Annual report of TAURON Polska Energia S.A. for the year 2017

13 March 2018

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

Ladies and Gentlemen,

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

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

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

To my satisfaction I may say that TAURON took advantage of the opportunities presented by the strong growth of the Polish economy. We generated sales revenue of PLN 7.8 bln in 2017. As a result of our effective actions EBITDA and net profit reached, respectively, PLN 268 mln and PLN 854 mln versus a loss posted in 2016.

TAURON, as a parent company of its Capital Group, stimulated actions resulting in the improvement of almost all operating and financial indicators in the individual lines of business. Higher hard coal production output and sales volume as well as rising electricity production, distribution and supply volumes should be noted.

Throughout TAURON Group we were steadfastly implementing the efficiency improvement program the effects of which, since its launch in 2016, topped one billion PLN. All efficiency improvement actions undertaken brought, in total, a positive financial effect of two billion PLN.

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

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

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

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

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

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

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

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

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

Yours respectfully,

Filip Grzegorczyk

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

Katowice, March 2018

SELECTED FINANCIAL DATA	in thousands PLN		in thousands EUR	
	2017 period from 01.01.2017 to 31.12.2017	2016 period from 01.01.2016 to 31.12.2016	2017 period from 01.01.2017 to 31.12.2017	2016 period from 01.01.2016 to 31.12.2016
Selected stand-alone financial data of TAURON Polska Energia S.A.				
Revenues on sales	7 792 025	7 995 328	1 835 707	1 827 211
Operating profit (loss)	262 788	(34 603)	61 910	(7 908)
Profit (loss) before tax	919 565	(149 134)	216 638	(34 082)
Net profit (loss)	854 351	(166 253)	201 275	(37 995)
Other total income	(6 713)	104 024	(1 582)	23 773
Total aggregate income	847 638	(62 229)	199 693	(14 222)
Profit (loss) per share (in PLN/EUR) (basic and diluted)	0.49	(0.09)	0.12	(0.02)
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	246 027	(232 887)	57 961	(53 223)
Net cash flows from investment activity	(1 353 288)	(619 543)	(318 818)	(141 587)
Net cash flows from financial activity	593 470	486 164	139 814	111 105
Increase/(decrease) in net cash and equivalents	(513 791)	(366 266)	(121 043)	(83 705)
	Status as at 31.12.2017	**Status as at 31.12.2016**	**Status as at 31.12.2017**	**Status as at 31.12.2016**
Fixed assets	27 371 425	25 855 329	6 562 475	5 844 333
Current assets	2 901 667	1 817 047	695 693	410 725
Total Assets	30 273 092	27 672 376	7 258 168	6 255 058
Share capital	8 762 747	8 762 747	2 100 925	1 980 729
Equity	17 377 906	16 530 268	4 166 464	3 736 498
Long-term liabilities	9 530 528	8 969 976	2 285 005	2 027 572
Short-term liabilities	3 364 658	2 172 132	806 698	490 988
Total liabilities	12 895 186	11 142 108	3 091 703	2 518 560

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

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

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

TAURON POLSKA ENERGIA S.A.

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

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

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

The audit report on the annual financial statements

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

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

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

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

Auditor’s responsibility

Our objective was to express an opinion on whether the accompanying financial statements give a true and fair view[1] of the financial position and results of the operations of the Company in accordance with International Accounting Standards, International Financial Reporting Standards and related interpretations announced in the form of European Commission regulations and adopted accounting policies.

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

[1] Translation of the following expression in Polish is ‘rzetelny i jasny obraz’.

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

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

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

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

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

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

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

Independence

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

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

Appointment of the audit firm

We were appointed to audit the Company's financial statements based on the Company's Supervisory Board resolution dated March 15, 2017. We have been auditing the financial statements of the Company consecutively since the beginning of the financial year ended 31 December 2017.

Most significant assessed risks

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

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

description of the nature of the risk of material misstatement (key audit matters)	*audit procedures in response to the identified risk*
1. Impairment of assets analysis *Why the issue is a key audit matter* As at December 31, 2017, the Company presented loans receivable and bought bonds (with a carrying amount of approximately PLN 7 476 mln), as well as shares (with a carrying amount of approximately PLN 20 913 mln) constituting in total approximately 94% of the Company's balance sheet total. According to IFRS, based on the analysis of the indicators for impairment of assets (shares), as well as based on identifying objective events indicating a possible loss of value of loans receivable and bought bonds, as described in note 11 to the financial statements, the Company has performed an impairment test for the above-mentioned assets. The issue was identified as key audit matter in the audit of the financial statements due to the value of the assets listed above, which is significant for the financial statements, as well as due to the element of professional judgment of the management and the complexity of the impairment tests. Tests of impairment require the Management Board to adopt a number of assumptions regarding future market and economic conditions, such as the strategy of TAURON Polska Energia SA, future changes in the prices of raw materials, electricity, property rights arising from certificates of origin of energy, CO2 emission rights and future revenues, costs and	*Audit approach* Our procedures, in relation to the key audit matter described, included, among others: • Overview of the process and identification of control mechanisms operating in the Company related to impairment tests of assets, as well as an understanding of the applied accounting policies and procedures, including internal control environment related to the process of assessing impairment indicators and performing of impairment tests, • Assessment of the assumptions made with regard to the grouping of assets into cash-generating units (CGU), • Assessment (with the assistance of valuation specialists) of estimates and assumptions made by the Company in order to determine the assets recoverable amount, including: - the key macroeconomic assumptions adopted by the Company for future years (including: discount rates, projected growth rate) by comparing them to market data and available external data; - arithmetical correctness of the discounted cash flows model, and - assumptions made to determine cash flows and residual values after the period covered by a detailed strategy; • Inquiries to employees of the financial department and the Management Board of the parent entity referring to the status of implementation of the adopted

cash flows, weighted average cost of capital ("WACC"), as well as the impact of potential and already approved Polish and European regulatory changes, including environmental protection and the expected shape of the power market, and the anticipated macroeconomic situation. The results of impairment tests could differ materially if the model used different assumptions. *A reference to disclosure in the financial statements* The Company disclosed information regarding impairment indicators, adopted estimates for the purpose of the impairment test, as well as impairment losses on the assets in note 11 of the notes to the financial statements for the year ended December 31, 2017.	assumptions, including the validity of key estimates, • Analysis of external sources of information such as industry press and evaluation of potential risk related to the implementation of the assumptions with the support of valuation specialists; • Reconciliation of source data used in impairment test models and assessment of impairment triggers for financial forecasts approved by the Management Board of the parent company; • Assessment of completeness of disclosures in the financial statements of the Company in terms of impairment in accordance with the International Accounting Standard 36 Impairment of assets and International Accounting Standard 39 Financial Instruments.
2. Claims, lawsuits and contingent liabilities *Why the issue is a key audit matter* The Company is a party to many significant claims and court cases. The most significant are potential and submitted claims identified by the Company related to the termination of long-term contracts for the purchase of electricity and property rights arising from certificates of origin of energy generated in renewable energy sources. The obligation to create adequate provision and its amount, as well as the	*Audit approach* Our procedures, in relation to the key audit matter described, included, among others: • Monitoring of external sources of information to identify breaches or potential violations of law and regulations by the Company; • Review of the documentation regarding court cases presented for the audit purposes and discussion of significant court cases with the Legal Project Management Team of the Company; • Analysis of the costs of legal services incurred during the year in order to confirm the completeness of entities providing legal services to the Company;

<table>
<tr>
<td>estimate of the value of contingent liabilities are the subject of the Management Board's judgment.

A reference to disclosure in the financial statements

The Company disclosed information regarding claims and court cases in note 44 of the notes to the financial statements for the year ended December 31, 2017.</td>
<td>Obtaining written explanations from lawyers serving the Company with regard to the court and disputable cases conducted by them, and analysis of the provided explanations;
Discussion of the selected court cases with internal specialists in the field of law;
Analysis and assessment of contingent liabilities and changes in the value of provisions for claims and court cases;
Review of minutes of meetings of the legal bodies of the Company as well as control reports of supervisory authorities and correspondence with these authorities.
Assessment of the completeness of disclosures regarding pending major court and out-of-court proceedings and related contingent liabilities in the financial statements.</td>
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<td>3. Change of the statutory auditor and audit of the opening balances

Why the issue is a key audit matter

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

In accordance with the provisions of the National Auditing Standard 510, in the wording of International Auditing Standard 510 "Initial Engagements - opening balances", the first-year audit of financial statements requires performing of a number of additional audit procedures that are limited in the</td>
<td>Audit approach

Our procedures, in relation to the key audit matter described, included, among others:
the initiating meeting with key personnel responsible for financial reporting of the Company as well as meetings with members of the audit team, including specialists planned to be involved in the audit procedures,
understanding of the Company’s operations, its business environment and key risk areas related to its operations,
understanding of the Company’s internal control environment, including also tests of identified controls,
understanding of the Company’s IT environment,
understanding of the accounting policy of the Company and assessing the continuity of its application,</td>
</tr>
</table>

case of the audit performed for a consecutive year. The purpose of these additional audit procedures is to collect sufficient and relevant audit evidence about whether: • opening balances contain misstatements that materially affect the financial statements for the current period and • appropriate accounting policy applied to the opening balances was used continuously in the preparation of financial statements for the current period, or whether the changes made were correctly accounted for and properly presented in accordance with the applicable financial reporting framework. Accordingly, this issue was identified as key audit matter for the audit of the financial statements of the Company.	• understanding of key areas of estimation and professional judgement of the Company's management, • communication with a key certified auditor acting on behalf of the previous audit firm including a discussion of key audit issues and a review of audit documentation from the previous reporting period, • assessment of the main audit issues from the previous reporting period and their impact on the financial statements for the current financial year, • obtaining a reasonable assurance of the opening balances by independently carrying out selected audit procedures in relation to this period. Our audit strategy has been discussed and agreed with the Management Board and the Audit Committee in order to know their expectations and discuss key reporting and auditing issues.

Opinion

In our opinion, accompanying financial statements:

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

Other matters

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

Report on other legal and regulatory requirements

Opinion on the Directors' Report

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

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

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

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

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

Opinion on the corporate governance application representation

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

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

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

Information on preparation of the statement on non-financial information

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

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

Warsaw, 12 March 2018

Key certified auditor

Leszek Lerch
Certified auditor no 9886

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

Rondo ONZ 1
00-124 Warsaw
Reg. No 130

TAURON POLSKA ENERGIA S.A.

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

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(in PLN '000)

STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended 31 December 2017	Year ended 31 December 2016
Sales revenue	**12**	7 792 025	7 995 328
Cost of sales	**13**	(7 414 707)	(7 837 567)
Profit on sale		**377 318**	**157 761**
Selling and distribution expenses	**13**	(23 309)	(19 326)
Administrative expenses	**13**	(88 751)	(81 368)
Other operating income and expenses		(2 470)	(91 670)
Operating profit (loss)		**262 788**	**(34 603)**
Dividend income	**15**	560 832	1 485 152
Interest income on bonds and loans	**15**	456 426	503 897
Interest expense on debt	**15**	(334 638)	(356 947)
Revaluation of shares and loans	**15**	(134 372)	(1 610 396)
Other finance income and costs	**15**	108 529	(136 237)
Profit (loss) before tax		**919 565**	**(149 134)**
Income tax expense	**16.1**	(65 214)	(17 119)
Net profit (loss)		**854 351**	**(166 253)**
Measurement of hedging instruments	**31.4**	(8 159)	127 252
Income tax expense	**16.1**	1 550	(24 178)
Other comprehensive income subject to reclassification to profit or loss		**(6 609)**	**103 074**
Actuarial gains/(losses)		(128)	1 173
Income tax expense	**16.1**	24	(223)
Other comprehensive income not subject to reclassification to profit or loss		**(104)**	**950**
Other comprehensive income, net of tax		**(6 713)**	**104 024**
Total comprehensive income		**847 638**	**(62 229)**
Earnings (loss) per share (in PLN):			
– basic and diluted, for net profit	**17**	0.49	(0.09)

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

(in PLN '000)

STATEMENT OF FINANCIAL POSITION

	Note	As at 31 December 2017	As at 31 December 2016
ASSETS			
Non-current assets			
Property, plant and equipment	**18**	449	1 276
Investment property	**19**	21 701	25 318
Intangible assets	**20**	1 263	2 191
Shares	**21**	20 912 679	14 874 418
Bonds	**22**	6 009 920	9 615 917
Loans granted	**25**	382 989	1 292 800
Derivative instruments	**23**	26 445	35 814
Other financial assets	**24**	2 724	1 524
Other non-financial assets	**29**	13 255	6 071
		27 371 425	**25 855 329**
Current assets			
Inventories	**26**	198 428	284 799
Receivables from buyers	**27**	719 133	840 656
Receivables arising from taxes and charges	**28**	36 094	120 586
Bonds	**22**	562 776	242 465
Loans granted	**25**	520 191	30 966
Derivative instruments	**23**	6 971	20 603
Other financial assets	**24**	131 640	55 354
Other non-financial assets	**29**	4 857	23 528
Cash and cash equivalents	**30**	721 577	198 090
		2 901 667	**1 817 047**
TOTAL ASSETS		**30 273 092**	**27 672 376**

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

(in PLN '000)

STATEMENT OF FINANCIAL POSITION – CONTINUED

	Note	As at 31 December 2017	As at 31 December 2016
EQUITY AND LIABILITIES			
Equity			
Issued capital	**31.1**	8 762 747	8 762 747
Reserve capital	**31.3**	7 657 086	7 823 339
Revaluation reserve from valuation of hedging instruments	**31.4**	23 051	29 660
Retained earnings / (Accumulated losses)	**31.5**	935 022	(85 478)
		17 377 906	**16 530 268**
Non-current liabilities			
Debt	**33**	9 472 454	8 754 047
Other financial liabilities	**38**	20 126	27 918
Derivative instruments	**23**	4 958	–
Deferred income tax liabilities	**16.3**	29 843	32 364
Provisions for employee benefits	**34**	3 147	2 534
Other provisions	**35**	–	152 943
Accruals, deferred income and government grants	**36**	–	170
		9 530 528	**8 969 976**
Current liabilities			
Debt	**33**	2 725 763	1 433 929
Liabilities to suppliers	**37**	413 265	473 637
Other financial liabilities	**38**	62 590	111 759
Derivative instruments	**23**	9 226	560
Liabilities arising from taxes and charges	**39**	70 119	20 209
Provisions for employee benefits	**34**	330	299
Other provisions	**35**	68 771	110 406
Accruals, deferred income and government grants	**36**	14 594	21 333
		3 364 658	**2 172 132**
Total liabilities		**12 895 186**	**11 142 108**
TOTAL EQUITY AND LIABILITIES		**30 273 092**	**27 672 376**

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

(in PLN '000)

STATEMENT OF CHANGES IN EQUITY

	Note	Issued capital	Reserve capital	Revaluation reserve from valuation of hedging instruments	Retained earnings/ (Accumulated losses)	Total equity
As at 1 January 2016		**8 762 747**	**11 277 247**	**(73 414)**	**(3 374 083)**	**16 592 497**
Coverage of prior years loss		–	(3 453 908)	–	3 453 908	**–**
Transactions with shareholders		**–**	**(3 453 908)**	**–**	**3 453 908**	**–**
Net profit (loss)		–	–	–	(166 253)	**(166 253)**
Other comprehensive income		–	–	103 074	950	**104 024**
Total comprehensive income		**–**	**–**	**103 074**	**(165 303)**	**(62 229)**
As at 31 December 2016		**8 762 747**	**7 823 339**	**29 660**	**(85 478)**	**16 530 268**
Coverage of prior years loss	**31.3**	–	(166 253)	–	166 253	**–**
Transactions with shareholders		**–**	**(166 253)**	**–**	**166 253**	**–**
Net profit (loss)		–	–	–	854 351	**854 351**
Other comprehensive income		–	–	(6 609)	(104)	**(6 713)**
Total comprehensive income		**–**	**–**	**(6 609)**	**854 247**	**847 638**
As at 31 December 2017		**8 762 747**	**7 657 086**	**23 051**	**935 022**	**17 377 906**

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

(in PLN '000)

STATEMENT OF CASH FLOWS

	Note	Year ended 31 December 2017	Year ended 31 December 2016
Cash flows from operating activities			
Profit before taxation (loss)		919 565	(149 134)
Depreciation and amortization		5 532	7 722
Interest and dividends, net		(685 709)	(1 625 894)
Impairment losses on shares and loans		134 372	1 610 396
Foreign exchange difference		(130 351)	23 367
Other adjustments of profit before tax		31 218	61 988
Change in working capital	**40.1**	(57 218)	(130 749)
Income tax paid		28 618	(30 583)
Net cash from (used in) operating activities		**246 027**	**(232 887)**
Cash flows from investing activities			
Purchase of property, plant and equipment and intangible assets		(524)	(1 344)
Purchase of bonds	**40.2**	(350 000)	(2 770 000)
Purchase of shares	**40.2**	(6 169 590)	(543 603)
Loans granted	**40.2**	(307 132)	(23 575)
Purchase of investment fund units		(75 000)	(25 000)
Total payments		**(6 902 246)**	**(3 363 522)**
Redemption of bonds	**40.2**	3 547 110	540 000
Repayment of loans granted	**40.2**	1 000 000	142 024
Dividends received		359 787	1 485 152
Interest received	**40.2**	642 017	474 126
Other proceeds		44	102 677
Total proceeds		**5 548 958**	**2 743 979**
Net cash from (used in) investing activities		**(1 353 288)**	**(619 543)**
Cash flows from financing activities			
Payment of finance lease liabilities		(3 442)	(3 208)
Repayment of loans and borrowings	**40.3**	(175 695)	(132 818)
Redemption of debt securities	**40.3**	(1 650 000)	(3 300 000)
Interest paid	**40.3**	(265 223)	(351 147)
Commission paid		(19 632)	(11 411)
Total payments		**(2 113 992)**	**(3 798 584)**
Issue of debt securities	**40.3**	2 707 462	4 284 607
Other proceeds		–	141
Total proceeds		**2 707 462**	**4 284 748**
Net cash from financing activities		**593 470**	**486 164**
Net increase / (decrease) in cash and cash equivalents		**(513 791)**	**(366 266)**
Net foreign exchange difference		2 038	1 179
Cash and cash equivalents at the beginning of the period	**30**	**(1 045 441)**	**(679 175)**
Cash and cash equivalents at the end of the period, of which:	**30**	**(1 559 232)**	**(1 045 441)**
restricted cash	**30**	49 792	56 787

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

INFORMATION ABOUT TAURON POLSKA ENERGIA S.A. AND BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS

1. General information about TAURON Polska Energia S.A.

These financial statements have been prepared by TAURON Polska Energia Spółka Akcyjna (the "Company") with its registered office in ul. ks. Piotra Ściegiennego 3 in Katowice, Poland, whose shares are publicly traded.

The Company was established by a notarized deed on 6 December 2006 under the name of Energetyka Południe S.A. On 8 January 2007, the Company was registered at the District Court for Katowice-Wschód, Business Division of the National Court Register, under number KRS 0000271562. The change of the name to TAURON Polska Energia S.A. was registered with the District Court on 16 November 2007.

The Company was assigned statistical number (REGON) 240524697 and tax identification number (NIP) 9542583988.

TAURON Polska Energia S.A. was established for an unlimited period.

The core business of TAURON Polska Energia S.A. is:

- head office and holding operations, except for financial holdings — PKD 70.10 Z;
- sales of electricity — PKD 35.14 Z;
- sales of coal — PKD 46.71.Z;
- sales of gaseous fuels in a network system — PKD 35.23.Z.

TAURON Polska Energia S.A. is the parent of the TAURON Polska Energia S.A. Capital Group (the "Group", the "TAURON Group").

The financial statements prepared by the Company cover the financial year ended 31 December 2017 and include comparative information for the year ended 31 December 2016. These financial statements were approved for publication by the Management Board on 12 March 2018.

The consolidated financial statements for the year ended 31 December 2017 prepared by the Company were approved for publication by the Management Board on 12 March 2018.

Composition of the Management Board

As at 31 December 2017, 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.

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

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

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.

2. Shares in related parties

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

(in PLN '000)

Item	Company name	Registered office	Core business	Share of TAURON Polska Energia S.A. in the entity's capital	Share of TAURON Polska Energia S.A. in the governing body
1	TAURON Wydobycie S.A.	Jaworzno	Hard coal mining	100.00%	100.00%
2	TAURON Wytwarzanie S.A.[1]	Jaworzno	Generation, transmission and distribution of electricity and heat	100.00%	100.00%
3	Nowe Jaworzno Grupa TAURON Sp. z o.o.[1]	Jaworzno	Generation, transmission and distribution of electricity and heat and sale of electricity	100.00%	100.00%
4	TAURON Ekoenergia Sp. z o.o.	Jelenia Góra	Generation of electricity	100.00%	100.00%
5	Marselwind Sp. z o.o.	Katowice	Production, transmission and sale of electricity	100.00%	100.00%
6	TAURON Ciepło Sp. z o.o.	Katowice	Production and distribution of heat	100.00%	100.00%
7	TAURON Serwis Sp. z o. o.	Katowice	Services	95.61%	95.61%
8	TAURON Dystrybucja S.A.	Kraków	Distribution of electricity	99.74%	99.75%
9	TAURON Dystrybucja Serwis S.A.	Wrocław	Services	100.00%	100.00%
10	TAURON Dystrybucja Pomiary Sp. z o.o.[2]	Tarnów	Services	99.74%	99.75%
11	TAURON Sprzedaż Sp. z o.o.	Kraków	Sale of electricity	100.00%	100.00%
12	TAURON Sprzedaż GZE Sp. z o.o.	Gliwice	Sale of electricity	100.00%	100.00%
13	TAURON Czech Energy s.r.o.	Ostrawa, Czech Republic	Sale of electricity	100.00%	100.00%
14	TAURON Obsługa Klienta Sp. z o.o.	Wrocław	Services	100.00%	100.00%
15	Kopalnia Wapienia Czatkowice Sp. z o.o.	Krzeszowice	Limestone quarrying and stone quarrying	100.00%	100.00%
16	Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.[3]	Warszawa	Sale of electricity	100.00%	100.00%
17	TAURON Sweden Energy AB (publ)	Sztokholm, Sweden	Services	100.00%	100.00%
18	Biomasa Grupa TAURON Sp. z o.o.	Stalowa Wola	Wholesale of waste and scrap	100.00%	100.00%
19	Wsparcie Grupa TAURON Sp. z o.o.[2, 4]	Tarnów	Services	99.74%	99.75%

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

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

Item	Company name	Registered office	Core business	Share of TAURON Polska Energia S.A. in the entity's capital and governing body
1	Elektrociepłownia Stalowa Wola S.A.[1]	Stalowa Wola	Generation of electricity	50.00%
2	TAMEH HOLDING Sp. z o.o.[2]	Dąbrowa Górnicza	Head office and holding operations	50.00%
3	TAMEH POLSKA Sp. z o.o.[2]	Dąbrowa Górnicza	Generation, transmission, distribution and sale of electricity and heat	50.00%
4	TAMEH Czech s.r.o.[2]	Ostrawa, Czech Republic	Production, trade and services	50.00%

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

3. Statement of compliance

These 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.

4. Going concern

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

5. Functional and presentation currency

Polish zloty is the functional currency of the parent and the presentation currency of these financial statements. These financial statements have been presented in the Polish zloty ("PLN") and all figures are in PLN thousand, unless stated otherwise.

6. Material figures based on professional judgement and estimates

When applying the accounting policy to the issues mentioned below, professional judgement of the management, along with accounting estimates, have been of key importance; they have impacted the figures disclosed in these financial statements and in the explanatory notes. The assumptions underlying the estimates have been based on the Management Board's best knowledge of current and future actions and events in individual areas. In the period covered by these 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 mentioned further in these financial statements.

The items of the financial statements which are exposed to the risk of material adjustment of the carrying amounts of assets and liabilities have been presented below. Detailed information regarding assumptions has been presented in notes to these financial statements, in line with the table below.

(in PLN '000)

Item	Significant accounting policies	Note	Estimates and assumptions
Shares	Note 9.4 Note 9.8	Note 21	As at the end of each reporting period, the Company verifies whether there is any objective indication that investemt in shares may be impaired. If the objective indication appears, the Company is obliged to perform impairment tests and to recognize the impairment or the reversal of the impairment recognized earlier.
Loan to a subsidiary	Note 9.7 Note 9.8	Note 25	As at the end of each reporting period, the Company verifies whether there is any objective indication that loans granted to subsidiary may be impaired. If the objective indication appears, the Company is obliged to perform impairment tests and to recognize the impairment or the reversal of the impairment recognized earlier. As at the end of each reporting period, the Company classifes the loan granted to subsidiiary as non-current or current assets In the event of planned maintenance of involvement in entity for longer than one year, the Comapny classifies the loan as non-current assets.
Provisions	Note 9.18 Note 9.19	Note 34 Note 35	The value of provisions is determined based on assumptions made by the Company as well as a methodology and calculation method that is appropriate for a specific provision. To this end, the Company verifies the probability of an outflow of resources embodying economic benefits and estimates reliably the amount necessary to fulfil the obligation. The Company recognized provisions if the probability of an outflow of resources embodying economic benefits is higher than 50%.
Deferred tax assets	Note 9.22	Note 16	As at the end of each reporting period, the Company asses the realisation of deferred tax assets and verifies deferred tax assets which were not recognized.
Derivative instruments	Note 9.9	Note 23	The Company measured derivative financial instruments at fair value at the end of each reporting period. Derivative instruments acquired and held for internal purposes are not measured at the end of the reporting period.
Intra-group bonds	Note 9.6	Note 22	As at the end of each reporting period, the Company classifes the intra-group bonds as non-current or current assets. In the event of intended rollover, bonds maturing within one year as of the end of reporting period are classified as long-term instruments.

Additionally, the Company's material estimates include contingent liabilities recognized, in particular, in relation to legal proceedings to which it is a party. Contingent liabilities have been discussed in more detail in Note 44 to these financial statements.

7. New standards and interpretations which have been published but are not yet effective

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

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

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

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

Key changes introduced by IFRS 9 *Financial Instruments*:

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

Instead of four classes of financial assets as determined under IAS 39 *Financial Instruments: Measurement and Recognition*, IFRS 9 *Financial Instruments* has introduced three:

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

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

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

(in PLN '000)

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

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

Impact on the financial statements as at 1 January 2018

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

Categories and classes of financial instruments in line with IAS 39	IAS 39		IFRS 9			Estimated effect of change
	At amortised/ at historical cost	At fair value	At amortised cost	Fair value through: Profit/loss	Fair value through: Other comprehensive income	Increase/ (decrease)
1 Financial assets at fair value through profit or loss, held for trading	**–**	**106 292**	**–**	**106 292**	**–**	**–**
Derivative instruments	–	4 934	–	4 934	–	–
Investment fund units	–	101 358	–	101 358	–	–
2 Financial assets available for sale	**39 244**	**–**	**–**	**39 244**	**–**	**–**
Long-term shares*	39 244	–	–	39 244	–	–
3 Loans and receivables	**8 228 015**	**–**	**7 550 923**	**177 274**	**–**	**(499 818)**
Receivables from buyers	719 133	–	716 526	–	–	(2 607)
Gross value	720 057	–	720 057	–	–	–
Impairment loss	(924)	–	(3 531)	–	–	(2 607)
Bonds	6 572 696	–	6 176 103	–	–	(396 593)
Gross value	6 572 696	–	6 572 696	–	–	–
Impairment loss	–	–	(396 593)	–	–	(396 593)
Loans granted under cash pool agreement	190 526	–	190 526	–	–	–
Other loans granted	712 654	–	461 077	150 959	–	(100 618)
Gross value	712 654	–	471 887	150 959	–	(89 808)
Impairment loss	–	–	(10 810)	–	–	(10 810)
Other financial receivables	33 006	–	6 691	26 315	–	–
4 Hedging derivative instruments	**–**	**28 482**	**–**	**28 482**	**–**	**–**
5 Cash and cash equivalents	**–**	**721 577**	**–**	**721 577**	**–**	**–**
Total estimated effect of the application of IFRS 9 on financial assets						**(499 818)**
1 Financial liabilities measured at amortised cost	**470 239**	**–**	**437 128**	**–**	**–**	**33 111**
Loan granted by European Investment Bank	470 239	–	437 128	–	–	33 111
Total estimated effect of the application of IFRS 9 on financial liabilites						**33 111**
Estimated effect on retained earnings						**(466 707)**
Deferred tax						**88 674**
Estimated effect on retained earnings after deferred tax						**(378 033)**

** Measurement at historical cost.*

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

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

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

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

As IFRS 9 *Financial Instruments* requires that equity interests in other entities be measured at fair value, also with respect to those shares which – due to limited availability of information – have thus far been measured at cost less impairment losses, considering that the key factors affecting the value of acquired shares did not change as at the end of the reporting period versus initial recognition, the Company relied on the historical cost as a reasonable approximation of fair value. In accordance with IFRS 9 *Financial Instruments* the above equity instruments will be measured at fair value through profit or loss.

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

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

– receivables from buyers and

– subsidiaries' bonds purchased and loans granted.

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

Based on analyses carried out the Company expects that the total value of loss allowance for expected credit losses on receivables from buyers following the application of IFRS 9 *Financial Instruments* will increase compared to the value estimated in line with the earlier principles, which will consequently decrease the retained earnings as at 1 January 2018, by PLN 2 607 thousand.

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

It is expected that due to the application of IFRS 9 *Financial Instruments* the total value of loss allowance for expected credit losses on originated loans and bonds purchased, measured at amortized cost, will decrease retained earnings of Company as at 1 January 2018 by PLN 407 403 thousand.

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

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

- **Hedge Accounting**

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

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

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

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

IFRS 15 *Revenue from Contracts with Customers*
Effective date in the EU: annual periods beginning on or after 1 January 2018.

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

Key principles introduced by IFRS 15 *Revenue from Contracts with Customers* include:

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

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

Impact on the financial statements as at 1 January 2018

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

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

In accordance with IFRS 15 *Revenue from Contracts with Customers*, if the consideration specified in the contract includes a variable amount, the entity estimates the amount of the consideration to which it will be entitled in exchange for the transfer of promised goods or services to the customer and includes part or all of the variable consideration only in the transaction price to the extent that there is a high probability that there will be no reversal of a significant portion of the amount of previously recognized cumulative revenues when the uncertainty about the amount of variable consideration is subsequently resolved. On the basis of the analysis, the Company did not identify contracts containing variable amounts of consideration.

Under contracts concluded with customers the Company does not offer any warranties for the products sold.

In accordance with IFRS 15 *Revenue from Contracts with Customers*, the transaction price is allocated to the performance obligations by reference to their relative standalone selling prices. According to the Company, the existing contracts with customers do not meet the requirements to be aggregated and treated as a single contract. Therefore, the implementation of IFRS 15 *Revenue from Contracts with Customers* will not affect the allocation of the transaction price to each performance obligation.

In terms of the services provided, the Company believes that the customer simultaneously receives and consumes the benefits from the service at the same time as the Company performs the service. Consequently, the Company transfers control and thus fulfills the obligation to perform the service over time. Therefore, in accordance with IFRS 15 *Revenue from Contracts with Customers*, the Company will continue to recognize revenues from the sale of services over time.

Pursuant to IFRS 15 *Revenue from Contracts with Customers*, the Company considers whether their contracts include a significant financing arrangement. As a practical expedient, the Company will not adjust the promised amount of consideration for the effects of a significant financing arrangement as it expects, at contract inception, that the interval between the transfer of the promised goods or services and payment by the customer is expected to be less than one year. Therefore, the Company shall not separate a significant financing arrangement for short-term advance payments.

The Company has not identified any contracts with customers for which the interval between the transfer of the promised goods or services and payment exceeds one year and therefore it is believed the contracts do not include a significant financing arrangement.

IFRS 15 *Revenue from Contracts with Customers* introduces new requirements regarding disclosures. According to the Company the effects of these disclosures will be insignificant.

The recognition and measurement requirements under IFRS 15 *Revenue from Contracts with Customers* apply also to the recognition and measurement of gain/loss on sale of non-financial assets (such as property, plant and equipment or intangible assets) if the sale does not take place in the usual course of business activity. Therefore, in the opinion of the Company the impact of implementation IFRS 15 *Revenue from Contracts with Customers* should not be material.

Following an analysis, of the contracts with customers the Company has concluded that implementation of IFRS 15 *Revenue from Contracts with Customers* does not affect the equity as at 1 January 2018.

IFRS 16 *Leases*

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

Under IFRS 16 *Leases*, the lessee recognizes the right-of-use asset and the lease liability. The right-of-use asset is treated similarly to other non-financial assets and depreciated accordingly. 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 the incremental borrowing rate. Lessors continue to classify leases as operating or finance leases, with the approach to lessor accounting substantially unchanged from IAS 17 *Leases*. A lease is classified by a lessor as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset. Otherwise, a lease is classified as an operating lease. A lessor recognizes finance income over the lease term of a finance lease, based on a pattern reflecting a constant periodic rate of return on the net investment. A lessor recognizes operating lease payments as income on a straight-line basis or another systematic basis if that basis is more representative of the pattern in which benefit from the use of the underlying asset is diminished.

Impact on the financial statements

A preliminary analysis of the impact of IFRS 16 *Leases* on the accounting policies has shown a change material for the Company, i.e. the need to recognize lease assets and liabilities for leases currently classified as operating leases in the financial statements. The Company analyses all its lease agreements to identify leases which require recognition of assets and liabilities in the financial statements. As at the date of approval of these financial statements for publication the Company had not carried out any analyses which would enable it to determine the impact of the planned changes on the financial statements. The analysis will be conducted at a later time.

Clarifications to IFRS 15 *Revenue from Contracts with Customers*

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

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

(in PLN '000)

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

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

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

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

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

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

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

8. Changes in the accounting policies

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

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

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

9. Significant accounting policies

9.1. Property, plant and equipment — Note 18

Items of property, plant and equipment are measured at acquisition price or manufacturing cost less depreciation and impairment losses. The initial value of fixed assets includes their cost increased by all expenses directly related to the purchase and bringing the asset to a usable condition. Depreciation is calculated by reference to the cost of the asset less its residual value. The depreciation method applied reflects the manner of the Company's consuming economic benefits generated by the asset.

Average residual useful lives by fixed asset group:

Tangible fixed assets by type	Average remaining depreciation period in years
Plant and machinery	–
Motor vehicles	less than 1 year
Other tangible fixed assets	2 years

The depreciation method and rate, as well as the residual value of fixed assets are reviewed at least at the end of each financial year with possible changes recognized as changes in estimates. Depreciation is recognized in profit or loss in an appropriate cost category corresponding to the function of the non-current asset.

9.2. Investment property — Note 19

The Company holds an investment property generating revenue from rental fees. The property is rented to a subsidiary. At initial recognition investment property is measured at cost including transaction costs. After initial recognition all investment properties held are measured in line with IAS 16 *Property, Plant and Equipment*, i.e. at cost. This means that the Company gradually depreciates the real property throughout its useful life.

9.3. Intangible assets — Note 20

Intangible assets include mostly software and licences as well as copyrights and related rights.

Intangible assets are measured at cost at initial recognition. After initial recognition intangible assets are measured at cost less accumulated amortization and impairment losses.

The Company assesses whether the useful life of an intangible asset is finite or indefinite and, if finite, estimates its duration or another measure providing the basis for determination of the useful life.

Intangible assets with a finite useful life are amortized over the period of their estimated use and tested for impairment each time when impairment indications occur. The period and method of amortizing intangible assets with a finite useful life are verified at least at the end of each reporting period; changes in the expected useful life or a pattern of consuming economic benefits generated by a given asset are treated as changes in estimates. Amortization of intangible assets with a finite useful life is recognized in profit or loss in an appropriate cost category corresponding to the function of the intangible asset.

The Company does not have any intangible assets with an indefinite useful life.

Average residual useful lives by intangible asset group:

Intangible assets by type	Average remaining amortization period in years
Software	2 years
Other intangible assets	6 years

9.4. Shares in subsidiaries — Note 21

Shares in subsidiaries are measured at cost less impairment losses. Impairment losses are recognized in line with IAS 36 *Impairment of Assets*, where the carrying amount is compared to the higher of the fair value less costs to sell and the value in use.

9.5. Shares in jointly-controlled entities — Note 21

Shares in co-subsidiaries are recognized at cost less impairment losses, if any.

9.6. Bonds — Note 22

Under the central funding model, the Company acquires bonds issued by the TAURON Group companies. The bonds are classified to loans and receivables, i.e. financial assets with fixed or determinable payments. Bonds with maturity of up to 12 months as of the end of the reporting period are classified to current assets and those with maturity of over 12 months as of the end of the reporting period – to non-current assets, however, it is not only the maturity, but also the Company's plans with respect to the rollover that matter.

Intra-group bonds maturing within one year, intended for rollover, are classified as long-term instruments. Such classification reflects the nature of funding under the intra-group bond issue scheme, which enables cash management in the medium and long term.

9.7. Loans granted — Note 25

Loans granted by the Company are mostly loans to subsidiaries and include cash pooling loans and loans to joint ventures. Loans are classified to loans and receivables and measured at amortized cost Loans maturing within 12 months as of the end of the reporting period are classified to current assets and loans maturing in more than 12 months as of the end of the reporting period – to non-current assets considering the expectations as regards the loan repayment as at the end of the reporting period.

9.8. Impairment of financial assets — Note 11

As at the end of each reporting period, the Company verifies whether there is any objective indication that a financial asset or a group of financial assets may be impaired.

Shares in subsidiaries and intra-group loans and bonds

The main item in the Company's financial assets are shares in subsidiaries and intra-group loans and bonds. The assets are tested for impairment, if there is any objective indication that the assets may be impaired. The amount of the impairment loss is the difference between the carrying amount of a financial asset or group of financial assets and the recoverable amount, which is the fair value less costs of disposal or the value in use, whichever is higher. The value in use is calculated as the present value of estimated future cash flows from the operations of subsidiaries and the estimated residual value discounted using the weighted average cost of capital.

Other financial assets

Other financial assets measured at amortized cost are tested for impairment, if there is any objective indication that the assets may be impaired. The amount of the impairment loss is the difference between the carrying amount of a financial asset and the present value of estimated future cash flows discounted using the initial effective interest rate (i.e. the one determined at initial recognition).

If the impairment loss decreases in the subsequent period and the decrease can be objectively related to an event taking place after the loss has been recognized, the prior impairment loss is reversed. The subsequent reversal of an impairment loss is recognized in profit or loss to the extent that the carrying amount of the asset does not exceed its amortized cost as at the date of reversal.

9.9. Derivative financial instruments — Note 23

Derivative financial instruments falling within the scope of IAS 39 *Financial Instruments: Measurement and Recognition* are classified as financial assets/financial liabilities measured at fair value through profit or loss, except derivatives which are designated as hedging instruments and subject to hedge accounting. Derivative instruments acquired and held for internal purposes as excluded from the scope of IAS 39 *Financial Instruments: Measurement and Recognition* 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 9.10). Other derivative instruments held by the Company as at the end of the reporting period are not subject to hedge accounting.

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

Derivative instrument	Methodology of determining fair value hierarchy
IRS	The difference between discounted floating-rate interest cash flows and those based on fixed interest rates. Reuters interest rate curve is the input data.
CCIRS	The difference between discounted interest cash flows relating to payments and receipts, in two different currencies, expressed in the valuation currency. Interest rate curves, basis spreads and NBP fixing for the relevant currencies from Reuters are the input data.
Forward currency contracts	The difference between discounted future cash flows: the forward price at the valuation date and the transaction price, multiplied by the nominal value of the contract in a foreign currency. NBP fixing and the implied interest rate curve from FX swap transactions for the relevant currency from Reuters are the input data.
Commodity forwards, futures	The fair value of forwards for the purchase and sale of emission allowances, electricity and other commodities is based on prices quoted on an active market or based on cash flows being the difference between the price reference index (forward curve) and the contract price.

9.10. Hedge accounting

In order to hedge the interest rate risk, the Company uses IRS (Interest Rate Swap) contracts. 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 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.

9.11. Other non-financial assets — Note 29

Other non-financial assets include mostly prepayments and advance payments for deliveries.

Prepayments are measured at the amount of reliably estimated expenses incurred by the entity, related to future reporting periods and resulting in an inflow of economic benefits to the entity in the future. Prepaid expenses may be settled based on the elapsed time or amounts paid.

9.12. Inventories — Note 26

The Company's inventories include acquired emission allowances and certificates of energy generated using renewable sources and in CHP units, intended for trading purposes.

At initial recognition inventories are measured at cost. At the end of the reporting period inventories are measured at cost or net realizable value, whichever is lower. If the cost is higher than the net realizable value, the Company recognizes an appropriate impairment loss.

Greenhouse gas emission allowances purchased for resale and generation of profit in the short term due to volatility of market prices are recognized within inventories. They are measured at fair value at initial recognition and at the end of each reporting period.

Releases of consumables and goods are measured using the weighted average method.

9.13. Receivables from buyers — Note 27

Receivables from buyers are recognized at originally invoiced amounts, except situations where the effect of the time value of money is material, less allowances/write-downs.

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.

9.14. Other financial assets — Note 24

Other financial assets include investment fund units, Tax Capital Group receivables, deposits, performance bonds, collateral transferred and receivables arising from sales of property, plant and equipment and intangible assets.

9.15. Cash and cash equivalents — Note 30

Cash and short-term deposits recognized in the statement of financial position include in particular cash at bank and in hand and short-term deposits with original maturity of up to three months.

The balance of cash and cash equivalents recognized in the statement of cash flows consists of the aforesaid cash and cash equivalent items. If the entity uses overdraft facilities as a cash management solution, in line with IAS 7 *Statement of Cash Flows* the balance of cash is presented in the statement of cash flows less the outstanding balance of such facilities. Additionally, cash is adjusted by the balances of loans granted and taken out in a cash pool transaction as their main objective is to manage liquidity on a day-to-day basis.

9.16. Issued capital — Note 31.1

In the financial statements, issued capital is presented at the amount specified in the articles of association and entered in the Company's court register.

9.17. Debt — Note 33

Loans, borrowings, bonds issued and finance lease liabilities are presented as debt in the statement of financial position of the Company.

At initial recognition, all loans, borrowings and bonds issued are measured at fair value less the cost incurred to obtain a loan or borrowing. After initial recognition interest-bearing loans and debt securities are measured at amortized cost using the effective interest method.

Amortized cost includes the cost incurred to obtain a loan, borrowing or debt securities and discounts or premiums relating to the liability.

Finance leases transferring substantially all the risks and rewards of ownership of a lease object to the Company 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.

9.18. Provisions for employee benefits — Note 34

In accordance with the Compensation Policy the employees of the Company 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;
- benefits from the Company's Social Benefit Fund.

The present value of such liabilities is calculated by an independent actuary at the end of each reporting period. 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 post-employment benefits are fully charged to other comprehensive income.

9.19. Other provisions — Note 35

Provisions are recognized if the Company has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and the amount of the obligation can be reliably estimated.

As at the end of the reporting period, a provision was recognized against the risk of an adverse decision arising from the pending inspection procedure.

In the reporting period, the Company recognized also a provision for the obligation to surrender energy certificates.

9.20. Liabilities to suppliers and other financial liabilities — Note 37, 38

Current liabilities to suppliers are recognized at amount due. Other financial liabilities include Tax Capital Group settlements, payroll liabilities, deposits, performance bonds, collateral received and liabilities arising from purchases of property, plant and equipment and intangible assets, measured at amount due since the discount effects are immaterial.

9.21. Receivables / Liabilities arising from taxes and charges — Note 28, 39

Settlements arising from 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.

9.22. 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 determined by the Company in line with provisions of the CIT Act and including the settlement of the Tax Capital Group the Company belongs to, as well as any previous year tax adjustments.

Deferred tax

The Company 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 carrying amount of the deferred tax asset is reviewed at the end of each reporting period. The Company reduces the carrying amount of the deferred tax asset to the extent the generation of taxable income sufficient to use the deferred tax asset in part or in whole is not probable. Unrecognized deferred tax asset is reviewed at the end of each reporting period and recognized to the extent its use is probable following generation of taxable income in the future. Deferred tax asset related to deductible differences concerning investments in subsidiaries is recognized insofar as their reversal is probable in the foreseeable future and where taxable income will be available to enable realization of deductible differences.

The deferred tax asset and liability are measured with the application of tax rates expected to be applicable in the period of realization of the asset or derecognition of the liability, with the consideration of tax rates (and tax regulations) that had been enacted or substantively enacted at the end of the reporting period.

Income tax related to items which are not recognized in profit or loss, i.e. items recognized in other comprehensive income or directly in equity, is recognized in other comprehensive income or in equity, respectively.

The Company offsets its deferred tax asset and deferred tax liability only if it has an enforceable legal title to offset its current tax receivables with liabilities and the deferred tax asset and liability concern the same tax authority.

9.23. Sales revenue Note 12

Revenue is recognized in the amount it is probable that future economic benefits relating to a transaction will flow to the Company and the amount of the revenue can be measured reliably. 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 recognition criteria set out below apply as well.

Revenue from sales of goods and materials is recognized if significant ownership-related risks and benefits from goods and materials have been transferred to the buyer and if the revenue amount can be reliably measured and incurred costs can be reliably estimated.

Revenue also includes amounts due for the sale of goods, materials and services related to the core business and determined based on the net price, adjusted by granted rebates and discounts and excise duty.

Revenue from sales of goods includes gains on the inventory of greenhouse gas emission allowances purchased for resale and generation of profit in the short term due to volatility of market prices, including the aggregate gain 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 *Financial Instruments: Measurement and Recognition*, related to purchases and sales of greenhouse gas emission allowances.

Gains on change in measurement and on exercising derivative commodity instruments falling within the scope of IAS 39 *Financial Instruments: Measurement and Recognition* and related to purchases and sales of other commodities are recognized in revenue from sales of goods.

9.24. Operating expenses Note 13

The Company presents expenses by function.

They include:

- cost of goods, 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;
- total sales, general and administrative expenses incurred in the reporting period (disclosed separately in the statement of comprehensive income).

The cost of sales includes losses on the inventory of greenhouse gas emission allowances purchased for resale and generation of profit in the short term due to volatility of market prices, including the aggregate 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 *Financial Instruments: Measurement and Recognition*, related to purchases and sales of greenhouse gas emission allowances.

Losses on change in measurement and on exercising derivative commodity instruments falling within the scope of IAS 39 *Financial Instruments: Measurement and Recognition* and related to purchases and sales of other commodities are recognized in cost of sales.

Costs that can be assigned directly to revenue generated by the Company impact 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 Company impact the profit or loss in the portion pertaining to the given reporting period, and match the revenue or other economic benefits.

(in PLN '000)

9.25. Finance income and costs Note 15

Finance income and costs include in particular items relating to:

- revenue from profit sharing in other entities, including dividends;
- interest;
- disposal/liquidation of financial assets;
- revaluation of financial instruments, except derivative commodity instruments falling within the scope of IAS 39 *Financial Instruments: Measurement and Recognition* in the case of which gains/losses on change in measurement and on exercising are presented within operating activities where gains/losses on the related trading in goods are also recognized;
- interest expense related to measurement of employee benefits, in line with IAS 19 *Employee Benefits*;
- changes in the balance of a provision resulting from the nearing deadline to incur the expense (discount unwinding effect);
- foreign exchange differences resulting from transactions performed during the reporting period and balance sheet measurement of assets and liabilities at the end of the reporting period, except for differences recognized in the initial value of a fixed asset;
- other items related to financing activities.

9.26. Translation of items denominated in foreign currencies

Foreign currency transactions are translated into PLN at initial recognition at the exchange rate applicable as at the transaction date. As at the end of the reporting period:

- monetary items denominated in foreign currencies are translated at the closing rate (the average exchange rate published by the National Bank of Poland as at the date);
- non-monetary items measured at historical cost and denominated in foreign currencies are translated at the exchange rate as at the original transaction date; and
- non-monetary items measured at fair value and denominated in foreign currencies are translated at the exchange rate as at the fair value measurement date.

Exchange differences from translation are recognized within finance income (costs), or, in the cases specified in the accounting principles (policy), capitalized in the value of assets.

Exchange rates applied for the purpose of balance sheet measurement:

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

9.27. Business combinations

Business combinations of entities under common control are accounted for using the pooling of interest method.

The method is based on the assumption that the combining entities are controlled by the same shareholder before and after the business combination, and therefore the continuity of common control is presented in the financial statements, while the changes in the net value of assets to reflect their fair value (or recognition of new assets) or goodwill measurement 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.

The following items are eliminated when a business combination is accounted for using the pooling of interest method:

- issued capital of the acquiree;
- mutual receivables and liabilities or other similar settlements of the combined entities;
- revenue and costs of business transactions executed in the period covered by the financial statements, which were effected before the business combination.
- gains or losses on business transactions concluded between the combined entities prior to the business combination, included in the amounts of the pooled assets and liabilities.

When accounting for business combinations of subsidiaries from the TAURON Group, the Company uses the consolidated financial statements as the source of the value of assets and liabilities in a subsidiary acquired. The value of the acquiree's shares in the subsidiaries was measured by reference to the entities' net asset value from the consolidated financial statements and the subsidiary's goodwill.

The difference between the net book value of assets recognized as a result of a business combination in the statement of financial position of the acquirer and the value of investments recognized thus far in the accounting records of the acquirer is recognized in the equity of the acquirer.

9.28. Statement of cash flows

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

9.29. Earnings (loss) per share

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

OPERATING SEGMENTS

10. Information on operating segments

10.1. Operating segments

The Company carries out its business in two operating segments, that is "Sales" and "Holding activity".

"Holding activity" segment assets include:

- shares in subsidiaries and jointly-controlled entities;
- bonds acquired from subsidiaries;
- cash pool loan receivables, including a cash pool deposit;
- receivables arising from other loans granted to related parties;
- assets arising from valuation of hedging instruments relating to issued bonds.

"Holding activity" segment liabilities include:

- bonds issued by the Company, including liabilities arising from valuation of hedging instruments relating to such bonds;
- loans obtained from the European Investment Bank to carry out investment projects in subsidiaries;
- liabilities due to loans from related parties, including under the cash pool agreement.

"Holding activity" segment includes intra-group receivables and liabilities arising from income tax settlements of the Tax Capital Group companies.

Finance income and finance costs include dividend income as well as net interest income and expense earned/incurred by the Company in relation to the central financing model adopted by the Group.

General and administrative expenses are presented under unallocated expenses, as they are incurred for the Group as a whole and are not directly attributable to a specific operating segment.

EBIT is the profit/loss on continuing operations before tax, finance income and finance costs, i.e. operating profit (loss).

EBITDA is the profit/loss on continuing operations before tax, finance income and finance costs, increased by amortization/depreciation and impairment of non-financial assets.

(in PLN '000)

For the year ended 31 December 2017

	Sales	Holding activity	Unallocated items	Total
Revenue				
Sales outside the Group	995 252	–	–	**995 252**
Sales within the Group	6 765 388	31 385	–	**6 796 773**
Segment revenue	**7 760 640**	**31 385**	**–**	**7 792 025**
Profit/(loss) of the segment	**320 154**	**31 385**	**–**	**351 539**
Unallocated expenses	–	–	(88 751)	**(88 751)**
EBIT	**320 154**	**31 385**	**(88 751)**	**262 788**
Net finance income/(costs)	–	812 855	(156 078)	**656 777**
Profit/(loss) before income tax	**320 154**	**844 240**	**(244 829)**	**919 565**
Income tax expense	–	–	(65 214)	**(65 214)**
Net profit/(loss) for the year	**320 154**	**844 240**	**(310 043)**	**854 351**
Assets and liabilities				
Segment assets	1 748 324	28 423 410	–	**30 171 734**
Unallocated assets	–	–	101 358	**101 358**
Total assets	**1 748 324**	**28 423 410**	**101 358**	**30 273 092**
Segment liabilities	543 154	12 115 606	–	**12 658 760**
Unallocated liabilities	–	–	236 426	**236 426**
Total liabilities	**543 154**	**12 115 606**	**236 426**	**12 895 186**
EBIT	**320 154**	**31 385**	**(88 751)**	**262 788**
Depreciation/amortization	**(5 532)**	**–**	**–**	**(5 532)**
Impairment	**100**	**–**	**–**	**100**
EBITDA	**325 586**	**31 385**	**(88 751)**	**268 220**
Other segment information				
Capital expenditure*	160	–	–	**160**

** Capital expenditure includes expenditures for property, plant and equipment and non-current intangible assets, except for energy certificates acquired by the Company.*

For the year ended 31 December 2016

	Sales	Holding activity	Unallocated items	Total
Revenue				
Sales outside the Group	1 669 734	–	–	**1 669 734**
Sales within the Group	6 323 024	2 570	–	**6 325 594**
Segment revenue	**7 992 758**	**2 570**	**–**	**7 995 328**
Profit/(loss) of the segment	**76 695**	**2 570**	**–**	**79 265**
Unallocated expenses	–	–	(113 868)	**(113 868)**
EBIT	**76 695**	**2 570**	**(113 868)**	**(34 603)**
Net finance income (costs)	–	(101 050)	(13 481)	**(114 531)**
Profit/(loss) before income tax	**76 695**	**(98 480)**	**(127 349)**	**(149 134)**
Income tax expense	–	–	(17 119)	**(17 119)**
Net profit/(loss) for the year	**76 695**	**(98 480)**	**(144 468)**	**(166 253)**
Assets and liabilities				
Segment assets	1 450 322	26 114 360	–	**27 564 682**
Unallocated assets	–	–	107 694	**107 694**
Total assets	**1 450 322**	**26 114 360**	**107 694**	**27 672 376**
Segment liabilities	785 879	10 221 533	–	**11 007 412**
Unallocated liabilities	–	–	134 696	**134 696**
Total liabilities	**785 879**	**10 221 533**	**134 696**	**11 142 108**
EBIT	**76 695**	**2 570**	**(113 868)**	**(34 603)**
Depreciation/amortization	**(7 722)**	**–**	**–**	**(7 722)**
Impairment	**197**	**–**	**–**	**197**
EBITDA	**84 220**	**2 570**	**(113 868)**	**(27 078)**
Other segment information				
Capital expenditure*	837	–	–	**837**

** Capital expenditure includes expenditures for property, plant and equipment and non-current intangible assets, except for energy certificates acquired by the Company.*

In the financial year ended 31 December 2017, revenue from sales to two major clients from the Capital Group accounted for 67% and 10% of the Company's total revenue in the "Sales" segment and amounted to PLN 5 208 284 thousand and PLN 799 943 thousand, respectively.

In the financial year ended 31 December 2016, revenue from sales to two major clients from the TAURON Capital Group accounted for 62% and 10% of the Company's total revenue in the "Sales" segment and amounted to PLN 4 934 454 thousand and PLN 810 728 thousand, respectively.

10.2. Geographic areas of operations

The majority of the Company's business operations are carried out in Poland. In the years ended 31 December 2017 and 31 December 2016, export sales amounted to PLN 147 938 thousand and PLN 164 540 thousand, respectively.

IMPAIRMENT OF FINANCIAL ASSETS

11. Impairment of financial assets

Considering the circumstances underlying the Company's long-term market cap being below its carrying amount and changes in the global commodity prices as well as changes in the local power coal market following the consolidation in the mining sector; amendments to the Act on Renewable Energy Sources and the publication of related obligations for the years 2018–2019 which affected the prices of renewable energy certificates; the adoption of the Act on capacity market and the analysis of functional solutions described in the draft regulation of the capacity market; continuing unfavourable market conditions as far as the profitability of conventional power industry is concerned; as well as the increase in the risk free rate, shares, borrowings and intra-group bonds were tested for impairment as at 31 December 2017 and 30 June 2017. Shares and intra-group loans and bonds accounted for about 94% of the balance sheet total as at the end of the reporting period.

The recoverable amount is the value in use. The calculation method has been presented below.

Relevant tests were conducted based on the present value of projected cash flows from operations of the key entities, by reference to detailed projections by 2027 and the estimated residual value. The projections used for the power generating and mining units cover the entire 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.

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

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

The key business assumptions affecting the estimated value in use of the tested entities are:

- There was adopted price path for power coal, other coal sizes and gaseous fuels. It has been assumed that in the years 2018–2020 the prices of power coal will remain at a similar level to that obtained in current contracts. Next in the years 2021–2040 a real depreciation of 8% is expected with the prices remaining at the 2040 levels (constant);
- There was adopted electricity wholesale price path for the years 2018–2027 with the perspective by 2040, taking into account such factors as the effect of the balance of the market supply and demand for electricity, costs of fuel as well as costs of acquiring greenhouse gas emission allowances. An increase of 3% compares to 2017 year is assumed by 2020, with a 13% growth rate by 2027 (vs. 2020), an increase of 10% between 2027 and 2040 and 2040 year prices thereafter (fixed);
- The operating reserve capacity mechanism is to remain in place until the end of 2020, i.e. until the capacity market will have been implemented;
- Procedural changes of the Polish market model towards the implementation of the power market mechanism were taken into account in accordance with the adopted and notified Capacity Market Act and the draft of capacity market regulations. It was planned to launch the capacity payment from 2021 and maintain it until 2035. The auctions will take the form of a one-time solution with division of capacity contracts according to the level of investment outlays – division of units into new, modernized and existing ones. The average annual capacity market budget in the period of the mechanism's operation was assumed at the level of approximately PLN 4,000 million;.
- There were adopted greenhouse gas emission limits for heat generation in line with the regulation of the Council of Ministers adjusted by level of operations, i.e. generation of heat;
- There was adopted greenhouse gas emission allowance price path for the years 2018–2027 with the perspective by 2040. It has been assumed that the market price will increase by ca. 173% compares to 2017 year by 2027, followed by a rise of ca. 22% between 2027 and 2040, with 2040 year price level thereafter (constant);
- There were taken into consideration green, red and yellow energy production volumes depending on the production capacity, along with the price path for individual energy certificates;

(in PLN '000)

- Limited support periods for green energy have been assumed in accordance with the Act on Renewable Energy Sources, which provides for new support mechanisms for renewable energy. The support period has been limited to 15 years as from the date of the first supply of electricity qualifying for an energy certificate to the distribution network;
- 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 or expanding the production capacity of the existing non-current assets as a result of replacement and development investments.

Fixed assets were also tested for impairment. To this end, the Company applied the relevant assumptions used for impairment testing of shares.

Sensitivity analyses conducted by the Company reveal that the capacity market mechanism (assuming that other market factors remain unchanged), the projected prices of electricity and coal, the prices of greenhouse gas emission allowances and the adopted discount rates are the key factors exerting an effect on the estimated cash flows of the key entities. If the capacity market mechanism was not taken into account in the assumptions made for estimating the value in use of shares and intra-group loans and bonds, the additional net impairment loss that would be recognized in the Company's profit or loss would be ca. PLN 4 970 million, provided that other market conditions remained unchanged.

Fixed assets were also tested for impairment. To this end, the Company applied the relevant assumptions used for impairment testing of shares.

Test results

The impairment tests carried out in line with IAS 36 *Impairment of Assets* as at 31 December 2017 indicated impairment of the carrying amount of shares in subsidiaries of PLN 211 398 thousand and reversal of an impairment loss of subsidiaries shares of PLN 72 603 thousand.

The impairment tests carried out in line with IAS 36 *Impairment of Assets* as at 30 June 2017 indicated impairment of the carrying amount of loans of subsidiaries of PLN 60 578 thousand and a reversal of an impairment loss of subsidiaries shares of PLN 120 057 thousand.

The aforesaid impairment losses were recognized in the Company's finance costs and concerned the following entities:

Company	WACC* assumed in tests as at			Recoverable amount of shares, intra-group loans and bonds as at 31 December 2017	Impairment loss recognized in the year ended 31 December 2017		Impairment loss reversed in the year ended 31 December 2017
	31 December 2017	30 June 2017 *(unaudited)*	31 December 2016		Shares	Loans granted	Shares
TAURON Wytwarzanie S.A.	8.39%	8.20%	7.79%	2 814 014	(63 528)	–	120 057
TAURON Ekoenergia Sp. z o.o.	8.78%	8.42%	7.67%	953 340	–	(60 578)	72 603
TAURON Wydobycie S.A.	10.20%	10.20%	6.95%	1 428 477	(147 870)	–	–

** The level of the weighted average cost of capital (WACC) in nominal terms before tax.*

(in PLN '000)

Following the repayment of a portion of an impaired loan of PLN 1 000 000 thousand by the subsidiary TAURON Ekoenergia Sp. z o.o. in October 2017 and the Company's acquisition of shares in the increased issued capital of TAURON Ekoenergia Sp. z o.o. totalling PLN 1 000 000 thousand, the previous impairment losses on loans of PLN 197 953 thousand and of PLN 60 578 thousand, recognized in the year ended 31 December 2016 and in the year ended 31 December 2017, respectively, have been reclassified and allocated to the value of shares.

Changes in impairment losses on shares in the year ended 31 December 2017 have been presented in the following table.

Company	Impairment as at 1 January 2017	Impairment loss recognized in the year ended 31 December 2017	Impairment loss reversed in the year ended 31 December 2017	Impairment loss reclassification	Impairment as at 31 December 2017	Carrying amount of shares including impairment losses as at 31 December 2017
TAURON Wytwarzanie S.A.	(5 403 825)	(63 528)	120 057	–	(5 347 296)	1 738 405
TAURON Ekoenergia Sp. z o.o.	(939 765)	–	72 603	(258 531)	(1 125 693)	814 072
TAURON Wydobycie S.A.	–	(147 870)	–	–	(147 870)	853 885

The necessity to recognize an impairment loss on shares in TAURON Wytwarzanie S.A. as at 31 December 2017 was mainly driven by the effect of the deferred tax liabilities, while the possibility to reverse the impairment loss as at 30 June 2017 was attributable, in particular, to the following circumstances:

- the functional solutions related to the capacity market discussed in the capacity market bill were analysed which led to a better understanding of the future of the market;
- the life of generating units has been extended and the production volumes increased as a result of greater modernization and replacement expenditure.

The possibility to reverse an impairment loss on shares in TAURON Ekoenergia Sp. z o.o. as at 31 December 2017 was mainly attributable to the effect of the deferred tax asset, while the necessity to recognize an impairment loss as at 30 June 2017 was driven, in particular, by the following circumstances:

- the prices of renewable energy certificates went down, the Act on Renewable Energy Sources was amended and an auction system was introduced;
- the risk-free rate and WACC for wind farms went up.

The necessity to recognize an impairment loss on shares in TAURON Wydobycie S.A. in the year ended 31 December 2017 was mainly driven by the following circumstances:

- the market prices of materials (including steel, copper and rubber) and the market rates for renting mining machines and equipment as well as the cost of labour in the coal mining industry went up;
- the effect of the deferred tax liabilities.

The loans extended to Elektrociepłownia Stalowa Wola S.A. were tested for impairment. The results of the test showed that there is no need for an impairment loss provided that the assumption are compliant with the impairment tests on shares.

(in PLN '000)

EXPLANATORY NOTES TO THE STATEMENT OF COMPREHENSIVE INCOME

12. Sales revenue

	Year ended 31 December 2017	Year ended 31 December 2016
Sale of goods for resale, finished goods and materials without elimination of excise	**7 667 345**	**7 899 621**
Excise	(2 630)	–
Revenue from sales of goods for resale and materials	**7 664 715**	**7 899 621**
Electricity	7 117 988	7 255 819
Gas	190 507	236 215
Property rights arising from energy certificates	14 939	36 137
Emission allowances	336 566	363 500
Other	4 715	7 950
Rendering of services	**127 310**	**95 707**
Trading income	52 711	54 517
Use of shares	31 385	2 570
Other	43 214	38 620
Total	**7 792 025**	**7 995 328**

The Company has been acting as an agent coordinating and supervising purchases, supplies and transportation of fuel. The Company purchases raw materials from third parties and from the TAURON Group companies, which were subsequently sold to related parties. It recognizes revenue from agency services (supply management).

In the year ended 31 December 2017, the value of raw materials purchased and subsequently resold in the aforementioned transactions was PLN 753 663 thousand. The Company recognized revenue from agency services of PLN 32 526 thousand.

Greenhouse gas emission allowances include:

- sales to the Group companies for purposes of allowance surrendering in fulfilment of the obligations related to greenhouse gas emissions – in the year ended 31 December 2017 sales to subsidiaries totalled PLN 336 290 thousand (versus PLN 363 007 thousand in the comparable period); and
- the total profit generated from trading in emission allowances and profit generated in a short term due to fluctuations in the market prices (trading portfolio), which has been described in more detail in note 9.23 to these financial statements, of PLN 276 thousand (in the year ended 31 December 2016 it was PLN 493 thousand).

13. Expenses by type

	Year ended 31 December 2017	Year ended 31 December 2016
Depreciation of property, plant and equipment and amortization of intangible assets	(5 532)	(7 722)
Materials and energy	(1 311)	(1 211)
Consultancy services	(6 598)	(7 994)
IT services	(13 160)	(12 422)
Rental services	(10 366)	(6 360)
Stock market services	(9 621)	(4 468)
Other external services	(9 532)	(7 638)
Taxes and charges	(4 375)	(3 238)
Employee benefits expense	(87 068)	(78 993)
Impairment loss on inventories	100	–
Allowance for receivables from clients	34	1 543
Advertising expenses	(22 207)	(29 198)
Other	(1 983)	(2 107)
Total costs by type	**(171 619)**	**(159 808)**
Selling and distribution expenses	23 309	19 326
Administrative expenses	88 751	81 368
Cost of goods for resale and materials sold	(7 355 148)	(7 778 453)
Cost of sales	**(7 414 707)**	**(7 837 567)**

(in PLN '000)

In the year ended 31 December 2017 the decrease cost of goods for resale and materials sold, includes the result of reversal of the provisions for onerous contracts with Elektrociepłownia Stalowa Wola S.A., totaling PLN 201 174 thousand, which has been discussed in more detail in Note 35 to these financial statements.

14. Employee benefits expenses

	Year ended 31 December 2017	Year ended 31 December 2016
Wages and salaries	(70 026)	(63 237)
Social security costs	(9 662)	(8 657)
Jubilee bonuses	(247)	526
Appropriations to the Social Fund	(520)	(404)
Costs of employee retirement plans	(2 475)	(3 075)
Post-employment benefits expenses – actuarial provisions	(606)	(787)
Other employee benefits expenses	(3 532)	(3 359)
Total	**(87 068)**	**(78 993)**
Items included in cost of sales	(22 741)	(23 131)
Items included in selling and distribution expenses	(7 640)	(8 910)
Items included in administrative expenses	(56 687)	(46 952)

15. Finance income and costs

	Year ended 31 December 2017	Year ended 31 December 2016
Income and costs from financial instruments	**659 477**	**(92 654)**
Dividend income	560 832	1 485 152
Interest income on bonds and loans	456 426	503 897
Other interest income	19 539	6 829
Interest expense	(334 638)	(356 947)
Commissions due to external financing	(19 068)	(18 814)
Gain/(loss) on derivative instruments	(18 042)	14 127
Exchange gains/(losses)	127 476	(29 669)
Surplus of impairment losses (recognised)/reversed on shares	(134 372)	(1 610 396)
Loss on disposal/liquidation of investment	–	(87 260)
Other	1 324	427
Other finance income and costs	**(2 700)**	**(21 877)**
Interest on discount (other provisions)	(2 330)	(11 502)
Other	(370)	(10 375)
Total, incl. recognized in the statement of comprehensive income:	**656 777**	**(114 531)**
Dividend income	560 832	1 485 152
Interest income on bonds and loans	456 426	503 897
Interest expense on debt	(334 638)	(356 947)
Revaluation of shares and loans	(134 372)	(1 610 396)
Other finance income and costs	108 529	(136 237)

In the year ended 31 December 2017 the Company recognized an impairment loss on shares in and loans of subsidiaries totalling PLN 327 032 thousand and released an impairment loss on shares of PLN 192 660 thousand. Impairment losses on shares have been presented in more detail in Note 21 hereto.

In the year ended 31 December 2017, exchange gains exceeded exchange losses by PLN 127 476 thousand. Exchange gains were mainly related to the Company's debt in the euro, i.e. loans obtained from a subsidiary, subordinated bonds issued in December 2016 and eurobonds issued in July 2017. The related surplus of exchange gains over exchange losses was PLN 128 270 thousand.

(in PLN '000)

16. Income tax

16.1. Tax expense in the statement of comprehensive income

Key items of the tax expense in the statement of comprehensive income:

	Year ended 31 December 2017	Year ended 31 December 2016
Current income tax	**(66 160)**	**(9 541)**
Current income tax expense	(66 429)	(9 541)
Adjustments of current income tax from prior years	269	–
Deferred tax	**946**	**(7 578)**
Income tax expense in profit or loss	**(65 214)**	**(17 119)**
Income tax expense in other comprehensive income	**1 574**	**(24 401)**

16.2. Reconciliation of the effective tax rate

	Year ended 31 December 2017	Year ended 31 December 2016
Profit/(loss) before tax	**919 565**	**(149 134)**
Tax at Poland's statutory tax rate of 19%	**(174 717)**	**28 335**
Adjustments to income tax from previous years	269	–
Tax resulting from tax non-deductible costs	(66 366)	(413 933)
Impairment loss on shares and loans in subsidiaries	(62 136)	(390 193)
Recognition of non-deductible provisions	(798)	(19 032)
Other	(3 432)	(4 708)
Tax resulting from income not included in taxable base	154 377	366 397
Dividends	106 558	282 179
Reversal of impairment loss on shares in subsidiaries	36 605	84 218
Reversal of non-deductible provisions	10 419	–
Other	795	–
Settlement of the TCG	21 223	2 082
Tax at the effective tax rate of 7.1% (2016: -11.5%)	**(65 214)**	**(17 119)**
Income tax expense in profit/(loss)	(65 214)	(17 119)

(in PLN '000)

16.3. Deferred income tax

Deferred income tax results from the following items:

	As at 31 December 2017	As at 31 December 2016
due interest on bonds and loans	29 275	66 356
difference between tax base and carrying amount of other financial assets	520	4 861
valuation of hedging instruments	5 412	6 962
other	4 812	4 300
Deferred tax liabilities	**40 019**	**82 479**
provision for employee benefits	660	544
other provisions and accruals	2 270	31 122
difference between tax base and carrying amount of fixed and intangible assets	821	1 107
difference between tax base and carrying amount of financial liabilities	4 125	15 887
other	2 300	1 455
Deferred tax assets	**10 176**	**50 115**
Deferred tax assets/(liabilities), net, of which:	**(29 843)**	**(32 364)**
Deferred tax assets/(liabilities), net – recognized in profit or loss	(24 403)	(25 349)
Deferred tax assets/(liabilities), net – recognized in other comprehensive income	(5 440)	(7 015)

Deferred tax asset related to deductible differences related to investments in subsidiaries is recognized insofar as their reversal is probable in the foreseeable future and where taxable income will be available to enable realization of deductible differences. According to the Company, deductible temporary differences related to recognition of impairment losses on shares in subsidiaries of PLN 6 675 915 thousand will not be reversed in the foreseeable future, as the investments are not intended for sale. Consequently, no related deferred tax asset has been recognized.

As taxable profit is forecast for the subsequent years for the Tax Capital Group ("TCG") of which the Company is a member, the deferred tax asset related to all deductible differences, except those described above, has been recognized in these financial statements in the full amount.

16.4. Tax Capital Group

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

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

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

At the same time, due to the Company's settlements, as the Representative Company, with the Tax Capital Group companies, it has reported a liability to these subsidiaries arising from tax overpayment of PLN 34 836 thousand, which has been presented in the statement of financial position as "Other financial liabilities", as well as receivables from the Tax Capital Group companies arising from tax underpayment of PLN 6 133 thousand, which have been presented in the statement of financial position as "Other financial assets".

On 30 October 2017 a relevant decision regarding the registration of the Tax Capital Group for the years 2018–2020 was given. Since 1 January 2018 the major companies which are members of the Tax Capital Group have not changed with respect to those listed in the Tax Capital Group agreement for the years 2015–2017.

(in PLN '000)

17. Earnings (loss) per share

Earnings (loss) per share (in PLN)	Year ended 31 December 2017	Year ended 31 December 2016
Basic and diluted, for profit (loss) for the financial year	0.49	(0.09)

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

	Year ended 31 December 2017	Year ended 31 December 2016
Net profit (loss) attributable to ordinary shareholders	854 351	(166 253)
Number of ordinary shares	1 752 549 394	1 752 549 394

(in PLN '000)

EXPLANATORY NOTES TO THE STATEMENT OF FINANCIAL POSITION

18. Property, plant and equipment

For the year ended 31 December 2017

	Plant and machinery	Motor vehicles	Other	Assets under construction	Property, plant and equipment, total
COST					
Opening balance	**5 918**	**6 857**	**11 635**	**–**	**24 410**
Direct purchase	–	–	–	130	**130**
Allocation of assets under construction	–	–	32	(32)	**–**
Sale	–	(580)	–	–	**(580)**
Liquidation	–	–	(932)	–	**(932)**
Closing balance	**5 918**	**6 277**	**10 735**	**98**	**23 028**
ACCUMULATED DEPRECIATION					
Opening balance	**(5 917)**	**(5 732)**	**(11 485)**	**–**	**(23 134)**
Depreciation for the period	(1)	(847)	(109)	–	**(957)**
Sale	–	580	–	–	**580**
Liquidation	–	–	932	–	**932**
Closing balance	**(5 918)**	**(5 999)**	**(10 662)**	**–**	**(22 579)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**1**	**1 125**	**150**	**–**	**1 276**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**–**	**278**	**73**	**98**	**449**

For the year ended 31 December 2016

	Plant and machinery	Motor vehicles	Other	Assets under construction	Property, plant and equipment, total
COST					
Opening balance	**6 761**	**6 857**	**10 798**	**–**	**24 416**
Direct purchase	–	–	–	837	**837**
Allocation of assets under construction	–	–	837	(837)	**–**
Sale/Liquidation	(843)	–	–	–	**(843)**
Closing balance	**5 918**	**6 857**	**11 635**	**–**	**24 410**
ACCUMULATED DEPRECIATION					
Opening balance	**(6 438)**	**(4 771)**	**(9 771)**	**–**	**(20 980)**
Depreciation for the period	(322)	(961)	(1 714)	–	**(2 997)**
Sale/Liquidation	843	–	–	–	**843**
Closing balance	**(5 917)**	**(5 732)**	**(11 485)**	**–**	**(23 134)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**323**	**2 086**	**1 027**	**–**	**3 436**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**1**	**1 125**	**150**	**–**	**1 276**

19. Investment property

	Year ended 31 December 2017	Year ended 31 December 2016
COST		
Opening balance	**36 169**	**36 169**
Closing balance	**36 169**	**36 169**
ACCUMULATED DEPRECIATION		
Opening balance	**(10 851)**	**(7 234)**
Depreciation for the period	(3 617)	(3 617)
Closing balance	**(14 468)**	**(10 851)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**25 318**	**28 935**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**21 701**	**25 318**

The investment property is composed of buildings located in Katowice-Szopienice, in ul. Lwowska 23 used based on a finance lease agreement with PKO Leasing S.A. The monthly lease payment is ca. PLN 346 thousand, while the monthly depreciation charge is PLN 301 thousand.

The Company is a party to a lease agreement with a subsidiary (the lessee) valid until 30 April 2018, whereby buildings and structures the rights to which result from the aforesaid lease agreement have been subleased. In the year ended 31 December 2017, rental income related to the investment property totalled PLN 5 654 thousand.

The Company estimates that fair value of investment property as at the end of reporting period accounts for about PLN 26 000 thousand.

(in PLN '000)

20. Non-current intangible assets

For the year ended 31 December 2017

	Software and licenses	Other intangible assets	Intangible assets not commissioned for use	Intangible assets, total
COST				
Opening balance	**2 259**	**4 125**	**–**	**6 384**
Direct purchase	–	–	30	**30**
Allocation of intangible assets not made available for use	–	30	(30)	**–**
Closing balance	**2 259**	**4 155**	**–**	**6 414**
ACCUMULATED AMORTIZATION				
Opening balance	**(2 046)**	**(2 147)**	**–**	**(4 193)**
Amortization for the period	(209)	(749)	–	**(958)**
Closing balance	**(2 255)**	**(2 896)**	**–**	**(5 151)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**213**	**1 978**	**–**	**2 191**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**4**	**1 259**	**–**	**1 263**

For the year ended 31 December 2016

	Software and licenses	Other intangible assets	Intangible assets not commissioned for use	Intangible assets, total
COST				
Opening balance	**3 539**	**4 185**	**–**	**7 724**
Liquidation	(1 280)	(60)	–	**(1 340)**
Closing balance	**2 259**	**4 125**	**–**	**6 384**
ACCUMULATED AMORTIZATION				
Opening balance	**(2 985)**	**(1 440)**	–	**(4 425)**
Amortization for the period	(341)	(767)	–	**(1 108)**
Liquidation	1 280	60	–	**1 340**
Closing balance	**(2 046)**	**(2 147)**	**–**	**(4 193)**
NET CARRYING AMOUNT AT THE BEGINNING OF THE PERIOD	**554**	**2 745**	**–**	**3 299**
NET CARRYING AMOUNT AT THE END OF THE PERIOD	**213**	**1 978**	**–**	**2 191**

21. Shares

Change in shares for the year ended 31 December 2017

No.	Company	Gross value				Impairment losses				Net value	
		Opening balance	(Decreases)	Increases	Closing balance	Opening balance	Decreases	(Increases)	Closing balance	Opening balance	Closing balance
1	TAURON Wydobycie S.A.	841 755	–	160 000	1 001 755	–	–	(147 870)	(147 870)	841 755	853 885
2	TAURON Wytwarzanie S.A.	7 236 727	(151 026)	–	7 085 701	(5 403 825)	120 057	(63 528)	(5 347 296)	1 832 902	1 738 405
3	TAURON Ciepło Sp. z o.o.	1 328 043	–	600 000	1 928 043	–	–	–	–	1 328 043	1 928 043
4	TAURON Ekoenergia Sp. z o.o.	939 765	–	1 000 000	1 939 765	(939 765)	72 603	(258 531)	(1 125 693)	–	814 072
5	Marselwind Sp. z o.o.	107	–	200	307	–	–	–	–	107	307
6	TAURON Serwis Sp. z o.o.	1 268	–	–	1 268	–	–	–	–	1 268	1 268
7	Nowe Jaworzno Grupa TAURON Sp. z o.o.	–	–	3 551 026	3 551 026	–	–	–	–	–	3 551 026
8	TAURON Dystrybucja S.A.	9 511 628	–	1 000 000	10 511 628	–	–	–	–	9 511 628	10 511 628
9	TAURON Dystrybucja Serwis S.A.	–	–	201 045	201 045	–	–	–	–	–	201 045
10	TAURON Sprzedaż Sp. z o.o.	613 505	–	–	613 505	–	–	–	–	613 505	613 505
11	TAURON Sprzedaż GZE Sp. z o.o.	129 823	–	–	129 823	–	–	–	–	129 823	129 823
12	TAURON Czech Energy s.r.o.	4 223	–	–	4 223	–	–	–	–	4 223	4 223
13	Kopalnia Wapienia Czatkowice Sp. z o.o.	41 178	–	–	41 178	–	–	–	–	41 178	41 178
14	Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.	55 056	–	–	55 056	–	–	(55 056)	(55 056)	55 056	–
15	TAURON Sweden Energy AB (publ)	28 382	–	–	28 382	–	–	–	–	28 382	28 382
16	Biomasa Grupa TAURON Sp. z o.o.	1 269	–	–	1 269	–	–	–	–	1 269	1 269
17	TAURON Obsługa Klienta Sp. z o.o.	39 831	–	–	39 831	–	–	–	–	39 831	39 831
18	TAMEH HOLDING Sp. z o.o.	415 852	–	–	415 852	–	–	–	–	415 852	415 852
19	PGE EJ 1 Sp. z o.o.	26 546	–	–	26 546	–	–	–	–	26 546	26 546
20	Magenta Grupa TAURON Sp. z o.o.	500	–	9 000	9 500	–	–	–	–	500	9 500
21	ElectroMobility Poland S.A.	2 500	–	–	2 500	–	–	–	–	2 500	2 500
22	Other	50	–	341	391	–	–	–	–	50	391
	Total	**21 218 008**	**(151 026)**	**6 521 612**	**27 588 594**	**(6 343 590)**	**192 660**	**(524 985)**	**(6 675 915)**	**14 874 418**	**20 912 679**

Changes in the balance of long-term investments in the year ended 31 December 2017 resulted mainly from the following transactions:

- Increase in the capital of TAURON Wydobycie S.A.

On 21 March 2017, the Extraordinary General Shareholders' Meeting of TAURON Wydobycie S.A. adopted a resolution to increase the company's issued capital from PLN 355 511 thousand to PLN 357 111 thousand, i.e. by PLN 1 600 thousand, through the issue of 160 000 new shares with the nominal value of PLN 10 each, which were subscribed by the Company for PLN 1 000 per one share, i.e. for the total of PLN 160 000 thousand. The aforesaid increase in the issued capital of TAURON Wydobycie S.A. was registered on 7 April 2017.

- TAURON Wytwarzanie S.A. to Nowe Jaworzno Grupa TAURON Sp. z o.o.

On 3 April 2017 TAURON Wytwarzanie S.A. was spun off under Article 529.1.4 of the Code of Commercial Companies by way of separation and transfer of a branch of activity involved in the preparation, development and operations of a new unit with the capacity of 910 MW in Elektrownia Jaworzno III to Nowe Jaworzno Grupa TAURON Sp. z o.o. An appropriate resolution was taken by the Extraordinary General Shareholders' Meeting of TAURON Wytwarzanie S.A. on 31 January 2017. Following the spin-off the Company reclassified the investment in TAURON Wytwarzanie S.A. in the amount of PLN 151 026 thousand to Nowe Jaworzno Grupa TAURON Sp. z o.o.

- Increase in the capital of TAURON Ciepło Sp. z o.o.

On 11 May 2017, the Extraordinary General Shareholders' Meeting of TAURON Ciepło Sp. o.o. adopted a resolution to increase the company's issued capital from PLN 1 098 348 thousand to PLN 1 104 348 thousand, i.e. by PLN 6 000 thousand, through the issue of 120 000 new shares with the nominal value of PLN 50 each and the total nominal value of PLN 6 000 thousand. The shares were acquired for PLN 5 thousand each, i.e. the total value of PLN 600 000 thousand. The aforesaid increase in the issued capital of TAURON Ciepło Sp. o.o. was registered on 20 June 2017.

- Increase in the capital of Nowe Jaworzno Grupa TAURON Sp. z o.o.

On 16 May 2017, the Extraordinary General Shareholders' Meeting of Nowe Jaworzno Grupa TAURON Sp. z o.o. adopted a resolution (to change the terms and conditions of increasing the issued capital of the company determined by the Extraordinary General Shareholders' Meeting on 19 April 2017) to increase the company's issued capital from PLN 1 850 thousand to PLN 31 850 thousand, i.e. by PLN 30 000 thousand, through the issue of 600 000 new shares with the nominal value of PLN 50 each and the total nominal value of PLN 30 000 thousand. The shares were acquired for PLN 5 thousand each, i.e. the total value of PLN 3 000 000 thousand. The aforesaid increase in the issued capital of Nowe Jaworzno Grupa TAURON Sp. z o.o. was registered on 26 June 2017.

On 29 June 2017, the Extraordinary General Shareholders' Meeting of Nowe Jaworzno Grupa TAURON Sp. z o.o. adopted a resolution to increase the company's issued capital by PLN 4 000 thousand, through the issue of 80 000 new shares with the nominal value of PLN 50 each. TAURON Polska Energia S.A. took all of new shares in the company for PLN 5 thousand per share, i.e. the total acquisition price of PLN 400 000 thousand. The increase in the issued capital of Nowe Jaworzno Grupa TAURON Sp. z o.o. was registered on 13 July 2017.

- Agreement for the transfer of shares in TAURON Dystrybucja Serwis S.A.

On 9 August 2017, the Company concluded an agreement for the transfer of shares with TAURON Dystrybucja S.A., a subsidiary, under the acceptance in lieu scheme in accordance with Article 453 of the Civil Law Act of 23 April 1964 (Journal of Laws of 2017 item 459 as amended). In line with the agreement TAURON Dystrybucja S.A. transferred 5 101 003 shares, constituting 100% of the issued capital of TAURON Dystrybucja Serwis S.A. with the value of PLN 201 045 thousand to the Company in order to be discharged from a portion of its obligation to pay out dividend to the Company in the amount of PLN 201 046 thousand.

- Increase in the capital of TAURON Ekoenergia Sp. z o.o.

On 24 October 2017 the Extraordinary Meeting of Shareholders of TAURON Ekoenergia Sp. z o.o. resolved to increase the issued capital of the company by PLN 10 000 thousand by creating 10 000 new shares with the nominal value of PLN 1000 each which were acquired by the Company for PLN 100 000 each, totalling PLN 1 000 000 thousand. On 26 and 27 October 2017 the Company advanced monies to increase the capital. After the end of the reporting period, on 2 March 2018 year, the increase in the issued capital of TAURON Ekoenergia Sp. z o.o. was registered.

- Increase in the capital of Magenta Grupa TAURON Sp. z o.o.

On 24 October 2017 the Extraordinary Meeting of Shareholders of Magenta Grupa TAURON Sp. z o.o. resolved to increase the issued capital of the company by PLN 1 000 thousand by creating 20 000 new shares with the nominal value of PLN 50 each which were acquired by the Company for PLN 450 each, totalling PLN 9 000 thousand. On 26 October 2017 the Company advanced monies to increase the capital. After the end of reporting period, on 11 January 2018, the increase in the issued capital of Magenta Grupa TAURON Sp. z o.o. was registered.

- Increase in the capital of TAURON Dystrybucja S.A.

On 26 October 2017 the Extraordinary Meeting of Shareholders of TAURON Dystrybucja S.A. resolved to increase the issued capital of the company by PLN 48 685 thousand by issuing 2 434 274 587 shares with the nominal value of PLN 0.02 each, which will be acquired by the Company for PLN 0.4108 each, totalling PLN 1 000 000 thousand. The increase in the issued capital of TAURON Dystrybucja S.A. was registered on 29 December 2017.

(in PLN '000)

- Impairment loss on shares in Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.

In the year ended 31 December 2017 the Company recognized an impairment loss of PLN 55 056 thousand on its shares in a subsidiary.

- Impairment of shares

In the year ended 31 December 2017 shares in subsidiaries were tested for impairment following which the impairment loss on the shares in TAURON Wytwarzanie S.A. totalling PLN 120 057 thousand and TAURON Ekoenergia Sp. z o.o. totalling PLN 72 603 thousand were released and an impairment loss on the shares in TAURON Wytwarzanie S.A. of PLN 63 528 thousand and shares in TAURON Wydobycie S.A. of PLN 147 870 thousand were recognized. Additionally, following the repayment of a loan by TAURON Ekoenergia Sp. z o.o. and subscription of shares in the company, the impairment loss on the loan of PLN 258 531 thousand was reclassified to the shares in TAURON Ekoenergia Sp. z o.o. The impairment tests have been discussed in more detail in Note 11 to these financial statements.

