ZESPÓŁ ELEKTROWNI PĄTNÓW–ADAMÓW–KONIN SA CAPITAL GROUP

CONSOLIDATED FINANCIAL STATEMENT FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017
WITH AUDIT REPORT

This is a translation of the document issued originally in Polish language.
The Polish original should be referred to in matters of interpretation.

19 APRIL 2018

(in thousand PLN)

CONSOLIDATED PROFIT AND LOSS ACCOUNT

For 12 months period ended 31 December 2017

	Note	*12 months period ended 31 December 2017*	*12 months period ended 31 December 2016*
Continuing operations			
Sales revenue	*13.1*	**2 443 075**	**2 704 711**
Cost of goods sold	*13.6*	(2 035 396)	(2 241 353)
Gross profit / (loss)		**407 679**	**463 358**
Other operating revenues	*13.2*	11 324	26 461
Selling and distribution expenses	*13.6*	(4 258)	(4 360)
Administrative expenses	*13.6*	(119 467)	(108 634)
Other operating expenses	*13.3*	(5 186)	(5 392)
Gross profit / (loss) from operations		**290 092**	**371 433**
Finance income	*13.4*	16 193	9 117
Finance costs	*13.5*	(47 652)	(72 672)
Profit / (loss) before tax		**258 633**	**307 878**
Income tax expense (taxation)	*15.1*	(75 089)	(57 592)
Net profit / (loss) for the period from continuing operations		**183 544**	**250 286**
Discontinued operations			
Profit/ (loss) for the period from discontinued operations		-	-
Net profit / (loss) for the period		**183 544**	**250 286**
Net profit/ (loss) attributable to equity holders of the parent		183 243	247 674
Net profit/ (loss) attributable to non-controlling interests		301	2 612

Adam Kłapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*

Profit / loss per share (in zloty):	*Note*	*12 months period ended 31 December 2017*	*12 months period ended 31 December 2016*
Basic, for profit for the period attributable to equity holders of the parent	*17*	3.61	4.87
Basic, for profit for the period from continuing operations attributable to equity holders of the parent	*17*	3.61	4.87
Diluted, for profit for the period attributable to equity holders of the parent	*17*	3.61	4.87
Diluted, for profit for the period from continuing operations attributable to equity holders of the parent	*17*	3.61	4.87

Adam Kłapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*

(in thousand PLN)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For 12 months period ended 31 December 2017

	Note	*12 months period ended 31 December 2017*	*12 months period ended 31 December 2016*
Net profit / (loss) for the period		**183 544**	**250 286**
Other comprehensive income			
Items to be reclassified to the profit / (loss) in subsequent reporting periods:			
Cash flow hedges	*14*	5 439	5 996
Income tax on other comprehensive income	*15.1, 14*	(1 033)	(1 139)
Other comprehensive income to be reclassified to the profit / (loss) in subsequent reporting periods		4 406	4 857
Items not to be reclassified to the profit / (loss) in subsequent reporting periods:			
Profits / (losses) on provisions for post-employment	*14*	(2 155)	4 613
Income tax on other comprehensive income	*15.1, 14*	409	(876)
Other comprehensive income not to be reclassified to the profit / (loss) in subsequent reporting periods		(1 746)	3 737
Net other comprehensive income		**2 660**	**8 594**
Comprehensive income for the period		**186 204**	**258 880**
Comprehensive income attributable to equity holders of the parent		185 903	256 268
Comprehensive income attributable to non-controlling holders		301	2 612

Adam Klapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*

(in thousand PLN)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2017

	Note	*31 December 2017*	*31 December 2016*
ASSETS			
Fixed assets			
Property, plant and equipment	*19*	3 280 835	3 391 246
Investment property		2 365	2 337
Intangible assets	*21*	6 679	119 282
Assets of removing overburden and other mining assets (long-term)	*22*	72 536	80 524
Other long-term financial assets	*23.1*	10 311	11 945
Other long-term non-financial assets	*23.2*	2 122	5 726
Deferred tax assets	*15.3*	72 928	90 998
Total fixed assets		**3 447 776**	**3 702 058**
Current assets			
Short-term intangible assets	*21*	261 654	273 036
Inventories	*25*	97 758	105 296
Trade and other receivables	*26*	253 261	246 025
Income tax receivables		17 731	10 227
Short-term financial derivatives (assets)	*33.4*	-	296
Other short-term financial assets	*23.1*	35 788	77 317
Other short-term non-financial assets	*23.2*	11 425	28 776
Amounts due from customers under long-term construction contracts	*13.8*	7 080	8 168
Cash and cash equivalents	*27*	322 201	350 101
Total current assets		**1 006 898**	**1 099 242**
Assets classified as held for sale		1 038	-
TOTAL ASSETS		**4 455 712**	**4 801 300**

Adam Kłapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*

	Note	*31 December 2017*	*31 December 2016*
LIABILITIES AND EQUITY			
Equity			
Share capital	*28*	101 647	101 647
Reserve capital	*29*	1 094 493	1 028 647
Revaluation reserve from valuation of hedging instruments		(2 678)	(7 084)
Other reserve capital	*29.1*	3 472	3 472
Retained earnings / Accumulated losses		884 095	769 302
Net profit / (loss)		183 243	247 674
Equity attributable to equity holders of the parent		**2 264 272**	**2 143 658**
Equity attributable to non-controlling interests		-	-
Total equity		**2 264 272**	**2 143 658**
Long-term liabilities			
Interest-bearing loans and borrowings	*30*	302 465	587 851
Long-term employee benefits	*24.1*	48 166	48 587
Trade liabilities and other long-term financial liabilities	*33.2*	5 146	5 069
Long-term financial derivatives (liabilities)	*33.4*	870	4 294
Long-term subsidies	*33.5*	44 509	43 302
Other long-term provisions and accruals	*31*	357 902	312 253
Deferred tax liability	*15.3*	432 900	388 359
Total long-term liabilities		**1 191 958**	**1 389 715**
Short-term liabilities			
Trade liabilities and other short-term financial liabilities	*33.1*	146 416	302 662
Current portion of interest-bearing loans and borrowings	*30*	349 573	421 958
Short-term financial derivatives (liabilities)	*33.4*	4 139	5 759
Other non-financial liabilities	*33.3*	107 387	116 431
Current income tax liability		1 092	166
Short-term employee benefits	*24.1*	5 457	6 503
Short-term subsidies	*33.6*	1 507	6 670
Amounts due to customers under long-term construction contracts	*13.8*	5 626	3 990
Other short-term provisions and accruals	*31*	378 285	403 788
Total short-term liabilities		**999 482**	**1 267 927**
Total liabilities		**2 191 440**	**2 657 642**
TOTAL LIABILITIES AND EQUITY		**4 455 712**	**4 801 300**

Adam Kłapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*

(in thousand PLN)

CONSOLIDATED STATEMENT OF CASH FLOWS

For 12 months period ended 31 December 2017

	Note	*12 months period ended 31 December 2017*	*12 months period ended 31 December 2016*
Cash flow from operating activities			
Profit /(loss) before tax		258 633	307 878
Adjustments for:			
Depreciation and amortization	*27*	195 692	207 829
Interests and shares in profits		32 129	44 717
(Profit) / loss on foreign exchange differences		(13 801)	10 752
(Profit) / loss on investing activities		2 516	15 219
(Increase) / decrease in receivables	*27*	11 701	3 123
(Increase) / decrease in inventories	*27*	7 537	52 219
Increase / (decrease) in payables except for loans and borrowings	*27*	(99 080)	(5 117)
Change in provisions, prepayments, accruals and employee benefits	*27*	328 799	239 186
Income tax paid		(19 679)	(24 074)
Allowances for emission of CO_2		(249 437)	(315 533)
Impairment write-down on fixed assets and mining assets		22 165	-
Other		1 623	(148)
Net cash flow from operating activities		**478 798**	**536 051**
Cash flow from investing activities			
Proceeds from sale of property, plant and equipment and intangible assets		3 478	3 723
Purchase of property, plant and equipment and intangible assets		(98 272)	(195 352)
Proceeds and expenses relating to other financial assets	*27*	1 451	7 773
Deposit termination for securing debt	*27*	35 630	-
Dividends paid		208	60
Interest paid		5	6
Other		(124)	82
Net cash flow from investing activities		**(57 624)**	**(183 708)**
Cash flow from financing activities			
Payment of finance lease liabilities		(7 012)	(15 038)
Proceeds from loans and borrowings and debt securities		-	12 295
Repayment of loans and borrowings and debt securities		(340 837)	(334 211)
Dividends paid		(65 562)	-
Interest paid		(33 373)	(48 632)
Other		(466)	(1 428)
Net cash flow from financing activities		**(447 250)**	**(387 014)**
Net increase / (decrease) in cash and cash equivalents		**(26 076)**	**(34 671)**
Cash and cash equivalents at the beginning of the period	*27*	**348 646**	**383 318**
Cash and cash equivalents at the end of the period		**322 570**	**348 647**

Adam Kłapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*

(in thousand PLN)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For 12 months period ended 31 December 2017

	Note	*Issued capital*	*Reserve capital*	*Revaluation reserve of financial instruments*	*Other reserve capital*	*Retained earnings / accumulated losses*	*Total*	*Non-controlling interest*	*Total equity*
as of 1 January 2017		**101 647**	**1 028 647**	**(7 084)**	**3 472**	**1 016 976**	**2 143 658**	**-**	**2 143 658**
Net profit for the period		-	-	-	-	183 243	183 243	301	183 544
Total other comprehensive income		-	-	4 406	-	(1 746)	2 660	-	2 660
Total income for the period		**-**	**-**	**4 406**	**-**	**181 497**	**185 903**	**301**	**186 204**
Distribution of profits from previous years		-	65 846	-	-	(65 846)	-	-	-
Dividend for previous years		-	-	-	-	(65 562)	(65 562)	-	(65 562)
Distribution of profits from previous years for CSBF		-	-	-	-	(28)	(28)	-	(28)
The effect of the 'put' option settlement on the shares of non-controlling interests	*29.3*	-	-	-	-	301	301	(301)	-
as at 30 December 2017		**101 647**	**1 094 493**	**(2 678)**	**3 472**	**1 067 338**	**2 264 272**	**-**	**2 264 272**

Adam Kłapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*

Rules (policies) of accountancy and additional explanatory notes to the consolidated financial statement are its integral part.

(in thousand PLN)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For 12 months period ended 31 December 2016

	Nota	*Issued capital*	*Reserve capital*	*Revaluation reserve of financial instruments*	*Other reserve capital*	*Retained earnings / Accumulated losses*	*Total*	*Non-controlling interest*	*Total Equity*	*Issued capital*
As at 1January 2016		**101 647**	**2 542 060**	**(11 941)**	**5 877**	**(752 820)**	**-**	**1 884 823**	**-**	**1 884 823**
		-	-	-	-	247 674	-	247 674	2 612	250 286
Net profit for the period		-	-	4 857	-	3 737	-	8 594	-	8 594
Total other comprehensive income		**-**	**-**	**4 857**	**-**	**251 411**	**-**	**256 268**	**2 612**	**258 880**
Total income for the period		-	(1 513 413)	-	(2 405)	1 515 818	-	-	-	-
Distribution of profits from previous years	*29.3*	-	-	-	-	2 612	-	2 612	(2 612)	-
Share of profits from previous years for ZFŚS		-	-	-	-	(45)	-	(45)	-	(45)
The effect of the settlement of a put option on the shares of non-controlling interests		**101 647**	**1 028 647**	**(7 084)**	**3 472**	**1 016 976**	**-**	**2 143 658**	**-**	**2 143 658**

Adam Kłapszta /President of the Board/

Aneta Lato-Żuchowska /Vice President of the Board/

Zygmunt Artwik / Vice President of the Board /

Elżbieta Niebisz / Vice President of the Board /

Aneta Desecka /Chief Accountant/

Rules (policies) of accountancy and additional explanatory notes to the consolidated financial statement are its integral part.

ZASADY (POLITYKI) RACHUNKOWOŚCI ORAZ DODATKOWE NOTY OBJAŚNIAJĄCE

1. General information

The Capital Group of Zespół Elektrowni Pątnów – Adamów – Konin SA ("the Group") consists of Zespół Elektrowni Pątnów – Adamów – Konin SA ("the parent company", "the Company", "ZE PAK SA"), with its head office in Konin at 45 Kazimierska str., and its subsidiaries (see Note 2). The Group's consolidated financial statement covers the year ended 31 December 2017 and includes comparative data for the year ended 31 December 2016. The parent company is entered into the Register of Entrepreneurs of the National Court Register kept by the District Court Poznań – Nowe Miasto and Wilda in Poznań, IX Commercial Division of the National Court Register, under the KRS number 0000021374.

The parent company was assigned the statistical number (REGON) 310186795.

The duration of the parent and member companies of the Capital Group is unlimited.

The main activities of the Group are:

1) generation and sale of electricity,
2) generation and sale of heat (steam and hot water),
3) lignite extraction.

(in thousand PLN)

2. Composition of the Group

The Group consists of Zespół Elektrowni Pątnów – Adamów – Konin SA and the following subsidiaries:

Entity	*Registered office*	*Scope of operations*	*Group's share in the capital in %*	
			31.12.2017	*31.12.2016*
Przedsiębiorstwo Remontowe „PAK SERWIS" sp. z o.o.	62-510 Konin ul. Przemysłowa 158	Construction and repair services	100.00%	100.00%
„Elektrownia Pątnów II" sp. z o.o.	62-510 Konin ul. Kazimierska 45	Electric Energy production and distribution from the 464 MW power unit	100.00%*	100.00%*
„PAK – HOLDCO" sp. z o.o.	62-510 Konin ul. Kazimierska 45	Holding activity	100.00%	100.00%
„PAK Infrastruktura" sp. z o.o.	62-510 Konin ul. Kazimierska 45	General construction of engineering objects, not classified elsewhere	100.00%	100.00%
„PAK GÓRNICTWO" sp. z o.o.	62-510 Konin ul. Kazimierska 45	Exploration and recognition of lignite	100.00%	100.00%
Energoinwest Serwis sp. z o.o. in liquidation	62-510 Konin ul. Spółdzielców 3	Repair-construction service	100.00%*	100.00%*
PAK Kopalnia Węgla Brunatnego Konin SA	62-540 Kleczew ul. 600-lecia 9	Lignite extraction	97.58%*	96.23%*
PAK Kopalnia Węgla Brunatnego Adamów SA	62-700 Turek Warenka 23	Lignite extraction	99.26%	98.41%
„Aquakon" sp. z o.o. in liquidation	62-610 Sompolno Police	Mechanical services, repairs, reclamation of land, production and trade of mineral water	96.2%*	92.57%*
Eko-Surowce sp. z o.o. in liquidation	62-540 Kleczew ul. 600-lecia 9	Vulcanization services, sales of lignite	100.00%*	96.23%*
PAK – Volt SA	00-834 Warszawa ul. Pańska 77/79	Trade of electricity	100.00%	100.00%
EL PAK Serwis sp. z o.o. in liquidation	62-510 Konin ul. Przemysłowa 158	Repair and maintenance of electric equipment, repair and maintenance of machines	100.00%*	100.00%*
PAK Adamów sp. z o.o	62-510 Konin Ul. Kazimierska 45	Buying and selling real estate	100.00%	-

* *Entities in which ZE PAK SA has an indirect share in the capital*

As of 31 December 2017, the share in the general number of votes held by the Group in subsidiaries is equal to the Group's share in capitals of these subsidiaries.

As a result of the process of redeeming shares from eligible employees and after the transfer of shares repurchased from the State Treasury, the share of ZE PAK SA Capital Group's companies in the shareholding of PAK KWB Konin SA increased to 97.58% and in PAK Coal Mine Brunatnego Adamów SA to 99.26%.

On 9 May 2017 PAK Górnictwo sp. Z o.o. has made agreements with PAK KWB Konin SA, PAK Serwis sp. z o.o. and EL PAK sp. z o.o., as a result of which PAK Górnictwo sp. z o.o. acquired shares in the following companies: EL PAK Serwis sp. z o.o., Aquakon sp. z o.o., Eko-Surowce sp. z o.o., Energoinwest Serwis sp. z o.o. On August 1, 2017, the Extraordinary General Meeting of Shareholders of four companies acquired by PAK Górnictwo sp. Z o.o. took resolution on terminating the companies and starting their liquidation as of 1 August 2017. The initiated liquidation process is a consequence of the restructuring of the auxiliary activity towards the main segments of the Capital Group. The activities carried out by the abovementioned companies will be carried out by PAK Górnictwo sp. Z o.o. that takes over the rights and obligations of the liquidated companies.

On 30 June 2017, EL PAK sp. z o.o. (acquired company) and PAK Serwis sp. z o.o. (acquirer) have merged into one Company, pursuant to Art. 492 § 1 point 1 of the CCC by transferring all the assets of EL PAK sp. z o.o. to PAK Service sp. z o.o. Legal status EL PAK sp. z o.o. ceased from 1 July 2017. This change in the Group's structure is also a consequence of the consolidation of auxiliary activities to the Group's main segments. As of December 31, 2016 ZE PAK SA held 100% of shares in EL PAK sp. Z o.o. On 16 October 2017 a new subsidiary has been set up – PAK Adamów Sp. z o.o., in which ZE PAK SA holds all the shares. The appointment of the new subsidiary company is related to preparation of the process of terminating the activity of Elektrownia Adamów.

3. Composition of the Management Board of the parent company

As the day of the report publication, ZE PAK SA Management Board is composed of the following members:

- Adam Kłapszta President of the Board,
- Aneta Lato-Żuchowska Vice President of the Board,
- Zygmunt Artwik Vice President of the Board,
- Elżbieta Niebisz Vice President of the Board,

On 3 March 2017, by the resolution of the Supervisory Board of the Company, Mr. Adam Kłapszta, who previously held the position of the Vice-President of the Management Board of the Company acting as the President of the Management Board, was appointed as the President of the Management Board of the Company. The resolution on entrusting the function of the President of the Management Board of the Company entered into force upon its adoption.

During a meeting of the Supervisory Board held on 3 March 2017, Ms. Katarzyna Sobierajska and Mr. Tomasz Zadroga stepped down from the positions of the Vice-Presidents of the Management Board of the Company as of 3 March 2017.

On 3 March 2017, the Supervisory Board of the Company appointed Ms. Elżbieta Niebisz to the position of the Vice-President of the Management Board. The resolution on the appointment became effective upon its adoption.

4. Approval of the financial statement

This consolidated financial statement was approved for issuing by the Management Board on 19 April 2018.

5. Essential values based on professional judgement and estimates

5.1. Professional judgement

The preparation of the consolidated financial statement of the Group requires, from the Management Board of the parent company, the judgements, estimates and assumptions, which affect the reported income, costs, assets, liabilities and the related notes and disclosures related to contingent liabilities. Uncertainty about these assumptions and estimates may result in the significant impairment of balance sheet values of assets and liabilities in the future.

In the process of application of the rules (policies) of accounting, the Management Board made the following judgements that have the greatest impact on the presented balance sheet values of assets and liabilities.

Capitalisation of foreign exchange rates

Due to executed investments, the Group’s companies use external financing sources.

The borrowing costs, which can be directly allocated to the implementing investments, are capitalized in the value of the capital work in progress until the commissioning of the capital work to use.

The companies capitalize the foreign exchange rates related to the received credits and loans in the foreign currency to the extent to which they represent an adjustment to the interest costs. The Group uses the cumulative approach in the scope of capitalisation of external borrowing costs. The cumulative approach considers an investment as a whole. That is why the amount of foreign exchange rates possible to be capitalised as an adjustment of external financing costs in the reporting period may be subject to changes together with changes in exchange rates in the period of investment.

Classification of lease contract

The Group classifies the lease as operating or financial one based on the assessment of the extent to which the risk and benefits of ownership of the leased asset come to the lessor and to the lessee. This assessment is based on the economic content of each transaction.

Identification of embedded derivatives

At each balance sheet date, the Group's management assesses whether under the contracts, there are economic characteristics and risk specific to the embedded derivative in a foreign currency, which are not closely related to the economic characteristics and risk of the host agreement.

5.2. Uncertainty of estimates

Basic assumptions concerning the future and other key sources of uncertainty occurring at the balance sheet date, to which vital risk of the significant adjustment of balance sheet value of assets and liabilities in the next financial year are related, are discussed below. The Group adopted assumptions and estimates concerning the future on the basis of the knowledge possessed during development of the financial statement. Occurring assumptions and estimates may be subject to change due to future events resulting from market fluctuations or fluctuation not controlled by the Group. Such fluctuations are reflected in estimates or assumptions at the moment of occurrence.

Loss in fixed assets

As a result of analyses conducted as of 31 December 2016, the Group identified the existence of circumstances, which would indicate possible loss in value of the asset components, in the form of the balance sheet net value of the Group's assets higher than the value of its market capitalisation. In relation to the above fact, the Group conducted value impairment tests of components of fixed assets. On the basis of the conducted tests, it was stated that there is a need to identify the Impairment write-downs against tangible fixed assets. Information about the conducted test is presented in note 19.1.

Evaluation of provisions for employee benefits

Provisions for employee benefits were estimated using actuarial methods. The assumptions adopted for that purpose were presented in the note 24.1.

Estimate was developed on the basis of following main assumptions:

- discount rate 3.5%
- estimated inflation rate 2.5%
- estimated salary increase rates depending on the company, in the range from 0% to 3%

Changes of the financial indexes, which are a basis of the estimation, would change the balance of the provisions by the amounts presented in the table below (in thousands zloty).

	(+) increase by 1 percentage point	*(-) decrease by 1 percentage point*
discount rate	(2 488)	2 947
salary increase rates	2 886	(2 127)

Component of deferred tax assets

The Group recognises the component of deferred tax assets on the basis of assumption that tax profit enabling to its use will be achieved. The deteriorations of the achieved tax results in the future, could lead to a situation, in which this assumption would become unjustified.

Fair value of financial instruments

The fair value of financial instruments, for which there is no active market, is determined using relevant measurement techniques. When selecting relevant methods and assumptions, the Group is guided by professional judgement. The way of determination of the fair value of particular financial instruments was presented in note 10.10.

Capitalisation of overburden stripping costs in the production phase

In cases justified by IFRIC 20, the Group capitalizes overburden stripping costs during the operation phase of an open pit mine. The basis for cost capitalisation is meeting the following conditions: the Group is likely to achieve future economic benefits associated with overburden stripping, the Group is able to identify the part of a coal seam, to which access was facilitated and the costs associated with overburden stripping regarding that part of the seam can be credibly appraised. The Group verifies the estimates regarding the above criteria on a regular basis, in order to ensure correct cost capitalisation.

Settlement period for assets related to overburden stripping and other mining assets

On a periodic basis, the Group verifies the settlement periods of assets related with overburden stripping and other mining assets, on the basis of current forecasts regarding the open pit exploitation.

Payment in shares

In order to settle employee shares, it was accepted that the start date of vesting for the shares was the date of the Company's commercialisation, and the date of granting entitlements to the shares was the date of the final hanging of the lists with the number of shares granted to PAK Kopalnia Węgla Brunatnego Konin SA and PAK Kopalnia Węgla Brunatnego Adamów SA's employees. Fair value of the programme on the day of the acquisition of control was determined on the basis of the fair value of PAK Kopalnia Węgla Brunatnego Konin SA and PAK Kopalnia Węgla Brunatnego Adamów SA companies. The process of acquisition of shares by entitled employees begun in February 2013 and lasted until 20 October 2014. The price of shares redemption was specified in PAK KWB Konin and PAK KWB Adamów's shares sale agreements dated 28 May 2012 and was established at the level of the price of purchase of shares of earlier purchased shares of mines index-linked by the consumption products and services price indicator.

Compensation for the termination of long-term contracts for sale of power and electricity

Note 34 presents the descriptions of essential contingent liabilities and essential law suits, including these concerning compensations for the termination of long-term contracts for the sale of power and electricity.

Revenue recognition

The Group uses the percentage of work completion method at settlement of long-term contracts. Use of this method requires from the Group estimation of proportions of completed works to all services to be performed.

On every balance sheet date, the Group updates the budgeted estimates of total revenues and costs of realised projects. The projected contract-related loss is recognised as costs of the period, when it was recognised in accordance with IAS 11.

Depreciation rates

The amount of depreciation rates is determined on the basis of the projected period of economic usability of tangible fixed asset components and intangible assets. The Group verifies accepted periods of economic usability on the basis of current estimates annually.

Uncertainty associated with tax settlement

Regulations regarding the goods and services tax, the corporate income tax and the burden associated with social insurance are subject to frequent changes. These frequent changes result in the lack of relevant benchmarks, incoherent interpretations and few established precedents, which could be applied. The binding legislation also contains ambiguities, which create differences in the opinions, in terms of legal interpretation of tax legislation, both, between state authorities, as well as state authorities and the enterprises.

