market prices of green certificates. The estimated amount of the net contractual loss on the performance of these agreements until the end of their assumed term (i.e. by 2023) approximated PLN 343 million, including current market prices of green certificates. The total value of contractual liabilities of the company estimated for the years 2017–2023 approximates PLN 417 million. The call to renegotiate the agreements resulted from amendments to the law, which could not have been predicted by the company despite taking due care, and which affected the supply of green certificates and resulted in a significant and long-lasting decrease in their prices, at the same time dramatically changing the system of subsidies to power generation from renewable sources. The system had been the key reason underlying the conclusion of these agreements. Its modification constitutes a substantial change in legal environment and exerts a direct and decisive impact on their profitability.

Annulment of the liqudation of the company Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.

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 annulment of the liqudation of the company.

These consolidated financial statements of the TAURON Polska Energia S.A. Capital Group, prepared for the year ended 31 December 2016 in accordance with the International Financial Reporting Standards, as endorsed by the European Union, have been presented on 100 consecutive pages.

Management Board of the Company

Katowice, 13 March 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 ....

Piotr Zawistowski – Vice-President of the Management Board ....

Oliwia Tokarczyk – Executive Director for Taxes and Accounting ....

TAURON
POLSKA ENERGIA

REPORT OF THE MANAGEMENT BOARD ON OPERATIONS OF TAURON POLSKA ENERGIA S.A. CAPITAL GROUP FOR THE FINANCIAL YEAR 2016

MARCH 2017

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1. TAURON CAPITAL GROUP

1.1. Basic Information on TAURON Capital Group

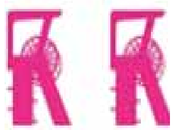
TAURON Polska Energia S.A. Capital Group (TAURON Capital Group) is a vertically integrated energy group located in the southern part of Poland. TAURON Capital Group conducts its operations in all key segments of the energy market (excluding electricity transmission which is the sole responsibility of the Transmission System Operator (TSO)), i.e. in the area of coal mining, generation, distribution as well as trading in electricity and heat.

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 77% used within TAURON Capital Group, and 23% sold to external clients
- EBITDA of the segment for 2016: PLN (82) million

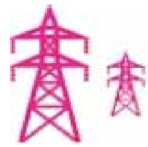
GENERATION

the second 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 143 MW_e
- 816 km of heat networks
- 16.8 TWh of gross electricity output, including 0.5 TWh from biomass
- 0.8 TWh of gross electricity production from wind and hydroelectric sources
- 11.5 PJ of heat production
- EBITDA of the segment for 2016: PLN 545 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
- 49.7 TWh of electricity distributed
- EBITDA of the segment for 2016: PLN 2,395 million

SALES

the second largest electricity supplier in Poland

- approx. 5.3 million clients
- 32 TWh of electricity retail sales
- EBITDA of the segment for 2016: PLN 490 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 2016: PLN 115 million

1.2. Segments of activity

In accordance with the *Business Model of TAURON Group* (Business Model), the operating activity is carried out in entities defined as: Corporate Centre, seven Business Areas, i.e. Trade, Mining, Generation, Renewable Energy Sources (RES), Heat, Distribution and Sales as well as Centres of Common Services (CUW). Detailed information concerning the aforementioned issues is provided in item 1.6. of this report.

For the needs of reporting the results of TAURON Capital Group, activities of TAURON Capital were assigned to the following five Segments hereinafter also referred to as Areas:

Mining Segment, comprising mainly mining, preparation and sales of hard coal in Poland – the activity provided by TAURON Wydobycie S.A. (TAURON Wydobycie). As of 1 January 2016 the Segment also comprises the company Nowe Brzeszcze Grupa TAURON sp. z o.o. (Nowe Brzeszcze GT), established as a result of acquisition of assets of a designated part of the Mining Plant (ZG) in Brzeszcze, as an organised part of the enterprise.

Generation Segment, comprising mainly generation of electricity in conventional sources, including co-generation, as well as generation of electricity from renewable energy sources, including burning and co-burning of biomass, and in hydroelectric power plants and wind farms. The Segment also comprises generation, distribution and sales of heat. Operations in this Segment are carried out by TAURON Wytwarzanie S.A. (TAURON Wytwarzanie), TAURON Ciepło sp. z o.o. (TAURON Ciepło) and TAURON EKOENERGIA sp. z o.o. (TAURON EKOENERGIA). In this Segment TAURON Serwis sp. z o.o. is also included. (TAURON Serwis), dealing mainly with repairs of generation installations.

Distribution Segment, comprising the distribution of electricity with the use of distribution grids located in southern Poland. The activities are conducted by TAURON Dystrybucja S.A. (TAURON Dystrybucja). This Segment also comprises the following companies: TAURON Dystrybucja Serwis S.A. (TAURON Dystrybucja Serwis) and TAURON Dystrybucja Pomiary sp. z o.o. (TAURON Dystrybucja Pomiary).

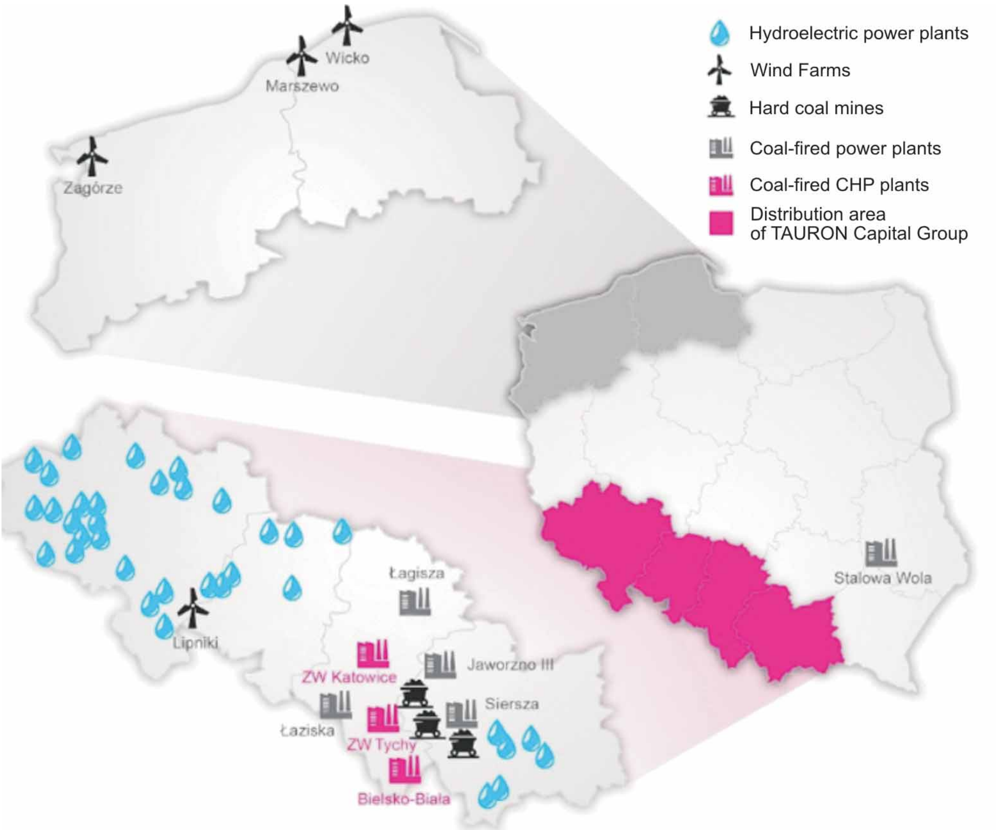
Sales Segment, comprising sales of electricity to end-customers and wholesale trading of electricity, as well as trade and management of CO_2 emission allowances, property rights arising from certificates of origin and fuels. Operations in this Segment are conducted by the following companies: TAURON 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 Segment, comprising activity in the scope of customer service for clients of TAURON Capital Group and provision of support services for companies of TAURON Capital Group in the scope of accounting and ICT, provided by TAURON Obsługa Klienta sp. z o.o. company (TAURON Obsługa Klienta), as well as extraction of stone, including limestone, for the needs of energy industry, metallurgy, construction and road building and production of sorbing agents for installations of flue gas desulphurisation using the wet method and for application in fluidized bed boilers – the activity carried out by Kopalnia Wapienia "Czatkowice" sp. z o.o. company (KW Czatkowice). This Segment also comprises the following companies: TAURON Sweden Energy AB (publ) (TAURON Sweden Energy), dealing with financial activities, Biomasa Grupa TAURON sp. z o.o. (Biomasa Grupa TAURON) dealing mainly with acquisition, transport and processing of biomass, KOMFORT-ZET sp. z o.o. (KOMFORT-ZET), dealing mainly with real estate administration as well as technical service of vehicles and Polska Energia – Pierwsza Kompania Handlowa sp. z o. o. in liquidation (PEPKH in liquidation).

TAURON Capital Group conducts its operations and acquires its revenues mainly from sales and distribution of electricity and heat, generation of electricity and heat, as well as from sales of hard coal.

The figure below shows the location of key assets of TAURON Capital Group as well as the distribution area where TAURON Dystrybucja acts as the Distribution System Operator (DSO).

Figure no. 2 Location of key assets of TAURON Capital Group



1.3. Organisation and structure of TAURON Capital Group

The parent entity, TAURON Polska Energia S.A. was established on 6 December 2006 under the implementation of the *Programme for Power Engineering.* 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 S.A.), ENION S.A. with its seat in Kraków (currently: TAURON Dystrybucja S.A.) and Elektrownia Stalowa Wola S.A. with its seat in Stalowa Wola (currently: TAURON Wytwarzanie S.A.). The Company was registered in the National Court Register on 8 January 2007 under the enterprise name: Energetyka Południe S.A. The change of the Company enterprise to its current name, i.e. TAURON Polska Energia S.A., was registered on 16 November 2007.

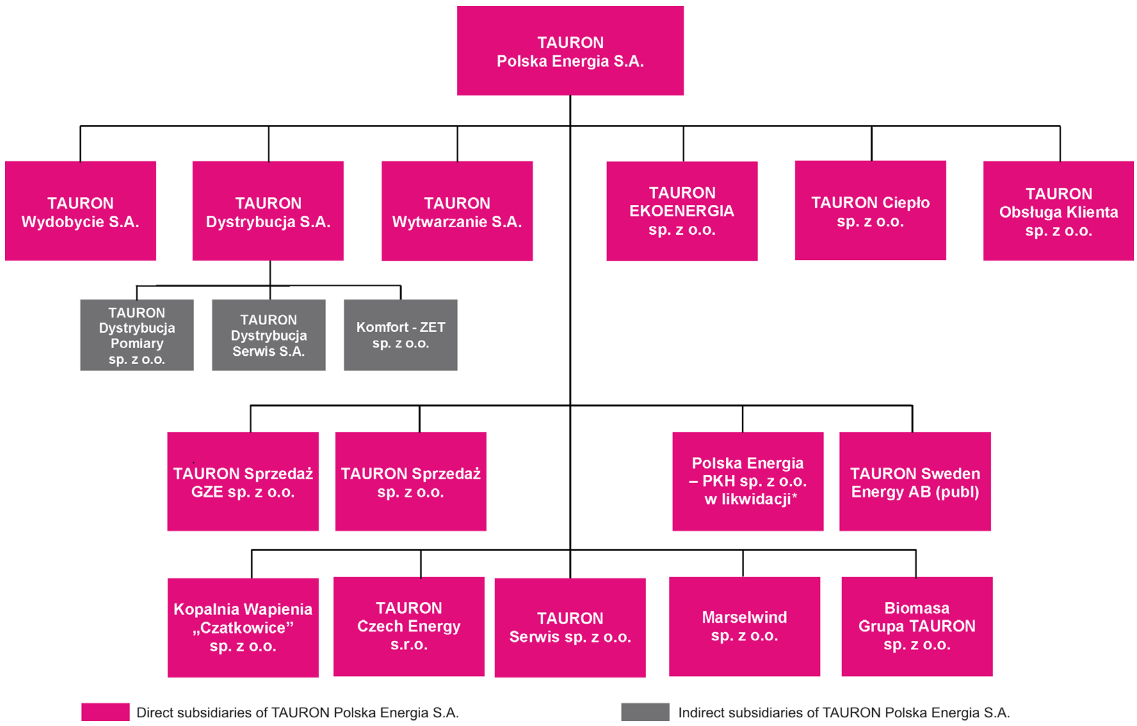
The Company does not hold any branches (plants).

As of 31 December 2016, the key companies of TAURON Capital Group, besides the parent company, TAURON, included 18 subsidiaries subject to consolidation, indicated in item 1.3.1. hereof. Moreover, as at 31 December 2016 the Company held, directly or indirectly, shares in other 34 companies and as at the day of drawing up this report the Company held, directly or indirectly, shares in other 35 companies.

1.3.1. Entities subject to consolidation

The figure below presents the structure of TAURON Capital Group, including the companies subject to consolidation, according to the status as at 31 December 2016.

Figure no. 3. Structure of TAURON Capital Group, including companies subject to consolidation as at 31 December 2016



** On 8 March 2017 the Extraordinary Meeting of Shareholders of the company PEPKH in liquidation adopted the resolution on continuation of the company business and waiving its liquidation.*

Moreover, TAURON Capital Group has investments in joint projects: Elektrociepłownia Stalowa Wola S.A. (EC Stalowa Wola), Elektrownia Blachownia Nowa sp. z o.o. w likwidacji (Elektrownia Blachownia Nowa in liquidation) 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), which are measured by equity method in the consolidated financial statements.

Detailed information concerning companies covered by consolidation and TAURON's share in their initial capital and in their governing body is presented in subsection 1.3.3 of this report.

1.3.2. Changes in organisation of TAURON Capital Group

In 2016 and until the day of this report, the following changes in the organisation of TAURON Capital Group took place:

Increase in the share capital of companies

1. On 29 January 2016 the District Court for Katowice-Wschód, 8th Commercial Department, registered the increase in the share capital of Nowe Brzeszcze GT company in the National Court Register, as adopted by the Extraordinary Shareholders' Meeting (SM) of Nowe Brzeszcze GT on 31 December 2015. The share capital of the company was increased from the amount of PLN 2,100,000 to the amount of PLN 5,000,000, i.e. by the amount of PLN 2,900,000, by way of issuance of 29,000 new shares with the nominal value of PLN 100 per share and with the total nominal value of PLN 2,900,000. The shares were taken up by TAURON as the existing sole shareholder of the company, in exchange for the cash contribution at a price of PLN 1,000 per share, i.e. for the total amount of PLN 29,000,000.

   The surplus of the price of taking up each new share in the increased share capital of the company over its nominal value, in the total amount of PLN 26,100,000 was transferred to the supplementary capital of the company which had been established under the aforementioned resolution.

   On 6 May 2016 the District Court for Kraków-Śródmieście in Kraków, 12th Commercial Department of the National Court Register, registered the increase in the share capital of the Nowe Brzeszcze GT company in the National Court Register, as adopted by the Extraordinary SM of Nowe Brzeszcze GT on 22 March 2016. The share capital of the company was increased from the amount of PLN 5,000,000 to the amount of PLN 55,000,000, i.e. by the amount of PLN 50,000,000 by way of issuance of 500,000 new shares with the nominal value of PLN 100 per share, with the total nominal value of PLN 50,000,000. The shares were taken up by TAURON as the existing sole shareholder of the company, in exchange for the cash contribution at a price of PLN 300 per share, i.e. for the total amount of PLN 150,000,000.

The surplus of price for taking up each share in the increased share capital of the company over its nominal value, at a level of PLN 200 per share, i.e. in the total amount of PLN 100,000,000 was transferred to the supplementary capital of the company.

On 25 August 2016 the District Court for Kraków-Śródmieście in Kraków, 12th Commercial Department of the National Court Register, registered the increase in the share capital of the Nowe Brzeszcze GT company in the National Court Register, as adopted by the Extraordinary SM of Nowe Brzeszcze GT on 11 August 2016. The share capital of the company was increased from the amount of PLN 55,000,000 to the amount of PLN 55,078,000, i.e. by the amount of PLN 78,000 by way of issuance of 780 new shares with the nominal value of PLN 100 per share, with the total nominal value of PLN 78,000. The shares were taken up by TAURON as the existing sole shareholder of the company, in exchange for the cash contribution at a price of PLN 5,000 per share, i.e. for the total amount of PLN 3,900,000.

The surplus of price for taking up of each share in the increased share capital of the company over its nominal value, at a level of PLN 3,822,000 was transferred to the supplementary capital of the company.

2. On 28 June 2016 the District Court for Katowice-Wschód, 8th Commercial Department, registered the increase in the share capital of TAURON Wydobycie company in the National Court Register, as adopted by the Extraordinary Shareholders' Meeting (SM) of TAURON Wydobycie on 29 April 2016. The share capital of the company was increased from the amount of PLN 352,040,780 to the amount of PLN 354,540,780, i.e. by the amount of PLN 2,500,000, by way of issuance of 250,000 new shares with the nominal value of PLN 10 per share, with the total nominal value of PLN 2,500,000. The shares were taken up by TAURON as the existing sole shareholder of the company, in exchange for the cash contribution at a price of PLN 1,000 per share, i.e. for the total amount of PLN 250,000,000.

   The surplus of the issue of each new share in the increased share capital of the company over its nominal value, at a level of PLN 990 per share, i.e. in the total amount of PLN 247,500,000 was transferred to the supplementary capital of the company.

   On 27 October 2016 the District Court for Katowice-Wschód, 8th Commercial Department, registered the increase in the share capital of TAURON Wydobycie company in the National Court Register, as adopted by the Extraordinary SM of TAURON Wydobycie on 28 September 2016. The share capital of the company was increased from the amount of PLN 354,540,780 to the amount of PLN 355,510,780, i.e. by the amount of PLN 970,000, by way of issuance of 97,000 new shares with the nominal value of PLN 10 per share, with the total nominal value of PLN 970,000. The shares were taken up by TAURON as the existing sole shareholder of the company, in exchange for the cash contribution at a price of PLN 1,000 per share, i.e. for the total amount of PLN 97,000,000.

   The surplus of the issue price in the increased share capital of the company over its nominal value, at a level of PLN 96,030,000 was transferred to the supplementary capital of the company.

3. On 11 October 2016 the District Court for Kraków-Śródmieście in Kraków, 12th Commercial Department of the National Court Register, registered the increase in the share capital of the TAURON Dystrybucja Pomiary company in the National Court Register, as adopted by the Extraordinary SM of TAURON Dystrybucja Pomiary on 14 September 2016. The share capital of the company was increased from the amount of PLN 207,000 to the amount of PLN 1,747,000, i.e. by the amount of PLN 1,540,000 by way of issuance of 1,540 new shares with the nominal value of PLN 1,000 per share, with the total nominal value of PLN 1,540,000. The shares were taken up by TAURON Dystrybucja as the existing sole shareholder of the company, in exchange for the cash contribution at a price of PLN 50,000 per share, i.e. for the total amount of PLN 77,000,000.

   The surplus of the price of taking up each share in the increased share capital of the company over its nominal value, at a level of PLN 75,460,000 was transferred to the share capital of the company.

4. On 22 November 2016 the District Court for Kraków-Śródmieście in Kraków, 12th Commercial Department of the National Court Register, registered the increase in the share capital of the TAURON Dystrybucja Pomiary company in the National Court Register, as adopted by the Extraordinary SM of KOMFORT-ZET on 22 November 2016. The share capital of the company was increased from the amount of PLN 110,000 to the amount of PLN 170,000, i.e. by the amount of PLN 60,000 by way of issuance of 60 new shares with the nominal value of PLN 1,000 per share, with the total nominal value of PLN 60,000. The shares were taken up by TAURON Dystrybucja as the existing sole shareholder of the company, in exchange for the cash contribution at a price of PLN 50,000 per share, i.e. for the total amount of PLN 3,000,000.

   The surplus of the price of taking up the shares in the increased share capital of the company over its nominal value, at a level of PLN 2,940,000 was transferred to the supplementary capital of the company.

5. On 21 December 2016 the Extraordinary SM of the PGE EJ 1 sp. z o.o. company (PGE EJ 1) adopted the resolution on the increase of the share capital from the amount of PLN 275,859,450 to the amount of PLN 310,858,470, i.e. by the amount of PLN 34,999,020 through creating 248,220 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 34,999,020. TAURON will take up 10% of new created shares, i.e. 24,822 shares with the total nominal value of PLN 3,499,902.

   The increase of the share capital was registered in the National Court Register on 15 February 2017.

Merger of companies

1. On 2 November 2016 the District Court for Katowice-Wschód, 8th Commercial Department of the National Court Register entered the merger of the following companies in the National Court Register: TAURON Serwis (the acquiring company) with TAURON Wytwarzanie Serwis sp. z o.o. (the acquired company). The merger was executed pursuant to art. 492 § 1 item 1 of the KSH (Code of Commercial Companies), i.e. through the assignment of the whole total assets of the company to the acquiring company (merger through acquisition).

   As a result of the merger, the increase in the share capital of the acquiring company took place, from the amount of PLN 65,000 to the amount of PLN 4,596,700, i.e. by the amount of PLN 4,531,700, through creating 90,634 new equal and indivisible shares with the nominal value of PLN 50 per share, received by partners of the acquired company in a quantity calculated in accordance with the exchange parity indicated in the merger plan. In connection with the merger, TAURON, as a partner of the acquired company, received 86,597 shares of the acquiring company with the nominal value of PLN 50 per share and the total nominal value of PLN 4,329,850, which constitute 95.61% share in the share capital of TAURON Serwis.

   The merger of the companies was preceded by:

   1) redemption of minority shareholders' shares pursuant to the resolution of 20 May 2016 of the Extraordinary SM of the TAURON Wytwarzanie Serwis sp. z o.o. company (TAURON Wytwarzanie Serwis) concerning the redemption of 18,763 shares in the share capital of the TAURON Wytwarzanie Serwis from net profit, against remuneration and under the partners' approval, and
   2) the acquisition of 63,910 shares of the TAURON Wytwarzanie Serwis company with the nominal value of PLN 50 per share and with the total value of PLN 3,195,500, constituting 95.54% of the share in the share capital of TAURON Wytwarzanie Serwis, by TAURON from TAURON Wytwarzanie on 4 August 2016, pursuant to the sales agreement.

   The merger of the companies was performed under the implementation of the project on *Reorganisation of the area of services in TAURON Group* aiming at centralisation of service activity carried out for TAURON Wytwarzanie and TAURON Ciepło in TAURON Serwis company.

2. On 1 December 2016 the District Court for Katowice-Wschód, 8th Commercial Department of the National Court Register entered the merger of the following companies in the National Court Register: TAURON Wydobycie (the acquiring company) with Nowe Brzeszcze GT (the acquired company). The merger took place pursuant to Article 492 § 1 item 1 of the KSH, i.e. through takeover and transfer of the entire assets of Nowe Brzeszcze GT to TAURON Wydobycie.

   As a result of the merger, no increase the share capital of TAURON Wydobycie company took place, as TAURON Wydobycie held 100% interest in the share capital of Nowe Brzeszcze GT company. The merger of the companies was preceded by the disposal of 55,078 shares of Nowe Brzeszcze GT company with the nominal value of PLN 100 each and the total nominal value of PLN 55,078,000, constituting 100% of the share in the share capital of Nowe Brzeszcze GT company by TAURON in favour of TAURON Wydobycie on 15 September 2016, pursuant to the sales agreement concluded on 9 September 2016.

   The merger of the companies was performed under the project on *Integration of assets of Nowe Brzeszcze Grupa TAURON sp. z o.o. in the Mining Area*.

Establishment of new companies

1. On 19 October 2016, TAURON and PGE Polska Grupa Energetyczna S.A. (PGE), ENEA S.A. (ENEA) and ENERGA S.A. (ENERGA) established the company under the enterprise name of ElectroMobility Poland S.A. (ElectroMobility Poland) with its registered office in Warsaw, where TAURON took up 2,500 shares with the nominal value of PLN 1,000 per share and the total nominal value of PLN 2,500,000, constituting 25% share in the share capital of the company. ElectroMobility Poland was registered in the National Court Register on 7 December 2016.

   The core area of the company activity will include conducting of research and analyses in the scope of development, promotion and popularisation of electromobility and development of electromobility industry in Poland. Electromobility is one of the areas to affect the electricity market. The level of preparation of the energy sector to popularise electric vehicles will determine whether electromobility creates the opportunities for growth of power sector innovation and the stimulus for its development. For the above reasons, energy groups decided to undertake a joint venture in this area.

2. On 15 December 2016 a company under the enterprise name of Magenta Grupa TAURON sp. z o.o. (Magenta Grupa TAURON) with its registered office in Katowice was established, where all 10,000 shares with the nominal value of PLN 50 per share and the total nominal value of PLN 500,000 were taken up by TAURON. The company was registered in the National Court Register on 31 January 2017.

Magenta Grupa TAURON was established in order to support the long-term development of TAURON Capital Group through investment in enterprises in the seed and start-up phase and conducting development projects responding to the needs of TAURON Capital Group.

Dissolution of companies

1. On 15 February 2016 the District Court for Kraków-Śródmieście, 12th Commercial Department of the National Court Register issued the decision on removal of the company: Ośrodek Szkoleniowo-Wypoczynkowy "JAGA" sp. z o.o. in liquidation bankruptcy (a subsidiary of TAURON Dystrybucja) from the National Court Register, which became final on 1 March 2016.

   The aforementioned removal from the Register was a consequence of closure of the bankruptcy proceedings of the company, comprising liquidation of its asset, in 2015.

2. On 30 August 2016 the District Court in Gliwice, 10th Commercial Department of the National Court Register issued the decision on removal of the company TAURON Wytwarzanie GZE sp. z o.o. from the National Court Register, which became final on 15 September 2016.

   The aforementioned removal was a consequence of the approval of the liquidation report of the company and concluding of its liquidation, adopted under the resolution of the Extraordinary SM of TAURON Wytwarzanie GZE sp. z o.o. of 29 September 2015, by the Extraordinary SM of the TAURON Wytwarzanie GZE sp. z o.o. Company on 8 June 2016, in accordance with Article 288 § 1 of the KSH.

Abandoning the demerger of TAURON EKOENERGIA company

With reference to resolutions adopted on 9 February 2015 by the Extraordinary SM of companies TAURON EKOENERGIA and Marselwind sp. z o.o. (Marselwind) concerning the division of TAURON EKOENERGIA company (the Divided Company), pursuant to Article 529 § 1 item 4 of the KSH, i.e. through the transfer of a part of the Divided Company assets, constituting an organised part of the enterprise, consisting of fixed assets and intangible assets associated with electricity generation in renewable energy sources – wind farms, to Marselwind (the Acquiring Company), in exchange for the interest in the increased share capital of the Acquiring Company, no division of wind assets and their transfer to Marselwid special purpose vehicle took place.

In connection with a significant change in legal and actual circumstances, on 28 September 2016 the Extraordinary SMs of companies: TAURON EKOENERGIA and Marselwind adopted resolutions concerning abandoning of the demerger of TAURON EKOENERGIA and waiver of demerger resolutions of 9 February 2015 concerning the demerger of TAURON EKOENERGIA through the separation and transfer of separated components of assets constituting a part of the enterprise to Marselwind company.

Events after 31 December 2016

Demerger of TAURON Wytwarzanie company through the transfer of assets to the newly established company, Nowe Jaworzno Grupa TAURON sp. z o.o. in organisation

On 31 January 2017 the Extraordinary SM of TAURON Wytwarzanie adopted the resolution concerning the demerger of TAURON Wytwarzanie company through separation, pursuant to Article 529 § 1 item 4 of the KSH, i.e. through the transfer of a part of TAURON Wytwarzanie assets in the form of an organised part of the enterprise comprising the investment process of construction of the new 910 MW unit at Elektrownia Jaworzno III, carried out in TAURON Wytwarzanie Oddział Jaworzno in Jaworzno, to the newly established company, Nowe Jaworzno Grupa TAURON sp. z o.o., in exchange for 37,000 shares of the company Nowe Jaworzno Grupa TAURON sp. z o.o., with the nominal value of PLN 50 per share and the total nominal value of PLN 1,850,000, to be taken up by the sole shareholder of the divided company, i.e. TAURON.

Upon adopting of the aforementioned resolution, the company – Nowe Jaworzno Grupa TAURON sp. z o.o. In organisation was established.

At the same time, on 31 January 2017 the resolution was adopted by Nowe Jaworzno Grupa TAURON sp. z o.o. in organisation shareholders, concerning the aforementioned division.

The demerger process demonstrates the implementation of the *Strategy of TAURON Group for 2016–2025*, pursuant to which the project on construction of 910 MW unit at Elektrownia Jaworzno III will be implemented under a new financing formula, assuming the separation of an organised part of the enterprise from TAURON Wytwarzanie company and sale of a part of shares to external partners.

Until the day of drawing up this report, the demerger of TAURON Wytwarzanie has not been registered in the National Court Register.

Waiver of liquidation of the company PEPKH in liquidation

On 8 March 2017, pursuant to Article 273 of the KSH, the Extraordinary SM of the company PEPKH in liquidation adopted the resolution on continuation of the company business and waiving its liquidation.

The waiver of the company liquidation resulted from the change in circumstances associated with the ongoing liquidation proceedings indicating the pertinence of continued existence of the company.

In connection with the changes in the organisation of TAURON Capital Group, as at the day of drawing up this report, the Company held, directly or indirectly, shares in 53 companies.

1.3.3. Organisational or capital links

The table below presents the list of significant direct and indirect subsidiaries, subject to consolidation, in which the Company held shares and stocks according to the status as at 31 December 2016.

Table no 1. Specification of significant subsidiaries covered by consolidation as at 31 December 2016 in which the Company holds direct and indirect share

No.	Company name	Registered Office	Core business area	Share of TAURON in the capital and governing body of the company
1.	TAURON Wydobycie*	Jaworzno	Hard coal mining	100.00%
2.	TAURON Wytwarzanie	Jaworzno	Generation, transmission and distribution of electricity and heat	100.00%
3.	TAURON EKOENERGIA	Jelenia Góra	Generation of electricity	100.00%
4.	Marselwind	Katowice	Generation, transmission and trading in electricity	100.00%
5.	TAURON Ciepło	Katowice	Production and distribution of heat	100.00%
6.	TAURON Dystrybucja	Kraków	Distribution of electricity	99.72%
7.	TAURON Dystrybucja Serwis**	Wrocław	Services	99.72%
8.	TAURON Dystrybucja Pomiary**	Tarnów	Services	99.72%
9.	TAURON Sprzedaż	Kraków	Trading in electricity	100.00%
10.	TAURON Sprzedaż GZE	Gliwice	Trading in electricity	100.00%
11.	TAURON Czech Energy	Ostrava, Czech Republic	Trading in electricity	100.00%
12.	TAURON Obsługa Klienta	Wrocław	Services	100.00%
13.	KW Czatkowice	Krzeszowice	Mining of limestone rocks and stone extraction	100.00%
14.	PEPKH in liquidation	Warsaw	Trading in electricity	100.00%
15.	TAURON Sweden Energy	Stockholm, Sweden	Services	100.00%
16.	Biomasa Grupa TAURON	Stalowa Wola	Biomass sourcing and trading	100.00%
17.	TAURON Serwis***	Katowice	Services	95.61%
18.	KOMFORT-ZET**	Tarnów	Services	99.72%

** On 1 December 2016 the merger of companies TAURON Wydobycie and Nowe Brzeszcze GT was registered.*
*** The share in TAURON Dystrybucja Serwis, TAURON Dystrybucja Pomiary and KOMFORT-ZET is held by TAURON indirectly, through its subsidiary, TAURON Dystrybucja. In addition, TAURON is the user of shares/stocks of TAURON Dystrybucja Serwis and TAURON Dystrybucja Pomiary companies.*
**** On 2 November 2016 the merger of TAURON Serwis and TAURON Wytwarzanie Serwis companies was registered.*

The table below presents the list of significant co-subsidiaries in which the Company held direct and indirect share, according to the status as at 31 December 2016.

Table no 2. Specification of significant subsidiaries covered by consolidation as at 31 December 2016 in which the Company holds direct and indirect share

No.	Company name	Registered Office	Core business area	Share of TAURON in the capital and governing body of the company
1.	EC Stalowa Wola*	Stalowa Wola	Generation of electricity	50.00%
2.	Elektrownia Blachownia Nowa in liquidation*	Kędzierzyn Koźle	Electricity generation	50.00%

No.	Company name	Registered Office	Core business area	Share of TAURON in the capital and governing body of the company
3.	TAMEH HOLDING**	Dąbrowa Górnicza	Activities of central companies and holdings	50.00%
4.	TAMEH POLSKA**	Dąbrowa Górnicza	Generation, transmission, distribution and trading in electricity and heat	50.00%
5.	TAMEH Czech**	Ostrava, Czech Republic	Production, trade and services	50.00%

** The share in EC Stalowa Wola and in Elektrownia Blachownia Nowa in liquidation is held by TAURON indirectly, through the s subsidiary, TAURON Wytwarzanie.*
*** The Companies create the capital group. TAURON holds a direct share in the capital and in the governing body of TAMEH HOLDING, holding a 100% share in the capital and the governing body of TAMEH POLSKA and TAMEH Czech.*

Other most significant investments in capital financial assets as at 31 December 2016 comprise engagement in the following entities:

1. SCE Jaworzno III sp. z o.o. with the value of PLN 36,283 thousand,
2. Przedsiębiorstwo Energetyki Cieplnej Tychy sp. z o.o. with the value of PLN 32,113 thousand,
3. PGE EJ 1 with the value of PLN 23,046 thousand,
4. Energetyka Cieszyńska sp. z o.o. with the value of PLN 15,063 thousand.

1.3.4. Major domestic and foreign investment

Purchase of equity securities

In the scope of purchase of shares and stocks in companies of TAURON Capital Group, the main investment of the Company included:

Purchase of shares in Nowe Brzeszcze GT

In 2016 TAURON took up new shares in the increased share capital of Nowe Brzeszcze GT company three times, in the total amount of PLN 182,900 thousand, including:

1) on 29 January 2016 TAURON acquired 29,000 shares at a price of PLN 1,000 per share, in the total amount of PLN 29,000 thousand,
2) on 6 May 2016 TAURON acquired 500,000 shares at a price of PLN 300 per share, in the total amount of PLN 150,000 thousand,
3) on 25 August 2016 TAURON acquired 780 shares at a price of PLN 5,000 per share, in the total amount of PLN 3,900 thousand.

Purchase of TAURON Wydobycie shares

In 2016 TAURON took up new shares in the increased share capital of TAURON Wydobycie twice, in the total amount of PLN 347,000 thousand, including:

1) on 28 June 2016 TAURON acquired 250,000 shares at a price of PLN 1,000 per share, in the total amount of PLN 250,000 thousand,
2) on 27 October 2016 TAURON acquired 97,000 shares at a price of PLN 1,000 per share, in the total amount of PLN 97,000 thousand.

Purchase of TAURON Wytwarzanie Serwis company shares

On 4 August 2016 TAURON purchased 63,910 shares of TAURON Wytwarzanie Serwis company, so far used by TAURON, from TAURON Wytwarzanie, with the nominal value of PLN 50 per share and the total nominal value of PLN 3,195,500, constituting 95.54% interest in the share capital of TAURON Wytwarzanie Serwis company.

Purchase of ElectroMobility Poland S.A. company shares

On 19 October 2016, TAURON acquired 2,500 shares in the newly established company, ElectroMobility Poland S.A., with the total nominal value of PLN 2,500 thousand, representing 25% interest in the share capital of this company. On 7 December 2016 the company was registered in the National Court Register.

Subsidies to the capital of PEPKH in liquidation

On 8 November 2016 the Extraordinary SM of PEPKH in liquidation adopted the resolution on contribution of subsidies to the company capitals in the amount of PLN 6,000 thousand. The subsidies were contributed with the aim of ensuring funding opportunities for the company operations. Funds within subsidies were contributed by TAURON on 9 November 2016.

Purchase of PGE EJ 1 company shares

On 21 December 2016 TAURON undertook to acquire 24,822 shares at a price of PLN 141 per share and with the total nominal value of PLN 3,499,902. The increase of the share capital was registered in the National Court Register on 15 February 2017.

Major investment in financial assets

Major investments of TAURON Capital Group in financial assets in the year ended on 31 December 2016 include:

1. Acquisition of participation units in investment funds for the total amount of PLN 25,000 thousand by TAURON as a parent entity. The carrying amount of units measured at a fair value amounted to PLN 25,316 thousand as at 31 December 2016.
2. Granting of loans to the co-subsidiary, EC Stalowa Wola in the total amount of PLN 23,575 thousand by TAURON as a parent entity. As at the balance sheet day the value of loans granted to EC Stalowa Wola amounted to PLN 256,067 thousand.
3. Concluding transactions hedging the interest rate swap (IRS) by TAURON as a parent entity, for the period from 4 to 5 years, hedging a part of interest rate risk in relation to cash flows associated with exposure to WIBOR 6M, determined under the dynamic risk management strategy, i.e. interest on securities with the nominal value of PLN 2,100,000 thousand. The carrying amount of the aforementioned instruments measured as at the balance sheet day reached PLN 36,641 thousand.

1.4. Strategy and Strategic Priorities of TAURON Capital Group

Until 1 September 2016 the *Corporate Strategy of TAURON Group for 2014–2017 with an outlook until 2023* was binding in TAURON Capital Group. Activities undertaken under this Strategy focused on 4 principal goals: growth in the most attractive areas of operations, operational and investment effectiveness at a level of best practice, management of exposure to market and regulatory risks, effective organisation building.

In 2016, works related to the implementation of strategic programmes were continued, such as: the construction of a power unit with the capacity of 910 MW_e at Elektrownia Jaworzno III, including the heat generation component with the heat capacity of 240 MW_t, preparation to commencement of the construction of the CCGT unit with the capacity of 449 MW_e at Elektrownia Łagisza, the construction of “Grzegorz” shaft including the infrastructure and the construction of the 800 m level at ZG Janina. Restructuring activities associated with the improvement of management processes, integration of companies and integration of support functions were continued.

On 2 September 2016 the TAURON Management Board adopted and the Supervisory Board issued a positive opinion on the document entitled *TAURON Group’s 2016–2025 Strategy* (the Strategy). The new Strategy is a response to the challenges stemming from the current and forecast situation on the market and in the power sector. Within the process of the Strategy preparation an in-depth analysis of the macroeconomic, market and regulatory environment as well as sector development forecasts was performed, translating them into opportunities and risks for TAURON Capital Group within the perspective of the nearest ten years. The capacity of TAURON Capital Group to finance current and planned investment projects was analysed to the extent enabling their implementation from funds generated by operating activity and by acquisition of debt financing. The aforementioned analyses and market trends provided basis for verification of market, macroeconomic assumptions and the investment plan.

1.4.1. Mission, vision and new values of TAURON Capital Group

The new Strategy defines the new Mission and Vision and determined key values of TAURON Capital Group:

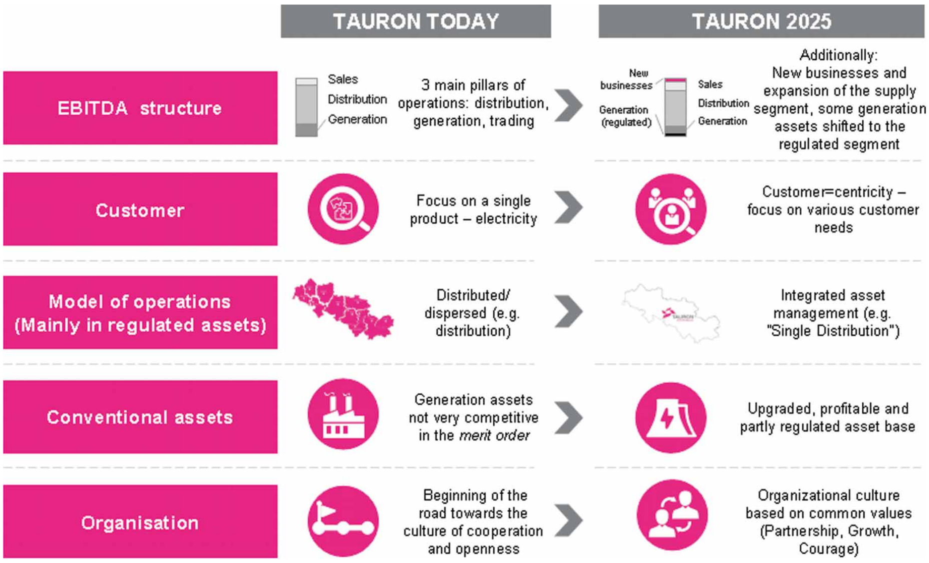
Mission of TAURON Capital Group
“With passion and commitment we are delivering modern solutions that provide energy in the constantly changing world.”

Vision of TAURON Capital Group
“We are a company that best meets customer needs in the Polish energy industry.”

The mission and vision best describe strategic plans of TAURON Capital Group. The Sales Segment as well as new products and services constitute the area of activity to be intensively developed by TAURON Capital Group. TAURON Capital Group adjusts its profile with the purpose of full concentration on the client, recognising the potential of new products, compatible services, new contract channels as a response to clients’ needs.

The figure below presents vision of TAURON Capital Group in 2025.

Figure no. 4 Vision of TAURON Capital Group in 2025



Key values to support the implementation of the Strategy include "Partnership", "Development" and "Courage". The values reflect the method to be applied by TAURON Capital Group in order to achieve its objectives. Within the partnership, client orientation, building of sustainable relations and commitment is essential. The development means orientation towards innovation, development of competence, skills and knowledge as well as searching for increasingly better solutions, to meet clients' expectations and enhance the quality of services. Courage means boldness and openness, determination as well as commitment and passion in achieving common goals.

The combination of those values shall lead to better understanding of clients' expectations, response to market challenges and development of organisational culture of TAURON Capital Group.

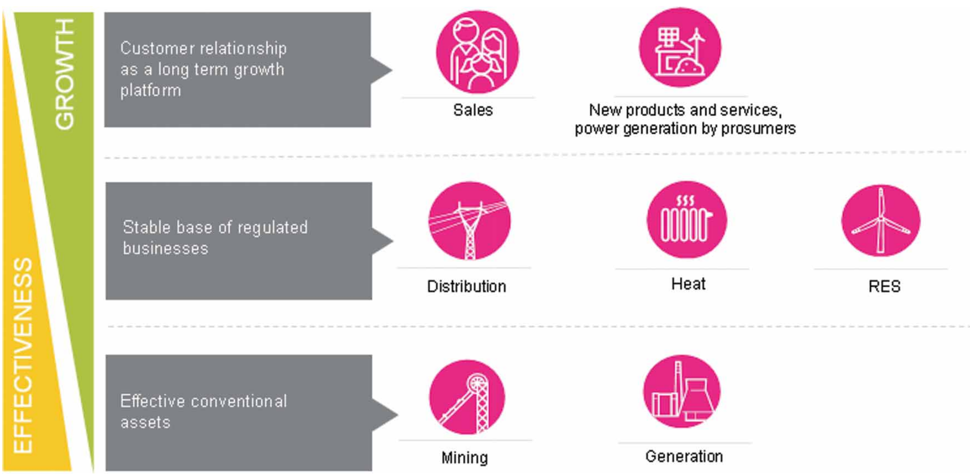
1.4.2. Strategy of the TAURON Capital Group for 2016–2025

The Strategy adopted for the years 2016–2025 presents the optimum expansion path that will ensure financial stability and growth perspective, 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 relations. The adopted mission and vision reflect new management philosophy and are in line with the customer-oriented growth concept.

The Strategy changes the approach of individual segments of activity of TAURON Capital Group to development, dividing them to those to be strongly developed by TAURON Capital Group, those to provide basis for financial stability and those in which strong emphasis on cost-effectiveness is needed. The above mentioned approach reflects the new management philosophy and emphasises the turn towards customer and its needs as well as building of innovative TAURON Capital Group open to new challenges.

The figure below shows the outlook of TAURON Capital Group's segments.

Figure no. 5 Outlook of TAURON Capital Group's segments



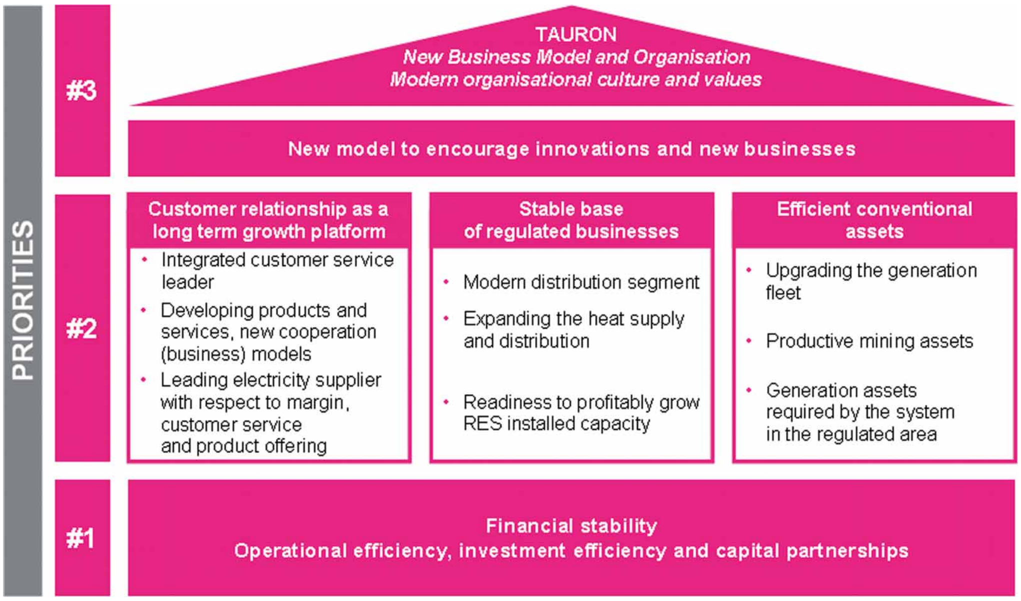
The Strategy determines three priorities which will transform the Group into an innovative energy concern, adjusted to market and client's needs, that ultimately guarantees the return on invested capital to its shareholders.

1. Ensuring the financial stability of TAURON Capital Group is implemented through the following actions:
   a) The *Efficiency Improvement Programme in TAURON Group for 2016–2018*, adopted in March 2016 and assuming achieving PLN 1.3 billion in savings in 2016–2018. The above savings comprise measures resulting in the cumulative EBITDA increase by approximately PLN 1 billion and consisting in CAPEX reduction by approximately PLN 0.3 billion in 2016–2018.
   b) Strategic Initiatives and CAPEX reduction in 2017–2020 will generate a financial effect at a level of PLN 1.9 billion. It will be achieved as a result of measures leading to the cumulative EBITDA increase by approximately PLN 1.2 billion and the CAPEX reduction by approximately PLN 0.7 billion. These are additional financial outcomes, besides the effects included in the Efficiency Improvement Programme.
   c) Suspension of the investment in the new CCGT unit at Łagisza Power Plant, resulting in not incurring CAPEX in the amount of approximately PLN 1.5 billion. It will be possible to resume the project in the case the regulatory and market environment turns favourable.
2. Building a strong capital group.

   The Strategy determines a new approach to the value chain where key tasks are set for each line of business. The 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 growth of TAURON Capital Group. In this segment, TAURON is planning rapid development of its offer for customers, which will allow for retaining the existing base of customers purchasing TAURON products and increasing profitability. Electricity distribution as well as heat generation and distribution segments are to constitute a stable base of regulated business of TAURON Capital Group. Mining and conventional generation segments have tasks related first of all to efficiency improvement. The following three pillars of building the strong capital group were defined:
   a) Customer relations based on integrated high quality service with the use of modern sales and customer service channels as well as developing a product and service offer.
   b) Stable base of regulated assets based on the refurbished electricity distribution and heat segments as well as readiness to develop renewable energy sources in case of favourable regulatory environment.
   c) Effective 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, will be shifted to the regulated segment of the power system.
3. Implementation of organisational changes supporting the implementation of the Strategy which will transform the TAURON Capital Group into a modern and innovative organisation:
   a) Implementing a new, process-oriented operational model. Five priority process streams have been identified around which operations of TAURON Capital Group will be concentrated, i.e. Strategy, Finance, Assets Management and Development, Client and Corporate Governance and Support. Such approach will allow for placing a greater emphasis on cross-sectional issues that will determine the competitive advantages of TAURON Capital Group in the future.
   b) Expanding research and development as well as innovative activities for which expenditures equal to 0.4% of the consolidated annual revenue are envisaged.
   c) Developing innovative projects based on the Corporate Venture Capital (CVC) type fund dedicated for this purpose or other similar solutions.

The figure below presents the implementation of the priorities based of pillars of the TAURON Capital Group's Strategy.

Figure no. 6 The figure below presents the implementation of the priorities TAURON Capital Group's Strategy



The implementation of the Strategy will enable to increase EBITDA from PLN 3.5 billion in 2015 to over PLN 4 billion in 2020 and over PLN 5 billion in 2025. The estimated recurring effect of the Efficiency Improvement Programme implementation in the form of impact on EBITDA of TAURON Capital Group is approx. PLN 0.4 billion starting from 2018 and the effect of Strategic Initiatives in the form of impact on EBITDA of TAURON Capital Group is approx. PLN 0.3 billion after 2020.

Within streamlining of CAPEX, the expenditures planned for 2016–2020 were reduced from PLN 20.2 billion to approx. PLN 18 billion. The Strategy assumes that the commenced and well advanced investment projects will be continued. The detailed analysis has indicated that 75% of the investment plan up to 2020 includes tasks continued or representing the implementation of the commitments undertaken. Those tasks include the investment in the 910 MW unit at Jaworzno III Power Plant and tasks in the Distribution Segment contracted or arising from regulatory requirements. Abandoning or postponing of those tasks would have an adverse impact on the value of TAURON Capital Group or is impossible due to legal or security requirements.

In the Mining segment investments at ZG Janina, the construction of “Grzegorz” shaft at ZG Sobieski will be continued and the planned investment projects at ZG Brzeszcze will be carried out. CAPEX in this line of business is approximately PLN 1.3 billion until 2020.

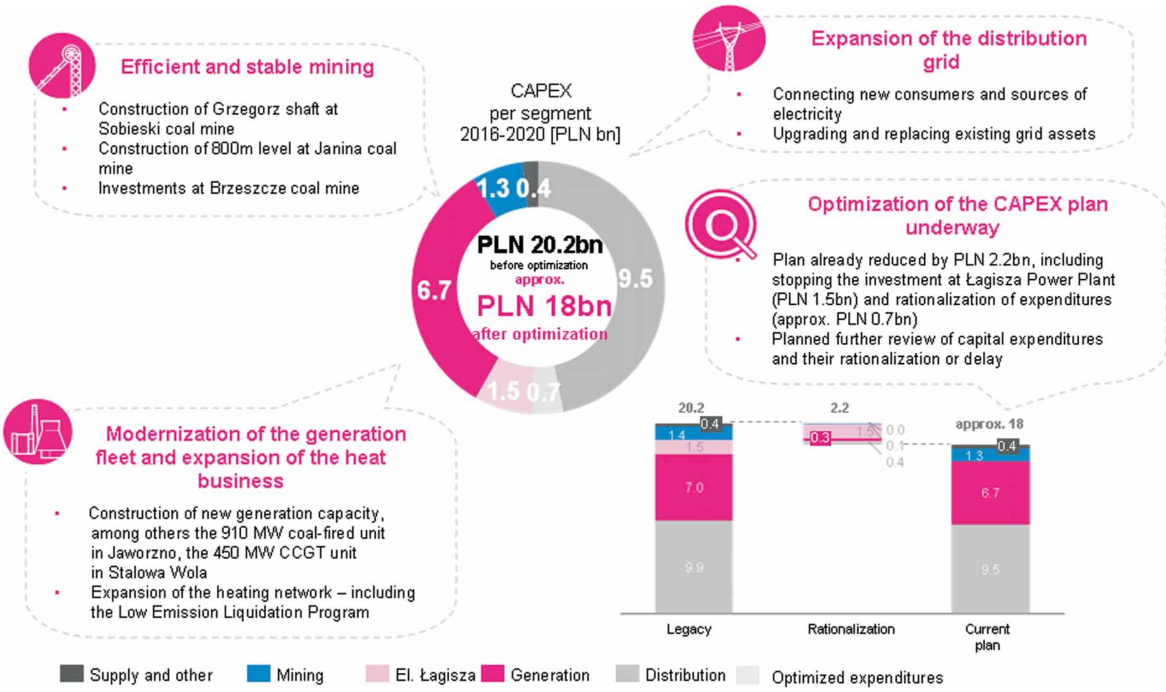
In the Generation Segment investment in construction of the 910 MW unit at Jaworzno III Power Plant, the CCGT unit at EC Stalowa Wola and investments in the heating networks will be continued. TAURON assumes implementation of construction of the 910 MW unit at Jaworzno III Power Plant under a new financing formula envisaging separation of an organised part of the enterprise and selling its shares to third party partners, provided they do not acquire a controlling stake. The change in the method of the unit construction would affect the decline in the net debt/EBITDA ratio, consequently, it would significantly mitigate the risk of exceeding the threshold level of this covenant (3.5x) contained in financing agreements.

The Strategy assumes that financial stability will be maintained and the net debt/EBITDA covenant at a level of 3.5x will not be exceeded, excluding sales of the minority share in the project on 910 MW unit construction at Jaworzno III Power Plant to external partners. It means that the planned change in the financing formula of this project is an additional element stabilising the financial situation of TAURON Capital Group. CAPEX in the Generation Segment amount to PLN 6.7 billion up to 2020.

More than 50% of the entire expenditure pool, i.e. PLN 9.5 billion by 2020, represents investments in distribution comprising connecting new customers and electricity sources as well as upgrading and replacing grid assets.

The figure below presents the capital expenditure by segments in 2016–2020.

Figure no. 7 Capital expenditure by segments in 2016–2020



In the scope of innovation and research-development activities the Strategy assumes expenditure at a level of 0.4 per cent of the consolidated annual revenue value.

In the area of investment the adjustment of the investment portfolio to market needs is the overarching objective.

In particular, activities will be oriented to:

a) Optimisation of asset structure in all areas of activity and adjustment to environmental requirements.
b) Implementation of only those investment projects which guarantee the expected level of return on equity and are not burdened with significant market risks.
c) Use of off-balance sheet forms of financing, in particular, through involving external partners.
d) Analysis of investment in the conventional generation segment, provided that mechanisms guaranteeing revenue are introduced (e.g. capacity market or other form of regulation).
e) Investing in projects in sectors related to the power sector (in particular services) in order to supplement the value chain within which TAURON operates as well as creating an offer of high margin services.

Assumed investment directions beyond 2020 include mainly the area of regulated power sector (i.e., inter alia, electricity distribution, heat generation and distribution) and the new power industry (i.e. e-mobility, dispersed heat and electricity generation, power generation by prosumers, Smart Home, Smart City solutions and energy-related services). The Company assumes that in the years 2020–2025 it will hold an investment capacity estimated at over PLN 6 billion.

In the long-term perspective, TAURON plans to pay out a dividend at a level of minimum 40% of the consolidated net profit. The intention of the Company is to ensure a dividend yield that would be competitive towards the yield offered by long-term debt instruments issued on the Polish market by investment grade rated companies.

1.4.3. Key challenges for TAURON Capital Group

The Strategy is a response of TAURON Capital Group to challenges posed by the business environment and requirements of the energy sector clients which have been changing dynamically over the recent years.

In the Strategy four key challenges for TAURON Capital Group have been defined: regulations, market, client and technologies.

Regulations Introduction of a dual commodity market – capacity market, decarbonisation policy of the European Union (EU) and successive regulations aiming at emission abatement, introduction of the qualitative regulation model in distribution, changes in the support system for RES installations as well as EU activities oriented towards a single electricity market.

Market Changing forecasts of electricity prices, over-supply and prices of coal, demand for electricity, demand for capacity, growing competition on the retail market, growing level of generation from RES, accompanied by simultaneous diversion of European players and limiting financing for conventional energy.

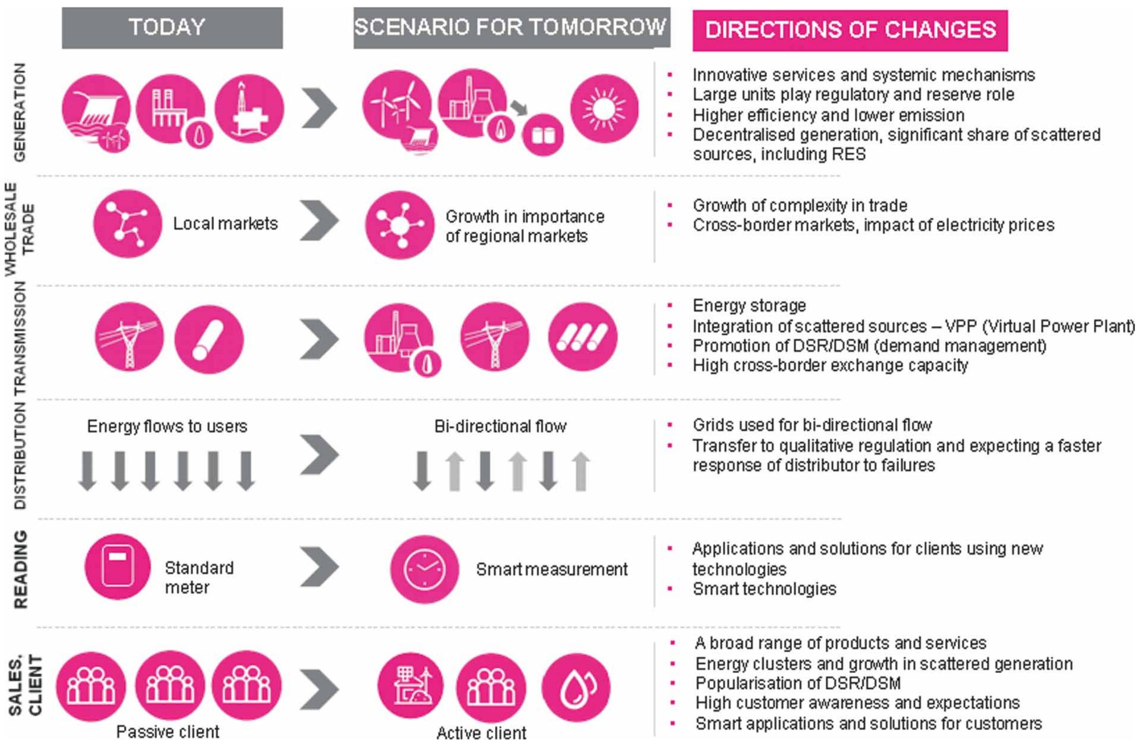
Client Growth of clients' awareness and requirements in the scope of satisfying the needs and complexity of the offer, growth of expectations in the scope of quality and availability of customer service.

Technologies Declining prices of renewable and scattered technologies, growing competitiveness of those sources in relation to conventional sources, change in the role of distribution in connection with the development of scattered energy, development of smart technology, microgeneration and energy storage.

In a long-term perspective, thorough changes of the overall power sector towards the so-called "energy of tomorrow" are important. The transformation of the systemic energy sector is foreseen towards decentralised generation, growing role of cross-border connections, energy storage and new energy services, such as "virtual power plants", demand management, scattered generation. It also results in the change of the role of distribution which has to face smart technologies, scattered generation, including prosumers, bi-directional flows, with simultaneous growth in quality and security of supplies.

The figure below shows key challenges for TAURON Capital Group.

Figure no. 8 Key challenges for TAURON Capital Group



1.4.4. Opportunities and threats

Defined key challenges for TAURON Capital Group create both opportunities and threats for operations of TAURON Capital Group.

The table below presents opportunities and threats for operations of TAURON Capital Group.

Table no 3. Opportunities and threats for operations of TAURON Capital Group

Opportunities	Threats
Regulations	
• Introduction of a dual commodity market – additional revenues for maintaining the generation capacity. • Possible support to electrical mobility (growth in electricity consumption). • Introduction of legal solutions supporting low emission abatement (e.g. electric heating, systemic heating).	• Growth in costs of conventional assets accompanied by growing environmental fees and further tightening of the decarbonisation policy. • Adverse impact of EU regulations related to the single energy market. • Potential lack of possibility to participate in the capacity market for units with emission exceeding 550 kg/MWh. • Changes in remuneration policy for distribution may limit investment in the area. • Lack of stability and predictability of regulations for RES sources, including the growth of maintenance costs of wind farms and hydroelectric power plants as well as uncertain future of RES sources based on biomass burning and co-burning (draft RES Directive). • Loss of support for co-generation after 2018.
Market	
• Cost-effective own mining base, competitive on the Polish market enabling stabilisation and predictability of fuel cost. • Access to the largest client base among energy companies in Poland. • Entering market segments surrounding the energy sector (e.g. service of equipment, IT services, etc.). • Commercialisation of innovative solutions developed within the research-development activity.	• Decline in the margin and decreased burden on conventional assets (worse profitability or the necessity to decommission old generation units due to entering the system of new high efficiency units and due to BAT requirements). • Loss of volume and profitability of the Sales Segment, in particular, in B2B. • Pressure on energy prices accompanied by growing volumes of cross-border exchange. • Growth of costs and limiting the access to financing.
Client	
• Competitive advantage in the scope of customer service quality. • Client segmentation and offering additional products in accordance with clients' needs. • Greater client awareness and expectations towards a comprehensive, personalised offer of additional services and products (increased product use by clients). • Expanding the offer of services for clients based on competence and trust in TAURON brand. • Growth through focusing on the client not generating large capital investments. • Development of modern and integrated sales and customer service channels. • New competence and business models based on research and development. • Maintaining the growth trend in electricity consumption by end consumers.	• Potential loss of clients associated with the growth in the number of competitors offering similar products to clients and due to low barriers of market entry of electricity sales. • Decline in customer loyalty – growing number of vendor's changes. • Greater awareness and requirements of clients in relation to the quality of service and product offer. • Energy independence of customers (prosumers, energy islands, clusters). • Construction of own generation sources by energy-intensive consumers, as a result of savings in electricity costs. • "Carbon leakage" – moving business operations to other countries due to energy costs".
Technologies	
• Decline in prices of renewable technologies. • Development of storage technology, smart technologies and technologies related to scattered generation. • Additional services for clients associated with new technologies (internet of things, dynamic tariffs, virtual power plants). • Development of scattered energy, including prosumer energy. • Development and implementation (commercialisation) of own innovative solutions providing competitive advantage.	• Need to adjust the grid to the growth in scattered generation (bi-directional flows). • Emergence of new, cost competitive technologies of electricity generation in our neighbouring countries.

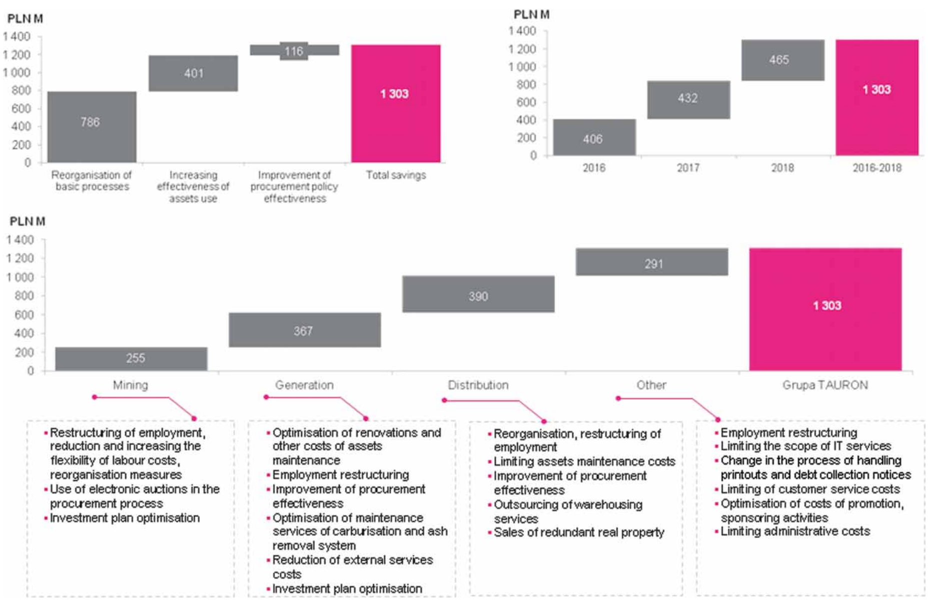
1.4.5. Implementation of the Strategy and priorities of TAURON Capital Group in 2017

2017 will be the period when materialisation of first effects of the new Strategy is planned. In accordance with the assumptions, the top priority will be to ensure financial stability in order to create solid foundations for the development of TAURON Capital Group. The efficiency improvement programme will be continued through reorganisation of core processes in the whole TAURON Capital Group and increasing the effectiveness of assets use. The Strategy will be implemented through:

a) The Efficiency Improvement Programme, adopted in March 2016 and assuming achieving financial effects at a level of PLN 1.3 billion in 2016–2018. The above savings comprise measures resulting in the cumulative EBITDA increase by approximately PLN 1.0 billion and consisting in CAPEX reduction by approximately PLN 0.3 billion in 2016–2018 in three areas of operations.

The figure below presents the Efficiency Improvement Programme in 2016–2018.

Figure no. 9 The Efficiency Improvement Programme in 2016–2018

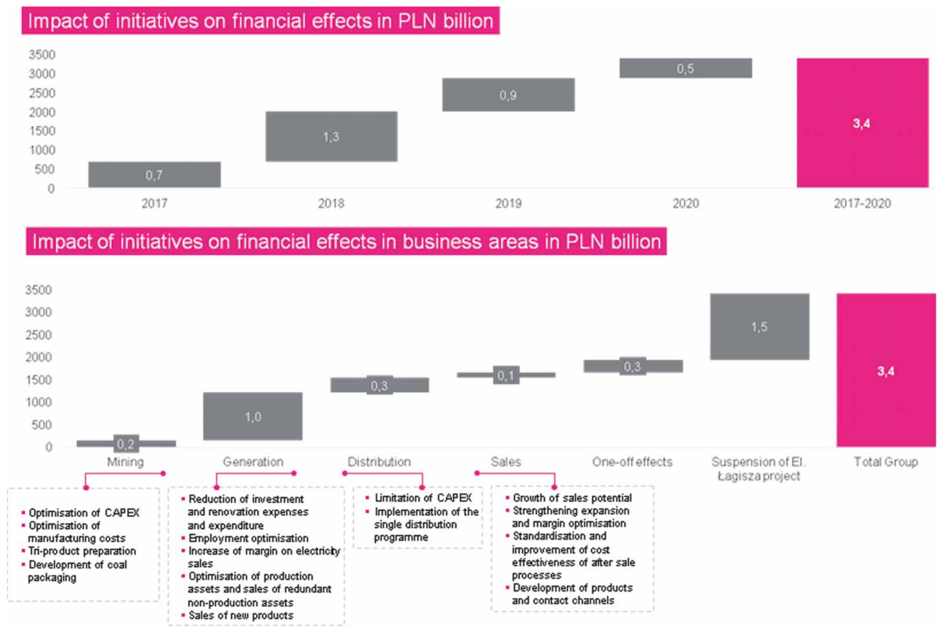


In 2016, under the Efficiency Improvement Programme savings of PLN 478 million were achieved in the Group, which constitutes 37% of planned savings, including PLN 263 million affecting EBITDA, PLN 215 million – CAPEX savings. The Generation Area has the highest share in achieved savings. The highest level of savings, amounting to PLN 272 million, was gained in the scope of effectiveness in assets use.

b) Strategic Initiatives and rationalisation of investment in 2017–2020 assuming gaining the financial effect at a level of PLN 3.4 billion. The above effects comprise measures affecting the cumulative EBITDA increase by approximately PLN 1.2 billion and consisting in CAPEX reduction by approximately PLN 0.7 billion and PLN 1.5 billion due to suspension of investment in the new unit in Elektrownia Łagisza in 2017–2020, with the breakdown into individual areas of operations.

The figure below presents strategic initiatives and rationalisation of investment in the years 2017–2020.

Figure no. 10 Strategic initiatives and rationalisation of investment in the years 2017–2020



In accordance with the determined objectives, TAURON Capital Group will develop the Sales Area and customer service. In this scope, introduction of consistent high standards of customer service is planned in each area of the value chain as well as the development of modern and integrated sales and customer service channels.

In the Distribution Area the programme on “Single Distribution” will be continued, based in activities associated with harmonisation of processes and system and implementation of the optimum and consistent structure of TAURON Dystrybucja in order to improve the operating and investment effectiveness of this Area.

In the Mining and Generation Areas tasks associated with further improvement of cost effectiveness and investment effectiveness will be continued. Introduction of regulations related to the capacity market in Poland and the announced reform of the European Emissions Trading System (EU ETS) will be significant for the generation assets.

In 2017 the following strategic investment projects will be continued: the construction of the 910 MW coal-fired unit at Elektrownia Jaworzno III, the construction of the 450 MW gas unit at EC Stalowa Wola, the construction of the “Grzegorz” shaft at ZG Sobieski, the construction of the 800m level at ZG Janina and the investment programme at ZG Brzeszcze. Significant expenditure will be allocated for connecting of new consumers as well as for modernisation and development of the distribution grid.

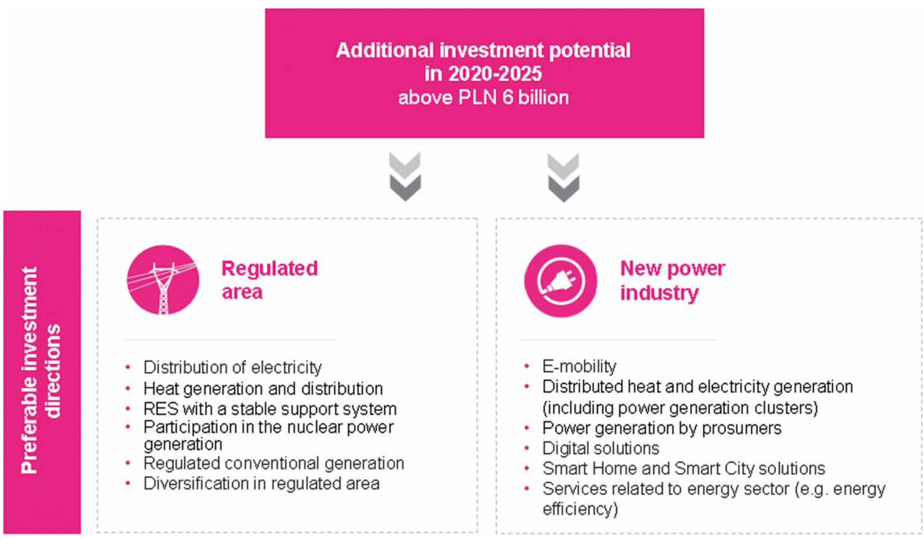
1.5. Characteristics of the policy and development directions of TAURON Capital Group

The Strategy of TAURON Capital Group determines its development in a shorter and longer-term perspective. Tasks for individual Business Areas of TAURON Capital Group have been defined in detail up to 2020 and financial effects of those tasks have been determined. The priority is to maintain the stable financial situation and to build solid foundations for growth in the changing environment. The implementation of this priority is fostered by the efficiency improvement programme and strategic initiatives aimed at cost and investment optimisation. In the period up to 2020 significant capital expenditure is planned, with the value of approximately PLN 18 billion, including over a half to be allocated for distribution assets generating the most stable revenues of TAURON Capital Group. At the same time, the Strategy determined priority directions of innovative and research-development activity which will provided basis for the development of new products and services in a longer-term perspective. In order to achieve this goal TAURON Capital Group adopted a new model of innovative and research-development activity, by creating a dedicated central organisation for the management and coordination of the said activity and allocating a budget at a level of 0.4% of revenue.

In a longer-term perspective, the Strategy assumes full use of the potential contained in assets of TAURON Capital Group, fostering innovation, organisational culture and predominantly, a broad client base. The Strategy assumes that in the years 2020–2025 TAURON Capital Group will gain the additional investment capacity at a level of approximately PLN 6 billion, to be allocated for projects which will generate value for TAURON Capital Group in a longer-term perspective. Investment is assumed in regulated areas, such as electricity distribution as well as heat distribution and generation, RES (provided that the stable support system is available), regulated conventional generation and in the area of new energy, i.e., for example, electromobility, scattered electricity and heat generation, smart solutions.

The figure below presents the outlook of investment directions after 2020.

Figure no. 11 Outlook of investment directions after 2020



The major competitive advantage of TAURON Capital Group is the base of 5.5 million clients. The most important activities in a short-term and long-term perspective will comprise relatively low capital-intensive activities associated with the development of products and services offer for consumers as well as the development of new activities based on TAURON Capital Group competence. The Strategy assumes that in 2025 new businesses will generate approximately 25% of the total margin or revenues on sales of the Sales Segment.

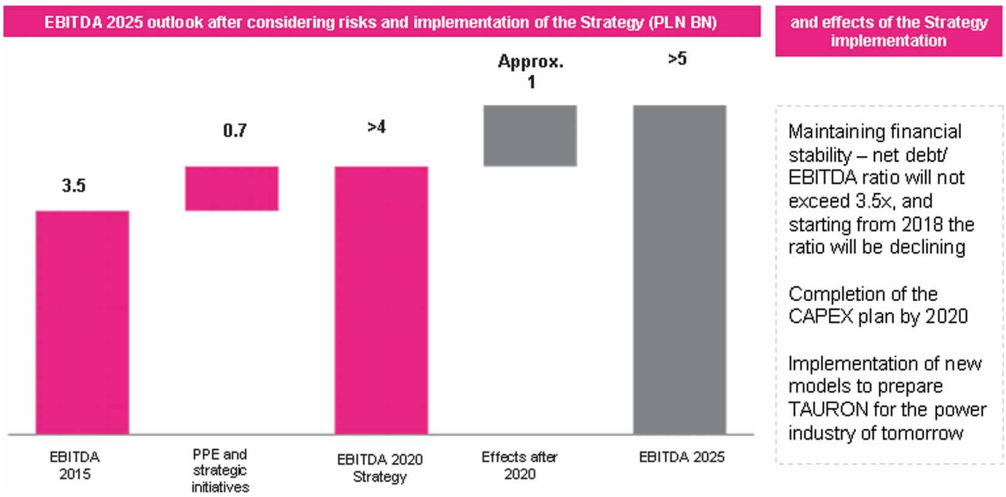
1.5.1. Perspective objectives and financial assumptions of the Strategy

Activities defined in the Strategy will enable the accomplishment of key objectives determined for TAURON Capital Group:

1) EBITDA over 4 billion in 2020.
2) Keeping the net debt/EBITDA covenants below 3.5.
3) Maintaining the high level of Customer Satisfaction Index (CSI).
4) Power plants with positive financial flows by 2020.
5) Maintaining the client base.
6) Leader in unit margin among 4 biggest energy vendors in Poland.
7) The new businesses will constitute at least 25% of the revenue/margin in 2025.

The figure below shows EBITDA 2025 outlook after considering risks and implementation of the Strategy and effects of the Strategy implementation.