Change in shares for the year ended 31 December 2016

No.	Company	Gross value				Impairment losses				Net value	
		Opening balance	(Decreases)	Increases	Closing balance	Opening balance	Decreases	(Increases)	Closing balance	Opening balance	Closing balance
1	TAURON Wydobycie S.A.	494 755	–	347 000	841 755	–	–	–	–	494 755	841 755
2	Nowe Brzeszcze Grupa TAURON Sp. z o.o.	2 102	(185 002)	182 900	–	–	–	–	–	2 102	–
3	TAURON Wytwarzanie S.A.	7 236 727	–	–	7 236 727	(4 487 895)	–	(915 930)	(5 403 825)	2 748 832	1 832 902
4	TAURON Wytwarzanie GZE Sp. z o.o. in liquidation	4 935	(4 935)	–	–	–	–	–	–	4 935	–
5	TAURON Ciepło Sp. z o.o.	1 328 043	–	–	1 328 043	(443 252)	443 252	–	–	884 791	1 328 043
6	TAURON Ekoenergia Sp. z o.o.	939 765	–	–	939 765	–	–	(939 765)	(939 765)	939 765	–
7	Marselwind Sp. z o.o.	107	–	–	107	–	–	–	–	107	107
8	TAURON Serwis Sp. z o.o.	–		1 268	1 268	–			–	–	1 268
9	TAURON Dystrybucja S.A.	9 511 628	–	–	9 511 628	–	–	–	–	9 511 628	9 511 628
10	TAURON Sprzedaż Sp. z o.o.	613 505	–	–	613 505	–	–	–	–	613 505	613 505
11	TAURON Sprzedaż GZE Sp. z o.o.	129 823	–	–	129 823	–	–	–	–	129 823	129 823
12	TAURON Czech Energy s.r.o.	4 223	–	–	4 223	–	–	–	–	4 223	4 223
13	Kopalnia Wapienia Czatkowice Sp. z o.o.	41 178	–	–	41 178	–	–	–	–	41 178	41 178
14	Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. in liquidation	49 056	–	6 000	55 056	–	–	–	–	49 056	55 056
15	TAURON Sweden Energy AB (publ)	28 382	–	–	28 382	–	–	–	–	28 382	28 382
16	Biomasa Grupa TAURON Sp. z o.o.	1 269	–	–	1 269	–	–	–	–	1 269	1 269
17	TAURON Obsługa Klienta Sp. z o.o.	39 831	–	–	39 831	–	–	–	–	39 831	39 831
18	TAMEH HOLDING Sp. z o.o.	415 852	–	–	415 852	–	–	–	–	415 852	415 852
19	PGE EJ 1 Sp z o.o.	23 046	–	3 500	26 546	–	–	–	–	23 046	26 546
20	Magenta Grupa TAURON Sp. z o.o.	–	–	500	500	–	–	–	–	–	500
21	ElectroMobility Poland S.A.	–	–	2 500	2 500	–	–	–	–	–	2 500
22	Other	114	(1 267)	1 203	50	–	–	–	–	114	50
	Total	**20 864 341**	**(191 204)**	**544 871**	**21 218 008**	**(4 931 147)**	**443 252**	**(1 855 695)**	**(6 343 590)**	**15 933 194**	**14 874 418**

22. Bonds

Under the central financing model, TAURON Polska Energia S.A. acquires bonds issued by the TAURON Group companies.

The table below presents the balances of acquired bonds and interest accrued as at the end of the reporting period, i.e. 31 December 2017 and as at 31 December 2016, broken down by individual companies issuing the bonds.

Company	As at 31 December 2017		As at 31 December 2016	
	par value of purchased bonds	accrued interest	par value of purchased bonds	accrued interest
TAURON Wytwarzanie S.A.	1 064 920	10 689	3 548 770	55 396
TAURON Dystrybucja S.A.	3 770 000	62 326	3 800 000	62 470
TAURON Ciepło Sp. z o.o.	1 075 000	15 169	1 673 260	46 848
TAURON Wydobycie S.A.	570 000	4 592	570 000	4 592
TAURON Obsługa Klienta Sp. z o.o.	–	–	85 000	12 046
Total	**6 479 920**	**92 776**	**9 677 030**	**181 352**
Non-current	6 009 920	–	9 612 030	3 887
Current	470 000	92 776	65 000	177 465

(in PLN '000)

Intra-group bonds maturing within one year, intended for rollover, are classified as long-term instruments. Such classification reflects the nature of funding under the intra-group bond issue scheme, which enables cash management in the medium and long term. The agreements provide for the possibility to roll over the bonds. As at 31 December 2017, the par value of bonds maturing within one year, which were classified as long-term bonds, was PLN 864 920 thousand.

Internal bonds maturing over one year, totalling PLN 470 000 thousand, were classified to short-term as their redemption took place at 22 February 2018.

23. Derivative instruments

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

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

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

The methodology of fair value measurement of the derivative financial instruments presented in the table above has been discussed in Note 9.9 to these financial statements.

Hedging derivative instruments (subject to hedge accounting) – IRS

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

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

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

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

(in PLN '000)

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

24. Other financial assets

	As at 31 December 2017	As at 31 December 2016
Receivables from the TCG	6 133	20 945
Units in investment funds	101 358	25 316
Bid bonds, deposits, collateral transferred	15 343	10 156
Initial margin deposits	11 140	–
Other	390	461
Total	**134 364**	**56 878**
Non-current	2 724	1 524
Current	131 640	55 354

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

25. Loans granted

	As at 31 December 2017			As at 31 December 2016		
	Principal	Interest	Total	Principal	Interest	Total
Value of items before allowance/write-down						
Loan granted to TAURON Ekoenergia Sp. z o.o.	120 000	19 268	139 268	1 120 000	129 802	1 249 802
Loans granted to EC Stalowa Wola S.A.	529 007	41 425	570 432	218 525	37 542	256 067
Loans granted to PGE EJ 1 Sp. z o.o.	2 940	14	2 954	–	–	–
Granted cash pool loans including accrued interest	189 928	598	190 526	15 306	544	15 850
Total	**841 875**	**61 305**	**903 180**	**1 353 831**	**167 888**	**1 521 719**
Allowance/write-down						
Loan granted to TAURON Ekoenergia Sp. z o.o.			–			(197 953)
Value of item net of allowance (carrying amount)			**903 180**			**1 323 766**
Non-current			382 989			1 292 800
Current			520 191			30 966

Loan to a subsidiary

On 27 February 2015, the Company entered into an agreement with its subsidiary, TAURON Ekoenergia Sp. z o.o., whereby TAURON Polska Energia S.A. granted a one-year loan of PLN 1 120 000 thousand to TAURON Ekoenergia Sp. z o.o. The purpose of the loan was to repurchase and redeem the same amount of intra-group bonds issued by the borrower in prior years to finance construction of wind farms. Under subsequent annexes, the loan repayment date was postponed to 27 February 2018.

On 26 and 27 October 2017 a portion of the loan extended by the Company to subsidiary TAURON Ekoenergia Sp. z o.o. was prematurely repaid. On both dates the amount prepaid by the subsidiary was PLN 500 000 thousand, i.e. PLN 1 000 000 thousand in total. Since the subsidiary TAURON Ekoenergia Sp. z o.o. repaid a portion of the loan and the shares in its increased capital were acquired by the Company, the impairment loss on the loan was reclassified to the shares in TAURON Ekoenergia Sp. z o.o., which has been discussed in more detail in Note 11 to these financial statements.

After the end of the reporting period, on 27 February 2018, a subsidiary repaid the remanding part of a loan of PLN 120 000 thousand.

As at 31 December 2017, the loan, including interest, whose carrying amount was PLN 139 268 thousand, was classified by the Company as a long-term loan, as the exposure was planned to be maintained for a period of more than one year of the end of the reporting period.

(in PLN '000)

Loans granted to joint ventures

The table below presents loans granted to joint venture Elektrociepłownia Stalowa Wola S.A. as at the end of the reporting period, i.e. 31 December 2017 and as at 31 December 2016:

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

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

Loans granted by the Company to Elektrociepłownia Stalowa Wola S.A. under agreements dated 30 March 2017 for purposes of debt repayment totalled PLN 290 742 thousand. The said loans were granted for purposes of the debtor's early payment of liabilities under loan agreements entered into in relation to the construction of a heat and power unit in Stalowa Wola, which has been discussed in more detail in Note 35 to these financial statements.

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

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

- The total outstanding principal amount of PLN 145 991 thousand under the refinancing loan agreement dated 30 March 2017 and a portion of the principal amount of PLN 4 009 thousand under the refinancing loan agreement dated 30 March 2017 for PLN 73 518 thousand were included in the debt consolidation agreement of 30 June 2017 for the total amount of PLN 150 000 thousand.

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

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

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

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

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

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

Loans granted under cash pool agreement

Detailed information on the cash pool service has been presented in Note 33.4 to these financial statements.

(in PLN '000)

26. Inventories

	As at 31 December 2017	As at 31 December 2016
Gross Value		
Energy certificates	250	250
Greenhouse gas emission allowances	198 459	271 729
Materials	40	23
Total	**198 749**	**272 002**
Measurement to net realisable value		
Energy certificates	(184)	(195)
Greenhouse gas emission allowances	(145)	(234)
Measurement to fair value		
Greenhouse gas emission allowances	8	13 226
Total	**(321)**	**12 797**
Net value		
Energy certificates	66	55
Greenhouse gas emission allowances	198 322	284 721
Materials	40	23
Total	**198 428**	**284 799**

Inventories are measured at net realizable value, except for the inventory of emission allowances purchased for resale and generation of profit in the short term due to volatility of market prices, which is measured at fair value as at the end of the reporting period.

27. Receivables from buyers

	As at 31 December 2017	As at 31 December 2016
Gross Value		
Receivables from buyers	719 144	840 665
Receivables claimed at court	913	890
Total	**720 057**	**841 555**
Allowance/write-down		
Receivables from buyers	(11)	(9)
Receivables claimed at court	(913)	(890)
Total	**(924)**	**(899)**
Net Value		
Receivables from buyers	719 133	840 656
Receivables claimed at court	–	–
Total	**719 133**	**840 656**

As at 31 December 2017 and 31 December 2016, the largest item of receivables from buyers was receivables from TAURON Sprzedaż Sp. z o.o., a subsidiary, amounting to PLN 481 526 thousand and PLN 478 220 thousand, respectively.

Ageing analysis of receivables from buyers as at 31 December 2017

	Not past due	Past due			Total
		<30 days	30–360 days	>360 days	
Value of item before allowance/write-down	719 112	39	37	869	**720 057**
Allowance/write-down	(33)	–	(22)	(869)	**(924)**
Net Value	**719 079**	**39**	**15**	**–**	**719 133**

Ageing analysis of receivables from buyers as at 31 December 2016

	Not past due	Past due			Total
		<30 days	30–360 days	>360 days	
Value of item before allowance/write-down	840 494	172	35	854	**841 555**
Allowance/write-down	(3)	(7)	(35)	(854)	**(899)**
Net Value	**840 491**	**165**	**–**	**–**	**840 656**

(in PLN '000)

Impairment losses on receivables from buyers

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**(899)**	**(2 582)**
Recognised	(74)	(66)
Reversed	49	1 749
Closing balance	**(924)**	**(899)**

Related-party transactions as well as related party receivables and liabilities have been presented in Note 47.1 hereto.

28. Receivables arising from taxes and charges

	As at 31 December 2017	As at 31 December 2016
Corporate Income Tax	–	83 162
VAT receivables	36 094	35 674
Excise duty receivables	–	1 750
Total	**36 094**	**120 586**

A drop in receivables arising from taxes and charges results mostly from a drop in CIT receivables in the Tax Capital Group. As at 31 December 2017, the Tax Capital Group had income tax liabilities of PLN 37 629 thousand, which has been discussed in more detail in Note 16.4 to these financial statements. As at 31 December 2016, the Tax Capital Group reported income tax receivables of PLN 83 153 thousand.

29. Other non-financial assets

	As at 31 December 2017	As at 31 December 2016
Prepaid expenses, including:	16 799	10 284
Prepaid fee on borrowings	*16 169*	*9 531*
Advance payments for deliveries	1 313	19 315
Total	**18 112**	**29 599**
Non-current	13 255	6 071
Current	4 857	23 528

30. Cash and cash equivalents

	As at 31 December 2017	As at 31 December 2016
Cash at bank and in hand	521 343	198 087
Short-term deposits (up to 3 months)	200 234	3
Total cash and cash equivalents presented in the statement of financial position, including:	**721 577**	**198 090**
restricted cash	49 792	56 787
Cash pool	(2 186 508)	(1 229 639)
Overdraft	(93 502)	(15 131)
Foreign exchange	(799)	1 239
Total cash and cash equivalents presented in the statement of cash flows	**(1 559 232)**	**(1 045 441)**

The balances of loans granted and taken out in cash pool transactions do not represent cash flows from investing or financing activities as they are mainly used to manage the Group's liquidity on a day-to-day basis. They are presented as an adjustment to the balance of cash instead.

Restricted cash includes mainly cash held in the settlement account for trading in electricity on the Polish Power Exchange (Towarowa Giełda Energii S.A), amounting to PLN 49 380 thousand.

Detailed information on cash pool balances has been presented in Note 33.4 to these financial statements.

(in PLN '000)

31. Equity

31.1. Issued capital

Issued capital as at 31 December 2017

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

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

31.2. Major shareholders

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

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

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

31.3. Reserve capital

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

31.4. Revaluation reserve from valuation of hedging instruments

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

The revaluation reserve from valuation of hedging instruments results from valuation of Interest Rate Swaps (IRS) hedging the interest rate risk arising from bonds issued, which has been discussed in more detail in Note 23 to these financial statements.

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

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

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

(in PLN '000)

31.5. Retained earnings and dividend limitation

Reserve capital – dividend limitation

	As at 31 December 2017	As at 31 December 2016
amounts subject to distribution	**4 032 169**	**4 032 169**
amounts from distribution of prior years profits	4 032 169	4 032 169
non-distributable amounts	**3 624 917**	**3 791 170**
decrease in the value of issued capital	3 390 037	3 556 290
settlement of mergers with subsidiaries	234 880	234 880
Total reserve capital	**7 657 086**	**7 823 339**

Retained earnings – dividend limitation

	As at 31 December 2017	As at 31 December 2016
distributable amounts or losses to be covered	**854 364**	**(166 240)**
profit (loss) for the year ended 31 December 2017	854 351	–
profit (loss) for the year ended 31 December 2016	–	(166 253)
adjustment of prior years profit	13	13
non-distributable amounts	**80 658**	**80 762**
actuarial gains and losses on provisions for post-employment benefits	140	244
settlement of mergers with subsidiaries	80 518	80 518
Total retained earnings (accumulated losses)	**935 022**	**(85 478)**

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

32. Dividends paid

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

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

(in PLN '000)

33. Debt

	As at 31 December 2017	As at 31 December 2016
Long-term portion of debt		
Subordinated hybrid bonds	791 355	839 330
Other issued bonds	7 113 161	6 089 821
Loans received from the European Investment Bank	873 770	1 035 927
Loans from the subsidiary	694 168	765 450
Finance lease	–	23 519
Total	**9 472 454**	**8 754 047**
Short-term portion of debt		
Subordinated hybrid bonds	1 597	1 693
Other issued bonds	34 233	11 287
Cash pool loans received, including accrued interest	2 377 034	1 245 489
Loans from the European Investment Bank	168 340	154 574
Loans from the subsidiary	27 112	2 300
Overdraft	93 502	15 131
Finance lease	23 945	3 455
Total	**2 725 763**	**1 433 929**

33.1. Bonds issued

Bonds issued as at 31 December 2017

Tranche/Bank	Maturity date	Currency	Principal at nominal value in currency	As at balance sheet date		of which maturing within (*after the balance sheet date*)		
				Accrued interest	Principal at amortized cost	up to 2 years	2–5 years	over 5 years
Bank Gospodarstwa Krajowego	20.12.2019	PLN	100 000	107	99 869	99 869	–	–
	20.12.2020	PLN	100 000	107	99 838	–	99 838	–
	20.12.2021	PLN	100 000	107	99 817	–	99 817	–
	20.12.2022	PLN	100 000	107	99 800	–	99 800	–
	20.12.2023	PLN	100 000	107	99 787	–	–	99 787
	20.12.2024	PLN	100 000	107	99 778	–	–	99 778
	20.12.2025	PLN	100 000	107	99 770	–	–	99 770
	20.12.2026	PLN	100 000	107	99 761	–	–	99 761
	20.12.2027	PLN	100 000	107	99 756	–	–	99 756
	20.12.2028	PLN	100 000	107	99 752	–	–	99 752
	20.12.2020	PLN	70 000	74	69 963	–	69 963	–
	20.12.2021	PLN	70 000	74	69 961	–	69 961	–
	20.12.2022	PLN	70 000	74	69 959	–	69 959	–
	20.12.2023	PLN	70 000	74	69 958	–	–	69 958
	20.12.2024	PLN	70 000	74	69 957	–	–	69 957
	20.12.2025	PLN	70 000	74	69 956	–	–	69 956
	20.12.2026	PLN	70 000	74	69 956	–	–	69 956
	20.12.2027	PLN	70 000	74	69 955	–	–	69 955
	20.12.2028	PLN	70 000	74	69 955	–	–	69 955
	20.12.2029	PLN	70 000	74	69 955	–	–	69 955
Bond Issue Scheme of 24 November 2015	29.12.2020	PLN	1 600 000	389	1 597 188	–	1 597 188	–
TPEA1119	4.11.2019	PLN	1 750 000	7 609	1 749 277	1 749 277	–	–
European Investment Bank	16.12.2034	EUR	190 000	1 597	791 355	–	–	791 355
Eurobonds EURBD050727	5.07.2027	EUR	500 000	24 425	2 069 193	–	–	2 069 193
Total				**35 830**	**7 904 516**	**1 849 146**	**2 106 526**	**3 948 844**

(in PLN '000)

Bonds issued as at 31 December 2016

Tranche/Bank	Maturity date	Currency	Principal at nominal value in currency	As at balance sheet date		of which maturing within (*after the balance sheet date*)		
				Accrued interest	Principal at amortized cost	up to 2 years	2–5 years	over 5 years
Bank Gospodarstwa Krajowego	20.12.2019	PLN	100 000	107	99 805	–	99 805	–
	20.12.2020	PLN	100 000	107	99 786	–	99 786	–
	20.12.2021	PLN	100 000	107	99 773	–	99 773	–
	20.12.2022	PLN	100 000	107	99 763	–	–	99 763
	20.12.2023	PLN	100 000	107	99 754	–	–	99 754
	20.12.2024	PLN	100 000	107	99 749	–	–	99 749
	20.12.2025	PLN	100 000	107	99 744	–	–	99 744
	20.12.2026	PLN	100 000	107	99 738	–	–	99 738
	20.12.2027	PLN	100 000	107	99 734	–	–	99 734
	20.12.2028	PLN	100 000	107	99 733	–	–	99 733
	20.12.2020	PLN	70 000	74	69 976	–	69 976	–
	20.12.2021	PLN	70 000	74	69 976	–	69 976	–
	20.12.2022	PLN	70 000	74	69 976	–	–	69 976
	20.12.2023	PLN	70 000	74	69 976	–	–	69 976
	20.12.2024	PLN	70 000	74	69 975	–	–	69 975
	20.12.2025	PLN	70 000	74	69 975	–	–	69 975
	20.12.2026	PLN	70 000	74	69 975	–	–	69 975
	20.12.2027	PLN	70 000	74	69 975	–	–	69 975
	20.12.2028	PLN	70 000	74	69 975	–	–	69 975
	20.12.2029	PLN	70 000	74	69 975	–	–	69 975
Bond Issue Scheme of 24 November 2015	29.12.2020	PLN	2 250 000	549	2 244 801	–	2 244 801	–
	25.03.2020	PLN	100 000	790	99 771	–	99 771	–
	9.12.2020	PLN	300 000	560	298 761	–	298 761	–
TPEA1119	4.11.2019	PLN	1 750 000	7 578	1 749 155	–	1 749 155	–
European Investment Bank	16.12.2034	EUR	190 000	1 693	839 330	–	–	839 330
Total				**12 980**	**6 929 151**	**–**	**4 831 804**	**2 097 347**

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

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

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

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

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

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

The amendments were signed with the following banks taking part in the Program: Bank Handlowy in Warsaw S.A., Bank BGŻ BNP Paribas S.A., Bank Zachodni WBK S.A., CaixaBank S.A. (Joint Stock Company) Branch in Poland, Industrial and Commercial Bank of China (Europe) S.A. Branch in Poland, ING Bank Śląski S.A., mBank S.A., MUFG

(in PLN '000)

Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland and Powszechna Kasa Oszczędności Bank Polski S.A. Due to the extension, the financing margin in the Scheme did not change.

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

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

A change in the balance of bonds, excluding interest which increased the carrying amount in the year ended 31 December 2017 and in the comparable period, has been presented below.

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**6 929 151**	**5 956 033**
Issue*	2 703 643	4 273 379
Redemption	(1 650 000)	(3 300 000)
Measurement change	(78 278)	(261)
Closing balance	**7 904 516**	**6 929 151**

** Costs of discount and issue have been included.*

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

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

(in PLN '000)

The Company hedges a portion of interest cash flows related to issued bonds using IRS contracts. The instruments are subject to hedge accounting, which has been discussed in more detail in Note 23 to these financial statements.

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

33.2. Loans from the European Investment Bank

As at 31 December 2017, the balance of loans obtained from the European Investment Bank was PLN 1 042 110 thousand, including interest accrued of PLN 6 100 thousand. As at 31 December 2016, the balance of loans obtained from the European Investment Bank was PLN 1 190 501 thousand, including interest accrued of PLN 7 086 thousand.

A change in the balance of loans from the European Investment Bank, excluding interest increasing their carrying amount, is presented below.

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**1 183 415**	**1 316 061**
Repaid	(147 568)	(132 818)
Measurement change	163	172
Closing balance	**1 036 010**	**1 183 415**

In the year ended 31 December 2017, the Company repaid PLN 147 568 thousand of the principal amount and PLN 41 017 thousand of interest.

33.3. Loans from a subsidiary

As at 31 December 2017, the carrying amount of loans from a subsidiary, TAURON Sweden Energy AB (publ), was PLN 721 280 thousand (EUR 172 932 thousand), including interest of PLN 27 112 thousand (EUR 6 500 thousand) accrued as at the end of the reporting period. As at 31 December 2016, the carrying amount of loans from a subsidiary, TAURON Sweden Energy AB (publ), was PLN 767 750 thousand (EUR 173 542 thousand), including interest of PLN 2 300 thousand (EUR 520 thousand) accrued as at the end of the reporting period.

A change in the balance of the loan from the subsidiary, excluding interest increasing its carrying amount, is presented below.

	Year ended 31 December 2017	Year ended 31 December 2016
Opening balance	**765 450**	**737 296**
Repaid	(28 127)	–
Measurement change	(43 155)	28 154
Closing balance	**694 168**	**765 450**

The Company's liability is a long-term loan granted under an agreement entered into in December 2014 by TAURON Polska Energia S.A. and TAURON Sweden Energy AB (publ). The interest rate on the loan is fixed and interest is paid annually, in December, until the final loan repayment date. The loan will be fully repaid on 29 November 2029.

In the year ended 31 December 2017, on 31 July 2017, the Company repaid the loan granted by the subsidiary TAURON Sweden Energy AB (publ) from 27 July 2015 of PLN 28 127 thousand (EUR 6 600 thousand) with interest of PLN 197 thousand (EUR 46 thousand).

33.4. Cash pool service

In order to optimize cash management, financial liquidity and finance income and costs, the TAURON Group has implemented a cash pool structure. On 18 December 2014, the Company concluded a new zero-balancing agreement with PKO Bank Polski S.A. for a 3-year term which may be extended by 12 months, with TAURON Polska Energia S.A. acting as an agent. The interest rates were determined on market terms.

(in PLN '000)

The balances of receivables and liabilities arising from cash pool transactions have been presented in the table below.

	As at 31 December 2017	As at 31 December 2016
Receivables from cash pool loans granted	189 928	15 306
Interest receivable on loans granted under cash pool agreement	598	544
Total Receivables	**190 526**	**15 850**
Loans received under cash pool agreement	2 374 430	1 244 471
Interest payable on loans received under cash pool agreement	2 604	1 018
Total Liabilities	**2 377 034**	**1 245 489**

Surplus cash obtained by the Company under the cash pool agreement is deposited in bank accounts.

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. As at 31 December 2017, the Company did not have any related liabilities.

33.5. Overdraft facilities

As at 31 December 2017, the balance of overdraft facilities included:

- an agreement for an overdraft in EUR with Bank Gospodarstwa Krajowego, concluded by the Company to finance transactions in emission allowances, power and gas, of EUR 22 069 thousand (PLN 92 048 thousand), together with interest accrued in the amount of EUR 9 thousand (PLN 39 thousand);
- an agreement for an overdraft in USD with mBank S.A., concluded by the Company for the purpose of financing margin deposits and commodity transactions, of USD 418 thousand (PLN 1 454 thousand).

As at 31 December 2016, the balance of overdraft facilities was PLN 15 131 thousand.

33.6. Finance lease liabilities

	As at 31 December 2017		As at 31 December 2016	
	Minimum lease payments	Present value of lease payments	Minimum lease payments	Present value of lease payments
Within 1 year	24 142	23 945	4 105	3 455
Within 1 to 2 years	–	–	23 716	23 519
Minimum lease payments, total	**24 142**	**23 945**	**27 821**	**26 974**
Less amounts representing finance charges	(197)	–	(847)	–
Present value of minimum lease payments	**23 945**	**23 945**	**26 974**	**26 974**
Non-current	–	–	23 519	23 519
Current	23 945	23 945	3 455	3 455

As at 31 December 2017 and 31 December 2016, the finance lease liability resulted from a lease of investment property.

33.7. Operating lease liabilities

As at 31 December 2017, the Company used a real property located in Katowice at ul. ks. Piotra Ściegiennego 3, based on a lease agreement.

The Company's registered office is located in the leased premises with the usable area of 9 931.39 square meters. In 2017, the average monthly rental fee with the service charges was PLN 818 thousand.

(in PLN '000)

34. Provisions for employee benefits

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

	Provision for retirement, disability and similar benefits	Employee electricity rates	Social Fund	Provisions, total
Opening balance	**1 653**	**1 083**	**97**	**2 833**
Current service costs	348	240	18	**606**
Actuarial gains and losses, of which:	153	(32)	7	**128**
arising from changes in financial assumptions	(19)	–	–	**(19)**
arising from changes in demographic assumptions	–	–	–	**–**
arising from other changes	172	(32)	7	**147**
Benefits paid	(158)	(7)	(1)	**(166)**
Interest expense	41	32	3	**76**
Closing balance	**2 037**	**1 316**	**124**	**3 477**
Non-current	1 719	1 307	121	**3 147**
Current	318	9	3	**330**

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

	Provision for retirement, disability and similar benefits	Employee electricity rates	Social Fund	Jubilee bonuses	Provisions, total
Opening balance	**1 547**	**1 314**	**282**	**5 422**	**8 565**
Current service costs	210	85	26	924	**1 245**
Actuarial gains and losses, of which:	(364)	(563)	(246)	(526)	**(1 699)**
arising from changes in financial assumptions	(30)	(304)	(32)	–	**(366)**
arising from changes in demographic assumptions	(130)	(119)	(12)	–	**(261)**
arising from other changes	(204)	(140)	(202)	(526)	**(1 072)**
Benefits paid	(9)	(4)	(1)	(693)	**(707)**
Past service costs	225	213	28	(5 280)	**(4 814)**
Interest expense	44	38	8	153	**243**
Closing balance	**1 653**	**1 083**	**97**	**–**	**2 833**
Non-current	1 361	1 077	96	–	**2 534**
Current	292	6	1	–	**299**

Measurement of provisions for employee benefits

Provisions for employee benefits were estimated using actuarial methods. Key actuarial assumptions made as at the end of the reporting period for purposes of calculation of the provision:

	31 December 2017	31 December 2016
Discount rate (%)	3.00%	3.00%
Estimated inflation rate (%)	2.50%	2.50%
Employee rotation rate (%)	7.93%	7.94%
Estimated salary increase rate (%)	2.50%	2.50%
Estimated electricity price increase rate (%)	3.50%	3.50%
Estimated increase rate for contribution to the Social Fund (%)	3.50%	3.50%
Remaining average employment period	17.11	13.06

(in PLN '000)

A sensitivity analysis of measurement results as at 31 December 2017 to changes in key actuarial assumptions by 0.5 percentage point has been presented below:

Provision	Measurement as at 31 December 2017	Financial discount rate		Planned increases in base amount	
		-0.5 p.p.	+0.5 p.p.	-0.5 p.p.	+0.5 p.p.
Provision for retirement, disability and similar benefits	2 037	2 136	1 948	1 948	2 136
Employee electricity rates	1 316	1 477	1 180	1 180	1 475
Social Fund	124	136	110	110	136
Total	**3 477**	**3 749**	**3 238**	**3 238**	**3 747**

A discount rate reduction by 0.5 percentage point would result in an increase in the provision for employee benefits from PLN 3 477 thousand to PLN 3 749 thousand. A discount rate increase by 0.5 percentage point, i.e. application of a 3.50% discount rate, would result in a decrease in the provision to PLN 3 238 thousand.

The benefits were calculated based on the assumptions set out in the Compensation Policy. Reducing the planned increases of compensation bases by 0.5 percentage point would result in a decrease in the provision for employee benefits down to PLN 3 238 thousand, while their increase by 0.5 percentage point would cause an increase in the provision up to PLN 3 747 thousand.

35. Other provisions

Change in other provisions for the year ended 31 December 2017

	Provisions for onerous contracts with a jointly-controlled entity and provision for costs	Other provisions	Provisions total
Opening balance	**198 844**	**64 505**	**263 349**
Unwinding of discount and change in discount rate	2 330	–	**2 330**
Recognision	2 250	4 277	**6 527**
Reversal	(203 424)	–	**(203 424)**
Utilisation	–	(11)	**(11)**
Closing balance	**–**	**68 771**	**68 771**
Non-current	–	–	**–**
Current	–	68 771	**68 771**

Change in other provisions for the year ended 31 December 2016

	Provisions for onerous contracts with a jointly-controlled entity and provision for costs	Other provisions	Provisions total
Opening balance	**182 877**	**15**	**182 892**
Unwinding of discount and change in discount rate	13 759	–	**13 759**
Recognision	2 221	64 509	**66 730**
Reversal	(13)	(3)	**(16)**
Utilisation	–	(16)	**(16)**
Closing balance	**198 844**	**64 505**	**263 349**
Non-current	152 943	–	**152 943**
Current	45 901	64 505	**110 406**

(in PLN '000)

Provision for onerous contracts with a joint venture and for costs

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

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

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

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

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

Reversal of the provision for costs relating to the electricity sales contract and the provision for losses which might be incurred under the take-or-pay clause was the result of the fulfilment of the conditions precedent under the conditional arrangement made on 27 October 2016 to determine the key boundary conditions of the restructuring of the "Construction of a gas and steam unit in Stalowa Wola" project. The conditions precedent were discharged on 31 March 2017 when Elektrociepłownia Stalowa Wola paid all its liabilities to the financing institutions, i.e. the European Investment Bank, European Bank for Reconstruction and Development and Bank Polska Kasa Opieki S.A. The funds for repayment of the said bank loans were obtained by Elektrociepłownia Stalowa Wola S.A. under loan agreements entered into with the Company and Polskie Górnictwo Naftowe i Gazownictwo S.A. as the lenders. To this end, the Company granted a loan of PLN 290 742 thousand, which has been discussed in more detail in Note 25 to these financial statements. Once the conditions precedent were discharged the following documents came into effect:

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

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

The changes to the gaseous fuel supply contract and the electricity sales contract include in particular the application of market price formulas for the contracts in question. Furthermore, due to delays in the project, the annex to the gaseous fuel supply contract provides for changes in the amount, time limits and methodologies of imposition of liquidated damages. According to the Management Board of the Company, the aforesaid changes constituted a basis for reversal of the provision for costs related to the electricity sales contract and the provision for losses which might be incurred under the take-or-pay clause in Q1 2017.

(in PLN '000)

Other provisions

As at 31 December 2017 other provisions included mainly the provisions for tax risks due to the pending inspection proceedings. As at 31 December 2016 the Company recognized a related provision of PLN 64 494 thousand. As at 31 December 2017, the relevant provision amounted to PLN 68 694 thousand. An increase in the provision by PLN 4 200 thousand, is attributable to interest accrued as at the year ended 31 December 2017.

The Company is a party to VAT inspection proceedings instigated by the Director of the Tax Inspection Office in Warsaw ("Director of the TIO"). The duration of the proceedings was extended by the Director of the Tax Inspection Office a number of times. The proceedings are to be closed on 28 April 2018.

36. Accruals, deferred income and government grants

	As at 31 December 2017	As at 31 December 2016
Unused holidays	2 587	2 577
Bonuses	6 499	10 867
Accruals relating to post-service benefits for members of the Management Board/key management personnel	1 764	2 230
Accruals relating to payments in lieu of jubilee bonuses	–	4 356
Other	3 744	1 473
Total	**14 594**	**21 503**
Non-current	–	170
Current	14 594	21 333

37. Liabilities to suppliers

As at 31 December 2017, the value of the said liabilities to the subsidiaries TAURON Wytwarzanie S.A. and TAURON Sprzedaż Sp. z o.o. was the highest: PLN 163 952 thousand and PLN 87 255 thousand, respectively. As at 31 December 2016, liabilities to the subsidiaries TAURON Wytwarzanie S.A. and TAURON Wydobycie S.A. were the highest and totalled PLN 106 417 thousand and PLN 98 682 thousand, respectively.

38. Other financial liabilities

	As at 31 December 2017	As at 31 December 2016
Liabilities arising from the TCG	34 836	75 662
Margin deposits	7 163	13 106
Commissions related to securities	5 889	8 020
Bid bonds, deposits and collateral received	5 400	5 681
Wages and salaries, deductions on wages and salaries as well as other employee related liabilities	6 424	3 770
Other	23 004	33 438
Total	**82 716**	**139 677**
Non-current	20 126	27 918
Current	62 590	111 759

(in PLN '000)

39. Liabilities arising from taxes and charges

	As at 31 December 2017	As at 31 December 2016
Corporate Income Tax	37 629	–
Personal Income Tax	1 878	1 484
VAT	25 385	15 850
Excise	880	–
Social security	4 311	2 846
Other	36	29
Total	**70 119**	**20 209**

An increase in liabilities arising from taxes and charges results mainly from a rise in CIT liabilities in the Tax Capital Group. As at 31 December 2017, the Tax Capital Group had income tax liabilities of PLN 37 629 thousand, which has been discussed in more detail in Note 16.4 to these financial statements. As at 31 December 2016, the Tax Capital Group reported income tax receivables of PLN 83 153 thousand.

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

Tax reports and other matters (e.g. customs or foreign currency transactions) may be audited by authorities competent to impose substantial penalties and fines, whereas any additional tax liabilities assessed during such audits have to be paid together with interest. Consequently, the figures presented and disclosed in these financial statements may change in future if a final decision is issued by tax inspection authorities.

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

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

(in PLN '000)

EXPLANATORY NOTES TO THE STATEMENT OF CASH FLOWS

40. Significant items of the statement of cash flows

40.1. Cash flows from operating activities

Changes in working capital

	Year ended 31 December 2017	Year ended 31 December 2016
Change in receivables	105 267	(254 506)
Change in inventories	86 371	(35 307)
Change in payables excluding loans and borrowings	(59 096)	21 190
Change in other non-current and current assets	11 211	60 110
Change in deferred income, government grants and accruals	(6 909)	1 867
Change in provisions	(194 062)	75 897
Change in working capital	**(57 218)**	**(130 749)**

40.2. Cash flows from investing activities

Purchase of bonds

Payments to purchase bonds, in the amount of PLN 350 000 thousand, are related to purchases of intra-group bonds issued by the following subsidiaries:

- TAURON Wytwarzanie S.A., totalling PLN 250 000 thousand;
- TAURON Wydobycie S.A., totalling PLN 100 000 thousand.

Purchase of shares

Payments to acquire shares of PLN 6 169 590 thousand were mainly related to the Company's transfer of funds to increase the issued capital of subsidiaries:

- Nowe Jaworzno Grupa TAURON Sp. z o.o., totalling PLN 3 400 000 thousand;
- TAURON Ekoenergia Sp. z o.o., totalling PLN 1 000 000 thousand;
- TAURON Dystrybucja S.A., totalling PLN 1 000 000 thousand;
- TAURON Ciepło Sp. z o.o., totalling PLN 600 000 thousand;
- TAURON Wydobycie S.A., totalling PLN 160 000 thousand;
- Magenta Grupa TAURON Sp. z o.o., totalling PLN 9 000 thousand;
- Marselwind Sp. z o.o., totalling PLN 200 thousand.

Loans granted

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

Redemption of bonds

Proceeds from redemption of bonds, in the amount of PLN 3 547 110 thousand, are related to redemption of intra-group bonds issued by the following subsidiaries:

- Nowe Jaworzno Grupa TAURON Sp. z o.o., totalling PLN 2 533 850 thousand;
- TAURON Ciepło Sp. z o.o., totalling PLN 598 260 thousand;
- TAURON Wytwarzanie S.A., totalling PLN 200 000 thousand;
- TAURON Wydobycie S.A., totalling PLN 100 000 thousand;
- TAURON Obsługa Klienta Sp. z o.o., totalling PLN 85 000 thousand;
- TAURON Dystrybucja S.A., totalling PLN 30 000 thousand.

(in PLN '000)

Repayment of loans granted

Loan repayment of PLN 1 000 000 thousand constitutes partial repayment of a loan granted to the subsidiary TAURON Ekoenergia Sp. z o.o., which has been discussed in more detail in Note 25 to these financial statements.

Interest received

	Year ended 31 December 2017	Year ended 31 December 2016
Interest received in relation to debt securities	642 017	472 445
Interest received in relation to loans granted	–	1 681
Total	**642 017**	**474 126**

40.3. Cash flows from financing activities

Repayment of loans and borrowings

The expenditure on repayment of loans and borrowings in the year ended 31 December 2017 totalling PLN 175 695 thousand is the repayment of:

- the loan installments to the European Investment Bank, totalling PLN 147 568 thousand;
- the loan obtained from the subsidiary TAURON Sweden Energy AB (publ), totalling PLN 28 127 thousand.

Redemption of debt securities

Payments on the redemption of debt securities in the year ended 31 December 2017 resulted from the redemption of a tranche of bonds with the par value of PLN 1 650 000 thousand under a bond issue scheme of November 2015, which has been discussed in more detail in Note 33.1 to these financial statements.

Interest paid

	Year ended 31 December 2017	Year ended 31 December 2016
Interest paid in relation to debt securities	(221 832)	(271 220)
Interest paid in relation to loans	(41 295)	(51 205)
Interest paid in relation to borrowings	(1 446)	(27 644)
Interest paid in relation to the finance lease	(650)	(603)
Exchange differences on loans and borrowings	–	(475)
Total	**(265 223)**	**(351 147)**

Issue of debt securities

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

- the issue of eurobonds totalling PLN 2 107 462 thousand, which has been discussed in more detail in Note 33.1 to these financial statements;
- the issue of tranches of bonds with the total par value of PLN 600 000 thousand under a bond issue scheme of November 2015, which has been discussed in more detail in Note 33.1 to these financial statements.

(in PLN '000)

FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

41. Financial instruments

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

Categories and classes of financial assets	Note	As at 31 December 2017		As at 31 December 2016	
		Carrying amount	Fair value	Carrying amount	Fair value
1 Financial assets at fair value through profit or loss, held for trading		**106 292**	**106 292**	**45 092**	**45 092**
Derivative instruments	23	4 934	4 934	19 776	19 776
Investment fund units	24	101 358	101 358	25 316	25 316
2 Financial assets available for sale		**39 244**		**29 703**	
Long-term shares	21	39 244		29 703	
3 Loans and receivables		**8 228 015**	**8 072 480**	**12 054 366**	**11 920 587**
Receivables from buyers	27	719 133	719 133	840 656	840 656
Bonds	22	6 572 696	6 506 729	9 858 382	9 814 505
Loans granted under cash pool agreement	33.4	190 526	190 526	15 850	15 850
Other loans granted	25	712 654	623 086	1 307 916	1 218 014
Other financial receivables		33 006	33 006	31 562	31 562
4 Financial assets excluded from the scope of IAS 39		**20 873 435**		**14 844 715**	
Shares in subsidiaries	21	20 457 583		14 428 863	
Shares in jointly-controlled entities	21	415 852		415 852	
5 Hedging derivative instruments	23	**28 482**	**28 482**	**36 641**	**36 641**
6 Cash and cash equivalents	30	**721 577**	**721 577**	**198 090**	**198 090**
Total financial assets, of which in the statement of financial position:		**29 997 045**		**27 208 607**	
Non-current assets		**27 334 757**		**25 820 473**	
Shares		20 912 679		14 874 418	
Bonds		6 009 920		9 615 917	
Loans granted		382 989		1 292 800	
Derivative instruments		26 445		35 814	
Other financial assets		2 724		1 524	
Current assets		**2 662 288**		**1 388 134**	
Receivables from buyers		719 133		840 656	
Bonds		562 776		242 465	
Loans granted		520 191		30 966	
Derivative instruments		6 971		20 603	
Other financial assets		131 640		55 354	
Cash and cash equivalents		721 577		198 090	

Categories and classes of financial liabilities	Note	As at 31 December 2017		As at 31 December 2016	
		Carrying amount	Fair value	Carrying amount	Fair value
1 Financial liabilities at fair value through profit or loss, held for trading		**14 184**	**14 184**	**560**	**560**
Derivative instruments	23	14 184	14 184	560	560
2 Financial liabilities measured at amortized cost		**12 670 253**	**12 699 476**	**10 774 316**	**10 808 300**
Arm's length loans, of which:		4 140 424	4 135 000	3 203 740	3 237 724
Liability under the cash pool loan	33.4	2 377 034	2 377 034	1 245 489	1 245 489
Loans from the European Investment Bank	33.2	1 042 110	1 044 424	1 190 501	1 193 410
Loans from the subsidiary	33.3	721 280	713 542	767 750	798 825
Overdraft	33.5	93 502	93 502	15 131	15 131
Bonds issued	33.1	7 940 346	7 974 993	6 942 131	6 942 131
Liabilities to suppliers	37	413 265	413 265	473 637	473 637
Other financial liabilities	38	82 586	82 586	139 177	139 177
Liabilities due to purchases of fixed and intangible assets	38	130	130	500	500
3 Liabilities under guarantees, factoring and excluded from the scope of IAS 39		**23 945**	**23 945**	**26 974**	**26 974**
Liabilities under finance leases	33.6	23 945	23 945	26 974	26 974
Total financial liabilities, of which in the statement of financial position:		**12 708 382**		**10 801 850**	
Non-current liabilities		**9 497 538**		**8 781 965**	
Debt		9 472 454		8 754 047	
Other financial liabilities		20 126		27 918	
Derivative instruments		4 958		–	
Current liabilities		**3 210 844**		**2 019 885**	
Debt		2 725 763		1 433 929	
Liabilities to suppliers		413 265		473 637	
Derivative instruments		9 226		560	
Other financial liabilities		62 590		111 759	

(in PLN '000)

Derivative financial instruments measured at fair value as at the end of the reporting period and classified as assets and liabilities measured at fair value through profit or loss, or designated as hedging derivatives (subject to hedge accounting), have been measured in line with the method described in Note 9.9 to these financial statements. Fair value hierarchy disclosures are provided in Note 23 to these financial statements. Measurement of investment fund units has been classified to Level 1 in the fair value hierarchy.

Financial instruments classified to other categories of financial instruments:

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

  Consequently, the fair value of the instruments in question has been disclosed in the tables above at their carrying amount.
- The Company did not disclose the fair value as at the end of the reporting period of shares in companies not quoted in active markets, categorised to financial assets available for sale. They are measured at cost less impairment losses as at the end of the reporting period. Following the adoption of IFRS 9 *Financial Instruments* as from 1 January 2018, the Company estimated the fair value of the above shares as at that date, which has been discussed in more detail in Note 7 to these financial statements. In accordance with the Company's accounting policy, shares in subsidiaries and jointly-controlled entities (joint ventures) – financial assets excluded from the scope of IAS 39 *Financial Instruments: Recognition and Measurement* – are also measured at cost less impairment losses.

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

For the year ended 31 December 2017

	Assets / liabilities at fair value through profit or loss	Financial assets available for sale	Loans and receivables	Financial liabilities measured at amortized cost	Hedging instruments	Financial assets / liabilities excluded from the scope of IAS 39	Total
Dividends	–	2 858	–	–	–	557 974	**560 832**
Interest income/(expense)	19 321	–	456 413	(335 282)	1 525	(650)	**141 327**
Commissions	–	–	–	(19 068)	–	–	**(19 068)**
Exchange differences	(2 483)	–	1 689	128 270	–	–	**127 476**
Impairment / revaluation	(11 820)	–	(32)	–	–	(134 372)	**(146 224)**
Other	(4 866)	–	–	–	–	–	**(4 866)**
Net financial income/(costs)	**152**	**2 858**	**458 070**	**(226 080)**	**1 525**	**422 952**	**659 477**
Revaluation	(13 514)	–	34	–	–	–	**(13 480)**
Gain/(loss) on realized commodity derivative instruments	8 737	–	–	–	–	–	**8 737**
Net operating income/(costs)	**(4 777)**	**–**	**34**	**–**	**–**	**–**	**(4 743)**
Remeasurement of IRS	–	–	–	–	(8 159)	–	**(8 159)**
Other comprehensive income	**–**	**–**	**–**	**–**	**(8 159)**	**–**	**(8 159)**

(in PLN '000)

For the year ended 31 December 2016

	Assets / liabilities at fair value through profit or loss	Financial assets available for sale	Loans and receivables	Financial liabilities measured at amortized cost	Hedging instruments	Financial assets / liabilities excluded from the scope of IAS 39	Total
Dividends	–	2 201	–	–	–	1 482 951	**1 485 152**
Interest income/(expense)	6 371	–	504 355	(275 686)	(80 658)	(603)	**153 779**
Commissions	–	–	–	(18 814)	–	–	**(18 814)**
Exchange differences	(2 148)	–	183	(27 704)	–	–	**(29 669)**
Impairment / revaluation	14 495	–	(197 840)	–	–	(1 412 443)	**(1 595 788)**
Gain/(loss) on disposal of investments	–	1 051	–	–	–	(88 311)	**(87 260)**
Other	(54)	–	–	–	–	–	**(54)**
Net financial income/(costs)	**18 664**	**3 252**	**306 698**	**(322 204)**	**(80 658)**	**(18 406)**	**(92 654)**
Revaluation	15 982	–	1 543	–	–	–	**17 525**
Gain/(loss) on realized commodity derivative instruments	(34 365)	–	–	–	–	–	**(34 365)**
Net operating income/(costs)	**(18 383)**	**–**	**1 543**	**–**	**–**	**–**	**(16 840)**
Remeasurement of IRS	–	–	–	–	127 252	–	**127 252**
Other comprehensive income	**–**	**–**	**–**	**–**	**127 252**	**–**	**127 252**

Impairment losses/revaluation

Following the performance of impairment tests for shares, bonds and loans as at 31 December 2017 and as at 30 June 2017, which has been discussed in more detail in Note 21 to these financial statements, the Company revalued its shares in subsidiaries.

Revaluation recognized within finance income (costs) affected mostly the following classes of financial instruments:

- shares in subsidiaries – impairment losses recognized by the Company exceeded those which were reversed by PLN 134 372 thousand;
- units in investment funds – a gain on measurement of PLN 1 356 thousand;
- derivative instruments – a loss on measurement of PLN 13 176 thousand.

Costs of derivative instruments used as hedges

In the year ended 31 December 2017, gains/losses from valuation of an IRS hedging instrument subject to hedge accounting were recognized within other comprehensive income. In 2017, the change in valuation was PLN (8 159) thousand. Gains/losses from revaluation of the hedging instrument, recognized in other comprehensive income, were recognized in profit/loss for the period as finance costs resulting from interest on issued bonds when the hedged item, i.e. interest on bonds, affected the profit/loss for the period. The amount of PLN 1 525 thousand was recognized in profit/loss for the period as a payment relating to a realized hedge for past interest periods.

42. Finance and financial risk management

The TAURON Group has implemented the policy for management of specific risks in the area of finance, which defines the strategy for management of the currency and interest rate risk. The policy has also introduced hedge accounting in the Group, which lays down the principles and defines the types of hedge accounting, along with the accounting treatment of hedging instruments and hedged items, to be applied as part of hedge accounting under IFRS. The policy for specific risk management in the area of finance and hedge accounting principles are applicable to the cash flow risk.

Hedge accounting

As at 31 December 2017, the Company was a party to hedging transactions covered by the policy for specific risk management in the area of finance and subject to hedge accounting. The Company hedges a portion of the interest rate risk inherent in cash flows related to issued bonds, which has been discussed in more detail in Note 23 to these financial statements.

Risks related to financial instruments which the Company is exposed to in its business operations:

- credit risk;
- liquidity risk;

- market risk, including:
  - interest rate risk;
  - currency risk;
  - raw material and commodity price risk related to commodity derivative instruments and price risk related to units held by the Company.

42.1. Credit risk

Credit risk regards potential credit events that may have the form of: a contractor's insolvency, partial repayment of receivables, a material payment delay or another unpredicted breach of contract terms.

The credit risk related to financial assets of the Company results from the inability to make payment by the other party to the agreement and the maximum exposure is equal to the carrying amount of these instruments.

Categories of financial assets held by the Company that give rise to credit risk exposure with different characteristics include:

- receivables from buyers;
- bonds;
- loans granted;
- other financial receivables;
- cash and cash equivalents;
- derivatives;
- units in investment funds;
- other financial assets.

42.1.1. Credit risk related to receivables from buyers

The Company monitors credit risk related to its operations on an ongoing basis. In 2017, the Company was exposed to counterparty credit risk resulting from commercial contracts. To mitigate the risk, as part of the regular analysis of reliability and financial standing of its counterparties, in justified cases the Company required security.

Receivables from buyers include amounts due from subsidiaries and corporate buyers from outside the Group. They do not bear any interest and mature within seven to thirty days, depending on the contract. Sales transactions are only entered into with clients subject to a verification procedure. This – in the opinion of the management – eliminates any additional credit risk, over the level defined by the allowance for bad debts applied to the Company's trade receivables.

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

42.1.2. Credit risk related to other financial assets

According to the Company credit risk exposure of other categories of financial assets is insignificant. Bonds acquired by the Company and loans granted concern mostly transactions with related parties. The items in question had not been overdue as at the end of the reporting period.

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

The entities the Company concludes derivative transactions with in order to hedge against interest rate and currency risk operate in the financial sector. They are Polish banks with high financial rating, sufficient equity and strong, stable market position.

(in PLN '000)

42.2. Liquidity risk

The Company maintains a balance between continuity, flexibility and cost of financing by using various sources of funding, which enable management of liquidity risk and effective mitigation of risk consequences.

Liquidity is managed at the Group level. The TAURON Group has adopted *Liquidity management policy for the TAURON Group*, which facilitates optimization of liquidity management at the TAURON Group and reduces the risk of liquidity loss by the Group and each company from the TAURON Group.

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

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

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

Ageing structure of financial liabilities presenting undiscounted payments under applicable agreements has been presented below.

Financial liabilities as at 31 December 2017

	Carrying amount	Contractual undiscounted payments	Including contractual undiscounted payments maturing during the period (from the reporting date)					
			less than 3 months	3–12 months	1–2 years	2–3 years	3–5 years	over 5 years
Financial liabilities other than derivative instruments								
Interest-bearing loans and borrowings (including bonds issued)	**12 174 272**	**(14 560 425)**	(2 537 566)	(413 335)	(2 322 897)	(2 189 338)	(981 420)	(6 115 869)
Liabilities to suppliers	**413 265**	**(413 265)**	(413 265)	–	–	–	–	–
Liabilities due to purchases of fixed and intangible assets	**130**	**(130)**	(130)	–	–	–	–	–
Other financial liabilities	**82 586**	**(82 586)**	(57 182)	(5 281)	(2 500)	(2 500)	(5 000)	(10 124)
Liabilities under finance lease	**23 945**	**(24 142)**	(1 474)	(22 668)	–	–	–	–
Derivative financial liabilities								
Derivative instruments – commodity	**4 539**	**(4 424)**	–	(4 424)	–	–	–	–
Derivative instruments – currency	**346**	**(346)**	(275)	(71)	–	–	–	–
Derivate instruments – CCIRS	**9 299**	**(47 125)**	–	(4 694)	(4 694)	(4 748)	(9 427)	(23 562)
Total	**12 708 382**	**(15 132 443)**	**(3 009 892)**	**(450 473)**	**(2 330 091)**	**(2 196 586)**	**(995 847)**	**(6 149 555)**

(in PLN '000)

Financial liabilities as at 31 December 2016

	Carrying amount	Contractual undiscounted payments	Including contractual undiscounted payments maturing during the period (from the reporting date)					
			less than 3 months	3–12 months	1–2 years	2–3 years	3–5 years	over 5 years
Financial liabilities other than derivative instruments								
Interest-bearing loans and borrowings (including bonds issued)	**10 161 002**	**(12 283 976)**	(1 297 437)	(399 745)	(475 139)	(2 290 161)	(3 668 348)	(4 153 146)
Liabilities to suppliers	**473 637**	**(473 637)**	(473 616)	(21)	–	–	–	–
Liabilities due to purchases of fixed and intangible assets	**500**	**(500)**	(500)	–	–	–	–	–
Other financial liabilities	**139 177**	**(139 177)**	(110 621)	(638)	(7 918)	(2 500)	(5 000)	(12 500)
Liabilities under finance lease	**26 974**	**(27 821)**	(1 021)	(3 084)	(23 716)	–	–	–
Derivative financial liabilities								
Derivate instruments – commodity	**560**	**(538)**	–	(538)	–	–	–	–
Total	**10 801 850**	**(12 925 649)**	**(1 883 195)**	**(404 026)**	**(506 773)**	**(2 292 661)**	**(3 673 348)**	**(4 165 646)**

As at 31 December 2017, the Company had granted guarantees, sureties and other forms of collateral to related parties in the total amount of PLN 825 876 thousand (excluding registered and financial pledges on shares) versus PLN 1 338 438 thousand as at 31 December 2016, which has been discussed in more detail in Note 44 to these financial statements. As at 31 December 2017, a corporate guarantee granted to a subsidiary to collateralize bonds issued by the entity up to EUR 168 000 thousand (PLN 700 711 thousand) was the key item. The guarantee is valid in the entire bond period, i.e. until the redemption date – 3 December 2029.

The guarantees and sureties granted by the Company constitute contingent liabilities and do not considerably affect the liquidity risk of the Company.

42.3. Market risk

Market risk results from possible adverse impact of fluctuations of the fair value of financial instruments or related future cash flows due to market price changes on the Company's performance.

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

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

42.3.1. Interest rate risk

The Company is exposed to the risk of interest rate changes related to floating interest rate borrowings acquired and investing in assets with floating and fixed interest rates. The Company is also exposed to lost benefit risk related to a decrease in interest rates in the case of fixed interest rate debt.

The purpose of interest rate risk management is to limit negative effects of market interest rate fluctuations on the Company's cash flows to an acceptable level and to minimize finance costs. In order to hedge interest rate risk related to floating-rate bonds issued, the Company entered into interest rate swap contracts (IRS), which has been discussed in more detail in Note 23 to these financial statements.

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

(in PLN '000)

Financial instruments by interest rate type as at 31 December 2017

Financial instruments	Fixed interest rate	Floating interest rate	Total
Financial assets			
Bonds	6 572 696	–	**6 572 696**
Loans granted	142 223	760 957	**903 180**
Cash and cash equivalents	–	721 577	**721 577**
Derivative instruments – IRS	28 482	–	**28 482**
Financial liabilities			
Bank overdrafts	–	93 502	**93 502**
Arm's length loans	1 763 390	2 377 034	**4 140 424**
Bonds issued	4 984 389	2 955 957	**7 940 346**
Obligations under finance leases	–	23 945	**23 945**
Derivative instruments – CCIRS	9 299	–	**9 299**

Financial instruments by interest rate type as at 31 December 2016

Financial instruments	Fixed interest rate	Floating interest rate	Total
Financial assets			
Bonds	9 858 382	–	**9 858 382**
Loans granted*	1 051 849	271 917	**1 323 766**
Cash and cash equivalents	–	198 090	**198 090**
Derivative instruments – IRS	36 641	–	**36 641**
Financial liabilities			
Bank overdrafts	–	15 131	**15 131**
Arm's length loans	1 958 251	1 245 489	**3 203 740**
Bonds issued	2 938 091	4 004 040	**6 942 131**
Obligations under finance leases	–	26 974	**26 974**

** The amount of a loan granted to a subsidiary on which an impairment loss has been recognized has been presented in the table above on a net basis, i.e. less the impairment loss.*

Other financial instruments of the Company which have not been presented in the tables above bear no interest and therefore are not exposed to the interest rate risk.

42.3.2. Currency risk

The Company's exposure to currency risk by financial instrument class as at 31 December 2017 and 31 December 2016 has been presented below.

Currency position as at 31 December 2017

	Total carrying amount in PLN	EUR		USD		GBP		CZK	
		in currency	in PLN	in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets									
Receivables from buyers	719 133	250	1 043	–	–	–	–	–	–
Other financial receivables	33 006	3 321	13 852	–	–	–	–	–	–
Cash and cash equivalents	721 577	2 577	10 748	314	1 093	485	2 280	11 003	1 796
Derivatives (assets)	33 416	1 169	4 876	16	58	–	–	–	–
Total	**1 507 132**	**7 317**	**30 519**	**330**	**1 151**	**485**	**2 280**	**11 003**	**1 796**
Financial liabilities									
Arm's length loans	4 140 424	172 932	721 282	–	–	–	–	–	–
Overdraft	93 502	22 069	92 048	418	1 454	–	–	–	–
Bonds issued	7 940 346	692 073	2 886 567	–	–	–	–	–	–
Liabilities to suppliers	413 265	65	271	3	10	1	5	–	–
Other financial liabilities	82 586	1 717	7 161	–	–	–	–	–	–
Derivatives (liabilities)	14 184	1 061	4 425	33	114	–	–	–	–
Total	**12 684 307**	**889 917**	**3 711 754**	**454**	**1 578**	**1**	**5**	**–**	**–**
Net currency position		**(882 600)**	**(3 681 235)**	**(124)**	**(427)**	**484**	**2 275**	**11 003**	**1 796**

(in PLN '000)

Currency position as at 31 December 2016

	Total carrying amount in PLN	EUR		USD		GBP	
		in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets							
Receivables from buyers	840 656	12	53	–	–	–	–
Other financial receivables	31 562	342	1 515	–	–	–	–
Cash and cash equivalents	198 090	5 983	26 469	306	1 279	499	2 567
Derivatives (assets)	56 417	3 649	16 143	100	416	–	–
Total	**1 126 725**	**9 986**	**44 180**	**406**	**1 695**	**499**	**2 567**
Financial liabilities							
Arm's length loans	3 203 740	173 542	767 750	–	–	–	–
Overdraft	15 131	3 032	13 415	410	1 716	–	–
Bonds issued	6 942 131	190 105	841 023	–	–	–	–
Liabilities to supplier	473 637	32	144	12	50	–	–
Other financial liabilities	139 177	2 958	13 088	94	393	2	10
Derivatives (liabilities)	560	122	538	5	22	–	–
Total	**10 774 376**	**369 791**	**1 635 958**	**521**	**2 181**	**2**	**10**
Net currency position		**(359 805)**	**(1 591 778)**	**(115)**	**(486)**	**497**	**2 557**

In 2017 and in 2016, TAURON Polska Energia S.A. used forward contracts for currency risk management purposes. The objective of these transactions is to hedge currency risk related to the operations of the Company. The Company did not use hedge accounting to hedge currency risk. As at 31 December 2017, liabilities arising from valuation of FX forwards held by the Company amounted to PLN 346 thousand (versus assets of PLN 3 217 thousand as at 31 December 2016).

In the year ended 31 December 2017, the Company entered into CCIRS transactions, whose fair value measurement is exposed to the risk of changes in the EUR/PLN exchange rate. These transactions are not subject to hedge accounting. As at 31 December 2017, the amount from valuation of CCIRS was PLN (9 299) thousand, which has been discussed in more detail in Note 23 to these financial statements.

42.3.3. Raw material and commodity price risk related to commodity derivative instruments and price risk related to units held by the Company

The Company concludes derivative contracts, with underlying instruments being commodities and raw materials. The Company's exposure to 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 of prices of the underlying raw materials/commodities. This way the Company hedges the price risk related to commodity derivative instruments by entering to opposite transaction. The risk is limited to open long and short positions concerning a given commodity or raw material.

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

As at 31 December 2017, the Company held units in investment funds with the carrying amount of PLN 101 358 thousand. As they are measured at fair value at the end of the reporting period, they are exposed to the price risk.

42.3.4. Market risk – sensitivity analysis

As for financial instruments held, the Company is exposed mostly to the risk of EUR/PLN, USD/PLN and GBP/PLN exchange rate changes as well as changes in reference interest rates for PLN, EUR and USD.

The analysis of sensitivity to changes in market risk factors is conducted by means of a scenario analysis. The Company relies on expert scenarios reflecting its judgment concerning the behaviour of individual market risk factors in the future.

The scenario analyses presented herein are aimed at examining the effect of changes in market risk factors on the Company's financial performance. The scope of the analysis includes only those items which meet the IFRS definition of financial instruments.

(in PLN '000)

Presented below is the sensitivity analysis for the interest rate, currency and price risks to which the Company is exposed as at the end of the reporting period, along with the effect of potential changes in individual risk factors on the gross profit/loss as well as other comprehensive income (gross), by class of financial assets and liabilities.

Interest rate risk sensitivity analysis

The interest rate risk sensitivity analysis is conducted by the Company 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 Company to the interest rate risk as at the end of the reporting period.

The Company identifies its exposure to the risk of changes in WIBOR, EURIBOR and LIBOR USD interest rates. As at 31 December 2017, its exposure to the risk of changes in LIBOR USD was immaterial, while the sensitivity analysis performed as at 31 December 2016 did not focus on changes in EURIBOR and LIBOR USD as their effect was considered insignificant. The tables below present sensitivity of the gross profit/loss as well as other comprehensive income (gross) 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.

For the year ended 31 December 2017

Classes of finacial instruments	31 December 2017		Sensitivity analysis for interest rate risk as at 31 December 2017					
			WIBOR				EURIBOR	
			WIBOR + 43 bp		WIBOR - 43 bp		EURIBOR + 1 bp	EURIBOR - 1 bp
	Carrying amount	Value at risk	*Profit/(Loss)*	*Other comprehensive income*	*Profit/(Loss)*	*Other comprehensive income*	*Profit/(Loss)*	
Loans granted	903 180	760 957	3 272	–	(3 272)	–	–	–
Cash and cash equivalents	721 577	721 577	3 034	–	(3 034)	–	1	(1)
Derivatives (assets)	33 416	28 482	–	21 217	–	(21 217)	–	–
Bank overdrafts	93 502	93 502	–	–	–	–	(9)	9
Arm's length loans	4 140 424	2 377 034	(10 221)	–	10 221	–	–	–
Bonds issued	7 940 346	5 053 777	(21 731)	–	21 731	–	–	–
Obligations under finance leases	23 945	23 945	(103)	–	103	–	–	–
Derivates (liabilities)	14 184	9 299	5 995	–	(5 995)	–	(146)	146
Total			**(19 754)**	**21 217**	**19 754**	**(21 217)**	**(154)**	**154**

The exposure to risk as at 31 December 2017 is representative for the Company's exposure to risk during the annual period preceding the aforementioned date, except for material transactions made at the end of 2017. They concern derivative instruments (liabilities), including CCIRS transactions entered into in November and December 2017, which are sensitive to both changes in WIBOR and EURIBOR interest rates. CCIRS instruments have been discussed in more detail in Note 23 to these financial statements.

(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			
			WIBOR + 60 bp		WIBOR -60 bp	
	Carrying amount	Value at risk	*Profit/(Loss)*	*Other comprehensive income*	*Profit/(Loss)*	*Other comprehensive income*
Loans granted	1 323 766	271 917	1 632	–	(1 632)	–
Cash and cash equivalents	198 090	198 090	1 007	–	(1 007)	–
Derivatives (assets)	56 417	36 641	–	40 992	–	(40 992)
Arm's length loans	3 203 740	1 245 489	(7 473)	–	7 473	–
Bonds issued	6 942 131	6 101 108	(36 607)	–	36 607	–
Obligations under finance leases	26 974	26 974	(162)	–	162	–
Total			**(41 603)**	**40 992**	**41 603**	**(40 992)**

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

Currency risk sensitivity analysis

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 Company identifies its exposure to foreign currency risk related to EUR/PLN, USD/PLN and GBP/PLN exchange rates, and additionally the CZK/PLN exchange rate in the year ended 31 December 2017. The tables below present sensitivity of the gross profit/loss to reasonably possible changes in the EUR/PLN, USD/PLN, GBP/PLN and CZK/PLN 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 2017

Classes of finacial instruments	31 December 2017		Sensitivity analysis for currency risk as at 31 December 2017							
			EUR/PLN		USD/PLN		GBP/PLN		CZK/PLN	
	Carrying amount	Value at risk	exchange rate EUR/PLN +6.2%	exchange rate EUR/PLN -6.2%	exchange rate USD/PLN +9.76%	exchange rate USD/PLN -9.76%	exchange rate GBP/PLN +9.35%	exchange rate GBP/PLN -9.35%	exchange rate CZK/PLN +6.34%	exchange rate CZK/PLN -6.34%
			Profit/(Loss)		*Profit/(Loss)*		*Profit/(Loss)*		*Profit/(Loss)*	
Receivables from buyers	719 133	1 043	65	(65)	–	–	–	–	–	–
Other financial receivables	33 006	13 852	859	(859)	–	–	–	–	–	–
Cash and cash equivalents	721 577	15 917	667	(667)	107	(107)	213	(213)	114	(114)
Derivatives (assets)	33 416	4 934	302	(302)	6	(6)	–	–	–	–
Overdraft	93 502	93 502	(5 705)	5 705	(142)	142	–	–	–	–
Arm's length loans	4 140 424	721 282	(44 720)	44 720	–	–	–	–	–	–
Bonds issued	7 940 346	2 886 567	(178 967)	178 967	–	–	–	–	–	–
Liabilities to suppliers	413 265	286	(17)	17	(1)	1	–	–	–	–
Other financial liabilities	82 586	7 161	(444)	444	–	–	–	–	–	–
Derivatives (liabilities)	14 184	14 184	19 394	(19 394)	(11)	11	–	–	–	–
Total			**(208 566)**	**208 566**	**(41)**	**41**	**213**	**(213)**	**114**	**(114)**

The exposure to risk as at 31 December 2017 is representative for the Company's exposure to risk during the annual period preceding the aforementioned date, except for material transactions made in the second half of 2017. These include issued bonds, consisting of eurobonds issued by the Company in July 2017, which has been discussed in more detail in Note 33.1 to these financial statements, and derivatives (liabilities), consisting of CCIRS transactions entered into in November and December 2017, which has been discussed in more detail in Note 23 to these financial statements.

(in PLN '000)

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		USD/PLN		GBP/PLN	
	Carrying amount	Value at risk	exchange rate EUR/PLN +7.8%	exchange rate EUR/PLN -7.8%	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/(Loss)		*Profit/(Loss)*		*Profit/(Loss)*	
Receivables from buyers	840 656	53	4	(4)	–	–	–	–
Other financial receivables	31 562	1 515	118	(118)	–	–	–	–
Cash and cash equivalents	198 090	30 315	2 065	(2 065)	177	(177)	296	(296)
Derivatives (assets)	56 417	19 776	6 624	(6 624)	57	(57)	–	–
Overdraft	15 131	15 131	(1 046)	1 046	(237)	237	–	–
Arm's length loans	3 203 740	767 750	(59 884)	59 884	–	–	–	–
Bonds issued	6 942 131	841 023	(65 600)	65 600	–	–	–	–
Liabilities to suppliers	473 637	194	(11)	11	(7)	7	–	–
Other financial liabilities	139 177	13 491	(1 021)	1 021	(54)	54	(1)	1
Derivatives (liabilities)	560	560	(42)	42	(3)	3	–	–
Total			**(118 793)**	**118 793**	**(67)**	**67**	**295**	**(295)**

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

Analysis of sensitivity to commodity price risk related to commodity derivative instruments

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

For the year ended 31 December 2017

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

For the year ended 31 December 2016

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

Unit 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 Company, the Company 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.

(in PLN '000)

For the year ended 31 December 2017

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

For the year ended 31 December 2016

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

43. Operational risk

The Company is 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 in the open market position.

Commercial operational risk is managed at the level of the TAURON Group, which has been discussed in more detail in Notes 45 and 46 to the consolidated financial statements of the TAURON Polska Energia S.A. Capital Group for the year ended 31 December 2017. The Company manages its commercial risk following the Commercial risk management policy developed and adopted in the TAURON Group.

The Company's exposure to the risk of prices of goods reflects the volume of electricity and gas acquired. The volume and cost of electricity and gas acquired have been presented below.

Fuel type	Unit	2017		2016	
		Volume	Purchase cost	Volume	Purchase cost
Electricity	MWh	42 245 897	6 962 695	41 966 994	7 152 963
Gas	MWh	2 561 368	201 315	3 084 545	249 878
Total			**7 164 010**		**7 402 841**

As for trading in coal, the Company is not exposed to the price risk, as it acts as an agent generating revenue from agency services only.

(in PLN '000)

OTHER INFORMATION

44. Contingent liabilities

As at 31 December 2017 and 31 December 2016 the Company's contingent liabilities arise mainly from collateral and guarantees granted to related parties. Contingent liabilities recognized as of below:

Type of contingent liability	Company in respect of which contingent liability has been granted	Beneficiary	As at 31 December 2017			As at 31 December 2016	
			Validity	EUR	PLN	EUR	PLN
corporate guarantee	TAURON Sweden Energy AB (publ)	holders of bonds issued by TAURON Sweden Energy AB (publ)	3.12.2029	168 000	700 711	168 000	743 232
corporate guarantee	TAURON Ekoenergia Sp. z o.o.	Business entities and buyers being parties to contracts with TAURON Ekoenergia Sp. z o.o. based on the electricity trading licence issued by the President of the Energy Regulatory Office	31.12.2030		16 400		–
blank promissory note with a promissory note declaration	TAURON Wytwarzanie S.A.	Regional Fund for Environmental Protection and Water Management in Katowice	15.12.2022		40 000		40 000
	TAURON Ciepło Sp. z o.o.		15.12.2022		30 000		30 000
financing commitment	TAURON Ciepło Sp. z o.o.	Regional Fund for Environmental Protection and Water Management in Katowice			–		178 300
guarantees issued by The Bank of Tokyo-Mitsubishi UFJ, Ltd.	Elektrociepłownia Stalowa Wola S.A.	Bank Polska Kasa Opieki S.A.			–		74 992
		European Investment Bank			–		156 000
		European Bank for Reconstruction and Development			–		83 494
registered pledges and financial pledge of shares in TAMEH HOLDING Sp. z o.o.	TAMEH Czech s.r.o. TAMEH POLSKA Sp. z o.o.	RAIFFEISEN BANK INTERNATIONAL AG	31.12.2028*		415 852		415 852
surety contract	Kopalnia Wapienia Czatkowice Sp. z o.o.	Regional Fund for Environmental Protection and Water Management in Kraków	15.06.2021		914		930
surety contract	TAURON Wydobycie S.A.	Millennium Leasing Sp. z o.o.			–		2 900
surety contract	Nowe Jaworzno Grupa TAURON Sp. z o.o.	Fund Advisors	28.09.2025		2 350		–
surety contract	TAURON Wytwarzanie S.A.	Polskie Sieci Elektroenergetyczne S.A.	4.08.2019		5 000		5 000
	TAURON Sprzedaż Sp. z o.o.	Polska Spółka Gazownictwa Sp. z o.o.	31.03.2018		15 000		15 000
	Elektrociepłownia Stalowa Wola S.A.	Operator Gazociągów Przesyłowych GAZ-SYSTEM S.A.	30.07.2020		1 667		–
	TAURON Czech Energy s.r.o.	CEZ a.s.		–	–	1 500	6 636
liability towards CaixaBank S.A. being result of guarantees issued by the bank for subsidiaries	TAURON Ciepło Sp. z o.o.	Elektrobudowa S.A.	31.12.2018		12 300		–
	other subsidiaries	various entities	2018–2020		1 534		263
liability towards Powszechna Kasa Oszczędności Bank Polski S.A. being result of guarantees issued by the bank for subsidiaries	subsidiaries	various entities			–		1 691

** Registered pledges are valid in the collateral period, i.e. until the total repayment or until release of the pledge by the pledgee. The financial pledge is valid in the entire collateral period or until release by the pledgee, not later than on 31 December 2028.*

The key items of contingent liabilities arising from guarantees, collateral and financing commitments are:

- Corporate guarantee

  Corporate guarantee given to secure the bonds issued by TAURON Sweden Energy AB (publ). The guarantee remains valid until 3 December 2029, i.e. until the date of redemption of bonds, and amounts to EUR 168 000 thousand (PLN 700 711 thousand). The beneficiaries of the guarantee are the bondholders.

- Registered and financial pledges on shares

  On 15 May 2015, TAURON Polska Energia S.A. established a financial pledge and registered pledges on 3 293 403 issued shares of TAMEH HOLDING Sp. z o.o., representing ca. 50% of the issued capital. RAIFFEISEN BANK INTERNATIONAL AG is the beneficiary of the aforesaid pledges. They include a first lien registered pledge on shares with the maximum collateral amount of CZK 3 950 000 thousand and a first lien registered pledge on shares with the maximum collateral amount of PLN 840 000 thousand. On 15 September 2016, Annex 1 was executed to the aforementioned agreement, whereby the maximum collateral amount was changed to PLN 1 370 000 thousand. The Company also agreed to establish a financial pledge and registered pledges of new shares acquired or taken up. Moreover, the Company assigned the rights to dividend and other payments.

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

  As at 31 December 2017, the carrying amount of shares in TAMEH HOLDING Sp. z o.o. was PLN 415 852 thousand.

- Financing commitments

  In order to enable TAURON Ciepło Sp. z o.o. to apply for a non-refundable grant for the projects undertaken under the "Low emission liquidation in the Silesia and Dabrowa urban area" scheme funded by the Regional Fund for Environmental Protection and Water Management in Katowice, the Company provided TAURON Ciepło Sp. z o.o. with a commitment to finance the latter with the total amount of PLN 178 300 thousand. The commitments were valid until 31 December 2017; they were not renewed.

- Bank guarantees issued on the Company's request by The Bank of Tokyo-Mitsubishi UFJ, Ltd.

  The Company requested bank guarantees to secure the liabilities of Elektrociepłowna Stalowa Wola S.A. under the standstill agreement. The bank guarantees, valid until 14 April 2017 and totalling PLN 314 486 thousand, were issued to:

  - 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.

  On 31 March 2017, Elektrociepłownia Stalowa Wola S.A. paid all its liabilities to the financing banks. The guarantees expired on 14 April 2017.

- Blank promissory notes

  The Company issued blank promissory notes along with promissory note declarations, totalling PLN 70 000 thousand, as collateral for loan agreements entered into by its subsidiaries with the Regional Fund for Environmental Protection and Water Management in Katowice. The collateral in the form of promissory notes is valid until the subsidiaries' payment of all their liabilities to the lender. The promissory notes are valid until 15 December 2022.

Key items of the Company's contingent liabilities arising from court proceedings:

- **Claims relating to termination of long-term contracts**

Claims relating to termination of long-term contracts against subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.

On 18 March 2015 the subsidiary in liquidation terminated long-term contracts concluded in the years 2009–2010 to purchase electricity and property rights from wind farms owned by the companies in the in.ventus group, Polenergia and Wind Invest. The reason for the termination of the contracts by Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. was that the counterparties had breached the contractual provisions by refusing to negotiate in good faith the terms and conditions of the contracts. A case was brought against the Company for the statements made in the notice of termination be declared void. In the case brought by Dobiesław Wind Invest Sp. z o.o. in 2016 the Regional Court in Warsaw dismissed the claim for declaring the termination of the contracts void. The claimant appealed against the ruling.

In 2016 the claims against the Company were changed to include claims for compensation for termination of the contracts totalling approx. PLN 40 000 thousand.

In October 2017 Dobiesław Wind Invest Sp. z o.o. filed a new lawsuit against Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. for payment of PLN 42 095 thousand of compensation and liquidated damages.

After the balance sheet date, in January 2018 the claims brought by Amon Sp. z o.o., Talia Sp. z o.o. and Mogilno III-VI have been amended by extending them with further claims for liquidated damages related to the termination of contracts in the total amount of approximately PLN 69 472 thousand.

In light of the current status of the proceedings and the related circumstances, the Group believes that the probability of losing the cases both as regards declaration of ineffectiveness of the termination notices and securing non-monetary claims and the claims for compensation does not exceed 50%. Therefore, no provision for the related costs has been recognized.

Claim relating to termination of long-term contracts against subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and TAURON Polska Energia S.A.

In November 2014 an action was brought against Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and TAURON Polska Energia S.A. by Dobiesław Wind Invest Sp. z o.o. to prevent an imminent danger of loss. It was claimed that the Company should revoke the liquidation of Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. in liquidation. A subsidiary claim was that TAURON Polska Energia S.A. should be obliged to provide security in the amount of PLN 183 391 thousand as a court deposit.

On 8 March 2017, pursuant to a decision of the Shareholders' Meeting of Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. the liquidation of the company was revoked. Therefore, in accordance with the order of the Regional Court in Krakow issued on 15 March 2017, the parties to the dispute exchanged pleadings to respond to the change in the company in which the claimant upheld their demands.

On 2 August 2017 the Company's representative in the case received pleadings from Dobiesław Wind Invest Sp. z o.o. which changed the claims. The claimant withdrew the initial claim against subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and changed the claim against the Company from a claim for prevention of an imminent danger of loss to a claim for compensation. Dobiesław Wind Invest Sp. z o.o. demands payment of approx. PLN 34 700 thousand with statutory interest as of the date of the claim to the date of payment. Moreover, the claimant seeks a ruling that the Company is liable for future damages of Dobiesław Wind Invest Sp. z o.o., which the latter estimates at approx. PLN 254 000 thousand, (resulting from the Company's alleged torts) and a security of approx. PLN 254 000 thousand in case the court does not establish the Company's liability for future losses. The factual basis of the claim, in accordance with the claimant, is the termination of the long-term contracts to sell electricity and property rights by subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.

An analysis of the justification of the statements of the claim shows that they are wholly groundless. At a hearing on 4 October 2017, upon request of TAURON Polska Energia S.A., the Court decided that the new statement of claim against TAURON Polska Energia S.A. would be examined separately. As far as the initial claims against TAURON Polska Energia S.A. and Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. (demand that the liquidation be revoked), the Court referred the case to be examined at a closed-door hearing and dismissed.

As the court will have to examine extensive evidence and conduct an analysis of a legal issue which has not been resolved before, it is too early to anticipate the outcome of the proceedings but it is very likely that the decision of the court will be favourable for the defendants.

Claims relating to termination of long-term contracts against TAURON Polska Energia S.A.

On 20 July 2017 the Company was served with a summons dated 29 June 2017 of Gorzyca Wind Invest Sp. z o.o. against TAURON Polska Energia S.A. for damages of approx. PLN 39 700 thousand and assessment of liability for future damages resulting from torts, including unfair competition, estimated by the claimant at approx. PLN 465 900 thousand. The case will be heard by a Regional Court in Katowice. On 18 September 2017 the Company responded to the summons and among other things requested that the claim be dismissed in full as manifestly unfounded. On 1 December 2017 Gorzyca Wind Invest Sp. z o.o. filed a reply to the defence in which it sustained the position presented in the claims and denied the position and arguments of the Company presented in the reply. By the decision of the District Court in Katowice of 8 February 2018, the proceedings brought by Gorzyca Wind Invest Sp. z o.o. against TAURON Polska Energia SA, is entirely carried out in camera, the announcement of the decision ending the proceedings will take place publicly.

Another summons, dated 29 June 2017, of Pękanino Wind Invest Sp. z o.o. against TAURON Polska Energia S.A. for damages of approx. PLN 28 500 thousand and assessment of liability for future damages resulting from torts, including unfair competition, estimated by the claimant at PLN 201 600 thousand was delivered on 21 August 2017. On 5 October 2017 the Company responded to the claim and among other things requested that the claim be dismissed in full as manifestly unfounded. On 1 December 2017 Pękanino Wind Invest Sp. z o.o. filed a reply to the defence in which it sustained the position presented in the claims and denied the position and arguments of the Company presented in the reply. By the date of approval of these financial statements for issue the date of the hearing had not been set.

On 16 October 2017 the Company was served a summons dated 29 June 2017 of Nowy Jarosław Wind Invest Sp. z o.o. against TAURON Polska Energia S.A. for damages of approx. PLN 27 000 thousand and assessment of liability for future damages resulting from torts, including unfair competition, estimated by the claimant at PLN 197 800 thousand. On 28 December 2017 the Company responded to the claim and among other things requested that the claim be dismissed in full as manifestly unfounded. By the date of approval of these financial statements for issue the date of the hearing had not been set.

The factual basis of all the claims, in accordance with the claimants, is the termination of the long-term contracts to purchase electricity and property rights resulting from energy certificates by subsidiary Polska Energia Pierwsza Kompania Handlowa Sp. z o.o. and the total amount of the future loss incurred by all members of the Wind Invest group estimated by the claimant will be PLN 1 212 900 thousand.

As at date of approval of these financial statements for issue, the Company stands a good chance of a favourable ruling, i.e. the changes are estimated at 70%.

- **Claims filed by Huta Łaziska S.A.**

Following the Company's business combination with Górnośląski Zakład Elektroenergetyczny S.A. ("GZE"), TAURON Polska Energia S.A. became a party to a court dispute with Huta Łaziska S.A. ("Huta"), against GZE and the State Treasury represented by the President of the Energy Regulatory Office. At present, the case is pending at the Regional Court in Warsaw.

Based on a decision of 12 October 2001, the President of the Energy Regulatory Office ordered GZE to resume electricity supplies to Huta (suspended on 11 October 2001 since Huta had not paid its liabilities) on such terms as set out in the agreement of 30 July 2001, in particular at the price of PLN 67/MWh, until final resolution of the dispute, and on 14 November 2001 the dispute was finally resolved pursuant to a decision stating that discontinuation of electricity supplies was not unjustified. Huta appealed against that decision. On 25 July 2006, the Court of Appeals in Warsaw issued a final and binding decision ending the dispute concerning GZE's energy supplies to Huta. The court dismissed Huta's appeal against the decision of the Regional Court in Warsaw dated 19 October 2005, in which the court had dismissed Huta's appeal against the decision of the President of the Energy Regulatory Office. Huta filed a cassation appeal against the decision of the Court of Appeals in Warsaw, which was dismissed by the judgment of the Supreme Court dated 10 May 2007. On 15 November 2001 (following the issue of the above decision by the President of the Energy Regulatory Office on 14 November 2001 and due to the growing indebtedness of Huta to GZE due to power supply) GZE again suspended power supply. Therefore, Huta has sued GZE for damages.

Under a suit of 12 March 2007 against GZE and the State Treasury represented by the President of the Energy Regulatory Office (jointly and severally) Huta claimed the payment of PLN 182 060 thousand together with interest from the date of filing the suit to the date of payment, in respect of damages for alleged losses resulting from GZE's failure to comply with the decision of the President of the Energy Regulatory Office dated 12 October 2001.

In this case, the courts of the first and second instance passed judgements favourable for GZE; however, in its judgement of 29 November 2011 the Supreme Court overruled the decision of the Court of Appeals and remanded the case for re-examination by that Court. On 5 June 2012, the Court of Appeals overruled the decision of the Regional Court and remanded the case for re-examination by the latter. The case has been heard by the first-instance court since 27 November 2012.

Based on a legal analysis of claims the Company believes that they are unjustified and the risk that they must be satisfied is remote. As a result, no provision has been recognized by the Company for any costs associated with those claims.

- **Claim filed by ENEA S.A.**

The claim filed by ENEA S.A. ("ENEA") against TAURON Polska Energia S.A. in a case heard by the Regional Court in Katowice since 2016 regards the payment of PLN 17 086 thousand with statutory interest calculated from 31 March 2015 to the payment date. ENEA's claim is based on charges relating to unjust enrichment of the Company associated with possible errors in determination of aggregate measurement and settlement data by ENEA Operator Sp. z o.o. (as the Distribution System Operator), used as the basis for settlements between ENEA and the Company and Polskie Sieci Elektroenergetyczne S.A. arising from non-balancing volumes on the Balancing Market between January and December 2012.

In the course of the proceedings, at the request of ENEA, the court decided to extend the suit against seven sellers for which TAURON Polska Energia S.A. acted as an entity in charge of trade balances in the distribution area of ENEA Operator Sp. z o.o. in 2012. The sellers included two subsidiaries of TAURON Polska Energia S.A., i.e.: TAURON Sprzedaż Sp. z o.o. (from which ENEA S.A. demanded PLN 4 934 thousand with statutory interest as of the date of serving a copy of the request to extend the suit until the date of payment) and TAURON Sprzedaż GZE Sp. z o.o. (from which ENEA S.A. demanded PLN 3 480 thousand with statutory interest as of the date of serving a copy of the request to extend the suit until the date of payment). The demand for payment of the above amounts as well as the amounts claimed from the other five sellers was submitted by the petitioner in case the claim against TAURON Polska Energia S.A. is dismissed. The case is pending. By the date of approval of these financial statements for publication, the hearing had been adjourned ex officio.

The Company did not recognize any provision as, in its opinion, the risk of losing the case is below 50%. Provisions were recognized by the subsidiaries of TAURON Polska Energia S.A. in the total amount of PLN 5 237 thousand (TAURON Sprzedaż Sp. z o.o.) and in the total amount of PLN 3 726 thousand (TAURON Sprzedaż GZE Sp. z o.o.). The said provisions cover the principal, interest reviewed as at 31 December 2017 and the cost of the proceedings.

As at 31 December 2017, the value of the claim against the Company is PLN 17 086 thousand, including statutory interest accrued between 31 March 2015 and the payment date. Should the claim filed against the Company be dismissed, the claim for payment by the Group companies totals PLN 8 414 thousand, including statutory interest accrued between the date of service of a copy of the request filed by ENEA S.A. to extend the suit by a specific Group company and the payment date. As new measurement data were presented by ENEA Operator sp. z o.o. in the course of the proceedings, the values of the claims against the Company and/or the Group companies may be expected to change.

(in PLN '000)

45. Security for liabilities

Agreement/transaction	Collateral	Collateral amount
Bond Issue Scheme dated 16 December 2010 with subsequent annexes	declaration of submission to enforcement	up to PLN 6 900 000 thousand, valid until 31 December 2018
Long-term Bond Issue Scheme in Bank Gospodarstwa Krajowego	declaration of submission to enforcement	up to PLN 2 550 000 thousand, valid until 20 December 2032
Bond Issue Scheme dated 24 November 2015	declaration of submission to enforcement	up to PLN 7 524 000 thousand, valid until 31 December 2023
Bank guarantee agreement with The Bank of Tokyo-Mitsubishi UFJ, Ltd.	declaration of submission to enforcement	up to PLN 377 383 thousand, valid until 27 October 2018
Agreement for hybrid funding in the form of a subordinated bond issue scheme of 6 September 2017	declaration of submission to enforcement	up to PLN 600 000 thousand, valid until 30 June 2034
Framework bank guarantee agreement concluded with CaixaBank S.A. The Company and TAURON Group companies can use the limit for guarantees to secure transactions (the maximum guarantee limit amount was determined at PLN 100 000 thousand).	authorization to debit the bank account maintained by CaixaBank S.A.	up to PLN 100 000 thousand
	declaration of submission to enforcement	up to PLN 120 000 thousand valid until 11 July 2021
Agreement with Bank Zachodni WBK S.A. on bank guarantees for Izba Rozliczeniowa Giełd Towarowych S.A.	authorization to debit the bank account maintained by BZ WBK S.A.	up to PLN 150 000 thousand
Overdraft agreement and intra-day limit (bank account agreement) at PKO Bank Polski S.A. (overdraft of up to PLN 300 000 thousand and intra-day limit of up to PLN 500 000 thousand)	authorizations to debit the bank account maintained by PKO Bank Polski S.A.	up to the total amount of PLN 800 000 thousand
	declaration of submission to enforcement	up to PLN 600 000 thousand, valid until 17 December 2021
	declaration of submission to enforcement	up to PLN 360 000 thousand, valid until 29 December 2021
Overdraft agreement with Bank Gospodarstwa Krajowego (in EUR, up to EUR 45 000 thousand)	authorization to debit the bank account maintained by Bank Gospodarstwa Krajowego	up to PLN 187 690 thousand (EUR 45 000 thousand)
	declaration of submission to enforcement	up to PLN 100 102 thousand (EUR 24 000 thousand) valid until 31 December 2019
	declaration of submission to enforcement	up to PLN 208 545 thousand (EUR 50 000 thousand) valid until 31 December 2020
Overdraft agreement with mBank (in USD, up to USD 2 000 thousand)	declaration of submission to enforcement	up to PLN 10 444 thousand (USD 3 000 thousand) valid until 31 March 2019
Security for adequate performance of obligations under Grant Agreements with the National Centre for Research and Development	blank promissory notes to secure the payment of the Company's liabilities	up to the total amount of PLN 4 244 thousand
Finance lease agreement concerning an investment property	The agreement covers an investment property. The agreement is collateralized by two blank promissory notes, assignment of receivables and authorization to debit a bank account.	As at 31 December 2017 the carrying amount of the leased asset was PLN 21 702 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 2017, the guarantees issued by the bank totalled PLN 50 000 thousand and were valid until 31 March 2018.