Tax settlements and other areas of activity (for example customs or foreign currency issues) can subjected to inspection by the authorities, which are entitled to impose large penalties and fines, and all additional tax liabilities, resulting from the inspection, must be paid together with high interest. These circumstances cause the tax risk in Poland to be higher than in countries with a more mature tax system.

As a consequence, the amounts shown and disclosed in financial statements can be changed in the future, as a result of the ultimate decision by a tax audit authority.

Amendments to the Tax Code were introduced on 15 July 2016 in order to reflect the provisions of the General Anti-Abuse Regulation (GAAR). The GAAR is supposed to prevent the creation and abuse of artificial legal structures, formed in order to avoid paying taxes in Poland. The GAAR defines tax evasion as an activity conducted mainly with the aim to obtain a tax benefit, contradictory in current circumstances to the subject matter and goal of the tax law regulations. According to GAAR, such an activity does not result in obtaining a tax benefit, if the manner of activity was artificial. All events of (i) unjustified division of operations, (ii) involvement of intermediaries, despite a lack of economic or business justification, (iii) elements mutually cancelling or compensating each other and (iv) other activities of a similar effect to the previously mentioned, can be treated as a prerequisite for the existence of artificial activities subject to GAAR provisions. The new regulations will require a much wider judgement when assessing the tax implications of individual transactions.

The GAAR clause shall be applied in relation to transactions made after it came into effect and to transaction, which were conducted prior to the GAAR entering into force but for which the benefits were or still are achievable after the date of entry into force. The implementation of the above regulations will enable Polish tax audit authorities to question the legal agreements and arrangements executed by the taxpayers, such as group restructuring and reorganisation.

The Group recognizes and measures assets or liabilities for current and deferred income tax by applying the requirements of IAS 12 *Income tax*, on the basis of the profit (tax loss), taxation base, unsettled tax losses, unused tax relief and tax rates, taking into account the uncertainties associated with tax settlements.

In the case of uncertainty whether a tax authority would and to what extent accept tax settlement of a transaction, the Group recognises these settlements taking into account the uncertainty assessment.

Impairment write-downs on receivables

On the balance sheet date, the Group evaluates whether there is objective evidence of the loss in value of the financial assets component or a group of financial assets. If the asset component value possible to recover is lower than its balance sheet value, a given entity establishes an impairment write-down to the level of current value of planned cash flows.

Provision for the liquidation of tangible fixed assets components

The group creates provisions for the liquidation of tangible assets in the event of such an obligation or undertaking such a liability by the Group's management. The provision is created in the amount resulting from the received offers concerning liquidation of components of tangible fixed assets. The Group updates the value of the provision on every balance sheet date. The value of the provision due to liquidation of components of tangible fixed assets is discounted on every balance sheet date. Provisions for the disassembly of the Adamów Power Plant assets are not created due to the lack of a legal obligation. The integrated permit received by Adamów Power Plant for conducting operations does not contain a clause on the obligation to liquidate assets, and therefore no provision has been created. The provision is described in note 31.3.2.

Provision for liquidation of ash storage yards

The Group creates the provision for liquidation of ash dumps due to a legal obligation resulting from the integrated approval entries. The basis of estimation are developments, technical and economic analyses developed by the Group, as well as received external offerings for planned directions of reclamation. At the end of each reporting period, the Group updates the value of the provision. The provision is described in note 31.3.2.

Reclamation and other provisions related to mining activity

The Group creates both, the provision for reclamation costs related to current extraction of coal on a given open pit, and the provision for costs of the final excavation. The provision is created on the basis of the estimates of future reclamation costs, as well as assumed start and finish dates of reclamation, on the basis of reports by independent experts estimating reclamation costs on the order of the Management Board, as well as internal estimates of the Group, and is discounted on every balance sheet date. The provisions are described in note 31.3.3.

Valuation of Energy certificates

The Group recognises the energy certificates of origin (green certificates) due to the energy production from renewable energy, gas, and peak load co-generation sources according to the fair value at the end of the month, in which they were produced. On the balance sheet date, the Group appraises certificates of origin to the net value possible to achieve – for green certificates on 31 December 2017 to the price of 45.29 PLN /MWh. A write-down against the certificate value is created in case the sale price possible to achieve, diminished by the disposition costs, is lower than the historical production cost.

Provision for liabilities for the emission of greenhouse gases and provisions for the redemption of certified emission reductions (EUA)

The Group recognises the provision for the redemption of greenhouse gases allowances and certified emission reductions. In association with completing the settlement period for the allocation of emission allowances NAP II, a new 2013-2020 settlement period related to emission allowances is effective as of 1 January 2013. The assumption of that period is to grant the Group free EUAs, resulting from the generation of thermal energy, however, the power sector was additionally covered by the possibility of derogation, resulting from Art. 10c of the ETS Directive, involving the granting of extra free allowances, under the condition of transferring declared investment expenses on the investments reported in the National Investment Plan.

Emissions in ZE PAK SA Group in 2016 amounted to 11 456 099 tons of CO_2.

As at January 1, 2017, the Group had physical assets in its EUA accounts in the amount of 13 820 841 tons. In January 2017, 1 345 000 EUA units purchased in futures contracts concluded at the turn of 2015 and 2016 accounted for the Group's accounts in the Union Registry. In addition, in February 2017, the Group received free EUA for heat for 2017 (Article 10a of the ETS Directive) in the amount of 83,317 EUA. Then in April 2017, the Group redeemed CO2 emissions for 2016 in the amount of 11 456 099 tons of CO2. The balance of EUA units in the Group after redemptions amounted to 3 793 059 EUA units.

In the following months, the Group continued to make further purchases of CO2 emission allowances. The total purchase of EUAs in the Group that influenced the Group Account in the Union Registry in 2017 amounted to 7 328 000 EUA, and the status of EUA units in the Group after all the operations described above as at 31 December 2017 amounted to 9 776 059 EUA.

As at December 31, 2017, the Group created a provision for allowances in respect of the actual volume of issue for the period from January 1, 2017 to December 31, 2017.

Details regarding the provision for liabilities for the redemption of greenhouse gas emission allowances and certified emission reduction units are presented in note 31.3.1.

Reclamation reserve

The Group did not create any restructuring reserves related to the end of the Adamów Power Plant operation, because in the opinion of the Management Board as at 31 December 2017, there were no conditions under IAS 37. If such requirements were met IAS 37 will be created.

6. Basis for development of the interim condensed consolidated financial statement

This consolidated financial statement was developed according to the historical cost principle, except for the derivatives and other financial instruments.

The balance sheet value of the recognised hedged assets and liabilities is adjusted with fair value changes, which may be attributed to the risk against which such assets and liabilities are hedged.

This consolidated financial statement is presented in Polish zloty (zloty) and all values, unless shown otherwise, are expressed in thousands of zloty.

This consolidated financial statement was developed under the assumption of continuing the activity over a period of at least 12 months after the balance sheet date. On the day of approving this financial statement, it cannot be stated that there are circumstances indicating a threat to the continuation of the activities by the Group’s companies, whereas, there are operations regarding the allocation of specified types of activity between the Group’s companies. The indicated actions will not impact the limitations of the scope of the business activity conducted by the ZE PAK SA Capital Group.

6.1. Statement of compliance

This consolidated financial statement was developed in conformity with the International Financial Reporting Standards ("IFRS"), approved by the EU ("EU IFRS"). At the date of approval of this report for publishing, taking into account the EU's ongoing process of implementation of IFRS; IFRS applicable to these financial statements do not differ from EU IFRS.

EU IFRS covers standards and interpretations adopted by the International Accounting Standards Board ("IASB").

The Group's companies keep their accounting books in accordance with the policy (rules) specified in the Act of 29 September 1994 on accounting ("the Act"), as amended, and the regulations issued therein ("Polish accounting standards"). The consolidated financial statement includes adjustments, which are not included in the accounting books of the Group's units, introduced in order to make their financial statements comply with IFRS.

6.2. Functional currency and financial statements currency

The functional currency of the parent company and other companies included in this consolidated financial statement and the presentation currency of this consolidated financial statement is the Polish zloty (zloty).

7. Amendments to the used accounting policies and to comparative data

The accounting (policy) rules applied for the development of this consolidated financial statement are coherent with the ones used for the development of the Company's consolidated financial statement for the year concluded on 31 December 2015, except the one shown below. The following amendments to the IFRS were applied in this consolidated financial statement according to their date of entry into force, however, they did not have a significant impact on the presented and disclosed financial information, did not apply to the transactions concluded by the Group:

- Amendments to IAS 12 *Recognition of deferred income tax assets in respect of unrealized losses*

  The changes clarify issues related to the creation of negative temporary differences in the case of debt instruments valued at fair value, an estimate of the likely future taxable income and an assessment of whether the income generated will allow realizing negative temporary differences. The changes are retrospective.

- Amendments to IAS 7 *Initiative on disclosure of information*

  The changes require the entity to disclose information that enables users of financial statements to evaluate changes in liabilities arising from financing activities. No comparative information is required for previous periods.

- Amendments to IFRS 12 *Disclosures about shares in other entities being part of changes resulting from the review of IFRSs 2014-2016*

  The changes clarify that the requirements in the standard also apply to the entity's shares in subsidiaries, joint arrangements (i.e. joint operations or joint ventures), affiliates or structured units not consolidated, which have been classified (or included in the group for sale, which has been classified) as held for sale or as discontinued operations in accordance with IFRS 5 *Fixed assets held for sale and discontinued operations.*

The Group did not decide on the earlier application of any other standard, interpretation, or amendment, which were issued but are not yet effective in light of the European Union regulations.

8. New standards and interpretations which were issued but are not effective yet

- IFRS 9 Financial Instruments (issued on 24 July 2014) – applicable to annual periods beginning on 1 January 2018 or later,

- IFRS 14 Regulatory Deferral Accounts (issued on 30 January 2014) – as per the decision of the European Committee, the approval process for the standard in the preliminary version will not be initiated prior to the standard being issued in the final version – until the day of approval of this financial statement not approved by the EU – applicable to the annual periods beginning on 1 January 2016 or later,

- IFRS 15 Revenue from Contracts with Customers (issued on 28 May 2014), covering the amendments to IFRS 15 Effective date of IFRS 15 (issued on 11 September 2015) – applicable to the annual periods beginning on 1 January 2018 or later,
- Amendments to IFRS 10 and IAS 28 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (issued on 11 September 2014) – works leading to the approval of these changes were delayed indefinitely by the EU - the effective date was delayed indefinitely by IASB,
- IFRS 16 Leasing (published on January 13, 2016) - applicable to annual periods beginning on January 1, 2019 or later,
- Amendments to IFRS 4 Application of IFRS 9 Financial Instruments, including IFRS 4 Insurance Contracts (published on September 12, 2016) - applicable to annual periods beginning on January 1, 2018 or later,
- Explanations to IFRS 15 Revenue from contracts with customers (published on April 12, 2016) - applicable to annual periods beginning on January 1, 2018 or later,
- Amendments to IFRS 2 Classification and valuation of payment transactions based on shares (published on June 20, 2016) - applicable to annual periods beginning on January 1, 2018 or later,
- Amendments to IAS 28 Investments in Associates and Joint Ventures as a part of Changes resulting from the review of IFRS 2014-2016 (published on December 8, 2016) - applicable to annual periods beginning on January 1, 2018 or later,
- Amendments to IFRS 1 Application of International Financial Reporting Standards for the first time as part of the Changes resulting from the review of IFRS 2014-2016 (published on December 8, 2016) - applicable to annual periods beginning on January 1, 2018 or later,
- KIMSF 22 Transactions in foreign currency and advances (published on December 8, 2016) - applicable to annual periods beginning on January 1, 2018 or later,
- Amendments to IAS 40: Transfer of investment property (published on December 8, 2016) - until the date of approval of these financial statements not approved by the EU - applicable to annual periods beginning on January 1, 2018 or later,
- IFRS 17 Insurance Contracts (published on May 18, 2017) - until the date of approval of these financial statements not approved by the EU - applicable to annual periods beginning on January 1, 2021 or later,
- IFRIC 23 Uncertainty related to the recognition of income tax (published on June 7, 2017) - until the date of approval of these financial statements not approved by the EU - applicable to annual periods beginning on January 1, 2019 or later,
- Amendments to IFRS 9 Early repayments with negative compensation (published on October 12, 2017) - applicable to annual periods beginning on January 1, 2019 or later,
- Amendments to IAS 28 Long-term shares in associates and joint ventures (published on 12 October 2017) - until the date of approval of these financial statements not approved by the EU - applicable to annual periods beginning on January 1, 2019 or later,
- Changes resulting from the review of IFRS 2015-2017 (published on December 12, 2017) - until the date of approval of these financial statements not approved by the EU - applicable to annual periods beginning on January 1, 2019 or later,
- Amendments to IAS 19 Change, limitation or settlement of the program (published on February 7, 2018) - until the date of approval of these financial statements not approved by the EU - applicable to annual periods beginning on January 1, 2019 or later.
- Amendments to References to the Conceptual Assumptions contained in International Financial Reporting Standards (published on March 29, 2018) - until the date of approval of these financial statements not approved by the EU - applicable to annual periods beginning on January 1, 2020 or later.

The dates of entry into force are dates resulting from the content of standards announced by the International Financial Reporting Council. The dates of application of standards in the European Union may differ from the dates of application resulting from the content of standards and are announced at the time of approval for application by the European Union.

8.1. Implementation of MSSF 9

In July 2014, the International Accounting Standards Board published the International Financial Reporting Standard 9 Financial Instruments ("IFRS 9"). IFRS 9 covers three aspects related to financial instruments: classification and measurement, impairment and hedge accounting. IFRS 9 applies to annual periods beginning on January 1, 2018 and later, with the possibility of earlier application.

The Group plans to apply IFRS 9 from the effective date of the standard, without transforming the comparative data.

In 2017, the Group carried out a detailed assessment of the impact of the introduction of IFRS 9 on the accounting principles (policy) applied by the Group with respect to the Group's operations or its financial results. This assessment is based on currently available information and may be subject to changes resulting from the acquisition of rational and documentable additional information during the period when the Group applies IFRS 9 for the first time.

The Group does not expect a material impact of the introduction of IFRS 9 on the statement of financial position and equity, except for the effects of the application of IFRS 9 on impairment. The Group expects an increase in impairment losses, with a negative impact on equity, as described below. In addition, as a result of the application of IFRS 9, the classification of some financial instruments will change.

- **Classification and valuation**

In connection with the application of IFRS 9 in the area of classification and valuation, the Group does not expect a material impact on the statement of financial position and equity, the expected changes relate to the presentation. It is expected that all financial assets so-far measured at fair value will continue to be measured at fair value. Trade receivables are maintained to obtain cash flows arising from the contract. The Group has no trade receivables subject to factoring. The Group uses a practical exemption and for trade receivables under 12 months does not identify significant elements of financing.

- **Impairment**

In accordance with IFRS 9, the entity measures the write-down for expected credit losses in the amount equal to the 12-month expected credit loss or expected credit losses in the life of the financial instrument. In the case of trade receivables, the Group will apply a simplified approach and measure the write-off for expected credit losses in the amount equal to the expected credit losses throughout their life.

For the purpose of estimating the expected credit losses, IFRS 9 indicates the validity of using both historical data in the field of repayment as well as reliable data available at the balance sheet date that may increase the accuracy of estimating the expected credit losses in future periods.

The Company identified the following classes of financial assets for which, in accordance with IFRS 9, it estimated the impact of expected loan losses on the financial statements:

- Trade receivables for deliveries and services,
- Other receivables, including those due to LTC settlement
- Sureties and bank deposits,
- Cash.

With respect to trade receivables, it is assumed that the repayment data can be used to estimate credit risk in the future, and therefore the credit losses were estimated using historical data on the maturities of trade receivables and their fulfilment. In order to estimate the expected loss for other financial assets, the insolvency risk was determined based on other data, in particular rating assessments made by rating agencies or given to counterparties as part of the internal credit risk assessment process, adjusted for the probability of default assessment.

The Group estimates that due to the nature of trade receivables, the impairment loss would increase by approximately PLN 637 thousand as at December 31, 2017, along with the associated increase in deferred tax liability by PLN 121 thousand.

- **Hedge accounting**

Because IFRS 9 does not change the general principles of the Group's hedge accounting due to the lack of a decision on the possibility of implementing the changes provided for in this standard, the application of IFRS 9 in the area of hedge accounting will not have a material impact on the Group's financial statements.

8.2. Implementation of MSSF 15

International Financial Reporting Standard 15 Revenue from contracts with clients ("IFRS 15"), which was issued in May 2014, and then amended in April 2016, establishes the so-called The Five Steps Model for Recognizing Revenue from Contracts with Customers:

1) Identification of contracts with the client;
2) Identification of obligations to perform the benefit contained in the contract;
3) Determining the transaction price;
4) Assigning the transaction price to the performance obligations included in the contract;
5) Recognition of revenue when the entity complies with its obligations.

In accordance with IFRS 15, revenues are recognized in the amount of remuneration which, according to the entity's expectation, is due in exchange for the transfer of promised goods or services to the client.

The new standard will replace all existing requirements regarding revenue recognition in accordance with IFRS. The standard applies to annual reporting periods beginning on January 1, 2018 and later. Earlier use is allowed.

The Group has the right to choose a full or modified retrospective approach, and the transitional provisions provide for some practical solutions. The Group plans to apply IFRS 15 from the effective date of the standard, without transforming the comparative data.

The Group's companies conduct activities in the area of generation and sale of electricity, production and sale of heat, extraction of lignite and maintenance and repair-construction services. Lignite sale and purchase transactions and selected other transactions were excluded from the analysis as eliminated in the consolidation process.

Based on the work carried out so far by the Group related to the implementation of IFRS 15, the identified areas of impact of IFRS 15 will not have a material impact on the results presented in the financial statements, except for:

- changes in the presentation of revenues from a part of construction contracts implemented in a consortium of contractors, which until now were presented in the full amount of the subject of the agreement and from 1 January 2018 will be recognized in the part of the implementation attributable to the Group's companies. According to the current state of analysis, revenues from sales and operating costs in 2017 would be lower by approx. PLN 13 million.
- recognition of revenues from trade balancing services for selected clients, which from 1 January 2018 will be separated from the value of goods. This change will only affect the transfer between revenue items in the amount of about PLN 1 million.

Disclosures in the financial statements

IFRS 15 introduces new requirements regarding the presentation and disclosure. The Group believes that the impact of some of these disclosures may be significant. In particular, the Group expects additional disclosures regarding significant judgments and changes in these judgments regarding the areas of long-term construction contracts and trade in electricity.

In addition, in accordance with the requirements of IFRS 15, the Group will present recognized revenues from contracts with customers, divided into categories, which reflect the manner in which economic factors affect the nature, amount, payment date and uncertainty of revenues and cash flows. The Group will also disclose information that will enable users of financial statements to understand the relationship between the disclosure of revenue divided into categories and the revenue information that the Group discloses for each reporting segment.

8.3. Implementation of MSSF 16

In January 2016, the International Accounting Standards Board issued the International Financial Reporting Standard 16 Lease ("IFRS 16"), which replaced IAS 17 Leasing, IFRIC 4 Determining whether the contract includes leasing, SKI 15 Operating leases - special promotional offers and SKI 27 Substance assessment transactions using the form of leasing. IFRS 16 sets out the accounting principles for leasing in terms of valuation, presentation and disclosure.

IFRS 16 introduces a single model of the lessee's accounting and requires the lessee to recognize assets and liabilities resulting from each lease with a period exceeding 12 months, unless the underlying asset is of low value. On the date of the commencement, the lessee recognizes an asset component due to the right of use of the underlying asset and a lease liability that reflects his obligation to make lease payments.

The lessee separately recognizes depreciation of the asset component under the right of use and interest on the lease liability.

The lessee updates the valuation of the lease liability after the occurrence of certain events (e.g. changes in the leasing period, changes in future lease payments resulting from a change in the index or the rate used to determine such charges). As a rule, the lessee recognizes the revaluation of the lease liability as an adjustment to the asset's value due to the right of use.

The Group is a lessee in the case of machine and car leasing contracts, rents office space and uses land, including perpetual usufruct.

Lessor accounting in accordance with IFRS 16 remains substantially unchanged from current accounting in accordance with IAS 17. A lessor will continue to recognize all lease agreements using the same classification principles as in IAS 17, distinguishing between operating leases and finance leases.

IFRS 16 requires broader disclosures from both the lessee and the lessor than in the case of IAS 17.

The lessee has the right to choose a full or modified retrospective approach, and the transitional provisions provide for some practical solutions.

IFRS 16 is effective for annual periods beginning on January 1, 2019 and later. Earlier application is permitted for entities that use IFRS 15 from or before the first application of IFRS 16. The group has not decided to apply IFRS 16 earlier.

As at the date of approval of these consolidated financial statements for publication, the Management Board is in the process of assessing the impact of the introduction of IFRS 16 on the accounting principles (policy) applied by the Group with respect to the Group's operations or its financial results.

9. Change of estimates

During the period covered by the financial statement, the following changes of estimates, affecting the values shown in the financial statements, occurred:

- estimates in the assumptions for the valuation of actuarial provisions,
- estimates in the scope of assumptions regarding the valuation of derivative instruments,
- estimates in the assumptions regarding the calculation of the revenue for compensation of LTC,
- estimates in the assumptions regarding the periods of economic usability of the capital work,
- estimates related to realisation of the deferred tax assets,
- estimates in the scope of assumptions regarding the valuation of provisions for ash storage reclamation,
- estimates in the assumptions for the valuation of the provision for the liquidation of components of tangible fixed assets,
- estimates regarding the valuation of long-term contracts,
- estimates in the scope of assumptions regarding the valuation of the reclamation provisions associated with mining activity
- estimates in the scope of fixed asset impairment.

The impact of changes in estimates on the value of the recoverable amount of property, plant and equipment was presented in Note 19.1.

The impact of estimate changes on the value of actuarial provisions was presented in note 5.2.

In case of the valuation of derivatives (IRS, options), the change in estimates is due to the market changes of risk factors on the interbank market, i.e. the exchange rate and market interest rates. The description of the used protections was included in note 40.3.1.

In the calculation of the revenue due to compensation, the change of estimates relates primarily to changes in the sale prices and purchase of energy on the Commodity Power Exchange and balancing market, the volume of energy production and purchase of energy in order to meet sale plans as well as the interest rate of the 5-year government bonds and the NBP deposit rate, affecting the discount rate. The value of the yearly impairment due to compensations for 2017 is (+) zloty 58.30 million. The principles of recognition of revenue for compensations to cover stranded costs are described in note 10.28.4.

The period of economic usability of the fixed assets is subject to verification at the end of each reporting period based on the expected functionality period, verified against the Management Board’s plans related to the modernisation, sale, and liquidation of the main components of assets. The effect of the changes is recognised in the year in which the verification was performed.

With reference to the deferred tax asset, for each balance sheet day an analysis is carried out and, if necessary, a revaluation write-down is created, which is described in more detail in note 15.3.

The description of the titles of the main recognised provisions and changes of provision items in the current and previous fiscal year was described in note 31.

Note 13.8 shows the values of revenues for construction contracts, taking into account the balance sheet measurement and the expected losses due to these contracts.

10. Significant accounting rules

10.1. Consolidation rules

This consolidated financial statement includes the financial statement of Zespół Elektrowni Pątnów – Adamów – Konin SA as well as financial statements of its subsidiaries, developed each time for the year concluded on 31 December 2017. The financial statements of the entities controlled by it (subsidiaries), after the taking into account the adjustments to ensure compliance with IFRS, are prepared for the same reporting period as the parent company’s statement, using consistent accounting rules, based on uniform accounting policies applied for transactions and economic events of a similar nature. In order to eliminate any differences in the applied accounting methods, adjustments are implemented.

All significant balances and transactions between the Group's entities, including unrealised profits arising from transactions within the Group, were entirely eliminated. Unrealised losses are eliminated, unless they prove the impairment.

Subsidiaries are subject to consolidation from the date on which they are controlled by the Group and cease to be consolidated from the date on which such control ends. The control of the parent company over an entity takes place when:

- it has power over a given entity,
- it is exposed to variable returns or has rights to variable returns due to its commitment in a given entity,
- it has the possibility to use the power to shape the level of the generated returns.

The Company verifies the fact of having control over other entities, if the situation, which indicates a change of one or more of the above-mentioned control conditions, occurred.

If the company has less than a majority of the voting rights of the entity, but the held voting rights are sufficient to unilaterally manage the relevant activities of the entity, it means that it holds power over the entity. When assessing whether the voting rights in a given entity are sufficient to ensure power, the Company analyses all significant circumstances, including:

- the size of the held voting rights block in comparison to the scale of shares and the degree of dispersion of the voting rights held by other shareholders;
- potential voting rights held by the Company, other shareholders, or other parties;
- rights under other contractual arrangements; and
- additional circumstances that may demonstrate that the Company has or does not have the possibility to manage relevant activities in the decision-making moments, including voting schemes observed during previous meetings of the shareholders.