Figure no. 12 EBITDA 2025 outlook after considering risks and implementation of the Strategy and effects of the Strategy implementation



Activities planned for the nearest years will enable to curb the decline in profitability. This will take place through increasing the production of electricity, coal and, to a minor extent, heat, simultaneously maintaining the stability in the Distribution Area.

1.5.2. Implementation of strategic investment

Major strategic investment projects under implementation

The table below presents the activities carried out in TAURON Capital Group in 2016, in connection with the implementation of the key strategic investment projects.

Table no 4. Implementation status of the major strategic investment projects

No.	Investment	Status of investment implementation
1.	Construction of the CCGT unit with the capacity of 449 MW_e, including the heat generation component with the capacity of 240 MW_t in Stalowa Wola (the investment is implemented with participation of the strategic partner – Polskie Górnictwo Naftowe i Gazownictwo S.A. (PGNiG)). **Contractor**: the contract with Abener Energia S.A. was rescinded Completion of the project is foreseen under the EPCM formula (contract manager).	In January 2016 the contract with the general contractor, Abener Energia S.A. was rescinded. Maintenance works of installed machines and equipment were carried out on an on-going basis and talks with suppliers and subcontractors of major installations were carried out. The concept of investment completion under the contract manager – EPCM formula and contracting of contractors was prepared, the development of tender documentation in this scope is in progress.

No.	Investment	Status of investment implementation
	Scheduled date of investment completion: 2019 **Progress level**: 85% **Expenditure incurred**: PLN 963.7 million	On 27 October 2016 a contingent agreement was concluded between TAURON, PGNiG and EC Stalowa Wola concerning determination of key boundary conditions for the project restructuring (the agreement regulates the conditions related to settlement of contractual penalties, market rules for pricing formulas used so far, financial restructuring issues, including the change of the financing formula to corporate finance, while maintaining the involvement of financial institutions). Negotiations with participation of the strategic partner and involved banks in the scope of further investment financing formula are in progress. Stocktaking of the completed part of the subject matter of the contract was completed.
2.	Construction of a new power unit with the capacity of 910 MW_e, for supercritical parameters on the premises of Elektrownia Jaworzno III (TAURON Wytwarzanie). **Contractor**: RAFAKO S.A. and Mostostal Warszawa S.A. consortium **Scheduled date of investment completion**: 2019 **Progress level**: 30.5% **Expenditure incurred**: PLN 2,055 million	The implementation of the project focused on the construction works and assembly of steel constructions. In the scope of main buildings, the top slab of the turbogenerator was installed and the assembly of the boiler load-bearing construction, including the grate was completed. The reinforced concrete structure of the electrical nave was constructed, including the underground cooling water pump station and pylon structure. Elements of the discharge system for the engine room and boiler house were delivered to the site, inter alia, membrane walls of the boiler, the generator. The erection process of successive cycles of the cooling tower coat was ongoing, the assembly of steel constructions of main buildings and installations in pylons was continued and construction works were carried out in the building of gypsum storage and electrical nave. Works were carried out in the area of surface reinforced concrete cooling water pump station and the building of electrical switching station of the flue gas desulphurisation system. The assembly of the absorber coat for the flue gas desulphurisation installation and assembly of cylindrical bunkers was ongoing. In the scope of auxiliary and accompanying services, works in the area of external ash disposal system and external carburisation system – part 1 and 2, were continued. Contractors for the power discharge system, kindling oil and office building were selected. Public procurement procedures for the selection of contractors for the track layout system, water and sewage network, flyovers of pipelines, heat and steam network, compressed air system, water supply system, water treatment station and wastewater treatment plant were continued. Preparations to announce the tender for the selection of the telecom and IT network were in progress. On 1 March 2017 the consortium signed an annex concerning the extension of the agreement for construction of the unit. As at that date, the level of project progress reached 31.8%.
3.	The construction of the installation for flue gas de-nitrification in 6 units of Jaworzno III Power Plant and 4 units of Łaziska Power Plant belonging to TAURON Wytwarzanie. **Contractor**: Jaworzno III Fortum Power and Heat Oy and ZRE K-ce, Łaziska – Strabag Sp. z o.o. and Strabag AG **Date of investment completion:** 2016 **Progress level** – Jaworzno III**:** 100% **Expenditure incurred**: PLN 655.5 million **Progress level** – Łaziska: 100% **Expenditure incurred**: PLN 418.4 million	At Elektrownia Jaworzno III modernisation of the installation of six units with the capacity of 200 MW was completed in 2016, using the SNCR technology (selective non-catalytic reduction of flue gas denitrification), reaching the assumed level of nitrogen oxides of 200 mg/m^3. At Elektrownia Łaziska the project was completed in 2015.
4.	Construction of the "Grzegorz" shaft (TAURON Wydobycie), including the infrastructure (surface and underground) and the accompanying headings. **Contractor**: The selection of the general contractor of the shaft is scheduled in the 1st quarter of 2017. **Scheduled date of investment project completion**: 2023 **Progress level**: 20% **Expenditure incurred**: PLN 84.5 million	Detailed documentation for the shaft was performed and accepted. Construction of the electrical switching station of the "Grzegorz" shaft and 2x20kV MV cable lines supplying the station was completed. The agreement with the general contractor for drilling of mining headings to the "Grzegorz" shaft at a level of 540 m was concluded. After handing over the site of works, drilling of mining excavations to the shaft was commenced. Under the conducted procurement procedure the contractor for the construction of the shaft, including the surface infrastructure, was selected (KOPEX Przedsiębiorstwo Budowy Szybów and Famur Pemug). In accordance with the verdict of the National Appeal Chamber, the selection was cancelled and the reassessment and selection was started.

No.	Investment	Status of investment implementation
5.	Construction of a 800 m level at ZG Janina in Libiąż (TAURON Wydobycie). **Contractor**: Consortium of KOPEX S.A. and KOPEX Przedsiębiorstwo Budowy Szybów S.A. (main task – shaft drilling) **Scheduled date of investment project completion**: 2020 **Progress level**: 49% **Expenditure incurred**: PLN 252.8 million	Works associated with the construction of the stone belt haulage and the road-railway system constituting a part of modernisation of the coal mechanical processing plant were completed. Drilling of horizontal headings (ventilation gallery) was completed. Works associated with deepening of the Janina shaft to the target depth of 822.5 m were carried out. The ventilation circuit at a level of 770m was also closed. Works related to shaft reinforcement and drilling of headings at a level of 800m are in progress. Works of the Tender Commission for the construction of the shaft surface infrastructure were commenced.
6.	Brzeszcze investment programme **Contractors**: TRANS-JAN, FAMUR and KOPEX Machinery Consortium, FAMUR and KPRGiBSz Consortium, MAS and Carbospec Consortium, Elektrometal Cieszyn **Scheduled date of investment completion**: 2025 **Progress level**: 21% **Expenditure incurred**: PLN 100.5 million	Reconstruction of the mining heading at level 510, drilling of horizontal headings and construction of the facility for small coal sales (‘nut’ and ‘peas’ assortments). The delivery of a longwall complex for longwalls at level 510 was completed. Moreover, agreements and deliveries for the construction of auxiliary infrastructure are executed, inter alia, in the scope of haulage automation and visualisation and installation of a hydrant network, including an internal fire protection installation for the Coal Mechanical Processing Plant.
7.	Construction of new generation capacity in co-generation at a level of 50 MW_e and 86 MW_t at ZW Tychy (TAURON Ciepło). **Contractor**: Elektrobudowa S.A. **Date of investment completion**: 2016 **Progress level**: 100% **Expenditure incurred**: PLN 597.9 million	In January 2016, the co-generation unit was successfully synchronised with the power system. In March 2016, adjustment operation of the unit was completed; required tests and trial were passed. On 20 June 2016 the unit was commissioned.

Project associated with the construction of the nuclear power plant

In relation to earlier activities arrangements concerning the joint implementation of the nuclear energy project in Poland, on 15 April 2015, TAURON, KGHM Polska Miedź S.A. (KGHM) and ENEA, as Business Partners, and PGE concluded the agreement for the purchase of shares in PGE EJ1 – a special purpose vehicle responsible for the preparation and execution of the investment comprising the construction and operation of the first Polish nuclear power plant with the capacity of approximately 3 thousand MW_e (the Project). Business Partners acquired 10% of shares each (30% of shares in total) in PGE EJ 1 company from PGE. TAURON paid the amount of PLN 16,044,000 for the shares purchased. At the same time, one of the commitments arising from the Shareholders' Agreement concluded between Business Partners and PGE on 3 September 2014 was fulfilled.

Pursuant to the Shareholders' Agreement, the parties committed, proportionally to the number of shares they hold, to finance the activities falling to the stage of the project development.

The Shareholders' Agreement provides that further decisions related to the project, including the decision concerning the declaration of continued participation of individual parties (including TAURON) in the consecutive stage of the Project, will be made after the completion of the preliminary stage.

Under the execution of the aforementioned Shareholders' Agreement, on 29 July 2015 the Extraordinary SM of PGE EJ 1 company adopted the resolution on increasing of the share capital from the amount of PLN 205,860,000 to the amount of PLN 275,859,450, i.e. by the amount of PLN 69,999,450 through creating 496,450 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 69,999,450. Accordingly, TAURON took up 49,645 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 6,999,945, which were covered by the cash contribution in the amount of PLN 6,999,945.

On 16 October 2015 the increase in the share capital of the PGE EJ 1 sp. z o.o. company was registered in the National Court Register.

On 21 December 2016 the Extraordinary SM of PGE EJ 1 special purpose vehicle adopted the resolution on increasing of the share capital from the amount of PLN 275,859,450 to the amount of PLN 310,858,470, i.e. by the amount of PLN 34,999,020 through creating 248,220 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 34,999,020. Accordingly, TAURON took up 24,822 new shares with the nominal value of PLN 141 per share and with the total nominal value of PLN 3,499,902, which it covered by the cash contribution at a level of PLN 3,499,902.

On 15 February 2017 the increase in the share capital of the PGE EJ 1 sp. z o.o. company was registered in the National Court Register.

Project on construction of the CCGT unit with the capacity of 413 MW_e, including the heat generation component with the capacity of 266 MW_t on the premises of Elektrownia Łagisza

In the Strategy adopted on 2 September 2016, under the priority of providing financial stability of TAURON Capital Group, the Project on construction of the CCGT unit at Elektrownia Łagisza in TAURON Wytwarzanie was suspended due to the loss of business justification. The completion of the investment was initially planned in 2019. It will be possible to resume the project in the case the regulatory and market environment turns favourable.

Project on construction of the CCGT unit at Elektrownia Blachownia Nowa

On 28 July 2016 TAURON, KGHM and TAURON Wytwarzanie signed the agreement under which they jointly decided to withdraw from execution of the project for the construction of CCGT unit at Elektrownia Blachownia Nowa Sp. and terminate the Shareholders' Agreement binding KGHM and TAURON Wytwarzanie, and commence the liquidation of Elektrownia Blachownia Nowa company. The project has been suspended since 2913. The Parties started the liquidation of the company.

Detailed information concerning the aforementioned event is included in subsection 7.2.1 hereof.

Capital expenditure

In 2016, the capital expenditure of TAURON Capital Group amounted to PLN 3,816.8 million and it was higher by approximately 8.6% as compared to the expenditure incurred in 2015, which amounted to approx. PLN 4,175.5 million. This results mainly from the decline of expenditure in Generation and Distribution Segments.

The table below presents the selected capital expenditure incurred in 2016, the highest in terms of value, within TAURON Capital Group Business Areas.

Table no 5. The highest capital expenditure in terms of value, incurred in 2016 within TAURON Capital Group Business Areas

Specification	Capital expenditure (PLN M)
Distribution	
Modernisation and reconstruction of existing grids	953
Construction of new connections	591
Generation	
Construction of new capacity at Elektrownia Jaworzno III (910 MW)	1,237
Construction of new capacity in co-generation at ZW Tychy (including the construction of BC-50 unit)	107
Investment associated with the development and maintenance of heating networks	57
Modernisation of hydroelectric power plants	18
Construction of flue gas de-nitrification installation and modernisation of units at Elektrownia Jaworzno III	11
Mining	
ZG Brzeszcze investment programme	105.5
Construction of a 800 m level at ZG Janina	61
Construction of the "Grzegorz" shaft, including the construction of the infrastructure and the accompanying headings	24

Detailed information concerning the capital expenditure incurred in individual Segments of TAURON Capital Group activity is included in section 2.3. of this report.

1.5.3. Assessment of implementation capacity of investment projects

Strategic investment of TAURON Capital Group as well as its financing is managed centrally at a level of the Company. On the basis of conducted analyses, the Management Board of the Company assesses that TAURON Capital Group is able to finance the current and future investment projects included in the Strategy from funds generated from operating activities and by acquisition of debt financing. The aforementioned assessment includes the change of the formula for financing of the 910 MW unit at Jaworzno III Power Plant assuming the separation of an organised part of the enterprise and selling the shares to third party partners, provided they do not acquire a controlling stake. The planned change in the financing formula of this project is an additional element stabilising the financial situation of TAURON Capital Group.

1.5.4. Building of TAURON Capital Group value

TAURON Capital Group conducts activities in all key segments of the energy market, i.e. in the area of coal mining, generation, distribution as well as trading in electricity and heat. The Strategy assumes that each Business Area will build the value of TAURON Capital Group, however, in the manner adjusted to market conditions for a given segment. The Sales Segment as well as new products and services constitute this area of activity which will be intensively developed by TAURON Capital Group. TAURON Capital Group is changing its profile towards full concentration on the customer. It means, through building sustainable relations with customers, introduction of harmonised 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 the current highest standard. The Sales Area and customer service will be the main areas of building the value of TAURON Capital Group. The area of electricity Distribution is the most stable area in terms of share in generating EBITDA of TAURON Capital Group. TAURON Capital Group plans to maintain the stable role of the Distribution Area and continue the existing investment policy. Through further modernisation and extension of the distribution grid, TAURON Capital Group will be able to fulfil the requirements in the scope of security and quality of supplies. The Generation and Mining Areas will continuously improve cost effectiveness and operating efficiency, while the potential development of conventional generation will depend on the market situation or regulations favourable for conventional generation, i.e. introduction of such solutions as the dual commodity market.

1.5.5. Directions of innovation development and research and development activity

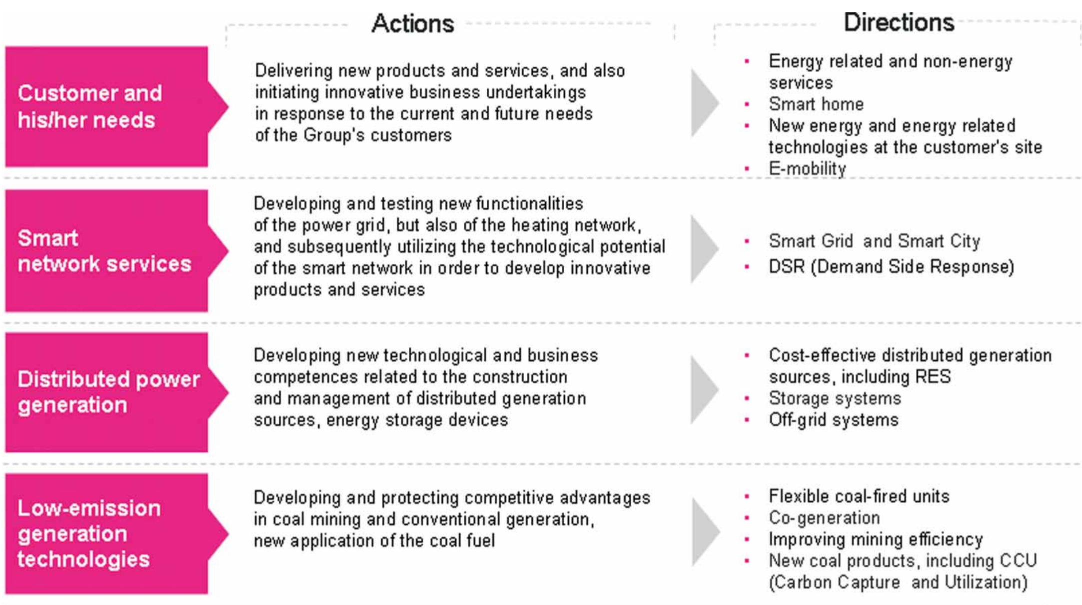
In the Strategy adopted in September 2016 TAURON Capital Group focuses on the dynamic development of the research and development area as well as innovation (R&D&I), identifying it as a path to new revenues in the future. As of 2017, allocation of minimum 0.4% of consolidated revenue for R&D&I is assumed, as well as the development based on, inter alia, Corporate Venture Capital (CVC) and the long-term return on the portfolio, as well as the annual revision in relation to the financial situation.

The Strategy also defines four priority directions of innovative and research-development activity:

1. Customer and its needs.
2. Smart grid services.
3. Scattered energy.
4. Low-emission generation technologies.

The figure below shows priority directions of innovative and research-development activity.

Figure no. 13 Priority directions of innovative and research-development activity



In the fourth quarter of 2017 works concerning the development of the Strategic Research Agenda (SAB) were undertaken. The document will translate the goals indicated in the Strategy Document into a “roadmap” of the R&D&I activity in TAURON Capital Group, capturing the specific challenges in each of the aforementioned four directions, simultaneously going beyond the perspective of the currently applicable Strategy within the adopted timeframe.

1.5.6. Important achievements in research and development

In 2016 companies of TAURON Capital Group carried out many research and development projects, including co-financed from external sources. The most significant projects are presented in the table below.

Table no 6. Selected projects carried out in 2016 by companies of TAURON Capital Group, co-financed from external sources

No.	Projects/programmes/tasks	Source of co-financing
1.	• Project *CO_2-SNG*, comprising chemical accumulation of energy through production of methane from the captured CO_2. • The *POLYGEN* project whose concept is based on using the polygeneration processing system in the process of gasification of locally available fuel (including selected waste fractions). • The *Smart Home* project, comprising the creation of a system of integrated devices allowing for effective remote management of electrical equipment and controlling of security at home. • The *Prointerface* project, comprising the construction of a system for individual assessment of disruptions in electricity quality in the distribution grid, including the power electronic interface to connect dispersed renewable energy sources.	Community of Knowledge and Innovation – KIC InnoEnergy (KIC InnoEnergy)
2.	• The *GEKON* Programme under which the project was executed in the scope of dynamic management of transmission capacity of power grids with the application of innovative measurement techniques. • The Applied Research Programme under which the project was implemented in the scope of production of demineralised water to replenish the water-steam circuit by means of electromembranary treatment.	National Centre for Research and Development (NCBR)
3.	• The *CERES* project aimed at introduction of a number of technological improvements in order to reduce the risk associated with produced mining waste.	The Research Fund for Coal and steel of the European Union
4.	• The *ICP4Life* project concerning the construction of the integrated collaborative platform for managing the product-service engineering lifecycle. • The *MOBISTYLE* project related to technological solutions to enable positive influence on clients' behaviour through raising consumers' awareness and the feeling of ownership.	Horizon 2020: Framework Programme for Research and Innovation

One of the most significant research and development undertakings implemented in 2016 in TAURON Capital Group is the *CO_2-SNG* project, related to CO_2 processing to synthetic natural gas with the use of electricity surplus from RES. The project is implemented by the international consortium grouping Polish and French entities, where TAURON Wytwarzanie is the consortium leader. The scope of the project covers transformation of carbon dioxide generated as a result of fuel combustion in industrial installation into synthetic natural gas – SNG. This gas will be generated as a result of CO_2 reaction with hydrogen derived from the electrolysis process, supplied by the surplus of cheap electricity coming from RES in the valleys of power system loads. The project assumes that this may be the method for storage of electricity surplus from renewable sources and simultaneously, a perspective solution for management of CO_2 generated in installations of TAURON Capital Group. For the implementation of the project, co-financing from KIC InnoEnergy was acquired.

The *POLYGEN* project launched in 2016 with the participation of TAURON Wytwarzanie received funding from the same source. The aim of the project is the development of the technological solution filling the market niche of environmentally-friendly and economically effective systems of thermal processing of municipal waste for small- and medium-scale applications. The concept of the project is based on using the polygeneration system generating three usable products in the gasification process of locally available fuel (e.g. selected waste fractions): heat, electricity and synthetic natural gas – SNG.

In 2016 the Company, jointly with partners from the EU countries, carried out works under the project on *An Integrated Collaborative Platform for Managing the Product-Service Engineering Lifecycle – ICP4Life*. It is the first project in TAURON Capital Group, financed under the Horizon 2020 programme. Project deliveries should open a new platform for companies of TAURON Capital Group for the purpose of cooperation between the energy supplier and the client, where completely new products will be developed.

In the past year the MOBISTYLE project received a positive decision on co-financing from the Horizon 2020 programme. The full name of the project is: Motivating end-users behavioural change by combined ICT based tools and modular information services on energy use, indoor environment, health and lifestyle. The overriding goal of the project is to introduce technological solutions to the market which will enable to affect positively customers' behaviour through raising the awareness and ownership feeling among consumers. The implementation of the project started in October 2016 and its results will be tested in five demonstration facilities in five different EU countries, including the area of implementation of AMIPlus initiatives in Wrocław.

In 2016, Companies of the Group took part in the preparation and submission of 27 applications for co-financing of research and development activities from the European Union funds, including the aforementioned *MOBISTYLE* and *POLYGEN* projects (Horizon 2020 and Research Fund for Coal and Steel of the European Union, KIC InnoEnergy, PARP, NCBR programmes), where the companies acted individually or as members of industrial and scientific-industrial consortia.

Moreover, in 2016 companies of TAURON Capital Group financed many other research and development activities from own funds, at various scale, enhancing the effectiveness of companies' performance and mitigating the environmental impact of processes they conduct.

In this area, cooperation of TAURON Distribution and Przedsiębiorstwo Komunikacji Miejskiej in Jaworzno in the scope of charging technology for electric buses, initiated last year, should be mentioned. Companies perform the annual test of the electric vehicle and charging infrastructure under standard operating conditions.

In 2016 works concerning launching of the Research Programme for the Power Sector (PBSE) by NCBR were carried out. The Feasibility Study of PBSE was submitted to NCBR in December 2014 by TAURON in cooperation with other enterprises from the energy sector, trade organisations and leading national universities. As a result of the multi-stage process of preparation and negotiations on, inter alia, the scope, the schedule and the budget of PBSE, in September 2016 NCBR launched the first call for proposals under this programme. The two-year period of preparation of companies of TAURON Capital Group resulted in elaboration and submission of 18 applications for co-financing of research and development projects under this programme, including 3 applications submitted by the Company. It is expected that the Programme shall provide support for the intensification of innovation in the energy sector, and consecutive competitions announced under the Programme will also support the directions of activities undertaken by TAURON Capital Group. At present, works in the scope of evaluation of submitted applications are in progress. NCBR decision on co-financing of individual projects is expected in the 2nd quarter of 2017.

The Company also conducted active measures in the scope of building the cooperation mechanisms between industry and science. In this scope, the Company participated in the activities of the Motorway of Technology and Innovation Institute, established in 2014, representing a new platform for cooperation between industry and Polish universities.

In 2016 the Company continued its activities implemented under KIC InnoEnergy, in particular, the Polish node of CC Poland Plus sp. z o.o. with its seat in Kraków (one of six in the EU). TAURON has the status of Associated Partner in the structures of KIC InnoEnergy. One of the areas of TAURON's interest covers the so-called clean coal technologies. At the same time, conducting research and coordination of activities in this area are the main activities of the company CC Poland Plus sp. z o.o., in which the Company is one of the shareholders. In 2016, representatives of the Company were involved in the activities of KIC InnoEnergy, associated with the evaluation of projects/initiatives proposed for implementation by other partners acting within KIC InnoEnergy structures, both on the national and on the international level.

In response to the Scale Up competition announced in mid-2016 by the Polish Agency for Enterprise Development (PARP), the application concerning the Pilot Maker Programme was submitted to the competition. This programme, combining the potential of start-ups with the infrastructure, experience and resources of large enterprises, received a positive opinion of PARP and a co-financing of almost six million. The leader of the programme is the techBrainers company, TAURON is the main partner and other partners include well-known Kross S.A and Amplus sp. z o.o. companies.

From the point of view of TAURON, the Pilot Maker programme is the first tool for building the area of cooperation between TAURON Capital Group and Start-Ups. At the same time, creating innovative product solutions in cooperation with Start-Ups is the area of activities to be undertaken by the special purpose vehicle, Magenta Grupa TAURON, established by TAURON in 2016. The business model of the new company was based on the latest methodologies of work demonstrating a possibility of integrating ideas and projects of Start-Ups with large enterprises. The company will deal, inter alia, with preparation of projects in the scope of smart technologies for home and solutions for transport supplied with electricity.

1.6. Business Model of TAURON Capital Group

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.

Considering changes taking place in the surroundings of TAURON Capital Group and challenges faced by TAURON Capital Group, on 4 May 2016 the Management Board of the Company adopted a new *Business Model of TAURON Group*.

The Business Model determines the business structure of TAURON Capital Group, defines the high-level architecture of processes and contains guidelines concerning key performance indicators of units constituting TAURON Capital Group. In this way, it describes the assumptions of organisation building and it is an element of the Strategy implementation.

1.6.1. Assumptions of the Business Model

The Business Model is based on assumptions understood as a set of general guidelines driving the works on the document. These assumptions include building of TAURON Capital Group value, focusing on Clients, transparent distribution of duties and responsibilities, effective information exchange, use of employees' knowledge, volatility of the Business Model, organisational cohesion of TAURON Capital Group.

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 entities, including, in particular, setting the operating objectives of companies, enabling the achievement of effects assumed in the new Strategy.

Within TAURON Capital Group, besides Business Areas established by the Company Management Board, comprising companies of TAURON Group, the established management areas operate within which the relevant cooperation rules apply.

In addition, within TAURON Capital Group, permanent Committees operate, including:

1) Project Assessment Committee,
2) TAURON Group Management Committee,
3) TAURON Group Compliance Committee,
4) Risk Committee.

The aforementioned Committees were established in order to enable performing of operations in accordance with principles of operating consistency, in compliance with the law and interests of TAURON Capital Group and its stakeholders.

The Committees fulfil the following functions:

1) opinion-making function for the Company Management Board,
2) decision-making function,
3) supervisory function for the management boards of TAURON subsidiaries.

The underlying task of the Committees is to monitor the implementation of coherent actions compliant with the *TAURON Group Code* and for the benefit of TAURON Capital Group business. The specific tasks of the Committees are defined in detail in the by-laws of their activity adopted by the Company Management Board.

1.6.2. Changes in the management rules of the Company and TAURON Capital Group

Changes in the management rules of the Company

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 all 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 Articles of Association to the competence of the General Meeting or the Supervisory Board lie within the competences of the Company 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 by competences of the Management Board as a collective body are described in detail in item 6.8.1. of this report.

In 2016 changes in the rules of managing the Company were introduced, arising from the new adopted Business Model, defined in the *Organisational Regulations of TAURON Polska Energia S.A.* (Organisational Regulations). In accordance with the Organisational Regulations, the Company is managed directly by the Management Board of the Company as well as through proxies, Executive Directors, Managing Directors or attorneys.

In accordance with the amended Organisational Regulations, the Company implements its tasks through:

1) **selected business units**:
   - Divisions comprising independent positions and business units reporting to individual members of the Management Board and supervised by them.
   - Offices, constituting business units reporting directly to individual members of the Management Board. The activities of the office are managed by the Office Manager.
   - Teams, constituting business units reporting directly to Executive Directors or Managing Directors. The activities of the team are managed by the Team Leader.
2) **independent positions**:
   - The Managing Director manages and leads the work of subordinated Executive Directors and Teams.
   - The Executive Director manages and leads the work of subordinated Teams.
   - Other independent positions which may be entrusted to Attorneys, Coordinators, Consultants or Specialists.
3) **temporary organisations** – Project Teams established with the aim of implementation of tasks and projects of the Company.

The **President of the Board** manages current business of the Company and takes decisions on all issues concerning the Company, which are not subject to decisions of the Management Board or other governing bodies of the Company, and supervises the performance of the division which reports to him directly.

In particular, the President of the Management Board:

1) manages the internal business of the Company and represents it within the external contacts,
2) coordinates all the issues connected with the performance of the Company Management Board,
3) performs actions in the scope of labour law on behalf of the Company (the employer),
4) supervises the performance of the division which reports to him directly,
5) issues the internal regulatory acts and intra-corporate regulatory acts in accordance with the binding regulations,
6) takes decisions related to managing of the Company business as usual,
7) performs all the real functions and legal acts, taking into consideration implementation of the Company's goals and targets,
8) undertakes any other activities providing for effective and efficient performance of the Company.

Vice-Presidents of the Management Board:

1) manage the current business operations of the Company within the scope delegated as well as supervise the performance of the divisions which report to them directly,
2) take decisions concerning issues which are not subject to the competence of the Management Board, within the scope of functions delegated to the subordinated independent positions and business units as well as other decisions within the powers of attorney and authorisations granted to them by the Management Board or the President of the Board, as well as:
3) manage the internal business of the Company and represent it within the external contacts,
4) supervise the performance of divisions which report directly to them,
5) take decisions related to managing of the Company business as usual,
6) perform all the real functions and legal acts, taking into consideration implementation of the Company's goals and targets,
7) undertake any other activities providing for effective and efficient performance of the Company.

Managing Directors and Executive Directors:

1) manage organisational units and/or independent positions reporting to them, being responsible for their performance results,
2) determine the goals, targets and tasks of subordinated business units or independent positions within their subjective competence,
3) coordinate the structures reporting to them, in accordance with the Company's interest and in compliance with the legal regulations,
4) implement the guidelines and recommendations of the relevant Member of the Management Board and keep them informed of the performance of subordinated business units / independent positions,
5) undertake any other necessary activities providing for effective and efficient performance of the tasks assigned,
6) Cooperate with other Members of the Management Board, separated business units and independent positions in the scope of tasks performed.

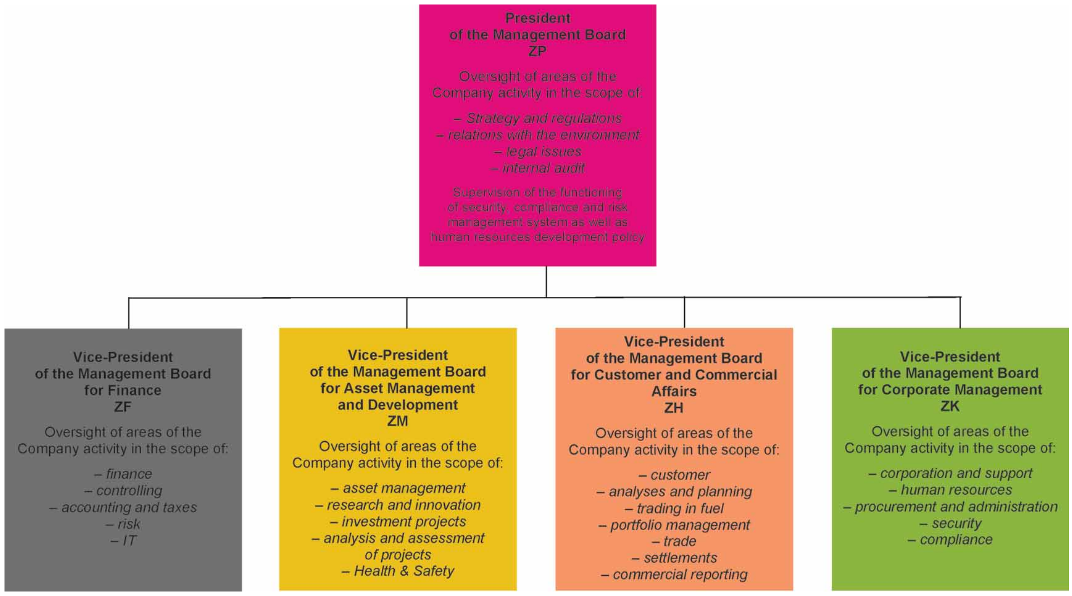
Business relations in the Company are based on the principle of a single person management which means that each employee has a single direct supervisor in business relations from whom he/she receives instructions and assignments and tow whom he/she is responsible for their execution. A employee receiving an instruction from a superior should execute such instruction notifying the direct supervisor thereof. Moreover, establishing of an additional reporting line is admitted in relation to independent positions and business units directly reporting to Members of the Management Board. The reporting line is based on a possibility to acquire direct information and issue individual official instructions.

A separate reporting type is the project reporting which is of temporary nature. Such reporting occurs in relations among employees of the Company or employees of the Company and companies of TAURON Capital Group, regardless their business relations, and applies to persons who are members of a project team.

Changes in the organisational structure of the Company performed in accordance with the Business Model were aimed at optimisation of operations of the Company and TAURON Capital Group. Areas assigned to individual members of the Management Board of the Company were verified.

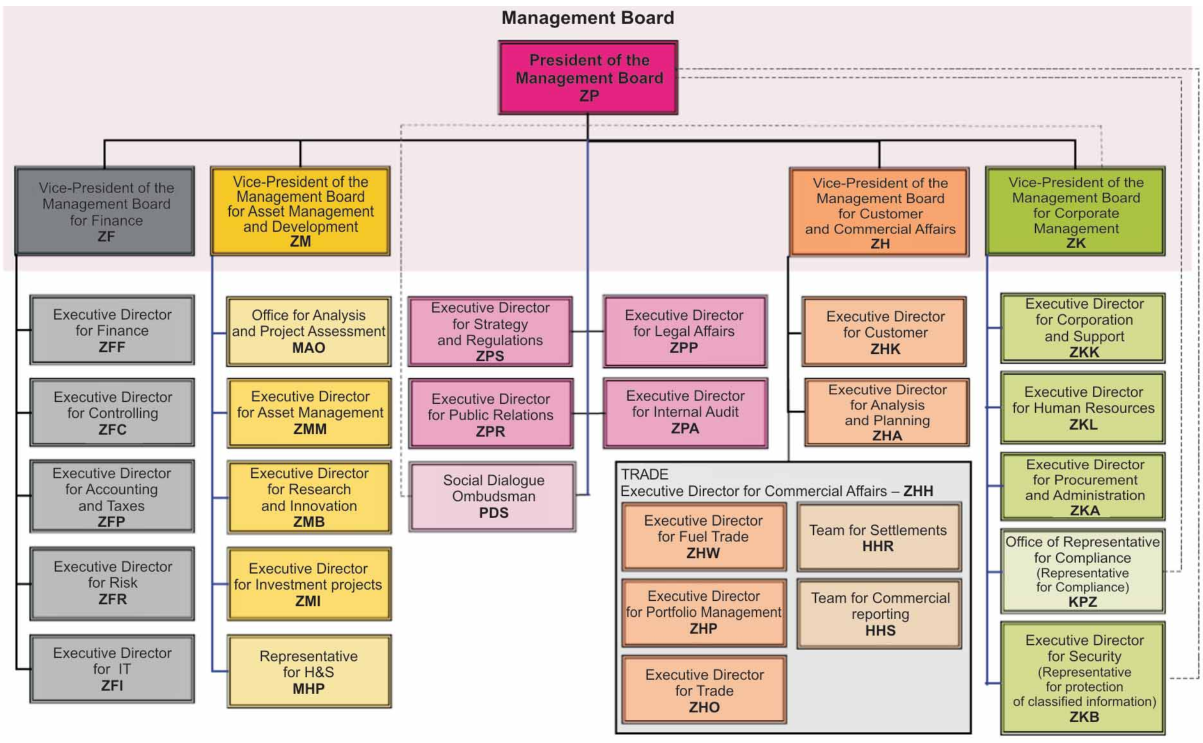
The figure below presents the distribution of responsibilities of Management Board Members.

Figure no. 14 Scheme of distribution of responsibilities of Management Board Members



The figure below presents the **structure of divisions reporting to individual Members of the Company Management Board,** to the level of business units and independent positions reporting directly to the Members of the Management Board, according to the status as at the day of drawing up this report.

Figure no. 15 Organisational chart of TAURON as at the day of drawing up this report



Changes in the management rules of TAURON Capital Group

Adopting of the new Business Model by the Management Board on 4 May 2016 started activities changing the organisation of operation of TAURON Capital Group business units. The Business Model defines the assumptions of operation (management) of TAURON Capital Group and indicates the distribution of tasks and responsibilities among defined units:

Corporate Centre – the superior business unit responsible for management of TAURON Capital Group activities and taking the most important decisions affecting TAURON Capital Group, Business Areas, Centres of Common Services and companies belonging to TAURON Capital Group.

Business Areas – seven areas of TAURON Capital Group core activity, defined in accordance with the links of electricity and heat production value chain, i.e.: Trade, Mining, Generation, Renewable Energy Sources (RES), Heat, Distribution and Sales.

Centre of Common Services – Centres of Common Services – units responsible for provision of specific support services (e.g. Accounting, IT, HR and payroll, insurance, customer service) in favour of other entities of TAURON Capital Group.

Five defined process streams around which activities of TAURON Capital Group shall concentrate underpin the construction of the Business Model, i.e.: Strategy, Finance, Asset Management and Development, Client, Corporate Governance and Support. The objective of distinguishing process streams is to pay greater attention to cross-sectional issues, referring to more than one Business Area, which will significantly determine the value of the Group in the future against other entities operating in the energy sector.

The figure below presents process streams around which operations of TAURON Capital Group shall be concentrated.

Figure no. 16 Process streams

1.6.3. Key process streams

The new Business Model identifies 23 mega processes passing through all units of TAURON Capital Group. In 2016, within the implementing activities, their owners were determined and the processes were decomposed to the lower level processes fully implemented in companies of TAURON Capital Group. For the processes implemented in TAURON company, a preliminary version of process documentation was elaborated, including diagrams showing the process and decision-making competence in detail. In the 1st half of 2017 intensive works related to improvements and common points will be were continued. By the end of the 1st half of 2017, issuance of new corporate regulations is planned, implementing the new Business Model in the scope of distribution of responsibilities and decision-making competence determining roles divided between the headquarters of TAURON Capital Group and the subsidiaries. Throughout 2017 the decomposition of the processes will continue and process documentation in companies of TAURON Capital Group will be developed.

The figure below shows the structure of processes in TAURON Capital Group (mega processes).

Figure no. 17 Structure of processes in TAURON Capital Group (mega processes)

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	

1.6.4. Business Areas of TAURON Capital Group

The operating activity of TAURON Capital Group is implemented based on seven Business Areas defined in accordance with the links of electricity and heat production value chain: Mining, Generation, Heat, Renewable Energy Sources (RES), Trade, Distribution and Sales.

The figure below shows the structure of TAURON Capital Group Business Areas.

Figure no. 18 Structure of TAURON Capital Group Business Areas

Business Areas					
Trade					
Mining	Generation	RES	Heat	Distribution	Sales

1.6.5. Centres of Common Services of TAURON Capital Group

Centres of Common Services (CUW) are the separated business units responsible for provision of specific support services, e.g. accounting, IT, HR and payroll, insurance, customer service, in favour of other units of TAURON Capital Group. The centralisation of support services is aimed at relieving the Corporate Centre and Business Areas from execution of processes which are not directly associated with the operations they conduct (so-called support processes) as well as at reducing costs of implementation of such processes owing to the benefits of scale and growth of operating effectiveness. Within the formal structure of TAURON Capital Group, CUW have been assigned to TAURON Obsługa Klienta.

2. OPERATIONS OF TAURON CAPITAL GROUP

2.1. Factors and unusual events significantly affecting the financial result achieved

2.1.1. Internal factors and their assessment

The following internal factors affected the operations and results of TAURON Capital Group in 2016, inter alia:

1) implementation of the OPEX Efficiency Improvement Programme in TAURON Capital Group, including the consolidation and restructuring projects, Voluntary Redundancy Programmes,
2) implementation of key investment projects, in particular, in the scope of construction of new and modernisation of the existing generation capacity, building new connections and modernisation of the existing distribution grids, heating networks, construction of underground excavations,
3) marketing actions in the scope of acquisition of new clients and loyalty activities in terms of maintaining existing clients,
4) centralising the financial management area in TAURON Capital Group, supported by such tools as: central model of financing, cash flow management policy with the cash pool, risk management policy in the financial area, insurance policy,
5) procurement management by the Company, in particular, fuel purchases for the needs of generation entities included in TAURON Capital Group.

Impact of the aforementioned factors on the financial result achieved in 2016 is described in item 4 of this Report. Effects of this impact are visible both in a short-term and long-term perspective.

2.1.2. External factors and their assessment

The following internal factors affected the operations and results of TAURON Capital Group in 2016:

1) Macroeconomic environment.
2) Market environment.
3) Regulatory environment.
4) Competitive environment.

2.1.2.1. Macroeconomic environment

The basic area of TAURON operations is the Polish market within which the Company takes advantage of positive trends occurring in it as well as is affected by such changes. The macroeconomic situation, both in individual sectors of economy and in financial markets, is a significant factor influencing the results achieved by the Company and TAURON Capital Group.

The GDP growth in Poland for 2016 reached the level of 2.8% (as compared to 3.9% in 2015). The domestic economy was predominantly driven by consumption of households, fostered by the favourable situation in the labour market and lack of growth in prices. At the end of 2016 the unemployment rate reached 8.3%, against 9.8% at the end of 2015, whereas the average level of wage in the national economy exceeded PLN 4,000 (against PLN 3,900 for 2015). The inflation rate for 2016 reached the value of -0.6% (deflation for 2015 amounted to -0.9%). A significant decline in the level of investment was the factor for which the GDP growth for 2016 reached a level significantly lower than in 2015.

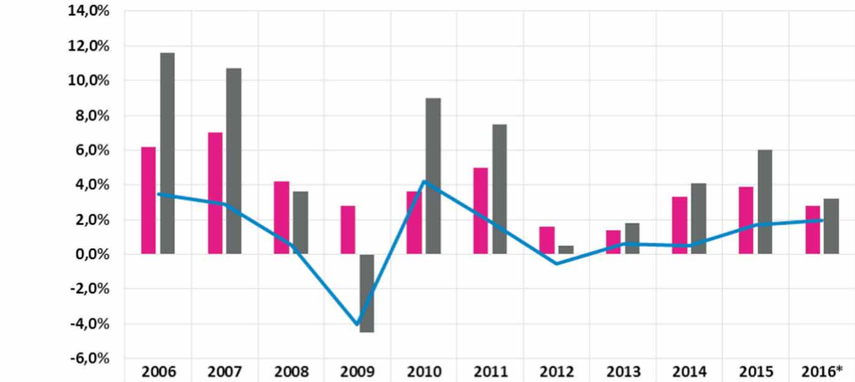
Throughout 2016 the average currency exchange rate increased – the EUR/PLN rate reached the average level of PLN 4.40 (against PLN 4.26 for 2015), whereas the USD/PLN rate reached the average level of PLN 4.20 (against PLN 3.90 for 2015).

A key factor affecting the results of the Company and TAURON Capital Group, depending largely on the economic growth rate, is the domestic demand for electricity and heat.

According to the data of Polskie Sieci Elektroenergetyczne S.A. (PSE), in 2016 a significant growth (1.97% YoY) in the domestic gross electricity consumption (KZEE) occurred, with the simultaneous growth of production in domestic power plants (0.53% YoY) – contrary to 2015, imports prevailed in the balance of interconnector exchange amounting to -2.0 TWh.

The figure below shows the growth of GDP, industrial output sold and change in KZEE.

Figure no. 19 Growth of GDP, industrial output sold and change in KZEE



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016*
GDP	6,2%	7,0%	4,2%	2,8%	3,6%	5,0%	1,6%	1,4%	3,3%	3,9%	2,8%
Industrial output sold	11,6%	10,7%	3,6%	-4,5%	9,0%	7,5%	0,5%	1,8%	4,1%	6,0%	3,2%
KZEE	3,5%	2,9%	0,5%	-4,0%	4,2%	1,9%	-0,6%	0,6%	0,5%	1,7%	2,0%

Data concerning GDP and industrial output sold for 2016 are based on preliminary estimates
Source: GUS, PSE

In 2016 a lower growth in industrial output sold was recorded as compared to 2015 (3.2% YoY according to the GUS preliminary forecasts), which was a phenomenon analogical to the scale of changes in GDP. At the same time, the growth in KZEE was stronger than in 2015, which occurred despite a slower pace of economic growth. The key non-economic reason included the average air temperatures in January, June, November and December 2016, as well as the fact that in August 2015 constraints in power supply occurred (power supply levels).

The figure below shows the KZEE process depending on the average monthly temperature.

Figure no. 20 KZEE process depending on the average monthly temperature

Source: PSE

In 2016, photovoltaic energy was the most dynamic area of the power industry, where the estimated growth in the capacity reached approximately 90 MW (approximately 95% YoY) and the total output reached approximately 120 GWh (growth by c.a. 124% YoY). Wind energy developed dynamically, although at a slower pace than in 2015, where the growth in the capacity installed by approximately 750 MW translated into the output in the range of 11.6 TWh (growth in production by 15.8% YoY).

A significant growth in production (by approximately 37.8% YoY) was also recorded in case of gas energy sector – in 2016 this area generated the total of 5.8 TWh. Production in coal-fired power plants (the basic fuel of TAURON Capital Group) amounted to 81.3 TWh at the national level, which means a minor decline in relation to 2015 (-0.65% YoY), whereas lignite-fired sources produced the total of 51.2 TWh in 2016, which makes a decline by 4.4% YoY.

Simultaneously, heat production increased at the national level. According to the ARE data for three quarters of 2016, the total of 183.95 PJ of heat was produced (by 1.2% more than in the corresponding period of 2015). Taking into account temperatures of November and December 2016 it should be expected that the heat production for the entire 2016 will show a higher growth rate.

2.1.2.2. Market environment

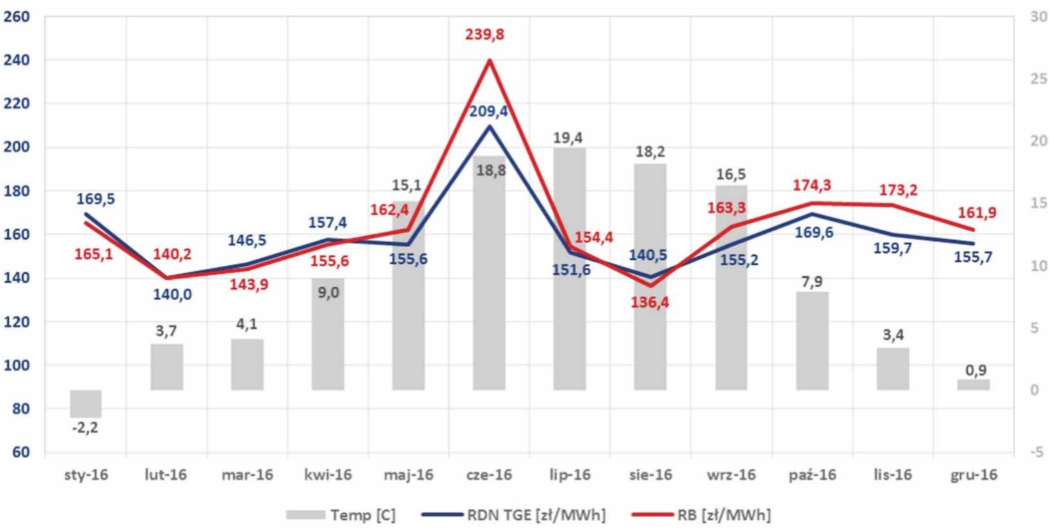
Electricity

In 2016 wholesale prices of energy in Poland recorded a slight growth in relation to 2015. The average price on the Day-Ahead Market (RDN) of Towarowa Giełda Energii S.A. (TGE) for 2016 amounted to PLN 159.22/MWh (+ PLN 2.27/MWh in relation to 2015), whereas the so-called CRO price on the balancing market (RB) reached PLN 164.19 /MWh(+ PLN 6.88/MWh on an annual basis). The major reason of slight growths in market prices in 2016 was the increased systemic demand for capacity which, on an annual basis, resulted in the growth of electricity consumption by over 3 TWh, to the level of 164.6 TWh. The impact of growth in electricity consumption was not set off even by relatively low coal prices, which dropped by PLN 0.99/GJ to the level of PLN 8.79/GJ. The growth of prices was also caused by the change in the electricity generation structure.

Despite commissioning of approx. 730 MW of new capacity in wind farms in 2016, a minor growth of production in RES did not result in the expected growth of production in this subsector. At the same time, in the previous year, a significant decline of production from cheap lignite-fired power plants was recorded, by as much as 4.4%, which had to be set-off by the growth of production in more expensive power plants, e.g. gas-fired, where production on an annual basis increased by 37.8% to the level of 5.8 TWh. In addition, the National Power System (KSE) was supported by imported energy at a quantity of almost 2 TWh.

The figure below presents the average monthly electricity prices on the SPOT and RB markets and the average temperatures.

Figure no. 21 Average monthly energy prices on the SPOT and RB markets and the average temperatures



On the forward market, contracts for 2017 were subject to relatively dynamic changes even at the beginning of the year. Traditionally, the beginning of the year demonstrates market optimism which is transferred from the SPOT area to the forward area. As a result of closing the BASE_Y-16 contract at a level of PLN 167.50/MWh, the BASE_Y-17 contract was the first to close the gap in January. Until the middle of the month its price increased from PLN 164.24/MWh to almost PLN 170/MWh, declining to the area of PLN 155/MWh by the end of the month. This was caused both by increasingly cheaper energy price on the SPOT market as well as a significant discounts on the CO_2 market where prices dropped from EUR 8.5/Mg to approximately EUR 5.7/Mg at the beginning of February. The increasingly cheaper CO_2 accompanied by low coal prices in the global markets maintained low prices on the Commodity Forward Market (RTT) by the end of March, supported by stable SPOT prices. Significant price volatility in April converted the declines in the BASE_Y-17 contract prices into an upward trend, continuing until June 2016, reaching the level of PLN 165.50/MWh.

High SPOT prices in June maintained prices at a level of PLN 162/MWh until the second decade of July, when the market started to discount consecutive price drops in the CO_2 market. Low CO_2 prices which occurred in the summer, reached their all-time lows in the 1st half of September, gaining levels ranging from EUR 4–4.2/Mg. The combination of low CO_2 prices and very cheap energy on the SPOT market, the price of which declined to PLN 155/MWh, reaching its all-time low in August, at the average monthly level of PLN 140/MWh, led to the decline in the BASE_Y-17 prices to approximately PLN 155.5/MWh.

The last quarter of 2016 was marked by the growth of prices. High coal prices maintained throughout the summer (approx. USD 58–60/Mg), accompanied by the dynamic growth in CO_2 prices whose direction of quotations indicated a possibility to return to the value of EUR 6/Mg, resulted in the growth of prices to approx. PLN 160/MWh. In addition the October growth in SPOT prices as a result of the failure in Turów and lower temperatures than forecast, allowed for breakthrough and growth in prices to approx. PLN 161–161.50/MWh. At the end of 2016 energy prices on the said market amounted to PLN 162/MWh.

The average volume-weighted price for the BASE Y-17 product amounted to PLN 160.27/MWh, whereas over 76.7 TWh was sold in total. As compared to trading in the BASE Y-16 product, the trade was almost two-fold lower. The average price on TGE amounted to PLN 159.77/MWh, at a volume of 51.5 TWh, whereas it was higher outside TGE, amounting to PLN 161.29/MWh for the volume of 25.2 TWh. The share of the volume sold with the participation of TGE in 2016 in the overall pool, reached almost 72% (43.7 TWh), and – with the participation of broker platforms – over 28% (17.1 TWh). The average volume-weighted prices obtained in 2016 for the exchange segment and brokers reached, respectively, PLN 159.30/MWh and PLN 159.32/MWh, which set the average price of the BASE Y-17 product at a level of PLN 159.32/MWh in 2016.

In case of the PEAK Y-17 contract, the quotations were very similar to the quotations for the base contract. The peak of quotations in 2016 occurred on 18 January 2016, reaching PLN 227.85/MWh, whereas the minimum level was recorded on 16 February 2016, amounting to PLN 202/MWh. The total trading volume recorded in 2016 for this product reached 7.3 TWh, including 70% (5.1 TWh) in the exchange segment, at the average price of PLN 209.94/MWh, and the share of brokers amounted to 30% (2.2 TWh), with the average price of PLN 209.98/MWh. In total, throughout the entire period of trading in the PEAK Y-16 product, 7.75 TWh of energy was sold, at an average price of PLN 209.93/MWh.

The figures below show the results of trading in Base Y-17 and PEAK Y-17 contracts.

Figure no. 22 Trading in BASE Y-17 and PEAK Y-17 contracts

Crude oil and coal

Year 2016 was significant for crude oil. Throughout the year, a significant surplus of the commodity occurred, which resulted in sales on the oil market and the decline of priced to level of 2000–2003. This situation was the effect of the policy of oil manufacturers based on the protection of market share and the price war resulting from such policy. Another factor affecting the situation in the oil market was also the so-called shale revolution in the USA; oil production in the USA increased by 65% over 5 years. Due to lifting of international sanctions, a significant quantity of oil from Iran, successively increasing the volume of exported oil throughout 2016, has also appeared on the market.

In February 2016 Brent oil was quoted at USD 27/bbl. The low price of the commodity resulted in suspension of many investments in new infrastructure; problems were also experienced by banks crediting this type of investment. Concerns appeared that such a situation will lead to very high oil prices in the future. In the 2nd and 3rd quarter prices started to recover, inter alia, owing to the standing of the Chinese economy, which was better than expected, and due to increased oil demand associated with the so-called holiday season. Oil prices were also positively affected by extraordinary situations, e.g. a huge fire in Canada nearby the largest oil fields, or the military actions and destruction of the oil sector infrastructure in the Middle East and in Nigeria.

At the same time, OPEC countries, in particular, Saudi Arabia, launched their efforts aimed at controlling oil supply in order to stabilise prices. The consensus was extremely difficult to achieve due to divergent interest of member states. It became possible only before the end of 2016. At a meeting of OPEC producers in Vienna on 12–13 December 2016 a solidarity-based limitation of oil production by 1.2 million bpd was agreed. Russia and other smaller countries, non-members of OPEC, also entered into the agreement. The total cut in production was agreed at a level of approximately 1.8 million bpd. Oil prices increased to the level of approximately USD 55–57/bbl, i.e. By 100% in relation to the lowest prices recorded in February 2016. Analysts expect that the average cost of Brent oil in 2017 will reach USD 57–58/bbl.

A similar situation occurred in the coal market. In the 1st quarter of 2016 coal price has reached its lowest level for over a decade. In February 2016 coal in ARA ports was quoted at only USD 36/Mg. The decline in prices was affected by such factors as the economic crisis in China or the shale revolution in the USA (cheap shale gas forced out coal). Both China and Europe are oriented towards the replacement of the energy mix and acquiring increasing energy quantities from renewable sources.

Starting from the 2nd quarter of 2016, the situation in the coal market started to improve due to disruptions in the supply side worldwide. As a result of low prices several spectacular bankruptcies of coal giants occurred, e.g. one of the biggest coal producers in the world, the American Peabody Energy company, or the Czech producer, OKD a.s. The Polish mining sector also experienced significant financial problems. In Columbia, which is the fifth biggest coal producer in the world, employees of the mining sector were on strike starting in March whereas in Australia the majority of operating coal mines were shut down. China introduced regulations aimed at limiting own coal output (closing unprofitable coal mines, followed by reduction of working days for the coal mine).

In Europe, due to decommissioning of the significant quantity of generating capacity in the nuclear power sector in France, the demand for coal increased in autumn, strengthening the demand side. Coal prices on the SPOT market with the delivery in winter months increased to the level of over USD 85/Mg. The price of contract with the delivery in 2017 reached the level of USD 70/bbl, which means a growth by almost 100% as compared to prices in February 2016.

Improvement of business conditions in the global coal market will certainly have a positive effect on the situation in the Polish mining sector. However, the growth of coal prices on the Polish market will only materialise in 2017.

In 2016 the index of Polish steam coal prices, PSCMI1 was contained in the range of PLN 188–201/Mg (PLN 8.52–8.93/GJ).

It is worth noting that the so-called backwardation phenomenon occurs in the global coal market, which means that coal with the delivery for the nearest periods is cheaper than coal with the delivery in the future.

Natural gas

2016 was the year of all-time lows in prices on the gas market. As early as in the first month, the average price on the spot market reached the level of almost PLN 30/MWh lower than in the previous year, amounting to approximately PLN 72.54/MWh. The peak of the downward trend was reached in March when the average price on the TGE Day-Ahead Market (RDN) amounted to only PLN 60.11/MWh. Following slight growths in the 2nd quarter, gas price in the 3rd quarter also turned out very low, in particular, in the last two months. On 11 September 2016 the price on this market reached a level of PLN 49.61/MWh. Throughout the summer period, contracts with the delivery on the following day (day-ahead) stayed around PLN 60 /MWh, as compared to PLN 85–90/MWh in the previous year. However, upon the start of the gas winter season a significant growth in prices was noticeable. In December day-ahead contracts were already priced at PLN 84.95/MWh, on average.

On the forward market, following low prices in the first quarter, quotations moved upwards, similar to the SPOT market. The same trend was again recorded in the 2nd half of 2016 when it demonstrated strong growth after the decline in the 3rd quarter. Ultimately, the reference annual contract gained the value of slightly over PLN 15/MWh throughout the year.

In terms of the development and liquidity of the domestic TGE, mainly almost two-fold growth in the trade volume on gas RDN is worth noting. The majority of 16 TWh was traded in the period of the gas winter season, i.e. in the period of the highest demand for gas.

In 2015, it was only 8.7 TWh and a year earlier – less by a half. Such a dynamic growth in trade on the spot market did not translate into the forward market where a decline in the volume by over 3% was recorded as compared to the previous year. In quantitative terms, however, trade in forward contracts continued to exceed significantly the trade in the market with immediate delivery. In 2016 it was almost 90 TWh, i.e. almost 5-fold the volume of the day-ahead contract.

2016 was an exceptional year not only due to all-time lows in prices. In the middle of the year the LNG terminal in Świnoujście received first vessels with commercial gas supplies in liquid form. Owing to commissioning of the regasification port, Poland gained access to the international market, consequently, it may purchase gas practically at any place worldwide, strengthening its negotiation position towards suppliers.

Moreover, in the November amendment to the energy law, gradual waiver of the obligation of traders to determine and submit tariffs for gas for approval was endorsed. These activities were associated with the necessity to execute the verdict of the European Union Court of Justice of September 2015, which held that the system of regulating natural gas prices is not compliant with the requirements of the EU law. Other change of key importance for the market was the waiver of the privilege related to the lack of obligation to maintain natural gas reserved for so-called "small vendors". Since the moment of entry into force of the amendment, each vendor importing gas from abroad, regardless the volume, shall be obliged to secure its sales by maintaining the specific volume in storage facilities.

The figure below presents the average monthly SPOT prices and prices for Y-17 contract in 2016 on the TGE.

Figure no. 23 Average monthly SPOT prices and Y-17 contract prices in 2016 on the TGE

CO_2 emission allowances

The market of CO_2 emission allowances in 2016 demonstrated exceptionally high volatility of prices. The decline of prices in January from the level of EUR 8.30/Mg to the level of EUR 4.90/Mg resulted from overlapping of several events unfavourable for the EU ETS market. The first of those factors was the record warm winter which contributed to visible declines in prices of electricity contracts in Germany, France and United Kingdom. Another factor fostering the decline were the data confirming the economic downturn coming from China. Reduced demand for coal affected record declines in coal prices in ARA ports at the beginning of the previous year (to the level of USD 37/Mg, the lowest since 2003). The third driver of the decline was the backloading mechanism which led to withdrawal of the last 200 million out of 900 million of EUA units throughout 2016. It translated directly to the increase in the volumes of allowances sold in auctions. The temporary rebound in prices occurred only after three months, i.e. in April, and it was only the result of increased demand for EUA units in connection with the need to clear emissions for 2015.

Continuing a high volatility of prices, in June the EU ETS market responded with the successive clear sales to the positive result of the referendum concerning the exit of Great Britain from the EU – the price dropped from EUR 6.00/Mg to the level of EUR 4.40/Mg. Such low prices continued throughout the holiday season, to recover to the level of EUR 6.60/Mg as a response to the (nuclear) energy crisis in France. In connection with the detection of irregularities in nuclear power plants, ASN (the Nuclear Safety Authority) ordered 12–13 of 58 reactors to suspend any work immediately. France secured the missing energy for the country through its import from Great Britain, Austria, Germany and Belgium. This situation resulted in the growth of electricity prices, increased generation from conventional sources (coal and gas-based), which translated directly into the growth in prices of commodities and CO_2 emission allowances. The situation improved as late as in December last year, when ASN conditionally permitted to resume operations of several reactors due to the concern that the French power system will not cope with the increased winter demand. The last significant event which affected EUA prices was the December voting in the ENVI environmental committee concerning the proposed shape of Phase 4 of EU ETS and the functioning of the Stabilisation Reserve. According to the proposal of ENVI committee, the Reserve mechanism should withdraw a double quantity of allowances over the first three years of its operation (24% instead of original 12%). In addition, in order to achieve 43% emission reduction, adopting of a higher linear reduction coefficient is proposed – at a level of 2.4%. Despite such tight proposals explicitly aiming at the growth in prices of EUA units, the price ultimately closed 2016 below its initial opening level – EUR 6.57/Mg.

The figure below presents the impact of political events and the environment on quotations of the forward product, EUA SPOT in 2016.

Figure no. 24 Impact of political events and the environment on quotations of the EUA SPOT product in 2016

Property rights

Year 2016 was a period of decline in prices of “green” certificates, triggered mainly by information on the new system of RES support. The implementation of the new system was planned at the beginning of 2016, however, in accordance with the Act of 29 December 2015, the deadline was postponed to 1 July 2016. The final shape of the RES support system was defined in the *Act of 22 June 2016 on the amendment to the Act on renewable energy sources and certain other acts of law*. Market uncertainty and the continued high surplus in the system of certificates caused that prices of property rights, confirming energy generation recorded the decline in prices in 2016. During the October session, the OZEX_A index reached its all-time low: PLN 32.57/MWh.

The average weighted session price amounted to PLN 73.63/MWh, i.e. by PLN 49.98/MWh less than in 2015. The PMOZE_A balance since the beginning of the register, amounted to 29.1 TWh at the end of December; the surplus, as compared to the previous year, increased by 2.04 TWh. At the end of 2016, the surplus amounted to 19.8 TWh, taking into consideration the rights blocked for redemption.

The level of the substitution fee determined for 2016 amounted to PLN 300.03/MWh, and the obligation to submit PMOZE_A certificates for redemption amounting to 15% in the first half of the year decreased to 14.35%. Along the reduction of the obligation in the scope of “green” certificates, as of the second half of the year a new type of certificates was introduced, confirming energy generation from agricultural biogas, so-called “blue” certificates, for which the scope of the obligation was 0.65% (equal to the reduction in the obligation for “green” certificates). The average weighted session price of PMOZE-BIO in 2016 was very close to the substitution fee of PLN 300.03/MWh and amounted to 295.52/MWh. The balance of register of this instrument at the end of the year amounted to PLN 48.01 GWh.

According to the *Act of 10 April 1997 on Energy Law,* amended in 2016, until 30 June 2015 it is possible to redeem property rights issued to co-generation units for the production in the previous year. Accordingly, until the end of the first half of the year, property rights from co-generation in 2015 were quoted. Since July 2016, only property rights confirming energy generation in 2016 have been quoted.

In 2016, the average price of property rights confirming energy generation in high-performance coal co-generation (PMEC-2016 – “red” certificates) amounted to PLN 10.76/MWh, whereas PMEC-2016 property rights at the end of 2016 reached the average level of PLN 10.68/MWh. The KECX index demonstrated high stability and ranged around the substitution fee amounting to PLN 11/MWh.

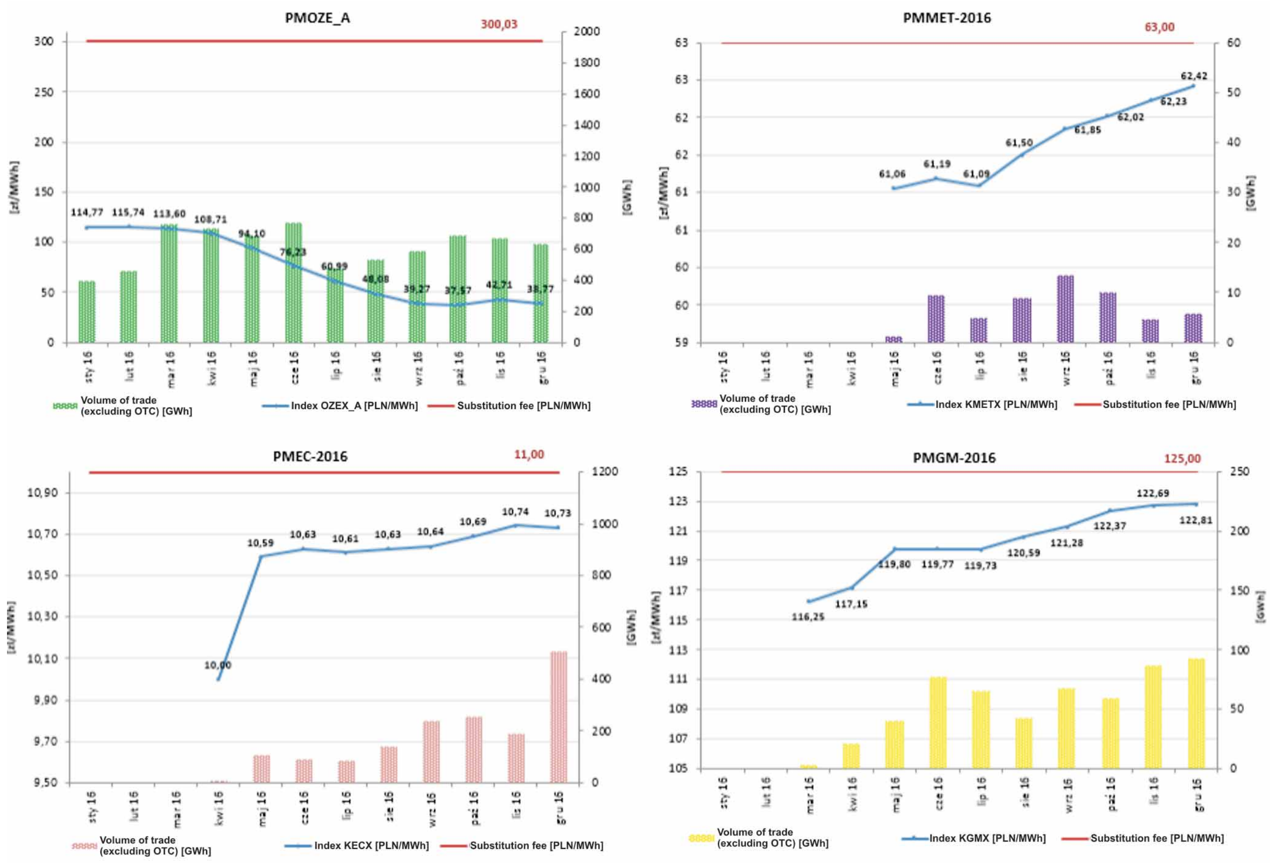
Analogically, the average price for PMGM-2015 gas co-generation amounted to PLN 118.85/MWh, with the substitution fee at a level of PLN 121.63/MWh, whereas the average price of “yellow” certificates, PMGM-2016 also oscillated around the substitution fee amounting to PLN 125/MWh, reaching PLN 121.13/MWh at the end of 2016.

“Violet” certificates representing co-generation rights confirming electricity generation during methane removal from coal mines throughout 2016 were quoted around the substitution fee amounting to PLN 63.26/MWh in the first half of the year, and their average weighted price, PMMET-2015 amounted to PLN 62.24/MWh. On the other hand, PMMET-2016 was traded, on average, at PLN 61.73/MWh at the end of December 2016, with the substitution fee at a level of PLN 63/MWh.

Property rights arising from the PMEF energy efficiency certificates, i.e. so-called “white” certificates, also demonstrated low volatility. With the substitution fee amounting to PLN 1,000/toe the average weighted price of the EFX index reached PLN 977.35/toe. The prices ranged from PLN 958.30 a 1,001.76/toe.

The figures below shows indices of property rights, so-called “green”, “violet”, “red” and “yellow” certificates.

Figure no. 25 Indices of property rights



2.1.2.3. Regulatory environment

Changes in the regulations of the energy sector

In 2016, the President of the Energy Regulatory Office (ERO) maintained the obligation to submit tariffs for households for approval, as a consequence, traders had a limited impact on margins generated in the Sales Segment (G tariff).

Arrangements in the scope of CO_2 emission allowances

2016 was the consecutive year when works on the reform of the CO_2 emission allowances trading system were continued in the European Parliament. The key issues considered during the works include so-called compensation mechanisms which could be used, inter alia, by Poland in the period 2021–2030, i.e. the rules of allocation of free CO_2 emission allowances for the energy sector and the rules of using the resources of the Modernisation Fund dedicated to investment in the energy sector. During the EU climate summit in October 2014, the European Council determined, inter alia, that the CO_2 emission reduction target for 2030 shall be 40% in relation to 1990, including 43% within installations covered by EU ETS, in relation to 2005. Within the arrangements adopted at that time, it was agreed that Poland would be able to provide maximum 40% of the pool of CO_2 emission allowances granted for the period 2021–2030 to the energy sector free of charge.

On 15 December 2016, the Committee on Environment, Public Health and Food Safety (ENVI) adopted a package of amendments to the draft EU ETS directive proposed by the European Commission (EC). The major proposals of amendments to the draft directive voted in the ENVI Committee refer to the elements presented below.

Distribution of the pool of allowances

1. The linear factor was proposed at a level of 2.4% (contrary to 2.2% in the Commission proposal of July 2015 and Council conclusions of October 2014).
2. The auction pool would amount to 57% (as in the original version of the project), however, a possibility would exist to reduce it by 5% due to the intention to limit the cross-sectoral correction factor; in addition, a possibility to eliminate 200 million allowances from the auction pool at the end of the 4th period was included, in case the allowances were not used for free allocation.
3. 2% of 57% of the auction pool would be allocated for the Modernisation Fund.
4. 3% of the total pool would be allocated for compensation of emission indirect costs.
5. 2% of the auction allowances pool would be allocated for the fund supporting economic transformation in countries with high employment in sectors based on coal use and GDP lower than the EU average.
6. 100% of revenue from auctions should be allocated for combating climate change.
7. Voluntary permanent removal of allowances from the auction pool by Member States would be possible, corresponding to the level of emission from decommissioned power units.
8. A possibility of permanent removal of any number of allowances from the auction pool – at the Member State's discretion.

Free allowances

1. Benchmarks would be determined based on real data on the improvement of production capacity from 2016–2017 for allocation for 2021–2025 and, analogically, from the data for years 2021–2022 benchmark levels would be determined in the consecutive five years of the 4th period; the changes in the value of benchmarks related to the improvement of production capacity would range from 0.25% to 1.75%.
2. Sectors exposed to the risk of carbon leakage would have to meet the quantitative criterion at a level of 0.12 in order to receive 100% of allowances free of charge (in the original project, the level is 0.18), whereas sectors which are not exposed would not receive allowances, except for the network heating sector for which the limit of 30% was included throughout the period 2021–2030.
3. The cross-sectoral correction factor – CSCF, would only comprise selected sectors (sectors where the criterion of trade intensity would fall below 15% and the criterion of carbon intensity would remain below 7 kg CO_2/EUR GVA).
4. A new protective mechanism for cement and clinker was proposed – importers of those products would be charged with fees but, at the same time, producers inside the EU would not receive free allowances; the mechanism could apply from 2019.
5. 400 million allowances for the needs of the NER reserve would originate from the pool of allowances for the 4th period, instead of the stabilisation reserve (MSR) on the allowances market, as proposed by the EC in the draft of July 2015.
6. The allocation of allowances would be more dynamic and dependent on real production levels – the allowances would include changes above 10%.

Funds

1. The Innovation Fund would amount to 600 million allowances and besides, inter alia, the CCS technology, it would also comprise the CCU technology Carbon Capture and Utilisation,
2. Authorised Member States would be able to transfer allowances from the derogation pool (Article 10 c) to the Modernisation Fund,
3. Neither the Modernisation Fund nor derogations could finance the construction of new coal-fired units (the emission factor of new installations would have to be lower than 450 gCO_2eq/kWh),
4. Greece would obtain a possibility to use 40% of allowances from its auction pool for purposes compliant with the goals of the Modernisation Fund.

MSR

1. Over the first 4 years of MSR functioning the number of allowances transferred from the auction pool to the MSR would be doubled to the level of 24% of the surplus available on the market;
2. 800 million allowances from the MSR would be permanently removed from the market.

The next stage of works in the Parliament will involve voting on compromise amendments at the plenary forum, whereas in the EU Council – the voting on the general approach to the draft EU ETS directive will be performed, scheduled in June 2017.

In 2016, pursuant to the *Act of 12 June 2015 on the greenhouse gas emission allowance trading scheme*, activities were undertaken, aiming at launching of the national auction platform, where CO_2 emission allowances would be traded under the EU ETS system. The Polish Financial Supervision Authority approved the auction platform to be operated by TGE and sales of allowances under the EU ETS system. However, prior to that, the exchange has to win the tender for the operator of the national auction platform to be organised by Poland.

At present, Poland, as one of three countries (besides Germany and Great Britain), in accordance with the auction regulation (*Regulation of the European Commission no. 1031/2010 of 12 November 2010 on the timing, administration and other aspects of auctioning of greenhouse gas emission allowances)* has been using a possibility of derogation from the rule of allowances sales at a single harmonised auction platform and as a state from the "opt-out" group, until the target platform is selected, sales of allowances through the EEX exchange. Currently, only two auction platforms conduct sales of emission allowances by means of auctions – the European Energy Exchange – EEX established in Leipzig, which arranges community auctions (for 24 EU Member States and Poland) and German auctions, whereas the ICE/ECX established in London conducts auctions for Great Britain.

The Ministry of Environment has informed that in the 1st quarter of 2017 the tender for conducting auctions of emission allowances at the national platform will be announced. It is estimated that in the years 2017–2020 Poland will have approximately 314 million CO_2 emission allowances for sale. With this reservation, the distribution of sales of the indicated pool of CO_2 emission allowances for individual years is as follows: in 2017 – 71 million allowances, in 2018 – 78 million allowances, in 2019 – 67 million allowances and in 2020 – 98 million allowances.

Act on Renewable Energy Sources (RES)

On 1 July 2016 the amendment to the *Act on Renewable Energy Sources* (RES) entered into force. The objective of the amendment was to eliminate interpretation doubts concerning the provisions of the Act of 20 February 2015 on renewable energy sources which have not yet entered into force.

In particular, the amendment was to streamline the situation of generators of electricity from RES and rules of granting public aid to such generators. Accordingly, the definition of prosumer was introduced into the Act – the end consumer purchasing electricity under a comprehensive agreement, generating electricity only from RES in a micro installation in order to use it for own needs not associated with the conducted economic activity.