Under the bank guarantee agreement made with CaixaBank S.A. (Spółka Akcyjna) Branch in Poland, at the request of the Company the bank issued bank guarantees to secure liabilities and transactions of the subsidiaries of TAURON Polska Energia S.A. totalling PLN 13 834 thousand (Note 44 to these financial statements) and to secure the transactions performed by the Company:

– for Operator Gazociągów Przesyłowych GAZ-SYSTEM S.A. – up to PLN 2 661 thousand, valid until 30 November 2018;

– for Polskie Sieci Elektroenergetyczne S.A. – up to PLN 4 041 thousand, valid until 11 February 2018.

46. Capital commitments

As at 31 December 2017 and 31 December 2016, the Company did not have any material capital commitments.

(in PLN '000)

47. Related-party disclosures

47.1. Transactions with related parties and State Treasury companies

The Company enters into transactions with related parties, as presented in Note 2 to these financial statements. In addition, due to the fact that the State Treasury of the Republic of Poland is the Company's majority shareholder, State Treasury companies are treated as related parties. Transactions with State Treasury companies are mainly related to the operating activities of the Company and are made on an arm's length terms.

The total value of transactions with the aforementioned entities and the balances of receivables and liabilities have been presented in the tables below.

Revenue and costs

	Year ended 31 December 2017	Year ended 31 December 2016
Revenue from subsidiaries	**8 629 630**	**9 706 997**
Revenue from operating activities	7 602 324	7 650 113
Dividend income	542 474	1 458 951
Revenue from sale of shares	–	96 691
Other operating income	5 669	5 345
Other finance income	479 163	495 897
Revenue from jointly-controlled entities	**56 611**	**126 811**
Revenue from State Treasury companies	**411 956**	**162 649**
Costs from subsidiaries	**(3 175 156)**	**(2 852 147)**
Costs of operating activities	(3 127 698)	(2 814 659)
Finance costs	(47 458)	(37 488)
Costs incurred with relation to transactions with jointly-controlled entities	**(3 183)**	**(12 521)**
Costs from State Treasury companies	**(532 007)**	**(571 124)**

Receivables and liabilities

	As at 31 December 2017	As at 31 December 2016
Loans granted to subsidiaries and receivables from subsidiaries	**7 561 140**	**11 940 640**
Receivables from buyers	658 936	795 482
Loans granted under cash pool agreement plus interest accrued	182 933	15 800
Other loans granted	139 268	1 249 802
Receivables from the TCG	6 078	20 945
Bonds	6 572 696	9 858 382
Other financial receivables	240	229
Other non-financial receivables	989	–
Loans granted to jointly-controlled entities and receivables from jointly-controlled entities	**579 381**	**274 502**
Receivables from State Treasury companies	**49 941**	**25 210**
Liabilities to subsidiaries	**3 406 474**	**2 413 451**
Liabilities to suppliers	288 965	335 344
Loans received under cash pool agreement plus interest accrued	2 355 765	1 229 344
Other loans received	721 280	767 750
Liabilities arising from the TCG	34 836	75 415
Other financial liabilities	5 257	5 259
Other non-financial liabilities	371	339
Liabilities to jointly-controlled entities	**503**	**1 209**
Liabilities to State Treasury companies	**28 952**	**55 389**

(in PLN '000)

Revenue from subsidiaries includes revenue from sales of coal to TAURON Wytwarzanie S.A. and TAURON Ciepło Sp. z o.o., which is presented in the statement of comprehensive income less cost in the amount of the surplus constituting the revenue due to agency services, presented in detail in Note 12 to these financial statements.

In the year ended 31 December 2017, the major contracting party as regards sales revenue from transactions made by TAURON Polska Energia S.A. with State Treasury companies was PSE S.A. Sales to that entity accounted for 95% of the total revenue from State Treasury companies.

In the year ended 31 December 2017, Polska Grupa Górnicza Sp. z o.o., PSE S.A. and Jastrzębska Spółka Węglowa S.A. were the major contracting parties of TAURON Polska Energia S.A. as regards costs incurred in transactions with State Treasury companies. Costs incurred in transactions with those entities represented 97% of total costs incurred in purchase transactions entered into with State Treasury companies.

In relation to agreements entered into with the joint venture Elektrociepłownia Stalowa Wola S.A., the Company recognized provisions for onerous contracts and for costs. In the year ended 31 December 2017 the Company reversed all these provisions, which has been discussed in more detail in Note 35 to these financial statements.

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

47.2. Executive compensation

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

	Year ended 31 December 2017	Year ended 31 December 2016
Management Board	**6 957**	**12 858**
Short-term benefits (with surcharges)	4 545	6 367
Temination benefits	2 104	5 806
Other	308	685
Supervisory Board	**739**	**1 159**
Short-term employee benefits (salaries and surcharges)	739	1 159
Other members of key management personnel	**13 832**	**13 284**
Short-term employee benefits (salaries and surcharges)	12 151	10 554
Temination benefits	776	1 911
Other	905	819
Total	**21 528**	**27 301**

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

No loans have been granted from the Company's Social Benefit Fund to members of the Management Board, Supervisory Board or other key executives.

48. Finance and capital management

Finance and capital are managed at the level of the TAURON Polska Energia S.A. Capital Group. During the period covered by these financial statements there were no significant changes in finance and capital management objectives, principles or procedures. Finance and capital management at the level of the TAURON Polska Energia S.A. Capital Group has been discussed in more detail in Note 51 to the Consolidated Financial Statements for the year ended 31 December 2017.

(in PLN '000)

49. Employment structure

The following note presents average employment in the annual periods ended 31 December 2017 and 31 December 2016.

	Year ended 31 December 2017	Year ended 31 December 2016
Management	1	5
Administration	330	249
Sales department	104	115
Total	**435**	**369**

50. 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 TAURON Polska Energia S.A. for the 2017 financial year (Section 4.8).

51. Structure of financial statements broken down by business activity type in line with Article 44 of the Energy Law

Under Article 44.2 of the Energy Law, TAURON Polska Energia S.A., as an energy company, is obliged to disclose specific items of the balance sheet and the statement of profit or loss broken down by individual types of business activity in notes to these financial statements.

The Company has identified the following types of business activities in accordance with Article 44.2 of the Energy Law:

- trade in gaseous fuels;
- other activity.

The principles of preparing a statement of comprehensive income (statement of profit or loss) broken down by type of business activity

The Company keeps accounting records which enable separate calculation of expense and revenue and the profit/loss for the activities mentioned above.

The Company has directly separated sales revenue and cost of sales related to individual types of activities.

Selling and distribution costs related to the entire sales process carried out by the Company have been divided proportionally to the sales revenue generated by the Company.

Other operating and financing activities have been identified as those related to other business activities of the Company.

Administrative expenses of the Company are incurred for the benefit of the entire Capital Group, hence they have been recognized in the statement of comprehensive income as unallocated items and are not directly attributable to a specific business activity, as such attribution would be unjustified. Also CIT charged to profit or loss has been presented under unallocated items.

(in PLN '000)

Statement of comprehensive income by type of activity for the 2017 financial year

	Gas	Other activity	Unallocated items	Total
Sales revenue	194 290	7 597 735	–	**7 792 025**
Cost of sales	(194 375)	(7 220 332)	–	**(7 414 707)**
Gross profit (loss)	**(85)**	**377 403**	**–**	**377 318**
Selling and distribution expenses	(580)	(22 729)	–	**(23 309)**
Administrative expenses	–	–	(88 751)	**(88 751)**
Other operating expenses	–	(2 470)	–	**(2 470)**
Operating profit (loss)	**(665)**	**352 204**	**(88 751)**	**262 788**
Dividend income	–	560 832	–	**560 832**
Interest income on bonds and loans	–	456 426	–	**456 426**
Interest expense on debt	–	(334 638)	–	**(334 638)**
Revaluation of shares and loans	–	(134 372)	–	**(134 372)**
Other finance income and costs	–	108 529	–	**108 529**
Profit (loss) before tax	**(665)**	**1 008 981**	**(88 751)**	**919 565**
Income tax expense	–	–	(65 214)	**(65 214)**
Net profit (loss) for the year	**(665)**	**1 008 981**	**(153 965)**	**854 351**

Statement of comprehensive income by type of activity for the 2016 financial year

	Gas	Other activity	Unallocated items	Total
Sales revenue	242 615	7 752 713	–	**7 995 328**
Cost of sales	(233 922)	(7 603 645)	–	**(7 837 567)**
Gross profit (loss)	**8 693**	**149 068**	**–**	**157 761**
Selling and distribution expenses	(586)	(18 740)	–	**(19 326)**
Administrative expenses	–	–	(81 368)	**(81 368)**
Other operating income and expenses	–	(59 170)	(32 500)	**(91 670)**
Operating profit (loss)	**8 107**	**71 158**	**(113 868)**	**(34 603)**
Dividend income	–	1 485 152	–	**1 485 152**
Interest income on bonds and loans	–	503 897	–	**503 897**
Interest expense on debt	–	(356 947)	–	**(356 947)**
Revaluation of shares and loans	–	(1 610 396)	–	**(1 610 396)**
Other finance income and costs	–	(136 237)	–	**(136 237)**
Profit (loss) before tax	**8 107**	**(43 373)**	**(113 868)**	**(149 134)**
Income tax expense	–	–	(17 119)	**(17 119)**
Net profit (loss) for the year	**8 107**	**(43 373)**	**(130 987)**	**(166 253)**

The principles of preparing a statement of financial position (balance sheet) broken down by type of business activity

The Company has directly separated receivables from buyers, liabilities to suppliers and other receivables and other liabilities related to individual types of its business activities.

Equity, provisions for employee benefits, cash as well as receivables and liabilities relating to taxes and charges have been presented as unallocated items in the statement of financial position.

The remaining assets and liabilities are related to other activities of the Company.

(in PLN '000)

Statement of financial position by type of activity as at 31 December 2017

	Gas	Other activity	Unallocated items	Total
ASSETS				
Non-current assets, of which:	**834**	**27 370 591**	**–**	**27 371 425**
Shares	–	20 912 679	–	**20 912 679**
Bonds	–	6 009 920	–	**6 009 920**
Loans granted	–	382 989	–	**382 989**
Other financial assets	834	1 890	–	**2 724**
Current assets, of which:	**20 912**	**2 123 084**	**757 671**	**2 901 667**
Receivables from buyers	20 413	698 720	–	**719 133**
Receivables arising from taxes and charges	–	–	36 094	**36 094**
Bonds	–	562 776	–	**562 776**
Loans granted	–	520 191	–	**520 191**
Other financial assets	499	131 141	–	**131 640**
Cash and cash equivalents	–	–	721 577	**721 577**
TOTAL ASSETS	**21 746**	**29 493 675**	**757 671**	**30 273 092**
EQUITY AND LIABILITIES				
Equity	**–**	**–**	**17 377 906**	**17 377 906**
Non-current liabilities, of which:	**–**	**9 497 538**	**32 990**	**9 530 528**
Debt	–	9 472 454	–	**9 472 454**
Deferred income tax liability	–	–	29 843	**29 843**
Provisions for employee benefits	–	–	3 147	**3 147**
Current liabilities, of which:	**4 081**	**3 290 128**	**70 449**	**3 364 658**
Debt	–	2 725 763	–	**2 725 763**
Liabilities to suppliers	4 081	409 184	–	**413 265**
Liabilities arising from taxes and charges	–	–	70 119	**70 119**
Provisions for employee benefits	–	–	330	**330**
Other financial liabilities	–	62 590	–	**62 590**
TOTAL EQUITY AND LIABILITIES	**4 081**	**12 787 666**	**17 481 345**	**30 273 092**

Statement of financial position by type of activity as at 31 December 2016

	Gas	Other activity	Unallocated items	Total
ASSETS				
Non-current assets, of which:	**1 109**	**25 854 220**	**–**	**25 855 329**
Shares	–	14 874 418	–	**14 874 418**
Bonds	–	9 615 917	–	**9 615 917**
Loans granted	–	1 292 800	–	**1 292 800**
Other financial assets	984	540	–	**1 524**
Current assets, of which:	**24 292**	**1 474 079**	**318 676**	**1 817 047**
Receivables from buyers	23 230	817 426	–	**840 656**
Receivables arising from taxes and charges	–	–	120 586	**120 586**
Bonds	–	242 465	–	**242 465**
Loans granted	–	30 966	–	**30 966**
Other financial assets	594	54 760	–	**55 354**
Cash and cash equivalents	–	–	198 090	**198 090**
TOTAL ASSETS	**25 401**	**27 328 299**	**318 676**	**27 672 376**
EQUITY AND LIABILITIES				
Equity	**–**	**–**	**16 530 268**	**16 530 268**
Non-current liabilities, of which:	**–**	**8 935 078**	**34 898**	**8 969 976**
Debt	–	8 754 047	–	**8 754 047**
Deferred income tax liability	–	–	32 364	**32 364**
Provisions for employee benefits	–	–	2 534	**2 534**
Current liabilities, of which:	**3 591**	**2 148 033**	**20 508**	**2 172 132**
Debt	–	1 433 929	–	**1 433 929**
Liabilities to suppliers	3 173	470 464	–	**473 637**
Liabilities arising from taxes and charges	–	–	20 209	**20 209**
Provisions for employee benefits	–	–	299	**299**
Other financial liabilities	418	111 341	–	**111 759**
TOTAL EQUITY AND LIABILITIES	**3 591**	**11 083 111**	**16 585 674**	**27 672 376**

52. Events after the end of the reporting period

Increase in the capital of Magenta Grupa TAURON Sp. z o.o.

On 11 January 2018, an increase in the issued capital of Magenta Grupa TAURON Sp. z o.o. of PLN 9 000 thousand in accordance with a resolution of the Extraordinary General Shareholders' Meeting of 24 October 2017 was registered by the National Court Register.

Loans to a joint venture

On 12 January 2018 and 28 February 2018, the Company entered into a loan agreement for PLN 27 000 thousand with Elektrociepłownia Stalowa Wola S.A. and an agreement to consolidate the borrower's debt of PLN 609 951 thousand, respectively, which has been discussed in more detail in Note 25 to these financial statements.

Increase in the capital of TAURON Ekoenergia Sp. z o.o.

On 2 March 2018, an increase in the issued capital of TAURON Ekoenergia Sp. z o.o. of PLN 1 000 000 thousand in accordance with a resolution of the Extraordinary General Shareholders' Meeting of 24 October 2017 was registered by the National Court Register.

Contributions to the capital of Polska Energia Pierwsza Kompania Handlowa Sp. z o.o.

On 1 March 2018, the Extraordinary General Shareholders' Meeting of Polska Energia Pierwsza Kopalnia Handlowa Sp. z o.o. adopted a resolution to impose an additional contribution of PLN 6 000 thousand on the Company, as the sole shareholder. On 7 March 2018, the contributions were made by the Company.

Financing a joint venture Elektrociepłownia Stalowa Wola S.A.

After the end of the reporting period, on 8 March 2018, a joint venture Elektrociepłownia Stalowa Wola S.A. signed a loan agreement with Bank Gospodarstwa Krajowego and Polskie Górnictwo Naftowe i Gazownictwo S.A., which has been discussed in more detail in Note 25 to these financial statements.

Signing admendments to Bond Issue Scheme agreements

After the end of the reporting period, on 8 March 2018 the period of availability of the funds under Bond Issue Scheme of 24 November 2015 was extended as a result of signing amendments to the agency and custody agreement as well as the underwriting agreement, as described in Note 33.1 to these financial statements.

Management Board of the Company

Katowice, 12 March 2018

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

Jarosław Broda – Vice-President of the Management Board ....

Kamil Kamiński – Vice-President of the Management Board ....

Marek Wadowski – Vice-President of the Management Board ....

Oliwia Tokarczyk – Executive Director in Charge of Taxes and Accounting ....

REPORT OF THE MANAGEMENT BOARD ON OPERATIONS OF TAURON POLSKA ENERGIA S.A. FOR THE FINANCIAL YEAR 2017

MARCH 2018

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1. TAURON POLSKA ENERGIA S.A.

1.1. General Information on the Company

TAURON Polska Energia Spółka Akcyjna (hereinafter referred to as the Company or TAURON) was established on 6 December 2006 as part of the *Program for the Power Sector*. The founders of the Company included: State Treasury represented by the Minister of Treasury, EnergiaPro S.A. with its seat in Wrocław, ENION S.A. with its seat in Kraków (currently: TAURON Dystrybucja S.A. that was formed as a result of a merger of then EnergiaPro S.A. and ENION S.A.), and Elektrownia Stalowa Wola S.A. with its seat in Stalowa Wola (currently a branch of 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 table below presents general information on the Company and the basic types of operations conducted by the Company.

Table no. 1. General information on TAURON

No.	General information	Basic types of operations conducted by the Company
1.	Name (enterprise): TAURON Polska Energia S.A.	
2.	Legal form: joint stock company	1) Head office and holding company operations, excluding financial holdings (PKD 70.10 Z),
3.	Seat (Head Office): Katowice	
4.	Website: www.tauron.pl	2) trading in electricity (PKD 35.14 Z),
5.	National Court Register: 0000271562 Sąd Rejonowy Katowice - Wschód w Katowicach	3) wholesale of fuels and derivative products (trading in coal and biomass) (PKD 46.71 Z),
6.	NIP: 9542583988	4) trading in gas fuels (PKD 35.23 Z).
7.	REGON: 240524697	
8.	The Company does not have any branches (plants)	

The below figure presents the level of TAURON's share capital as of December, 2017, by the number and type of shares.

Figure no. 1. TAURON's share capital (paid up) as of December, 2017, by the number and type of shares

Share capital (paid up)
PLN 8,762,746,970.00
number of shares:
1,752,549,394

AA series shares
(bearer shares)
1,589,438,762 shares
Nominal value per share: PLN 5

BB series shares
(ordinary, registered shares)
163,110,632 shares
Nominal value per share: PLN **5**

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

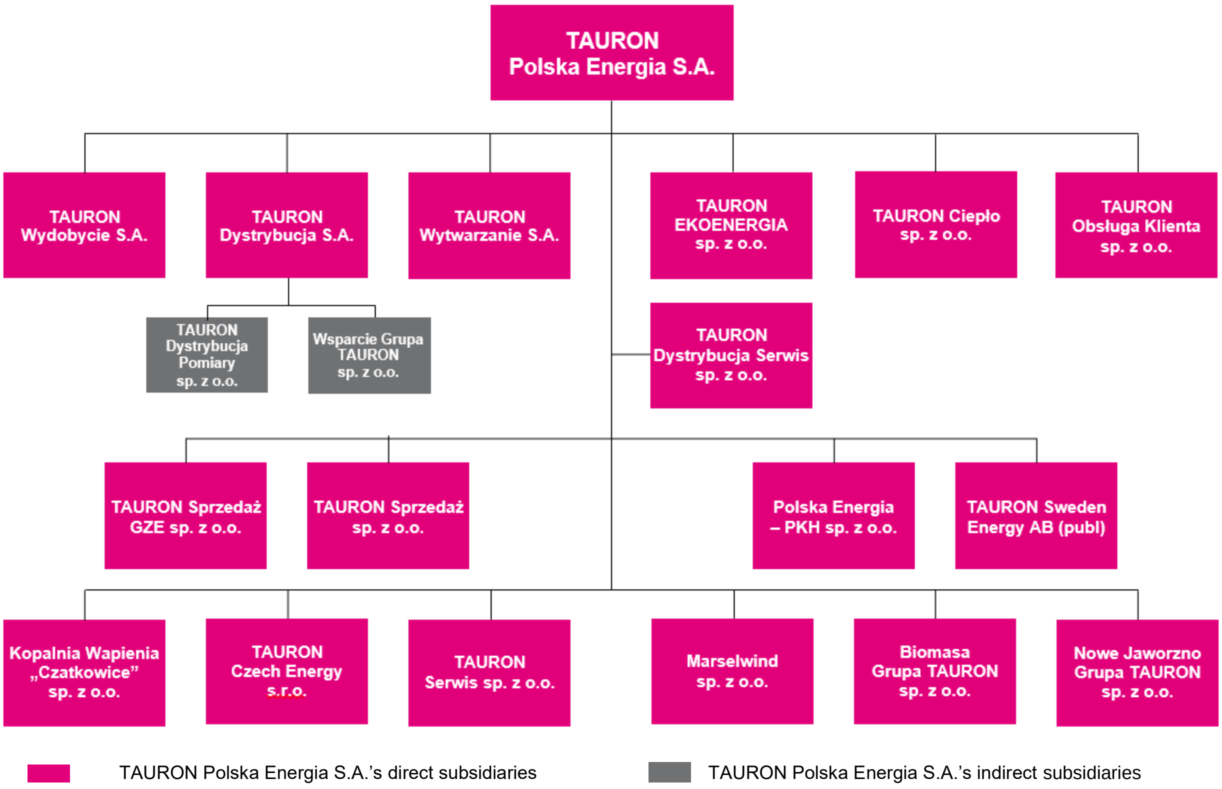
1.2. TAURON Capital Group's organization and structure

As of December 31, 2017 TAURON Capital Group's key subsidiaries, besides the TAURON parent company, included 19 subsidiaries subject to consolidation, listed in section 1.2.1. of this report. Furthermore, as of December 31, 2017, the Company held, directly or indirectly, shares in the other 38 subsidiaries.

1.2.1. Units subject to consolidation

The below figure presents TAURON Capital Group's structure, including the subsidiaries subject to consolidation, as of December 31, 2017.

Figure no. 2. TAURON Capital Group's structure, including the subsidiaries subject to consolidation, as of December 31, 2017



TAURON Capital Group also holds stakes in joint ventures: Elektrociepłownia Stalowa Wola S.A. (EC Stalowa Wola) and TAMEH HOLDING sp. z o.o. (TAMEH HOLDING), TAMEH POLSKA sp. z o.o. (TAMEH POLSKA) and TAMEH Czech s.r.o. (TAMEH Czech) that are valued using the equity method in the consolidated financial statements.

Detailed information on subsidiaries subject to consolidation and TAURON's share in their stock capital, as well in the parent company, is provided in section 1.2.2. of this report.

1.2.2. Organizational or equity ties

The below table presents a list of material direct or indirect subsidiaries subject to consolidation in which the Company held shares as of December 31, 2017.

Table no. 2. List of material subsidiaries subject to consolidation as of December 31, 2017

#	Subsidiary name	Seat	Main subject of operations	TAURON's share in the subsidiary's capital	TAURON's share in the subsidiary's parent company
1.	TAURON Wydobycie	Jaworzno	Hard coal mining	100.00%	100.00%
2.	TAURON Wytwarzanie[1]	Jaworzno	Electricity and heat generation, transmission and distribution	100.00%	100.00%
3.	Nowe Jaworzno GT[1]	Jaworzno	Electricity and heat generation, transmission and distribution, as well as electricity trading	100.00%	100.00%
4.	TAURON EKOENERGIA	Jelenia Góra	Electricity generation	100.00%	100.00%
5.	Marselwind	Katowice	Electricity generation, transmission and trading	100.00%	100.00%
6.	TAURON Ciepło	Katowice	Heat production and distribution	100.00%	100.00%
7.	TAURON Serwis	Katowice	Services	95.61%	95.61%
8.	TAURON Dystrybucja	Kraków	Electricity distribution	99.74%	99.75%
9.	TAURON Dystrybucja Serwis	Wrocław	Services	100.00%	100.00%
10.	TAURON Dystrybucja Pomiary[2]	Tarnów	Services	99.74%	99.75%

#	Subsidiary name	Seat	Main subject of operations	TAURON's share in the subsidiary's capital	TAURON's share in the subsidiary's parent company
11.	TAURON Sprzedaż	Kraków	Electricity trading	100.00%	100.00%
12.	TAURON Sprzedaż GZE	Gliwice	Electricity trading	100.00%	100.00%
13.	TAURON Czech Energy	Ostrava, Czech Republic	Electricity trading	100.00%	100.00%
14.	TAURON Obsługa Klienta	Wrocław	Services	100.00%	100.00%
15.	KW Czatkowice	Krzeszowice	Limestone and rock extraction	100.00%	100.00%
16.	PEPKH[3]	Warsaw	Electricity trading	100.00%	100.00%
17.	TAURON Sweden Energy	Stockholm, Sweden	Services	100.00%	100.00%
18.	Biomasa Grupa TAURON	Stalowa Wola	Waste and scrap metal wholesale	100.00%	100.00%
19.	Wsparcie Grupa TAURON[2,4]	Tarnów	Services	99.74%	99.75%

[1]On April 3, 2017 TAURON Wytwarzanie subsidiary was split and an organzied part of the enterprise was spun off to Nowe Jaworzno GT subsidiary.

[2]Share in TAURON Dystrybucja Pomiary and Wsparcie Grupa TAURON (formerly KOMFORT - ZET sp. z o.o.) is held by TAURON indirectly via TAURON Dystrybucja subsidiary. TAURON is a user of TAURON Dystrybucja Pomiary subsidiary's shares.

[3] On March 8, 2017 the Extraordinary GM of the PEPKH subsidiary in liquidation passed a resolution on revoking the liquidation of this company.

[4] On September 6, 2017 KOMFORT-ZET sp. z o.o. changed its name to "Wsparcie Grupa TAURON sp. z o.o.".

The below table presents a list of material joint subsidiaries subject to consolidation in which the Company held shares as of December 31, 2017.

Table no. 3. List of material joint subsidiaries subject to consolidation as of December 31, 2017

#	Subsidiary name	Seat	Main subject of operations	TAURON's share in the capital and subsidiary's parent company
1.	EC Stalowa Wola[1]	Stalowa Wola	Electricity generation	50.00%
3.	TAMEH HOLDING[2]	Dąbrowa Górnicza	Central companies and holding operations	50.00%
4.	TAMEH POLSKA[2]	Dąbrowa Górnicza	Electricity and heat generation, transmission, distribution and trading	50.00%
5.	TAMEH Czech[2]	Ostrava, Czech Republic	Production, trading and services	50.00%

[1]Share in EC Stalowa Wola is held by TAURON indirectly via TAURON Wytwarzanie subsidiary.

[2]Subsidiaries form a capital group. TAURON holds a diet share in the capital and the parent company of TAMEH HOLDING subsidiary that holds a 100% share in the capital and the parent company of TAMEH POLSKA and TAMEH Czech.

Due to the change to the organization of TAURON Capital Group as of the day of drawing up this report TAURON holds, directly or indirectly, shares in 57 subsidiaries.

The other most important equity investment in financial assets as of December 31, 2017 includes involvement in PGE EJ 1 sp. z o.o. (PGE EJ 1) worth PLN 26 546 thousand.

1.2.3. Major domestic and foreign investments

Taking up or purchasing share securities

Major investments in share securities made by the Company in 2017 and by the day of drawing up this report include:

Taking up shares in Nowe Jaworzno GT

In 2017 TAURON took up new shares Nowe Jaworzno GT's share capital three times:

1) On January 31, 2017 the Extraordinary GM of TAURON Wytwarzanie passed a resolution on the split of TAURON Wytwarzanie subsidiary by way of spinning off under art. 529 § 1 clause 4) of the Commercial Companies Code, i.e. by transferring some assets of TAURON Wytwarzanie in the form of an organized part of the enterprise including the investment process related to the construction of the new 910 MW power generation unit at Jaworzno III Power Plant, carried out by TAURON Wytwarzanie Oddział Elektrownia Jaworzno III in Jaworzno, to the newly established Nowe

Jaworzno GT company (in organization) in exchange for 37 000 shares in the Nowe Jaworzno GT company with the nominal value of PLN 50 per share and the total nominal value of PLN 1 850 000 that were taken up by the sole shareholder of the split company - TAURON. On April 3, 2017 Nowe Jaworzno GT company was registered in the National Court Register.

2) On June 26, 2017 the District Court for Katowice – Wschód, 8th Commercial Department registered in the National Court Register an increase in the share capital of Nowe Jaworzno GT, passed by the Extraordinary GM of the company on May 16, 2017. The subsidiary's share capital was increased from PLN 1 850 000 to PLN 31 850 000, i.e. by PLN 30 000 000, by way of issuance of 600 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 30 000 000. All of the new shares were taken up by the subsidiary's existing sole shareholder – TAURON. at the price of PLN 5 000 per share, i.e. for the total amount of PLN 3 000 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 2 970 000 000, was allocated to the company's spare capital.

3) On July 13, 2017 the District Court for Katowice – Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of Nowe Jaworzno GT, passed by the Extraordinary GM of Nowe Jaworzno GT on June 29, 2017. The subsidiary's share capital was increased from PLN 31 850 000 to PLN 35 850 000, i.e. by PLN 4 000 000, by way of issuance of 80 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 400 000 000. All of the new shares were taken up by the subsidiary's existing sole shareholder – TAURON. at the price of PLN 5 000 per share, i.e. for the total amount of PLN 400 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 396 000 000, was allocated to the company's spare capital.

Taking up shares in TAURON Dystrybucja

On December 29, 2017 the District Court for Kraków - Śródmieścia in Kraków, 11th Commercial Department, registered in the National Court Register an increase in the share capital of TAURON Dystrybucja subsidiary, passed by the Extraordinary GM of the company on October 26, 2017. The subsidiary's share capital was increased from PLN 511 925 759.22 to PLN 560 611 250.96, i.e. by PLN 48 685 491.74, by way of issuing 2 434 274 587 new ordinary registered shares with the nominal value of PLN 0.02 each, i.e. with the total amount of PLN 48 685 491.74. All the shares will were taken up by TAURON at the price of PLN 0.4108 per share, i.e. for the total amount of PLN 1 000 000 000.34, where the surplus of the issuing price of each share above its nominal value in the amount of PLN 0,3908 per each such share, i.e. in the total amount of PLN 951 314 508.60 was allocated to the company's spare capital.

In conjunction with the increase of the share capital TAURON's share in the subsidiary's share capital increased from 99.72% to 99.74%.

Taking up shares in TAURON EKOENERGIA

On March 2, 2018, the District Court for Wrocław – Fabryczna in Wrocław, 9th Commercial Department, registered in the National Court Register an increase in the share capital of TAURON EKOENERGIA passed by the Extraordinary GM on October 24, 2017. The share capital was increased by PLN 10 000 000 by way of issuing 10 000 new shares with the nominal value of PLN 1 000 each and the total nominal value of PLN 10 000 000. All the new shares were taken up by the existing sole shareholder of the company - TAURON at the price of PLN 100 000 per share, i.e. for the total amount of PLN 1 000 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 99 000 per each new share, i.e. in the total amount of PLN 990 000 000 was allocated to the company's spare capital.

Taking up shares in TAURON Ciepło

On June 20, 2017 the District Court for Katowice – Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of TAURON Ciepło, passed by the Extraordinary GM of TAURON Ciepło on May 11, 2017. The subsidiary's share capital was increased from PLN 1 098 348 500 to PLN 1 104 348 500, i.e. by PLN 6 000 000, by way of issuance of 120 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 6 000 000. All of the new shares were taken up by the subsidiary's existing sole shareholder – TAURON. at the price of PLN 5 000 per share, i.e. for the total amount of PLN 600 000 000, where the surplus of the price of taking up each new share in the company's increased share capital above its nominal value in the amount of PLN 4 950 per each new share, i.e. in the total amount of PLN 594 000 000 was allocated to the company's spare capital

Taking up shares in TAURON Wydobycie

On April 7, 2017 the District Court for Katowice – Wschód, 8th Commercial Department registered in the National Court Register an increase in the share capital of Tauron Wydobycie, passed by the Extraordinary GM of TAURON Wydobycie on March 21, 2017. The subsidiary's share capital was increased from PLN 355 510 780 to PLN 357 110 780, i.e.

by PLN 1 600 000, by way of issuance of 160 000 new “K” series registered shares with the nominal value of PLN 10 per share and the total nominal value of PLN 1 600 000. All of the “K” series shares were taken up, by way of a private placement subscription, by the subsidiary’s sole shareholder – TAURO, at the price of PLN 1 000 per share, i.e. for the total amount of PLN 160 000 000, where the surplus of the price of taking up each new share in the company’s increased share capital above its nominal value in the amount of PLN 990 per each new share, i.e. in the total amount of PLN 158 400 000, was allocated to the company’s spare capital

Taking up shares in Magenta Grupa TAURON sp. z o.o.

On January 11, 2018 the District Court for Katowice – Wschód, 8th Commercial Department, registered in the National Court Register an increase in the share capital of Magenta Grupa TAURON sp. z o.o. (Magenta GT), passed by the Extraordinary GM of the company on October 24, 2017. The subsidiary’s share capital was increased from PLN 500 000 to PLN 1 500 000, i.e. by PLN 1 000 000, by way of issuance of 20 000 new shares with the nominal value of PLN 50 per share and the total nominal value of PLN 1 000 000. All of the new shares were taken up by the subsidiary’s existing sole shareholder – TAURON. at the price of PLN 450 per share, i.e. for the total amount of PLN 9 000 000, where the surplus of the price of taking up each new share in the company’s increased share capital above its nominal value in the amount of PLN 400 per each new share, i.e. in the total amount of PLN 8 000 000 was allocated to the company’s spare capital.

Taking up shares in ElectroMobility Poland S.A.

On January 3, 2018 the Extraordinary General Meeting of the Shareholders of ElectroMobility Poland S.A. passed a resolution on increasing the company’s share capital from PLN 10 000 000 to PLN 30 000 000, i.e. by PLN 20 000 000, by way of increasing the nominal value of the existing shares from PLN 1 000 per share up to PLN 3 000 per share, as part of which TAURON took up, in proportion to the shares held, the increased nominal value of 2 500 shares held from the total amount of PLN 2 500 000 up to the total amount of PLN 7 500 000, i.e. in the total amount of PLN 5 000 000.

Purchase of shares in TAURON Dystrybucja Serwis

In conjunction with the August 9, 2017 conclusion of the agreement between TAURON and TAURON Dystrybucja on the transfer of shares in TAURON Dystrybucja Serwis in order to release TAURON Dystrybucja from the obligation to pay out a dividend to TAURON (datio in solutum), TAURON became the owner of 5 101 003 shares in TAURON Dystrybucja Serwis, used up to now from TAURON Dystrybucja, representing 100% of shares in its share capital.

Major investments in financial assets

TAURON Capital Group’s major investments in financial assets in the year ended on December 31, 2017 include:

1. Purchasing by TAURON, being the parent company, of participation units in investment funds for the total amount of PLN 75 000 thousand. As of the balance sheet day the value of participation units in investment funds reached PLN 101 358 thousand.
2. Granting by TAURON, being the parent company, of loans to the EC Stalowa Wola joint subsidiary for the total amount of PLN 304 192 thousand. As of the balance sheet day the amount of loans granted to EC Stalowa Wola reached PLN 570 432 thousand.

Investments in financial assets were finance using own funds and the funds obtained as part of the central financing model functioning at TAURON Capital Group. With respect to the above additionally it should be indicated that to finance the transactions: taking up of shares in the increased share capital of TAURON Dystrybucja and taking up of shares in the increased share capital of TAURON EKOENERGIA the funds coming from TAURON Eurobond issue that had taken place on July 5, 2017 were dedicated. Taking up of shares in the above indicated companies represented accomplishing the main goal of the issue stated in the Eurobond issue prospectus, according to which the funds obtained from the issue were to be used, first of all, to refinance the costs of constructing and purchasing wind farms and to finance the investments of TAURON Capital Group in the Distribution segment.

1.3. Strategy and strategic priorities of TAURON Capital Group

TAURON Group’s 2016-2025 Strategy (Strategy), adopted by the Management Board of TAURON on September 2, 2016 and positively evaluated by the Supervisory Board, was implemented in 2017. This Strategy is the response to the challenges stemming from the current and forecast situation on the electricity market and in the power sector. In the process of preparing the Strategy a thorough analysis was conducted of the macroeconomic, market and regulatory environment as well as of the forecasts on the directions of the sector's growth, including translating them into opportunities and risks facing TAURON Capital Group over the next ten years. TAURON Capital Group's ability to finance the current and planned investment projects was reviewed in detail with a view that their completion could be achieved using funds generated from operations and debt financing. The above analyses and market trends were the basis for verifying market and macroeconomic assumptions as well as the CAPEX plan.

1.3.1. TAURON Capital Group's mission, vision and values

Strategy defines the Mission and Vision and specifies the key values of TAURON Capital Group:

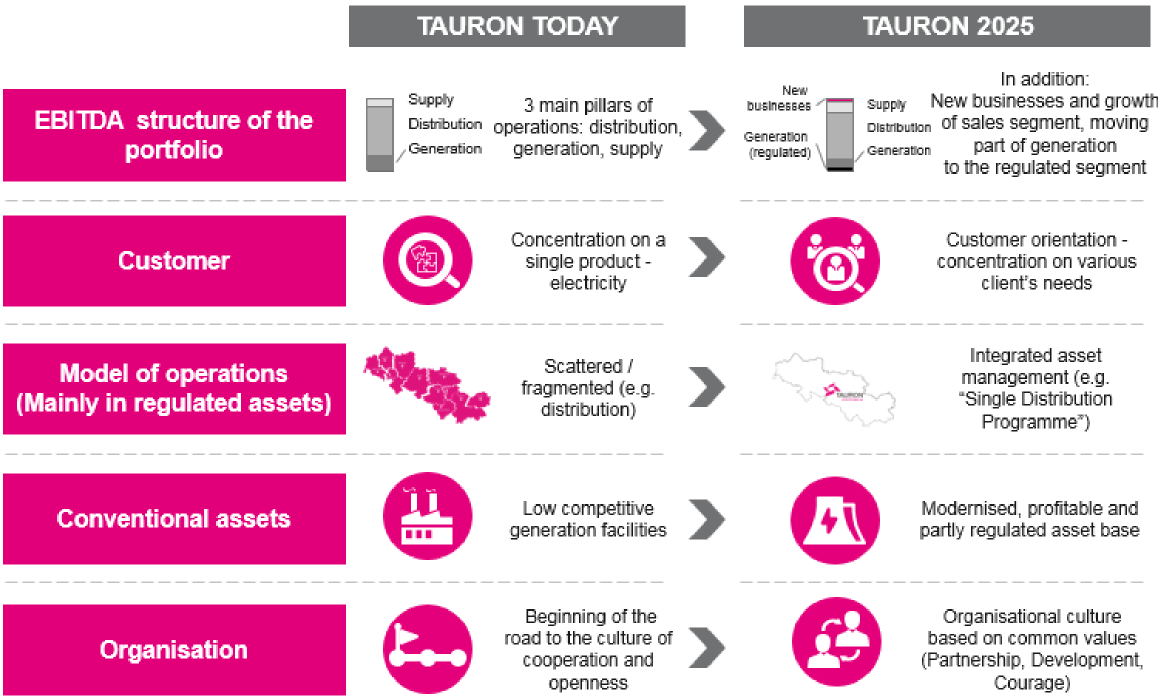
TAURON Capital Group's Mission
" With passion and commitment we are delivering modern solutions that provide energy in the constantly changing world."

TAURON Capital Group's Vision
"We are a company that best meets customer needs in the Polish energy industry."

Mission and vision best describe TAURON Capital Group's strategic intentions. The Supply segment and new products represent the field of operations that TAURON Capital Group is intensely developing. TAURON Capital Group is adjusting its profile in order to ensure full focus on the customer, while appreciating the potential of new products, compatible services, modern contact channels as a way to shape the response to customer needs.

The below figure presents TAURON Capital Group's 2025 Vision.

Figure no. 3. TAURON Capital Group's 2025 Vision



The key values that are to support the implementation of the Strategy include "Partnership", "Development" and "Courage". The values reflect the way in which TAURON Capital Group wants to achieve its goals. What is important as part of the partnership is customer orientation, development of sustainable relationships and engagement. Development means focus on innovations, developing competences, skills and knowledge and seeking ever better solutions meeting customer needs and raising the quality of services. Courage means boldness and openness, determination as well as engagement and passion in achieving common goals.

Combination of such values is to lead to a better understanding of customer expectations, responding to market challenges and developing TAURON Capital Group's organizational culture.

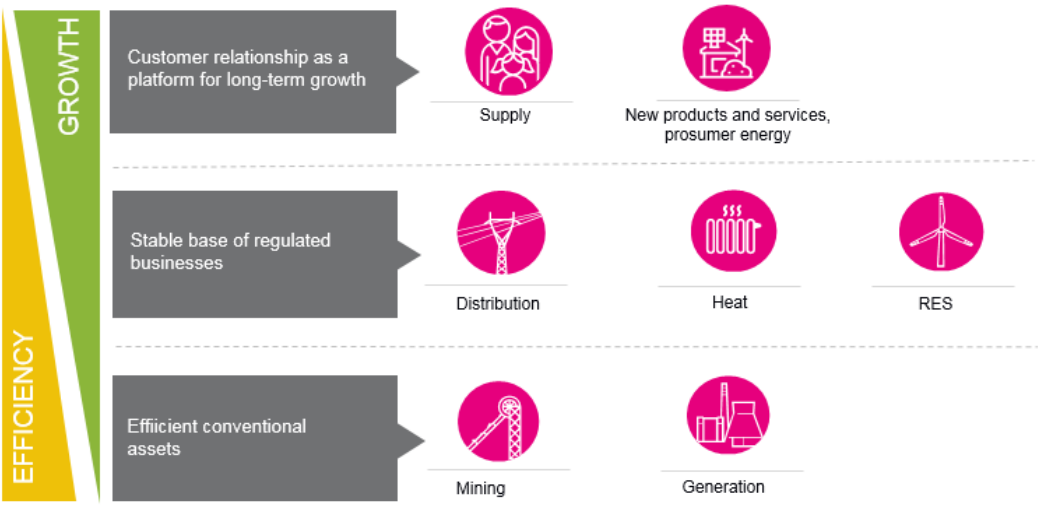
1.3.2. TAURON Capital Group's 2016-2025 Strategy

The adopted 2016-2025 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 relationships. The adopted mission and vision reflect new management philosophy and are in line with the customer-oriented growth concept.

Strategy describes the approach to developing individual segments of TAURON Capital Group's operations, dividing them into ones that TAURON Capital Group is planning to strongly expand, ones that will constitute the foundation of the financial stability and ones where strong emphasis on cost efficiency is required. The above reflects a new management philosophy and emphasizes a turn towards the customer and his/her needs as well as towards developing an innovative, open to new solutions TAURON Capital Group.

The below figure presents the prospects of TAURON Capital Group's segments

Figure no. 4. Prospects of TAURON Capital Group's segments



Strategy sets the priorities that will transform TAURON Capital Group into an innovative, aligned to the market and customer needs, growing energy company ultimately providing a return on invested capital for its shareholders.

1. Ensuring TAURON Capital Group's financial stability to be achieved through the following actions:
   a) TAURON Group's 2016-2018 Efficiency Improvement Program, adopted in March, 2016 and assuming achieving PLN 1.3bn in savings in 2016-2018. The above savings include actions resulting in the cumulative EBITDA increase by approximately PLN 1bn and involving CAPEX reduction by approximately PLN 0.3bn in 2016-2018.
   b) Strategic Initiatives and CAPEX reduction in 2017-2020 will bring a financial effect of PLN 1.9bn. It will be achieved as a result of actions leading to the cumulative EBITDA increase by approximately PLN 1.2bn and the CAPEX reduction by approximately PLN 0.7bn. These are additional financial outcomes, beside the effects generated by the Efficiency Improvement Program.
   c) Stopping the investment in the CCGT unit at Łagisza Power Plant, resulting in not incurring PLN 1.5bn in CAPEX. It will be possible to resume the project in case the regulatory and market environment turns favorable.
2. Building a strong capital group.

   Strategy defines a new approach to the value chain where key tasks are set for each Line of Business. Strategy does not assume balanced growth along each link of the value chain. Sales and development of new products and services are to constitute a strong base for the Group's growth. The Group is planning to rapidly develop its offering for the customers in this segment which will allow for retaining the existing base of customers that purchase TAURON products and increasing profitability. Electricity distribution as well as heat generation and distribution segments are to constitute a stable base of the Group's regulated businesses. Mining and conventional generation segments have tasks related first of all to efficiency improvement. The following three pillars of the strong capital group were defined:
   a) Customer relationships based on integrated high quality service with the use of modern sales and customer service channels as well as developing a product and service offering.
   b) Stable base of regulated assets based on the upgraded electricity distribution and heat segments as well as readiness to grow renewable energy sources in case the regulatory environment turns favorable.
   c) Efficient conventional assets, i.e. mining and conventional generation segments, which as a result of improving cost efficiency and productivity will be competitive on the market or, in case of generation assets, they will be shifted to the regulated segment of the power system.

3. Implementing organizational changes supporting the implementation of the Strategy that will transform Tauron Capital Group into a modern and innovative organization:

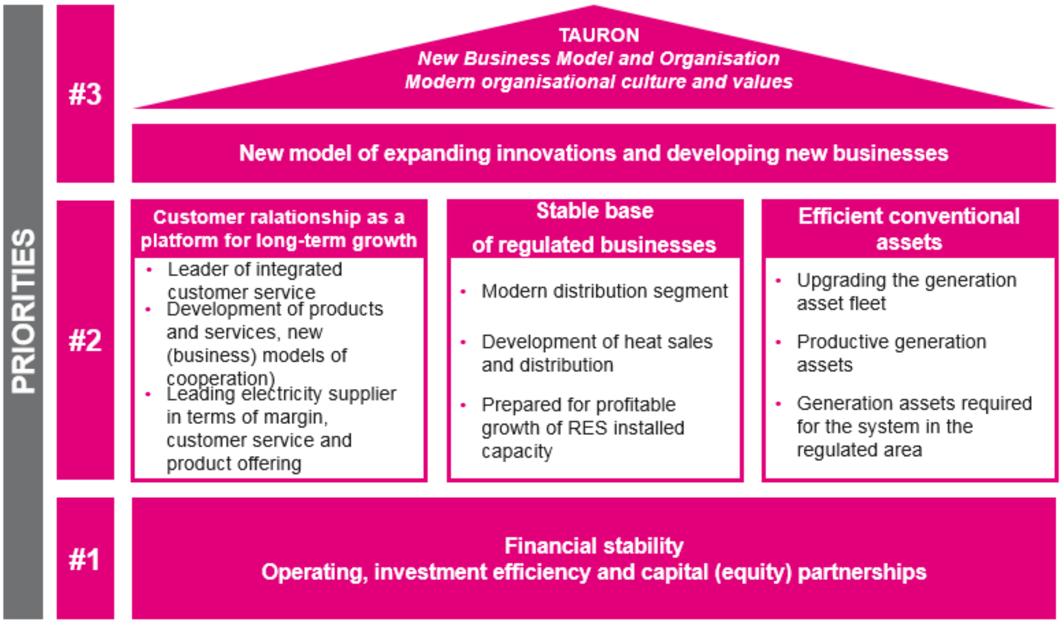
   a) Implementing a new, process-oriented operational model. Five priority process streams have been identified around which TAURON Capital Group's operations will be concentrated, i.e. Strategy, Finance, Asset Management and Development, Customer and Corporate Management and Support. Such approach will allow for placing a greater emphasis on cross-sectional issues that will determine TAURON Capital Group's competitive advantages in the future.

   b) Expanding research and development as well as innovative activities for which expenditures equal to 0.4% of the consolidated revenue a year are envisaged.

   c) Developing innovative projects based on the Corporate Venture Capital (CVC) type fund dedicated for this purpose or similar solutions.

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

Figure no. 5. Implementation of priorities based on the pillars of TAURON Capital Group's Strategy



The implementation of the Strategy will allow for increasing EBITDA from PLN 3.5bn in 2015 to more than PLN 4bn in 2020 and to more than PLN 5bn in 2025. Estimated, recurring effect of implementing the Efficiency Improvement Program in the form of an impact on the Group's EBITDA will be approximately PLN 0.4bn starting from 2018, while the effect of implementing the Strategic Initiatives in the form of an impact on the Group's EBITDA will be approximately PLN 0.3bn beyond 2020.

As part of rationalizing CAPEX the expenditures planned for 2016-2020 were reduced from PLN 20.2bn to approx. PLN 18bn. It is assumed that the commenced and well advanced investment projects will be continued. The detailed analysis revealed that 75 percent of the CAPEX plan until 2020 are tasks that are either a continuation or are related to keeping the commitments made. Such tasks include the investment in the 910 MW unit at Jaworzno III Power Plant as well as the contracted or resulting from regulatory requirements tasks in the distribution segment. Resigning or delaying these tasks would have a negative impact on the Group's value or is impossible due to legal or safety reasons.

In the Mining segment investments at Janina coal mine and the construction of Grzegorz shaft at Sobieski coal mine will be continued and the planned investments at Brzeszcze coal mine will be carried out. CAPEX in this line of business is approximately PLN 1.3bn until 2020.

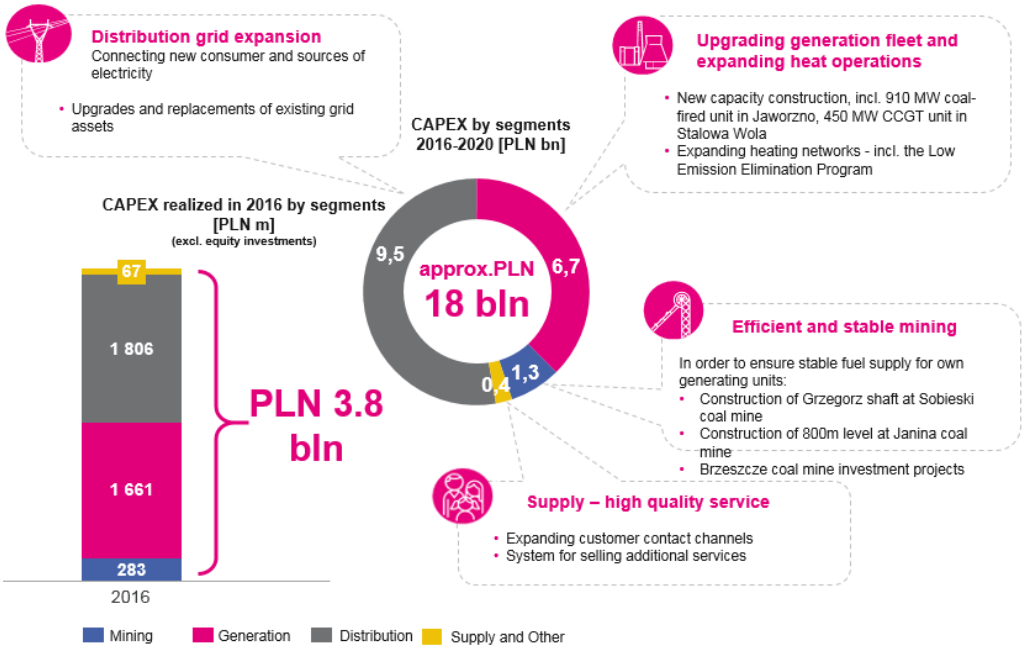
In the Generation segment investments in the construction of the 910 MW unit at Jaworzno III Power Plant and the CCGT unit at Stalowa Wola Combined Heat and Power Plant as well as the investments in the heating networks will be continued. TAURON assumes that the construction of the 910 MW unit at Jaworzno III Power Plant will be carried out under a new financing formula envisaging spinning off of an organized part of the enterprise and selling its shares to third party partners, provided they do not acquire a controlling stake. A change of the way the unit's construction is financed would reduce the net debt/EBITDA ratio, and thus significantly lower the risk of breaching the threshold value of this covenant (3.5x) defined in the financing agreements.

Strategy assumes maintaining financial stability and not breaching the net debt/EBITDA covenant of 3.5x without taking into account selling a minority stake in the construction of the 910 MW unit to third party partners. This means that the planned change of this project's financing formula represents an additional element that would stabilize TAURON Capital Group's financial position. Generation segment's capital expenditures amount to PLN 6.7bn until 2020.

More than 50 percent of the entire CAPEX, i.e. PLN 9.5bn by 2020, are investments in the Distribution segment that include connecting new customers and generation sources as well as upgrading and replacing grid assets

The below figure presents capital expenditures by segments in 2016-2020.

Figure no. 6. Capital expenditures by segments in 2016-2020



With respect to innovative as well as research and development activities the Strategy assumes expenditures equal to 0.4% of the consolidated revenue a year.

The overall objective in terms of CAPEX is to align the investment portfolio to the market needs.

In particular the actions to be undertaken will be aimed at:

1. Optimizing the asset structure in all lines of business and achieving compliance with the environmental requirements.
2. Carrying out only those investment projects that guarantee the expected return on capital and are not burdened with material market risks.
3. Using off-balance sheet forms of financing, in particular by engaging third party partners.
4. Reviewing investment projects in the conventional generation segment, provided mechanisms that guarantee revenue are introduced (e.g. capacity market or another form of regulation).
5. Investing in projects in sectors that are related to the power industry (in particular, services) in order to complement the value chain that TAURON is operating in, and also developing a high margin services offering.

Assumed directions of investments beyond 2020 include first of all the regulated segments of the power sector (i.e., among others, electricity distribution, heat generation and distribution, participation in the nuclear power generation and regulated conventional generation) and the new power industry (i.e. e-mobility, distributed heat and electricity generation, power generation by prosumers, Smart Home, Smart City solutions and energy related services). Strategy assumes that in 2020-2025 TAURON Capital Group's estimated investment potential will be more than PLN 6bn.

1.3.3. Key challenges for TAURON Capital Group

Strategy is TAURON Capital Group's response to the challenges posed by the business environment and the requirements of the energy sector's customers that have been changing fast over the last few years.

Strategy defines four key challenges facing TAURON Capital Group: regulations, market, customer and technologies.

Regulacje

Introduction of the dual-product market – capacity market, the European Union's (EU) decarbonization policy and successive regulations aimed at reducing emissions, introduction of the quality based regulation in the distribution segment, changes to the support for RES installations and EU actions aimed at developing a common electricity market.

Rynek

Changing forecasts of electricity prices, hard coal oversupply and prices, demand for electricity, demand for capacity, growing competition on the retail market, rising level of RES generation along with the withdrawal of the European players and the reduction of the financing for the conventional power generation.

Klient

Growing awareness of the customers and the requirements with respect to satisfying their needs as well as comprehensiveness of the offering, increased expectations with respect to customer service quality and availability.

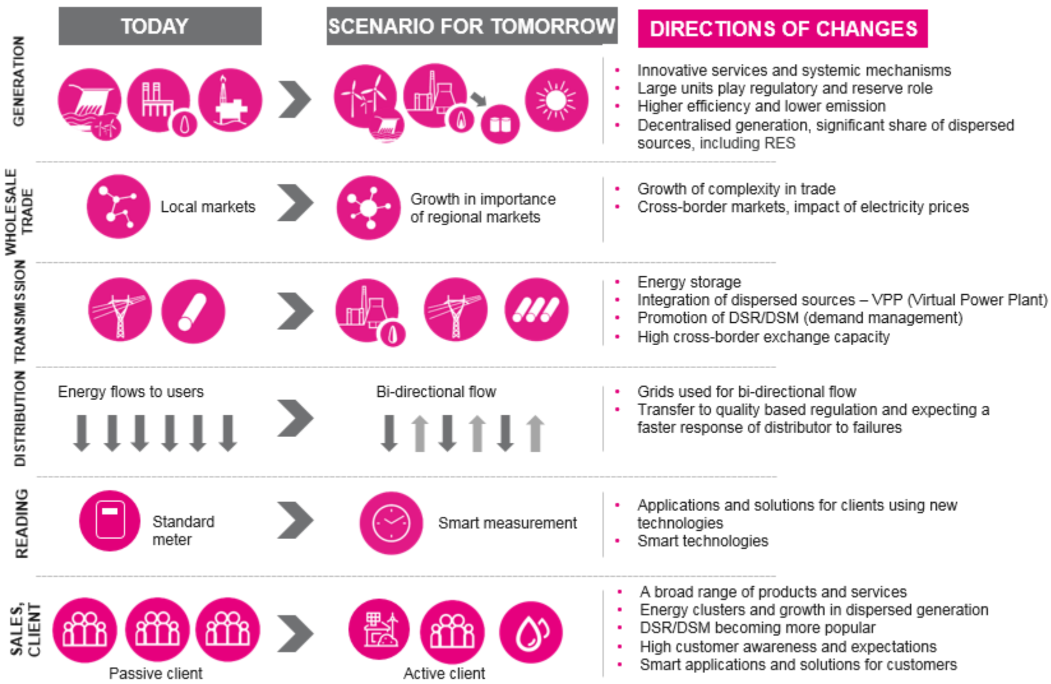
Technologia

Falling prices of renewable and dispersed technologies, rising competitiveness of such sources versus conventional sources, a change of the role of the distribution service due to the expansion of dispersed power generation, advancement of smart technologies, microgeneration and energy storage.

In the long term profound changes of the entire power sector, towards the so-called "power industry of tomorrow", are important. A transformation of the system power sector towards decentralized generation, increased role of transborder connections, energy storage and new energy services, as for example "virtual power plants", demand side management, dispersed generation. This also leads to a change of the role of the distribution segment that must deal with smart technologies, electric vehicle charging infrastructure, distributed generation, including prosumers, bi+directional flows, while at the same time raising the quality and security of supplies.

The below figure presents the key challenges facing TAURON Capital Group.

Figure no. 7. Key challenges facing TAURON Capital Group



1.3.4. Opportunities and threats

The defined key challenges facing TAURON Capital Group create both opportunities as well as threats for TAURON Capital Group's operations.
The below table presents opportunities and threats for TAURON Capital Group's operations

Table no. 4. Opportunities and threats for TAURON Capital Group's operations

Opportunities	Threats
Regulations	
• Introduction of the dual-product market – additional revenue for maintaining generation capacity. • Support for electromobility (growing electricity consumption). • Introduction of legal regulations supporting the reduction of low emissions (e.g. system district heating, increasing the share of eco-pea coal in the sales). • Expected support for the cogeneration beyond 2018	• Rising costs of electricity production from conventional assets, growing environmental costs and further tightening of the decarbonization policy. • Negative impact of the EU regulations related to the common energy market. • Lack of stability and predictability of the regulations for the RES sources, including rising costs of maintaining wind farms and hydro-electric power plants as well as uncertain future of the RES sources based on the biomass burning and co-firing technology (RES directive draft). • Lack of support for the cogeneration beyond 2018
Market	
• Cost effective, own mining assets, competitive on the Polish market, allowing for stabilization and predictability of the fuel cost. • Access to the largest, among Poland's energy companies, customer base. • Entry to the energy related services market segments based on the competences held. • Commercialization of innovative solutions developed as part of research and development operations.	• Declining margins and lower utilization of conventional assets (deteriorating profitability, required outlays for upgrades or the need to shutdown old generating units due to the new high efficiency units entering the system and due to the BAT requirements). • Loss of volume and profitability of the Supply Segment, in particular in the B2B area. • Pressure on electricity prices with the growing transborder exchange volumes. • Rising costs and limited availability of financing. • Increased prices of products and services negatively impacting investment efficiency.
Customer	
• Competitive advantage with respect to customer service quality. • Customer segmentation and offering additional products in line with customer expectations. • Greater customer awareness and expectations towards comprehensive, personalized offering of additional services and products (greater customer product saturation). • Expanding an offering of services for customers based on competences held and trust in TAURON brand. • Growth through concentration on a customer that is not generating large capital investments. • Developing modern and integrated sales and customer service channels. • New competences and business models based on research and development operations. • Maintaining an upward trend in electricity consumption trend by final consumers.	• Potential loss of customers due to an increase in the number of competitors offering customers similar products and due to low electricity supply market entry barriers. • Decreasing customer loyalty – growing number of supplier switchings. • Greater customer awareness and requirements with respect to service quality and product offering. • Power independence of consumers (prosumers, energy (power) islands, clusters). • Energy intensive consumers building their own generation sources, as a result of the drive to reduce electricity costs. • "Carbon leakage" – moving business operations to other countries due to the cost of energy.
Technologies	
• Falling prices of renewable technologies. • Advancement of storage technologies, smart technologies and technologies related to dispersed (distributed) generation. • Additional services for customers related to new technologies (internet of things, dynamic tariffs, virtual power plants). • Advancement of dispersed (distributed) power generation, including prosumers. • Developing and implementing (commercializing) of own innovative solutions that provide a competitive advantage.	• The need to adapt the grid to the growth of dispersed (distributed) power generation (bi-directional flows). • Arrival of new, cost competitive electricity generation technologies in countries neighbouring with Poland.

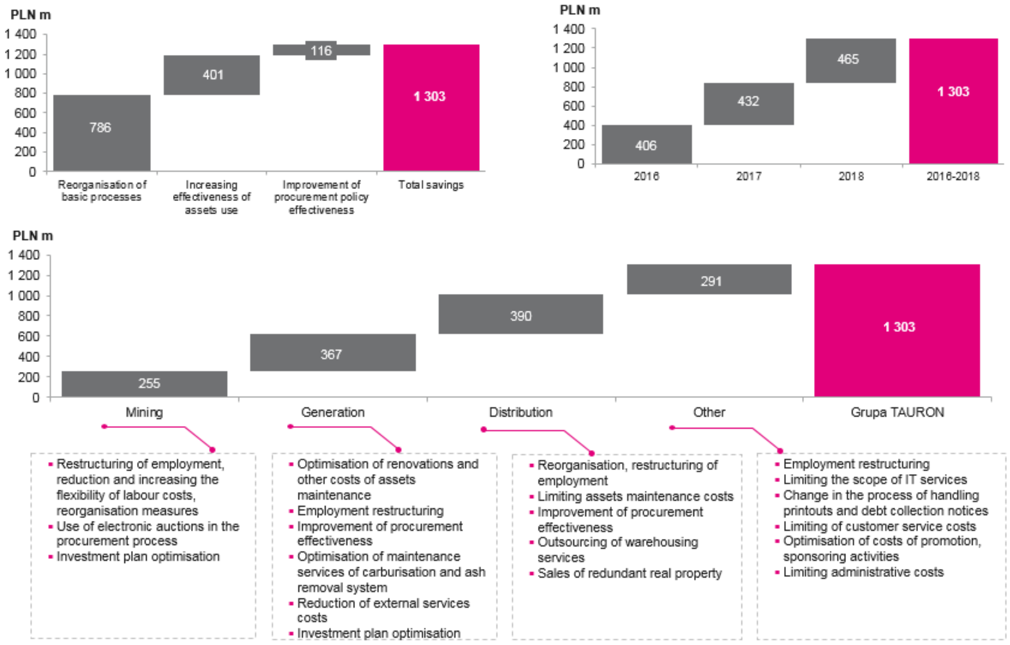
1.3.5. Implementation of the Strategy and priorities of TAURON Capital Group in 2017

2017 was the time when the first effects of the Strategy adopted in September 2016 were achieved. In accordance with the Assumption the most important priority was to ensure financial stability in order to lay down solid foundations for the expansion of TAURON Capital Group. As part of the Strategy actions in the form of Strategic Initiatives were taken and the Efficiency Improvement Program was continued, involving reorganizing core processes throughout TAURON Capital Group and raising asset utilization efficiency. Strategy is implemented by:

1) Achieving TAURON Capital Group's strategic objectives, which are:
   - EBITDA above PLN 4 bln in 2020. The objective is being achieved through actions related to the implementation of the Strategic Initiatives and initiatives carried out as part of the Efficiency Improvement Program the implementation of which in 2017 brought higher returns than planned at the stage of developing the Strategy. In 2017 EBITDA of more than PLN 3.5 bln was achieved, this is a better result than in 2016 when EBITDA of more than PLN 3.3 bln was achieved.
   - Maintaining the net debt/EBITDA covenants below 3.5. One of the priorities of the Strategy is to ensure financial stability. Maintaining the covenants is both an effect of actions leading to improved financial results as well as actions aimed at improving investment efficiency. As part of the Strategy the investment portfolio was optimized and modern financing in the form of a hybrid bond issue was obtained. At the end 2017 the net debt/EBITDA ratio reached 2.3x.
   - Maintaining a high Customer Satisfaction Index (CSI). TAURON Capital Group is an industry leader in customer service quality. Annual customer satisfaction surveys performed by an external company confirm a high satisfaction level of TAURON Capital Group's customers. The overall result of the September 2017 survey proved maintaining a high 2016 index level of 80 points.
   - Power plants generating positive cash flows by 2020. Achievement of this goal will be the result of a number of actions undertaken within TAURON Capital Group, among others: optimizing the costs of the generating units and TAURON Capital Group's trading (commercial) strategy, as well as the impact of the external environment, both the regulatory one, as well as the market one (support for RES and cogeneration, fuel prices, property rights prices, electricity prices).
   - Maintaining the customer base. TAURON Capital Group is Poland's distributor and the second largest electricity supplier. Maintaining the customer base represents for TAURON Capital Group a long term growth platform and is implemented by both, actions improving the quality of services, among others an expansion of customer communications channels, as well as a broad product offering. At the end of 2017 TAURON Capital Group provided services for almost 5.4 mln customers of the Supply Segment and more than 5.5 mln customers of the Distribution Segment.
   - Unit margin leader among Poland's largest 4 electricity suppliers. Maintaining the leader's position is based both on maintaining a high volume of electricity supplied, as well as the ability to generate a positive financial result. TAURON Capital Group, by concentrating on the customer, is developing a broad, profitable base of products and services offered to our customers. Based on the data for 9 months of 2017 TAURON Capital Group maintained the leading position among Poland's largest 4 utilities.
   - New businesses are to represent at least 25% of revenue/margin in 2025. This objective is to be a response to the challenges posed by the competitive environment. Achieving climate improvement targets and building the European energy market will have an impact on the increase of competition in the power sector, therefore actions are undertaken aimed at developing new businesses and we place our bets on innovations.
2) Efficiency Improvement Program, adopted in March, 2016 and assuming achieving PLN 1.3 bln in savings in 2016-2018. The above savings include actions resulting in the cumulative EBITDA increase by approximately PLN 1 bln and involving CAPEX reduction by approximately PLN 0.3 bln in 2016-2018 within three scopes of operations.

The below figure presents the 2016-2018 Efficiency Improvement Program.

Figure no. 8. 2016-2018 Efficiency Improvement Program

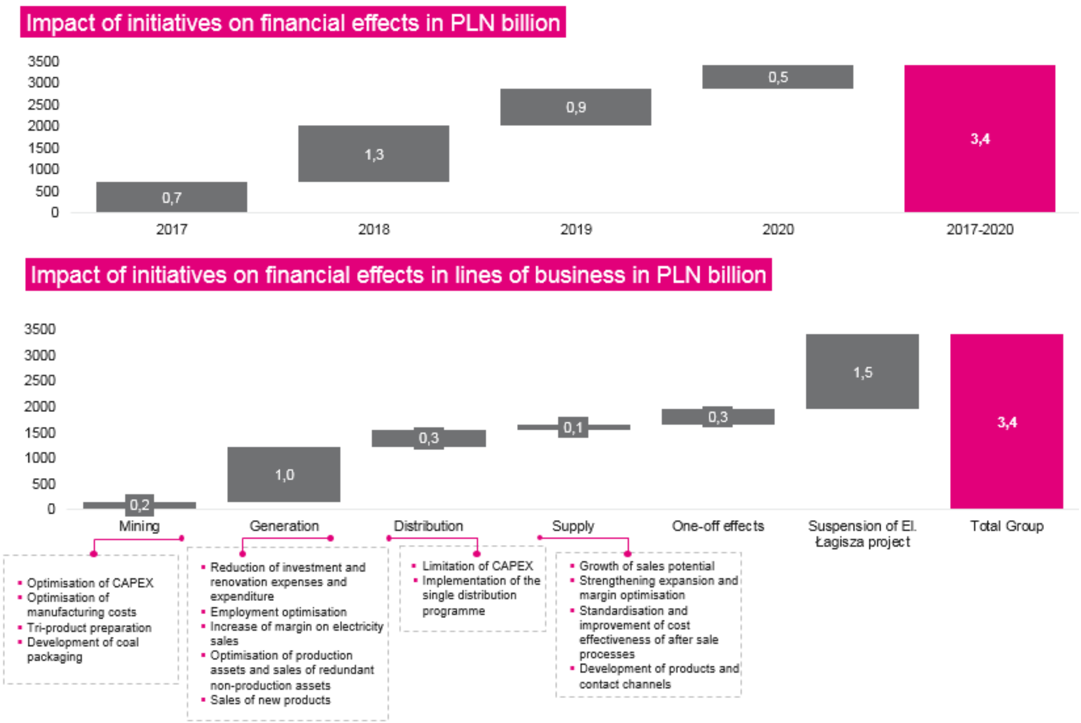


TAURON Capital Group's Efficiency Improvement Program brought, in 2016-2017, savings of PLN 1 091 mln which represents 84% of the planned savings, out of which PLN 640 mln impacted EBITDA, while PLN 451 mln was applicable to CAPEX savings. The largest contribution to the savings achieved came from the Generation Line of Business.

3) Strategic Initiatives and CAPEX rationalization in 2017-2020 assuming financial effects of PLN 3.4 bln, including the cumulative EBITDA increase by approximately PLN 1.2 bln, CAPEX reduction by approximately PLN 0.7 bln and stopping the investment in the new unit at Łagisza Power Plant worth PLN 1.5 bln.

The below figure presents Strategic Initiatives and CAPEX rationalization in 2017-2020.

Figure no. 9. Strategic Initiatives and CAPEX rationalization in 2017-2020



In accordance with the objectives set TAURON Capital Group will be expanding the Supply Line of Business and customer service. In this respect a further introduction of coherent, high customer service standards in each area of the value chain and the growth of modern and integrated sales and customer service channels is planned.

In the Distribution Line of Business the "Single Distribution" program based on actions related to unifying the processes and systems as well as implementing an optimal and coherent structure of TAURON Dystrybucja so as to improve operational and investment efficiency of this Line of Business will be continued.

In the Mining and Generation Lines of Businesses tasks related to a further improvement of the cost and investment efficiency will be carried out. The introduction of the detailed regulations related to the capacity market in Poland and the planned auctions related thereto will be important for the generation assets.

In 2017 Strategic Initiatives brought a financial effect of PLN 937 mln, out of which PLN 320 mln impacted EBITDA, while PLN 617 mln was applicable to CAPEX savings (including PLN 428 mln due to stopping the Łagisza investment project). The largest contributions to the savings achieved came from the Generation (PLN 314 mln) and Distribution (PLN 103 mln) Lines of Business.

In 2018 TAURON Capital Group's largest investment projects will be continued in line with the adopted Strategy, including:

i. in the Mining Line of Business: construction of the Grzegorz shaft, 800 m level at Janina Coal Mine and investment projects at Brzeszcze Coal Mine,

ii. in the Generation Line of Business: construction of the 910 MW hard coal-fired unit in Jaworzno, the 450 MW CCGT unit in Stalowa Wola,

iii. in the Distribution Line of Business: investment tasks related to the grid construction and upgrading.

Furthermore, the Low Emission Elimination Program in the Silesia and Dąbrowa conurbation as well as the project related to implementing heat production at unit no. 10 and construction of peaking and backup boilers at Łagisza Power Plant, as a consequence of planned shutdown of 120 MW units at this site, will be carried out.

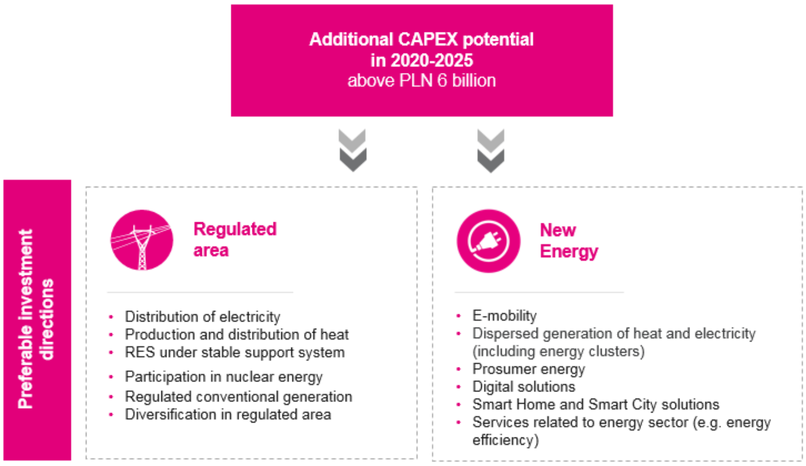
1.4. Description of TAURON Capital Group's expansion policy and directions

Strategy sets the directions of TAURON Capital Group's short and long term expansion. The tasks for TAURON Capital Group's individual Lines of Business were defined in detail until 2020 and the financial effects for such tasks were set. The priority is to maintain stable financial position and lay down solid foundations for growth in a changing environment. This priority is to be achieved through the Efficiency Improvement Program and Strategic Initiatives aimed at the cost and investment optimization. It is planned that by 2020 PLN approximately 18 bln worth of CAPEX will be spent, with more than half on the distribution assets generating TAURON Capital Group's most stable revenue. Strategy sets the priority directions for the innovations as well as research and development activities that will be the basis for developing new products and services in the longer term. In order to achieve this goal TAURON Capital Group adopted a new model for the innovations as well as research and development activities, setting up a dedicated central organization for managing and coordinating such operations and allocating a budget of 0.4% of revenue thereto.

In the longer term Strategy assumes full utilization of the potential of TAURON Capital Group's assets, supporting innovations, organizational culture and, first of all, the broad customer base. Strategy assumes that in 2020-2025 TAURON Capital Group will gain an additional CAPEX potential in the region of approximately PLN 6 bln to be used for projects that will generate value for TAURON Capital Group in the longer term. TAURON Capital Group will be investing in the regulated areas such as electricity distribution as well as heat distribution and generation, RES (on the condition of a stable support system), regulated conventional generation and in the new power sector, e.g. electromobility, dispersed (distributed) electricity and heat generation, smart solutions.

The below figure presents the outlook for CAPEX directions beyond 2020.

Figure no. 10. Outlook for CAPEX directions beyond 2020



TAURON Capital Group's main competitive advantage is the base of 5.5 mln customers. The most important actions in the short and long term will be relatively low capital intensive actions related to an expansion of the product and service offering for the consumers and developing new operations based on TAURON Capital Group's competences. Strategy assumes that in 2025 new businesses will be generating approx. 25% of the total margin or revenue from the Supply Segment's sales.

1.4.1. Long term goals and financial assumptions of the Strategy

Actions defined in the Strategy will allow for achieving the set key goals for TAURON Capital Group:

1) EBITDA above PLN 4 bln in 2020
2) Maintaining the net debt/EBITDA covenants below 3.5x
3) Maintaining a high Customer Satisfaction Index (CSI)
4) Power plants generating positive cash flows by 2020
5) Maintaining the customer base
6) Unit margin leader among Poland's largest 4 electricity suppliers
7) New businesses will represent at least 25% of revenue/margin in 2025

The below figure presents the 2025 EBITDA outlook taking into account the risks and the implementation of the Strategy as well as the effects of the implementation of the Strategy.

Figure no. 11. 2025 EBITDA outlook taking into account the risks and the implementation of the Strategy as well as the effects of the implementation of the Strategy

Actions planned for the coming years will allow for stopping the profitability decline. This will be achieved by optimizing operations in the Generation and Mining Segments while at the same time maintaining stability in the Distribution Line of Business.

1.4.2. Implementation of strategic investment projects

Nuclear power plant construction project

On February 15, 2017 PGE EJ 1's share capital increase was registered in the National Court Register, in line with the resolution passed by the Extraordinary GM of the PGE EJ 1 special purpose vehicle on December 21, 2016. The share capital was increased from PLN 275 859 450 to PLN 310 858 470, i.e. by PLN 34 999 020, by way of issuance of 248 220 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 34 999 020. TAURON took up 24 822 new shares with the nominal value of PLN 141 per share and the total nominal value of PLN 3 499 902, paid for by cash in the amount of PLN 3 499 902.

On September 3, 2014 TAURON, ENEA S.A. (ENEA) and KGHM Polska Miedź S.A. (Business Partners) concluded the Partners' Agreement governing the rules of cooperation in the implementation of Poland's first nuclear power plant construction project. On April 15, 2015 the above entities concluded the agreement on the purchase of shares in PGE EJ 1 - a special purpose vehicle responsible for preparing and implementing an investment project involving the construction and operation of a nuclear power plant with the capacity of approximately 3 thousand MWe (Project). Each Business Partner acquired from PGE a 10% stake (30% of shares in total) in the PGE EJ 1 special purpose vehicle. TAURON paid PLN 16 044 000 for the acquired stake. This way one of the commitments under the Partners' Agreement, according to which the parties undertook to jointly, in proportion to the stakes held, finance operations as part of a project milestone, was fulfilled

The Partners' Agreement envisages that the successive decisions related to the project, including the decision on the declaration to further continue participation in a subsequent project stage by the individual parties (including TAURON), will be taken following the completion of the preliminary stage.

In 2017 PGE EJ 1 carried out the scope of the works related to conducting environmental and siting research at Żarnowiec and Lubiatowo-Kopalino sites.

Coal gasification project

On April 20, 2017 TAURON signed a letter of intent with Grupa Azoty S.A., defining general rules of commencing cooperation aimed at implementing the coal gasification project.

The product of the technological process system that the letter of intent is applicable to is primarily the synthesis gas (syngas) with the composition that would allow using it directly to produce hydrogen, ammonia, methanol or other chemicals. The parties came to the conclusion that the current natural gas consumption in the nitrogen fertilizers manufacturing industry could partly be replaced with the synthesis gas (syngas) obtained as a result of coal gasification. This opens new prospects for the mining industry, increasing Poland's security of electricity supply by developing low emission technology.

The project is at the preFeed (Preliminary Front End Engineering Design) and accompanying analyses, including market research, stage. As part of the project Grupa Azoty commissioned works related to documentation, in particular a preliminary selection of licensors and updating of the analyses. The Project's estimated value will reach between EUR 400 mln and EUR 600 mln, depending on the selected technology version.

TAURON has declared its participation in the Project's implementation in accordance with the rules that will be defined by the Parties in separate agreements, including assuming selecting and completing an installation that would ensure maximizing the use of hard coal coming from TAURON Capital Group's coal mines. If TAURON is not able to provide appropriate quantity or parameters of coal required by the installation, it shall be permitted to supplement the supply with coal coming from other suppliers.

The letter of intent expresses the readiness of the parties to commence talks and defines the general cooperation framework and does not cause, at the current stage, any financial or management implications for either Party. The Parties declared an intention to cooperate and expressed the will to sign further agreements, including agreements related to establishing a joint special purpose vehicle (SPV) to carry out the project. Either Party shall have the right to terminate the letter of intent at one month's notice.

CCGT unit construction project at Elektrownia Blachownia Nowa sp. z o.o.

On December 19, 2017 the Extraordinary GM of Shareholders of Elektrownia Blachownia Nowa sp. z o.o. in liquidation confirmed, through applicable resolutions, the completion of the company's liquidation process. The remaining assets (funds) were split into two equal parts and transferred to KGHM and TAURON Wytwarzanie.

The above was the consequence of the agreement signed on July 28, 2016 between: TAURON, KGHM and TAURON Wytwarzanie, under which the companies decided in unison to withdraw from implementing the CCGT unit construction project at Elektrownia Blachownia Nowa sp. z o.o., suspended since 2013, and terminate the Partners' Agreement signed between KGHM and TAURON Wytwarzanie, and also to proceed to the liquidation of Elektrownia Blachownia Nowa sp. z o.o.

1.4.3. Evaluation of the capability to complete the intended investment projects

TAURON Capital Group's strategic investment projects and the financing thereof are centrally managed at the Company's level. Based on the analyses completed the Company's Management Board assesses that TAURON Capital Group is able to finance the current and future intended investment projects included in the Strategy using funds generated from operations and obtaining debt financing.

1.4.4. Building TAURON Capital Group's value

TAURON Capital Group is conducting operations in all key segments of the energy market, i.e. hard coal mining as well as electricity and heat generation, distribution and trading. Strategy assumes that each Line of Business will be building TAURON Capital Group's value, but in a manner aligned to the market conditions for the given segment. Supply Line of Business as well as the new products and services represent the field of operations that will be intensely expanded by TAURON Capital Group. TAURON Capital Group is changing its profile towards full concentration on the customer. This is achieved by building sustainable relationships with customers, introducing consistent, high customer service standards in each link of the value chain, modern and integrated sales and customer service channels (omnichannel and e-commerce), adapted to today's highest standards. Supply segment and customer service will the main drivers for building TAURON Capital Group's value. Electricity Distribution Line of Business is the most stable line of business in terms of contribution to generating TAURON Capital Group's EBITDA. TAURON Capital Group is planning to maintain a stable role of the Distribution Line of Business and continue the up to now investment policy. Through further upgrades and expansion of its distribution grid TAURON Capital Group will be able to meet the requirements in terms of security and quality of supplies. Generation and Mining Lines of Business will continue to improve the cost and operating efficiency, while a potential expansion of the conventional generation will depend on the market situation or favorable regulations for the conventional generation.

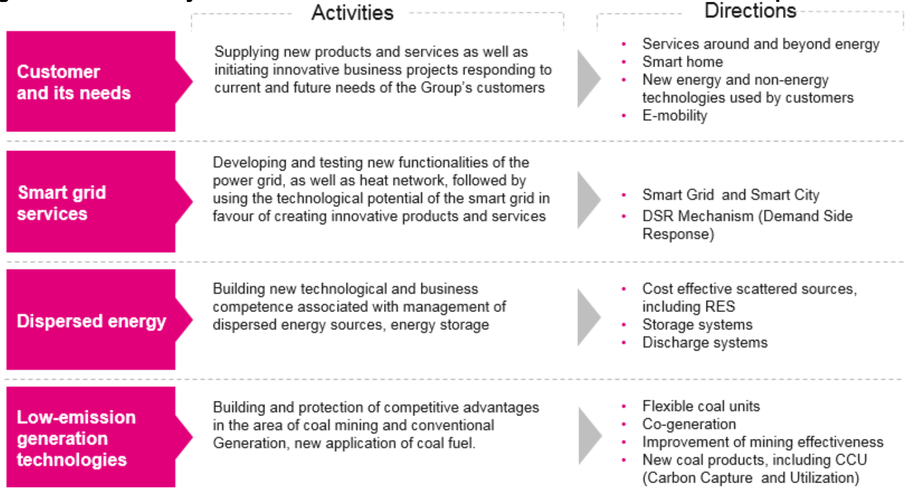
1.4.5. Directions for advancing innovations as well as research and development activities

In its adopted Strategy TAURON Capital Group places its bet on a dynamic expansion of the research and development as well as innovations line of business (R+D+I), viewing it as a way to achieve new revenue in the future. It is assumed that, starting from 2017, minimum 0.4% of consolidated revenue will be spent on R+D+I, as well as on expansion based on, among others, Corporate Venture Capital (CVC) and long term return on the portfolio, and also an annual revision depending on the financial position.

The research and development as well as innovations line of business (R+D+I), in line with the Strategy, introduced portfolio based management of research and development projects in accordance with the priority directions of innovations as well as research and development activities.

The below figure presents the priority directions of innovations as well as research and development activities.

Figure no. 12. Priority directions of innovations as well as research and development activities



The directions of innovations as well as research and development activities were taken into account in the works on developing the Strategic Research Agenda (SRA) conducted in 2017. This document will constitute a conversion of the goals indicated in the Strategy into a ”road map” for the R+D+I operations of TAURON Capital Group, accommodating the specifics of the challenges in each of the above four directions and at the same time reaching in the adopted timeframe beyond the timeline of the current Strategy in force.

Additionally, process based management introduced in the R+D+I line of business provided more effective and timely implementation of the R+D portfolio projects by TAURON and TAURON Capital Group’s subsidiaries. The change of the line of business operations’ organization ensured effective supervision of the Corporate Center over the R+D projects’ implementation by TAURON Capital Group’s subsidiaries and management of financial and non-financial resources.

1.4.6. Major achievements in the field of research and development

In 2017, TAURON has been continuing and also initiating research projects, among others, in the European programme Horizon 2020 and the Sectoral Electricity Research Program (PBSE) addressed to the electricity sector.

With co-financing from the Horizon 2020 program, the company has been working on the following projects:

- *An Integrated Collaborative Platform for Managing the Product-Service Engineering Lifecycle - ICP4Life*. This project’s deliverables are to provide the companies of TAURON Capital Group with a new platform of collaboration between the energy supplier and customers, with entirely new products to be develop on this platform.
- *Motivating end-users Behavioral change by combined ICT based tools and modular Information services on energy use, indoor environment, health and lifestyle*. The overarching goal of the project is to introduce to the market the technology solutions that will allow to positively influence customer behaviours by raising consumer awareness and sense of ownership. The project was commenced in October 2016 and its results will be tested in five showcase premises in five EU Member States, including implementation of the AMIPlus initiatives in Wrocław.

In 2017 TAURON launched a new project under the Horizon 2020 program under the name of ”*Transformation of an electricity supplier’s business model with a view to energy efficiency based on changing human behaviors and the use of information and communications technologies*”. The project activities are aimed at implementing a solution that will increase electricity efficiency consumption by actively engaging customers in their behaviors related to electricity consumption with the use of information and communications technologies as well as DSM mechanisms.

In 2017, work was progressing on launching the projects under the PBSE organised by the National Centre for Research and Development. Two year long preparations by the companies of TAURON Capital Group resulted in obtaining co financing for 8 R&D projects, including TAURON obtaining co financing for 2 projects. These projects cover the work on a system for optimising operation of conventional generating plants and development of creation of local electric grids – micro grids. It is expected that the Sectoral Programme will provide support to intensification of implementation of innovations in the energy sector, and that the follow up contests announced under this Programme will also be supporting the directions of work conducted by TAURON Capital Group.

In 2017 TAURON continued activities with respect to building mechanisms for cooperation between industry and science as well as between industry and startups. In this regard the participation in the works of the Technology and Innovations Highway Institute (Instytut Autostrada Technologii i Innowacji), set up in 2014, that is the new platform for cooperation between industry and Polish universities, took place. In the Pilot Maker program, co-financed by the Polish Agency for Enterprise Development (PARP) as part of the Scale Up competition, 3 startup selection processes were carried out. Since the beginning of 2017 in the entire program TAURON reviewed almost 130 solutions prepared by startups. i.e. 46 in the first selection process, 23 in the second selection process and 60 in the third selection process. 30 startups began cooperating with TAURON on preparing solutions in response to the technological challenges defined by TAURON Capital Group. Currently 26 startups are testing their solutions on TAURON’s infrastructure or preparing their solutions for such tests (pilots). The program’s leader is techBrainers sp. z o.o., the main partner is TAURON, the other partners are well known companies Kross S.A. and Amplus sp. z o.o.

In 2017 TAURON Capital Group was carrying out works as part of KIC InnoEnergy, in particular the Polish node of InnoEnergy Central Europe sp. z o.o. with its seat in Kraków (one of six in the EU). Within the structures of KIC InnoEnergy TAURON holds the Associated Partner status. One of TAURON’s areas of interests are the so-called clean coal technologies. At the same time conducting of tests and coordinating of activities in this area are the main tasks of CC Poland Plus sp. z o.o., of which TAURON is one of the shareholders. In 2017 the Company’s representatives were engaged in the works of KIC InnoEnergy, related to evaluating projects/initiatives proposed to be implemented by other partners operating within the structures of KIC InnoEnergy, both on the national, as well as international level.

In 2017, TAURON has received several awards relating to its Research, Development and Innovation activities. Gazeta Bankowa has for the 15th time awarded its "Leader" title to institutions that in 2016 have performed the most interesting implementations in several industries. TAURON was awarded the second prize in energy, fuel and chemicals category for implementation of the "Innovation Zone" at the TAURON Capital Group that allows company employees to submit solutions that improve effectiveness of operation of the entire organisation.