Changes in the parent company's ownership that do not result in the loss of control of the subsidiary are recognised as equity transactions. In such cases, in order to reflect changes in relative shares in the subsidiary, the Group adjusts the balance value of the controlling and non-controlling shares. Any differences between the amount of the adjustment of non-controlling shares and the fair value of the paid or received amount are recognised in the equity and attributed to owners of the parent company.

10.2. Investments in associates and joint ventures

The associates are entities, which are influenced directly by the parent company or through its subsidiaries, and which are neither its subsidiaries nor joint ventures.

Joint ventures constitute contractual arrangements, under which two or more parties undertake a business activity that is subject to joint control.

The financial year of associates, joint ventures, and the parent company is the same. Associates and joint ventures apply accounting rules included in the Act. Before calculating the share of associates and joint ventures in net assets, relevant adjustments are made, in order to make the financial data of these entities comply with IFRSs applied by the Group.

The Group's investments in associates and joint ventures are included in the consolidated financial statement using the equity method. According to the equity method, the investment in the associate or joint venture is initially recognised in accordance with the cost, and then adjusted to reflect the Group's share in the financial result and other complete revenue of the associate or joint venture. If the Group's share in losses of the associate or joint venture exceeds the value of its shares in this entity, the Group discontinues recognising its share in further losses. Additional losses are recognised only to the extent relevant to the legal or customary obligations adopted by the Group or payments made on behalf of the associate or joint venture.

An investment within the associate or joint venture is recognised using the equity method from the date on which the entity acquired the status of a joint venture or associate. On the day of making an investment in the associate or joint venture, the amount by which the value of the investment costs exceeds the Group's share in the net fair value of the identifiable assets and liabilities of this entity is recognised as the value of the company and is included in the balance sheet value of the investment. The amount, by which the Group's share in the net fair value of the identifiable assets and liabilities exceeds the cost of the investment, is directly recognised in the financial result in the period in which the investment was made.

When assessing the need for recognition of the value impairment of the Group's investment in the associate or joint venture, the requirements of IAS 39 are applied. If necessary, the entire balance sheet amount of the investment is tested for the value impairment in accordance with IAS 36 "Value Impairment of Assets" as a single component of assets, comparing its recoverable value with the balance sheet value. The recognised value impairment is part of the value balance sheet of the investment. A reversal of the value impairment is recognised in accordance with IAS 36 to the extent that is relevant to the further increase in the recoverable value of the investment.

The Group ceases to apply the equity method on the day when the investment is no longer the associate or joint venture and when it is classified as the one for sale. The difference between the balance sheet value of the associate or joint venture at the date of cessation of the use of the equity method and the fair value of the retained shares and profits from the partial disposal of shares in the entity is taken into account when calculating the profit or loss on the sale of the associate or joint venture.

The Group continues to apply the equity method, if the investment in an associate becomes an investment in a joint venture, or the other way around: if the investment in a joint venture becomes an investment in an associate. In case of such changes of the ownership shares, the revaluation is not performed.

If the Group reduces the share in the associate or joint venture, but it still settles the share using the equity method, it partially transfers to the financial result the profit or loss, which were previously recognised in other comprehensive income, corresponding to the decrease in the share, if the profit or loss is subject to reclassification to the financial result at the time of sale of the related assets or liabilities.

10.3. Calculation of items denominated in foreign currency

Transactions denominated in currencies other than zloty are calculated into Polish zloty using the exchange rate applicable on the date of conclusion of the transaction.

At the balance sheet date, assets and liabilities denominated in currencies other than zloty are calculated into Polish zloty using the average exchange rate determined for a given currency by the Polish National Bank at the end of the reporting period. The foreign exchange differences, which arise from the calculation, are respectively recognised in the financial revenue item (costs), or in cases of the rules (policy) of accounting, capitalised in the value of assets. Assets and non-monetary liabilities recognised at historical cost in a foreign currency are disclosed at the historical exchange rate of the transaction date. Assets and non-monetary liabilities recognised as per the fair value expressed in a foreign currency are converted to the fair value at the rate of the evaluation date. Profits or losses arising from the recalculation of assets and non-monetary liabilities recognised within the fair value are recognised in accordance with the recognition of profit or loss, which arises from changes in the fair value (i.e., in other comprehensive income or profit or loss, respectively, depending on where the change in the fair value is recognised).

(in thousand PLN)

The following exchange rates were adopted for the purposes of the balance sheet valuation:

	31 December2017	*31 December 2016*
EUR	4.1709	4.4240
GBP	4.7001	5.1445
USD	3.4813	4.1793

10.4. Tangible fixed assets

Tangible fixed assets are stated according to the acquisition price / production cost reduced by the redemption and impairment write-downs for the loss in value. The initial value of fixed assets includes the acquisition price increased by all costs directly related to the acquisition and adaptation of the asset components to a condition for its intended use. The cost also includes the cost of replacing the individual components of machinery and devices when incurred, if the recognition criteria are met. Any costs incurred after the date when a fixed asset is put into operation, such as the maintenance and repair costs, encumber the profit or loss when incurred.

Fixed assets, at the time of their acquisition, are divided into components with a significant value, to which a separate period of the economic usability can be attributed. The costs of general overhauls are also classified as components.

The redemption is calculated on a straight-line basis for an estimated useful life of a given component of assets, amounting to:

Type	**Period**
Buildings and structures	2 - 61 years
Machinery and technical devices	2 - 61 years
Means of transport	2 - 39 years
Other fixed assets	2 - 26 years

The final value, useful life and a depreciation method for the asset components are annually verified and, if necessary, adjusted with effect from the beginning of the just ended financial year. Any changes resulting from the conducted review are recognised as a change in estimates.

A given item of the tangible fixed assets may be removed from the balance sheet after its sale, or if any economic benefits, arising from the further use of such a component of assets, are expected. Any profits or losses resulting from removal of a given component of assets from the balance sheet (calculated as the difference between potential net income from the net sale and the balance sheet value of a given item) are recognised in the profit and loss of the period, in which such removal was made.

Commenced investments relate to fixed assets under construction or assembly and are reported in accordance with the acquisition or production costs reduced by potential impairment write-downs for the loss in value. The fixed assets under construction are not subject to redemption until the completion of their construction and putting the fixed asset into operation. Financing costs subject to capitalisation are also a value element of fixed assets under construction. The question of their capitalisation is described in more detail in note 10.12.

10.4.1. Fixed assets intended for sale

Fixed assets and their groups are deemed as held for sale when their balance sheet value is recovered rather by means of a sale transaction than through their further use. This condition can be met only when the sale transaction is highly probable and the assets' component is available for immediate sale in its present condition. The classification of the assets' component as intended for sale assumes the intention of the company's management board to conduct the sale transaction within one year from the date of classification. The fixed assets classified as held for sale are measured at the lower of two values:

the balance sheet value or fair value reduced by costs related to the sale.

If the Group wants to make a sale transaction, which would result in losing control over its subsidiary, all assets and liabilities of this entity are classified as held for sale, regardless of whether the Group keeps non-controlling interests after this transaction.

If the Group is committed to implement the sales plans for the sale of investments in the joint venture or associate, or part of such an investment, an investment or part of it intended for sale are classified as meant for sale after the fulfilment of the above-mentioned criteria, and the Group discontinues the use of the equity method of accounting for part of the investment classified as meant for sale. The other part of the investment in an associate or joint venture, which is not classified as intended for sale, is still settled using the equity method. The Group discontinues using the equity method at the time of sale, if the sale transaction causes a loss of significant influence on the associate or joint venture.

After the sale transaction, the Group settles retained shares in accordance with IAS 39, unless these shares enable a further classification of this entity as an associate or joint venture; in such case, the Group still continues to apply the equity method.

10.5. Investment properties

The initial recognition of the investment properties takes place according to the acquisition price or production cost, taking into account the transaction costs. The balance sheet value of the investment properties includes the cost of replacing the individual components of the investment property at the time of its incurrence, if the recognition criteria are met, and it does not include costs of the current maintenance of these properties. After the initial recognition, the value of investment properties is reduced by redemption and impairment write-downs for the loss in value.

Investment properties are removed from the balance sheet upon their sale or permanent withdrawal of the given investment property from use, when no future benefits of its sale are expected. Any profits or losses arising from removal of the investment property from the balance sheet are recognised in the income statement of the period in which the aforementioned removal took place.

The transfer of assets to investment properties is made when there is a change in their use confirmed by the owner ceasing to use the assets' component or the conclusion of an operating leasing agreement.

The Group as investment properties presents post-mining lands for which the reclamation process was completed. Such lands, in accordance with the plans of companies executing extraction activities, will be sold in the future.

10.6. Assets concerning stripping and other mining assets

Assets concerning overburden stripping and other mining assets include activated costs incurred in the pre-production phase of the mine, in particular:

- expenses related to the creation of sharing excavation,
- the asset associated with the creation of the provision for reclamation, in the part in which it relates to the removed overburden within the frameworks of works connected with the excavation of the initial excavation,
- the asset associated with the creation of provisions for large, one-off costs related to the areas on which open-pit mining proceeds.

In any case, the Group settles activated costs on a straight-line basis in the period of the economic usability of the duration of particular open pits (the exploitation period adopted for particular open pits). The adopted depreciation periods and depreciation methods are periodically reviewed, at least at the end of each financial year. The assets related to the removal of overburden and other mining assets with the economic usability of less than 12 months are classified within short-term assets.

The write-down against settlement of mining assets is recognised as operating costs within the depreciation costs.

10.7. Expenses related to exploration and evaluation of mineral resources

Within the mining assets item, the Group also shows expenses related to the exploration and evaluation of mineral resources.

The Group activates the expenses related to the exploration and evaluation of mineral resources until the end of the exploration works. The next step is to verify if the identified resources demonstrate the technical feasibility and economic viability of extracting. In the absence of viability of extracting, all the incurred expenses are written off in other operating costs.

Within the costs associated with the exploration and evaluation of mineral resources, the following element can be distinguished, among other things:

- topographical, geological, geochemical, and geophysical analyses,
- drilling,
- open-pit mining works,
- sampling,
- acquisition of extraction rights.

10.8. Intangible assets

Intangible assets acquired in a separate transaction or created (if they meet the recognition criteria for development costs) are measured at initial recognition, at their acquisition price or production cost, respectively. The acquisition price of intangible assets acquired in a business combination transaction is equal to their fair value at the date of the combination. Following the initial recognition, intangible assets are stated at their acquisition price or production cost reduced by the redemption and value impairment write-downs. The expenses incurred on the intangible assets produced internally, except for the activated assets incurred on the development works, are not activated and are recognised in the costs for the period, in which they were incurred.

The Group determines whether the period of use of the intangible assets is definite or indefinite. Intangible assets with a definite useful life are depreciated over the period of use and are subjected to the value impairment tests whenever there are premises indicating their value loss. The depreciation period and method of intangible assets with a definite useful life are verified at least at the end of each fiscal year. Changes in the expected useful life or the expected method of consuming the economic benefits from a given component of assets are recognised through a change of the period or depreciation method, and treated as changes in estimates. Depreciation write-downs for components of intangible assets with a definite useful life are recognised in the profit or loss in the expense of the category, which corresponds to the function of a given component of intangible assets.

Intangible assets with an indefinite useful life and those that are not in use are subject to the annual value impairment test, with respect to particular assets or at the level of the cash generating unit.

Usufruct periods are verified annually and, if necessary, adjusted with effect from the beginning of the just ended financial year. Any changes resulting from the conducted review are recognised as a change in estimates.

Research and development costs

Research costs are recognised in the profit or loss at the time they are incurred. The expenses incurred on the development works executed within the framework of a given venture are transferred to a subsequent period, when it can be assumed that it will be recovered in the future. After the initial recognition of expenses for the development works, a historical cost model is applied, which requires the asset components to be recognised according to the acquisition prices/production costs reduced by the accumulated depreciation and accumulated impairment write-downs against the loss in value. The capitalised expenses are depreciated by the expected period of obtaining revenue from the sale of a given venture.

A summary of the policies applied in relation to the Group's intangible assets is as follows:

	Concessions, patents and licenses	*Computer software*	*Other*
Periods of use	5 years	2 years	5 years
Applied depreciation method	Straight-line method	Straight-line method	Straight-line method
Internally produced or acquired	Acquired	Acquired	Acquired
The value impairment test	The annual assessment of whether there are any prerequisites indicating the occurrence of the loss in value.	The annual assessment of whether there are any prerequisites indicating the occurrence of the loss in value.	The annual assessment of whether there are any prerequisites indicating the occurrence of the loss in value.

Profits or losses resulting from removal of intangible assets from the balance sheet are valued according to the difference between the income from the net sales and the balance sheet value of a given asset component and are recognised in the profit or loss, when they are removed from the balance sheet.

The company also shows the CO_2 emission allowances received or acquired for own needs, as intangible assets.

A detailed description of the accounting policy in respect of CO_2 emission allowances was included in note 10.27.

10.9. Leasing

The Group as a lessee

Financial lease agreements, which substantially transfer all risks and benefits related to holding a leased asset onto the Group, are recognised in the financial situation statement on the lease commencement date according to the lower of the two following values: the fair value of the fixed asset constituting a subject of the lease or the current value of minimal lease payments. Lease payments are allocated between the financial costs and reduction of the balance of the lease liabilities in a way that allows the obtaining of a constant interest rate on the remaining unpaid liability. Financial costs are recognised in profit or loss, unless the capitalisation requirements are met.

The principles of depreciation of fixed assets used under financial leasing should be coherent with the principles used for depreciation of the Group's own assets subject to depreciation. In the event of a lack of sufficient certainty that the lessor will obtain a tenure prior to the end of the lease period, fixed assets used under financial lease agreements are depreciated over the shorter of the two periods: the estimated useful life of a fixed asset or the lease term. The lease agreements, under which the lessor substantially retains all the risks and benefits of ownership of the leased asset, are classified as operating lease agreements. Lease payments under the operating lease agreement and subsequent lease instalments are recognised as operating costs in profit or loss on a straight-line basis over the lease term.

Conditional lease payments are recognised as a cost in the period in which they become due.

10.10. Fair value measurement

The Group measures financial instruments such as instruments available for sale, derivative instruments at the fair value, at each balance sheet date. In addition, the fair value of financial instruments measured in accordance with the depreciated cost was included in note 41.

The fair value is defined as the price that would be received from the sale of an asset or paid in order to transfer a liability in the transaction conducted on normal sale conditions of a component of assets between market participants at the valuation date in the current market conditions. The valuation of fair value is based on the assumption that the sale transaction of a component of assets or the transfer of a liability occurs either:

- on the main market for a given component of assets or liability,
- in the event of absence of a principal market, in the market, this is most advantageous for the asset or liability.

Both, the main and the most advantageous markets must be available to the Group.

The fair value of a component of assets or liability is measured at the assumption that market participants, when determining the price of a component of assets or liability, act in their best economic interest.

The fair value of a component of non-financial assets takes into account the market participant's ability to generate economic benefits by making the greatest and the best use of the component of assets or its sale to another market participant that would provide the greatest and the best use of this component of assets.

The Group uses measurement techniques that are relevant to the circumstances and for which sufficient data to determine the fair value, with maximum use of relevant observable input data and minimal use of unobservable input data, are available.

All assets and liabilities that are measured at the fair value, or their fair value is disclosed in the financial statement, are classified in the fair value hierarchy as described below on the basis of the lowest level of input that is significant to the valuation of fair value treated as a whole:

- Level 1 – Quoted (unadjusted) market prices on the active market for identical assets and liabilities,
- Level 2 – Valuation techniques, for which the lowest level of input data, which is significant for the fair value measurement as a whole, is directly or indirectly observable,
- Level 3 – Valuation techniques, for which the lowest level of input data, which is significant for the valuation of the fair value as a whole, is unobservable.

At each balance sheet date, in the event of assets and liabilities existing per each balance sheet date in the financial statement, the Group evaluates whether there were transfers between levels of the hierarchy through a re-assessment of the classification into different levels, following the materiality of input data from the lowest level, which is essential for the valuation to the fair value treated as a whole.

Summary of essential procedures for the fair value measurement

The Management Board of the Group determines the rules and procedures for both, the systematic valuation of non-listed financial assets at the fair value, as well as one-time valuations, e.g. in case of assets intended for sale within a discontinued activity.

In order to determine the fair value, independent experts are engaged to perform the valuation of significant assets such as assets available for sale and financial liabilities, measured at the fair value. Internal valuation models are also used.

In order to perform the above valuations, independent experts, unrelated to the Group and with qualifications appropriate to conduct such valuations, as well as having current experience in such valuations in locations, where there are assets of the Group are appointed.

For the purposes of disclosure of the fair value measurement, the Group established classes of assets and liabilities based on the type, characteristics, and risks of the various components of assets and liabilities and the level in the fair value hierarchy, as described above.

10.11. Loss in value of non-financial fixed assets

At the balance sheet date, the Group evaluates whether there are any prerequisites indicating that loss in value of the component of non-financial fixed assets may have occurred. In the event when there are such prerequisites, or in case of the necessity to conduct an annual impairment test, the Group estimates the recoverable value of a given component of assets or a cash generating unit, which the component of assets belongs to.

The recoverable value of a component of assets or a cash generating unit corresponds to the fair value reduced of effecting the sale of the given component of assets or respectively the cash generating unit, or its value in use, depending on which one is higher. The recoverable value is determined for an individual asset, unless a given asset component does not independently generate cash inflows that are largely independent of those generated by other assets or groups of assets. If the balance sheet value of a component of assets is higher than its recoverable value, the loss in value occurs, and the write-down to the determined recoverable value is made.

In assessing the value in use, the projected cash flows are discounted to their current value using a discount rate prior to entailing the effects of taxation reflecting the current estimated value of money in time as well as the risk typical for a given component of assets. Impairment write-downs for the loss in value of assets used in the continued activity are recognised in the category of costs, which are consistent with the function of the asset component, in case of which the loss in value was identified.

At each balance sheet date, the Group assesses whether there are any prerequisites indicating that the value impairment write-down, which was recognised in previous periods, in relation to a given asset component, is unnecessary or whether it should be reduced. If such prerequisites exist, the Group estimates the recoverable value of the component of assets. The previously recognised impairment write-down for the loss in value is reversed only if, from the time of recognition of the impairment write-down, a change of the estimated values applied to determine the recoverable value of a given component of assets occurred. In this case, the balance sheet value of the component of assets is increased to its recoverable value. The increased amount cannot exceed the balance sheet value of the component of assets that would have been determined (after taking into account redemption) if, in the previous years, the impairment write-down for the loss in value, in relation to this component of assets, was not recognised. A reversal of the impairment write-down for the loss in value of the component of assets is immediately recognised as income. After the reversal of the impairment write-down, in the following periods, the depreciation write-down related to a given component is adjusted in a way, which within the remaining period of use of this component of assets allows systematically writing down the verified balance sheet value of the component of assets reduced by the final value.

10.12. Borrowing costs

Borrowing costs are capitalised as part of the fixed assets production cost. Borrowing costs consist of interests calculated using the effective interest rate method, financial encumbrances due to financial lease agreements and foreign exchange differences resulting from the external financing up to the amount corresponding to the adjustment of the interest cost. In terms of foreign exchange differences, the cumulative approach is applied.

10.13. Financial assets

Financial assets are classified into the following categories:

- financial assets maintained to the maturity date,
- financial assets measured at the fair value by the financial result,
- loans and receivables,
- available-for-sale financial assets

Financial assets maintained until the maturity date

Financial assets maintained to the maturity date are the financial assets quoted in the active market, and which are not derivative instruments with definite or possible to define payments as well as with the fixed maturity date, which the Group intends and has the possibility to hold to that time, other than:

- determined at the initial recognition as measured at the fair value by the financial result,
- determined as available-for-sale,
- meeting the definition of loans and receivables.

Financial assets maintained to the maturity date are measured at the depreciated cost using the effective interest rate method. Financial assets held to the maturity date are classified as long-term assets if their maturity exceeds 12 months from the balance sheet date.

Financial assets measured at the fair value by the financial result

The component of financial assets measured at the fair value by the financial result is a component that meets one of the following conditions:

a) it is classified as held for trading. The components of financial assets are classified as held for trading, if they are:
   - principally acquired for the purpose of selling in a short period of time,
   - part of the portfolio of identified financial instruments that are managed together and for which there is a probability to generate profit in a short period of time,
   - derivatives, except for the derivatives that are part of hedge accounting and financial guarantee contracts,

b) in accordance with IAS 39, classified into this category upon the initial recognition.

The financial assets measured at the fair value by the financial result are measured at the fair value taking into account their market value at the balance sheet date without the sale transaction costs. Changes in the value of these financial instruments are recognised in the income statement as financial revenues or costs. If the contract contains one or more embedded derivatives, the whole contract can be classified as financial assets measured at the fair value by the financial result. It does not apply to cases where the embedded derivative does not significantly influence the cash flows of the contract or it is clear without conducting or after a superficial analysis that if a similar hybrid instrument was firstly considered then separating the embedded derivative would be prohibited. Financial assets at the initial recognition can be classified to the category measured at the fair value by the financial result if the following criteria are met: (i) such classification eliminates or significantly reduces inconsistency in terms of recognition or valuation (accounting mismatch); or (ii) assets are a part of a group of financial assets, which are managed and measured on the basis of the fair value, in accordance with a documented risk management strategy; or (iii) financial assets contain embedded derivatives that should be recognised separately.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in the active market. They are included in current assets, if their maturity date does not exceed 12 months from the balance sheet date. The granted loans and receivables with the maturity date exceeding 12 months from the balance sheet date are classified as fixed assets.

Assets available for sale

The available-for-sale financial assets are the financial assets which are not derivatives, and which were classified as available for sale or those that do not belong to any of the three previously mentioned categories. Financial assets available for sale are recognised in accordance with the fair value increased with the transaction costs that can be directly attributed to the acquisition or issue of the component of financial assets. In the event of a lack of exchange quotations on the active market and if it is not possible to reliably determine their fair value using alternative methods, the available-for-sale financial assets are measured at the acquisition price adjusted by the impairment writ-down for the loss in value. The positive and negative differences between the fair value of the available-for-sale assets (if there is a market price established on the active market or if their fair value can be determined by some other reliable method), and their acquisition price, after deduction of the deferred tax, are included in other comprehensive income. The decrease in value of the available-for-sale assets caused by the loss in value is recognised as a financial cost.

The acquisition and sale of the financial assets are recognised at the transaction date. At the time of the initial recognition, a component of financial assets is measured at the fair value, increased, in case of the component of assets not classified as the measured at the fair value by the financial result, with the transaction costs, which can be directly attributed to the acquisition.

The component of financial assets is removed from the balance sheet when the Group loses control over the contractual rights that comprise a given financial instrument; it usually occurs when the instrument is sold or when all the cash flows attributed to a given instrument are transferred to an independent third party

In a situation, in which the Group:

- has a legally enforceable right to compensate the recognised amounts, and
- intends to settle on a net basis, or at the same time to realise the component of assets and settle the liability

a financial asset component and financial liability are compensated and presented in the financial statement in the net amount.

The framework agreement described in IAS 32.50 does not constitute grounds for compensation, if both above described criteria are not met.

10.14. Loss in value of financial assets

At the balance sheet date, the Group evaluates whether there are objective prerequisites of the loss in value of the component of financial assets or the group of financial assets.

10.14.1.Assets recognised in accordance with the depreciated costs

If there are objective prerequisites that a loss in value of the granted loans and receivables, measured in accordance with the depreciated cost, occurred, then the cost of the impairment write-down for the loss in value equals to the difference between the balance sheet value of the component of financial assets (excluding future credit losses that have not been incurred yet), discounted using the initial (i.e. determined at the initial recognition) effective interest rate method. The balance sheet value of the asset component is decreased using a write-down account. The amount of the loss is recognised in profit or loss.

The Group firstly evaluates whether there are objective prerequisites for the loss in value of the individual financial assets which are individually significant, as well as prerequisites of the loss in value of the financial assets that individually are not significant. If the conducted analysis shows that there are no objective prerequisites for the loss in value, regardless of whether it is significant or not, the Group includes this component to the group of financial assets with similar credit risk characteristics and jointly assesses in terms of the loss in value. The assets that are individually assessed for the loss in value, and for which the impairment write-down for the loss in value was recognised, or it was considered that the current write-down will not change, are not taken into account in the total assessment of the group of assets in terms of the loss in value.

If the impairment write-down for the loss in value decreased in the next period, and the decrease can be objectively associated with an event occurred after the impairment write-down recognition, then the previously recognised impairment write-down is reversed. The subsequent reversal of the impairment write-down for the loss in value is recognised in profit or loss to the extent, in which as of the date of reversal, the balance sheet value of the component of assets does not exceed its depreciated cost.