The regulation covered a wide range of entities, including small and medium-sized entrepreneurs. The existing support system based on feed-in tariffs for the smallest generators in micro installations was abandoned in favour of clearing of electricity surplus generated by a given micro installation, so-called discounts by a prosumer.

In accordance with the amendment to the Act, a new support system for electricity generators in RES was introduced, the so-called auction system. New installations, established after the entry into force of the amendment, may receive support only by means of submission of the relevant electricity sales bid at an auction arranged by the ERO President. In case of winning the auction, the generator shall have a guaranteed support at a level of energy price offered throughout the period of support defined in the relevant regulation. RES installations operating prior to the entry into force of the amendment may either remain in the existing support system and receive certificates of origin or transfer to the auction system.

On 30 December 2016 the first RES auction was carried out. The auction sequence, eligible auction baskets and maximum volumes and the value of energy purchased, were defined in the relevant regulations. The regulation was also issued concerning the calculation of the value of public aid for generators of electricity from RES, defining the method of calculating the public aid received, required to be presented in the processes of submission of the energy sales bid in the auction.

Act on investment in the scope of wind farms

The *Act on investment in the scope of wind farms* adopted on 20 May 2016 defines a permissible distance between residential buildings and location and construction of wind farms. In accordance with its provisions, the minimum distance of a wind farm from a residential building or a building with a residential function, as well as from natural protection forms and promotional forest complexes, should be equal to or higher than ten-fold total height of a wind turbine. In case of power plants existing before the day of entry into force of the aforementioned Act which do not fulfil the condition of the minimum distance, it will be only possible to perform overhauls and activities required for the due utilisation of a power plant, excluding a possibility to increase useful parameters of a power plant or increase its environmental impact. Deployment of new wind farms will be possible only on the basis of the local spatial development plan. Consequently, investment in new wind farms will be much more difficult due to the necessity to search for appropriate location meeting the distance criterion and included in the land use plan. In addition, due to the change of the definition of a wind farm and recognising the whole facility as a construction facility, the principles related to the assessment of a real estate tax will change and, consequently, the resulting costs will increase.

New Draft Act on Energy Efficiency

As of 1 October 2016 the *Act on energy efficiency* entered into force, replacing the Act of 15 April 2011, extended by half a year. The new Act implements the provisions of *Directive 2012/27/EU of 25 October 2012 on energy efficiency*. The provisions of the Act envisage measures in areas of increasing energy savings by end users and increasing energy savings in the scope of energy generation, transmission and distribution. The market mechanism leading to accomplishment of the objectives of the Act will be a system of energy efficiency certificates (“white” certificates) submitted for redemption by energy undertakings as a fulfilment of the obligation to implement projects aimed at energy efficiency improvement.

The Act waives the obligation to conduct a tender as a result of which the ERO President selected projects aimed at energy efficiency improvement, for which energy efficiency certificates could be obtained. It increases the flexibility in acquisition of efficiency investment. In addition, enterprises will have a possibility to clear the obligation within 3 years.

The new regulations also stipulate gradual waiver of a possibility to pay the substitution fee for the failure to fulfil the obligation. Undertakings using at least 100 GWh per year will have a possibility to use an alternative mechanism of energy efficiency improvement.

The Act introduces a new obligation to conduct an energy audit every four years for an energy undertaking defined in the Act on freedom of establishment, excluding micro, small and medium-sized entrepreneurs. The circle of entities subject to this obligation is very broad, since it includes large entrepreneurs, irrespective of the industry and electricity, heat or natural gas consumption. The audit should take into account at least 90% of the energy consumed. An obliged undertaking must perform the first audit within a period of 12 months as of the entry into force of the Act.

The Act defines the principles of development of the national action plan related to energy efficiency improvement by the Minister of Energy every three years.

Operating Power Reserve (ORM)

In 2016 the ORM did not change in the functional area. However, the parameters of the model have significantly changed, which is associated with the change of the base for model calculation. The hourly budget of the ORM was increased from PLN 106.2 thousand to PLN 128.8 thousand and the hourly reference price – CRRM, from PLN 37.28/MWh to PLN 41.20/MWh. The hourly quantity of required operating capacity reserve increased from 3,451.09 MW/h to 4,155.37 MW/h. Changes in the aforementioned parameters did not significantly affect electricity prices in the current market. The average CRR price in 2016 increased by PLN 1.70/MWh, i.e. to PLN 32.76/MWh.

Draft Act on the Capacity Market

Considering low electricity prices affecting the lack of binding investment decisions which may generate future problems related to the provision of security of energy supply to the KSE, in 2016 works related to the mechanism ensuring maintaining of the generation capacity at an adequate level in a medium- and long-term perspective were carried out in Poland. At the beginning of July the Ministry of Energy, jointly with PSE, presented the proposal of functional solutions of the dual commodity market introducing, besides payment for energy, payments for preparedness to provide the service of capacity supply or reduction.

Following the consultations with the industry, on 30 November 2016 the draft *Act on the capacity market* was published, assuming creation of the capacity market centralised within the KSE, with auctions for capacity supply or reduction in annual and quarterly periods. Further works on the draft will proceed in the current year and as early as at the end of this year the first auction contracting the capacity shall be held, whereas the mechanism itself will be launched in 2021.

The objective of the capacity market is to ensure the security of electricity supplies to end consumers in a medium and long-term perspective. The mechanism shall constitute the incentive to construct new and modernise existing generation capacity, instead of its decommissioning, simultaneously creating conditions for the development of the demand reduction services – DSR. Costs of the capacity market shall be incurred by consumers within the component of the transmission tariff referred to as the capacity fee.

Draft European Regulations under so-called "Winter package"

On 30 November 2016 the EC published a set of proposals (EU Strategy on Heating and Cooling) related to draft directives and regulations intended to improve the transformation of the EU energy policy towards the model focusing on customer and clean energy. The overall proposal was defined as the "Winter package" and it has been the biggest single amendment to the EU energy regulations since 2011 when the Third energy package entered into force.

The main assumptions of the current package include further integration and development of RES sources, strengthening of competitiveness and client's role as well as increasing the harmonisation and integration of wholesale energy markets in the EU. In addition, the Commission relies on the growth of energy efficiency, security of supplies and harmonisation of energy union management rules.

From the point of view of Poland, the most important provisions refer to strengthening of the role of the Agency for the Cooperation of Energy Regulators – ACER, establishment of regional operating centres for transmission grid operators – ROC, establishment of the Agency Associating Distribution Grid Operators – EU-DSO and introduction of a number of constraints for Member States intending to introduce the capacity market. According to the new rules, in order for a country to be able to introduce the capacity market mechanism, it has to agree on its principles with its neighbouring countries, demonstrate that the interconnectors are incapable to set off the potential capacity deficit and open the mechanism introduced for suppliers from areas of other Operators. In addition, the draft contains a provision which has not been consulted earlier, stating that sources emitting more than 550 gCO_2/kWh, will not be permitted to take part in capacity markets, which in practice undermines Polish plans of revitalising power plants producing energy based on domestic coal deposits. The battle for amendments to the unfavourable provisions of the regulation is already ongoing at the forum of trade associations, and the waiver of the carbonisation criterion will certainly be one of the priorities for the Polish energy sector.

Amendment to the Act on natural gas reserves

On 2 September 2016 the amendment to the *Act of 22 July 2016 on the amendment to the Act on Energy Law and certain other acts* of law, entered into force. According to the assumptions of the legislator this act should contribute to liquidation of the shadow fuel market, strengthen market competition and improve the state energy security. In particular, the amendments introduced under the Act refer to the market of natural gas and liquid fuel.

The amended Act introduced the following changes:

1) The entity importing natural gas is obliged, by 1 October 2017, to maintain required natural gas reserves. Under the current legal status, the requirement to maintain mandatory reserves of natural gas refers to energy undertakings carrying out economic activity related to import of natural gas from abroad for the purpose of its further resale to consumers. In accordance with the amendment to the Act, the requirement to maintain mandatory reserves of natural gas shall refer to energy undertakings carrying out economic activity in the scope of foreign natural gas trade as well as to any other entities importing natural gas.
2) Entities which did not maintain gas reserves will determine the size of required reserves based on the level of corresponding to at least 30-day average daily gas import in the period from 1 January 2017 to 30 September 2017. The currently applicable provisions of the Act on reserves grant the exemption from the obligation to maintain natural gas reserves to energy undertakings with the number of consumers not exceeding 100 thousand, whose natural gas import does not exceed 100 million m^3 during a calendar year. This exemption used to be granted by the Minister of Energy pursuant to an administrative decision. In accordance with the provisions of the amended Act, the obligation to maintain natural gas reserves will be unconditional and a possibility to obtain the exemption will be waived. Exemptions from the obligation to maintain natural gas reserves granted earlier will apply until 30 September 2017.
3) Entities carrying out economic activity in the scope of foreign natural gas trade and entities importing natural gas may outsource, having obtained the approval of the ERO President, performing of tasks in the scope of maintaining the required natural gas reserves to other entity carrying out economic activity in the scope of foreign natural gas trade or entity importing natural gas – this service is known as so-called "ticket service".

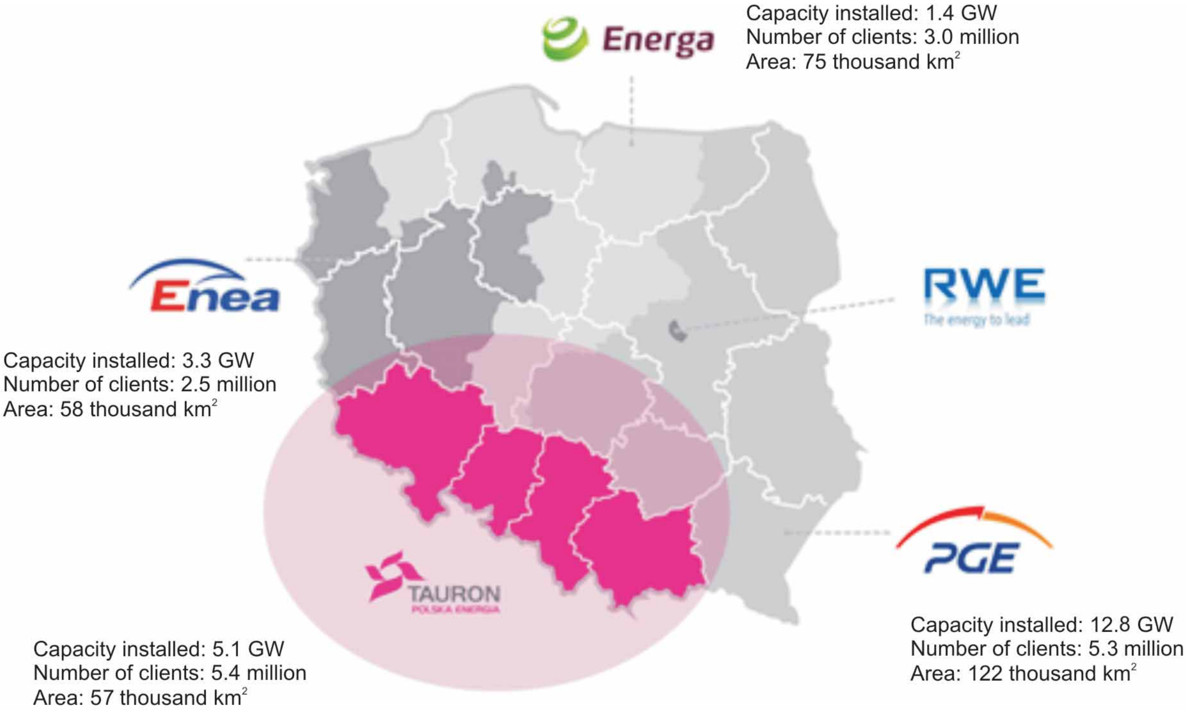
2.1.2.4. Competitive environment

Energy Groups in Poland

At present, besides TAURON Capital Group, three large, vertically integrated energy groups operate on the Polish energy market: PGE, ENEA and ENERGA.

The figure below presents the competitive environment of TAURON Capital Group according to the available data, i.e. for 2015.

Figure no. 26 Competitive environment of TAURON Capital Group (data for 2015)



Owing to the vertically integrated structure, the above entities have a strong position on the domestic market. Moreover, foreign energy groups are also present on the Polish market.

According to the data for 2015 in the generation sub-sector the consolidated energy groups (PGE, TAURON, ENEA, ENERGA) held 60% of market share. Moreover, smaller, although important entities on the Polish market of electricity included: EDF Polska Centrala sp. z o.o. (EDF) (8%), Zespół Elektrowni Pątnów-Adamów-Konin S.A. (ZE PAK) (7%) and Engie Energia Polska S.A. (Engie) (6%). The ZE PAK Group is the second generator of electricity from lignite in Poland, with the share of electricity generated based on lignite resources at a level of approximately 97%. On the other hand, EDF, besides the 8% share in the domestic electricity production, has the 15% share in the market of network heat. Engie occupied the leading position in the country in terms of biomass use.

In the electricity distribution sector the energy groups: TAURON, PGE, ENEA, ENERGA held over 95% of share in the electricity distribution market. Among other electricity distributors, Innogy Stoen Operator sp. z o.o. is one of the largest entities, supplying electricity to approximately 978 thousand clients in Warsaw and the neighbourhood.

TAURON Capital Group is the biggest distributor of electricity in Poland In 2015, share of TAURON Capital Group in electricity distribution to end clients amounted to approximately 38%. The distribution grids of TAURON Capital Group cover over 18% of the territory of the country. On the other hand, the share in the market of sales to end consumers amounted to approximately 24%.

TAURON Capital Group is the second biggest electricity producer in Poland. According to the data for 2015, both in terms of installed capacity and production of electricity, it was overtaken only by PGE. The share in the domestic electricity production market reached approximately 37% for PGE and 11% for TAURON. Share of PGE in the Polish market of distribution and sales of electricity to end consumers reached 27% and 31%, respectively.

The third biggest energy enterprise in Poland is ENEA (data for 2015), with the share in the market of energy production reaching ab. 9%, in the distribution market – ab. 14% and in sales market – ab. 14%.

On the other hand, ENERGA held market share in the Polish market of electricity production reaching approximately 2% and, respectively, approx. 17% and 13% for each, distribution and sales.

The table below shows information on the capacity installed as of 31 December 2015 and electricity generated in 2015.

Table no 7. Capacity installed and production of electricity according to energy groups

No.	Group	Capacity installed		Generation*	
		Quantity (GW)	Share (%)	Quantity (GW)	Share (%)
1.	PGE	12.8	32	61	37
2.	TAURON	5.1	13	19	12
3.	ENEA	3.3	8	14	8
4.	EDF	3.0	7	14	8
5.	PAK	2.5	6	11	7
6.	Engie	1.9	5	9	6
7.	ENERGA	1.4	3	4	2
8.	CEZ	0.6	1	3	2
9.	Other	9.7	25	30	18
	Total	**40.3**	**100**	**165**	**100**

** Quantity of gross electricity generated in 2015.*
Source: ARE, information of companies published on websites, own estimates in case of companies publishing net production

The table below presents the basic information concerning the share of individual energy groups in the scope of electricity distribution, according to the data for 2015.

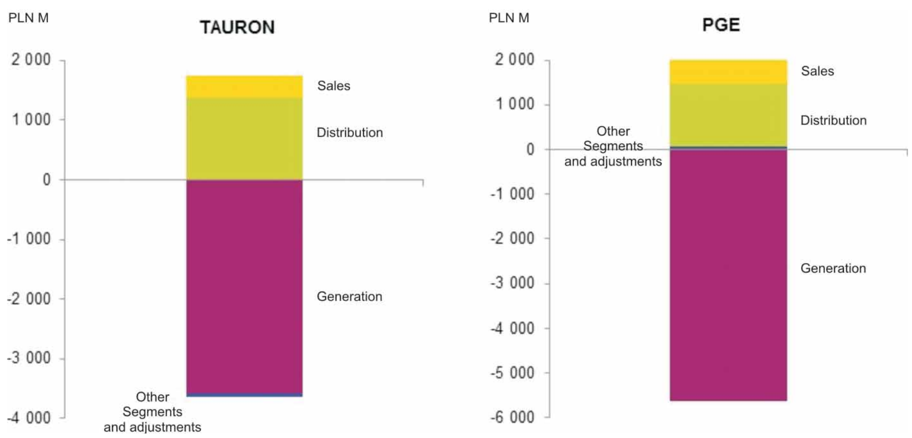
Table no 8. Distribution of electricity to end consumers, according to energy groups

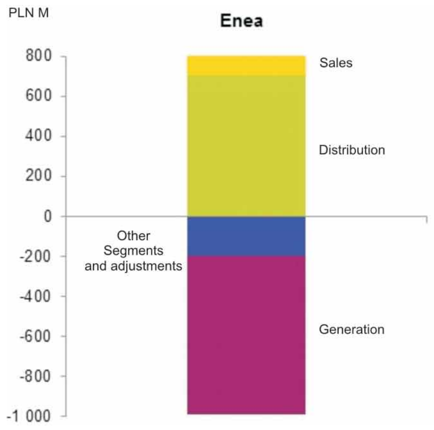
No.	Group	Distribution	
		Quantity (TWh)	Share (%)
1.	TAURON	47	38
2.	PGE	33	27
3.	ENERGA	21	17
4.	ENEA	18	14
5.	Other	5	4
	Total	**125**	**100**

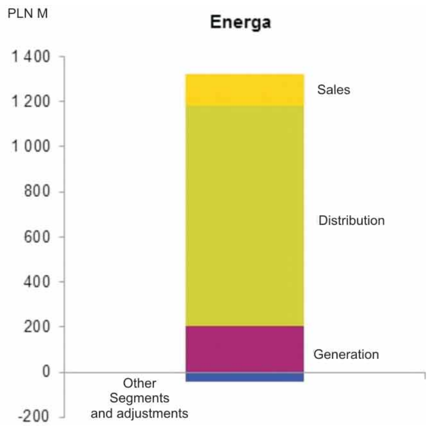
Source: ARE, information of companies published on the websites

The figure below shows information concerning EBIT in the structure, according to major segments.

Figure no. 27 EBIT – estimated structure according to major segments in 2015*







** In order to maintain comparability of the presented segments, in the Generation Segment, Mining, RES and Heat are also presented; in the Generation Segment impairment write-offs are also included.*
Source: Annual reports of Companies

TAURON Capital Group is the energy undertaking fully integrated vertically, using synergies arising from the scale and scope of the activities carried out.

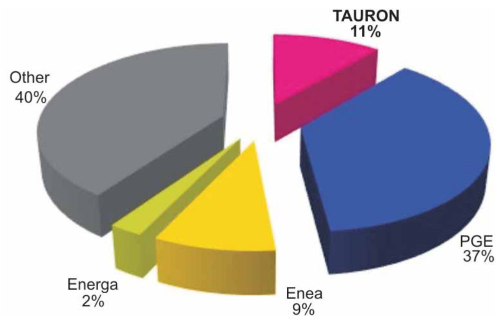
TAURON Capital Group controls the whole value chain, from coal extraction to the supply of electricity to end clients. It performs activities in all key segments of the energy market (excluding electricity transmission), i.e. in the area of coal mining, generation, distribution as well as trade of electricity and heat.

In 2015, significant impairment write-offs were applied to tangible fixed assets which had a significant impact on results of the Generation Segment of all energy groups. In 2015, PGE Group, TAURON and ENEA recorded negative net results, mainly resulting from write-offs due to impairment losses of generation assets, i.e. PGE – write-offs in the amount of PLN 8.9 billion, TAURON – write-offs in the amount of PLN 3.4 billion, ENEA – write-offs in the amount of PLN 1.5 billion.

Generation

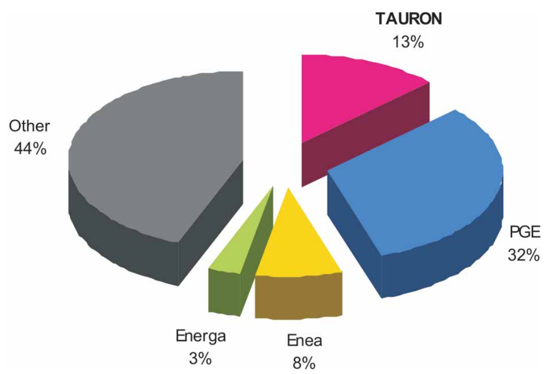
The figures below present information on electricity generated in 2015 and the capacity installed as at 31 December 2015.

Figure no. 28. Gross electricity output – estimated market share in 2015



Source: ARE, information of companies published on the websites

Figure no. 29. Installed capacity – estimated market share in 2015



Source: ARE, information of companies published on the websites

TAURON Capital Group is the second biggest electricity producer in Poland.

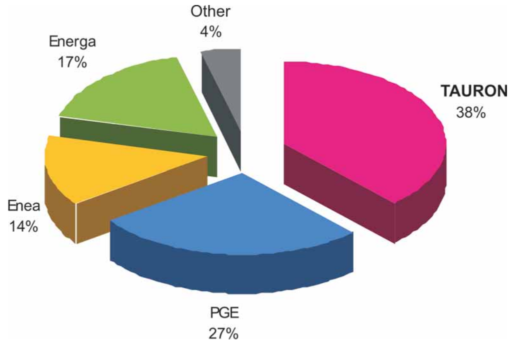
Based on ARE data for 2015, the share of TAURON Capital Group in the domestic market of electricity generation, measured by the gross electricity output, amounted to approximately 11%, which gives TAURON Capital Group the second position in Poland. The generation assets of TAURON Capital Group are concentrated in southern Poland. In this region, coal deposits are also located, used for combustion processes in power plants and co-generation plants of TAURON Capital Group. The location of generation assets of TAURON Capital Group in the vicinity of coal deposits allows for optimisation of costs associated with the transport of this raw material.

The generation assets of TAURON Capital Group comprise 91% of coal-fired entities, including 10% of modern high efficiency generation entities. Capacity installed in wind farms amounts to 3.9%, in hydroelectric power plants – to 2.8%, in biomass-fired generation assets – to 2.3% of the overall capacity installed in TAURON Capital Group.

Distribution

The following chart presents the basic information concerning the share of individual energy groups in the scope of electricity distribution according to the data for 2015.

Figure no. 30 Electricity distribution – estimated market share in 2015



Source: ARE, information of companies published on the websites

TAURON Capital Group is the leader on the Polish market in terms of the number of clients of the distribution and the volume of electricity distributed.

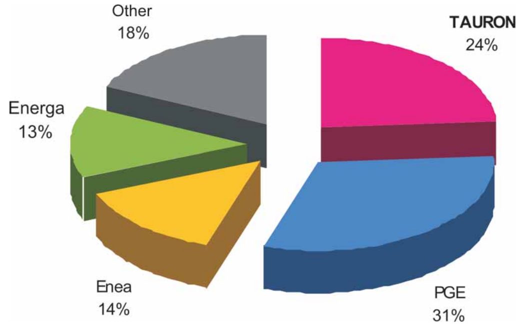
According to the data for 2015, 2014 and 2013 TAURON Capital Group, with the volume of electricity supplied to end clients by the Distribution Segment, at the level of, respectively, 47.0 TWh, 45.6 TWh and 45.2 TWh, occupied the first position in terms of the quantity of electricity supplied. In 2016, the volume of energy supplied to end consumers amounted to approximately 47.5 TWh. TAURON Capital Group is the largest electricity distributor in Poland, also in terms of revenues gained from distribution activity.

It should be stressed that the distribution activity of TAURON Capital Group, due to the natural quasi monopoly at the indicated area, is the source of stable and predictable revenues, constituting the essential part of consolidated revenues of the whole TAURON Capital Group. The geographical area of electricity distribution, where the companies of the Distribution Segment and the Sales Segment have historically operated, is the area characterised by its high level of industrialisation and dense population, which influences the demand for electricity, both among households and among enterprises. The number of clients of the Distribution Segment is almost 5.5 million.

Sales

The following chart presents the basic information concerning the share of individual energy groups in the scope of electricity sales to energy consumers, according to the data for 2015.

Figure no. 31 Sales of electricity to end consumers – estimated market share in 2015



Source: ARE, information of companies published on the websites

TAURON Capital Group is the second biggest electricity supplier in Poland.

TAURON Capital Group, with the volume of electricity sales to end consumers at a level of 29.5 TWh in 2015, was the second electricity supplier in this segment in Poland, following PGE Capital Group. On the other hand, in 2015, retail sales of electricity reached the level of 35.9 TWh. In 2016, the volume of electricity retail sales reached the level of approximately 32 TWh, including about 27.9 TWh to end consumers. The number of clients of the Sales Segment amounts to approximately 5.3 million.

Individual energy groups in electricity sales segments are geographically associated mainly with areas where they act as the DSO – this refers mainly to Clients classified as households and small companies. Additionally, a broader and more open competition among the groups is limited by the obligation to submit the tariff for households to the ERO President for approval. The requirement to provide price tariffs influences the possibilities of price positioning in product offers and, consequently, their attractiveness for clients. Such limitations do not apply to business and institutional clients. Among main competitors of TAURON Capital Group in this segment, on the one hand, an upward trend in the scope of retail sales volume and, on the other hand, the downward trends of results in this area is noticeable, which may result from the assumptions adopted in market strategies of those Groups.

The table below presents the main sources of competitiveness.

Table no 9. Sources of competitiveness

No.	Area of operations	Area of initiatives	Sources of competitiveness
1.	Mining, Generation	1) Mitigation of price and fuel supply risk 2) Investment in generation assets 3) Operating expenses	1) Own coal resources – security of supplies and control of mining costs 2) High efficiency generation assets with competitive unit cost of production 3) Improvement of operational effectiveness
	RES, Heat	1) Operating expenses 2) Investment in heating networks	1) Improvement of operational effectiveness 2) Development of regulated activity
2.	Distribution	1) Operating expenses 2) Investment effectiveness 3) Improvement of grid reliability indicators	1) Implementation of target business model 2) Cooperation with the ERO President in the scope of remuneration on investment 3) Implemented IT systems, separated processes, clear distribution of responsibilities
3.	Sales	1) Operating expenses 2) Margin on sales, development of products adjusted to clients' needs, development in new business areas	1) Effectively allocated operating expenses 2) Brand, current client base, held sales channels, experience in the scope of product and procurement portfolio management

2.2. Factors essential for development

As in the past, the operations of TAURON Capital Group will be most significantly affected by the such factors as:

External:

1) the macroeconomic situation, especially in Poland, and the economic situation in the area in which TAURON Capital Group operates, as well as at the EU level and global economy level, including volatility of interest rates and currency rates, etc., influencing the valuation of assets and liabilities recognised by the Company in the statement of financial situation,
2) political environment, especially in Poland as well as at the EU level, including the positions and decisions of public administration institutions and bodies, e.g.: Office for Competition and Consumers Protection (UOKiK), ERO and EC.
3) changes in regulations related to the energy sector as well as changes in the legal environment, including: tax law, commercial law, environmental protection law, in particular: the announced liberalisation of electricity prices for households, the announcement of the ERO President related to the application of maximum prices in tariffs for G group (instead of fixed priced), in order to protect consumers against rapid changes of prices upon full liberalisation,
4) planned introduction of the mechanism for generation capacity compensation (so-called capacity market) and decisions concerning the future shape of ORM and intervention cold reserve,

5) the support system for electricity generation in high-performance co-generation, resulting, on the one hand, in the growth of redemption costs of “red” and “yellow” certificates of electricity sellers to end consumers, and, on the other hand, in the growth of revenues on sales of “red” and “yellow” certificates of generators of energy in co-generation,
6) situation in the electricity sector, including the activity and measures undertaken by competition in the energy market,
7) the number of CO_2 emission allowances allocated free of charge, as well as prices of the allowances purchased – under the circumstances of the deficit in free allowances,
8) electricity prices on the wholesale market,
9) sales prices of electricity and coal as well as distribution tariffs, as factors influencing the level of revenues,
10) prices of certificates of origin of energy from renewable sources and co-generation,
11) a new system of RES support, so-called RES auctions,
12) prices of energy raw materials,
13) environmental protection requirements,
14) research and technical progress,
15) demand for electricity and other products of the energy market, considering the changes arising from seasonality and weather conditions.

Internal:

1) activities implemented under the Strategy,
2) activities in the area of optimisation of processes in all companies of TAURON Capital Group,
3) decisions in the scope of implementation of key investment projects,
4) geological and mining conditions of extraction,
5) potential failures of equipment, installations and grids belonging to TAURON Capital Group.

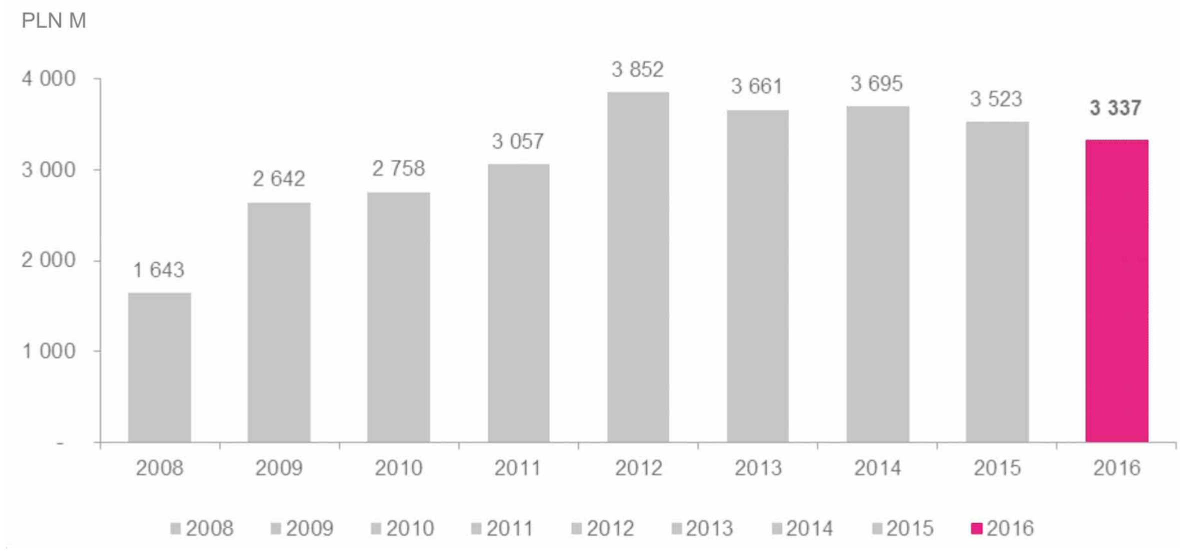
The activity of TAURON Capital Group demonstrates seasonality which refers, in particular, to production, distribution and sales of heat, distribution and sales of electricity to individual consumers and sales of coal to individual consumers for heating purposes. Sales of heat depends on the atmospheric conditions, in particular, on the air temperature, and it is higher in the autumn and winter season. The level of electricity sales to individual consumers depends on the length of a day, which usually makes electricity sales in this group of consumers lower in the spring and summer season and higher in the autumn and winter season. Sales of coal to individual consumers is higher in the autumn and winter season. The seasonality of the remaining areas of TAURON Capital Group operations is limited.

Changes in the aforementioned external factors may constitute premises committing TAURON Capital Group, in accordance with the International Accounting Standard 36, to perform impairment tests on assets. Results of such tests may affect the financial results of TAURON Capital Group in the perspective of the subsequent reporting periods.

2.3. Financial results of TAURON Capital Group

The figure below shows the EBITDA results of TAURON Capital Group in 2008–2016.

Figure no. 32 EBITDA of TAURON Capital Group in 2008–2016



The table below shows the EBITDA results of TAURON Capital Group, broken down into individual Segments of activity for the years 2014–2016. Data for individual Segments do not comprise consolidation exclusions.

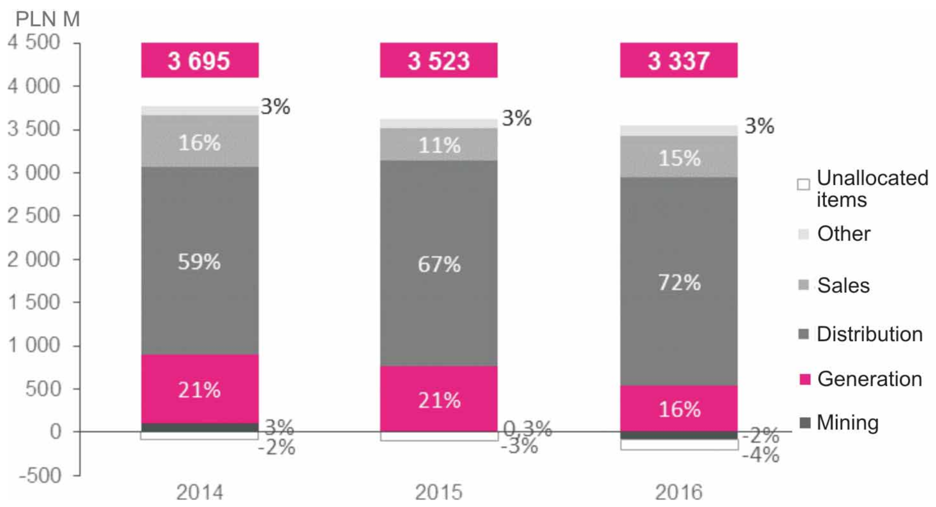
Table no 10. EBITDA results of TAURON Capital Group, broken down into individual Segments of activity*

No.	EBITDA (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)	Change (2016–2015)
1.	Mining	**(82,130)**	9,137	98,420	–	(91,267)
2.	Generation	**545,311**	754,751	792,803	72.3%	(209,440)
3.	Distribution	**2,394,812**	2,372,129	2,172,288	101.0%	22,683
4.	Sales	**490,005**	380,405	608,213	28.8%	109,600
5.	Other	**114,570**	100,320	106,215	114.2%	14,250
6.	*Unallocated items*	***(125,754)***	*(93,514)*	*(83,395)*	*134.5%*	*(32,240)*
	Total EBITDA	**3,336,814**	**3,523,228**	**3,694,544**	**94.7%**	**(186,414)**

** The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

The figure below presents the structure of EBITDA of TAURON Capital Group in the years 2014–2016.

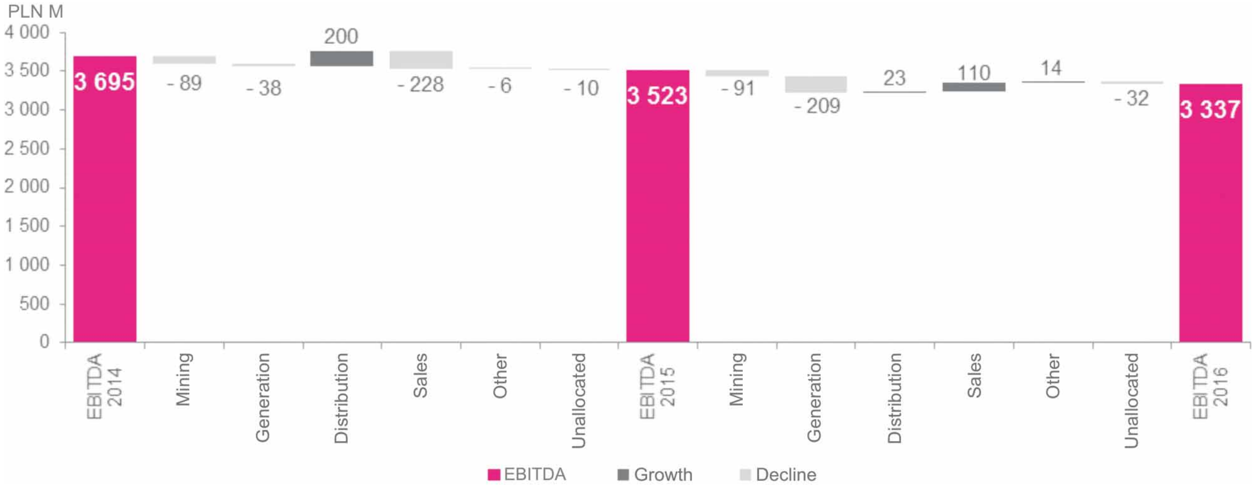
Figure no. 33 Structure of EBITDA of TAURON Capital Group in the years 2014–2016



The Distribution, Generation and Sales Segments have the highest share in EBITDA of TAURON Capital Group.

The figure below presents the change in EBITDA result of TAURON Capital Group in the years 2014–2016.

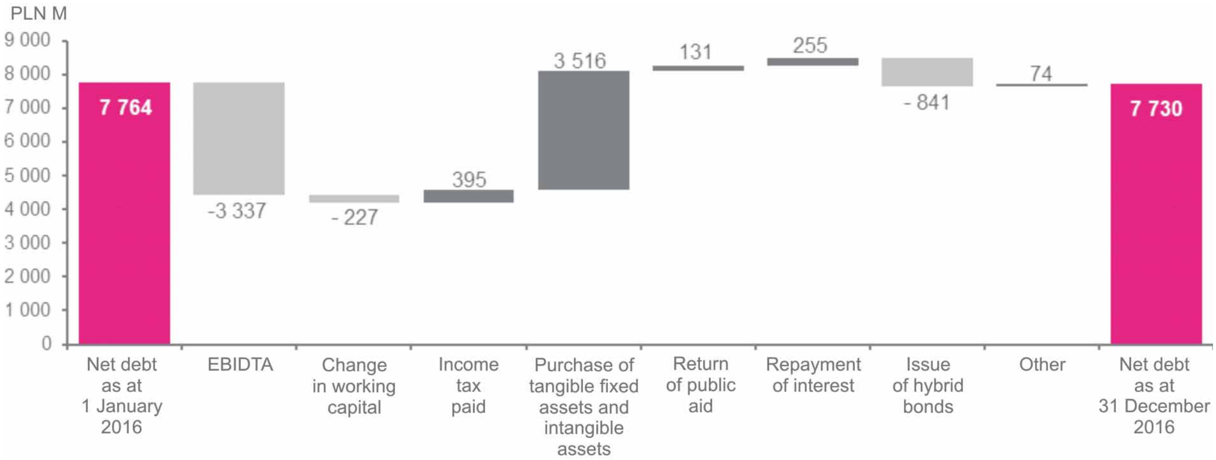
Figure no. 34 Change in EBITDA of TAURON Capital Group in 2014–2016



Cash flows of TAURON Capital Group in 2016

The figure below presents cash flows of TAURON Capital Group in 2016.

Figure no. 35 Cash flows of TAURON Capital Group in 2016



2.3.1. Mining Segment

The table below presents the results of the Mining Segment in the years 2014–2016.

Table no 11. Results of Mining Segment*

Specification (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)	Change (2016–2015)
Mining					
Revenue on sales	**1,311,143**	**1,205,944**	**1,194,024**	**108.7%**	**105,199**
coal – coarse and medium assortments	*346,251*	*346,778*	*359,857*	*99.8%*	*(527)*
steam coal	*918,647*	*836,772*	*803,647*	*109.8%*	*81,875*
other revenues	*46,245*	*22,394*	*30,520*	*206.5%*	*23,851*
Operating profit	**(205,163)**	**(104,328)**	**(6,829)**	**–**	**(100,835)**
Depreciation and write-downs	123,033	113,465	105,249	108.4%	9,568
EBITDA	**(82,130)**	**9,137**	**98,420**	**–**	**(91,267)**

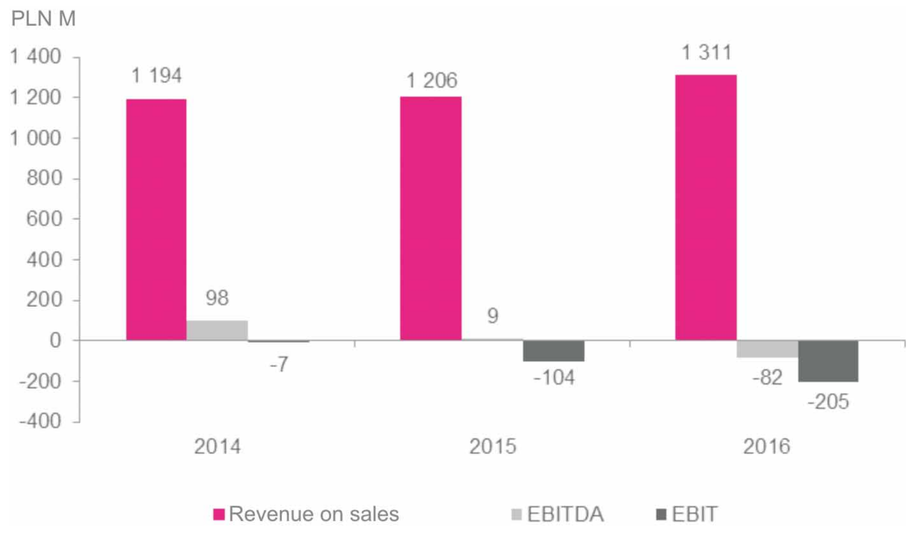
** The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

The operating results, EBIT and EBITDA of the Mining Segment in 2016 reached a lower level than in 2015, which was affected by the following factors:

1) commencement of ZG Brzeszcze activity in the structures of the Segment in 2016,
2) sales of the volume of coal dust lower by 2.6%,
3) price of coal dust sold lower by 13.4%,
4) gaining lower revenues for other assortments, as a result of sales of a volume of medium assortments lower by 7.2% and coarse assortments – by 1.6%, obtaining a price lower by 5.1% and 0.3%, respectively, as a result of coal oversupply in the domestic market and, accordingly, considerable price competition among market participants,
5) lower own cost of coal sold, as a result of:
   a) labour costs lower by 8.0% as a consequence of average employment lower by 522 FTEs,
   b) sales of a part of coal from reserves in 2015, which resulted in recognising of a higher value of coal reserves in own cost in this period. In the period of 2016 the volume of coal produced by TAURON Wydobycie was higher than coal sold, which results in allocation of production costs in the company balance sheet,
6) recognising, in the result of 2015, costs related to:
   a) adjustment of the status of commercial coal and semi-product inventories following the physical stocktaking,
   b) verification of the real value of pre-payments of costs arising from works associated with drilling of production access workings and longwall reinforcement,
   c) settlement of longwall decommissioning costs at ZG Sobieski,
   d) reversal of actuarial provisions for the Company Social Benefits Fund and coal benefit in its part for current pensioners.
7) recognising the following events in other operating activities:
   a) reversal of the provision for ZG Brzeszcze liquidation fund in connection with the change in the discount rate,
   b) Creating a provision for real estate tax in connection with verdicts of administrative courts in 2016 in connection with taxation of mining enclosures.

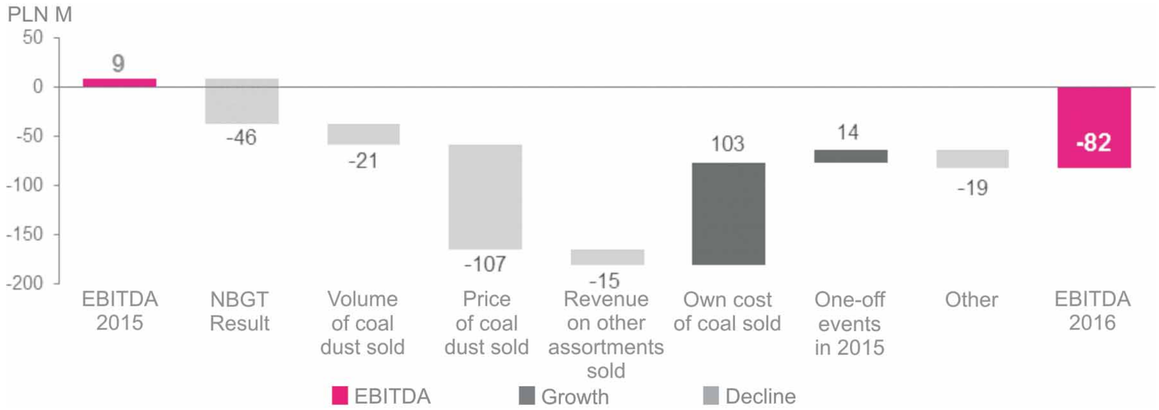
The figure below shows the financial data of the Mining Segment for the years 2014–2016.

Figure no. 36 Financial data of the Mining Segment for the years 2014–2016



The figure below shows the EBITDA result of the Mining Segment, including the significant factors affecting the YoY change.

Figure no. 37 EBITDA result of Mining Segment



Strategic goals and initiatives

The strategic goal of the Mining Segment defined under the Strategy comprises: the stable supply of cost-competitive fuel to TAURON Capital Group, adequate in terms of quality as well as the development of the product offer and maximisation of the margin mass generated by sales of other products.

The goals set out in the Strategy will be implemented through the implementation of strategic initiatives comprising, inter alia: optimisation of costs and capital expenditure, tri-product preparation at ZG Sobieski and ZG Janina and the extension of the packaging line for 'ekogroszek' fine coal.

Major investments

In 2016, in the Mining Segment the total capital expenditure incurred reached approximately PLN 283 million, including the following strategic investment projects:

1) PLN 24 million for the construction of the "Grzegorz" shaft, including the construction of the infrastructure and the accompanying headings,
2) PLN 61 million for the construction of a 800 m level at ZG Janina,
3) PLN 100 million for the investment programme at ZG Brzeszcze (including the purchase of the longwall complex – PLN 73 million).

Other expenditure in the Mining Segment is incurred for the preparation and operation of mining (mainly the purchase of machines and equipment, drilling of headings, longwall preparation).

Development perspectives

The current situation of hard coal mining in Poland (the ongoing restructuring process), unfavourable perspectives for this fuel in the EU energy policy, as well as competitive pressure of imported coal allows for the assumption that in the nearest years market conditions under which domestic coal producers will operate, will remain difficult and demanding. At the same time, due to energy independence issues coal will continue to be used as the basic fuel in the Polish energy sector, including TAURON Capital Group.

The Strategy assumes that planned strategic initiatives and implemented investment projects will enable that the Mining Segment of TAURON Capital Group will continue to belong to the most effective segments in Poland (benchmarks for coal mines in Poland for 2015 show that coal mines of TAURON Wydobycie, next to Lubelski Węgiel "Bogdanka" S.A. coal mine, are classified among most effective mines, both in terms of unit mining cost and efficiency per employee).

In accordance with the Strategy, the main directions of activities in the Mining Segment comprise:

1) continuation of investment projects at ZG Janina and ZG Sobieski,
2) implementation of the investment programme at ZG Brzeszcze,
3) optimisation of costs and expenditure in order to maintain the position of TAURON Wydobycie as the second most cost-effective coal producer in Poland (following Lubelski Węgiel "Bogdanka" S.A. coal mine),
4) construction of the portfolio of products adjusted to internal needs, including the provision of coal supplies for generation units of TAURON Capital Group at a level of 70–80% of demand,
5) development of product offer for clients outside TAURON Capital Group.

Investment implemented by TAURON Capital Group in the Mining Segment is oriented towards the growth of efficiency and increase in the share of coal from own mines in the purchase structure of TAURON Capital Group. The aforementioned factors create the potential for the improvement of the Mining Segment profitability.

2.3.2. Generation Segment

The table below presents the results of the Generation Segment in the years 2014–2016.

Table no 12. Results of the Generation Segment*

Specification (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)	Change (2016–2015)
Generation					
Revenue on sales	**4,356,101**	**5,376,280**	**4,963,651**	**81.0%**	**(1,020,179)**
electricity	*3,101,505*	*4,021,274*	*3,264,510*	*77.1%*	*(919,769)*
heat	*861,029*	*814,045*	*824,791*	*105.8%*	*46,984*
property rights arising from certificates of electricity origin	*335,673*	*480,698*	*574,291*	*69.8%*	*(145,025)*
wind of blast furnace	*0*	*0*	*159,422*	*–*	*0*
compressed air	*61*	*56*	*71,122*	*108.9%*	*5*
other revenues	*57,833*	*60,207*	*69,515*	*96.1%*	*(2,374)*
Operating profit	**(752,813)**	**(3,477,076)**	**72,093**	**–**	**2,724,263**
Depreciation and write-downs	1,298,124	4,231,827	720,710	30.7%	(2,933,703)
EBITDA	**545,311**	**754,751**	**792,803**	**72.3%**	**(209,440)**

** The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

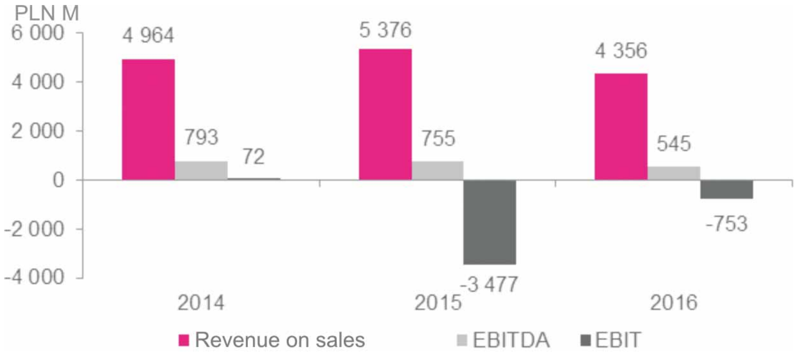
In 2016, the revenue on sales in the Generation Segment was lower by 19% as compared to the corresponding period of the previous year, due to lower revenue on electricity sales (mainly due to a lower volume of sales) and lower revenue on sales of property rights to electricity certificates of origin (lower volume of production from RES, lower price of PMOZE, lack of support to hydroelectric power plants with the electrical capacity above 5 MW_e and limiting the support for co-burning as of 1 January 2016). Higher revenue on sales of heat arise from the higher volume of heat sales and transmission (lower external temperatures in the heating season YoY) and higher sales prices.

The following factors affected the level of achieved results:

1) higher costs of CO_2 reserve – the effect of a higher deficit of free CO_2 emission allowances in relation to CO_2 emission YoY and higher costs of term CO_2 contracting YoY,
2) higher revenues from the ORM – the effect of a higher volume of available capacity (lower contracting sales of electricity YoY) and a higher unit rate of the ORM YoY,
3) revenues from the Intervention Cold Reserve (gained since 1 January 2016),
4) lower unit variable costs of generation, due to the decline in unit consumption costs of coal and biomass and optimisation of use of generation units,
5) decline in electricity prices in the term wholesale market YoY, translating into a lower volume of electricity sales YoY (including, within resale of energy purchased),
6) lower price and volume of property rights from RES (effect of PMOZE oversupply in the market, lack of support to hydroelectric power plants with the installed electrical capacity over 5 MW_e and limitation of the support to co-burning as of 1 January 2016, and lower production from RES YoY; optimisation of performance of biomass units and worse wing conditions in relation to the previous year),
7) higher margin for heat – mainly the effect of the decline in prices of fuel used for heat production and a higher volume of heat transmission (lower external temperature in the heating season (4.6°C in 2015, 4.0°C in 2016),
8) recognising impairment write-offs of tangible fixed assets, intangible assets and goodwill as a result of impairment tests,
9) other factors – mainly lower fixed costs (the highest reduction in the area of repairs and external services).

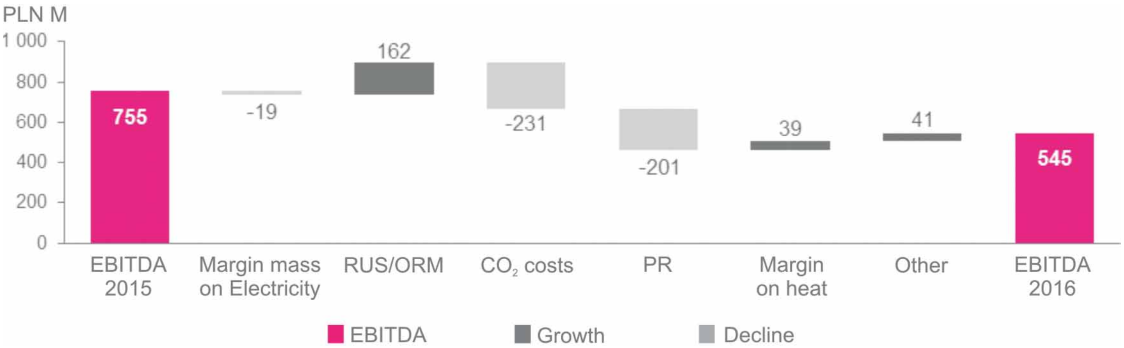
The figure below shows the financial data of the Generation Segment for the years 2014–2016.

Figure no. 38 Financial data of the Generation Area for the years 2014–2016



The figure below shows the EBITDA result of the Generation Segment, including significant factors influencing the YoY change.

Figure no. 39 EBITDA result of the Generation Segment



Strategic goals and initiatives

The main goals of the Generation Segment defined under the Strategy include:

1) for TAURON Wytwarzanie company: Sustaining the loss in value of assets and modernising the fleet,
2) for TAURON Ekoenergia company: Raising the profitability of generation assets held and preparation of the option for the profitable development of the area,
3) for TAURON Ciepło company: Development of heat sales and distribution.

The goals set out in the Strategy will be implemented through the implementation of strategic initiatives comprising, inter alia: reducing costs and capital expenditure, optimisation of employment, optimisation of production assets and sales of redundant non-production assets.

Major investments

In 2016, in the Generation Segment the total capital expenditures incurred reached PLN 1,661 million, including the following strategic investment projects:

1) PLN 1,237 million – construction of the coal-fired unit with the capacity of 910 MW at Elektrownia Jaworzno III,
2) PLN 107 million – construction of new capacity in co-generation at ZW Tychy (50 MW),
3) PLN 11 million – construction of flue gas denitrification installations and modernisation of 200 MW blocks at Elektrownia Jaworzno.

Moreover, expenditure of approx. PLN 57 million was incurred for investment associated with the development of the heating network, PLN 18 million – for modernisation of hydroelectric power plants and approx. PLN 80 million – for replacement and repairs expenditure in TAURON Wytwarzanie. In Stalowa Wola, the investment with participation of the strategic partner, PGNiG, is under implementation, comprising the construction of the CCGT unit of 449 MW_e capacity, with the heat generation component of 240 MW_t capacity. Completion of this investment is scheduled in 2019. In January 2016, the contract with the general contractor was rescinded. A new agreement for gas supplies was negotiated with PGNiG. In connection with the suspension of financing by banks, talks concerning further project financing are in progress.

Development perspectives

Available forecasts and analyses indicate that the conditions under which domestic electricity producers will act shall remain unfavourable, mainly due forecast conservative developments in electricity prices as well as a decrease in production volumes in conventional generation units (arising, inter alia, from the age and low efficiency and the growing share of production from RES). Interim mechanisms introduced by the TSO (ORM, intervention cold reserve) have a positive impact on producers of electricity.

Ensuring KSE operating security understood mainly as a possibility of demand balancing by generation resources will remain the key issue in the nearest years. To that end, introduction of the capacity market is planned in Poland, which should enable to obtain an additional source of revenue by the generation units.

The major strategic direction determined for conventional assets of the Generation Segment includes obtaining the economic effectiveness or permanent decommissioning. Activities within the Area will focus, inter alia, on the completion of the construction of the coal-fired unit in Jaworzno with the capacity of 910 MW, including the implementation of the project with the strategic partner through sales of a part of shares while maintaining the control. Integration of assets management in the Generation and Heat Segments is planned, in coordination with the Mining Segment.

In the scope of RES options for the development of RES installations are prepared, assuming the favourable support system and the development of a profitable model of their performance.

In the scope of heat generation, distribution and trade, significant activities include the participation in the Low Emission Liquidation Programme, searching for solutions in the multi-fuel co-generation area and increasing the use of existing infrastructure.

2.3.3. Distribution Segment

The table below presents the results of the Distribution Segment in the years 2014–2016.

Table no 13. Results of the Distribution Area*

Specification (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)	Change (2016–2015)
Distribution					
Revenue on sales	**6,310,216**	**6,450,274**	**6,074,646**	**97.8%**	**(140,058)**
distribution services	*5,892,510*	*6,022,144*	*5,656,807*	*97.8%*	*(129,634)*
connection fees	*103,636*	*125,698*	*121,044*	*82.4%*	*(22,062)*
maintenance of street lightning	*116,462*	*116,042*	*111,634*	*100.4%*	*420*
other revenues	*197,608*	*186,389*	*185,161*	*106.0%*	*11,219*
Operating profit	**1,363,236**	**1,371,577**	**1,209,344**	**99.4%**	**(8,341)**
Depreciation and write-downs	1,031,576	1,000,552	962,944	103.1%	31,024
EBITDA	**2,394,812**	**2,372,129**	**2,172,288**	**101.0%**	**22,683**

** The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

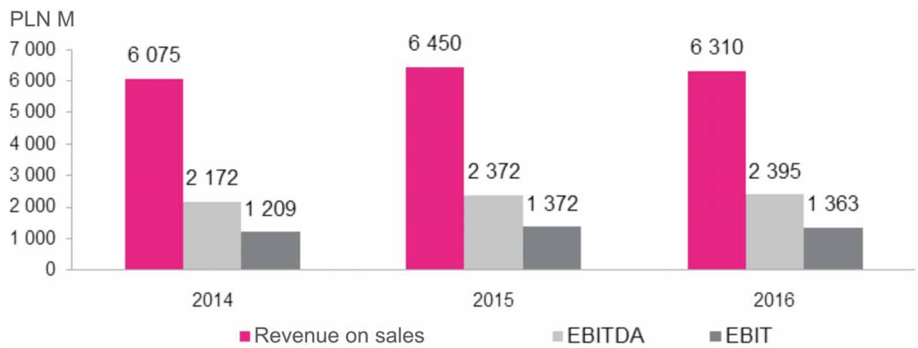
In 2016, as compared to 2015, the Distribution Segment recorded a decline in revenue by approximately 2.2% and the change of results at the EBIT and EBITDA operating level by -0.6% and 1.0%, respectively. The following reasons affected the dynamics of the results:

1) decrease of the average rate of distribution service sales to end consumers in each tariff group, excluding A group, mainly as a result of WACC reduction in the 2016 tariff,
2) growth of supplies to industrial consumers as a result of GDP and production growth, in particular, among consumers in B group; a decline in supplies to consumers in A group as a result of difficulties in the mining and metallurgical sector as well as ongoing restructuring of companies in those sectors,
3) decline in energy volume supplied to households as a result of one-off recognition of a favourable estimation associated with migration of clients to the Central Billing System in the previous year,
4) growth in purchase costs of transmission services as a result of a higher rate of the qualitative fee applied for higher electricity consumption and the RES fee introduced as of July 2016,

5) significantly lower price of energy balancing in the contract with TAURON Capital Group; a favourable effect was also obtained due to reduction in the purchase of the Hedge volume,
6) in accounting terms (with additional estimation), a higher indicator of grid losses YoY, mainly as a result of recognition of a favourable estimation associated with migration of clients to the Central Billing System in the 1st half of 2015,
7) reduction of revenues on connecting fees from entities connected to the HV and MV grid (inter alia, wind farms); a lower level of fees also in connection with the implementation of HV connection at PKP Energetyka in 2015,
8) reduction of revenue on fees for over-standard passive energy off-take as a result of the decline in energy price on the competitive market recognised in the calculation of the fee,
9) increase of the revenue due to elimination of collisions, mainly as a result of implementation of tasks in the 4th quarter,
10) lower costs of the actuarial provision – a one-off event in December 2016 associated with the harmonisation of the Company Collective Bargaining Agreement in companies of the Distribution Segment; the reduction of the retirement age was also a premise for partial reversal of the provision,
11) lower fixed costs, including, in particular: lower costs of provision for the Voluntary Redundancy Programme, lower costs of customer service in TAURON Obsługa Klienta, lower costs of tree logging, favourable balance of allowance for uncollectible accounts,
12) growth of costs of taxes and fees as a result of implemented investment and growth in the value of grid assets and in connection with creating of the provision for risk of increased periodical fees for transmission line easement for the power infrastructure located on the premises of forest districts,
13) higher result on other core activity.

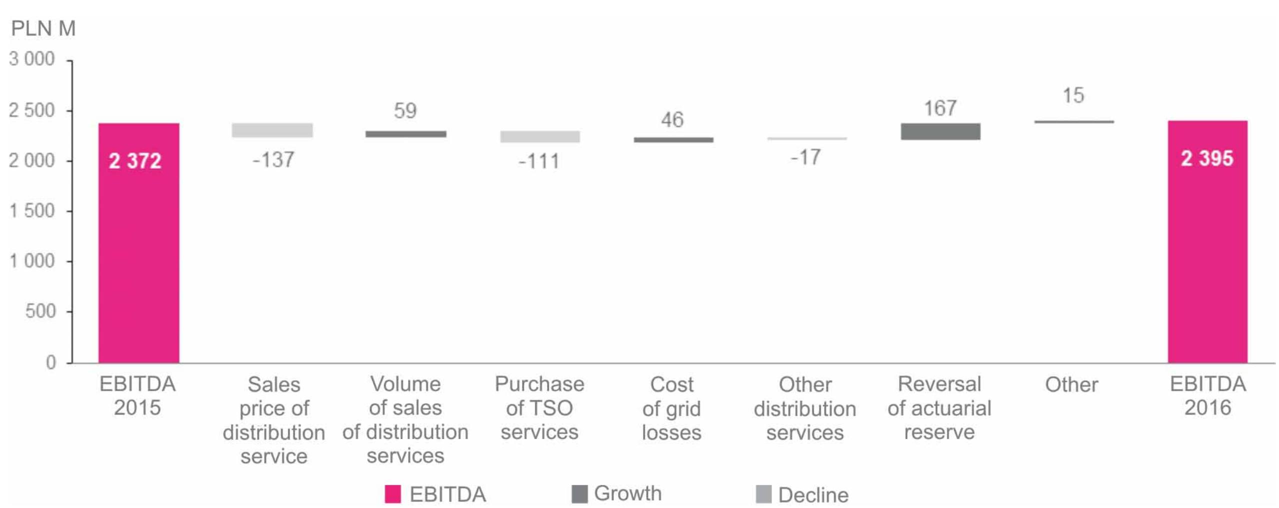
The figure below shows the financial data of the Distribution Segment for the years 2014–2016.

Figure no. 40 Financial data of the Distribution Segment for the years 2014–2016



The figure below presents the EBITDA result of the Distribution Segment, including significant factors influencing the YoY change.

Figure no. 41 EBITDA result of the Distribution Segment



Strategic goals and initiatives

The main goal of the Distribution Segment defined under the Strategy is: To maintain the position of a leader on the Polish market in the area of security and effectiveness of grid functioning.

The assumed goals will be implemented through key strategic initiatives: The “Single Distribution” programme comprising projects optimising operating processes in the company; activities affecting the improvement of customer satisfaction and simultaneously the improvement of the company image; the electrical mobility programme and storage systems.

Major investments

In 2016, in the Distribution Segment the total capital expenditures incurred reached PLN 1,806 million. The main directions of investment included:

1) PLN 591 million for investment associated with connecting of new consumers,
2) PLN 953 million for investments associated with the modernisation and replacement of the grid.

Moreover, in 2016 expenditure for the implementation of the following Strategic Investment Projects was incurred: *The system of grid assets management* – approx. PLN 35 million, *The construction of the Grid Management Centre in Kraków* – approx. PLN 6 million. Expenditures in the total amount of PLN 200 million were also incurred on: the construction of the building of the Grid Management Centre in Wrocław, communications and IT, buildings and structures, vehicles, modernisation of street lightning and other tasks associated with core operations.

Development perspectives

The new challenges generating development needs in the Distribution Segment will include prosumers, energy clusters and the developing electromobility sector. The smart grid and smart metering technologies will be significant for further development of the energy sector. Such solutions will introduce additional functionalities, both on the supplier and client side, and they will definitely influence the development of the industry. The Distribution Segment has to continue activities oriented towards ensuring of reliable electricity supply with the adequate quality. To accomplish this purpose, significant capital expenditure will be necessary for the replacement of assets, required changes in the construction technology, automation, smart meters and introduction of energy storage as an element stabilising grid parameters. Moreover, the client has to be in the focus of attention in the distribution area, therefore further simplification of procedures and the development of new communication channels is extremely significant.

It should be taken into account that such challenges will be implemented on the regulated market which determines the activity of the Company with new elements of the DSO policy introduced by the ERO President and the associated risks, i.e. the updated approach to the average weighted capital cost, correction factors of enterprise efficiency improvement in the scope of operating costs and the level of the balancing difference, continuation of qualitative regulation.

2.3.4. Sales Segment

The table below presents the results of the Sales Segment in the years 2014–2016.

Table no 14. Results of the Sales Segment*

Specification (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)	Change (2016–2015)
Sales					
Revenues on sales	**14,016,190**	**15,873,355**	**15,277,451**	**88.3%**	**(1,857,165)**
electricity, including:	*8,814,692*	*10,357,041*	*9,708,534*	*85.1%*	*(1,542,349)*
revenues from retail sales of electricity	*7,145,644*	*8,111,002*	*7,950,864*	*88.1%*	*(965,357)*
greenhouse gas emission allowances	*363,500*	*94,086*	*183,451*	*386.3%*	*269,414*
fuel	*1,583,672*	*1,972,403*	*1,935,135*	*80.3%*	*(388,730)*
distribution service (transferred)	*3,183,232*	*3,377,473*	*3,332,151*	*94.2%*	*(194,241)*
other revenues, including commercial services	*71,094*	*72,353*	*118,180*	*98.3%*	*(1,259)*
Operating profit	**479,374**	**369,529**	**582,307**	**129.7%**	**109,845**
Depreciation and write-downs	10,631	10,876	25,906	97.7%	(245)
EBITDA	**490,005**	**380,405**	**608,213**	**128.8%**	**109,600**

** The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

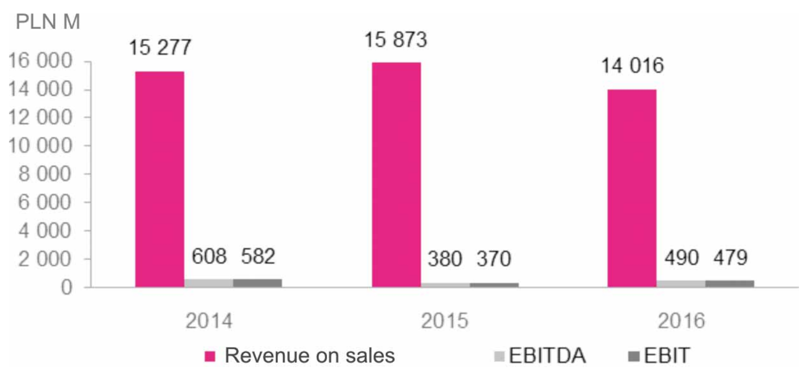
In 2016, revenues on sales reached a level lower by 11.7% in relation to 2015, mainly due to the decline of revenue on sales of electricity, fuel and the distribution service (transferred). The decline in revenues on sales of electricity is recorded due to the lower volume of both wholesale and retail sales. The transfer of competence in biomass sales from TAURON to Biomasa Grupa TAURON is the main reason of the decline in the revenues on sales in the scope of fuel trade. The overall decline in revenues was partly set off by the growth in the sales volume of greenhouse gases emission allowances.

The operating results, EBIT and EBITDA in 2016 reached a lower level than in the previous year, which was mainly affected by the following factors:

1) a lower volume of retail electricity sales (by 3.9 TWh) – the main reasons should be attributed to the loss of large business clients in the area of activity of TAURON Capital Group as well as the slowdown in external expansion rate due to enhanced sales policy of competitive companies,
2) a lower unit margin on retail trade in electricity – the adverse impact on the result is caused by loyalty programmes for business segment clients – at prices resulting from market wholesale levels of prices of electricity and property rights, securing loyalty of mass clients – transfer from the tariff to the product price list and the reduction of the tariff price for households in TAURON Sprzedaż by 0.88% as of 2016,
3) a growth in the level of revenues from fixed trade fees – the growth in the fee arises from conducting active loyalty actions in the mass segment, aimed at acquisition of clients and minimising of the number of losses resulting from activity of competition on the area of activity of companies of TAURON Capital Group. Sales with the trade fee (reduction of the floating component of the price and transfer of this revenue to the fixed component) guarantees both the profitability of sales and market competitiveness in the scope of products offered,
4) a growth in costs of the redemption obligation of property rights for PMOZE from 14% to 14.35%, for PMMET from 1.3% to 1.5%, for PMGM from 4.9% to 6.00% and introduction of the obligation for PMOZE-BIO (0.65%),
5) lower purchase costs for PMOZE – exploiting the favourable market situation (mainly through the decline in prices of green certificates at the TGE),
6) Lower level of fixed costs – the deviation results mainly from lower purchase costs of sales and marketing actions,
7) provision for EC Stalowa Wola – in connection with the violation of the schedule and material technical conditions of the contract with the general contractor of the project concerning the construction of the CCGT Unit in Stalowa Wola, which affect both the security and reliability of unit performance as well as its future effectiveness and costs of its performance, on 29 January 2016 EC Stalowa Wola rescinded the contract with the general contractor. In connection with the foregoing, in 2015 TAURON recognised provisions for agreements generating charges with the joint venture – EC Stalowa Wola in the total amount of PLN 182,9 million. In 2016 the provision was increased by about PLN 4,4 million.
8) Higher result on trading in CO_2 emission allowances and gas fuel (taking advantage of the favourable situation in the process of effective portfolio hedging under the downward trend of prices on the gas market and simultaneous increase in the volume of sales).

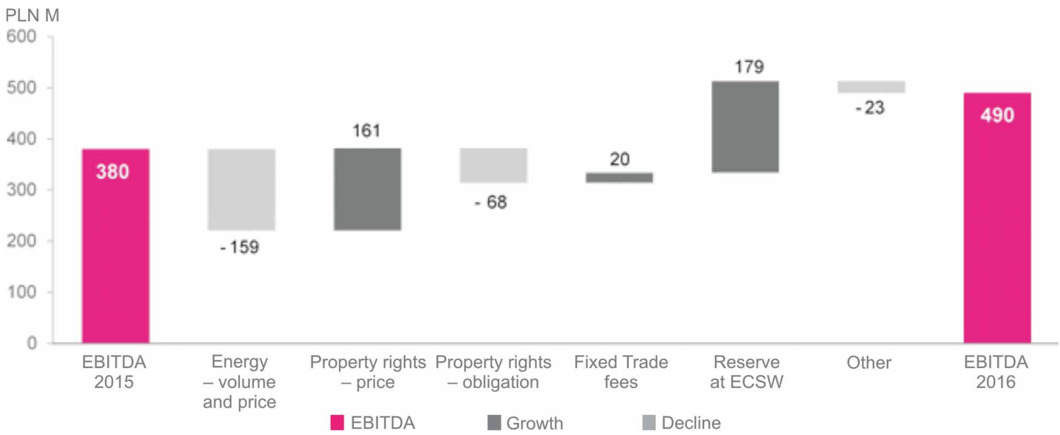
The figure below shows the financial data of the Sales Segment for the years 2014–2016.

Figure no. 42 Financial data of the Sales Segment for the years 2014–2016



The figure below shows the EBITDA result of the Sales Segment, including significant factors influencing the YoY change.

Figure no. 43 EBITDA result of the Sales Segment



Strategic goals and initiatives

The main goal for the Sales Segment defined in the Strategy is: to achieve the position of a leader in relations with clients through the high quality of service and product leadership.

The goals determined in the Strategy will be accomplished through the implementation of strategic initiatives comprising, inter alia: growth of sales potential through transformation of service channels into integrated channels of contact with clients focusing on sales and product advice, growth in the value of products and services sales to mass clients through the development of the product offer and sales techniques, development of products and building communication channels in the scope of specialised products and the partnership offer addressed to the mass client segment, as well as to business clients, strengthening of expansion and optimisation of sales margins in business segments.

Major investments

In 2016, in the Sales Segment the total capital expenditures incurred amounted to PLN 1.5 million.

Development perspectives

Growing competition in the Sales Segment as well as the demanding situation on the wholesale electricity market leads to the decline of sales volume and margin erosion. Due to the aforementioned conditions, the Strategy assumes that a platform for long-term growth in the Sales Segment will be based on maintaining long-term relations with the client (quality of service) and the development of new products and business models.

In order to implement the strategic vision of TAURON Capital Group and respond to clients' needs in the best way in the Polish energy sector, the Sales Segment focuses on the following activities:

1) Identifying client's needs and the development of tailored product offer,
2) development of innovation aiming at working out new products and services for the client (including the development of services associated with energy and non-energy services, services such as *smart home*, development in the area of *e-mobility*),
3) maintaining the leadership in customer service quality,
4) development of modern and integrated sales and customer service channels (*omni-channel*, *e-commerce*).

2.3.5. Other Segment

The table below presents the results of the Other Segment in the years 2014–2016.

Table no 15. Results of Other Area*

Specification (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)	Change (2016–2015)
Other					
Revenue on sales	**827,928**	**927,953**	**870,035**	**89.2%**	**(100,025)**
customer service, accounting and IT services	*560,166*	*581,050*	*604,118*	*96.4%*	*(20,884)*

Specification (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)	Change (2016–2015)
electricity and property rights arising from certificates of electricity origin	*12,827*	*73,927*	*168,592*	*17.4%*	*(61,100)*
biomass	*111,087*	*171,326*	*0*	*64.8%*	*(60,239)*
aggregates	*90,491*	*89,102*	*91,214*	*101.6%*	*1,389*
other revenues	*53,357*	*12,548*	*6,111*	*425.2%*	*40,809*
Operating profit	**42,642**	**32,596**	**56,593**	**130.8%**	**10,046**
Depreciation and write-downs	71,928	67,724	49,622	106.2%	4,204
EBITDA	**114,570**	**100,320**	**106,215**	**114.2%**	**14,250**

** The three-year period is presented due to transparency of information. The approximate (due to significant changes in the organisation of Segments, as compared to the period before 2012) results in the five-year period are presented in subsection 4.6. of this report.*

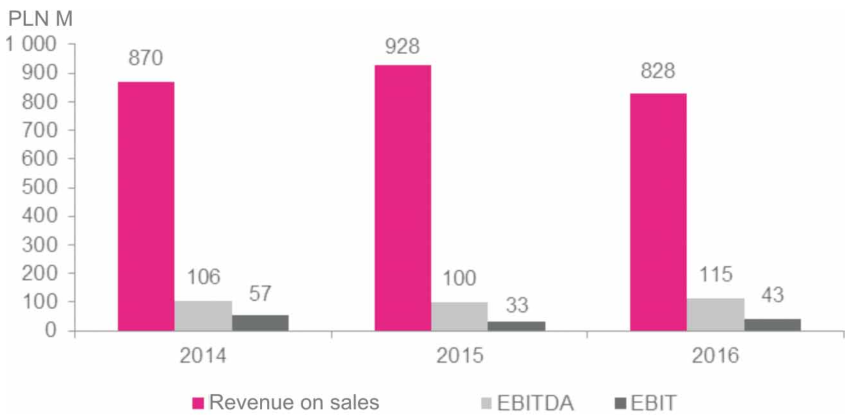
In 2016 revenues on sales of the Other Segment dropped by approx. 11% as compared to the previous year; the main reasons of this situation should be attributed to the loss of revenues on sales of electricity and property rights.