In 2017, at the Grand Gala of Leaders of the Energy World and Production at the EuroPOWER conference, TAURON was awarded a prize in the "Leaders of the Energy World and Production" competition for the energy industry's first start-up accelerator programme – the PilotMaker. Additionally, for its participation in the PilotMaker programme, TAURON received the Wprost 2017 Innovator prize in energy industry category.

2. TAURON POLSKA ENERGIA S.A. OPERATIONS

2.1. Factors and non-typical events that have a significant impact on earnings achieved

2.1.1. Internal factors and the assessment thereof

In 2017 no material internal factors that would have a significant impact on the financial result achieved occurred.

2.1.2. External factors and the assessment thereof

The Company's and TAURON Capital Group's operations and earnings in 2017 were impacted by the following external factors:

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

2.1.2.1. Macroeconomic environment

TAURON's core business operations are conducted on the Polish market and the Company takes advantage of the positive trends occurring thereupon as well as it is affected by the changes thereof. The macroeconomic situation, both in the individual sectors of the economy as well as on the financial markets, is a significant factor impacting the earnings generated by the Company and TAURON Capital Group.

2017 was generally positive for the Polish economy. The Central Statistics Office (GUS) informed in March 2017 that all economic indicators improved. Registered (official) jobless rate reached 8.5% in February 2017. Additionally, Moody's raised Poland's Gross Domestic Product (GDP) growth rate forecast to 3.2% year on year. All this information allowed for strengthening of the Polish currency both versus EUR as well as USD. In March 2017 the USD/PLN exchange rate declined 2.54% to PLN 3.96, while the EUR/PLN exchange rate dropped 1.74% to PLN 4.23 zł. In April 2017 more positive information on the Polish economy surfaced. In March 2017 the manufacturing industry's sold output rose 11.1% year on year. The actual monthly industrial production growth rate reached 17.6%.

In the subsequent months of 2017 more positive information was published. In June 2017 average wages in the enterprises sector rose to PLN 4 508. Also, employment in the enterprises sector went up, leading to the fall of the jobless rate to 7.1%. Furthermore, in Poland, similar to the Eurozone, an increase of the manufacturing industry's PMI was observed reaching 53,1 and 56.8, accordingly.

It should be noted that CPI rose 1,5% in the period under review. In November 2017 the consumer products and services price index increased 2.50% on annual basis and 0.50% on monthly basis. GDP growth rate reached 4.9% year on year in Q3 2017, versus 4% in Q2 2017. According to the Central Statistics Office (GUS) data GDP growth rate for the entire 2017 reached 4.6% versus 3.6% expected earlier which undoubtedly proves the strengthening of the country's economy.

According to the data of Polskie Sieci Elektroenergetyczne S.A. (PSE, TSO) 2017 brought a significant increase (2.13% year on year) of the gross national electricity consumption (KZEE), covered mainly by the rise of production from the domestic power plants (1.98% year on year) – and increased imports (14.41% year on year) that reached 2.23 TWh in 2017.

Due to the increased demand for electricity in the National Power System in 2017 TAURON Wytwarzanie's generating units produced approx. 8,8% more gross electricity than in 2016. Increased electricity output had a direct impact on the volume of consumed coal.

2.1.2.2. Market environment

Electricity

Wholesale electricity prices on the Day Ahead Market (RDN) of the Polish Power Exchange (Towarowa Giełda Energii S.A. - TGE) in 2017 in Poland, in spite of rising commodity and CO_2 emission allowance prices, were on an averaged annualized basis lower than in 2016 and reached 157.84 PLN/MWh (-1,38 PLN/MWh in comparison to 2016). The CRO price on the Balancing Market (RB) reached 166.65 PLN/MWh (+2,46 PLN/MWh on an annualized basis).

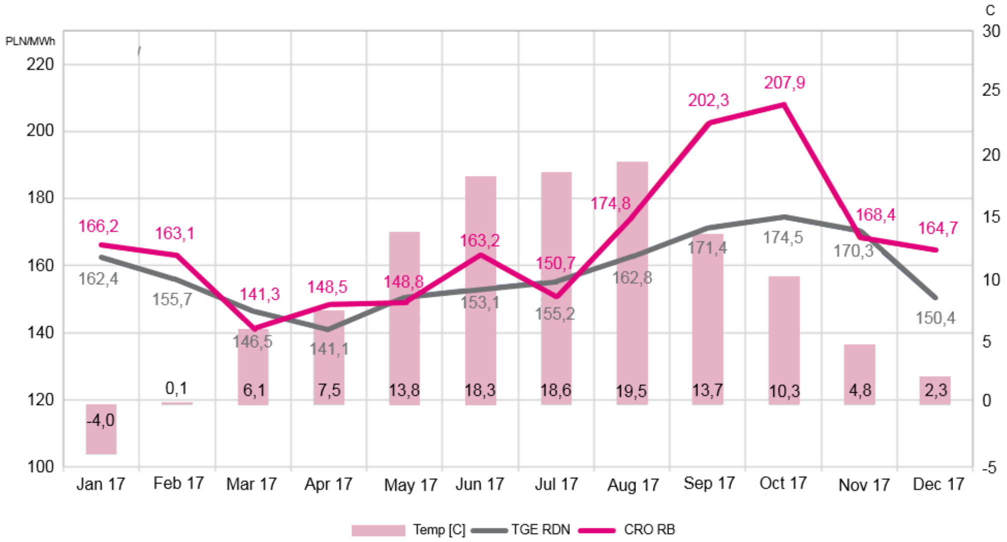
The main reason for a slight price decline on the RDN was a good situation in the National Power System (KSE) and relatively low and very low prices in the 1st half of 2017. The situation improved in the 2nd half of 2017. Rising demand for capacity (year on year increase by 3.99 TWh to 168.4 TWh) in combination with overhaul plans for the centrally dispatched generating units had a significant impact on the increase of CRO prices that were higher, on average, by 8.81 PLN/MWh than the prices on the RDN.

The impact of the rising electricity consumption on the increase of electricity prices was to a certain extent offset by the record volume of electricity produced by the wind sources (14.4 TWh, increase by 2.7 TWh in comparison to 2016). In 2017, in spite of the rising demand, generation output from hard coal fired power plants declined (to 78.7 TWh, i.e. by 1.5 TWh in comparison to 2016). Rising demand was satisfied by increased production at more expensive power plants, for example, the gas-fired ones, the output from which, on an annualized basis, rose 37.8% to 5.8 TWh.

In spite of commissioning approx. 730 MW of new capacity in wind power plants in 2016, a slight increase of the production from RES did not bring the expected output increase in this sub-sector. At the same time a significant, by as much as 4.4%, drop of production from cheap lignite fired power plants was observed in 2017 which had to be offset by the rising production at more expensive power plants, for example, the gas-fired ones, the output from which, on an annualized basis, rose 24.2% to 7.2 TWh. Additionally, KSE was supported by electricity imports in the volume of almost 2.4 TWh.

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

Figure no. 13. Average monthly electricity prices on the SPOT and RB markets, as well as average temperatures

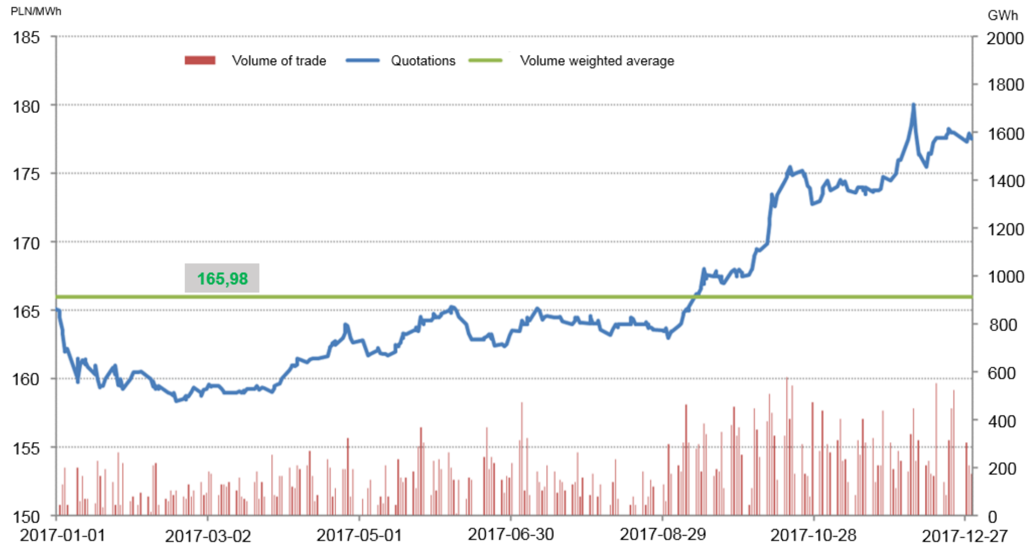


The base load contract with the delivery in 2018 was in a clear upward trend on the futures market in 2017. BASE_Y-18 contract prices, after the closing of the BASE_Y-17 contract, began with an up gap in the region of approx. 3 PLN/MWh. However, the gap was quickly closed due to the declining CO_2 prices to the level below 160 PLN/MWh at the end of the first decade of January 2017. In the second half of January 2017 the prices rose and fluctuated in the approx. 160-161 PLN/MWh range. Subsequent months brought stabilization of prices. Only at the end of the summer holidays period rising electricity prices were observed on the energy markets almost all over Europe. The biggest price increases occurred in France, Spain and in Germany (fears of a repeat of the cold 2016/2017 winter and problems with satisfying the demand). In August 2017 the BASE_Q4-17 and BASE_Q1-18 products were particularly high priced, frequently above 50.00 EUR/MWh, i.e. much higher than the reference quarterly product listed on TGE. In September 2017 the average price of the BASE_Y-18 futures contract reached 166.80 PLN/MWh, i.e. it was 3.00 PLN/MWh higher than in August 2017. Forward market electricity prices in October 2017 continued the upward trend commenced in September.

Factors supporting the demand side remained unchanged. A high coal price on the world markets, rising EUA unit prices and a tight situation in the French power system as well as the approaching winter effectively supported reaching new price peaks on the forward products. Additionally, high SPOT price levels also had a clear impact on the wholesale market prices. In October 2017 the average price of the BASE_Y-18 futures contract reached 172.70 PLN/MWh, i.e. it was almost 6.00 PLN/MWh higher than in September. However, the biggest price increase occurred at the beginning of December 2017, when the price of the BASE_Y-18 contract was close to 180 PLN/MWh. The average volume weighted price of the BASE_Y-18 product reached 165.98 PLN/MWh, with the total trading volume reaching 65.2 TWh, i.e. it was more than 10 TWh lower than in 2016.

The below figure presents the BASE Y-18 contracts performance.

Figure no. 14. BASE Y-18 contracts performance



Crude oil and coal

2017 on the crude oil market was characterized by the continuation of the upward trend following the declines that had taken place in 2014-2015. The crude oil prices fluctuated in the 44,35-67.1 USD/bbl range in the period under review.

The beginning of 2017 was characterized by low price volatility. In February crude oil prices fluctuated in the 54.4-57.45 USD/bbl range. At that time investors were analyzing the agreement between the OPEC cartel and Russia, aimed at reducing the crude oil output, and the data on the crude oil production output and inventory levels in the US. It should be noted that a large role in OPEC is played by Saudi Arabia and this country is interested in high oil prices due to the largest IPO in history – the stock market debut of Saudi Aramco.

On March 26, 2017 an OPEC meeting was held in Vienna during which, however, no unequivocal and binding decisions on production levels were taken. Two days later cyclone Debbie hit the north-western coast of Australia which led to a rise of commodity prices, including also crude oil. In spite of OPEC and Russia's efforts the United States did not join the agreement aimed at reducing oil production, on the contrary, in April 2017 the US observed an increase of its output by almost 0.5 mln bpd, and as a result the worldwide crude oil inventory did not decrease to the expected levels which had a direct impact on the mood on the market.

The second half of 2017 was characterized by a strong anxiety on the market caused by weather related natural disasters and political turmoil. Hurricanes Harvey and Irma had a strong impact on oil prices at the end of August and beginning of September. As a result of the forces of nature a number of US refineries had to stop their operations which led to problems with excessive stockpiles of extracted oil.

Due to increased exports of US oil to other markets the US WTI oil price discount versus the Brent oil widened. Petrol price increased, refining margins rose due to smaller supply of petrol. The strengthening of the crude oil prices in September was due to the "restart" of the US refining industry, but also due to the rising geopolitical tensions. An important factor was also an increase of tension between North Korea and the US and Japan.

Additionally, Kurdistan announced an independence referendum which led to a sharp reaction from Turkey. It threatened to cut off oil supplies from Iraqi oil field in the Kirkuk area to the Ceyhan port in Turkey, which would substantially reduce oil supply.

The situation on the coal market was similar. In Q1 2017 the coal prices were not highly volatile. However, looking at the entire 2017 an upward trend of this commodity should be emphasized. Prices moved in the range between 61.75, and 90.75 USD/Mg. Relative peace on the market was due to investors waiting for the decision of the Chinese National Development and Reform Commission - NDRC, on limiting the number of days in a year when coal may be extracted. Furthermore, safety issues also arose in China – as a result of ad-hoc audits mining was suspended at coal mines that did not meet safety requirements.

On the other hand, due to the beginning of the season characterized by the lower demand for coal, prices on the worldwide market began to drop. Unexpectedly, the aftermath of cyclone Debbie that hit Australia became a factor inhibiting the market declines observed. Particularly strong price hikes during that time were applicable to coke with Australia being one of its main producers, where some mines were closed and the railway infrastructure was destroyed due to difficult conditions as a result of weather related natural disasters. Following the disruptions related to cyclone Debbie coal prices with the delivery in 2018 returned to lower levels. However, Australia was soon hit with flooding rains and finally the price stayed at a relatively high level of 66 USD/Mg.

Additionally, in China, due to overhauls, a very important railway line that connects regions where coal is extracted with the Quindango port was temporarily closed. As a result of these occurrences coal prices with the delivery in 2018 went up by a few dollars - to 68 USD/Mg. Only after a few weeks the situation began to normalize. Finally, the coal at ARA ports with the delivery in 2018 cost 66.50 USD/Mg. In the subsequent months of 2017 temperatures were rising and the precipitation was declining which as a consequence led to the falling water levels. In China the hydroelectric plants' production fell by as much as 70%, and hydro is the second largest source of energy in this country, following coal. Additionally, continued disruptions on the supply side, as a consequence of cyclone Debbie and flooding rains, led to the rising demand on the market.
Coal prices in September at ARA ports with the delivery in 2018 were in an upward trend that began already in March 2017. In the period under review coal prices with the delivery in 2018 reached the maximum level of 84.25 USD/Mg, i.e. the highest value since 2014. Such increases were caused by the strong demand in the Asia region and speculations related to the possibility of a repeat of last year's problems of nuclear plants in France and higher coal consumption in Europe. At the end of the month the prices suffered a correction which was due to the lower demand for coal in China, related to the approaching National Days holidays lasting a full week. Also, a transition period for a ban on coal imports from North Korea was introduced which led to increased supply. Finally, at the end of the year coal prices landed at levels not seen since 2013, reaching 90 USD/Mg.

Natural gas

Year 2017 brought price increases on the gas market following the record low prices in 2016. The average price on the Day Ahead Market for gas on the Polish Power Exchange (TGE) reached 84.69 PLN/MWh in 2017 and it was more than PLN 13 higher than in 2016. Contracts with the delivery on the day ahead were particularly high priced in the first two and the last two months of 2017, i.e. during the gas winter season, when the demand for fuel is the highest. Prices in January and in December topped 100 PLN/MWh a number of times. The maximum value was achieved on December 13, 2017 and it reached 105.10 PLN/MWh. High prices in Q1 2017 were the result of increased demand for gas all over Europe, caused by unavailability of some nuclear plants in France (which led to a larger generation from gas-fired sources) and a relatively long cold period.

In Poland the daily average temperatures on a few January days did not exceed -11ºC, while temperatures above 0ºC began to appear only in mid-February 2017. Due to increased gas consumption an extension of the cold spell may have led to real problems with availability of gas fuel in Europe. Fears of a repeat of the situation that occurred at the end of 2016 / beginning of 2017 were also the reason for high prices at the end of 2017. The distribution of prices on the spot market in 2017 was characteristic for the gas demand distribution (a clear drop of prices during the period of lower demand in the summer).

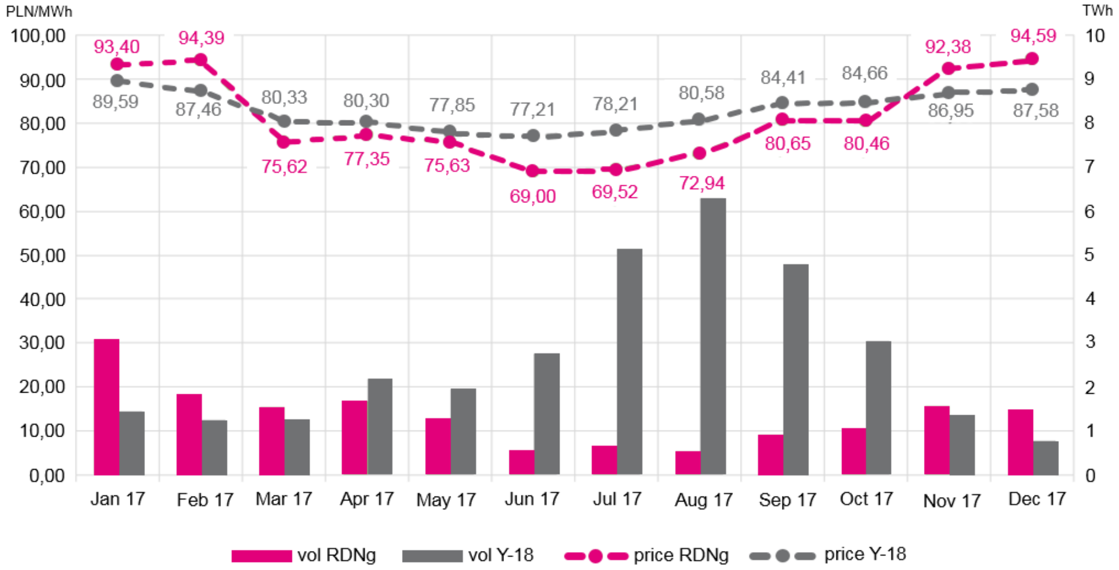
Similar to the markets with a shorter delivery period, on the forward contracts market Q1 and Q3 were characterized by a markedly higher price. The reference one year contract in 2017 was priced within the 76.80-92.27 PLN/MWh range, while upon expiration it was priced at 86.50 PLN/MWh.

The total trading volume on TGE in 2017 reached more than 138.5 TWh. As compared to the previous year an increase by 21% occurred. The forward contracts market had the biggest share in the trading volume, generating a volume at the level close to 115 TWh. On the spot market the total volume of the day ahead contracts and weekend contracts reached more than 19 TWh, which was 0.5 TWh less than in the previous year. A similar slight decline was also observed on the Day Ahead Market for gas where the trading volume reached 4.7 TWh.

The key event for the development of the gas market in Poland was the first historic LNG delivery from the US. A ship carrying liquid gas entered the terminal in Świnoujście on June 7, 2017. While the new rules of maintaining mandatory gas inventory came into force on October 1, 2017. According to these rules importers that want to maintain mandatory gas inventory outside Poland must – in order to ensure their ability to transfer such gas to Poland in case of an energy crisis - reserve the so-called continuous transmission capabilities on the transborder lines (interconnectors). The reserved transmission capabilities are to allow for transmitting the entire inventory to Poland in any conditions within maximum 40 days and additionally they cannot be used for any other purposes, for example commercial (trading) ones.

The below figure presents average monthly SPOT and Y-18 contract prices on TGE in 2017.

Figure no. 15. Average monthly SPOT and Y-18 contract prices on TGE in 2017



CO_2 emission allowances

The CO_2 emission allowances market in 2017 was characterized by high price volatility, caused to a large degree by political factors. During the period under review the prices moved within the 4.29-8.30 EUR/Mg range.

Q1 2017 market should, finally, be deemed as being in the downward trend, in spite of major political events at the EU level, related to the 4th trading period of the European CO_2 Emission Allowances Trading System (EU ETS). The first factor indicating a downward trend were clear declines of electricity contract prices in Germany and France, previously featuring high volatility due to the design problems of the French nuclear plants. Another factor impacting the entire 2017 year was a record high volume offered at the CO_2 emission allowances auctions, Poland's first auction was held on March 29, 2017. It worth noting that the weather conditions in Q1 2017 supported increased utilization of the renewable energy sources. Events that occurred in Q2 2017 resulted in a change of the market mood, and as a consequence a reversal of the downward trend. The main themes attracting the market's attention were:

1. Redemptions of the CO_2 emission allowances – by April 30 every year all industrial installations covered by the EU ETS shall have an obligation to perform the so-called redemptions of the emission allowances the number of which must correspond to the verified emission volume from last year. In case the installation operator does not complete the redemption at the right time, this may lead to an imposition of a financial penalty of 100 EUR/ $MgCO_2$. For comparison it is worth mentioning that the average EUA price quoted on the market during the period of redemptions fluctuated around 5 EUR/Mg.
2. France's presidential elections.
3. Publishing information on the current oversupply volume on the market - by May 15 every year the European Commission undertook to publish data on the oversupply on the market, and this way it will be possible to estimate what oversupply volume will be allocated to the MSR in the subsequent year.
4. G7 meeting – during which one of the leading themes was the ecological policy, and in particular the theme of the so-called "Paris Agreement". The climate agreement signed in Paris in 2015 by 195 states from all over the world constitutes an action plan aimed at limiting the rise of temperatures worldwide. During the G7 summit the US President raised his objections against the above mentioned agreement. Finally the US does not respect this document.

July 2017 for the emission allowances market was a month that continued the upward trend commenced in June. The prices fluctuated between 4.99 EUR/Mg and 5.62 EUR/Mg, while the average price for the period under review reached 5.27 EUR/Mg. Continued price increases on the market were to a large degree a consequence of the weather conditions in Europe. Extended period of high temperature and low precipitation led, first of all, to increased demand for electricity (substantial increase of use of cooling devices) and secondly, a difficult hydrological situation in some EU countries. The above mentioned factors of fundamental nature increased the intensity of the use of the hard coal-fired power plants, and thus contributed to an increase of demand for EUAs. In August the ASE Agency ordered a re-checking of all nuclear reactors located in France in order to finally verify the safety of the installations. This information led to a wave of speculations related to the possibility of a repeat of the 2016 situation. The last month of Q3 2017 featured a substantial price volatility. During only 8 session days the price rose by almost 33%. In the beginning of the month market transactions were made at the level of 5.82 EUR/Mg, while a few days later, the CO_2 emission allowances were contracted at the level of 7.72 EUR/Mg. Such large increases were a consequence of rising fears related to the situation of the French nuclear power plants, as well as the German elections. Furthermore, following the takeover of the EU presidency by Estonia, the works related to the legislation of the EU ETS system's phase 4 were accelerated. October 2017 for the emission allowances market was a month of continued strong growth commenced in the previous month. The EUA prices fluctuated between 6.77 EUR/Mg and 8.05 EUR/Mg, which indicates that in the period under review the prices went up by 18.91%, i.e. by 1.28 EUR/Mg. The price increase was caused mainly by the speculative factors, related to the legislation of the EU ETS system's phase 4, surfacing information on the manner of Great Britain exiting the system, as well as related to the problems of the nuclear power plants in France. Additionally, EUA price increases were impacted by the strong upward trend on the coal market. In November 2017 a working group made up of representatives of three main European institutions completed the works on the EU ETS system's phase 4 that will be in force in 2021-2030. In accordance with the agreements reached the reform defined among others:

1) Market Stabilization Reserve (MSR),
2) Linear Reduction Factor (LRF),
3) quantity of emission allowances available at the CO_2 emission allowances auctions,
4) quantity of free of charge emission allowances granted during the regulation period,
5) modernization and innovation fund.

It is worth noting that the so-called Modernization Fund, and specifically its provisions, prevented the completion of the legislation in October 2017. In its current form the provision on the emission conditions was removed from the provisions setting up the Modernization Fund, however a provision prohibiting the Modernization Fund from subsidizing coal-fired units. In December 2017 the growth trend, developing since Q2, was continued – the prices were moving within the 6.94-8.30 EUR/Mg range.

The below figure presents the impact of the legislative works and the environment on the EUA SPOT product price in 2017.

Figure no. 16. The impact of the legislative works and the environment on the EUA SPOT product price in 2017

Property rights

2017 has brought upon significant changes on the property rights market, mainly related to amendments of legal regulations. Lasting oversupply of PMOZE_A property rights in the market has caused that since June 2017 the average monthly values of the OZEX_A index have been dropping from 37.98 PLN/MWh in January to a historic minimum of 24.38 PLN/MWh in June. In the same period, the surplus on the PMOZE_A register increased by 8.6% to 25.42 TWh. Beginning with July 2017, the prices started to slowly grow back. Compared to 2016, the average weighted price of the OZEX_A index has dropped by nearly 50% to 38.83 PLN/MWh, while the balance on the PMOZE_A register by the end of 2017 was

28.14 TWh that when taking into account the rights blocked for redemption leaves a value of 24.90 TWh at the end of 2017. One should also note the trading volume in “green” certificates in 2017, which amounted to over 10 TWh. So far this was the biggest trade in the history of “green” property rights (higher by as much as 36% than in 2016). According to the *act of 20 July 2017 on amendment of the act on the renewable energy sources*, which came into force on 25 September 2017, the substitution fee in force until September 2017 was 300.03 PLN/MWh, while for the following three months of 2017 this fee dropped to 92.03 PLN/MWh, being 125% of the weighted average price of 2016. The obligation to submit PMOZE_A certificates for redemption increased to 15.40%.

The prices of certificates confirming energy generation from agricultural biogas (called “blue” certificates) for which the obligation rate in 2017 was 0.6% were above the substitution fee that was 300.03 PLN/MWh. From January to May the monthly average prices of the TGEozebio index were dynamically growing, respectively from 301.15 PLN/MWh to as high as 408.08 PLN/MWh. In the following two months this trend has reversed and the prices returned to the substitution fee level. Finally the average weighted value of the index at the end of 2017 was 333.89 PLN/MWh. The total traded volume was 522.5 GWh, and the PMOZE_BIO register balance at the end of 2017 was 309 GWh. Taking into account the certificates blocked for redemption, this value has dropped to 206 GWh.

According to the *act of 10 April 1997, the Energy Law,* amended in 2016, until 30 June of each calendar year the property rights issued to cogeneration units for generation in the previous year may be redeemed. Due to the above, until the end of H1 listings included the property rights for cogeneration both in 2016 and in 2017, while in H2 listings included exclusively the property rights confirming energy generation in 2017.

Until the end of June 2017, the PMEC-2016 (high-efficiency cogeneration) was traded, listed in a narrow price band from 10.76 PLN/MWh in January to 9.27 PLN/MWh in June. However, as of beginning of May 2017, the POLPX started listing PMEC-2017 with opening at 9.68 PLN/MWh. Until the end of 2017, also in case of this instrument the volatility of the KECX index was symbolic and with respect to the monthly values was a mere 0.11 PLN/MWh, while by the end of 2017 the listings ended at 9.79 PLN/MWh. The market prices fluctuated slightly below the substitution fee defined at 10 PLN/MWh.

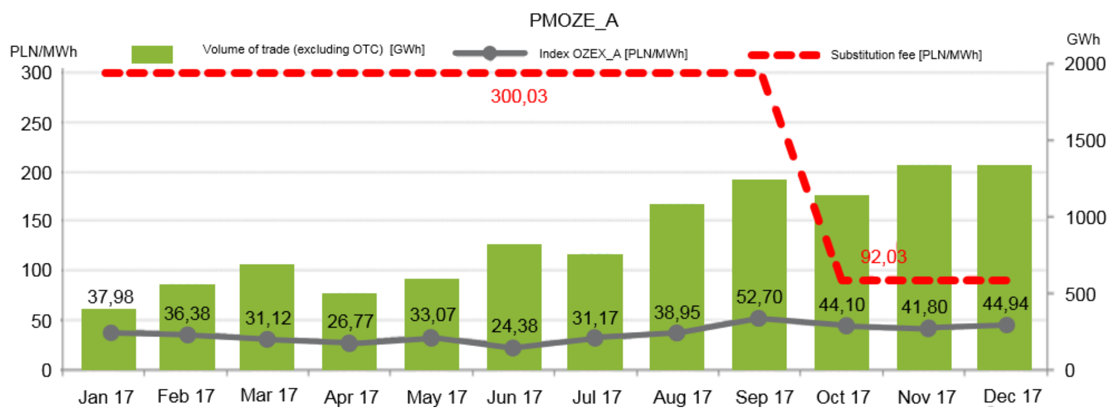
In gas cogeneration the situation was very much alike. By the end of June 2017, the PMGM-2016 instrument was still listed, closing at 112.21 PLN/MWh. This level, like in case of the coal based cogeneration, was determined by the substitution fee, for 2016 set at 125 PLN/MWh. The PMGM-2017 instrument, concerning generation in 2017, was listed already in March 2017, with the average KGMX index at 116.00 PLN/MWh. Until the end of 2017 its value was increasing on month to month basis, reaching 117.14 PLN/MWh in December. The average listings in 2017 for PMGM-2017 instrument were 116.48 PLN/MWh and were just c.a. 3.50 PLN/MWh below the substitution fee, which for 2017 has dropped to 120 PLN/MWh.

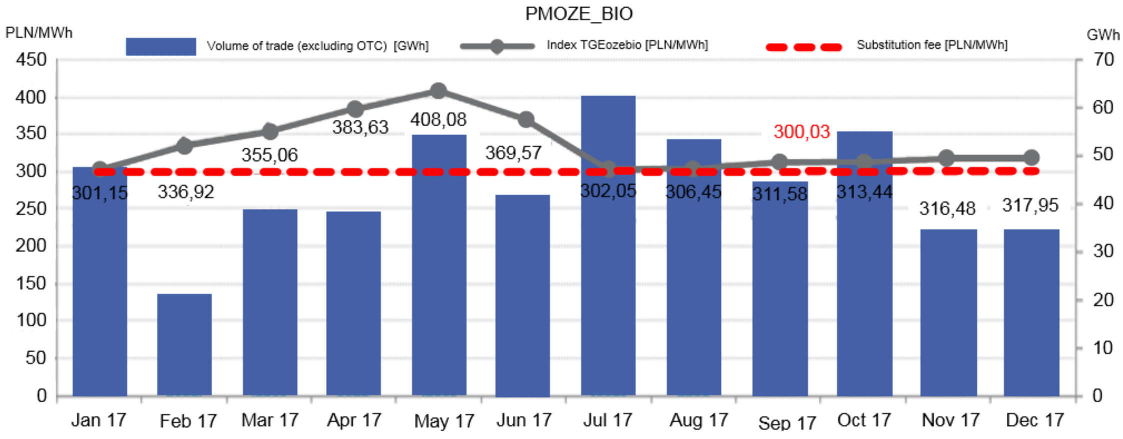
The situation on the market in PMMET property rights confirming energy generation from firing methane was developing similarly to that in case of “yellow” and “red” certificates. Until the end of June 2017 the PMMET-2016 instrument was still listed, with its average value of the KMETX index being 62.19 PLN/MWh. The substitution fee concerning production in 2016 was 63 PLN/MWh, while for 2017 it was lower by 7 PLN/MWh and determined the market prices. The PMMET-2017 instrument for production from the previous year was listed on average at 54.88 PLN/MWh.

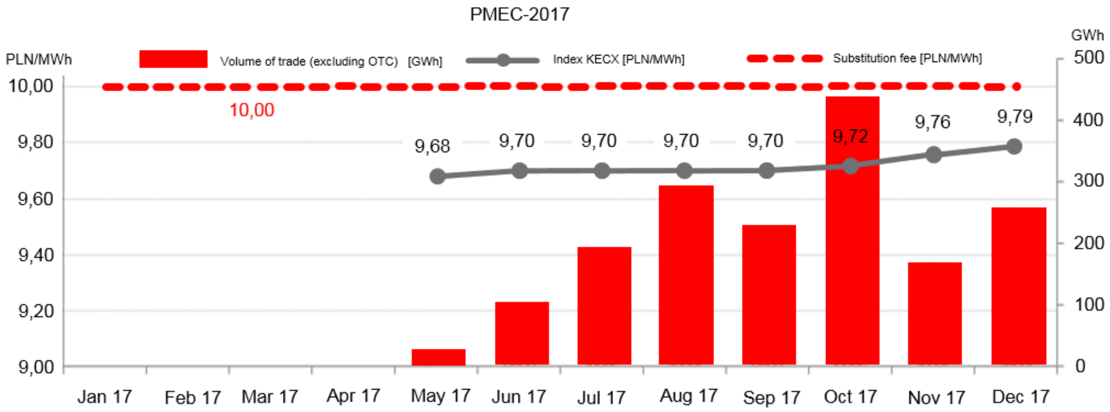
The property rights due to the PMEF certificates of energy efficiency (the so-called ”white” certificates) continued the downward trend. At the beginning of 2017 the average monthly prices dropped from 1 219,38 PLN/toe in January to the historical lows of 385.86/toe. Finally the weighted average index reached 693.36 PLN/toe and it was as much as 807 PLN/toe lower than the substitution fee set for 2017 at PLN 1 500.00/toe.

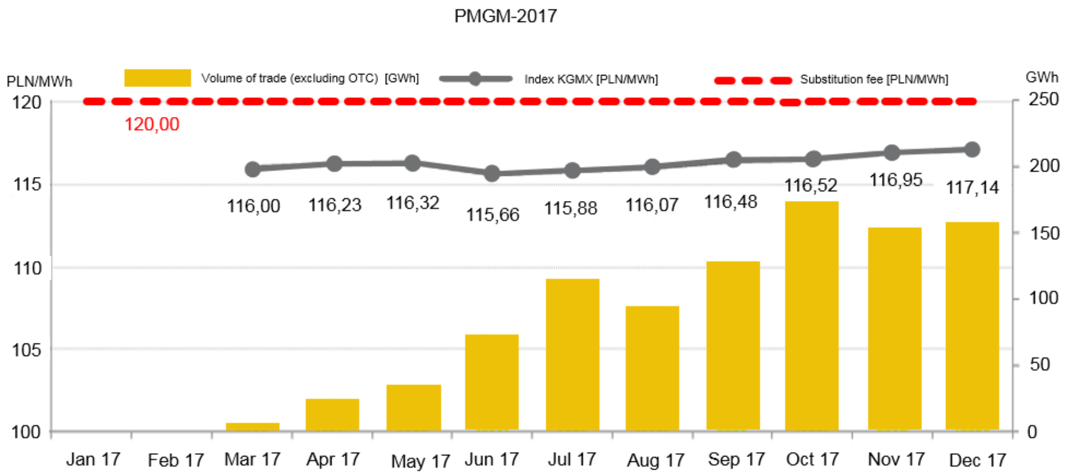
The below figure presents the property rights indices, the so-called ”green”, ”blue”, ”red”, ”yellow” and ”violet” certificates

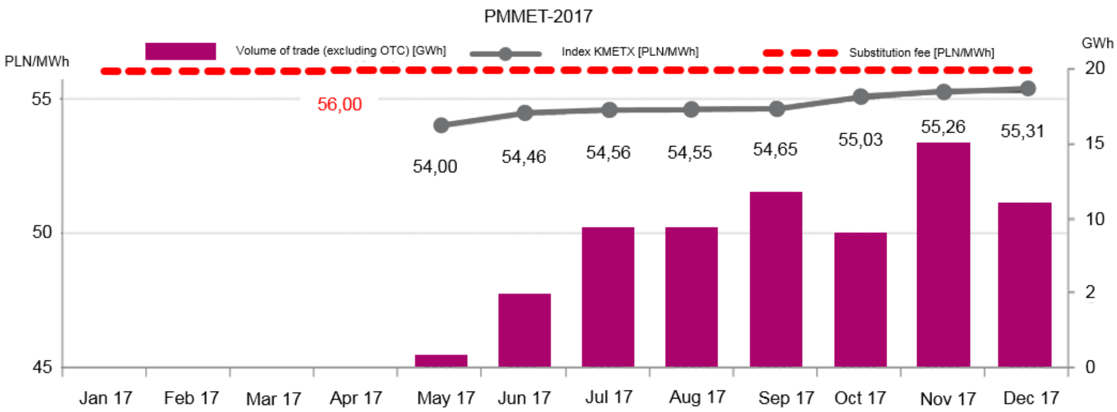
Figure no. 17. Property rights indices




PMOZE_BIO
PLN/MWh
GWh
Volume of trade (excluding OTC) [GWh]
Index TGEozebio [PLN/MWh]
Substitution fee [PLN/MWh]
300,03
301,15
336,92
355,06
383,63
408,08
369,57
302,05
306,45
311,58
313,44
316,48
317,95
Jan 17
Feb 17
Mar 17
Apr 17
May 17
Jun 17
Jul 17
Aug 17
Sep 17
Oct 17
Nov 17
Dec 17


PMEC-2017
PLN/MWh
GWh
Volume of trade (excluding OTC) [GWh]
Index KECX [PLN/MWh]
Substitution fee [PLN/MWh]
10,00
9,68
9,70
9,70
9,70
9,70
9,72
9,76
9,79
Jan 17
Feb 17
Mar 17
Apr 17
May 17
Jun 17
Jul 17
Aug 17
Sep 17
Oct 17
Nov 17
Dec 17


PMGM-2017
PLN/MWh
GWh
Volume of trade (excluding OTC) [GWh]
Index KGMX [PLN/MWh]
Substitution fee [PLN/MWh]
120,00
116,00
116,23
116,32
115,66
115,88
116,07
116,48
116,52
116,95
117,14
Jan 17
Feb 17
Mar 17
Apr 17
May 17
Jun 17
Jul 17
Aug 17
Sep 17
Oct 17
Nov 17
Dec 17


PMMET-2017
PLN/MWh
GWh
Volume of trade (excluding OTC) [GWh]
Index KMETX [PLN/MWh]
Substitution fee [PLN/MWh]
56,00
54,00
54,46
54,56
54,55
54,65
55,03
55,26
55,31
Jan 17
Feb 17
Mar 17
Apr 17
May 17
Jun 17
Jul 17
Aug 17
Sep 17
Oct 17
Nov 17
Dec 17

2.1.2.3. Regulatory environment

Capacity market law

On December 28, 2017 the President of the Republic of Poland signed the *act of December 8, 2017 on the capacity market*, that came into force on January 18, 2018. This act has a significant impact on the future functioning of the Polish energy sector. The essential goal of the act is to satisfy the deficit of generation capacity due to the foreseen growth of demand for the peak capacity and the simultaneous substantial scope of the planned retirements of generating units from operation. The law defines, among others:

1) rules of providing the service of maintaining readiness to deliver electric capacity and defines the principles of compensation for fulfilling the capacity obligation,
2) organization of the capacity market,
3) rights and obligations of the capacity market participants.

The finally adopted law envisages:

1) permitting foreign capacity market units to take part in the auctions,
2) liquidating price baskets for the new, refurbished and existing units,
3) introducing the possibility of concluding capacity contracts lasting up to 15 or up to 5 years for the new units or up to 5 years for the refurbished or planned units of demand reduction depending on the unit levels of capital expenditures referred to the net achievable capacity,
4) introducing, for the new or refurbished units with emission levels below 450 kgCO_2/MWh and cogeneration units feeding the heating systems, the possibility of concluding 2 years longer capacity contracts,
5) taking into account the lack of the possibility to comply with the capacity obligation greater than 40% due to a force majeure occurrence.

Furthermore, it was specified in detail that the period of incurring capital expenditures for the needs of the first main auction shall cover the period from January 1, 2014, and for the needs of the second main auction, from January 1, 2017. For the delivery periods falling in 2021-2023 foreign capacities will be taking part in the capacity market solely by participating in additional auctions. Capacity agreements will not be subject to enforcement until the day the European Commission's decision on their compliance with the internal market or a decision that this solution does not constitute public aid is issued.

Currently the energy sector is awaiting the publishing of the draft capacity market regulations which is to be published in the coming months and for the executive ordinances. The regulations will describe in detail the course of an auction, including the detailed description of the electricity demand curve. The first capacity auctions are to be held in Q4 2018 and they will be applicable to the 2021-2023 time frame.

BAT conclusions

Best Available Technologies (BAT) mean the most efficient and advanced stage of development and methods of conducting the given operations that indicate the possible use of individual techniques as the base when setting the admissible emissions values and other conditions aimed at preventing arising, and if it is not possible, reducing emissions and impact on the environment as a whole.

BAT conclusions is a document drawn up based on the reference document on the best available technologies, the so-called BREF. BAT conclusions for large combustion plants (LCP) as an executive decision to directive 2010/75/EU on industrial emissions (IED Directive) will be directly applicable. They define the new requirements with respect to admissible emissions values and the monitoring obligation. A consequence of their implementation will be the need to adapt the fuel combustion installations to the requirements defined in the BAT Conclusions by constructing or refurbishing generation sources, flue gases cleaning (scrubbing) installations and in certain cases additionally installing the continuous monitoring systems for the pollutants so far not covered by such an obligation which means the need to bear exceptionally high capital expenditures.

On April 28, 2017 the representatives of the member states in the European Commission passed the new standards tightening the emission standards for the manufacturing industry, i.e. the so-called BAT conclusions for large utility scale combustion facilities. On August 17, 2017 the executive decision of the European Commission (EE) 2017/1442 of July 31, 2017, introducing the conclusions related to the best available technologies (BAT) with respect to large utility scale combustion facilities, was published in the Official Journal of the European Union. Upon publishing the BAT conclusions became a part of the legal order in force in Poland and they will be the basis for issuing the integrated permits.

Apart from more stringent restrictions for the SO_2, NO_x and dust emissions the BAT conclusions introduce emission standards for substances not covered thereby so far, namely for mercury, hydrogen chloride, hydrogen fluoride and ammonia, and also in specific cases order installing continuous monitoring for the pollutants not covered by such an obligation so far. The existing installations have 4 years to adapt to the new requirements and they will have to comply therewith after August 17, 2021. BAT conclusions will be applicable to the facilities and installations burning fuels with the capacity not lower than 50 MW in fuel. They are applicable to both the new facilities that will obtain an integrated permit following the publishing of the conclusions, as well as to the facilities already in operation. New, more stringent requirements related to the permitted values of pollutant emissions will have a significant impact on the future of the European coal-fired power plants.

According to the Ministry of the Environment adapting large industrial installations, including the ones generating electricity and heat, to the tighter SO_2, NO_x and dust emission standards and introduced for the first time binding emission levels for mercury, hydrogen chloride, hydrogen fluoride and ammonia will cost at least PLN 10 bln. Both the costs as well as the schedule of the investment projects aimed at adapting the installations covered by the tightening will be an enormous challenge for the energy sector, especially due to the fact that the refurbishing will have to encompass practically all the power generation units currently in operation. Although the IED Directive provides for an option to obtain temporary derogations from meeting the limit emission values defined based on the BAT conclusions, but such derogation may be granted only if achieving the limit emission values were to lead to unproportionally high costs in relation to the benefits for the environment due to the geographical location of the installations, local environmental conditions or the technical features of the installation.

Further tightening of the emission limits is to take place as a result of subsequent revisions of the conclusions that are to be published every 8 years.

Act on Renewable Energy Sources (RES)

In 2017 works were underway on successive amendments of the *Act on Renewable Energy Sources (RES* law) passed on February 20, 2015. A draft amendment of the law was published and sent for public consultations in June 2017, with its main goal being to ensure the compliance of the provisions of the RES law with the regulations on public aid issued by the European Commission. The amendments presented make the provisions of the Act on RES fully compliant with the requirements defined in the guidelines on public aid related to environment protection and energy goals in 2014-2020, that permit, as compliant with the common market principles, such market instruments as auctions or tender procedures in line with the competition principles that are open for all producers generating electricity from RES competing against one another on equal terms that should substantially ensure that subsidies are reduced to the minimum.

The scope of the amendment defined, among others, a rule on cumulating public aid, new split into auction baskets, additional support rules were proposed in the form Feed-in-tariff (FIT) and Feed-in-premium (FIP) tariffs for electricity generators from renewable sources dedicated for micro and small RES installations that use stable and predictable energy sources (hydroelectricity, biogas, agricultural biogas) with an installed capacity lower than 500 kW – FIT and a capacity not lower than 500 kW and lower than 1 MW – FIP;

On 30 August 2017, the *ordinance of the Minister of Energy of 11 August 2017 on amendment of the quantity share of electricity volume resulting out of the redeemed certificates of origin confirming generation of electricity from renewable sources in 2018 - 2019* came into force, defining the levels of obligations. These levels are 17.5% and 18.5% respectively, while for the “blue” certificates the share for 2018 and 2019 is 0.5%. The new obligations should result in reduction of certificate surplus on the market, and thus increase of their prices that will be capped by a new substitution fee defined for each year.

On 25 September 2017, the act of *20 July 2017, amending the act on renewable energy sources,* came into force. The key change introduced with this amendment is the discontinuation of the fixed substitution fee in the amount of 300.03 PLN/MWh and relating it to the market prices of certificates of origin of energy from certain RES (“green” and “blue” certificates). This fee is to be equal to 125% annual weighted average price of property rights resulting out of certificates of origin of RES energy, published pursuant to Article 47 (3) 2) of the *act of 20 February 2015 on renewable energy sources*, however not more than 300.03 PLN/MWh.

On 13 December 2017, on power of EU State aid regulations, the European Commission has approved the Polish program concerning energy from renewable sources. The decision by the European Commission has influenced intensification of work on amendment of the RES act concerning support for RES generators; therefore adoption of another amendment to the RES act is expected in Q1 2018.

In H1 2017, based on the ordinances to the RES act adopted by the Council of Ministers, concerning: the order of conducting the auction sales of electricity from renewable sources in 2017, the maximum volume and value of electricity from renewable sources that may be sold in auctions in 2017 and the reference price of electricity from renewable sources in 2017 and the terms binding the producers who have won auctions in 2017, two RES auctions were conducted for new build and existing producers with installed capacities of up to 1 MW. Subsequent auctions planned to be held in H2 2017 were cancelled by amendment to the previous ordinances.

Amendment to the Water Law Act

The *act of July 20, 2017, the Water Law* was announced on August 23, 2017, however the majority of the new Water law provisions came into force on January 1, 2018.

The act implements into the Polish law, among other, the EU regulations defined in the Water Framework Directive, stating that all water users must incur the costs thereof. The fees shall be applicable to the energy sector, fish growers, farmers and businesses using large quantities of water for their production.

In case of the energy sector the fee for water consumption by hydroelectric power plants is to be borne by the owners of hydroelectric power plants solely for the volume of electricity generated using the reclaimable water and for the intake of non-reclaimable process water.

With respect to the fee for water intake to ensure operation of cooling systems of power plants or combined heat and power plants such fee will be borne solely for the difference between the quantity of water taken for such purposes, and the quantity of water discharged to water streams or to the ground from the cooling systems.

Another fee is the fee for discharging the water from the cooling systems of power plants or combined heat and power plants to water streams or to the ground.

Arrangements concerning the European Union's CO_2 emissions allowance scheme

The beginning of 2017 saw intensification of work on the EU ETS legislation; however, already in 2016 the EU's administration bodies received the preliminary decisions on phase 4 of the EU ETS for consultation. On 15 February 2017, the European Parliament has adopted selected legislative proposals submitted by the ENVI and ITRE committees concerning the shape of the EU ETS in 2021-2030. However, on 28 February 2017 a meeting of environment ministers of the Members States of the European Union was held in Belgian's capital, which adopted the postulates voted at the European Parliament despite objections by nine countries (including Poland), thus demonstrating that EU Member States in majority are for increasing restrictions on greenhouse gas emissions.

Preliminary approval of the resolutions of these institutions has paved the way to further stage of the legislation path adopted in the EU. A working party consisting of representatives of the European Parliament, the European Council and the European Commission (the Trilog) has on 8-9 November 2017 agreed on the compromise text of the draft directive on the reform of the EU ETS in the 4th trading period (2021-2030). The text of the approved reform stipulates, among others:

1) Raising the linear reduction factor (LRF) from the current level of 1.74% to 2.2%.
2) Introduction of the market stability reserve (MSR) mechanism that in principle is to reduce the number of allowances traded in the market to 800 million. In its first years of operation (2019-2023) the mechanism will be absorbing 24% of allowances from the auctioning share and transfer them into reserve. As of 2024, the CO_2 emissions allowances absorption mechanism will be reduced to 12%. Moreover, as of 2023, the allowances held in the MSR in excess of the auctioning share from the previous year will be eliminated.
3) In the fourth trading period the total available auctioning share will constitute 57% with possibility of increase by 3%.
4) Establishment of the Innovation and Modernization Funds. The Innovation Fund in principle is to support modern low emissions technologies with around 400 million allowances. The Modernisation Fund will support the lowest GDP Member States in modernization of their energy sectors. The Fund may not be used for supporting energy generation using fossil fuels (with the exception of energy sectors of Romania and Bulgaria).
5) Sectors at risk of carbon leakage shall be allocated 100% of free of charge allowances.

At present, the reform of the fourth trading period of the EU ETS is at the last stage of the approval path provided for by the EU legislative procedure process.

The exchange obligation

The act of 8 December 2017 on the capacity market announced on 3 January 2018 has amended the act of *10 April 1997 – the Energy Law*. In the new wording of the energy Law „energy undertakings dealing with electricity generation are required to sell not less than 30% (previously not less than 15%) of electricity generated in a given year at commodity exchanges in understanding of the *act of 26 October 2000 on commodity exchanges*, or on market organised by a leading undertaking operating a regulated market on the territory of the Republic of Poland (…). The obligation for 2018 shall be fulfilled by energy undertakings dealing with electricity generation with respect to electricity generated as of 1 January 2018.

In December 2017, the total volume of electricity traded in the SPOT and futures markets operated by the POLPX was 13.3 TWh, on year on year basis an increase of 51.2%. In December 2017, the volume of electricity traded in the futures market was 10.8 TWh, meaning an increase by 74.4% comparing to the same period of the previous year, and the trade volume on the SPOT market reached 2.5 TWh, meaning a drop by 3.7% year on year.

However, throughout the entire 2017 the total volume of electricity traded in the SPOT and futures markets was 111.7 TWh, meaning a decrease of 11.8% comparing to the volume in 2016. In 2017 the electricity trading volume on the futures market was 86.4 TWh, meaning a drop of 12.7% comparing to 2016, and the trading volume on the SPOT market reached 27.6 TWh, meaning a drop of 8.6% year on year.

Operating reserve (OR)

In 2017, the OR model did not change functionally. However, the model parameters have changed due to the change of the model calculation baseline. The hourly OR budget was increased from PLN 128 758.72 to PLN 144 070.61 and the CRRM reference hourly price changed from PLN 41.20/MWh to PLN 41.79 /MWh. The hourly required operating reserve volume changed from 3 451.09 MW/h to 3 447.49 MW/h. The COR weighted average price in 2017, determined based on the data published by the Polish Power Grid (PSE) was PLN 33.88/MWh.

Amendment of the act on natural gas stocks

On 2 August 2017, the act of *7 July 2017 came into force amending the act on stocks of crude oil, petroleum products and natural gas, the principles of proceeding in circumstances of a threat to the fuel security of the State and disruption on the petroleum market and certain other acts,* which amended *the act of 16 February 2007 on stocks of crude oil, petroleum products and natural gas, the principles of proceeding in circumstances of a threat to the fuel security of the State and disruption on the petroleum market*, *the act of 10 April 1997 – the Energy Law* and *the act of 22 July 2016 on amendment of the act – the Energy Law and certain other acts*.

The key changes introduced by the above amendment notably include:

1) supplementing the *act of 7 July 2017 came into force amending the act on stocks of crude oil, petroleum products and natural gas, the principles of proceeding in circumstances of a threat to the fuel security of the State and disruption on the petroleum market* with a definition of an entity performing imports of natural gas – the definition considers as an entity performing imports a natural person, legal person or organisational entity not having a legal personality, including an energy undertaking being an owner of a gas transmission system, which performs import of natural gas into the territory of the Republic of Poland for its own needs,
2) unambiguous resolution of doubts concerning the admissible methods of maintaining the mandatory stocks of natural gas by deciding that stocks of gas may be maintained exclusively physically in storage installations connected to the gas transmission or distribution systems,
3) definition of obligations of the operator of a gas storage system and operator of a gas transmission system, aimed at maintaining the mandatory stocks of natural gas at specified level,
4) imposition on the gas transmission system operator of the obligation to notify the President of the Energy Regulatory Office about using the transmission capacities reserved for delivery of total volumes of the mandatory stock of natural gas maintained outside the territory of the Republic of Poland to the domestic transmission or distribution network for other purposes, within 7 of becoming aware of this fact,
5) imposition on energy undertakings performing economic activities of cross-border trade in natural gas and an entity performing imports of natural gas of the obligation to provide the operator of the transmission system with information about the location of storage of mandatory stocks of gas for the purpose of validation of the technical capabilities of delivery of such stock to the gas system,
6) clarification of the rules and procedures in force in the event of activation of the mandatory stock of natural gas for the purpose of balancing the gas system at times of disturbances of gas supply or unforeseen increase of its consumption,
7) clarification of issues relating to imposition of fines on entities that fail to meet the specific statutory obligations,
8) introduction of a transition period during which an undertaking resigns from operations subject to licence and then is relieved from the obligations to maintain mandatory stock of natural gas.

Abolishment of tariff obligation

The *act of 30 November 2016 amending the act – the Energy Law and certain other acts* a time schedule was introduced for abolishment of the obligation of gaining approval by the President of the Energy Regulatory Office and application of Tariffs for gas fuels, as of:

1) 1 January 2017, for trade (sales) of gas at a virtual point, sales of LNG and CNG and sales through tenders, auctions or public procurement,
2) 1 October 2017, for final consumers (with exception of household consumers),
3) 1 January 2024, for household consumers.

“Winter Package” and Network Codes

In 2017, at the EU level, work has been conducted focused on elaboration of the final provisions of 11 documents constituting the “Winter Package” proposed by the European Commission on 30 November 2016. The key documents include: Regulation on the Governance of the Energy Union, amendment of the Regulation on the Internal Energy Market, amendment of the Directive on the Internal Energy Market, amendment of the Directive on the Use of Energy from Renewable Sources, amendment of the ACER regulation, amendment of the Energy Efficiency Directive and the Regulation on Risk Preparedness in the Electricity Sector. The documents submitted by the European Commission present the vision of changes that would be implemented in the Union’s energy sector.

The entire “Winter Package” in the proposed shape is intended to guarantee the best possible functioning of non-controllable RES by creating broad opportunities for flow of energy they generate between the Member States. At the same time proposals include transferring a range of – so far national – competences from Member States to the regional and the EU levels. Building an energy union is in principle focused on streamlining the reporting obligations imposed on the Member States and supervision over fulfillment of the goals of the EU climate policy (both the 2030 goals and obligations arising out of the Paris Agreement) with particular attention to decreasing the CO_2 emissions and increasing the use of renewable energy sources.

A lot of stress is placed on growing the internal energy market with particular consideration to the infrastructure interconnecting the energy systems of individual Member States and initiatives to increase the flexibility of operation of the systems with a view to significantly increase the share of renewable energy sources. The Member States are also required to report the progress in improving energy efficiency, including presenting plans for renovation and modernization of buildings, both public and private.

Initially, the proposals presented by the European Commission provided it with authority to act at the EU level if in the opinion of the European Commission the goals of the energy union or the climate goals could not be achieved due to insufficient contributions by the Member States. Such authority would impose, for example, on the Member States the duty of financial contributions when in the opinion of the European Commission the Union’s goal of RES share would not be pursued collectively. The contributions would be paid into the EU financial platform “contributing” towards development of renewable projects, established at the EU level and managed directly or indirectly by the European Commission. Member States could use as financial contribution their proceeds from greenhouse gas emissions allowances auctions. The European Commission would also be empowered to adopt delegated acts to establish and allow functioning and financing of the aforementioned financial platform. The proposed amendments of the rules governing the functioning of the internal energy market presented the mechanisms limiting the possibilities of use of capacity mechanisms by Member States, by limiting participation in these mechanisms to units with emissions below 550 gr CO_2/kWh, practically unattainable for coal based technologies. The text of the currently amended Renewable Sources Directive presents proposals for limiting the possibility of counting the energy generated from biomass towards achievement of domestic RES goals.

The work on final versions of the texts of regulatory acts constituting the “Winter Package” have been conducted within a “Trilog” of the European Parliament, European Council and the European Commission and at the present stage no agreement has been reached that could gain mutual acceptance.

In 2017, significant part of work was finalised on Network Codes and Guidelines that are the measures used under the EU law for the purpose of construction of Union-wide harmonised market in electricity and gas. The Codes are implemented legally as Regulations of the European Commission that are directly applicable in the Member States without the necessity for their implementation in national legislations. The Codes define common rules for operation and management of energy systems and are intended to eliminate the technical obstacles to further integration of the European electricity and gas markets; they are also intended to foster deregulation and ongoing growth of competition in these markets, as well as to improve service standards and security of supply. The Codes are being developed by ENTSO-E/ENTSO-G and have to comply with the non-binding framework guidelines developed by ACER. Network Codes and Guidelines may be divided into three families:

Market	defines the rules for operation of the electricity balancing market, short term markets – day ahead and intraday, as well as long term markets – forward capacity allocation.
Connection	defines the rules and requirements relating to connection of generators and demand to the electricity networks. It also defines the requirements for high voltage direct current networks and connections.
Operations	defines the requirements and rules for transmission system operators to assure system operation security, effective use of interconnected systems and resources and prevention of propagation or escalation of incidents, to avoid widespread disruptions and blackouts, as well as to allow efficient and quick restoration of electricity systems.

At present all of the eight proceeded Network Codes and Guidelines became effective and the stage of their implementation commences. This process will require further extensive consultations and conducting joint projects, both on the national and the European arenas. Implementation of provisions of the Codes will to a significant extent remodel the principles of operation of the Polish energy market in the upcoming years.

2.2. Material growth impacting factors

The most material impact on TAURON's operations will come, similar as it was in the past, from the following factors:

External factors:

1) macroeconomic situation, particularly in Poland, as well as the economic situation of the area on which TAURON Capital Group is conducting operations and at the EU and global economy level, including changes of interest rates, FX rates, etc., impacting valuation of assets and liabilities listed by the Company in the statement of financial position,
2) political environment, particularly in Poland and at the EU level, including the positions and decisions of the state administration institutions and offices, e.g.: UOKiK, URE (ERO) and the European Commission,
3) changes to the regulations related to the power sector, and also changes in the legal environment, including: tax law, commercial law, environment protection law,
4) introduction of the generation capabilities compensation mechanism (the so-called capacity market) and decisions on the future shape of the OCR (ORM) and cold intervention reserve,
5) support system for electricity generation using high efficiency cogeneration, resulting, on one hand, in the costs of redeeming ”red” and ”yellow” certificates with the suppliers of electricity to final consumers, on the other hand, in revenue from the sale of ”red” and ”yellow” certificates with the generators of electricity using cogeneration. The current support system is in force until the end of 2018; no information on its shape beyond 2018,
6) new RES support system, the so-called RES auctions,
7) situation in the power sector, including the activities and actions of the competition on the energy market,
8) number of CO_2 emission allowances allocated for free, and also prices of allowances purchased – in case of a deficit of free allowances,
9) wholesale electricity prices,
10) electricity and coal sales prices and distribution tariffs based on the adopted DSO operations regulation model, as factors impacting the revenues level,
11) prices of certificates of origin of energy from renewable sources and from cogeneration,
12) prices of fuels (energy resources),
13) environment protection requirements,
14) new non-energy products,
15) science (research) and technical progress,
16) demand for electricity and the other energy market products, taking into account changes due to seasonality and weather conditions.

Changes of the above mentioned external factors may constitute premises obliging TAURON Capital Group, in accordance with the International Accounting Standard 36, to conduct asset impairment tests. The results of these tests may have an impact on TAURON Capital Group's financial results in the subsequent reporting periods.

Internal factors:

1) steadfast implementation of the Strategy and achieving the assumed financial and non-financial effects,
2) actions with respect to optimizing processes taken by all of TAURON Capital Group's subsidiaries,
3) decisions with respect to the implementation of the key investment projects,
4) geological and mining conditions of hard coal extraction,
5) potential failures of TAURON Capital Group's equipment, installations and grids.

The impact of the above factors on the financial results achieved in 2017 is described in section 4 of this report. The effects of this impact are visible both in the short term, as well as in the long term.

2.3. What can be expected in 2018

2017 was the year of growth, both for the world economy, as well as for the Polish economy. According to the World Bank's forecasts the world economy will accelerate in 2018 even more than in 2017, and the estimated 2018 GDP growth rate worldwide will reach 3.1%.

With respect to the Polish economy analysts are predicting the 2018 GDP growth rate to continue at the level of approx. 4%[1], the unemployment rate to drop to approx. 6% and the inflation to increase (the annual average inflation rate at the level of approx. 2.3%)[2]. Poland's economy growth rate is to a large extent determined by internal consumption, however foreign investment is also the key factor. Investors TFI and BZ WBK analysts are expecting strong consumption (impacted, among others, by the declining unemployment and rising wages) in 2018, and also investments to increase, including private sector investments. Good economic situation in the Eurozone will provide a strong support for the expansion of the Polish manufacturing industry and fuel Poland's exports.

Poland's power sector can expect big challenges related to the industry regulations in 2018. The detailed capacity market regulations (ordinances, regulations) as well as the first certification process and, as a consequence, the first auctions. This will allow for developing detailed plans with respect to the future of many generating units in Poland.

In 2018, in accordance with the public announcements, works on Poland's fuel and energy policy that will set the long term expansion (growth) directions and also works on the new support system for the cogeneration will be conducted. Also, probably the decision on the future of the nuclear energy in Poland will be taken. The above material issues will impact the developing of the detailed expansion (growth) directions for Poland's energy sector. The construction of the Baltic Pipe gas pipeline, with respect to which the final investment decision should be taken by the end of the year, while the completion of its construction is expected at the end of 2022, will have a real impact on the situation of Poland's energy sector and energy security.

For KSE 2018 will be the year of commissioning or launching the full operation in the system of new conventional units with the total capacity of more than 3 GW. Also, numerous projects implemented based on the first RES auction should be commissioned (the volume contracted for 2018 reached close to 70 GWh).

Following the 2017 acquisitions on the power market (the acquisition of EDF assets by PGE Group and ENGIE assets by ENEA Group) these assets will be integrated and the impact of this concentration on the market will be visible, first of all in the generation segment.

The capacity market, and also RES auctions, should stimulate appetite for investments in new capacity. On the other hand, in case of the distribution grids the rising number of dispersed RES sources and microinstallations pose challenges in terms of ensuring the reliability of electricity supplies which will require capital expenditures on grid upgrades and replacements.

As consumption is rising the domestic electricity production is expected to increase, including electricity generated from RES. Wholesale coal prices and EUA prices can be expected to rise, and, as a consequence, also electricity and property rights prices.

[1] 2018 GDP growth rate forecasts: World Bank 4%, OECD 3,5%, government's budget assumptions 3.8%, European Commission 4.2%, NBP 4%
[2] NBP's forecasts

2.4. Core products, goods and services

The below table presents the statement of comprehensive income for the financial year 2017 broken down into the Company's main lines of business versus 2016.

Table no. 5.Statement of comprehensive income for the financial year 2017 broken down into the Company's main lines of business

Item (PLN thou.)	Financial year ended December 31, 2017				Financial year ended December 31, 2016 *(data converted)*			
	Total operations	Supply	Holding operations	Unassigned items	Total operations	Supply	Holding operations	Unassigned items
Revenue								
Sales revenue outside the Group	**995 252**	995 252	-	-	**1 669 734**	1 669 734	-	-
Intra-group sales revenue	**6 796 773**	6 765 388	31 385	-	**6 325 594**	6 323 024	2 570	-
Total revenue of the segment	**7 792 025**	**7 760 640**	**31 385**	**-**	**7 995 328**	**7 992 758**	**2 570**	**-**
Profit/(loss) of the segment	**351 539**	**320 154**	**31 385**	**-**	**79 265**	**76 695**	**2 570**	**-**
Unassigned costs	**(88 751)**	-	-	(88 751)	**(113 868)**	-	-	(113 868)
EBIT	**262 788**	**320 154**	**31 385**	**(88 751)**	**(34 603)**	**76 695**	**2 570**	**(113 868)**
Net financial revenues (costs)	**656 777**	-	812 855	(156 078)	**(114 531)**	-	(101 050)	(13 481)
Profit/ (loss) before tax	**919 565**	**320 154**	**844 240**	**(244 829)**	(149 134)	76 695	(98 480)	(127 349)
Income tax	**(65 214)**	-	-	(65 214)	**(17 119)**	-	-	(17 119)
Net profit / (loss)	**854 351**	**320 154**	**844 240**	**(310 043)**	**(166 253)**	**76 695**	**(98 480)**	**(144 468)**
EBITDA	**268 220**	**325 586**	**31 385**	**(88 751)**	**(27 078)**	**84 220**	**2 570**	**(113 868)**

The Company's operations are reported in two segments: "Supply" and "Holding operations".

Financial revenue and costs include revenue due to dividend as well as net interest revenue and costs gained and incurred by the Company due to the operation of TAURON Capital Group's central financing model. in. The financial costs include impairment write offs on the value of shares and stocks.

Unassigned items include the Company's overhead costs, as they are incurred for the benefit of entire TAURON Capital Group, thus, they cannot be directly allocated to a Line of Business.

As the parent entity TAURON performs the consolidating and management function at TAURON Capital Group.

As a result of implementing the Business Model and centralizing of the functions, TAURON concentrated many competences related to the functioning of TAURON Capital Group's subsidiaries and is currently carrying out operations, among others, in the following areas:

1) wholesale trading in electricity and related products, in particular, with respect to providing commercial services for the subsidiaries, securing the fuel requirements, CO_2 emission allowances and certificates of origin electricity,
2) purchasing management,
3) financial management,
4) corporate risk management,
5) managing the functioning of the IT model,
6) coordinating research and development activities carried out by TAURON Capital Group,
7) advisory services with respect to accounting and taxes,
8) legal support (services),
9) audit.

The above functions are gradually limited at TAURON Capital Group's subsidiaries. Such centralization is aimed at improving TAURON Capital Group's efficiency.

The core operations of the Company, besides managing TAURON Capital Group, include wholesale electricity trading on the territory of the Republic of Poland, based on the license for trading in electricity issued by the President of ERO for the period from June 1, 2008 until May 31, 2018.

The Company is focusing on purchasing and selling electricity for the needs of securing the purchase and sales positions of entities included in TAURON Capital Group and on wholesale electricity trading. Electricity sales performed by the Company in the financial year 2017 were mainly addressed to the following subsidiaries: TAURON Sprzedaż sp. z o.o. (TAURON Sprzedaż) and TAURON Sprzedaż GZE sp. z o.o. (TAURON Sprzedaż GZE).

The Company's additional operations include wholesale trading of natural gas on the territory of the Republic of Poland based on the license for trading in gas fuels issued by the President of ERO for the period from May 4, 2012 until May 4, 2022. The Company is focusing on selling natural gas for the sales needs of TAURON Sprzedaż and securing gas Leeds related to the production of heat and electricity of TAURON Wytwarzanie and TAURON Ciepło.

The competence of the Company also includes management of the property rights related to certificates of origin of electricity for the needs of TAURON Capital Group, representing the confirmation of electricity generation from renewable sources (including sources using agricultural biogas), in high-performance co-generation, in gas-fired co-generation, in mining methane-fired or biomass burning co-generation, from sources using agricultural biogas as well as the property rights related to electricity efficiency certificates.

The Company also acts as a competence centre in the area of management and trading in CO_2 emission allowances for TAURON Capital Group's subsidiaries. Due centralizing the trading in emissions, a synergy effect was obtained, based on optimizing the costs of utilizing the resources of entities included in TAURON Capital Group. Due to centralizing of this function in TAURON the Company is responsible for settlements of CO_2 emission allowances, securing the emission demand of the subsidiaries, taking into account the allowances allocated and the support in the process of acquiring limits of allowances for the following periods. In implementing the aforementioned goals the Company is an active participant of trading in CO_2 emission allowances.

In addition, TAURON also acts as the Market Operator and the entity responsible for trade balancing for TAURON Capital Group's subsidiaries and for external customers. These functions are carried out on the basis of the Transmission Agreement of 21 June 2012 concluded with the TSO – PSE. The Company currently holds exclusive control over generation capacity with respect to trading and technical capabilities related thereto, it is responsible for optimizing the generation, i.e. the selection of generation units for operation as well as relevant distribution of loads in order to execute the contracts concluded, taking into consideration the technical conditions of the generation units, the grid constraints and other factors, in various time horizons. Within the services provided for the Generation Line of Business the Company participates in preparing the overhaul plans, developing plans of available (dispatchable) capacity as well as production plans for the generation units, in various time horizons, as well as in agreeing them with the relevant grid operator. TAURON is also developing its competence with respect to the Market Operator function based on the transmission agreement with GAZ – System S.A. Since July 2015 TAURON, as one of the first entities in Poland, launched a balancing group for entities trading in gas.

In accordance with the adopted Business Model, TAURON performs management function with respect to managing the purchasing of production fuels for the needs of the generating entities included in TAURON Capital Group.

In addition, on January 15, 2014 the Company launched commercial activities related to the new product - Gasoil Futures contracts, based on the valuation of diesel oil. The product is available on the ICE Futures Europe platform that TAURON has been the member of since 2012. Gasoil contracts may be used by market participants both as a hedging instrument as well as a commercial tool. Gasoil products demonstrate high liquidity and prices of contracts refer to prices for all trade distillates in Europe and outside.

In February 2015 trading in further products of crude oil market was commenced - Brent Crude, WTI Crude, the valuation of which is associated with oil prices, and Heating Oil - a product priced based on heating oil quotations. With respect to the aforementioned products trading is concentrated not only on trading in individual contracts (outright) but also on trading in spreads created both between specific products as well as calendar spreads, corresponding to the deadlines for settling individual contracts.

TAURON uses trading in derivative products as a commercial tool in order to accomplish additional margin.

2.5. Markets and supply sources

2.5.1. Markets

Wholesale trading

TAURON conducts wholesale electricity and gas trading 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 in electricity, natural gas, CO_2 emission allowances and related products, with the purpose of generating profits on volatility of prices over time. The Company's operations also cover wholesale markets both in Poland and abroad, as well as the SPOT market and forward market.

In Poland, TAURON is an active participant of TGE and the OTC platform managed by a London energy broker - Tradition Financial Services. On February 1, 2016 TAURON signed an agreement with TGE on performing a market maker function with respect to instruments related to electricity on the RTT. In accordance with the aforementioned agreement TAURON provides not only the liquidity of products defined in the agreement, through issuance of buy and sell orders during the session but also animates the market through increasing own transactions made on the market. As a result, after exceeding a certain level of transactions market share, TAURON benefits by obtaining preferential clearing rates.

TAURON is actively participating in auctions related to the cross-border (interconnector) exchange of electricity transmission capacity on the Polish-Czech, Polish-German and Polish-Slovak border, managed by the CAO auction office. Trading on the German market with respect to trading in financial instruments such as futures, is mainly carried out through the EEX exchange. On the other hand, on the Czech and Slovak markets trading is performed through a subsidiary - TAURON Czech Energy s.r.o. Moreover, the Company is operating on exchanges of KOTE a.s. (Czech Republic) and OKTE a.s. (Slovakia).

TAURON has been steadfastly developing its competence with respect to gas fuel wholesale trade. The Company is an active participant of the gas market operated by TGE, executes transactions on the SPOT market as well as on the products of the RTT forward market. It is involved in proprietary trading activity on an international gas exchange POWERNEXT Pegas. The Company is present on the hub: GASPOOL, New Connect Germany and Tittle Transfer Facility.

Besides proprietary trading, the presence on the New Connect Germany hub (German market) also allows for physical gas deliveries to the Czech Republic. Furthermore, the Company is a participant of the Intercontinental Exchange (ICE) on the National Balancing Point (NBP) hub. Gaining access to new hubs is a consequence of the activity aimed at increasing TAURON's gas related competence and access to new sources. The volume of the OTC market transactions concluded by the Company is also successively increasing. By operating on the gas market the Company is securing commodity supplies for entities of TAURON Capital Group; moreover, proptrading operations are carried out on the forward market, aimed at taking advantage of the volatility of gas prices to generate additional margins.

Expanding the scale of its operations on the gas market TAURON is increasing its presence on foreign markets. Agreements concluded by the Company with German transmission system operators: GASCADE Gastransport and ONTRAS Gastransport GmbH as well as Czech NET4GAS s.r.o., enable purchasing gas in Germany and selling it on the Czech market.

TAURON is a participant of the European capacity trading platform, PRISMA European Capacity Platform GmbH, where it purchases interconnector capacity. With respect to capacity booking on the domestic market, the Company is operating as a participant of the auction platform, GSA GAZ-SYSTEM Auctions. Gas trading on the Czech and Slovak markets as well as interconnector gas exchange between Poland and the Czech Republic is carried out through TAURON Czech Energy s.r.o. subsidiary.

The competence of the Company also includes management of certificates of origin for the needs of TAURON Capital Group, that constitute a confirmation of generation of electricity from renewable sources, in high-performance co-generation, in gas fuel fired co-generation, in mining methane fired or biomass burning co-generation, from sources using agricultural biogas as well as energy efficiency certificates and guarantees of origin. Such operations involve active monitoring of electricity production for which property rights are issued and analyzing the demand for certificates by TAURON Capital Group's subsidiaries. The Company conducts operating supervision over purchases of property rights allocated for the fulfillment of the statutory obligation imposed on TAURON Capital Group's subsidiaries to redeem those rights and over sales of property rights acquired due to the production carried out by TAURON Capital Group's subsidiaries.

The Company also acts as the competence centre with respect to CO_2 emission allowances for TAURON Capital Group's subsidiaries and external customers. The management of CO_2 emission allowances is based on determining the demand for CO_2 emission allowances for TAURON Capital Group's installations, defining the strategy of commercial activities in the procedure in case of a deficit or surplus of allowances, replacing EUA units with cheaper CER units and active management of free allowances pool, in order to generate additional benefits. While fulfilling the role of the administrator of facilities in TAURON Capital Group, the Company is also responsible for CO_2 emission settlements of individual facilities through the redemption of allowances in the Register of Allowances. As part of the aforementioned activities, TAURON concludes sale agreements on behalf of TAURON Capital Group's subsidiaries and administers the account in the Register of Allowances. On behalf of TAURON Capital Group TAURON actively participates in consultations of legal acts on the national and European level, as well as supports the Generation Segment's subsidiaries in the process of acquiring free allowances. While implementing the above goals with respect to 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.

2.5.2. Supply sources - fuels

Fuel purchases - coal

In 2017 the Company continued coal and coal sludge purchases for the needs of: TAURON Wytwarzanie, TAURON Ciepło and TAMEH POLSKA, under agreements concluded with:

1. TAURON Wydobycie,
2. Polską Grupą Górniczą sp. z o.o. (w tym z kopalń byłego Katowickiego Holdingu Węglowego S.A.),
3. Jastrzębską Spółką Węglową S.A.,
4. Węglokoks Kraj Sp. z o.o.,
5. TRANSLIS Sp. z o.o.,
6. EP Coal Trading Polska S.A.,
7. HALDEX S.A.

The below table presents the quantity of coal purchased in 2017.

Table no. 6. Quantity of coal purchased in 2017

No.	Type of Supplier	unit	Coal quantity	Share (%)
1.	Suppliers from outside TAURON Capital Group	*Mg*	3 555 119	43,5%
2.	Supplier from within TAURON Capital Group	*Mg*	4 614 416	56,5%
	Total	*Mg*	8 169 535	**100,0%**

2.6. Timeline

The below figure presents the timeline of selected highlights associated with the operations of TAURON that took place in 2017.

Figure no. 18. Timeline

TAURON'S 2017 HIGHLIGHTS

JANUARY - FEBRUARY

- Split of TAURON Wytwarzanie by spinning off and transferring assets covering the construction of the 910 MW unit in Jaworzno to the newly formed company Nowe Jaworzno GT.
- Adoption of the *Rules of compensating members of the subsidiaries' corporate bodies.*
- Conclusion with Cracow University of Economics and Katowice University of Economics of a letter of intent on, among others, organizing postgraduate studies, internships, and promoting power industry related professions.
- Launch of a new website for customers.
- Conclusion with Banco Santander S.A. of the agreement on the provision of clearing services on EEX, EPEXSPOT, ICE, POWERNEXT with respect to processing transactions related to electricity, gas, CO_2 emission allowances and other commodity products.

MARCH - APRIL

- Implementation by TAURON Capital Group's subsidiaries of the process management based on the Business Model adopted in 2016
- Publishing of TAURON's and TAURON Capital Group's 2016 earnings
- Appointment of members of the Management Board of TAURON for the 5th common term.
- Selection of certified auditor.
- Launch of the TAURON Capital Group's Ambassador with its goal to build a positive image of TAURON Capital Group in the academic community and recruit top students.
- Adoption of *TAURON Capital Group's Corporate Social Responsibility Code*.

MAY - JUNE

- Launch of the projects qualified to the sector based "PBSE" Program as part of operation 1.2 " Sector based R+D programs".
- Publishing of TAURON's and TAURON Capital Group's Q1 2017 earnings
- Ordinary GM of TAURON.
- Appointment of Members of TAURON's Supervisory Board for the 5th common term.
- Passing of amendments to the Company's Articles of Association by the Ordinary GM of TAURON.
- Concluding with the investment funds managed by Polski

JULY - AUGUST

- TAURON eurobond issue o with the nominal value of EUR 500 mln.
- Granting by Fitch rating agency of a rating for the eurobonds issued by TAURON.
- Adoption of the *Strategic Research Agenda of TAURON Group*.
- Adoption of *TAURON Group's Environmental Policy*.
- Adoption of *TAURON Group's 2017-2025 CAPEX Strategy.*
- Approval of TAURON Group's 2017-2020 Investment Portfolio.
- Adoption of *TAURON Group's 2017-2025 Sustainable*

SEPTEMBER - OCTOBER

- Launch of the program to implement the GDPR regulations at TAURON Groups.
- Establishing the Tax Capital Group for 2018-2020.
- Launch of the project with respect to developing and implementing a new IT infrastructure in order to improve customer service.
- Introducing for use by TAURON Capital Group's subsidiaries of a new compensation policy for members of the supervising and managing authorities.
- Adoption of the *2018-2025 TAURON Brand Strategy*.
- Inclusion of TAURON in the *The Best of The Best* group and receipt of the top prize for the integrated report in the *The Best Annual Report* competition.

NOVEMBER - DECEMBER

- Publishing of TAURON's and TAURON Capital Group's Q3 2017 earnings
- Adoption of *TAURON Group's 2018-2025 Sponsoring Strategy.*
- Launch of the Project aimed at developing a detailed strategic research agenda for TAURON Capital Group with respect to 3 of 4 project portfolios.
- Adoption of a model for the operations of Shared Services Centers at TAURON Obsługa Klienta.
- Adoption of policies related to social, personnel, human rights respect and corruption counteraction related issues.
- Affirming by Fitch rating agency and ihc of TAURON's Outlook and granting of the rating for the hybrid bond issue worth PLN 400 mln.
- Extending until February 28, 2018 of the validity term of the agreement on cooperation in the 910 MWe unit construction project at Jaworzno III Power Plant with the investment funds managed by Polski Fundusz Rozwoju S.A.

2.7. Key events and accomplishments with a significant impact on the operations

The more important events and accomplishments that had a significant impact on TAURON Capital Group's operations that occurred in 2017, as well as until the day of drawing up this report are listed below. Additionally the above events should include concluding agreements significant for TAURON Capital Group's operations, described in detail in section 9.2.1. of this report.

Key business events in 2017

Eurobond issue by TAURON

On June 14, 2017 TAURON, in agreement with a consortium of investment banks, commenced activities aimed at conducting a eurobond issue of a nominal value not higher than EUR 500 mln that included in particular conducting meetings with investors in Europe. Conducting of a eurobond issue was dependent on market conditions, and the issue size, the final issue price and the interest rate of the eurobonds were determined following the meetings with investors in Europe.

The Company's intention was to file for admission of the eurobonds to trading on the regulated market of the London Stock Exchange, as well as to use the proceeds from the eurobonds issue to cover TAURON Capital Group's expenses.

On June 28, 2017 the following parameters of the eurobonds were set:

1) Total nominal value: EUR 500 mln,
2) Maturity: 10 years,
3) Interest periods: annual,
4) Coupon: 2.375 % per annum,
5) Yield as of issue date: 2.439% per annum (i.e. mid-swap + 1.63%),
6) Issue price: 99.438% of the nominal value.

The condition for the bond issue was the signature of the documentation of the transaction and the fulfillment of the conditions indicated therein.

On July 5, 2017 the Company issued eurobonds with the above indicated parameters that were admitted to trading on the regulated market of the London Stock Exchange on July 10, 2017.

On the same day Fitch rating agency granted the "BBB" rating for unsecured and unsubordinated debt in the form of the Company's 10-year eurobonds with the total nominal value of EUR 500 mln. The rating reflects the Company's leading position in the regulated and stable distribution segment that generates a significant part of TAURON Capital Group's EBITDA (72% in 2016).

The Company disclosed information on the above events in the following regulatory filings (current reports): no. 28/2017 of June 14, 2017, no. 30/2017 of June 28, 2017, no. 31/2017 of July 5, 2017 and no. 32/2017 of July 5, 2017.

TAURON ratings and outlooks affirmed; rating assigned to the hybrid bonds program

On December 21, 2017 Fitch rating agency (”Fitch") affirmed long-term foreign and local currency IDRs of TAURON at 'BBB' with a stable outlook and assigned local currency rating of 'BB+' and national rating of 'BBB+(pol) to the PLN400 million hybrid bonds program.

Full list of rating actions includes:

1) long-term foreign and local currency IDRs affirmed at 'BBB'; stable outlook,
2) short-term foreign and local currency IDRs affirmed at 'F3',
3) existing hybrid bonds affirmed at 'BB+',
4) national long-term rating affirmed at 'A+(pol)'; stable outlook,
5) national senior unsecured rating affirmed at 'A+(pol)',
6) foreign currency senior unsecured rating of Eurobonds affirmed at 'BBB',
7) ratings assigned to PLN400 million hybrid bonds program: local currency rating of 'BB+' and national rating of 'BBB+(pol).

Information on the above event was published in the regulatory filing (current report): no. 41/2017 of December 21, 2017.

Termination of the long term agreements on the purchase of the property rights by a subsidiary

On February 28, 2017 TAURON Sprzedaż filed a statement on the termination of the long term agreements on the purchase of the property rights arising from the certificates of origin of electricity from renewable energy sources (the so-called “green” certificates). Parties to the agreements concluded in 2008 are the below listed counterparties that own facilities generating electricity from renewable sources:

1) in.ventus limited liability company EW Dobrzyń limited partnership,
2) in.ventus limited liability company Ino 1 limited partnership,
3) in.ventus limited liability company EW Gołdap limited partnership.

The agreements were terminated effective immediately as a result of the parties failing to achieve an agreement while trying to renegotiate the contracts under the procedure provided for in the agreements. The financial implication of the termination of the agreements will be TAURON Sprzedaż avoiding a loss equal to the difference between the contractual prices and the market price of the ”green” certificates. An estimated net value of the above mentioned loss due to the performance of the agreements until the end of the originally assumed agreements’ term (i.e. until 2023), based on the current market prices of the ”green” certificates is approximately PLN 343 mln. Estimated total net value of the contractual obligations of TAURON Sprzedaż in 2017-2023 is approximately PLN 417 mln. The above figure was calculated based on the pricing formulas assumed in the agreements for the period running from the day of drawing up this report until the end of the originally assumed agreements’ term (i.e. until 2023).

The above event was described in detail in the regulatory filing (current report) no. 6/2017 of February 28, 2017.

Signing of the letter of intent on the coal gasification project

On April 20, 2017 a Letter of intent was signed between TAURON and Grupa Azoty S.A. defining the general rules of commencing cooperation aimed at implementing the coal gasification project.

The parties signed the Letter of intent due to the fact that among various coal conversion methods of key importance in the medium and long term are those that are offering efficient utilization of coal resources, in line also with the direction of the European Union’s policy. This is due, among others, to the need to reduce the ecological burden (footprint) of the power generation and chemical processes, including to significantly reduce the CO_2 emissions.

The detailed information on the above event is provided in section 1.5.2. of this report.

The Company disclosed information on the signature of the letter of intent in the regulatory filing (current report) no. 12/2017 of April 20, 2017.

Important corporate events in 2017

Dismissal and appointment of members of the Company's Management Board

On March 15, 2017 the Company's Supervisory Board dismissed, effective as of the end of day on March 15, 2017, all members of the Company's Management Board of the 4th common term of office, i.e.: Filip Grzegorczyk - President of the Management Board, Jarosław Broda - Vice-President of the Management Board for Asset Management and Development, Kamil Kamiński - Vice-President of the Management Board for Corporate Governance, Marek Wadowski - Vice-President of the Management Board for Finance, Piotr Zawistowski - Vice-President of the Management Board for Customer and Trade.

At the same time the Supervisory Board on March 15, 2017 appointed as of March 16, 2017 the following persons to TAURON's Management Board of the 5th common three-year term of office: Filip Grzegorczyk, as the President of the Management Board, Jarosław Broda, as Vice-President of the Management Board for Asset Management and Development, Kamil Kamiński as Vice-President of the Management Board for Corporate Governance, Marek Wadowski as Vice-President of the Management Board for Finance.

On March 15, 2017 Piotr Zawistowski up to then performing the function of Vice-President of the Management Board for Customer and Trade provided the Supervisory Board with the information on the resignation from applying for being selected to be a member of TAURON's Management Board of the 5th common term of office. Due to the change made to the Company's Organizational Regulations the Supervisory Board made, as of April 14, 2017, a change of the existing position held by Kamil Kamiński to Vice-President of the Management Board for Customer and Corporate Support.

The Company disclosed information on the change to the composition of the Management Board in the regulatory filing (current report) no. 10/2017 of March 15, 2017.

Changes to the Supervisory Board's composition

On May 25, 2017 the Company received Jacek Rawecki a statement on the resignation, as of May 26, 2017, from the function of a member of the Company's Supervisory Board. Jacek Rawecki did not provide the reason for the submitted resignation.

On May 29, 2017 the Minister of Energy, acting pursuant to § 23, clause 1, sections 1) and 3) of the Company's Articles of Association, appointed the following persons to be members of the Company's Supervisory Board of the 5th common term of office as of May 29, 2017:

1. Beata Chłodzińska,
2. Teresa Famulska,
3. Barbara Łasak-Jarszak,
4. Jan Płudowski,
5. Agnieszka Woźniak.

On May 29, 2017 the Ordinary GM of the Company, acting pursuant to § 22, clause 1 of the Company's Articles of Association, appointed the following persons to be members of the Company's Supervisory Board of the 5th common term of office:

1. Radosław Domagalski - Łabędzki,
2. Paweł Pampuszko,
3. Jacek Szyke.

The Company disclosed information on the above events in the regulatory filings (current reports): no. 19/2017 of May 25, 2017 and no. 22/2017 of May 29, 2017. The information on appointed members of the Supervisory Board was disclosed in the regulatory filing (current report) no. 27/2017 of June 5, 2017.

Decision of TAURON's Management Board on the motion filed to the Ordinary GM of the Company to cover the Company's net loss for the financial year 2016 from the Company's spare (supplementary) capital and not recommend the use of the spare (supplementary) capital for the dividend payout

On March 13, 2017 TAURON's Management Board of the Company adopted the resolution on filing a motion to the Ordinary GM of the Company to cover the Company's net loss in the financial year 2016 in the amount of PLN 166 252 898.52 from the Company's spare (supplementary) capital.