10.14.2.Financial assets stated at cost

If there are the objective prerequisites that the loss in value of the unquoted equity instrument, which is not stated in accordance with the fair value, because its fair value cannot be reliably determined, of the equity instrument, which is linked to and has to be settled by delivery of such an unquoted equity instrument, the amount of the impairment write-down for the loss in value is determined as the difference between the balance sheet value of the component of financial assets and the current value of the estimated future cash flows, which are discounted using the current market rate of return for similar financial assets.

10.14.3.Available-for-sale financial assets

If there are objective prerequisites that there was a value of a financial asset component available for sale was impaired, then the amount constituting the difference between the asset component acquisition price (decreased by any repayments of the capital and depreciation) and its fair value, decreased by any impairment write-downs against the component value loss, previously recognised in profit or loss, is derecognised from the equity and transferred to profit or loss. The reversal of the impairment write-down for the loss in value of the equity instruments classified as available for sale cannot be recognised in profit or loss. If the fair value of the debt instrument available for sale increases during the next period, and this increase can be objectively associated with an event occurred after recognition of the impairment write-down for the loss in value in profit or loss, then the amount of the reversible impairment write-down is recognised in profit or loss.

10.15. Other non-financial assets

The Group recognises prepayments as other non-financial assets, if the following conditions are met:

- they result from past events – expenses incurred for the operational purpose of entities,
- their extent can be reliably determined,
- they will result in the impact of economic benefits to the entities in the future,
- they apply to future reporting periods.

Write-offs of active prepayments of costs can occur appropriately to the passage of time and the amount of benefits. The time and method of settlement is justified by the nature of the settled costs, respecting the precautionary principle.

At the end of the reporting period, the Group verifies the active prepayments of costs in order to check whether the degree of certainty associated with the achievement of economic benefits by the entity, after the expiry of the current financial period, is sufficient to show a given item as a component of assets.

During the reporting period, the subjects of prepayments are, among others:

- costs of property insurance,
- costs of current charges for perpetual usufruct of lands,
- deductions for social insurance fund,
- subscriptions,
- other costs related to next reporting periods.

Other non-financial assets include, in particular, the public and legal settlement receivables (except for CIT settlements, which are presented in a separate item of the financial statement), as well as advance payments for future purchases of tangible fixed assets, intangible assets and inventories. The advance payments are presented according to the nature of the assets, to which they relate – respectively, as fixed or current assets. As non-monetary assets, the advance payments are not subject to discount.

10.16. Embedded derivatives

Embedded derivatives are separated from the contracts and treated as derivatives, if the following conditions are met:

- the economic characteristics and risks of the embedded instrument are not closely related to the economic characteristics and risks of the contract, to which a given instrument is embedded;
- a separate instrument with the same performance conditions as the embedded instrument would conform to the definition of the derivative;
- a hybrid (complex) instrument is not stated at the fair value, and the changes of its fair value are not recognised in profit or loss.

The embedded derivatives are stated in a similar way as separate derivatives, which are not treated as hedging instruments.

The scope, in which, according to IAS 39, the economic characteristics and risks specific to the embedded derivative in a foreign currency are closely related to the economic characteristics and risks appropriate for the host agreement (the basic contract) also covers the situations, when the currency of the host agreement is a typical currency for the purchase or sale contracts of non-financial items on the market of a given transaction.

The Group assesses whether a given embedded derivative is separated at the time of its initial recognition.

10.17. Financial derivative instruments and securities

The derivatives used by the Group in order to secure against the risk related to the changes of interest rates and exchange rates are mainly the forward foreign exchange contracts and contracts for the interest rates change (interest rate swaps). Such derivatives are measured at the fair value. Derivatives are stated as assets when their fair value is positive, and as liabilities – when their value is negative.

Profits or losses for the fair value changes of derivatives, which do not comply with the hedge accounting principles are directly stated in the net financial result of the financial year.

The fair value of forward foreign exchange contracts is determined by the reference to the current forward rates for contracts with a similar maturity date. The fair value of contracts for the interest rate swaps is determined by the reference to the market value of similar instruments.

Within the hedge accounting, securities are classified as:

- the fair value hedge securing against the risk of changes in the fair value of a recognised component of assets of liabilities, or
- cash flow hedges securing against the changes in cash flows, which can be attributed to a specific kind of risk related to a recognised component of assets, liability or forecasted transaction, or
- hedging shares in the net assets within a foreign entity.

Securing the currency risk of the substantiated future liability is settled as the cash flow hedge.

At the inception of the hedge, the Group formally determines and documents the hedging relationship as well as the risk management objective and strategy for establishing the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the characteristics of the hedged risk as well as a method of assessing the hedge instrument effectiveness in the compensation for the risk of changes of the fair value of the hedged item or cash flows related to the hedged risk.

It is expected that the hedge will be highly effective in the compensation for changes of the fair value or cash flows resulting from the hedged risk. The hedge effectiveness is constantly assessed to determine whether it is highly effective within all the reporting periods for which it was established.

In addition, the Group secures the cash flow associated with purchasing CO_2 emission allowances in the form of short-term forward contracts.

Due to the fact that contracts for the purchase of non-financial assets are concluded in order to secure own needs, they are excluded from the scope of IAS 39.

10.17.1.Fair value security

The fair value hedge is a hedge against changes in the fair value of a recognised component of assets or liability, or an unrecognised substantiated future liability, or a separated part of such a component of assets, liability or substantiated future liability, which can be attributed to a specific type of risk, and which could influence profit or loss. In case of hedging the fair value, the balance sheet value of the hedged item is adjusted with profits and/or losses for changes of the fair value, resulting from the hedged risk, the hedging instrument is measured to the fair value, and profits or losses for the hedging instrument and the hedged item are recognised in the profit or loss.

If an unrecognised substantiated future liability is designated as a hedged item, the subsequent cumulative changes of the fair value of the substantiated future liability resulting from the hedged risk are recognised as an asset component or a liability, and arising profits or losses are included in the profit or loss. Changes of the fair value of the hedging instrument are also recognised in the profit or loss.

The Group discontinues to use the hedge accounting principles, if a hedging instrument expires, is sold, terminated, or executed, and if the hedge fails to fulfil the criteria of hedge accounting, or if the Group revokes the hedging relationship. Any adjustment of the balance sheet value of the hedged financial instrument, to which the depreciated cost method is applied, is subject to depreciation, and the write-offs are recognised in the profit or loss. The depreciation can begin as soon as the adjustment is made, however, not later than at the time of ceasing the adjustment of the item hedged with changes of the fair value resulting from the hedged risk.

10.17.2.Cash flow security

The cash flow hedge is a hedge against the exposure to variability in cash flows, which can be attributed to a specific type of risk related to a recognised component of assets, liability, or highly probable planned transaction, and which could influence profit or loss. The part of profits or losses related to the hedge instrument, which constitutes an effective security is recognised in other comprehensive income, and an ineffective part is recognised in profit or loss.

If a hedged planned transaction subsequently results in the recognition of a component of financial assets or a financial liability, the associated profits, or losses, which were included in other comprehensive income and accumulated in equity, are transferred to the income statement within the same period, or in the periods, during which the acquired component of assets or liability affect the profit or loss.

If hedging the planned transaction subsequently results in the recognition of a component of non-financial assets or non-financial liability, or the planned transaction related to a component of non-financial assets or non-financial liability becomes a substantiated future liability, to which the fair value hedge will be applied, then, the profits or losses that were recognised in other comprehensive income are excluded from the equity and included in the acquisition price or other balance sheet value of the component of assets of liability.

The profits or losses resulting from changes of the fair value of derivatives, which do not meet the conditions for the application of hedge accounting principles are directly recognised in the net financial result for the current period.

The Group discontinues using the hedge accounting principles when the hedging instrument expires or was sold, its use terminated or it was executed, or the hedge no longer meets the conditions, which allow the application of hedge accounting principles to it. In such a case, the total profit or loss on a hedging instrument, which were recognised in other comprehensive income and accumulated in the equity are still stated in the equity until the forecast transaction takes place.

If the Group no longer expects that the forecast transaction will occur, then the total net profit or loss, accumulated in the equity, are charged to the net financial result for the current period.

10.18. Inventories

Inventories are measured at the lower of the two values: the acquisition price/production cost and the net sale price possible to achieve.

The costs incurred on bringing each component of inventories to its current location and condition – both with regard to the current and previous year – are recognised as follows:

- production fuel - weighted average method
- spare parts and other materials - weighted average method

The net sale price, which is possible to achieve, is an estimated sale price in the ordinary course of business, decreased with costs of completion as well as the estimated costs necessary to complete the sale.

Certificates of Energy origin

Energy origin certificates received free of charge due to the production from renewable, gas, and co-generation sources are shown according to the fair value at the end of the month, in which they were produced. The outgoings of energy origin certificates are measured according to the FIFO method.

10.19. Trade receivables and other receivables

The delivery and service receivables are recognised and stated according to initially invoiced amounts, including the write-down against doubtful receivables. The write-down against receivables is estimated when the recovery of the full number of receivables is no longer probable.

When the impact of the time value of money is significant, the value of the provision size is determined by discounting the predicted future cash flows to the current value, using the discount rate reflecting the current market estimates of the time value of money as well as the possible risk related to a given liability. If a method involving discounting was applied, then the increase in liabilities due to the passing time is recognised as financial revenues.

Other receivables include, in particular, receivables for settlements with employees.

Advance payments for future purchases of tangible fixed assets, intangible assets and inventories are recognised in the item for other non-financial assets. The advance payments are shown according to the nature of the assets, to which they relate – as fixed or current assets, respectively. As non-monetary assets, the advance payments are not subject to discount.

Budgetary receivables are presented as other non-financial assets, except for the receivables due to corporate income tax, which constitute a separate item in the financial statement.

10.20. Cash and cash equivalents

Cash and short-term deposits in the balance sheet include cash in bank and in hand as well as short-term deposits with the original maturity date that does not exceed three months.

The balance of cash and cash equivalents in the consolidated statement of cash flows consists of the above-mentioned cash and cash equivalents.

10.21. Interest-bearing bank loans, borrowings and debt securities

At the time of the initial recognition, all bank credits, loans, and debt securities are recognised at the fair value, decreased by the costs associated with obtaining a credit or loan.

After the initial recognition, the interest credits, loans and debt securities are measured in accordance with the depreciated cost.

While determining the depreciated cost, the costs associated with obtaining a credit or loan as well as discounts or premiums achieved in connection with the liability are taken into account.

Revenues and costs are recognised in the profit or loss, when the liabilities are removed from the balance, and also as a result of the settlement with the effective interest rate method.

10.22. Trade liabilities and other financial liabilities

Short-term liabilities for deliveries and services are stated in the payable amount.

Financial liabilities, which are measured at the fair value by the financial result, include financial liabilities intended for trading as well as financial liabilities initially classified to the categories measured to the fair value by the financial result. Financial liabilities are classified as intended for trading if they were acquired for the purpose of selling in the near future. Derivatives, including separated embedded instruments, are also classified as designed for trading unless they are considered effective hedging instruments. Financial liabilities at the initial recognition can be classified in the categories measured at the fair value by the financial result if the following criteria are met: (i) this classification eliminates or significantly reduces inconsistency of treatment when both the valuation and principles of recognising losses or profits are subject to other regulations; or (ii) liabilities are part of the group of financial liabilities, which are managed and measured on the basis of the fair value, in accordance with a documented risk management strategy; or (iii) financial liabilities contain embedded derivatives that should be recognised separately.

The financial liabilities measured at the fair value by the financial result are measured at the fair value taking into account their market value at the balance sheet date without the sale transaction costs. Changes in the fair value of these instruments are recognised in profit or loss as costs or financial revenues.

Other financial liabilities, which are not financial instruments measured at the fair value by the financial result, are measured in accordance with the depreciated cost using the effective interest rate method.

The Group excludes a financial liability from its balance when the liability expires – i.e. when the contractual obligation is fulfilled, redeemed or terminated. Replacing the existing debt instrument with the instrument of essentially different conditions made between the same entities is recognised by the Group as termination of the original financial liability and recognition of a new financial liability. Similarly, significant modifications of the contractual provisions concerning an existing financial liability are recognised by the Group as termination of the original one and recognition of a new financial liability. The difference of reference balance sheet values arising due to the replacement is shown in the profit or loss.

10.23. Other non-financial liabilities

Other non-financial liabilities include, in particular, liabilities for the value added tax, other public-legal liabilities (except for liabilities due to the corporate income tax, which is recognised in a separate item of the financial statement), as well as liabilities for the received advance payments, which will be settled by the supply of goods, services or fixed assets. Other non-financial liabilities are recognised in the amount that requires payment.

10.24. Sharing profits for employee purposes and special funds

In accordance with the Polish economic practice, the stockholders/shareholders of entities can distribute the profits for employee purposes in the form of making a contribution to a social fund or other special funds. In the financial statement, in accordance with IFRS, this part of the profit distribution is recognised as operating costs of the period, in which the profit distribution was approved by a Shareholders Meeting, due to the fact that the Groups Companies are burdened with neither legal nor customary obligation to this type of the profit distribution.

10.25. Share-based payments

Share-based payments is a transfer of equity instruments of the entity or their equivalents made by the entity or its shareholders to the third parties (including employees), who provided goods and services to a given company, unless the transfer is made for the purpose that is other than paying for goods and services provided for the entity.

The Group includes goods and services received or acquired within the framework of the share-based payment transactions in the equity instruments as well as the corresponding increase in the equity when it obtains these goods and services. If the goods or services obtained or acquired within the framework of the share-based payment transactions are not classified to be recognised as assets, the entity includes them as the cost.

The Group evaluates the obtained goods or services and the corresponding increase in the equity at the fair value of the obtained goods or services, unless it is impossible to reliably estimate their fair value. If the group is unable to reliably estimate the fair value of the obtained goods or services, it indirectly determines their value and the corresponding increase in equity by the reference to the fair value of the granted equity instruments.

The own share-based payments resulting from the entitlement of the PAK Kopalnia Węgla Brunatnego Konin SA and PAK Kopalnia Węgla Brunatnego Adamów SA employees to the free acquisition of the companies' shares on the basis of the Act of 30 August 1996 on the commercialisation and privatisation are recognised in accordance with the above rules. The Group recognises the costs of employee benefits for to this reason from the date of taking control over PAK Kopalnia Węgla Brunatnego Konin SA and PAK Kopalnia Węgla Brunatnego Adamów SA On the other side, the Group recognises the share-based payment programmes in the item of the retained profits, at the same time, allocating a part to the non-controlling shareholders' equity.

10.26. Provisions

Provisions are created when the Group is burdened with the existing liability (the legal or customary expected one) resulting from past events, and when it is probable that the fulfilment of this liability will result in the necessity of the economic benefits outflow, and the amount of this liability can be reliably estimated. If the Group expects the costs covered by the provision to be reimbursed, for example under an insurance contract, then the reimbursement is recognised as a separate component of assets, but only when it is virtually certain that the reimbursement of this will actually occur. The costs related to a given provision are stated in the income statement after the reduction by any reimbursement.

When the impact of the time value of money is significant, the value of the provision size is determined by discounting the forecast future cash flows to the current value, using the discount rate reflecting the current market estimates of the time value of money as well as the possible risk related to a given liability. If a method of discounting was applied, then the increase in liabilities due to the passage of time is recognised as financial costs.

In particular, the Group creates the following provisions:

- **provisions for post-employment benefits as well as jubilee awards**

In accordance with the remuneration systems, the Group's employees are entitled to the following benefits:

- retirement or disability benefits, payable at the time of retirement,
- death benefits for families of deceased employees,
- coal benefits for employees of PAK KWB Konin SA and PAK KWB Adamów SA

The amount of benefits depends on the number of years of employment and the average salary of the employee. The Group creates provisions for these future liabilities for the purpose of allocating the costs to the periods that they concern. The current value of these liabilities at each balance sheet date is calculated by an independent actuary. The accumulated liabilities are equal to the discounted payments, which will be made in the future, taking into account the rotation of employment and they relate to the balance sheet date. Demographic information and information about the rotation of employment are based on historical data. Profits and losses of actuarial calculations are recognised in profit or loss and other comprehensive income.

- **Provision for the liquidation of fixed assets components**

The provision for liquidation of fixed assets is created in the event of the legal obligation occurrence or making the commitment by the management board of the Group. The provision is created on the basis of estimates of the future liquidation costs based on available offers related to the fixed assets liquidating services, taking into account the rules set out in IFRIC 1. The discount effect is recognised in the income statement.

- **Provision for the liquidation of ash storage yards**

The Group creates a provision for liquidation of ash dumps due to a legal obligation resulting from the integrated approval entries. This provision is created on the basis of ash storage yard future reclamation cost estimates, resulting from the studies and technical-economic analyses, developed by the management of the Group, as well as the received external offers for planned directions of reclamation.

- **Provision for the submission of redemption of Energy origin certificates**

The provision for the obligation to present the redemption of certificates of origin of energy produced from renewable energy sources or in peak load co-generation is recognised as follows:

- in a part covered by the certificates of origin held at the balance sheet date – in the value of the held certificates,
- in a part uncovered by the certificates of origin at the balance sheet date – at the lower value of the market value of the certificates required to fulfil the obligation at the balance sheet date, and a possible penalty.

- **Provisions for the liabilities due to the emission of greenhouse gasses and provisions for the redemption of certified emission reduction (EUA)**

The provision for liabilities due to the emission of greenhouse gases included in the system of emission allowances is created only when the actual production shows a shortage of emission allowances in respect of the allowances granted for the whole reporting period.

The provision is created by net liabilities method, in the amount of:

- in a part covered by the allowances held at the balance sheet date – in the value of the held allowances, i.e. purchased at the balance sheet value, received in the zero value.
- in the part uncovered by the allowances on the balance sheet date – at the lower of the market values of the allowances required to satisfy the obligation and a possible penalty.

o **Reclamation and other provisions associated with mining activity**

- the provision for liquidation of facilities and mining areas

On the basis of the Geological and Mining Law act, the companies conducting extraction activities are obliged to reclaim the areas of extraction works. Due to this, the Group creates a provision both, for the costs of area reclamation related to current coal extraction on a given open pit and for the costs of the final excavation reclamation in the state of advancement of coal extraction in particular open pits on every reporting date.

The provision for the final excavation reclamation is created in correspondence with the assets' component (in the part in which it relates to the initial excavation, on the basis of the volume of the final excavation), and in correspondence with the income statement (in the remaining part, taking into account the state of advancement of coal extraction in particular open pits on a given reporting date). In correspondence with the assets' component, the Group also creates a provision for the external dump reclamation. The provision for reclamation costs associated with current coal mining is created in correspondence with the income statement.

The provision is created on the basis of estimation of future reclamation costs based on reports of independent experts estimating reclamation costs on the order of the company's management boards executing extraction activities. Estimates concerning projected reclamation costs are analysed periodically; on every reporting date, the size of provision is verified in accordance with current assumptions within discount rate, inflation, and the size of extraction. Write-down for the provision related to extraction of a given year charges operating costs (other costs by type), and the difference resulting from the provision discount from previous years influences financial costs. The use of the provision is settled in correspondence with financial costs at the end of every reporting period. The use of the provision in the part concerning taxes and charges is settled as a reduction of costs incurred during the reporting period of tax costs and charges, while the use of the provision in the part related to other liquidation and reclamation costs is settled as a reduction of other costs by type.

- The provision for the costs related to the preparation of exploitation areas

The Group, within run activities, is obliged to restore to the original condition, or to rebuild damages caused by the mine operations. Due to this, the Group creates the provision for projected costs, to pay which it is obliged on the basis of concluded agreements. Estimates concerning projected costs related to the mine operations are updated on every reporting date. The creation of the provision is recognised, on the other side, within the framework of mining assets.

10.27. CO_2 emission allowances

The CO_2 emission allowances obtained free of charge are recognised in the financial statement as allowances intended for own needs at a zero value in the intangible assets item. The emission allowances and their equivalents purchased by the Group for own needs are recognised as intangible assets. These allowances are measured at the acquisition price. The provision for liabilities due to the emission of greenhouse gases included in the system of emission allowances is created only when the actual production emission shows a shortage of emission allowances in respect of the allowances granted for the entire reporting period. This provision is created according to the FIFO principle.

The cost of the created provision is presented in the income statement, in the cost of sales.

10.28. Revenues

Revenues are recognised to the extent that it is probable that the Group will achieve economic benefits associated with the transaction, and the amount of revenues can be reliably measured. Revenues are recognised at the fair value of the received or receivable payment, after deduction of the value added tax (VAT), as well as excise tax and discounts. Revenues are also recognised according to the below criteria.

10.28.1.Sale of goods and products

Revenues are recognised if the significant risk and benefits of the equity related to goods and products were transferred to the buyer and the amount of revenues can be reliably measured.

Sales revenues also include the sales revenues of green and red certificates. At the time of production, the certificates of origin held for sale are included in the sales revenues, and therefore, in order to avoid inflating revenues at the time of selling, the costs of selling certificates are recognised as an adjustment of the sales revenues.

10.28.2.Provision of Services

Revenues from services are recognised on the basis of the extent of their completion.

The percentage progress status for the services completion is determined as a relation between the incurred costs and estimated costs, which are necessary to complete the order.

If it is impossible to reliably estimate the contract results, then the revenues generated due to this contract are recognised only to the amount of incurred costs which the Group expects to recover.

10.28.3.Contracts for construction services

The construction contract is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology, and function or their ultimate purpose or use.

If it is possible to reliably estimate the outcome of the contract for a construction service, the revenues and costs related to the contract for a construction service are recognised as the revenues and costs according to the extent of the contract execution at the end of the reporting period.

The contract performance progress is obtained by determining the share of contract costs, incurred due to the works executed until the valuation date, in the estimated total contract costs.

When the outcome of a contract cannot be estimated reliably:

a) negative revenues should be recognised only to the extent of incurred contract costs, which have a probability of being recovered; and

b) the contract costs are recognised as a cost for the period, in which they were incurred.

When it is probable that the total contract costs will exceed the total contract revenue, the expected loss shall be immediately recognised as an expense.

The gross payable amount from the employers for the works under the contract is recognised in the financial situation statement as assets and the gross amount payable to the employers for the works under the contract - as liabilities.

10.28.4.Revenues from compensation for stranded costs

The Group receives compensation for the coverage of the stranded costs pursuant to the Act of 29 June 2007 on the principles of coverage of costs incurred by producers due to early termination of long-term agreements for the sale of power and electricity. Revenue from compensation is recognised successively with the earned compensation rights at the end of each fiscal year, until the end of their validity period.

Per each revenue recognition moment, the Group determines a factor for estimated stranded costs to the total amount of received, returned, and expected discounted annual advance payments (including the previously received advance payments). The revenue amount for a given fiscal year is the product of the indicator and previously received amounts of advance payments adjusted with annual impairments, decreased by the revenues for compensation recognised in the previous years.

The difference between the total amount of the recognised revenue and the total amount of the received advance payments to the total amount of the stranded costs are recognised by the Group as:

- receivables, in the event of a negative difference between the total amount of received advance payments and the revenue recognised in relation to compensation,
- liabilities, in the event of a positive difference between the total amount of received advance payments and the revenue recognised in relation to compensation.

10.28.5. Government subsidies

In the event of a justified certainty that a grant will be acquired and all the associated requirements will be satisfied, then the government grants are recognised as per their fair value.

If the grant relates to a given cost item, then it is recognised as revenue in a manner commensurate with the costs, the grants is intended to compensate. If the grant relates to an asset component, then its fair value is recognised on the revenue account for future periods and then, gradually, through equal yearly write-downs, recognised in the profit or loss over the estimated period of use of the associated asset component.

If the Group receives non-monetary grants, both the component of the assets and the grant are recognised at nominal value and gradually, by equal annual write-offs, are included in profit or loss during the estimated useful life of the received component of assets.

10.29. Costs

Costs of goods sold

The cost of goods sold includes:

- the production cost incurred during the reporting period, adjusted for the change in the level of products (finished products, semi-finished products and production in progress), as well as adjusted for the cost of manufacturing products for own needs,
- the value of sold goods and materials according to the acquisition cost,
- the creation of the impairment write-downs against the value of tangible fixed assets, intangible assets and inventories,

The production costs, which can be directly allocated to the revenues achieved by the entities, influence the financial result of the entities for the reporting period, in which the revenues occurred.

The production costs, which can be only indirectly allocated to the revenues and other benefits achieved by the entities, influence the financial result of the entities in the part, in which they relate to a given reporting period, providing their adequacy to the revenues and other economic benefits, including the valuation of fixed assets and inventories.