Higher results of the Other Segment YoY arise from the following events:

1) recognising the result of KOMFORT-ZET company in 2016 in connection with covering it by consolidation in accordance with the *Accounting Policy of TAURON Group,*
2) recognising the result of Biomasa Grupa TAURON company in 2015 in connection with covering it by consolidation in accordance with the *Accounting Policy of TAURON Group*,
3) gaining a higher margin on sales of stone assortments,
4) decline in turnover on sales of electricity and property rights, which reduced the accomplished negative margin.

The figure below shows the financial data of the Other Segment for the years 2014–2016.

Figure no. 44 Financial data of the Other Area for the years 2014–2016



Major investments

In the Other Segment the level of capital expenditures incurred in 2016 reached 65 million. They include mainly expenditure on IT systems.

2.4. What can be expected in 2017

Forecasts of the macroeconomic situation of Poland for 2017 allow for anticipation of a moderate economic recovery, with the GDP growth in the range of 2.7%–3.6%[1] and the unemployment rate at a level of 8%[2], against estimated values for 2016 amounting to 2.3%–2.8%[3] and 8.9%, respectively.

[1] *The forecast of the World Bank of 11 January 2017 estimates the GDP growth of Poland for 2017 at a level of 2.7%, the forecast of Standard & Poor's of 10 January 2017 indicates the level of 3.3%, the assumptions to the draft Budget Act for 2017 – 3.6%.*

[2] *According to the assumptions of the draft Budget Act for 2017.*

[3] *The forecast of the World Bank of 11 January 2017 and the forecast of Standard & Poor's if 10 January 2017.*

According to the forecasts, the economic situation in 2017 will be driven by domestic demand, development of entrepreneurship and innovation as well as the inflow of the EU funds from the 2014–2020 perspective, providing hopes of stimulating the investment, in particular, in the 3rd and 4th quarter of 2017.

The above mentioned conditions allow for assumption that the growth rate of KZEE in 2017 will be at least maintained. According to the TSO operating data, KZEE for 11 months of 2016 increased by 1.59% as compared to the corresponding period of 2015.

In connection with the implementation of the Efficiency Improvement Programme, in 2017 TAURON Capital Group plans to reach savings at a level of PLN 432 million (including PLN 338 million to affect the level of EBITDA, and PLN 94 million to refer to CAPEX savings). In addition, due to the implementation of strategic initiatives, TAURON Capital Group plans to reach additional financial effects at a level of PLN 273 million (including PLN 155 million to affect the level of EBITDA, and PLN 118 million to refer to limitation of CAPEX savings).

2.5. Basic products, goods and services

The table below presents volumes of production and sales in TAURON Capital Group for the years 2016–2014.

Table no 16. Volumes of production and sales for the years 2016–2014

No.	Volumes of production and sales	unit	2016	2015	2014	Change in % (2016/2015)
1.	Commercial coal production	*M Mg*	**6.37**	4.91	5.40	129.7%
2.	Net production of electric energy	*TWh*	**16.80**	18.56	17.35	90.5%
	including production from RES	*TWh*	***1.32***	*1.63*	*1.82*	*81.0%*
3.	Heat production	*PJ*	**11.52**	11.51	13.41	100.1%
4.	Distribution of electricity	*TWh*	**49.68**	49.20	47.90	101.0%
5.	Retail sales of electricity (in total, by Areas: Sales and Generation)	*TWh*	**32.04**	35.94	36.43	89.2%
6.	Number of clients – Distribution	*thou.*	**5,474**	5,418	5,378	101.0%

2.6. Sales markets and sources of supply

2.6.1. Sales markets

Mining Segment

The basic activity of the Mining Segment is carried out by TAURON Wydobycie company 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 – as the accompanying mineral from the Breszcze deposit. Within TAURON Group three mines operate: ZG Sobieski, ZG Janina and, as of 1 January 2016 – ZG Brzeszcze.

Depending on the coal assortment, coal has the following trade parameters:

1) calorific value from 19 MJ/kg to 30 MJ/kg,
2) ash content from 11% to 23%,
3) sulphur content from 0.4% to 1.4%.

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,
2) sales of coarse, medium and small amount of fine coal assortments through the organised sales network all over the country.

Sales of coal from TAURON Wydobycie is mainly provided in the region of southern and central Poland, in particular, the following provinces: Śląskie, Małopolskie, Podkarpackie, Świętokrzyskie and Dolnośląskie.

In 2016, sales of hard coal amounted to approximately 6.1 million Mg, including 4.7 million Mg (about 77%) to companies of the Generation Segment. As compared to 2015, it means a growth by approximately 19% which results from the execution of coal sales by ZG Brzeszcze which started its operations in the structures of TAURON Wydobycie as of 1 January 2016. Without recognising sales of ZG Brzeszcze, the volume of sales was lower by 3% due to the lower demand in the scope of coal dust. The reason is the continuing difficult market situation, resulting mainly from oversupply of coal dust in relation to the demand and its selling off by competitive companies below production costs.

Production of commercial coal in 2016 was higher by approx. 30% than in the corresponding period of the previous year, as a result of launching the production at ZG Brzeszcze. Without recognising the production accomplished by this plant, the production accomplished by other mines of TAURON Wydobycie was higher by approximately 6%.

Generation Segment

The basic activity of the Generation Segment within TAURON Capital Group comprises generation of electricity and heat performed in:

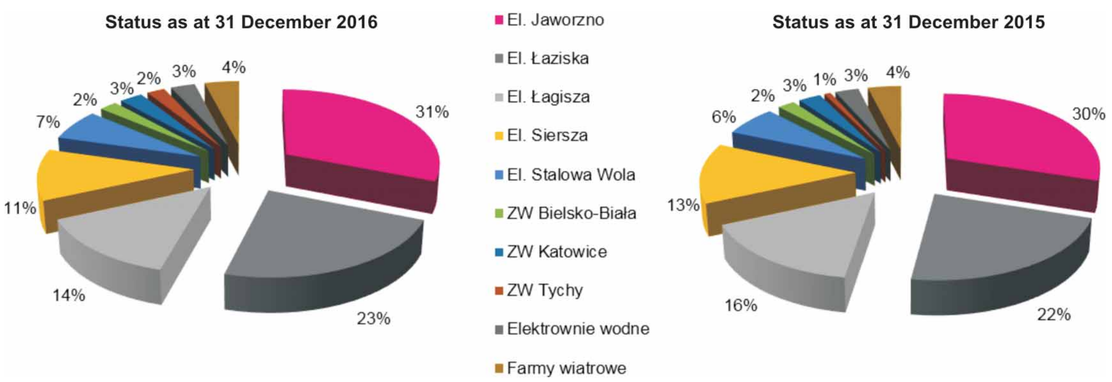
1) coal-fired and biomass burning power plants and combined heat and power plants,
2) hydroelectric power plants,
3) wind farms.

Moreover, the activity of the Generation Segment comprises trade, distribution and transmission of heat.

The total installed electric capacity of generation units of the Generation Segment at the end of 2016 amounted to 5.0 GW_e of electric capacity and 2.4 GW_t of heat capacity.

The figure below presents the structure of installed electric capacity of the Generation Segment as at 31 December 2016 and 31 December 2015.

Figure no. 45 Structure of installed electric capacity of the Generation Segment according to the status on 31 December 2016 and 31 December 2015



In 2016, the Generation Area produced approximately 16.8 TWh of electricity (including 1.3 TWh from RES), i.e. by about 9% less in relation to 2015 when the production of electricity amounted to approximately 18.6 TWh (including 1.6 TWh from RES). In 2016, sales of electricity from own production, including energy purchased for trading purposes, reached approximately 15.5 TWh, which means a decline by approximately 28% in relation to 2015.

The lower electricity production results mainly from the adopted trading strategy taking into account changeable market conditions and unfavourable wind conditions (on the other hand, favourable hydrological conditions had an impact on the lower level of production in hydroelectric power plants).

In 2016 the electricity generated by the Generation Segment was sold mainly to the Sales Segment of TAURON Capital Group (59%), as well as at the TGE and to external consumers. In 2016, the share of electricity sales on the balancing market was significantly higher in relation to 2015.

Heat sales of the Generation Segment in 2016 amounted to 15.8 PJ and it was higher by approximately 6% in relation to the corresponding period of 2015. The share of heat generated in own sources in the total level of heat sales in 2016 amounted to approximately 59%.

Moreover, due to electricity generation from RES and in co-generation, the Generation Segment acquires certificates of origin, which are subsequently purchased by companies of the Sales Area and submitted to the President of ERO for redemption.

Distribution Segment

TAURON Dystrybucja company acts as the DSO, pursuant to the decision of the President of ERO. The Distribution Segment provides services to approximately 5,474 thousand end consumers.

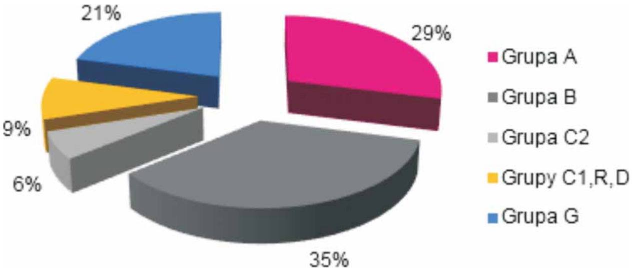
The activities of the Distribution Segment cover the area of about 57 thousand km^2, located mainly in the Śląskie, Małopolskie, Dolnośląskie and Opolskie provinces and, in addition, in the Podkarpackie, Łódzkie and Świętokrzyskie provinces. The operating functions are fulfilled by eleven branches of the company, located in: Bielsko-Biała, Będzin, Częstochowa, Gliwice, Jelenia Góra, Kraków, Legnica, Opole, Tarnów, Wałbrzych and Wrocław.

In 2016 the sales volume of electricity distribution services amounted to 49.68 TWh, i.e. it increased in relation to 2015 by approximately 0.48 TWh, i.e. 2.7%.

In the volume of supply of the distribution services sales to tariff consumers in the scope of individual levels of voltage makes 95.6%: high voltage (A group), medium voltage (B group) and low voltage (C,G,R). The total quantity of electricity supplied in 2016 within sales of distribution services to tariff consumers connected to the TAURON Dystrybucja grid, amounted to 47.5 TWh (estimated) and it was higher as compared to 2015 by about 0.47 GWh, i.e. by 1%.

The figure below presents electricity distribution in 2016 according to tariff groups (the structure in relation to 2015 has not changed).

Figure no. 46 Distribution of electricity according to tariff groups in 2016 (MWh)



Sales of distribution services is carried out on the basis of comprehensive agreements as well as agreements on provision of distribution services concluded with consumers. The first type of agreement covers both sales of electricity by the companies of the Sales Se and supply of this energy by the company acting as the DSO. The second type of agreement regulates only supplies of electricity by the company acting as the DSO. In case of this type of agreements, the purchase of electricity is regulated in separate agreements for electricity sales, concluded by a consumer with the seller it selects.

Share of sales value of distribution services under the comprehensive agreements in the total value of sales of distribution services to end consumers in 2016 reached about 54% whereas the volume of supplies in the total volume of supplies to end consumers amounted to approximately 36%.

Sales Segment

The Sales Segment comprises activities in the scope of wholesale of electricity and other products of the energy market as well as activity in the scope of retail sales of electricity. On the other hand, operations within wholesale trading 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. Activity in the area of retail sales comprises sales of electricity to end customers, including key accounts.

TAURON conducts wholesale trade of electricity and natural gas for the needs of securing the purchase and sales positions of entities from TAURON Capital Group. The Company also deals with *proprietary trading* activities, i.e. trading of electric energy, natural gas, CO_2 emission allowances and related products, with the purpose of generating profits on volatility of prices over time. The activity of the Company comprises wholesale markets both in the country and abroad, and it is conducted on the SPOT market and forward market. In Poland, TAURON is an active participant of TGE and OTC platforms conducted by the London energy broker – Tradition Financial Services. On 1 February 2016 TAURON concluded the agreement with TGE for fulfilment of a market maker function in the scope of instruments for electricity at the RTT. TAURON actively participates in auctions of the cross-border exchange of energy transmission capacity on the Polish-Czech, Polish-German and Polish-Slovakian border, managed by the CAO auction office. Trade in the German market in the scope of trading in financial instruments such as futures, is mainly carried out through EEX exchange. On the other hand, in the Czech and Slovakian markets trade is performed through the subsidiary – TAURON Czech Energy. Moreover, the Company operates on exchanges of KOTE a.s. (Czech Republic) and OKTE a.s. (Slovakia).

In the scope of wholesale trading in gas fuel the company is an active participant of the gas market operated by TGE. It is involved in proprietary trading activity on an international gas exchange – POWERNEXT Pegas. In February 2016 the company extended its activity on the POWERNEXT gas exchange by new hubs: New Connect Germany (NCG) and Tittle Transfer Facility (TTF). Besides prop trading, entering new NCG hubs (German market) will also enable physical gas deliveries to the Czech Republic and to Poland via the Czech Republic. On the other hand, entering

TTF hub (Dutch market) provides access to the most liquid market on the continent, which will enable prop trading activity and increasing of gas trading volumes. Acting on the gas market the Company secures commodity supplies to entities in TAURON Capital Group.

Agreements concluded by the Company with German transmission system operators: GASCADE Gastransport and ONTRAS Gastransport GmbH, enable the purchase and import of gas from the area of the German gas hub-GASPOOL. TAURON is the participant of the European capacity trading platform, PRISMA European Capacity Platform GmbH, where it purchases interconnector capacity. In the scope of capacity booking in the domestic market, the Company operates as the participant of the auction platform, GSA GAZ-SYSTEM Auctions. Through the TAURON Czech Energy company, gas trading in the Czech market is also carried out as well as interconnector gas exchange between Poland and Czech Republic.

The Company provides operating supervision over purchases of property rights allocated for the fulfilment of the statutory obligation of companies of TAURON Capital Group to redeem those rights and over sales of property rights acquired from production of companies of TAURON Capital Group.

The Company also acts as the competence centre in the area of CO_2 emission allowances for the companies of the TAURON Capital Group and the external customers. While implementing the above goals in the area of CO_2 emission allowances trading, the Company actively participates in trading on the European Climate Exchange (the ICE), the EEX exchange in Leipzig and the OTC market.

In 2016, the Sales Segment operated in the market environment where the level of competitiveness in individual segments did not change significantly as compared to the previous years. In 2016, the market of households (individual clients), irrespective of its announced liberalisation, was still subject to the obligation of electricity sales price approval by the President of ERO.

According to the ERO data, from mid-2007 until November 2016, i.e. since the beginning of the liberalisation process of the energy market, approximately 458 thousand of households and approximately 174 thousand of institutional entities which changed their electricity supplier have been recorded.

In the segment of institutions and economic operators (business client), where the competition is high and companies have already been using liberalisation of electricity prices for several years, the progress of the liberalisation has resulted in the increasing awareness of business clients expecting competitive solutions. The enhanced sales activity of energy companies exerts increasing price pressure. New entities competing for clients have also appeared, and the transparency of energy market mechanisms is already the requirement in activities on this market, since business clients use a possibility to change the supplier more willingly. The high potential is perceived in the household segment where the number of supplier changes makes a minor percentage.

In 2016 over 81 thousand consumers of electricity changed their supplier (including approximately 15 thousand institutional clients and approximately 66 thousand households). In 2016 the dynamics of changes in case of households amounted to 64%, and in case of institutional entities – to 42%.

In 2016 the retail sales of electricity conducted by the Sales Segment to approximately 5.3 million clients reached about 32.0 TWh, i.e. 89.2% of the level reached in 2015 when the sales amounted to about 35.9 TWh. The reduced volume of sales was mainly driven by two factors: lack of energy sales to PSE in 2016 (approx. 1.7 TWh in 2015) and market factors. The slowdown in the expansion rate on the external area, mainly due to the aggressive pricing policy of competitive companies aiming at acquisition of clients form the portfolio of sales companies of TAURON Capital Group (mainly, clients from the SME segment and medium-sized clients from the business segment).

The segmentation of clients used by TAURON Capital Group (strategic, business and mass clients), depending on the quantity of electricity consumed, is aimed adjusting the product offer, sales channels and marketing communication to the expectations in the specific segment of clients.

The table below presents categories of TAURON Capital Group end clients, resulting from the segmentation used and the specific nature of their business.

Table no 17. Categories of end consumers of TAURON Capital Group

No.	Group of clients	Description of clients
1.	Strategic clients	Clients 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.

No.	Group of clients	Description of clients
2.	Business clients	Clients 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 clients – small and medium-sized enterprises	Clients dealing with sales, services, banking, catering and small entrepreneurs.
4.	Mass clients – households	Households.

The table below presents information concerning the quantity of electricity sold by companies of TAURON Capital Group, operating in the area of electricity sales to clients as well as the number of clients, divided into individual client segments, in 2016.

Table no 18. Quantity of electricity sold by the Sales Area and the number of clients in 2016

No.	Kind of clients	Quantity of Electricity sold (TWh)	Number of clients (thou.)
1.	Strategic clients	6.5	1
2.	Business clients	11.0	181
3.	Mass clients, including:	11.1	5,138
	households	*9.3*	*4,787*
4.	Sales to TAURON Dystrybucja to cover balancing differences	3.2	0.001
5.	Other (export, own needs)	0.1	
	Sales Segment	**31.9**	**5,320**

The process of the progressing liberalisation and the associated clients' rising awareness in the scope of mechanisms of energy market functioning is reflected in the level of loyalty in individual segments of purchasers. This situation results in activities in the scope of protection of own client base against the actions of the competition, through the introduction of loyal customer agreements. Clients from the business segment of TAURON Capital Group are most advanced in this process, where over 96% of the volume of the agreements concluded results from individually negotiated commercial terms.

In 2016, the sales offer of the TAURON Sprzedaż company to the business segment comprised two media – electricity and gas fuel. Due to clients' awareness in the scope of energy market mechanisms and the acquired skills of using those mechanisms, TAURON Sprzedaż focused its activities on the protection of the client base held. In particular, activities oriented towards client loyalty building were continued. It was recognised that particular attention would be paid to building of an offer meeting clients' expectations. Clients were offered a selection of a number of products taking into account their needs and the specific nature of electricity consumption, including ecological, exchange and technical products.

While expanding the offer in the developing gas fuel sales area, the *TAURON Gaz Giełda* (TAURON Gas Exchange) product was introduced, based on market prices determined in relation to quotations of TGE RTT indices. Moreover, for the purpose of intensification of electricity and gas contracting, the *TAURON Multipakiet* (TAURON Multipackage) product was introduced in June, which ensures simultaneous contracting of clients in the scope of both media during single business negotiations.

In 2016, the process of migration of mass segment clients (individual clients and small and medium-sized enterprises) from the tariff to the product area was continued. At the end of 2016, TAURON Capital Group sold energy to approximately 34% of clients in this segment under agreements with a guarantee of commercial terms and conditions in the specific period (loyalty agreements), and 66% of clients bought energy at tariff prices.

The key element of the commercial offer for mass clients in 2016 was the combined product called *Elektryk (Electrician),* based assistance functionality, used by over 663 thousand clients. Within products based on assistance, the product called *Serwisant* (Service provider) was also functioning and approximately 90 thousand clients used this offer. In the framework of the campaign *TAURON means more than electricity,* in 2016 TAURON Sprzedaż conducted sales of gas to mass market clients.

These products will also constitute the background of the offer in 2017. Changes introduced in the consumer law had a significant impact on the organisation of sales and service processes in 2015. All sales activities in 2016 were conducted with the intention to maintain the expected level of sales margins and build the potential for sales of other services and additional products in the subsequent years.

2.6.2. Supply sources – fuel

Coal

In 2016 the purchase of coal by TAURON for the needs of TAURON Wytwarzanie and TAURON Ciepło was continued, based on the multi-annual and annual agreements. In 2016, about 59.5% of the current demand of TAURON Capital Group for fuel required for generation of electricity and heat was satisfied by hard coal coming from own coal mines. The remaining part of the demand was covered from external sources, where Polska Grupa Górnicza sp. z o.o. had the highest share (about 30% of the demand).

Biomass

In order to secure the supply of fuel for the needs of electricity and heat generation by units using biomass as a fuel in the technological process, the Biomasa Grupa TAURON company acquired biomass under the concluded master agreements and orders for the purchase of biomass from domestic producers and suppliers. The master agreements and orders covered the purchase of biomass for the co-burning process and for the needs of dedicated units 100% supplied with biomass. In the period from 1 January to 31 December 2016 master agreements and orders Biomasa Grupa TAURON purchased the following quantities of biomass:

1) Co-burning process – 3.62 thousand Mg, including 2.16 thousand Mg of agro biomass, the remaining 1.46 thousand Mg constituting wood biomass.
2) For the needs of dedicated RES boilers – 535.93 thousand Mg, including 125.52 thousand Mg of agro biomass, the remaining 410.41 thousand Mg constituting wood biomass.

The Company conducted the resale of biomass purchased under master agreements to TAURON Wytwarzanie and TAURON Ciepło under agreements for biomass sales concluded between companies.

Gas

Fuel purchases – Gas

In 2015 TAURON started high-methane gas purchases to TAURON Wytwarzanie (to Elektrownia Stalowa Wola) and TAURON Ciepło (to Zespół Elektrociepłowni Bielsko-Biała EC1) through TAURON Sprzedaż company. The gas supplied was purchased under the complex agreement for gas fuel supply and the agreement with PGNiG. In addition, some part of gas came from purchases on TGE. The said gas was purchased by TAURON from ArcelorMittal Poland, Zdzieszowice Branch, under the multiannual agreement for the supply of coke-oven gas. The transmission of the coke-oven gas was conducted within the agreement for provision of transmission services of the coke-oven gas concluded with Polska Spółka Gazownictwa sp. z o.o. Oddział w Zabrzu, Zakład w Opolu Zabrze Branch, Plant in Opole.

Sales of gas to end clients

In 2016, TAURON Capital Group continued the development of high-methane gas sales to end clients (business and mass clients). Such sales took place through TAURON Sprzedaż and TAURON Czech Energy companies.

Securing of gas supplies to end clients was based on trading on European gas exchanges (including, to a considerable extent, on the gas market operated by the TGE), as well as based on OTC contracts.

2.7. Timeline

The figure below shows the timeline presenting selected events associated with the operations of TAURON Capital Group which took place in 2016.

Figure no. 47 Timeline

EVENTS IN TAURON CAPITAL GROUP IN 2016

JANUARY – FEBRUARY

- Changes in the composition of the TAURON Management Board.
- Commencement of effectiveness of the updated Sustainability Strategy.
- Synchronisation of the new heat unit at ZW Tychy TAURON Ciepło with the national power network.
- TAURON's declaration concerning the application of Best Practice of GPW Listed Companies 2016.
- Launching the project covering integration of Nowe Brzeszcze GT assets in the Mining Area.
- Rescinding of the agreement with Abener Energia S.A. – the general contractor of the CCTG unit in Stalowa Wola by EC Stalowa Wola.
- Launching the programme covering the reorganisation of service area in TAURON Capital Group.
- Issue of 22,500 shares with the total value of PLN 2,250,000,000.

MARCH – APRIL

- Publication of TAURON and TAURON Capital Group financial results for 2015.
- Adoption of the efficiency improvement programme in TAURON Group for 2016–2018.
- Holding Bondholders' Meeting for issued bonds series TPEA1119.
- Concluding agreements with TGE concerning reporting of transaction data.
- Commencement of the investment project comprising the reconstruction of ventilation headings and drilling of headings at the Andrzej VIII shaft, level 900 m at Nowe Brzeszcze GT.
- Commencement of the implementation of the investment project comprising the delivery of a brand-new high efficiency longwall complex, including the equipment for Nowe Brzeszcze GT.
- Adoption of a new Business Model of TAURON Group.
- Concluding the agreement by TAURON, PGE, Enea, Energa, PSE and Association of Private Employers of the Energy Sector concerning the rules of participation in the Tripartite Team for the Energy Sector.

MAY – JUNE

- Publication of TAURON and TAURON Capital Group financial results for 2016 Q1.
- Launching the programme comprising reorganisation of CUW in TAURON Obsługa Klienta.
- Launching the programme covering building of Customer-oriented organisation in TAURON Capital Group.
- Concluding a Letter of Intent by TAURON, the National Centre for Nuclear, Warsaw University of Technology, ENEA, ENERGA, PGE aimed at commencement of the cooperation oriented to conducting studies and analyses in the scope of development, promotion and dissemination of electromobility in Poland.
- Launching the TAURON PRO Programme.
- Holding the Ordinary GM of TAURON.
- Adopting the amendments to TAURON Articles of Association aimed at implementation of Best Practice of GPW Listed Companies 2016.
- Changes in the composition of the TAURON Supervisory Board.
- Launching the project aimed at centralisation of HR common services in TAURON Capital Group.

JULY – AUGUST

- Publication of TAURON and TAURON Capital Group financial results for the first half of 2016.
- Concluding the Agreement concerning suspending the implementation of the project to build CCGT unit in Elektrownia Blachownia Nowa by TAURON with KGHM and TAURON Wytwarzanie.
- Launching the investment programme at Nowe Brzeszcze GT.
- Commencement of the preparatory works at TAURON Ciepło under the project comprising liquidation of low emission sources on the area of Silesia-Dąbrowa Górnicza conurbation.
- Acquisition of TAURON Wytwarzanie Serwis shares by TAURON from TAURON Wytwarzanie.
- Establishment of the Polish National Foundation foundation, jointly with other founders.
- Commencement of TAURON activity in the scope of natural gas trade on the ICE exchange.

SEPTEMBER – OCTOBER

- Adoption of the TAURON Group's 2016–2025 Strategy.
- Adoption of the dividend policy for 2016–2025.
- Withdrawal from execution of project concerning the construction of the CCGT unit at Elektrownia Łagisza.
- Concluding the agreement by TAURON with Fitch Polska S.A. concerning determining of the rating for the issue of subordinated bonds.
- Establishment of the ElectroMobility Poland company jointly with PGE, ENEA and ENERGA.
- Concluding the investment agreement by TAURON, ENEA, ENERGA, PGE and ElectroMobility Poland regulating the rules of cooperation in order to implement a joint project.
- Granting the main award for *The Best Annual Report* to TAURON, for the third time, for the best annual report for 2015.
- Concluding the agreement concerning the conditions for further execution of the project on the "Construction of a CCGT Unit at Stalowa Wola".

NOVEMBER – DECEMBER

- Publication of TAURON and TAURON Capital Group financial results for 2016 Q3.
- Changes in the composition of the TAURON Management Board.
- Confirmation of the long-term foreign and local currency ratings of TAURON at "BBB" level, and the change of the outlook from negative to stable by the Fitch rating agency.
- Holding the Extraordinary GM of TAURON.
- Completion of the integration process of ZG Nowe Brzeszcze with TAURON Wydobycie.
- Concluding the programme agreement by TAURON with the European Investment Bank (EIB) concerning the hybrid financing, with the value of EUR 190 million in the form of bonds.
- Launching the project comprising co-burning of alternative fuel in generation units of TAURON Wytwarzanie and TAURON Dystrybucja companies.
- Establishment of the company Magenta Grupa TAURON.
- Changes in the composition of the TAURON Supervisory Board.

2.8. Important events and achievements of TAURON Capital Group significantly affecting its operations

The most important events significantly affecting the operations of TAURON Capital Group, which occurred in 2016, as well as until the day of drawing up this report are as follows:

Important corporate events in 2016

Changes in the personal composition of the Management Board

On 8 January 2016 the Supervisory Board dismissed Anna Striżyk – Vice-President of the Management Board for Economics and Finance, from the Management Board.

As of 29 January 2016, the Supervisory Board appointed Marek Wadowski as Vice-President of the Management Board for Economics and Finance.

On 14 November 2016, the Supervisory Board dismissed Remigiusz Nowakowski – the President of the Management Board from the Management Board.

As of 15 November 2016, the Supervisory Board appointed Filip Grzegorczyk as the President of the Management Board.

The Company informed of the changes in the personal composition of the Management Board in current reports: no. 2/2016 of 8 January 2016, no. 5/2016 of 29 January 2016 and no. 39/2016 of 14 November 2016.

Changes in the personal composition of the Supervisory Board

On 6 June 2016 the Supervisory Board Members, Maciej Koński and Renata Wiernik-Gizicka submitted their resignations from the function of Member of TAURON Polska Energia S.A. Supervisory Board.

On 8 June 2016 the Ordinary GM of the Company, acting pursuant to § 22 (1) of the Company Articles of Association, adopted the resolution on the appointment of Jacek Rawecki and Stefan Świątkowski to the Company Supervisory Board of fourth joint term of office.

On 14 November 2016 a Member of the Supervisory Board, Wojciech Myślecki submitted his resignation from the function of Member of TAURON Polska Energia S.A. Supervisory Board.

On 16 December 2016 the Minister of Energy, acting pursuant to § 23(1)(3) of the Company Articles of Association appointed Agnieszka Woźniak as a member of the Supervisory Board of TAURON Polska Energia S.A.

On 30 December 2016 the Minister of Energy, acting pursuant to § 23(1)(3) of the Company Articles of Association:

– dismissed Michał Czarnik and Anna Biesialska from the Supervisory Board of TAURON Polska Energia S.A.,
– appointed Jan Płudowski and Stanisław Bortkiewicz to the Supervisory Board of TAURON Polska Energia S.A.

The Company informed of the aforementioned events in current reports no. 23/2016 of 6 June 2016, no. 28/2016 of 8 June 2016, no. 40/2016 of 14 November 2016, no. 47/2016 of 16 December 2016 and no. 50/2016 of 30 December 2016.

Management Board's recommendation on dividend payout from the reserve capital

On 10 March 2016 the Management Board of the Company adopted the resolution to recommend to the Ordinary GM the allocation of the Company reserve capital in the part covering sums carried forward from previous years' profits to pay the amount of PLN 175,254,939.40 as a dividend to the Company shareholders, which means that the dividend per share will amount to PLN 0.10. The Management Board decided to submit the recommendation to the Company Ordinary GM determining:

– dividend record day on the 90th (ninetieth) day counting from the day of adoption of the GM resolution concerning the use of the Company reserve capital,
– dividend payment day on the 14th (fourteenth) business day counting from the dividend record day.

The recommendation of the Management Board concerning the level of the dividend to be paid to Company shareholders shows the intention to continue the existing practice of dividend payment by the Company and takes into account in particular the financial result for 2015 as well as the level of reserve capital established from profits for previous years, the investment programme of TAURON Capital Group under implementation and the covenants defined in financing agreements. The proposed level of the dividend would allow the Company to maintain the debt ratio at a safe level.

On 17 March 2016 the Supervisory Board of the Company approved the aforementioned recommendation of the Management Board concerning the dividend.

The Ordinary GM of the Company convened on 8 June 2016 did not adopt the resolution concerning the use of the Company reserve capital by allocation of its part for payment of the dividend to shareholders of the Company.

The Company informed of the aforementioned events in current reports: no. 14/2016 of 10 March 2016, no. 15/2016 of 17 March 2016 and no. 24/2016 of 8 June 2016.

Shareholder's request to convene the General Meeting of the Company and include particular items on the agenda

On 30 March 2016, KGHM – a shareholder representing 10.39% of the Company share capital, submitted a request to convene the GM of the Company and to include adoption of a resolution to change the composition of the Company Supervisory Board on the agenda. In the rationale KGHM stressed that convening the GM would enable KGHM, as the Company shareholder, to present a motion to introduce a change in the composition of the Company Supervisory Board. At the same time, the Company Management Board informed that the General Meeting would be convened in line with applicable legal regulations and relevant information about convening the meeting and its agenda would be announced in a separate report and published on the Company website.

The Company informed of the Shareholder's request in the current report no. 17/2016 of 30 March 2016.

Decisions of the Ordinary General Meeting of TAURON

On 8 June 2016 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 2015, Financial statements of TAURON and the Report of the Management Board on the operations of the Company for the financial year 2015, covering of net loss for the financial year 2015 from the reserve capital, acknowledgement of the fulfilment of duties by members of the Company Management Board and Supervisory Board, amendments to the Company Articles of Association, amendment to the By-laws of the General Meeting of the Company, determining the number of members of the Company Supervisory Board, appointment of members of the Supervisory Board.

It was decided to cover the net loss of the Company for the financial year 2015 in the amount of PLN 3,453,908,315.26 (say: three billion four hundred fifty three million nine hundred eight thousand three hundred fifteen and 26/100) from the Company reserve capital.

The Company informed of convening of the GM and on the provisions of draft resolutions in current reports no. 19/2016 and no. 20/2016 of 12 April 2016. The Company informed of decisions of the GM concerning: covering of net loss, adopted resolutions, specification of shareholders holding at least 5% of votes at the GM, amendments to the Company Articles of Association and appointment of Supervisory Board members, in current reports: no. 24/2016, no. 25/2016, no. 26/2016, no. 27/2016 and no. 28/2016 of 8 June 2016.

Amendments to Articles of Association of TAURON Polska Energia S.A.

On 12 April 2016 the Management Board of the Company publicly informed of its intention to amend the Company Articles of Association, thus in the agenda of the Ordinary General Meeting of the Company including of an item concerning amendments to the Articles of Association of TAURON Polska Energia S.A. has been planned. The draft resolution including rationale containing the proposed amendments to the Company Articles of Association was published in the current report concerning convening of the Ordinary GM. It should be mentioned that on 8 March 2016 the Supervisory Board of the Company issued positive opinion concerning the motion of the Management Board to the GM concerning the amendment to the Company Articles of Association.

On 8 June 2016 the Ordinary GM of the Company adopted the resolution on the amendment to the Company Articles of Association.

On 30 June 2016 the District Court for Katowice-Wschód, 8th Commercial Department of the National Court Register issued the decision on entry of the amendments to the Company Articles of Association, adopted by resolution no. 44 of the Company Ordinary GM of 8 June 2016 concerning the amendments to the Company Articles of Association to the register of entrepreneurs of the National Court Register.

On 26 July 2016 the Supervisory Board of TAURON Polska Energia S.A. acting pursuant to § 20 section 1 item 13 of the Company Articles of Association adopted a uniform text of the Articles of Association of TAURON Polska Energia S.A. that includes the amendment to the Articles of Association entered by the District Court for Katowice-Wschód in Katowice, 8th Commercial Division to the National Court Register.

Introduction of the amendments to the Company Articles of Association was aimed at implementing the recommendations and detailed rules contained in "*Best Practice of GPW Listed Companies 2016*" to be applied in the Company, which will facilitate maintaining good relations with investors and provide an effective tool supporting the respect of shareholders' rights. Moreover, the said implementation will have a positive impact on development of TAURON relations with its market environment.

In the scope of the amendments to the Company Articles of Association, changes of streamlining and editorial nature were also taken into consideration, including, inter alia, deleting in Section IX. "Transitional provisions" of the wording applicable until the day of filing of the motion by TAURON for admission of at least one Company share to trading in the regulated market, which had taken place in 2010.

The Company informed of the aforementioned events in the current reports no. 18/2016 of 12 April 2016, no. 27/2016 of 08 June 2016, no. 29/2016 of 01 July 2016 and 31/2016 of 26 July 2016.

Shareholder's request to convene the Extraordinary General Meeting of the Company and include particular items on the agenda

On 4 November 2016 TAURON received a request in electronic form, from the Minister of Energy exercising the rights of the State Treasury as the shareholder representing 30.06% of the Company share capital, to convene the Extraordinary GM of the Company and include the following items in the agenda of the meeting:

1. Adoption of the resolution concerning the principles for determining remuneration for members of the management board of TAURON Polska Energia S.A. with its seat in Katowice.
2. Adoption of the resolution concerning the principles for determining remuneration for members of the supervisory board of TAURON Polska Energia S.A. with its seat in Katowice.

In the rationale it was indicated that the principles for determining remuneration of members of management boards in companies where the State Treasury is a shareholder are regulated by the provisions of the *Act of 9 June 2016 concerning the principles for determining the remuneration of individuals managing selected companies.* The Minister of Energy, exercising the duty defined in Article 2(1) and Article 2(2)(1) of the above mentioned act requests the Company GM to adopt resolutions concerning the principles for determining remuneration for members of the managing body and the supervisory body.

The Company informed of the Shareholder's request in the current report no. 38/2016 of 4 November 2016.

Extraordinary General Meeting of TAURON Polska Energia S.A.

On 18 November 2016, the Management Board of TAURON, acting pursuant to Article 398, Article 399 § 1 and Article 402[1] of the KSH and § 30(1) of the Company Articles of Association, convened the Extraordinary GM of the Company for 15 December 2016. and published the draft resolutions received from the Minister of Energy.

On 15 December 2016 the Management Board of the Company provided the text of resolutions adopted on that day by the Extraordinary GM of the Company, including the results of voting. At the same time, the Company informed that the GM did not withdraw from discussing any of the items on the agenda and no objections were raised to the report of the GM by any of the shareholders.

Information concerning the aforementioned events was included in current reports: no. 43/2016 and 44/2016 of 18 November 2016 and no. 46/2016 of 15 December 2016.

Important business events in 2016

Settlement of the agreement with Kompania Węglowa

On 19 January 2016 the settlement of the agreement with Kompania Węglowa was carried out, whose signing was reported by the Company in the current report no 7/2013 of 1 March 2013, and whose subject was the purchase of hard coal by the TAURON. The Agreement was concluded for a period of three years from 1 January 2013 to 31 December 2015 and its estimated net value determined as at the day of concluding of the agreement amounted to PLN 2.4 billion net.

Pursuant to the performed settlement, the value of the turnover accomplished under the agreement amounted to PLN 2.014 billion net, i.e. approximately 84% of the net value of the agreement estimated initially and approximately 7% less than equivalent of 10% of Company equity used as the threshold value for material agreements as at the day of submission of the report.

The Company informed of the aforementioned event in the current report no. 4/2016 of 19 January 2016.

Convening Bondholders' Meeting of bonds series TPEA1119 and agreements signed with some Bondholders

The Management Board of TAURON, acting pursuant to the *By-laws of Bondholders' Meeting* constituting the attachment to the Terms and Conditions of the issue of bonds series TPEA1119, designated by the Central Securities Depository of Poland with the code PLTAURN00037 and listed in the Alternative Trading System on the Catalyst market organised by BondSpot S.A., with maturity falling on 4 November 2019, convened, on their own initiative, the Meeting of Bondholders to take place on 3 March 2016. The subject of the Bondholders' Meeting will be adoption of the resolution on the amendments to terms and conditions of the bonds' issue through amending of the definition of "Financial Debt" included in item 1.1 of the Terms and Conditions of the Bonds' Issue and the amendment to the provisions of Grounds for Early Redemption contained in item 9.1(e) of the Terms and Conditions of the Bonds' Issue.

The detailed description of the amendments to the Terms and Conditions of the Bonds' Issue is contained in the current report no. 8/2016 of 10 February 2016.

On 3 March 2016, Bondholders representing 91.44% of votes appeared at the Bondholders' Meeting, accordingly, the Bondholders' Meeting was unable to adopt the resolution concerning the amendments to the terms and conditions of the bond issue. Considering the foregoing, TAURON, as the Issuer, proposed Bondholders who attended the Bondholders' Meeting to sign, against agreed remuneration, bilateral agreements under which Bondholders who sign these agreements commit irrevocably with respect to the Issuer, to take part in every bondholders' meeting concerning the bonds during the effective term of a given agreement and vote at every bondholders meeting, with all bonds, against the resolution allowing bondholders to submit to the Issuer a request for early redemption in the event of a potential breach, i.e. if the debt ratio defined in the terms and conditions of the bond issue exceeds 3.0x but does not exceed 3.5x, taking into consideration the new definition of financial debt and the principles for calculation of the financial ratio included in the agreement.

Detailed information was published in the current report no. 12/2016 of 3 March 2016.

On 22 March 2016 the Management Board informed that in execution of the proposal presented to the Bondholders at that meeting, until 21 March 2016 agreements were signed with Bondholders representing 6,937 Bonds of TPEA1119 series which constitute 39.64% of the total nominal value of all TPEA1119 series Bonds and entitles to exercising of 39.64% of votes resulting from all Bonds.

Under the concluded agreements, TAURON will pay each Bondholder who is a party to the agreement a remuneration in the amount of 0.20% per year of the total nominal value of the Bonds held by a given Bondholder that are the subject of such agreement.

According to the by-laws of the Bondholders' meeting constituting an annex to Terms and Conditions of TPEA1119 Bonds Issue, to adopt resolution of the Bondholders' meeting, presence of Bondholders representing at least 50% of votes is required. Resolutions are passed with 66 and 2/3 percent of votes of Bondholders present at the meeting. TPEA1119 series bonds were issued on 4 November 2014 in the amount of 17,500 pieces, as bearer, uncollateralized, coupon bonds with floating interest rate and nominal value of PLN 100,000 each. The Bonds are dematerialized at the securities depository run by KDPW S.A., assigned ISIN code: PLTAURN00037 and traded in the Alternative Trading System on the Catalyst market organised by BondSpot S.A. The maturity date of the Bonds shall fall on 4 November 2019.

Detailed information was included in the current report no. 16/2016 of 22 March 2016.

Information about planned write-off of impaired generation assets of the Generation Segment in financial statements for 2015

On 15 February 2016, following the completion of main works related to impairment tests on assets, in line with the requirements of the International Accounting Standard 36, the Management Board of TAURON publicly announced information on the expected impact of non-cash one-off event in the form of a write-off of unprofitable generation units in the Generation Segment. The Generation Segment comprises companies generating electricity and heat from conventional and renewable sources.

For testing purposes, the recoverable amount has been determined based on analysis of discounted cash flow generated by individual cash-generating centres. Key business assumptions affecting the evaluation of the recoverable amount included the adopted curves of electricity and fuel prices, CO_2 emission limits for electricity generation, tariff revenue of heat companies and maintenance of generation capacity of existing fixed assets as a result of executing capacity replacement investments.

The reason behind the write-offs lies primarily in market conditions that have been unfavourable for electricity generators and the resulting application of more conservative forecasts of electricity prices and reduced generation volumes in future.

To partially set off the impact of unfavourable market conditions and improve the situation of the TAURON Capital Group over a longer-term perspective, the Company Management Board has launched works on the update of *Corporate Strategy of TAURON Group for 2014–2017 with an outlook until 2023*. Within that process a review of the investment portfolio has been initiated to verify investment projects. The Company also finalised works on the new Effectiveness Improvement Programme for 2016–2018 which should generate further savings. In addition, achievement of synergies inside the Group was planned through simplification of the management model. The Company indicated that market trends were dominating in terms of development of long-term perspective for planning electricity generation profitability, which could have led to the necessity to apply further write-offs if the unfavourable trends persisted.

In relation to the consolidated financial statements of TAURON Capital Group for the financial year ended on 31 December 2015, the conducted tests have indicated that it was necessary to write-off major part of the TAURON Capital Group's generation assets in the electricity and heat generation segment due to partial or full impairment – including generation units of various capacities (in particular, 200 MW and 150 MW), biomass-fired units and cogeneration units. The total value of estimated write-offs resulting from impairment of tangible and intangible assets and goodwill in the Generation segment, charging prime costs, amounts to PLN 3,564 million and their impact on net result amounts to PLN 2,916 million. The write-offs will have no impact on EBITDA understood by TAURON Capital Group as EBIT increased by depreciation and write-offs for non-financial assets.

In relation to separate financial statements of TAURON for the financial year ended on 31 December 2015 the conducted test indicated that it was necessary to write-off the impairment of shares in TAURON Wytwarzanie and TAURON Ciepło in the total amount of PLN 4,931 million. The expected impact of those write-downs on the net result in the separate statement amounts to PLN 4,931 million.

The Company reserves that the values presented above represent estimated values and may be subject to change. The final results of tests and amounts of impairment write-offs were presented in financial statements of TAURON and TAURON Capital Group for 2015, published on 9 March 2016.

Detailed information concerning the aforementioned issue is included in the current report No. 9/2016 of 15 February 2016.

Exceeding of the 10% equity threshold in trade turnover between companies of TAURON Capital Group and companies of PSE Group

On 29 February 2016, the Company received documents concerning the mutual provision of services to companies of TAURON Capital Group enabling the settlement with companies of PSE Group, in reference to current reports no. 1/2012 of 5 January 2012, no. 37/2012 of 7 November 2012, no. 42/2013 of 15 October 2013, no. 30/2014 of 8 July 20144 and current report no. 11/2015 of 10 April 2015, regarding trade turnover between companies of TAURON Capital Group and PSE. In accordance with the aforementioned documents, as of 10 April 2015, i.e. as of the day of submission of the current report no. 11/2015, the net trade turnover generated between companies of TAURON Capital Group and companies of PSE Group amounted to approximately PLN 2,180 million (including approximately PLN 1,500 million of cost items for TAURON Capital Group companies, and about PLN 680 million of revenue items), accordingly, the value of turnover exceeded 10% of the Company equity.

The turnover of the highest value, i.e. approximately PLN 1,400 million net, was generated under the agreement of 16 December 2013, concluded between TAURON Dystrybucja and PSE. The subject of the aforementioned agreement, concluded for an indefinite period of time, is the provision of transmission services by PSE, understood as the transport of electricity via the transmission grid. Its estimated value over a period of 5 years following its conclusion, is about PLN 7,478 million. The services are cleared in accordance with the rules and rates approved by the President of the ERO, defined in the tariff, and taking into account the provisions of the Instruction for Transmission System Operation and Maintenance. The above mentioned agreement does not stipulate any liquidated damages and it does not contain any conditions precedent or terminating conditions.

The Company informed of the aforementioned event in the current report no. 10/2016 of 29 February 2016.

Purchasing of own bonds by TAURON and issue of bonds under the bond issue programme

On 29 February 2016 the Company purchased, with the intention to redeem, 22,500 bonds (“Bought Back Bonds”) out of 30,000 tranche C bonds issued on 12 December 2011 under the bond issue programme of 16 December 2010. TAURON informed of the issue of the said bonds in the current report no. 60/2011. The early buyback does not cover the remaining 7,500 pcs of Tranche C Bonds which, according to the terms and conditions of the bond issue, were redeemed on 12 December 2016.

The Bonds bought back on 29 February 2016 were acquired at the issue price of PLN 100,000, thus the total nominal value of bought back and redeemed bonds amounts to PLN 2,250,000,000. The amount of buy-back was increased by interest due from the first day of the last interest period preceding the buy-back until the day of that buy-back (excluding that day). The purchase with the intention to redeem was executed based on bilateral agreements concluded between TAURON and bondholders of Tranche C Bonds and the main purpose of the transaction is to extend the maturity of debt incurred by the Company in the form of bonds. Funds to refinance the Bought Back Bonds were obtained by TAURON under a new bond issue programme (TAURON informed of signing of the agreement for the new bond issue program in the current report No. 49/2015 of 24 November 2015), under which, on 29 February 2016 the Company issued 22,500 bonds with the total nominal value of PLN 2,250,000,000 (“Bonds”) with the maturity date on 29 December 2020. The Bonds were issued in PLN as uncollateralized, dematerialized, coupon securities and taken up at the issue price equal to the nominal value amounting to PLN 100,000. The interest rate on bonds was determined based on WIBOR 6M rate increased by a fixed margin. The Bonds will be redeemed at the issue price on the maturity date and interest will be paid in arrears at the end of each interest period to bondholders who hold the Bonds on the record date. Interest payable under the Bonds will be paid in semi-annual periods (subject to the first, four-month period). On account of Bond holding, the Bondholders will be entitled to cash payments only. The Bonds have been taken up by financial institutions that are parties to the bond issue programme, i.e. Bank BGŻ BNP Paribas S.A., Bank Handlowy w Warszawie S.A., Bank of Tokyo-Mitsubishi UFJ (the Netherlands) BV, Bank of Tokyo-Mitsubishi UFJ (Polska) S.A., Bank Zachodni WBK S.A., CaixaBank S.A. (Spółka Akcyjna) Oddział w Polsce, Industrial and Commercial Bank of China (Europe) S.A. Oddział w Polsce, ING Bank Śląski S.A., mBank S.A. (mBank) and PKO BP S.A. (PKO BP). As a result of the transaction TAURON improved its debt structure by moving the maturity date of the bonds in the amount referred to above by five years, which has a positive impact on the Issuer’s financial and economic standing in view of investment expenditures planned for the coming years. As of the day of bond issue, the Management Board of the Company does not recognise any threats in relation to complying with the commitments resulting from the Bonds. The Company informed that as of 31 December 2015 the value of its liabilities amounted to PLN 9.7 billion. At the same time due to, inter alia, execution of its investment programme, the Issuer anticipated that the debt level may increase during the period until the maturity date of the Bonds.

The Company informed of the aforementioned event in the current report no. 11/2016 of 29 February 2016.

Adoption of the efficiency improvement programme in TAURON Group for 2016–2018

On 9 March 2016 the Management Board adopted the *Efficiency Improvement Programme in TAURON Group for the years 2016–2018*.

The Programme was drafted with account being taken of current market conditions and the need to keep financial standing of the Company stable. Proposals of initiatives were developed whose implementation will bring efficiency improvement at a level of approximately PLN 1.3 billion in the years 2016–2018 (cumulative effect of the Programme over three years). Execution of the Programme will allow to increase of EBITDA of TAURON Capital Group by approximately PLN 400 million in 2018 (sustainable, recurring effect at this level in subsequent years). TAURON Capital Group expects to improve its operational efficiency in most areas – the largest share falling in Distribution and Generation Areas.

Information concerning the Efficiency Improvement Programme is presented in item 1.4.5. hereof.

The Company informed of the adoption of the Programme in the current report no. 13/2016 of 9 March 2016.

Information about planned recognition of a write-off of impaired generation assets of the Generation Segment in financial statements for the 1st half of 2016

On 26 July 2016, following the completion of main works related to impairment tests on assets, in line with the requirements of the International Accounting Standard 36, Impairment of Assets, the Management Board of TAURON publicly announced information on the expected impact of non-cash one-off event in the form of a write-off of the carrying amount of generation units in the Generation Segment. The Generation Segment comprises companies generating electricity and heat from conventional and renewable sources.

The reason behind the write-offs lies primarily in changes in market environment that have been unfavourable for electricity generators and must have been taken into account for test purposes, including the decline in prices of certificates of electricity origin from renewable sources and new regulations in the RES segment. The value of the write-off related to conventional sources results from continued unfavourable trend in electricity prices and the expected higher supply of electricity from sources competitive to domestic coal-fired plants. At the same time, in the assumptions to the forecasts account has been taken of estimated impact of introduction of the so-called capacity market. The abovementioned market conditions have an impact on decrease of cash flows that determine the recoverable amount of individual units on the one hand, and lead to reversal of impairment write-offs made previously for heat and electricity generation units on the other.

In reference to consolidated financial statements of TAURON Capital Group for the 1st half of 2016 ended on 30 June 2016 the conducted tests indicated that it was necessary to write-off the impairment of tangible and intangible assets and company value as well as to reverse the write-off made previously in the Generation Segment. Total net amount of write-offs (i.e. the excess of write-offs over reversals) amounts to approx. PLN 0.7 billion. This amount includes impairment write-offs related to wind farms at a level of approx. PLN 0.5 billion and impairment write-offs related to generation assets in the area of electricity and heat generation at a level of approx. PLN 0.2 billion net. The total estimated impact on reduction of the financial net result will amount to is approx. PLN 0.6 billion. The value of the abovementioned write-offs will have no impact on EBITDA understood by the Group as EBIT increased by amortisation, depreciation and write-offs for non-financial assets.

In reference to standalone financial statements of TAURON for the 1st half of 2016 ended on 30 June 2016 the conducted tests indicated that it was necessary to recognise the write-offs due to impairment of shares in TAURON Wytwarzanie and TAURON Ekoenergia companies as well as the reversal of the write-off previously made for the company TAURON Ciepło in the total net amount of approx. PLN 1.0 billion. Expected estimated impact of the above write-offs on the net result presented in standalone financial statements is approx. PLN 1.0 billion.

The Company reserves that the values presented above represent estimated values and may be subject to change. The final results of tests and the level of impairment write-offs due to the loss of the carrying amount of assets were presented in the financial statements of TAURON and TAURON Capital Group for the 1st half of 2016, published on 17 August 2016.

Detailed information concerning the aforementioned issue is included in the current report No. 30/2016 of 26 July 2016.

Estimated consolidated financial figures for the first half of 2016

On 29 July 2016 the Management Board of the Company publicly presented selected estimated consolidated financial data of TAURON Polska Energia Capital Group for the 1st half of 2016.

Detailed information concerning the aforementioned financial data is included in the current report No. 33/2016 of 29 July 2016.

Adoption of the TAURON Group's 2016–2025 Strategy

On 2 September 2016 the Management Board of the Company adopted and the Supervisory Board issued a positive opinion on the document entitled *TAURON Group's 2016–2025 Strategy* (the Strategy). The Strategy is a response to the challenges stemming from the current and forecast situation on the market and in the power sector. Within the process of the Strategy preparation an in-depth analysis of the macroeconomic, market and regulatory environment as well as sector development forecasts was performed, translating them into opportunities and risks for TAURON Capital Group within the perspective of the nearest ten years. The capacity of TAURON Capital Group to finance current and planned investment projects was analysed to the extent enabling their implementation from funds generated by operating activity and by acquisition of debt financing. The aforementioned analyses and market trends provided basis for verification of market, macroeconomic assumptions and the investment plan.

The Strategy presents the 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 relations. The adopted mission and vision reflect new management philosophy and are in line with the customer-oriented growth concept.

The description of the *TAURON Group's 2016–2025 Strategy* is included in subsection 1.4 hereof.

Detailed information concerning the aforementioned event was published in the current report no. 34/2016 of 2 September 2016.

Adoption of the 2016–2025 dividend policy

On 2 September 2016 the Management Board of the Company informed that as part of the Strategy adopted by the Company, the Company adopted the 2016–2025 dividend policy.

Detailed information concerning the 2016–2025 dividend policy is included in subsection 5.2 hereof.

Information of the aforementioned event was published in the current report no. 35/2016 of 2 September 2016.

Publication of estimated financial results of TAURON Polska Energia Group for Q3 2016

On 28 October 2016 TAURON published selected estimated consolidated financial figures of TAURON Polska Energia Capital Group, cumulatively for the period of Q1–Q3 2016 and for Q3 2016.

The publication of the interim report for the 3rd quarter 2016 took place on 9 November 2016.

Detailed information on estimated financial results was published in the current report no. 37/2016 of 28 October 2016.

Confirmation of ratings and revision of the outlook for TAURON from negative to stable

On 14 November 2016 Fitch rating agency affirmed the long-term foreign and local currency ratings at "BBB" and revised the outlook from negative to stable. According to Fitch the outlook revision reflects measures undertaken by the Company to improve its financial profile over the next five years, including a reduction of long-term planned capex and management's plan of no dividends until 2019. The stable outlook also reflects the reduced risk of covenant breach and improved medium-term liquidity of the Company as compared to 4Q 2015 when the outlook was revised to negative. The full list of ratings includes:

- long-term foreign and local currency rating at "BBB"; outlook revised from negative to stable,
- short-term foreign and local currency IDRs affirmed at "F3",
- national long-term rating affirmed at "A+(pol)"; outlook revised to stable from negative,
- national senior unsecured rating affirmed at "A(pol)".

Information on the aforementioned event was published in the current report no. 41/2016 of 14 November 2016.

Other important events in 2016

Appointment of certified auditor

On 10 May 2016, the Supervisory Board of the Company, acting pursuant to § 20 section 1 item 6) of the Articles of Association appointed Deloitte Polska Spółka z ograniczoną odpowiedzialnością Spółka komandytowa with its registered office in Warsaw as the entity authorised to examine standalone and consolidated financial statements of the Company for the year 2016.

Subsequently, on 19 May 2016 the Supervisory Board of the Company appointed the same company as the entity authorised to review standalone and consolidated semi-annual financial statements and consolidated financial statements of the Company for the period ending on 30 June 2016.

To date, services provided by Deloitte for the Company included examination of standalone and consolidated financial statements for the years: 2007, 2013, 2014 and 2015 as well as review of standalone and consolidated semi-annual financial statements and consolidated financial statements for the periods ending on 30 June in the years: 2013, 2014 and 2015. TAURON also used advisory and training services provided the scope that in no way limited the impartiality and independence of the auditor.

The certified auditor was appointed following a single-source non-public procurement procedure. The agreement with Deloitte Polska Spółka z ograniczoną odpowiedzialnością Spółka komandytowa was concluded by the Management Board of the Company for a period necessary to perform the contracted services.

The Company informed of the aforementioned events in current reports: no. 21/2016 of 10 May 2016 and no. 22/2016 of 20 May 2016.

Return of public aid granted for covering of KWK Brzeszcze losses

In the 1st quarter of 2016, Nowe Brzeszcze GT returned public aid, including interest, in the total amount of PLN 131,076,718.99. The first instalment of the returned public aid in the amount of PLN 5,083,644.50 was transferred on 15 January 2016 whereas the second instalment in the amount of 125,993,074.49 – on 31 March 2016.

The return of public aid resulted from the provisions of the agreement for the purchase of a part of KWK Brzeszcze assets from Spółka Restrukturyzacji Kopalń S.A. of 31 December 2015 (current report no. 63/2015), containing, in particular, the obligation of the buyer (i.e. Nowe Brzeszcze GT) to return public aid granted to Spółka Restrukturyzacji Kopalń S.A. to cover current production losses of KWK Brzeszcze Branch.

Obtaining free carbon dioxide emission allowances

In accordance with Directive 2003/87/EC of the European Parliament and the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC, TAURON Capital Group is entitled to receive free emission allowances pursuant to Article 10c of the aforementioned Directive ("derogation allowances"). In April 2016 accounts of TAURON Capital Group installations were supplied with free allowances due to electricity generation for 2015. At the same time, in February 2016 all installations belonging to companies of TAURON Capital Group received allocations of free emission allowances for heat production for 2016, pursuant to Article 10a of Directive 2003/87/EC. In order to acquire free allowances due to derogation for the consecutive year, on 29 September 2016 TAURON Capital Group submitted material and financial reports on the implementation of investment tasks included in the KPIs for the period from 1 July 2015 to 30 June 2016. The expected allocation of allowances for 2016 should be transferred to accounts of the installations at the beginning of 2017. At present, taking into consideration the current level of electricity and heat production as well as the level of CO_2 contracting, generation companies of TAURON Capital Group hold a sufficient quantity of emission allowances to cover the demand for allowances in 2016.

Completion of the construction of new generation capacity in co-generation at a level of 50 MW_e and 86 MW_t at ZW Tychy

On 20 June 2016 the co-generation unit was commissioned at ZW Tychy, with the electrical capacity of 59.2 MW_e in condensation performance (50.8 MW_e in heating performance) and heat capacity of 86 MW_t; the conversion of the biomass boiler and development of the water coal-fired WR boiler with the capacity of 40 MW_t was completed, including the management associated with the above mentioned units. The commencement of the project was driven by the necessity to adjust the existing source to more stringent emission standards applicable as of January 2016.

The implementation of the project enabled maintaining of the status of ZW Tychy as the basic heat generator for consumers located on the territory of Tychy city and the Katowice Special Economic Zone – Tychy sub-area.

Extension of activity on Intercontinental Exchange

On 4 July 2016 TAURON extended its activity in the scope of trading in natural gas on the largest exchange of gas and oil in Europe – Intercontinental Exchange, in the scope of UK Natural Gas Futures product.

The former activity on Intercontinental Exchange comprised the following petroleum products: LS Gas Oil, Brent Crude, WTI Crude, Heating Oil Gas. Entering the market in the United Kingdom (through the National Balancing Point – NBP hub) provides the Company with access to the most liquid natural gas market on the continent which enables it to conduct proprietary trading and increase volumes and revenues due to gas trading. The access to new hubs and exchanges is a consequence of activity aiming at enhancing the competence by TAURON in the scope of operations on the gas market and gaining access to new sources of this fuel.

Important events after 31 December 2016

Information on the intention to recognise write-offs due to the loss in the carrying amount of generation units of the Generation segment in the financial statements as at 31 December 2016

Due to the completion of major works associated with impairment tests of assets as at 31 December 2016, on 14 February 2017 the Management Board of TAURON decided to recognise write-offs due to the loss in the carrying amount of generation units of the Generation Segment. The Generation Segment comprises companies generating electricity and heat from conventional and renewable sources. The requirement to recognise those events in financial results arises mainly from the following changes in the market environment taken into account in the tests: 1) regulations in the area of renewable energy sources, 2) decline in prices of certificates of origin for energy from renewable sources, 3) continuing unfavourable market conditions (in terms of profitability of coal-based power industry).

The write-offs recognised as at 31 December 2016 in the consolidated financial statements of TAURON for the year ended on 31 December 2016 (in relation to companies of the Generation Segment): 1) the value of created write-offs related to wind farms: approx. PLN 281 million, 2) the value of reversed net write-offs (i.e. the surplus of reversed write-offs against their value at creation) related to the generation assets in the area of electricity and heat generation: approx. PLN 204 million, 3) the total net write-off amount (i.e. the excess of created write-offs over their value at reversal): approx. PLN 77 million, 4) the total estimated impact on charging the net financial result: approx. PLN 62 million.

The write-offs recognised as at 31 December 2016 in the separate financial statements of TAURON for the year ended on 31 December 2016 (in relation to companies of the Generation Segment): 1) the value of created write-offs due to the loss in the carrying amount of stocks and shares held and the intragroup loan: approx. PLN 613 million, 2) the total estimated impact on charging the net financial result: approx. PLN 613 million.

The value of the aforementioned write-offs will not affect the EBITDA result, understood by the Company as EBIT increased by depreciation and write-offs for non-financial assets.

The Company reserves that the values presented above represent estimated values and may be subject to change. The final results of the tests and amounts of impairment write-offs due to the loss in the carrying amount of assets will be presented in the financial statements of TAURON Polska Energia S.A. for 2016, to be published on 15 March 2017.

The above information was published in the current report no. 3/2017 of 14 February 2017.

Estimated financial figures of TAURON Polska Energia Group for Q3 2016

On 14 February 2017 TAURON published selected estimated consolidated financial data and operating data of TAURON Polska Energia S.A. Capital Group for 2016 and 2016 Q4, taking into account results of impairment tests of assets, of which the Company informed in the current report no. 3/2017 of 14 February 2017.

Detailed information on estimated financial results was published in the current report no. 4/2017 of 14 February 2017.

Termination of long-term contracts for the purchase of property rights by a subsidiary

On 28 February 2017 TAURON Sprzedaż submitted declarations on the termination of long-term contracts for the purchase of property rights arising from certificates of origin of energy from renewable sources (so-called green certificates, hereinafter referred to as "PMOZE") by TAURON Sprzedaż. The following customers, comprising installations generating electricity from renewable sources are parties to the contracts concluded in 2008:

1) in.ventus spółka z ograniczoną odpowiedzialnością EW Dobrzyń spółka komandytowa,
2) in.ventus spółka z ograniczoną odpowiedzialnością Ino 1 spółka komandytowa,
3) in.ventus spółka z ograniczoną odpowiedzialnością EW Gołdap spółka komandytowa.

The Contracts shall be terminated with immediate effect due to the failure of the parties to reach an agreement under contractual negotiations in accordance with the procedure envisaged under the Contracts. As a result of termination of the Contracts TAURON Sprzedaż will avoid a loss constituting a difference between contractual prices and the market price of "green" certificates. The estimated value of the aforementioned loss due to continued execution of the Contracts until the end of their originally assumed term (i.e. by 2023) – considering the current market prices of green certificates – shall amount to approximately PLN 343 million net. The total value of contractual liabilities of TAURON Sprzedaż estimated for the period 2017–2023 shall amount to approximately PLN 417 million net.

The above value was calculated according to the price formulas adopted in the Contracts for the period from the day of drawing up this report until the end of their originally assumed effective term (i.e. by 2023).

The amendments to legal regulations which entered into force after the day of concluding the aforementioned Contracts, providing basis for the notice of renegotiation:

1) repealing of the *Act of 8 January 2010 on the amendment to the Act on Energy Law and on the amendment to certain other acts of law*, effective as of 31 December 2012 (Journal of Laws of 2010, no. 21 item 104), *regulation of the Minister of Economy of 14 August 2008 concerning the detailed scope of obligations to acquire certificates of origin and present them for redemption, to pay the substitution fee, to purchase electricity and heat generated in renewable energy sources and the obligation to confirm data related to quantities of electricity generated in a renewable energy source* (Journal of Laws of 2008, no. 156 item 969) (the "MG Regulation of 2008"), as a result of entry into force of the *regulation of the Minister of Economy of 18 October 2012 concerning the detailed scope of the obligations to acquire certificates of origin and present them for redemption, to pay the substitution fee, to purchase electricity and heat generated in renewable energy sources and the obligation to confirm data related to quantities of electricity generated in a renewable energy source* (Journal of Laws of 2012 item 1229) (the "MG Regulation of 2012"),
2) entry into force of the *Act of 20 February 2015 on renewable energy sources* ("RES Act") and the subsequent amendments to the provisions of the RES Act, including in particular, the *Act of 22 June 2016 on the amendment to the Act on renewable energy sources and certain other acts of law* (Journal of Laws of 2016, item 925),
3) entry into force of the *Regulation of the Minister of Energy of 17 October 2016 concerning the change of the qualitative share of the total electricity arising from redeemed certificates of origin confirming generation of electricity from renewable sources in 2017* (Journal of Laws of 2016, item 1753).

TAURON indicated that TAURON Sprzedaż had no possibility to envisage, despite applying due diligence and care, that the amendments to the legal regulations described above would take place.

The MG Regulation of 2012 significantly affected the increase in the supply of property rights arising from certificates of origin referred to in Article 9e(1) of the *Act of 10 April 1997 on Energy Law* (Journal of Laws of 2012, item 1059, as amended) – currently Article 44(1) of the RES Act, resulting in permanent and significant decline in PMOZE prices. A significant increase in the PMOZE supply as of 2012 results from the reduction of minimum shares of non-forest biomass in the total quantity of biomass supplied to the combustion process in relation to the requirements of the MG Regulation of 2008. The RES Act passed in 2015 has totally changed the system of support to electricity production in renewable energy sources which provided principal grounds for concluding the Contract and constitutes a significant change in the legal framework, posing direct and critical impact on profitability of the Contracts. The RES Act stipulates gradual abandoning of the support to electricity production in renewable energy sources through the system of certificates of origin in favour of the auction system.

The above information was published in the current report no. 6/2017 of 28 February 2017.

Conclusion of the annex with the consortium RAFAKO S.A. – MOSTOSTAL WARSZAWA S.A., for construction of power unit at Elektrownia Jaworzno III

On 01 March 2017 the management board of TAURON's subsidiary – TAURON Wytwarzanie (the "Contracting Authority") signed an annex with the consortium RAFAKO S.A. – MOSTOSTAL WARSZAWA S.A., (the "Contractor") to the contract for construction of 910 MW_e ultra-supercritical power unit (the "Unit") at Jaworzno III – Elektrownia II power plant (currently implemented within the separated branch of the Contracting Authority – 910 MW Jaworzono Branch in Jaworzno) in the scope of: steam boiler, turbine set, main building, electrical and process control and automation system (AKPiA) of the Unit.

Pursuant to the Annex, net price of the Contract will be increased by the amount of PLN 71.05 million, i.e. up to the amount of PLN 470 million, and the deadline for delivery of the subject matter of the Contract will be extended by 8 months, i.e. by the 67^{th} month following the date of concluding of the Contract at the latest, which means that the new assumed deadline of handover of the Unit for operation is November 2019.

The decision on signing of the annex by TAURON Wytwarzanie was made on 28 February 2017. On the same day, concluding of the annex under the terms indicated above was also positively evaluated by TAURON Management Board.

Introduction of amendments to the Contract resulted from the requirement to change the foundation method of the Unit facilities to indirect method as well as arrangement of additional works by the parties, favourable for the Contracting Authority for technical and economic reasons (construction of the foundation for the fifth zone of the electrofilter (EF) and extension of the EF switchboard building). The additional works will enable the Contracting Authority to gain savings during the envisaged shutdown of the Unit in 2021 in order to adjust a part of the Unit for the purpose of fulfilment of future requirements of BAT conclusions. The Contracting Authority partly acknowledged the legitimacy of the Contractor's claims associated with the aforementioned circumstances and variation order requests. Claims arising from the change in design standards (EUROCODES) were not deemed legitimate by the Contracting Authority.

In connection with the foregoing, warranties granted by the Contractor were extended:

1) by 6 months in relation to the availability of the Unit for direct deliveries carried out by RAFAKO S.A., maximum sustainable efficiency of the boiler, technical minimum of the Unit and content of free water in exhaust behind IOS, vibration level for the structure,
2) 12 months in the construction and engineering scope of the Unit.

The Contractor shall also ensure adequate extension of the performance bond.

Signing of the Annex shall change the terms of the Contract with the Contractor, however, it will not affect any changes of the whole investment budget. The level of project progress reached approximately 31.8%. At present, the assembly of the technological part of the boiler and assembly of steel constructions of the main buildings is in progress. Reinforced concrete works in the electrical switching station building, erection works of the cooling tower and construction works in the building of the electrical nave and cooling water pump station are continued.

The Company informed of the amendment to the aforementioned agreement in current reports: no. 5/2017 of 28 February 2017 and no. 7/2017 of 1 March 2017.

In addition, events resulting from the contracts and agreements concluded, significant for the operations, described in subsection 7.2.1 of this report should be also considered as important events with material impact on operations of TAURON Capital Group in the financial year 2016.

2.9. Awards and distinctions

In 2016 TAURON and companies of TAURON Capital Group received the following awards and distinctions.

Figure no. 48 Awards and distinctions

AWARDS AND DISTINCTIONS GRANTED TO TAURON and COMPANIES OF TAURON CAPITAL GROUP IN 2016

JANUARY

- Distinguishing TAURON with the award in the *Webstarfestival* competition in the category: "integrated marketing campaign" for communication activities promoting the "Serwisant 24H" product.
- Handing over of the *Top Event 2015* award to TAURON Dystrybucja for the project "Wawel – Light Alchemy" during the Evential Forum in Warsaw.

FEBRUARY

- Granting the *Top Eventuality of 2015* award to TAURON Dystrybucja for the project "Wawel – Light Alchemy" (2015); First place in the category "Marketing events and PR".

MARCH

- Recognising TAURON Group's Investor Relations, for the second time, as the best among companies of WIG30 Index in the competition organised by "Parkiet" Exchange Journal and the Chamber of Brokerage Houses. The quality of investor relations was evaluated by representatives of financial institutions (analysts, brokers and managers) as well as Internet users.
- Distinguishing nine initiatives conducted in TAURON Capital Group in the area of sustainable development in the report on "Responsible business in Poland. Good practices" issued by Responsible Business Forum.
- Granting the *MP Power Award* to TAURON Dystrybucja for the project "Wawel – Light Alchemy" (2015) in two categories: "Best event" and "Best visual image".

APRIL

- Granting the *Top Quality QI 2016* award to TAURON Sprzedaż in the "Product" category for "Serwisant 24H". The *Top Quality QI* is the project aimed at promoting effective quality management methods in companies and institutions. Another goal is to indicate and promote such companies and institutions.
- Granting the award to the fair stand of TAURON Wydobycie for the original and modern style of trade fair presentation. Award granted during the 23rd National Fair of Residential building materials and interior equipment – DOM.

MAY

Granting the award to TAURON for the highest value of the debut in the Catalyst market in 2015 in connection with introduction of 17,500 bonds with the total value of PLN 1.75 billion ito the alternative trading system. The issue was the second biggest offer in the history of the domestic market of corporate securities.

SEPTEMBER

- Distinguishing TAURON Obsługa Klienta with the title of *IT Leader* 2016 in the category "public utility" for perfectly conducted centralisation of billing systems for mass clients, comprising over 5 million clients.
- Granting the award to branches of TAURON Wydobycie mining plants: Mechaniczny dół (ZG Brzeszcze), Oddział Robót Przygotowawczych (ZG Sobieski) and Oddział Wydobywczy (ZG Janina) in the *Safe Branch* competition organised by the Safe Mining Foundation.

OCTOBER

- Obtaining by TAURON, for the third consecutive time, of the main award in the category of enterprises for the annual report for 2015 from the jury of *The Best Annual Report* competition organised by the Institute of Accounting and Taxes. At the same time, the Company joined the group of *Best of the Best,* comprising companies using the highest reporting standards. Similar to 2015, the internet version of the annual report was distinguished.
- Granting the *"Wprost" Innovator 2016* award to TAURON Sprzedaż for innovativeness for "Serwisant Gazowy 24H".

NOVEMBER

- TAURON was listed among ten top companies in the ranking of "Rzeczpospolita" daily and the Forum of Responsible Business "Educational activities of business. List of most significant initiatives" for the educational action of TAURON "Energy for the senior".
- Granting the distinction to TAURON EKOENERGIA in the Economic Plebiscite *Sudety Crystals 2016* in the category "Best company of responsible business" for activities in favour of employees and the local environment.
- Distinction for TAURON Gaz Giełda (TAURON Sprzedaż) for innovativeness in the *Innovation Laurel 2016* competition. The organiser od the competition is the Chief Technical Organisation, the association of scientific and technical organisations with over 180 years of tradition.
- CIJ Awards award granted to TAURON Sprzedaż in the category: Best Energy Supplier 2016 in the competition organised by Roberts Publishing Media Group, the issuer of CIJ, the trade journal in English, devoted to commercial real estate in Central and Eastern Europe.
- Best Interoperability Performance Award for TAURON Dystrybucja. Award for the AMIplus Smart City Wrocław project received during the European Utiity Week conference in Barcelona for the effective implementation and high level of interoperability.
- Granting a brown statue to TAURON in the competition on *Kraków Culture Sponsor 2015*.
- Obtaining of the "Reliable company 2016" Certificate by TAURON Wydobycie – the distinction confirming reliability of enterprises towards clients and customers.

DECEMBER

- Accepting TAURON, for the fourth consecutive time, to the RESPECT Index – a group of listed companies managed in responsible and sustainable manner.
- QUALITY OF THE YEAR Award for "Serwisant Gazowy 24H" in the category: Product, granted to TAURON Sprzedaż. The Quality of the Year is the distinction for quality promoting efforts of companies and enterprises operating in Poland.
- Mining Success of the Year in the "Ecology" category. The competition organised by the Mining Chamber of Industry and Commerce and the School of Underground Exploitation. The award was granted to TAURON Wydobcie for the implementation of the first system for neutralisation of acid waters of surface discharge in Poland, in the area of the mining waste treatment facility of ZG Janina in Libiąż.
- Granting the award to ZG Janina belonging to TAURON Wydobycie as the most distinguished for the Foundation of Mining Families.

JANUARY 2017 (awards for 2016)

- Granting the *Laurel of Skills and Competence 2016* award to the Opole branch of TAURON Dystrybucja by Ople Chamber of Commerce for supporting the economic development of Opole Silesia.
- Distinction for TAURON Dystrybucja for the highest growth of training policy effectiveness indicators in 2014–2016. The award granted by the PSTD (Polish Society for Training and Development).

2.10. Information concerning the employment structure in TAURON Capital

2.10.1. Policy of Human Resources Management in TAURON Group

The *Policy of Human Resources Management in TAURON Group* (the Policy) was adopted for application in 2015. It is a common document for all companies of TAURON Capital Group.