At the same time, in reference to the information on the adoption of the 2016-2025 dividend policy, provided in the regulatory filing (current report) no. 35/2016 of September 2, 2016, the Company's Management Board decided not to recommend to the Ordinary GM of the Company taking of the decision on the use of the Company's spare (supplementary) capital for the payout of the dividend for 2016 to the Company's shareholders.

The above decision was dictated by the needs related to the implementation of the investment program worth approx. PLN 18 bln by 2020 and ensuring TAURON Capital Group's financial stability, including in particular maintaining the net debt/EBITDA ratio defined in TAURON's financial agreements at the level not higher than 3.5x.

Additionally, in accordance with the information published by the company in the regulatory filing (current report) no. 41/2016 of November 14, 2016 the planned stopping of the dividend payout until 2019 was one of the factors enabling the Fitch rating agency to maintain TAURON's long term rating at investment grade level and to change the outlook from negative to stable.

The Company disclosed information on the above decision in the regulatory filing (current report) no. 8/2017 of March 13, 2017.

Shareholder's request to include particular items on the agenda of the General Meeting of the Company

On May 5, 2017 the State Treasury of the Republic of Poland, as a shareholder representing more than one twentieth of TAURON's share capital, submitted a request to include on the agenda of the Ordinary General Meeting of the Company convened on May 29, 2017 additional items related to a change of the resolution no. 5 of the Extraordinary GM of December 15, 2016 on the principles of setting the compensation of the members of the Management Board and a change to the Company's Articles of Association the scope of which was indicated in detail in the content of the regulatory filing (current report) no. 16/2017 of May 5, 2017.

State Treasury indicated as a justification for the proposed changes the need to align the principles of setting the compensation of the members of the Management Board and the content of the Company's Articles of Association to the requirements of the *Act of December 16, 2016 on the state assets management principles*.

The introduction of the amendment to the Company's Articles of Association was aimed at implementing a more transparent split of competences of the Company's corporate authorities, transparent asset management principles, investment decision making principles, manner of appointing members of the supervisory and management authorities and setting their compensation, as well as standards related to actions taken by the management boards of companies, among others in such areas as: consulting, marketing, sponsoring or meals and entertainment expenses.

The draft resolutions received from the State Treasury to be the subject of discussions at the Ordinary GM of the Company and the proposed changes to the Company's Articles of Association were published on May 19, 2017. Meanwhile on May 25, 2017 the State Treasury filed a change to the draft resolution on the change of § 20 of TAURON's Articles of Association and withdrew the draft resolution on the change of § 35 of TAURON's Articles of Association.

The Company disclosed information on the above events in the regulatory filings (current reports) no. 16/2017 of May 5, 2017, 17/2017 and 18/2017 of May 19, 2017 and 20/2017 and 21/2017 of May 25, 2017.

Ordinary General Meeting of TAURON

On May 29, 2017 the Ordinary GM of the Company was held which adopted resolutions concerning, inter alia: the approval of the Consolidated financial statements of TAURON Capital Group and the Report of the Management Board on the operations of TAURON Capital Group for the financial year 2016, the Financial statements of TAURON and the Report of the Management Board on the operations of TAURON for the financial year 2016, covering of net loss for the financial year 2016 from the spare (supplementary) capital, acknowledgement of the fulfillment of duties by members of the Company's Management Board and Supervisory Board, determining the number of members of the Company's Supervisory Board and appointing of members of the Supervisory Board, changing resolution no. 5 of the Ordinary GM of December 15, 2016, as well as amending the Company's Articles of Association.

It was decided to cover the net loss of the Company for the financial year 2016 in the amount of PLN 166 252 898,52 from the Company's spare (supplementary) capital.

The Company disclosed information on convening the Ordinary GM and on the content of the draft resolutions in the regulatory filings (current reports) no. 13/2017 and no. 14/2017 of April 27, 2017. The Company disclosed information on the adopted resolutions and the decisions of the Ordinary GM concerning: covering of the net loss, amendments to the Company's Articles of Association and appointment of the Supervisory Board members in the regulatory filings (current reports): no. 22/2017, no. 23/2017, no. 24/2017 of May 29, 2017.

Amendments to TAURON's Articles of Association

On May 29, 2017 the Ordinary GM of the Company adopted the resolutions on the amendments to the Company's Articles of Association.

As part of the passed amendments to the Company's Articles of Association the majority of the provisions of the *Act of December 16, 2016 on the state assets management principles* were implemented directly in the Company's Articles of Association. Also the competences of the Supervisory Board were extended and it shall express its consent for the conclusion of agreements on legal, marketing services, public relations and social communications services and consulting services related to management if the envisaged total net compensation for the services provided exceeds PLN 500 000, on annualized basis, with respect to donations granted or other agreements of similar effect with the value exceeding PLN 20 000 or 0.1 % of the total assets, determined based on the last approved financial statements and relieving of debt exceeding PLN 50 000 or 0,1 % of the total assets. Furthermore, the competences of the Supervisory Board were extended by including: tasks related to determining the manner of exercising the voting rights at TAURON Capital Group's subsidiaries' GMs on issues regarding setting up companies, amending the Articles of Association or the Agreement, transformations or liquidations, raising or reducing share capital, divesting and leasing out the company's enterprises or its organized part and establishing a limited property right thereupon, redeeming shares, setting the compensation of members of management boards or supervisory boards, claims for redressing damage inflicted upon formation of the company or exercising management or supervision, with respect to issues mentioned in art. 17 of the *Act of December 16, 2016 on the state assets management principles*. Also the principles of divesting fixed asset components were defined and procedures for selecting members of the management board following the qualification proceeding by the Supervisory Board the goal of which will be to verify and evaluate the candidates' qualifications were introduced, as well as the requirements for candidates for members of management authorities were defined.

On July 12, 2017 the District Court for Katowice-Wschód, the 8th Commercial Department of the National Court Register, entered into the Register of Entrepreneurs of the National Court Register the amendments to the Company's Articles of Association, adopted by the Ordinary GM of the Company by way of resolutions no. 39-45 of May 29, 2017 on amendments to the Company's Articles of Association.

On July 17, 2017 the Supervisory Board of TAURON, acting pursuant to § 20, clause 1, section 13 of the Company's Articles of Association, adopted a consolidated text of the Articles of Association of TAURON that includes the amendment to the Articles of Association entered into the National Court Register by the District Court for Katowice-Wschód in Katowice, the 8th Commercial Division.

The information on the above events was provided in the regulatory filings (current reports): no. 24/2017 of May 29, 2017, 33/2017 of July 12, 2017 and 34/2017 of July 17, 2017.

Other important events in 2017

Appointment of certified auditor

On March 15 2017 the Company's Supervisory Board appointed Ernst & Young Audyt Polska Limited Liability Company Limited Joint-Stock Partnership as the entity authorized to examine TAURON's standalone and consolidated financial statements for the financial year 2017 and review TAURON's standalone and consolidated interim financial statements for the period ending on June 30, 2017. To date the services provided by Ernst & Young for the Company included examinations of the Company's standalone and consolidated financial statements for the years: 2008 - 2012, as well as reviews of the Company's standalone and consolidated interim financial statements for the periods ending on 30 June in the individual years from 2010 to 2012. The Company also used advisory and training services provided by Ernst & Young to the extent that in no way limited the impartiality and independence of the auditor. The certified auditor was appointed in accordance with the regulations in force, following a non-public order award procedure conducted by way of offer and acceptance. The agreement with Ernst & Young will be concluded by the Management Board of the Company for a period required to perform the contracted services

The Company disclosed information on the above event in the regulatory filing (current report) no. 9/2017 of March 15, 2017.

Submission of the lawsuits in connection with the termination by PEPKH of long-term contracts for the purchase of power and property rights

1. On July 20, 2017 TAURON received the lawsuit of June 29, 2017 of Gorzyca Wind Invest sp. z o.o. with its seat in Warsaw against TAURON for payment of damages in the amount of PLN 39.7 mln and determination of liability for damages that may arise in the future due to torts, including unfair competition acts, estimated by the plaintiff to be worth PLN 465.9 mln. The case is pending before the Regional Court in Katowice. The factual basis for the lawsuit, according to the plaintiff, is the termination by PEPKH - TAURON's subsidiary, of the long term contracts for the purchase of electricity and property rights arising from certificates of origin, and the total amount of the future damages suffered by all of Wind Invest's subsidiaries will reach, according to the plaintiff, PLN 1 212.9 mln. TAURON disclosed information on the termination of the above mentioned agreements in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

2. On August 2, 2017 a submission was made to TAURON's power of attorney appointed in the lawsuit conducted before the Regional Court in Cracow, file reference no. IX GC 983/14, filed by Dobiesław Wind Invest sp. z o.o. with its registered office in Warsaw against TAURON and its subsidiary, i.e. PEPKH (to prevent the imminent danger of damage to Dobiesław Wind Invest sp. z o.o., by obligating TAURON and PEPKH and to revoke the liquidation of PEPKH), of a pleading of Dobiesław Wind Invest sp. z o.o. containing a change to the lawsuit.

   The plaintiff changed the lawsuit's claim in such a manner that it had withdrawn its original legal action against PEPKH, while it changed the legal action against TAURON from the claim to prevent the imminent danger of damage into the claim for the payment of compensation.

   Dobiesław Wind Invest sp. z o.o. was demanding: 1) payment of PLN 34.7 mln including statutory interest accrued from the day the claim was filed until the payment date, 2) determination that TAURON is liable towards Dobiesław Wind Invest sp. z o.o. for damages that may arise in the future, estimated by the plaintiff at PLN 254 mln (and stemming from TAURON's alleged torts), 3) that injunctive relief be granted against TAURON for the amount of PLN 254 mln in case the court does not find TAURON liable for the damages that may arise in the future.

   The factual basis for the lawsuit, according to the plaintiff, is the termination by TAURON's subsidiary - PEPKH with its registered office in Warsaw of the long-term contracts for the purchase of electricity and property rights arising from certificates of origin, as described by TAURON in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

   The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

3. On August 21, 2017 TAURON received the lawsuit of June 30, 2017 of Pękanino Wind Invest sp. z o. o. with its seat in Warsaw against the Issuer for payment of damages in the amount of PLN 28.5 mln and determination of liability for damages that may arise in the future due to torts, including unfair competition acts, estimated by the plaintiff to be worth PLN 201.6 mln.

   The case is pending before the Regional Court in Katowice. The factual basis for the lawsuit, according to the plaintiff, is the termination by PEPKH – the Issuer's subsidiary, of the long term contracts for the purchase of electricity and property rights arising from certificates of origin. The Issuer disclosed information on the termination of the above mentioned agreements in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

   The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

4. On October 16, 2017 TAURON received the lawsuit of June 30, 2017 of Nowy Jarosław Wind Invest sp. z o. o. with its seat in Warsaw against the Issuer for payment of damages in the amount of PLN 27 mln and determination of liability for damages that may arise in the future due to torts, including unfair competition acts, estimated by the plaintiff to be worth PLN 197.8 mln. This is the last of four announced lawsuits by Grupa Wind Invest companies in this case.

   The case is pending before the Regional Court in Katowice. The factual basis for the lawsuit, according to the plaintiff, is the termination by TAURON's subsidiary, i.e. PEPKH, of the long term contracts for the purchase of electricity and property rights arising from certificates of origin. TAURON disclosed information on the termination of the above mentioned agreements in the regulatory filing (current report) no. 7/2015 of March 19, 2015.

   The preliminary assessment of the justification for the claims contained in the lawsuit indicates that they are completely groundless.

The Company disclosed information on the above events in the regulatory filings (current reports): no. 35/2017 of July 20, 2017, no. 37/2017 of August 3, 2017, no. 38/2017 of August 21, 2017 and no. 39/2017 of October 16, 2017.

Important events after December 31, 2017

Selection of certified auditor

On February 26, 2018 TAURON's Supervisory Board selected the audit company Ernst & Young Audyt Polska Limited Liability Company Limited Joint-Stock Partnership ("Ernst & Young") to conduct an audit of the standalone and consolidated financial statements of TAURON for the financial year 2018 and a review of the interim standalone and consolidated financial statements of TAURON for the six months ending on June 30, 2018.

The selection of Ernst & Young to conduct an audit of the standalone and consolidated financial statements of the Company took place in conjunction with the need to bring the agreement concluded with Ernst & Young on auditing the financial statements for the financial year 2017 in line with the requirements of the regulations of art. 66 clause 5 of the law of September 29, 1994 on accounting in the version given thereto by the law of May 11, 2017 on certified auditors, audit companies and public supervision, including with respect to the period for which the first audit agreement should be concluded (i.e. for a period not shorter than 2 years). An amendment to the agreement with Ernst & Young will be concluded for the period required to complete the entrusted activities.

The detailed information was provided in the regulatory filings (current reports): no. 3/2018 of February 26, 2018.

2.8. Prizes and accolades (honorable mentions)

In 2017 TAURON received the following awards and accolades

Figure no. 19. Prizes and accolades (honorable mentions)

PRIZES AND HONORABLE MENTIONS AWARDED TO TAURON IN 2017

MARCH

- Awarding of a special prize to TAURON in the competition for the best investor relations among WIG30 index companies, organized by the Stock Market and Investors Paper ”Parkiet” and the Chamber of Brokerage Houses.
- Honorable mention for twelve initiatives conducted by TAURON Capital Group in the field of sustainable growth in the report ”Responsible business in Poland. Best practice” authored by Forum Odpowiedzialnego Biznesu.

APRIL

- Awarding of the *2016 Transparent Company of the Year”* title to TAURON by the Stock Market and Investors Paper ”Parkiet” for business transparency and quality of the market communications.
- Awarding of the prize to TAURON in the ”Leaders of the Energy World” competition for the energy industry’s first startup accelerator program PilotMaker.
- Awarding of the ”Leader” title to TAURON during the Techno Biznes 2017 Gala for implementing the ”Innovation Zone” application, allowing the company’s personnel to submit solutions improving the entire organization’s operations.

JUNE

- Awarding the Hero of the capital market 2017 title to TAURON in the Individual Investors Association’s competition. Individual investors appreciated TAURON’s high standards in the investor relations area and applying of the best practices in the communications addressed thereto.
- Awarding the ”Platinum MegaWatt” trophy to TAURON by TGE for being most active on the electricity market among electric utilities in 2016

OCTOBER

- Including TAURON in *The Best of the Best* group and awarding the top prize for the integrated annual report in the “The Best Annual Report” competition organized by the Institute of Accounting and Taxes. Thus the Company confirmed its position among companies that can boast the highest reporting standards.
- Awarding TAURON the *Golden Laurel of ”Super Business”* prize by business section of the ”Super Express” daily in the ”Corporate Social Responsibility”. TAURON was appreciated for the ”Houses of Positive Energy” - competition organized for orphanages and educational care facilities.
- Awarding TAURON the Wprost Innovator 2017 prize in the energy sector category for participating in the Pilot Maker program, one of the most advance accelerator programs on the Polish market dedicated to implementing solutions developed by startUPs at large enterprises.

DECEMBER

- TAURON’s inclusion, for the fifth time in a row, in the RESPECT Index - a group of listed companies managed in responsible and sustainable manner included in this index.

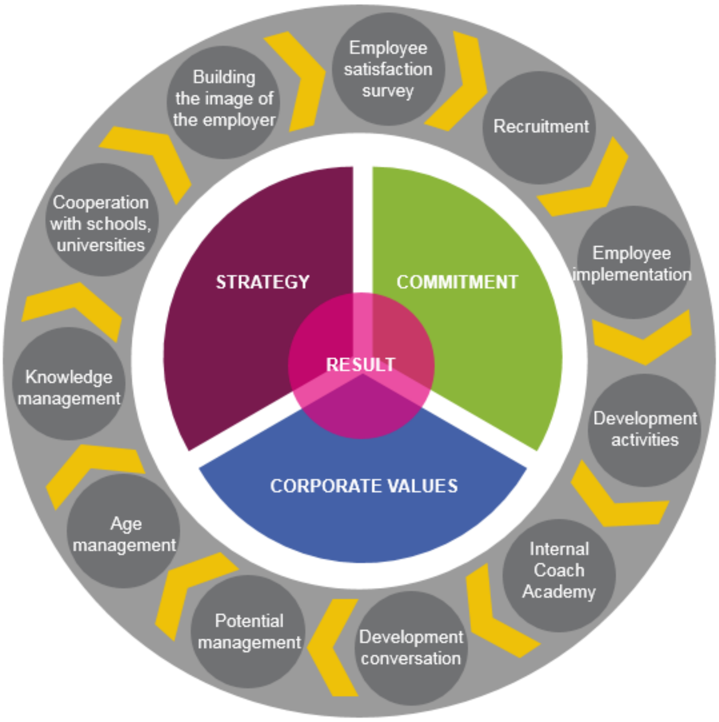
2.9. Information on TAURON Capital Group’s employment

2.9.1. Policy of Human Resources Management at TAURON Group

Adoption by TAURON Capital Group of the management by process style of management in 2017 led to updating of the applicable in all companies *Human Resources Management Policy at TAURON Group*, which together with the core values of Partnership, Development and Courage constitute the signposts for management and employees in meeting new challenges and efficiency increasing activities. TAURON Capital Group strives to develop, motivate and win employees capable of attaining the assumed objectives. The overriding purpose is to support the management in effective implementation of changes and promoting new initiatives. TAURON Capital Group seeks to establish conditions fostering development of knowledge and skills, and creating a work environment of cooperation and partnership, where innovativeness and all optimizing initiatives will be the basis for taking actions.

The below figure presents the assumptions of the *Policy of Human Resources Management at TAURON Group*.

Figure no. 20. Assumptions of the Policy of Human Resources Management at TAURON Group



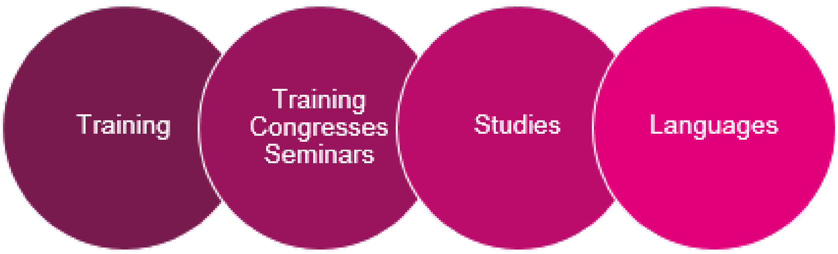
Interdisciplinary teams in the HR area of TAURON Group

Partnership attitudes as one of the core corporate values are being instilled already when developing systemic solutions. Challenges facing the HR function are undertaken in adherence to a principle of establishing workgroups consisting of HR staff from companies of the TAURON Capital Group. Team members are appointed by the HR Management Council of TAURON Capital Group, consisting of top HR manager of the Group. This proven style of HR project management results in standardizing and optimizing HR management processes, improving at the same time task completion quality with consideration of the specific requirements in each of the Group companies. Such participative approach is reflected in effectiveness of solutions and building a consistent image of the HR function.

2.9.2. Development and training

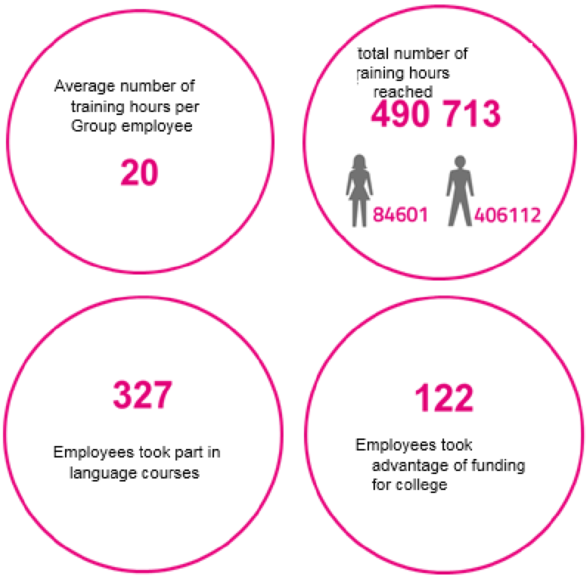
Employees of TAURON Capital Group's subsidiaries are participating various forms of development activities:
The below figure presents the forms of development activities of employees of TAURON Capital Group's subsidiaries.

Figure no. 21. Forms of development activities of employees of TAURON Capital Group's subsidiaries



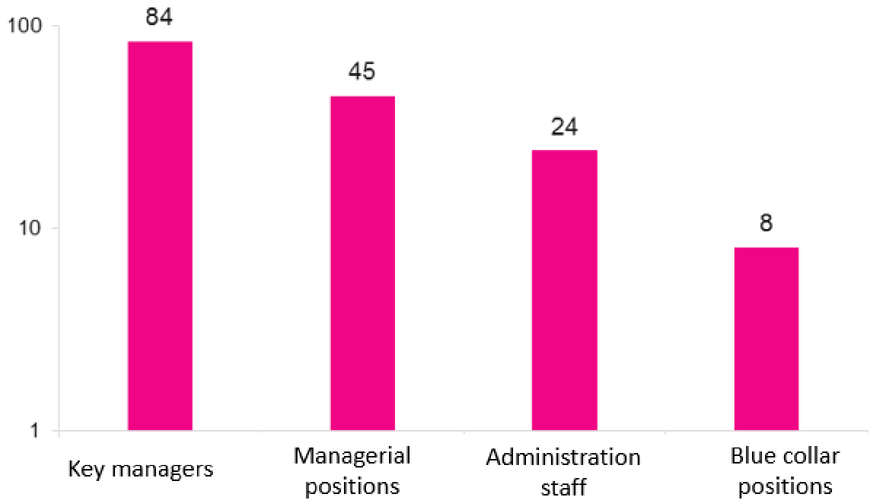
The below figure presents TAURON Capital Group's key 2017 training statistics.

Figure no. 22. TAURON Capital Group's key 2017 training statistics



The below figure presents the average number of training hours per employee, broken down into job (work position) groups.

Figure no. 23. The average number of training hours per employee, broken down into job (work position) groups



HR initiatives organized by TAURON Group

Initiative

Employee satisfaction poll (survey) at TAURON Capital Group. The Employee satisfaction poll at TAURON Capital Group took place between end of April and beginning of May 2017. The questionnaire ensured full anonymity and for the first time in history of the TAURON Capital Group was performed in all companies of the Group. Purpose of the poll was to acquire staff opinions as to the most important issues related with their working environs, including values of the company, communicating with superiors and within the company, team atmosphere and cooperation, work safety and hygiene and availability of training and development opportunities.

46% of TAURON Capital Group employees participated in the poll (3769 used hardcopy questionnaires and 7751 filled-in the electronic forms). Of the participants, 84% declared high levels of commitment to their work, 80% stated satisfaction with employee relationships and 70% expressed satisfaction with working conditions at TAURON Capital Group.

Initiative

TAURON Group's Competence Model. *TAURON Group's Competence Model* was developed in mid-2017 as a result of interaction between representatives of individual group companies, coming from a variety of business areas and the HR function. The model reflects strategy, mission, vision and key values, i.e.: Partnership, Development, Courage, and also involves business challenges facing TAURON Capital Group. The model assumes continuing staff development and supporting the attaining of results within TAURON Capital Group. Each employee has awareness of what competences and behaviors are expected of him/her; thus enabling not just performance of assigned tasks, but also developing of own professional capacities. The model affects a multitude of human resources management processes, including recruitment, adaptation, development and employee assessment. Also, individual companies held workshops devoted to the Model, addressed both to managers and employees.

Initiative

Cooperation with universities. TAURON Capital Group cooperated with almost 50 educational establishments (universities, secondary and vocational schools) all over the country. As part of the cooperation, pupils, students and graduates may apply for internship and training at TAURON Capital Group. 693 persons worked as interns in 2017. Through the cooperation partnership relations with the academic community are built - the scientific (academic) staff (faculty) and students. TAURON as a leader can influence education and gaining professional competence amount future adepts in the industry. Best students and graduates were searched for both at universities, through cooperation with university Career Offices and through participation in the largest national fair - Absolvent Talent Days. Furthermore, TAURON Group's Ambassador program was launched in 2017 with its goal to expand cooperation with universities, build a positive image of TAURON Capital Group and recruit top students from the business needs point of view. The program is announced for the given academic year, and the target group includes students in the 2^{nd} to 5^{th} year of their studies.

Initiative

The "Join Us" internship program at TAURON. TAURON launched an internship (traineeship) program in 2017, the purpose of which is to prepare most talented students at Polish universities to enter the job market. Participants are offered a versatile professional development program in state-of-the-art energy industry. Trainees are acquainted with the Company's structure, determinants and rules. The program heavily focuses on forming appropriate attitudes to the tasks assigned, attention to quality and timeliness of performing assigned tasks, valid cooperation with other persons and units within the Company, developing own initiative, acquiring teamwork skills. The program is addressed to 4th and 5th year university students.

Initiative

TAURON Group Open University. TAURON Group Open University is a cycle of lectures conducted since 2014 by the most outstanding experts specializing in various disciplines of science, politics, business, culture and personal development. Through participation in the lectures we want to provide Employees with access to current knowledge and information. In addition, this initiative allows to create a platform for the exchange of ideas and experience among employees from various companies and, consequently, to provide even better support for the implementation of TAURON Capital Group's strategic objectives.

UNIWERSYTET OTWARTY GRUPY TAURON

TAURON Group Open University was launched in order to offer the following opportunities to employees:

1) lifelong learning through exploring new issues and acquiring new skills,
2) active participation in the reality surrounding us through learning new phenomena and the skill to face them,
3) comprehensive, broadly understood development,
4) learning and using the latest technologies,
5) development of own personality, values and pro-social attitudes,
6) exploring various areas of science, life, culture and arts.

So far, 17 lectures have been provided, attended by over 3 000 employees of all TAURON Capital Group's subsidiaries. 6 lectures were organized in 2017, attended by almost 1 000 employees in total.

Initiative

Values: Partnership, Development, Courage - their implementation within the TAURON Capital Group companies. 2017 was devoted to implementing our core values: Partnership, Development and Courage ("PRO") at TAURON Capital Group's subsidiaries. Workshops introducing staff to the PRO Values program were held throughout the Group. 100% of the lines of business underwent. The workshops were conducted by the managers and HR representatives.

PRO Values are a symbol of, and determine TAURON Capital Group's organizational culture; hence it is importance for each employee to be guided by such values in performing his/her everyday duties.

TAURON PRO

PARTNERSTWO

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.

ROZWÓJ

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.

ODWAGA

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

Developing managers. The Managers Development Program comprises a comprehensive growth initiative the purpose of which is to support management level staff in both their business as well as personal efficiency, and to consciously develop model leadership attitudes within the entire TAURON Capital Group. Core values of TAURON Capital Group, i.e. Partnership, Development and Courage, guide individual actions within the program and constitute its second foundation. Developed competence enables the participants to become even more efficient leaders, whereas values determine the areas and objectives where their efficiency attains best results. The Program has been prepared and implemented based on globally proven solutions and expertise of coaches and experts involved in the Program. The development process is practical in nature and at the same time delivers inspiration and nurtures uniqueness. More than 70 key managers at TAURON Capital Group participate in the Program.

Initiative

International Family Day festivities at TAURON Capital Group. 2017 marked the fourth year in which TAURON participated in public festivities associated with the International Family Day, the purpose of which is to strengthen family ties through sincere discussion and by building and strengthening identity of the young generation. All TAURON Capital Group companies participated in the 2017 festivities. On the agreed day, employees were allowed to work 2 hours less on full pay, and free time was to be devoted to their families and friends. The companies also organized competitions promoting leitmotif of the campaign, which this year read "Cooking within the family circle". The festivities continued at TAURON, TAURON Dystrybucja and TAURON Ciepło where visits of children, and even grandchildren, at parent workplaces were organized. Visits were accompanied by entertainment and attractions.

Initiative

Management by Objectives training for management staff. In 2017 TAURON held a series of workshop course dedicated to management staff, devoted to the Management by Objectives methods, particularly principles of setting and cascading objectives based on the SMART model. The goal of the workshops was to make the participants familiar with the principles of evaluating attaining of objectives and giving constructive return information. Also, tools used to support employees in attaining their objectives and tools for assessment of subordinates were presented. More than 60% of the Company's management staff participated in the two-day workshops.

Initiative

Policies combating Mobbing and Discrimination at the TAURON Group. The *Policy of combating Mobbing and Discrimination at the TAURON Group* was developed in the second half of 2017. The policy document applies throughout the entire TAURON Capital Group. The policy defines principles for counteracting mobbing and discrimination at the workplace and in relation to performing duties, ensures implementation of labor law provisions and includes internal regulations enforced by the employer. Intervening activities and actions aimed at alleviating abusing mobbing or discrimination behaviors against employees were presented, as well as consequences awaiting perpetrators.

2.9.3. Social dialogue

The Management Board of TAURON conducts a constructive and open dialogue with the workforce (social party), mainly aimed at maintaining high quality and effectiveness of mutual cooperation. During regular meetings and consultations, the workforce representatives are informed about issues associated with:

1) TAURON Capital Group's economic and financial situation of TAURON Capital Group,
2) TAURON Group's 2016-2018 Efficiency Improvement Program and Strategic Initiatives,
3) Voluntary Redundancy Programs underway at TAURON Capital Group's subsidiaries,
4) issues related to employee affairs at TAURON Capital Group.

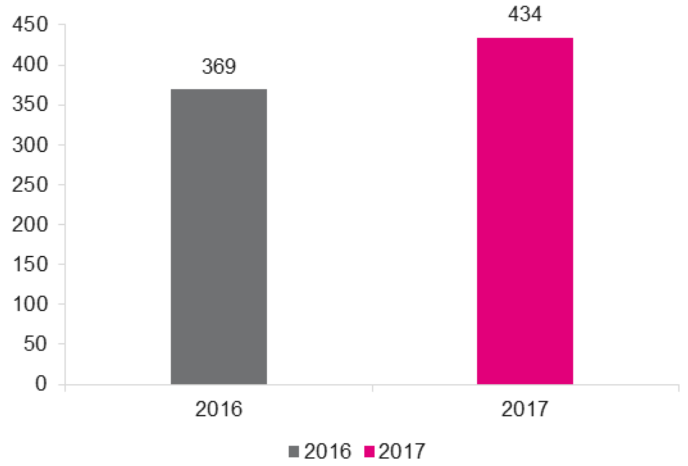
As part of the conducted social dialogue the Management Board of TAURON provided many answers to the correspondence from the trade union organizations and the Ministry of Energy. In parallel, ongoing communication is maintained at TAURON Capital Group's subsidiaries between Management Boards and trade union organizations operating at the given employer. TAURON takes an active part in meetings at the national level with the representatives of the government, employees and employers (within the activities of the Tri-party Team for the Energy Sector).

2.9.4. Key headcount data

TAURON's average headcount reached 434 FTEs in 2017 which means an increase versus the headcount in 2016, when the average employment was 369 FTEs.

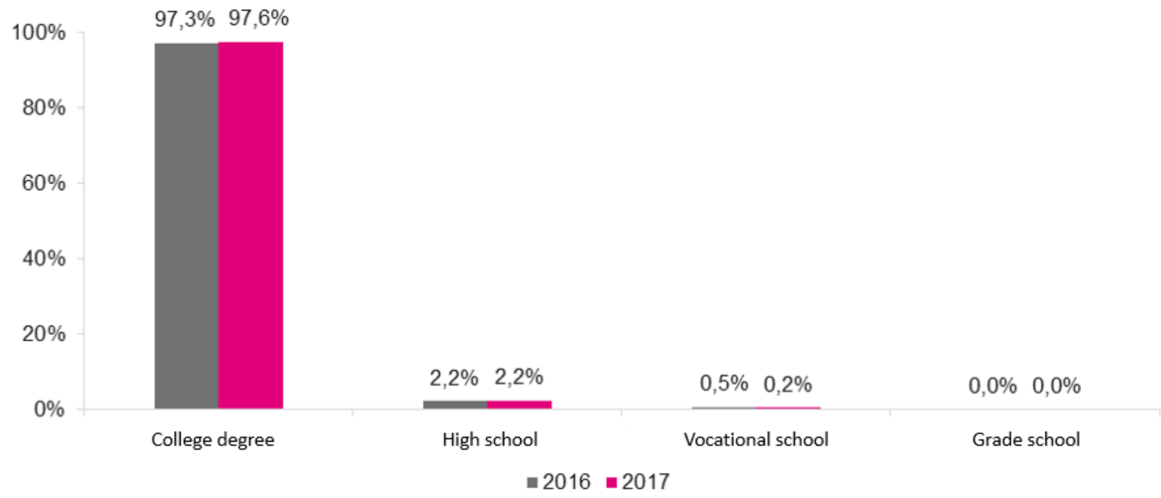
The below figure presents TAURON's average headcount in FTEs (rounded up to the full FTE) in 2016 and in 2017.

Figure no. 24. TAURON's average headcount in 2016 and in 2017 (FTEs)



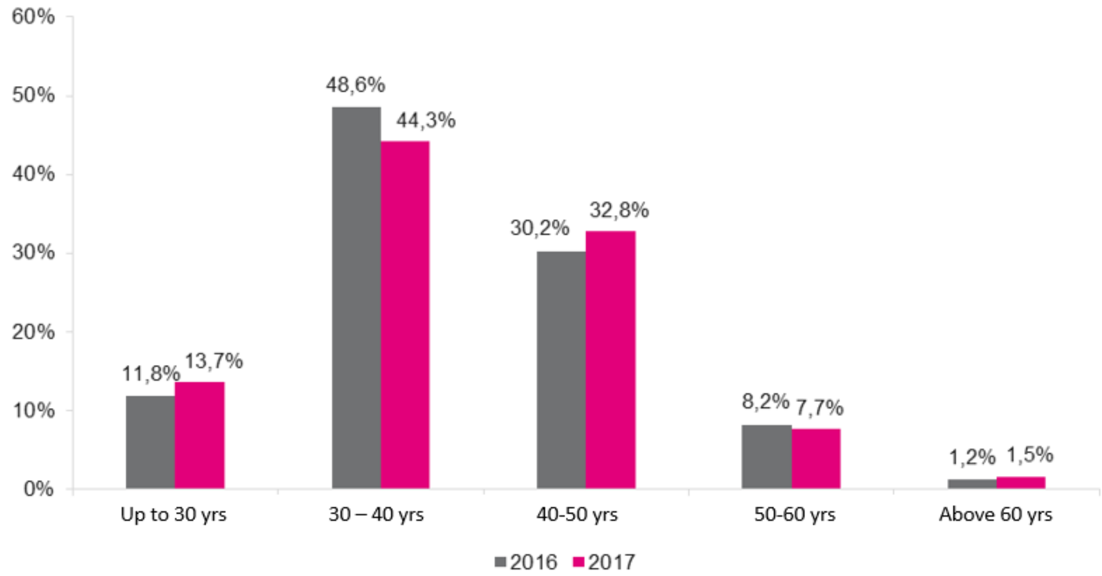
The below figure presents the structure of employment at TAURON by education level as of December 31, 2016 and December 31, 2017.

Figure no. 25. Structure of employment at TAURON as of December 31, 2016 and December 31, 2017 (by education level)



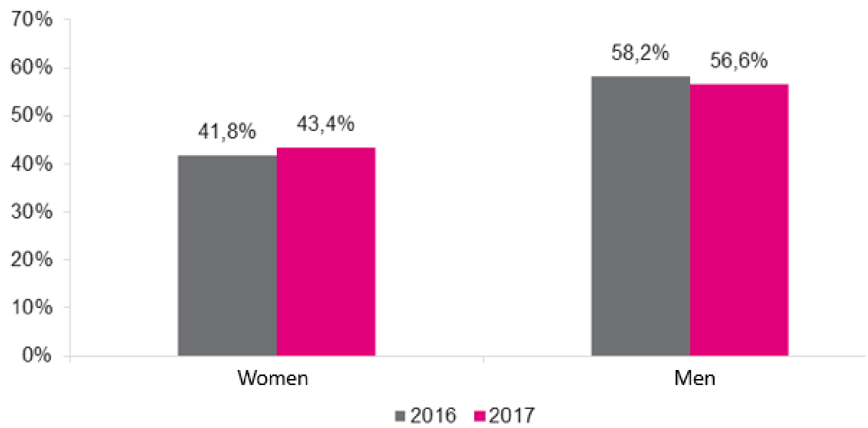
The below figure presents the structure of employment at TAURON by age as of December 31, 2016 and December 31, 2017.

Figure no. 26. Structure of employment at TAURON as of December 31, 2016 and December 31, 2017 (by age)



The below figure presents the structure of employment at TAURON by gender as of December 31, 2016 and December 31, 2017.

Figure no. 27. Structure of employment at TAURON as of December 31, 2016 and December 31, 2017 (by gender)



2.10. Corporate Social Responsibility (CSR) Policy

TAURON Group's 2017-2025 Sustainable Development Strategy

Undertakings commenced in 2016 were continued in 2017 in order to strengthen TAURON Capital Group's position as a leading, innovative and modern enterprise that is steadfastly implementing its Strategy and Business Model.

On August 1, 2017 TAURON's Management Board adopted the updated *TAURON Group's 2017-2025 Sustainable Development Strategy* (Sustainable Development Strategy) that was developed based on *TAURON Group's 2016-2025 Strategy*, taking into account feedback of the stakeholders, and also the current challenges facing the energy sector. Sustainable Development Strategy constitutes the framework of actions with respect to TAURON Capital Group's Corporate Social Responsibility.

Sustainable Development Strategy is based on 5 directions. Two of them are of leading nature as they are related to the operations on the market - "Orientation towards the customer and his/her needs" and "Reliability and quality of the supply of products and services for customers". The other three are the supporting directions and they include "Labor safety, ethical culture and employee engagement", "Environment protection" and "Social and business partnership". For each direction obligations (18 in total) that TAURON is intending to fulfill by the end of 2025 were defined. For each obligation key initiatives were formulated that support their implementation and they were assigned to the individual organizational units (business units) of TAURON Capital Group.

Reporting non-financial data

Sustainable Development Strategy is directly associated with all of TAURON Capital Group's lines of business. It streamlines both the approach to the CSR as well as the methodology for assessing the effectiveness of measures undertaken based on Global Reporting Initiative (GRI) indicators.

In 2017 TAURON Capital Group published its integrated report for the second time. Apart from the financial data the document presented the complete view of the company's operations, including its impact on the economy, society and environment.

The integrated formula provided a clear way to show the relationships and dependencies between the financial and non-financial aspects of the operations of all of TAURON Capital Group's subsidiaries and thus constituted a comprehensive and transparent document, presenting the company's operations, its Business Model, Strategy, most important changes, opportunities and risks, and also the results from the point of view of all stakeholder groups. Combining the financial data with the non-financial aspects of the company was also aimed at showing the potential reached due to the synergies between the core operations and the non-business activities.

The report was prepared in accordance with the highest reporting standards – GRI G.4, and it was subjected to external verification by an independent auditor. The Company was also audited in connection with joining the RESPECT Index - the index comprising companies listed on the stock exchange, operating in accordance with the rules of sustainable development. In 2017, TAURON achieved, for the fifth time, a positive result and was included in this most prestigious ranking of socially responsible companies.

Key CSR projects

One of the directions of the Sustainable Development Strategy is the social and business partnership. The resulting goals are implemented, among others, through the activities of TAURON Foundation which allows for even more effective implementation of CSR goals with respect to taking care of safety of local communities and actions for public benefit.

TAURON Capital Group, operating in the south of Poland, holds the leading position in electricity distribution and its supply on the territory of the Lower Silesia, Opole, Silesia and Małopolska regions. Because of that the range of actions conducted for the benefit of the communities in which TAURON Capital Group's subsidiaries are operating, is very broad. Many projects are supported which are important for the inhabitants of the Upper and Lower Silesia, Opole, Małopolska and Podkarpacie tegions. Among others, TAURON is cooperating with the Mountain Voluntary Emergency Service (GOPR), with the goal to improve safety in the mountains.

In 2017 TAURON continued also its cooperation, commenced in 2014, with the SIEMACHA Association - one of the leading NGOs in the country focusing on the implementation of projects in the area of education, sports and therapy, providing systemic assistance to children and teenagers. As part of this cooperation TAURON's patronage covered sports activities of the association, gaining the title of *TAURON - SIEMACHA's sports partner*. In 2017 such projects were supported as *Football Children's Day with TAURON* and *Juliada.*

Activities carried out by TAURON Capital Group's subsidiaries are also worth mentioning. In 2017 the campaign, implemented by TAURON Sprzedaż, called: *TAURON does not go door to door to sell electricity or gas* was continued. Its stage focused on raising awareness of customers on the energy market, in particular, in order to protect them against practices of unfair salesmen. On the other hand, TAURON Dystrybucja has been conducting, since 2013, an educational program for children and teenagers called *TAURON fuses. Switch on for the kid's benefit.* Its main goal is to improve safety by popularizing the rules of safe electricity use.

In 2017 TAURON Foundation, the Company and TAURON Dystrybucja implemented the thirteenfth edition of the Houses of Positive Energy campaign, addressed to 24-hour custody and caretaking facilities, aimed at improving the living conditions of children from orphanages and educating, motivating them to act, opening prospects and enabling to set themselves apart in a positive manner. Since refreshing the campaign's formula, i.e. since 2011, 523 orphanages have taken part in the campaign. Young persons taking part in the campaign are competing for a financial prize every year in order to fulfill their youth passions, dreams and wishes.

In 2017 the Foundation also accomplished its goals, in particular, through supporting private individuals and legal entities, institutions and organizations in their activities consistent with the Foundation's goals, transferring by way of donations PLN 3 074 896.41.

TAURON is a signatory of the declaration signed on June 17, 2009 during the national conference as part of the cycle *Responsible Energy*, comprising the principles of sustainable development in the energy sector in Poland.

In 2013, the Company joined a group of signatories of the *Business declaration for the sustainable development*, consequently undertaking to get involved in the implementation of strategic goals of the *Vision of sustainable development for the Polish business 2050*.

Since 2014, TAURON has also been a member of the Responsible Business Forum.

2.10.1. **Energy security**

Ensuring energy security to customers is the first of the obligations included in the Sustainable Development Strategy. As an essential element of Poland's energy system, TAURON optimizes processes in individual lines of its business operations: generation, distribution and supply of electricity and heat, in order to ensure stable power supplies with high quality parameters to customers. In order to ensure continuity of power supply, TAURON not only implements new investment projects but also conducts ongoing maintenance works and upgrades of its infrastructure held as well as actively searches for new solutions.

In 2017 TAURON Dystrybucja upgraded almost 1 300 km of existing grids and 36 main power supply points. The Company also built 2 500 km of new lines including the connections. Also 4 new main power supply points were built. Investment projects are also conducted by TAURON Ciepło. In 2017 the total capacity under the agreements with customers on new connections to the heating network reached 47.2 MW.

On August 30, 2017 an agreement on financing the Low Emission Elimination Program (Program Likwidacji Niskiej Emisji - PLNE) in 8 cities of the Silesia and Dąbrowa metropolitan area covered by the low emission, i.e.: Będzin, Chorzów, Czeladź, Dąbrowa Górnicza, Katowice, Siemianowice Śląskie, Sosnowiec, Świętochłowice, was signed. TAURON Ciepło is planning to connect, under PLNE, by the end of 2022, approximately 1300 buildings which represents approximately 183 MW of heat capacity in total. Ultimately, as a result of the construction and refurbishment of the heating networks under PLNE, 100 km of modern heating networks (pre-insulated) will be built.

Under PLNE, by the end of 2017 TAURON Ciepło concluded, additionally, agreements with customers on connecting building to the heating networks with the total capacity of 14 MW.

At the same time, in order to guarantee stable supplies, TAURON Dystrybucja conducts ongoing measures minimizing the risk of failure as well as shortening the response time necessary to find the place of failure and to remedy it. It is fostered, inter alia, by the implementation of the modern system of Grid Assets Management or the increase of the grid automation level. For several years, rules of prioritization of investment needs have been applicable in TAURON.

They are aimed at addressing the expenditure to places that have the strongest impact on the improvement of electricity supplies and effectiveness of the distribution grid performance, including the enhancement of the qualitative electricity indicators.

Moreover, taking care for comfort and security of persons having contact with electricity and the equipment supplied by it, TAURON Dystrybucja has been carrying out the educational and information campaign called *TAURON Fuses* addressed to children and teenagers. In 2017 a multimedia educational platform was developed and launched, providing teachers, pupils and parents with access to educational materials. Some of them are adapted to the needs of disabled pupils. The Company is also the initiator and co-organizer of other social campaigns enhancing the level of energy supply reliability (e.g. “Stop the illegal electricity intake” campaign).

Innovative technological solutions represent an important element of the energy supply process. Accordingly, TAURON Capital Group puts strong emphasis on activities in the area of research and development, resulting not only in innovative solutions with respect to, inter alia, reducing the emission of hazardous substances from combustion processes but also innovative products and services for individual customers (e.g. Electricity with an electrician 24 h, offering ”Your 300”, Preferential 0 percent interest rate for those buying boilers from TAURON).

Since 2016 the Zone of Innovation has been operating in TAURON Capital Group’s intranet, within which competitions for employees are organized. Its objective is to promote innovative organizational culture and encourage employees to submit innovative solutions optimizing daily work. After the announcement of the competition results, the proposals are archived and available in the Zone of Innovation to all users. The first competition launched in the Zone of Innovation was related to safety at work place. In 2017 all projects that won prizes in the “Safe at work” competition were implemented. They included, e.g. representing a compendium of Occupational Health and Safety, safety boards and books at TAURON Wydobycie’s Janina Coal Mine and the boards promoting the slogan ”Always in good form!”, presenting simple exercises dedicated to office workers, placed at all TAURON Capital Group’s subsidiaries’ sites nest to network printers. The Research and Development Team was also conducting Works on further initiatives aimed at engaging the workforce to be innovative.

2.10.2. Customer orientation

At the time of intense changes in the market environment, progressing digitization and mobility of the society also a visible change of customer expectations is taking place who are becoming more active and aware, expect a broad and comprehensive offering and modern service channels. Meeting the needs of almost 5.3 mln customers, and also orientation towards their needs is reflected in the Sustainable Development Strategy in which customer related issues represent the two leading directions: ”Reliability and quality of the supply of products and services for customers” and ”Orientation towards the customer and his/her needs”.

Efforts aimed at accomplishing the assumed obligations in this respect are based on many measures in each of the value chain areas, inter alia, through grid modernization, searching for solutions enhancing customer satisfaction, ensuring security of customer interests, care for vulnerable customers and disadvantaged groups as well as through continuous education in the area of effective use electricity and its safe utilization.

TAURON analyses market trends on an on-going basis as well as conducts cyclical customer satisfaction surveys concerning the services and products offered. Owing to such activities the Company endeavors to meet customers’ expectations, satisfying their current and future needs, to the largest extent possible. At the same time, complaint handling procedures are improved, allowing for prompt and efficient response in situations reported by customers. All measures constituting the customer service process are conducted in compliance with the highest ethical standards.

Seeking not to limit the relations with customers only to the provision of products and services, as well as having the awareness of many threats which may potentially affect a customer in various aspects of electricity purchase or use, TAURON conducts educational campaigns addressed to electricity users.
The educational and informational functions are fulfilled, inter alia, by the action “Energy for the senior”, implemented by the Team of Customer Rights Ombudsman operating within the customer area in TAURON. The initiative is addressed to the elderly who are most exposed to activities of unfair energy vendors (salesmen). Its aim is to educate customers how to move across the energy market. The action is based on the inter-sectoral cooperation of business, public administration represented by consumer rights ombudsmen and non-governmental organizations, i.e. universities of third age, senior clubs as well as associations of retired and pensioners. Within the workshops, both lectures for a broad group of audience and intimate educational meetings are organized.

2.10.3. Customer satisfaction survey

One of key tools of customer satisfaction evaluation at TAURON Capital Group is the CSI survey (poll). This survey is conducted on a regular basis, once a year, at the turn of the 2^{nd} and 3^{rd} 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 S.A. (ENERGA) and PGE.

In accordance with the adopted plan the CSI poll, representing one of key tools of customer satisfaction evaluation at TAURON Capital Group, was conducted in June - August 2017 by an independent research agency - TNS Polska S.A.

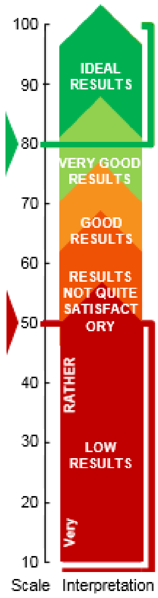
The survey covered randomly selected customers of the Household segment (1 000 customers), Small enterprises (200 customers) and Corporations and large enterprises (300 customers) and a group of customers of other energy companies, such as: ENEA, ENERGA and PGE.

As a result of conducted surveys the CSI was determined to be at the following level:
1) Households - 80 points,
2) Small enterprises - 71 points,
3) Corporations and large enterprises - 77 points.

The below figure presents results of surveys conducted in the Household segment, achieved by TAURON in the period from 2011 to 2017, and the level of the CIS indicator reached in 2017, as compared to other energy groups

Figure no. 28. Results of the survey covering households in 2011-2017

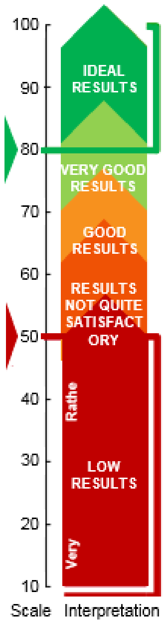
TAURON	2017	2016	2015	2014	2013	2012	2011
Settlements and payments	89	89	87	86	80	79	79
Loyalty indicator	**85**	**86**	**84**	**83**	**77**	**77**	**73**
Failures and outages	82	82	80	77	76	75	74
CSI indicator	**80**	**80**	**79**	**76**	**73**	**73**	**71**
Customer service	79	82	80	81	78	80	77
Image	76	78	75	73	69	67	66
Prices and tariffs	70	70	67	63	57	55	50



The below figure presents the results of the TAURON survey as compared to other Energy Groups in 2017.

Figure no. 29. Results of the TAURON survey as compared to other Energy Groups in 2017

	TAURON	COMPETITION TOTAL	Energa	Enea	PGE	innogy
Settlements and payments	89	86	85	88	87	83
Loyalty indicator	**85**	**81**	**79**	**81**	**84**	**69**
Failures and outages	82	80	81	80	81	76
CSI indicator	**80**	**76**	**74**	**77**	**79**	**69**
Customer service	79	76	73	75	80	63
Image	76	72	71	72	74	61
Prices and tariffs	70	66	67	66	68	55



2.10.4. Impact on natural environment

Environmental protection in the energy sector is the area controlled and regulated by the EU and national legal regulations as well as the local law, therefore, it is strongly associated with the business operations of TAURON Capital Group, in particular, in the context of contemporary challenges related to minimizing the environmental impact throughout the value chain: from mining, through generation and distribution, up to the supply of electricity and heat to final consumers. Considering the sustainable development rules, TAURON Capital Group's subsidiaries are optimizing the processes of management of the resources used (water, raw materials and materials) and are also conducting an active policy of waste management (both process related waste as well as the other waste arising as a result of the operations conducted).

The pro-ecological education conducted by the individual TAURON Capital Group's subsidiaries, addressed both to children and youth as well as to adults, also plays an important role in the area of environmental protection.

TAURON Capital Group's subsidiaries are actively engaging in many information and educational programs concerning environmental protection and energy saving and conservation which are addressed both to employees, local communities and to customers. Such actions include the educational campaign to combat low emission called ”Breathe with Air”, launched in 2016 and continued in 2017.

A confirmation of the above actions was the adoption in July 2017 of *TAURON Group's Environmental Policy*, in which it was stated that TAURON Capital Group accepts responsibility for taking care of natural environment and the consequences of the use of its resources for the benefit of the current and future generations, recognizing as important the social obligation to ensure environment protection both in its operations, as well as among its customer partners.

The most important actions with respect to environment protection

TAURON Capital Group's subsidiaries are conducting responsible environmental protection policy and apply due diligence to ensure that both the operations conducted as well as the implemented investment projects are compliant with the requirements and include technological advancements with respect to environment protection.

The most important actions with respect to environment protection conducted by TAURON Capital Group in 2017 included:

1) continuation of the construction of the 910 MW unit capacity at Jaworzno III Power Plant, whose commissioning will significantly influence the reduction of emissions of NO_x, SO_2, CO_2 and particulate matter (TAURON Wytwarzanie),
2) Projects started: Revamping of the mechanical sewage treatment plant with chemicals support at the Jaworzno III Power Plant - Power Plant II (TAURON Wytwarzanie), modernization of the electrofilter of unit no. 5 at Jaworzno III Power Plant in order to reduce dust emission (TAURON Wytwarzanie),
3) Projects started at Łaziska Power Plant: revamping of the hydrochloric acid, sodium hydroxide, iron sulphate unloading station to enable unloading of truck takers and commencing with project on protecting the mazut unit area against penetration of hazardous substances into the environment (TAURON Wytwarzanie),
4) General overhaul of electrofilter No. 1 and partial upgrade of lighting system to LED technology within the general overhaul of Power Unit No. 1 at Siersza Power Plant (TAURON Wytwarzanie),
5) Low Emissions Elimination Program implementation (TAURON Ciepło),
6) Revamping of hydroelectric power stations to reduce oils leakage and contamination of natural environment risks caused by installation failures (TAURON EKOENERGIA),
7) Launching of project associated with construction of a fish ladder at the Marszowice Hydroelectric power station (TAURON EKOENERGIA),
8) Construction and reconstruction of the sanitary and rainwater sewerage system for ZG Sobieski with up-connection to the municipal grid (TAURON Wydobycie),
9) Revamping of transformer stations to protect the water environment (transformer stations equipped with trays) and elimination of intrusive sources of noise (TAURON Dystrybucja),
10) Launching of the project associated with heat recuperation at the limestone milling unit (KW Czatkowice),
11) Launching of the project associated with automatic road sprinkling using process water supply (KW Czatkowice),
12) Thermal revamping of vehicle service station and control room building (KW Czatkowice),
13) Revamping of the heating system - laying of external gas supply network by Polska Spółka Gazownictwa sp. z o.o. (PSG) (KW Czatkowice),
14) Reconstruction of the Dumping Station with construction of dust removal system for reducing random emissions (KW Czatkowice),

15) Pro-ecological initiatives - educational campaign developing ecological awareness of young people: "Clean up of the Pilchowski Reservoir", where 159 students of partner schools within operating area of TAURON EKOENERGIA together with teachers and employees of TAURON EKOENERGIA completed the 19th campaign of cleaning shores of the Pilchowski Reservoir. Over 400 120-liter bags of refuse were collected (TAURON EKOENERGIA),

16) Continuing of the long-lasing "Our Stork" campaign, i.e. construction of successive stork nest poles and performing necessary maintenance of existing nest poles (TAURON Dystrybucja).

The exemplified above actions are aimed at ensuring the compliance of TAURON Capital Group operations with regulations applicable in protection of the environment, with consideration of local circumstances, specific nature of our business, striving at the same time to improve efficiencies.

Minimizing the negative impacts on the environment

Minimizing of the negative impacts on the environment is effectively implemented the specifics of the sector, technology advancements and access to the environmentally friendly technologies.

TAURON Capital Group is monitoring on an ongoing basis the main aspects of the direct and indirect impact on the environment of its operations.

The effects of implementing the capex plan over many years, related to adapting TAURON Wytwarzanie's conventional sources to comply with the tightened emission requirements allowed, in 2017, for the operations of the generation units at values well below the NO_X, SO_2, dust emission standards currently in force and in many cases close to the values of the future environmental requirements.

The below table presents the estimated levels of NO_X, SO_2, dust and CO_2 emissions from fuel combustion for electricity generation purpose for selected TAURON Capital Group's subsidiaries in 2017.

Table no. 7. Annual levels of NO_X, SO_2, dust and CO_2 emissions from fuel combustion for electricity generation purpose for 2017

No.	Subsidiary name	SO_2 emission (Mg)	NO_X emission (Mg)	Dust emission (Mg)	CO_2 Emissions (Mg)
1.	TAURON Wytwarzanie, including:	13 385	13 701	733	14 654 964
	Oddział Jaworzno III	3 423	5 438	143	6 919 502
	Oddział Łaziska	3 430	3 302	182	3 879 920
	Oddział Łagisza	2 343	2 294	161	1 869 428
	Oddział Siersza	2 686	1 706	177	1 538 045
	Oddział Stalowa Wola	1 503	961	70	448 069
2.	TAURON Ciepło, including:	3 522	1 610	217	1 913 711
	ZW Bielsko-Biała	979	278	29	500 989
	ZW Kamienna Góra[3]	52	17	6	17 208[3]
	ZW Katowice	1 572	660	84	877 950
	ZW Tychy	591	543	18	422 857
	CC Olkusz	143	39	10	40 239
	CC Zawiercie	127	43	9	36 079
	Other (local heating plants[3]	58	30	61	18 38
3.	KW Czatkowice	3	6	14	5 909
	Total	**16 910**	**15 317**	**964**	**16 574 584**

[1]Total emission of dust from fuel combustion

[2]CO_2 emission within the meaning of EU ETS - according to Annual Reports on CO_2 Emission (status in January 2017, the level of emission prior to verification)

[3]Installations not covered by EU ETS. Estimated value, prior to verification at the end of the 1st quarter of 2017

TAURON Capital Group accepts responsibility for taking care of natural environment and the consequences of the use of its resources. In 2017 TAURON Capital Group's subsidiaries accrued fees in the total amount of approximately PLN 38.6 million, i.e. approximately 8% more than in 2016.

The below table presents the level of fees for the use of the environment for business purposes due for 2017 at selected TAURON Capital Group's subsidiaries.

Table no. 8. The level of fees for the use of the environment for business purposes due for 2017.

No.	Subsidiary name	Fees for use of the environment for business purposes due for 2017 (PLN thous.)
1.	TAURON Wytwarzanie	21 012
2.	TAURON Wydobycie	13 372
3	TAURON Ciepło	4 074
4.	TAURON Dystrybucja	100[2]
5.	KW Czatkowice	50
6.	TAURON Dystrybucja Serwis	12[2]
7.	TAURON Obsługa Klienta	1,9
8.	TAURON EKOENERGIA[1]	< 0,8
9.	TAURON Sprzedaż	1,6
	Total	**38 623,5**

[1]Total amount below PLN 800 a year is not subject to the statutory exemption from paying fees for the use of the environment for business purposes.
[2]Estimate data, the annual settlement has not been closed.

Sustainable development

TAURON Capital Group is taking actions aimed at improving energy efficiency in order to reduce or not increase the consumption of fuels and monitoring climate impact.

In 2017 within TAURON Capital Group a number of investment projects were submitted, associated with the improvement of energy efficiency in the Distribution and Mining lines of business, whose direct environmental effect is the reduction of CO_2 emission. This effect was partly confirmed through the allocation of the so-called “white” certificates as a result of the tender, resolved in July 2017, carried out by the President of ERO based on the rules in force before, i.e. 2016 rules. The remaining part of the effect will only be confirmed in 2018 through the allocation of the property rights certificates according to the new principles of the amended energy efficiency law.

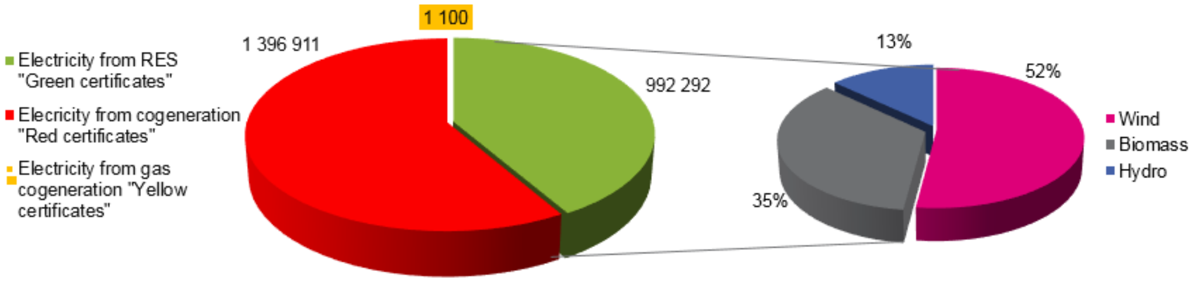
Furthermore, in 2017 an energy efficiency audit was completed for all of TAURON Capital Group’s Lines of Business in order to identify optimization areas.

Although the core production of TAURON Capital Group is based on the traditional energy relying on solid fossil fuel, TAURON Capital Group, in its basic volume of production, includes high efficiency generation of electricity and heat in the co-generation system and supplements its offering with electricity generated from renewable sources or in generation based on gas which is reflected in the quantity of property rights to the certificates of origin of electricity generated:

- 992 292 MWh, so-called “green” certificates,
- 1 396 911 MWh, so-called “red” certificates,
- 1 100 MWh, so-called “yellow” certificates.

The below figure presents the structure of the property rights to the certificates of origin obtained by TAURON Capital Group in 2017.

Figure no. 30. Structure of the property rights to the certificates of origin (MWh)



Management of by-products

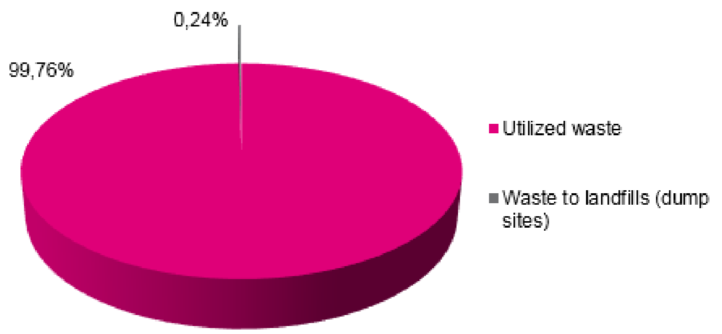
TAURON Capital Group, caring for the natural environment, minimises the quantity of waste deposited in the environment through their introduction to the market, to be used as substitutes for natural materials.

Waste generated by TAURON Capital Group is mainly used in the construction, road building and mining sector. The waste is broadly used by cement and concrete plants. It was also used as the material for reclamation of unfavourably transformed areas.

In 2017 TAURON Capital Group's conventional power generation segment generated approximately 2.2 million Mg of furnace waste, including 99.76% that was managed on the market and only 0.24% was deposited directly at the dumping sites.

The below figure presents the structure of energy waste management.

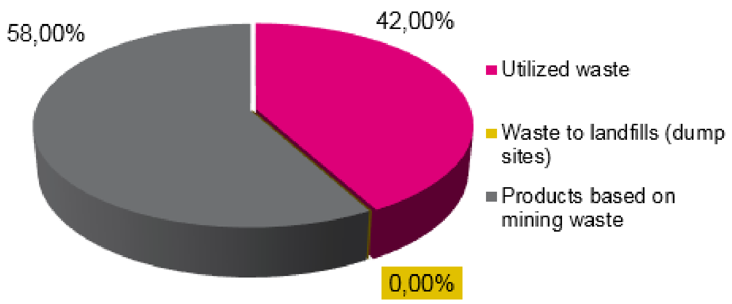
Figure no. 31. Structure of energy waste management



In 2017 hard coal mining at TAURON Capital Group generated 1.1 million Mg of mining waste and 1.4 Mg of full value aggregate products. The products obtained were used in various industries, among others in the construction and mining. waste comprised aggregate and sludge originating from coal processing and preparation. 100% of the waste generated was used for the business purposes.

The below figure presents the structure of mining waste management.

Figure no. 32. Structure of mining waste management



TAURON Capital Group is seeking to implement the model of closed circuit (circular) economy. It is planned that the maximum of generated process waste is used within TAURON Capital Group, consequently reducing the consumption of natural resources and the product's carbon footprint.

2.10.5. Sponsoring activities

In 2017 TAURON introduced significant changes to its internal regulations related to the sponsoring activities. New *Rules of conducting sponsoring activities by TAURON Group* taking into account the *Best practice with respect to conducting the sponsoring activities by companies with the State Treasury shareholding. TAURON Group's 2018-2025 sponsoring strategy* was adopted. The sponsoring activities were conducted based on the *Plan of conducting the sponsoring activities by TAURON Group in 2017*, adopted by the Management Board and granted a positive opinion by the Supervisory Board.

The main objective of TAURON Capital Group's sponsoring activities is to support its business and communications goals in reference to *TAURON Group's 2016-2025.*

The sponsoring activity was carried out based on negotiated agreements, according to standardized provisions. Moreover, this activity was monitored, analyzed and reported on an on-going basis, through detailed reports on the implementation of sponsoring agreements, surveys and analyses conducted in quarterly and annual cycles by specialized external entities and the supervision of companies of TAURON Capital Group.

In accordance with the implemented procedures, the assessment of effectiveness of the activities conducted was carried out, through opinion surveys, measurement of the value and size of brand exposure in media, in the context of the activities conducted, measurement of implementation of sales targets, with reporting of the obtained results. As a result of the promotion effectiveness measurement, an independent research entity initially estimated the advertising equivalent in relation to activities completed in 2017. Comparing the summarized value obtained in this way to the sum of all expenditure arising from sponsoring agreements the ROI ratio at a level of approximately PLN 7.2. was obtained. It means that each zloty (PLN) spent for that purpose generated promotional benefits to TAURON Capital Group whose preliminary value is independently estimated at approximately PLN 7.2. The ongoing verification of the aforementioned value should not significantly change the value of this ratio.
The confirmation of the financial effectiveness of the activities conducted is the high positioning of TAURON brand in an independent research report, *Sponsoring Monitor 2017*, which is the only source of this type of information on the Polish market. According to this report, TAURON is ranked seventh in the TOP 10 list of sponsors and it is the most recognized (noticeable) sponsor versus its direct competitors. More than 200 brands were classified In the ranking, which is the result of opinion polls. In spite of relatively lower outlays on sponsoring versus some of its direct competitors, TAURON achieved a better result, being ranked 3 positions higher than the next group and finding itself among the very top group of the most recognized (noticeable) sponsors. Because of a relatively low level of TAURON Capital Group's sponsoring expenditures its position in this ranking can be regarded as truly very high. Taking into account an indicative value of Poland's sponsoring market according to the *Sponsoring Insight* data and the data from the above mentioned ranking it can be extrapolated that the effect achieved gives TAURON Capital Group a 9-11% market share – which in comparison to other power sector entities is a result that puts TAURON in a position of the leader of efficiency and effectiveness of the funds invested in these activities.

In 2017 sponsoring activities were carried out by TAURON and TAURON Sprzedaż. Both companies implemented 24 projects with 16 customers in total. The preliminary data related to accomplished advertising equivalents referring to activities ended in 2017 indicate that the best results were achieved by activities under projects related to professional sports, i.e. KS Vive TAURON Kielce, Lang Team (among others Tour de Pologne) and Polish Ski Association. Among projects underway such activities as sponsoring of TAURON Arena Kraków were characterized by a strong potential.

3. TAURON RISK MANAGEMENT AT TAURON CAPITAL GROUP

3.1. Risk management objective and principles

Risk at TAURON Capital Group is understood as an uncertain occurrence or a group of occurrences that, in case of materializing, will have an impact on achieving by TAURON Capital Group of its defined strategic goals, both negatively (threat), as well as positively (opportunity).

In line with its Strategy the Company is implementing the process of managing the risk related to the operations of TAURON Capital Group. The primary goals of risk management include ensuring the broadly understood security of TAURON Capital Group's operations. In particular, risk management is to ensure increased predictability of TAURON Capital Group achieving its strategic goals, including sustainable financial generation of its financial results.

TAURON Capital Group's risk management:

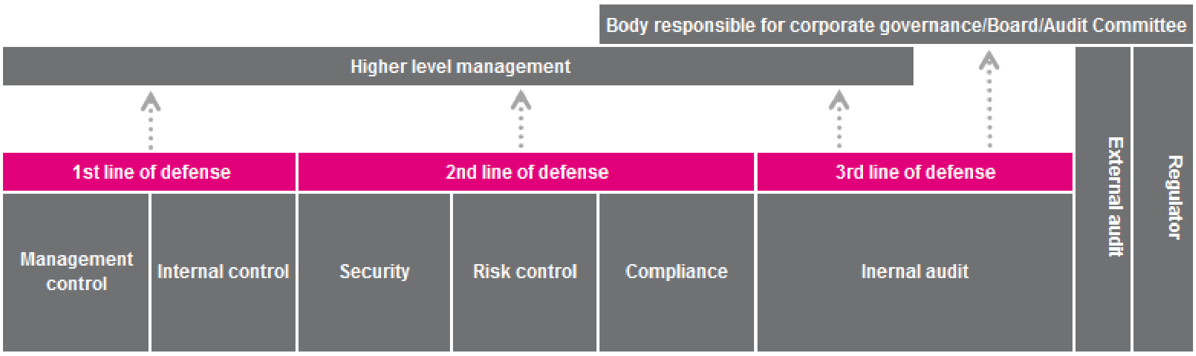
1) covers all elements of the value chain,
2) provides centralized risk measurement, monitoring and control function, and also ability to evaluate the full risk profile in the organization and coherent risk management principles,
3) ensures independence of the risk taking function from its control and monitoring,
4) ensures a clear split of competences and responsibilities, in particular by introducing the risk ownership function,
5) is an active process, focused on an appropriately early identification of threats, allowing for taking preventive measures,
6) is a systematic and continuously improved process which allows for aligning it on an ongoing basis to TAURON Capital Group's specifics and organizational structure, as well as to the changing environment,
7) places a strong emphasis on developing awareness, training and encouraging personnel to use the knowledge of risks in daily activities,
8) co-creates at TAURON Capital Group the internal audit system, constituting, along with the compliance and security management functions, an element of the three line defence.

3.2. Risk management using the "Three Defence Lines Model"

In order to ensure security of the functioning of the organization the "Three Defence Lines Model" is implemented by TAURON Capital Group, comprising internal control (audit), independent control (audit) within the second defence line and institutional control (audit). In particular, the risk management function co-creates a system of internal control (audit) at TAURON Capital Group, constituting an element of the second defence line, next to the function of ensuring the compliance and security management.

The below figure presents the "Three Defence Lines Model"

Figure no. 33. Three Defence Lines Model



Functions of the individual defence lines:

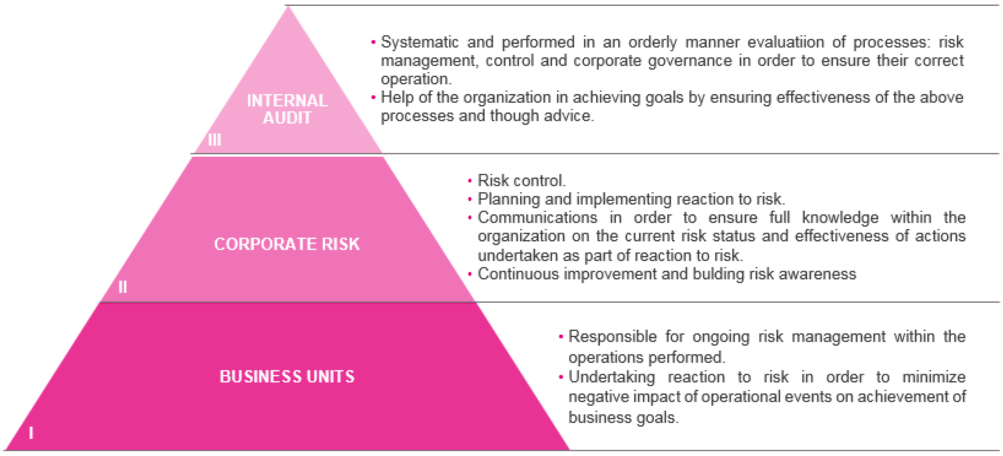
1st line of business units obliged to perform ongoing control embedded in the tasks implemented and the functional control.

2nd line of
a) function of risk management implemented in accordance with the adopted *Corporate risk management strategy at TAURON Group* and detailed policies related to main risk categories,
b) function of ensuring compliance understood as adjustment of the organization to the applicable legal regulations,
c) function of ensuring information security and technical safety.

3rd line of internal audit responsible for creating the internal control system and adequate functioning of the three defence lines model.

The below figure presents risk management as a function of the second defence line.

Figure no. 34. Risk management as a function of the second defence line

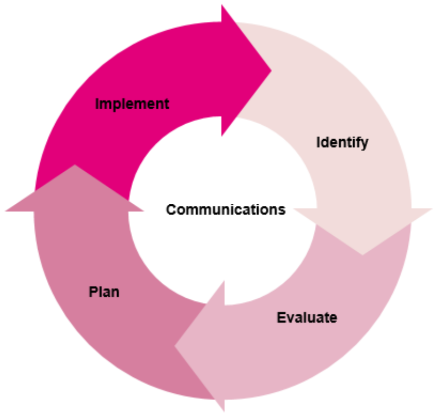


3.3. Risk management process and its participants

The process of enterprise risk management ensures the comprehensive and consistent risk management rules linked with each other in terms of methodology and information. The process of enterprise risk management means continuous measures comprising risk identification, risk assessment, planning of risk response, implementation of the adopted risk response and communication between risk management process participants.

The below figure presents the risk management process.

Figure no. 35. Risk management process



Risk identification - consisting in determining the potential events that may affect the implementation of business goals of TAURON Capital Group.

Risk assessment - consisting in determining of potential financial and non-financial effects of risk materialisation influencing the implementation of specific goals.

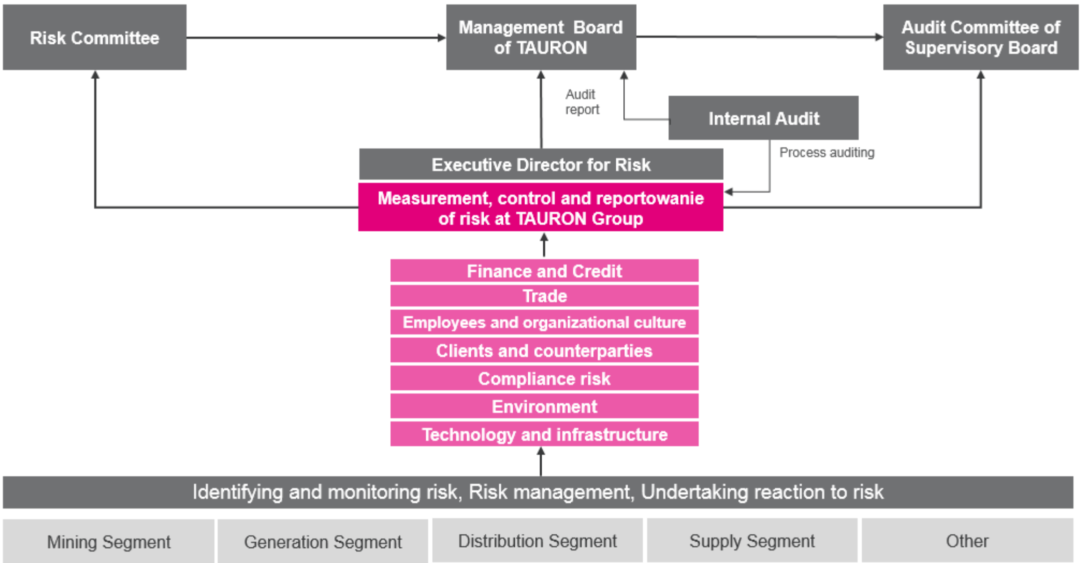
Planning - consisting in preparation of the dedicated response to the risk identified in order to achieve the desirable goals.

Implementation of risk response - consisting in practical implementation of the responses to identified risk prepared in the planning process.

Communication - consisting in continuous information flow among participants of the process which should ensure full knowledge concerning the current risk status and effectiveness of activities conducted within the response to risk. The periodical risk reporting is also an element of this process

The below figure presents the risk management process.

Figure no. 36. Diagram of the management risk communication



3.4. Architecture of the enterprise risk management system (ERM[3])

The enterprise risk management system (ERM), implemented at TAURON Capital Group's level, constitutes a set of rules, standards and tools allowing for implementing the primary goal of risk management which is, broadly understood, ensuring safety (security) of TAURON Capital Group's operations. This system is governed by the document entitled *Corporate risk management strategy at TAURON Group* that defines TAURON Capital Group's corporate risk management rules and its goal is to ensure the consistency of managing the individual risk categories that were detailed in separate regulations, aligned with the specifics of the individual threat groups.

The below figure presents the ERM system.

Figure no. 37. ERM system

[3] Enterprise Risk Managment

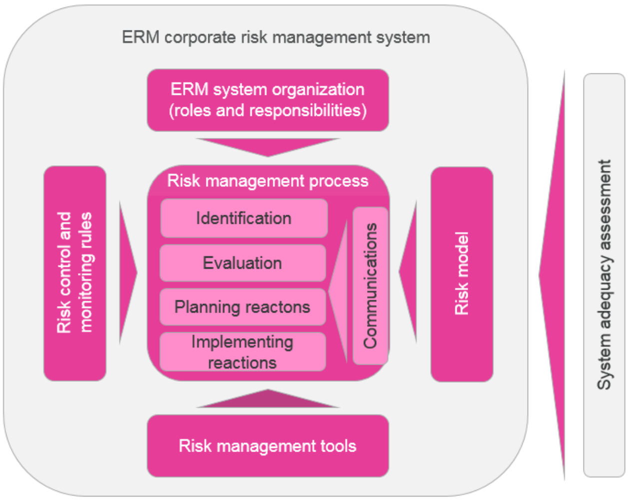
The detailed description of the rules and tools for managing the individual risk categories is provided further on in this section,

The risk management process described in detail in section 3.3 of this report is the center (core) of the system. Moreover, the architecture of the ERM system comprises elements to ensure effective functioning of the process, including:

- risk management tools,
- risk models,
- control and monitoring rules,
- organization of the ERM system

The below figure presents the architecture of the ERM system,

Figure no. 38. 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 organization**, roles and responsibilities of risk management process at TAURON Capital Group were defined. Participants of the process include, in particular: TAURON Supervisory Board, Audit Committee of TAURON Supervisory Board, Management Board of TAURON, Risk Committee, Executive Director for Risk at TAURON, Executive Director for Audit at TAURON, management boards of subsidiaries, Risk Owners, Risk Management Coordinators and Executors of risk response.

The below figure presents the organizational structure and documentation of the risk management process.

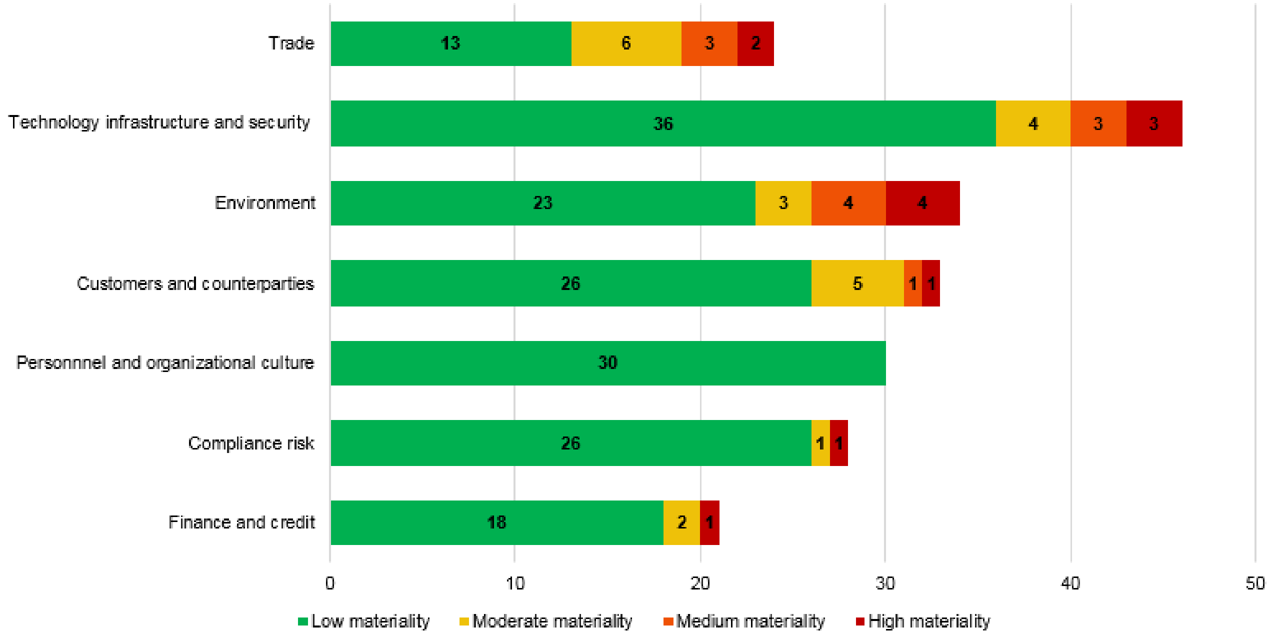
Figure no. 39. Organizational structure and documentation of the risk management process

Supervisory Board Audit Committee						
Management Board						
Management	Risk Committee Commercial (Trade) Risk Managment Team			Financial and Credit Risk Management Team		Internal Audit
Organizational by-laws	TAURON Group's corporate risk management strategy					Internal audit regulations
	TAURON Group's commercial risk (trade) management policy	TAURON Group's operational risk management policy	TAURON Group's project management risk policy	TAURON Group's credit risk management policy	TAURON Group's financial area specific risk management policy	
	Market Risk Team	Corporate Risk Team		Credit Risk Team	Executve 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 Committee					Reporting to President of Management Board

Risk model defines a consistent risk classification, enabling a consistent and comprehensive capturing of risk across TAURON Capital Group. Each risk identified is assigned to specific categories and sub-categories.

The below figure presents the main risk categories defined by TAURON Capital Group, including the number of key threats:

Figure no. 40. Number of risks monitored, broken down into categories



As part of the implementation of the **risk control and monitoring rules** the Management Board of TAURON approves risk tolerance, taking into consideration the specific nature and scope of operations of TAURON Capital Group. The level of the tolerance defines the value of the maximum permitted risk exposure at TAURON Capital Group and the rules of measurement of individual risks in the organization ensure the consistency of risk measurement with the applied tolerance definition. The risk tolerance constitutes basis for allocation of its level to the global limits dedicated to a single risk or many key risks. Subsequently global limits are allocated to operating limits within the key risk management.

A supplementary tool used for risk monitoring and control comprises the Early Warning System based on the catalogue of Key Risk Indicators - KRI and Early Warning Indicators - EWI. The system functioning based on the KRI and EWI indicators enables an appropriately early identification of threats by measuring the causes of the individual threats. At the same time this system Allows for an appropriately early ta king of remedy actions, before the individual threats actually materialize.

3.4.1. Commercial (trading) risk management

TAURON Capital Group's commercial (trading) risk management is understood as reducing unplanned volatility of its operating result, due to price fluctuations on the commodity markets and volume deviations in the individual areas of TAURON Capital Group's commercial (trading) operations. The commercial (trading) risk, due to the specifics of the operations conducted, constitutes one of TAURON Capital Group's key risks. TAURON Capital Group is made up of subsidiaries operating both in the Mining and the Generation Lines of Business as well as in the Supply Line of Business. Due to the opposing positions in these Lines of Business the risk is, to a certain degree, naturally diversified. However since these Lines of Business do not fully offset each other, and due to the diverse nature of the exposures, TAURON Capital Group is displaying sensitivity to the volatility of the prices of electricity, gas and related products.

In order to efficiently manage this group of risks the commercial (trading) risk management system was established, tied on the organizational and information level to TAURON Capital Group's process used to develop a commercial (trading) position hedging strategy. In particular *TAURON Group's commercial (trading) risk management policy* introduces an early warning system and a system used to limit risk exposure in the individual commercial areas. The basic operating measure of TAURON Capital Group's market risk is Value at Risk, defining the maximum admissible change of the position's value over the given time horizon and at a specific probability level. Value at Risk represents a dynamic risk measure which in contrast to static measures allows for determining potential negative effects before their factual occurrence. Due to the limitations of the statistical measures the commercial (trading) risk management system also uses a number of supplementary risk measures enabling a safe operation of the commercial (trading) areas.

The organizational structure of the commercial (trading) risk management system envisages a strict split of competences as part of which risk management is decentralized, where the supervision and risk control are performed centrally at

TAURON's level. In particular an element of the organizational structure of the commercial risk management system is the split of TAURON Capital Group's trading operations into: Front Office, Middle Office and Back Office. The goal of such a split of tasks is to guarantee the independence of the operating functions carried out by the Front Office from the risk control carried out by the Risk Area, and it ensures an appropriate level of operational flexibility. For the needs of of the risk management process such placement of responsibility is assumed in order to ensure an optimal approach to the given type of threat, especially taking advantage of the economy of scale and the synergy effect. Such approach ensures efficiency of the commercial processes conducted and appropriate supervision over one of the main business processes conducted by TAURON Capital Group.

The below figure presents a breakdown of TAURON Capital Group's trading operations.

Figure no. 41. Breakdown of TAURON Capital Group's trading operations

PARTICIPANT	ROLES AND RESPONSIBILITIES OF PARTICIPANTS
Front Office	• Concludes transactions on commodity and related products market, • Manages portfolio within TAURON Capital Group, • Manages operationally trade risk within risk limits set.
Middle Office	• Identifies, aggregates and measures trade risk exposure, • Ensures independent risk evauation and measurement of the result generated, • Conducts monitoring of trade operations in terms of their compliance with the adopted policy, operational procedures and market conditions, • Performs supervision over the structure of portfolios in terms of its alignment wth the trading operations.
Back Office	• Responsible for confirming, setting and invoicing trade transactions, • Responsible for archiving data related to trade transactions.

3.4.2. Financial risk management

As part of financial risk management TAURON Capital Group is managing the FX risk and interest rate risk, based on the rules and standards in line with the best practices in this respect. The main goal of managing these risks is to minimize the sensitivity of TAURON Capital Group's cash flows to the financial risk factors and to minimize the financial costs and the hedging costs as part of a transaction with the use of derivative instruments. In cases when it is possible and economically justified TAURON Capital Group uses the derivative instruments the characteristics of which allows for applying the hedging accounting.

With respect to the financial risks TAURON Capital Group also identifies and actively manages the liquidity risk understood as a potential loss or limitation of the ability to pay current expenses, due to an inadequate value or structure of liquid assets in relation to short term obligations or an insufficient level of the actual net inflows from the operations. TAURON Capital Group's liquidity position is monitored on an ongoing basis for any potential deviations from the assumed plans and the availability of external sources of financing the amount of which substantially exceeds the expected short term demand, mitigates the risk of losing liquidity. For this purpose TAURON applies specific rules of determining the liquidity position, both of the individual subsidiaries, as well of entire TAURON Capital Group, which allows for securing funds to cover a potential liquidity gap, both by allocating funds among subsidiaries (cash pool mechanism), as well as with the use of external financing, including overdrafts.

Risk associated with financing is identified at three levels:

1) Risk of failure to raise new financing, understood as a lack of possibility to acquire new funding, which would result in suspension of the investment process or the lack of possibility to re-finance the current debt,
2) Risk of cost increase understood as the growth in financing margin,
3) Risk of termination of financing in case of breach of covenants and the necessity to repay current financing.

Within the mitigation of risk associated with financing TAURON Capital Group Company conducts a policy of funding acquisition at least 24 months in advance in relation to the planned date of its use. It means that TAURON Capital Group should hold signed programs of guaranteed financing or hedge this financing through collection of funds on TAURON Capital Group's accounts. Such a policy is mainly aimed at ensuring a higher comfort in acquisition of external financing and reducing the risk of incurring new liabilities under unfavorable market conditions. At the same time, the Company diversifies financing sources by active measures with respect to the acquisition of various debt instruments, also outside the Polish market.

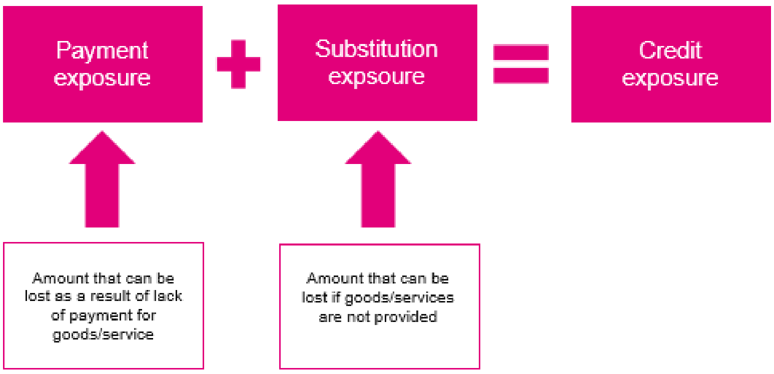
3.4.3. Credit risk management

Credit risk is understood as a possibility to incur a loss due to trade partners (counterparties) failing to fulfill their contractual obligations (default). TAURON Capital Group is using a decentralized credit risk management system, however the control, limiting and reporting of this risk category is carried out centrally, on the parent Company level. *TAURON Group's Credit Risk Management Policy* in place defines credit risk management principles on TAURON Capital Group's level, aimed at effectively minimizing the impact of this risk on achieving TAURON Capital Group's goals.