10.30. Other operating revenues and costs

Other operating income and costs include items mainly related to:

- the disposal of tangible fixed assets, intangible assets,
- the creation and reversal of provisions, except for the provisions related to the financial operations or included in operating expenses,
- free transfer or receiving, including the way of donation of assets, as well as cash.
- the compensation, penalties, and fines, as well as other costs not related to the usual business activity.

10.31. Revenues and financial costs

Revenues and financial costs especially include the revenues and costs related to:

- the sale of financial assets,
- the revaluation of financial instruments, except for the financial assets available for sale, the revaluation effects of which are included in the revaluation capital,
- the revenues due to the share in profits of other entities,
- the interest (including the valuation effect with a depreciated cost),
- the changes in the value of the provision resulting from the fact of approaching the date of incurring the cost (the unwinding of the discount effect),
- the foreign exchange differences which are a result of the operations performed during the reporting period and the balance sheet valuation of assets and liabilities at the end of the reporting period, except for the foreign

exchange differences recognised in the initial value of the fixed asset, to the extent in which they are considered as an adjustment of the interest costs and foreign exchange differences,

- other items connected with the financial activity of the company.

Revenues and costs for the foreign exchange rates are presented after compensation.

The revenues and costs due to the interest are successively presented as they grow, including the effective interest rate method in relation to the net balance sheet value of a given financial instrument, based on the concept of materiality.

Dividends are recognised at the time of establishment of the shareholders' rights to these dividends.

10.32. Taxes

10.32.1.Current tax

The liabilities and receivables for the current tax for the current period and previous periods are measured in the amount of the expected payment to the tax authorities (subject to return from tax authorities), using the tax rates and regulations, which were legally or actually applicable as at the balance sheet date.

10.32.2.Deferred tax

For the purpose of financial reporting, the deferred tax is provided, using the balance liability method in relation to all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their balance sheet value presented in the financial statement.

The provision for the deferred tax is recognised in reference to all positive temporary differences:

- except for the situation when the provision for the deferred tax arises from the initial recognition of the company's value or of the assets' component or liability on a transaction other than a combination of the entities, and at the time of its conclusion have no influence on the gross financial result, as well as on the taxable income or tax loss, and
- in case of positive temporary differences resulting from the investment in subsidiaries or associates and shares in joint ventures – except for the situations where dates of the reversal of temporary differences are subject to the investor's control and it is probable that in the predictable future, temporary differences shall not be reversed.

The assets for the deferred tax are recognised in relation to all negative temporary differences, as well as unused tax credits and unused tax losses transferred to future years, to the extent that it is probable that the taxable income, which allows using the above-mentioned differences, assets, and losses, will be achieved:

- except for a situation when the assets for the deferred tax associated with negative transition differences as a result from the initial recognition of the assets or liability component for a transaction other than a combination of the entities, and at the time of its conclusion, have no influence on the gross financial result, nor on the taxable income or tax loss, and
- in case of negative temporary differences resulted from the investment in subsidiaries or associates and shares in joint ventures, the assets' component for the deferred tax is recognised in the balance sheet only to the extent that it is probable that in the predictable future, the above mentioned temporary differences will be reversed and the taxable income, which enables the negative temporary differences to be deducted, will be achieved.

The balance sheet value of the asset component for the deferred tax is reviewed on every balance sheet date and reduced to the extent that it is no longer probable that the taxable income sufficient for a partial or complete realisation of the assets' component for the deferred tax will be achieved.

An unrecognised deferred tax asset is re-assessed as at each balance sheet date, and is recognised at the amount reflecting the likelihood of achieving the future taxable income allows the recovery of this asset component.

The deferred tax assets and provisions for the deferred tax are evaluated with the use of the tax rates that are expected to be applicable in the period, in which the assets component is realised or the provision is reversed, the basis for which will be tax rates (and tax regulations) applicable at the balance sheet date, or those which will certainly be effective as at the balance sheet date in the future.

The income tax on items recognised outside of the profit or loss is recognised outside of the profit or loss: other total income related to the items recognised in other comprehensive income or directly in the equity, relating to the items recognised directly in the equity.

The companies of the Group compensate the deferred income tax assets with the provisions for the deferred income tax provisions only and solely if it has an executable legal right to compensate receivables with current tax liabilities, and the deferred income tax is related to the same taxpayer and the same tax authority.

10.32.3. Value added tax and excise tax

Revenues, costs, assets and liabilities are recognised after deducting the value added tax, with the exception of:

- the situation when the value added tax paid at the time of the assets or service purchase is impossible to be recovered from the tax authorities; it is then recognised as part of the acquisition price of the assets' component or as a cost item part, and
- receivables and liabilities, which are stated with the amount of the value added tax.

The net amount of the value added tax, which is recoverable or payable to the tax authorities, is included in the financial statement as part of receivables or liabilities.

The net amount of the value added tax and excise tax, which are recoverable or payable to tax authorities are included in the financial statement as parts of receivables or liabilities.

10.33. Net profit per one share

The net profit per share for each period is calculated by dividing the net profit for a given period by the weighted average number of shares in a given reporting period.

10.34. Acquisition under joint control

The situation, in which a particular transaction or economic phenomenon, requiring inclusion in the statement drawn up in accordance with IFRS, is not regulated by the provisions of the various standards, was settled by IAS 8 point 10–12. These provisions impose on the entity, which draws up the statement in accordance with IFRS, the obligation to create its own list of accounting rules, indicating the characteristics of the following accounting principles: a faithful presentation of the financial position, results of operations and cash flows, reflection of the substance of the transaction, neutrality, caution and completeness in all aspects.

According to the analyses conducted by the Company, the commonly used method for the settlement of such transactions is pooling of interests, and such a method was applied by the Company. At the bottom of this method, there is an assumption that merging entities, both before and after the transaction, were controlled by the same shareholder, and therefore the consolidated financial statement reflects the continuity of joint control and does not reflect any changes in the value of net assets to fair values (or recognition of new assets), or the valuation of the company's value, since none of the merging entities is not actually acquired. The settlement takes place on the day of the merger and the previous data is not adjusted.

10.35. Obligation to purchase non-controlling interests

The Company's obligation to redeem the employee shares is recognised at the date of taking control, and refers to situations in which employees have the option of selling shares. According to the selected policy, non-controlling interests receive the allocation of the result and other total incomes in the subsequent reporting periods. At the end of every reporting period, the adjustment of non-controlling interest takes place, as if they were acquired while simultaneously recognising the liability due to the option to redeem shares. The difference between the value of the non-controlling shares derecognised at the reporting date and the recognised financial liability is included in the position of retained profits.

11. Acquisition of ventures

In the period between 1 January 2017 and 31 December 2017, there were no new acquisitions of ventures.

12. Operating segments

For the purpose of management, the Group was divided into parts on the basis of manufactured products and provided services.

Therefore, there are following operating segments:

- The Generation Segment covering production of electricity both from conventional sources (including cogeneration) and by combustion and co-combustion of biomass. Basic fuels used by the Generation Segment are lignite and biomass. The Generation Segment covers following entities:
  - Zespół Elektrowni "Pątnów – Adamów – Konin" SA
  - "Elektrownia Pątnów II" Sp. z o.o.
  - "PAK – HOLDCO" Sp. z o.o.
  - "PAK Infrastruktura" Sp. z o.o.
- The Mining Segment covering the extraction of lignite. In the Mining Segment, within the Capital Group ZE PAK SA:
  - „PAK Kopalnia Węgla Brunatnego Konin" SA
  - „PAK Kopalnia Węgla Brunatnego Adamów" SA
- The Renovation Segment performing services in the scope of construction and renovation services. The Segment covers activities of:
  - Przedsiębiorstwo Remontowe „PAK SERWIS" sp. z o.o.
  - „Energoinwest Serwis" sp. z o.o. in liquidation
  - „EL PAK Serwis" sp. z o.o. in liquidation
- The Sales Segment performing services of the sale of electricity. The Sales Segment also includes the "PAK – Volt" SA company.

ZE PAK SA Group operates also in other kinds of activities, included in the 'Other' column. In 2017 there is included the activity of the following companies: of Eko-Surowce sp. Z o.o. - in liquidation, Aquakon sp. z o.o. - in liquidation, PAK Adamów sp. z o.o. and PAK Górnictwo sp. z o.o. Due to the acquisition of other activities by PAK Górnictwo Sp. z o.o., which became the core business of this company, in 2017 data of this company are presented in the 'Other' segment. On 30 June 2017, EL PAK sp. Z o.o. (acquired company) and PAK Serwis sp. z o.o. (acquirer) have merged into one Company. The activity of the two companies is included in the 'Renovation' segment.

Transaction prices used in transactions between operating segments are determined on the basis of commercial principles, like in transactions with non-related entities.

Revenues due to transactions between segments are eliminated in the process of consolidation.

The Board monitors separate results of the operating activities of segments in order to decide on allocation of resources, evaluation of this allocation's outcomes, and the results of activities. The basis of assessment of the results of activities is profit or loss on the operating activity and EBITDA.

Segments' results for periods concluded on 31 December 2017 and 31 December 2016 are presented below:

(in thousand PLN)

12 months period ended 31 December 2017

	Generation	Mining	Renovation	Sale	Other	Consolidation adjustment	Total
Sales revenue to external customers	1 757 534	6 481	95 886	575 826	7 348	-	2 443 075
Sales revenue between segments	338 848	808 025	180 441	5	161 371	(1 488 690)	-
Sales revenue	**2 096 382**	**814 506**	**276 327**	**575 831**	**168 719**	**(1 488 690)**	**2 443 075**
Cost of goods sold	(1 795 567)	(760 653)	(244 485)	(566 903)	(159 569)	1 491 781	(2 035 396)
Gross profit / (loss)	**300 815**	**53 853**	**31 842**	**8 928**	**9 150**	**3 091**	**407 679**
Other operating income	4 481	5 878	714	501	239	(489)	11 324
Selling and distribution expenses	(2 568)	(4)	-	(534)	(1 152)	-	(4 258)
Administrative expenses	(42 709)	(48 336)	(17 328)	(4 431)	(6 663)	-	(119 467)
Other operating expenses	(2 322)	(1 667)	(836)	(343)	(273)	255	(5 186)
Finance income	18 611	1 542	468	127	28	(4 583)	16 193
Finance costs	(34 473)	(15 279)	(920)	(94)	(67)	3 181	(47 652)
Profit before tax	**241 835**	**(4 013)**	**13 940**	**4 154**	**1 262**	**1 455**	**258 633**
Income tax expense	(46 265)	(23 479)	(3 898)	(869)	178	(756)	(75 089)
Net profit/loss for the period from continuing operations	**195 570**	**(27 492)**	**10 042**	**3 285**	**1 440**	**699**	**183 544**
Profit / (loss) from operating activities, without financial operations and income tax	**257 697**	**9 724**	**14 392**	**4 121**	**1 301**	**2 857**	**290 092**
Depreciation / Amortization	123 081	69 529	6 339	73	1 900	(1 274)	199 648
Change in impairment	-	22 165	-	-	-	-	22 165
EBITDA	**380 778**	**101 418**	**20 731**	**4 194**	**3 201**	**1 583**	**511 905**

(in thousand PLN)

12 months period ended 31 December 2016

	Generation	Mining	Renovation	Sale	Other	Consolidation adjustment	Total
Sales revenue to external customers	1 742 513	8 103	67 815	878 419	7 861	-	2 704 711
Sales revenue between segments	434 773	823 774	243 879	5	94 635	(1 597 066)	-
Sales revenue	**2 177 286**	**831 877**	**311 694**	**878 424**	**102 496**	**(1 597 066)**	**2 704 711**
Cost of goods sold	(1 875 674)	(695 462)	(297 418)	(869 559)	(103 973)	1 600 733	(2 241 353)
Gross profit / (loss)	**301 612**	**136 415**	**14 276**	**8 865**	**(1 477)**	**3 667**	**463 358**
Other operating income	6 787	18 835	1 237	1	303	(702)	26 461
Selling and distribution expenses	(2 726)	-	-	(470)	(1 164)	-	(4 360)
Administrative expenses	(37 625)	(41 576)	(20 875)	(4 589)	(3 971)	2	(108 634)
Other operating expenses	(1 959)	(2 684)	(769)	(42)	(75)	137	(5 392)
Finance income	5 628	3 389	221	277	6	(404)	9 117
Finance costs	(56 484)	(16 368)	(160)	(2)	(62)	404	(72 672)
Profit before tax	**215 233**	**98 011**	**(6 070)**	**4 040**	**(6 440)**	**3 104**	**307 878**
Income tax expense	(35 607)	(19 333)	(824)	(731)	(507)	(590)	(57 592)
Net profit/loss for the period from continuing operations	**179 626**	**78 678**	**(6 894)**	**3 309**	**(6 947)**	**2 514**	**250 286**
Profit / (loss) from operating activities, without financial operations and income tax	**266 089**	**110 990**	**(6 131)**	**3 765**	**(6 384)**	**3 104**	**371 433**
Depreciation / Amortization	112 206	105 323	6 796	71	1 974	(4 671)	221 699
Change in impairment	-	455	-	-	-	-	455
EBITDA	**378 295**	**216 768**	**665**	**3 836**	**(4 410)**	**(1 567)**	**593 587**

(in thousand PLN)

13. Revenues and costs

13.1. Sales revenue

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Revenues by type		
Electricity sale	1 513 909	1 611 297
Electricity sold from the market	579 571	737 746
Energy certificates of origin	700	812
Construction contracts	82 906	59 506
Compensation related to PPA termination	181 335	207 158
Heat	57 175	60 541
Other	30 579	29 186
Excise	(3 100)	(1 535)
Total	2 443 075	2 704 711

Territorial structure	*12 months period ended 31 December 2017*	*12 months period ended 31 December 2016*
Poland	2 434 894	2 685 820
EU Countries	7 951	17 121
Outside EU	230	1 770
Total sale revenues	2 443 075	2 704 711

13.2. Other operating revenues

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Compensations received	2 258	3 650
Depreciation of fixed assets purchased from MLF*	523	348
Reversal of write-downs against receivables	257	-
Grants settlement	1 549	12 940
Grants received	3 644	-
Reversal of provisions for costs and losses and liabilities write-off	1 558	7 323
Other	1 535	2 200
Total	11 324	26 461

**MLF – Mining Liquidation Fund*

The largest components of the "Other" item in 2017 are revenues from revaluation of materials in the amount of PLN 104 thousand reimbursement of property tax in the amount of PLN 244 thousand, revenues from the sale of scrap in the amount of PLN 112 thousand.

(in thousand PLN)

13.3. Other operating expenses

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Loss on the sale of property, plant and equipment	225	1 384
Creation of provisions	1 493	527
Impairment write-down on receivables	207	438
Compensations paid	72	371
Costs of court and enforcement proceedings	288	565
Electricity-related damage	211	160
Donations given	375	229
Real estate tax for previous years	532	268
Compensatory pensions	236	261
Other	1 547	1 189
Total other operating expenses	5 186	5 392

The main components of the "Other" item in 2017 are the utilization costs in the amount of PLN 197 thousand, the settlement of provisions for energy certificates of PLN 343 thousand, the costs of removing damage in the amount of PLN 322 thousand.

13.4. Financial income

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Interest income	3 527	4 919
Dividend	208	60
Foreign exchange gains	12 378	-
Valuation of interest rate hedging instruments (SWAP)	-	296
Other	80	3 842
Total financial income	16 193	9 117

13.5. Financial costs

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Interest expenses	27 228	37 667
Valuation and realization of derivative financial instruments	7 036	7 379
Foreign exchange losses	-	12 782
Reserve discount for the liquidation of power units	746	429
Actuarial reserves discount	1 530	1 093
Reserve discount for reclamation	9 855	7 682
Other	1 257	5 640
Total of financial costs	47 652	72 672

(in thousand PLN)

In the "Other" item in 2017, there are mainly presented the commissions referring to loans, bank loans and guarantees in the amount of PLN 560 thousand, reversal of the discount for the mining damage provision in the amount of PLN 127 thousand and revaluation of the investment in the amount of PLN 418 thousand.

13.6. Costs by type

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Depreciation / Amortisation	199 648	221 699
Impairment write-downs against property, plant and equipment	22 165	455
Impairment write-downs against inventories	(852)	10 188
Materials	252 602	336 435
External services	112 451	66 041
Taxes and charges, excluding excise duty	201 592	204 688
Costs of allowances for emission of CO_2	289 942	311 328
Employee benefits	461 291	488 005
Other costs by type	39 350	48 354
Cost of goods for resale and raw materials sold and resale of electricity from the market	555 156	747 216
Total cost by type	2 133 345	2 434 409
Items included in cost of goods sold	2 035 396	2 241 353
Items included in selling and distribution expenses	4 258	4 360
Items included in administrative expenses	119 467	108 634
Change in the stocks of finished goods	(28 710)	77 800
Cost of goods and services for internal needs	2 934	2 262

13.7. Depreciation costs and impairment write-downs included in the profit or loss

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Items included in the cost of manufacture of sold products:		
Fixed assets depreciation	176 897	182 044
Depreciation of mining asset	8 812	14 384
Intangible assets depreciation	714	875
Impairment of inventory	-	11 859
Impairment of tangible fixed assets	22 165	(1 338)
Impairment of intangible assets	-	1 338
	208 588	209 162
Items included in selling and distribution costs:		
Fixed assets depreciation	15	85
	15	85

(in thousand PLN)

Items included in administrative costs		
Fixed assets depreciation	12 744	23 878
Intangible assets depreciation	466	433
Impairment of tangible fixed assets	-	455
	13 210	24 766

13.8. Construction agreements

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Revenues from contracts for construction services recognised in the period	82 906	59 506
Revenues invoiced in the period	85 630	48 597
Balance sheet valuation	(2 724)	10 909
Costs applied in the period	82 364	51 153
Expected losses due to the contracts recognised in the period	357	(78)
Results due to performance of the contracts included in the period	185	8 431

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Gross amount payable by contracting parties due to works resulting from the contract	7 080	8 168
Gross amount paid to contracting parties due to works resulting from the contract	5 626	3 990

14. Components of other comprehensive income

Components of other total revenues present as follows:

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Cash flow securities		
Profits (losses) for the period	5 072	7 379
Adjustment resulting from reclassification of profits (loses) included in the profit or the loss	367	(1 383)
Gross cash flow securities for the period	**5 439**	**5 996**
Income tax concerning cash flow securities	(1 033)	(1 139)

(in thousand PLN)

Net cash flow securities for the period	**4 406**	**4 857**
Actuarial gross profits (losses) concerning provisions for post-employment employee benefits	**(2 155)**	**4 613**
Income tax concerning actuarial profits (losses)	409	(876)
Actuarial net profits (losses) concerning provisions for post-employment employee benefits	**(1 746)**	**3 737**
Other gross comprehensive income	**3 284**	**10 609**
Income tax concerning other comprehensive income	**(624)**	**(2 015)**
Other net comprehensive income	**2 660**	**8 594**

15. Income tax

15.1. Tax load

The main components of tax load for the year ended 31 December 2017 and 31 December 2016 are as follows:

Included in the profit or the loss	*12 months period ended 31 December 2017*	*12 months period ended 31 December 2016*
Current income tax		
Current income tax load	13 077	11 491
Deferred income tax load		
Related to creation and reversal of temporary differences	61 990	45 541
Other changes	22	560
Tax load in the consolidated profit or loss	**75 089**	**57 592**
Included in the consolidated statement of the comprehensive income		
Net profit (loss) tax due to revaluation of cash flow securities	(1 033)	(1 139)
Actuarial allowance concerning actuarial profits/losses	409	(876)
Tax advantage/(tax load) included in comprehensive income	**(624)**	**(2 015)**

(in thousand PLN)

15.2. Fixing of an effective tax rate

The agreement of income tax on the gross financial result before taxation according to the statutory tax rate with the income tax calculated according to the effective tax rate of the Group for the year ended on 31 December 2017 and 31 December 2016 is as follows:

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Gross profit before taxation from continuing operations	**258 633**	**307 878**
Tax at the statutory tax rate applicable in Poland, amounting to 19%	**49 141**	**58 497**
Adjustment concerning the current income tax from previous years	(273)	1
Not included tax losses	(82)	(4 639)
Usage of the tax losses not recognised earlier	(786)	(22)
Fixed costs that are not tax deductible costs	1 332	4 387
Revenues that are not taxable	301	(170)
Change related to the different tax rate in Germany (30%)	-	168
Others	25 456	(630)
Tax a tan effective tax rate of 29.03% (in 2016 18.71%)	**75 089**	**57 592**
Income tax in profit and loss account	**75 089**	**57 592**

Explanation of the main components of the item "Other"

In connection with the update of financial projections for PAK KWB Adamów SA, deferred income tax assets of PLN 19 658 thousand will not be used. There are also no assets on the write-down of excavators, which we treat as a permanent difference in the amount of PLN 4 211 thousand.

(in thousand PLN)

15.3. Deferred income tax

Deferred income tax results from the following items:

			Consolidated profit and loss account for 12 months period ended	
	31 December 2017	*31 December 2016*	*31 December 2017*	*31 December 2016*
Deferred tax asset				
Balance sheet provisions	130 959	127 581	3 787	3 787
Overburden and other mining assets	7 946	7 571	375	375
Interest and exchange rate differences	4 832	11 377	(6 545)	(6 545)
Hedging instruments	781	1 910	(2 162)	(2 162)
Valuation of non-terminated agreements for building services	1 610	1 726	(116)	(116)
Tax loss from previous years	30 361	35 964	(5 603)	(5 603)
Impairment write-down on inventories	1 475	1 936	(461)	(461)
Impairment write-down on receivables	667	714	(47)	(47)
Impairment write-downs on fixed assets	3 083	-	3 083	3 083
Difference between the carrying amount and tax value of fixed assets	7	3 537	(3 530)	(3 530)
Settlements with employees	3 813	5 139	(1 326)	(1 326)
Other	25 419	39 487	(14 068)	(14 068)
Total	210 953	236 942	(25 989)	(25 989)

Provision under deferred income tax

(in thousand PLN)

Difference between the balance sheet value and the tax value of fixed assets	487 308	436 426	50 882	50 882
Receivables under PPAs	11 078	16 787	(5 709)	(5 709)
Energy certificates	352	2 615	(2 263)	(2 263)
Interest and exchange rate differences	456	2 531	(2 075)	(2 075)
Valuation of non-terminated construction agreements	1 851	2 247	(396)	(396)
Accrued receivables under contractual penalty fees	-	-	-	-
Mining asset	-	-	-	-
Purchased CO_2 allowances	50 145	73 632	(23 487)	(23 487)
Other	(24)	65	(89)	(89)
Total	551 166	534 303	16 863	16 863
After offsetting the balances at the level of the Group companies, the deferred tax is presented as:				
Asset	**92 687**	**90 998**		
Provision	**432 900**	**388 359**		
The total load of deferred tax:				
– in correspondence with the total income			448	448
– in correspondence with the financial result			6 777	6 777

The item other deferred tax asset on main items as at December 31, 2017 consists of the valuation of preferential loans in Pątnów II Power Plant sp. o.o. in the amount of PLN 8 076 thousand (as at 31 December 2016, the amount of PLN 8 352 thousand), PLN 12 948 thousand is a provision for the redemption of CO2 emission rights in Elektrownia Pątnów II sp. z o.o. (as at 31 December 2016, PLN 11 954 thousand).

The status of tax settlements of the Group companies in respect of tax losses as at 31 December 2017, including deferred tax, is presented below.

As at 31 December 2017 Elektrownia Pątnów II sp. Z o.o. showed a tax loss of PLN 78 639 thousand. The accumulated value of tax losses as at December 31, 2017 amounted to PLN 87 548 thousand. The company created a tax asset on the value of accumulated tax losses, assuming that these losses will be fully settled with tax revenues of future periods. The value of the tax asset created as at 31 December 2017 amounts to PLN 16 634 thousand.

As at 31 December 2016 Elektrownia Pątnów II sp. Z o.o. showed a tax loss of PLN 9 312 thousand. Since the tax loss for 2016, the company has created an asset for deferred tax. Following the findings of the tax audit for 2016 in the area of corporate income tax, the Company adjusted the amount of tax loss for 2016 to PLN 8 910 thousand.

Tax losses, in accordance with the tax regulations in force in Poland, may be deducted from future taxable income generated by the company in successive five tax years, however, the amount of reduction in any of these years may not exceed 50% of the loss amount. As at December 31, 2016, the legal right to deduct 50% of unsettled tax loss for 2011 in the amount of PLN 88 517 thousand was barred. The company included the accounting effects of the limitation of the entire tax loss for 2011 by making write-downs of the tax asset in the financial results for 2013 and 2015. Therefore, the final limitation of the tax loss for 2011 had no effect on the financial result of 2016.