The Policy was developed on the basis of:

a) diagnosis of effectiveness of the Human Resources Management area in the companies of TAURON Capital Group,

b) analysis of benchmarks and good market practice,

c) Integrated Human Resources Management System at TAURON Polska Energia S.A.,

d) Joint activities of representatives of the Human Resources Management area from all companies of TAURON Capital Group.

Objectives of the Policy:

1. Orientation of employees towards achieving results in areas compliant with the Strategy and with the CSR Strategy.
2. Determining consistent standards and ensuring high quality human resources management processes taking into account modern solutions and best market practices.
3. Building consistent organisational culture of TAURON Capital Group based on corporate values and supporting innovativeness.
4. Raising the level of employees' engagement and motivation.

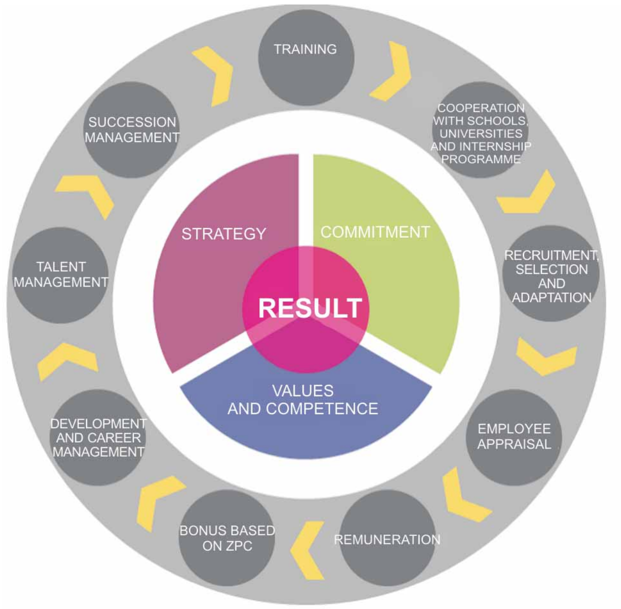
Assumptions of the Policy:

1. Result-orientation of employees – processes of human resources management support result-orientation and concentration of employees on achieving the best possible results, inter alia, through assessment of the accomplishment of bonus targets and area KPIs.
2. Orientation of employees to the implementation of the Strategy and Sustainability Strategy of TAURON Capital Group. The policy enables consistent acquisition, maintaining and development of key competence for the implementation of the Strategy and maintaining of business continuity of companies and TAURON Capital Group.
3. Supporting the enhancement of the level of employees' engagement and motivation, through strengthening of both individual relations of employees and supervisors as well as introduction of system solutions associated with building incentive systems, development, training and monitoring of job satisfaction.
4. Coherence of the Policy with corporate values of TAURON Capital Group and promoting the behaviour compliant with them as well as building of consistent organisational culture based on values.

   VALUES: Partnership, Development, Courage are the overriding values for the implementation of tasks within activities associated with human resources management.
5. Determining consistent standards and ensuring high quality human resources management processes taking into account modern solutions and best market practices, e.g. recruitment standards, cooperation with schools and universities. The coherence is implemented through key substantive areas of human resources management, with the support of the relevant tools, e.g. talent management programme and competence model in relation to which works were started in 2016. Members of Management Boards of companies of TAURON Capital Group and key managers were invited to the project group.

The figure below presents the assumptions of the *Policy of Human Resources Management in TAURON Group.*

Figure no. 49 Assumptions of the Policy of Human Resources Management in TAURON Group



Good practice

Principle 70/20/10

Any development activities are implemented in accordance with the principle of effective learning where:

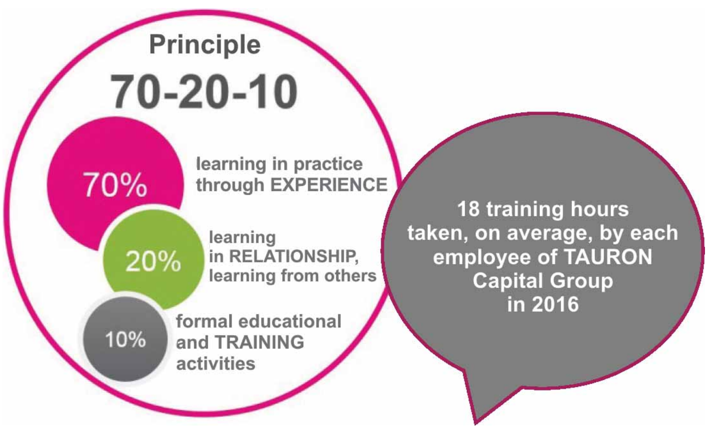
70% – is learning through implementation of a new type of tasks; work in project teams; temporary assignment of an employee to fulfil other role within the Company or TAURON Capital Group; self-education (e.g. professional literature),

20% – is the observation of persons with higher competence in the specific area; development talks; regular feedback; coaching and mentoring sessions,

10% – is represented by internal and external training, studies, language courses, conferences.

The figure below presents the principle of effective learning 70/20/10.

Figure no. 50 Principle of effective learning 70/20/10

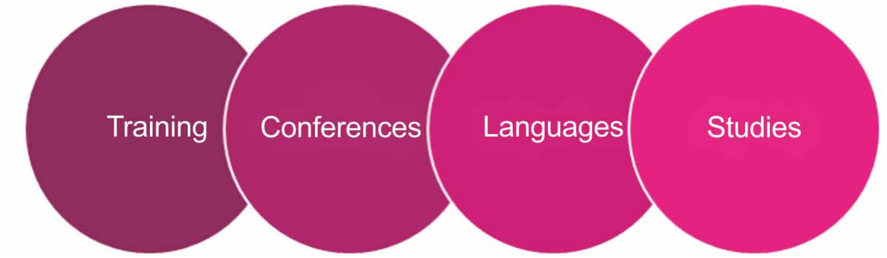


2.10.2. Development and training

Employees of companies of TAURON Capital Group develop in various forms of development activities.

The figure below shows the forms of development activities of employees of TAURON Capital Group companies.

Figure no. 51 Forms of development activities of employees of TAURON Capital Group companies



451,236 is the total number of training hours of our employees during a year

153 employees used co-financing forms to study at the university

268 employees participated in language courses

The figure below presents the total number of training hours, divided into genders, in TAURON Capital Group in 2016.

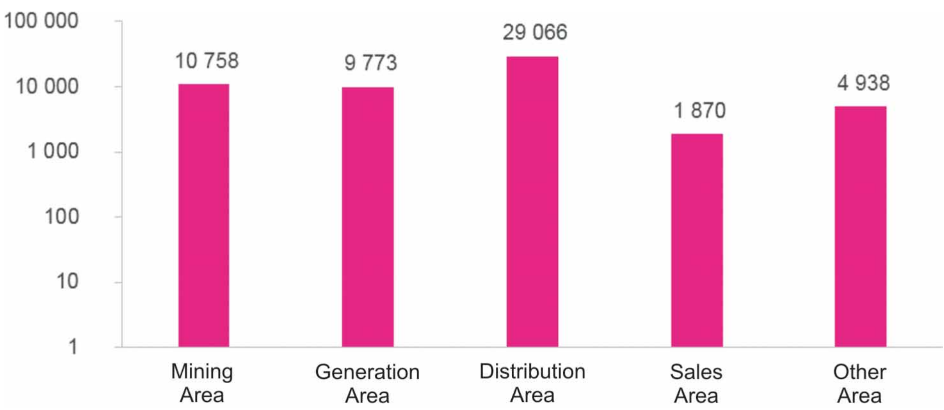
Figure no. 52 The total number of training hours, divided into genders, in TAURON Capital Group in 2016

	WOMEN	MEN	TOTAL
The total number of training hours, divided into genders, in TAURON Capital Group	62,257	388,979	451,236
Number of employees*	5,403	20,139	25,542
Average number of training hours	12	19	18

** Number of employees as at 31 December 2016.*

The figure below presents the total number of training days divided into activity Segments.

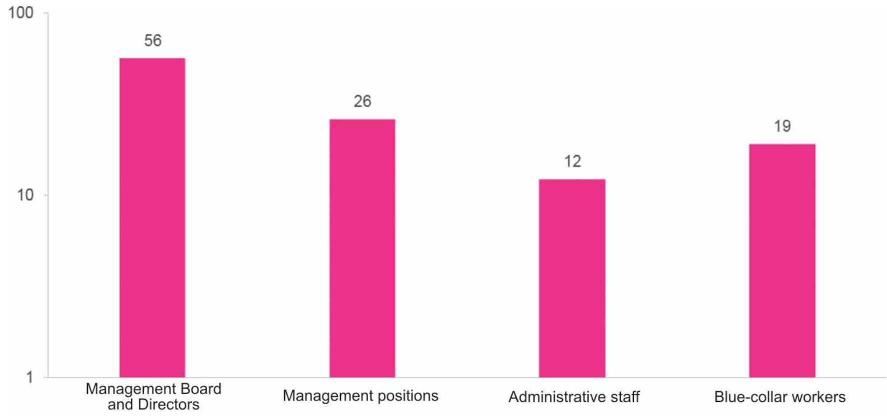
Figure no. 53 The total number of training days divided into activity Segments*



** Number of training days divided by the employment status in persons as at 31 December 2016.*

The figure below shows the average number of training hours per employee, according to job groups.

Figure no. 54 The average number of training hours per employee, according to job groups



Development initiatives organised in TAURON Capital Group in 2016

Initiative

Development programme in TAURON Dystrybucja – "We are building a team of leaders"

The programme was addressed to the senior management staff. The aim of the programme was to strengthen leadership competence in terms of, inter alia, new challenges and the Single Distribution programme implemented (Office Managers, HR Managers in Branches, Branch Functional Directors). 74 employees participated in the programme, including also employees of TAURON Dystrybucja Serwis and TAURON Dystrybucja Pomiary. In TAURON Dystrybucja 68 persons participated.

Initiative

Development programme "Effective Leaders in a Single Distribution"

The programme is addressed to the medium-level management staff of TAURON Dystrybucja, TAURON Dystrybucja Serwis and TAURON Dystrybucja Pomiary (heads of divisions, departments, regions, senior foremen, coordinators from regions, coordinators of measurement areas). It covers, in total, approximately 500 leaders. In TAURON Dystrybucja almost 420 persons participate in the programme. The aim of the programme is to prepare managers to new challenges, associated, inter alia, with the "Single Distribution" project, enhance knowledge and skills in the scope of leadership as well as increase leadership effectiveness. The programme was designed for 3 years (2015–2017) and it was launched in July 2015. The programme develops such competence as: human resources management, management of results, change management, strategic thinking, decision-making, client-orientation.

Initiative

Internal Trainer Programme at TAURON Obsługa Klienta

Internal Trainers are persons selected among employees of TAURON Obsługa Klienta, with key competence, trainer potential and willing to share their knowledge with others. The number of active Internal Trainers in 2016 is 9 persons. In November 2016 the recruitment process was conducted, as a result of which the number of Internal Trainers increased to 21 persons. 443 employees of TAURON Obsługa Klienta took advantage of 46 training courses. Moreover, in 2016 work on introduction of the internal trainer programme in the across the entire TAURON Capital Group started.

Initiative

Cooperation with universities

TAURON Capital Group cooperated with over 50 educational establishments (universities, secondary and vocational schools) all over the country. In the framework of the cooperation, pupils, students and graduates may apply for internship and training in TAURON. Only in the previous year 1084 persons used this form of education. Through the cooperation partnership relations with the academic community are built – the scientific staff 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.

Within the framework of promotion of the energy professional job TAURON Distribution delivered numerous lectures dedicated to teachers, addressed to partner secondary school teachers. Under the projects executed, training activities and educational trips were organised for students, e.g. a visit to ZG Janina mining gallery, excursions to hydroelectric power plants. In the past year TAURON Capital Group also cooperated with research and educational centres, e.g. in the scope of the project concerning the improvement of efficiency of power units. Within the initiative of the Research and Innovation area, workshops with university deans were also conducted.

Initiative

TAURON Group Open University

TAURON Group Open University is a cycle of lectures provided by the most distinguished 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 strategic objectives.

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, 12 lectures were provided, attended by over 2,000 employees of all companies of TAURON Capital Group.

Initiative

Post-graduate studies for employees of TAURON Capital Group companies

Following TAURON's initiative, post-graduate studies for employees of TAURON Capital Group companies were launched. The most important goal while organising post-graduate studies for employees of companies is to acquire coherent knowledge on the specific issue, accordingly, the organisation strives to standardise processes in TAURON Capital Group and introduce common solutions oriented towards increasing the financial result of the organisation. In 2016 the dedicated post-graduate studies on "The natural gas market – opportunities and barriers for development" were completed at the AGH University of Science and Technology in Kraków, and post-graduate studies on "Procurement management in business" were launched at Jagiellonian University.

Initiative

The policy of recruitment, selection and adaptation of employees of TAURON Group companies

As of 2015 TAURON Capital Group has a common *Policy of recruitment, selection and adaptation of employees of TAURON Group companies*, consequently, this process is consistent in all companies. The main form of recruitment in the entire TAURON Capital Group is the internal recruitment. While launching the recruitment process, we first distribute the announcement to employees of companies by placing it on internal intranet, i.e. Taruonet. We promote this recruitment channel through mailing distributed to all employees of TAURON Capital Group and regular announcements on Tauronet. Should internal recruitment be unsuccessful, we shall start search for employees outside the internal potential, searching for new employees on the market. In such a case we place job offers both on the company website and on other recruitment portals.

Initiative

PRO Value

During the work on the Strategy which requires specific attitudes and behaviours to be implemented, new values of TAURON Capital Group were defined in 2016: Partnership, Development and Courage (acronym from Polish: PRO). The PRO values were developed at workshops with employees, organised by TAURON, attended by over 80 persons from various companies and various levels of the organisation. The work on implementation of the PRO values contained several stages: workshops for the staff, PRO website on Tauronet, arts competition for employees, PRO zone in PROspect, PROsave TAURON competition, workshops for members of Management Boards. PRO values create roadsigns on the path towards the implementation of the Strategy as well as in relations with co-workers, clients, partners and the environment.

PARTNERSHIP

We are partners for clients and for each other in implementation of common goals.
We build sustainable relations: based on trust and mutual respect.
We engage in anything important for our clients and the Group.

DEVELOPMENT

We are innovative: we overcome barriers, determine trends and create changes.
We continuously develop competence, skills and knowledge.
We search for increasingly improved solutions: we meet current and future clients' needs, continuously enhancing the quality of our services.

COURAGE

We discuss problems and the boldest ideas openly and courageously.
We are determined in implementing what we believe in with the purpose of reaching common goals.
We face challenges of the changing environment with commitment and passion.

Initiative

Talent Management Programme in TAURON

The Talent Management Programme in TAURON represents an integrated approach to development and career of employees. It is a development activity which, as a rule, does not cover all Employees, but only those distinguishing with high potential and achieved results. The programme is the support to the process of their development and exploitation of their potential in TAURON and TAURON Capital Group. In 2016 the kick-off meeting of the anniversary, 5th issue of the programme took place: Over 60% of graduates of the Talent Management Programme were promoted in the structures of TAURON Capital Group.

Initiative

Adaptation Programme in TAURON

The kick-off meeting of the Adaptation programme in Tauron took place in September 2016. This meeting was attended by new employees who joined the community of TAURON employees as of the beginning of 2016. The training sessions currently take place on a monthly basis in two-day sessions. Each month such meetings are open by a member of TAURON Management Board. On the first day, information on the overall TAURON Capital Group is provided as well as issues important for employees are presented. The second day is devoted to the presentation of business areas. Selected areas from each business stream are presented by TAURON employees (in the framework of development of their expert competence) who participated in the Talent Management Programme. While introducing new employees, in the first period of work in TAURON Capital Group, each of them had own mentor to assist him/her in the adaptation process. The objective of the process is to ensure efficient functioning of a newly recruited employee and possibly fast achieving of the level of efficiency expected on his/her position.

Initiative

E-learning platform

Employees of selected companies of TAURON Capital Group may use the e-learning platform containing many training courses. They include both specialised training and training courses developing interpersonal skills. In 2016, all users of the platform accomplished more than 20,000 training courses. Also last year the training entitled “Be safe in the network” was launched. In TAURON Obsługa Klienta the training on “Safety in road traffic” was launched for employees holding a driving licence and a permit to drive a company vehicle. 1,194 employees out of 1,217 persons authorised to drive company vehicles passed the training.

Platforma e-learning
Kliknij po więcej!

2.10.3. Social dialogue

The Management Board of TAURON conducts a constructive and open dialogue with the social side, mainly aimed at maintaining high quality and effectiveness of mutual cooperation. Within the framework of the aforementioned dialogue, the following solutions were jointly developed in 2016:

a) at a meeting on 11 July 2016, in the presence of the Secretary of State at the Ministry of Family, Labour and Social Policy, the Ombudsman of Social Dialogue was appointed in TAURON Group.

b) on 13 September 2016 the Agreement on cooperation within the social dialogue in TAURON Group was signed, defining the rules of cooperation of TAURON Management Board with the Social Council.

During regular meetings and consultations, representatives of the social side are informed about issues associated with:

a) the economic and financial situation of TAURON Capital Group,

b) the Efficiency Improvement Programme in TAURON Group for 2016–2018,

c) Voluntary Redundancy Programmes in companies of TAURON Capital Group,

d) issues related to employee affairs in TAURON Capital Group.

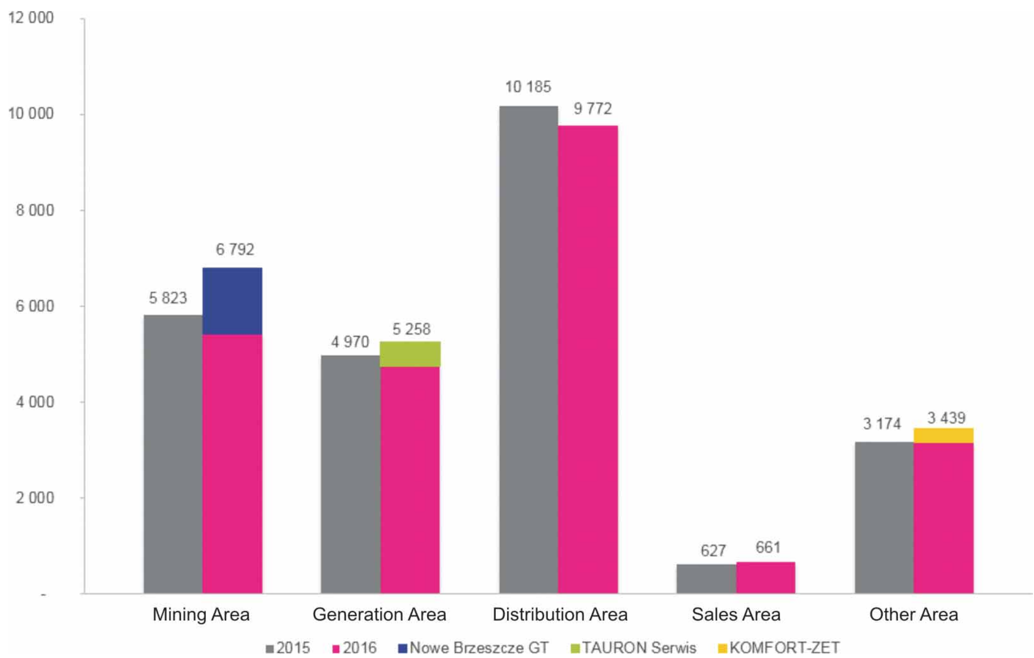
Within the framework of conducted social dialogue the Management Board of TAURON provided many answers to the correspondence from trade union organisations and the Ministry of Energy. In parallel, current communication is maintained in companies of TAURON Capital Group between Management Boards and trade union organisations operating at a given employer. TAURON takes active part in meetings at the national level with representatives of the government, employees and employers (within the activities of the Tripartite Team for the Energy Sector).

2.10.4. Key data concerning employment

In 2016, the average employment in TAURON Capital Group reached 25,922 FTEs, which means an increase against the employment in 2015, when the average employment amounted to 24,778 FTEs.

The figure below presents levels of average employment in TAURON Capital Group in FTEs (rounded up to the full FTE), divided into individual Segments of operations in 2015 and 2016.

Figure no. 55 Average employment in TAURON Capital Group in 2015 and 2016* (FTEs)



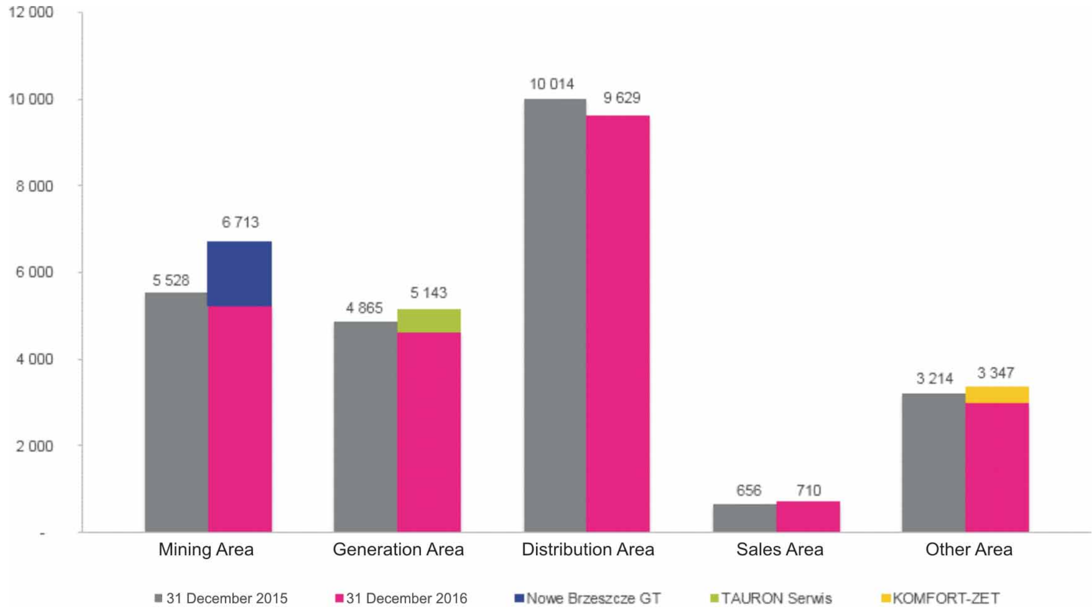
** The average employment comprises Nowe Brzeszcze GT, TAURON Serwis and KOMFORT-ZET companies which were covered by the consolidated reporting in 2016.*

Changes in the level of the average employment in individual Segments of activity in 2016, as compared to the average employment in 2015, result, among others, from covering the following companies under the consolidated financial reporting in 2016: Nowe Brzeszcze GT, TAURON Serwis and KOMFORT-ZET and from the implemented Voluntary Redundancy Programmes in Areas: Distribution, Generation and Other, as well as resignation of employees leaving TAURON Capital Group.

As at 31 December 2016, 25,542 persons were employed in companies of TAURON Capital Group. The increase in employment by 1,265 persons was recorded, as compared to the employment status as at 31 December 2015 which reached 24,277 persons.

The figure below presents the employment in TAURON Capital Group in persons, according to the status as at 31 December 2015 and 31 December 2016.

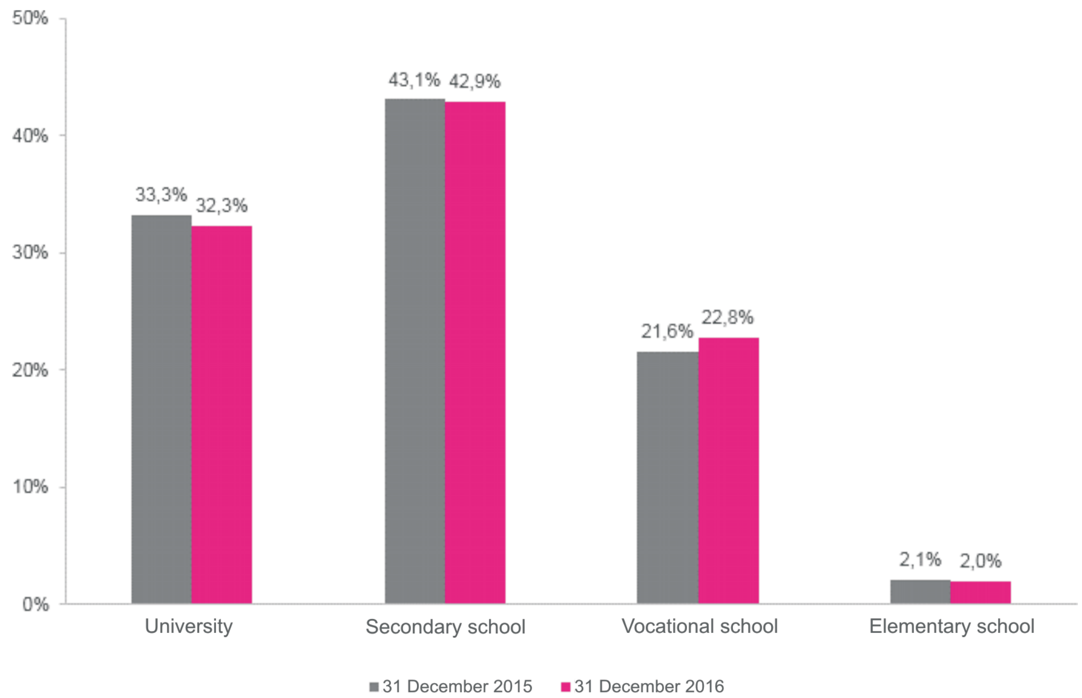
Figure no. 56 Employment in TAURON Capital Group as at 31 December 2015 and 31 December 2016* (persons)



** The average employment comprises Nowe Brzeszcze GT, TAURON Serwis and KOMFORT-ZET companies which were covered by the consolidated reporting in 2016.*

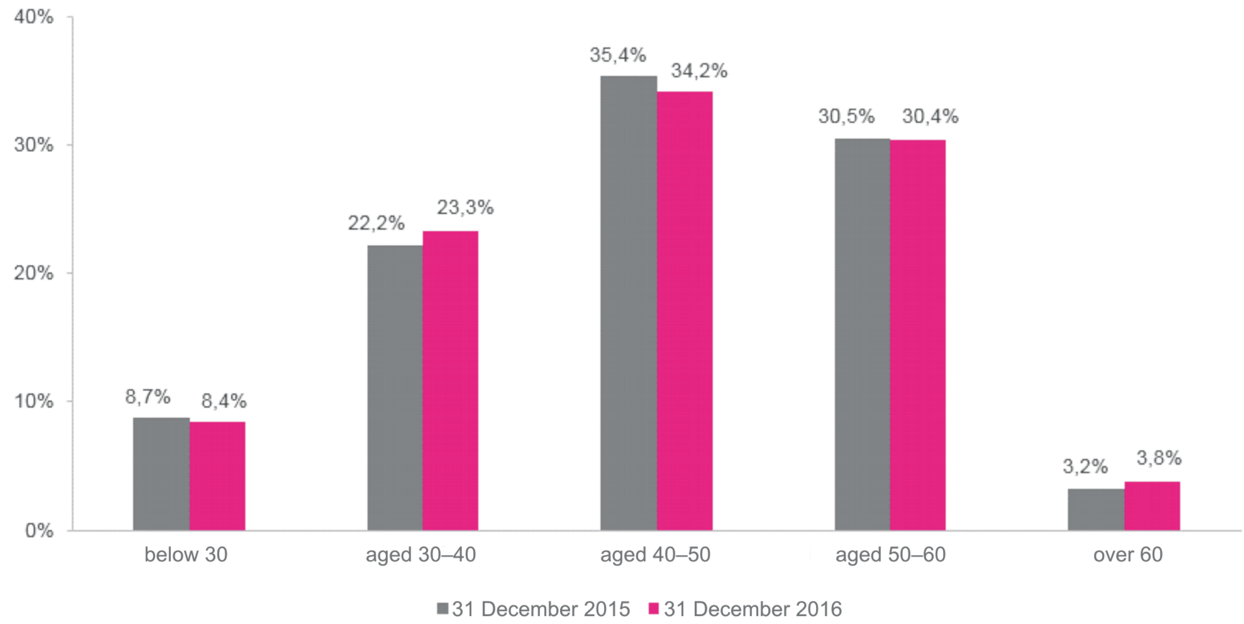
The figure below presents the structure of employment in TAURON Capital Group according to education as at 31 December 2015 and 31 December 2016.

Figure no. 57 Employment structure in TAURON Capital Group as at 31 December 2015 and 31 December 2016 (education)



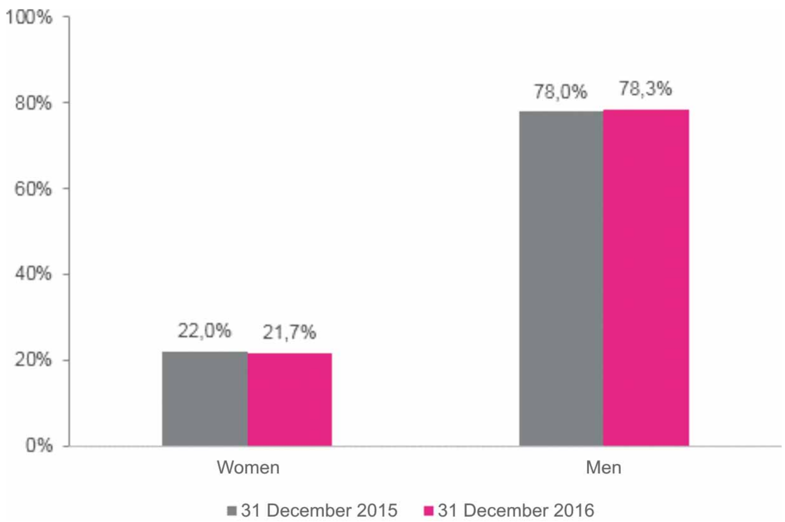
The figure below presents the structure of employment in TAURON Capital Group according to age as at 31 December 2015 and 31 December 2016.

Figure no. 58 Structure of employment in TAURON Capital Group as at 31 December 2015 and 31 December 2016 (age)



The figure below presents the structure of employment in TAURON Capital Group according to gender as at 31 December 2015 and 31 December 2016.

Figure no. 59 Structure of employment in TAURON Capital Group as at 31 December 2015 and 31 December 2016 (gender)



2.11. Corporate Social Responsibility (CSR) Policy

In 2011, acknowledging that communication of non-financial measures is particularly important in case of listed companies, in the *Corporate Strategy of TAURON Group for 2011–2015 with an outlook until 2020*, the need to develop and implement the CSR strategy (within integration of the PR function), at a level of the company and "TAURON Group". Accordingly, in 2012 the *Strategy of Corporate Social Responsibility, i.e. the Strategy of Sustainable Development of TAURON Group for 2012–2015, with the outlook up to 2020* was developed (Sustainability Strategy).

In connection with the expiry of the Sustainability Strategy at the end of 2015 as well as the fulfilment of over 95% of goals assumed in the document, in December 2015 the Management Board of TAURON adopted the updated *Strategy of Sustainable Development of TAURON Group for 2016–2018, with the outlook up to 2020*.

The core of the new Sustainability Strategy remained unchanged, however, the wording of the document has been simplified. This Strategy was developed based on the international trends in the CSR area and it takes into account the opinion of TAURON Capital Group environment as well as future challenges to be faced by the energy sector. It is based on five strategic directions: two primary (ensuring energy supply security, customer orientation) and three secondary (ethical culture and engaging workforce, environment protection and social and business partnership). Within each direction were determined (18 in total) which TAURON intends to fulfil by the end of 2018. For each of the obligations key initiatives were formulated, supporting their implementation, which are assigned to individual business units in companies.

The Sustainability Strategy is directly associated with all areas of TAURON Capital Group activities. It streamlines both the approach to the CSR and the methodology for the assessment of effectiveness of measures undertaken based on Global Reporting Initiative (GRI) indicators. In 2016, the fourth report on sustainable development was published. For the first time, it was integrated with the annual report (integrated report). However, the report traditionally presented measures undertaken by TAURON Capital Group in the CSR area in 2015 as well as the summary of the Sustainability Strategy for 2012–2015. The report was prepared in accordance with the highest reporting standards – GRI G.4, which was confirmed by the certification obtained – GRI Materiality Matters' Check and it was subject to external verification by an independent auditor. The Company was also audited in connection with joining the RESPECT Index – the index comprising companies listed at the stock exchange, operating in accordance with the rules of sustainable development. In 2016, TAURON achieved, for the fourth time, a positive result and was included in this most prestigious ranking of socially responsible companies.

One of the directions of the Sustainability 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 actions within the area of care for safety of local communities and actions for public benefit.

TAURON Capital Group, operating in the area of southern Poland, has a leading position in energy sales and generation. These conditions cause that the scope of actions conducted for the benefit of the communities in which companies of TAURON Capital Group operate, is very broad. Many projects are supported which are important for inhabitants of the regions of Upper and Lower Silesia, Opolskie, Małopolska and Podkarpacie Regions. Among others, TAURON cooperates with the Mountain Voluntary Emergency Service (GOPR), with the purpose of enhancing safety in the mountains.

In 2016, TAURON continued the cooperation with the SIEMACHA Association – one of the leading NGOs in the country focusing on implementation of projects in the area of education, sports and therapy, providing systemic assistance to children and teenagers. In the scope of the established cooperation, TAURON's patronage covered sports activities of the association, gaining the title of *TAURON – SIEMACHA's sports partner*. In 2016, such projects were supported as *Foootball Children's Day with TAURON*, *Juliada 2015, TAURON Basket Game* or *I swim with TAURON*.

Activities carried out by companies of TAURON Capital Group are also worth mentioning. In 2016, the campaign called *TAURON Fuses* was continued. Its stage implemented by TAURON Sprzedaż focused on raising awareness of clients on the energy market, in particular, in order to protect against practices of unfair sellers. On the other hand, a part of the project devoted to education of children and teenagers was conducted by TAURON Dystrybucja, teaching the rules of safe electricity use.

fundacja TAURON

In 2016, TAURON Foundation and the Company implemented, based on the employee voluntary programme, the twelfth issue of the *Houses of Positive Energy* action, addressed to 24-hours custody and caretaking facilities, aimed at improvement of the living conditions of children from orphanages. The action covered all the facilities within the area of operations of TAURON Capital Group. In the years 2011–2016, 465 orphanages from five provinces participated in the action. In 2016, the Foundation also accomplished its goals, in particular, through supporting natural and legal persons, institutions and organisations in their activities consistent with the Foundation goals, transferring donations in the amount of PLN 948,500.

TAURON is also the signatory of the declaration signed on 17 June 2009 during the national conference under 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 clients is one of two leading directions of the Sustainability Strategy. As an essential element in the energy system of the country, TAURON optimises processes in individual areas of activity: generation, distribution and sales of electricity and heat, in order to ensure stable supplies with high qualitative parameters to clients. In order to provide for the continuity of supplies, TAURON not only implements new investment projects but also conducts ongoing maintenance works and modernisation of the infrastructure held as well as actively searches for new solutions.

In 2016 TAURON Dystrybucja modernised almost 1,800 km of existing grids and 37 main supply points. The Company also built 2.4 thousand km of new lines (including connections). Investment projects are also conducted by TAURON Ciepło. In 2016 the capacity of clients newly connected to the heating network amounted to 30.64 MW, and the length of new commissioned heating networks reached 12.3 km (including the connectors). In 2016 TAURON Ciepło also conducted investment in new generation capacity. 3 boilers at ZW Katowice were commissioned, with the capacity of 114 MW_t as well as the BC-50 heating unit at ZW with the capacity of 86 MW_t and 65 MW_e.

At the same time, in order to guarantee stable supplies, TAURON Dystrybucja conducts ongoing measures minimising 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. The Company is also the initiator and co-organiser of other social actions enhancing the level of energy supply reliability as well as aimed at protection of health and life of persons staying in the vicinity of energy infrastructure (e.g. "Stop the illegal electricity intake" action).

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, inter alia, in the scope of reducing the emission of hazardous substances from combustion processes but also innovative products and services for individual clients.

In 2016 the Zone of Innovation was created on the Intranet of TAURON Capital Group, within which competitions for employees are organised. Its objective is to promote innovative organisational culture and encourage employees to submit innovative solutions optimising 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.

2.11.2. Customer orientation

The overriding objective of TAURON Capital Group is to meet customers' expectations and needs. It is perfectly emphasised in the new Strategy. Customer orientation is also the second leading direction of Sustainability Strategy, next to energy security.

Efforts aimed at accomplishing the assumed goals in this scope 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 clients and disadvantaged groups as well as through continuous education in the area of effective energy use and utilisation.

TAURON analyses market trends on an on-going basis as well as conducts cyclical client satisfaction surveys concerning the services and products offered. Owing to such activities the Company endeavours to meet clients' expectations, satisfying their current and future needs, to the extent feasible. At the same time, complaint procedures are improved, allowing for prompt and efficient response in situations reported by clients. All measures constituting the customer service process are conducted in compliance with the highest ethical standards.

Preventing limiting the relations with clients only to the provision of products and services, as well as having the awareness of many threats which may potentially affect a client in various aspects of electricity purchase or use, TAURON conducts educational actions addressed to energy users.

The educational and information functions are fulfilled, inter alia, by the action "Energy for the senior", implemented by the Team of Client Rights Ombudsman operating within the client area in TAURON. The initiative is addressed to the elderly who are most exposed to activities of unfair energy vendors. Its aim is to educate clients 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 organised.

2.11.3. Customer satisfaction surveys

One of key elements tools of customer satisfaction evaluation in TAURON Capital Group is the CSI survey. This survey is conducted on a regular basis, once a year, at the turn of the 3rd and 4th 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 survey, as one of the key tools for the evaluation of customer satisfaction in TAURON Capital Group, was conducted in September – November 2016, by an independent research agency – TNS Polska.

The survey covered randomly selected clients of the Household segment (1,000 clients), Small enterprises (200 clients) and Corporations and large enterprises (300 clients) and a group of clients of other energy companies, such as: ENEA, Energa and PGE.

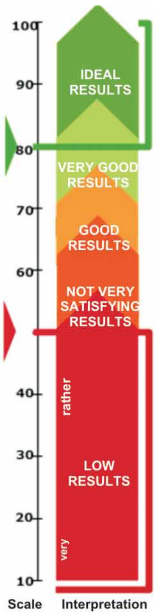
As a result of conducted surveys, the CSI was determined at the following level:

1) Households – 80%,
2) Small enterprises – 73%,
3) Corporations and large enterprises – 75%.

The figure below presents results of surveys conducted in the Household segment, achieved by TAURON in the period from 2011 to 2016, and the level of the CIS reached in 2016, as compared to other energy groups.

Figure no. 60 Results of survey covering households in 2011–2016

TAURON	2016	2015	2014	2013	2012	2011
Settlements and Payments	89	87	86	80	79	79
Loyalty ratio	**86**	**84**	**83**	**77**	**77**	**73**
Customer service	82	80	81	78	80	77
Failures and shutdowns	82	80	77	76	75	74
CSI ratio	**80**	**79**	**76**	**73**	**73**	**71**
Image	78	75	73	69	67	66
Prices and tariffs	70	67	63	57	55	50



The figure below presents the results of the survey in TAURON Capital Group as compared to other Energy Groups in 2016.

Figure no. 61 Results of the survey in TAURON Capital Group as compared to other Energy Groups in 2016

TAURON	Energa	Enea	PGE	RWE
80	71	76	72	76

2.11.4. Impact on the 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 business activity, in particular, in the context of contemporary challenges related to the environmental impact of energy generation processes and diversification of electricity sources. Considering the sustainable development rules, companies of TAURON Capital Group optimise the processes of management of the resources held (water, raw materials, materials) and conduct active policy of waste management (both processing and municipal).

The pro-ecological education conducted by companies of TAURON Capital Group, addressed both to children and to adults, also plays an important role in the area of environmental protection.

Companies of TAURON Capital Group actively engage in many information and educational programmes concerning environmental protection and energy saving which are addressed both to employees, local communities and to customers.

2016 was another year of educational activity associated with combating low emission.

The most important actions in the area of environmental protection

Companies of TAURON Capital Group conduct the responsible environmental protection policy and apply due diligence to ensure that the implemented investments are compliant with the requirements and consider the technological developments in the area of environmental protection.

The most important actions in the area of environmental protection conducted in TAURON Capital Group in 2016 included:

1) the continuation of construction of the power unit with 910 MW capacity in Jaworzno III Power Plant, whose commissioning will significantly influence the reduction of ambient air emission of NO_x, SO_2, CO_2 and particulate matter (TAURON Wytwarzanie),
2) modernisation of the electrofilter of unit no. 5 at Elektrownia Jaworzno III in order to reduce dust emission (TAURON Wytwarzanie),
3) modernisation of Water Demineralisation Station of TAURON Wytwarzanie, Branch Elektrownia Stalowa Wola in order to reduce the annual consumption of HCL and NaOH, including full elimination of the sludge, three new reverse osmosis lines,
4) enclosure of steam generator reducing fuel and electricity consumption for start-ups of power units in Elektrowna Łaziska in order to reduce CO_2 and SO_2 emission (TAURON Wytwarzanie),
5) installation of product generation from bottom ash of 460 MW unit in Elektrownia Łagisza in Będzin,
6) completion of the construction of a system for pre-treatment of acid sludge discharged from mining waste treatment facility at ZG Janina (TAURON Wydobycie),
7) conducting activities aimed at limiting mining waste generation through aggregate production (TAURON Wydobycie),
8) construction and reconstruction of sanitary water sewage network at ZG Sobieski (TAURON Wydobycie).
9) modernisation of hydroelectric power plants, aimed, among others, at mitigation of the hazard of environmental contamination with oils (TAURON EKOENERGIA),
10) completion of modernisation of the dust exhaustion installation of an open dumping site (KW Czatkowice),
11) reduction of environmental noise emission (KW Czatkowice),
12) modernisation of the cooling system of crushers at Preliminary Crushing Station (KW Czatkowice),
13) forestation of the protective belt across the area of approximately 2 ha (KW Czatkowice),
14) programme of investment activities in the scope of constructing safeguards against soil and water contamination with oil derivatives (TAURON Dystrybucja),
15) assembly of insulation screens on elements of transformers and poles in order to protect birds sitting on supporting structures of overhead lines (TAURON Distrybucja).

Compliance with the requirements in the scope of emission of pollutants into the air

As of January 2016, as a result of transposition of Directive 2010/75/EC on industrial emissions (so-called IED) into the national legislation, for a part of sources of energy combustion with the capacity of > 50 MW (in fuel) more stringent requirements apply in the scope of permissible air pollution emission standards (NO_X, SO_2, dust).

The investment programme implemented over the recent years focusing on construction and modernisation of fuel denitrification, desulphurisation and dust extraction in companies of TAURON Capital Group enabled the reduction of air emission in 2016.

Emissions of dust and gaseous pollutants into the air are mainly associated with activities of companies of TAURON Capital Group within the conventional energy segment (electricity and heat production) and fuel combustion for the needs of technological processes.

The table below presents the estimated levels of NO_X, SO_2, dust and CO_2 emissions from energy fuel combustion for selected companies of TAURON Capital Group in 2016.

Table no 19. Annual levels of NO_X, SO_2, dust and CO_2 emissions from energy fuel combustion for 2016

No.	Company name	SO_2 emission (Mg)	NO_X emission (Mg)	Dust emission (Mg)	CO_2 Emissions (Mg)
1.	TAURON Wytwarzanie, including:	12,295	12,501	701	13,366,194**
	Oddział Jaworzno III	2,620	4,226	144	5,481,776
	Oddział Łaziska	3,716	3,409	195	3,703,360
	Oddział Łagisza	1,873	2,366	87	2,061,954
	Oddział Siersza	2,342	1,582	193	1,597,860
	Oddział Stalowa Wola	1,744	918	82	521,244
2.	TAURON Ciepło, including:	3,348	1,330	219	1,561,537**
	ZW Bielsko-Biała	1,063	243	44	545,908
	ZW Kamienna Góra	70	17	4	15,663
	ZW Katowice	1,341	543	92	657,921
	ZW Tychy	407	411	20	255,502
	CC Olkusz***	225	48	1	37,139
	CC Zawiercie***	172	42	3	33,231
	Other (local heating plants)	70	27	55	16,174
3.	TAURON Wydobycie	55.2	37.7	45.0	26.3
4.	KW Czatkowice	4.6	6.3	3.4*	5,636
	Total	**15,702**	**13,875**	**968**	**14,933,394**

** Total emission of dust from fuel combustion.*
*** CO_2 emission within the meaning of EU ETS – according to Annual Reports on CO_2 Emission (status in February 2017, the level of emission prior to verification).*
**** Estimated value, prior to verification at the end of the 1st quarter of 2017.*

Emission abatement in 2016 was reflected in the level of fees for the use of the environment. In 2016 companies of TAURON Capital Group accrued fees in the total amount of approximately PLN 35.7 million, i.e. by approximately 20% less than in the previous year.

The table below presents the level of fees for economic use of the environment due for 2016 in individual companies of TAURON Capital Group.

Table no 20. The level of estimated fees for economic use of the environment due for 2016

No.	Company name	Fees for economic use of the environment due for 2016 (PLN thous.)
1.	TAURON Wytwarzanie	20,900
2.	TAURON Wydobycie	11,084
3.	TAURON Ciepło	3,593
4.	TAURON Dystrybucja	101
5.	KW Czatkowice	54
6.	TAURON Dystrybucja Serwis	12
7.	TAURON Obsługa Klienta	1
8.	TAURON EKOENERGIA	< 0.8
9.	TAURON Sprzedaż	1.5
	Total	**35,747**

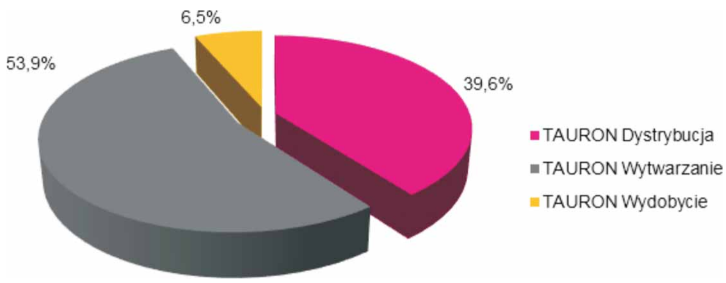
Sustainable development

In order to reduce the consumption of non-renewable resources, TAURON Capital Group implements solutions enabling to obtain higher energy savings and use of various sources of energy.

In 2016 within TAURON Capital Group, 9 investment projects were submitted, associated with the improvement of energy efficiency in three business areas, whose direct environmental effect is the reduction of CO_2 emission. This effect was confirmed through allocation of so-called “white” certificates.

The figure below presents the structure of the volume of “white” certificates obtained in TAURON Capital Group in 2016.

Figure no. 62 Structure of the volume of “white” certificates obtained in TAURON Capital Group in 2016

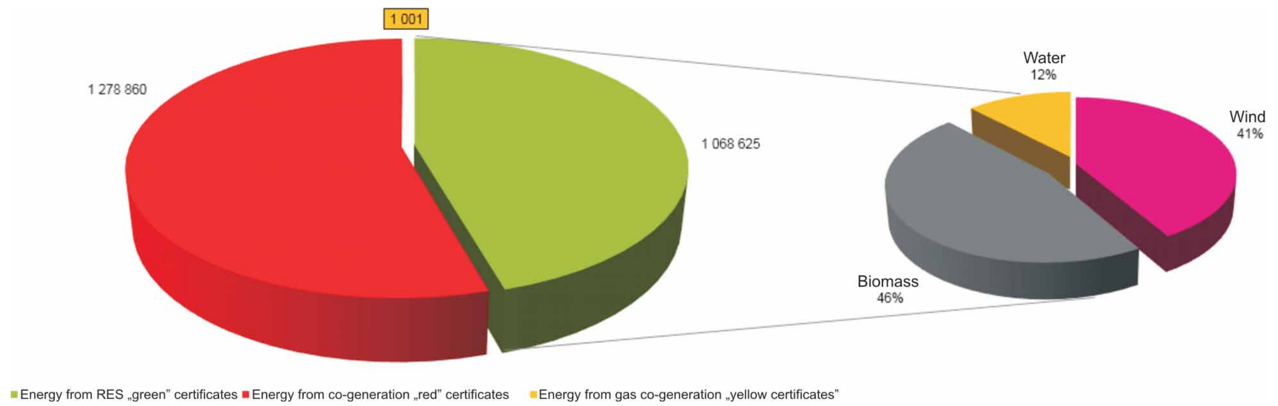


Although the core production of TAURON Capital Group is based on the traditional energy relying on solid fossil fuel, TAURON Capital Group, in its basic volume of production, includes high efficiency generation of electricity and heat in the co-generation system and supplements its offer by energy generated in renewable sources or in generation based on gas:

– 1,068,624.6 MWh, so-called “green” certificates,
– 1,278,830.2 MWh, so-called “red” certificates,
– 1,000.6 MWh, so-called “yellow” certificates.

The figure below shows certificates of origin.

Figure no. 63 Certificates of origin (MWh)



Management of by-products

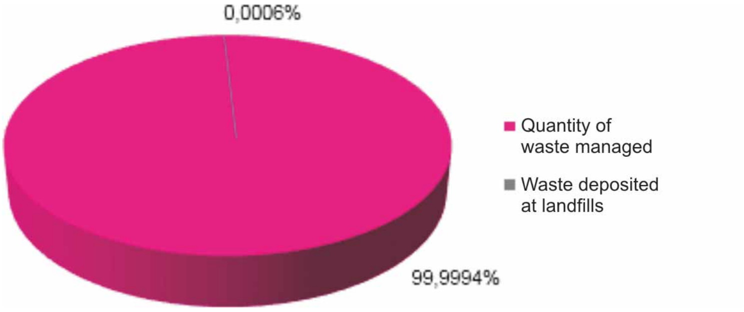
TAURON Capital Group, caring for the natural environment, minimises the quantity of waste deposited in the environment through their introduction to the market, to be used as substitutes for natural materials.

Waste generated in TAURON Capital Group is mainly used in the construction, road 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 2016 the conventional energy sector of TAURON Capital Group generated approximately 1.7 million Mg of furnace waste, including 99.9994% managed in the market and only 0.0006% deposited directly at the dumping site.

The figure below presents the structure of energy waste management.

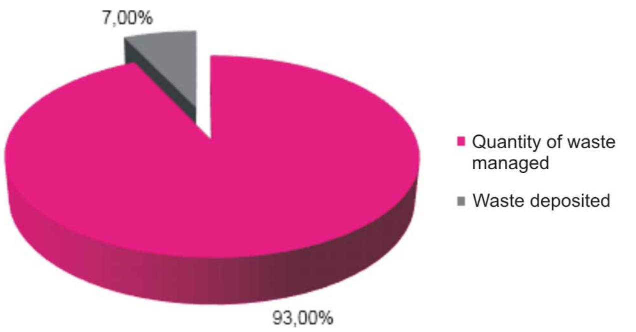
Figure no. 64 Structure of energy waste management (Mg)



In 2016, hard coal mining in TAURON Capital Group generated 1.4 million Mg of mining waste. The waste comprised aggregate and sludge originating from coal processing and preparation. 93% of the overall waste generated was economically used.

The figure below presents the structure of mining waste management.

Figure no. 65 Structure of mining waste management (Mg)



TAURON Capital Group strives to implement the model of closed circuit economy. It is planned that the maximum of generated process waste is used within TAURON Capital Group, consequently reducing the product's carbon footprint.

2.11.5. Sponsoring activity

In 2016, TAURON conducted sponsoring activity based on the applicable *Rules of conducting sponsoring activity in TAURON Polska Energia S.A. Group*, the *Research methodology for the selection, planning, analysing and reporting of sponsoring activity effectiveness*, the guidelines of the *Strategy of TAURON brand* and the *Plan of conducting sponsoring activity in TAURON Group in 2016*, adopted by the Management Board and positively reviewed by the Supervisory Board.

The main objective of the conducted activities was the support of commercial activity as well as the growth and strengthening of the knowledge and range of TAURON brand effect, assuming that TAURON brand is an important asset of TAURON Capital Group enabling to increase its value and support business objectives in an indirect way.

The sponsoring activity was carried out based on negotiated agreements, according to standardised 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 specialised 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 2016. 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 6.34. was obtained. It means that each zloty spent for that purpose generated promotional benefits to TAURON Capital

Group whose preliminary value is estimated at approximately PLN 6.34. 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 2016*, 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 active sponsor in the energy sector.

In 2016, sponsoring activity was carried out by TAURON and TAURON Sprzedaż. Both companies implemented the total of 32 projects with 26 customers. The preliminary data related to accomplished advertising equivalents referring to activities ended in 2016 indicate that the best results were achieved by activities under projects in the scope of professional sport, i.e. the agreement with the Polish Basketball League for the season 2015/2016 (inter alia, TAURON Basket Liga), Lang Team (inter alia, Tour de Pologne) and in the scope of culture, i.e. The agreement with Scorpio Studio (Jack Strong film). Among projects under implementation, such activities as sponsoring of KS VIVE TAURON Kielce demonstrated a high potential.

3. RISK MANAGEMENT IN TAURON CAPITAL GROUP

3.1. Objectives and principles of risk management

Taking care for implementation of the applicable Strategy, the Company implements the risk management process in relation to operations of TAURON Capital Group. The risk management system in TAURON Capital Group should provide for predictability of achievement of the strategic goals, including stable creation of the financial result.

In particular, the risk management system:

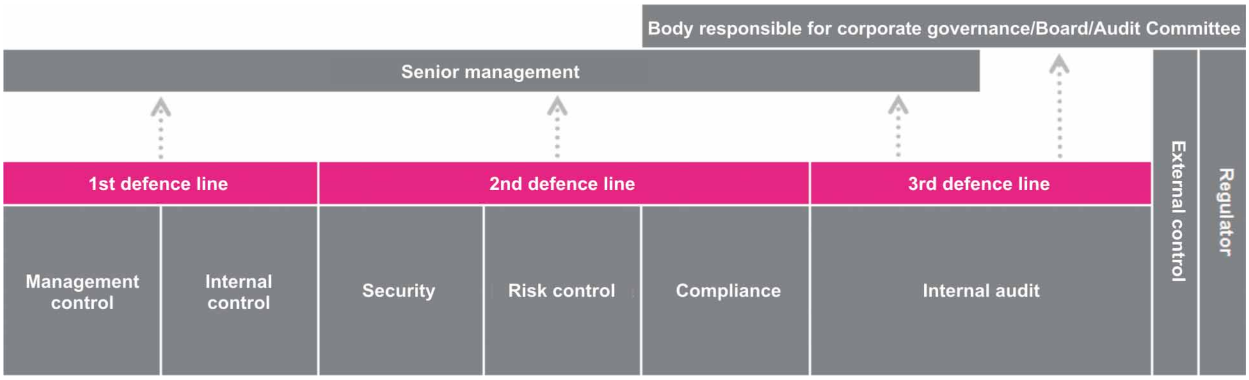
1) comprises all elements of value chain of TAURON Capital Group,
2) stipulates centralisation of the function of risk assessment, monitoring and control, ensuring consistent rules of risk management and a possibility to assess a full risk profile in the organisation,
3) is a proactive process oriented to adequately early identification of threats, allowing to undertake preventive measures,
4) is a systematic process, subject to continuous improvement in order to adjust it to the specific nature and organizational structure of TAURON Capital Group as well as the changing environment,
5) puts strong emphasis on building risk management awareness, training and encouraging employees to use knowledge on risks in their daily activities.

3.2. Risk management in the model of “three defence lines”

In order to ensure security of the organisation functioning, the model of “three defence lines” operates in TAURON Capital Group, comprising internal control, independent control within the second defence line and institutional control. In particular, the risk management function creates a system of internal control in TAURON Capital Group constituting an element of the second defence line, next to the function of ensuring the compliance and security management.

The figure below presents the model of “three defence lines”.

Figure no. 66 Model of three defence lines



Functions of individual defence lines:

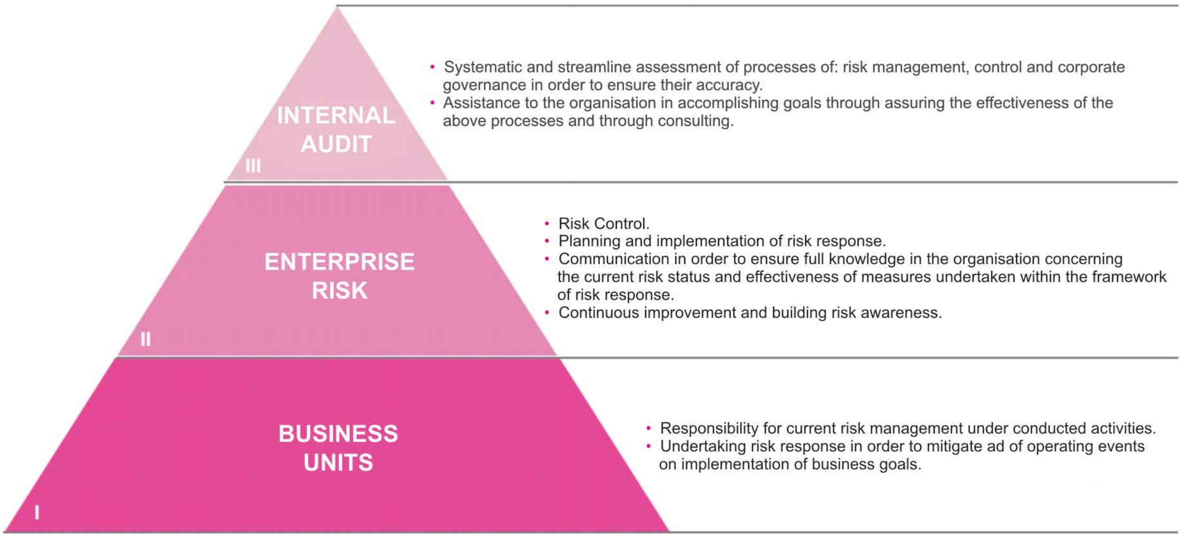
First Line of Defence is: Business units obliged to perform ongoing control embedded in implementing tasks and the functional control.

Second Line of Defence is:
- the function of risk management implemented in accordance with the adopted *Corporate risk management strategy in TAURON Group* and detailed policies related to main risk categories,
- the function of assuring the compliance understood as adjustment of the organisation to the applicable legal regulations,
- the 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 defence lines model.

The figure below presents risk management as a function of the second defence line.

Figure no. 67 Risk management as a function of the second defence line

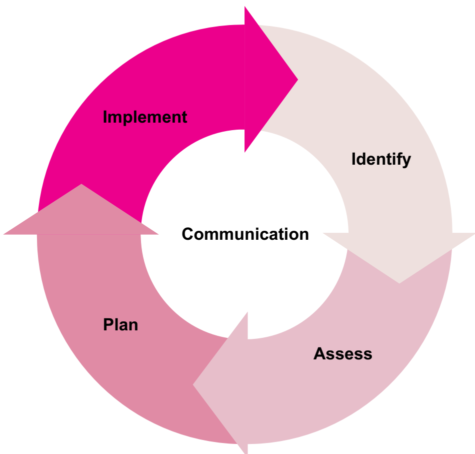


3.3. The risk management process and its participants

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 table below presents the risk management process.

Figure no. 68 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.

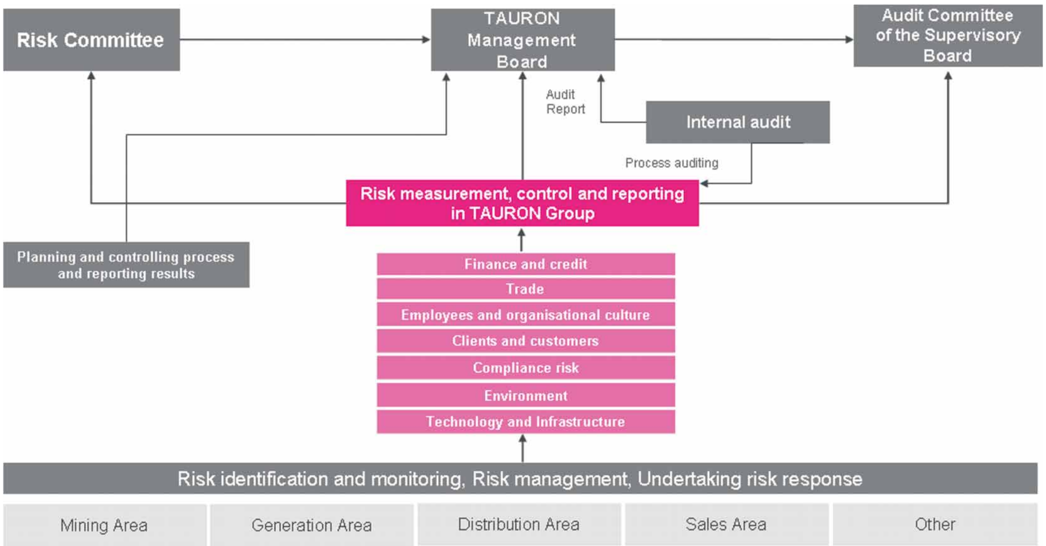
Planning – consisting in preparation of the dedicated response to the risk identified in order to achieve the desirable goals.

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 figure below presents the risk management process.

Figure no. 69 Diagram of management risk communication



3.4. Architecture of the enterprise risk management system (ERM)[1]

The enterprise risk management system (ERM) ensures the comprehensive and consistent risk management rules linked with each other in terms of methodology and information. The rules are described in the *Corporate risk management strategy in TAURON Group* and in associated policies for key risk categories.

The figure below shows the ERM system.

Figure no. 70 ERM System

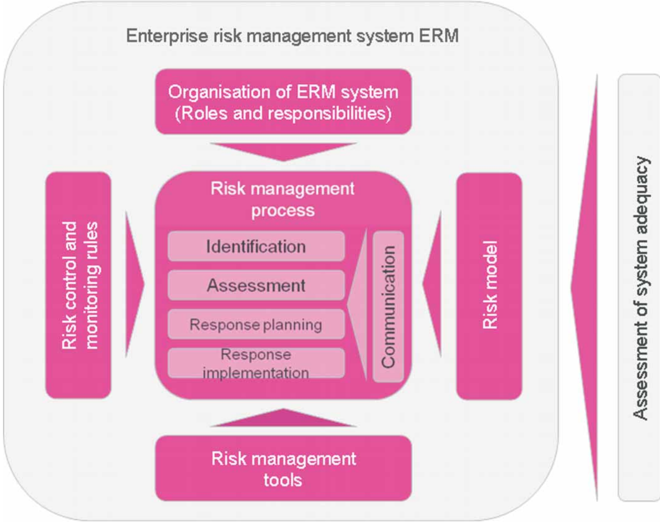
The risk management system described in detail in section 3.3 is the centre of the system. Moreover, the architecture of the ERM system comprises elements to ensure effective functioning of the process, including:

1) risk management tools,
2) risk models,
3) control and monitoring rules,
4) organisation of the ERM system.

[1] *Enterprise Risk Management*.

The figure below shows the architecture of the ERM system.

Figure no. 71 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 in 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 pf risk response.

The figure below presents the organisational structure and documentation of the risk management process.

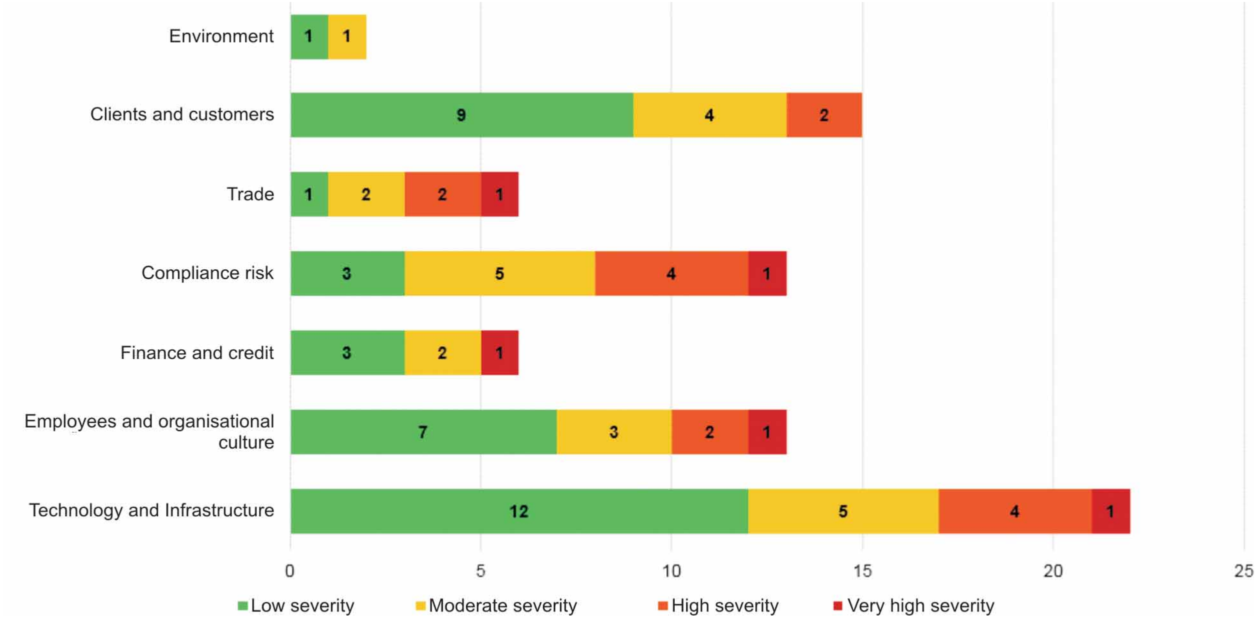
Figure no. 72 Organisational structure and documentation of the risk management process

Supervisory Board **Audit Committee**						
Management Board						
Management	**Risk Committee** Team for Commercial Risk Management Team for Financial and Credit Risk Management					**Internal audit**
Organisational Regulations/ Bylaws	**Strategy of enterprise risk management in TAURON Group**					Internal Audit regulations
	Policy of commercial risk management in TAURON Group	**Policy of operating risk management in TAURON Group**	**Policy of risk management in projects in TAURON Group**	**Policy of credit risk management in TAURON Group**	**Policy of management of risk specific in financial area in TAURON Group**	
	Market Risk Team	Corporate Risk Team		Credit Risk Team	Executive Director for Finance	Internal Audit Team
	Executive Director for Risk					Executive Director for Internal Audit
	Reporting to Supervisory Board, Management Board of TAURON, Members of Risk Committees					Reporting to the President of the Board

Risk model defines risk classification, consistent in TAURON Capital Group, enabling harmonised and complex capturing of risk across TAURON Capital Group. Each risk identified is assigned to specific categories and sub-categories.

The figure below presents the number of key risks, broken down into categories.

Figure no. 73 Number of key risks, broken down into categories



In the framework of the implementation of **risk control and monitoring rules** the Management Board of TAURON approves the risk tolerance, taking into consideration the specific nature and scope of operations of TAURON Capital Group. The level of the tolerance is determined as a value 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 specific risks, which may subsequently be allocated to operating limits within specific risk management. A supplementary tool used for risk monitoring and control comprises the system of Key Risk Indicators – KRI and Early Warning Indicators – EWI.

3.4.1. Commercial risk management

The commercial risk management in TAURON Capital Group is understood as limiting the unplanned volatility of the operating result of TAURON Capital Group, arising from volatility of prices in commodity markets and deviations of the volume in individual areas of commercial activity of TAURON Capital Group. Due to the specific nature of conducted activities, the commercial risk is one of key risks in TAURON Capital Group. TAURON Capital Group comprises companies of the Mining Area, Generation Area and Sales Area. In connection with the occurrence of opposite positions in those Areas the risk is, to a certain extent, subject to natural diversification, however, due to incomplete balancing of those Areas as well as a divergent nature of exposure, TAURON Capital Group demonstrates vulnerability to volatility of prices of electricity, gas and related products.

For the purpose of effective management of this group of risks, a commercial risk management system has been created which is associated in terms of organisation and information with the strategy of hedging the commercial position functioning at a level of TAURON Capital Group. In particular, the applicable *Commercial risk management policy in TAURON Group* introduces the early warning system and the system of limiting risk exposure in individual commercial areas. The basic operating measure of market risk in TAURON Capital Group is the measure of the value exposed to risk, i.e. Value at Risk, determining the maximum allowable change in the value of position in the applied time horizon and at a defined probability level. The Value at Risk is a dynamic risk measure which, contrary to statistical measures, demonstrates the preceding ownership allowing to determine potential adverse effects still before their actual occurrence. The risk area, however, with the awareness of certain limitations of this type of statistical measures, also uses a number of supplementary risk measures used for ensuring safe functioning of trade areas.

The organisational structure of the commercial risk management system stipulated a strict distribution of competences within which risk management is decentralised, whereas risk steering and control takes place centrally, from the level of TAURON. In particular, the element of commercial risk management structure is the division of the commercial activity of TAURON Capital Group into Front, Middle and Back Office. Such a distribution of tasks is aimed at ensuring the independence of the operating functions executed by the Front Office in relation to the risk control functions fulfilled by the Risk Area and ensures the adequate level of operational flexibility. For the needs of the risk management process such placing of responsibility is assumed that optimum approach to a certain type of threat can be guaranteed, using, in particular, the effect of scale and the synergy effect. Such approach ensures the effectiveness of commercial processes conducted and the appropriate supervision of one of major business processes conducted within TAURON Capital Group.

The figure below shows the distribution of commercial activity of TAURON Capital Group

Figure no. 74 Distribution of commercial activity of TAURON Capital Group

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

TAURON Capital Group manages financial risk, understood as currency risk and interest rate risk in accordance with the prepared and adopted regulations *Policy of risk management specific for the financial area in TAURON Group*, which is the collection of principles and standards compliant with the best practices in this area. The main goal of financial risk management is to minimise TAURON Capital Group cash flows sensitivity to financial risk factors and to reduce financial costs and collateral costs as a part of transactions with the use of derivative instruments. The indicated policy also defines the rules of hedge accounting application, including the types of cash flow collaterals and the accounting treatment of hedging instruments and items hedged, in accordance with the International Financial Reporting Standards (IFRS). In accordance with the said policy, TAURON Capital Group, in case where it is feasible and economically justified, uses derivative instruments whose characteristics enables the application of hedge accounting.

Within financial risks, TAURON Capital Group also identifies liquidity risk demonstrated as a possibility of loss or limiting the ability to settle current expenditure due to inadequate level or structure of liquid assets in relation to short-term liabilities, or inadequate level of real net inflows from operating activities. The liquidity situation of TAURON Capital Group is monitored on an on-going basis in terms of potential deviations against the assumed plans and the availability of external sources of financing whose amount significantly exceeds the expected demand in a short term mitigates the risk of losing liquidity. The implemented *Financial Liquidity Management Policy of TAURON Group* defines rules of determining a liquidity position both for individual companies and for the whole TAURON Capital Group, which enables to secure funds to cover a potential liquidity gap, both through allocation of funds among companies (the cash pool mechanism), as well as using external financing, including the overdraft.

Risk associated with financing is identified at three levels:

1) Risk of failure to raise nee 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 infringement of covenants and the necessity to repay current financing.

Within the mitigation of risk associated with financing the 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 should hold signed programmes of guaranteed financing or hedge this financing through collection of funds on TAURON 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 in the scope of acquisition of various debt instruments, also outside the Polish market.

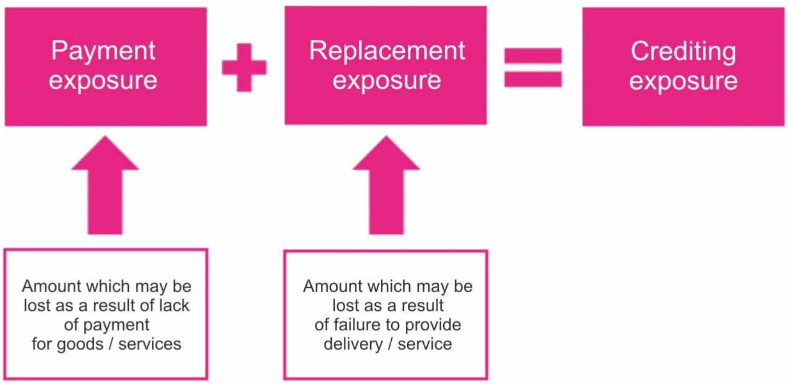
3.4.3. Credit risk management

Credit risk refers to potential losses resulting from the failure of trade partners to fulfil the contractual obligations. The commercial activity of TAURON Capital Group is exposed to credit risk – customers are evaluated from the perspective of their creditworthiness. The general rule is that the customer, prior to concluding of a contract, is subject to examination of its financial standing and receives a credit limit constituting limiting of the maximum exposure due to commercial engagement.

TAURON Capital Group has a decentralised credit risk management system, however, the control, limiting and reporting of credit risk is provided centrally, from the Company level. The applicable *Credit risk management policy in TAURON Group* defines the set of principles and rules in the scope of credit risk management at a level of TAURON Capital Group, to result in effective mitigation of credit risk impact on the implementation of the TAURON Group objectives. Credit risk management results from controlling of the level of credit risk exposure generated upon concluding of a contract with customers by companies of TAURON Capital Group. Risk exposure is understood as the amount that may be lost if a customer fails to fulfil its obligations within the specific period of time (considering the value of collaterals contributed by the customer). Credit exposure is calculated for the current day and divided into exposure due to payment and exposure of replacement.

The figure below shows the components of credit exposure.

Figure no. 75 Components of credit exposure



The value of credit risk to which TAURON Capital Group is exposed is monitored using the Value at Risk method, with the application of the Credit Risk Plus model. It is an analytical method which, through the Monte Carlo simulation, calculates the value at risk based in distribution of probability of total loss, determined based on credit exposure and financial standing of clients.

3.4.4. Operating risk management

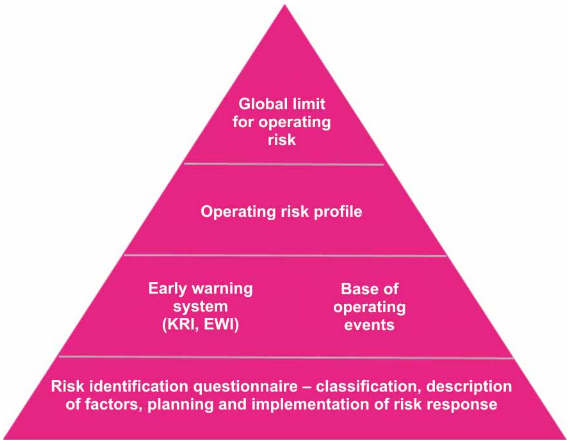
Operating risk is understood as a possibility to incur a loss due to inadequate or unreliable internal procedures, human error and system failure, or external events, also comprising legal risk, reputation risk and risk of non-compliance. Operating risk, due to the specific nature of threats and possibilities to manage it, constitutes a separate risk group occurring in activities of TAURON Capital Group. The said risk is a complex phenomenon, it occurs in each process and type of activity, it is multidimensional and relates to various types of activities and operations. The level of operating risk is associated with the level and complexity of organizational structure, number and complexity of IT systems and the number of conducted business processes. Operating risk demonstrates the lack of possibility of total elimination of its sources and the analysis of its factors and parameters (inter alia, frequency and severity) as well as their assessment requires complex methods of analysis and measurement.