Credit risk management is carried out by controlling the credit exposure generated upon the conclusion of contracts by TAURON Capital Group's subsidiaries. The general rule is that prior to concluding a contract every entity is subjected to an examination of its financial standing and receives a credit limit which caps the maximum exposure due to the given trade. Credit exposure is, in this context, understood as an amount that may be lost if a counterparty fails to fulfill its obligations (defaults) within a certain time (taking into account the value of collaterals contributed thereby). Credit exposure is calculated as of the current day and is split into exposure due to payment (payment exposure) and replacement exposure.

The below figure presents credit exposure components.

Figure no. 42. Credit exposure components



Based on the exposure value and the evaluation of the financial standing of specific customers the credit risk value that TAURON Capital Group is exposed to is calculated using the Credit Value at Risk method. It is an analytical method that, based on the mathematical Monte Carlo simulation model, calculates the exposure value based on the total loss probability distribution.

3.4.4. Operational risk management

Operational risk is understood as a possibility to incur a loss due to inappropriate or unreliable internal procedures, human and system errors or as a consequence of external events. It also includes legal risk, reputational risk and non-compliance risk. Operational risk, due to the specific nature of the threats and the ability to manage them, constitutes a separate group of risks affecting TAURON Capital Group's operations. This risk is a complex issue, occurs in every process and type of operations, it is multi-dimensional and applies to various types of activities and operations. In particular, the exposure to the operational risk factors is related to the size and complexity of the organizational structure, the number and complexity of IT systems and to the number of business processes conducted. The operational risk is characterized by the lack of the ability to totally eliminate its sources, and the analysis of its factors and parameters (among others, frequency and severity), and also the evaluation thereof requires the use of complex measurement and analysis methods.

In order to effectively manage the operational risk TAURON Capital Group is using appropriate tools, presented on the below diagram. In particular, they include the operational risk profile, operational events database, global operational risk limit and the related system of operational limits and also the early warning system operating on a large scale.

The below figure presents risk management system tools.

Figure no. 43. Risk management system tools

Global operational risk limit is the basic tool for the operational risk control and represents the allocation of risk tolerance adopted by TAURON Capital Group. The global operational risk limit can be subsequently allocated to TAURON Capital Group's individual lines of business, the operational risk sub-categories as well as to the specific operational risks.

Operational risk profile is aimed at identifying areas, processes or activities with an excessive exposure to threats stemming from specific operational risk factors. Operational risk profile is expressed in particular in the structural dimension that includes types of operational events, TAURON Capital Group's organizational structure and processes, in the scale dimension that includes estimated potential losses, taking into account especially historical values of actual losses, as well as the tools used to mitigate the threats. For the needs of measuring the operational risk and defining the operational risk Profile the individual types of the operational risk are broken down (due to the nature of the occurrence thereof) into continuous and one-off risks.

Early warning system is defined in order to monitor the operational risk level for each identified threat. Early Warning Indicators (EWI) are selected from the Key Risk Indicators (KRI) set as the ones that are subject to continuous control with respect to the caution thresholds set for them, i.e. acceptance, mitigation and escalation thresholds.

Operational events database is created for the needs of identifying new risk factors, and in parallel in order to define the risk profile for TAURON Capital Group. It allows for keeping the records of cases that are characterized by a potential or actual loss for the organization. The goal of maintaining the operational events database is to determine the frequency and severity of the individual operational risk factors, as well as the areas and processes they occur in.

Risk identification questionnaire is a document in the form of a table form that constitutes a tool supporting the performance of the risk management process with respect to risk identification, specifying the detailed information that should be collected in this process.

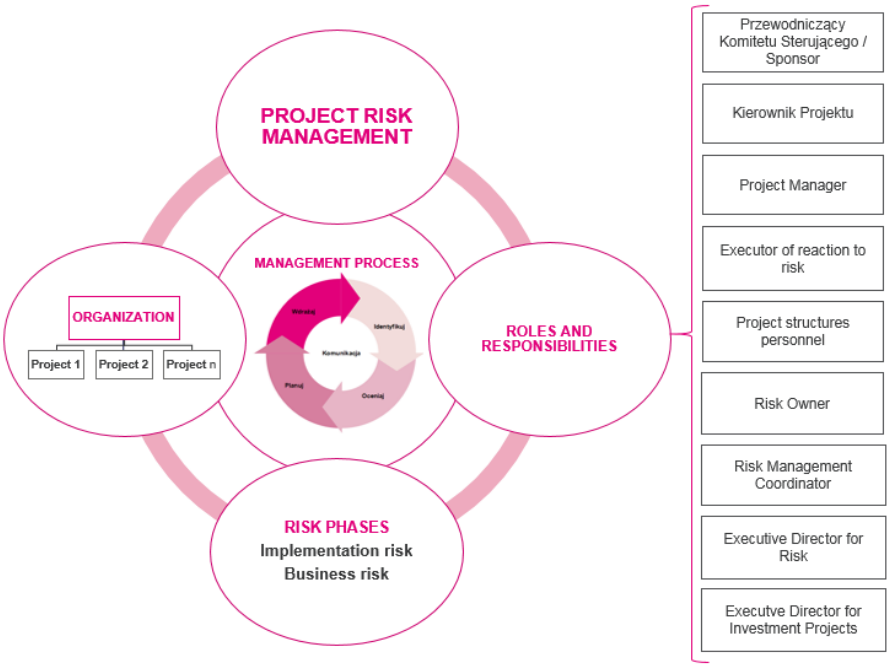
3.4.5. Project risk management

TAURON Capital Group is conducting a number of investment projects in many lines of its business operations. These projects, due to their scale and often very complicated nature of implementation, represent a source of threats that may have an impact on the schedule, budget or quality of the final products. Systematic use of the provisions of *TAURON Group's Project Risk Management Policy* is aimed at mitigating these risks, supporting at the same time the accomplishment of the organization's strategic goals. This regulation, in particular, defines the basic principles of project risk management, ensuring coherence, comprehensive approach and unequivocal understanding in this area. The goal of the actions taken is to achieve the required probability of the project's completion while complying with the defined schedule, budget and quality of the products received. The overall objective is to obtain the expected benefits from the project's completion and to achieve TAURON Capital Group's strategic goals.

Project risk management is also applicable to managing the risk stemming from the projects and having an impact on the organization. The process of managing the risk stemming from the projects includes identification, valuation of such risks, defining and monitoring early warning indicators as well as planning and implementing actions related to managing such risks. In case of risks having an impact on the organization the risk valuation is made as the absolute value of the impact including indicating the impact period broken down into individual accounting periods, in reference to the assumed EBITDA or the assumptions made in the organization for the long term projections. In case of the most important risks having an impact on the organization the Plans of reactions to the risk and back-up Plans are developed. The evaluation of project risks and risks stemming from the projects for the organization is taken into account when making the key decisions related to launching and implementing such projects.

The below figure presents the project risk management model

Figure no. 44. Project risk management model



3.5. Description of the most significant risks related to TAURON Capital Group's operations

The below table presents the most significant risks identified for TAURON Capital Group.

Table no. 9. Most significant risks identified for TAURON Capital Group

#	Risk name	Risk description	Risk trend	Risk response
Finance and credit				
1.	Interest rate and FX rate risk	Risk related to an unfavorable impact of interest rates and FX rates on TAURON Capital Group's financial results.	→	• Ongoing monitoring of risk exposure in order to minimize negative impact of changes to the market factors, • Transfer of risk through the use of derivative instruments
2.	Liquidity / financing risk	Risk related to the manner of financing operations, due to the enterprise's capital structure.	→	• Diversification of the sources of financing including arranging guaranteed financing programs and securing alternative sources of financing. • Implementing the central financing policy. • Analyzing the market and the availability of the sources of financing. • Monitoring the schedules and the date of announcing the financing program.
3.	Credit risk	Risk related to a potential occurrence of overdue accounts payable or a conclusion of a contract with a counterparty that will turn out to be insolvent.	→	• Regular monitoring of the counterparties' financial standing. • Periodic customer scoring, credit rating of each customer prior to submitting an offer/concluding a contract. • Use of protection mechanisms (hedging) in commercial agreements
Trade				
4.	Market risk	Risk related to an unfavorable change of prices on the electricity market and on the related products markets, having a negative impact on TAURON Capital Group's financial results.	↗	• Monitoring and updating the hedging strategy. • Ongoing monitoring of exposure to the above mentioned risk in order to minimize negative impact of changes to the market factors. • Limits (caps) on trade positions within risk mandates.
Workforce and organizational culture				
5.	Social dispute risk	Risk related to collective disputes, strikes, social conflicts being the	→	• Conducting social consultations with respact to the planned changes.

#	Risk name	Risk description	Risk trend	Risk response
		consequence of a lack of the personnel's satisfaction with the economic and social situation.		• Conducting a policy of dialogue with the workforce. • Preparing and implementing motivational solutions for the personnel. • Standardizing the tasks and requirements towards the personnel. • Developing organizational culture based on values. • Conducting active internal communications on personnel matters.
6.	Human resources risk	Risk related to the temporary or permanent loss of specialized staff and difficulties in its restoration.	↘	• Taking measures aimed at developing a model that would enhance workforce motivation • Developing competences by training the personnel.
7.	Occupational Health and Safety Risk	Risk related to accidents at work resulting from non-compliance with the Occupational Health and Safety as well as Fire Protection regulations	→	• Implementing manuals and rules defining safe organization of work. • Stimulating workforce development by conducting periodic Occupational Health and Safety and additional specialist training. • Analyzing and updating, based on needs, the evaluation of the professional risk at individual work stations (positions). • Maintaining a high standard of equipping the personnel with protection means and enforcing the appropriate use thereof. • Performing measurements of harmful factors in the work environment.
Customers and contractors				
8.	Customer service risk	Risk related to non-compliance with the customer service standards.	→	• Monitoring and analyzing external customer satisfaction indicators and indicators related to complaints • Taking additional measures, e.g. with respect to internal regulations, defining standards of conduct as a result of the analysis of indicators. • Developing key account managers' competences and skills. • Continued raising of customer service standards.
9.	Risk related to performance of agreements by subcontractors	Risk related to improper performance by subcontractors of the works commissioned, termination of the agreement and delays, changes to the budget, scope related thereto	↘	• Concluding agreements with subcontractors in accordance with TAURON Capital Group's standards. • Analyzing the performance of the subject of the agreement, examining the quality of services provided by subcontractors. • Evaluating the financial standing and credibility of the subcontractors.
10.	Purchasing process risk	Risk related to the volatility of the situation on the supplies/services market, volatility of demand for the given type of product/supply/service on the market, decline of the availability of supplies/services of appropriate quality, leading to the purchase order value increase risk.	→	• Preparing a plan of purchase orders and updating thereof. • Aggregating purchases of selected product groups. • Consolidating purchase orders. • Concluding long term agreements. • Taking into account the price risk related to commodity prices/FX rate fluctuations in contracts with contractors
11.	Volume and margin risk	Unfavorable changes or terminations of commercial agreements by customers, leading to the declining revenue from operations; loss and lack of acquiring new customers.	↗	• Conducting marketing campaigns, acquiring new customers. • Taking actions focused on retaining the existing customers and recovering the lost ones. • Ongoing updating of the offering, launching sales of multi-package type products.
Compliance risk				
12.	Internal fraud risk	Appropriation or temporary use of the company's assets, destruction of TAURON Capital Group's property, abuse of work position to derive various types of personal gain by forcing specific behavior of customers while performing work related activities.	↘	• Strict adherence to internal procedures aimed at achieving protection against abuse (security procedures, reviews of authorizations). • Conducting compliance type activities. • Promoting best practices, improving procedures, training. • Enforcing and promoting the provisions of *TAURON Group's Code of Responsible Business* in force.
13.	External fraud risk	Third party actions aimed at, among others, theft, robbery, physical burglary, computer hacking, information theft, forgery..	↘	• Monitoring potential and actual security incidents. • Anti-virus protection of workstations. • Physical protection of facilities. • Conducting security tests.
14.	Risk of unethical behaviors	Risk related to the occurrence of behaviors not in line with the generally accepted by the society	↘	• Functioning of the whistleblowing system in the organization. • Lack of organizational culture based on TAURON Capital Group's values and principles.

#	Risk name	Risk description	Risk trend	Risk response
		social coexistence rules, moral standards and lobbing.		• Training, building awareness through meetings, TAURONET, press materials. • Functioning of Ethics Committees in the organization operating based on the adopted regulations.
15.	Legal risk	Risk related to non-compliance with the legal regulations, misinterpretation of the new provisions and regulations, court disputes (litigations), requirements imposed by URE/UOKiK/KNF/GIODO, etc.	→	• Continuous monitoring of the legal environment and changes to the legal regulations. • Implementing the required changes to internal regulations. • Appointing working groups tasked with preparing and implementing the required changes stemming from the legal environment. • Continuous cooperation with the authorities overseeing the energy market and the capital market. • Training for the personnel on the changes being introduced.
16.	Risk of breaching contractual provisions (default)	Risk related to the possibility of being in default in performing the obligations under agreements concluded with counterparties.	→	• Optimizing the sales and service processes. • Updating and adapting agreement samples to the changes to the law. • Monitoring complaints and proceedings of URE/UOKiK.
Environment				
17.	Reputational risk	Current and future impact on the company's revenue and capital due to the negative public opinion backlash.	→	• Continuous monitoring of the Company's external and internal threats. • Media monitoring, developing contacts and relationships with the media within TAURON Capital Group. • Preparing procedures for the Company's communications with the external and internal environment (stakeholders).
18.	Regulatory risk	Unfavorable impact of the domestic and European level legislation due to the need to pass or adapt to the legal regulations and to incur the required financial costs in order to comply therewith.	↗	• Continuous monitoring of the legal environment and changes to the regulations. • Analyzing draft legal acts and planning the required adaptation steps. • Implementing the required changes into internal regulations. • Cooperation with the regulator.
19.	License risk	No ability to conduct operations as a result of a prolonged process of obtaining a license or amending the licenses held. Unfavorable legal changes with respect to licensed operations.	→	• Ongoing control of the correct performance of licensing obligations. • Monitoring changes to the legal acts with respect to licensing obligations. • Legal support for the license extension and obtaining process
Technology and infrastructure				
20.	Environmental risk	Potential negative impact of the operations on the environment and of non-alignment to and non-compliance with the environmental requirements of the domestic and community law.	→	• Ongoing supervision over compliance with the conditions of the environmental decisions. • Maintaining the required efficiency of the devices reducing the emission of pollutants. • Frequent evaluation of the compliance of actions with the legal requirements with respect to environment protection. • Implementing investment projects in environment protection in order to minimize the adverse impact of the mining and processing operations conducted.
21.	Weather risk	Impact of weather conditions on the operations of the enterprise, both with respect to technological aspects as well as the commercial ones.	→	• Upgrading (refurbishing) hydroelectric structures aimed at optimizing the utilization of water resources. • Preparing plans of overhauls, inspections and maintenance activities with flexible provisions on deadlines for completing the works. • Continuous monitoring of wind conditions and icing on the wind farms' blades. • Continuous technical oversight over the operation of individual wind farms, conducted by the companies operating the farms. • Monitoring and analyzing new technological solutions that reduce the impact of adverse weather conditions on the volume of electricity generated. • Increase in acquisitions and takeovers.
22.	Company asset failure risk	Impact of failures of machines and devices, overhauls, upgrades (refurbishments), maintenance and management of production and non-production assets on achieving the company's goals.	→	• Optimizing capital expenditures on asset replacements, ongoing monitoring of the condition of machines, devices and installations. • Raising professional qualifications and work culture of the personnel by organizing courses and training.

#	Risk name	Risk description	Risk trend	Risk response
				• Responding to an emergency situation by the technical personnel and automatic process safety interlocks. • Insuring assets against fortuitous events (excluding underground assets). • Introducing IT tools with respect to improving the monitoring and managing failure indicators (ratios).
23.	IT risk	Risks related to the IT infrastructure security, failures of the IT infrastructure	↗	• Developing and maintaining plans aimed at ensuring continuity of IT infrastructure's operation. • Periodic identifying and categorizing IT resources based on the service restoration targets. • Use of IT solutions with appropriate technical parameters, providing an acceptable level of reliability and efficiency of operation (including also UPS devices, GSM modem, mobile phones). • Planning and conducting training on IT continuity. • Storing and protecting the back-up data.
24.	Asset security and protection risk	Risk related to compromising the integrity of machines/devices and to the security of information, including its improper processing and unauthorized disclosure.	↘	• Monitoring the implementation of the developed plans to protect the facilities that are subject to mandatory protection. • Maintaining and updating contingency procedures/plans. • Implementing/updating and oversight over compliance with the information security rules in force. • Regular personnel training with respect to security procedures in force.
25.	Geological risk	Impact of geological factors on the mining operations.	↗	• Making test drillings for the better intelligence on the positioning of coal deposits. • Continuing to take preventive measures in areas under threat in order to improve the geological and mining conditions and to provide protection against natural threats (including, among others, long-drilled blasting hole shooting in order to break the rock mass)

4. ANALYSIS OF TAURON POLSKA ENERGIA S.A.'S FINANCIAL POSITION AND ASSETS

4.1. Overview of economic and financial data disclosed in the consolidated annual financial statements

Statement of comprehensive income

The below table presents the annual standalone statement of comprehensive income. .

Table no. 10. Annual standalone statement of comprehensive income in 2017 - 2015

Statement of comprehensive income prepared in accordance with the IFRS (PLN thousand)	2017	2016	2015	Change in % (2017/2016)
Continued operations				
Sales revenue	**7 792 025**	7 995 328	9 062 246	**97%**
Own cost of goods, materials and services sold	(7 414 707)	(7 837 567)	(9 073 869)	95%
Gross profit (loss) from sales	**377 318**	157 761	(11 623)	**239%**
Cost of sales	(23 309)	(19 326)	(21 372)	121%
Overheads	(88 751)	(81 368)	(96 341)	109%
Other operating revenues and costs	(2 470)	(91 670)	4 969	3%
Operating profit (loss)	**262 788**	(34 603)	(124 367)	**-**
Operating profit margin (%)	*3,4%*	*(0,4)%*	*(1,4)%*	-
Revenue from dividend	560 832	1 485 152	1 510 624	38%
Interest revenue from bonds and loans	456 426	503 897	449 437	91%
Interest costs on debt	(334 638)	(356 947)	(357 055)	94%
Revaluation write-offs of stocks and shares	(134 372)	(1 610 396)	(4 931 147)	8%
Other financial revenues and costs	108 529	(136 237)	1 714	-
Gross profit (loss)	**919 565**	(149 134)	(3 450 794)	**-**
Gross profit margin (%)	*11,8%*	*(1,9)%*	*(38,1)%*	-
Income Tax	(65 214)	(17 119)	3 114	381%
Net profit (loss) from continuing operations	**854 351**	(166 253)	(3 453 908)	**-**
Net profit margin (%)	11,0%	(2,1)%	(38,1)%	-
Other total income	**(6 713)**	104 024	69 720	**-**
Total income	**847 638**	(62 229)	(3 384 188)	**-**
EBITDA	**268 220**	(27 078)	(115 856)	**-**
EBITDA margin (%)	***3,4%***	*(0,3)%*	*(1,3)%*	-

In 2017 the Company posted operating profit of PLN 263 mln, among others due to dissolving, in full, of the provisions, set up in 2015 and updated in 2016, stemming from the agreements involving charges related to the joint venture. Dissolving of the above provisions is related to the fulfillment of the suspending conditions under the conditional agreement signed on October 27, 2016 on establishing the basic boundary conditions of the restructuring of the "Construction of the CCGT unit in Stalowa Wola" project. The suspending conditions were fulfilled by making by EC Stalowa Wola, on March 31, 2017 of the payment of all accounts payable due to all the existing financing institutions, i.e. European Investment Bank, European Bank for Reconstruction and Development, Polska Kasa Opieki S.A.

Better 2017 earnings are also a consequence of TAURON achieving positive margins, first of all on trading in electricity, coal and CO_2 emission allowances.

In 2017, similar to 2016, impairment write-offs for the value of stocks and shares in subsidiaries were recognized in the financial results, due to the completed impairment tests related to stocks and shares in subsidiaries as well as bonds and loans as of December 31, 2017 and as of June 30, 2017.

Revenue

The below table presents the Company's sales revenue in 2017 - 2015.

Table no. 11. Company's sales revenue

Item (PLN thous.)	2017	2016	2015	Change in % (2017/2016
Sales Total	**8 963 044**	**10 011 343**	**11 053 252**	**90%**
Sales revenue	**7 792 025**	**7 995 328**	**9 062 246**	**97%**
Revenue from sales of goods and materials:	**7 664 715**	**7 899 621**	**8 963 672**	**97%**
Electricity (without excluding excise tax)	7 117 988	**7 255 819**	8 558 477	98%
Greenouse gas emission allowances	336 566	363 500	94 031	93%
Gas	190 507	236 215	119 774	81%
Property rights related to origin of electricity	14 939	36 137	186 358	41%
Other	4 715	7 950	5 032	59%
Revenue from sales of services	**127 310**	**95 707**	**98 574**	**133%**
Sales of commercial (trading) services	52 711	54 517	56 703	97%
Other	74 599	41 190	41 871	181%
Revenue form other operations	**1 427**	**1 041**	**7 103**	**137%**
Revenue from financial operations	**1 169 592**	**2 014 974**	**1 983 903**	**58%**
Revenue from dividend	560 832	1 485 152	1 510 624	38%
Revenue from bonds and loans interest	456 426	503 897	449 437	91%
Other financial revenue	152 334	25 925	23 842	588%

Revenue from sales of goods and materials represents 86% of the total revenue, while financial revenue represents 13%, which is a consequence of the implemented Business Model and centralizing of functions by TAURON.

The goal of the adopted solution is to hedge the buy and sell positions of TAURON Capital Group's entities, to perform the function of the Market Operator and entity responsible for the commercial (trading) balances of TAURON Capital Group's subsidiaries and to optimally manage, among others, the property rights and the CO_2 emission allowances.

A relatively large share of revenue from bonds and loans interest is a consequence of the implemented central financing model and the *Policy for managing TAURON Group's liquidity* including the cash pooling functioning at TAURON Capital Group, which allows for efficient management of the finances of all of TAURON Capital Group's subsidiaries.

The lower revenue from the sales of goods and materials achieved in the reporting period was impacted by the lower revenue from the sales of:

1. electricity, as a result of lower electricity sales prices (3.3%) versus 2016, as a result of, among others, reduced liquidity of the forward products,
2. natural gas, due to reduced sales volume,
3. property rights related to the origin of electricity due to realizing, in the previous years, of the transactions aimed at securing the positions of TAURON Capital Group's subsidiaries,
4. greenhouse gas emission allowances (sales to TAURON Capital Group's subsidiaries for the purpose of redeeming the allowances in conjunction with the fulfillment of the obligation due to greenhouse gas emissions as well as sales as part of the trading operations).

Under the revenue from sales of services TAURON recognizes revenue from:

1. intermediary services related to coal purchase transactions on the marker for TAURON Capital Group's subsidiaries (+3% versus 2016),
2. commercial (trade) balancing services (+3% versus 2016),
3. provision of the OH/OHT services (+4% versus 2016),
4. management of property rights and CO_2 emission allowances (-41% versus 2016).

Due to its holding operations the Company is reporting material financial revenue. Its decline is mainly a consequence of lower revenue from dividends by 62% and lower bonds and loans interest by 9%. The increase of the other financial revenue is a result of a surplus of positive FX differences over the negative ones in the amount of PLN 127.5 mln. The positive FX differences were to a large extent due to the FX differences related to the Company's obligations under its EUR debt, i.e. the loans received from the subsidiary, the subordinate bonds issued in December 2016 and the euro bonds issued in July 2017. The surplus of positive FX differences over the negative ones resulting from that reached PLN 128.3 mln.

The Company's operations are primarily conducted on the territory of Poland. Sales to foreign customers in the years ended on December 31, 2017 and December 31, 2016 reached, respectively, PLN 170.0 mln and PLN 190,8 mln zł.

Costs

The below table presents the level and structure of the costs incurred by the Company in 2017 – 2015.

Table no. 12. Level and structure of the costs

Item (PLN thous.)	2017	2016	2015	Change in % (2017/2016)
Total costs	**(8 043 479)**	**(10 160 477)**	**(14 504 046)**	**79%**
Cost of goods, materials and services sold	(7 414 707)	(7 837 567)	(9 073 869)	95%
Costs of sales and overheads	(112 060)	(100 694)	(117 713)	111%
Costs of other operations	(3 897)	(92 711)	(2 134)	4%
Costs of financial operations	(512 815)	(2 129 505)	(5 310 330)	24%

In 2017 the total costs of the Company's operations represented 79% of the level of costs in 2016, mainly as a result of recognizing, in the financial costs in 2017, of the consequences of setting up and reversing the impairment write-offs for the value of stocks and shares in subsidiaries in the amount much lower than the amount recognized in 2016. The costs of goods, materials and services sold constitute the largest share of the total cost (92%).

Cost of goods, materials and services sold in 2017 is lower by 5% as compared to 2016, which was mostly due to lower costs of electricity purchase arising from the lower electricity purchase price.

In relation to 2016, the costs of sales and overheads were higher in 2017 by approximately 11%. The rise was mainly related to the costs of compensation (due to increased headcount), stock market services and rent which is associated with centralizing of functions by TAURON in accordance with the implemented Business Model.

Costs of other operations include mainly premiums paid to external organizations and donations, and the decrease of the costs by 96% is due to setting up, in 2016, of a provision related to tax risks in conjunction with an audit (inspection) proceeding underway and recognizing the liability arising as a result of the Company having declared its contribution to the founding fund of the Polish National Foundation (Polska Fundacja Narodowa).

The financial costs include the results of revaluation of stocks and shares associated with the completion of impairment tests and reversal of write-offs on the value of stocks and shares in subsidiaries and loans granted to the subsidiaries:

1) Result of the impairment tests conducted as of June 30, 2017, in accordance with *IAS 36 Impairment of assets*, indicated an impairment of the carrying amount of the loan granted to a subsidiary in the amount of PLN 60.6 mln and a reversal of write-offs on the value of shares in a subsidiary in the amount of PLN 120.0 mln.
2) Result of the impairment tests conducted as of December 31, 2017, in accordance with *IAS 36 Impairment of assets*, indicated an impairment of the carrying amount of stocks and shares in subsidiaries in the amount of PLN 211.4 mln and a reversal of write-offs on the value of shares in a subsidiary in the amount of PLN 72.6 mln.

Furthermore, under financial costs in the item related to revaluation of shares, stocks and loans the write-off on the value of shares in the PEPKH subsidiary in the amount of PLN 55.06 mln, booked in the year ended on December 31, 2017, was recognized.

Lower financial costs are primarily the result of recognizing, in 2017, the write-offs on the value of stocks and shares in the amount much lower (by 90%) than in 2016, and also recognizing, in 2016, of the negative result on the sale of the shares in Nowe Brzeszcze Grupa TAURON sp. z o.o. subsidiary, booking a write-off revaluating the loan granted to a subsidiary and negative FX differences, which did not occur in the current reporting period.

The Company's assets and financial position

The below table presents the Company's annual standalone statement of financial position.

Table no. 13. Annual standalone statement of financial position (material items)

Statement of financial standing prepared in accordance with the IFRS (PLN thousand)	As of December 31, 2017	As of December 31, 2016	As of December 31, 2015	Change in % (2017/2016)
ASSETS				
Fixed assets	**27 371 425**	**25 855 329**	**24 866 370**	106%
Stocks and shares	20 912 679	14 874 418	15 933 194	141%
Bonds	6 009 920	9 615 917	7 451 601	62%
Loans granted	382 989	1 292 800	1 417 165	30%
Current assets	**2 901 667**	**1 817 047**	**1 607 786**	160%
Inventory	198 428	284 799	249 492	70%
Trade receivables and other receivables	755 227	961 242	623 209	79%
Bonds	562 776	242 465	215 040	232%
Cash and equivalents	721 577	198 090	168 255	364%
TOTAL ASSETS	**30 273 092**	**27 672 376**	**26 474 156**	**109%**
LIABILITIES				
Equity	**17 377 906**	**16 530 268**	**16 592 497**	105%
Long-term liabilities	**9 530 528**	**8 969 976**	**5 069 118**	106%
Liabilities due to debt	9 472 454	8 754 047	4 876 546	108%
Short-term liabilities	**3 364 658**	**2 172 132**	**4 812 541**	155%
Liabilities due to debt	2 725 763	1 433 929	4 057 048	190%
Liabilities towards suppliers and other liabilities	475 855	585 396	517 220	81%
Derivatives	9 226	560	96 942	1 648%
TOTAL LIABILITIES	**30 273 092**	**27 672 376**	**26 474 156**	**109%**

As of December 31, 2017 fixed assets represented the biggest share of the total assets (90%), where the dominating item is the value of stocks and shares (69% of the total assets) and bonds (20% of the total assets).

The following events had the biggest impact on an increase of the value of stocks and shares by 41% year on year:

1) increase of the share capital of TAURON Wydobycie in the amount of PLN 160 mln,
2) transfer of the shares from TAURON Wytwarzanie to Nowe Jaworzno GT in the amount of PLN 151 mln,
3) increase of the share capital of TAURON Ciepło in the amount of PLN 600 mln,
4) increase of the share capital of Nowe Jaworzno GT in the amount of PLN 3 400 mln,
5) transfer of the shares in TAURON Dystrybucja Serwis from TAURON Dystrybucja to the Company in the amount of PLN 201 mln,
6) increase of the share capital of TAURON EKOENERGIA in the amount of PLN 1 000 mln,
7) increase of the share capital of TAURON Magenta Grupa TAURON in the amount of PLN 9 mln,
8) increase of the share capital of TAURON Dystrybucja in the amount of PLN 1 000 mln.

Additional factors that led to a change of this balance sheet item were impairment write-offs on the value of stocks and shares booked, updated or dissolved as a result of impairment tests conducted due to the loss of value of stocks and shares of subsidiaries. The impairment tests completed proved the need for booking or increasing the already booked write-offs in the following subsidiaries:

- TAURON Wydobycie in the amount of PLN 147.9 mln,
- TAURON Wytwarzanie in the amount of PLN 63.5 mln,

and also dissolving of the write-offs on the value of stocks and shares in:

- TAURON Wytwarzanie in the amount of PLN 120.0 mln,
- TAURON EKOENERGIA in the amount of PLN 72.6 mln.

Furthermore, due to the repayment of the loan by TAURON EKOENERGIA and taking up of shares in this subsidiary, the impairment write-off related to the loan in the amount of PLN 258.5 mln was reclassified (converted) as the value of shares in TAURON EKOENERGIA. At the same time, an impairment write-off on the value of shares in the PEPKH subsidiary in the amount of PLN 55.06 mln was booked in the year ended on December 31, 2017.

Under the *Bonds* item the value of bonds issued by the subsidiaries and purchased by TAURON is provided. A year on year decline is the result of redeeming of the bonds issued in previous years by the subsidiaries.

As of December 31, 2017 and December 31, 2016, equity represented, respectively, 57% and 60% of total liabilities.

The liabilities of the Company due to loans and credits received and due to bonds, as of December 31, 2017, were related to bonds issued under the bond issue program worth PLN 7 940.3 million, loans from related entities drawn under the *Agreement on cash pool services,* in the amount of PLN 2 377.0 million, loans received from the European Investment Bank (EIB) in the amount of PLN 1 042.1 million (including interest), the loan from a subsidiary in the amount of PLN 721,3 mln, financial lease in the amount of PLN 23.9 mln and an overdraft in the amount of PLN 93.5 million drawn in order to finance security deposits (margins) for the commodity product transactions and pollution emission allowances transactions.

Statement of cash flows

The table below presents the statement of cash flows prepared according to the IFRS.

Table no. 14. Statement of cash flows (material items)

Statement of Cash Flows prepared in accordance with the IFRS (PLN thousand)	2017	2016	2015	Change in % (2017/2016)
Cash flows from operating activities				
Gross profit (loss)	919 565	(149 134)	(3 450 794)	-
Adjustments	(673 538)	(83 753)	3 608 403	-
Net cash from operating activities	**246 027**	**(232 887)**	**157 609**	**-**
Cash flows from investing activities				
Purchase of stocks and shares	(6 169 590)	(543 603)	(53 377)	-
Purchase of bonds	(350 000)	(2 770 000)	(4 155 000)	-
Redemption of bonds	3 547 110	540 000	2 267 266	657%
Repayment of loans grantem	1 000 000	142 024	14 500	704%
Loans grantem	(307 132)	(23 575)	(168 124)	-
Dividends received	359 787	1 485 152	1 510 624	24%
Interest received	642 017	474 126	267 464	135%
Net cash from investing activities	**(1 353 288)**	**(619 543)**	**(318 640)**	**-**
Cash flows from financing activities				
Issue of debt securities	2 707 462	4 284 607	310 000	63%
Redemption of debt securities	(1 650 000)	(3 300 000)	(450 000)	-
Credits/ loans drawn	0	0	322 358	-
Credits/ loans repayment	(175 695)	(132 818)	(132 818)	-
Dividends paid	0	0	(262 882)	-
Interest paid	(265 223)	(351 147)	(344 332)	-
Net cash from financing activities	**593 470**	**486 164**	**(587 079)**	122%
Increase/(decrease) in net cash and equivalents	**(513 791)**	**(366 266)**	**(748 110)**	**-**

Statement of Cash Flows prepared in accordance with the IFRS (PLN thousand)	2017	2016	2015	Change in % (2017/2016)
Net FX exchange differences	2 038	1 179	1 147	173%
Cash opening balance	**(1 045 441)**	**(679 175)**	**68 935**	**-**
Cash closing balance	**(1 559 232)**	**(1 045 441)**	**(679 175)**	**-**

The balance of cash received from operating, investing and financing activities of the Company for 2017, taking into account the opening cash balance, was PLN (1 559.2) million. The closing cash balance results from the adjustment of cash by the balance of loans granted and received under cash pooling transactions, due to the fact that they do not constitute cash flows from investing or financing activities, as they are used mainly for current liquidity management.

4.2. Differences between the financial results reported in the annual report and the forecasts of results for the given year published earlier

The Management Board of the Company did not publish any forecasts of the earnings of TAURON for 2017. This decision was due to the considerable volatility of the market and a substantial number of factors affecting its predictability.

4.3. Key financial and non-financial ratios

Financial ratios

The below table presents key financial ratios of TAURON.

Table no. 15. Key financial ratios of TAURON

No.	Item	2017	2016	2015	Change in % (2017/2016)
1.	**Gross Profitability** (gross profit / sales revenue)	11,8%	(1,9)%	(38,1)%	-
2.	**Net Profitability** (net profit / sales revenue)	11,0%	(2,1)%	(38,1)%	-
3.	**Return on equity** (gross profit / equity)	5,3%	(0,9)%	(20,8)%	-
4.	**Return on assets** (net profit / total assets)	2,8%	(0,6)%	(13,0)%	-
5.	**EBIT (PLN thou.)** (operating profit)	262 786	(34 603)	(124 367)	-
6.	**EBIT Margin** (EBIT / sales revenue)	3,4%	(0,4)%	(1,4)%	-
7.	**EBITDA (PLN thou.)** (operating profit before depreciation)	268 218	(27 078)	(115 856)	-
8.	**EBITDA Margin** (EBITDA / sales revenue)	3,4%	(0,3)%	(1,3)%	-
9.	**Current liquidity ratio** (current assets / short-term liabilities)	0,86	0,84	0,33	103%

The Company's 2017 EBIT was primarily affected by the dissolving of the provision related to the agreements involving charges stemming from EC Stalowa Wola joint venture in the amount of PLN 203.4 mln.

In 2016 the negative value of EBIT was a consequence of recognizing the liability arising as a result of the Company having declared its contribution to the founding fund of the Polish National Foundation (Polska Fundacja Narodowa) and setting up a provision related to tax risk in conjunction with an audit (inspection) proceeding underway.

The 2017 gross and net profits were impacted by the booked and reversed write-offs on the value of stocks and shares in subsidiaries and the value of loans granted for the total amount of PLN 134 million. On the other hand, negative values of the 2016 gross and net profit were primarily due to booking and dissolving write-offs on the value of stocks and shares in subsidiaries in the amount of PLN 1 412,4 mln and recognizing the result on the sale of shares in Nowe Brzeszcze GT in the amount of PLN 88.3 mln.

The operating profit's level is typical for a company conducting operations involving managing a holding entity (costs related to managing TAURON Capital Group are included in operating activities while revenues gained from dividends are recognized under financial activities).

The Company's ability to pay its accounts payable was not in jeopardy in 2017.

Non-financial ratios (indicators)

The non-financial ratios (indicators) in TAURON Capital Group are closely associated with the specific nature of its operations, its resources and the adopted Strategy, including:

1) assessment of investment opportunities,
2) methods of human resources management,
3) risk optimization,
4) customer satisfaction surveys (polls),
5) centralizing of governance (management) functions at TAURON Capital Group, limiting the non-core operations,
6) development of organizational structures and management procedures.
7) Process management and implementation of the PRO values (Partnership – Development – Courage).

The description of the monitoring of the implementation (performance) of the above mentioned indicators (ratios) is provided in the individual sections of the report, while the summary of the key non-financial efficiency indicators (ratios) associated with the operations of TAURON Capital Group is provided in section 8.2. of this report.

4.4. Proceeds from securities issues

Under the bond issue program concluded on 24 November 2015 between the Company and the consortium of banks In 2017 TAURON conducted bond issues and redemptions under the existing program (i.e the bond issue program concluded with the consortium of banks on November 24, 2015), and also completed the eurobond issue.

Eurobond issue

On July 5, 2017 TAURON issued eurobonds with the nominal value of EUR 500 mln. Eurobonds are unsecured, senior, coupon bearing securities. Eurobonds' maturity date is 10 years from the date of issue. The interest rate is based on a fixed rate of 2.375% per annum. The yield as of the date of issuance was 2.439% per annum with the issue price equal to 99.438% of the nominal value. In accordance with the eurobond issue prospectus the proceeds from the issue were to be used to refinance the costs of the construction and acquisition of wind farms by one of TAURON Capital Group's subsidiaries, financing of TAURON Capital Group's investment projects in the distribution segment and for general corporate purposes. Eurobonds were granted BBB rating by Fitch rating agency. Fulfilling this obligation in Q4 2017 TAURON completed the redistribution of the funds obtained from the bond issue by recapitalizing the following subsidiaries: TAURON EKOENERGIA and TAURON Dystrybucja, as a result of which TAURON EKOENERGIA made a repayment of a substantial portion of the debt related to the construction and acquisition of wind farms and TAURON Dystrybucja received funds to cover the expenditures related to the investment projects implemented by this subsidiary.

Eurobonds were admitted to trading on the regulated market of the London Stock Exchange.

Information on the eurobond issue was disclosed in detail in the regulatory filings (current reports) described in section 2.8. of this report.

Bond issues and redemptions in 2017

The bonds issue program signed on 24 November 2015 between TAURON and a consortium of banks led to issue in 2017 by TAURON of bonds having the total part value of PLN 600 mln, according to the following specification:

1) Bonds issue on 30 January 2017 with total par value of PLN 100 mln - redeemed on 30 July 2017,
2) Bonds issue on 01 March 2017 with total par value of PLN 100 mln - redeemed on 01 September 2017,
3) Bonds issue on 31 March 2017 with total par value of PLN 300 mln - redeemed on 30 June 2017,
4) Bonds issue on 30 June 2017 with total par value of PLN 100 mln - redeemed on 30 July 2017

Funds received from the above bonds issue were used as stated in issue documents, i.e. to cover investment outlays of the TAURON Capital Group and for general corporate purposes.

Also, TAURON redeemed early the following bonds issued within the bonds issue program signed on 24 November 2015:

1) Redemption of PLN 100 mln par value of bonds on 25 September 2017,
2) Redemption of PLN 300 mln par value of bonds on 09 December 2017,
3) Redemption of PLN 650 mln par value of bonds on 29 December 2017.

The below table presents the summary of issued and non-redeemed bonds as of December 31, 2017.

Table no. 16. Summary of issued and non-redeemed bonds as of December 31, 2017

No.	Value of bonds issues (thou.)	Type and level of interest rate	Redemption term of the last series	Balance as of 31 December 2016 (thou.)
1.	1 750 000 PLN	WIBOR 6M + fixed margin	04.11.2019	1 750 000 PLN
2.	1 700 000 PLN	WIBOR 6M + fixed margin	20.12.2029	1 700 000 PLN
3.	1 600 000 PLN	WIBOR 6M + fixed margin	29.12.2020	1 600 000 PLN
4.	190 000 EUR	Fixed interest rate	16.12.2034	190 000 EUR
5	500 000 EUR	Fixed interest rate	05.07.2027	500 000 EUR

4.5. Financial instruments

4.5.1. Application of financial instruments in order to eliminate price changes, credit risk, material disruptions of cash flows and loss of financial liquidity

As part of financial risk management in 2017 TAURON Capital Group continued to hedge the risk of volatility in cash flows resulting from its debt based on WIBOR reference rate. Moreover, in 2017 TAURON Capital Group hedged the currency exposure arising from the trading operations (mainly due to the purchase of CO_2 emission allowances) by concluding forward contracts. In 2017 TAURON Capital Group was also implementing the strategy of hedging its foreign currency exposure generated by interest payments on the financing obtained in EUR by concluding forward contracts and CIRS transactions. The goal of these transactions was to hedge against the risk of cash flow volatility resulting from currency rate fluctuations.
The below table presents active forward derivative transactions as of December 31, 2017 (due to the adopted centralized model of financial risk management, the data refers only to TAURON)

Table no. 17. Information on forward transactions and derivatives as of December 31, 2017

No.	Type of transaction concluded	Total denomination of the specific type of transaction (thou.)	Currency			Maturity date of the specific type of transaction		Valuation of transaction of the specific type as of December 31, 2017 (thou.)
			PLN	EUR	other	up to one year	above one year	
1.	IRS	2 100 000	X				X	24 482
2.	CIRS	1 262 120	X				X	- 9 299
3.	Forward	6 610		X		X		- 346

With respect to hedging the risk arising from price volatility and the credit risk TAURON Capital Group did not use financial instruments.

On the other hand, as part of liquidity loss risk management debt instruments referred to in section 4.6 are used.

4.5.2. Objectives and methods of financial risk management

The objectives and methods of financial risk management at TAURON are presented in section 3.4.2 of this report.

4.6. Objectives and methods of financial risk management

TAURON has a centralized financial management function in place and thus effective management of finance of entire TAURON Capital Group is possible. The main tools enabling effective management include: the implemented central financing model and the appropriate internal corporate regulations as well as the cash pooling implemented by TAURON

Capital Group. Additionally, the financial management system is supported by the central policy of managing the financial risk at TAURON Capital Group and the central Insurance policy of TAURON Capital Group. In these areas TAURO plays the role of the management body and decision maker with respect to the directions of measures undertaken, enabling determining the relevant limits of risk exposure.

In accordance with the adopted central model of financing TAURON is responsible for acquiring the financing for TAURON Capital Group's subsidiaries. Funds acquired both internally (from TAURON Capital Group's subsidiaries generating financial surpluses), as well as externally (from the financial market) are subsequently transferred to TAURON Capital Group's subsidiaries, reporting the requirement for financing (for this purpose, besides cash pooling, the intra-group bond issue program is implemented).

Such model of acquiring the funding sources enables, first of all, decreasing of the cost of capital, increasing the possibility to obtain financing, reduces the number and form of hedges established on assets of TAURON Capital Group and covenants required by financial institutions, as well as reduces the administrative costs. The central model of financing also enables acquiring financing sources unavailable for individual subsidiaries, such as, for example, issue of eurobonds.

Another key element influencing the efficiency of financial management is the policy of financial liquidity management. Through implementation of relevant forecasting standards it becomes possible to establish the precise liquidity position allowing for optimizing the moment of fund raising as well as the maturity term and types of deposit instruments as well as the appropriate level of the liquidity reserve. The above factors lead to both, cost reduction as well as liquidity safety improvement. The current liquidity management is supported by the implemented cash pooling mechanism. Its overriding goal is to provide for current financial liquidity at TAURON Capital Group, while at the same time limiting the costs of short term external financing and maximizing the financial revenue due to investing cash surpluses. Owing to the cash pooling structure TAURON Capital Group's subsidiaries facing short term deficits of funds, may use funds of the subsidiaries generating financial surpluses, without the need to acquire external financing.

Moreover, a unified program of bank guarantees was implemented at TAURON. Under the agreements concluded by TAURON with banks it is possible to issue guarantees to secure the liabilities of TAURON Capital Group's subsidiaries companies within the centralized limit. The above mentioned measure reduced the cost of guarantees acquired, made their acquisition independent of the individual subsidiaries' financial standing and limited the total number of actions required to obtain a guarantee.

In 2017 TAURON demonstrated full capacity to pay its accounts payable with the payment deadlines thereof.

4.7. Principles of preparing annual financial statements

Financial statements have been drawn up in accordance with the IFRS approved by the EU.

The IFRS comprise standards and interpretations approved by the International Accounting Standards Board as well as the International Financial Reporting Interpretation Committee.

The financial statements have been prepared with the assumption of the continuation of business operations by TAURON in the foreseeable future. As of the date of approval of the consolidated financial statements for publication, no circumstances have been detected, indicating any risk for business continuity by TAURON.

The accounting principles (policy) adopted for drawing up of the consolidated financial statements are presented in note 9 of the Consolidated financial statements for the year ended on December 31, 2017.

4.8. Information on the entity authorized to audit financial statements

On April 27, 2017 TAURON concluded the agreement with Ernst & Young Audyt Polska Limited Liability Company Limited Joint-Stock Partnership on conducting an audit of:

1) financial statements of the Company for 2017, prepared in accordance with the requirements of the IFRS,
2) financial statements of selected subsidiaries of TAURON Capital Group for 2017, prepared in accordance with the IFRS,
3) consolidated financial statements for 2017, prepared in accordance with the requirements of the IFRS.

The Agreement also covers conducting a review of the interim, half year financial statements of the Company and the consolidated financial statements of TAURON Capital Group, prepared in accordance with the IFRS requirements for the period ending on June 30, 2017.

The above audit company was also selected, on February 26, 2018 by TAURON's Supervisory Board to audit the standalone and consolidated financial statements of TAURON for the financial year 2018 and the review of the interim standalone and consolidated financial statements of TAURON for the period ending on June 30, 2018. The detailed information on the conclusion of the amendment to the agreement with the above audit company is provided in section 2.7. of this report.

The audit of the standalone and consolidated financial statements of TAURON for the financial year 2016, the financial statements of selected TAURON Capital Group's subsidiaries for the financial year 2016 and the review of the interim standalone and consolidated financial statements of TAURON for the period ending on June 30, 2016 were conducted by Deloitte Polska Limited Liability Company Limited Joint-Stock Partnership.

The compensation of the certified auditors for the services provided for TAURON Capital Group's subsidiaries is shown in the below table.

Table no. 18. Compensation of the certified auditors for the services provided for TAURON

No.		Year ended on December 31, 2017 (PLN thou.)	Year ended on December 31 2016 (PLN thou.)
1.	Mandatory audit	178	105
2.	Other certifying services provided to TAURON Capital Group, including reviews of financial statements	77	45
3.	Tax advisory services	0	0
4.	Other services (including training) provided for TAURON Capital Group	3	158
	Total	**258**	**308**

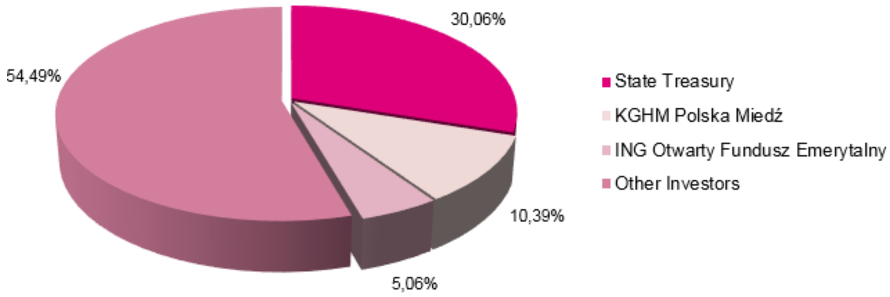
5. SHARES AND SHAREHOLDERS

5.1. Structure of shareholding

As of December 31, 2017 and as of the day of drawing up this report the Company's share capital was, in accordance with an entry in the National Court Register, PLN 8 762 746 970 and was split into 1 752 549 394 shares with a nominal value of PLN 5 per share, including 1 589 438 762 ordinary AA series bearer shares and 163 110 632 registered BB series shares.

The below figure presents the structure of shareholding as of December 31, 2017 and as of the day of drawing up this report.

Figure no. 45. Structure of shareholding as of December 31, 2017 and as of the day of drawing up this report



5.2. Dividend policy

As part of its Strategy adopted on September 2, 2016 the Company adopted its dividend policy. In the long term TAURON is planning to pay out a dividend of minimum 40 percent of the consolidated net profit. The Company's intention is to provide a dividend yield that would be competitive versus the yield offered by long term debt instruments issued on the Polish market by investment grade rated companies. The final recommendation on the dividend will be impacted by additional factors, including in particular

1) TAURON Capital Group's liquidity position,
2) Market situation,
3) Implementation of the investment policy,
4) Cost and ability to obtain financing,
5) Legal requirements and provisions of the financing agreements, in particular related to not breaching the defined level of the leverage ratio,
6) Ensuring investment grade rating.

The forecasts that are the basis for the Strategy indicate that 2020 will be the first year in which the dividend payout will be possible.

The below table presents the dividends paid out in 2010-2014.

Table no. 19. Dividends paid out in 2010-2014

Dividends paid out in 2010-2014						
#	Financial year for which the dividend was paid out	Dividend amount paid out (PLN)	Net profit %	Dividend per share (PLN)	Dividend record date	Payment date
1.	2010	262 882 409,10	31%	0.15	30.06.2011	20.07.2011
2.	2011	543 290 312,14	44%	0.31	02.07.2012	20.07.2012
3.	2012	350 509 878,80	24%	0.20	03.06.2013	18.06.2013
4.	2013	332 984 384,86	25%	0.19	14.08.2014	04.09.2014
5.	2014	262 882 409,10	23%	0.15	22.07.2015	12.08.2015

5.3. Number and nominal value of the Company's shares, as well as of the shares in units related to the Company, held by members of the Management Board and the Supervisory Board

As of December 31, 2017 and as of the day of drawing up this report members of the Management Board and members of the Supervisory Board did not have any TAURON shares, nor they held any shares in units related to the Company.

5.4. Agreements related to potential changes to the shareholding structure

Management Board has no information on the existence of agreements (including also the ones concluded past the balance sheet date), as a result of which changes in the proportions of shares held by the existing shareholders and bondholders may occur in the future.

5.5. Own shares buybacks

In 2017 and as of the day of drawing up this report the Company did not own any of its shares.

5.6. Employee stock award programs

In 2017 no employee stock award programs were implemented by the Company.

5.7. Shares performance on the Warsaw Stock Exchange (WSE)

TAURON shares have been listed on the Main Market of the Warsaw Stock Exchange since June 30, 2010. In 2017 TAURON share price fluctuated between PLN 2.76 and PLN 4.12 (at closing prices). During the last session of 2016 the share price was PLN 2.85, while a year later the price reached PLN 3.05. This means that the rate of return[4] on the investment in TAURON shares was 7 percent in 2017.

Performance of shares listed on WSE in 2017 was impacted by favorable, both global as well as local factors. Investors were convinced that the government's economic policy allowed for a further strong GDP growth, while PLN was one of the strongest currencies on the market. Also energy sector companies became more attractive for investors, which led to a 15% rise of the WIG-Energia index.

Apart from very good economic conditions and the growing demand for electricity TAURON share price last year was also positively impacted by activities with respect to obtaining financing aimed at ensuring TAURON Capital Group's financial stability, in particular the July 2017 issue of 10-year Eurobonds worth EUR 500 mln.

As of December 31, 2017 TAURON shares were included in the following stock exchange indices:

1. **WIG** - index that includes all companies listed on WSE's Main Market that meet basic criteria for inclusion in indices. TAURON's share in WIG: 0.96%.
2. **WIG-Poland** – national index that groups solely shares of domestic companies listed on WSE's Main Market that meet basic criteria for inclusion in indices. TAURON's share in WIG-Poland index: 1.11%.
3. **WIG20** - index calculated on the basis of the value of the portfolio of shares of 20 largest and most liquid companies listed on WSE's Main Market. TAURON's share in WIG20 index: 1.46%.
4. **WIG30** - index that includes 30 of the largest and most liquid companies listed on WSE's Main Market. TAURON's share in WIG30 index: 1.35%.
5. **WIG-Energia** - sector based index that comprises companies included in WIG index and are also qualified to the energy sector. TAURON's share in WIG-Energia: 15.98%.
6. **Respect Index** - index that groups in its portfolio companies that operate in accordance with the highest corporate social responsibility standards. TAURON's share in RESPECT Index: 2.65%.
7. **MSCI Emerging Markets Europe** - index that includes key companies in 15 developed countries in Europe. TAURON's share in MSCI Emerging Markets Europe Index: 0.02%.
8. **MSCI Poland Index** - index that includes more than 20 key companies listed on WSE. TAURON's share in MSCI Poland Standard Index: 1.26%.

[4] *Rate of return calculated taking into account the investor's income from the dividend and assuming that the additional income realized is re-invested. Methodology in accordance with WSE Statistical Bulletin.*

The below table presents key data on the Company's shares in 2011-2017.

Table no. 20. Key data on TAURON shares in 2011-2017

#		2011	2012	2013	2014	2015	2016	2017
1.	Share price high (PLN)	6.81	5.61	5.39	5.69	5.29	3.19	4.12
2.	Share price low (PLN)	4.65	4.08	3.85	4.04	2.37	2.31	2.75
3.	Last share price (PLN)	5.35	4.75	4.37	5.05	2.88	2.85	3.05
4.	Capitalization at the end of the period (PLN m)	9 376	8 325	7 659	8 850	5 047	4 995	5 345
5.	Capitalization at the end of the period (%)	2.1	1.59	1.29	1.5	0.98	0.9	0.8
6.	Book value (PLN m)	15 922.47	16 839.41	17 675,34	18 106.79	18 837	16 348.99	17 880
7.	P/E	8.1	5.5	5,5	7.8	4.2	x	3.02
8.	P/BV	0.59	0.49	0,43	0.49	0.27	0.31	0.31
9.	Rate of return ytd[1] (%)	-16.73	-5.03	-3,64	20.07	-40.78	-1.04	7.02
10.	Dividend yield (%)	2.8	6.5	4,6	3.8	5.2	-	-
11.	Trading volume (PLN m)	5 574.82	3 198.94	3 103,56	3 134.81	3 062.52	3 199.02	2 737.33
12.	Trading volume share (%)	2.21	1.7	1.41	1.53	1.5	1.69	1.16
13.	Average volume per session	3 721 539	2 667 725	2 793 020	2 489 329	3 190 195	4 662 087	3 261 765
14.	Average number of transactions per session	1 373	960	1 022	1 106	1 431	1 465	1 323

Source: WSE Statistical Bulletin

[1] Rate of return calculated taking into account the investor's income from the dividend and assuming that the additional income realized is re-invested. Methodology in accordance with WSE Statistical Bulletin.

The below graphs present historical TAURON share price performance and trading volumes, including against WIG20 and WIG-Energia indices.

Figure no. 46. TAURON share price and trading volumes in 2017

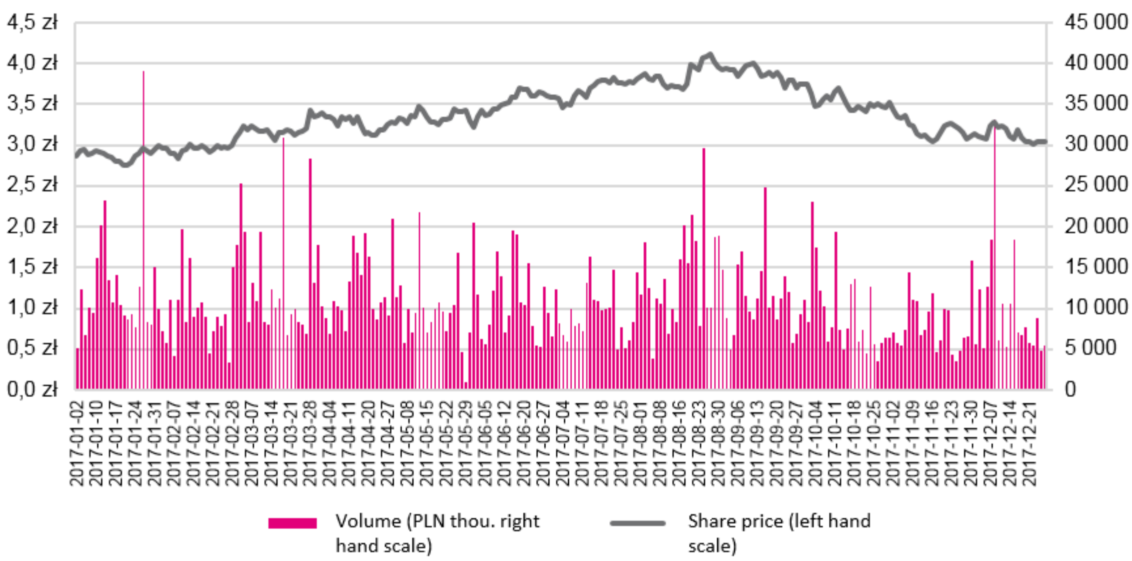


Figure no. 47. TAURON share price and trading volumes since the market debut until December 31, 2017

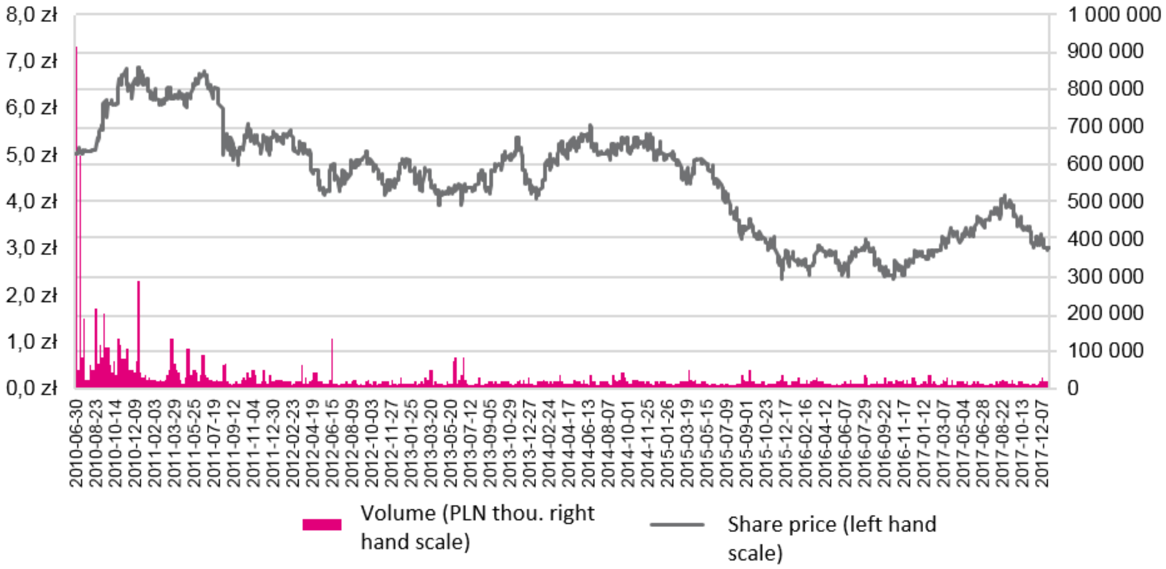
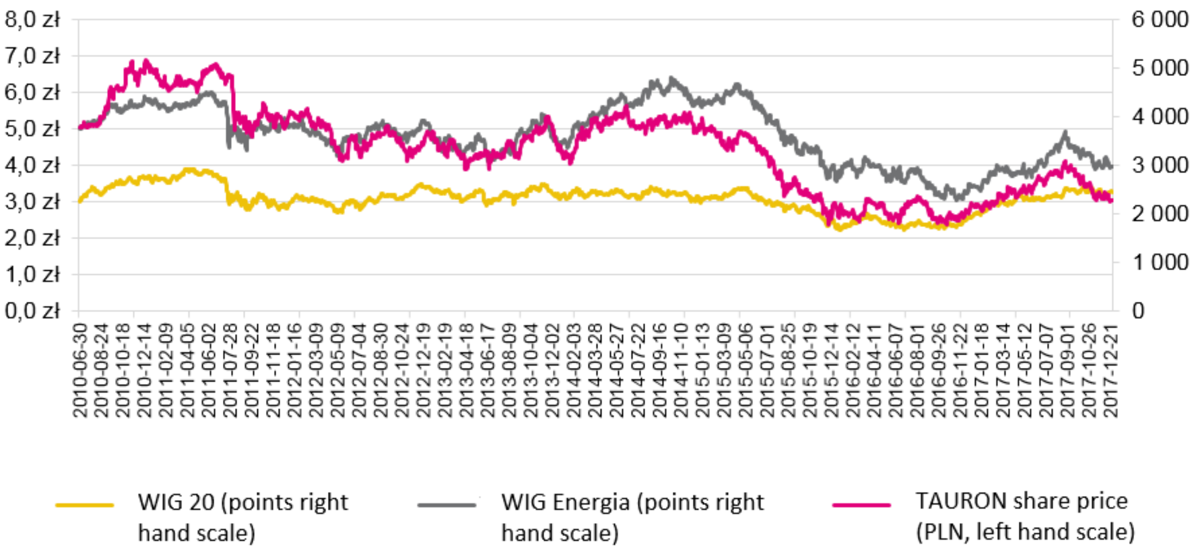


Figure no. 48. TAURON share price versus WIG20 and WIG-Energia indices since the market debut until December 31, 2017



Recommendations for the shares of TAURON Polska Energia S.A.

In 2017 analysts from brokerage houses and investment banks issued 11 recommendations for TAURON shares in total, including:

1) three ”Buy” recommendations,

2) four ”Hold” recommendations,

3) four ”Sell” recommendations.

The below table presents a list of recommendations issue in 2017.

Rekomendacje dla akcji TAURON Polska Energia S.A.

Table no. 21. Recommendations issued in 2017

#	Date of issuing recommendation	Institution issuing recommendation	Recommendation / target price
1.	15.11.2017	Societe Generale	Buy / PLN 4.50
2.	21.03.2017	Societe Generale	Buy / PLN 4.00

#	Date of issuing recommendation	Institution issuing recommendation	Recommendation / target price
3.	10.01.2017	Pekao Investment Banking	Buy / PLN 4.00
4.	20.11.2017	DM BZ WBK	Hold / PLN 3.40
5.	14.09.2017	Exane BNP Paribas	Hold / PLN 4.00
6.	27.06.2017	mBank	Hold / PLN 3.67
7.	20.03.2017	Raiffeisen Centrobank	Hold / PLN 3.50
8.	08.08.2017	DM PKO BP	Sell / PLN 3.40
9.	26.01.2017	DM BOŚ	Sell / PLN 2.50
10.	08.02.2017	DM Banku Handlowego (Citi)	Sell / PLN 2.50
11.	07.07.2017	DM Banku Handlowego (Citi)	Sell / PLN 2.50

5.8. Investor relations

Accurate and regular communications is one of the key priorities of TAURON with respect to conducting the dialogue with investors. It is provided both in the form of mandatory activities required by law (e.g. by disclosing information in the current and periodic regulatory filings) but also using many additional tools addressed directly to institutional and individual investors. The Company organizes itself as well as participates in many investor conferences and roadshows organised by entities operating on the capital market, both in Poland and abroad.

During meetings with investors, the Strategy, the investment projects underway, the financial situation of TAURON Capital Group is presented as well as information on the current standing and outlook of the energy sector.

In connection with the publishing of periodical reports the Company organized conferences for investors and analysts during which members of the Management Board discussed financial results and presented the most important events in the reported periods. The conferences were broadcast on the Internet in Polish and in English. A possibility listening via telephone was also provided. This way all interested investors were able to receive the information at the same time. Separate meetings devoted to discussion of financial results are also regularly arranged for representatives of key media, so that information concerning the standing of TAURON Capital Group could reach all investors via diverse channels.

Besides meetings accompanying the publication of periodical reports, in 2017 members of the Management Board and representatives of the Investor Relations Team took part in 16 conferences and roadshows, during which approximately 100 meetings with managers and capital market analysts were held. Representatives of TAURON met institutional investors not only in Poland, but also in the US, Great Britain, Austria, Germany, Holland, France and Czech Republic.

In connection with the growing role of Internet channels and social media, much emphasis was put on their development with respect to the communications with investors. Via the YouTube service broadcasts of events important for investors are provided: earnings conferences, GMs, Investor Days and comments of the President of the Management Board on the financial results. On the other hand, on Facebook, announcements of significant events are published by the Company, including links to websites where the broadcasts may be followed or participation in an investor chat is possible. TAURON also launched a corporate profile on Twitter where entries related to investor relations appear. Being aware of the fact that the website is a significant source of information for investors, in particular, the *Investor Relations* tab; the Company takes cares of its content and validity of the content provided therein. *Investor Relations* section contains a lot of useful information on the current events, financial results or GMs. It also provides presentations and video broadcasts of conferences summarising the financial results.

In 2017, similar to 2016, TAURON participated in events addressed to individual investors. The company was, inter alia, a partner of the “WallStreet” conference in Karpacz, as well as winter and summer sports competitions of the capital market “Capital Market Games”. As party of the regular communications with this sizeable group of investors, 4 chats with a representative of the Management Board took place in 2017, in which approximately 100 investors took part each time.

Activities with respect to investor relations are appreciated by participants of the capital market and investors. In 2017 the Company was awarded successive prizes for the high quality of investor relations.

In March 2017, the Company was awarded a special prize in the competition for the best investor relations among WIG30 index companies, organized by the Stock Market and Investors Paper ”Parkiet” and the Chamber of Brokerage Houses.

In June 2017 TAURON was awarded the "Hero of the capital market 2017" title in the company category. The winner in the competition organized by the Individual Investors Association was selected based on the vote of the investors who appreciated TAURON's high standards in the field of investor relations and applying the best practice with respect to the communications address to the individual investors.

In the past year TAURON was among the laureates of the "2016 Transparent Company of the Year" ranking for business transparency and quality of the market communications. The ranking, organized by the Stock Market and Investors Paper ”Parkiet" and the Institute of Accounting and Taxes (Instytut Rachunkowości i Podatków), was based on a survey in which three most important market communications area were evaluated, i.e. financial statements and reporting, investor relations and corporate governance rules.

TAURON is also regularly awarded prizes in the top annual report competitions. The Company finished first in the previous three editions of ”The Best Annual Report" competition organized by the Institute of Accounting and Taxes (Instytut Rachunkowości i Podatków), qualifying, in 2017, to the elite ”The Best of the Best" category. In last year's edition of the competition TAURON was also awarded the top prize for the integrated annual report.

Company is maintaining high quality of reporting to meet the expectations of the broadest possible group of recipients of its communications - customers, shareholders, analysts, as well as media representatives. This is why in 2017 the team working on the design of the integrated annual report focused on the compliance of its structure and content with the international integrated reporting standards. The result of these works is a modern, multimedia online report online presenting the most important information on TAURON Capital Group.

TAURON has been included in the RESPECT Index since 2013, and in December 2017, for the fifth time, the Company found itself in the group of stock market listed entities that apply the highest sustainable growth standards

2017 investor relations highlights and activities are presented in the below table.

Table no. 22. Highlights and activities performed as part of investor relations in 2017

#	Date	Highlight (event)
1.	15.03.2017	Full year 2016 stand-alone and consolidated earnings reports published
2.	16.03.2017	Management Board's meeting with analysts and fund managers to present FY 2016 earnings, Warsaw
3.	16.03.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
4.	21-22.03.2017	Participation in DM PKO BP CEE Capital Markets Conference, London
5.	27-28.03.2017	Participation in Raiffeisen Centrobank Investor Conference, Austria, Zürs
6.	10.05.2017	Q1 2017 earnings report published
7.	11.05.2017	Management Board's meeting with analysts and fund managers to present Q1 2017 earnings, Warsaw
8.	11.05.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
9.	25.05.2017	Meetings with fund managers following Q1 2017 earnings, DM Banku Handlowego (Citi), Warsaw
10.	29.05.2017	TAURON's Ordinary GM
11.	20.06.2017	Eurobond Roadshow, Germany
12.	21.06.2017	Eurobond Roadshow, Netherlands
13.	22.06.2017	Eurobond Roadshow, Great Britain
14.	23.06.2017	Eurobond Roadshow, France
15.	26.06.2017	Eurobond Roadshow, Warsaw
16.	17.08.2017	H1 2017 earnings report published
17.	18.08.2017	Management Board's meeting with analysts and fund managers to present H1 2017 earnings, Warsaw
18.	18.08.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
19.	24.08.2017	Meetings with fund managers following H1 2017 earnings, Societe Generale, Warsaw

#	Date	Highlight (event)
20.	11-12.09.2017	Participation in 14th Annual Emerging Europe Investment Conference, Pekao Investment Banking, Warsaw
21.	26-27.09.2017	Participation in Mining&Energy Conference, DM PKO BP, Katowice
22.	11-12.10.2017	Participation in Erste Group Investor Conference, Austria, Stegersbach
23.	08.11.2017	Q3 2017 earnings report published
24.	09.11.2017	Management Board's meeting with analysts and fund managers to present Q3 2017 earnings, Warsaw
25.	09.11.2017	Chat for individual investors as part of cooperation with the Individual Investors Association
26.	15.11.2017	Meetings with fund managers following Q3 2017 earnings, DM mBanku, Warsaw
27.	20-21.11.2017	Participation in Poland Investment Forum NY, JP Morgan, New York
28.	01.12.2017	Participation in BZ WBK Energy & Mining Conference, Warsaw
29.	05.12.2017	Participation in Wood's Winter Conference in Prague, Prague

6. STATEMENT ON APPLICATION OF CORPORATE GOVERNANCE

Pursuant to § 91(5)(4) of the Regulation of the Minister of Finance of 19 February 2009 *on current and periodical information submitted by issuers of securities and conditions to acknowledge as equivalent information required by legal regulations of a country not being a member state* (Journal of Laws no.33 item 259 as amended), and the *Best Practice of GPW Listed Companies 2016* (Best Practice 2016), the Company's Management Board submits the statement on application of corporate governance in 2017.

6.1. Indication of applied set of corporate governance rules

In 2017 the Company was subject to the corporate governance rules, described in the document *Best Practice of GPW Listed Companies*(Best Practice 2016), adopted by the Supervisory Board of the GPW Board no. 27/1414/2015 of 13 October 13, 2015, which came into force on January 1, 2016.

The text of the Best Practice 2016 the Company is subject to is published on the GPW website at the address: www.gpw.dobre-praktyki.pl.

6.2. Indication of abandoned rules of corporate governance

In 2017 the Company did not apply the following detailed rules provided in Best Practice 2016:

1) IV.Z.2. concerning ensuring of publicly available real-time broadcasts of general meetings, due to the lack of the relevant provisions of the Articles of Association enabling the aforementioned broadcast. In order to enable the application of the rule, the Company Management Board requested the Ordinary GM of the Company to adopt the relevant amendment to the Company Articles of Association ensuring publicly available real-time broadcast of general meetings. However, the Ordinary GM of the Company convened on 8 June 2016 did not adopt the amendment to the Company Articles of Association proposed by the Company Management Board in this respect,
2) VI.Z.1. concerning the construction of incentive schemes in a way necessary, among others, to tie the level of compensation of members of the Company's management board and key managers to the actual long-term financial standing of the Company and long-term shareholder value creation as well as the Company's stability. This rule was not applied due to the compensation and bonus system applicable in TAURON in relation to members of the Management Board of the Company and its key managers stipulates that the level of compensation will be tied to the financial situation of the Company within the annual perspective, in conjunction with the implementation of strategic objectives,
3) VI.Z.2. stating that in order to tie the compensation of members of the management board and key managers to the Company's long-term business and financial goals, the period between the allocation of options or other instruments linked to the Company's shares under the incentive scheme and their exercisability should be no less than two years. 2 years This rule was not applied due to the compensation and bonus system applicable in TAURON in relation to Members of the Management Board of the Company and its key managers does not provide that compensation should be tied to instruments linked with the Company shares.

In 2017 the following rules did not apply to the Company:

1) I.Z.1.10. concerning placing financial projections on the Company website - if the company has decided to publish them - published at least in the last 5 years, including information about the degree of their implementation - due to the fact that financial forecasts are not published,
2) III.Z.6. stating that where the Company has no separate internal audit function in its organization, 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 organizational structure.

Furthermore, the Management Board of the Company, adopting the detailed rules of Best Practice 2016 designated as: I.Z.1.3, I.Z.1.15, I.Z.1.16, II.Z.1, II.Z.6, II.Z.10.1, II.Z.10.2, II.Z.10.3, II.Z.10.4, V.Z.5, V.Z.6, VI.Z.4., indicated the manner of applying them. The detailed description of the manner of applying the above rules is provided in the *Information on the status of applying by the Company of the recommendations and rules provided in Best Practice 2016,* constituting an appendix to the above mentioned report on not applying the detailed rules provided in Best Practice 2016 and provided on the Company's website.

In 2017 the Company developed and introduced into use the document *Diversity Policy at TAURON Group*, that was described in detail in section 6.12. of this report. Before that the Company had not had a single document describing the applied policy of diversity in relation to the authorities of the Company and its key managers, referred to in the rule designated as I.Z.1.15. of Best Practice 2016, in the report published on February 1, 2016 concerning the abandoned detailed rules of corporate governance contained in Best Practice 2016, the Company indicated the method of applying the diversity policy. It was indicated at then that the rules on diversity management were introduced for application under many documents constituting internal legal acts.

Information concerning abandonment of recommendations provided in Best Practice 2016 for application

In 2017 the Company did not apply only the recommendation provided in Best Practice 2016, designated as IV.R.2 concerning ensuring a possibility to shareholders to participate in the GM using electronic communication means, due to the lack of such shareholders' expectation. This decision is expressed by the failure of the Company GM on 8 June 2016 to adopt the relevant amendments to the Company Articles of Association ensuring publicly available real-time broadcast of general meetings.

The other recommendations provided in Best Practice 2016 were applied by the Company in 2017.
W 2017 r.

6.3. Description of main characteristics of internal control and risk management systems in relation to the process of generating the financial statements and consolidated financial statements

The internal audit and risk management system with respect to the process of drawing up the financial statements and consolidated financial statements is implemented on three levels:

Level I

General principles of management at the Company and TAURON Capital Group. TAURON Capital Group's subsidiaries operate based on organizational regulations and possess defined organizational structures based on internal documents adopted for the entire Group. These define the business units responsible for preparing financial statements and consolidated financial statements. Such units have the duty to perform regular control of the tasks vested and functional control of their activities. Business Model of the TAURON Capital Group resulted in implementation of Process Documentation of Megaprocess 3.4 Accounting, containing procedures associated with financial reporting of the Company and the TAURON Capital Group. Process documents define responsibilities of business units within the reporting processes.

Level II

Risk management. TAURON Capital Group implemented a Risk Area managed by the Executive Director for Risk Management, whose role is to oversee and establish the risk management process for the entire TAURON Capital Group. These functions are implemented within the Company by Corporate, Market and Credit Risk Management Teams. The purpose of risk management is to improve the predictability of attaining strategic objectives by the TAURON Capital Group, including stable creation of the financial result through early identification of threats allowing preventive activities to commence. Risk management standards applicable at the TAURON Capital Group have been defined in the *Strategy for corporate risk management at the TAURON Group* and in policies for managing specific risks. The ERM system encompasses all spheres of TAURON Capital Group business and business processes within the Group, including the process of preparing financial statements. Risks associated with his process are managed, monitored and reported within the ERM system. Standardization aims to ensure coherence in managing the individual risk categories, defining general principles, standards and tools of system architecture. Oversight of the ERM system at TAURON Capital Group is performed by the Risk Committee.

Level III

Internal Audit. Internal Audit Department is functioning in the Company. The goal of the Internal Audit is planning and implementing audit tasks, including performance of commissioned ad-hoc inspections, and also activities of advisory and opinion (feedback) providing nature. Methods and rules of implementing the Internal Audit function are defined by the Process Documentation of the Megaprocess 1.5 Audit along with the related document *Regulations of Internal Audit at TAURON Group.* The introduction of Megaprocess 1.5 Audit was a consequence of the adoption of the Business Mode by the Management Board of TAURON. In implementing the internal audit function the Company shall be acting in compliance with the *TAURON Group's Corporate Social Responsibility Code* and the International Standards for the Professional Practice of Internal Auditing.

Key aspects with respect to internal control and risk management in reference to the process of preparing financial statements and consolidated financial statements include:

Supervision over application of consistent accounting rules by TAURON Capital Group's subsidiaries when developing reporting packages for the purpose of preparing TAURON Capital Group's consolidated financial statements

In order to ensure consistent accounting principles based on International Financial Reporting Standards (IFRS) approved by the European Union the Accounting Policy of TAURON Polska Energia S.A. Capital Group (Accounting Policy) was developed and implemented in TAURON Capital Group. This document shall be accordingly updated in case there are changes to the regulations. The rules defined in the Accounting Policy shall be applicable to TAURON's stand-alone financial statements and TAURON Capital Group's consolidated financial statements. TAURON Capital Group's subsidiaries shall be obligated to apply the Accounting Policy when preparing the reporting packages that provide the basis for preparing TAURON Capital Group's consolidated financial statements.

Furthermore, TAURON Capital Group developed and implemented an intra-group regulation that comprehensively regulates issues related to the rules and deadlines for preparing the reporting packages for the purpose of consolidated financial statements. The reporting packages shall be validated by the holding company's Consolidation and Reporting Office and by an independent certified auditor during an audit or review of TAURON Capital Group's consolidated financial statements.

Procedures used to authorize and provide opinions on the Company's financial statements and TAURON Capital Group's consolidated financial statements

The Company has implemented financial statements' authorization procedures. Quarterly, half year and full year financial statements of the Company and TAURON Capital Group's consolidated financial statements shall be approved by the Company's Management Board before being published. Full year financial statements of TAURON and TAURON Capital Group's consolidated financial statements shall be additionally presented for evaluation to the Company's Supervisory Board before being published. Vice President of the Management Board for economic and financial affairs (Chief Financial Officer) shall oversee the preparation of financial statements, while the Management Boards of the subsidiaries included in the consolidation shall be responsible for preparing the reporting packages for TAURON Capital Group's consolidated financial statements.

Supervisory Board's structure includes the Audit Committee of the Supervisory Board of TAURON Polska Energia S.A., whose membership, competence and description of activities are provided in clause 6.11.3 of this report

IT systems as well as financial and accounting processes

TAURON Capital Group's subsidiaries maintain accounting books (ledgers) which constitute the basis for preparing financial statements using ERP financial and accounting computer systems, enabling system audits of the correctness of the document flow and classifying of the business events. Consolidated financial statements are prepared using an IT tool used to consolidate financial statements, providing system control with respect to the coherence (integrity) and timeliness of preparing the consolidation data.

TAURON Capital Group's subsidiaries have implemented IT and organizational solutions that provide control of access to the financial and accounting system and ensure adequate protection and archiving of the accounting books. Access to IT systems is restricted based on applicable access rights assigned to authorized personnel. Control mechanisms are applied in the process of granting and changing access rights to the financial and accounting systems. Granted rights are also subject to periodic verification.

Due to the integration of the accounting functions and the transfer of TAURON Capital Group's material subsidiaries' financial and accounting services to CUW-R (Shared Cervices Center – Accounting) TAURON Capital Group's financial and accounting processes were gradually unified. The subsidiaries adjusted their own procedures to the flow of the financial and accounting processes, taking into account the specifics of the individual segments.

TAURON Capital Group's Business Model clearly distributes responsibilities with respect to the financial and accounting processes between the Company (indicated as the Corporate Centre) and the subsidiaries and CUW R, indicating that the Corporate Centre is the owner of processes associated with accounting and reporting of TAURON Capital Group. With respect to the tasks of the Corporate Centre, strategic functions associated with the development of the model of operations and standards of TAURON Capital Group were indicated in the area of accounting and supervision of the implementation of standards in the accounting area in the subsidiaries and CUW R. Moreover, it was indicated that the Company as the Corporate Centre is responsible for drawing up the Company's financial statements and the consolidated financial statements of TAURON Capital Group. A clear split of responsibilities and strong emphasis on the fulfillment of the supervisory functions by the Corporate Centre in relation to CUW R and the subsidiaries is, inter alia, aimed at improving the process of preparing the financial statements.

Subjecting the Company's financial statements and TAURON Capital Group's consolidated financial statements to an audit and reviews by an independent certified auditor

Full year financial statements of the Company and full year consolidated financial statements of TAURON Capital Group are subject to an audit by an independent certified auditor. Half year financial statements of the Company and half year consolidated financial statements of TAURON Capital Group are subject to a review by a certified auditor. In 2017 the Company selected an entity authorized to audit and review the financial statements of the material subsidiaries of TAURON Capital Group and the consolidated financial statements. The agreement with the entity authorized to audit financial statements was concluded to conduct an audit and review of the 2017 financial statements. Due to the selection by TAURON's Supervisory Board on February 26, 2018 of an audit company to conduct an audit of the Company's and TAURON Capital Group's 2018 financial statements and a review of the Company's and TAURON Capital Group's 2018 financial statements for the period ended on June 30, 2018 it is planned that an amendment to the agreement with the audit company will be signed.

Due to the coming into force of the *law of May 11, 2017 on certified auditors, audit companies and public supervision*, the Audit Committee TAURON's Supervisory Board adopted the following regulations on October 16, 2017:

1) *Policy of selecting an audit company to conduct an audit and review of the financial statements and consolidated financial statements of TAURON Polska Energia S.A.,*
2) *Procedure of selecting an audit company to conduct an audit and review of the financial statements and consolidated financial statements of TAURON Polska Energia S.A., and*
3) *Policy of providing at TAURON Group, by an audit company conducting of an audit of the annual financial statements and consolidated financial statements of TAURON Polska Energia S.A., entities related to this audit company and a member of the audit company's network, of the permitted services that are not an audit.*

The above regulations in a clear manner define the principles and rules of the process of selecting an audit company to audit the Company's financial statements, as well as the principles of providing permitted services for the benefit of TAURON Capital Group's, in order to ensure independence of an audit company and certified auditors towards the Company and guarantee for the Company the provision of audit services of high subject matter quality, while meeting the required deadlines that the Company must comply with.

Principle of changing the Company and TAURON Capital Group's audit company

The principle of changing the Company's and TAURON Capital Group's audit company was changed in 2017. The following rule was established in the *Policy of selecting an audit company to conduct an audit and review of the financial statements and consolidated financial statements of TAURON Polska Energia SA*, adopted by the Audit Committee of the Company's Supervisory Board on October 16, 2017:

1). maximum period of continuous orders for audits to be conducted by the same audit company or an entity related to that audit company or any member of the network operating in the European Union countries that such audit companies are members of, shall not exceed 5 years,
2) after a 5-year duration of the order neither the audit company, nor any member of its network operating within the European Union shall conduct an audit of the Company for the subsequent 4 years,
3) a key certified auditor shall not conduct an audit of the Company for a period longer than 5 years,
4) a key certified auditor may again conduct an audit of the Company after at least 3 years have elapsed from the completion of the last audit.

Before that the principle adopted by the Supervisory Board of the Company on August 27, 2010 had been in force according to which the rule was adopted concerning changing of the entity authorized to audit the financial statements of the Company and TAURON Capital Group at least once every five 5 financial years. The entity authorized to audit the financial statements of the Company and TAURON Capital Group was able to perform these activities again after the elapse of two financial years.

6.4. Shareholders holding substantial blocks of shares

The below table presents shareholders holding, as of December 31, 2017 and as of the day of drawing up this report, directly or indirectly substantial blocks of the Company's shares.

Table no. 23. Shareholders holding, directly or indirectly, substantial blocks of shares

#	Shareholders	Number of shares held	Percentage share in share capital	Number of votes held	Percentage share in the total number of votes
1.	State Treasury	526 848 384	30.06%	526 848 384	30.06%
2.	KGHM Polska Miedź S.A.	182 110 566	10.39%	182 110 566	10.39%
3.	Nationale-Nederlanden Otwarty Fundusz Emerytalny	88 742 929	5.06%	88 742 929	5.06%

Since the day of publishing the previous periodical report, i.e. since November 8, 2017, until the day of publishing this report the Company did not receive any notifications from its shareholders on any changes in the ownership structure of substantial blocks of TAURON shares.

6.5. Holders of securities providing special control rights

The Company did not issue securities that would provide special control rights with respect to the Company.

6.6. Restrictions on exercising the voting right

Restrictions on exercising the right to vote are provided in § 10 of the Company's Articles of Association which are available on the Company's website http://www.tauron.pl/.

The above restrictions on exercising the voting right are formulated in the following way:

1. The voting right of shareholders holding over 10% of total votes in the company shall be limited so that none of them can exercise more than 10% of the total votes in the company at the General Meeting of Shareholders.
2. The restriction on exercising the voting right mentioned in clause 1 above shall not apply to the State Treasury and entities controlled thereby in the period during which the State Treasury, together with entities controlled thereby, hold a number of the company's shares that entitle them to exercise at least 25% of the total votes in the company.
3. Votes of shareholders who have a parent/subsidiary relationship in the understanding of § 10 of the Articles of Association (Shareholder Cluster) shall be aggregated; in case the aggregate number of their votes exceeds 10% of total votes in the company it shall be subject to reduction. Rules of votes' aggregation and reduction are defined in clauses 6 and 7 below.
4. A shareholder, in the understanding of § 10 of the Articles of Associations, shall be any party (entity), including its parent and subsidiary company, entitled directly or indirectly to a voting right at the General Meeting of Shareholders on the basis of any legal title; it shall also be applicable to a party (entity) that does not hold the company's shares, and in particular to a user, lien holder, party (entity) entitled on the basis of a depositary receipt under regulations of the Act of July 29, 2005 on financial instruments trading, as well as a party (entity) entitled to take part in the General Meeting of Shareholders in spite of disposing of its shares after the date of establishing (registering) the right to take part in the General Meeting of Shareholders.
5. A parent company and subsidiary company, for the purposes of § 10 of the Articles of Association, shall be understood, accordingly, as a party (entity):
   1) having the status of a controlling undertaking, controlled undertaking or, at the same time, both the status of a controlling undertaking and controlled undertaking in the understanding of the *Act of February 16, 2007 on the protection of competition and consumers*, or
   2) having the status of a parent company, higher level parent company, subsidiary company, lower level subsidiary company, co-controlled company or one that has both the status of a parent company (including a higher level parent company) and the status of a subsidiary (including a lower level subsidiary company and a co-controlled company) in the understanding of the *Act of September 29, 1994 on accounting*, or
   3) which has (parent company) or one which is under controlling influence (subsidiary company) in the understanding of the *Act of September 22, 2006 on transparency of financial relationships between public bodies and public undertakings and on financial transparency of some undertakings*, or
   4) whose votes due to the company's shares owned directly or indirectly are subject to aggregation with votes of another party (entity) or other parties (entities) on conditions defined in the *Act of July 29, 2005 on a public offering and conditions of introducing financial instruments to an organized trading system and on public companies* in connection with holding, disposing of or acquiring large blocks of the company's shares.
6. Aggregation of votes is based on totalling the number of votes held by individual shareholders that are members of the Shareholders' Cluster.
7. Reduction of votes involves decreasing the total number of votes in the company that shareholders that are members of the Shareholders' Cluster, are entitled to exercise at the General Meeting of Shareholders to the level of 10% of total votes in the company. Reduction of votes shall take place in accordance with the following rules:
   1) number of votes of a shareholder who holds the largest number of votes in the company among all shareholders that are members of the Shareholders' Cluster shall be reduced by a number of votes equal to a surplus above 10% of total votes in the company held by all shareholders that are members of the Shareholders' Cluster,
   2) if, despite the above mentioned reduction, the total number of votes that shareholders that are members of the Shareholders' Cluster are entitled to exceeds 10% of the total votes in the company, a further reduction of votes held by other shareholders that are members of the Shareholders' Cluster shall be made. The further reduction of individual shareholders' votes shall take place in an order established on the basis of the number of votes that

individual shareholders that are members of the Shareholders' Cluster hold (from the highest to the lowest one). The further reduction shall take place until the total number of votes held by shareholders that are members of the Shareholders' Cluster does not exceed 10% of the total votes in the Company,

3) in any case a shareholder whose voting rights have been reduced shall have the right to exercise at least one vote,
4) restriction on exercising the voting right shall also apply to a shareholder absent at the General Meeting of Shareholders.