On April 24, 2017, the company received an individual interpretation of tax law provisions regarding the recognition over time of tax deductible expenses, expenses due to the return of Zarządca Rozliczeń SA of funds to cover stranded costs. This interpretation recognizes that the company's position regarding the settlement of the above-mentioned costs is incorrect. In the current tax returns for the years 2014 - 2017, the company assumed that the repayment of stranded costs from the company to Zarządca Rozliczeń SA, whose legitimacy results from the LTC Act, constitute tax deductible costs when these payments are made. On the other hand, the tax authorities consider that these costs are recognized as tax deductible costs on the day they are incurred, i.e. posted in the accounts. In the light of receiving an individual tax interpretation, taking into account unsettled tax losses, the Management Board of the Company assessed that there is no risk of tax arrears on this account. The company appealed against the individual interpretation received. On July 7, 2017, Elektrownia Pątnów II Sp. z o.o. submitted to the Provincial Administrative Court in Poznań (via the Director of the National Tax Information Service) a complaint against the abovementioned individual interpretation of tax law. On January 18, 2018, the Provincial Administrative Court in Poznań, in response to a complaint filed by the Pątnów II Power Plant, issued a verdict abrogating the contested Interpretations of the Director of the National Tax Information dated 20 April 2017. A description of court cases can be found in note 34.1

As at December 31, 2017, PAK KWB Konin SA settled all tax losses for the years 2012-2015 in the amount of PLN 22 327 thousand. As at 31 December 2017, the deferred tax asset is PLN 54 806 thousand, it does not include tax losses.

As at December 31, 2017, PAK KWB Adamów SA reported a taxable income of PLN 782 thousand. Deferred income tax asset is PLN 8 346 thousand. In 2017, there was a decrease in the deferred tax asset resulting from the assessment of the possibility of its settlement resulting from the update of the financial projections. The above was charged to the net financial result, reducing it by PLN 19 385 thousand.

As at 31 December 2016, ZE PAK SA disclosed an asset due to unsettled tax losses for 2013-2014 in the amount of PLN 4 638 thousand and an asset due to tax loss for 2016 in the amount of PLN 25 346 thousand. As at December 31, 2017, the Company achieved taxable profits, thanks to which it was able to account for and present in the financial statements the use of all assets for 2013-2014 and 50% of 2016 assets in the amount of PLN 12 673 thousand.

16. Social services fund assets and liabilities of the Company Social Benefits Fund (MFŚS)

The Act of 4 March 1994 (as amended) on the Company Social Benefits Fund as amended, states that the Social Insurance Fund is formed by employers employing more than 50 full-time employees. The Group forms such a fund and makes periodical write-offs based on the amounts agreed with trade unions. In addition, the Group’s companies contribute some social assets to the Fund. The aim of the Fund is to finance social activities, loans granted to the Group’s employees and other social costs.

(in thousand PLN)

The subsidiaries, PAK KWB Konin SA, PAK KWB Adamów SA, El PAK Serwis Sp. Z o.o – in liquidation, EKO-Surowce SP. z o.o – in liquidation, Energoinwest-Serwis sp. z o.o. – in liquidation, Aquakon Sp. z o.o. – in liquidation, PAK-Volt SA, do not belong to the Intercompany Social Benefits Fund.

The Group compensated the assets of the Fund with their obligations to the Fund because these assets do not constitute separate assets of the Group. According to the above fact, the net balance as of 31 December 2017 is zloty 5 617 thousand (as of 31 December 2016 – zloty 6 983 thousand respectively).

The below tables present the analytics of assets, liabilities, and costs of the Fund.

	31 December 2017	*31 December 2016*
Loans granted to the employees	4 921	4 221
Cash	7 355	10 612
Liabilities due to the Fund	(6 659)	(7 850)
Balance after compensation	5 617	6 983

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Write-offs for the Fund in the financial period	6 167	9 530

17. Profit per one share

Basic profit per one share is calculated with division of net profit/loss for the period of the parent company's ordinary shareholders by weighted average of number of issued ordinary shares occurring during the period.

Diluted profit per one share is calculated with division of net profit for the period of the parent company's ordinary shareholders by weighted average of number of issued ordinary shares occurring during the period corrected by weighted average of ordinary shares, which would be issued by converting all diluting potential equity instruments into ordinary shares.

Data concerning profit and shares that served to calculated basic and diluted profit per one share were presented below:

	31 December 2017	*31 December 2016*
Net profit / (loss) on continued activities of the parent company’s shareholders	183 243	247 674
Profit / (loss) on abandoned activities of the parent company’s shareholders	-	-
Net profit / (loss) of ordinary shareholders used for calculation of diluted profit / (loss) per one share	183 243	247 674
The average weighted number of ordinary shares used for calculation of basic and diluted profit / (loss) per one share	50 823 547	50 823 547

(in thousand PLN)

The below table shows the profit per one share in Polish zlotys for the year ended 31 December 2017 and 31 December 2016 presented in the profit and loss account.

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Basic and diluted from profit for the financial year attributable to the shareholders of the parent company	3,61	4,87
Basic and diluted from profit from continuing operations attributable to the shareholders of the parent company	3,61	4,87

In the period between the balance sheet day and the day of development of this financial statement, there were no other transactions concerning ordinary shares or potential ordinary shares.

18. Dividends – paid and proposed for payment

The dividend from ordinary shares for 2016, paid on August 16, 2017, amounted to PLN 65 562 thousand.

The value of the dividend per one share paid for 2016 was PLN 1.29.

Due to the loss incurred in 2015, in 2016 no dividend for 2015 was paid.

Until the publication of these consolidated financial statements, the Management Board did not present any proposals for the distribution of the financial result for 2017.

(in thousand PLN)

19. Tangible fixed assets

12 months period ended 31 December 2017

	Land and perpetual usufruct	*Buildings and constructions*	*Plant and machinery*	*Motor vehicles*	*Other*	*Assets under construction*	*Total*
Gross value as at 1 January 2017	235 209	2 014 362	4 862 243	69 615	29 082	243 951	7 454 462
Direct purchase	2 720	2 348	5 926	700	1 158	89 720	102 572
Repairs	-	-	68 504	20	(56)	(63 973)	4 495
Transfer from fixed assets under construction	26 749	6 646	12 373	738	527	(47 033)	-
Sale and liquidation	(608)	(7 310)	(7 088)	(1 633)	(970)	(11)	(17 620)
Gross value as at 31 December 2017	264 070	2 016 046	4 941 958	69 440	29 741	222 654	7 543 909
Depreciation and impairment write-downs as at 1 January 2017	7 932	1 128 103	2 763 323	38 921	20 766	104 171	4 063 216
Depreciation write-down for the period	3 133	45 343	132 975	6 478	1 727	-	189 656
Impairment write-down	-	1 441	106	17	(124)	20 725	22 165
Sale and liquidation	-	(5 538)	(4 085)	(1 375)	(965)	-	(11 963)
Depreciation and impairment write-downs as at 31 December 2017	11 065	1 169 349	2 892 319	44 041	21 404	124 896	4 263 074
Net value as at 1 January 2017	227 277	886 259	2 098 920	30 694	8 316	139 780	3 391 246
Net value as at 31 December 2017	253 005	846 697	2 049 639	25 399	8 337	97 758	3 280 835

* *this item also includes land exploited for extraction of minerals using the opencast method*

(in thousand PLN)

12 months period ended 31 December 2016

	Land and perpetual usufruct	*Buildings and constructions*	*Plant and machinery*	*Motor vehicles*	*Other*	*Assets under construction*	*Total*
Gross value as at 1 January 2016	224 845	1 927 606	3 968 357	70 298	28 563	1 119 880	7 339 549
Direct purchase	47	25	1 532	332	703	60 920	63 559
Repairs	-	-	3 155	-	-	58 213	61 368
Transfer from fixed assets under construction	11 750	88 537	894 553	-	205	(995 045)	-
Sale and liquidation	(1 433)	(1 806)	(5 354)	(1 015)	(389)	(17)	(10 014)
Gross value as at 31 December 2016	235 209	2 014 362	4 862 243	69 615	29 082	243 951	7 454 462
Depreciation and impairment write-downs as at 1 January 2016	5 431	1 024 186	1 994 014	30 556	19 012	791 121	3 864 320
Depreciation write-down for the period	2 508	53 378	138 718	9 269	2 134	-	206 007
Impairment write-down (change of state)	-	51 530	634 082	-	-	(686 950)	(1 338)
Sale and liquidation	(7)	(991)	(3 491)	(904)	(380)	-	(5 773)
Depreciation and impairment write-downs as at 31 December 2016	7 932	1 128 103	2 763 323	38 921	20 766	104 171	4 063 216
Net value as at 1 January 2016	219 414	903 420	1 974 343	39 742	9 551	328 759	3 475 229
Net value as at 31 December 2016	227 277	886 259	2 098 920	30 694	8 316	139 780	3 391 246

** this item also includes land exploited for extraction of minerals using the opencast method*

As of 31 December 2017, the balance sheet value of fixed assets, under financial lease agreements amounts to 4 195 thousand (as of 31 December 2016 – zloty 61 365 thousand).

Land and buildings of the balance sheet value of PLN 354 237 thousand (as of 31 December 2016 – PLN 368 122 thousand) are covered by a mortgage established to secure bank credits of the Group (note 36).

The value of capitalised external financing costs for the year concluded on 31 December 2017 amounted to PLN 2 961 thousand (in the year ended 31 December 2016 – PLN 3 211 thousand).

19.1. The value impairment test of assets of ZE PAK SA Capital Group

In accordance with IAS 36, at the end of every reporting period, the Group's Management Board evaluates whether there are any prerequisites indicating that there may have occurred loss in value of the component of fixed assets. In case of statement that there are such prerequisites, the Group estimates recoverable number of assets' components. Due to the above, the Group always analyses: prerequisites that may affect loss in value of any of assets' components, as well as determining cash generating units (CGU) within the Group's companies.

As mentioned in note 5.2., the main prerequisite to analyse the value impairment of the components identified by the Management Board is the steady lower market value of the Group's net assets than their balance sheet value. Additional prerequisites, which the Management Board took into account when assessing the need for the test, were the prerequisites resulting from market conditions in the environment, in which the companies in the Group run activities, out of which the most important are:

- Regulations introduced by the Power Market Act of December 8, 2017, which entered into force on January 18, 2018;
- The price of certificates of origin of energy generated in renewable sources ("green certificates") maintained on a relatively low level due to oversupply of renewable energy property rights;
- increasing fluctuations of the CO_2 emission allowances' prices (caused by the aggravating climate policy of the European Union)

The above-mentioned prerequisites were analysed in relation to all centres generating independent cash flows:

According to IAS 36: "A cash-generating unit is the smallest identifiable group of assets that generates cash inflows, which are largely independent of the cash inflows from other assets or groups of assets. If there is any indication that an asset may be impaired, a recoverable amount shall be estimated for the individual asset. If it is not possible to estimate the recoverable amount of the individual asset, an entity shall determine the recoverable amount of the cash-generating unit to which the asset belongs (the asset's cash-generating unit)."

In distinguishing CGU within the companies of the Group, the independence of generating cash flows in terms of the functioning of the individual companies was analysed.

The parent company of the Group that is ZE PAK SA, apart from the manufacturing operations, within which it is responsible for ensuring a certain level of efficiency of the generating units and implementations of production schedules, is focused on the significant operational and financial functions at the Group level as well.

Elektrownia Pątnów II sp. z o.o. – the second electricity producer in the Group, pursuant to the Act on termination of long-term agreements, is involved in the programme of coverage of stranded costs by the end of 2025.

The final settlement of this programme is planned in 2026.

The lignite coal mines, PAK KWB Konin SA and PAK KWB Adamów SA, conduct the business at several open pits.

In these companies, as profit generating units, smaller groups of assets that generate independent cash inflows were not, however, distinguished because of the many reasons, inflows generated by particular groups of assets are very closely connected with each other. As a result, the mine is expected to provide the power plant with a certain amount of coal; it is irrelevant, from which open pit it will come from. As a result, coal is supplied to the power plant from several open pits interchangeably. The organisational structure and registration systems are subordinated to such an established production target.

The above arguments determined distinguishing the following units generating independent cash flows within the ZE PAK SA Capital Group:

- ZE PAK SA
- Elektrownia Pątnów II sp. z o.o.
- PAK KWB Konin SA
- PAK KWB Adamów SA

Moreover, the remaining CGUs were distinguished within the following segments: Repairs, Sales, and Others.

Conducting the value impairment test of fixed assets, the Group based on the financial model for 2018-2047 reflecting strategic priorities of the parent company – ZE PAK SA

In ZE PAK SA, one centre generating economic benefits has been established, in which the following generation assets operate: Pątnów I power plant, Konin power plant -collector, Konin power plant – biomass unit and Adamów power plant – which ended its operation on 1 January 2018.

For each of the above units, it is possible to determine the economic benefits generated, however, these influences are to a certain degree dependent on each other, and therefore they should be considered together as one centre.

The following assumptions were adopted to estimate the use value of tangible fixed assets:

- Electricity prices have been adopted on the basis of developed forecasts divided into BASE, PEAK and OFFPEAK prepared for ZE PAK SA by an independent external advisor. For the nearest forecast period, prices resulting from concluded contracts were accepted,
- production assumptions result from the adopted investment and renovation program of ZE PAK SA,
- the Company assumed the use of the free CO_2 emission allowances in the amount resulting from Article 10a of Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003,
- the costs of lignite coal purchased for generation were specified on the basis of the delivery schedule and the prices agreed with the appropriate schedules in financial projections of the subsidiaries,
- the effects of restructuring costs for the withdrawal of old capacities in Konin Power Plant and Adamów Power Plant were taken into account,
- the effects of restructuring costs for the withdrawal of the old units in the Konin and Adamów Power Plants were taken into account,
- revenues from the capacity market were accepted from 2021; the assumed rates have been estimated by the Group's internal services based on available forecasts of the amount of support for the energy sector,
- the forecast of the margin on the biomass block was estimated assuming that the support mechanism will be the auctions,
- the weighted average cost of capital after tax (WACC) was assumed during the projection period at 8.25%.

The test was performed as at December 31, 2017.

Based on the conducted tests, it was not necessary to recognize impairment losses on property, plant and equipment.

In case of Elektrownia Pątnów II sp. z o.o. due to the participation of this unit in the Stranded Capital Completion Scheme (LTC) and the estimate of such receipts, no impairment of property, plant and equipment was found. Based on available and prospective coal resources, in particular Ościsłowo and Dęby Szlacheckie deposits, the planned operation time of the plant covers the period up to 2047.

Like in relation to the other CGUs operating within the segments of Repairs, Sales and Other, indications of a possible value impairment of assets were not identified as well.

The basis of tests for both brown coal mines is long-term financial projections including periods of operation of both mines and their particular open pits, which were agreed with assumptions accepted in the ZE PAK SA's model. Adjusting the financial projections of mines to periods of operation of the generating units results from the assumption that the only recipients of the products are the companies of the Capital Group.

The financial projections for PAK KWB Konin SA and PAK KWB Adamów SA were built taking into account the following parameters:

(in thousand PLN)

- the volume of production (extraction of coal) and revenue were determined on the basis of forecasts of the main recipient of coal that is ZE PAK SA and Elektrownia Pątnów II sp. z o.o. and the projected price curve of coal, based on an agreement on the financing of open pits,
- stripping and extraction of coal were developed according to the schedule of utilisation of current and predicted open pits, including Ościsłowo till 2036
- the level of investment expenses enabling to build new open pit ensuring supplying the power plants and maintaining specified production capacities during their operation was accepted,
- the effects of employment restructuring processes were taken into account,
- costs of the following events were included:
    - costs of reclamation of open pits
    - pension provisions
    - costs of compensations due to the group dismissals
    - revenues from sale of the asset after the end of open pit utilisation.
- weighted average cost of capital after taxation (WACC) in the projection period for PAK KWB Adamów SA at 8.03% and for PAK KWB Konin SA at the level of 8.25% was adopted; the higher discount rate reflects the higher risk associated with the operation of PAK KWB Konin SA in the long term (longer perspective of the forecast), in particular in relation to investment activities related to the development of new brown coal deposits.

Based on the conducted tests, it was found that there is no need to recognize revaluation allowances for property, plant and equipment for CGU PAK KWB Adamów SA and for CGU PAK KWB Konin SA.

Based on the results of the tests, it was also not necessary to include additional revaluation allowances for CGU ZE PAK SA assets. On the basis of the conducted analysis and test results, there was also no increase in the estimated usable potential of fixed assets for CGU ZE PAK SA, so there was also no reversal of previously recognized impairment losses in the amount of PLN 1 880 000 thousand.

Sensitivity analysis

Changes of financial parameters underlying the evaluation of the recoverable amount would change the present value of the discounted cash flow with the amounts presented below.

The results of the sensitivity analysis showed that a significant impact on the value in use of the tested assets is the issue of taking into account the power market. In the pessimistic scenario, if the market power for MW was included at the level of 50% assumed for testing, while the remaining assumptions remain unchanged, the amount of additional net write-off would be PLN 129.5 million.

Zespół Elektrowni Pątnów-Adamów-Konin SA	*(+) increase by 1.0 percentage points*	*(-) decrease by 1.0 percentage points*
Weighted average cost of capital	(PLN 43 m)	PLN 46 m
	(+) increase by 1%	(-) decrease by 1%.
Change in sales revenues (electricity price)	PLN 54 m	(PLN 54 m)
	(+) increase by 5%	(-) decrease by 5%.
Change in cost of sales (price of 1 EUA)	(PLN 57 m)	PLN 57 m
	(+) increase by 10%	(-) decrease by 10%
change in the market power rate for 1MW	PLN 68 m	(PLN 68 m)

PAK KWB Konin SA	(+) increase by 1,0 p.p.	(-) decrease by 1,0 p.p.
Weighted average cost of capital	(PLN 76 m)	PLN 88 m

(in thousand PLN)

	(+) increase by 1%	(-) decrease by 1%
Change in sales revenues	PLN 44.5 m	(PLN -44.5 m)

In the case of a decrease in revenues from sales by 1.43 % in a perspective of the forecast as the other parameters of the recoverable value determination remain unchanged and in case of increase of the weighted average cost of capital by 0.82 percentage points, while the other model parameters are unchanged, the recoverable value of the CGU would be equal to the balance sheet value.

PAK KWB Adamów SA	(+) increase by 1,0 p.p.	(-) decrease by 1,0 p.p.
Weighted average cost of capital	PLN 3 m	(PLN 3 m)
	(+) increase by 1%	(-) decrease by 1%
Change in sales revenue	PLN 2 m	(PLN 2 m)

In the case of a decrease in revenues from sales by 8.7% in a perspective of the forecast as the other parameters of the recoverable value determination remain unchanged, and in case of a decrease of the weighted average cost of capital by 5.0 percentage points, while the other model parameters are unchanged, the recoverable value of the CGU would be equal to the balance sheet value.

20. Lease

20.1. Liabilities under financial lease agreements and lease agreement with purchase option

Fixed assets used on the basis of financial lease agreements include mostly cars, tracked dozers and loaders, tractors, and trailers.

As of 31 December 2017, and 31 December 2016, future minimal lease payments due to financial lease agreements and lease agreements with purchase option, as well as current value of minimal net lease payments are as follows:

	As at 31 December 2017		*As at 31 December 2016*	
	minimum payments	*present value of payments*	*minimum payments*	*present value of payments*
Up to 1 year	1 768	1 636	7 572	7 189
1 to 5 years	2 962	2 606	4 249	3 962
Over 5 years	-	-	-	-
Total minimal lease payments	4 730	4 242	11 821	11 151
Minus finance expenses	(488)	-	(670)	-
resent value of minimal lease payments, including:	4 242	4 242	11 151	11 151
Short-term	1 636	1 636	7 171	7 189
Long-term	2 606	2 606	3 980	3 962

(in thousand PLN)

21. Intangible assets

Long-term intangible assets – 12 months period ended 31 December 2017

	CO_2 Emission units (EUA)	*Patents and licenses*	*Computer software*	*Other*	*Total*
Gross value as of 1 January 2016	114 503	21 540	1 998	431	138 472
Transfer EUA	(114 503)				(114 503)
Increases	-	(440)	(42)	(4)	(486)
Decreases	2 266	786	25	1	3 078
Gross value as of 31 December 2016	2 266	21 886	1 981	428	26 561
Depreciation and impairment write-downs as at 1 January 2016	-	16 943	1 903	344	19 190
Depreciation write-down for the period	-	1 058	99	23	1 180
Impairment write-down	-	-	-	-	-
Decreases	-	(440)	(44)	(4)	(488)
Depreciation and impairment write-downs as at 31 December 2016	-	17 561	1 958	363	19 882
Net value as at 1 January 2016	114 503	4 597	95	87	119 282
Net value as at 31 December 2016	2 266	4 325	23	65	6 679

In the EUA Transfer, the Group presents transfer of CO_2 allowances between long-term and short-term intangible assets.

(in thousand PLN)

Long-term intangible assets – 12 months period ended 31 December 2016

	CO_2 Emission units (EUA)	*Patents and licenses*	*Computer software*	*Other*	*Total*
Gross value as of 1 January 2016	12 054	19 558	1 949	395	33 956
Transfer EUA	(14 671)	-	-	-	(14 671)
Increases	-	-	(26)	-	(26)
Decreases	117 120	1 982	75	36	119 213
Gross value as of 31 December 2016	114 503	21 540	1 998	431	138 472
Depreciation and impairment write-downs as at 1 January 2016	-	14 525	1 719	323	16 567
Depreciation write-down for the period	-	1 080	207	21	1 308
Impairment write-down	-	1 338	-	-	1 338
Decreases	-	-	(23)	-	(23)
Depreciation and impairment write-downs as at 31 December 2016	-	16 943	1 903	344	19 190
Net value as at 1 January 2016	12 054	5 033	230	72	17 389
Net value as at 31 December 2016	114 503	4 597	95	87	119 282

In the EUA Transfer, the Group presents transfer of CO2 allowances between long-term and short-term intangible assets.

(in thousand PLN)

Short-term intangible assets

	31 December 2017	*31 December 2016*
	CO2 emission units (EUA)	*CO2 emission units (EUA)*
Gross value as of 1 January	273 036	354 389
Purchase of EUA	187 220	258 365
Redemption of EUA	(313 105)	(354 389)
Transfer of EUA	114 503	14 671
Gross value as of 31 December	261 654	273 036
Redemption and impairment as of 1 January	-	-
Impairment write-down of a period	-	-
Depreciation and impairment write-down as of 30 December	-	-
Net value as of 1 January	273 036	354 389
Net value as of 31 December	261 654	273 036

22. Assets for overburden removal and other mining assets

As of 31 December 2017, the item of assets concerning overburden stripping and other mining assets includes the assets related to overburden stripping and other mining assets in PAK KWB Konin in the amount of PLN 72 536 thousand.

	31 December 2017	*31 December 2016*
As of 1 January	80 524	94 057
Increases	824	1 306
Decreases	-	(455)
Depreciation for the period	(8 812)	(14 384)
As of December	72 536	80 524
long-term	72 536	80 524
short-term	-	-

(in thousand PLN)

23. Other assets

23.1. Other financial assets

	31 December 2017	*31 December 2016*
Deposits for debt service security	35 616	76 484
Investments and deposits	14	2 540
Investments and FLZG* deposits	8 365	7 810
Shares	313	167
Other	1 791	2 261
Total other financial assets	46 099	89 262
short-term	35 788	77 317
long-term	10 311	11 945

**MLF – Mining Liquidation Fund*

The main components of the "Other" item are guarantee deposits in the amount of PLN 640 thousand and loans granted to employees in the amount of PLN 277 thousand.

23.2. Other non-financial assets

	31 December 2017	*31 December 2016*
VAT receivables	6 402	22 184
Insurance	1 527	1 561
Other receivables from the state budget	-	-
Other non-financial assets	-	98
Other accruals	2 756	3 359
Delivery prepayments	115	905
Prepayments for intangible assets	-	187
Prepayments for assets under construction	2 451	5 880
Prepayments for tangible assets – land	-	-
Other	296	328
Total other non-financial assets:	13 547	34 502
short-term	11 425	28 776
long-term	2 122	5 726

The largest components of the item "other accruals in 2017" are settlements regarding license fees in the amount of PLN 748 thousand.

(in thousand PLN)

24. Employee benefits

24.1. Pension benefits and other post-employment benefits

The Group's entities pay the retiring employees amounts of one-time retirement benefits and other post-employment benefits in the amount specified by the Collective Labour Agreement. In relation to this, the Group, on the basis on the evaluation made by a professional pension actuary company, creates a provision for the current value of the liability due to one-time retirement and other benefits.