In TAURON Capital Group a set of rules of operation and procedures has been defined with the purpose of minimisation of risk effects arising from operating risk. Those rules cover all elements of the value chain of TAURON Capital Group and all the employees of TAURON Capital Group take part in the risk management process. Each unit in the organisational structure assuming operating risk is responsible for active management of its operating risk under the activity implemented.

With the aim of effective implementation of the operating risk management process, TAURON Capital Group uses tools, including, inter alia, the operating risk profile, the base of operating events, the global limit of operating risk and the associated system of operating limits, including the early warning system.

The figure below presents the tools of the risk management process.

Figure no. 76 Tools of the risk management process



Global limit for operating risk is the basic tool of operating risk control constituting the allocation of risk tolerance adopted in TAURON Capital Group. The global limit for operating risk may be subsequently allocated to individual activity areas of TAURON Capital Group, subcategories of operating risk as well as to individual operating risks.

Operating risk profile is aimed at identification of areas, processes or activities excessively exposed to threats arising from individual operating risk factors. The operating risk profile is expressed, in particular, in the structural dimension comprising types of operating events, organisational structure of TAURON Capital Group and processes, in the dimension of scale comprising estimated potential losses, taking into account, in particular, historic values of real losses as well as tools used in order to mitigate threats. For the needs of operating risk measurement and defining the operating risk profile, individual types of operating risk are divided (due to the nature of their occurrence) into continuous and one-off risks.

Early warning system is defined in order to monitor operating risk level for each identified threat. From the set of Key Risk Indicators – KRI, Early Warning Indicators – EWI, are separated, subject to permanent control in terms of prudential thresholds determined for them, i.e. the threshold of acceptance, mitigation and escalation.

Base of operating events is created for the needs of identification of new risk factors in order to determine risk profile in TAURON Capital Group. It allows for recording of cases demonstrating the potential or real loss for the organisation. The objective of maintaining the base of operating events is to determine the frequency and the severity of individual operating risk factors as well as areas and processes in which they occur.

3.4.5. Risk Management in projects

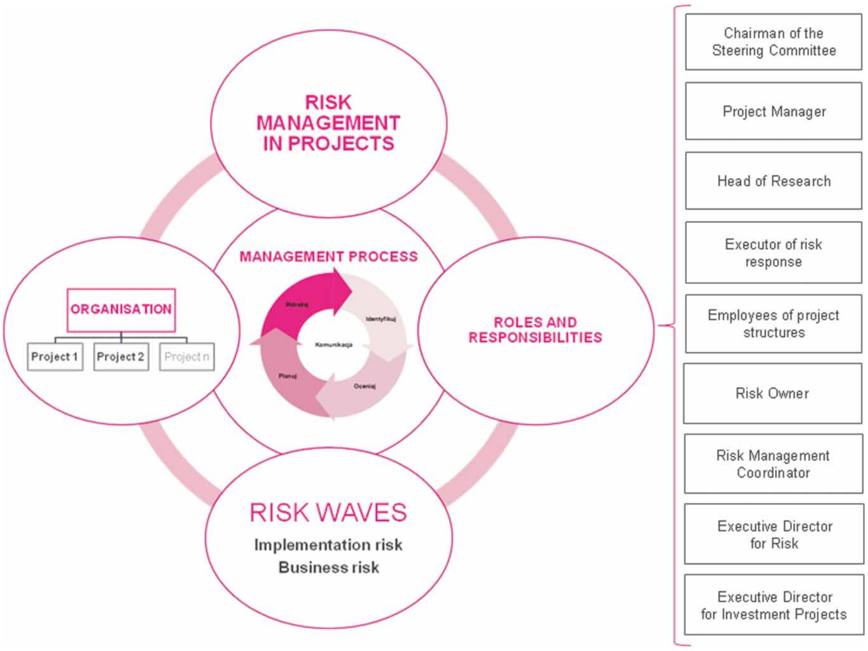
Risk management in projects supports the implementation of strategic goals of TAURON Capital Group owing to systematic application of the provisions of the applicable *Policy of Risk Management in Projects in TAURON Group*. This regulation defines the basic rules of risk management in projects, ensuring the consistency in their application, completeness of the approach and explicit understanding. The objective of the activities undertaken is to achieve the required probability of project implementation maintaining the defined schedule, budget and quality of received products. The overriding objective is to gain the expected benefits arising from project implementation.

Risk management in projects refers to any types of risk associated with planning and implementation of projects and each referred project structure undertaking risk is responsible for active management of this risk under the project implemented.

Moreover, in order to ensure effective risk management in projects in TAURON Capital Group, the requirements of the complex ERM system were introduced into this area.

The figure below presents the model of risk management in projects.

Figure no. 77 Risk Management in projects



3.5. Description of the most significant risks associated with the operations of TAURON Capital Group

The table below presents the most significant risks identified for TAURON Capital Group.

Table no 21. The most significant risks identified for TAURON Capital Group

No.	Risk Name	Risk description	Risk trend	Risk response
Finance and credit				
1.	Risk of market factors	Risk connected with unfavourable impact of interest rates and currency exchange rates on the financial result of TAURON Capital Group.	↘	• Current monitoring of the level of exposure to risk in order to mitigate adverse effects of changes in market factors. • Risk transfer through the use of derivatives.
2.	Risk of liquidity / financing	Risk associated with the method of financing the activity arising from the structure of capital in the enterprise.	→	• Diversification of financing sources including the arrangement of guaranteed financing programmes and ensuring alternative financing sources. • Implementation of the central financing policy. • Analysis of the market and availability of financing sources. • Monitoring of schedules and deadlines of announcement of the financing programme.
3.	Credit risk	Risk associated with a possibility of occurrence of overdue receivables or concluding of a contract with a customer which may turn out insolvent.	→	• Regular monitoring of the financial standing of customers. • Cyclical clients' scoring, credit rating of each client prior to the submission of the offer/concluding of the contract. • Application of hedges in commercial agreements.
Trade				
4.	Risk of goods prices	Risk associated with the unfavourable change in prices in the energy market and markets of related products exerting adverse impact on the financial result of the Group.	↗	• Monitoring and updating of hedging strategy. • Current monitoring of the level of exposure to risk in order to mitigate adverse effects of changes in market factors. • Limiting of trade positions within risk mandates.

No.	Risk Name	Risk description	Risk trend	Risk response
Employees and organisational culture				
5.	Risk of employees	Risk connected with the infringement of the binding legal regulations, rules, procedures and internal regulations applicable in TAURON Capital Group. The risk also comprises the issue of errors and negligence of employees as well as a possibility of class actions and employee claims as well as loss of specialised staff.	→	• Undertaking measures aimed at developing the model strengthening employee motivation. • Development of competence through employee training. • Application of binding internal instructions and regulations.
Clients and customers				
6.	Risk of customer service	Risk associated with failure to comply with the customer service standards.	↘	• Monitoring and analysis of external client satisfaction indicators and indicators related to complaints. • Undertaking additional measures, e.g. in the area of internal regulations defining the standards of procedure as a result of indicator analysis. • Development of competence and skills of key account managers. • Continuous raising of customer service standards.
7.	Risk of contract implementation by subcontractors	Risk associated with undue fulfilment of assigned work by subcontractors, rescinding of the agreement and associated delays, changes in budget, scope.	→	• Concluding agreements with subcontractors compliant with the standards of TAURON Capital Group. • Analysis of the subject matter of the agreement, examining the quality of services performed by subcontractors. • Evaluation of financial standing and reliability of subcontractors.
8.	Risk of volume	Unfavourable changes or termination of commercial agreements by clients, leading to the decline in revenue from conducted activity.	→	• Conducting marketing activities, acquiring new clients. • Conducting activities focusing on maintaining the existing clients and recovery of lost clients. • Current product updating, introduction of multipackage type of product into sale.
Compliance risk				
9.	Risk of internal fraud	Misappropriation or temporal use of elements of the company assets, destruction of TAURON Capital Group assets, abuse of official position to acquire various types of personal benefits through enforcing specific client behaviour while performing official duties.	→	• Strict application of internal procedures aimed at securing against abuse (security procedures, reviews of authorisations). • Conducting compliance-oriented measures. • Promoting best practice, improvement of procedures, training. • Enforcement and promoting of the provisions of the *Code of Business Ethics of TAURON Group*.
10.	Risk of external fraud	Actions of third persons aimed at, inter alia, theft, robbery, physical burglary, computer crime, theft of information, counterfeiting.	→	• Monitoring of potential and real incidents associated with security. • Anti-virus protection at workstations. • Physical security of facilities. • Performing security tests.
11.	Risk of concessions	Lack of possibilities to carry out activity as a result of prolonged process of concession acquisition or obtaining changes of concessions held. Unfavourable legal amendments the regulating licensed activity.	→	• Current control of appropriate fulfilment of concessional obligations. • Monitoring of amendments to legal acts in terms of concessional obligations. • Legal support to the process associated with extension of concession.
12.	Risk of failure to comply with the legal regulations	Risk associated with the failure to comply with the legal regulations, wrong interpretation of new provisions and regulations, requirements imposed by ERO / UOKiK / KNF / GIODO etc.	→	• Permanent monitoring of the legal environment and changes in legal regulations. • Implementation of required amendments to internal regulations. • Establishment of working groups aimed at preparation and implementation of required amendments arising from the legal environment. • Permanent cooperation with authorities supervising the energy market and the capital market. • Training of employees related to introduced amendments.

No.	Risk Name	Risk description	Risk trend	Risk response
Environment				
13.	Risk of reputation	Current and future impact on incomes and capital of the company arising from the negative assessment of public opinion.	→	• Permanent monitoring internal and external threats of the Company. • Monitoring of media, building relations with media within TAURON Capital Group. • Preparation of communication procedures of the Company with the external and internal environment.
14.	Risk of competition	Unfavourable impact of competition activities on clients and financial results of TAURON Capital Group.	↗	• Launching product lines dedicated for clients. • Launching sales of additional products for current loyal customers. • Introduction of a possibility to combine TAURON products into multi-offers.
15.	Regulatory risk	Unfavourable impact of legislation at the national and European level arising from, the necessity to adopt or adjust to legal regulations and incur required financial costs in order to comply with them.	↗	• Permanent monitoring of the legal environment and changes in legal regulations. • Analysis of draft legal acts and planning required adjustment activities. • Implementation of required amendments to internal regulations.
Technology and Infrastructure				
16.	Environmental risk	Potential adverse effect of activity on the environment and adjustment and compliance with the environmental requirements of the national and Community law.	→	• Current oversight of compliance with environmental decisions. • Maintaining a required level of efficiency of pollution abatement equipment. • Performing frequent assessment of compliance of activities with the legal requirements in the scope of environmental protection. • Implementation of investments in the scope of environmental protection in order to mitigate effects of unfavourable impacts of conducted mining and processing activity.
17.	Risk of weather	Impact of atmospheric factors in functioning of the enterprises, both in technological and commercial terms.	→	• Modernisation of water structures aimed at optimisation of the method to use water resources. • Preparation of renovation plans, overhauls and service with flexible provisions concerning the deadlines of performing the works. • Permanent monitoring of the wind conditions and icing of wind turbine blades. • Permanent technical oversight of the operation of individual wind turbines conducted by companies operating wind farms. • Monitoring and analysis of new technological solutions limiting the impact of unfavourable weather conditions on the level of electricity produced.
18.	Risk of assets failure	Impact of failure of machines and equipment, repairs, modernisation, maintenance and management of production and non-production assets for the company needs.	→	• Optimisation of capex for assets replacement, active monitoring of the condition of machines, equipment and installations. • Upgrading professional qualifications and work culture of employees through organising courses and training activities. • Responding to emergency situation through technical service and protective automation. • Insuring assets against force majeure events (excluding underground). • Introduction of IT tools in the area of improvement of monitoring and management of failure indicators.
19.	IT Risk	Risk associated with security of IT infrastructure, failures of IT infrastructure.	↗	• Elaboration and maintaining plans of IT continuity assurance. • Periodical identification and categorisation of IT resources based on goals related to recovery of services. • Application of IT solutions with the adequate technical parameters, ensuring the acceptable level of reliability and operating efficiency (including UPS devices, GSM modem, mobile phones). • Planning and conducting of training in the scope of IT continuity and security. • Storage and protection of backup data.

No.	Risk Name	Risk description	Risk trend	Risk response
20.	Security risk	Risk connected with the violation of integrity of machines and equipment and security of information comprising its inappropriate processing and unauthorised disclosure.	→	• Monitoring of implementation of developed plans of protecting facilities subject to mandatory security. • Maintaining and updating of contingency plans/procedures. • Supervision of compliance with the binding information protection rules. • Regular employee training in the scope of applicable security procedures.
21.	Geological risk	Impact of geological factors on mining activities.	→	• Performing control openings for better identification of coal deposits. • Continuation of preventive measures in areas at risk for the improvement of geological and mining conditions and protection against natural disasters (including, inter alia, preliminary shooting in order to decompress the rock mass).

4. ANALYSIS OF FINANCIAL AND ECONOMIC SITUATION OF TAURON CAPITAL GROUP

4.1. Overview of economic and financial values disclosed in the consolidated annual financial statement

Consolidated statement of financial standing

The table below presents the annual consolidated statement of financial situation – **assets**.

Table no 22. Annual consolidated statement of financial standing – assets (significant items)*

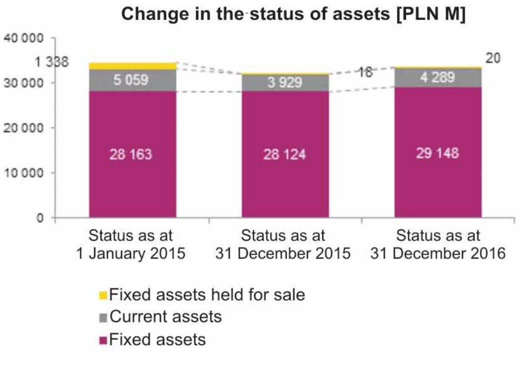
Statement of financial standing (PLN thous.)	Status as at 31 December 2016	Status as at 31 December 2015	Status as at 1 January 2015	Dynamics (2016/2015)
ASSETS				
Fixed assets	**29,148,253**	**28,124,185**	**28,162,749**	**103.6%**
Tangible fixed assets	26,355,189	24,882,817	24,850,942	105.9%
Current assets	**4,308,641**	**3,947,248**	**6,396,444**	**109.2%**
Cash and equivalents	384,881	364,912	1,420,909	105.5%
Fixed assets and assets of TAURON Capital Group for disposal, classified as held for trade	19,612	17,898	1,337,705	109.6%
TOTAL ASSETS	**33,456,894**	**32,071,433**	**34,559,193**	**104.3%**

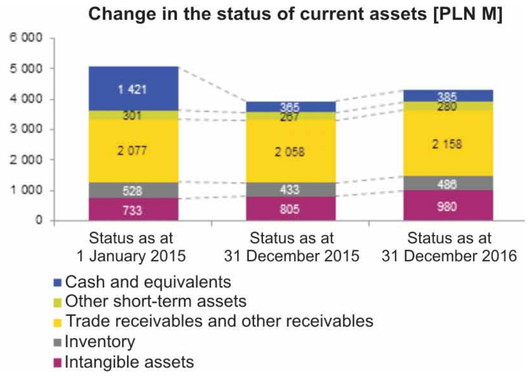
** Due to the limited comparability of earlier periods, data are presented in a three-year horizon. Data comprising earlier periods are presented in section no. 4.6 of this report.*

As of 31 December 2016 the statement on financial situation of TAURON Capital Group indicates balance sheet total assets higher by o 4.3%.

The figure below shows the change in the status of assets and current assets.

Figure no. 78 Change in the status of assets and current assets





In the year ended on 31 December 2016, TAURON Capital Group, having considered the following premises:

1) long-term maintaining of the market value of Company net assets at a level below the carrying amount,
2) decline in prices of certificates of origin for energy from renewable sources,
3) introduction of new regulations in the RES Area,
4) continuing unfavourable market conditions in terms of profitability of coal-based power industry,
5) increase in risk-free rate,

recognised impairment write-offs and the reversal of previously created tangible fixed assets as a result of impairment test of assets, conducted as at 31 December 2016 and 30 June 2016. Results of the conducted tests indicated that a part of assets of the Generation Segment should be covered by an additional write-off in the amount of PLN 1,942.9 thousand. The conducted test has also confirmed the legitimacy to reverse the write-offs in this Segment in the amount of PLN 1,208.2 million.

The sensitivity analysis for individual entities generating cash flows indicated that the factors most significantly influencing the useful value of the assets tested are related to:

1) the capacity market,
2) change in electricity price,
3) change in hard coal prices,
4) change in the average weighted cost of capital.

The change in the price of CO_2 emission allowances and property rights from RES have a lower impact on the valuation.

Despite the application of impairment losses, the value of tangible fixed assets increased by PLN 1,024 million (3.6%), which is the resultant of the following events:

1) growth in the value of tangible fixed assets as a result of investments in tangible fixed assets ongoing in companies of TAURON Capital Group (mainly in TAURON Wytwarzanie, TAURON Dystrybucja and TAURON Ciepło) and intangible assets (mainly TAURON Dystrybucja and TAURON Obsługa Klienta),
2) reclassification of property rights and greenhouse gases emission allowances acquired in previous years to current assets, in connection with the requirement to fulfil the legal obligation of their redemption.

The following factors had an impact on the growth in the value of current assets by approximately PLN 361 million (9.2%):

1) growth in the value of certificates of origin of electricity and greenhouse gas emission allowances – CO_2 by 21.7% as a result of acquisition in 2016 and reclassification from the long-term part of emission rights in connection with the statutory requirement to submit them for redemption to the relevant public administration authorities (in 2017, due to the fulfilment of the redemption obligation for 2016). In 2016 due to the decline in prices the value of certificates of origin is lower by 14.7%,
2) The growth in the value of inventory by 12.2% is the effect of acquisition of CO_2 emission allowances by TAURON Capital Group, with the intention of their resale, which did not take place in 2015,
3) growth in the value of other financial assets by 176% mainly due to the growth in the fair value in relation to derivative instruments,
4) insignificant growth in receivables from consumers by PLN 64 million, additionally strengthened by the growth of tax receivables by PLN 35.5 million (growth in the share of receivables due to income tax, with the decline in receivables due to VAT).

The table below presents the annual consolidated statement on financial situation – **liabilities**.

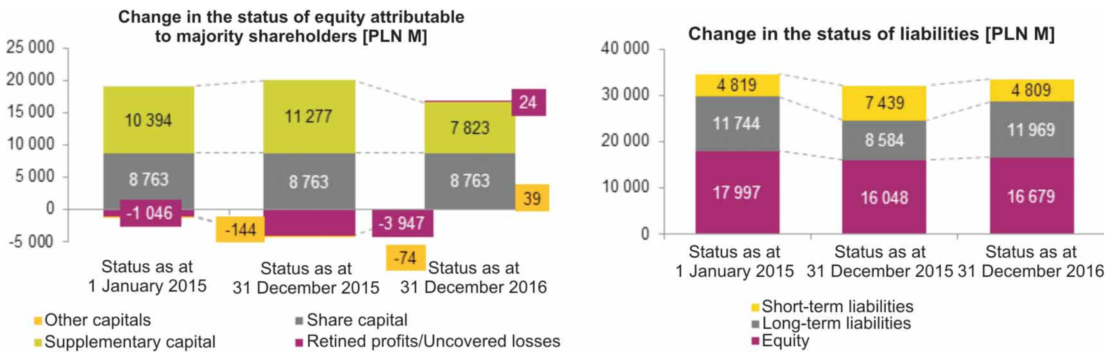
Table no 23. Annual consolidated statement of financial standing – liabilities (significant items)*

Statement of financial standing (PLN thous.)	Status as at 31 December 2016	Status as at 31 December 2015	Status as at 1 January 2015	Dynamics (2016/2015)
LIABILITIES				
Equity attributable to shareholders of the parent entity	**16,649,266**	**16,018,328**	**17,966,448**	**103.9%**
Non-controlling shares	30,052	29,829	30,116	100.7%
Long-term liabilities	**11,968,719**	**8,583,950**	**11,744,092**	**139.4%**
Loans, credits and debt securities	8,759,789	4,924,127	7,468,775	177.9%
Short-term liabilities	**4,808,857**	**7,439,326**	**4,818,537**	**64.6%**
Current portion of interest-bearing credits, loans and debt securities	219,740	3,214,520	644,991	6.8%
TOTAL LIABILITIES	**33,456,894**	**32,071,433**	**34,559,193**	**104.3%**

** 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 figure below shows the change in the status of liabilities and equity.

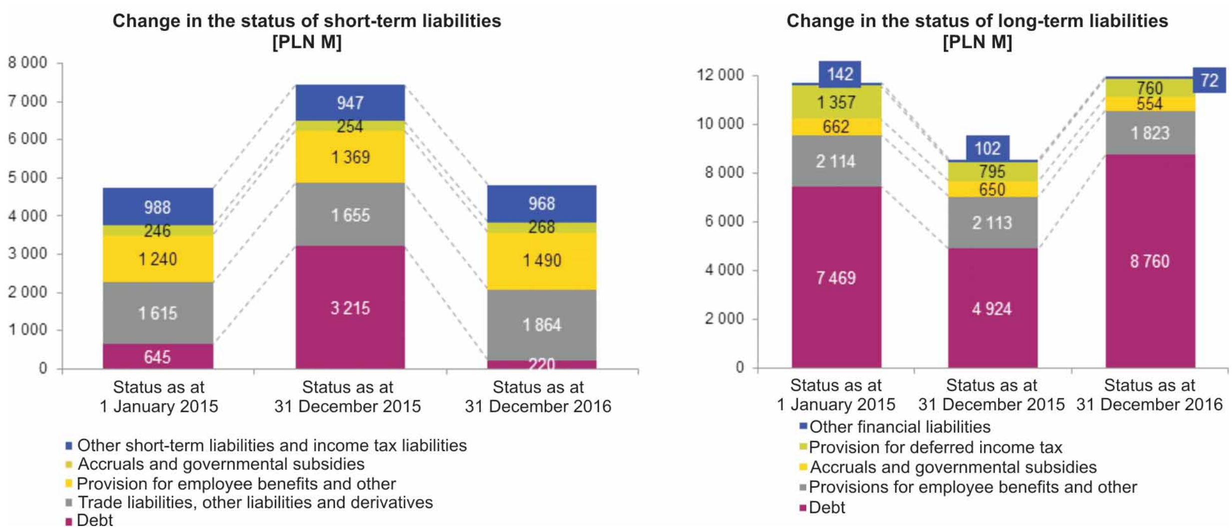
Figure no. 79 Change in the status of liabilities and equity



Similar to the previous years, in 2016 the dominating source of assets financing was equity whose share in the total liabilities amounted to 49.9%.

The figure below shows the change in the status of liabilities.

Figure no. 80 Change in the status of liabilities



The following factors had an impact on the growth in the value of long-term liabilities by approximately PLN 3,385 million (39.4%):

1) Growth in liabilities due to debt by 77.9% as a result of issue of bonds with the nominal value of PLN 4,285 million in the reporting period,
2) Decline in the value of provisions for employee benefits by 20.9% as a result of changes in the Company Collective Bargaining Agreements, mainly in companies of the Distribution Segment, change in the retirement age in all companies, arising from the amendment to the law and change in actuarial assumptions,
3) Growth in the value of provisions for costs of dismantling of tangible fixed assets and area reclamation by 19.1%, which is associated with recognising the provision for liquidation of mining plants in connection with the acquisition of ZG Brzeszcze.

The value of short-term liabilities of TAURON Capital Group decreased by PLN 2,630 million (35.4%), which resulted from the following factors:

1) Redemption of bonds with the nominal value of PLN 3,300 million during 2016,
2) Growth in the value of investment liabilities by 34.8% and liabilities towards suppliers – a growth of 4.9%,
3) A decline of the value of provisions by 5.2%, which is the resultant of a lower value of provision due to presentation of certificates of electricity origin as a result of the decline in prices of property rights and the growth in the value of provision for a liability due to emission of gases covered by the CO_2 emission allowances systems in connection with emission level exceeded by installations of the Generation Segment over the number of free allowances,
4) Growth by 105.8% in other provisions as a result of creation of the provision for the return of the subsidies, court disputes and customers' claims.

Consolidated statement of comprehensive income

The table below presents the annual consolidated statement of comprehensive income. Due to the changes in Segments and in order to maintain the comparability, the results are presented for three years.

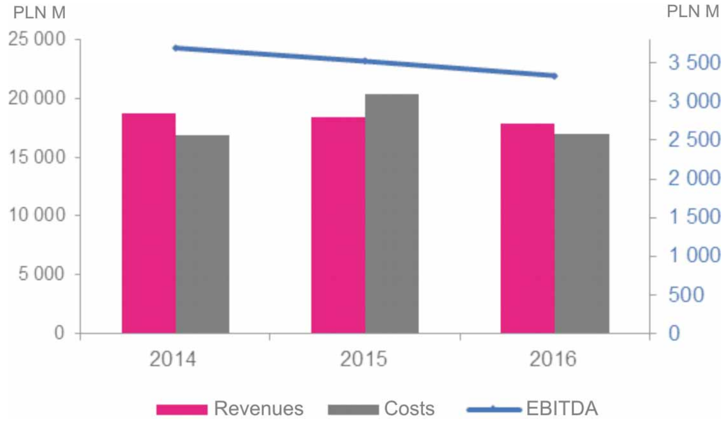
Table no 24. Annual statement of comprehensive income for 2014–2016*

Statement of comprehensive income (PLN thous.)	2016	2015	2014	Dynamics (2016/2015)
Revenues on sales	**17,646,489**	**18,264,440**	**18,577,479**	96.6%
Own cost of sales (including sales costs and overheads)	(16,829,480)	(20,137,894)	(16,862,130)	83.6%
Other operating revenues and costs	(15,487)	(27,762)	114,764	55.8%
Operating profit (loss)	**801,522**	**(1,901,216)**	**1,830,113**	**–**
Operating profit margin (%)	*4.5%*	*(10.4)%*	*9.9%*	–
Financial revenues	65,279	73,185	85,906	89.2%
Financial expenses	(417,980)	(367,673)	(416,868)	113.7%
Share in the profit (loss) of joint venture	60,040	7,933	(936)	756.8%
Gross profit (loss)	**508,861**	**(2,187,771)**	**1,498,215**	–
Gross profit margin (%)	*2.9%*	*(12.0)%*	*8.1%*	–
Income Tax	(138,724)	383,556	(312,655)	–
Net profit (loss) for financial year	**370,137**	**(1,804,215)**	**1,185,560**	–
Net profit margin (%)	*2.1%*	*(9.9)%*	*6.4%*	–
Other comprehensive income for financial year including tax	277,748	122,076	(290,384)	227.5%
Total income for financial year	**647,885**	**(1,682,139)**	**895,176**	–
Profit attributable to:				
Shareholders of the parent entity	**367,468**	**(1,807,317)**	**1,180,893**	–
Non-controlling shares	2,669	3,102	4,667	86.0%
EBIT and EBITDA				
EBIT	**801,522**	**(1,901,216)**	**1,830,113**	–
EBITDA	**3,336,814**	**3,523,228**	**3,694,544**	94.7%

** 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 figure below presents the financial results of TAURON Capital Group for 2014–2016.

Figure no. 81 Financial results of TAURON Capital Group for 2014–2016



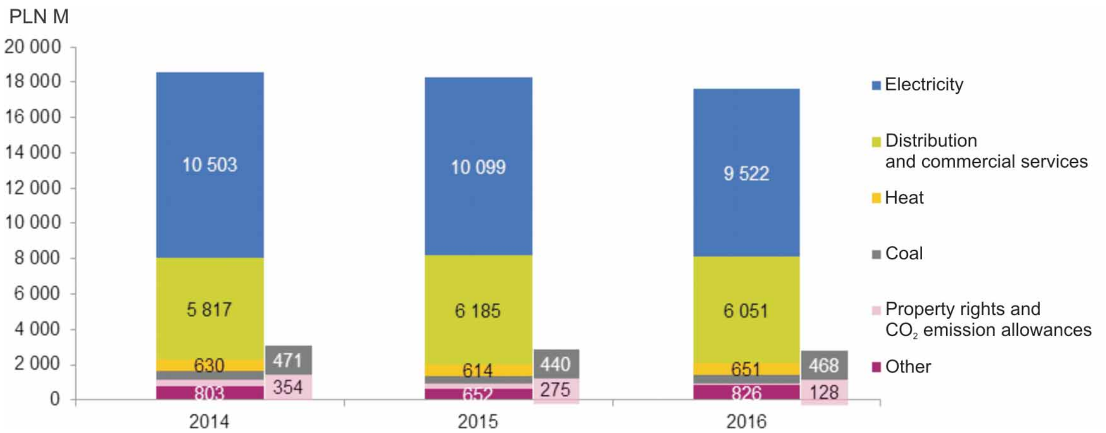
In the reporting period ended on 31 December 2016, TAURON Capital Group gained revenues on sales lower by 3.4% as compared to the values achieved in 2015, due to lower revenue on sales of:

1) electricity – a lower volume of retail sales (by 10.8%), partly set off by the growth in the volume of sales on the wholesale market (by 3.5%),
2) distribution service – a rate for distribution services delivered to end consumers lower by 2.9% and lower revenues on connecting fees,
3) certificates of origin – a decline in prices and volume.

The aforementioned declines were partly compensated through gaining higher revenues on gas sales (increase in the volume as a result of acquisition of new clients), heat energy (higher volume and prices), coal (higher volume of sales) and ORM. Moreover, as of 1 January 2016 TAURON Capital Group has been gaining revenues from the Intervention Cold Power Reserve.

The figure below presents the structure of revenues of TAURON Capital Group in the years 2014–2016.

Figure no. 82 Structure of revenues of TAURON Capital Group in 2014–2016*



** 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.*

As compared to 2015 TAURON Capital Group gained higher revenues on sales only in the Mining Segment, which results from the acquisition of ZG Brzeszcze in 2016 and sales of a higher volume of coal.

The highest decline in revenue on sales was recorded in companies of the Generation Segment (by 19.0% and the Sales Segment (by 11.7%) – as a result of generating lower revenue on sales of electricity.

The dynamics of revenues from sales of products outside TAURON Capital Group was as follows: Mining (107.2%), Generation (110.3%), Distribution (103.1%), Sales (92.2%) and Other (97.7%).

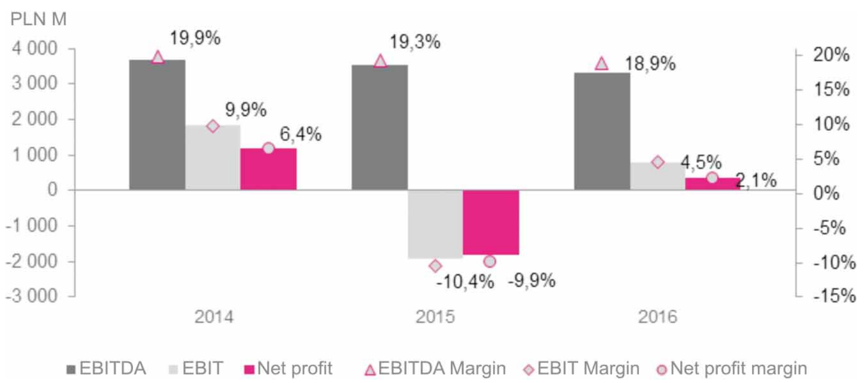
In the reporting period ended on 31 December 2016 costs of activity of TAURON Capital Group amounted to PLN 16.8 billion, which means that their level was lower by 16.4% than costs incurred in 2015. The above difference results from recognition and reversal of write-offs on tangible fixed assets at a level significantly lower than the write-off created in the year ended on 31 December 2015.

Should the aforementioned one-off events be disregarded in the results, the level of TAURON Capital Group costs in 2016 would be lower than costs incurred in the corresponding period of 2015 by over 3.3%, which results from the following factors:

1. commencement of activity of the new company, ZG Brzeszcze in the Mining Segment as of 1 January 2016, which affected the growth in operating costs YoY,
2. decline in the consumption of materials and energy, in connection with lower prices of fuel purchase and lower electricity production,
3. growth in costs of taxes and fees, which is associated with higher costs of CO_2 reserve as a result of a higher deficit of free CO_2 emission allowances in relation to CO_2 emission YoY and higher costs of term CO_2 contracting YoY,
4. growth in costs of distribution services, mainly as a result of higher purchase costs of transmission services due to a higher rate of the qualitative fee applied to higher electricity consumption, and the RES fee introduced as of July 2016,
5. lower costs of electricity sold resulting from a lower volume,
6. lower costs of amortisation and depreciation – the effect of write-offs due to the impairment in the value of tangible fixed assets and intangible assets applied as at 31 December 2015 and 30 June 2016,
7. accomplishment of commercial coal sales below the volume of coal produced, which did not take place in the corresponding period of the previous year. In 2015 TAURON Capital Group carried out sales of coal from reserves, which resulted from limited production as a result of geological and mining disturbances and deterioration in the qualitative parameters of the dredging spoils.

The figure below shows the financial result of TAURON Capital Group and the level of accomplished margins.

Figure no. 83 Financial results of TAURON Capital Group and the level of accomplished margins in 2014–2016*



** 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 2016 TAURON Capital Group achieved the EBITDA result at a level lower than in 2015 and the EBITDA margin reached a level lower by 0.4%. As a result of creation in 2015 and creation and reversal in 2016 of the impairment write-off in TAURON Capital Group due to the permanent loss in value of some assets of the Generation Segment, a significant change is visible between the EBIT result, gross profit and net profit. Should the effects of the impairment write-off be disregarded, the EBIT margin would be lower by 4.6%, and net profit – by 7.2%. In the reporting period the EBIT margin would amount to 9%, as compared to 9.1% in the previous year, whereas the net profit margin would reach 5.9% and 6.1%, respectively.

In accordance with the presented consolidated statement of comprehensive income, the total comprehensive income of TAURON Capital Group, taking into account the net profit increased or decreased by the change in value of hedging instruments, currency translation differences arising from conversion of a foreign entity and other revenues after tax, amounted to PLN 647.9 million in 2016, as compared to PLN (1,682.1) million generated in the corresponding period of 2015.

The total income attributable to shareholders of the parent entity reached about PLN 644.9 million, as compared to PLN (1,685.3) million gained in 2015, and the net profit attributable to shareholders of the parent entity reached PLN 367.5 million, as compared to PLN (1,807.3) million gained in the same period of the previous year.

Statement of Cash Flows

The table below presents the statement of cash flows.

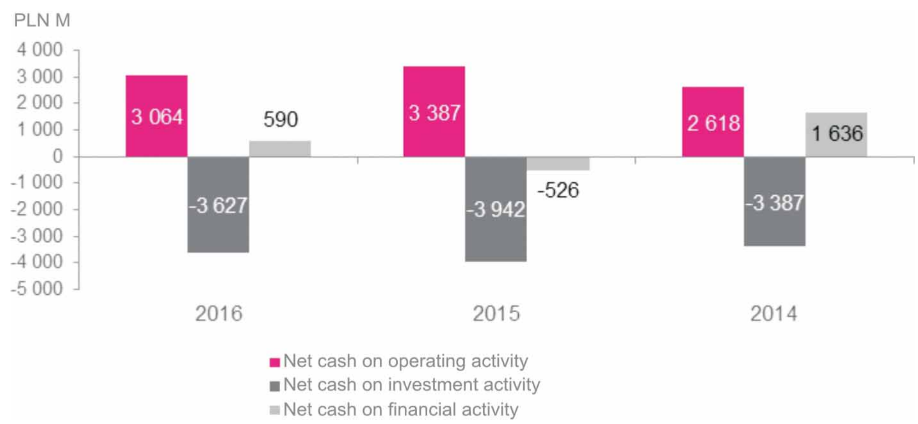
Table no 25. Statement of Cash Flows (significant items) in 2014–2016

Statement of Cash Flows (PLN thous.)	Year ended 31.12.2016	Year ended 31.12.2015	Year ended 31.12.2014	Dynamics (2016/2015)
Cash flows from operating activities				
Gross profit/(loss)	508,861	(2,187,771)	1,498,215	–
Adjustments	2,555,354	5,575,229	1,119,692	45.8%
Net cash from operating activities	**3,064,215**	**3,387,458**	**2,617,907**	90.5%
Cash flows from investment activity				
Purchase of tangible fixed assets and intangible assets	(3,516,296)	(3,973,510)	(3,464,578)	88.5%
Net cash from investment activities	**(3,627,458)**	**(3,942,122)**	**(3,386,733)**	92.0%
Cash flows from financial activities				
Cash inflows due to loans/credits	914	295,000	0	0.3%
Repayment of loans/credits	(140,331)	(140,585)	(169,971)	99.8%
Issue of debt securities	4,284,607	310,000	3,653,234	1382.1%
Redemption of debt securities	(3,300,000)	(450,000)	(1,148,200)	733.3%
Dividends paid to shareholders of the parent company	0	(262,882)	(332,984)	0.0%
Net cash from financial activities	**590,261**	**(525,692)**	**1,635,749**	–
Increase/(decrease) in net cash and equivalents	**27,018**	**(1,080,356)**	**866,923**	–
Cash opening balance	**327,715**	**1,408,071**	**541,148**	23.3%
Cash closing balance	**354,733**	**327,715**	**1,408,071**	108.2%

** 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 figure below presents the cash flows in the years 2016–2014.

Figure no. 84 Cash flows in 2016–2014



The accomplished positive value of cash flows on operating activities in 2016 was lower than the stream of cash accomplished in the previous year by approximately PLN 323 million. The following factors had the most noticeable impact on the change in this item of cash flow account:

1) decline in the gross financial result (no impairment write-off taken into account) and depreciation as a non-cash factor by PLN 248 million,
2) income tax payment higher than in 2015 – a decline in the stream of operating expenditure by PLN 283 million, which resulted from the advance payment on account of income tax, contributed by the Tax Capital Group in the amount of PLN 300 million and the advance payment for 2015 Q4 in the amount of PLN 89 million. Cash flows due to settlement of the Tax Capital Group in 2015 were of expenditure nature and amounted to PLN 112 million,
3) Positive stream of op flows arising from the change in the working capital – change by PLN 235 million YoY.

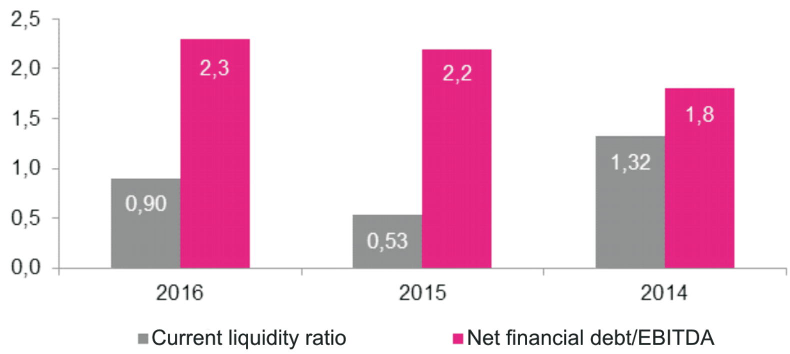
The value of cash flows on investment activities in 2016 was negative and it was lower by approximately 8% than the investment expenditure recorded in 2015, as a result of the impact of the following factors:

1) lower expenditure on the purchase of fixed assets and intangible assets – a decline by 11.5%. In the current period the highest expenditures were incurred by the Generation and Distribution Segments.
2) return of public aid in the amount of PLN 131 million by Nowe Brzeszcze GT company – currently ZG Brzeszcze in TAURON Wydobycie.

The positive value of cash of financial nature results from the issue of bonds performed in 2016, with the total nominal value of PLN 4,285 million and from the redemption of bonds issued in previous years, with the nominal value of PLN 3,330 million and the repayment of credits and loans in amount of PLN 140 million. The value of financial expenses due to paid interest on financial liabilities amounted to PLN 255 million and it was lower by 7.7% YoY.

TAURON Capital Group continues the development process and keeps strengthening its market position. It should be stressed that the value of operating flows shows a positive balance, consequently enabling TAURON Capital Group to finance its current operations independently. The ratio of current liquidity and the net debt to EBITDA ratio remain at a safe level.

Figure no. 85 The ratio of current liquidity and the net debt to EBITDA ratio in 2016–2014*



** Excluding the issue of hybrid bonds.*

4.2. Characteristics of the structure of assets and liabilities of the consolidated balance sheet

Structure of the annual consolidated statement of financial standing

The table below shows the structure of the annual consolidated statement of financial standing.

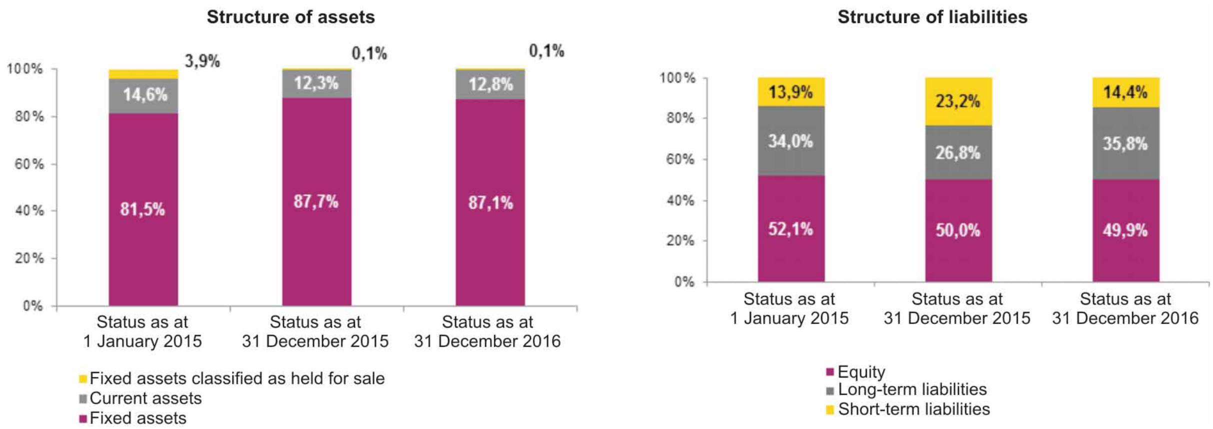
Table no 26. Structure of the annual consolidated statement of financial standing

Consolidated statement of financial standing	Status as at 31 December 2016	Status as at 31 December 2015	Status as at 1 January 2015
ASSETS			
Fixed assets	**87.1%**	**87.7%**	**81.5%**
Current assets	**12.8%**	**12.3%**	**14.6%**
Fixed assets classified as held for sale	0.1%	0.1%	3.9%
TOTAL ASSETS	**100.0%**	**100.0%**	**100.0%**

Consolidated statement of financial standing	Status as at 31 December 2016	Status as at 31 December 2015	Status as at 1 January 2015
LIABILITIES			
Equity attributable to shareholders of the parent entity	49.8%	49.9%	52.0%
Non-controlling shares	0.1%	0.1%	0.1%
Total equity	**49.9%**	**50.0%**	**52.1%**
Long-term liabilities	35.8%	26.8%	34.0%
Short-term liabilities	14.4%	23.2%	13.9%
Total liabilities	**50.1%**	**50.0%**	**47.9%**
TOTAL LIABILITIES	**100.0%**	**100.0%**	**100.0%**
Financial liabilities	8,138,502	8,138,647	8,113,766
Net financial liabilities	7,730,259	7,763,963	6,665,318

The figure below presents the structure of assets and liabilities.

Figure no. 86 Structure of assets and liabilities



According to the status as at 31 December 2016, similar to 2015, the value of fixed assets has the highest share in the structure of assets. In the structure of fixed assets, tangible fixed assets of the following sectors have the biggest share: Distribution(59.1%), Generation (33.7%) and Mining (6.4%).

As at 31 December 2016, equity and financial liabilities represented the highest 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 debt ratio, as compared to the European benchmarks for the sector, and the positive stream of cash flows from operating activities.

4.3. Significant off-balance sheet items

As at 31 December 2016, significant contingent liabilities of TAURON Capital Group were related to:

1) potential claims not reported by owners of land with unregulated status due to the lack of detailed record of unregulated land and the resulting inability to reliably estimate the amount of potential claims, and as a consequence, a possibility to create provisions,
2) the proceedings instituted on 17 September 2013 by the President of OCCP 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*,
3) the anti-monopoly proceedings instituted by the UOKiK President pursuant to the decision of 19 December 2014, in connection with the suspected abuse of the dominating position by TAURON Sprzedaż and TAURON Sprzedaż GZE on the market of reserve electricity sales,

4) the anti-monopoly proceedings instituted by the UOKiK President pursuant to the decision of 15 October 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 electricity generated in renewable energy sources and determining the purchase of this energy by the requirement 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,*
5) the explanatory proceedings conducted by the President of OCCP against TAURON Sprzedaż and TAURON Sprzedaż GZE,
6) the administrative proceedings instituted by the ERO President against TAURON Dystrybucja concerning imposing of the fine due to the failure to maintain facilities, equipment and installations in due technical condition and the violation of the terms defined in the concession,
7) the 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 the Steelworks to fulfil the obligation to pay receivables due to energy supplies, which consequently caused the suspension of electricity supplies to the Steelworks by GZE in 2001,
8) the action brought by ENEA against TAURON due to alleged unjustified benefit gained by the Company in connection with the settlements of imbalanced on the Balancing Market, performed with the PSE company in the period from January to December 2012; the claim for payment amounts to PLN 17,086 thousand,
9) legal actions associated with the termination of long-term contracts by PEPKH in liquidation,
10) the 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,
11) bank guarantees issued on instruction of TAURON in order to hedge liabilities of the common undertaking of EC Stalowa Wola to institutions financing the joint venture; the total value of guarantees issued amounts to PLN 314,486 thousand,
12) the value of real estate tax imposed on energy installations used for generation and transmission of electricity as well as equipment of underground mining headings.

Detailed information concerning off-balance items is included in notes 48 and 49 of the Consolidated financial statement for the year ended on 31 December 2016.

4.4. Differences between the financial results recognised in the annual report and the forecasts of results for the year as published earlier

The Management Board of the Company did not publish any forecasts of financial results TAURON Capital Group for 2016. This decision resulted from the considerable volatility of the market and substantial number of variables affecting its predictability.

4.5. Basic financial and non-financial ratios

Financial ratios

The table below presents the basic financial ratios of TAURON Capital Group.

Table no 27. The basic financial ratios of TAURON Capital Group*

Ratios	Definition	2016	2015	2014
PROFITABILITY				
EBIT Margin	Operating result / Revenue on sales	**4.5%**	(10.4)%	9.9%
EBITDA Margin	EBITDA/ Revenue on sales	**18.9%**	19.3%	19.9%
Net Profitability	Net result/ Revenue on sales	**2.1%**	(9.9)%	6.4%
Return on Equity (ROE)	Net result/ Closing balance of equity	**2.2%**	(11.2)%	6.6%
LIQUIDITY				
Current liquidity ratio	Current assets (excluding assets held for trade) / Short-term liabilities	**0.90**	0.53	1.32
DEBT				
General debt ratio	Total obligations/ total liabilities	**0.50**	0.50	0.48
Net financial debt/ EBITDA	(Financial liabilities - Cash)/ EBITDA	**2.31**	2.20	1.80
OTHER RATIOS				
Earnings per share (EPS)	Net result attributable to shareholders of the parent entity / Number of ordinary shares	**0.21**	(1.03)	0.67

** 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 2016 the net profitability ratio of TAURON Capital Group reached a level higher than achieved in the previous year, as a result of recognising the revaluation write-offs on the generation assets of the Generation Segment. Due to various values of write-offs the indicators are not comparable. Disregarding the write-offs, in each year the net profitability ratio was lower by 5.5% and it would amount to 5.8% for 2016 and 6.1% for 2015, respectively.

The current liquidity ratio reached a value higher than in 2015, which resulted from recognising of financial liabilities as at 31 December 2015 in the amount of PLN 3,214 million, repaid in 2016.

The total debt ratio as well as Net debt/EBITDA ratio reflect the share of liabilities in TAURON Capital Group financing. The current level of this ratio enables TAURON Capital Group to acquire external financing required to implement the investments planned. The change in the level of the ratio in 2016 results from the decline in the EBITDA result of TAURON Capital Group (by approximately PLN 186 million) while maintaining comparable net debt calculated against the ratio.

The EPS ratio (calculated in relation to net profit attributable to shareholders of the parent entity) is higher in 2016 than in 2015 due to recognising the impairment write-off in the result in both years.

Non-financial ratios

The non-financial ratios in TAURON Capital Group are closely associated with the specific nature of its activities, the resources held and the adopted Strategy, including:

1) assessment of investment opportunities,
2) methods of human resources management,
3) risk optimisation,
4) Clients' satisfaction feedback surveys,
5) centralisation of governance functions in TAURON Capital Group, restricting the non-core activities,
6) development of organisational structures and management procedures.

4.6. Most significant financial and operating data of TAURON Capital Group for 2012–2016

The table below presents the most significant financial data and operating data of TAURON Capital Group for the years 2012–2016.

Table no 28. Financial and operating data for the period 2012–2016*

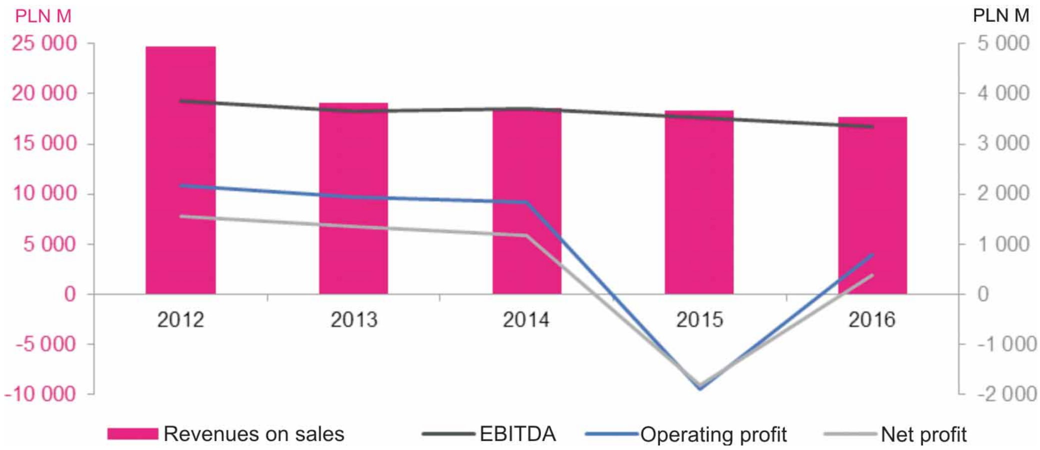
Basic information	unit	2016	2015	2014	2013	2012	Change % (2016/2015)
Statement of comprehensive income							
Revenues on sales	PLN M	17,646	18,264	18,577	19,131	24,753	97%
Operating profit	PLN M	802	(1,901)	1,830	1,934	2,165	–
Total financial revenues	PLN M	125	81	86	99	131	154%
Net financial expenses	PLN M	(418)	(368)	(418)	(347)	(347)	114%
Gross profit	PLN M	509	(2,188)	1,498	1,684	1,948	–
Income Tax	PLN M	(139)	384	(313)	(337)	(397)	–
Net profit	PLN M	370	(1,804)	1,186	1,346	1,551	–
attributable to shareholders of the parent entity	PLN M	367	(1,807)	1,181	1,308	1,476	–
attributable to non-controlling shares	PLN M	3	3	5	38	74	86%
EBITDA	PLN M	3,337	3,523	3,695	3,661	3,852	95%
Statement of financial standing							
Fixed assets	PLN M	29,148	28,124	28,163	27,567	25,471	104%
Current assets	PLN M	4,309	3,947	6,396	4,789	5,766	109%
Total equity	PLN M	16,679	16,048	17,997	17,793	16,800	104%
Total liabilities	PLN M	16,778	16,023	16,563	14,562	14,474	105%
Long-term liabilities	PLN M	11,969	8,584	11,744	9,304	9,081	139%
Short-term liabilities	PLN M	4,809	7,439	4,819	5,258	5,392	65%
Net financial debt	PLN M	7,730	7,764	6,665	5,227	4,535	100%
Capital expenditure	PLN M	3,817	4,175	3,090	3,780	3,472	91%
Cash flow account							
Net cash from operating activities	PLN M	3,064	3,387	2,618	4,079	3,479	84%
Net cash from investment activity	PLN M	(3,627)	(3,942)	(3,387)	(4,180)	(3,283)	87%
Net cash from financial activity	PLN M	590	(526)	1,636	(249)	190	–
Cash closing balance	PLN M	355	328	1,408	541	892	108%
Ratios							
EBIT Margin	%	4.5%	(10.4)%	9.9%	10.1%	8.7%	–
EBITDA Margin	%	18.9%	19.3%	19.9%	19.1%	15.6%	98%
Net financial debt/ EBITDA	number	2.32	2.20	1.80	1.43	1.18	105%
Net earnings per share	PLN/share	0.21	(1.03)	0.67	0.75	0.84	–
Dividend per share	PLN/share	–	0.15	0.19	0.20	0.31	0%
Operating data							
Commercial coal production	M Mg	6.37	4.91	5.40	5.45	5.57	130%
Net production of electric energy	TWh	16.80	18.56	17.35	21.72	21.43	91%
Net production of electric energy from RES	TWh	1.32	1.63	1.82	1.39	1.22	83%
Heat production	PJ	11.52	11.51	13.41	15.62	16.36	100%
Retail sales of electricity***	TWh	32.04	35.94	36.43	41.30	44.74	89%

Basic information	unit	2016	2015	2014	2013	2012	Change % (2016/2015)
Distribution of electricity	*TWh*	49.68	49.20	47.90	47.90	47.85	101%
Number of clients (Distribution)	*million*	5.47	5.42	5.38	5.33	5.30	101%

** 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 2010.*
*** Excluding the issue of hybrid bonds.*
**** The volume of retail sales for 2014 has been presented comparatively to 2015 in connection with reclassification of agreements of some consumers (from retail sales to wholesale).*

The figure below presents the financial data of TAURON Capital Group for the years 2012–2016.

Figure no. 87 Financial data of TAURON Capital Group for 2012–2016



The table below presents EBITDA results of TAURON Capital Group, divided into Segments of activity.

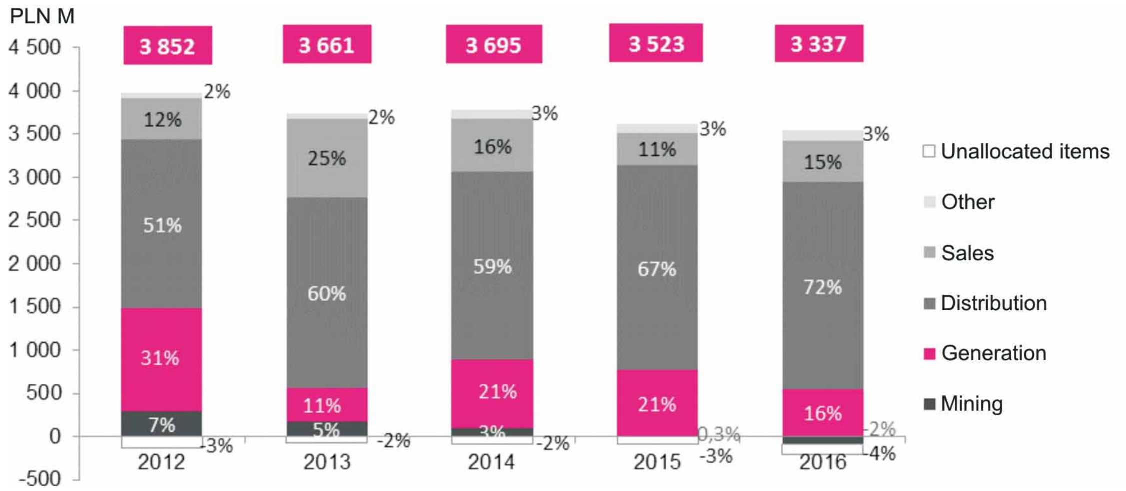
Table no 29. EBITDA results of TAURON Capital Group, broken down into individual Segments of activity*

No.	EBITDA (PLN M)	2016	2015	2014	2013	2012	Dynamics (2016/2015)	Change (2016–2015)
1.	Mining	**(82)**	9	98	166	287	–	(91)
2.	Generation	**545**	755	793	400	1,194	72%	(209)
3.	Distribution	**2,395**	2,372	2,172	2,208	1,956	101%	23
4.	Sales	**490**	380	608	899	478	129%	110
5.	Other	**115**	100	106	63	67	114%	14
6.	*Unallocated items*	***(126)***	*(94)*	*(83)*	*(75)*	*(131)*	134%	(32)
	Total EBITDA	**3,337**	**3,523**	**3,695**	**3,661**	**3,852**	95%	(186)

** 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 2010.*

The figure below presents the financial data of TAURON Capital Group for the years 2012–2016.

Figure no. 88 EBITDA Structure of TAURON Capital Group in 2012–2016



Basic information for 2012–2016 according to Segments

The figures below present the financial data for 2012–2016 according to Segments.

Figure no. 89 Data of Mining Segment for 2012–2016

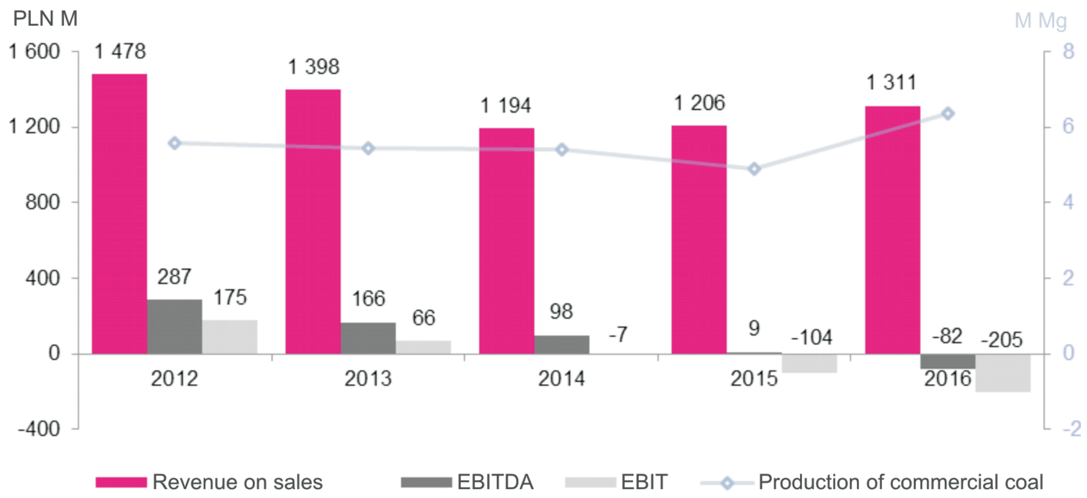


Figure no. 90 Data of Generation Segment for 2012–2016

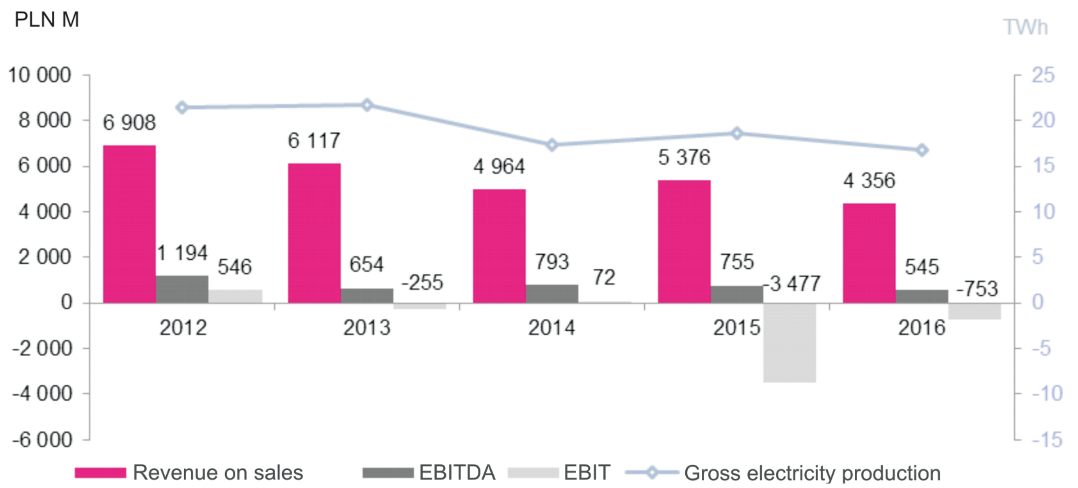


Figure no. 91 Data of Distribution Segment for 2012–2016

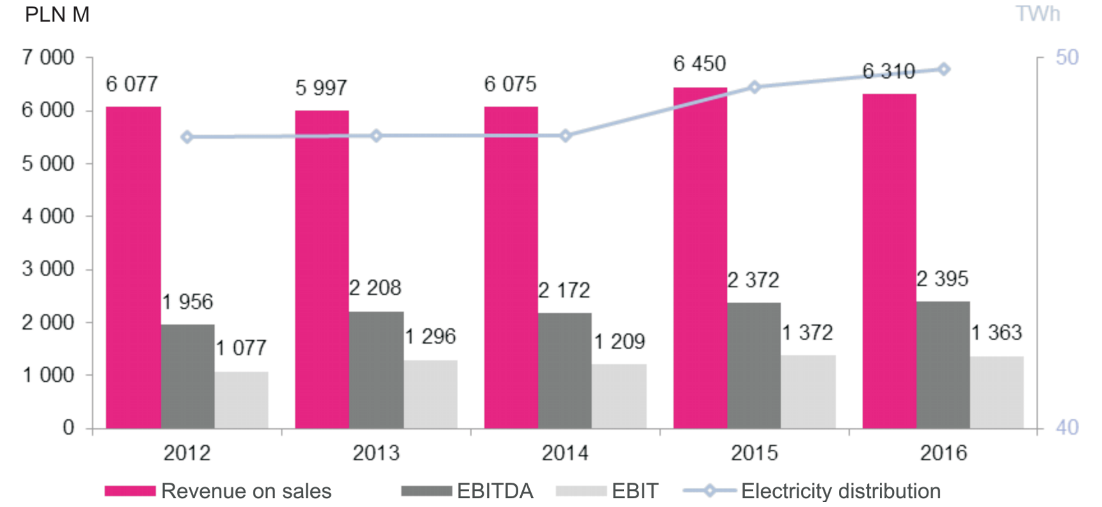


Figure no. 92 Data of Sales Segment for 2012–2016

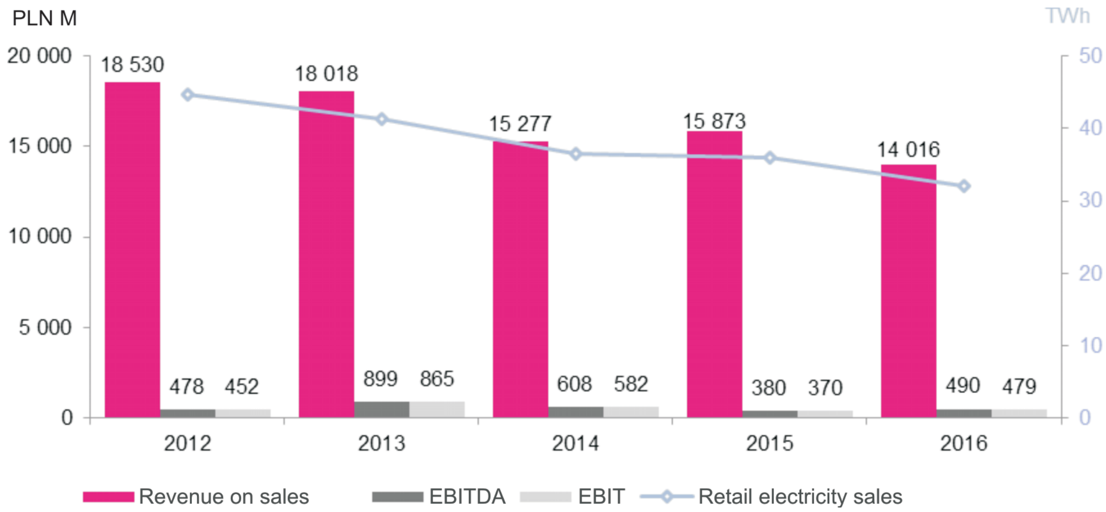
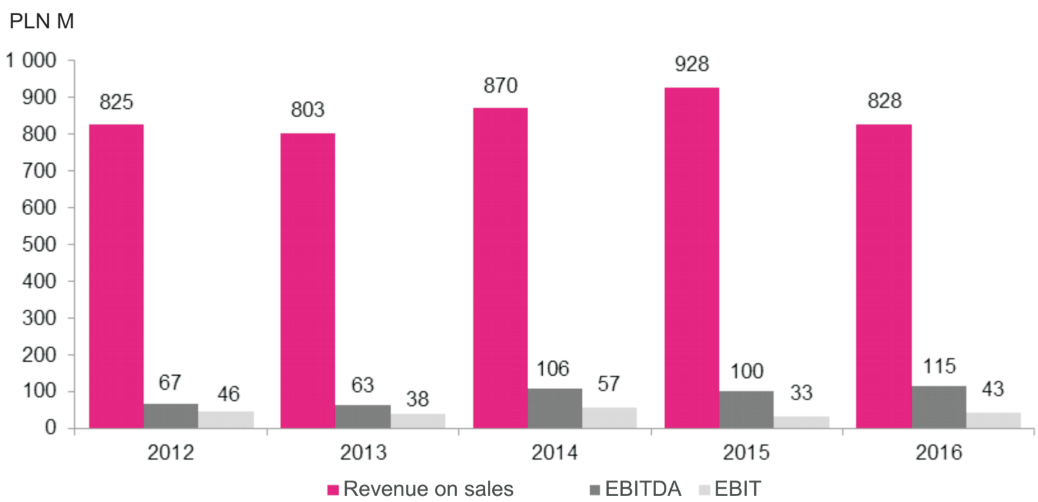


Figure no. 93 Data of Other Segment for 2012–2016



4.7. Income from the issue of securities

In 2016 TAURON conducted issues of bonds under programmes concluded so far (i.e. the programme of long-term bonds concluded with Bank Gospodarstwa Krajowego (BGK) and the bond issue programme of

24 November 2015 concluded with the consortium of banks), as well as under the new financing acquired from EIB, referred to below.

Issue of bonds and their acquisition by EIB

On 14 December 2016, the following agreements were signed between TAURON and EIB:

a) project agreement (the “Project Agreement”) determining detailed requirements relating to the financed investment task,

b) subscription agreement (the “Subscription Agreement”) providing basis for conducting the issue of hybrid bonds (“Bonds”) with the value of EUR 190,000 thousand Funds to be acquired through the issuance of Bonds will be allocated for covering expenditure of TAURON Dystrybucja associated with the development and modernisation of power grid infrastructure in the years 2016–2020.

The Bonds issued will represent subordinated, unsecured bearer coupon securities to be acquired by the EIB under the operations of the European Fund for Strategic Investments launched by the EIB in cooperation with the EC for the purpose of implementation of so-called Juncker Plan. In accordance with the Subscription Agreement the Bonds were issued in a single series on 16 December 2016. The redemption deadline will fall 18 years after the issue date, whereas in accordance with hybrid financing characteristics, the first financing period of 8 years has been defined (“1st Financing Period”), during which neither earlier redemption of the Bonds by the Company nor earlier sale of the Bonds by the EIB to third parties will be possible (in both cases, subject to exceptions defined in the Agreement). In the 1st Financing Period, the Bonds will bear interest at a fixed rate, whereas in the consecutive 10-year financing period (“2nd Financing Period”) – at a floating rate (Euribor 6M) increased by the agreed margin. The Agreement stipulates a possibility to postpone payment deadlines of interest on Bonds, maximum until the day of redemption of the Bonds or until the fifth day following taking the decision on payment of the dividend. As a result of subordinated nature of the Bonds, in case of TAURON bankruptcy or liquidation, any liabilities arising from the Bonds will have a priority order for the payment only before TAURON shareholders’ claims. The issue of Bonds will have a positive impact on the financial stability of TAURON Capital Group since the Bonds are excluded from calculation of the debt ratio constituting a covenant for some TAURON financing programmes. Moreover, 50% of the Bonds amount has been classified as equity in the rating model by the rating agency, which has a positive impact on the rating of TAURON Capital Group. The bonds obtained rating of Fitch rating agency at a level of BB+.

Under the aforementioned bond issue programme, on 16 December 2016 TAURON issued bonds for the total amount of EUR 190,000 thousand.

Issue of bonds and their acquisition by BGK

Within the long-term bond issue programme concluded on 31 July 2013, as amended by subsequent annexes, between the TAURON and BGK, in 2016 TAURON issued bonds for the total amount of PLN 490,000 thousand according to the following specification:

1) on 8 January 2016, issue of three series of bonds, with the total nominal value of PLN 210,000 thousand, with the redemption term in the years 2023–2025,

2) on 9 December 2016, issue of four series of bonds, with the total nominal value of PLN 280,000 thousand, with the redemption term in the years 2026–2029.

Issue of bonds and their acquisition by commercial banks

Under the bond issue programme concluded on 24 November 2015 between the Company and the consortium of banks, in 2016 TAURON issued bonds for the total amount of PLN 2,950,000 thousand according to the following specification:

1) on 29 February 2016 the issue of bonds with the total nominal value of PLN 2,250,000 thousand, with the redemption term on 29 December 2020,

2) on 25 March 2016 the issue of bonds with the total nominal value of PLN 100,000 thousand, with the redemption term on 25 March 2020,

3) on 30 March 2016 the issue of bonds with the total nominal value of PLN 300,000 thousand, with the redemption term on 30 September 2016,

4) on 9 December 2016 the issue of bonds with the total nominal value of PLN 300,000 thousand, with the redemption term on 09 December 2020.

The objective of the issue of bonds was the financing of CAPEX of TAURON Capital Group, excluding the bonds issued on 29 February 2016 issued in order to acquire funds for the purchase of 22,500 bonds from C tranche, issued on 12 December 2011, with the purpose of redemption, with the redemption date falling on 12 December 2016. Information on the aforementioned event is presented in detail in section 2.8 of this report.

The table below presents the specification of issued and non-redeemed bonds as at 31 December 2016.

Table no 30. Specification of issued and non-redeemed bonds as at 31 December 2016

No.	Issuer	Interest rate	Redemption term of the last series	Balance as at 31 December 2016 (thou.)
1.	TAURON	WIBOR 6M + fixed margin	04.11.2019	PLN 1,750,000
2.	TAURON	WIBOR 6M + fixed margin	20.12.2029	PLN 1,700,000
3.	TAURON	WIBOR 6M + fixed margin	29.12.2020	PLN 2,650,000
4.	TAURON	Fixed interest	16.12.2034	EUR 190,000
5.	TAURON Sweden Energy	Fixed interest	03.12.2029	EUR 168,000

4.8. Financial instruments

4.8.1. Application of financial instruments in the scope of elimination of price changes, credit risk, significant disruptions of cash flows and loss of financial liquidity

The financial risk in TAURON Capital Group is managed by TAURON. The centralisation of the financial risk management function is aimed at optimisation of the process, including the minimisation of TAURON Capital Group costs in this scope. Within the financial risk management, in 2016 TAURON Capital Group hedged the risk of volatility in cash flows resulting from the indebtedness held, based on WIBOR reference rate. Moreover, in 2016, TAURON Capital Group hedged the currency exposure arising within the commercial activities (mainly due to the CO_2 emission allowances trading) by concluding forward contracts. The aim of these transactions was to secure the Company against the risk of cash flow volatility resulting from currency rates fluctuations.

The table below presents active forward derivative transactions as at 31 December 2016 (due to the adopted centralised model of financial risk management, the data refer only to TAURON).

Table no 31. Information on forward transactions and derivatives as at 31 December 2016

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 at 31 December 2016 (thou.)
			PLN	EUR	other	up to one year	above one year	
1.	IRS	2,100,000	X				X	36,640
2.	Forward	46,497		X		X		3,189
		477		X			X	50

In the scope of hedging the risk arising from price volatility and the credit risk, TAURON Capital Group did not use financial instruments.

On the other hand, under liquidity loss risk management debt instruments referred to in subsection 4.10 are used.

4.8.2. Goals and methods of financial risk management

The objectives and methods of financial risk management in TAURON Capital Group are presented in section 3.4.2 of this report.

4.9. Financial outlook

Considering the current market situation, it is expected that the results of TAURON Capital Group in the forthcoming years will be affected both by internal factors and by external factors.

The results of the **Mining Segment** should systematically improve in the perspective of the nearest years. In order to improve / optimise the results, the Mining Area will implement the investment tasks and the technical and organisational tasks aimed at raising own production capacity based on the deposits held, in the cost-effective way.

It is expected that the financial situation in the **Generation Segment** in the perspective of the nearest several years will not improve in relation to the current situation, due to the macroeconomic and sectoral conditions under which electricity producers will operate. In a longer time horizon, new generation units currently under construction, demonstrating better production parameters, will have an impact on improvement of the current status. It is also expected that, in a longer perspective, growth in electricity prices will occur due to higher prices of CO_2 emission allowances, as a result of EC administrative measures (aimed at triggering of growth in these prices). In activities associated with heat distribution, growth in revenues is foreseen due to the implemented low emission liquidation programmes promoting systemic heat. The activity associated with electricity generation in RES is subject to statutory regulation which, to a large extent, determine the profitability. The activities conducted in the scope of cost effectiveness improvement in the whole Area will have impact on the improvement of its results.

In the **Distribution Segment**, the estimated level of remuneration from invested capital and the measures implemented in the scope of cost effectiveness improvement will play a key role in the developments of the operating result. It is expected that the estimated level of operating profit in the nearest years will be lower than that reached in 2016. 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 capital cost, correction factors of enterprise efficiency improvement in the scope of operating costs and the level of the balancing difference, continuation of qualitative regulation.

In the **Sales Segment** a stable level of operating profit is expected in the following years. In the nearest years the necessity to incur higher costs has to be taken into account, in connection with conducing expansive activities and measures aimed at minimising the number of clients leaving as well as recovery of clients lost in the previous years under the circumstances of growing activity of the competition.

The **Other Segment** is mainly responsible for rendering common services as well as for implementation and finalisation of projects serving mainly for the provision of services to the Distribution and Sales Areas in the scope of contacts and top settlements with clients at the highest level. In addition, services for companies of TAURON Capital Group are provided, inter alia, in the scope of financial and accounting service and IT. Those activities enable to achieve synergy effects across TAURON Capital Group and improve cost effectiveness.