8. Each shareholder who is going to take part in the General Meeting of Shareholders, in person or through a proxy, shall be obliged to, without a separate notice mentioned in clause 9 below, notify the Management Board or the Chairperson of the General Meeting of Shareholders that she/he holds, directly or indirectly, more than 10% of the total votes in the company.
9. Notwithstanding the provisions of clause 8 above, in order to establish the basis for aggregating and reducing the votes, a Company's shareholder, Management Board, Supervisory Board and individual members of such bodies shall have the right to demand that a shareholder of the Company provide information whether she/he is a party (entity) having the status of a parent or subsidiary company towards another shareholder in the understanding of § 10 of the Articles of Association. The entitlement mentioned in the preceding sentence shall also include the right to demand the revealing of the number of votes that the company's shareholder holds on its own or jointly with other shareholders of the Company.
10. A party (entity) that has failed to fulfill or has fulfilled the information obligation mentioned in clauses 8 and 9 above improperly, shall, until the failure to fulfill the information obligation has been remedied, be able to exercise its voting right with respect to one share only; exercising voting rights with respect to other shares by such party (entity) shall be null and void.

6.7. Restrictions on transfer of securities ownership right

As of December 31, 2017 and as of the day of drawing up this report TAURON's Articles of Association do not envisage limitations on the transfer of the Company's securities ownership right.
However, in accordance with the *law of July 24, 2015 on the control of some investments* an entity intending to purchase or achieve a material shareholding or purchase the dominating control over TAURON, which is an entity subject to protection, shall, each time, be obligated to submit a notification to the control body – Minister of Energy of its intention to do so, unless such obligation rests on other entities.

6.8. Rules on appointing and dismissing managing and supervising persons and their powers

6.8.1. Management Board

Rules on appointing and dismissing members of the Management Board

Management Board of the company shall be composed of one to six persons, including the President and Vice Presidents. Members of the Management Board shall be appointed and dismissed by the Supervisory Board for a common term of office lasting 3 years, except for the 1st term that lasted 2 years.

Each of the Management Board members can be dismissed or suspended in office by the Supervisory Board or the GM.

In order to recruit a person with whom an agreement on performing the management board level function at the Company, Supervisory Board announces the competition and conducts a qualification procedure for the position of the President or Vice President aimed at verifying and assessing the candidates' qualifications and selecting the best candidate. A candidate for a member of the Management Board must meet the requirements set forth in §16 clauses 3 and 4 of the Company's Articles of Association. The announcement of the qualification process is published on the Company's web site and in the Public Information Bulletin of the Ministry of Energy. The Company notifies the shareholders of the results of the qualification procedure.

Management Board's competence

Management Board shall conduct the company's affairs and represent the company in all court and out of court proceedings. Any matters related to conducting the Company's affairs, not assigned, based on the legal regulations or the provisions of the Articles of Association, to the scope of competence of the General Meeting of Shareholders or Supervisory Board, shall be within the scope of competence of the Management Board.

In accordance with the Articles of Association, all issues which go beyond the regular scope of the Company's activities shall require a resolution of the Management Board, in particular, the following issues listed in the below table:

Table no. 24. Management Board's competence

Matters that require a resolution of the Management Board
as of December 31, 2017 and as of the day of drawing up this report

1. Management Board bylaws,
2. company's organizational regulations,
3. establishment and liquidation of branches,
4. appointment of a proxy,
5. taking on credits and loans,
6. approving annual material and financial plans of the company and of the Capital Group as well as the Capital Group's Corporate Strategy,
7. assuming contingent liabilities in the understanding of the *Act of September 29, 1994 on accounting*, including granting guaranties and sureties by the company as well as issuing bills of exchange, subject to § 20 clause 2 item 4 and 5 of the company's Articles of Association,
8. making donations, cancelling interest or releasing from debt, subject to § 43 clause 3 items 1 and 2 of the company's Articles of Association,
9. purchase of real estate, perpetual usufruct or shares in real estate or in perpetual usufruct, subject to § 20 clause 2 item 1 of the company's Articles of Association,
10. purchase of fixed assets excluding real estate, perpetual usufruct or share in real estate or perpetual usufruct with the value equal to or exceeding the PLN equivalent of EUR 10,000, subject to the provisions of § 20 clause 2 item 2 of the Company's Articles of Association,
11. disposal (control) of fixed assets including real estate, perpetual usufruct or share in real estate or perpetual usufruct with the value equal to or exceeding the PLN equivalent of EUR 10,000, subject to the provisions of § 20 clause 2 item 3 of the company's Articles of Association,
12. defining the way the voting right will be exercised at the General Meeting of Shareholders or the Meeting of Shareholders of companies in which the company holds shares, on matters within the scope of competence of the General Meeting of Shareholders or the Meeting of Shareholders of such companies, subject to the provisions of § 20 clause 3 item 9 of the company's Articles of Association,
13. rules of conducting sponsoring activities,
14. adoption of the annual plan of sponsoring activities,
15. matters which the Management Board refers to the Supervisory Board or the General Meeting of Shareholders for review.

6.8.2. Supervisory Board

Rules on appointing and dismissing members of the Supervisory Board

Supervisory Board shall be composed of five to nine persons, appointed for a common term of office lasting three years, except for the first term that lasted 1 year. In accordance with the Company's Articles of Association members of the Supervisory Board shall be appointed and dismissed by the General Meeting of Shareholders, subject to the following:

1) during the time when the State Treasury, together with the State Treasury controlled entities in the understanding of § 10 clause 5 of the Articles of Association, hold a number of the company's shares that entitle them to exercise at least 25% of the total votes in the company, the State Treasury, represented by the minister competent to handle the State Treasury's affairs, shall be entitled to appoint and dismiss members of the Supervisory Board in the number equal to half of the maximum number of members of the Supervisory Board defined in the Articles of Association (in case such number is not integral it shall be rounded down to an integral number, for example 4.5 shall be rounded down to 4) and increased by 1, provided that the State Treasury:

   a) shall be obliged to vote at the General Meeting of Shareholders on establishing the number of members in the Supervisory Board that would correspond to the maximum number of members of the Supervisory Board defined in the Articles of Association in case such a motion is submitted to the Management Board by a shareholder or shareholders who hold a number of votes that entitle them to exercise at least 5% of the total number of votes in the Company,

   b) shall be excluded from the voting at the General Meeting of Shareholders on appointing and dismissing other members of the Supervisory Board, including independent members of the Supervisory Board; this shall not, however, apply to the case when the Supervisory Board cannot act due to its membership being smaller than required by the Articles of Association, and the shareholders present at the General Meeting of Shareholders, other than the State Treasury, do not supplement the membership of the Supervisory Board in accordance with the distribution of seats in the Supervisory Board defined in this section;

2) during the time when the State Treasury, together with the State Treasury controlled entities in the understanding of § 10 clause 5 of the Articles of Association, hold a number of the company's shares that entitle them to exercise less than 25% of the total number of votes in the company, the State Treasury, represented by the minister competent to handle the State Treasury's affairs, shall be entitled to appoint and dismiss one member of the Supervisory Board.

3) appointing and dismissing members of the Supervisory Board by the State Treasury pursuant to the above mentioned clause 1) or 2) shall take place by means of a statement submitted to the Company.

In accordance with the Best Practice at least two members of the Supervisory Board shall meet the criteria of independence. Phrase an "independent member of the Supervisory Board" shall denote an independent member of the Supervisory Board in the understanding of Appendix II to the *European Commission's Recommendation of February 15, 2005 related to the role of non-executive directors or members of a supervisory board of publicly listed companies and a supervisory board's committee* (2005/162/EC).

Members of the Supervisory Board shall submit to the Company, prior to their appointment as members of the Supervisory Board, a written statement on compliance with the independence criteria. In case a situation occurs where the independence criteria are not complied with a member of the Supervisory Board shall be obligated to forthwith inform the company thereof. The company shall inform shareholders of the up to date number of independent members of the Supervisory Board.

Supervisory Board's competence

Supervisory Board shall continuously oversee the Company's activities in all areas of its operations.

According to the Company's Articles of Association the Supervisory Board's tasks and competences shall include in particular the matters listed in the below table.

Table no. 25. Supervisory Board's competence

Matters that require a resolution of the Supervisory Board
as of December 31, 2017 and as of the day of drawing up this report
Competences related to providing opinions

1. evaluate the Management Board's report on the company's operations (Directors' Report) as well as the financial statements for the last financial year with respect to their compliance with books, documents as well as with the actual status. This shall also apply to the Capital Group's consolidated financial statements, provided they are prepared,
2. evaluate the Management Board's recommendations on profit distribution or loss coverage,
3. submit a written report to the General Meeting of Shareholders on the outcome of activities covered in clauses 1 and 2,
4. prepare once a year and submit to the General Meeting:
   a) evaluation of the company situation, including the assessment of the internal control, risk management systems, compliance and internal audit functions, including all significant control mechanisms, in particular, those related to financial reporting and operations,
   b) 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 fulfillment of information obligations by the Company, in relation to the application of corporate governance principles defined in the Regulations of the Exchange and provisions related to current and periodical information submitted by issuers of securities,
   d) assessment of rationality of sponsoring, charitable policy, or other similar policy pursued by the Company, or information concerning the lack of such policy,
5. prepare, along with the report on the results of the Company's annual financial statements' evaluation, the Supervisory Board's opinion on the financial viability of the company's capital investments in other commercial law entities made in the given financial year,
6. provide opinions on the Capital Group's Corporate Strategy,
7. provide opinions on the rules of conducting sponsoring activities,
8. provide opinions on the annual plan of conducting sponsoring activities as well as on the annual report on its implementation,
9. provide opinions on the reports prepared, by the Management Board, on entertainment expenses, expenditures on legal services, marketing services, public relations and social communications service as well as advisory services related to management,
10. provide opinions on the changes of the rules of divesting fixed assets, defined in § 38[1] of the Company's Articles of Association.

Competences that include

Matters that require a resolution of the Supervisory Board

1. selecting a certified auditor to carry out an audit of the company's financial statements and the Capital Group's consolidated financial statements,
2. defining the scope and deadlines for submitting the company's and the Capital Group's annual material and financial plan by the Management Board,
3. adopting the consolidated text of the company's Articles of Association, prepared by the company's Management Board,
4. approving the Management Board's bylaws,
5. approving the organizational regulations of the company's enterprise,
6. purchasing real estate, perpetual usufruct or shares in real estate or in perpetual usufruct with the value exceeding the PLN equivalent of EUR 5,000,000, except for real estate, perpetual usufruct or shares in real estate or in perpetual usufruct purchased from the Capital Group's subsidiaries,
7. purchasing fixed assets, excluding real estate, perpetual usufruct or share in real estate or perpetual usufruct, bonds issued by the Capital Group's subsidiaries and other fixed assets purchased from the Capital Group's subsidiaries of the value exceeding the PLN equivalent of EUR 5,000,000,
8. disposing of fixed assets, including real estate, perpetual usufruct or share in real estate or perpetual usufruct, of the value equal to or exceeding the PLN equivalent of EUR 5,000,000, except for real estate, perpetual usufruct or shares in real estate or in perpetual usufruct, and also other fixed assets that as a result of disposing will be sold or encumbered in favor of the Capital Group's subsidiaries,
9. assuming contingent liabilities, including granting guaranties and sureties by the company with the value exceeding the PLN equivalent of EUR 5,000,000,
10. issuing bills of exchange of the value exceeding the PLN equivalent of EUR 5,000,000,
11. making an advance payment on account of the expected dividend,
12. taking over or purchasing shares in other companies than the Capital Group's subsidiaries with the value exceeding the PLN equivalent of EUR 5,000,000, except for situations when taking over shares in such companies takes place in exchange for the company's liabilities as a part of composition or bankruptcy proceedings,
13. selling shares with the value exceeding the PLN equivalent of EUR 5,000,000 along with defining the conditions and procedure to be applied in their sale, except for:
    a) selling shares which are traded on the regulated market,
    b) selling shares that the company holds in the amount not exceeding a 10% interest in the share capital of particular companies,
    c) selling shares in favor of the Capital Group's subsidiaries,
14. concluding a material agreement with a shareholder holding at least 5% of the total number of votes in the Company or a related company, with a proviso, that this obligation shall not cover typical transactions and concluded at arm's length as part of the business operations conducted by the Company with entities that are members of TAURON Capital Group,
15. concluding an agreement on legal services, marketing services, public relations and social communications services as well as advisory services related to management, if the amount of total net compensation for the services provided exceeds PLN 500 000, on a yearly basis,
16. amending an agreement on legal services, marketing services, public relations and social communications services as well as advisory services related to management, increasing the compensation above the amount mentioned in the above clause j,
17. concluding an agreement on legal services, marketing services, public relations and social communications services as well as advisory services related to management, under which the maximum compensation amount is not envisaged,
18. concluding a donation agreement or another agreement with similar consequences of the value exceeding PLN 20 000 or 0.1% of the total assets in the understanding of the *law of September 29, 1994 on accounting*, determined on the basis of the last approved financial statements,
19. relieving from debt or from another agreement with similar consequences of the value exceeding PLN 50 000 or 0.1% of the total assets in the understanding of the *law of September 29, 1994 on accounting*, determined on the basis of the last approved financial statements,
20. granting a permission to establish the company's branches abroad,
21. defining the way of exercising the voting right at the General Meeting of Shareholders or at the Meeting of Shareholders of companies in which the company holds more than 50% of shares, with respect to the following matters:
    a) selling and leasing out the company's enterprise or its organized part as well as establishing a limited proprietary right on them if their value exceeds the PLN equivalent of EUR 5 000 000,
    b) dissolving and liquidating the company.
22. defining the manner of exercising the voting right by a representative of TAURON during the GMs of companies (subsidiaries) with respect to which the Company is a dominating entrepreneur in the understating of art. 4 section 3 of the *law of February 16, 2007 on competition and consumer protection*, with respect to the following issues:
    a) company setting up another company,
    b) change to the Articles of Association or the shareholders agreement and the subject of the company's operations,
    c) merging, transforming, splitting, dissolving and liquidating the company,
    d) increasing or decreasing the company's share capital,
    e) selling and leasing out the company's enterprises or its organized part and establishing a limited property right thereupon,
    f) redeeming (retiring) of shares,

Matters that require a resolution of the Supervisory Board
g) setting the compensation of members of Management Boards and Supervisory Boards, h) provision on claims for remedying damage inflicted when setting up the company or performing management or supervision, i) matters mentioned in art. 17 *of the law of December 16, 2016 on the principles of managing state property,* subject to § 15 clause 4 of the Company's Articles of Association, 23. approving compensation policy for the capital group.
Competences related to the Management Board
1. appoint and dismiss members of the Management Board, 2. establish the rules of compensation and the amounts of compensation for the members of the Management Board, subject to § 18 of the Company's Articles of Association, 3. suspend members of the Management Board from office for important reasons, 4. delegate members of the Supervisory Board to temporarily perform duties of the members of the Management Board who cannot perform their duties and establish their compensation subject to the provision that the total compensation of the delegated person as a Member of the Supervisory Board's as well as on account of being delegated to temporarily perform duties of a Member of the Management Board shall not exceed the compensation established for the Member of the Management Board to replace whom the Member of the Supervisory Board was delegated, 5. conduct a recruitment process for the position of a Member of the Management Board, 6. conduct a competition in order to select a person with whom an agreement to perform the management board functions in the Company shall be concluded and conclude such agreement to perform the management board functions in the Company, 7. grant a permission to Members of the Management Board to take positions in governing bodies of other companies.
Other competences of the Company's Supervisory Board
1. prepare reports on overseeing the implementation of investment projects by the Management Board, including fixed asset purchases, and in particular provide opinions on the correctness and effectiveness of expenditures related thereto, 2. approve the Management Board's annual report on the supervision over the implementation of investment projects, 3. pass regulations describing in detail the Supervisory Board's procedures.

6.9. Description of the procedure of amendment of the Company's Articles of Association

Amendments to the Company's Articles of Association in accordance with the provisions of the Ksh, in particular: amendments to the Company's Articles of Association take place by means of resolution of the GM, at the majority of two thirds of the votes, and then requires issuing a decision by a proper court on entering the change into the register of entrepreneurs. The consolidated text of the Company's Articles of Association, including amendments passed by the General Meeting, shall be adopted by the Supervisory Board by means of a resolution.

In accordance with the Company's Articles of Association, a material amendment to the subject of activities requires two thirds of votes under the presence of persons representing at least a half of the share capital.
Ordianary GM on May 29, 2016 adopted the resolutions concerning amendments to the Company's Articles of Association; the relevant information s provided in section 2.8. of this report.

6.10. Procedures of the General Meeting of Shareholders, its fundamental powers and description of shareholders' rights and the manner of exercising thereof

The Company's General Meeting of Shareholders' procedures and its empowerments are defined in the company's Articles of Association and in the Regulations of the General Meeting of Shareholders of TAURON Polska Energia S.A. which are available on the Company's website http://www.tauron.pl/.

Procedures of the General Meeting of Shareholders

General Meeting of Shareholders shall be convened by a notice published on the company's website and in a manner defined for providing current information by public companies. In case the General Meeting is convened by an entity or a body other than the Management Board on the basis of regulations of the Code of Commercial Companies, as convening a General Meeting of Shareholders requires the Management Board's cooperation, the Management Board shall be obligated to perform any activities required by law in order to convene, organize and conduct General Meetings of Shareholders that take place either at the Company's seat or in Warsaw.

General Meeting of Shareholders shall be opened by the Chairperson of the Supervisory Board, and in case he/she is absent the following persons shall be entitled to open the General Meeting of Shareholders in the given order: Vice Chairperson of the Supervisory Board, President of the Management Board, a person designated by the Management Board or the shareholder who registered at the General Meeting of Shareholders such number of shares that provide the right to exercise the highest number of votes. Then, the chairperson of the General Meeting of Shareholders shall be elected from among persons entitled to participate in the General Meeting of Shareholders.

General Meeting of Shareholders shall pass resolutions irrespective of the number of shares represented at the Meeting, unless regulations of the Code of Commercial Companies, as well as provisions of the company's Articles of Association state otherwise. General Meeting of Shareholders may order a break in the meeting by the majority of two thirds of votes. The breaks shall not exceed 30 days in total.

A break in the GM session may take place only in exceptional situations indicated on a case-by-case basis in the justification to the resolution, prepared based on reasons presented by a shareholder requesting the announcement pf the break.

The GM resolution concerning a break shall clearly indicate the date of resumption of the session, however, such a date must not create a barrier for participation of the majority of shareholders in resumed meeting, including minority shareholders.

Competence of the General Meeting of Shareholders

In accordance with the Company's Articles of Association the matters listed in the below table shall require a resolution of the General Meeting of Shareholders.

Table no. 26. Competence of the General Meeting of Shareholders

Matters that require a resolution of the General Meeting of Shareholders
as of December 31, 2017 and as of the day of drawing up this report
1. reviewing and approving the financial statements of the Company and the consolidated financial statements of TAURON Capital Group for the previous financial year for the previous financial year as well as the Management Board's report on the Company's operations (Directors' Report) and the Management Board's report on the operations of TAURON Capital Group 2. granting the acknowledgement of the fulfillment of duties to the members of the Company's corporate bodies, 3. profit distribution and coverage of loss, 4. appointing and dismissing members of the Supervisory Board, 5. suspending members of the Management Board in performance of their duties, 6. establishing the amount of compensation for members of the Supervisory Board, subject to § 29 clause 4 of the company's Articles of Association, 7. establishing the principles of determining compensation and the amount of compensation of members of the Management Board taking into account the provisions of the *law of June 9, 2016 on the principles of determining compensation of persons managing some companies*, 8. selling and leasing out the company's enterprise or its organized part as well as establishing a limited proprietary right on them, 9. concluding a credit, loan, surety agreement or any other similar agreement by the company with a member of the Management Board, Supervisory Board, proxy, liquidator or for the benefit of any such person. Concluding a credit, loan, surety or any other similar agreement by a subsidiary with a member of the Management Board, Supervisory Board, proxy, liquidator or for the benefit of any such person, 10. increasing and decreasing the company's share capital, 11. issuing convertible bonds or senior bonds as well as registered securities or bearer securities entitling their holder to subscribe or acquire the shares, 12. purchasing of treasury shares in cases required by the regulations of the Code of Commercial Companies, 13. mandatory redemption of shares (squeeze-out) in accordance with the provisions of art. 418 of the Code of Commercial Companies, 14. setting up, using and liquidating reserve capitals, 15. using supplementary capital, 16. provisions related to claims to repair damage caused while establishing the company or serving on the management board or performing supervision, 17. merger, transformation and division of the company, 18. redemptions (retirements) of shares, 19. amendment to the Articles of Association and change of the subject of the Company's operations, 20. dissolving and liquidating the company.

In accordance with the provisions of the CCC the decision on issue and repurchase of shares in included within the competence of the General Meeting.

Description of shareholders' rights and the manner of exercising thereof

Description of the Company's shareholders' rights related to the General Meeting of Shareholders in accordance with the Company's Articles of Association, Code of Commercial Companies and the *Regulations of the General Meeting of Shareholders of TAURON Polska Energia S.A.* is presented in the below table.

Table no. 27. Description of the shareholders' rights related to the General Meeting of Shareholders

#	Shareholders' rights	Description of shareholders' rights
1.	Convene a General Meeting of Shareholders	Shareholders representing at least one twentieth of the share capital, may request convening of an Extraordinary General Meeting of Shareholders. Such request should include a concise justification. It may be submitted to the Management Board in writing or in an electronic form, to the company's e-mail address, provided by the company on its website under the "Investor Relations" tab. Shareholders representing at least a half of the share capital or at least a half of all votes in the company may convene an Extraordinary General Meeting of Shareholders and appoint a chairperson of such General Meeting.
2.	Include matters (items) in the agenda of the General Meeting of Shareholders	Shareholders representing at least one twentieth of the share capital, may request that certain matters (items) be included in the agenda of the forthcoming General Meeting of Shareholders. Such request, including a justification or a draft resolution related to the proposed item of the agenda, should be submitted to the Management Board not later than 21 days prior to the set date of the General Meeting of Shareholders in electronic form to the company's e-mail address or in writing to the company's address.
3.	Become acquainted with the list of shareholders	Shareholders may become acquainted with the shareholders' list at the company's Management Board's seat for three weekdays preceding directly the General Meeting of Shareholders. Shareholders may also request that the list of shareholders be sent to them free of charge by electronic mail, providing the address to which the list should be sent.
4.	Participate in the General Meeting of Shareholders	Only persons who are Shareholders sixteen days before the date of the General Meeting of Shareholders (date of registering to participate in the General Meeting of Shareholders) shall have the right to take part in the General Meeting of Shareholders. In order to participate in the General Meeting shareholders should submit a request to issue a name bearing affidavit on the right to take part in the General Meeting of Shareholders to an investment (brokerage) company running their securities account. Such request should be submitted not earlier than following the announcement on convening of the General Meeting of Shareholders and not later than on the first weekday following the day of registering the participation in the General Meeting of Shareholders.
5.	Represent a shareholder by a proxy	Shareholders may take part in the General Meeting of Shareholders as well as exercise the voting right in person or through a proxy. Shares' co-owners may take part in the General Meeting of Shareholders and exercise the voting right only through a joint representative (proxy). A proxy may represent more than one shareholder and vote differently based on shares of each shareholder..
6.	Elect the Chairperson of the General Meeting of Shareholders	Shareholders shall elect the Chairperson of the General Meeting of Shareholders from among the persons entitled to take part in the General Meeting of Shareholders. Each of the participants of the General Meeting of Shareholders shall have the right to propose one candidate for the post of the Chairperson. Chairperson shall be elected by a secret ballot, by an absolute majority of votes. In case there is just one candidate for the Chairperson, election can take place by acclamation.
7.	Elect the Returning Committee	Each shareholder may propose no more than three candidates for members of the Returning Committee to be elected by the General Meeting of Shareholders, and vote for three candidates maximum.
8.	Submit a draft resolution	During the General Meeting of Shareholders a shareholder shall have the right, until the discussion on a certain item of the agenda is closed, to submit a proposal of changes to the content of a draft resolution proposed for adoption by the General Meeting of Shareholders, as part of the given item of the agenda, or put forward his/her own draft of such resolution. Proposals of changes or draft resolutions, including justifications, may be submitted in writing to the Chairperson or verbally to be recorded in the minutes of the meeting.
9.	Raise an objection	Shareholders who voted against a resolution and, after the General Meeting of Shareholders has adopted it, want to raise their objection, should, immediately after the results of the voting have been announced, raise their objection and request it be included in the minutes of the meetings before proceeding to the next item of the agenda. In case such objection is raised later, which however shall not take place later than by the time the General Meeting of Shareholders is closed, the shareholders shall indicate against which resolution passed by the General Meeting they are raising their objection. Shareholders raising their objection against a resolution of the General Meeting may request their concise justification of the objection be recorded in the minutes of the meeting.

6.11. Composition of the Company's managing and supervising bodies and their committees, its changes, description of operation

6.11.1. Management Board

The current, fifth term of office of the Management Board began its run on March 16, 2017, i.e. on the day of appointing the Management Board of the Company for the fifth common term of office. In accordance with the Company's Articles of Association the common term of office shall last 3 years.

Composition of the Management Board as of December 31, 2017 and as of the day of drawing up this report

1. Filip Grzegorczyk - President of the Management Board,
2. Jarosław Broda - Vice-President of the Management Board for Asset Management and Development,
3. Kamil Kamiński - Vice-President of the Management Board for Customer and Corporate Support,
4. Marek Wadowski - Vice-President of the Management Board for Finance.

Changes to the Management Board's composition in 2017 and in the period up to the day of drawing up this report

As of January 1, 2017 the Management Board was composed of the following members: Filip Grzegorczyk (President of the Management Board), Jarosław Broda (Vice-President of the Management Board), Kamil Kamiński (Vice-President of the Management Board), Marek Wadowski (Vice-President of the Management Board) and Piotr Zawistowski (Vice-President of the Management Board).

On March 15, 2017 the Company's Supervisory Board dismissed, effective as of the end of day on March 15, 2017, all members of the Company's Management Board. On the same day Piotr Zawistowski up to then performing the function of Vice-President of the Management Board for Customer and Trade provided the Supervisory Board with the information on the resignation from applying for being selected to be a member of TAURON's Management Board of the 5th common term of office. The other members of the Management Board were appointed as of March 16, 2017 to the Company's Management Board of the 5th common term of office.

There were no other changes to the composition of the Management Board by the day of publishing this report

Experience and competences of members of the Management Board

Filip Grzegorczyk - President of the Management Board

A graduate of the Faculty of Law and Administration and the Faculty of International and Political Studies of the Jagiellonian University in Cracow where the obtained a PhD degree in the EU law, and then a post-PhD degree in the business law.

He also completed the Summer Advanced Course program in the European Law at the University of London, King's College, Centre of European Law as well as the International Business and Trade Summer School program at Catholic University of America – Columbus School of Law and the Ecole de droit français Université d'Orléans. He holds the position of Professor at the University of Economics in Cracow, where he is a lecturer at the Faculties of Management and Economics and International Relations.

He has broad professional experience in the energy and fuel sector. In 2011-2013 he was associated with Kompania Węglowa as a management board proxy for energy sector development at Kompania Węglowa S.A. In 2007-2008 he was a member of the Management Board of TAURON. From November 2015 he served as the Undersecretary of State at the Ministry of State Treasury. He speaks fluent English and French.

He has been holding the position of the President of the Management Board of TAURON Polska Energia S.A. since November 15, 2016. He is currently overseeing the following areas of the operations: strategic management and regulatory solutions, relationships with the environment (stakeholders), legal support and investor relations, risk management, legal and internal audit, security and compliance as well as human resources development and social dialogue policy.

Jarosław Broda - Vice-President of the Management Board

A graduate of the Warsaw School of Economics, a holder of a postgraduate diploma in project management from the Kozmiński University.

He has experience in the area of consolidation and operation of the energy sector, privatization of state-owned utility groups, developing processes associated with the restructuring and strategy building as well as energy entities' expansion projects.

Since the beginning of his professional career he has been associated with the energy sector's entities, holding senior executive and managerial positions. He gained his professional experience working at the Ministry of State Treasury as well as at TAURON and GDF Suez Energia Polska. Recently associated with GDF Suez Energia Polska – Katowice and GDF Suez (Branch Energy Europe) where he was responsible for market analyses and developing the company's expansion strategy, regulatory management and M&A projects. He was also involved in developing the sales and marketing expansion strategy in Europe. Since mid-2015 he was responsible for developing the commercial strategy and the contract for difference related to the nuclear project in Great Britain.

He has been holding the position of the Vice-President of the Management Board of TAURON Polska Energia S.A. since December 8, 2015. He is currently overseeing the following areas of the operations: asset management, research and innovation, investment projects and programs as well as occupational health and safety.

Kamil Kamiński - Vice-President of the Management Board

A graduate of the Faculty of Management and Social Communications of the Jagiellonian University. A holder of the MBA Executive diploma (Stockholm University School of Business/ Cracow University of Economics) and the Post-MBA Diploma in Strategic Financial Management (Rotterdam School of Management, Erasmus University/ GFKM).

He has experience in the area of building company value, mergers and acquisitions, business integration and strategy operationalization as well as management of comprehensive projects in the public and private sectors. He was involved in complex transformation and restructuring processes of enterprises in the energy and fuel as well as transportations logistics sectors.

He gained his professional experience acting in the capacity of the President or Vice-President of the Management Board and holding senior managerial positions. From the beginning of 2014 he was associated with Węglokoks Capital Group where, within the structures of Węglokoks Energia, he participated in the consolidation of electricity and heat generation assets of Kompania Węglowa and Węglokoks. At that time he was the head of the Management Committee. Previous professional experience includes, among others, work at the Research and Development Centre of the Refining Industry (OBR) in Płock or Jan Paweł II International Cracow-Balice Airport. He also managed the operations of John Menzies PLC in Poland. For many years he cooperated with Lotos Group where he supported the development of the aviation fuel segment which resulted in the *joint venture* with Air BP Ltd. and the establishment of Lotos Air BP.

He has been holding the position of the Vice-President of the Management Board of TAURON Polska Energia S.A. since December 8, 2015. He is currently overseeing the following areas of the operations: corporate management, human resources, marketing strategy and customer relations, IT systems functioning and management, personal data protection as well as procurement and administration.

Marek Wadowski – Vice President of the Management Board

A graduate of the Faculty of Economics of the University of Economics in Katowice. He also completed post graduate studies at École Supérieure de Commerce Toulouse where he obtained Mastère Spécialisé en Banque et Ingéniere Financière diploma and the Executive MBA studies at the Kozminski University in Warsaw.

He has professional experience in the field of financial, controlling and accounting process management in industry (power sector, mining, steel industry), as well as in financing of investment projects and international commercial transactions. He was involved in the implementation of the *due diligence* projects and valuations of many enterprises (using income-based, equity and comparison valuation methods). From the beginning of his professional career he was associated with the energy, mining and steel sector entities, acting in the capacity of the President or the Vice-President of the Management Board and holding senior managerial positions. He gained his professional experience working at BRE Corporate Finance S.A., Huta Cynku Miasteczko Śląskie S.A. and at Jastrzębska Spółka Węglowa S.A. Capital Group's subsidiaries. From 2008, acting in the capacity of the Vice-President of the Management Board in charge of the financial division at Jastrzębska Spółka Węglowa S.A. Capital Group's subsidiaries, he was responsible, inter alia, for structuring commercial transactions, implementing the foreign exchange risk hedging policy, financial costs reduction, liquidity management, acquiring funds from the consortium of banks in the form of a bond issue program. He was also involved in the IPO of JSW S.A. (implementation of the International Accounting Standards, modification of the management information system, preparing the IPO prospectus, talks with investors). He held the position of the President of the Management Board at Towarzystwo Finansowe Silesia where he was involved in the bond issue program for Kompania Węglowa and was dealing with the acquisition of debt financing from the consortium of banks.

He has been holding the position of the Vice-President of the Management Board of TAURON Polska Energia S.A. since January 29, 2016. He is currently overseeing the following areas of the operations: finance and insurance policy, controlling and planning, analyses, accounting and tax policy. Additionally, until the Vice-President of the Management Board for Commercial Affairs is appointed, he also oversees the following areas: electricity and property rights trading, fuel trading, portfolio management and electricity tradinginance, controlling, business analyses, accounting and taxes, risk and IT.

The description of the experience and competences of the members of the Management Board is published on the Company's website http://www.tauron.pl/.

Description of the operations

Management Board of the company shall act on the basis of the Code of Commercial Companies and other legal regulations, provisions of the company's Articles of Association and provisions of the *Bylaws of the Management Board of TAURON Polska Energia Spółka Akcyjna with its seat in Katowice* which are available on the company's website http://www.tauron.pl/. When performing their duties members of the Management Board shall be acting in accordance with the principles included in Best Practice 2016.

2 members of the Management Board or one member of the Management Board together with a proxy shall be entitled to make valid statements on behalf of the Company. In case the Management Board includes one person, one member of the Management Board or a proxy shall be entitled to make valid statements on behalf of the Company.

Meetings of the Management Board shall be convened by the President of the Management Board or a Vice President of the Management Board designated thereby. Meetings of the Management Board shall also be convened on the motion of the majority of Vice Presidents of the Management Board as well as on the motion of the Chairperson of the Supervisory Board. The meetings shall be held at the company's seat on the date set by the person that convened the meeting. In justified cases the Management Board's meetings may be held outside the company's seat. The President of the Management Board or a Vice President of the Management Board designated thereby shall chair the meetings of the Management Board.

Management Board shall vote in an open ballot. The result of the ballot shall be recorded in the minutes of the meeting. President of the Management Board shall order a secret ballot at the request of any Vice President of the Management Board.

Resolutions of the Management Board shall be passed by an absolute majority of votes in the presence of 3/5 of the members of the Management Board. In case of an equal number of votes the President of the Management Board shall have a casting vote. Management Board may pass resolutions by voting in writing or using means of direct remote communications. Voting in accordance with the above procedures shall be ordered by the President of the Management Board or a Vice President of the Management Board designated thereby, including setting the deadline for casting votes by members of the Management Board. Submission of a dissenting opinion shall be allowed. Such dissenting opinion shall be recorded in the minutes of the meeting, including the justification thereof. Decisions of the Management Board related to ongoing issues that do not require passing of a resolution shall be recorded solely in the minutes of the meeting.

In case there are fewer members of the Management Board than the foreseen number of divisions (areas of responsibility), members of the Management Board may combine performing duties related to managing two divisions or introduce a different split of competences that would not be in conflict with the assignment of competences made by the Supervisory Board.

The internal divisi on, among members of the Management Board, of the tasks and responsibilities for the individual areas of the Company's operations (Divisions) defined in the *Organizational Regulations of TAURON Polska Energia S.A.* and including the independent work positions (jobs) as well as organizational units reporting to the individual Members of the Management Board and supervised thereby, shall be defined by the above Organizational Regulations, while the diagram showing the above mentioned division is published on the Company's website.

The structure of the divisions reporting to the individual Members of the Management Board is defined on the diagram (flowchart) of the Company's organizational structure, described in section 8.1.2. of this report.

6.11.2. Supervisory Board

The current, fifth term of office of the Supervisory Board, began on May 29, 2017, i.e. on the day of holding the Ordinary GM of the Company approving the financial statements for the last full financial year of the tenure of the members of the Supervisory Board of the fourth term, i.e. for the financial year 2016. In accordance with the Company's Articles of Association it shall be a common term of office and it shall last for 3 years.

The composition of the Supervisory Board as of December 31, 2017 and as of the date of drawing up this report

1. Beata Chłodzińska - Chair of the Supervisory Board,
2. Teresa Famulska - Deputy Chair of the Supervisory Board,
3. Jacek Szyke - Secretary of the Supervisory Board,
4. Radosław Domagalski - Łabędzki - Member of the Supervisory Board,
5. Katarzyna Łasak- Jarszak - Member of the Supervisory Board,
6. Paweł Pampuszko - Member of the Supervisory Board,
7. Jan Płudowski - Member of the Supervisory Board,
8. Agnieszka Woźniak - Member of the Supervisory Board.

Changes to the Supervisory Board's membership in 2017

As of January 1, 2017 the Supervisory Board was composed of the following members: Beata Chłodzińska (Chair of the Supervisory Board), Anna Mańk (Vice-Chair of the Supervisory Board), Jacek Szyke (Secretary of the Supervisory Board), Stanisław Bortkiewicz (Member of the Supervisory Board), Leszek Koziorowski (Member of the Supervisory Board), Jan Płudowski (Member of the Supervisory Board), Jacek Rawecki (Member of the Supervisory Board), Stefan Świątkowski (Member of the Supervisory Board) and Agnieszka Woźniak (Member of the Supervisory Board).

On May 25, 2017 Jacek Rawecki submitted a statement on the resignation, as of May 26, 2017, from the function of a member of the Company's Supervisory Board.

On May 29, 2017 the State Treasury, acting within its personal powers defined in § 23, clause 1, sections 1) and 3) of the Company's Articles of Association, appointed the following persons to be the members of the Company's Supervisory Board of the 5th common term of office: Beata Chłodzińska, Teresa Famulska, Barbara Katarzynę Łasak-Jarszak, Jan Płudowski i Agnieszka Woźniak.

On May 29, 2017 the Ordinary GM of the Company appointed the following persons to be the members of the Company's Supervisory Board of the 5th common term of office: Radosław Domagalski – Łabędzki, Paweł Pampuszko and Jacek Szyke.

There were no other changes to the composition of the Supervisory Board by the day of publishing this report.

Information on the independence of members of the Supervisory Board as of December 31, 2017

The independence requirements defined in the Best Practice and Appendix II to the *European Commission's Recommendation of February 15, 2005 related to the role of non-executive directors or members of a supervisory board of publicly listed companies and a supervisory board's committee* (2005/162/EC) are met by the following members of the Supervisory Board:

1) Teresa Famulska,
2) Barbara Łasak-Jarszak,
3) Paweł Pampuszko,
4) Jan Płudowski,
5) Jacek Szyke.

The other members of the Supervisory Board do not meet the independence requirements defined in the Best Practice.

As of the day of drawing up this report a member of the Supervisory Board, Beata Chłodzińska, met the independence requirements defined in the Best Practice.

Experience and competences of the members of the Supervisory Board

Beata Chłodzińska - Chair of the Supervisory Board

A graduate of the Faculty of Law and Administration of the Warsaw University. She is a licensed legal counsel.

In 2001-2016 she was associated with the Ministry of State Treasury where she was providing legal services, most recently as the Deputy Director at the Legal and Litigation Department. She is currently working at PKN Orlen S.A. in the legal area.

She gained professional experience associated with supervising the operations of the State Treasury owned companies by, among others, holding seats on the supervisory boards of the following companies: Polska Agencja Prasowa S.A. with its seat in Warsaw, Centrum Techniki Okrętowej S.A. with its seat in Gdańsk, Chemia Polska sp. z o.o. with its seat in Warsaw, Międzynarodowa Korporacja Gwarancyjna sp. z o.o. with its seat in Warsaw.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since August 12, 2015. In the Supervisory Board of the 5th common term of office she is the Chair of the Supervisory Board, the Head of the Nominations and Compensation Committee of the Supervisory Board, as well as a member of the Audit Committee of the Supervisory Board and a member of the Strategy Committee of the Supervisory Board.

Teresa Famulska - Deputy Chair of the Supervisory Board

A graduate of the University of Economics in Katowice, a Professor of economics appointed by the President of the Republic of Poland at the request of the Board of the Faculty of Finance and Insurance of the University of Economics in Katowice.

She has been associated with the University of Economics in Katowice since 1981. She is currently the Head of the Public Finance Department holding the full Professor's position. In 1998-2013 she was working at the School of Banking and Finance, recently as a dean, holding the full Professor's position.

An author of approximately 150 domestic and foreign publications in the field of finance, mainly public finance (including taxes and tax systems) and corporate finance. Apart from academic work she is continuously involved in business practice, participating, among others, in several dozen science and research projects. She conducts numerous lectures and training courses for the finance and management personnel of enterprises and for the tax authorities staff as part of the post-graduate studies and in cooperation with, among others, the Polish Economic Society (Polskie Towarzystwo Ekonomiczne) and the Accountants Association in Poland (Stowarzyszenie Księgowych w Polsce). Since 2007 she has been working at the State Examination Commission on Tax Advisory Services, where she has been the Head of the Commision since 2010. Since 2007 a member of the Financial Ediucation Committee of the Polish Academy of Science, where she was a member of the Board of the Committee in 2011-2015. Furthermore, she is a member of the Main Board of the Polish Finance and Banking Association (Zarząd Główny Polskiego Stowarzyszenia Finansów i Bankowości), International Fiscal Association, Center for Information and Organization of Public Finance and Tax Law Research of Central and Eastern European Countries (Centrum Informacji i Organizacji Badań Finansów Publicznych i Prawa Podatkowego Krajów Europy Środkowej i Wschodniej) and Polish Economic Society (Polskie Towarzystwo Ekonomiczne).

She was awarded the following orders and accolades: Silver Cross of Merit (Srebrny Krzyż Zasługi), Silver Medal for Long-term Service (Srebrny Medal za Długoletnią Służbę), Medal of the Commission of National Education (Medal Komisji Edukacji Narodowej), awards of the Minister of National Education and of the President of the University of Economics in Katowice.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2015. In the Supervisory Board of the 5th common term of office she is the Vice-Chair of the Supervisory Board and the Head of the Audit Committee of the Supervisory Board

Jacek Szyke - Secretary of the Supervisory Board

A graduate of Faculty of Economics of Łódź University and of the Faculty of Electric Engineering of the Technical University in Poznań where he also obtained a PhD in technical science.

He has yearslong professional experience associated with the utility scale power industry where he climbed up all levels of the career ladder, starting with an intern, through foreman, Head of the Safety and Instrumentation and & Control Department (Zakład Energetyczny Kalisz and Łódź), Engineer On Duty Responsible for the Operation (Elektrociepłownia Łódź), up to the position of the Chief Engineer (Zakład Energetyczny Łódź and Płock) and General Manager (Zakład Energetyczny Płock and Elektrociepłownia Siekierki). He also worked as the Contract Manager in Libya. The owner and President of the JES ENERGY consulting company.

State orders awarded: Golden Cross of Merit (Złoty Krzyż Zasługi), Knight's Order (Krzyż Kawalerski). Industry orders awarded: Distinguished for the following sectors: Power, Construction, Communications, Firefighting, Culture and Heat industry.

The author of more than 100 articles, publications and books, including: ”Wspomnienia o tradycji i zwyczajach pracy w energetyce” (Memories of traditions and customs related to working in the power utilities sector), ”O energetyce z sentymentem" (About electric utilities sector with a sentiment), ”Historia Polskiej Elektroenergetyki” (History of Poland's Power Industry), ”Złota Księga Elektroenergetyki” (Golden Book of Power Industry), ”Grupa TAURON - monografia” (TAURON Group – monograph).

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since September 14, 2010. In the Supervisory Board of the 5th common term of office he is the Secretary of the Supervisory Board and the Head of the Strategy Committee of the Supervisory Board as well as a member of the Audit Committee of the Supervisory Board.

Radosław Domagalski - Łabędzki - Member of the Supervisory Board

A graduate of Łódź University (master's degree in law). Completed Executive MBA studies at Rutgers University in New Jersey. Visiting fellow at the German Munster and Mannheim Universities.

A manager with a broad practical experience in managing complex international business projects. He prepared and effectively implemented an expansion strategy in Asia for one of Poland's largest capital groups.

In 2006-2013 the President of the Management Board of Magellan Trading Shanghai Co. Ltd in China. Prior to that he worked as a lawyer at GSP Group Sp. z o.o. in Łódź, and also at American Enterprise Institute in Washington – one of the largest American think-thanks.

Between December 2015 and October 2016 the Undersecretary of State at the Ministry of Development, responsible, among others, for promoting the Polish economy, a member of the Financial Supervision Commission (Komisja Nadzoru Finansowego).

Since October 2016 until March 10, 2018 he was the President of the Management Board of KGHM Polska Miedź S.A.

Co-founder of the Polish-Chinese Chamber of Industry and Commerce in Shanghai. An author of many business publications.

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2017. In the Supervisory Board of the 5th common term of office he is a member of the Audit Committee of the Supervisory Board.

Barbara Katarzyna Łasak - Jarszak - Member of the Supervisory Board

A graduate of the Faculty of Law and Administration of the Warsaw University.

Between January 1997 and February 2017 she was working at the Legal Department of the Ministry of State Treasury. Between April 1998 and February 2017 she headed an organizational unit of the Legal Department providing legal services for the Ministry. Since March 1 2017 the Head of the State Property and Finance Division of the State Treasury Department of the Chancellery of the Prime Minister where she is dealing with. among others, with the issues related to the new principles of managing the state owned property.

In 1999-2001 a member of the Disciplinary Commission of the Ministry of State Treasury. In 1999-2005 deputy public finance auditor for the Minister of State Treasury.

He has yearslong professional experience of holding seats on supervisory boards of State Treasury owned companies, including: ZPP ”Lenora” sp. z o.o., Koneckie Zakłady Odlewnicze S.A., Uzdrowisko Busko-Zdrój S.A., ŚWWG Polmos S.A., Stocznia Gdynia S.A., Archimedes S.A., PSO ”Maskpol” S.A., ZG ”Dom Słowa Polskiego” S.A. in liquidation, Fundusz Rozwoju Spółek S.A., Zakłady Mięsne Nisko S.A.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2017. In the Supervisory Board of the 5th common term of office she is a member of the Nominations and Compensation Committee of the Supervisory Board.

Paweł Pampuszko - Member of the Supervisory Board

A graduate of the Faculty of Law and Administration of the University of Silesia in Katowice, a lawyer entered on the list of lawyers maintained by the Solicitors Regulation Authority (Izba Adwokacka) in Katowice.

During his yearslong professional career he gained significant experience with respect to negotiating contracts as part of major industrial and business undertakings, and also preparing and conducting significant court disputes where it was necessary to become familiar with non-legal specialist issues and close cooperation with specialists in other fields. He was also actively involved in identifying and eliminating deficiencies in the operations of the corporations' authorities.

He gained professional experience related to providing legal services for business entities by working in 2005-2009, among others, at Kancelaria Biura Prawne Babula i Wspólnicy sp. k., Kancelaria Adwokatów i Radców Prawnych Ślązak, Zapiór & Partnerzy, SILEGE S.C. and Woszym Technologies sp.j. In 2009-2011 he was running his own legal practice. Since 2011 till now he has been a founding partner at law firm Kuś-Zielińska, Pampuszko i Wspólnicy – Adwokaci i Radcy Prawni sp.j.

He was a member of supervisory authorities in the non-government organizations and corporations: CHK S.A. and Medicina Pro Humana Foundation.

He is an author of publications on medical law.

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since May 29, 2017. In the Supervisory Board of the 5th common term of office he is a member of the Strategy Committee of the Supervisory Board.

Jan Płudowski - Member of the Supervisory Board

A graduate of the Faculty of Electric Engineering of the Silesian University of Technology in Gliwice. He also completed post-graduate studies at the Faculty of Electric Engineering of the Gdańsk University of Technology, at the University of Economics (formerly K. Adamiecki Academy of Economics) in Katowice in the field of corporate finance management and at the Faculty of Management and Services Economics of the University of Szczecin in the field of marketing and corporate management.

Professionally associated with the power sector, he gained professional experience by climbing up all levels of the career ladder. He was working, among others, as the Regional Chief Power Engineer (PKP Śląska Dyrekcja Okręgowa Kolei Państwowych (Polish State Railways' Silesian Regional Board) in Katowice), Director of Zakład Energetyki Kolejowej (Railways' Power Unit) in Katowice and the Head of the Power Management Department (PKP Dyrekcja Energetyki Kolejowej (Polish State Railways' Power Unit Board) in Warsaw), Director of the Cash Flow Office ("PKP Energetyka" sp. z o.o. in Warsaw). He is currently holding the position of the Project Coordinator Director at "PKP Energetyka" S.A. in Warsaw.

In 2007-2008 he was a member of the Supervisory Board of Spółka Energetyczna Jastrzębie S.A.

He has been a member of the Supervisory Board of TAURON Polska Energia S.A. since December 30, 2016. In the Supervisory Board of the 5th common term of office he is a member of the Audit Committee of the Supervisory Board and a member of the Strategy Committee of the Supervisory Board.

Agnieszka Woźniak - Member of the Supervisory Board

A graduate of the Faculty of Law and Administration of the UMCS University in Lublin. A lawyer by education.

In 2001-2015 she worked at the Ministry of Economy where she climbed up all levels of the career ladder, starting from a referendary, through the positions of a specialist, chief specialist, head of division, deputy director and director. Since 2005 an appointed civil servant. She has been associated with the Ministry of Energy since it was formed, i.e. since November 2015, where she is currently holding the position of the Director of the Minister's Office.

She has yearslong experience in personnel management. She was dealing with matters related to audits, organizational affairs of the office, public procurement, personnel issues. She was also holding the position of the Plenipotentiary of the General Director for the Integrated Management System.

She has experience related to supervising the operations of State Treasury owned companies. Between January 2009 and June 2014 a member of the Supervisory Board of Węglokoks S.A. with its seat in Katowice.

She has been a member of the Supervisory Board of TAURON Polska Energia S.A. since December 16, 2016. In the Supervisory Board of the 5th common term of office she is a member of the Nominations and Compensation Committee of the Supervisory Board and a member of the Strategy Committee of the Supervisory Board.

The detailed description of the experience and competences of the members of the Supervisory Board is published on the Company's website http://www.tauron.pl/.

Description of the operations

Detailed description of the Supervisory Board's operations is provided in the Code of Commercial Companies, the company's Articles of Association which are available on the company's website http://www.tauron.pl/ and in the *Regulations of the Supervisory Board of TAURON Polska Energia S.A. with its seat in Katowice*.

The main form of the Supervisory Board overseeing the Company's operations shall be the meetings of the Supervisory Board. Supervisory Board shall perform its obligations collectively. Meetings of the Supervisory Board shall be convened by the Chairperson of the Supervisory Board or Vice Chairperson of the Supervisory Board by presenting a detailed agenda:

1) in accordance with the decisions taken by the Supervisory Board,
2) of his/her own initiative,
3) at a written request of each member of the Supervisory Board,
4) at a written request of the Management Board.

Meetings of the Supervisory Board shall be held at the Company's seat. In justified cases a meeting may be convened at a different venue.

In order to convene a meeting all members of the Supervisory Board must be invited in writing at least 7 days before the date of the Supervisory Board's meeting. For important reasons the Chairperson of the Supervisory Board may shorten this period to 2 days, defining the way the invitations should be distributed. Notifications of the Supervisory Board's meeting shall be sent by fax or electronic mail and confirmed by phone. In the notification of the Supervisory Board's meeting the Chairperson shall define the date of the meeting, venue of the meeting and the detailed draft agenda. Supervisory Board shall meet on as needed basis, however not less frequently than once every 2 months. Supervisory Board may hold meetings without convening a formal meeting if all members of the Supervisory Board are present and nobody objects against the fact of holding the meeting or against the agenda.

A change of the proposed agenda may occur when all members of the Supervisory Board are present at the meeting and no one raises an objection against the agenda. An issue not included in the agenda should be included in the agenda of the next meeting.

Participation in a meeting of the Supervisory Board shall be a Supervisory Board member's duty. A member of the Supervisory Board shall provide information on the reason for his/her absence in writing. Excusing an absence of a member of the Supervisory Board shall require a resolution of the Supervisory Board. Members of the company's Management Board may take part in the Supervisory Board's meetings unless the Supervisory Board raises an objection. Participation of the Management Board's members in the Supervisory Board meetings shall be mandatory if they have been invited by the Chairperson of the Supervisory Board. Other persons may also take part in the meetings if they have been invited in the above mentioned way.

Supervisory Board may seek opinions of legal counsels who provide regular legal advice for the company, as well as, in justified cases, it may appoint and invite to meetings of the Supervisory Board appropriate experts in order to seek their opinion and make the right decision. In the above mentioned cases the Supervisory Board shall pass a resolution on commissioning the selected expert (auditing, consulting company) to carry out the work, obligating the Company's Management Board to conclude an applicable agreement.

Meetings of the Supervisory Board shall be chaired by the Chairperson of the Supervisory Board, and in case of his/her absence by the Vice Chairperson. For important reasons, with the consent of the majority of members of the Supervisory Board present at the meeting, the chairperson chairing the meeting shall be obligated to subject to a vote a motion to interrupt the meeting and set the date of resuming the meeting of the Supervisory Board. Supervisory Board shall make decisions in the form of resolutions. Supervisory Board's resolutions shall be passed mainly at its meetings. Supervisory Board shall pass resolutions if at least half of its members are present at the meeting and all its members have been invited in the appropriate way defined in the Regulations. Subject to the mandatory legal regulations in force, including the Code of Commercial Companies and the provisions of the company's Articles of Association, the Supervisory Board shall pass resolutions by an absolute majority of votes of the persons present at the meeting where the absolute majority of votes shall be understood as more votes cast "for" than "against" and "abstain". Resolutions shall not be passed on matters not included in the agenda unless all members of the Supervisory Board are present and nobody raises an objection. This shall not apply to resolutions on excusing a Supervisory Board's member's absence at the meeting. Resolutions shall be voted on in an open ballot. A secret ballot shall be ordered:

1) at the request of at least one member of the Supervisory Board,
2) in personnel related matters.

In accordance with the company's Articles of Association the Supervisory Board may pass resolutions in writing or using means of direct remote communications. Passing a resolution in such way shall require a prior notification of all members of the Supervisory Board of the content of the draft resolution. Passing resolutions this way shall not apply to appointing the Chairperson, the Vice Chairperson and the Secretary of the Supervisory Board, appointing or suspending from office a member of the Management Board and dismissing these persons, as well as other matters that require a secret ballot vote. When voting on a resolution in the aforementioned way a member of the Supervisory Board shall indicate his/her vote, i.e. "for", "against" or "abstain". In case a member of the Supervisory Board fails to indicate his/her vote by the time defined by the Chairperson the resolution shall not be passed. A resolution with a note that it has been passed in writing or by voting using means of direct remote communications shall be signed by the Chairperson of the Supervisory Board.

Resolutions passed this way shall be presented at the forthcoming meeting of the Supervisory Board along with the result of the voting.

Members of the Supervisory Board shall be allowed to take part in the meeting and vote on resolutions during such meeting using means of direct remote communications, i.e. a conference call or a video conference, subject to a proviso that at least half of its members are present at the meeting's venue indicated in the notification of the meeting and a secure communications link is technically possible.

Members of the Supervisory Board shall take part in meetings and exercise their rights and responsibilities in person, and while performing their duties they shall be obliged to act with due diligence. Members of the Supervisory Board shall be obliged to keep confidential information related to the company's activities that they have acquired in connection with holding their seat or on another occasion. Supervisory Board shall perform its activities collectively.

Supervisory Board may, for important reasons, delegate its individual members to perform certain supervision actions on their own for a defined period of time. Supervisory Board may delegate its members, for a period not longer than three months, to temporarily perform duties of members of the Management Board who have been dismissed, submitted their resignation or if for other reasons they cannot perform their functions. The above mentioned delegation shall require obtaining a consent of the member of the Supervisory Board who is to be delegated.

The detailed description of the activities of the Supervisory Board in the last financial year is provided in the Report on the Activities of the Supervisory Board, submitted on annual basis to the General Meeting of Shareholders and then published on the company's website http://www.tauron.pl/.

Supervisory Board may appoint from among its members permanent or temporary (ad-hoc) working groups, committees to perform specific actions. Supervisory Board's standing committees shall be:

1) Audit Committee of the Supervisory Board of TAURON Polska Energia S.A. (Audit Committee),
2) Nominations and Compensation Committee of the Supervisory Board of TAURON Polska Energia S.A. (Nominations and Compensation Committee),
3) Strategy Committee of the Supervisory Board of TAURON Polska Energia S.A. (Strategy Committee).

Membership, tasks and rules of operation of the above mentioned committees shall be defined in the regulations thereof passed by the Supervisory Board.

6.11.3. Audit Committee

Due to the changes to the membership of the Supervisory Board of the Company introduced in 2017, the Supervisory Board also made changes to the membership of the Audit Committee.

Members of the Audit Committee as of December 31, 2017 and as of the day of drawing up this report

1. Teresa Famulska - Head of the Audit Committee,
2. Beata Chłodzińska - Member of the Audit Committee,
3. Radosław Domagalski-Łabędzki - Member of the Audit Committee,
4. Jan Płudowski - Member of the Audit Committee,
5. Jacek Szyke - Member of the Audit Committee.

Changes to the Audit Committee's membership

As of January 1, 2017 the Audit Committee was composed of the following members: Beata Chłodzińska (Head of the Audit Committee), Jacek Rawecki and Jacek Szyke.

On January 30, 2017 the Supervisory Board appointed the following members of the Audit Committee: Stanisław Bortkiewicz and Jan Płudowski. On the same day the Audit Committee elected, from among its members, Stanisław Bortkiewicz as the Head of the Audit Committee.

On May 25, 2017 Jacek Rawecki submitted a statement on the resignation, as of May 26, 2017, from the function of a member of the Company's Supervisory Board. Consequently, his membership in the Audit Committee also expired.

On May 29, 2017, due to the end of the 4th term of the Supervisory Board mandates of members of the Supervisory Board expired and consequently their membership in the Audit Committee expired.

On June 20, 2017, due to the appointment, as of May 29, 2017, of members of the Supervisory Board of the 5th term, the Supervisory Board appointed the Audit Committee with the following members: Beata Chłodzińska, Radosław Domagalski - Łabędzki, Teresa Famulska, Jan Płudowski and Jacek Szyke. On the same day the Audit Committee, during the first meeting of the 5th term, elected Teresa Famulska as the Head of the Audit Committee.

No other changes to the membership of the Audit Committee had been made as of the day of disclosing this report.

Information on the independence of members of the Audit Committee as of December 31, 2017

The membership (composition) of the Audit Committee is in compliance with the requirements defined in the *law of May 11, 2017 on certified auditors, audit companies and public supervision*. The evaluation of independence and the statutory requirements with respect to the knowledge and skills of the individual members of the Audit Committee was made by the Supervisory Board Rada based on the relevant statements submitted by the members of the Audit Committee. Three members of the Audit Committee comply with the statutory requirements related to independence, including the Head of the Audit Committee who also has knowledge and skills in the field of accounting and auditing financial statements. Two members of the Audit Committee: Jacek Szyke and Jan Płudowski, knowledge and skills in the field of energy, i.e. the Company's industry.

The independence requirements defined for the members of the Audit Committee by the above law are met by the following members of the Audit Committee:

1) Teresa Famulska,
2) Jan Płudowski,
3) Jacek Szyke.

The other members of the Audit Committee do not meet the independence requirements defined by the above law.

As of the day of drawing up this report a member of the Supervisory Board, Beata Chłodzińska, met the independence requirements defined by the above law.

Tasks and competence of the Audit Committee

The tasks and competence of the Audit Committee with the coming into force on June 21, 2017 of the law of May 11, 2017 on certified auditors, audit companies and public supervision, have been verified and aligned with the current legal regulations in force and adopted by the Supervisory Board at the motion of the Audit Committee in the form of the new Regulations of the Audit Committee of the Supervisory Board of TAURON Polska Energia S.A.

The tasks and competence of the Audit Committee as of the day of drawing up this report are presented in the below table.

Table no. 28. Competence of the Audit Committee

Competence of the Audit Committee
as of December 31, 2017 and as of the day of drawing up this report
1. monitoring: 1) the Company's financial reporting process, 2) the effectiveness of internal control, risk management, compliance and internal audit systems, including with respect to the financial reporting, 3) monitoring of performing of financial revisions, in particular performing of an audit by an audit company, taking into account any conclusions (motions) and arrangements of the Audit Supervision Committee stemming from an audit (inspection) performed at an audit company, 2. controlling and monitoring of independence and impartiality of the chartered accountant (certified auditor) and the entity entitled to examine financial statements, including rendering by them services other than financial audit, monitoring the independence of a certified auditor and audit company, in particular in case other services than an audit are provided for the benefit of the Company, 3. performing the evaluation of independence of the certified auditor and expressing consent for performing by him of permitted services not constituting the audit within the Company, 4. developing the policy foe selecting the auditing company to perform the audit, 5. developing a policy of performing by the auditing company performing the audit, entities related with the auditing company and members of the auditing company's corporate network of permitted services no constituting the audit, 6. defining the procedure for selecting the auditing company by the Company, 7. presenting to the Supervisory Board of recommendation for selection of the auditing company responsible for performing the statutory audit or review of financial statements, as required under Art. 130 Paras 2 and 3 of the *Act of 11 May 2017 on certified auditors, auditing companies and public oversight* and in Art. 16.2 *Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC*, in line with policies referred to above in items 4 and 5, 8. informing the Supervisory Board of audit results and explaining as to who did the audit contribute to trustworthiness of financial reporting in the Company, and also what was the role of the Audit Committee in course of the audit, 9. presenting recommendations aimed at ensuring reliability of the financial reporting process within the Company, 10. performing other activities vested with audit committees pursuant to *Act of 11 May 2017 on certified auditors, auditing companies and public oversight*, *Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC* and *Act of 29 September 1994 - the Accounting Act.*

The detailed description of the activities of the Audit Committee in the last financial year is provided in the report on the activities of the Supervisory Board submitted on annual basis to the General Meeting of Shareholders and published on the Company's website http://www.tauron.pl/.

6.11.4. Nominations and Compensation Committee

Due to the changes to the membership of the Supervisory Board of the Company introduced in 2017, the Supervisory Board also made changes to the membership of the Nominations and Compensation Committee

Members of the Nominations and Compensation Committee as of December 31, 2017 and as of the day of drawing up this report

1. Beata Chłodzińska - Head of the Nominations and Compensation Committee,
2. Barbara Łasak - Jarszak - Member of the Nominations and Compensation Committee,
3. Agnieszka Woźniak - Member of the Nominations and Compensation Committee.

Changes to the Nominations and Compensation Committee's membership

As of January 1, 2017 the Nominations and Compensation Committee was composed of the following members: Beata Chłodzińska (Head), Leszek Koziorowski i Agnieszka Woźniak.

On May 29, 2017, due to the end of the 4th term of the Supervisory Board mandates of members of the Supervisory Board expired and consequently their membership in the Nominations and Compensation Committee expired.

On June 20, 2017, due to the appointment, as of May 29, 2017, of members of the Supervisory Board of the 5th term, the Supervisory Board appointed the Nominations and Compensation Committee with the following members: Beata Chłodzińska, Barbara Łasak - Jarszak and Agnieszka Woźniak. On the same day the Nominations and Compensation Committee, during the first meeting of the 5th term, elected Beata Chłodzińska as the Head of Nominations and Compensation Committee.

No other changes to the membership of the Nominations and Compensation Committee had been made as of the day of disclosing this report.

Tasks and competence of the Nominations and Compensation Committee

The tasks and competence of the Nominations and Compensation Committee did not change in 2017.
The tasks and competence of the Nominations and Compensation Committee as of December 31, 2017 and as of the day of drawing up this report are presented in the below table.

Table no. 29. Competence of the Nominations and Compensation Committee

Competence of the Nominations and Compensation Committee
as of December 31, 2017 and as of the day of drawing up this report
1. recommending to the Supervisory Board a recruitment procedure for the positions of members of the company's Management Board, 2. evaluating candidates for members of the Management Board and providing the Supervisory Board with opinions in this respect, 3. recommending to the Supervisory Board a form and content of agreements to be concluded with members of the Management Board, 4. recommending to the Supervisory Board a compensation and bonus system for members of the Management Board, 5. recommending to the Supervisory Board the need to suspend a member of the Management Board for important reasons, 6. recommending to the Supervisory Board the need to delegate a member of the Supervisory Board to temporarily perform the duties of members of the Management Board who cannot perform their duties, along with a compensation proposal.

The detailed description of the activities of the Nominations and Compensation Committee in the last financial year is provided in the Report on the activities of the Supervisory Board submitted on annual basis to the General Meeting of Shareholders and published on the Company's website http://www.tauron.pl/.

6.11.5. Strategy Committee

Due to the changes to the membership of the Supervisory Board of the Company introduced in 2017, the Supervisory Board also made changes to the membership of the Strategy Committee

Members of the Strategy Committee as of December 31, 2017 and as of the day of drawing up this report

1. Jacek Szyke - Head of the Strategy Committee,

2. Beata Chłodzińska - Member of the Strategy Committee,
3. Paweł Pampuszko - Member of the Strategy Committee,
4. Jan Płudowski - Member of the Strategy Committee,
5. Agnieszka Woźniak - Member of the Strategy Committee.

Changes to the Strategy Committee's membership

As of January 1, 2017 the Strategy Committee was composed of the following members: Jacek Szyke (Head), Beata Chłodzińska, Anna Mańk i Stefan Świątkowski.

On March 15, 2017 the Supervisory Board passed a resolution on appointing as members of the Strategy Committee: Stanisław Bortkiewicz and Jan Płudowski.

On May 29, 2017, due to the end of the 4th term of the Supervisory Board mandates of members of the Supervisory Board expired and consequently their membership in the Strategy Committee expired.

On June 20, 2017, due to the appointment, as of May 29, 2017, of members of the Supervisory Board of the 5th term, the Supervisory Board appointed the Strategy Committee with the following members: Jacek Szyke, Beata Chłodzińska, Paweł Pampuszko, Jan Płudowski i Agnieszka Woźniak. On the same day the Strategy Committee, during the first meeting of the 5th term, elected Jacek Szyke as the head of the Strategy Committee.

No other changes to the membership of the Strategy Committee had been made as of the day of disclosing this report.

Tasks and competence of the Strategy Committee

The tasks and competence of the Strategy Committee did not change in 2017. The tasks and competence of the Strategy Committee as of December 31, 2017 and as of the day of drawing up this report are presented in the below table.

Table no. 30. Competence of the Strategy Committee

Competence of the Strategy Committee
as of December 31, 2017 and as of the day of drawing up this report
1. evaluating the Company's and TAURON Capital Group's Strategy and presenting the results of such evaluation to the Supervisory Board, 2. recommending to the Supervisory Board the scope and deadlines for submitting the long term strategic plans by the Management Board, 3. evaluating the impact of planned and currently undertaken strategic investment projects on the Company's assets, 4. monitoring the implementation of strategic investment tasks, 5. evaluating activities related to the use of material Company's assets, 6. providing opinions on strategic documents submitted to the Supervisory Board by the Management Board

The detailed description of the activities of the Strategy Committee in the last financial year is provided in the report on the activities of the Supervisory Board submitted on annual basis to the General Meeting of Shareholders and published on the Company's website http://www.tauron.pl/.

6.11.6. Description of activities of the Committees of the Supervisory Board

The detailed description of the operations of the Committees of the Supervisory Board is provided in the Regulations of individual Committees of the Supervisory Board of TAURON Polska Energia S.A.

The Committees of the Supervisory Board are advisory and opinion-making bodies acting collectively as a part of the Supervisory Board and perform support and advisory functions towards the Supervisory Board. The tasks of the Committees of the Supervisory Board are carried out by submitting motions, recommendations, opinions and statements on the scope of its tasks to the Supervisory Board, by means of resolutions. The Committees of the Supervisory Board are independent of the Management Board of the Company. The Management Board may not issue binding orders to the Committees of the Supervisory Board concerning performing their tasks.

The Audit Committee and the Nominations and Compensation Committee of the Supervisory Board are composed of three to five members, while the Strategy Committee is composed of three to seven members. The activities of the individual Committees are managed by their Chairpersons (Heads).

Meetings of the Committees are convened by the Chairperson of the specific Committee on his/her own initiative or upon the motion of a member of the Committee or Chairperson of the Supervisory Board and they are held on as needed basis.

In case of the Audit Committee the meetings are convened at least on a quarterly basis. The Chairpersons of the Committees may invite members of the Supervisory Board, who are not members of the specific Committee, members of the Management Board and employees of the Company as well as other persons working or cooperating with the Company to the meetings of the Committees. The Chairperson of the specific Committee or a person appointed by him/her submits motions, recommendations and reports to the Supervisory Board .

The Committees of the Supervisory Board pass resolutions if at least a half of their members were present at the meeting and all their members have been duly invited. The resolutions of the Committees of the Supervisory Board are adopted by an absolute majority of votes present at the meeting, where the absolute majority of votes is understood as more votes given “for” than “against” and “abstain”. The Committees of the Supervisory Board may pass resolutions in writing or by using means of direct remote communication.

Members of the Committees of the Supervisory Board may also participate in meetings and vote of the adopted resolutions by using means of direct remote communication, i.e. tele- or videoconferences.

The Company’s Management Board shall be informed about recommendations and assessments submitted to the Supervisory Board by the given Committee of the Supervisory Board. Every year, the Committees of the Supervisory Board provide public record information, through the Company, on their memberships, the number of meetings held and participation in the meetings during the year as well as on their main activities. In addition, the Audit Committee performs an assessment of the independence of the certified auditor and expresses its consent for the provision thereby of the permitted services that are not an audit of the Company.

The Company’s Management Board provides the possibility to use the services of external advisers by the Committees to the extent required for performing the obligations of the Committees.

6.12. Description of the policy of diversity applied to the governing bodies of the Company

Diversity and openness are an integral part of both, TAURON Capital Group’s business operations, as well its management policy. All of TAURON Capital Group’s subsidiaries apply the policy of equal treatment and strive to ensure diversity in terms of gender, educational background, age and professional experience in relation to all employees and key managers.

With respect to the members of the corporate bodies of TAURON, i.e. the Management Board and the Supervisory Board, persons acting as Members of the Management Board are selected by the Supervisory Board, while Members of the Supervisory Board are selected by the Minister of Energy. In 2017, acting within its statutory powers, the State Treasury appointed 5 Members of the Supervisory Board and the Ordinary GM of TAURON on May 29, 2017 elected 3 Members of the Management Board. Information concerning qualifications and professional experience of persons appointed to the Management Board and the Supervisory Board is published in the relevant regulatory filings (current reports) as well as on the Company’s website.

Members of the Management Board are appointed by the Supervisory Board after conducting a qualification procedure designed for verifying and assessing their qualifications and selected the best candidates. Announcement of qualification process is published on the Company’s web page and in the Public Information Bulletin of the Ministry of Energy. The competition is open for any person meeting requirements set forth in the Company’s By-laws and formal requirements specified in the announcement. Candidates are required to possess university level education, at least five years of employment and minimum three years of experience as managers, and have to meet requirements set forth in other legislation. No special requirements are placed on features such as sex, type of education, age and professional expertise, to the Supervisory Board is capable of assessing candidates to the Management Board with consideration of their overall capabilities and diversity requirements.

The *Diversity Policy of the TAURON Group* was implemented in 2017, the purpose of which is to strengthen awareness and organizational culture open to diversity. Implementation of the Diversity Policy enables employees to full realize their individual potential in the job environment.

Also, actions have been undertaken to prevent any discrimination by structuring the appropriate atmosphere and culture at the workplace based on key PRO corporate values - Partnership, Development and Courage, confirmed through the *Policy of combating Mobbing and Discrimination at the TAURON Group*.

7. COMPENSATION POLICY WITH RESPECT TO THE MANAGEMENT AND SUPERVISORY STAFF

7.1. Compensation system for members of the Management Board and key managers

7.1.1. General information on the adopted compensation system for members of the Management Board

In 2017 the principles of compensation of members of the Company's Management Board defined in the Resolution of the Extraordinary GM of TAURON of December 15, 2016 *on the principles for determining compensation of members of the Management Board* (Principles for determining compensation) were in force at the Company, as subsequently amended and detailed by the Supervisory Board of the Company pursuant to the resolution of December 19, 2016 *on the principles for determining compensation of members of the Management Board TAURON Polska Energia S.A.* as subsequently amended. The above principles for determining compensation are in line with the provisions of the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies*.

The adopted principles for determining compensation define the compensation system for members of the Management Board in connection with outstanding tasks aimed at the implementation of the adopted Strategy, directions of expansion and financial plans. The overriding objective of the adopted compensation system is to ensure an incentive-based compensation of the senior management staff and to create basis for their development.

Overall objectives of the compensation policy are:

1) ensuring a consistent and motivational compensation system for members of the Management Board,
2) linking the compensation rules with monitoring of the implementation of adopted strategic plans and implementation of the financial plans,
3) setting the level of compensation for the Management Board members in connection with the implementation of the management tasks set,
4) increasing the Company's value through the development of the senior management staff,
5) improving the compensation systems leading to the implementation of the Company's strategy and expansion directions.

Model of compensation for members of the Management Board is based on a two-component system for determining compensation, composed of a fixed part constituting the monthly base wage and a variable part constituting the supplementary compensation for the Company's financial year, dependent on achieving specific management objectives.

System of compensation for members of the Management Board assumes linking the variable part of the compensation with the outstanding management goals stemming from the provisions of the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies* and set, based upon these provisions, by the GM the Supervisory Board of the Company. The goal of adopting in the system of compensation, of the dependence of the compensation's variable part on achieving the management goals set is, in particular, to implement the adopted Strategy, the directions of the Company's expansion and financial plans, it also shapes a new organizational culture of the Company.

Taking into account the applicable regulations, the level of compensation for members of the Management Board is defined by the Supervisory Board, within the brackets determined by the Company's GM.

Members of the Management Board of the Company are neither covered by the bonus program based on the capital of the Company, nor do they receive any compensation or awards due to fulfilment of their functions in governing bodies of TAURON Capital Group's subsidiaries.
In 2017 the Supervisory Board updated the *Policy of compensation for Members of the supervision and management authorities (bodies) including the description of the principles for the determination thereof at TAURON Polska Energia S.A.,* in force since February 24, 2011.

7.1.2. General information on the adopted compensation system for key managers

The rules concerning compensation and bonus system for key managers and other employees are defined in the *Regulations on Compensation of Employees of TAURON Polska Energia S.A.,* adopted for application by the Management Board of the Company.

In 2017 the *Principles of Compensation at TAURON Group* were developed representing the guidelines for TAURON Capital Group's subsidiaries with respect to the personnel compensation systems, particularly taking into account the bonus system for key managers based on the management by objectives system consistent throughout TAURON Capital Group, representing a combination of the planning process, efficiency measurement process and evaluation process.

The compensation and bonus system for key managers stipulates that the level of compensation should be tied to the financial situation of TAURON Capital Group in an annual perspective, in connection with the implementation of strategic goals.

The overriding assumption of the compensation system in force is to ensure the optimum and motivating compensation level, depending on the value and type of work on a given position as well as the quality of work and effects achieved by employees.

The structure of the compensation consists of the following elements:

1) fixed part - constituting the base salary determined in accordance with the table of grade categories applicable in the Company and monthly rates of personal grade. The allocated level of basic salary reflects the value and type of work as well as the quality of employee's work, defined through the assessment of employee's competence level

2) variable part - which depends on performance results, defined through the level of accomplishment of targets and tasks within the MBO bonus system,

3) benefits - which are defined in the internal regulations of the Company

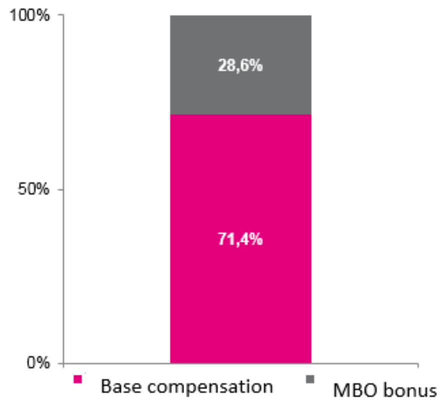
The MBO bonusing system based on market principles of awarding bonuses ensures focusing activities of key management staff on attaining objectives defined within the Strategy, as well as individual strategic objectives and development directions of individual companies within the TAURON Capital Group. This system also ensures cascading of objectives defined by the Company's Management Board at the TAURON Capital Group level and at the Company level, down to concrete, parametric tasks vested with employees of lower structural levels. The MBO bonusing system has been tied with the management by process style of operations at the TAURON Capital Group, *inter alia* by aligning the objectives with Megaprocesses defined within the TAURON Capital Group. Therefore, the introduced culture of Management by Objectives reflects the specific features of each function implemented in the Company and allows use of dialogue mechanisms between the superior and subordinate during the process of setting and assessing objectives, leading to attaining overall efficiency throughout the entire organization.

At the same time, this took enables precise correlating of KPIs defined for members of the Management Board with objectives defined for the given year for key managers of the Company. Initial assessment of accomplished objectives takes place after end of the first 6 months and after end of the year, members of the Management Board conduct final assessment of KPI performance by key managers.

Moreover, in March 2017 the bonus system for the trading area aimed at motivating to generate higher revenue for TAURON Capital Group. The trading bonus covered key managers in the trading area, however the bonus system sets an additional bonus for them only once they have topped annual trade plans.

Employees of the Company do not receive any compensation or awards on account of functions fulfilled in governing bodies of TAURON Capital Group's subsidiaries.
The below figure presents the structure of compensation for key manager positions.

Figure no. 49. Structure of compensation for key manager positions



7.1.3. Rules, terms and conditions as well level of compensation of members of the Management Board

The total amount of compensation understood as the value of salaries, awards and benefits received in cash, in kind or in any other form, due or paid by the Company to the Management Board members in 2017 reached the gross amount of PLN 4 534 thousand.

The compensation of members of the Company's Management Board in 2017, broken down into components, is presented in the below table.

Table no. 31. Compensation of members of the Company's Management Board in 2017 broken down into components

#	Name	Period of holding the position in 2017	Compensation[1] (PLN '000)	Bonus[1] (PLN '000)	Other benefits[1] (PLN '000)	Total (PLN '000)
1.	Filip Grzegorczyk[2]	01.01.2017 - 31.12.2017	793	-	24	817
2.	Jarosław Broda[3]	01.01.2017 - 31.12.2017	803	226	79	1 108
3.	Kamil Kamiński[3]	01.01.2017 - 31.12.2017	792	181	77	1 050
4.	Marek Wadowski[3]	01.01.2017 - 31.12.2017	863	181	36	1 080
5.	Piotr Zawistowski	01.01.2017 - 15.03.2017	186	226	69	481
	Total		**3 437**	**812**	**285**	**4 534**

[1]*excluding markups (surcharges)*

[2]*compensation in accordance with the agreement on the provision of management services in force*

[3]*from January 1, 2017 till March 15, 2017 the compensation in accordance with the labor agreement, while from March 16, 2017 till December 31, .2017 the compensation in accordance with the agreement on the provision of management services*

Members of the Management Board did not receive compensation or bonuses for performing functions in the corporate bodies of TAURON Capital Group's subsidiaries in 2017.

From January 1, 2017 till March 15, 2017 members of the Management Board received the compensation in accordance with the labor agreement (except for the President of the Management Board who received the compensation in accordance with the agreement on the provision of management services). From March 16, 2017 all members of the Management Board appointed for the 5th term received the compensation in accordance with the agreement on the provision of management services, prepared in accordance with the *law of June 9, 2016 on the principles of determining the compensation of persons managing certain companies.*

Model of compensation for members of the Management Board, defined in the agreements on the provision of management services is based on a two-component system for determining compensation, composed of a fixed part (monthly base wage) and a variable part (supplementary compensation for the Company's financial year), dependent on fulfiling specific result-based criteria, i.e. achieving management objectives.

System of compensation for members of the Management Board assumes linking the variable part of the compensation with the outstanding management goals stemming from the provisions of the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies* and set, based upon these provisions, by the GM the Supervisory Board of the Company. The goal of adopting in the system of compensation, of the dependence of the compensation's variable part on achieving the management goals set is, in particular, to implement the adopted Strategy, the directions of the Company's expansion and financial plans, it also shapes a new organizational culture of the Company.

The variable part of the compensation represents up to 60% of the fixed part of the compensation for the financial year, assuming the management goals set by the Supervisory Board for the given financial year have been achieved.

The Supervisory Board determines the percentage level of the variable part of the compensation for each of the following management goals:

1) achieving EBITDA at the level approved in the material and financial plan for a given financial year,
2) achieving the Net debt/EBITDA ratio at the level approved in the material and financial plan for a given financial year,
3) implementation of the "2016 – 2018 Efficiency Improvement Program" and achieving the total effect at the level approved in the material and financial plan for a given financial year,
4) implementation of the non-financial management goals objectives.

The variable part of the compensation for achieving the financial management goals is allocated based on the data derived from the audited consolidated financial statements of the Company for the given financial year.

The variable part of the compensation for achieving the non-financial management goals is allocated based on the achievement of specific objectives in the given financial year, based on the assessment of their performance by the Supervisory Board.

7.1.4. Agreements concluded with managing persons which envisage compensation in case of their resignation or dismissal from the position held, without material reason, or if their dismissal or resignation takes place as a result of the merger of the Company through takeover

According to the agreements on the provision of management services concluded with the members of the Management Board on March 15, 2017 envisage, in case of termination or dissolution of the agreement by the Company for reasons other than defined therein, a payout of the severance payment at a level of three–fold fixed part of the compensation, under the condition of fulfilment of the function by them over a period of at least 12 months prior to the termination of the agreement.

Furthermore, due to the access of members of the Management Board to confidential information the disclosure of which could expose the Company and TAURON Capital Group's subsdiaries to losses, the aforementioned agreements on the provision of management services include non-competition provisions applicable after the expiry of the term of office. Under the aforementioned agreements members of the Management Board undertook to refrain from conducting competitive activities in the specified period in return for compensation.
Members of the Company's Management Board did not hold positions of members of Management Boards of subsidiaries (companies included) in TAURON Capital Group prior to being appointed as members of the Company's Management Board.

7.1.5. Non-financial components of compensation allocated to members of the Management Board and key managers

Non-financial components of the compensation of members of the Management Board

Members of the Management Board, in accordance with the agreements on provision of management services, are entitled to:

1) refinancing by the Company of the cost of training up to the net amount of PLN 15 000 in a calendar year,
2) use a company car,
3) use the technical devices required to perform the obligations under the concluded agreement.

Non-financial components of the compensation of key managers

Staff members employed at key positions by the Company are entitled to use the following benefits and non-financial components of the compensation offered by the Company:

1) participate in the Employee Pension Scheme operated by the employer (under the condition of being employed in the Company or one of the subsidiaries of TAURON Capital Group over a period of at least one year),
2) use the medical package financed from the Company funds,
3) use a company car allocated for sole disposal,
4) use company accommodation in case if the availability of the employee is required due to the nature of his/her work and scope of responsibilities.

7.1.6. Information on changes to the compensation policy over the last financial year

On May 29, 2017 the Ordinary GM amended resolution no. 5 of the Extraordinary GM of TAURON of December 15, 2016 *on the principles for determining compensation of members of the Management Board,* by adding an extra management goal to be achieved by members of the Management Board by December 31, 2017, making the payment of the variable part of the compensation contingent, covering the performance of the obligations mentioned in art. 17-20, art. 22 and art. 23 *of the law of December 16, 2016 on the state assets management principles.*

With a view to implement the principles to determine compensation passed by the GM in December 2016 r., on March 15, 2017 agreements on the provision of management services were concluded with the members of the Management Board appointed for the common 5th term in office. The agreement on the provision of management services with the President of the Management Board had been concluded earlier, meanwhile labor contracts had been concluded earlier with the other members of the Management Board.

7.1.7. Assessment of functioning of the compensation policy in terms of fulfilment of its objectives, in particular, the long-term growth in shareholders' value and stability of the undertaking performance

The applied compensation system for members of the Management Board is compliant with the *Act of June 9, 2016 on the principles for determining compensation of persons managing certain companies*. The incentive-based and consistent system is provided, linked with the monitoring of annual financial plans and the adopted Strategy and development (expansion) directions

The form, structure and level of compensation correspond to market conditions and are oriented towards enabling the recruitment and maintaining of individuals fulfilling the criteria required for running the Company in the manner taking into account shareholders' interests (building the Company's value for shareholders), as well as prevent conflicts of interest from arising among members of the Management Board and shareholders. At the same time, they are constructed in the manner which is transparent for investors, so that their trust towards the Company is built and they are able to express their opinions using the applicable procedures.

Information policy on the form, structure and level of compensation of members of the Management Board and the Supervisory Board is conducted by the Company in communication with the Supervisory Board in a manner that is in compliance wth the regulations in force and best market practice.

The disbursement of variable components of compensation is linked with the pre-defined, measurable management goals. The set management goals should foster long-term stability of the Company.

The indicators (criteria) determining obtaining and level of variable components of the compensation are defined in accordance with the SMART principle, thus, they also display such features as: precision, measurability, achieveability, materiality and defining in time.
The compensation and bonus system for both Members of the Management Board of the Company as well as the key managers in force at TAURON supports the implementation of strategic goals and determines the compensation depending on the financial situation of the Company and TAURON Capital Group in an annual perspective.

7.2. Compensation system for members of the Supervisory Board

In 2017 the system of compensation for members of the Supervisory Board of the Company defined in the Resolution of the Extraordinary GM of TAURON of December 15, 2016 *on the principles for determining compensation for members of the Supervisory Board of TAURON Polska Energia S.A.* was in force, adopted as the implementation of the provisions of *the Act of 9 June 2016 concerning principles for determining compensation of persons managing certain companies* (Journal of Laws of 2016, item 1202).

In accordance with the aforementioned Resolution of the Extraordinary GM a monthly compensation of Supervisory Board members is determined as a product of the average monthly compensation in the enterprise sector, excluding payment of profit distribution bonuses in the fourth quarter of the preceding year, announced by the President of the Central Statistics Office and the multiplier:

1) for the chairperson of the Supervisory Board – 1.7
2) for other members of the Supervisory Board – 1.5

Members of the Supervisory Board are entitled to receive the compensation irrespective of the frequency of formally convened meetings.

The compensation does not apply for a month in which a member of the Supervisory Board was not present at any of the formally convened meetings, for unjustified reasons. The decision on excusing or failure to excuse the absence of a member of the Supervisory Board at its meeting is taken by the Supervisory Board by means of a resolution.

The compensation is calculated on a pro rata basis, in relation to the number of days when the function was fulfilled in case if the appointment or dismissal occurred during the calendar month.

The Company covers costs incurred in connection with the fulfilment of functions assigned to members of the Supervisory Board, in particular: costs of return transfer between the place of residence and the venue of the Supervisory Board meeting or meeting of the Supervisory Board Committee, costs of individual supervision and costs of accommodation and board.

Compensation of supervising personnel

The compensation of members of the Company's Supervisory Board in 2017 is presented in the below table.

Table no. 32. Compensation of members of the company's Supervisory Board in 2017

#	Name	Period of holding the position in 2017	Compensation (PLN '000)
1.	Beata Chłodzińska	01.01.2017 - 31.12.2017	89
2.	Teresa Famulska	29.05.2017 - 31.12.2017	47
3.	Jacek Szyke	01.01.2017 - 31.12.2017	79
4.	Radosław Domagalski - Łabędzki	29.05.2017 - 31.12.2017	47
5.	Barbara Łasak - Jarszak	29.05.2017 - 31.12.2017	47
6.	Paweł Pampuszko	29.05.2017 - 31.12.2017	47
7.	Jan Płudowski	01.01.2017 - 31.12.2017	79
8.	Agnieszka Woźniak	01.01.2017 - 31.12.2017	79
9.	Jacek Rawecki	01.01.2017 - 26.05.2017	32
10.	Leszek Koziorowski	01.01.2017 - 29.05.2017	33
11.	Stefan Świątkowski	01.01.2017 - 29.05.2017	33
12.	Anna Mańk	01.01.2017 - 29.05.2017	33
13.	Stanisław Bortkiewicz	01.01.2017 - 29.05.2017	33
	TOTAL		**677**

7.3. Liabilities arising from pensions and similar benefits for former the Members of the Management Board and the Supervisory Board

The Company does not have any liabilities towards former the Members of the Management Board and the Supervisory Board arising from pensions and similar benefits.