The amount of the provision and the agreement of changes in provisions during the accounting period are presented in the following table:

	Provision for pension, retirement, and post-mortem benefits	*Anniversary premiums*	*Subsidies to electricity/coal benefits*	*Total*
as of 1 January 2017	**28 292**	**3 086**	**23 712**	**55 090**
Current service cost	1 144	265	-	1 409
Interest costs	736	108	830	1 674
Actuarial profits and losses	1 699	(67)	736	2 368
Paid benefits	(2 689)	(680)	(2 835)	(6 204)
Past service cost	4 326	(177)	-	4 149
Other	(4 863)	-	-	(4 863)
as of 31 December 2017	**28 645**	**2 535**	**22 443**	**53 623**
Long-term provisions	12 886	2 157	19 679	34 722
Short-term provisions	15 759	378	2 764	18 901

The main component of the "Other" item is the release of provisions related to the liquidation of Energoinwest sp. z o.o., EL PAK Serwis sp. z o.o., EKO Surowce sp. z o.o. and Aquakon sp. z o.o. The new provisions were created in the company PAK Górnictwo sp. z o.o., which took over the activities of liquidated companies.

	Provision for pension, retirement, and post-mortem benefits	*Anniversary premiums*	*Subsidies to electricity/coal benefits*	*Total*
as of 1 January 2016	**42 310**	**16 352**	**27 794**	**86 456**
Current service cost	2 103	1 543	-	3 646
Interest costs	1 020	425	723	2 168
Actuarial profits and losses	(2 535)	(299)	(1 823)	(4 657)
Paid benefits	(4 079)	(2 351)	(2 982)	(9 412)
Past service cost	(10 527)	(12 584)	-	(23 111)
Other	-	-	-	-
as of 31 December 2016	**28 292**	**3 086**	**23 712**	**55 090**
Long-term provisions	25 159	2 547	20 881	48 587
Short-term provisions	3 133	539	2 831	6 503

(in thousand PLN)

The main assumptions adopted by the actuary as of the balance sheet date for calculation of the amount of the liability are as follows:

	12 months period ended 31 December 2017	
discount rate	3.3%	3.5%
expected inflation rate	2.5%	2.5%
expected remuneration growth rate	depending on the company in rage from 0 % to 3 %	depending on the company in rage from 0 % to 3 %

25. Inventories

	31 December 2017	*31 December 2016*
Production fuel	7 564	9 161
Spare parts and other materials	79 001	74 608
Certificates of origin of energy	11 119	21 406
Goods	74	121
Inventory total according to the lower of two values: acquisition price (costs of production) and the net value possible to acquire	97 758	105 296

Certificates of origin of energy due to the energy production from renewable energy sources, gas sources, and peak load co-generation are presented according to fair value at the end of the month, in which they were produced.

According to the records, as at 31 December 2017, the Group held, in total, 36 836.654 MWh of green certificates including 4 014.442 MWh of green energy for production in June 2017, produced and not yet verified by URE.

In the fourth quarter of 2017, the Group did not receive any certificates. During this period, no property rights resulting from certificates of origin of electricity from renewable energy sources were sold. During the current reporting period, the Group stopped production from renewable sources because of too low prices of market rights.

26. Trade and other receivables

	31 December 2017	*31 December 2016*
Trade receivables	151 814	126 793
Receivables due to compensation related to the termination of the PPAs	58 303	88 350
Receivables due to security of purchase of electricity in the balancing market	7 695	8 674
Other receivables	35 449	22 208
Net receivables	253 261	246 025
Impairment write-down on receivables	41 522	41 947
Gross receivables	294 783	287 972

In the ‘other receivables’ item, as of 31 December 2017, the Group presents mainly receivables due to the security deposit in the amount of PLN 25 676 thousand.

(in thousand PLN)

Terms of transactions with affiliates are presented in the note 37.

Receivables due to supplies and services are not subject to interest and the date of payment is usually within the 14-day period.

The Group has appropriate policy concerning the sale to the verified clients only. Thanks to that, according to the management, there is no additional credit risk exceeding the level specified by non-collectible receivables impairment write-downs, specific to the Group's trade receivables.

As of 31 December 2017, receivables due to supplies and services and other receivables in the amount of PLN 41 522 thousand (as of 31 December 2016: PLN 41 947 thousand) were included in the write-off. Changes in the impairment write-downs on receivables were as follows:

	31 December 2017	*31 December 2016*
Impairment write-down as at 1 January	41 947	41 840
Increase	56	568
Use	(2)	(315)
Redemption	(479)	(146)
Impairment write-down as at 31 December	41 522	41 947

Below is an analysis of trade receivables and other receivables which as at 31 December 2017 and as at 31 December 2016 were past due, but were not considered as irrecoverable and were not written off.

			Expired but recoverable				
	Total without write-down	*Unexpired*	<30 days	30-60 days	60-90 days	90-120 days	>120 days
31 December 2017	253 261	248 044	3 521	410	547	28	711
31 December 2016	246 025	217 297	10 135	6 929	5 246	2 507	3 911

27. Cash and cash equivalents

Cash at bank are subject to interest at volatile interest rates, whose amount depends on the interest rate on one-day bank deposits. Short-term deposits are established for various periods; from one day to three months, depending on current Group's demand for cash and are subject to interest at fixed interest rates. The fair value of cash and cash equivalents as of 31 December 2017 amounts to PLN 322 201 thousand (as of 31 December 2016: PLN 350 101 thousand).

The balance of cash and cash equivalents in the consolidated cash flow statement consisted of the following items:

Cash structure

	31 December 2017	*31 December 2016*
Cash in hand and at bank:	229 387	229 498
Short-term deposits	92 814	120 603

(in thousand PLN)

Total cash and cash equivalents in the balance sheet	322 201	350 101
Foreign exchange differences	369	(1 454)
Total cash and cash equivalents in cash flow statement	322 570	348 647

Explanation of changes in balance sheet items and changes to items recognized in the statement of cash flows

	31 December 2017	*31 December 2016*
Depreciation:		
Depreciation shown in the income statement	199 648	221 699
Settlement of subsidies	(1 502)	(2 877)
Depreciation shown in the cash flow statement	(2 454)	(10 993)
depreciation shown in cash flow statement	195 692	207 829

The settlement of sale-and-lease-back concerns an excess due to sale of assets components and lease them back in PAK KWB Konin. The amount of PLN 2 454 thousand adjusted for depreciation (in 2016, the amount of PLN 10 993 thousand).

	31 December 2017	*31 December 2016*
Receivables:		
Balance sheet change in trade receivables and other receivables	(7 236)	22 098
Balance sheet change in other long and short-term non-financial assets	19 916	(11 978)
Balance sheet change in amounts due from clients under PPAs	1 089	(4 819)
Change in advances for fixed assets under construction	(3 429)	(1 637)
Other changes	1 361	(541)
Change in receivables shown in the cash flow statement	11 701	3 123

	31 December 2017	*31 December 2016*
Liabilities:		
Balance sheet change in trade liabilities and other financial liabilities, long and short-term	(156 170)	(10 524)
Balance sheet change in other non-financial liabilities	(9 044)	(6 123)
Balance sheet change in amounts paid to clients under PPAs	1 635	(6 090)

(in thousand PLN)

Change in liabilities under investment settlements	(2 992)	57 179
Purchase of debt securities	-	5 030
New lease agreements and payment of lease liabilities	6 750	15 192
Change in liabilities under purchase of allowances of emission CO_2	59 951	(59 951)
Other changes	790	170
Change in liabilities shown in the cash flow statement	(99 080)	(5 117)

	31 December 2017	*31 December 2016*
Change in provisions, prepayments and accruals and employee benefits:		
Change in provisions and prepayments	20 137	(87 883)
Change in long and short-term employee benefits	(1 459)	(31 367)
Decrease of provision from redemption EUA	313 105	354 389
Change in actuarial provisions indicated in other comprehensive income	(2 155)	4 613
Other changes	(829)	(566)
Change in provisions, prepayments and accruals and employee benefits	328 799	239 186

In the item of expenditures and receipts associated with other financial assets in consolidated financial statement there were presented inflows and outflows of the cash earmarked for debt service and received guarantees.

28. Share capital and other capitals

28.1. Share capital

Share capital	*31 December 2017*	*31 December 2016*
50 823 547 shares with a nominal value of PLN 2 each	101 647	101 647

28.1.1. Share nominal value

All the issued shares have a nominal value of zloty 2 each and were paid up.

28.1.2. Shareholders rights

The shares of all series are equally preferred in terms of dividend and return on the capital.

28.1.3. Shareholders with significant share

	31 December 2017	*31 December 2016*
Elektrim SA		
share in capital	0.39%	0.39%
share in voting right	0.39%	0.39%
*Embud II sp. z o.o.**		

share in capital	1.16%	1.16%
share in voting right	1.16%	1.16%
Trigon XIX Fundusz Inwestycyjny Zamknięty		
share in capital	19.68%	19.68%
share in voting right	19.68%	19.68%
Argumenol Investment Company Limited		
share in capital	30.32%	30.32%
share in voting right	30.32%	30.32%
Nationale - Nederlanden OFE		
share in capital	9.97%	9.97%
share in voting right	9.97%	9.97%
Towarzystwo Funduszy Inwestycyjnych PZU SA		
share in capital	6.06%	6.06%
share in voting right	6.06%	6.06%
OFE PZU Złota Jesień		
share in capital	5.24%	5.24%
share in voting right	5.24%	5.24%
Others		
share in capital	27.18%	27.18%
share in voting right	27.18%	27.18%
	100.00%	100.00%

**- in 2016 the company acted under the name Embud sp. z o.o.*

According to the Company's knowledge on the basis of notifications submitted by the shareholders

29. Supplementary capital

As of 31 December 2017, the structure of the supplementary capital origin in the amount of zloty 1 094 493 thousand is as follows:

• from the sale of shares above their nominal value	380 030
• created in accordance with the articles of association above the statutory (minimum) value	587 748
• other, including:	126 715
- Takeover of PAK Odsiarczanie sp. z o.o.	65 922
- Liquidation of fixed assets	60 793

29.1. Other reserve capital

The ZE PAK SA Company was founded as a result of the commercialisation of the Zespół Elektrowni PAK State-owned Company made pursuant to the Act of 13 July 1990 on the privatisation of state-owned companies. The so-called Privatisation Fund, shown as part of the reserve capital in the balance sheet of the company, was created by the Zespół Elektrowni PAK state-owned company on the basis of the Act of 31 January 1989 on financial economy of state-owned companies.

The value of the reserve fund consists of the Privatisation Fund in the amount of zloty 3 472 thousand, which was created from the profit of 1994, on the basis of a resolution of the Extraordinary General Meeting of the newly established Company, and the values related to the redemption of own shares in the amount of zloty 2 405 thousand. Due to the negative result of ZE PAK SA for 2015 in the amount of zloty 1,515,851 thousand, the General Meeting of the Company, on 28 June 2016, adopted a resolution no. 5 on covering the Company's loss for 2015. According to the resolution, the General Meeting allocated the amount of zloty 2 405 thousand from the reserve capital. The total value of other reserve capitals, as of 31 December 2017, is zloty 3 472 thousand.

(in thousand PLN)

Cash accumulated in this fund were to be reserved for employees' purchase from the State Treasury shares after transformation of the enterprise into the company and its privatisation (purchase of up to 10% of the shares for a half price). The Act of 30 August 1996 on the commercialisation and privatisation of state-owned enterprises introduced in 1996 granted employees the right to acquire 15% of the company's shares belonging to the State Treasury free of charge. Therefore, the objectives, which the privatisation fund was to serve, do not exist. However, the capital in the company's liabilities remained.

29.2. Undivided financial result and restrictions on payment of dividend

The undivided profit also includes amounts, which are not subject to division that is they may not be paid in the form of dividend. They are:

- Retained profits/losses of subsidiaries owned by the shareholders of the parent company,
- differences in values of retained profits between the statutory statement and the IFRS statement of the parent company,
- The equivalent of 8% of the statutory write-offs from profit for the capital and other write-offs made on the basis of existing provisions in the contracts of subsidiaries.

In the Group, as of 31 December 2017, the full amount of undivided profit (including the equivalent of reserve and supplementary capitals created within the division of profits in the previous years) is subject to the restriction on payment of dividend. The following conditions are the basis of such an assumption:

- Statutory financial statements of all companies included in the ZE PAK SA Capital Group are prepared in accordance with the Polish accounting standards. The dividend may be paid on the basis of the financial result determined in a separate annual financial statement prepared for the statutory purposes.
- According to the requirements of the Code of Commercial Companies, a parent company is required to create a reserve capital for coverage of losses. At least 8% of the profit for a given financial year, recognised in a separate financial statement of the company is transferred to this category of the capital, until this capital reaches at least one third of the parent company's issued capital. The use of supplementary and reserve capitals is decided by the General Meeting. However, parts of the supplementary capital in the amount of the one-third of the initial capital can be used only to cover the loss demonstrated in the separated financial statement of the parent company and is not divided for other purposes.

As of 31 December 2017, there are no other restrictions on the payment of the dividend.

29.3. Non-controlling interest

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
At the beginning of the period		
Acquisition - defining non-controlling interest at the acquisition date	30 971	30 971
Employee share program - correction of the original settlement	(955)	(955)
The result of subsidiaries in a given year - attribution to non-controlling interests	589	2 612
Settlement PUT options - the recognition of the commitment to purchase employee shares	(30 971)	(30 971)
Settlement PUT option - recognition of the difference between the value of non-controlling interest and obligation at end of period	366	(1 657)
Total	-	-

(in thousand PLN)

Allocation of the result to the non-controlling interests

In the consolidated financial statement, 15% of the PAK KWB Adamów SA's result and 15% of the PAK KWB Konin SA's result for the period from 19 July 2012 – 31 December 2013 and from 1 January 2014 – 31 December 2014 were allocated as a profit of non-controlling shareholders. In 2015, 2016 and 2017 in connection with the ongoing employee shares redemption, the profit for non-controlling shareholders was allocated in proportion to the shares volume of non-controlling shareholders.

Recognition of ZE PAK SA's obligation to purchase the remaining shares in PAK KWB Konin SA and PAK KWB Adamów SA

In accordance with the IFRS, ZE PAK SA recognised the obligation to purchase the shares of PAK KWB Konin SA and PAK KWB Adamów SA possessed by the non-controlling interest on the day of the acquisition of control.

In the shares sale agreement of KWB Konin SA and KWB Adamów SA concluded between ZE PAK SA and the State Treasury on 28 May 2012 (hereinafter "Shares Sale Agreement"), ZE PAK SA submitted an irrevocable offer of purchasing the remaining shares of both mines to the State Treasury, under the terms set forth in this agreement, which will not be acquired from the State Treasury by the entitled employees and their legal successors on the basis of the Act of 30 August 1996 on the commercialisation and certain powers of employees. In accordance with the provisions of this act, the entitled employees of KWB Konin SA and KWB Adamów SA are entitled to acquire free of charge up to 15% of the shares of the company covered by the State Treasury on the date of entering a given company into the register. In accordance with the Shares Sale Agreement, ZE PAK SA's purchase of the remaining mines' shares from the State Treasury, not covered by the entitled employees or by their legal successors, will take place at a price per share equal to, respectively, the price of one share of KWB Konin SA and KWB Adamów SA in the transaction of sale of 85% of KWB Konin SA and KWB Adamów SA's shares of Konin to ZE PAK SA by the State Treasury, index-linked by the consumption products and services price indicator announced by the CSO President. In accordance with the Shares Sale Agreement, the offer of purchasing the remaining shares of KWB Konin SA and KWB Adamów SA are submitted by ZE PAK SA to the State Treasury, which is referred to above, was binding until 28 February 2017. The remaining shares of KWB Konin SA and KWB Adamów SA were purchased from the Treasury.

In addition, in accordance with the Shares Sale Agreement, ZE PAK SA obliged to, under the terms as provided for in this agreement, submit to the entitled employees of KWB Konin SA and KWB Adamów SA, who acquired free of charge the shares from the State Treasury on the basis of the Act of 30 August 1996 on the commercialisation and certain powers of employees, the offer to purchase these shares at a prices equal to, respectively, the price of one share of KWB Konin SA and KWB Adamów SA in the transaction of sale of 85% of KWB Konin SA and KWB Adamów SA's shares of Konin to ZE PAK SA by the State Treasury. In the implementation of this obligation, after the expiry of the prohibition on trading the employee shares specified in article 38 paragraph 3 of the Act of 30 August 1996 on the commercialisation and certain powers of employees, ZE PAK SA began the process of employee share redemption, within which ZE PAK SA offered the people, who expressed the interest in disposal of PAK KWB Konin SA and PAK KWB Adamów SA's shares, to redeem them under terms set forth in the Shares Sale Agreement. By the end of 2016, as a result of that redemption process, most employee shares of PAK KWB Konin SA and PAK KWB Adamów SA were acquired. ZE PAK SA still plans to purchase the employee shares of PAK KWB Konin SA and PAK KWB Adamów SA and continues the redemption process at the currently offered price.

As of 31 December 2017, the remaining amount on the purchase of PAK KWB Konin SA and PAK KWB Adamów SA amounted to PLN 3 755 thousand.

30. Interest-bearing loans and borrowings

Short-term	*Maturity*	*31 December2017*	*31 December 2016*
Bank loan (syndicated) in the amount EUR 240 000 thousand; interest rate at EURIBOR 3M + bank margin	20.07.2019	136 840	142 567
Overdraft facility at BZ WBK in the amount of zloty 50 000 thousand; interest rate at WIBOR 1M + bank margin	30.06.2018	23	28 670
Overdraft in Alior Bank SA in the amount of PLN 67 000 thousand, bearing interest at WIBOR 1M + bank margin	30.05.2018	59 025	63 061

(in thousand PLN)

Working capital loan in Bank Millennium SA in the amount of PLN 76 500 thousand, bearing interest at WIBOR 3M + bank margin	31.12.2017	-	28 765
Investment loan in the amount of PLN 577 000 thousand (Loan A), bearing interest at WIBOR 3M + bank margin	20.03.2020	141 662	146 260
Investment loan in the amount of PLN 90 000 thousand (Loan B), bearing interest at WIBOR 3M + bank margin	20.03.2020	12 023	12 369
Overdraft in Alior Bank SA in the amount of PLN 1000 thousand, bearing interest at WIBOR 1M + bank margin	30.05.2017	-	266
TOTAL		**349 573**	**421 958**

Long-term	*Maturity*	*31 December 2017*	*31 December 2016*
Investment loan (syndicated) in the amount of EUR 240 000 thousand, bearing interest at the EURIBOR 3M rate + bank's margin	20.07.2019	101 431	244 556
Investment loan in the amount of PLN 577 000 thousand (Loan A), bearing interest at WIBOR 3M + bank margin	20.03.2020	150 931	283 045
Investment loan in the amount of PLN 90 000 thousand (Loan B), bearing interest at WIBOR 3M + bank margin	20.03.2020	50 103	60 250
TOTAL		**302 465**	**587 851**

31. Provisions and accruals

31.1. Accruals

	31 December 2017	*31 December 2016*
Provision for bonuses and holiday leaves	28 770	29 371
Provision for employment termination costs	2 173	-
Audit of financial statements	563	570
Other	1 328	1 902
Total	32 834	31 843
short-term	32 834	31 843
long-term	-	-

The main component of the item "Other" is the provision for a penalty for exceeding the amount of dust introduced into the air in 2015 in the amount of PLN 1 190 thousand. The group appealed against this decision to the Provincial Inspectorate for Environmental Protection in Poznań. The case went to the Chief Inspector of Environmental Protection.

(in thousand PLN)

31.2. Change in provisions

	Provision for EUA redemption	*Provision for the fixed assets liquidation costs*	*Provision for the reclamation of ash storage yards*	*Provision for the long-term contract loss*	*Provision for the certificates of origin of energy redemption*	*Reclamation provisions and other provisions related to mining activities*	*Other*	*Total*
As of 1 January 2017	313 105	16 848	1 005	13	7 838	307 837	37 552	684 198
increase	289 942	747	1	397	1 616	70 385	1 023	364 111
decrease	(313 105)	(1 002)	(250)	(40)	(932)	(15 806)	(13 821)	(344 956)
As of 31 December 2017	289 942	16 593	756	370	8 522	362 416	24 754	703 353
long-term	-	16 593	540	-	-	336 292	4 477	357 902
Short-term	289 942	-	216	370	8 522	26 124	20 277	345 451
as of 1 January 2016	354 389	16 419	1 698	148	9 449	330 561	53 487	766 151
increase	313 105	429	-	86	7 838	1 676	1 500	324 634
decrease	(354 389)	-	(693)	(221)	(9 449)	(24 400)	(17 435)	(406 587)
as of 31 December 2016	313 105	16 848	1 005	13	7 838	307 837	37 552	684 198
long term	-	16 848	755	-	-	287 966	6 684	312 253
short term	313 105	-	250	13	7 838	19 871	30 868	371 945

31.3. Description of significant titles of provisions

31.3.1. The provision for liabilities due to the emission of greenhouse gases (EUA)

The Group recognises the provision for the redemption of greenhouse gases emission allowances.

Since 1 January 2013, the next reporting period of 2013 – 2020 concerning emission allowances has been applicable. This period's assumption is granting the Group the free EUA allowances resulting from the production of heat, although power engineering was additionally covered by opportunity of derogation. Derogation resulting from Article 10c of the ETS Directive is based on granting additional free allowances, provided that declared investment expenses for investments reported to the National Investment Plan are paid. The ZE PAK SA submits to the Ministry of the Environment the annual material and financial statements from investment expenses paid for tasks reported to the National Investment Plan, applying for granting free EUAs for the subsequent reporting years at the same time.

In September 2017, the Company submitted a material and financial statement to the Ministry of Environment regarding the free EUAs under article 10c for the incurred investment expenses in the period from 1 July 2016 to 30 June 2017. However, due to the uncertainty in terms of the creation of a dual-commodity market, including the power market at the moment, which will impact directly the modernisation of units number 3 and 4 in the Pątnów Power Plant, the Company did not apply for the free allowances. In connection with the above, the Group did not receive EUAs for 2017 due to art. 10c.

As at January 1, 2017, the Group had physical assets in its EUA accounts in the amount of 13 820 841 tons. In February 2017, the Group received free EUA for heat for 2017 (Article 10a of the ETS Directive) in the amount of 83,317 EUA. In addition, in the first quarter of 2017, the Group completed purchases of emission allowances under futures contracts concluded at the turn of 2015 and 2016 for the production needs of 2016. After these operations, the status of the EUAs held on the Group's accounts in the Union Register as at March 31, 2017 was 15 249 158. After the cancellation process in April 2017, the EUA units in the accounts of the Group in the Union account in the amount of 3 793 059, which will be used for the needs of 2017 cancellations. Since the beginning of 2017, the Group has been making purchases of EUA units on the SPOT market as well as on the forward market. As at December 31, 2017, 9 776 059 EUA units are physically listed on the Group's accounts. The units purchased by the Group will mostly be used for redemption 2017 and partly provide security for the needs of electricity production by the Group's power plants in 2018.

The provision of CO2 for the Group, which the Group intends to redeem for 2017, is charged to basic operating activities. Upon the actual cancellation of entitlements, the previously created reserve will be used.

31.3.2. Provision for reclamation of ash storage yards and costs of liquidation of fixed assets

The Group creates the provision for future costs of reclamation of the land on the basis of legal obligation resulting from the "Integrated Permits." The basis of estimation of the provision size are specialised studies and technical and economical expert reports developed by domestic services or external experts. The value of the provision is estimated and verified on every balance sheet date on the basis of current cost estimates and a discount. As of 31 December 2017, the created provision amounted to PLN 756 thousand.

Due to the legal obligation to liquidate fixed assets after their period of use, the Group creates the provision for projected future costs, which will be necessary to pay for fulfilment of this obligation. As of 31 December 2017, the provision due to this amounted to PLN 16 593 thousand.

31.3.3. Reclamation provisions and other provisions related to mining activities

PAK KWB Konin SA and PAK KWB Adamów SA are obliged to reclaim areas of extraction works pursuant to the Geological and Mining Law act. Due to this, the Group creates the provision both for costs of area reclamation related to current coal extraction on a given open pit and for costs of the final excavation reclamation in the state of advancement of coal extraction in particular open pits on every balance sheet day.

The provision is created on the basis of estimation of future reclamation costs based on reports of independent experts estimating reclamation costs on the order of the Management Board. Estimates concerning projected reclamation costs are analysed periodically; on every reporting date, the volume of provision is verified in accordance with current assumptions within discount rate, inflation, and the volume of extraction.

PAK KWB Konin SA and PAK KWB Adamów SA, within run activities, are obliged to restore to the original condition, or to rebuild damages caused by the mine operations. Due to this, the Group creates the provision for projected costs, to pay which it is obliged on the basis of concluded agreements. Estimates concerning the projected costs related to the mine operations are updated on every reporting date.