4.10. Assessment of financial resources management

TAURON Capital Group has a centralised financial management area at the level of TAURON, accordingly, effective management of finance of the entire TAURON Capital Group is possible. The main tools enabling effective management include the implemented central financing model as well as the *Policy of liquidity management of TAURON Group*, including the cash pooling operating in TAURON Capital Group. Moreover, the financial management system is supported by the central *Policy of managing risks specific in the financial area of TAURON Group* and the central *Insurance policy of TAURON Group,* where the Company plays the role of the management body and decision maker in the scope of directions of measures undertaken, allowing for determining the relevant limits of risk exposure.

In accordance with the adopted central model of financing, TAURON is responsible for acquisition of financial resources for companies of TAURON Capital Group. Resources acquired both internally (from companies of TAURON Capital Group generating financial surpluses), as well as externally (from the financial market) are subsequently transferred to companies of TAURON Capital Group, reporting the demand for financing (for this purpose, besides cash pooling, the intra group bond issue programme has been implemented).

Such model of acquisition of funding sources allows, among other things, for decreasing of the costs of capital, increasing of the possibility to obtain financing, it reduces the number and form of hedges established on assets of TAURON Capital Group and covenants required by financial institutions, as well as reduces administrative costs. The central model of financing also enables to acquire financing sources unavailable for individual companies, such as, for example, issue of Euro bonds.

Another key element influencing the effectiveness of financial management is the policy of liquidity management. Through implementation of relevant forecasting standards it becomes possible to establish the precise liquidity position allowing for optimising of selection of the moment of fund raising as well as the maturity term and types of deposit instruments as well as the appropriate level of liquidity provision. The above factors influence both the cost reduction and safety enhancement. The current liquidity management is supported by the implemented cash pooling mechanism. Its overriding goal is to provide for current financial liquidity in TAURON Capital Group, with simultaneous limitation of costs of short-term external financing and maximising of financial revenue due to cash surpluses held.

Owing to the cash pooling structure, companies of TAURON Capital Group facing short-term deficits of funds, may use funds of companies recognising financial surpluses, without the need to acquire external financing.

Moreover, a coherent programme of bank guarantees operates in TAURON Capital Group. Under the agreements concluded by TAURON with banks it is possible to issue guarantees to secure liabilities of TAURON Capital Group companies within a centralised limit. The above mentioned activity reduced the cost of guarantees acquired, made their acquisition independent of an individual company standing and limited the total number of activities required to obtain the guarantee.

In 2016, TAURON Capital Group demonstrated full capacity to settle its liabilities on the payment date.

4.11. Principles of preparation of the annual consolidated financial statements

The consolidated financial statement has been drawn up in accordance with the IFRS adopted 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.

Companies of TAURON Capital Group and the parent entity keep their books and prepare their financial statements in accordance with the IFRS, excluding KOMFORT-ZET, which keeps its books and draws up its financial statements in accordance with the Accounting Act, as well as TAURON Czech Energy and TAURON Sweden Energy, keeping their books and preparing their financial statement in accordance with the accounting principles applicable, respectively, in the Czech Republic and in Sweden.

The consolidated financial statement contains adjustments which are not included in the ledgers of TAURON Capital Group entities, introduced in order to bring the consolidated statement into compliance with IFRS.

The consolidated financial statement has been prepared with the assumption of continuation of business operations by the TAURON Capital Group companies in the foreseeable future. As at the date of approval of the consolidated financial statement for publication, no circumstances have been recognised, indicating any risk for business continuity by the TAURON Capital Group companies.

The accounting principles (policy) adopted for drawing up of the consolidated financial statement are presented in note 9 of the Consolidated financial statement for the year ended on 31 December 2016.

4.12. Information concerning the entity authorised to examine financial statements

On 15 June 2016 TAURON concluded the agreement with Deloitte Polska Spółka z ograniczoną odpowiedzialnością Spółka komandytowa for conducting the audit of:

1) financial statements of the Company for 2016, prepared in accordance with the requirements of the IFRS,
2) financial statements of selected companies of TAURON Capital Group for 2016, prepared in accordance with the IFRS,
3) consolidated financial statements for 2016, prepared in accordance with the requirements of the IFRS.

The Agreement also covers conducting of the interim reviews of semi-annual financial statements of the Company and consolidated financial statements of TAURON Capital Group, prepared in accordance with the IFRS for period ending on 30 June 2016.

The level of remuneration of the statutory auditors for the services provided to the companies of TAURON Capital Group is shown in the table below.

Table no 32. The level of remuneration of the statutory auditors for the services provided to the companies of TAURON Capital Group

No.		Year ended 31 December 2016 (PLN thous.)	Year ended 31 December 2015 (PLN thous.)
1.	Obligatory audit, including:	752	652
	consolidated financial statements	25	25
	separate financial statement of the parent entity	80	80
	separate financial statements of the subsidiaries	647	547

No.		Year ended 31 December 2016 (PLN thous.)	Year ended 31 December 2015 (PLN thous.)
2.	Other certifying services provided to TAURON Capital Group, including reviews of financial statements	438	556
3.	Tax advisory services	0	0
4.	Other services (including training) provided to TAURON Capital Group	244	505
	Total	**1,434**	**1,713**

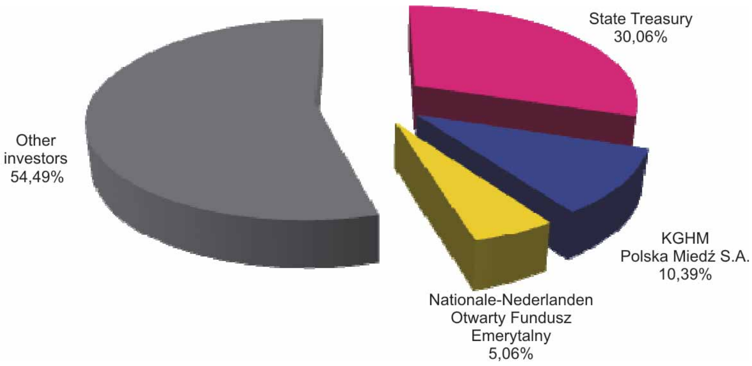
5. SHARES AND SHAREHOLDERS

5.1. Structure of shareholding

As at 31 December 2016 and as at the day of drawing up this report, the share capital of the Company, in accordance with the entry to the National Court Register, amounted to PLN 8,762,746,970 and it was divided into 1,752,549,394 shares with the nominal value of PLN 5 each, including 1,589,438,762 ordinary bearer shares of AA series and 163,110,632 ordinary registered shares of BB series.

The figure below presents the structure of shareholding as at 31 December 2016 and as at the day of drawing up this report.

Figure no. 94 Structure of the shareholding as at 31 December 2016 and as at the day of this report



5.2. The dividend policy

Within the endorsed Strategy the Company adopted the dividend policy. In the long-term perspective, TAURON plans to pay out a dividend at a level of minimum 40% of the consolidated net profit. The intention of the Company is to provide a dividend yield that would be competitive towards 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 affected by additional factors, including in particular:

1) The liquidity situation of TAURON Capital Group,
2) Market situation,
3) Implementation of the investment policy,
4) Cost and ability to raise financing,
5) Legal requirements and provisions of the financing agreements, in particular related to not breaching the defined value of the leverage ratio,
6) Ensuring investment grade rating.

The forecasts underlying the Strategy indicate that 2020 will be the first year when the dividend payout will be possible.

The table below presents the level of the dividend paid in the years 2010–2014.

Table no 33. The level of the dividend paid in the years 2010–2014

Dividend paid for 2010–2014						
No.	Financial year for which the dividend was paid	Amount of dividend paid (PLN)	% of profit net	Value of dividend per share paid (PLN)	Dividend record day	Date of dividend payment
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 shares as well as shares and stocks in affiliated entities of the Company held by the members of the management and supervisory bodies

As at 31 December 2016 and as at the day of this report, Members of the Management Board and members of the Supervisory Board did not hold stocks or shares of the Company and stocks or shares in affiliated entities of the Company.

5.4. Agreements concerning potential changes in the shareholding structure

The Management Board is not aware of existence of any agreements (including agreements concluded after the balance sheet day), as a result of which changes in the ratio of the shares held by shareholders and bondholders may occur in the future.

5.5. Purchase of own shares

In 2016 and as at the day of drawing up this report, the Company did not hold any own shares.

5.6. Programmes of employee shares

In 2016, no employee shares programmes operated in the Company.

5.7. Listing of shares on the Warsaw Stock Exchange (GPW)

Shares of TAURON have been listed at the Primary Market of GPW since 30 June 2010. In 2016 the price of TAURON shares ranged from PLN 2.38 to PLN 3.17 (according to closing prices). The price of shares during the last session in 2015 reached the level of PLN 2.88. A year later, the price reached PLN 2.85. The return rate[1] on investment in TAURON shares in 2016 amounted to -1%, whereas the WIG20 index in this period increased by almost 5%, and the WIG-Energia index dropped by almost 13%. The major reasons of continued lateral trend on the exchange included results of the Polish economy, worse than the forecasts, outflow of foreign investors and uncertainty concerning the impact of changes in the pension system on the equity market.

It should be stressed that in 2016 the quotations of the biggest European energy groups also did not manage to lose the long-term downward trend.

On the other hand, the main reasons of the general discount on valuation of domestic energy companies in 2016 included: regulatory uncertainty related to the future support system of renewable energy sources, write-offs related to the impairment in the value of assets in the electricity generation segment and risks associated with the involvement of energy companies on projects in the coal mining sector or related to building generation capacity based on hard coal.

The measures striving to guarantee financial stability of TAURON Capital Group in the forthcoming years supported quotes of TAURON shares in 2016. The most important measures included: the development of the new strategy, the implementation of consecutive Efficiency Improvement Programme for 2016–2018, raising the maximum level of the net debt/EBITDA covenant from 3.0x to 3.5x and the issue of hybrid bonds.

In experts' opinion, the majority of risks associated with the energy sector has already been included in share prices, which may create the opportunity of selective purchases in 2017. Analysts and experts of the sector list the following factors as the most important opportunities for the industry: implementation of the capacity market mechanism, systematic cost reduction and rebound of coal prices which will translate to the improvement of financial results of coal mines.

As at 31 December 2016, TAURON shares were included in the following exchange indices:

1. **WIG** – comprising all companies listed at the Primary Market of GPW which meet the base criteria of participation in the indices, Share of TAURON in WIG index: 1.07%.
2. **WIG-Poland** – the national index which includes only shares of national companies listed at the Primary Market of GPW, which meet the base criteria of participation in the indices. Share of TAURON in WIG-Poland index: 1.11%.
3. **WIG20** – index calculated based on the value of share portfolio of 20 biggest and most liquid companies of the Primary Market of GPW. Share of TAURON in WIG20 index: 1.68%.
4. **WIG30** – index comprising 30 biggest and most liquid companies listed at the Primary Market of GPW. Share of TAURON in WIG30 index: 1.56%.

[1] *The return rate calculated, including the income of the investor due to dividends, and assuming that the additional income gained will be reinvested. Methodology compliant with the GPW Statistical Bulletin.*

5. **WIG-Energia** – the sectoral index comprising companies participating in the WIG index and simultaneously classified to the energy sector. Share of TAURON in WIG-Energia index: 17.06%.
6. **Respect Index** – the index grouping in their portfolio companies operating in accordance with the highest standards of social responsibility. Share of TAURON in Respect Index: 2.94%.
7. **MSCI Emerging Markets Europe 10/40 Index** – the index comprising key companies listed at exchanges of emerging markets. Share of TAURON in MSCI Emerging Markets Europe 10/40 Index: 0.25%.
8. **MSCI Poland Index** – the index comprising over 20 key companies listed at GPW. Share of TAURON in MSCI Poland Index: 1.59%.

The table below presents the key data concerning the Company shares in the years 2011–2016.

Table no 34. Key data concerning TAURON shares in the years 2011–2015

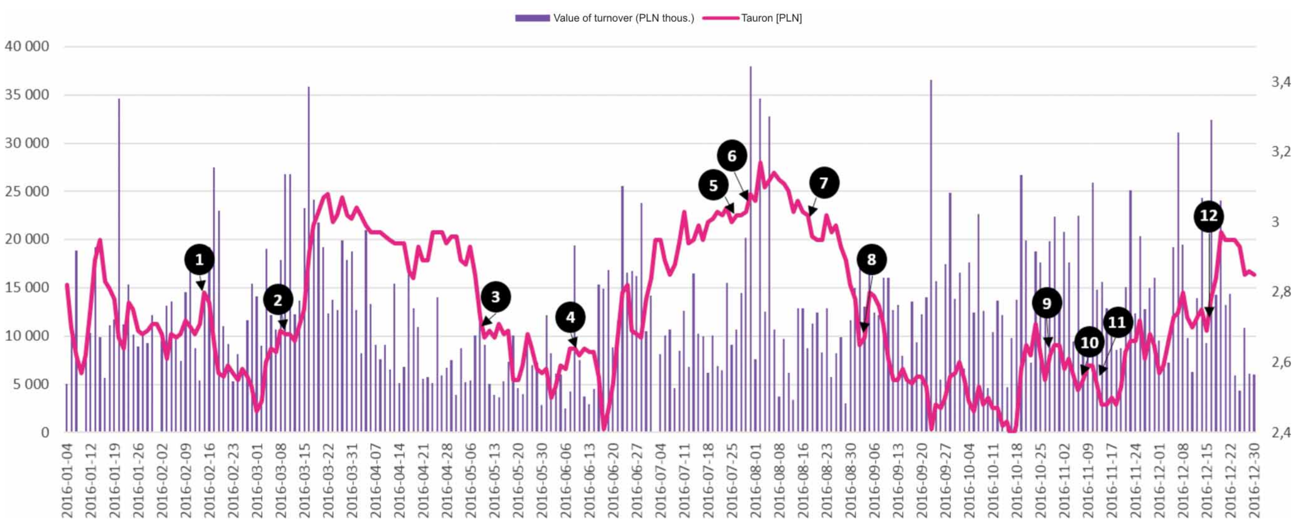
No.		2011	2012	2013	2014	2015	2016
1.	Maximum price (PLN)	6.81	5.61	5.39	5.69	5.29	3.19
2.	Minimum price (PLN)	4.65	4.08	3.85	4.04	2.37	2.31
3.	Last price (PLN)	5.35	4.75	4.37	5.05	2.88	2.85
4.	Capitalisation at the end of the period (PLN million)	9,376	8,325	7,659	8,850	5,047	4,995
5.	Capitalisation at the end of the period (%)	2.10	1.59	1.29	1.50	0.98	0.90
6.	Book value (PLN million)	15,922.47	16,839.41	17,675.34	18,106.79	18,837.00	16,348.99
7.	C/Z	8.10	5.50	5.50	7.80	4.2	x
8.	C/WK	0.59	0.49	0.43	0.49	0.27	0.31
9.	Return rate since the beginning of the year (%)	-16.73	-5.03	-3.64	+20.07	-40.78	-1.04
10.	Dividend rate (%)	2.8	6.5	4.6	3.8	5.2	–
11.	Turnover value (PLN million)	5,574.82	3,198.94	3,103.56	3,134.81	3,062.52	3,199.02
12.	Share in trade (%)	2.21	1.70	1.41	1.53	1.50	1.69
13.	Average volume per session	3,721,539	2,667,725	2,793,020	2,489,329	3,190,195	4,662,087
14.	Average number of transactions per session	1,373	960	1,022	1,106	1,431	1,465

Source: GPW Statistical Bulletin

** The return rate calculated, including the income of the investor due to dividend, and assuming that the additional income gained will be reinvested. Methodology compliant with the GPW Statistical Bulletin.*

The figures below present the historical developments of TAURON share price and the value of turnover, including, in comparison with WIG20 and WIG-Energia indices.

Figure no. 95 Graph of TAURON share price and value of turnover in 2016



	Date	Event
1	15.02.2016	• Information about planned write-off of impaired generation assets of the Generation Segment in financial statements for 2015
2	09.03.2016	• Publication of the consolidated annual report for 2015 • Adoption of efficiency improvement programme in TAURON Group for 2016–2018
3	11.05.2016	• Publication of the periodical report for the 1st quarter of 2016
4	08.06.2016	• Ordinary General Meeting of TAURON
5	26.07.2016	• Information about planned recognition of a write-off of impaired generation assets of the Generation Segment in financial statements for the 1st half of 2016
6	29.07.2016	• Publication of estimated consolidated financial data for the 1st half of 2016
7	17.08.2016	• Publication of the periodical report for the 1st half of 2016
8	02.09.2016	• Adoption of the TAURON Group's 2016–2025 Strategy • Adoption of the dividend policy for 2016–2025
9	28.10.2016	• Publication of estimated financial figures of TAURON Polska Energia Group for Q3 2016
10	09.11.2016	• Publication of the periodical report for the 3rd quarter of 2016
11	14.11.2016	• Confirmation of ratings and revision of the outlook for TAURON from negative to stable by Fitch agency
12	15.12.2016	• Extraordinary General Meeting of TAURON

Figure no. 96 Graph of TAURON share price and the value of turnover from the exchange debut until 31 December 2016

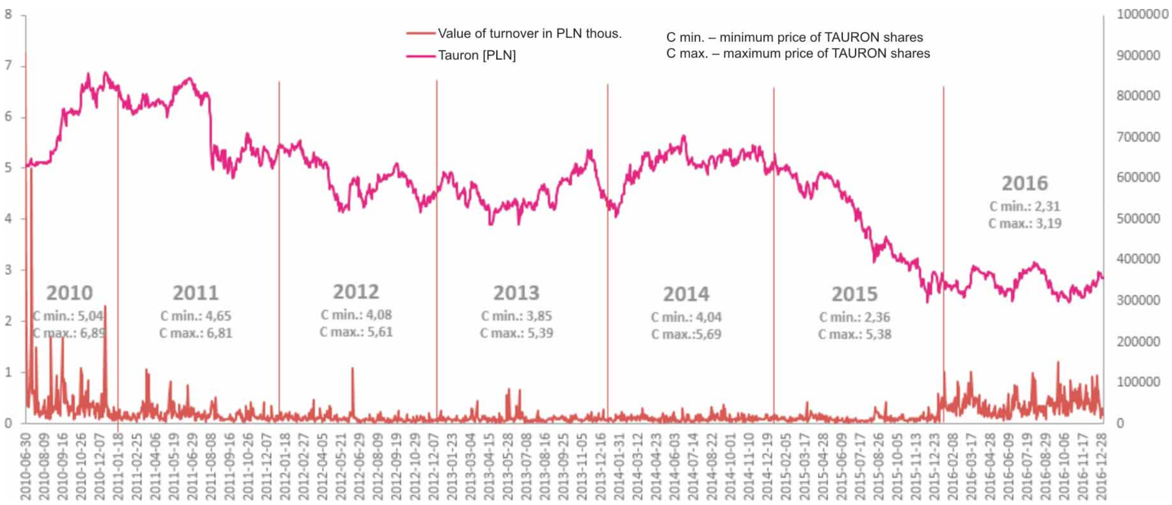


Figure no. 97 Graph of TAURON share price compared to WIG20 and WIG-Energia indices in 2016

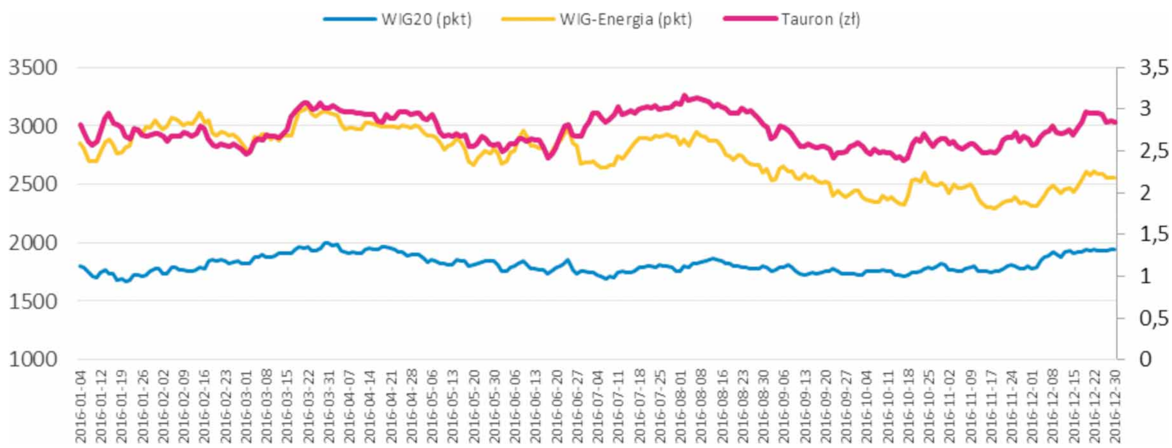
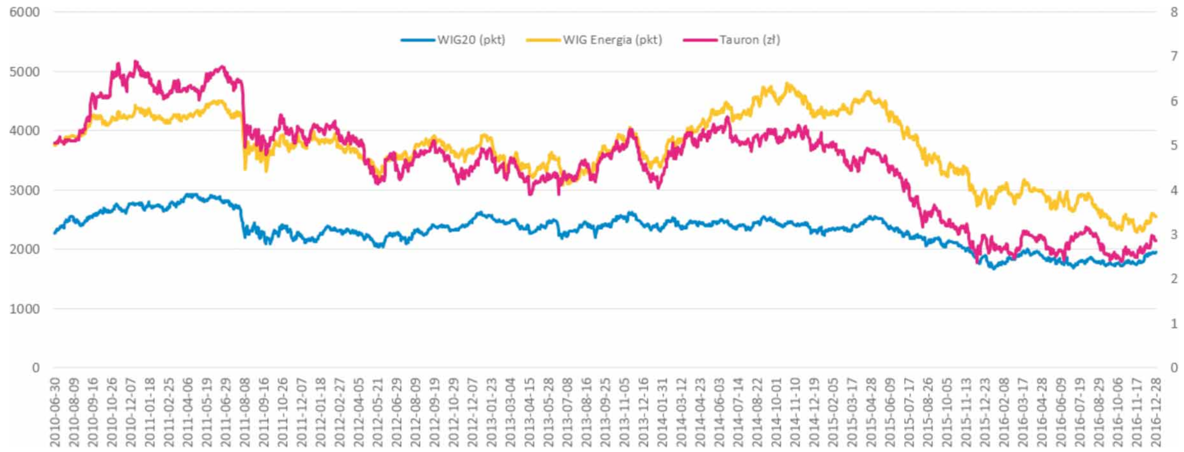


Figure no. 98 Price of TAURON shares compared to WIG20 and WIG-Energia indices from the exchange debut until 31 December 2016



Recommendations for TAURON Polska Energia S.A. shares

In 2016 the analysts of brokerage houses and investment banks issued the total of 24 recommendations for TAURON shares, including:

1) Eight "buy" recommendations,
2) Eight "keep" recommendations,
3) Eight "sell" recommendations.

The table below presents the list of recommendations issued in 2016.

Table no 35. Recommendations issued in 2016

No.	Date of recommendation	Recommendation/target price	Recommending institution
1.	27.01.2016	Sell / PLN 2.50	UBS
2.	01.02.2016	Keep / PLN 2.71	Wood&Co
3.	08.02.2016	Sell / PLN 2.00	Ipopema
4.	11.03.2016	Buy / PLN 3.30	Societe Generale
5.	05.04.2016	Buy / PLN 3.80	Raiffeisen Centrobank
6.	13.04.2016	Keep / PLN 3.00	Deutsche Bank
7.	20.04.2016	Sell / PLN 2.70	Trigon
8.	09.05.2016	Sell / PLN 2.70	DM PKO BP
9.	19.05.2016	Sell / PLN 2.38	Haitong Bank
10.	24.05.2016	Buy / PLN 2.84	DM BZ WBK
11.	25.05.2016	Keep / PLN 2.79	DM PKO BP
12.	20.06.2016	Buy / PLN 3.20	J.P. Morgan
13.	29.06.2016	Keep / PLN 2.70	Citi
14.	9.08.2016	Sell / PLN 2.81	DM BZ WBK
15.	19.08.2016	Buy / PLN 3.70	Societe Generale
16.	04.10.2016	Buy / PLN 3.03	DM mBank
17.	10.10.2016	Sell / PLN 2.00	Citi
18.	21.11.2016	Buy / PLN 3.40	Societe Generale
19.	22.11.2016	Keep / PLN 2.70	Deutsche Bank

No.	Date of recommendation	Recommendation/target price	Recommending institution
20.	22.11.2016	Sell / PLN 2.31	DM BZ WBK
21.	04.12.2016	Keep / PLN 2.50	DM BOŚ
22.	06.12.2016	Buy / PLN 3.03	DM mBank
23.	19.12.2016	Keep / PLN 2.58	Haitong Bank
24.	20.12.2016	Keep / PLN 2.89	DM PKO BP

5.8. Investor relations

The reliable and transparent communication with investors is one of the priorities of TAURON. It is provided both in the form of activities required by law (e.g. current and periodical reports) and also through 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, implemented investment projects, 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 publication of periodical reports, the company organised conferences for analysts and managers 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 Internet in Polish and in English. A possibility of their listening via telephone was also provided. Owing to such solution, all investors interested in TAURON Capital Group had a possibility to follow those events directly and receive 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 standing of TAURON Capital Group can reach all investors via diverse channels.

Besides meetings accompanying the publication of periodical reports, in 2016 members of the Management Board and representatives of Investor Relations Office took part in 12 conferences and roadshows, during which over 100 meetings with managers and analysts were held. Representatives of TAURON Capital Group met institutional investors not only in Poland, but also in the USA, Great Britain, Austria, Germany and Czech Republic.

In connection with the growing role of Internet channels, much emphasis was put on technical aspects of communication with investors – additional communication channels are used, such as the dedicated application for mobile devices. On the YouTube portal broadcasts of events important for investors are placed: reporting conferences, GMs, Investor Days and comments of the President of the Management Board on the results. On the other hand, on Facebook, announcements of significant events are published, including links to websites where the broadcasts may be followed or participation in investor chat is possible. In mid-2016 the Company decided to expand its communication channels and launched a corporate profile on Twitter where entries in the area of investor relations appear.

Being aware that the website is a significant source of information for investors, in particular, the tab on *Investor Relations*; the company cares for its content and validity of the content contained therein. The Section on *Investor Relations* contains a lot of useful information on the current events, financial results or GMs. It also contains presentations and video broadcasts of conferences summarising the financial results.

In 2016, the company 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”. Within the regular communication with this sizeable group of investors, 4 chats with a representative of the Management Board took place in 2016, in which approximately 100 investors took part each case. Activity in the scope of contacts with individual investors resulted in joining the programme of Individual Investors’ Association “10 of 10 – a company friendly to investors” and receiving of the distinction “Hero of the Capital Market” in 2014.

The activity in the area of investor relations is appreciated by participants of the capital market and investors. In 2016 the company received successive awards for the high quality of investor relations. In March 2016, within the biggest survey of investor relations in Poland, organised by the Journal of Stock Exchange and Investors, “Parkiet” and the Chamber of Brokerage Houses, participants of the internet questionnaire survey granted the first place to TAURON in terms of quality of investor relations among companies of WIG30 index. In May 2016, during the “Stock Market Review Gala 2015” TAURON receive a GPW award for the highest value of the debut in the Catalyst market in 2015 in connection with introduction of 17,500 bonds with the total value of PLN 1.75 billion to the alternative trading system. In October 2016, for the third time, TAURON received the main award in the competition for “The Best Annual Report”, granted by the Institute of Accounting and Taxes, consequently joining the “The Best of The Best” group comprising companies using the highest reporting standards. Similar to 2015, the jury of the competition additionally distinguished the internet version of the annual report.

Since 2013 TAURON has been included in the RESPECT Index, and in December 2016, for the fourth consecutive time the Company was specified among listed entities observing the principles of sustainable development.

The following table presents the timeline of events and activities carried out within investor relations which took place in 2016.

Table no 36. Timeline of events and activities carried out within investor relations in 2016

No.	Date	Event
1.	09.03.2016	Publication of the separate and consolidated annual report for 2015
2.	10.03.2016	Meeting of the Management Board with analysts managing funds, connected with the publication of the financial results for 2015
3.	10.03.2016	Chat with individual investors was organised in cooperation with the Association of Individual Investors
4.	16.03.2016	Participation in DM PKO BP CEE Capital Markets Conference in London
5.	23.03.2016	Meeting with the management associated with the publication of the financial results for 2015, Societe Generale, Warsaw
6.	11–13.04.2016	Participation in the conference of Raiffeisen Institutional Investors’ Conference, Zürs, Austria
7.	11.05.2016	Publication of the periodical report for the 1st quarter of 2016
8.	12.05.2016	Meeting of the Management Board with analysts managing funds, connected with the publication of financial results for the 1st quarter of 2016
9.	12.05.2016	Chat with individual investors in cooperation with the Association of Individual Investors
10.	16.05.2016	Participation in the IPOPEMA and GPW, Poland Capital Markets Day, New York
11.	03–05.06.2016	Participation the 20th in DM PKO BP conference in Warsaw
12.	09.06.2016	Meeting with the management associated with the publication of the financial results for 2016, Societe Generale, Warsaw
13.	08.06.2016	Ordinary GM of TAURON
14.	17.08.2016	Publication of the periodical report for the 1st half of 2016
15.	18.08.2016	Meeting of the Management Board with analysts and fund managers, connected with the publication of the financial results for the 1st half of 2016
16.	20.08.2016	Chat with individual investors in cooperation with the Association of Individual Investors
17.	05.09.2016	Presentation of TAURON Group’s Strategy for 2026–2025 – Management Board meeting with media, analysts and managers, GPW, Warsaw
18.	12–13.09.2016	Participation in the Pekao Investment Banking, Warsaw conference: 13th Annual Emerging Europe Investment Conference, Warsaw
19.	21.09.2016	Roadshow with DM PKO BP, Frankfurt
20.	27–28.09.2016	Participation in DM PKO BP Conference: Mining and Energy 2016, Wrocław
21.	03.10.2016	Participation in DM BZ WBK Energy & Mining, Warsaw
22.	12–13.10.2016	Participation in the Erste Group Investor Conference, Stegersbach 2016 (Austria)
23.	09.11.2016	Publication of the periodical report for the 3rd quarter of 2016
24.	10.11.2016	Meeting of the Management Board with analysts managing funds, connected with the publication of the financial results for the 3rd quarter of 2016, Warsaw
25.	16.11.2016	Chat with individual investors in cooperation with the Association of Individual Investors
26.	30.11–02.12.2016	Participation in the WOOD’s Winter in Prague – Emerging Europe Conference, Prague
27.	15.12.2016	Extraordinary GM of TAURON

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 Management Board submits the Statement on Application of Corporate Governance in 2016.

6.1. Indicating the applied set of corporate governance rules

In 2016 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 2015, which entered into force on 1 January 2016.

The text of the Best Practice 2016 the Company is subject to is published on the GPW website: http://www.corp-gov.gpw.pl.

In connection with the entry into force of the aforementioned set of Best Practice 2016 as of 1 January 2016, the Management Board of the Company adopted the recommendations and rules defined in the aforementioned document for application, excluding the rules defined in: IV.Z.2, VI.Z.1, VI.Z.2.

At the same time, the Management Board recognised that the following recommendations and rules of Best Practice 2016 do not apply to the Company: I.Z.1.10, III.Z.6, IV.R.2.

Pursuant to § 29 item 3 of the *Regulations of Giełda Papierów Wartościowych w Warszawie S.A.*, on 1 February 2016 the Company submitted a report concerning the waiver of the detailed rules contained in Best Practice 2016, via the Electronic Information Base (EBI system). At the same time, the Company published information on its website concerning the status of application of recommendations and rules contained in Best Practice 2016 by the Company.

Moreover, the Management Board of the Company, adopting the detailed rules of the 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 method of their application. The detailed description of the method of applying the aforementioned rules has been included in the *Information concerning the status of application of recommendations and rules contained in the set of Best Practice 2016 by the Company,* constituting the annex to the report on the waiver of detailed rules contained in the Best Practice 2016 document and posted on the Company website.

6.2. Indicating the abandoned rules of corporate governance

In 2016 the Company did not apply the following detailed rules contained 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 scope.
2) VI.Z.1. concerning the construction of incentive schemes in a way necessary, among others, to tie the level of remuneration 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 remuneration 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 remuneration 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 remuneration 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 remuneration 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 remuneration should be tied to instruments linked with the Company shares.

Due to the lack of a single document in the Company 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 in 1 February 2016 concerning the abandoned detailed rules of corporate governance contained in the set of Best Practice 2016, the Company indicated the method of its application. The rules on diversity management were introduced for application under many documents constituting internal legal acts, including the *TAURON Group's Code of Business Ethics*. The Company plans to develop and implement the diversity policy for application in a single formal document.

At the same time, while adopting the Best Practice 2016 for application, the Management Board of the Company indicated that the following rules do 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.

Information concerning abandonment of recommendations contained in Best Practice 2016 for application

In 2016 the Company did not apply only the recommendation contained 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 16 May 2013 to adopt the resolution concerning the amendment to the Company Articles of Association which was to enable the shareholders to participate in the GM using electronic communication means, as well as the failure of the Ordinary GM of the Company held on 8 June 2016 to adopt the relevant amendment to the Company Articles of Association ensuring publicly available real-time broadcast of general meetings.

Other recommendations contained in Best Practice 2016 were applied by the Company.

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 control and risk management system in relation to the process of generating financial statements and consolidated financial statements is implemented through:

Supervision over application of coherent accounting principles by companies of TAURON Capital Group while compiling the consolidated financial statements of TAURON Capital Group

In order to ensure coherent accounting principles based on IFRS, approved by the EU, in TAURON Capital Group *the Accounting Policy of TAURON Polska Energia S.A.* was developed and implemented (Accounting Policy). The document is subject to relevant amendments and updates in case of amendments to the regulations. The rules contained in the Accounting Policy are applicable to separate financial statements of TAURON and consolidated financial statement of TAURON Capital Group. Companies of TAURON Capital Group are obliged to apply the Accounting Policy while preparing the reporting packages which provide basis for compiling of the consolidated financial statement of TAURON Capital Group. The reporting packages are verified by the Office for Consolidation and Reporting in the parent company as well as by the independent auditor during examination or review of consolidated financial statements of TAURON Capital Group.

Procedures of authorisation and reviewing of financial statements of the Company and consolidated financial statements of TAURON Capital Group

In the Company, procedures of authorisation of financial statements have been implemented. Quarterly, semi-annual and annual financial statements of the Company as well as consolidated financial statements of TAURON Capital Group are approved by the Company Management Board before publication. The annual financial statements of the Company as well as consolidated financial statements of TAURON Capital Group are additionally presented for review by the Company Supervisory Board before publication. The Vice President of the Board, Chief Financial Officer supervises the preparation of financial statements, whereas management boards of companies covered by consolidation are responsible for compiling of the reporting packages for the TAURON Capital Group consolidated financial statement.

In the structures of the Company Supervisory Board, the Audit Committee of the Supervisory Board of TAURON Polska Energia S.A. operates, whose composition, competence and description of activities is included in item 6.11.3 of this report.

IT systems and financial and accounting processes

Companies of TAURON Capital Group keep ledgers providing basis for the preparation of financial statements in the computer financial and accounting systems of ERP class. The consolidated financial statements are prepared using the IT tool designed for consolidation of financial statements.

In the companies of TAURON Capital Group IT and organizational solutions operate which control the access to financial-accounting systems and provide adequate protection and archiving of the ledgers. Access to IT systems if restricted by relevant authorisations for the entitled employees.

In connection with the integration of the accounting function and the transfer of the financial and accounting service of individual companies of TAURON Capital Group to CUW-R, gradual harmonisation of financial and accounting processes in TAURON Capital Group took place. Companies adjust own procedures to the financial and accounting processes, taking into account the specific character of individual segments.

The new Business Model clearly distributed responsibilities in the scope of financial and accounting processes between the Company (indicated as the Corporate Centre) and subsidiaries and CUW R, indicating that the Corporate Centre is the owner of processes associated with accounting and reporting of TAURON Capital Group. In the scope of 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 implementation of standards in accounting area in subsidiaries and CUW R. Moreover, it was indicated that the Company as the Corporate Centre is responsible for drawing up the Company financial statement of and the consolidated financial statement of TAURON Capital Group. A clear distribution of responsibilities and strong emphasis on fulfilment of supervisory functions by the Corporate Centre in relation to CUW R and the subsidiaries is, inter alia, aimed at improvement of the process of financial statement preparation.

Internal audit

In the Company Internal Audit Team operates whose objective is to plan and implement the auditing tasks, among others, of advisory nature, as well as to perform the commissioned ad hoc inspections. The procedures and rules of implementation of the audit are specified in *Regulations of Internal audit in TAURON Group* as well as in rules of cooperation binding in individual companies of TAURON Capital Group. While implementing the function of internal audit, the Company acts in compliance with the TAURON Group's Code of Ethics and International Standards of Internal Audit Professional Practice.

Submission of financial statements of the Company and consolidated financial statements of TAURON Capital Group to examination or review by an independent chartered accountant

Annual financial statements of the Company and consolidated statements of TAURON Capital Group are subject to examination by an independent auditor. Semi-annual financial statements of the Company and semi-annual consolidated statements of TAURON Capital Group are subject to review by a chartered accountant. In 2016 the Company selected the entity authorised to examine and review financial statements for significant companies of TAURON Capital Group as well as the consolidated financial statement. The agreement with the entity authorised to examine financial statements was concluded for the examination of financial statements for years 2016.

The rule concerning the change of the entity authorised to examine financial statements of the Company and TAURON Capital Group

Pursuant to the resolution of the Supervisory Board of the Company No 343/II/2010 of 27 August 2010, 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 per five 5 financial years. The entity authorised to audit the financial statements of the Company and TAURON Capital Group may perform these activities again after the lapse of two financial years.

6.4. Shareholders holding large blocks of shares

The table below presents shareholders holding, as at 31 December 2016 and as at the day of drawing up this report, directly or indirectly large blocks of shares of the Company.

Table no 37. Shareholders holding large blocks of shares

No.	Shareholders	Number of shares held	Percentage interest in share capital	Number of votes held	Percentage interest in the general 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 (Open Pension Fund)	88,742,929***	5.06%	88,742,929	5.06%

** In accordance with the shareholder's notification of 28 February 2013.*
*** In accordance with the shareholder's notification of 23 March 2011.*
**** In accordance with the shareholder's notification of 28 December 2011.*

Since the day of submission of the previous periodical report, i.e. 9 November 2016, until the date of publication of this report, the Company has not received any notifications from shareholders concerning changes in proprietary structure of significant blocks of shares of TAURON.

During the Ordinary GM convened on 8 June 2016 and the Extraordinary GM convened on 9 November 2015, the following shareholders holding at least 5% of votes at those GMs were present:

1. State Treasury,
2. KGHM Polska Miedź S.A.,
3. Nationale-Nederlanden Otwarty Fundusz Emerytalny (formerly: ING Otwarty Fundusz Emerytalny).

6.5. Owners of securities providing special control rights

In the financial year 2016, the Company did not issue securities which would provide special control rights towards to the Company.

6.6. Limitations in exercising the voting right

Limitations concerning exercising of the voting right are included in § 10 of the Company Articles of Association available on the Company website http://www.tauron-pe.pl/.

The aforementioned limitations on performing of the voting right have been formulated in the following way:

1. The voting right of shareholders holding over 10% of total votes in the Company shall be limited in the way that none of them can exercise more than 10% of the total votes in the Company at the GM.
2. Voting right limitation included in point 1 above does not apply to the State Treasury and entities subsidiary to the State Treasury in the period of time in which the State Treasury together with subsidiary entities subsidiary of the State Treasury has a number of the Company’s shares entitling to performing at least 25% of total votes in the Company.
3. Shareholders’ votes, between which there is a controlling or dependence relationship within the meaning of § 10 of the Articles of Association (Association of Shareholders) are cumulated; in case when the cumulated number of votes exceeds 10% of total votes in the Company, it is subject to reduction. Rules of votes accumulation and reduction are defined in items 6 and 7 below.
4. A shareholder, within the meaning of § 10 of the Articles of Association is every person, including its parent Company and subsidiary, which is entitled directly or indirectly to hold a voting right at the GM on the basis of any legal title; it also applies to a person who does not hold any Company shares, and in particular to a user, pledgee, person entitled on the basis of a depositary receipt under the regulations of the *Act of 29 July 2005 on financial instruments trading*, as well as a person entitled to take part in the GM despite having disposed of shares held after the date of establishing the right to participate in the GM.
5. A parent company and subsidiary company, for the purposes of § 10 of the Articles of Association, is, respectively, understood as a person:
    1) holding a status of a dominating entrepreneur, subsidiary or has both the status of a dominating entrepreneur and a subsidiary, within the meaning of the provisions of the *Act of 16 February 2007* on *competition and consumers’ protection* or,
    2) holding a status of a parent company, a higher level parent company, a subsidiary, a lower level subsidiary or which has both the status of a parent company (including a parent company with a higher status) and a subsidiary (including a lower level subsidiary or co-subsidiary) within the meaning of *Accounting Act* of *29 September 1994*, or
    3) which exerts (a parent company) or which is under (a subsidiary) a determining influence within the meaning of the *Act of 22 September 2006 on the transparency of financial relationships between public bodies and public entrepreneurs and on financial transparency of some entrepreneurs*, or
    4) whose votes resulting from the Company’s shares owned directly or indirectly are subject to accumulation with votes of another person or other persons on conditions defined in the *Act of 29 July 2005 on 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 shares.
6. Accumulation of votes is based on aggregating of the number of votes held by particular shareholders of Shareholders’ Group.

7. Reduction of votes is based on decreasing the total number of votes in the Company that shareholders, who are a part of Association of Shareholders, are entitled to at the General Meeting to the level of 10% of total votes in the Company. Reduction of votes is performed in accordance with the following rules:
    1) number of votes of a shareholder who holds the largest amount of votes in the Company among all shareholders who are members of the Association of Shareholders is subject to reduction by a number of votes equal to surplus of over 10% total number of votes in the Company that all shareholders in total are entitled to hold and who are members of the Association of Shareholders,
    2) if, despite the aforementioned reduction, the total number of votes that shareholders who are members of the Association of Shareholders are entitled to hold exceeds 10% of the total number of votes in the Company, further reduction of votes held by other shareholders who are members of the Association of Shareholders is performed. Further reduction of particular shareholders' votes takes place in order established on the basis of the amount of votes that particular shareholders who are members of the Association of Shareholders hold (from the highest to the lowest one). Further reduction is performed until the moment when the total number of votes held by shareholders who are members of the Association of Shareholders does not exceed 10% of the total number of votes in the Company,
    3) in each case the shareholder whose voting right has been limited shall have the right to exercise at least one vote,
    4) limitation of execution of the voting right also applies to a shareholder absent at the GM.
8. Each shareholder who is going to take part in the GM, directly or through a proxy is obliged to, without a separate notice stipulated referred to in item 9 below, notify the Management Board or the Chairperson of the GM that she/he holds, directly or indirectly, more than 10% of the total number of votes in the Company.
9. Notwithstanding the provisions of item 8 above, in order to establish the basis for accumulation and reduction of votes, the Company's shareholder, the Management Board, the Supervisory Board or particular members of these bodies have the right to demand that the Company shareholder provides information whether she/he is a person holding the status of an entity dominating or subordinate towards other shareholder within the meaning of § 10 of the Articles of Association. The aforementioned entitlement includes also the right to demand revealing the number of votes that the Company's shareholder has independently or jointly with other shareholders of the Company.
10. A person who has failed to fulfil or fulfilled the information obligation stipulated in items 8 and 9 above improperly, until the moment of improvement of the information obligation performed improperly shall have the voting right from one share only; performing voting rights from other shares by such a person shall be null and void.

6.7. Limitations on transfer of securities property rights

As at 31 December 2016 and as at the day of this report, there are no limitations in the Company on the transfer of proprietary rights of Company securities.

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

The Management Board of the Company consists of one to six persons, including the President and Vice-Presidents. Members of the Management Board are appointed for the period of a joint term of office which lasts three years, except for the first term of office which lasted two years.

Members of the Management Board or the whole Management Board are appointed and dismissed by the Supervisory Board. Each of the Management Board members can be dismissed or suspended in office by the Supervisory Board or the GM.

Competence of the Management Board

The Management Board handles the Company's affairs and represents the Company in all court and out-of-court activities. All issues connected with managing of the Company affairs not restricted by any legal regulations or provisions of the Company Articles of Associations to the competence of the GM or the Supervisory Board lie within the competence of the Management Board.

In accordance with the Company Articles of Association, all issues which go beyond the regular scope of Company activities require the resolution of the Management Board, in particular, the following issues listed in the table below:

Table no 38. Competence of the Management Board

Issues requiring resolution of the Management Board
as at 31 December 2016 and as at the day of this report

1. bylaws of the Management Board,
2. organizational regulations of the Company enterprise,
3. establishment and liquidation of branches,
4. appointment of a proxy,
5. Incurring credits and loans,
6. adopting annual material and financial plans of the Company and the Capital Group, and the Corporate Strategy of the Capital Group,
7. incurring contingent liabilities within the meaning of the *Accounting Act of 29 September 1994*, including granting guarantees and sureties by the Company as well as issuing bills of exchange, subject to § 20 section 2 items 4 and 5 of the Company Articles of Association,
8. making donations, redemption of interest or discharge from debt, subject to § 43 item 2 p.1 and 2 of the Company Articles of Association,
9. purchase of real property, perpetual usufruct or shares in property or in perpetual usufruct, subject to § 20 item 2 p. 1 of the Company Articles of Association,
10. purchase of components of fixed assets excluding real property, perpetual usufruct or share in real property or perpetual usufruct, with the value equal to or exceeding the equivalent of EUR 10 thousand in PLN, subject to the provisions of § 20 section 2 item 2 of the Company Articles of Association,
11. disposal of the components of fixed assets including real property, perpetual usufruct or share in real property or perpetual usufruct, with the value equal to or exceeding the equivalent of EUR 10 thousand in PLN, subject to the provisions of § 20 section 2 item 3 of the Company Articles of Association,
12. defining exercising a voting right at GMs or at SMs of companies in which the Company holds stocks or shares, in relation to issues covered by the competence of the GM or SM of such companies, subject to the provisions of § 20 section 3 item 9 of the Company Articles of Association,
13. rules of conducting sponsoring activity,
14. adoption of the annual plan of sponsoring activity,
15. issues, whose examination the Management Board refers to the Supervisory Board or to the GM.

6.8.2. Supervisory Board

Rules on appointing and dismissing members of the Supervisory Board

The Supervisory Board consists of five to nine persons, appointed for the joint term of office which lasts three years, except for the first term of office which lasted one year. In accordance with the Company Articles of Association, members of the Supervisory Board are appointed and dismissed by the General Meeting, subject to the following provisions:

1) in the period, in which the State Treasury, including, together with entities dependent on the State Treasury within the meaning of § 10 item 5 of the Articles of Association, holds a number of shares of the Company authorising to exercise at least 25% of the total number of votes in the Company, the State Treasury is represented by the minister competent for the State Treasury affairs, is entitled to appoint and dismiss members of the Supervisory Board in the amount equal to half of the maximum number of the composition of the Supervisory Board defined in the Articles of Association (if the number is not integral it is rounded down to an integral number, for example 4.5 is rounded down to 4 increased by 1, provided that the State Treasury:
   a) is obliged to vote at the GM on determining the number of Supervisory Board members corresponding to the maximum number of Supervisory Board members defined in the Articles of Association or in case of submitting such a motion to the Management Board by a shareholder or shareholders who hold a number of votes authorising to exercise at least 5% of the total number of votes in the Company,
   b) is excluded from the voting right at the GM concerning appointing and dismissing of other members of the Supervisory Board, including independent members of the Supervisory Board; it does not, however, apply to the case when the Supervisory Board cannot act due to a composition smaller than required by the Articles of Association, and the shareholders present at the GM other than the State Treasury do not supplement the composition of the Supervisory Board in accordance with the distribution of places in the Supervisory Board defined in this item;
2) in the period of time in which the State Treasury, together with entities dependent on the State Treasury within the meaning of § 10 item 5 of the Articles of Association, has a number of the Company’s shares entitling to perform under 25% of total voting rights in the Company, the State Treasury, represented by a minister competent for the issues of the State Treasury shall be entitled to appoint and dismiss one member of the Supervisory Board.
3) appointing and dismissing of members of the Supervisory Board by the State Treasury pursuant to the aforementioned item 1) or item 2) takes place by means of a statement submitted to the Company.

At least two members of the Supervisory Board should meet the criteria of independence (independent members of the Supervisory Board). The definition of an *independent member of the Supervisory Board* shall mean an independent member of the supervisory board within the meaning the Recommendation of the European Commission of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board (2005/162/EC), taking into consideration Best Practice of Warsaw Stock Exchange (GPW) Listed Companies.

Independent members of the Supervisory Board submit a written declaration of having fulfilled the prerequisites of independence to the Company, before being appointed to the Supervisory Board. In case of a situation causing failure to fulfil the of independence, a member of the Supervisory Board is required to immediately notify the Company of this fact. The Company shall inform shareholders of the current number of independent members of the Supervisory Board.

Competence of the Supervisory Board

The Supervisory Board carries out continuous supervision over the Company's activities in all areas of its operations.

In accordance with the Company Articles of Association, the tasks and competences of the Supervisory Board include, in particular the following issues listed in the table below:

Table no 39. Competence of the Supervisory Board

Issues requiring the resolution of the Supervisory Board	
as at 31 December 2016 and as at the day of drawing up this report	
Opinion-making competence	
1.	assessment of the Management Board report on the Company operations as well of the financial statement for the previous financial year in the scope of their compliance with the books, documents as well as with the actual status. It also applies to the consolidated financial statement of the Capital Group, provided that it is generated,
2.	assessment of the Management Board conclusions on profit distribution or loss coverage,
3.	submitting of a written report to the General Meeting on the results of operations covered by items 1 and 2,
4.	preparation once a year and submission 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 operating activity, 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.	preparing, together with the report on results of the annual financial statement of the Company, an opinion of the Supervisory Board on the issue of economic legitimacy of involving the Company capital committed in a given financial year in other entities of commercial law,
6.	giving opinions on the Corporate Strategy of the Capital Group,
7.	giving opinions and approval of the rules of conducting sponsoring activity,
8.	giving opinions on the annual plan of conducting of the sponsoring activity as well as annual reports on its implementation,
Decision-making competence	
1.	selecting of the chartered accountant to carry out the examination of the Company financial statement and consolidated financial statement of the Capital Group,
2.	determining the scope and deadlines of submitting of annual material and financial plans as well as long-term strategic plans of the Company and the Capital Group, by the Management Board,
3.	adopting of consolidated text of the Company Articles of Association, prepared by the Company Management Board,
4.	approval of the bylaws of the Company Management Board,
5.	approving of the organisational regulations of the Company enterprise.
6.	purchase of real property, perpetual usufruct or shares in property or in perpetual usufruct with the value exceeding the equivalent of EUR 5,000 thousand in PLN, excluding the real property or perpetual usufruct, or share in real property or in perpetual usufruct acquired from companies of the Capital Group,
7.	purchase of components of fixed assets excluding real property, perpetual usufruct or share in real property or perpetual usufruct, bonds issued by companies of the Capital Group and other components of fixed assets acquired from companies of the Capital Group, of the value equal to or exceeding the equivalent of EUR 5,000 thousand in PLN,
8.	disposal of components of fixed assets, including real property, perpetual usufruct or share in real property or perpetual usufruct, of the value equal to or exceeding the equivalent of EUR 5,000 in PLN, excluding the real property or perpetual usufruct, or share in real property or in perpetual usufruct, as well as other components of fixed assets which, as a result of the disposal, shall be sold or encumbered to the benefit of companies of the Capital Group,

Issues requiring the resolution of the Supervisory Board	
as at 31 December 2016 and as at the day of drawing up this report	
9.	incur contingent liabilities, including granting guaranties and sureties by the Company with the value exceeding the equivalent of EUR 5,000 in PLN,
10.	issuing bills of exchange with the value exceeding the equivalent of EUR 5,000 in PLN,
11.	advance payment on account of the expected dividend,
12.	taking over or purchase of shares or stocks in companies other than Companies of the Capital Group, with the value exceeding the equivalent of 5,000 EUR in PLN, excluding the situations when the takeover of stocks or shares of such companies occurs in exchange for Company liabilities under the composition or bankruptcy proceedings,
13.	disposal of stocks or shares with the value exceeding the equivalent of EUR 5,000 in PLN, including defining of the conditions and procedure for their disposal, excluding: a) disposal of shares which are traded on the regulated market, b) disposal of stocks or shares that the Company holds in the amount not exceeding 10% share in the initial capital of particular companies, c) disposal of shares or stocks to the benefit of Companies of the Capital Group,
14.	concluding of the material agreement with the shareholder holding at least 5% of the total number of votes in the Company or an affiliate, excluding transactions typical and concluded under market terms within operations conducted by the Company with entities included in TAURON Capital Group,
15.	granting permission to establish Company branches abroad,
16.	defining the method of performing the voting right at the GM or at the SM of companies in which the Company holds over 50% of stocks or shares, in the following matters: a) disposal and leasing of the Company enterprise or its organised part as well as establishing a limited proprietary right thereupon if their value exceeds the equivalent of the amount of EUR 5,000 in PLN, b) winding up and liquidation of the Company.
Competence of the Company Supervisory Board related to the Management Board	
1.	appointing and dismissing members of the Management Board,
2.	establishing the rules of remuneration and the level of remuneration for the Members of the Management Board, subject to § 43 item 1 p.1 of the Company Articles of Association,
3.	suspending members of the Management Board in performance of their duties, due to material reasons,
4.	delegating members of the Supervisory Board to temporarily perform actions of the members of the Management Board who cannot perform their duties and establishing their remuneration subject to the provision that the total remuneration of the person delegated as the Supervisory Board's member as well as on account of being delegated to temporary performing actions of a member of the Management Board shall not exceed the remuneration established for the member of the Management Board, for whom the member of the Supervisory Board was delegated,
5.	conducting recruitment proceedings for the position of a Management Board member,
6.	conducting of a competition in order to select a person with whom an agreement to perform management in the Company shall be concluded,
7.	granting permission to the Management Board members to take positions in governing bodies of other companies.
Other competences of the Company Supervisory Board	
1.	preparing reports of the Supervisory Board on supervision of implementation of investments by the Management Board, including the purchase of fixed assets, and in particular, giving opinions on the correctness and effectiveness of spending financial resources related to the above expenditures,
2.	adopting by-laws describing in detail the procedures of performance of the Supervisory Board.

6.9. Description of the procedure of amendment of the Company Articles of Association

Amendments to the Company Articles of Association in accordance with the provisions of the Ksh, in particular: amendments to the Company 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 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 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.

The GM on 8 June 2016 adopted the resolution concerning the amendments to the Company Articles of Association; the relevant information was provided in section 2.7. hereof.

6.10. Way of operating of the General Meeting, its fundamental authorities and description of shareholders' rights and mode of their performance

The way of operating of the Company GM and its powers are included in the Company Articles of Association and in the *Regulations of the General Meeting of TAURON Polska Energia S.A.* which are available at the Company website http://www.tauron-pe.pl/.

Operation of the General Meeting

The General Meeting is convened by announcement on the Company website and in the manner defined for providing current information by public companies. In case the GM is convened by an entity or body other than the Management Board on the basis of CCC provisions, and the convening of the GM requires cooperation with the Management Board, the Management Board is obliged to perform all actions defined under legal regulations in order to summon, organise and conduct the GM which shall take place in the Company registered office or in Warsaw.

The GM is opened by the Chairperson of the Supervisory Board, and in case of his/her absence the following persons shall be authorised to open the GM in the following order: Vice-Chairperson of the Supervisory Board, President of the Management Board, a person appointed by the Management Board or a shareholder who registered shares authorising him/her to exercise the largest number of votes at the GM. Subsequently, among persons authorised to take part in the GM the Chairperson of the Meeting is selected.

The GM shall adopt resolutions irrespective of the number of shares represented at the Meeting, unless the provisions of the CCC as well as provisions of the Company Articles of Association state otherwise. The General Meeting may order the adjournment of the meeting by the majority of two thirds of votes. In total, the breaks shall not exceed 30 days.

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

In accordance with the Company Articles of Association, the following issues listed in the table below require Resolutions of the GM.

Table no 40. Competence of the General Meeting

Issues which require the resolution of the General Meeting	
as at 31 December 2016 and as at the day of drawing up this report	
1.	examination and approval of financial statement of the Company and the consolidated financial statement of TAURON Capital Group for the previous financial year as well as the Management Board's report on the Company operations and the Management Board's report on the operations of TAURON Capital Group,
2.	granting the acknowledgement of the fulfilment of duties to the members of the governing bodies of the Company,
3.	profit distribution and coverage of loss,
4.	appointing and dismissing of members of the Supervisory Board,
5.	suspending members of the Management Board in performance of their duties,
6.	establishing the rules of remuneration for the members of the Supervisory Board, subject to § 29 item e of the Company Articles of Association,
7.	disposal and lease of the Company enterprise or its organized part as well as establishing a limited proprietary right on them,
8.	concluding of a credit, loan, surety agreement or any other similar agreement by the Company with a member of the Management Board, Supervisory Board, proxy and liquidator or for any of these persons. Concluding of a loan, surety or any other similar agreement with a member of the Management Board, Supervisory Board, a proxy, a liquidator or in favour of any of those persons,
9.	increasing and lowering the share capital of the Company,
10.	issue of convertible bonds or priority bonds as well as registered securities or bearer securities authorising its owner to subscribe or acquire the shares,
11.	purchasing treasury shares in cases required by the regulations of the CCC,
12.	compulsory redemption of shares pursuant to the stipulations of Article 418 of the CCC,
13.	creating, using and liquidation of reserve capitals,
14.	using of supplementary capital,
15.	provisions concerning claims to repair a damage caused while establishing a Company or providing management or supervision,
16.	merger, transformation and division of the Company,
17.	redemption of shares,
18.	amendment to the Articles of Association and change of the scope of the Company operations,
19.	dissolving and liquidation of the Company.

In accordance with the provisions of the CCC the decision on issue and repurchase of shares in included in the competence of the General Meeting.

Description of shareholders' rights and mode of their execution

The table below presents the description of rights of the Company shareholders associated with the General Meeting, in accordance with the Company Articles of Association, CCC and the *Regulations of the General Meeting of TAURON Polska Energia S.A.*

Table no 41. Description of the Company shareholders' rights associated with the General Meeting

No.	Shareholder rights	Description of shareholders' rights
1.	Convening of the GM	A shareholder or shareholders representing at least one twentieth part of the share capital, may demand convening of the Extraordinary GM. Such a demand should include a concise justification. It can be submitted to the Management Board in writing or send in electronic form, to the Company e-mail address, indicated by the Company on at its website in "Investor Relations" tab. A shareholder or Shareholders representing at least a half of the share capital or at least a half of all votes in the Company may convene the Extraordinary GM and appoint the Chairperson of this Meeting.
2.	Placing issues on the agenda of the GM	Shareholders representing at least one twentieth of the share capital may demand including certain issues on the agenda of the nearest GM. Such a demand, including a justification or a draft resolution on the proposed item on the agenda shall be submitted to the Management Board not later than 21 days before the determined date of the GM in electronic form to the Company e-mail address, or in writing to the Company address.
3.	Getting acquainted with the list of shareholders	Shareholders may become acquainted with the shareholders' list in the Company Management Board registered office during three working days directly preceding the GM. Shareholders may demand sending him/her a list of shareholders free of charge by electronic mail, providing the address to which the list shall be sent.
4.	Participation in the GM	The right to take part in the GM shall be granted only to persons who were shareholders sixteen days before the date of the GM (registration date in the GM). In order to participate in the GM shareholders should submit a request to issue a certificate addressed to their name, concerning the right to take part in the GM to the investment Company holding their securities account. Such a request shall be submitted not earlier than a day after the announcement on convening of the GM and not later than on the first working day following the day of registering participation in the GM.
5.	Representing the shareholder by a proxy	Shareholders may take part in the GM as well as exercise the voting right personally or through a proxy. Persons co-authorized by means of shares may take part in the General Meeting and perform the voting right only through a joint representative (a proxy). The proxy may represent more than one Shareholder and vote differently based on shares of each Shareholder.
6.	Election of the Chairman of the General Meeting	Shareholders select the Chairperson among persons entitled to take part in the GM. Each of the members of the GM shall have the right to submit one candidate to the post of the Chairperson. The election of the Chairperson takes place under secret ballot, with an absolute majority of votes. In case if only one candidate has been registered, the election can take place by acclamation.
7.	Appointment of the Returning Committee	Each Shareholder shall submit no more than three candidates to the member of Returning Committee, selected by the GM and vote for maximum three candidates.
8.	Submission of draft resolution	Until closing the discussion on a certain point of the agenda of the GM shareholders shall be authorised to submit a proposal of changes to the content of a draft of resolution proposed for adoption by the GM within a given item of the agenda or to put forward his/her draft of such a resolution. The proposal of changes or a draft of the resolution may be submitted in writing to the Chairperson or orally to the minutes of the meeting.
9.	Raising objections	Shareholders who voted against a resolution, and after its adoption by the GM want to raise their objection shall immediately after the announcement of results of voting raise their objection and demand its including in the minutes before proceeding to the next item of the agenda. In case of raising an objection at a later time which, however, shall not take place later than until closing of the GM, shareholders shall indicate which resolution passed at this GM they challenge. Shareholders raising their objection against the GM resolution may submit a concise justification of the objection to the minutes of the GM.

6.11. Composition of managing and supervising bodies and their committees, its changes, description of performance

6.11.1. Management Board

The current, fourth term of office of the Management Board began to run on 17 March 2014, i.e. on the day of dismissal of all members of the Management Board of the third term by the Supervisory Board, and the appointment of the Management Board of the Company for the fourth common term of office. In accordance with the Company Articles of Association the common term of office lasts three years.

Personal composition of the Management Board as at 31 December 2016 and as at the day of 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 Corporate Management,
4. Marek Wadowski – Vice-President of the Management Board for Finance,
5. Piotr Zawistowski – Vice-President of the Management Board for Customer and Commercial Affairs.

Changes in the personal composition of the Management Board in 2016 and in the period until the day of drawing up this report

As at 01 January 2016 the Management Board consisted of the following members: Remigiusz Nowakowski (President of the Management Board), Jarosław Broda (Vice-President of the Management Board), Anna Striżyk (Vice-President of the Management Board), Kamil Kamiński (Vice-President of the Management Board) and Piotr Zawistowski (Vice-President of the Management Board).

On 8 January 2016 the Supervisory Board dismissed Anna Striżyk – Vice-President of the Management Board for Economics and Finance, from the Management Board.

As of 29 January 2016, the Supervisory Board appointed Marek Wadowski as Vice-President of the Management Board for Economics and Finance.

On 14 November 2016, the Supervisory Board dismissed Remigiusz Nowakowski – the President of the Management Board from the Management Board.

As of 15 November 2016, the Supervisory Board appointed Filip Grzegorczyk as the President of the Management Board.

Until the day of submission of this report, no other changes in the composition of the Management Board have taken place.

Experience and competences of members of the Management Board

Filip Grzegorczyk – President of the Management Board

Graduate of the Faculty of Law and Administration and the Faculty of International and Political Studies at the Jagiellonian University in Kraków, where he obtained the title of PhD in EU law, and then also his habilitation in the field of the economic law.

He also completed the Summer Advanced Course in European Law at University of London, King's College, Centre of European Law; the International Business and Trade Summer School at Catholic University of America – Columbus School of Law and École de droit français Université d'Orléans. He holds the position of professor at the University of Economics in Kraków, where he is a lecturer at the Faculties of Management and Economics and International Relations.

He has broad professional experience in energy and fuel sector. In 2011–2013, he worked for Kompania Węglowa (as management board proxy for energy sector development). In 2007–2008 he was a member of the management board of TAURON. Since November 2015 he worked as the Undersecretary of State at the Ministry of State Treasury. He speaks English and French fluently.

Acting as the President of the Management Board of TAURON Polska Energia S.A. since 15 November 2016. He currently supervises the performance of the following business units: strategy and regulations, relations with the environment, legal and internal audit. In addition, he supervises the functioning of security, compliance and risk management system as well as human resources development policy.

Jarosław Broda – Vice-President of the Management Board

Graduate of Warsaw School of Economics, holder of a postgraduate diploma in project management at Kozminski University.

Holds experience in the area of consolidation and operation of the energy sector, privatisation of state-owned energy groups, development of processes associated with the restructuring and strategy building as well as development projects of energy entities.

Since the beginning of his professional career he has been associated with energy sector 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 preparation of the company development strategy, regulatory management and M&A projects. He also participated in drafting of sales and marketing development strategy in Europe. From mid-2015 he was responsible for the development of the commercial strategy and contract for difference under a nuclear project in Great Britain.

Acting as the Vice President of the Management Board of TAURON Polska Energia S.A. since 08 December 2015. He currently supervises the performance of the following business areas: asset management, research and innovation, investment projects, project assessment and analyses and occupational health and safety.

Kamil Kamiński – Vice-President of the Management Board

Graduate of the Faculty of Management and Communications of Jagiellonian University. The holder of MBA Executive diploma (Stockholm University School of Business/ Cracow University of Economics) and post-MBA Diploma in Strategic Financial Management (Rotterdam School of Management, Erasmus University/ GFKM).

He has broad experience in the area of building company value, mergers and acquisitions, business integration, strategy operationalization as well as management of complex projects in public and private sectors. He took part in complex transformation and restructuring processes of enterprises in the sectors of energy and fuel and transport logistics.

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 consolidation of electricity and heat generation assets of Kompania Węglowa and Węglokoks. At that time he managed the works of the Management Committee. Previous professional experience includes, among other things, work at the Research and Development Centre of the Refining Industry (OBR) in Płock or Jan Paweł II International Airport in Kraków-Balice. 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 aviation fuel segment, which resulted in the joint venture with Air BP Ltd. and establishment of Lotos Air BP.

He has been acting in the capacity of the Vice-President of the Management Board of TAURON Polska Energia S.A. since 8 December 2015. As Vice-President of the Management Board for Corporate Management he oversees the following areas of the Company's operation: corporate matters and support, human resources, procurement and administration, security and compliance.

Marek Wadowski – Vice President of the Management Board

Graduate of University of Economics in Katowice. He also completed post graduate studies École Supérieure de Commerce Toulouse where he obtained Mastère Spécialisé en Banque et Ingéniere Financière diploma and Executive MBA studies at Kozminski University in Warsaw.

He has professional experience in the field of accounting, controlling and financial processes management in industry (power sector, mining, metallurgical industry), as well as in financing of investments and international commercial transactions. He took part in the implementation of due diligence projects and enterprise valuation (using income-based, equity and comparison valuation methods).

Since the beginning of his professional career, he has been associated with energy, mining and metallurgical sector entities, having acted in the capacity of the President or the Vice-President of the Management Board and holding senior executive positions. He gained his professional experience working for BRE Corporate Finance S.A., Huta Cynku Miasteczko Śląskie S.A. and in companies of Jastrzębska Spółka Węglowa S.A. Capital Group. From 2008, acting in the capacity of the Vice-President of the Management Board in charge for the financial division in companies of Jastrzębska Spółka Węglowa Capital Group, he was responsible, inter alia, for structuring of commercial transactions, implementation of foreign exchange risk hedging policy, financial costs reduction, liquidity management, acquisition of funds from the consortium of banks in the form of a bond issue programme. He also took part in the IPO of Jastrzębska Spółka Węglowa S.A. (implementation of International Accounting Standards, modification of management information system, development of IPO prospectus, talks with investors). He acted in the capacity of the President of the Management Board at Towarzystwo Finansowe Silesia where he was involved in bond issue program for Kompania Węglowa and dealt with the acquisition of debt financing from the consortium of banks.

Acting as the Vice President of the Management Board of TAURON Polska Energia S.A. since 29 January 2016. Currently supervises performance of the following business units: finance, controlling, accounting and taxes, risk and IT.

Piotr Zawistowski – Vice President of the Management Board

Graduate of Wrocław University of Economics where he completed MA studies in Enterprise Management. He also completed postgraduate studies in Sales Management at WSB University in Wrocław. He is a Commodity Exchange Broker.

He has experience in the area of trading in electricity, gas and related products in the country and abroad, commercial risk management, portfolio management in the scope of purchase and sales of electricity, property rights, CO_2 emission allowances and fuels. He took active part in works related to unbundling of electricity supply and distribution, in particular in establishment of EnergiaPro Gigawat (currently a part of TAURON Sprzedaż).

Since the beginning of his professional career he has been associated with energy sector entities, holding senior executive and managerial positions. He gained his professional experience working at Zakład Energetyczny Legnica, EnergiaPro Koncern Energetyczny (currently a part of TAURON Dystrybucja), EnergiaPro Gigawat and at TAURON, where he acted in the capacity of Portfolio Management Department from 2008, participating in many key projects, managing, among others, the works related to the development of the business model of TAURON Group or integration with GZE Group companies (Vattenfall) in the trading segment. From May 2014 he acted in the capacity of the President of the Management Board of TAURON Obsługa Klienta.

He has been acting in the capacity of the Vice-President of the Management Board of TAURON Polska Energia S.A. since 8 December 2015. As Vice-President of the Management Board for Customer and Commercial Affairs he oversees the following areas of the Company's operation: customers, analyses and planning, fuel trading, portfolio management, trading, settlements and sales reporting.

The detailed description of experience and competences of Management Board members is published on the Company website http://www.tauron.pl/.

Description of operation

The Management Board of the Company operates on the basis of Ksh and other regulations of law, provisions of the Company Articles of Association and provisions of the *Bylaws of the Management Board of TAURON Polska Energia Spółka Akcyjna z siedzibą w Katowicach*, which is available on the website of the Company http://www.tauron-pe.pl/. While performing their obligations, members of the Management Board are driven by the rules included in Best Practice.

Cooperation of two members of the Management Board or one member of the Management Board together with a proxy is required for submitting of statements on behalf of the Company. Should the Management Board be single person, one member of the Management Board or a proxy shall be entitled to submit statements on behalf of the Company.

Meetings of the Management Board are convened by the President of the Management Board or a Vice-President of the Management Board appointed by him/her. Meetings of the Management Board are also convened upon the motion of the majority of Vice-Presidents of the Management Board as well as upon the motion of the Chairperson of the Supervisory Board. The meetings take place in the Company's seat, on the date set by the person convening the meeting. In justified cases, the Management Board's meetings may take place outside the seat of the Company. The President of the Management Board or the Vice-President appointed by him/her shall chair meetings of the Management Board.

The Management Board votes in an open ballot. Results of the voting are recorded in the minutes of the meeting. The President of the Management Board orders a secret ballot on request of any Vice-Presidents of the Management Board.

Resolutions of the Management Board are passed by an absolute majority of votes in the presence of 3/5 of the Management Board members. In case of an equal number of votes the President of the Board has a casting vote. The Management Board may pass resolutions in a written mode or by using means of direct remote communication. Voting in the aforementioned modes is ordered by the President of the Management Board or the Vice-President appointed by him/her, defining the deadline to vote by the members of the Management Board. It is acceptable to submit a different opinion. It shall be recorded in the minutes together with justification. Decisions of the Management Board, regulating business as usual, not requiring a resolution, are recorded only in the minutes.

Whenever there are less Vice-Presidents of the Management Board than Divisions, Vice-Presidents of the Management Board may combine responsibilities within two divisions, or distribute their competence in any other way which is compliant with the distribution of responsibilities adopted by the Supervisory Board.

Scope of activities of the President of the Management Board covers competence in the area of operations of business units reporting to the Division of the President of the Board, in accordance with the organisational structure of the Company.

Scope of activities of the Vice-Presidents of the Management Board covers competence in the area of operations of business units reporting to the Divisions of the Vice-Presidents of the Board, in accordance with the organisational structure of the Company.

The structure of the divisions reporting to individual members of the Management Board is specified in the organisational chart of the Company, presented in item 1.6.2 of this report.

6.11.2. Supervisory Board

The current, fourth term of office of the Supervisory Board, started on 15 May 2014, i.e. on the day of convening of the Ordinary General Meeting of the Company approving the financial statement for the last full financial year of the tenure of the members of the Supervisory Board of the third term, i.e for the financial year 2013. In accordance with the Company Articles of Association this is a joint term of office and it shall last for three years.

Personal composition of the Supervisory Board as at 31 December 2016 and as at the date of drawing up this report

1. Beata Chłodzińska – Chairwoman of the Supervisory Board,
2. Anna Mańk – Deputy Chairwoman of the Supervisory Board,
3. Jacek Szyke – Secretary of the Supervisory Board,
4. Stanisław Bortkiewicz – Member of the Supervisory Board,
5. Leszek Koziorowski – Member of the Supervisory Board,
6. Jan Płudowski – Member of the Supervisory Board,
7. Jacek Rawecki – Member of the Supervisory Board,
8. Stefan Świątkowski – Member of the Supervisory Board,
9. Agnieszka Woźniak – Member of the Supervisory Board.

Changes in the personal composition of the Supervisory Board in 2016

As at 1 January 2016 the Supervisory Board consisted of the following Members: Beata Chłodzińska (Chairwoman of the Supervisory Board), Anna Mańk (Deputy Chairwoman of the Supervisory Board), Jacek Szyke (Member of the Supervisory Board), Anna Biesialska (Member of the Supervisory Board), Michał Czarnik (Member of the Supervisory Board), Maciej Koński (Member of the Supervisory Board), Leszek Koziorowski (Member of the Supervisory Board), Wojciech Myślecki (Member of the Supervisory Board) and Renata Wiernik-Gizicka (Member of the Supervisory Board).

On 6 June 2016 the Company received statements from the following Supervisory Board Members concerning the resignation from the function of Member of TAURON Polska Energia S.A. Supervisory Board, in which they declared that they had resigned for personal reason:

1) Maciej Koński,
2) Renata Wiernik-Gizicka.

On 8 June 2016 the Ordinary GM of the Company, acting pursuant to § 22 (1) of the Company Articles of Association, adopted the resolution on the appointment of the following members to the Company Supervisory Board of the common fourth term of office:

1) Jacek Rawecki,
2) Stefan Świątkowski.

On 14 November 2016 a Member of the Supervisory Board, Wojciech Myślecki submitted his resignation from the function of Member of TAURON Polska Energia S.A. Supervisory Board. (No reasons of submitted resignation were provided).

On 16 December 2016 the Minister of Energy, acting pursuant to § 23(1)(3) of the Company Articles of Association appointed Agnieszka Woźniak as a member of the Supervisory Board of TAURON Polska Energia S.A.

On 30 December 2016 the Minister of Energy, acting pursuant to § 23(1)(3) of the Company Articles of Association,

- dismissed the following members of the Supervisory Board of TAURON Polska Energia S.A.:
  1) Michał Czarnik,
  2) Anna Biesialska,
- appointed the following members of the Supervisory Board of TAURON Polska Energia S.A.:
  1) Jan Płudowski,
  2) Stanisław Bortkiewicz.