At the same time, it is indicated that due to the Company's liabilities towards former members of TAURON Management Board, in 2017 the total amount of PLN 2 258 thousand was paid due to bonuses for the accomplishment of KPIs in 2016 and compensations for compliance with the non-competition clause.

8. STATEMENT ON NON-FINANCIAL INFORMATION

8.1. TAURON Group's Business and Operational Model

TAURON Capital Group comprises selected companies managed jointly as a uniform economic body consisting of independent commercial law companies, led by TAURON as the parent entity.

In 2017 the *Business Model of TAURON Group* adopted by the Management Board of the Company on May 4, 2016 was in force. In order for TAURON Capital Group to effectively carry out the tasks the above document was updated by the Management Board of TAURON. A document called *Business and Operational Model of TAURON Group* (Business Model) adopted on January 23, 2018 defines TAURON Capital Group's management model, defines the high-level architecture of processes and contains guidelines concerning key performance indicators of units constituting TAURON Capital Group.

8.1.1. Assumptions of the Business Model

The key assumptions of the Business Model include building of TAURON Capital Group value, focusing on customers, transparent distribution of duties and responsibilities, effective information exchange, use of employees' knowledge, volatility of the Business Model, organisational integrity of TAURON Capital Group.

8.1.2. Company management principles

In accordance with the provisions of the *By-laws of the Management Board of TAURON Polska Energia Spółka Akcyjna with its seat in Katowice*, the Management Board conducts the affairs of the Company and represents it in all judicial and extra-judicial proceedings. All issues connected with managing the Company, which are not restricted by legal regulations and provisions of the Company's Articles of Association to the competence of the General Meeting or the Supervisory Board lie within the competence of the Company's Management Board. Cooperation of two members of the Management Board or one member of the Management Board together with a proxy is required for submitting statements on behalf of the Company.
Issues covered within the competence of the Management Board as a collective body are described in detail in section 6.8.1. of this report.

In accordance with the *Organisational Regulations of TAURON Polska Energia S.A.* (Organisational Regulations), the Company is managed directly by the Management Board of the Company as well as through proxies, Executive Directors, Managing Directors or power of attorneys.

The Company implements its tasks through:

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

8.1.3. TAURON Capital Group management principles

The main regulatory act of TAURON Group is the *Code of TAURON Group* adopted by the Management Board of the Company which regulates its operations, ensuring the implementation of the goals through tailored solutions in the area of management of TAURON Capital Group's entities, including, in particular, setting the operating objectives of companies, enabling the achievement of effects assumed in the new Strategy.

Regulations implemented in 2016 together with the Business Model led to introduction of the management by processes structure within the entire TAURON Capital Group, consisting in establishing of process subordination running horizontally within all companies of the Group. Members of the Management Board are responsible for the allocated to them process streams which are subsequently divided into Megaprocesses. Megaprocesses are owned by named managing and executive directors at TAURON. Process documentation (maps, diagrams and process sheets) defines and describes decision authorities and actions to be undertaken by individual organizational units within companies of the TAURON Capital Group. Owners of Megaprocesses decompose these into lower level processes and appoint their owners. Each process has its owner and process metrics defined by the higher level process owner. Process documentation defines the decision dependences and authorities for repeatable processes.

Management by processes model has been implemented to benefit from operating synergies between companies of the TAURON Capital Group, share and use best practices, standardize and automate processes, and to ensure coherence of actions taken within Group companies to support implementation of Group Strategy.

The essence of management by processes lies in unending search for and implementation of efficiencies along with clear and transparent division of authorities and responsibilities. Processes are modified to improve their efficiencies. Process documentation is published in the Intranet and available to all employees.

Authorities and process dependences described in process documentation supplement authorities set forth in the organizational structure of individual companies and support operations of TAURON Capital Group companies as a single organism.

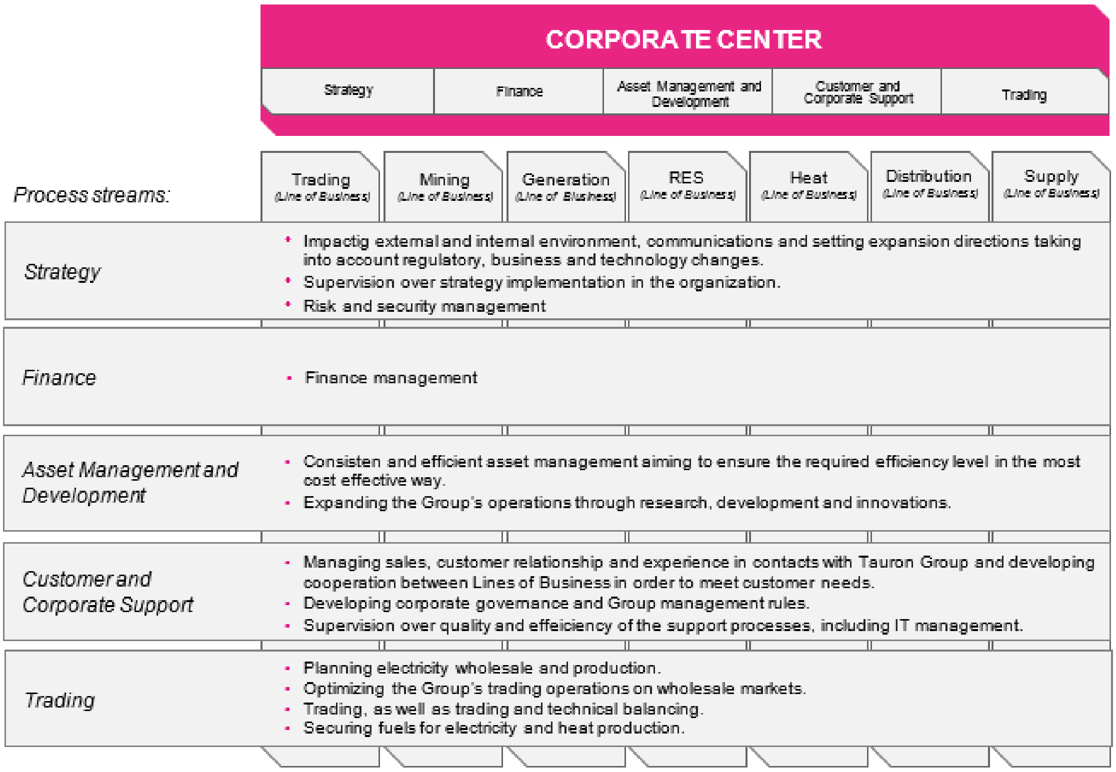
Within TAURON Capital Group the Standing Committees of TAURON Capital Group are operating, including:

1) Investment Committee,

2) Risk Committee.

The aforementioned Committees were established in order to enable performing of operations in accordance with the principles of operating consistency, in compliance with the law and interests of TAURON Capital Group and its stakeholders.
The below figure presents process streams cutting across TAURON Capital Group's Lines of Business

Figure no. 50. Process streams



Business Model identifies 23 mega processes cutting across all units of TAURON Capital Group.

The below figure presents the structure of TAURON Capital Group's processes (mega processes).

Figure no. 51. Structure of TAURON Capital Group's processes (megaprocesses)

Management processes	
1.1 Strategy	1.5 Audit
1.2 Controlling	1.6 Asset management
1.3 Corporate communications	1.7 Research and innovations
1.4 Risk management	

Operational processes	
2.1 Mining	2.4 Electricity and heat distribution
2.2 Electricity and heat production	2.5 Supply and customer service
2.3 Trading	

Support processes	
3.1 Corporate management	3.7 IT support
3.2 Mergers and acqusitions	3.8 Legal services (support)
3.3 Finance management	3.9 Purchasing
3.4 Accounting	3.10 Ensuring security
3.5 Tax management	3.11 Project implementation
3.6 Human capital management	

8.1.4. TAURON Capital Group's Lines of Business

In accordance with the Business Model in force activities are underway aimed at fully implementing the distribution of roles and responsibilities base on assigning the process competences, among:

Corporate Center – superior business unit responsible for management of TAURON Capital Group's operations and taking the most important decisions affecting TAURON Capital Group, Lines of Business, Shared Services Centers and TAURON Capital Group's subsidiaries.

Lines of Business – seven lines of TAURON Capital Group's core operations, defined in accordance with the links of the electricity and heat production value chain, i.e.: Trading, Mining, Generation, Renewable Energy Sources (RES), Heat, Distribution and Supply.

Shared Services Center – units responsible for the provision of specific support services (e.g. Accounting, IT, HR and payroll, insurance, customer service) in favor of other entities of TAURON Capital Group.

TAURON Capital Group's business operations are conducted based on seven Lines of Business defined in accordance with the links of the electricity and heat production value chain: Mining, Generation, Renewable Energy Sources (RES), Heat, Trading, Distribution and Supply.

The below figure presents the structure of TAURON Capital Group's Lines of Business.

Figure no. 52. Structure of TAURON Capital Group's Lines of Business

Lines of Business					
Trading					
Mining	Generation	RES	Heat	Distribution	Supply

TAURON Capital Group's Shared Services Centers (CUW)

Centralizing of the support services is aimed at relieving the Corporate Centre and Lines of Business from execution of processes which are not directly associated with the conducted business operations (so-called support processes) as well as at reducing costs of the implementation of such processes due to the economy of scale and increase of the operational efficiency. Within the formal structure of TAURON Capital Group, CUWs were placed in TAURON Obsługa Klienta, TAURON Ubezpieczenia sp. z o.o. and Wsparcie Grupa TAURON subsidiaries.

8.1.5. Changes in the principles of managing TAURON Capital Group

Changes in the principles of managing the Company

Three amendments were introduced in 2017 in the Organizational By-laws at TAURON aimed to optimize management processes, i.e.:

1. The following key amendments to the Organizational By-laws were enforced on 14 April 2017:
   a) Vice-President of the Management Board for Finance was vested with oversight of the development of forecasting s and tools necessary for analyzing the wholesale and retail markets by subordinating to him the activities of the Executive Director for Business Analyses,
   b) The following positions were changed: Vice-President of the Management Board for Corporate Management to Vice-President of the Management Board for Clients and Corporate Support, and Vice-President of the Management Board for Clients and Trade to Vice-President of the Management Board for Trade,
   c) The Vice-President of the Management Board for Clients and Corporate Support was vested with oversight of representing client interest inside and outside the organization by subordinating to him the Executive Director for Client Affairs,
   d) The sphere of project analysis and assessment was subordinated to the Executive Director for Investment Projects at the Division of the Vice-President of the Management Board for Asset Management and Development,
2. The following key amendments to the Organizational By-laws were enforced on 17 July 2017:
   a) The sphere of the Executive Director for External Relations at the Division of the President of the Management Board was integrated with the sphere of Executive Director for Strategy and Regulations by creating a single sphere of Executive Director for Strategic Management. Integration of both these spheres of activities was justified in light of the operational synergies existing in several planes of operations, particularly in light of the correlation between external communications and building relationships, including relationships with public administration and international authorities as well as with professional industrial organizations,
   b) The sphere of investor relations previously subordinated in the Division of the President of the Management Board to the Executive Director for External Relations was transferred to the Executive Director for Legal Issues. The purpose of this change wad to concentrate in the legal area all tasks related with ensuring adherence by the Company to principles of corporate governance and information duties of a securities issuer.
3. The following key amendments to the Organizational By-laws were enforced on 25 October 2017:
   a) The President of the Management Board was vested with:
      a) oversight over functioning of the risk management system of the TAURON Capital Group by subordinating to him the activities sphere of the Executive Director for Risk Management, who was subordinated previously to the Vice-president of the Management Board for Finance,
      b) creating and overseeing the Company's and TAURON Capital Group system of legal compliance by subordinating the sphere of the Attorney for Compliance to the Executive Director for Security and Compliance,
      c) coordinating and overseeing security activities, including IT security, technical infrastructure security, protection of confidential information and physical security by subordinating to him the sphere of the Executive Director for Security and Compliance, who was previously subordinated to the Vice-president of the Management Board for Clients and Corporate Support.
   b) Vice-president of the Management Board for Clients and Corporate Support was vested with:

a) overseeing the formulation of the IT area functioning and management model by subordinating to him the sphere of the Executive Director for IT, who was previously subordinated to the Vice-president of the Management Board for Finance,

b) overseeing the formulation of strategy as well as standard and guidelines for protection of personal data in the Company and in the TAURON Capital Group, now subordinated to the Executive Director for IT.

At the time, due to the vacancy on position of Vice-president of the Management Board for Trade, these functions were temporarily vested as from 14 April 2017 to the Vice-president of the Management Board for Assets Management and Development, and as from 25 October 2017 temporarily to the Vice-president of the Management Board for Finance.

The below figure presents the diagram of the split of responsibilities of members of the Management Board.

Figure no. 53. Diagram of the split of responsibilities of members of the Management Board

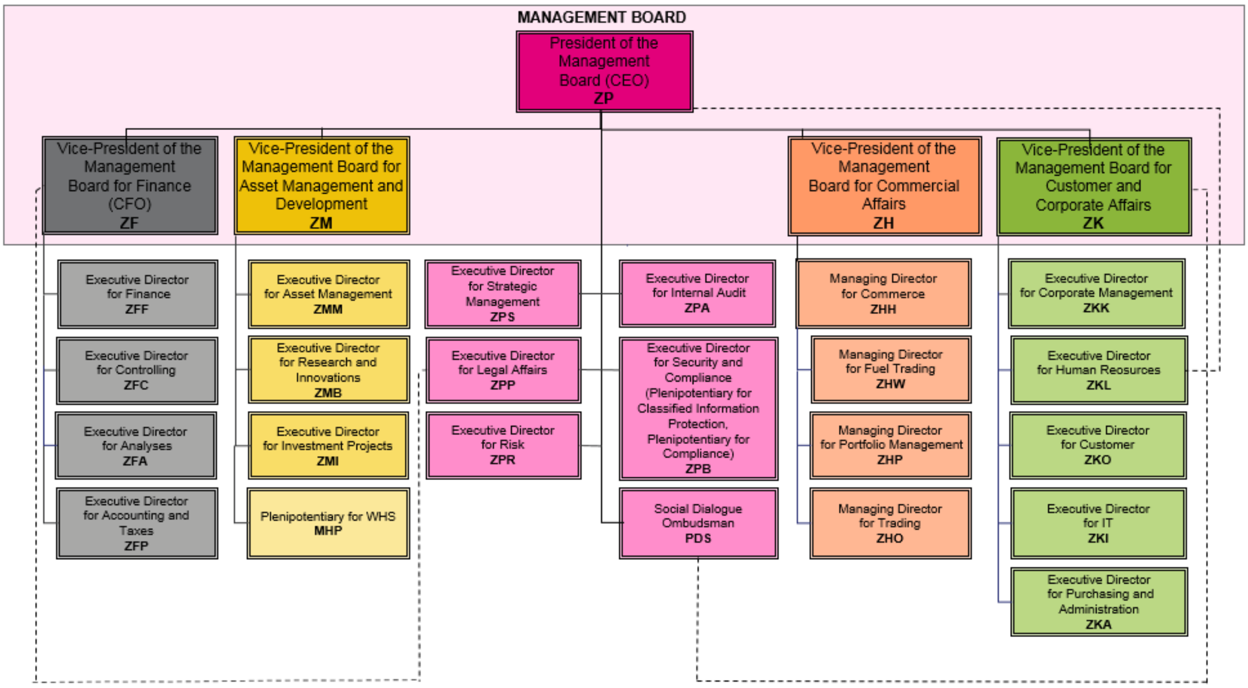
Introducing the above changes to the Organizational By-laws the required modifications of the scopes of the individual business units in the Company's structure were made.

In the general part of the Organizational By-laws provisions on establishing additional reporting lines and prinicples of proceeding in case of conflicting instructions were modified. Furthermore, the power to issue intra corporate regulatory acts was also granted to the Vice President of the Management Board empowered by the Management Board.

Changes to the organisational structure of the Company were aimed at optimizing the operations of the Company and TAURON Capital Group. Areas assigned to the individual divisions managed by members of the Management Board of the Company were revised.

The below figure presents the divisions assigned to the individual members of the Management Board, down to the level of business units and independent work positions reporting directly to members of the Management Board, as of the day of drawing up this report.

Figure no. 54. TAURON's organizational diagram (flowchart) as of the day of drawing up this report



Changes in the principles of managing the TAURON Capital Group

Activities undertaken in implementing the management by processes structure resulted in updating of the Business Model. Scope of authorities and functions attributed to individual Megaprocesses were specified in further detail and supplemented to fully reflect the performed activities in the documents and to ensure possibly high effectiveness. Most important changes include allocation of activities in occupational safety, hygiene and environmental protection to the assets management Megaprocess, transfer of activities related with market forecasting from the trade Megaprocess to the controlling Megaprocess and including public aid activities into the controlling Megaprocess. Some other minor modifications and changes were made in line with the Business Model Structure.

Owners of the Megaprocesses were defined in course of 2017 implementation processes of the Business Model and the Megaprocesses devolved to lower level processes being implemented in their entirety in all companies of the TAURON Capital Group. Full documentation of processes active within TAURON was prepared and published.

Process documentation (maps, diagrams and sheets) were developed, implemented and published in H2 2017 in key companies of the TAURON Capital Group, i.e. at TAURON Wydobycie S.A., TAURON Wytwarzanie S.A., TAURON EKOENERGIA sp. z o.o., TAURON Ciepło sp. z o.o., TAURON Dystrybucja S.A., TAURON Sprzedaż sp. z o.o. and TAURON Obsługa Klienta sp. z o.o.

Process design activities led to identification and elimination of much inefficiency and products of processes not generating added value, as well as added were actions necessary and required for effective implementation of objectives and assumptions resulting from the Strategy. These activities were supported through workshops and training courses for employees participating in process modeling and creating process documentation.

New statutes and company deeds were adopted in 2017 within the TAURON Capital Group companies, implementing principles of management set forth in the *Act of 16 December 2016 on principles of managing State-owned assets*. Provisions defining scope of authorities of corporate bodies that were described in process documents were removed form the deeds. This served to avoid overlaps and prolonging of decision processes in the scope that has been allocated in process documents to other units and persons.

Implementation of the Business Model redefined, redesigned all repeatable processes unifying descriptions that were published in implemented through process documentation. Implemented process documents and tool as well as acquired within the TAURON Capital Group competences in process management and process optimization throughout the Group have become a starting point for attaining further efficiencies and operating effectiveness.

Activities associated with design and implementing of key processes in remaining operating companies of the TAURON Capital Group shall be continued in 2018.

8.2. Key non-financial performance indicators in operations of TAURON Capital Group

Being among the biggest energy sector holdings in Central and Eastern Europe, with operations along the entire energy value chain, the TAURON Capital Group is aware of the influence it has on its broad surroundings – natural environment, stakeholders (employees, customers, shareholders, local communities, suppliers, representatives of authorities and institutions), the micro- and macroeconomic situation and the industry it operates in. While studying its social influence and impacts on the economy, lives of employees, customers, natural environment and communities, the TAURON Capital group is continuously monitoring the non-financial indicators of its operations and presents the results annually in its integrated report.

The integrated formula allows a clear presentation of relations and dependencies between the financial and non-financial aspects of the operations of all companies of the TAURON Capital Group. This makes it a comprehensive and transparent document presenting the company operations, its business model, strategy, key changes, opportunities and risks as well as results from the point of view of all stakeholder groups. Combining the financial data with the non-financial aspects of the TAURON Capital Group is also intended to demonstrate the potential achieved through synergy of the core business with non-business operations, based on the Strategy.

Within the 5 directions set by the Strategy, 18 commitments were made, and due to the need to monitor the extent of their achievement, each commitment was assigned a metric and initiatives.

The key non-financial performance metrics of the TAURON Capital Group include, in line with the Sustainable Development Strategy, the system average interruption frequency index (SAIDI), number of innovative R&D initiatives submitted in employee competitions, the level and monitoring of the Customer Satisfaction Index (CSI), the complaints index as well as offering match indicator.

Striving for the customer relations not to be limited only to providing products and services, while being aware of the numerous threats that may be encountered by customers in various aspects of using or purchasing electricity, TAURON is conducting educational campaigns targeted at electricity consumers, while the performance indicator of these activities is, e.g., the number of delivered initiatives such as “Energy for Seniors”.

The non-financial indicators also concern TAURON Capital Group’s impact on natural environment. Having in mind the sustainable development principles, the companies of the TAURON Capital Group are optimising their resource management processes (water, raw materials and materials) and are executing active waste management policies (with respect to process and communal waste). Important role in environment protection is also played by the pro-environmental education conducted by individual companies of the TAURON Capital Group, addressed to children as well as to adults.

The non-financial performance metrics of environmental operations of the companies of the TAURON Capital Group also include the number and reach of information and education programmes about environment protection addressed to the customers, employees and the local communities.

The non-financial performance metrics of the TAURON Capital Group operations in employee dimension are, for example, indices of injuries, vocational diseases, days lost and absences, as well as fatal work accidents according to regions and gender, as well as the average number of training hours per year per employee according to gender and job category.

The non-financial performance indicators included in the integrated report of the TAURON Capital Group also presented the dual benefits indicators (dual indicators), i.e. non-financial indicators that are clearly related to financial indicators. An example here is energy consumption dynamics. Reduction of electricity consumption is good for the environment (first benefit) and at the same time reduces costs and improves the results of an entity.

The use of non-financial performance indicators allows the TAURON Capital Group a more comprehensive company mapping in the annual integrated reports, presenting processes and events taking place, as well as including in the analyses the factors impacting its success in a longer time horizon.
Non-financial indicators presented in the annual report of the TAURON Capital Group comprehensively present the social impact, characterise the way in which TAURON intends to remedy its negative impact on the natural and social environment and the ways it contributed to its improvement.

8.3. Description of TAURON’s policies

For the purpose of implementation in the national legislation of the Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014, amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups (Non-financial Information Disclosure Directive), the Polish act of 29 September 1994 on accounting (the Accounting Law) was amended.

According to Article 49 b (2) and (3) of the Accounting Law, the scope of information contained in a non-financial report was extended with the description of policies applied with respect to social, employee, natural environment, respect for human rights and corruption countering issues, as well as with description of due diligence procedures applied under these policies and their results.

To assure compliance of the operations of the TAURON Capital Group with the new regulatory requirements, the Management Board of TAURON has in 2017 adopted for use throughout the TAURON Group the following regulations:

1) Customer Oriented Social Policy of the TAURON Group (the Customer Oriented Social Policy),
2) Diversity Policy of the TAURON Group (the Diversity Policy),
3) Environmental Policy of the TAURON Group (the Environmental Policy),
4) Human Rights Respect Policy of the TAURON Group along with Code of Conduct of Business Partners of the TAURON Group Companies (the Human Rights Respect Policy or the Code of Conduct of Business Partners),
5) Work Health and Safety Policy of the TAURON Group (the WHS Policy),
6) Anticorruption Policy of the TAURON Group (the Anticorruption Policy).

Each of the above documents comprehensively presents its subject matter along with an exhaustive description of measures taken by TAURON Capital Group's subsidiaries to achieve the targets adopted in the relevant areas.

8.3.1. Social issues

The responsibilities taken on by the TAURON Capital Group in the area of social issues are governed by the adopted Customer Oriented Social Policy (PRO), aimed at assuring appropriate organisational and business conditions required for achievement of the strategic goals of the TAURON Capital Group concerning its customer and market environment relations. The Customer Oriented Social Policy defines the measures taken by TAURON under a customer dialogue, stresses the importance of building lasting relations both with the customers and the market environment.

8.3.2. Employee issues

Diversity and openness constitute an integral part of both the business operations of the TAURON Capital Group as well as of its *Human Resources Management Policy of the TAURON Group*. The companies of the TAURON Capital Group observe the equal treatment policy and strive to assure diversity with respect to gender, education type, age and professional experience with respect to all employees, and in particular Company authorities and its key managers.

Streamlining of the above measures is supported by the Diversity Policy implemented at the TAURON Capital Group with the key objective of strengthening organisational awareness and culture welcoming diversity.
In employee related matters the TAURON Capital Group also takes measures to prevent discrimination by creating appropriate working atmosphere and culture based on corporate values (Partnership, Development and Courage), as confirmed by implementation of the *Counter Mobbing and Counter Discrimination Policy at the TAURON Group*.

8.3.3. Natural environment

TAURON Capital Group takes on responsibility for caring for the natural environment and the consequences of using its resources. Considering it an important social responsibility, since many years TAURON has been commencing a range of measures aimed at minimising the negative impact of its operations on natural environment.

All companies of TAURON Capital Group have adopted the Environmental Policy that defines the approach to environmental management, including the general direction of environmental operations of the organisation and the principles it follows in environment related matters. The environmental policy is the benchmark for assessing the operation of all companies in the area of environment protection and environmental management; it also documents the values and the vision followed by TAURON Capital Group in its influence on the natural environment.

8.3.4. Respect of human rights

The principles followed by the TAURON Capital Group in the context of respect for human rights and measures taken to prevent their violation as well as support for a climate of dignity and mutual respect are expressed in the Human Rights Respect Policy. This document defines the rules for actions and conduct with respect to human rights that are dedicated to all stakeholders of the TAURON Capital Group, in particular the employees, trading partners and business partners, and include: prohibition of mobbing and discrimination, observing employment and remuneration conditions, work health and safety (WHS).

Due to the nature of operations of the TAURON Capital Group, the area of respect for human rights gives prominent place to aspects relating to work safety assurance. For this reason a separate document was developed that defines the values, rules of conduct and principles of actions concerning the WHS. The goal of the WHS Policy is to achieve the four fundamental goals of work health and safety, being:

1) Assuring optimal working conditions to everyone employed by and working for the TAURON Capital Group.
2) Raising the qualifications of employees of the TAURON Capital Group aimed at building knowledge, commitment and competences of all employees in the area of improvement of their safety and safety of co-workers and persons present at their places of work.
3) Implementing and improving an effective WHS management system, closely related to ongoing operations of the TAURON Capital Group.
4) Eliminating of work related accidents to everyone employed by and working for the TAURON Capital Group and other persons present at the premises of business operations of the companies of the TAURON Capital Group.

Provisions contained in the WHS Policy bind all employees of the TAURON Capital Group as well as all contractors and suppliers of products and services, and any other persons present at the premises of the TAURON Capital Group. The WHS reporting procedures at the TAURON Capital Group are compliant with the Labour Law regulations governing the operation of work place accidents register and informing external authorities about work related accidents and vocational diseases.

Without a business based on respect for human rights there is no possibility to collaborate with the market at the top level. The TAURON Capital Group also expects its business partners to observe the rules and respect human rights of their own employees and to abstain from any forms of breach. As a consequence of supporting the responsible and ethical business conduct, the Code of Conduct of Business Partners was implemented.

8.3.5. Countering corruption

The goal of the Anticorruption Policy in force is to define uniform rules and standards of conduct that allow identifying, countering and mitigating the risk of occurrence of corrupt practices and other kinds of fraud at the companies of the TAURON Capital Group. TAURON has a zero tolerance policy towards corruption and other fraud with respect to all aspects of business and non-business operations of the TAURON Capital Group.

The Anticorruption Policy defines acts of corruption and other practices contrary to the legal regulations in force, internal regulations and corporate regulations of the TAURON Capital Group or ethics. The document defines the obligations relating to countering corruption, potential areas of corruption risk as well as the warning signals the employees should be paying attention to in their daily work. According to the provisions of the Anticorruption Policy, the TAURON Capital Group operates appropriate communication channels allowing the employees to immediately and securely (including anonymous) report potential cases of breach.

8.4. Description of the results of application of policies by TAURON

The basic premise of the Customer Oriented Social Policy is an ongoing survey of general customer satisfaction. At the TAURON Capital Group, one of the key tools for their satisfaction evaluation is the Customer Satisfaction Index (CSI). The survey is performed every Q2/Q3 by an independent research agency. It includes a randomly selected group of customers of TAURON and a group of customers of other energy utilities, such as: ENEA, ENERGA and PGE.

The effects of application of the Customer Oriented Social Policy also include educational initiatives oriented at disadvantaged groups, primarily energy sensitive customers and seniors. The range of topics of these initiatives includes the commercial dangers on the energy market, consumer rights, ways to overcome difficulties with paying the electricity bills, assistance in understanding the bill, etc. In this way TAURON is helping the disadvantaged groups in informed and safe use of the energy market. Educational activities take the form of:

1) information campaigns (e.g. Strangers? Do not answer the door!, i.e. *TAURON is not knocking on doors to sell electricity or gas*),
2) organising educational meetings addressed to senior citizens “Energy for Seniors” (in 2017, five meetings were held - in Limanowa, Nowy Targ, Cieszyn, Wałbrzych and in Bytom),
3) organisation of educational workshops addressed to social assistance workers: “Customer on the horizon” (in 2017, four meetings were held - in Siemianowice Śląskie, Wałbrzych, Kraków and in Wrocław).

The results of implementation of the assumptions of the Customer Oriented Social Policy also include simplification of the marketing communication of products and services as well as providing the customers with an option to pay their distribution service fees and connection charges using electronic payments. Moreover, the partners TAURON collaborates with in the offerings (suppliers of specialised equipment) and in expanding the sales channels (at present, sales through real estate agencies – over 10 partners in total) are selected according to the procedures for establishing collaboration.

Presently the TAURON Capital Group is working on operationalization of the principles of the implemented employee related policies. The measures taken are targeted at creating a culture based on corporate values of Partnership, Development and Courage that support dialogue, openness, mutual tolerance and teamwork.

Moreover, in 2017 an e-learning training was launched on countering mobbing and discrimination at the TAURON Capital Group, which supports the procedures of reporting incidents that may indicate occurrence of mobbing or discrimination.

The result of application of the Environmental Policy by the TAURON Capital Group is a gradual reduction of both the direct and indirect influence on the environment and conducting relevant communication assuring understanding of the operations of the TAURON Capital Group that may be impacting the environment.

The TAURON Capital Group observes all the internationally recognized human rights and supports their protection, while at the same time preventing situations where these rights would be directly or indirectly violated. The Human Rights Respect Policy is binding on all employees, and with the implementation of the Code of Conduct of Business Partners – also on TAURON's business partners. Currently the process of operationalization of the document is under way. Due to the above it is not possible to comprehensively present the results of application of the above policy at present.

The WHS Policy streamlines the rules on the WHS that the TAURON Capital Group has been observing long before the development of this document. The expected result of operationalisation of the WHS Policy is a continuing improvement of work health and safety standards that is to result in, among others, elimination of work related accidents and minimisation of occurrence of vocational diseases and potentially accident prone incidents.
Each and every employee of the TAURON Capital Group is required to study the content of the Anticorruption Policy, respect it unconditionally and sign a statement on having studied its content. Introduction of the Anticorruption Policy at the TAURON Capital Group contributes towards continued improvement of awareness concerning identification of corrupt practices and promotion of honesty and transparent conduct.

8.5. Description of due diligence procedures in operation under the policies applied by TAURON

One of the key metrics of due diligence used in the Customer Oriented Social Policy are the cyclically determined Key Performance Indicators (KPIs) concerning, for example, the number of complaints submitted to the TAURON Capital Group. In its operations TAURON pays particular attention to the procedures aimed at raising customer awareness, thus preventive measures are developed and implemented after post-collection reconnection of electricity supply, i.e. the customers are informed about the need to prepare their premises for renewed electricity supply so as to prevent occurrence of hazards to people and property.

TAURON is planning further delivery of information campaigns, trainings and other initiatives facilitating understanding of the Customer Oriented Social Policy by the employees and developing customer oriented attitudes with:

1) e-learning on products and services offered, increasing the level of knowledge about the customers, primarily addressed to all employees of the TAURON Capital Group,
2) an educational program building customer oriented awareness for all employees of the TAURON Capital Group,
3) development of a knowledge base available to all employees of the TAURON Capital Group (it will provide the employees with the knowledge on current customer oriented initiatives and with the content deepening the knowledge and awareness of employees about customer focus, consumer rights, good practices in customer relations and building positive customer experience in contacts with the TAURON brand).

With respect to employee issues under the policies applied at the TAURON Capital Group, regulations are in force on remuneration and labor law, as well as a standardized *Human Resources Management Policy at the TAURON Group* and *Rules of Compensation at TAURON Group*.

Moreover, respecting the freedom of association, the TAURON Capital Group has a Social Council and dozens of trade union organizations.

The general direction of environmental measures at the TAURON Capital Group includes minimising the negative impact on the environment taking into account the specifics of the sector, technical progress and access to environmentally friendly technologies, achieved by:

1) assuring compliance of operation of all companies of the TAURON Capital Group with the environment protection regulations, taking into account the local conditions and specifics of business operations,
2) collaborating with all parties to and participants in the processes,
3) monitoring and exchange of "industry good environmental practices",

4) ongoing monitoring of the main aspects of direct and indirect environmental impact of operations.

TAURON Capital Group strives to respect human rights and to understand the values of local communities by holding open dialogues with those affected by the company operations. When making business decisions, TAURON analyses the extent of their potential impact on the local communities of the region and seeks to balance its impact on the environment, which is reflected in its *Human Rights Respect Policy*, with its provisions also defining the path for reporting violation of its rules.

Under the due diligence procedures in operation under the human rights respect policies, changes were introduced to the template TOR and detailed TOR documents that constitute attachments to the *Rules for Awarding Contracts at the TAURON Group*, resulting in the requirement on every business partner of the companies of the TAURON Capital Group to submit the statement on having reviewed the Code of Conduct of Business Partners.

Under the due diligence procedures aimed at improving the WHS standards, the TAURON Capital Group measures and benchmarks its results with respect to the WHS both internally and externally, and uses the best identified practices. Moreover it seeks to develop its own best practices in the WHS and conducts internal and external audits with participation of the management staff, employees and their representatives, WHS services and contractors. TAURON also works on initiatives raising the awareness of the WHS among employees, including information and training activities, as well as campaigns oriented at increasing the employee engagement in shaping the work health and safety system at the TAURON Capital Group.

TAURON Capital Group encourages its employees and third parties to come forward with any information on breaches of the Anticorruption Policy and other violations using the dedicated communications channels. The employees and third parties may submit their doubts or request the assistance of the Compliance Officer in case of doubt as to whether a justified suspicion arises in specific situation of breach of provisions of the Anticorruption Policy or other legal regulations, internal company regulations or corporate regulations of the TAURON Capital Group or of ethical standards. All submissions are treated with confidence and studied with due diligence.

TAURON is taking measures to raise employee knowledge and awareness of combating corruption. In 2017, TAURON has organized workshops for the members of the management staff on topics of corruption. Similar trainings particularly dedicated to the staff from procurement and investments areas took place also at the other companies of the TAURON Capital Group. In 2018, TAURON is planning to deliver information initiatives, trainings and other measures facilitating correct understanding of the Anticorruption Policy by the employees and following its principles in their daily work.

8.6. Description of significant risks related to operations of TAURON that may exert adverse impact on the policies applied by TAURON, as well as description of management of these risks

Under the risk management process employed by the TAURON Capital Group, risks related to operations of the companies were identified that could exert adverse impact on the social, employee, natural environment, respect for human rights and anticorruption issues as well as on policies employed by TAURON.

According to regulations in force, for every identified risk its Risk Owner is appointed and made responsible for this risk management, risk records are developed containing descriptions of mitigation measures conducted, risk measurement parameters and early warning indicators are defined and in particular cases separate risk response and backup plans are developed. These risks are included in the risk model that defines the categories of risks present in the operations of TAURON.

The key risks include: social risk, human capital management risk, WHS risk, internal communication risk, environmental risk, procurement process risk, legal risk and compliance risk.
The below table below characterizes the risks related to the operations of TAURON that could exert adverse impact on the policies employed by TAURON.

Table no. 33. Risks related to the operations of TAURON that could exert adverse impact on the policies employed by TAURON

#	Risk name	Risk description	Risk response
1.	Social risk	The risk includes failing to meet customer service standards, to deliver on sales agreements, external communications and marketing activities and the personal data protection related risk. Risk materialisation could result in loss of reputation and customer trust, customer disputes, non-achievement of goals including sales targets and possible penalties for legal noncompliance concerning personal data protection.	• Adoption and execution of Customer Oriented Social Policy. • Holding a dialogue with customers, including customer satisfaction surveys, tailoring the product offering to their needs, looking after high customer service levels. • Building relations with the customers and market environment. • Responsibility for the product including quality and security of supply, tailoring the product offering to customer needs. • Customer personal data privacy and security protection.

#	Risk name	Risk description	Risk response
			• Implementing tools supporting execution of customer focused social policy. • Standardisation of customer agreement templates and their adaptation to legislation changes and optimisation of sales and service processes. • Delivery of promotional activities in line with the adopted *TAURON brand strategy* and *TAURON Group sponsoring strategy for 2018-2025*, taking into account respect for human rights and conducting responsible marketing.
2.	Human capital management risk	Risk relating to employee issues including diversity, inclusion, employment conditions and respect of right of association, capital management, career paths and recruitment management, training system, work health and safety management. Risk materialisation results in employee complaints, collective disputes, strikes, loss of specialised staff and problems with its restoration.	• Adoption and execution of the Employee Recruitment, Selection and Adaptation Policy. • Adoption and execution Counter Mobbing and Counter Discrimination Policy. • Looking after development of employee competences, including through participation in trainings. • Holding consultations with social organisations within the TAURON Capital Group. • Execution of the staffing policy based on the Competence Model and Rules of Compensation, and Rules of Work. • Adoption and implementation of the Diversity Policy. • Adoption and implementation the Human Rights Respect Policy.
3.	Work Health and Safety (WHS) risk	Risk relating to ensuring health and safety at work. Risk materialisation result is employee injury, health loss or excessive employee exposure to hazards.	• Prioritisation of employee, customer, contractor and stakeholder safety in the business activities performed. • Adoption and execution of the *Work Health and Safety Policy of the TAURON Group*. • Assuring optimal working conditions. • Raising employee qualifications with respect to work safety improvements. • Conducting trainings, implementation and improvement of WHS management system.
4.	Internal communication risk	Risk relating to assuring optimal and effective communication within the TAURON Group and transmission of honest information to employees of the TAURON Capital Group while observing confidentiality of sensitive information. Risk materialisation result is a loss of trust in the employer, increased social unrests, loss of reputation and negative impact on the TAURON brand.	• Building relations with the social side at the TAURON Capital Group and close cooperation with the Social Dialogue Spokesperson. • Use and development of available communications tools to provide significant information to the employees of the TAURON Capital Group. • When providing significant information – organisation of fact to face meetings of the management staff with the employees. • Ongoing monitoring of situation and events at companies of the TAURON Capital Group that could result in social unrests. • Regular meetings with the representatives of companies dealing with internal communication to exchange information. • Developing the Communication Strategy for the TAURON Group.
5.	Environmental risk	Risk relating to impact of business operations on natural environment and the use of its resources, pollution control and prevention, protection of water sources and waste management. Risk materialisation result is a degradation of natural environment and penalties for failing to meet environmental requirements, the need to remedy them, to limit production, possibility of benefiting from subsidy programmes and loss of image of the TAURON Capital Group.	• Adoption and implementation of *Environmental Policy of the TAURON Group.* • Conducting business operations impacting the natural environment according to sustainable development principles. • Identification of areas of environmental impact and assuring the operation of the TAURON Capital Group in compliance with the environment protection laws. • Continuing development of knowledge and environmental responsibility culture among the employees, customers and business partners of the TAURON Capital Group. • Seeking solutions aimed at implementing circular economy principles at the TAURON Capital Group and actively seeking technical and organisational solutions that minimise the negative impact of operations on the environment. • Improvement of energy efficiency and efficient water management. • Offering products / services that take into account the aspect of limiting the negative environmental impact.

#	Risk name	Risk description	Risk response
			• Promoting conservation of nature and relevant collaboration with local government and central government administration bodies.
6.	Procurement process risk	Risk relating to the exercised procurement procedures, taking into account prevention of violation of human rights by business partners, countering corruption and fraud in procurement processes and observing ethical and moral standards in their progress. Risk materialisation result are non-optimal purchase contracts, need to annul tendering procedures, loss of image of the TAURON Capital Group and credibility to stakeholders.	• Adoption and implementation of the Code of Conduct of Business Partners of the TAURON Group. • Adoption and execution of the *Anticorruption Policy of the TAURON Group*. • Adoption and execution of the *Human Rights Respect Policy*. • Standardisation of conducting procurement processes and their transparency. • Building lasting business partner relationships based on trust and mutual respect. • Expecting the business partners to observe the legal regulations, ethics standards and fair trading practices, including work health and safety, prevention of discrimination and unequal treatment, respecting employee human rights and dignity, transparent HR policy, environment protection, fair competition, fraud prevention and combating, as well as information security and protection. • Use of standard template agreements and standard clauses in contracts providing for respect for human rights by the business partners of the TAURON Capital Group.
7.	Legal risk	Risk relating to non-observance of legal regulations, misinterpretation of new rules and regulations, requirements imposed by the regulator and the supervisory bodies.	• Ongoing monitoring of the legal environment and amendments to legal regulations, including in scope of social issues, respect for human rights, countering corruption, environment protection and employee issues. • Implementation of the required amendments to the in-house regulations. • Appointing working parties tasked with developing and implementing the required changes resulting from the legal environment. • Ongoing cooperation with the bodies supervising the energy market and the capital market. • Training the employees in legal regulations and in-house regulations.
8.	Compliance risk	Compliance risk includes the risk of internal fraud, external fraud and non-ethical conduct. Risk relating to misappropriation or improper use of Company assets, their devastation, abuse of official position for personal gains, acts by third parties aimed at theft, burglary, counterfeiting and related to occurrence of conduct violating generally accepted social coexistence standards, moral standards and mobbing.	• Adoption and implementation of *Code of Conduct of Business Partners of the TAURON Group*. • Adoption and execution of the *Anticorruption Policy of the TAURON Group*. • Adoption and execution of the *Human Rights Respect Policy*. • Adoption and execution of the *Counter Mobbing and Counter Discrimination Policy*. • Adoption and implementation of the *Diversity Policy*. • Use of internal procedures aimed at fraud prevention (security procedures, reviews of authorisations), their testing and improvement. • Promoting best practices, improvement of procedures, conducting trainings and observing the Code of Business Ethics of the TAURON Group and operation of a fraud reporting system. • Building an organisational culture based on values and principles of the TAURON Group.

9. OTHER MATERIAL INFORMATION AND EVENTS

9.1. Proceedings pending before the court, competent arbitration authority or public administration authority

During the reporting period no proceedings were pending before any court, competent arbitration authority or public administration authority, related to the Company, the standalone or aggregate value of which would represent at least 10% of TAURON's equity.

Furthermore, during the reporting period no proceedings were pending before any court, competent arbitration authority or public authority body, related to the subsidiaries of TAURON Group, the standalone or aggregate value of which would represent at least 10% of TAURON's equity.

9.2. Information on agreements concluded by TAURON Capital Group's subsidiaries

9.2.1. Agreements significant for TAURON Capital Group's operations

In the financial year 2017 and until the day of drawing up this report TAURON Capital Group's subsidiaries concluded the following agreements significant for the operations of TAURON Capital Group:

Concluding of the amendment to the agreement with the RAFAKO S.A. - MOSTOSTAL WARSZAWA S.A. consortium on the construction of a power generation unit at Jaworzno III Power Plant

On March 1, 2017 the Management Board of TAURON's subsidiary - TAURON Wytwarzanie (Ordering Party) signed with the RAFAKO S.A. - MOSTOSTAL WARSZAWA S.A. consortium (Contractor) an amendment to the agreement on the construction of a 910 MWe power generation unit for super critical parameters at Jaworzno III Power Plant - Elektrownia II, currently carried out by the Ordering Party's spun off branch – Oddział Jaworzno 910 MW in Jaworzno, with respect to: steam boiler, turbine set, main building, electric part and the unit's instrumentation and control (I&C).

Under the amendment the agreement's net price was increased by PLN 71.05 mln, i.e. to PLN 4 470 mln, and the deadline for completing the subject of the agreement was extended by 8 months, i.e. until the 67th month from the date of concluding the agreement at the latest which means that the new assumed date of handing over the unit for operation is November 2019.

The decision to sign by TAURON Wytwarzanie of the above mentioned amendment was taken on February 28, 2017. On the same day also the Management Board of TAURON issued a positive opinion on the conclusion of the amendment on the above mentioned terms.

Amendments to the agreement were due to the need to change the unit's facilities' foundations to the deep foundations, and also due to the parties to the agreement agreeing on additional works beneficial to the Ordering Party for technical and economic reasons (erecting the foundation for the fifth electrofilter (EF) zone and extending the EF switchgear building). The additional works will allow the Ordering Party to achieve savings during the planned outage of the unit in 2021 in order to partly adapt the unit to comply with the future BAT conclusions requirements. The Ordering Party partly accepted the Contractor's claims related to the above circumstances and the change necessity protocols as justified. The claims due the change of the design standards – EUROKODY, were not accepted as justified by the Ordering Party.

Due to the above the warranties granted by the Contractor were extended:

1) by 6 months with respect to the Unit's availability for the direct shipments carried out by RAFAKO S.A., boiler maximum continuous rating, unit's technical minimum and flue gas water content behind FGD, vibration level for a structure,
2) by 12 months with respect to the unit's design and construction.

The Contractor will also ensure an appropriate extension of the agreement's performance bond.

Signing of the amendment changed the terms of the agreement with the Contractor, however it had no impact on the change of the entire investment project's budget.

The Company provided information on the amendment to the above mentioned agreement in the regulatory filings (current reports): no. 5/2017 of February 28, 2017 and no. 7/2017 of March 1, 2017.

Coming into force of the agreement and amendments on the terms of further implementation of the "CCGT unit's construction at Stalowa Wola" project

On March 31, 2017, in reference to the earlier concluded agreements and amendments on the terms of further implementation of the "CCGT unit's construction at Stalowa Wola" project (Project), as described in the regulatory filing (current report) no. 36/2016 of October 27, 2016 ECSW issued an instruction to make the payment to the institutions so far providing the financing for ECSW, i.e. European Investment Bank, European Bank for Reconstruction and Development, Bank Polska Kasa Opieki S.A. (Financing Institutions) of PLN 581.4 mln as the repayment of all of ECSW's liabilities towards the Financing Institutions. Upon the crediting of the Financing Institutions' bank accounts the suspending conditions were met and at the same time the documents described in the above mentioned report (filing) came into force, i.e.:

1) agreement on establishing the basic boundary conditions of the Project's restructuring among TAURON, PGNiG and ECSW,
2) amendment to the electricity sale Agreement of March 11, 2011 (Electricity Sale Agreement) among TAURON, PGNiG and ECSW,
3) amendment to the gas supply Agreement of March 11, 2011 (Gas Agreement) between PGNiG and ECSW.

The agreement governs, first of all, the conditions of settling the liquidated damages, making the so far used pricing formulas market based and the Project's financial restructuring issues and it constitutes a reflection of the will of the Project's sponsors, i.e.: TAURON and PGNiG (Sponsors) with respect to the continuation of the CCGT unit's construction, making changes to the Gas Agreement and the Electricity Sale Agreement and changing Project's financing formula from project finance to corporate finance.

Changes to the Gas Agreement and the Electricity Sale Agreement envisage in particular making the pricing formulas used in these agreements market based. Furthermore, due to the delay in the Project's implementation, the amendment to the Gas Agreement envisages a change with respect to amounts, deadlines and methodology used to assess liquidated damages.

ECSW acquired the funds for the bank loans' repayment under loan agreements according to which each of the Sponsors granted ECSW a PLN 290.7 mln loan.

In accordance with the provisions of the standstill agreement mentioned in the regulatory filing (current report) no. 36/2016 the Financing Institutions were obligated to return the bank guarantees received from the Sponsors for the total amount of approx. PLN 629m, where the total amount of bank guarantees provided by TAURON was PLN 314.5 mln.

Irrespective of the above the Sponsors, along with ECSW, are continuing joint works aimed at acquiring new financing for the CCGT unit's construction project at Stalowa Wola the terms and the structure of which would be more favorable than the existing agreements.

The Company disclosed information on the above event in the regulatory filing (current report) no. 11/2017 of March 31, 2017.

The bank guarantees for PLN 314.5 mln issued at TAURON's instruction in order to guarantee the banks' liabilities under the loans granted to ECSW mentioned in the above regulatory filing (current report) expired in April 2017.

Signing of the agreement on potential cooperation in the implementation of the construction of a 910 MW power generation unit project at Jaworzno III Power Plant and the termination of the investment agreement related to the CCGT unit at Łagisza Power Plant

In reference to the Strategy that assumes an implementation of the construction of a 910 MW power generation unit project at Jaworzno (Project) under the new financing formula, envisaging spinning off of an organized part of an enterprise including the above mentioned investment project into a new special purpose vehicle, and then external partners joining the company, on June 1, 2017 TAURON signed the Agreement on the preliminary terms of potential cooperation as part of the Project with Fundusz Inwestycji Infrastrukturalnych – Kapitałowy Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych and Fundusz Inwestycji Infrastrukturalnych – Dłużny Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych (Funds), managed by Towarzystwo Funduszy Inwestycyjnych BGK S.A. A part of the investment portfolio of the above mentioned Funds is managed by Polski Fundusz Rozwoju S.A.

Under the Agreement the Funds expressed a preliminary interest in investing in the Project PLN 880 mln in total, by way of the Funds taking up new shares in the Nowe Jaworzno GT special purpose vehicle, that is currently TAURON's wholly owned company currently implementing the Project. The Funds' share in the share capital of Nowe Jaworzno GT cannot be higher than 50% minus one share. The other shares in Nowe Jaworzno GT will be held by the Company or by the Company and an additional Investor (Investors), where the Company will own at least 50% plus one share in Nowe Jaworzno GT. The Agreement expresses the will of the parties to conduct, in good faith, negotiations aimed at defining the rules of potential cooperation in implementing the Project. The joining of the Project by the Funds will be dependent on the results of the detailed analysis of the Project by the Funds, the parties agreeing and fulfilling the conditions defined in the documentation of the transaction and the Funds obtaining the required investment consents to take part in the Project. The Agreement shall be valid until December 31, 2017.

At the same time on June 1, 2017 an agreement was signed between TAURON Wytwarzanie and PFR under which the investment agreement concluded between the above mentioned entities aimed at the joint implementation of the project ”Construction of a 413 MWe CCGT unit at TAURON Wytwarzanie Spółka Akcyjna Oddział Elektrownia Łagisza in Będzin” was terminated. The Company provided information on the conclusion of the investment agreement in the regulatory filing (current report) no. 17/2015 of July 13, 2015. The termination of the investment agreement is in line with the assumptions of the Strategy envisaging stopping of the investment in the CCGT unit at Łagisza Power Plant which translates into the reduction of capital expenditures for this purpose by approximately PLN 1.5 bln.

In reference to the term (expiration date) of the above mentioned Agreement, on December 29, 2017 TAURON signed an amendment under which the Agreement on potential cooperation in the implementation of the 910 MW power generation unit construction project in Jaworzno was extended until February 28, 2018.

The other provisions of the above mentioned Agreement were not changed.

On February 28, 2018 TAURON informed of the will, expressed by the parties to the Agreement, to continue activities aimed at signing agreements that will define the terms of the Funds’ equity investment in the Special Purpose Vehicle.

The intention of the parties is to have the Funds join the Special Purpose Vehicle and participate in the successive recapitalizations of the Special Purpose Vehicle, by taking up the newly created shares in exchange for financial contributions up to the total maximum amount of PLN 880 mln.

The Funds’ share in the Special Purpose Vehicle’s share capital, as of the day the Unit is commissioned, should reach approx. 14%, while TAURON’s share should reach at least 50% + 1 share. Joining the Special Purpose Vehicle by the Funds will be contingent on the fulfillment of the conditions that will be defined in the agreements.

The Company disclosed information on the above events in the regulatory filings (current reports): no. 25/2017 of June 1, 2017, no. 43/2017 of December 29, 2017 and no. 4/2018 of February 28, 2018.

Extension of the bond issue program

On June 20, 2017 amendments were signed to the agreements related to the bond issue program (Program), i.e. agency and custody agreement and underwriting agreement of the conclusion of which the Company provided information in the regulatory filing (current report) no. 49/2015 of November 20, 2015. Under the above amendments the following extension of the Program was made:

a) one year, i.e. until December 31, 2021 (”Extension Period I”). Program amount in Extension Period I will be PLN 5.32 bln maximum, and the following banks joined the extension: MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland, Bank Zachodni WBK S.A., CaixaBank S.A. (Joint Stock Company) Branch in Poland, Industrial and Commercial Bank of China (Europe) S.A. Branch in Poland, ING Bank Śląski S.A., Powszechna Kasa Oszczędności Bank Polski S.A. and mBank S.A.,

b) by two years, i.e. until December 31, 2022 (”Extension Period II”). Program amount in Extension Period II will be PLN 2.45 bln maximum, and the following banks joined the extension: MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland and Powszechna Kasa Oszczędności Bank Polski S.A.

Until December 31, 2020 the Program amount will not change and will be PLN 6.27 bln maximum. The margin of the financing under the Program did not change due to the extension made.

On the other hand on March 9, 2018 amendments to the agency and custody agreement as well as the underwriting agreement were signed, the result of which is an extension by some banks of the period of availability of the funds under the Program.

This means that the maximum value of the Program:

a) is PLN 6.27 bln until December 31, 2020 (this amount did not change as a result of signing the amendments),

b) is PLN 6.07 bln until December 31, 2021 (it had been PLN 5.32 bln before the amendments were signed),

c) is PLN 5.82 bln until December 31, 2022 (it had been PLN 2.45 bln before the amendments were signed).

The amendments were signed with the following banks taking part in the Program: Bank Handlowy in Warsaw S.A., Bank BGŻ BNP Paribas S.A., Bank Zachodni WBK S.A., CaixaBank S.A. (Joint Stock Company) Branch in Poland, Industrial and Commercial Bank of China (Europe) S.A. Branch in Poland, ING Bank Śląski S.A., mBank S.A., MUFG Bank (Europe) N.V., MUFG Bank (Europe) N.V. S.A. Branch in Poland and Powszechna Kasa Oszczędności Bank Polski S.A.

The information on the above events was disclosed by the Company in the regulatory filings (current reports) no. 29/2017 of June 20, 2017 and no. 6/2018 of March 9. 2018.

Conclusion of the coal purchase agreement with Polska Grupa Górnicza S.A.

On January 18, 2018 a coal purchase agreement was signed between TAURON and Polska Grupa Górnicza S.A. with the subject of the agreement being the purchase of thermal coal for the production needs of TAURON Capital Group's power generating units. The estimated value of coal supplies in the 2018-2021 time frame, based on the coal price agreed for 2018, will reach the net amount of approximately PLN 2.15 bln. The coal price was agreed for the first year of the agreement's term, while in the subsequent years the coal price will be indexed based on the formula included in the agreement, taking into account changes of the market conditions. The above agreement was concluded for an indefinite period of time and it provides for liquidated damages in the amount of 10 percent of the value of unrealized deliveries in the given year.

The information on the above event was disclosed by the Company in the regulatory filing (current report) no. 1/2018 of January 18, 2018.

Financing for EC Stalowa Wola subsidiary

On March 8, 2018 in reference to the current report no. 11/2017 of March 31, 2017 with respect to the information on actions related to obtaining new financing for the CCGT unit construction project at Stalowa Wola, EC Stalowa Wola (Loan Taker), i.e. entity in which the TAURON holds indirectly, via its TAURON Wytwarzanie S.A. subsidiary, a 50% stake in the share capital; signed a loan agreement with BGK and PGNiG.

Under the above mentioned agreement BGK and PGNiG will grant the Loan Taker a loan in the amount of PLN 450 mln each, to be used to refinance the Loan Taker's debt towards the Issuer and PGNiG (PLN 600 mln) and to cover the Loan Taker's further capital expenditures (PLN 300 mln). The agreement was concluded for the period lasting until June 14, 2030.

As of March 8, 2018 the Loan Taker's current loan liabilities towards the Issuer were approximately PLN 610 mln.

The loan agreement provides for the funds to be paid out to the Loan Taker after the suspending conditions have been met, with one of them being presenting to BGK of a bank guarantee issued at the Issuer's instruction and securing the Loan Taker's debt towards BGK. The bank guarantee will be renewed annually, and its value will not exceed PLN 517.5 mln.

The information on the above event was disclosed by the Company in the regulatory filing (current report) no. 5/2018 of March 8, 2018.

9.2.2. Transactions with related entities on terms other than at arm's length

All transactions with related entities are concluded at arm's length.

The detailed information on the transactions with related entities is provided in note 49 of the consolidated financial statements for the year ended on December 31, 2017.

9.2.3. Signed and terminated credit and loan agreements

Working capital credits and short term loans

In accordance with the financing model adopted by TAURON Capital Group, only TAURON may act as a party to working capital credits and short-term loans raised with external institutions.

TAURON Capital Group is using a true cash pooling structure, implemented under the cash management agreement concluded with PKO BP (the former agreement expired on December 17, 2017, while the new agreement came into force on December 18, 2017, valid until December 17, 2020). The cash pooling structure is based on daily limits granted to individual participants by the agent managing the service, i.e. TAURON. As a result of implementing the cash pooling mechanism, cash transfers are performed between accounts of participants of the service and the agent's account. Within the cash pooling structure TAURON uses at PKO BP:

1) overdraft limit in the amount of PLN 300,000 thousand, based on the overdraft agreement concluded with the bank in October 2017, with the repayment date falling on December 29, 2017 (the former overdraft limit agreement of December 2014 expired on December 29, 2017), and

2) intraday limit in the amount of PLN 500,000 thousand, effective until December 17, 2020 (the effective date was extended under the amendment to the bank account concluded in October 2017). The intraday limit is a daily limit which must be fully repaid by the end of each day on which it was used).

As part of financing its ongoing operations following agreements were also in force:

1) overdraft agreement with BGK, up to the amount of EUR 45,000 thousand with the repayment date of December 31, 2017. The overdrawn amount is used for financing of the transactions of purchase/ sale/ exchange of CO2 emission allowances, trading in electricity and gas made on the European exchanges, (accordingly, under amendments no. 1 and no. 2 to the overdraft agreement, concluded in May and December 2017, its amount was raised from EUR 25 000 thou. to EUR 45 000 thou. and the effective date was extended until December 31, 2018).

2) overdraft agreement concluded with mBank for the amount not exceeding of USD 2,000 thousand, to be used for financing the ongoing operations, in particular, for financing the collateral margin and commodity products transactions. The repayment deadline of the loan, pursuant to the amendment of January 12, 2017, falls on March 31, 2018.

The use of above described foreign currency loans is aimed at mitigating the FX risk related to the trade transactions concluded.

The EUR 6 600 thou. loan agreement concluded with TAURON Sweden Energy, valid until July 30, 2017, expired in 2017. The loan was repaid in full by the deadline stated in the agreement.

The below table presents a detailed summary of the working capital loan and credit agreements effective as of December 31, 2017.

Table no. 34. Summary of TAURON Capital Group's working capital loan and credit agreements as of December 31, 2017

No.	Type of agreement	Interest rate	Amount of credit/loan (thou.)	Period of financing	Balance as of December 31, 2017 (thou.)
1.	Overdraft facility	LIBOR 1M + fixed margin	2 000 USD	16.04.2015 - 30.03.2018	417 USD
2.	Overdraft facility	EURIBOR 1M + fixed margin	45 000 EUR	09.05.2017 - 31.12.2018	22 060 EUR
3.	Overdraft facility	WIBOR O/N + fixed margin	300 000 PLN	30.12.2017 - 29.12.2020	0 PLN
4.	Intraday limit	None	500 000 PLN	18.12.2017 r. - 17.12.2020	0 PLN

Investment credits and loans

The Company did not take on new credit and loan agreements and did not terminate any existing credit and loan agreements in 2017.

The below table presents a detailed summary of investment credit and loan agreements as of December 31, 2017.

Table no. 35. Summary of investment credit and loan agreements as of December 31, 2017

No.	Parties to the agreement	Type of agreement and interest rate	Amount of credit/loan (thou.)	Period of financing	Balance as of December 31, 2017 (thou.)
1.	EIB loan	fixed margin	210 000 PLN	30.01.2012 - 15.12.2021	84 000 PLN
2.	EIB loan	fixed margin	300 000 PLN	20.02.2012 - 15.12.2021	120 000 PLN
3.	EIB loan	fixed margin	450 000 PLN	16.07.2012 - 15.06.2024	265 909 PLN
4.	EIB loan	fixed margin	200 000 PLN	25.01.2013 - 15.09.2024	127 273 PLN
5.	EIB loan	fixed margin	250 000 PLN	22.02.2013 - 15.09.2024	159 091 PLN

No.	Parties to the agreement	Type of agreement and interest rate	Amount of credit/loan (thou.)	Period of financing	Balance as of December 31, 2017 (thou.)
6.	EIB loan	fixed margin	295 000 PLN	17.07.2015 - 15.03.2027	280 250 PLN
7.	Loan from TAURON Sweden Energy	fixed margin	166 572 EUR	03.12.2014 - 29.11.2029	166 572 EUR

9.2.4. Loans and sureties granted as well as sureties and guarantees received

Loans granted

In 2017 TAURON granted financing to its co-subsidiary, EC Stalowa Wola, in the form of loans to be used for the current operations of EC Stalowa Wola and the repayment of loan instalments of this subsidiary towards the European Investment Bank, European Bank for Reconstruction and Development and Pekao S.A. Furthermore, the agreement consolidating ECSW's debt due to the loans granted to the company before was signed in 2017.

In 2017 the PLN 1 120 000 thou. loan agreement concluded with TAURON EKOENERGIA was still in force. Under amendment no. 2 to this agreement, signed on February 22, 2017, the repayment date was extended until February 27, 2018. In the meantime, in November 2017, a partial early loan repayment was made in the amount of PLN 1 000 000 thou.

On November 8, 2017 the Company concluded, with PGE EJ 1 sp. z o.o., an agreement on a PLN 2 940 thou. loan for the period of 3 years from the date of concluding the agreement, i.e. until November 6, 2020.

The below table presents a summary of loans granted by TAURON and effective as of December 31, 2017.

Table no. 36. Summary of loans granted by TAURON and effective as of December 31, 2017

No.	Type of agreement/Beneficiary	Interest rate type	Loan amount under the agreement (thou.)	Effective term	Balance as of December 31, 2017 (thou.)
1.	Loan EC Stalowa Wola	WIBOR 3M + fixed margin	177 000 PLN	20.06.2012 - 31.12.2032	177 000 PLN
2.	Loan EC Stalowa Wola	WIBOR 3M + fixed margin	15 850 PLN	14.12.2015 - 31.12.2027	15 850 PLN
3.	Loan EC Stalowa Wola	WIBOR 6M + fixed margin	15 300 PLN	15.12.2016 - 31.12.2027	11 000 PLN
4.	Loan EC Stalowa Wola	WIBOR 6M + fixed margin	150 000 PLN	30.06.2017 - 28.02.2018	150 000 PLN
5.	Loan EC Stalowa Wola	WIBOR 6M + fixed margin	175 157 PLN	01.11.2017 - 28.02 2018	175 157 PLN
6.	TAURON EKOENERGIA	fixed interest rate	1 120 000 PLN	27.02.2015 - 27.02.2018	120 000 PLN
7.	PGE EJ 1	fixed interest rate	2 940 PLN	08.11.2017 - 06.11.2020	2 940 PLN

Sureties and guarantees granted

TAURON Capital Group's principles of granting collaterals are based on TAURON Capital Group's regulation in force.

The below table presents a summary of collaterals granted by TAURON effective as of December 31, 2017.

Table no. 37. Summary of collaterals granted by TAURON, effective as of December 31, 2017

No.	Beneficiary	Agreement/Collateral	Entity whose liabilities constitute the subject of collateral	Amount (thou.)	Effective date
1.	WFOŚiGW	Bills of exchange with a promissory note	TAURON Wytwarzanie	40 000 PLN	15.12.2022
2.	WFOŚiGW	Bills of exchange with a promissory note	TAURON Ciepło	30 000 PLN	15.12.2022
3.	WFOŚiGW	Surety agreement	KW Czatkowice	914 PLN	15.06.202.
4.	PSG	Surety agreement	TAURON Sprzedaż	15 000 PLN	31.03.2018

No.	Beneficiary	Agreement/Collateral	Entity whose liabilities constitute the subject of collateral	Amount (thou.)	Effective date
5.	PSE	Surety agreement	TAURON Wytwarzanie	5 000 PLN	04.08.2019
6.	GAZ-SYSTEM	Surety agreement	EC Stalowa Wola	1 667 PLN	30.07.2020
7.	Doradcy Funduszu (Fund (Advisors)	Surety agreement	Nowe Jaworzno GT	2 350 PLN	28.09.2025
8.	Businesses and consumers that concluded an agreement TAURON Ekoenergia based on the electricity trading license granted by the President of ERO	Corporate guarantee	TAURON EKOENERGIA	16 400 PLN	31.12.2030
9.	NCBiR	Bills of exchange with a promissory note	TAURON	1 869 PLN	31.03.2026
10.	NCBiR	Bills of exchange with a promissory note	TAURON	2 375 PLN	31.07.2024
11.	Bondholders	Corporate guarantee	TAURON Sweden Energy	168 000 EUR	03.12.2029

The following framework (master) agreements, under which bank guarantees were issued, continued to be in force in 2017:

1) Framework (master) agreement of June 8, 2015 on a limit on bank guarantees, concluded with BZ WBK, with the effective date of June 7, 2018 and an extension option by another 12 months. The limit amount of PLN 150 000 thou. to be used by TAURON and its subsidiaries in favor of the beneficiary - Izba Rozliczeniowa Giełd Towarowych S.A. (IRGIT).
2) Framework (master) Agreement of July 12, 2016 on a limit on bank guarantees, concluded with CaixaBank S.A. (Joint Stock Company) Branch in Poland (CaixaBank), under which a limit was granted for the period of 36 months, i.e. until July 11, 2019 . The maximum effective term of the bank guarantees issued within the limit shall not exceed July 11, 2020. The limit to be used by TAURON and its subsidiaries in conjunction with their operations.

Within the bank guarantee limit obtained from BZ WBK in 2017 TAURON was ordering issuing of bank guarantees for the benefit of IRGIT as a security for the transactions made on TGE, with the effective term of less than one year.

The below table presents a summary of bank guaranties granted under the agreements effective as of December 31, 2017.

Table no. 38. Summary of bank guaranties granted under the agreements effective as of December 31, 2017

No.	Bank	Company	Beneficiary	Type of guarantee	Amount (thou.)	Launch date	Effective date
1.	BZ WBK	TAURON	IRGIT	payment	30 000 PLN	11.08.2016	31.03.2018
2.	BZ WBK	TAURON	IRGIT	payment	20 000 PLN	14.12.2016	31.03.2018
3.	CaixaBank	TAURON	PSE	performance bond	4 041 PLN	01.01.2017	11.02.2018
4.	CaixaBank	TAURON	GAZ-SYSTEM	performance bond	2 661 PLN	01.12.2017	30.11.2018
5.	CaixaBank	KW Czatkowice	PGE	performance bond	147 PLN	09.09.2016	31.01.2018
6.	CaixaBank	TAURON Dystrybucja Serwis	Strabag Infrastruktura Południe	performance bond	116 PLN	09.09.2016	15.06.2019
7.	CaixaBank	TAURON Wydobycie	Polskie Koleje Państwowe	performance bond	103 PLN	01.01.2017	31.12.2018
8.	CaixaBank	TAURON Ciepło	Elektrobudowa	payment	12 300 PLN	02.01.2017	31.12.2018

No.	Bank	Company	Beneficiary	Type of guarantee	Amount (thou.)	Launch date	Effective date
9.	CaixaBank	KW Czatkowice	PGE Paliwa (formerly EDF Paliwa)	performance bond	187 PLN	12.01.2017	30.01.2018
10.	CaixaBank	KW Czatkowice	PGE Paliwa (formerly EDF Paliwa)	performance Bond	412 PLN	01.07.2017	30.01.2018 [1]
11.	CaixaBank	TAURON Dystrybucja	Gmina Sosnowiec	performance Bond	53 PLN	06.10.2017	06.10.2018
12.	CaixaBank	KW Czatkowice	PGE Górnictwo i Energetyka Konwencjonalna	performance bond	515 PLN	24.10.2017	30.01.2020

[1]As of January 1, 2018 by way of amendment no. 1 to the guarantee the guarantee value was increased to PLN 761 thou. and the term was extended to January 31, 2019

Sureties and guarantees received

The below table presents a summary of collaterals received by TAURON effective as of December 31, 2017.

Table no. 39. Summary of collaterals received by TAURON, effective as of December 31, 2017

No.	Entity whose liabilities constitute the subject of collateral	Entity issuing collateral	Type of collateral	Amount in currency (thou.)	Effective date
1.	Polenergia Obrót S.A	PKO BP	Bank guarantee	750 EUR	28.02.2019
2.	Ezpada s.r.o.	Ezpada A.G.	Corporate guarantee	1 000 EUR	28.02.2018
3	Interenergia S.A.	NDI S.A.	Corporate guarantee	10 000 PLN	06.11.2019

9.3. Information on other agreements and events

Concluding of the agreement with TAURON Wydobycie on coal sales

On February 1, 2017 a multi-year agreement on coal sales for electricity generation purposes was concluded between TAURON and TAURON Wydobycie the subject of which was the purchase of coal by the Company for the needs of the generation units of TAURON Wytwarzanie and TAURON Ciepło. The agreement was concluded for the period until 31 December 31, 2019.

Signing of the hybrid financing agreements with BGK

On September 6, 2017 the Company and Bank Gospodarstwa Krajowego (BGK) signed the documentation of the subordinate bond issue program, constituting the basis for conducting a hybrid bond issue worth up to PLN 400 000 thousand.

The Company may carry out the hybrid bond issue in several series, and the period of the availability of funds was set as up to June 30, 2019. The financing period is 12 years from the issue date, however in accordance with the characteristic of the hybrid financing the first period of financing was defined as 7 years (the so-called *non-call period)*, during which an early redemption of the hybrid bonds by TAURON will not be possible BGK will not be able to sell them to third parties (in both cases subject to the exceptions defined in the documentation). The agreement also provides for an option to defer payment of interest on the hybrid bonds, until the hybrid bonds' redemption day as a maximum. Due ot the subordinate nature of the hybrid bonds, in case of TAURON's bankruptcy or liquidation the obligations under the hybrid bonds will have a priority of being satisfied only ahead of TAURON's shareholders' liabilities. A potential hybrid bond issue will have a positive impact on TAURON's financial stability because the bonds are excluded from calculating the leverage ratio (net debt/EBITDA ratio) which constitutes a covenant in some of TAURON's financing programs. Furthermore, 50% of the hybrid bonds amount will be classified by Fitch rating agency as equity in the rating model, which will have a positive impact on TAURON's rating. The hybrid bonds were granted BB+ rating by Fitch rating agency. In 2017 the Company did not conduct a bond issue under the above mentioned program. , and the hybrid financing, due to its cost, is treated as an option in case of potential implementation of new investment projects and represents a financial security for the Group.

Tax Capital Group (Podatkowa Grupa Kapitałowa - PGK)

Due to the elapse, on December 31, 2017, of the three-year period of PGK's operation, on September 26, 2017 selected TAURON Capital Group's subsidiaries concluded the PGK agreement in the form of a notary authenticated deed. On

October 30, 2017 the Head of the First Silesian Tax Office in Sosnowiec issued a decision on PGK's registration for the period of subsequent tax years 3, i.e. from January 1, 2018 until December 31, 2020. The new PGK includes the following subsidiaries: TAURON, TAURON Wytwarzanie, TAURON Dystrybucja, TAURON Sprzedaż, TAURON Sprzedaż GZE, TAURON Ciepło, TAURON Wydobycie, TAURON EKOENERGIA, TAURON Obsługa Klienta, TAURON Serwis, KW Czatkowice, Biomasa GT, TAURON Dystrybucja Serwis, Marselwind, Magenta GT, TAURON Ubezpieczenia sp. z o.o., En-Energia I sp. z o.o., En-Energia II sp. z o.o., En-Energia III sp. z o.o. and En-Energia IV sp. z o.o. Setting up of a new PGK will allow for taking advantage of the tax settlements synergy effect, i.e. deducting the tax loss of the subsidiaries that are members of the PGK from the income of the other subsidiaries. At the same time it will allow for continuing a unified system of settlements and for ensuring consistent interpretation of the tax regulations at the PGK level.

Revoking of the license for trading of natural gas abroad

As of September 30, 2017, at TAURON's request the President of the Energy Regulatory Office (ERO-URE), by way of the decision no. DRG.DRG-1.4112.38.2017.KL, revoked TAURON'S license for trading of natural gas abroad.

The revoking of the license involves obtaining an exemption from the need to maintain mandatory natural gas inventory (stock), beginning as of October 1, 2017, in connection with the coming into force of the amendment to the *law of February 16, 2007 on the inventory (stock) of oil products and natural gas.*

At the same time, taking into account the nature of its operations related to supplying TAURON Capital Group's subsidiaries with gas and the active participation in wholesale trading, TAURON has an option to purchase gas on the domestic market under its license for trading gas fuels. Gas contracting is conducted directly on the Polish Power Exchange (Towarowa Giełda Energii S.A.), both by way of futures market contracts, as well as SPOT market transactions. Furthermore, the Company contracts gas purchases and sales on the OTC market, based on commercial agreements concluded. Therefore, it should be pointed out that purchasing of gas fuel for the wholesale trading purpose as well as the security of supply and securing of the gas needs of TAURON Capital Group's subsidiaries are not in jeopardy.

Events occurring after December 31, 2017

Contribution of additional payments to the capital of PEPKH

Acting in accordance with the resolution of the Extraordinary GM PEPKH of March 1, 2018 on imposing on TAURON as a sole shareholder an obligation to make additional payments, on March 7, 2018 TAURON contributed additional payments to the share capital of the above mentioned company in the total amount of PLN 6 000 thou. The resolution of the Extraordinary GM as passed in order to ensure financing for the operations of PEPKH.

Management Board of the Company

Katowice, March 12, 2018

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

Appendix A: GLOSSARY OF TERMS AND LIST OF ABBREVIATIONS

The glossary of trade terms and the list of abbreviations and acronyms most commonly used in this report is presented below.

Table no. 40. Explanation of abbreviations and acronyms and trade terms used in the report

#	Abbreviation and trade term	Full name/explanation
1.	BGK	Bank Gospodarstwa Krajowego with its seat in Warsaw
2.	Biomasa GT	Biomasa Grupa TAURON sp. z o.o. with its seat in Stalowa Wola
3.	BZ WBK	Bank Zachodni WBK S.A. with its seat ine Wrocław
4.	B2B	B2B (business-to-business) an acronym denoting transactions between two or more business entities
5.	CC	Central heating plant (Centralna Ciepłownia) in Olkusz lub Zawiercie
6.	Cash pooling	Cash pooling used by the Company – the consolidation of balances of bank accounts through physical transferring of cash from the accounts of TAURON Capital Group's subsidiaries in the bank in which cash pooling is operated to the bank account of the Pool Leader whose function is performed by the Company. At the end of each working day, cash is transferred from the bank accounts of TAURON Capital Group's subsidiaries which show positive balance to the bank account of the pool leader. At the beginning of each working day the bank accounts of TAURON Capital Group's subsidiaries are credited from the bank account of the pool leader with the amount required to maintain the financial liquidity of the TAURON Capital Group's subsidiary on the given working day.
7.	Color certificates	Property rights resulting from the certificates of origin of electricity generated in the way subject to support, the so-called colored certificates: 1) **green** - certificates of origin of electricity from RES, 2) **violet** - certificates of origin of electricity generated in co-generation fired using methane released and captured during underground mining works in active, in liquidation or liquidated hard coal mines, or using gas obtained from biomass processing, 3) **red** - certificates of origin of electricity from co-generation (CHP certificates - Combined Heat and Power), 4) **yellow** - certificates of origin of electricity generated in co-generation from gas-fired sources or with the total installed capacity below 1 MW, 5) **blue** - certificates of origin of electricity generated from agricultural biogas. **White** - energy efficiency certificates (mechanism stimulating and forcing pro-savings behaviors.
8.	CIRS	Transaction involving a swap between counterparties of interest payments assessed on amounts denominated in various currencies and determined according to various interest rates
9.	CSI	Customer Satisfaction Index – index used in marketing to determine the level of customer satisfaction with the products or services offered by a company
10.	CSR	Corporate Social Responsibility
11.	CUW	Shared Services Center (Centrum Usług Wspólnych), np. CUW R – accounting services
12.	DM	Brokerage House (Dom Maklerski)
13.	Good Practices 2016	Good Practices of WSE Listed Companies 2016, in force as of January 1, 2016
14.	EIB	European Investment Bank with its seat in Luxembourg
15.	EBIT	Earnings Before Interest and Taxes
16.	EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
17.	EC Stalowa Wola/ECSW	Elektrociepłownia (Combined Heat and Power Plant – CHP) Stalowa Wola S.A. with its seat in Stalowa Wola
18.	ENEA	ENEA S.A. with its seat in Poznań
19.	ENERGA	ENERGA S.A. with its seat in Gdańsk
20.	ERM	Enterprise Risk Management system
21.	EU ETS	European Union CO_2 Emission Allowances Trading System
22.	EUA	European Union Allowance – an allowance to introduce the carbon dioxide (CO_2) equivalent to the air, within the meaning of Article 2 section 4 of the *Act of July 17, 2009 on the management system of emissions of greenhouse gases and other substances*, which is used for settlements of emission level within the system and which can be managed under the rules provided in the *Act of April 28, 2011 on the system of greenhouse gases emission allowances trading (Journal of Laws No. 122, item 695)*

#	Abbreviation and trade term	Full name/explanation
23.	EUR	Euro - a common European currency introduced in some EU member states
24.	GAZ-SYSTEM	Transmission Pipelines Operator GAZ-SYSTEM S.A. with its seat in Warsaw
25.	GPW	Warsaw Stock Exchange (Giełda Papierów Wartościowych w Warszawie S.A.) with its seat in Warsaw
26.	TAURON Capital Group	TAURON Capital Group Polska Energia S.A.
27.	GZE	Górnośląski Zakład Elektroenergetyczny
28.	IRGIT	Izba Rozliczeniowa Giełd Towarowych S.A. with its seat in Warsaw
29.	IRS	Interest Rate Swap, one of basic derivatives that is the subject of trading on the interbank market
30.	KGHM	KGHM Polska Miedź S.A. with its seat in Lubin
31.	KIC InnoEnergy	Knowledge and Innovations Community KIC InnoEnergy with its seat in Kraków
32.	Audit Committee	Audit Committee of the Supervisory Board of TAURON Polska Energia S.A.
33.	Nominations and Compensation Committee	Nominations and Compensation Committee of the Supervisory Board of TAURON Polska Energia S.A.
34.	Strategy Committee	Strategy Committee of the Supervisory Board of TAURON Polska Energia S.A.
35.	KPI	Key Performance Indicators, financial and non-financial indicators used as ways to measure progress of achieving goals of an organization
36.	KSE	National Power System (Krajowy System Elektroenergetyczny)
37.	Ksh	Commercial companies code
38.	KW Czatkowice	Kopalnia Wapienia (Limestone Mine) ”Czatkowice” sp. z o.o. with its seat in Krzeszowice
39.	Model Biznesowy	Document entitled *TAURON Group’s Business and Operational Model* (which is an update of *TAURON Group’s Business Model* adopted by the Management Board on May 4, 2016)
40.	mBank	mBank S.A. with its seat in Warsaw
41.	Marselwind	Marselwind sp. z o.o. with its seat in Katowice
42.	Mg	Mega gram – million grams (1 000 000 g) i.e. a ton
43.	MSR	CO_2 Emission Allowances Market Stability Reserve
44.	ISSR	International Financial Reporting Standards
45.	Nowe Jaworzno GT	Nowe Jaworzno Grupa TAURON sp. z o.o. with its seat in Jaworzno
46.	Line of Business	Seven areas of TAURON Capital Group’s core operations set up by the Company: Trading, Mining, Generation, RES, Heat, Distribution and Supply
47.	OPEC	Organization of the Petroleum Exporting Countries with its seat in Vienna
48.	ORM	Operational Capacity Reserve (OCR)
49.	OSD	Distribution System Operator (DSO)
50.	OSP	Transmission System Operator (TSO)
51.	OTC (OTC market)	Over The Counter Market
52.	OZE	Renewable Energy Sources (RES)
53.	OZEX_A	Green certificates index price
54.	Efficiency Improvement Program	TAURON Group’s 2016-2018 Efficiency Improvement Program
55.	PEPKH	Polska Energia - Pierwsza Kompania Handlowa sp. z o.o. with its seat in Warsaw
56.	PGE	PGE Polska Grupa Energetyczna S.A. with its seat in Warsaw
57.	PGE EJ 1	PGE EJ 1 sp. z o.o. with its seat in Warsaw
58.	PGNiG	Polskie Górnictwo Naftowe i Gazownictwo S.A. with its seat in Warsaw
59.	PKB	Gross Domestic Product (GDP)

#	Abbreviation and trade term	Full name/explanation
60.	PKO BP	Powszechna Kasa Oszczędności Bank Polski S.A. with its seat in Warszawie
61.	PLN	Polish zoty currency symbol - zł
62.	PMEC	Property rights for certificates of origin confirming generation of electricity in the other co-generation sources
63.	PMEF	Property rights for energy efficiency certificates
64.	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
65.	PMMET	Property rights for certificates of origin confirming generation of electricity in co-generation fired using methane released and captured during underground mining works in active, in liquidation or liquidated hard coal mines, or using gas obtained from biomass processing
66.	PMOZE_A	Property rights for certificates of origin confirming generation of electricity in RES after March 1, 2009
67.	PMOZE-BIO	Property rights for certificates of origin confirming generation of electricity from agricultural biogas from July 1, 2016
68.	PSE	Polskie Sieci Elektroenergetyczne S.A. with its seat in Konstancin-Jeziorna
69.	PSG	Polska Spółka Gazownictwa sp. z o.o. with its seat in Warsaw
70.	RB	Balancing Market (Rynek Bilansujący)
71.	RDN	Day Ahead Market (Rynek Dnia Następnego)
72.	RESPECT Index	Stock market index grouping stock market companies operating in accordance with the sustainable growth principles
73.	RTT	Futures Commodity Market (Rynek Terminowy Towarowy)
74.	Segment, Segments of operations	TAURON Capital Group's segments of operations used in the statutory reporting process. TAURON Capital Group's results from operations are allocated to the following five Segments (also called Line of Business or Areas in this report): Mining, Generation, Distribution, Supply and Other.
75.	SPOT (SPOT market)	With respect to electricity, it is the place where trade transactions for electricity are concluded for which the period of delivery falls, at the latest, three days after the date of the transaction's conclusion (usually it is one day before the date of delivery). Operation of the SPOT market for electricity is strongly tied to the operation of the balancing market run by the TSO
76.	Company/TAURON	TAURON Polska Energia S.A. with its seat in Katowicach
77.	Strategy	Document entitled *TAURON Group's 2016 – 2025 Strategy* adopted by the Management Board on September 2, 2016
78.	Sustainable development strategy	Document entitled *TAURON Group's 2017 – 2025 Sustainable development strategy* adopted by the Management Board on August 1, 2017, which is an update of the document entitled *TAURON Group's 2016 – 2018 Sustainable development strategy with an outlook until 2020*
79.	TAMEH Czech	TAMEH Czech s.r.o. with its seat in Ostrava, Czech Republic
80.	TAMEH HOLDING	TAMEH HOLDING sp. z o.o. with its seat in Dąbrowa Górnicza
81.	TAMEH POLSKA	TAMEH POLSKA sp. z o.o. with its seat in Dąbrowa Górnicza
82.	TAURON/Company	TAURON Polska Energia S.A. with its seat in Katowice
83.	TAURON Ciepło	TAURON Ciepło sp. z o.o. with its seat in Katowice
84.	TAURON Czech Energy	TAURON Czech Energy s.r.o. with its seat in Ostrava, Czech Republic
85.	TAURON Dystrybucja	TAURON Dystrybucja S.A. with its seat in Kraków
86.	TAURON Dystrybucja Pomiary	TAURON Dystrybucja Pomiary sp. z o.o. with its seat in Tarnów
87.	TAURON Dystrybucja Serwis	TAURON Dystrybucja Serwis S.A. with its seat in Wrocław
88.	TAURON EKOENERGIA	TAURON EKOENERGIA sp. z o.o. with its seat in Jelena Góra
89.	TAURON Obsługa Klienta	TAURON Obsługa Klienta sp. z o.o. with its seat in Wrocław
90.	TAURON Serwis	TAURON Serwis sp. z o.o. with its seat in Katowice
91.	TAURON Sprzedaż	TAURON Sprzedaż sp. z o.o. with its seat in Kraków

#	Abbreviation and trade term	Full name/explanation
92.	TAURON Sprzedaż GZE	TAURON Sprzedaż GZE sp. z o.o. with its seat in Gliwice
93.	TAURON Sweden Energy	TAURON Sweden Energy AB (publ) with its seat in Stockholm, Sweden
94.	TAURON Ubezpieczenia	TAURON Ubezpieczenia sp. z o.o. with its seat in Katowice
95.	TAURON Wydobycie	TAURON Wydobycie S.A. with its seat in Jaworzno
96.	TAURON Wytwarzanie	TAURON Wytwarzanie S.A. with its seat in Jaworzno
97.	TAURON Wytwarzanie Serwis	TAURON Wytwarzanie Serwis sp. z o.o. with its seat in Jaworzno
98.	TGE	Towarowa Giełda Energii S.A. with its seat in Warsaw
99.	EU	European Union
100.	UOKiK	Office of Competition and Consumer Protection (Urząd Ochrony Konkurencji i Konsumentów)
101.	USD	United States Dollar – US dollar's international acronym
102.	ERO (URE)	Energy Regulatory Office (Urząd Regulacji Energetyki)
103.	WFOŚiGW	Regional Environment Protection and Water Management Fund (Wojewódzki Fundusz Ochrony Środowiska i Gospodarki Wodnej) in Katowice or in Kraków
104.	Wsparcie Grupa TAURON	Wsparcie Grupa TAURON sp. z o.o. with its seat in Tarnów (formerly KOMFORT-ZET sp. z o.o.)
105.	WZ/ZW	General Meeting (GM) / Shareholders' Meeting
106.	ZG	Coal Mine (Zakład Górniczy) (Sobieski, Janina or Brzeszcze)
107.	ZW	Generation Plants (Zakłady Wytwarzania) in Bielsko-Biała, Kamienna Góra, Katowice or Tychy

Appendix B: INDEX OF TABLES AND FIGURES

The list of tables and figures presented in this report is provided below.

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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 Financial statements of TAURON Polska Energia S.A.
and the Management Board's report on the operations
of TAURON Polska Energia S.A.**

I, the undersigned, represent that, to my best knowledge, the Financial statements of TAURON Polska Energia S.A. 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 Polska Energia S.A.

I also certify that the Management Board's report on the operation of TAURON Polska Energia S.A. gives the true picture of the development, achievements and situation of TAURON Polska Energia S.A., 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	....

12 March 2018

date

STATEMENT

of the Management Board of TAURON Polska Energia S.A.
on the appointment of the entity authorized to audit financial statements
(Financial statements of TAURON Polska Energia S.A.)

I, the undersigned, represent that the entity authorized to audit financial statements and examining the financial statements of TAURON Polska Energia S.A. was appointed in accordance with legal regulations, and this entity and auditors examining the statements have met conditions for developing an impartial and independent report on the review of the audited financial statements in accordance with applicable regulations and professional standards.

Management Board Members:

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

12 March 2018

date