Until the day of submission of this report, no other changes in the composition of the Supervisory Board have taken place.

Experience and competences of members of the Supervisory Board

Beata Chłodzińska – Chairwoman of the Supervisory Board

Graduate of the Faculty of Law and Administration of Warsaw University. She is a legal counsel.

She has professional experience associated with supervising companies with State Treasury ownership. Professionally affiliated with the Ministry of Energy, currently coordinating the activities of the Team of Legal Counsels at the Legal Office. She represented the State Treasury on supervisory boards of companies supervised by the Ministry.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 12 August 2015. Currently acting in the capacity of the Chairwoman of the Supervisory Board as well as the Chairwoman of the Nominations and Remunerations Committee, a member of the Audit Committee of the Supervisory Board and the Strategy Committee of the Supervisory Board.

Anna Mańk – Deputy Chairwoman of the Supervisory Board

Graduate of Warsaw School of Economics and postgraduate studies in financial and economic law at University of Łódź.

She has professional experience in the scope of supervision and ownership transformations at the Ministry of State Treasury. Professionally associated with the Ministry of State Treasury, holding senior executive positions, currently acting in the capacity of Director General of the Ministry of State Treasury in liquidation, acting as the liquidator. She represented the State Treasury on supervisory boards of companies supervised by the Ministry, including those listed on the GPW.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 2 December 2015. Currently acting in the capacity of Deputy Chairwoman of the Supervisory Board and a member of the Strategy Committee of the Supervisory Board.

Jacek Szyke – Secretary of the Supervisory Board

Graduate of Faculty of Economics at Łódź University and Electric Faculty of Technical University in Poznań, where he also obtained PhD in technical sciences.

He has broad professional experience associated with power industry where he had climbed through all levels in the career ladder, working both in the country and abroad. Holding senior executive and managerial positions he worked, inter alia, at ZE Kalisz, EC Łódź, ZE Płock and EC Siekierki. He is an honorary President of the Chamber of Power Engineering and Energy Consumers. He is a consultant in electrical engineering matters. Author of many improvement recommendations, designs, publications and books on energy industry and power engineering.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 14 September 2010. Currently acting in the capacity of the Secretary of the Supervisory Board, Chairman of the Strategy Committee of the Supervisory Board and the Member of the Audit Committee of the Supervisory Board.

Stanisław Bortkiewicz – Member of the Supervisory Board

Graduate of Medical University of Gdańsk, medical doctor, manager, entrepreneur and business adviser with experience gained over the years.

He has rich experience in the scope of managing large production and service companies as well as in the scope of consulting, training and restructuring activity. He acted in the capacity of President of the Management Board of large companies many times, including, inter alia: Pracownicza Spółka Ursus S.A., ZPC Ursus S.A., MPWiK S.A. In Warsaw and Director for Strategy and Development at BOT Górnictwo i Energetyka S.A., and subsequently, at PZU S.A. Since 1990 he has been conducting own economic activity and he is the shareholder of economic, commercial, production and service entities. He also carried out consulting activity, providing advisory services to many large companies. In the framework of his professional activity he carried out many projects in the scope of organisational and financial restructuring of enterprises. Since February 2016 he has been acting in the capacity of Director of Office for Corporate Affairs in Telewizja Polska S.A.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 30 December 2016. Currently acting as the Chairman of the Audit Committee of the Supervisory Board.

Leszek Koziorowski – Member of the Supervisory Board

Graduate of Faculty of Law and Administration of Warsaw University, legal counsel in the Regional Chamber of Attorneys in Warsaw.

He has rich experience in the scope of securities law, which he gained as a counsel in the Securities Commission, arbitrator in the Stock Exchange Court at the Warsaw Stock Exchange and in Arbitration Court at the Private Employers' Organisation "Lewiatan", and a judge of the Stock Exchange Court. At present, he is the general partner in a law firm where he deals with legal advice in the scope of capital market law and preparation of companies for listing at the stock exchange. Author of numerous publications concerning capital market law, received multiple recommendations as the best legal counsel in Poland in the aforementioned scope. He was the member of numerous supervisory boards.

Appointed as the member of the Supervisory Board of TAURON Polska Energia S.A. as of 14 September 2010, he acted as the member of the Supervisory Board in the period until 15 May 2014, i.e. the day of termination of the third joint term of office of the Supervisory Board. In the aforementioned period he acted as the secretary of the Supervisory Board and member of the Audit Committee of the Supervisory Board. Re-elected to the Supervisory Board as of 1 September 2014. Currently acting as the member of the Committee on Nominations and Remunerations of the Supervisory Board.

Jacek Rawecki – Member of the Supervisory Board

Graduate of the Faculty of Social Sciences of the University of Wrocław. Currently, in the course of preparation of a PhD thesis at the Faculty of Law and Administration of the Cardinal Stefan Wyszyński University in Warsaw, taking part in the Master of Business Administration management studies at the University of Economics in Wrocław.

Performing management functions since 2006. At present, he is the First Vice-President of the Management Board of KGHM Polska Miedź S.A. for Supply Chain Management. Previously, he was, among others, the President of the Management Board of Katowicki Węgiel Sp. z o.o., director of the local branch of Agencja Mienia Wojskowego, director for marketing and development of PUH Brajt. in Wrocław. Former President of the Management Board of KGHM Metraco S.A. In Legnica, later the member of the Management Board of Przedsiębiorstwo Budowlane ARS Sp. z o.o. He has experience in ownership supervision – he was a member of the Supervisory Board of Grupa Energetyczna Katowice Sp. z o.o. and a secretary of the Supervisory Board of EnergiaPro Gigawat Sp. z o.o.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 8 June 2016. Currently acting as the member of the Audit Committee of the Supervisory Board.

Stefan Świątkowski – Member of the Supervisory Board

Graduate of Łódź University of Technology (Master's Degree in mathematics), the University of Leeds in the United Kingdom (Master of Science in mathematics), and INSEAD in France (MBA).

He has many years of experience in financial management, risk management, and strategic management. At present, he is the Vice-President of the Management Board for Finance at KGHM. Earlier he served as the Vice President of the Management Board of FM Bank/Polski Bank Przedsiębiorczości and the bank PKO BP responsible for risk management. He was also the Finance Director at Europejski Fundusz Leasingowy S.A. and the ALCO Director at Lukas Bank S.A. He also worked in Bank Handlowy S.A. at various positions related to risk and strategy management and at McKinsey & Company Poland sp. z o.o. as a consultant. He has experience in supervising commercial companies and partnerships. Author of articles on economic issues and a novel about Polish privatisation.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 08 June 2016. Currently acting as the member of the Strategy Committee of the Supervisory Board.

Jan Płudowski – Member of the Supervisory Board

Graduate of the Faculty of Electrical Engineering of Silesian University of Technology in Gliwice. He completed postgraduate studies at the Faculty of Electrical and Control Engineering of Gdańsk University of Technology, at the University of Economics in Katowice, Department of Enterprise Finance Management and at the Faculty of Management and Economics of Services of University of Szczecin, Department of Marketing and Management in Enterprise.

Professionally associated with the energy sector, he gained his professional experience holding positions at all levels of professional career. He worked, inter alia, at the following positions: Chief Regional Power Engineer (PKP Silesian Regional Directorate of State Railway in Katowice), Director of Railway Energy Department in Katowice and Head of Energy Management Division (PKP Directorate of Railway Energy in Warsaw), Director of the Office for Cash Flows ("PKP Energetyka" sp. z o.o. In Warsaw). He currently acts in the capacity of Director – Project Coordinator at "PKP Energetyka" S.A. in Warsaw. In the years 2007–2008 he acted in the capacity of a member of the Supervisory Board of the Energy Company Jastrzębie S.A.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 30 December 2016. Currently acting as the member of the Audit Committee of the Supervisory Board.

Agnieszka Woźniak – Member of the Supervisory Board

Graduate of the Faculty of Law and Administration at Maria Curie-Skłodowska's University in Lublin. She is a lawyer by profession.

Has many years of experience in human resources management. She dealt with internal inspections, office organizational matters, procurement, HR matters. She held the position of the representative of the Director-General for integrated management system. She also has experience in supervision over companies with State Treasury shareholding. Currently she holds the position of Director of the Minister Office at the Ministry of Energy.

Appointed to the Supervisory Board of TAURON Polska Energia S.A. as of 16 December 2016. Currently acting as the member of the Nominations and Remuneration Committee of the Supervisory Board.

The detailed description of experience and competences of the member of the Supervisory Board is published on the Company website http://www.tauron.pl/.

Description of operation

A detailed description of the Supervisory Board operations is included in the CCC, in the Company Articles of Association, which is available on the Company website http://www.tauron-pe.pl/ and in the *Bylaws of the Supervisory Board of TAURON Polska Energia S.A. z siedzibą w Katowicach*.

The main form of performing supervision by the Supervisory Board over the Company's operations are meetings of the Supervisory Board. The Supervisory Board performs its obligations collectively. Meetings of the Supervisory Board are convened by the Chairperson of the Supervisory Board or Vice-Chairperson of the Supervisory Board by presenting a detailed agenda:

1) in accordance with arrangements adopted by the Supervisory Board,
2) on his/her own initiative,
3) on a written request of each member of the Supervisory Board,
4) on a written request of the Management Board.

Meetings of the Supervisory Board take place in the Company's seat. In justified cases the venue of the meeting may be changed.

In order to convene a meeting, a written invitation of all members of the Supervisory Board at least 7 days before the date of the Supervisory Board meeting is required Due to material reasons the Chairperson of the Supervisory Board may reduce this period to 2 days, defining the mode of giving the invitation. Notifications of the Supervisory Board meeting are sent by means of fax or electronic mail. In the notification on the Supervisory Board meeting the Chairperson defines the date of the meeting, venue of the meeting as well as detailed draft of the agenda. The Supervisory Board shall meet when the need arises, however, not less frequently than once in every two months. The Supervisory Board may meet without convening a formal meeting if all members of the Supervisory Board are present and nobody appeals against the fact of holding the meeting or against the agenda.

A change of the proposed agenda may take place when all members of the Supervisory Board are present at the meeting and nobody appeals against the agenda. An issue not included on the agenda should be included in the agenda of the next meeting.

Taking part in meetings of the Supervisory Board is a duty of the Supervisory Board Member. A Member of the Supervisory Board shall give reasons of his/her absence in writing. Justification of the Supervisory Board Member's absence requires the resolution of the Supervisory Board. Members of the Management Board may take part in the meetings of the Supervisory Board meetings unless the Supervisory Board raises an objection. Participation of Management Board members in the Supervisory Board meetings is compulsory if they were invited by the Chairperson of the Supervisory Board. Other persons may also take part in the meetings if they were invited in the above mentioned way.

The Supervisory Board may seek opinion of legal advisers who render 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 ask their advice and make an appropriate decision. In the aforementioned cases the Supervisory Board shall pass a resolution concerning commissioning the work to a selected expert (audit or consulting company, law firm) obliging the Company's Management Board to conclude an appropriate 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 of the Supervisory Board. Due to material reasons, with the consent of the majority of the members of the Supervisory Board present at the meeting, the person chairing the meeting is obliged to submit to voting a motion to stop the meeting and establish a new date of resuming the Supervisory Board meeting. The Supervisory Board makes decisions in the form of resolutions. The Supervisory Board resolutions are passed mainly at meetings. The Supervisory Board adopts resolutions if at least half of its members are present at the meeting and all its members were invited in the way defined in the By-laws of the Supervisory Board. Subject to unconditionally binding legal regulations, including the CCC as well as provisions of the Company Articles of Association, the Supervisory Board passes resolutions by an absolute majority of votes of the persons present at the meeting, where the absolute majority of votes is understood as more votes submitted "for" than "against" and "abstain". Resolutions cannot be passed on issues not included in the agenda unless all members of the Supervisory Board are present and nobody voices an objection. This shall not apply to resolutions concerning justifying the Supervisory Board member's absence at the meeting. Voting of the resolutions is performed in an open ballot. A secret ballot is ordered:

1) on request of at least one of the members of the Supervisory Board,
2) in case of personal issues.

The Supervisory Board, in accordance with the Articles of Association, may pass resolutions in writing or by using means of direct remote communication. Passing a resolution in such a mode requires a justification and a prior submitting of the draft of the resolution to all members of the Supervisory Board. Passing resolutions in this mode does not apply to appointing of the Chairperson, the Deputy Chairperson and the Secretary of the Board, appointing or suspending of a member of the Supervisory Board and dismissing of such persons as well as other issues the settlement of which requires a secret ballot. Voting on a resolution passed in the aforementioned mode, a member of the Supervisory Board indicates the mode of his/her voting, "for", "against" or "abstain". Resolution with a note that it was passed in a written mode or by mode of voting using means of direct distance communication shall be signed by the Chairperson of the Supervisory Board. Resolutions passed according to this procedure shall be presented at the first coming meeting of the Supervisory Board, including the announcement of the voting result.

A possibility is allowed for members of the Supervisory Board to participate in the meeting and vote on the resolutions adopted within such a meeting using means of direct remote communication, i.e. tele- or videoconferences, provided that at the venue of the session, indicated in the notice of the meeting, at least half of the members are present as well as the technical possibility to ensure secure connection is provided.

Members of the Supervisory Board shall take part in meetings and perform their duties personally and while performing their duties, they are obliged to exercise due diligence. Members of the Supervisory Board are obliged to keep information connected with the Company activity which they have acquired in connection with holding their seat or at other occasion secret. The Supervisory Board executes its obligations collectively.

The Supervisory Board may, due to material reasons, delegate particular members to perform certain actions independently for a defined period of time. The Supervisory Board may delegate its members, for a period no longer than three months, to temporary performance of duties of Management Board members who have been dismissed, submitted their resignation or if due to other reasons they cannot perform their functions. The aforementioned delegation requires obtaining permission from a Supervisory Board member who is to be delegated.

The detailed description of activities of the Supervisory Board in the previous financial year is contained in the Report on Activities of the Supervisory Board, submitted on annual basis to the GM and then published on the Company website http://www.tauron-pe.pl/.

The Supervisory Board may appoint among its members permanent or temporary working groups or committees to perform particular actions. The permanent committees of the Supervisory Board include:

1) Audit Committee of the Supervisory Board of TAURON Polska Energia S.A., (Audit Committee),
2) Nominations and Remuneration Committee of the Supervisory Board of TAURON Polska Energia S.A. (Nominations and Remuneration Committee),
3) Strategy Committee of the Supervisory Board of TAURON Polska Energia S.A. (Strategy Committee).

Composition, tasks and rules of operation of the aforementioned committees are defined in their regulations adopted by the Supervisory Board.

6.11.3. Audit Committee

In connection with the changes in the composition of the Supervisory Board of the Company of the fourth joint term of office performed in 2016, the Supervisory Board changed the composition of the Audit Committee.

Composition of the Audit Committee as at 31 December 2016

1. Beata Chłodzińska – Member of the Audit Committee,
2. Jacek Rawecki – Member of the Audit Committee,
3. Jacek Szyke – Member of the Audit Committee.

Changes in the personal composition of the Audit Committee

As at 01 January 2016 the Audit Committee consisted of the following members: Wojciech Myślecki (Chairman), Beata Chłodzińska, Michał Czarnik i Jacek Szyke.

On 8 January 2016 the Supervisory Board appointed Anna Biesialska as a member of the Audit Committee.

On 26 July 2016, Anna Biesialska resigned from her function of the member of the Audit Committee.

On 26 July 2016 the Supervisory Board appointed Jacek Rawecki as a member of the Audit Committee.

On 14 November 2016 a Member of the Supervisory Board, Wojciech Myślecki submitted his resignation from the function of Member of TAURON Polska Energia S.A. Supervisory Board. Consequently, his membership in the Audit Committee expired.

On 30 December 2016 the Minister of Energy, acting pursuant to § 23(1)(3) of the Company Articles of Association dismissed Michał Czarnik from the Supervisory Board of TAURON Polska Energia S.A. Consequently, his membership in the Audit Committee expired.

On 30 January 2017 the Supervisory Board appointed Stanisław Bortkiewicz and Jan Płudowski as members of the Audit Committee.

Personal composition of the Audit Committee as of the day of drawing up this report:

1. Stanisław Bortkiewicz – Chairman of the Audit Committee,
2. Beata Chłodzińska – Member of the Audit Committee,
3. Jan Płudowski – Member of the Supervisory Board,
4. Jacek Rawecki – Member of the Audit Committee,
5. Jacek Szyke – Member of the Audit Committee.

Tasks and competence of the Audit Committee

The table below presents the tasks and competences of the Audit Committee as at the day of drawing up this report.

Table no 42. Competence of the Audit Committee

Issues requiring the resolution of the Audit Committee	
as at 31 December 2016 and as at the day of this report:	
1.	monitoring of financial reporting process,
2.	monitoring of the accuracy of financial information presented by the Company,
3.	monitoring of the efficiency of internal control, risk management systems, compliance and internal audit functions existing in the Company,
4.	monitoring of performing of financial revisions,
5.	monitoring of independence and impartiality of the chartered accountant and the entity entitled to examine financial statements, including rendering by them services other than financial audit,
6.	recommending of an entity entitled to examine financial statements to perform financial audit to the Supervisory Board.

The detailed description of activities of the Audit Committee in the previous financial year is contained in the Report on Activities of the Supervisory Board, submitted on annual basis to the GM and then published on the Company website http://www.tauron-pe.pl/.

6.11.4. Nominations and Remuneration Committee

In connection with the changes in the composition of the Supervisory Board of the Company of the fourth joint term of office performed in 2016, the Supervisory Board changed the composition of the Nominations and Remuneration Committee.

Personal composition of the Nominations and Remuneration Committee as at 31 December 2016 and as at the day of drawing up this report

1. Beata Chłodzińska – Chairwoman of the Nominations and Remuneration Committee,
2. Leszek Koziorowski – Member of the Nominations and Remuneration Committee,
3. Agnieszka Woźniak – Member of the Nominations and Remuneration Committee.

Changes in the personal composition of the Nominations and Remuneration Committee

As at 01 January 2016 the Nominations and Remuneration Committee consisted of the following members: Leszek Koziorowski (Chairman), Anna Biesialska, Beata Chłodzińska and Renata Wiernik-Gizicka.

On 06 June 2016 a Member of the Supervisory Board, Renata Wiernik-Gizicka submitted her resignation from the function of Member of TAURON Polska Energia S.A. Supervisory Board. Consequently, her membership in the Nominations and Remuneration Committee expired.

During its meeting on 19 December 2016 the Supervisory Board appointed Agnieszka Woźniak as a Member of the Nominations and Remunerations Committee.

On 30 December 2016 the Minister of Energy, acting pursuant to § 23(1)(3) of the Company Articles of Association dismissed Anna Biesialska from the Supervisory Board of TAURON Polska Energia S.A. Consequently, her membership in the Nominations and Remuneration Committee expired.

Until the day of submission of this report, no other changes in the composition of the Nominations and Remuneration Committee have taken place.

Tasks and competence of the Nominations and Remuneration Committee

The table below presents the tasks and competences of the Nominations and Remunerations Committee as of 31 December 2016 and on the day of this report.

Table no 43. Competence of the Nominations and Remuneration Committee

Issues requiring the resolution of the Nominations and Remunerations Committee	
as at 31 December 2016 and as at the day of drawing up this report	
1.	recommendations to the Supervisory Board on a recruitment procedure for the positions of the Company Management Board members,
2.	assessing candidates for members of the Management Board as well submitting an opinion in this scope to the Supervisory Board,
3.	recommendations to the Supervisory Board on the form and contents of agreements concluded with members of the Management Board,
4.	recommendations to the Supervisory Board on remuneration and bonus system of the members of the Management Board,
5.	recommendations to the Supervisory Board on the need to suspend a member of the Management Board due to material reasons,
6.	recommendations to the Supervisory Board on 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 together with a proposal of remuneration.

The detailed description of activities of the Nominations and Remuneration Committee in the previous financial year is contained in the Report on Activities of the Supervisory Board, submitted on annual basis to the GM and then published on the Company website http://www.tauron-pe.pl/.

6.11.5. Strategy Committee

In connection with the changes in the composition of the Supervisory Board of the Company of the fourth joint term of office performed in 2016, the Supervisory Board changed the composition of the Strategy Committee.

Composition of the Strategy Committee as at 31 December 2016 and as at the day of drawing up this report

1. Jacek Szyke – Chairman of the Strategy Committee,
2. Beata Chłodzińska – Member of the Strategy Committee,
3. Anna Mańk – Member of the Strategy Committee,
4. Stefan Świątkowski – Member of the Supervisory Board.

Changes in the Strategy Committee personal composition

As at 01 January 2016 the Strategy Committee consisted of the following members: Jacek Szyke (Chairman), Beata Chłodzińska, Anna Mańk, Maciej Koński and Wojciech Myślecki.

On 06 June 2016 a Member of the Supervisory Board, Maciej Koński submitted his resignation from the function of Member of TAURON Polska Energia S.A. Supervisory Board. Consequently, his membership in the Strategy Committee expired.

On 26 July 2016 the Supervisory Board appointed Stefan Świątkowski as a member of the Strategy Committee.

On 14 November 2016 a Member of the Supervisory Board, Wojciech Myślecki submitted his resignation from the function of Member of TAURON Polska Energia S.A. Supervisory Board. Consequently, his membership in the Strategy Committee expired.

Tasks and competence of the Strategy Committee

The table below presents the tasks and competences of the Strategy Committee as at 31 December 2016 and as at the day of drawing up this report.

Table no 44. Competence of the Strategy Committee

Issues requiring the resolution of the Strategy Committee	
as at 31 December 2016 and as at the day of drawing up this report	
1.	assessment of the Strategy of the Company and the Capital Group and presenting its results to the Supervisory Board,
2.	recommending the scope and terms of submitting the strategic multi-annual plans to the Supervisory Board,
3.	assessment of impact of the planned and undertaken strategic investments on assets of the Company,

Issues requiring the resolution of the Strategy Committee	
as at 31 December 2016 and as at the day of drawing up this report	
4.	monitoring the implementation of the strategic investment tasks,
5.	assessment of activities concerning availability of significant Company assets,
6.	opinion on strategic documents submitted to the Supervisory Board by the Management Board.

The detailed description of activities of the Strategy Committee in the previous financial year is contained in the Report on Activities of the Supervisory Board, submitted on annual basis to the GM and then published on the Company website http://www.tauron-pe.pl/.

6.11.6. Description of activities of the Committees of the Supervisory Board

A detailed description of the Supervisory Board operations is included 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 duties.

The Committees of the Supervisory Board consist of three to five members. The activities of the individual Committees are managed by their Chairpersons.

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 as needed. 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 Management Board shall be informed about recommendations and assessments submitted to the Supervisory Board by the Committees of the Supervisory Board. Every year, the Committees of the Supervisory Board provide public record information, through the Company, on the composition of the Audit Committee, number of meetings held and participation in the meetings during the year as well as on main activities. In addition, the Audit Committee confirms its positive assessment of the independence of financial audit process and submits a short description of steps taken to formulate such a motion.

The Company Management Board provides the possibility to use the services of external advisers by the Committees in the scope required for performing the obligations of the specific Committee.

6.12. Description of the policy of diversity applied to the governing bodies of the Company

The Company uses the policy of equal treatment and strives to ensure diversity in terms of gender, educational background, age and professional experience in relation to all employees, in particular, in relation to the governing bodies of the Company and its key managers. As at the day of completion of the report, TAURON did not have the diversity policy formulated in the form of a single document. The rules on diversity management were introduced for application under many documents constituting internal legal acts, including the *TAURON Group’s Code of Business Ethics*.

In relation to members of the corporate bodies of the Company, i.e. The Management Board and the Supervisory Board, persons acting as Members of the Management Board are selected by the Supervisory Board, whereas Members of the Supervisory Board are selected by the Minister of Energy within the statutory powers and GM TAURON. Information concerning qualifications and professional experience of persons appointed to the Management Board and the Supervisory Board is published in the relevant current reports as well as in the Company website.

TAURON plans to develop and implement the diversity policy for application in a single formal document.

6.13. Remuneration policy of management and supervisory staff

6.13.1. Remuneration system of Management Board members and key managers

6.13.1.1. General information on the adopted remuneration system for members of the Management Board

In 2016 the principles of remuneration of members of the Company Management Board defined in the *Remuneration Policy for Members of supervisory and management bodies, including the description of the rules of defining the policy in TAURON Polska Energia S.A.* applied (Remuneration Policy), adopted by the Supervisory Board of the Company pursuant to the resolution no. 15/II/2011 of 24 February 2011 as well as the rules of development of remuneration of Members of the Management Board (Rules of remuneration development), defined in the Resolution of the Extraordinary GM of WZ TAURON of 15 December 2016 specified in detail by the Supervisory Board of the Company pursuant to the Resolution no. 94/IV/2016 of 15 December 2016 *concerning the amendment to the Articles of Association the development of remuneration of Members of the Management Board of TAURON Polska Energia S.A.* The Rules of remuneration development were adopted as the implementation of the provisions of the *Act of 9 June 2016 concerning principles for determining remuneration of persons managing certain companies* (Journal of Laws of 2016, item 1202).

Both the Remuneration policy and the Rules of remuneration development define the remuneration system for members of the Management Board, in connection with outstanding tasks aimed at implementation of the adopted strategy of the Company, development directions and financial plans. The overriding objective of the adopted remuneration system is to ensure an incentive-based remuneration of the senior management staff and to create basis for its development.

Objectives if applicable remuneration systems:

1) ensuring an incentive-based and consistent remuneration system,
2) linking the remuneration rules with monitoring of implementation of the adopted strategic plans and implementation of the financial plans,
3) developing the level of remuneration of Management Board members in connection with the implementation of the delegated tasks,
4) growth in the Company value through the development of the senior management staff,
5) improvement of remuneration systems translating into implementation of the Company strategy and development directions.

The remuneration and bonus system for Members of the Management Board of the Company applicable in the Company stipulates that the level of remuneration should be tied to the financial situation of the Company and growth in an annual perspective, in connection with the implementation of strategic goals. The said systems do not envisage that remuneration shall be tied with instruments associated with the Company shares.

The remuneration model contained both in the Remuneration policy and in the Rules of remuneration development assume a two-component system for determining of the remuneration for members of the Management Board. Flat-rate monthly salary (fixed remuneration) and supplementary remuneration for a given financial year (variable remuneration), depending on the level of accomplishment of the management goals.

In the scope of the remuneration model of the top management staff, remuneration consisting of a fixed and variable part has been adopted, depending on the fulfilment of the specific resultant criteria.

Taking into account the applicable regulations, the level of remuneration for members of the Management Board is defined by the Supervisory Board, within the brackets determined by the Company GM.

Members of the Management Board of the Company are neither covered by the bonus programme based on the capital of the Company, nor do they receive any remuneration or awards due to fulfilment of their functions in governing bodies of companies belonging to TAURON Capital Group.

6.13.1.2. General information on the adopted remuneration system for key managers

The rules concerning remuneration and bonus system for key managers and other employees are defined in the *Regulations* on *Remuneration of Employees of TAURON Polska Energia S.A.,* adopted for application by the Management Board of the Company.

The remuneration and bonus system for key managers stipulates that the level of remuneration should be tied to the financial situation of the Company in an annual perspective, in connection with the implementation of strategic goals. It assumes a two-component system for defining of the remuneration, comprising the basic monthly salary and a variable incentive component based on the implementation of the assigned tasks, both of financial and non-financial nature.

The overriding assumption of the applicable remuneration system is to ensure the optimum and motivating remuneration 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 remuneration consists of the following elements:

1) a fixed part – constituting the basic 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 internal regulations of the Company.

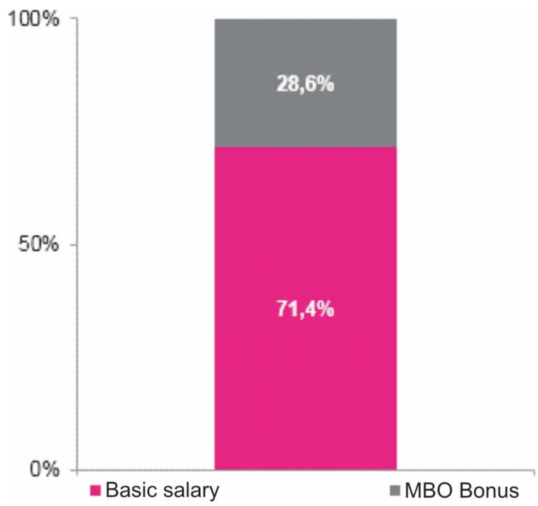
The bonus system based on market bonus mechanisms enables cascading the objectives set by the Management Board at a level of TAURON Capital Group and at a level of the Company, to specific tasks, defined by parameters, assigned to employees at lower levels of the organisation. Accordingly, the culture of managing through objectives applied in the Company reflects the specific nature of individual functions implemented in the Company and allows for application of mechanisms based on dialogue of the supervisor with the subordinate during the process of determining and assessment of implementation of objectives translating into the effectiveness of the overall organisation. At the same time, this tool enables precise correlating of objectives (KPIs) defined for members of the Management Board with objectives set for key managers of the Company for a given year. The preliminary assessment of accomplishment of the objectives takes place after the first semi-annual period, whereas after the end of the second half of the year members of the Management Board perform the final evaluation of the implementation of the objectives of Company key managers.

Moreover, in 2016 works on building a bonus system for the trade area started, aimed at motivating to achieve higher revenue for TAURON Capital Group.

Employees of the Company do not receive any remuneration or awards on account of functions fulfilled in governing bodies of companies belonging to TAURON Capital Group.

The figure below presents the structure of remuneration for the position of a key manager.

Figure no. 99 Structure of remuneration for the position of a key manager



6.13.1.3. Rules, terms and conditions and level of remuneration of Management Board members

The total amount of remuneration 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 2016 amounted to PLN 8,024 thousand gross.

The table below presents the remuneration of the Company Management Board members for 2016, divided into components.

Table no 45. Remuneration of members of the Company Management Board for 2016, divided into components

No.	Name and surname	Period of holding the function in 2016	Remuneration* (PLN thous.)	Bonus* (PLN thous.)	Other benefits* (PLN thous.)	Total (PLN thous.)
1.	Jarosław Broda	01.01.2016 – 31.12.2016	900	197	122	1,219
2.	Filip Grzegorczyk**	15.11.2016 – 31.12.2016	98	0	0	98
3.	Kamil Kamiński	01.01.2016 – 31.12.2016	900	194	51	1,145

No.	Name and surname	Period of holding the function in 2016	Remuneration* (PLN thous.)	Bonus* (PLN thous.)	Other benefits* (PLN thous.)	Total (PLN thous.)
4.	Remigiusz Nowakowski	01.01.2016 – 14.11.2016	884	249	166	1,299
5.	Anna Striżyk	01.01.2016 – 08.01.2016	30	53	0	83
6.	Marek Wadowski	29.01.2016 – 31.12.2016	829	151	40	1,020
7.	Piotr Zawistowski	01.01.2016 – 31.12.2016	900	197	164	1,261
	Total		**4,541**	**1,041**	**543**	**6,125**

** No overheads.*
*** Agreement for provision of management services.*

Members of the Management Board did not receive any remuneration or awards in 2016 on account of functions fulfilled in governing bodies of companies belonging to TAURON Capital Group.

In relation to Members of the Management Board listed in the above table, the Remuneration Policy applied, excluding the President of the Management Board to whom the Rules of remuneration development were applied.

Taking into account the foregoing, assumptions to two remuneration systems were presented:

1. The Remuneration Policy for Members of supervisory and management bodies, including the description of the rules of its defining in TAURON Polska Energia S.A.

   The remuneration policy, adopted by the Supervisory Board of the Company pursuant to the resolution no. 15/II/2011 of 24 February 2011 consists of two components for determining the remuneration, the fixed part (monthly basic salary) and the variable part, depending on fulfilment of specific target criteria (implementation of the task commissioned). Both the monthly basic salary as well as the result-based criteria, whose fulfilment determines the level of an annual bonus, are defined by the Supervisory Board of the Company.

   The Supervisory Board determines the percentage level of the annual bonus for each of the following ratios:

   1) consolidated EBITDA derived from the approved consolidated material and financial plan for a given financial year,
   2) consolidated gross profit derived from the approved consolidated material and financial plan for a given financial year,
   3) current liquidity ratio measured for TAURON Capital Group derived from the approved consolidated material and financial plan for a given financial year,
   4) implementation of non-financial objectives indicated for a given year in the approved Strategy.

   The components of the annual bonus of financial nature are allocated based on the data derived from the audited consolidated financial statements of the Company for the first half of a given financial year and for a given financial year. The component of the annual bonus of non-financial nature is allocated in connection with the achievement of specific objectives in a given financial year, based on the semi-annual and annual assessment of their performance by the Supervisory Board.

   In order to enable the use of benefits available to the Company employees by members of the Management Board, the remuneration policy was supplemented with a catalogue of additional benefits of social and welfare, communication and insurance nature.

   In accordance with the aforementioned Remuneration Policy the employment contract is concluded with Members of the Management Board.

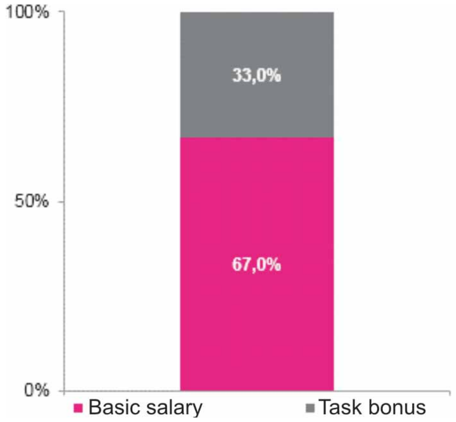
2. The rules of development of remuneration for Members of the Management Board

   The Rules of remuneration development adopted pursuant to the Resolution of the Extraordinary GM of WZ TAURON of 15 December 2016, specified in detail by the Supervisory Board of the Company of 19 December 2016 concerning the rules of development of remuneration of Members of the Management Board of TAURON Polska Energia S.A., comprise a two-component system for defining the remuneration, consisting of the fixed part (monthly basic salary) and the variable part (supplementary remuneration) constituting the motivating element of the remuneration depending on the accomplishment of management targets in a given financial year. Both the monthly basic salary and the variable part is determined by the Supervisory Board of the Company pursuant to the rules and the general catalogue of management targets defined by the TAURON GM.

   In accordance with the aforementioned Rules of remuneration development an agreement for provision of management services for the period of fulfilment of the function is concluded with a Member of the Management Board, with the obligation of personal rendering of services, irrespective of whether the member acts in the scope of conducted economic activity.

The figure below presents the structure of remuneration of Members of the Management Board.

Figure no. 100 Structure of remuneration for the position of a Management Board member



6.13.1.4. 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 agreement for provision of management services concluded with the President of the Management Board, in case of termination or dissolution of the Agreement by the Company for reasons other than defined therein, a Management Board Member may be awarded a severance payment at a level not higher than three-fold fixed part of the remuneration, under the condition of fulfilment of the function by the Member over a period of at least 12 months prior to the termination of this agreement. On the other hand, employment contracts concluded with other Management Board Members do not envisage severance payment in case of their resignation or dismissal from the position held, without material reason, or if their dismissal or resignation is caused by merger of the Company through takeover.

In connection with the access of members of the Management Board to confidential information whose disclosure could expose the Company and companies of TAURON Capital Group to losses, the aforementioned agreement for provision of management services includes non-competition provisions applicable after the expiry of the term of office. On the other hand, non-competition agreements have been concluded with other members of the Management Board. Under the aforementioned agreements, persons refraining from conducting competitive activity in the specified period may receive compensation.

Members of the Company Management Board did not hold positions of members of Management Boards of companies included in TAURON Capital Group.

6.13.1.5. Non-financial components of remuneration allocated to members of the Management Board and key managers

Members of the Management Board, excluding the President of the Board employed under the agreement for provision of management services, and staff members employed at key positions in the Company are entitled to use benefits and non-financial components of remuneration offered by the Company.

Within the additional benefits the aforementioned employees are entitled, inter alia to:

1) participate in the Employee Pension Scheme operated by the employer (under the condition of being employed in the Company or one of the companies 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.

Pursuant to the agreement for provision of management services technical devices and resources constituting the Company assets are made available, required for the fulfilment of the function, including the right of exclusive use of a company car.

6.13.1.6. Information on changes in the remuneration policy over the last financial year

In the financial year 2016 the Extraordinary GM of TAURON introduced new rules of remuneration development for members of the Management Board as the implementation of the provisions of the Act of 9 June 2016 *concerning* *principles for determining remuneration of persons managing certain companies*. Accordingly, work was commenced with the purpose of development of a new Remuneration Policy, compliant with the aforementioned Resolution of the Extraordinary GM of TAURON and the Resolution of the Supervisory Board 19 December 2016 concerning the development of remuneration of Members of the Management Board of TAURON Polska Energia S.A.

Information concerning the aforementioned rules of development of remuneration of Members of the Management Board is contained in section 6.13.1.3 hereof.

6.13.1.7. Assessment of functioning of the remuneration 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 remuneration system for members of the Management Board is compliant with the adopted Remuneration policy and the rules of development of remuneration. The incentive-based and consistent system is provided, linked with the monitoring of annual financial plans and the adopted Strategy and development directions.

The form, structure and level of remuneration 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 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 ensure the incentive function for the Management Board.

The disbursement of variable components of remuneration is linked with the pre-defined, measurable result criteria fostering the long-term stability of the Company, including also the criteria other than financial, associated with the generation of the long-term value of the Company.

The indicators determining obtaining and level of variable components of the remuneration are defined in accordance with the SMART principle, thus, they also indicate such features as: precision, measurability, possibility to achieve, significance and defining in time.

The remuneration and bonus system for Members of the Management Board of the Company applicable in TAURON supports the implementation of strategic goals and determines the remuneration depending on the Company financial situation in an annual perspective.

6.13.2. Remuneration system of members of the Supervisory Board

In the period until 15 December 2016 the rules of remuneration for members of the Supervisory Board of the Company defined in the Remuneration policy and in the Resolution of the Ordinary GM of TAURON no. 29 of 6 May 2011 *concerning determining of the rules and level of remuneration for members of the Supervisory Board of TAURON Polska Energia S.A.* were applicable. On the other hand, as of 15 December 2016 the remuneration system for Members of the Supervisory Board applies, defined in the Resolution of the Extraordinary TAURON GM no. 6 of 15 December 2016 concerning the *rules of development of remuneration of Members of the Supervisory Board*, adopted as the implementation of the provisions of the *Act of 9 June 2016 concerning principles for determining remuneration of persons managing certain companies* (Journal of Laws of 2016 item 1202).

Both the earlier remuneration system of members of the Supervisory Board binding until 15 December 2016 as well as the system applicable as at the day of drawing up this report comprises a single-component monthly remuneration, adopting diversification of its level depending on the function in the Supervisory Board.

In accordance with the aforementioned Resolution of the Extraordinary TAURON GM of 15 December 2016, a monthly remuneration of Supervisory Board members is determined as a product of the average monthly remuneration 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 Statistical 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 remuneration irrespective of the frequency of formally convened meetings.

The remuneration 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 remuneration 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.

Remuneration of key supervising personnel

The table below presents the remuneration of members of the Company Supervisory Board Members for 2016.

Table no 46. Remuneration of members of the Supervisory Board of the Company for 2016

No.	Name and Surname	Period of holding the function in 2016	Remuneration and awards (PLN thous.)
1.	Anna Biesialska	01.01.2016 – 30.12.2016	106
2.	Stanisław Bortkiewicz	30.12.2016 – 31.12.2016	0
3.	Beata Chłodzińska	01.01.2016 – 31.12.2016	142
4.	Michał Czarnik	01.01.2016 – 30.12.2016	106
5.	Maciej Koński	01.01.2016 – 06.06.2016	47
6.	Leszek Koziorowski	01.01.2016 – 31.12.2016	107
7.	Anna Mańk	01.01.2016 – 31.12.2016	130
8.	Wojciech Myślecki	01.01.2016 – 14.11.2016	94
9.	Jan Płudowski	30.12.2016 – 31.12.2016	0
10.	Jacek Rawecki	08.06.2016 – 31.12.2016	59
11.	Jacek Szyke	01.01.2016 – 31.12.2016	118
12.	Stefan Świątkowski	08.06.2016 – 31.12.2016	60
13.	Renata Wiernik Gizicka	01.01.2016 – 06.06.2016	47
14.	Agnieszka Woźniak	16.12.2016 – 31.12.2016	3
	Total		**1,019**

6.13.3. Liabilities arising from pensions and similar benefits for former the Members of the Management Board and the Supervisory Board

In the Company no liabilities towards former the Members of the Management Board and the Supervisory Board occur, arising from pensions and similar benefits.

At the same time, it is indicated that sue to Company liabilities towards former members of TAURON Management Board, in 2016 the total amount of PLN 5,616 thousand was paid due to bonuses for accomplishment of KPIs in 2015 (excluding overheads) and compensations for compliance with the non-competition clause.

7. OTHER SIGNIFICANT INFORMATION AND EVENTS

7.1. Proceedings pending before the court, competent arbitration authority or public authority body

During the reporting period no proceedings were pending before any court, competent arbitration authority or public authority body, related to the Company or subsidiaries of TAURON Capital Group, whose single or aggregate value would exceed at least 10% of the Company equity.

7.2. Information on agreements concluded by companies of TAURON Capital Group

7.2.1. Agreements significant for operations of TAURON Capital Group

In the financial year 2016 the companies of TAURON Capital Group concluded the following agreements significant for operations of TAURON Capital Group:

Withdrawal from execution of project for the construction of CCGT unit in Elektrownia Blachownia

On 28 July 2016, in reference to current report No. 61/2016 of 30 December 2013 on suspending the project for the construction of CCGT unit in Elektrownia Blachownia Nowa, on 28 July 2016 the companies: TAURON, KGHM and TAURON Wytwarzanie signed the agreement under which they jointly decided to withdraw from execution of the project for the construction of CCGT unit in Elektrownia Blachownia Nowa and terminate the Shareholders' Agreement binding KGHM and TAURON Wytwarzanie, which meant expiry of all obligations specified in the Shareholders' Agreement and termination of all works defined therein, in particular, those defined in the preliminary schedule of project execution, as well as in further arrangements and covenants.

KGHM and TAURON Wytwarzanie jointly agreed to participate in winding up of the Elektrownia Blachownia Nowa which would be carried out in line with the provisions of the articles of association of the Company and generally applicable laws.

The Parties will cooperate with each other and with the Company to guarantee execution of the Agreement. The Parties agreed to terminate the agreement of 30 December 2013 under which they decided to suspend temporarily the project for the construction of CCGT unit in Elektrownia Blachownia Nowa.

The Company informed of the aforementioned event in the current report no. 32/2016 of 28 July 2016.

Agreement on the conditions for further execution of the project on "Construction of a CCGT Unit in Stalowa Wola"

On 27 October 2016, in reference to current report No. 9/2016 of 11 March 2011 concerning concluding of material agreements under the project "Construction of CCGT unit in Stalowa Wola":

1) a conditional agreement was concluded between TAURON, PGNiG and EC Stalowa Wola ("Agreement") concerning determination of boundary conditions for the project restructuring,
2) annex to the electricity purchase agreement of 11 March 2011 ("Electricity Purchase Agreement") between TAURON, PGNiG and EC Stalowa Wola,
3) annex to the gas fuel supply agreement of 11 March 2011 ("Gas Supply Agreement") between PGNiG and EC Stalowa Wola.

Agreement

First of all, the negotiated Agreement sets forth the rules of settlement of contractual penalties that may be imposed by PGNiG on the basis of the Gas Supply Agreement as it currently stands, and addresses the issues related to financial restructuring of the Project. Furthermore, it defines the direction of changes that must be made in EC Stalowa Wola key trading transactions, i.e. in the method of purchase of gas fuel and sale of the generated electricity, which are to be introduced on the basis of the annexes to the Gas Supply Agreement and the Power Purchase Agreement.

The Agreement reflects the intent of the Project sponsors, i.e. TAURON and PGNiG to go ahead with the construction of the CCGT unit, amend the Gas Supply Agreement and the Power Purchase Agreement and change the method of funding the Project from project finance to corporate finance, with continued involvement of the financing institutions.

Power Purchase Agreement and Gas Supply Agreement

The conditional amendments to the Gas Supply Agreement and the Power Purchase Agreement provide, in particular, for introducing market rates for the pricing formulas used under these agreements. Furthermore, in view of delays in the Project implementation, the annex to the Gas Supply Agreement provides for changes to the amounts, times and methodologies of charging contractual penalties.

Conditions Precedent

The Agreement and the annexes to the Gas Supply Agreement and Power Purchase Agreement enter into force simultaneously at the moment of amendment of the agreements for Project financing or repayment of the last of institutions currently funding EC Stalowa Wola (i.e. EIB, European Bank for Reconstruction and Development (EBRD), Bank Polska Kasa Opieki S.A. (Pekao)).

Standstill agreement

At the same time, TAURON, PGNiG, EIB, EBRD, Pekao and EC Stalowa Wola entered into Standstill Agreement, the purpose of which is to ensure that the institutions currently providing financing to EC Stalowa Wola would refrain from calling the loans granted to EC Stalowa Wola immediately due and payable, and from satisfying their claims from the security provided in respect of these loans.

The Standstill Agreement shall remain in force until 31 March 2017. It is assumed that new documentation to restructure the Project financing may be negotiated and signed by that date.

The entry into force of the Standstill Agreement is conditional, in particular, on the financial institutions being provided with bank guarantees up to the amount of about PLN 629 million until 30 October 2016, where 50% share determines the amount of bank guarantees each of the Sponsors should provide to the financial institutions (i.e. about PLN 314.5 million).

Notwithstanding the foregoing, EC Stalowa Wola will have the right to give notice to the financial institutions of voluntary early repayment of the loans by 20 March 2017. According to preliminary estimates, the newly signed documents should enable completion of the Project in 2019.

The Company informed of the aforementioned event in the current report no. 36/2016 of 27 October 2016.

Signing agreements on hybrid financing with the European Investment Bank

On 14 December 2016, the following agreements were signed between TAURON and EIB:

1) project agreement (the “Project Agreement”) determining detailed requirements relating to the financed investment task,
2) subscription agreement (the “Subscription Agreement”) providing basis for conducting the issue of hybrid bonds (“Bonds”) with the value of EUR 190 million.

Funds to be acquired through the issuance of Bonds will be allocated for covering expenditure of TAURON Dystrybucja S.A. associated with the development and modernisation of power grid infrastructure in the years 2016–2020.

Detailed information concerning the aforementioned issues is provided in section 4.7. of this report.

Information on the aforementioned event was published in the current report no. 45/2016 of 14 December 2016.

Concluding the agreement with Nowe Brzeszcze GT for coal sales

On 4 January 2016 the agreement for coal sales for energy generation purposes was concluded between TAURON and Nowe Brzeszcze GT, the subject matter of which is the purchase of coal by the Company for the needs of generation units of TAURON Wytwarzanie and TAURON Ciepło. The agreement was concluded for a period until 31 December 2016.

Concluding the agreement with TGE for acting in the capacity of a market maker

On 1 February 2016 TAURON concluded the agreement with TGE for fulfilment of a market maker function in the scope of instruments for electricity at the RTT (commodity forward market). The aim of the cooperation is to increase the liquidity of animated instruments and to intensify the cooperation between TGE and TAURON.

The task of the animator is to ensure maintaining of trading liquidity and increase the number of transactions concluded on the TGE in products covered by the agreement. The effect of such activity is to enable the execution of purchase and sales orders at market prices by market participants. Through the fulfilment of the market maker function at TGE, TAURON obtains preferential rates for transaction fees and, additionally, through increasing the share of transactions, the Company gains additional discounts on transaction fees in the general trade.

Simultaneously, work with the Commodity Clearing House (IRGIT) was carried out in order to negotiate and sign an agreement concerning the level of fees for the market maker. This agreement introduces reduced rates for the market maker in the period from 1 February 2016 to 31 January 2017, i.e. in the period of effectiveness of the agreement for the fulfilment of a market maker function at TGE.

Conclusion of the annex for coal sales to TAMEH POLSKA

As of 1 July 2016 TAURON resumed coal sales to TAMEH POLSKA after a period of suspension of agreement execution (from 01 April 2015 to 30 June 2016), which resulted from the change in the market situation. The resumption of coal supplies occurred as a result of TAURON's offer of more favourable prices than attainable on the market by TAMEH POLSKA, after signing the relevant annex to the agreement.

Signing the Agreement with PSE on electricity sales for covering of transmission grid losses

On 5 October 2016 TAURON concluded the agreement for electricity sales with PSE for covering of losses in the transmission grid in the period from 1 January 2017 to 31 December 2017. The agreement was concluded as a result of public procurement procedure conducted by PSE.

With reference to the provisions of § 91 item 6 point 3 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*, the Company hereby informs that it is not aware of any other agreements concluded, significant for the operations of the Company, other than the agreements mentioned above, including the agreements concluded between shareholders (partners), insurance agreements, cooperation or collaboration agreements.

7.2.2. Transactions with the affiliated entities under terms other than arm's length basis

All transactions with affiliated entities are concluded on arm's length basis.

Detailed information on significant transactions with affiliated entities has been provided in note 51 of the consolidated financial statements for the year ended on 31 December 2016.

7.2.3. Information on agreements on credits and loans raised and terminated

Working capital credits and loans for financing current activity

In accordance with the financial model adopted in TAURON Capital Group, only TAURON may act as the party to working capital credits and short-term loans raised with external institutions.

In TAURON Capital Group the real cash pooling structure operates, implemented under the agreement for cash management concluded with PKO BP. 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 implementation of the cash pooling mechanism, cash transfers are performed between accounts of participants of the service and the Agent's account. Within the operation of the cash pooling the Company uses the overdraft limit at PKO BP in the amount of PLN 300,000 thousand, based on the Overdraft Agreement concluded with the bank in December 2014, with the repayment date maturing on 29 December 2017 and the intraday limit in the amount of PLN 500,000 thousand, effective until 17 December 2017 (the intraday limit is a daily limit which must be fully repaid by the end of each day on which it was used).

Within the framework of financing its current activity TAURON concluded:

1) An overdraft agreement with BGK up to the amount of EUR 25,000 thousand, for financing of the transactions of purchase/ sales/ exchange of CO_2 emission allowances, trading in electricity and gas on the European exchanges, with the repayment deadline until 31 December 2017,
2) An overdraft agreement with mBank BGK up to the amount not exceeding of USD 2,000 thousand, allocated for financing of current activity, in particular, for financing of the collateral margin and commodity transactions. The repayment deadline of the loan, pursuant to the annex of 29 January 2016, falls on 31 March 2017.

The table below presents detailed specification of working capital loan and credit agreements effective in TAURON Capital Group in 2016.

Table no 47. Specification of working capital loan and credit agreements effective in TAURON Capital Group as at 31 December 2016

No.	Type of agreement	Interest rate	Amount of credit/loan (thou.)	Financing period	Balance as at 31 December 2016 (thou.)
1.	Overdraft facility	LIBOR 1M + fixed margin	USD 2,000	16.04.2015 – 30.03.2017	USD 411
2.	Overdraft facility	EURIBOR 1M + fixed margin	EUR 25,000	31.12.2015 – 31.12.2017	EUR 3,032
3.	Overdraft facility	WIBOR O/N + fixed margin	PLN 300,000	30.12.2014 – 29.12.2017	PLN 0
4.	Intraday Limit	None	PLN 500,000	18.12.2014 – 17.12.2017	PLN 0

Investment credits and loans

The table below presents detailed specification of investment credits and loan agreements effective in TAURON Capital Group as at 31 December 2016, whose party, in case of credit facilities, is the EIB, and in case of loans – the Regional Fund of Environmental Protection and Water Management in Katowice (for TAURON Wytwarzanie and TAURON Ciepło) and the Regional Fund of Environmental Protection and Water Management in Kraków (for KW Czatkowice) (WFOŚiGW).

Table no 48. Specification of investment credits and loan agreements effective in TAURON Capital Group as at 31 December 2016

No.	Parties to the agreement	Type of agreement	Interest rate	Amount of credit/loan (thou.)	Implementation term	Balance as at 31 December 2016 (thou.)
1.	TAURON – EIB	Credit	fixed margin	PLN 210,000	15.12.2021	PLN 105,000
2.	TAURON – EIB	Credit	fixed margin	PLN 300,000	15.12.2021	PLN 150,000
3.	TAURON – EIB	Credit	fixed margin	PLN 450,000	15.06.2024	PLN 306,818
4.	TAURON – EIB	Credit	fixed margin	PLN 200,000	15.09.2024	PLN 145,455
5.	TAURON – EIB	Credit	fixed margin	PLN 250,000	15.09.2024	PLN 181,818
6.	TAURON – EIB	Credit	fixed margin	PLN 295,000	15.03.2027	PLN 295,000
7.	TAURON Wytwarzanie – WFOŚiGW	Loan	base rate + fixed margin	PLN 40,000	15.12.2022	PLN 24,000
8.	TAURON Ciepło – WFOŚiGW	Loan	fixed margin	PLN 30,000	15.12.2022	PLN 18,103
9.	KW Czatkowice – WFOŚiGW	Loan	fixed margin	PLN 914	31.05.2021	PLN 807
10.	KW Czatkowice – WFOŚiGW	Loan	fixed margin	PLN 513	30.06.2018	PLN 154
11.	KW Czatkowice – WFOŚiGW	Loan	fixed margin	PLN 128	30.09.2018	PLN 45
12.	KW Czatkowice – WFOŚiGW	Loan	fixed margin	PLN 154	30.09.2018	PLN 54
13.	KW Czatkowice – WFOŚiGW	Loan	fixed margin	PLN 256	30.09.2018	PLN 90
14.	KW Czatkowice – WFOŚiGW	Loan	fixed margin	PLN 94	15.12.2018	PLN 38

In 2016, companies of TAURON Capital Group did not terminate any credit and loan agreements.

7.2.4. Information on loans and sureties granted as well as sureties and guarantees received

Loans granted

Besides companies covered by consolidation, in 2016 TAURON granted financing to the co-subsidiary, EC Stalowa Wola in the form of 5 loans allocated for the current activity of EC Stalowa Wola and repayment of loan instalments of this company.

On 30 December 2016 TAURON signed an annex with EC Stalowa Wola to the loan agreement up to the amount of PLN 2,600 thousand, pursuant to which the repayment of the loan, including accrued interest shall be made in a one-off operation, by 30 June 2017 at the latest.

The table below presents the specification of loans granted by TAURON to companies of TAURON Capital Group effective as at 31 December 2016.

Table no 49. Specification of loans granted by TAURON, effective as at 31 December 2016

No.	Type of agreement	Interest rate	Loan amount arising from the agreement (thou.)	Effective term	Balance as at 31 December 2016 (thou.)
1.	EC Stalowa Wola	WIBOR 1 M + fixed margin	PLN 5,500	22.01.2016 – 30.06.2017	PLN 5,500
2.	EC Stalowa Wola	WIBOR 1 M + fixed margin	PLN 1,200	22.04.2016 – 30.06.2017	PLN 600
3.	EC Stalowa Wola	WIBOR 1 M + fixed margin	PLN 3,100	27.05.2016 – 30.06.2017	PLN 3,100
4.	EC Stalowa Wola	WIBOR 1 M + fixed margin	PLN 3,800	31.08.2016 – 30.06.2017	PLN 2,875

No.	Type of agreement	Interest rate	Loan amount arising from the agreement (thou.)	Effective term	Balance as at 31 December 2016 (thou.)
5.	EC Stalowa Wola	WIBOR 6M + fixed margin	PLN 15,300	15.12.2016 – 31.12.2027	PLN 11,000
6.	EC Stalowa Wola	WIBOR 3M + fixed margin	PLN 177,000	20.06.2012 – 31.12.2032	PLN 177,000
7.	EC Stalowa Wola	WIBOR 6M + fixed margin	PLN 2,600	25.11.2015 – 30.06.2017	PLN 2,600
8.	EC Stalowa Wola	WIBOR 3M + fixed margin	PLN 15,850	14.12.2015 – 31.12.2027	PLN 15,850

Sureties and guarantees granted and received

The guaranties and sureties effective in 2016 arise from the adopted financing model of TAURON Capital Group and they were provided by TAURON in connection with the conducted trading operations and as the collateral for repayment of loans granted, among others by WFOŚiGW in Katowice and WFOŚiGW in Kraków.

The table below presents the specification of collaterals granted by TAURON to companies of TAURON Capital Group, effective as at 31 December 2016

Table no 50. Specification of securities granted by TAURON, effective as at 31 December 2016

No.	Beneficiary	Agreement/Collateral	Party to the agreement	Amount (thou.)	Effective date
1.	WFOŚiGW	Bill of exchange with a promissory note	TAURON Wytwarzanie	PLN 40,000	15.12.2022
2.	WFOŚiGW	Bill of exchange with a promissory note	TAURON Ciepło	PLN 30,000	15.12.2022
3.	WFOŚiGW	Surety agreement	KW Czatkowice	PLN 914	15.06.2021
4.	WFOŚiGW	Surety agreement	KW Czatkowice	PLN 513	31.07.2018
5.	WFOŚiGW	Surety agreement	KW Czatkowice	PLN 256	31.10.2018
6.	WFOŚiGW	Surety agreement	KW Czatkowice	PLN 128	31.10.2018
7.	WFOŚiGW	Surety agreement	KW Czatkowice	PLN 154	31.10.2018
8.	WFOŚiGW	Surety agreement	KW Czatkowice	PLN 94	15.01.2019
9.	Bondholders	Corporate guarantee	TAURON Sweden Energy	EUR 168,000	03.12.2029
10.	PSG	Surety agreement	TAURON Sprzedaż	PLN 15,000	31.03.2017
11.	PSE	Surety agreement	TAURON Wytwarzanie	PLN 5,000	04.08.2019
12.	Millennium Leasing	Surety agreement	TAURON Wydobycie	PLN 2,900	30.10.2017

TAURON has also concluded the following agreements concerning the issuance of bank guarantees:

1) the general agreement of 8 June 2015 for the bank guarantee limits, concluded with BZ WBK, with the effective term until 7 June 2018, and the limit up to PLN 150,000 thousand, to be used by TAURON and its subsidiaries in favour of Izba Rozliczeniowa Giełd Towarowych S.A. (IRGIT).
2) The agreement for the limit for bank guarantees of 12 July 2016 concluded with CaixaBank S.A (Spółka Akcyjna) Oddział w Polsce (CaixaBank) pursuant to which the limit for 36 months was granted, i.e. Until 11 July 2019. At the same time, the maximum period of effectiveness of bank guarantees must not exceed the date of 11 July 2019, to be used by TAURON and subsidiaries in connection with conducted operations.
3) Agreement for the guarantee limit concluded on 25 October 2016 with The Bank of Tokyo-Mitsubishi UFJ, Ltd. (BTM UFJ). The guarantee limit up to the amount of PLN 314,486 thousand is allocated for bank guarantees granted in accordance with the standstill agreement of 15 September 2016 concluded between TAURON, EC Stalowa Wola, PGNiG and banks financing EC Stalowa Wola with the validity term until 14 April 2017.

   At the same time, on 31 December 2016 the General Agreement of 22 September 2011 expired, including its subsequent annexes, for granting bank guarantees, concluded with PKO BP, for the amount of PLN 100,000 thousand, to be used by TAURON and its subsidiaries.

The table below presents the specification of bank guaranties granted under the agreements effective as at 31 December 2016.

Table no 51. Specification of bank guaranties granted under the agreements effective as at 31 December 2016

No.	Bank	Company	Beneficiary	Type of guarantee	Amount (thou.)	Date of commencement	Date of effectiveness
1.	BZ WBK	TAURON	IRGIT	payments	PLN 30,000	14.12.2016	17.01.2017
2.	BZ WBK	TAURON	IRGIT	payments	PLN 40,000	11.08.2016	17.01.2017
3.	BZ WBK	TAURON	IRGIT	payments	PLN 30,000	11.08.2016	17.01.2017
4.	BTM UFJ	TAURON	Bank Pekao	payments	PLN 74,992	30.10.2016	14.04.2017
5.	BTM UFJ	TAURON	EBOR	payments	PLN 83,494	30.10.2016	14.04.2017
6.	BTM UFJ	TAURON	EIB	payments	PLN 156,000	30.10.2016	14.04.2017
7.	CaixaBank	TAURON	GAZ-SYSTEM	performance bond	PLN 3,664	01.12.2016	30.11.2017
8.	CaixaBank	KW Czatkowice	PGE	performance bond	PLN 147	09.09.2016	31.01.2018
9.	CaixaBank	TAURON Dystrybucja Serwis	Strabag Infrastruktura Południe	performance bond	PLN 116	09.09.2016	15.06.2019

Moreover, on 31 December 2016 four guarantees issued within the limit in PKO BP in the previous years expired, i.e.:

1) TAURON Wydobycie guarantee in favour of Polskie Koleje Państwowe S.A. in the amount of PLN 76 thousand,
2) KW Czatkowice guarantee in favour of CEZ Chorzów S.A. in the amount of PLN 1,422 thousand,
3) TAURON Dystrybucja guarantee in favour of Jelenia Góra city in the amount of PLN 97 thousand,
4) TAURON Dystrybucja Serwis guarantee in favour of Dragados Oddział w Polsce S.A in the amount of PLN 96 thousand.

At the same time, under the agreement on limit for bank guarantees concluded with BZ WBK during 2016 TAURON ordered issuance of bank guarantees in favour of IRGIT for hedging the transactions carried out at TGE, with the effective term below one year.

Within TAURON Capital Group, in order to secure the transactions executed by the Company on the TGE in electricity markets and participation in the system of securing the liquidity of transaction settlement, in the 1st quarter the agreement of 14 October 2015 was effective, pursuant to which TAURON Wytwarzanie granted the surety to TAURON in favour of the IRGIT, on account of the settlement of future transactions up to the amount of PLN 123,000 thousand. The agreement was effective until 31 March 2016.

Company Management Board

Katowice, 13 March 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	....
Piotr Zawistowski	– Vice-President of the Management Board	....

Appendix A: GLOSSARY OF TERMS AND LIST OF ABBREVIATIONS

Below the glossary of trade terms and the list of abbreviations and acronyms most commonly used in this report, is presented.

Table no 52. Explanation of abbreviations and acronyms, and trade terms applied in the text of the report

No.	Abbreviation and trade term	Full name/explanation
1.	ARE	Agency of Energy Market (Agencja Rynku Energii S.A.) with the seat in Warsaw
2.	BGK	Bank Gospodarstwa Krajowego with the seat in Warsaw
3.	Biomass TAURON Group	Biomasa Grupa TAURON sp. z o.o. with the seat in Stalowa Wola
4.	BZ WBK	Bank Zachodni WBK S.A. with the seat in Wrocław
5.	B2B	(business-to-business) the acronym designating transaction between two or more economic operators
6.	Cash pooling	Cash pooling operating in the Company – consolidation of balances of bank accounts through physical cross-posting of cash from accounts of TAURON Capital Group in the bank in which cash pooling operates to the bank account of Pool Leader whose function is fulfilled by the Company. At the end of each working day, from cash is cross-posted from the bank accounts of companies of TAURON Capital Group which show positive balance to the bank account of Pool Leader. At the beginning of each working day, bank accounts of companies of TAURON Capital Group are credited from the bank account of the Pool Leader with the amount demanded to maintain cash flow of the company of TAURON Capital Group on a given working day.
7.	Colour certificates	Property rights resulting from certificates of origin of energy generated in the way subject to support, the so-called colour certificates: 1) **green** – certificates of origin of electricity from renewable energy sources, 2) **violet** – certificates of origin of electric energy generated in cogeneration, burning methane released and captured during underground mining works in active, under liquidation or liquidated hard coal mines, or burning gas acquired from biomass processing, 3) **red** – certificates of origin of electric energy from co-generation (CHP certificates – Combined Heat and Power), 4) **yellow** – certificates of origin of electric energy generated in cogeneration from sources of total installed capacity below 1 MW or gas-burning, 5) **blue** – certificates of origin of electricity from agricultural biogas. **White** – certificates of energy efficiency (mechanism stimulating pro-saving behaviour).
8.	CSI	(Customer Satisfaction Index) Index used in marketing to determine the level of clients' satisfaction from products or services offered by the company
9.	CSR	(Corporate Social Responsibility) social responsibility of business
10.	CUW	Centre of Common Services, CUW R – services in the area of accounting
11.	DM	Brokerage House
12.	Best Practice 2016	Best Practice of GPW Listed Companies 2016, effective as of 01 January 2016
13.	EIB	The European Investment Bank with the seat in Luxemburg
14.	EBIT	(Interest Rate Swap) result on operating activity before taxing
15.	EBITDA	(Earnings Before Interest, Taxes, Depreciation and Amortization) result on operating activity before taxing, increased by amortization and depreciation
16.	EC Stalowa Wola	Elektrociepłownia Stalowa Wola S.A. with the seat in Stalowa Wola
17.	ElectroMobility Poland	ElectroMobility Poland S.A. company with its registered office in Warsaw
18.	Elektrownia Blachownia Nowa in liquidation	Elektrownia Blachownia Nowa sp. z o.o. with the seat in Kędzierzyn Koźle.
19.	ENEA	ENEA S.A. with the seat in Poznań
20.	ENERGA	ENERGA S.A. with the seat in Gdańsk
21.	ERM	Enterprise risk management system

No.	Abbreviation and trade term	Full name/explanation
22.	EU ETS	(European Union Emission Trading System) the European system of CO_2 emission allowances trading
23.	EUA	(European Union Allowances) – allowance to introduce the equivalent to the air, within the meaning of art. 2 item 4 of the Act of 17 July 2009 on the management system of emissions of greenhouse gases and other substances, carbon dioxide (CO_2), which is used for settlements of emission size within the system, which can be managed based on principles stipulated in the *Act of 28 April 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	Operator of Transmission Gas Pipelines GAZ-SYSTEM S.A. with its seat in Warsaw
26.	GPW	Warsaw Stock Exchange (Giełda Papierów Wartościowych w Warszawie S.A.) with the seat in Warsaw
27.	GRI	Global Reporting Initiative
28.	TAURON Capital Group	TAURON Polska Energia S.A. Capital Group
29.	GUS	Central Statistical Office
30.	GZE	Górnośląski Zakład Elektroenergetyczny
31.	IRGIT	Izba Rozliczeniowa Giełd Towarowych S.A. (Commodity Exchange Clearing House) with the seat in Warsaw
32.	IRS	(Interest Rate Swap) contract on exchange of interest rate payments, one of the basic derivatives subject to trade at the interbank market
33.	EC	European Commission
34.	KGHM	KGHM Polska Miedź S.A. with the seat in Lubin
35.	KIC InnoEnergy	Community of Knowledge and Innovation – KIC InnoEnergy, with its seat in Kraków
36.	Audit Committee	Audit Committee of the Supervisory Board of TAURON Polska Energia S.A.
37.	Nominations and Remuneration Committee	Nominations and Remuneration Committee of the Supervisory Board of TAURON Polska Energia S.A.
38.	Strategy Committee	Strategy Committee of the Supervisory Board of TAURON Polska Energia S.A.
39.	KPI	(Key Performance Indicators) key financial and non-financial indicators used as measures in processes of measurement of the level of organisation goal accomplishment
40.	KSE	National Power System
41.	KSH	Code of Commercial Companies
42.	KW Czatkowice	Kopalnia Wapienia Czatkowice sp. z o.o. with the seat in Krzeszowice
43.	KWK Brzeszcze	“Brzeszcze” Coal Mine with the seat in Brzeszcze
44.	KZEE	National consumption of electricity
45.	Business model	The document entitled *Code of TAURON Group*, adopted by the Management Board of the Company
46.	mBank	mBank S.A. with the seat in Warsaw
47.	Marselwind	Marselwind sp. z o.o. with the seat in Katowice
48.	Mg	Megagram – million gram (1,000,000 g) i.e. 1 t
49.	MSR	(Market Stability Reserve) stabilisation reserve on the market of allowances
50.	IFRS	International Financial Reporting Standards
51.	NCBR	National Centre for Research and Development with its registered Warsaw
52.	Nowe Brzeszcze GT	Nowe Brzeszcze Grupa TAURON sp. z o.o. with the seat in Brzeszcze, currently ZG Brzeszcze in TAURON Wydobycie
53.	Business Area	Seven Business Areas of core activity of TAURON Capital Group: Trade, Mining, Generation, RES, Heat, Distribution and Sales.

No.	Abbreviation and trade term	Full name/explanation
54.	KZEE	(Organization of the Petroleum Exporting Countries with its seat in Vienna
55.	ORM	Operating Power Reserve
56.	DSO	Distribution System Operator
57.	TSO	Transmission System Operator
58.	OTC (OTC market)	(Over The Counter Market) – the European market operating outside the regulated exchange market
59.	RES	Renewable Energy Sources
60.	Efficiency Improvement Programme	the Efficiency Improvement Programme in TAURON Group for 2016–2018
61.	PEPKH in liquidation	Polska Energia – Pierwsza Kompania Handlowa sp. z o.o. with the seat in Warsaw, in liquidation
62.	PGE	PGE Polska Grupa Energetyczna S.A. with the seat in Warsaw
63.	PGE EJ1	PGE EJ1 sp. z o.o. with the seat in Warsaw
64.	PGNiG	Polskie Górnictwo Naftowe i Gazownictwo S.A. with its registered office in Warsaw
65.	GDP	Gross Domestic Product
66.	PKO BP	Powszechna Kasa Oszczędności Bank Polski S.A. with the seat in Warsaw
67.	PLN	The symbol of Polish currency – Polish Zloty
68.	PMEC	Property rights for certificates of origin confirming generation of electricity in other co-generation sources
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, burning methane released and captured during underground mining works in active, under liquidation or liquidated hard coal mines, or burning gas acquired from biomass processing
71.	PMOZE	Property rights for certificates of origin confirming generation of electricity in RES in the period before 1 March 2009
72.	PMOZE_A	Property rights for certificates of origin confirming generation of electricity in RES in the period after 1 March 2009
73.	PMOZE-BIO	Property rights resulting from certificates of origin of electricity generated from agricultural biogas as of 1 July 2016
74.	PSE	Polskie Sieci Elektroenergetyczne S.A. with the seat in Konstancin-Jeziorna
75.	PSG	Polska Spółka Gazownictwa sp. z o.o. with the seat in Warsaw
76.	RB	Balancing Market
77.	RDN	Day Ahead Market
78.	RESPECT Index	Exchange index where companies operating in accordance with the sustainable development rules are listed
79.	RTT	Commodity Forward Market
80.	Segment, Segments of activity	Segments of activity of TAURON Capital Group used in the process of statutory reporting. Results of TAURON Capital Group, activities were assigned to the following five Segments hereinafter also referred to as Areas: Mining, Generation, Distribution, Sales and Other
81.	SPOT (SPOT Market)	In relation to electric energy, it is the place of concluding of trade transactions for electric energy, for which the period of delivery falls at the latest, three days after the date of transaction (usually one day before the date of delivery). Functioning of SPOT market for electric energy is strongly linked with RB operating provided by the TSO
82.	Company, TAURON	TAURON Polska Energia S.A. with the seat in Katowice
83.	Strategy	The document entitled *Strategy of TAURON Group for 2016–2025* being the update of the document *Corporate Strategy of TAURON Group for 2014–2017 with estimates until the year 2023,* effective until 1 September 2016

No.	Abbreviation and trade term	Full name/explanation
84.	Sustainability Strategy	The document entitled *Sustainability Strategy of TAURON Group for 2016–2018 with estimates until the year 2020*, being the update of the document *Sustainability Strategy of TAURON Group for 2012–2015 with estimates until the year 2020*
85.	TAMEH Czech	TAURON Czech s.r.o. with the seat in Ostrava, Czech Republic
86.	TAMEH HOLDING	TAMEH HOLDING sp. z o.o. with the seat in Dąbrowa Górnicza
87.	TAMEH POLSKA	TAMEH HOLDING sp. z o.o. with the seat in Dąbrowa Górnicza
88.	TAURON/Company	TAURON Polska Energia S.A. with the seat in Katowice
89.	TAURON Ciepło	TAURON Ciepło sp. z o.o. with the seat in Katowice
90.	TAURON Czech Energy	TAURON Czech Energy s.r.o. with the seat in Ostrava, Czech Republic
91.	TAURON Dystrybucja	TAURON Dystrybucja S.A. with the seat in Kraków
92.	TAURON Dystrybucja Pomiary	TAURON Dystrybucja Pomiary sp. z o.o. with the seat in Tarnów
93.	TAURON Dystrybucja Serwis	TAURON Dystrybucja Serwis S.A. with the seat in Wrocław
94.	TAURON EKOENERGIA	TAURON EKOENERGIA sp. z o.o. with the seat in Jelenia Góra
95.	TAURON Obsługa Klienta	TAURON Obsługa Klienta sp. z o.o. with the seat in Wrocław
96.	TAURON Serwis	TAURON Serwis sp. z o.o. with the 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 the seat in Gliwice
99.	TAURON Sweden Energy	TAURON Sweden Energy AB (publ) with the seat in Stockholmm, Sweden
100.	TAURON Wydobycie	TAURON Wydobycie S.A. with the seat in Jaworzno
101.	TAURON Wytwarzanie	TAURON Wytwarzanie S.A. with the seat in Jaworzno
102.	TAURON Wytwarzanie Serwis	TAURON Wytwarzanie Serwis sp. with the seat in Jaworzno
103.	TGE	Towarowa Giełda Energii S.A. (Polish Power Exchange) with the seat in Warsaw
104.	EU	European Union
105.	UOKiK	Office for Competition and Consumer Protection (Urząd Ochrony Konkurencji i Konsumentów)
106.	USD	(United States Dollar) international abbreviation of American dollar
107.	ERO	Energy Regulatory Office (Urząd Regulacji Energetyki)
108.	WFOŚiGW	Regional Fund of Environmental Protection and Water Management in Katowice or in Kraków
109.	GM/SM	General Meeting/ Shareholders' Meeting
110.	ZG	Mining Plant
111.	ZW Bielsko-Biała, ZW Kamienna Góra, ZW Katowice, ZW Tychy	Generation Plants in Bielsko-Biała, Kamienna Góra, Katowice, Tychy

Appendix B: INDEX OF TABLES AND FIGURES

Below the list of tables and figures occurring in this report is provided.

List of Tables

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STATEMENTS OF THE MANAGEMENT BOARD OF TAURON POLSKA ENERGIA S.A.

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 my best knowledge, the Consolidated financial statements of TAURON Capital Group and comparable figures were prepared in accordance with applicable accounting rules and give the true and fair picture of the assets, financial standing and performance of TAURON Capital Group.

I also certify that the Management Board's report on the operations of TAURON Capital Group gives the true picture of the development, achievements and situation of TAURON Polska Energia S.A. Capital Group, including the description of key risks and threats.

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	....
Piotr Zawistowski	– Vice-President of the Management Board	....

13 March 2017

Date

STATEMENT

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	....
Piotr Zawistowski	– Vice-President of the Management Board	....

13 March 2017
Date