In 2017, PAK KWB Konin SA and PAK KWB Adamów SA commissioned an external company to prepare a study on the estimation of the costs of reclamation and management of excavations and mining exploitation areas. As a result of the update, the area, time and directions of reclamation changed, which resulted in an increase in the provision for reclamation. In PAK KWB Adamów SA this is mainly due to a change in the direction of the reclamation of these areas in relation to the original assumptions, conducting inventory of areas subject to reclamation and changes in relation to the planned exclusion of these areas from mining operations. However, in PAK KWB Konin SA, the change in the amount of reclamation reserves results mainly from changes in the surface of the final lake in Jóźwin open-pit and in Drzewce open-pit. The provision for decommissioning and reclamation of mining areas and for the preparation of operational areas at PAK KWB Konin SA and PAK KWB Adamów SA as at December 31, 2017 amounted to PLN 362 416 thousand and increased compared to the year ended December 31, 2016 by PLN 54 579 thousand. While calculating the provision, the Group adopted the following assumptions: discount rate at 3.3%, inflation level at 2.5%.

31.3.4. Provision for redemption of Energy certificates

Due to the sale of electricity to the final recipients, the Group is obliged to redeem the specified number of certificates of origin of energy from renewable energy sources, gas, and peak load co-generation. As of 31 December 2017, the provision due to this amounted to PLN 8 522 thousand.

31.3.5. Other provisions

In PAK KWB Konin, the main items of other reserves as of 31 December 2017 are: provisions for mining damage in the amount of PLN 3 547 thousand, the provisions for pending legal proceedings in the amount of PLN 530 thousand. In PAK KWB Adamów: provisions for permanent taking out of production for the final reservoir of Adamów open pit in the amount of PLN 15 828 thousand, the provision for mining damage in the amount of PLN 3 383 thousand, the provisions for legal proceedings in the amount of PLN 355 thousand.

32. CO2 emission allowances

Since 1 January 2013, the next reporting period of 2013 – 2020 concerning emission allowances has been applicable. This period's assumption is granting the Group the free EUA allowances resulting from the production of heat, although power engineering was additionally covered by opportunity of derogation. Derogation resulting from Article 10c of the ETS Directive is based on granting additional free allowances, provided that declared investment expenses for investments reported to the National Investment Plan are paid.

The Group submitted a material and financial statement to the Ministry of the Environment for the incurred investment expenses from 1 July 2016 to 30 June 2017. However, due to the uncertainty regarding the emergence of a dual-commodity energy market, including power market, which will have a direct impact on the possible modernisation of units nos. 3 and 4 in the Pątnów Power Plant, despite showing further small expenses, the Group has not applied for free allowances in view of the possible need to return them for not carrying out further modernisation of these units. Therefore, the Group did not receive EUAs for 2017 under Article 10c.For the Elektrownia Pątnów II sp. z o.o.'s system, a specified number of CO_2 emission allowances was allocated. However, for this system, any investment task that would cover receivables for CO_2 emission allowances were not reported to the National Investment Plan, so allocation of free EUA units for this system depends on expenses for tasks conducted for the systems of ZE PAK SA. In 2013-2017, ZE PAK SA did not incur significant expenses so that the part of them would meet the requirements for receiving free EUA allowances by Elektrownia Pątnów II. Currently, Elektrownia Pątnów II sp. z o.o. does not assume that it will receive any free allowances for surplus of the expenses incurred by ZE PAK SA.

In the first half of 2017, the Group received free EUA for heat for 2017 (Article 10a of the ETS Directive) in the amount of 83,317 tonnes. In addition, in the first quarter of 2017, the Group completed purchases of emission allowances as part of forward contracts concluded at the turn of 2015 and 2016 for the production needs of 2016. During 2017, the Group continued to purchase CO2 emission allowances both on the SPOT market and in futures contracts, which will mostly be used to cancel in 2017 and partly provide security for the needs of electricity production in 2018. In April 2017, the Group redeemed CO2 emissions for 2016 in the amount of 11 456 099 tons, and after purchases in the following months, the physical holding of the Group's units on accounts in the Union Registry as at

(in thousand PLN)

December 31, 2017 amounted to 9 776 059 tons, of which 7 051 715 tonnes of ZAK SA and 2 724 344 tons of Pątnów II Power Plant sp. z o. o.

Risk of return of free allowances for CO2 emissions due to discontinuation of investments in blocks 3 and 4 and a gas-steam block

Due to the suspension of investments in blocks 3 and 4 and the gas and steam block, the Management Board of the Company estimated the potential risk of returning free CO2 emission rights in the amount of approximately EUR 6.5 million with interest.

In connection with the submission to the European Commission of a revised National Investment Plan for 2013-2020, the Company asked the Minister of the Environment for the possibility of replacing suspended investment tasks with new tasks. In response, the Minister of the Environment asked for a list of tasks whose deadline for completion indicated in the plan is endangered.

On February 28, 2018, the Company filed a letter to the Minister of the Environment, in which it expressed a desire to balance the value of issued CO2 emission rights for investments related to blocks 3 and 4, the costs of planned investments to be converted. By the date of this report, the Company did not receive a response from the Minister of the Environment.

As at the date of this report, there was no risk of potential reimbursement of free CO2 allowances received related to the above investment tasks and no grounds for creating any provisions for this. The report discloses a conditional obligation regarding the return of allowances.

The following tables present the carbon dioxide emission rights granted under the National Allocation Plan, purchased on the secondary market together with the division into the part used for own needs and sold in the periods ended on December 31, 2017 and December 31, 2016.

CO2 emission allowances in the year ended 31 December 2017

(in tons)		*Zespół Elektrowni Pątnów-Adamów-Konin SA*	*„Elektrownia Pątnów II" sp. z o.o.*
	Emission of CO_2	8 260 668	2 605 436
EUA	Balance at the beginning of the period	12 900 660	920 181
	Purchased	3 496 000	3 832 000
	Free of charge	83 317	-
	Redemption*	(9 428 262)	(2 027 837)
	Sale	-	-
	Exchange	-	-
	Balance at the end of the period	7 051 715	2 724 344

** Physical redemption of the allowances for a given year takes place in the first months of the next year.*

(in thousand PLN)

CO2 emission allowances in the year ended 31 December 2016

(in tons)		*Zespół Elektrowni Pątnów-Adamów-Konin SA*	*„Elektrownia Pątnów II" sp. z o.o.*
	CO_2 emission	9 428 262	2 027 836
EUA	Balance at the beginning of the period	9 689 990	2 567 596
	Purchased	12 687 500	703 000
	Free of charge	430 676	-
	Redemption*	(9 907 506)	(2 350 415)
	Sale	-	-
	Exchange	-	-
	Balance at the end of the period	12 900 660	920 181

** Physical redemption of the allowances for a given year takes place in the first months of the next year.*

33. Trade liabilities, other liabilities and accruals

33.1. Trade liabilities and other financial liabilities (short-term)

	31 December 2017	*31 December 2016*
Trade liabilities	100 503	186 493
Liabilities due to the put option	3 755	6 061
Investment liabilities	15 530	12 814
Liabilities to employees due to salaries	14 452	15 325
other	12 176	81 969
total	146 416	302 662

In the other liabilities line as of 31 December 2017, the Group presents mainly liabilities due to financial lease in the amount of PLN 1 636 thousand (PLN 7 189 thousand in 2016). The remaining amount in the other liabilities item as of 31 December 2017 concerns mostly settlements with employees and deductions from the pay roll amounting to PLN 7104 thousand (PLN 5 315 in 2016) and settlements due to security amounting to PLN 1 111 thousand (PLN 1579 thousand in 2016).

Liabilities due to the put option concern obligation of ZE PAK SA to redeem the employee shares pursuant to the PAK KWB Konin SA and PAK KWB Adamów SA's shares sale agreement, in case when employees request for re-sale. The agreement's provisions determine the price and term of redemption. In accordance with IFSR, ZE PAK recognised the obligation to redeem shares owned by non-controlling interests on the day of the acquisition of control. In relation with the ongoing process of the employee shares redemption, as of 31 December 2017, the remaining liability amount is PLN 3 755 thousand.

Principles and terms of payment of above financial liabilities:

Terms of transactions with affiliates are presented in the note 37 of additional information and explanations.

Liabilities due to supplies and services are not subject to interest and are usually settled within either the 14-day, or 30-day period.

Liabilities due to interests are usually settled within either monthly or quarterly periods during the whole financial year.

(in thousand PLN)

33.2. Trade liabilities and other financial liabilities (long-term)

	31 December 2017	*31 December 2016*
Liability due to financial lease	2 606	3 962
Short-term liabilities to other entities – over 12 months	415	483
Other	2 125	624
Total	5 146	5 069

33.3. Other non-financial liabilities

	31 December 2017	*31 December 2016*
VAT tax liabilities	18 238	13 637
Liabilities due to environmental charges	39 115	48 650
Liabilities due to the excise tax	971	543
Liabilities due to social insurance	23 203	24 373
Personal income tax	6 273	6 200
Other budget liabilities	5 115	7 405
Advanced payments for deliveries	936	4 299
Service charge	11 060	10 771
Other	2 476	553
Total	107 387	116 431

Liabilities due to environmental charges concern charges for air pollution, waste storage, intake of water, and wastewater disposal. The year is a settlement period.

Liabilities due to mining fees concern charges for the extracted mineral resulting from the Geological and Mining Law. The half-year is a settlement period.

33.4. Derivative financial instruments

	31 December 2017	*31 December 2016*
Instruments securing floating interest rates (SWAP)	4 112	10 053
Other currency options	897	-
Total	5 009	10 053
short-term	4 139	5 759
long-term	870	4 294

(in thousand PLN)

33.5. Grants and deferred income (long-term)

	31 December 2017	*31 December 2016*
Long-term grants	41 504	43 006
Other	3 005	296
Total	44 509	43 302

The main component of the "Other" item is land obtained free of charge from the Poviat Starosty and the Commune, amounting to PLN 2 852 thousand

33.6. Grants and deferred income (short-term)

	31 December 2017	*31 December 2016*
Settlement of short-term leaseback	-	5 163
Short-term grants	1 502	1 502
Other	5	5
Total	1 507	6 670

34. Contingent liabilities and description of significant judicial cases

Apart from liabilities described in notes 34.1, 35 and 36 below, as of 31 December 2017, the Group have any other contingent liabilities, guarantees and sureties granted.

34.1. Court proceedings

Compensation for the termination of long-term contracts for sale of power and electricity in Elektrownia Pątnów II

Elektrownia Pątnów II sp. z o.o., receives compensation (advances and their annual adjustments) for the coverage of the stranded costs pursuant to the Act of 29 June 2007 on the principles of coverage of costs incurred by producers due to early termination of long-term agreements for the sale of power and electricity. Appropriately calculated advances and adjustments are recognized in basic sales revenues, with a negative adjustment equivalent to a decrease in revenue. On the basis of the decision of the President of the Energy Regulatory Office SA (“the ERO President”), issued on 31 July 2009, the company was obliged to return the compensation scheme administrator, Zarządca Rozliczeń SA, the amount of zloty 52 493 thousand, due to the negative adjustment of stranded costs for 2008. The company’s Management Board did not agree with the ERO President’s decision and appealed to the Regional Court of Warsaw – Court for Protection of Competition and Consumers (“SOKiK”).

Finally, the issue of a negative correction for 2008 was settled in the judgment of the Court of Appeal of November 4, 2014. Pursuant to this judgment and taking into account the previous settlements between Pątnów II Power Plant sp. o.o. and Zarządca Rozliczeń SA, the company had to return PLN 81.5 million to Zarządca Rozliczeń SA. The judgment of the court was included in the company's statement for the third quarter of 2014 (decrease in revenues by PLN 81.5 million).

On 15 April 2015, Elektrownia Pątnów II sp. z o.o. submitted a cassation appeal from this judgement. On February 24, 2016, the Supreme Court refused to accept the cassation complaint. The judgement of the Supreme Court ended the proceedings.

The judgement of the Court of Appeal in Warsaw of 4 November 2014 is legally binding and is subject to execution by Elektrownia Pątnów II sp. z o.o. In accordance with the arrangements made between Elektrownia Pątnów II sp. z o.o. and Zarządca Rozliczeń SA, the amount being the dispute subject was subsequently repaid to Zarządca Rozliczeń SA according to the adopted payment schedule. The las payment was made on July 28, 2017.

Consequently, the issue of settlement of stranded costs for 2008 between Elektrownia Pątnów II sp. Z o.o. and Zarządca Rozliczeń SA has been completed.

Proceedings due to determining the amount of the annual adjustment of the stranded costs for 2016

On 27 March 2017, the President of the Energy Regulatory Office ("the ERO President") initiated ex officio administrative proceedings in order to determine the amount of the annual adjustment of stranded costs for 2016 for Elektrownia Pątnów II sp. z o.o.

On 27 July 2017 the President of ERO issued a decision fixing the annual cost of stranded costs for Elektrownia Pątnów II sp. z o.o. for 2016 in the amount of PLN 88 354 thousand.

On 29 September 2017, Zarządca Rozliczeń SA paid the amount resulting from the decision of the President of ERO for Elektrownia Pątnów II Sp. z o.o.

The proceeding is completed.

Proceedings on failure to comply with the obligations referred to in Article 49a paragraph 1 and 2 of the Act – Energy law

On 27 September 2016, the President of the Energy Regulatory Office initiated administrative proceedings against Elektrownia Pątnów II sp. z o.o. on its failure to comply with the obligations, referred to in Article 49a paragraph 1 and 2 of the Act – Energy law, i.e. obligation of selling electricity generated in the period from 1 January 2012 to 31 December 2012 by means of the so-called pubic trading.

On 12 October and 21 December 2016, Elektrownia Pątnów II sp. z o.o. sent the appropriate explanations and its position in the above-mentioned issue to the ERO President.

On 28 April 2017 ERO President issued a decision to discontinue the aforementioned proceedings.

The proceeding is completed.

Prosecution of individual interpretation of tax law in scope of returns to Zarządca Rozliczeń S.A. the negative corrections resulting from LTC Act

On 7 July 2017 Elektrownia Pątnów II sp. z o.o. submitted to the Provincial Administrative Court in Poznań (through the Director of National Tax Information Office) a complaint about the individual interpretation of the tax law issued by the Director of National Tax Information dated 20 April 2017 in scope of repayment for Zarządca Rozliczeń SA, on the basis of the agreement between the Parties, liability for repayment of stranded costs for 2008 and other future repayments (negative corrections) from Elektrownia Pątnów II Sp. Z o.o. for Zarządca Rozliczeń S.A., that validity will be based on the Act dated 29 June 2007 of the principles of covering the costs incurred by generators in connection with the termination of long-term contracts for sale of power and electricity (Dz. U. z 2017 r., item 569 with changes, hereinafter referred to as "LTC Act").

On 10 August 2017, the Director of the National Treasury Information Division sent to the Voivodship Administrative Court in Poznań the answers to the above mentioned complaint.

In the opinion of Elektrownia Pątnów II sp. z o.o., all the repayments from Elektrownia Pątnów II Sp. z o.o. for Zarządca Rozliczeń S.A. arising from the LTC Act constitutes the costs of obtaining revenues at the actual time of those payments. The Company reserves the right to include these costs in the settlement for the tax year, in which Zarządca Rozliczeń SA was paid / will be paid. The above is included in the regulation in article 42 pint 4 of LTC Act.

The above opinion complies also with the broad case law in this scope.

Having a different opinion the Director of National Treasury Department, who issued the individual interpretation considered the Company's position to be incorrect and stated that the repayments for Zarządca on the basis of the agreement made in 2014-2017 (within the scope of repayments) in 2017 (in scope of future, not made repayments), and other repayments from The Company for Zarządca, which validity will be based on LCT Act, constitute or will constitute the revenue costs on the day of incurring the costs, i.e. posting in accounting books.

On 18 January 2018, the company won a dispute with the Director of the National Tax Information in the aforementioned case, before the Court of Appeals in Poznań. The verdict of the court means that the company correctly recognized the costs of obtaining income from the abovementioned title.

On 27 March 2018, the Director of the National Tax Information appealed against the court's judgment.

The proceeding is in progress.

Proceedings due to failure to perform obligation to maintain stocks of fuel

On 17 September 2008 and 29 May 2009, the ERO President initiated proceedings on imposing a pecuniary penalty on the ZE PAK SA company due to failure to perform the obligation to maintain fuel stocks securing continuity of electricity and heat supplies to recipients as of 31 December 2007, 31 March 2008, 1 July 2008, 1 September 2008, 1 October 2008, 1 November 2008, 1 December 2008, 1 January 2009, 1 February 2009, and 1 March 2009.

On the basis of the decision of the ERO President of 28 December 2010, the pecuniary penalty, due to failure to perform the obligation to maintain fuel stocks in the quantity securing continuity of electricity and heat supplies to recipients, was imposed on ZE PAK SA in 2008 and 2009 in the amount of zloty 1,500 thousand. Initially, the Company created the provision for the costs of the penalty in the full amount in 2010, which it then redeemed in 2015 in connection with the penalty payment.

On 30 January 2014, the Court for Protection of Competition and Consumers decided about a dismissal of the company's appeal against the ERO President's decision. On 30 April 2014, the Company submitted the appeal to the Court of Appeal in Warsaw.

On 13 May 2015, the Court of Appeal in Warsaw dismissed the Company's appeal against the judgement of the Court for Protection of Competition and Consumers of 30 January 2014 that consequently upholds the decision of the ERO President.

On 11 December 2015, the Company submitted a cassation appeal from the judgement of the Court of Appeal of Warsaw of 13 May 2015 before the Supreme Court.

On 22 March 2017, the Supreme Court issued a judgement, which revoked the contested sentence of the Court of Appeal in Warsaw of 13 May 2015 and handed over the case to the Court of Appeal in Warsaw for repeated examination and stating on costs of cassation proceedings.

On April 11, 2018, the Warsaw Court of Appeal passed a judgment, which changed the verdict of the Court of Competition and Consumer Protection of January 30, 2014 – by repealing the decision of the President of the Energy Regulatory Office of December 28, 2010. From this judgment, the ERO President is entitled to file a cassation appeal.

The proceeding is not completed.

Proceedings on refund of excise duty overpayment

In light of the regulations mandatory within the European Union, especially regulations of Article 21 paragraph 5 of the Energy Directive, in relation to Article 6 paragraph 1 of the Horizontal Directive, after 1 January 2006, the object of excise tax is sale of energy at the last stage of trade, i.e. sale by the distributor to the final recipient (consumer). Taxation with this tax does not cover an earlier stage of trade, e.g. between the producer of electricity and its distributor. In this case, the tax obligation arises at the time of supply of electricity to the consumer.

As at 1 March 2009, the Act of 6 December 2008 on excise duty entered into force, according to which the sale of electricity to an entity which is not its final customer is not subject to excise duty.

Due to the above fact, pursuant to Article 75 § 1, in relation to Article 75 § 2 of the Act of 29 August 1997 – Tax Ordinance, ZE PAK SA submitted applications for stating overpayment of the excise tax for 2006, 2007, 2008, as well as January and February 2009 for the total amount of PLN 626 million, with the justification that pursuant to the regulations of the EU law and the judicial decisions of the Provincial Administrative Courts, the activities executed by ZE PAK SA are not subject to the excise tax. Particular applications were recognised at the following levels: the Customs Office in Kalisz, the Customs Chamber in Poznań, and, currently, the Provincial Administrative Court in Poznań („PAC"), as well as the Supreme Administrative Court. Due to the position of judicature presented in the course of court proceedings, the amount of overpayment, the repayment of which the Company submits, has been reduced to the amount of damages caused by economic analyses, i.e. currently up to the amount of approximately PLN 108 million.

Moreover, in association with the rulings of the Administrative Courts regarding other power companies, in the subject of overpaid excise duty and the resolution I GPS 1/11 of the National Administrative Court ("NSA") of 22 June 2011 (where the NSA ruled that transferring the tax load in price, excludes the possibility to return the overpayment), notwithstanding the ongoing administrative proceedings, on 10 February 2012, the Company initiated a civil-law proceedings, filling an application to summon the State Treasury to a conciliation hearing regarding the amount of PLN 626 406 thousand, to the District Court Warszawa Śródmieście. A conciliatory settlement was not reached since during the hearing of 16 April 2012, the representatives of the Treasury did not agree to settle. Simultaneously, the Company, waiting for the results of the tax proceedings regarding the previously submitted application for overpayment, submitted in writing, on 14 September 2012, in the Customs Chamber in Poznań, additional explanations in the form of results of a detailed economic analysis, the purpose of which was to demonstrate whether the Company suffered loss related to the payment of excise tax to which it was not obliged. The Company's opinion is that the submitted document also applies to other overpayment applications from the entire period embraced by the proceedings, i.e. between January 2006 and February 2009. Ultimately, all applications were included in the cause lists of the Provincial Administrative Court (WSA) and the Supreme Administrative Court (NSA). As of the date of development of this statement, the status of the proceeding is as follows:

- Twenty two cases for the period of January 2006 – November 2007 (excluding November 2006) were conducted again from the start by the Head of the Customs Office, after the cases returned from the Supreme Administrative Court. The Company submitted monthly economic analyses of suffering the prejudice. After the negative decisions of the Head of the Customs Office and then of the Head of Customs Chamber, complaints were submitted to the Provincial Administrative Court in Poznań, Hearings before the Provincial Administrative Court in Poznań took place on 4 and 18 November 2015. In all cases, negative judgements for the Company were issued. In February 2016, the Company submitted cassation appeals to the Supreme Administrative Court. The Supreme Administrative Court dismissed the Company's cassation appeals in the abovementioned 22 cases at the hearings held on April 10 and 11, 2018.
- 14 proceedings for the period of December 2007 – February 2009 (excluding July 2008) on 26 January 2017, hearings took place before the Provincial Administrative Court in Poznań. In all the cases, the Company's appeals against the Customs Chamber in Poznań were dismissed. The Company submitted applications for a written justification of the judgement, which were obtained on 7 March 2017, to the Provincial Administrative Court. Currently, the Company analyses justifications and prepares the applications of cassation appeals to the Supreme Administrative Court,
- the proceeding for November 2006 was concluded with a negative judgement of the Supreme Administrative Court of 8 December 2011,
- the proceeding for July 2008 reached the recognition of our cassation appeal by the Supreme Administrative Court. On the hearing on 29 April 2015, the Supreme Administrative Court dismissed the Company's cassation appeal and pointed out that it fully agrees with the Provincial Administrative Court in Poznań in the judgement, against which the cassation appeal was submitted.

Notwithstanding the foregoing proceedings, ZE PAK SA lodged a complaint against the actions of the Polish authorities to the European Commission ("EC"), pursuant to art. 258 of the Treaty on the Functioning of the European Union. The opinion issued by the EC may oblige the Polish tax authorities to pass a ruling beneficial to ZE PAK SA. On 21 March 2017, ZE PAK SA received a "pre-closure letter" from the EC, which initially denied the relevance of ZE PAK SA's position, however, at the same time giving the right to a second comment on the subject, which ZE PAK SA exercised. On 9 June 2017, a letter summarising the reasoning of ZE PAK SA, in terms of the overpaid excise tax. Currently, ZE PAK SA is awaiting the EC to take the final position on the case in question.

In case of the Elektrownia Pątnów II sp. z o.o., the proceedings for all periods (one case) were included in the cause lists of the Provincial Administrative Court after a negative decision of the Head of Customs Chamber. The aforementioned company does not have access to comparative analyses of suffering the prejudice. On 4 November 2015, a hearing in the Provincial Administrative Court in Poznań took place. On 18 November 2015, a negative ruling was given. On 8 February 2016, the company filed a cassation appeal to the Supreme Administrative Court. Currently, Elektrownia Pątnów II sp. z o.o. is awaiting the setting of a hearing before the Supreme Administrative Court. The Supreme Administrative Court dismissed the Company's cassation complaint at the hearing held on April 11, 2018.

Proceedings on an environmental decision issued to PAK KWB Konin SA concerning lignite deposit in Tomisławice

PAK KWB Konin SA is a party in the administrative proceedings related to the environmental decision regarding the lignite deposit in Tomisławice. On 7 August 2007, the Head of Wierzbinek Commune issued an environmental decision regarding the lignite open cast. On 5 December 2008, this decision was contested by nine physical persons supported by the Greenpeace organisation due to alleged major infringement of the regulations of the law.

On 25 March 2009, the Self-government Appeal Court dismissed the application to reverse the environmental decision. The plaintiffs applied for the judicial review. On 4 May 2009, after the judicial review, the Self-government Appeal Court sustained its previous decision. The plaintiffs again appealed against the environmental decision. On 5 May 2010, the Provincial Administrative Court in Poznań ruled that the environmental decision, pursuant to which the license for the extraction of lignite at the Tomisławice deposit was granted, infringes the regulations of the law in a major manner. PAK KWBK SA and the Self-government Appeal Court submitted an appeal against this judgement. On 21 March 2012, the Supreme Administrative Court overturned the contested decision of the Provincial Administrative Court in Poznań and referred the matter for reconsideration. On 6 November 2012, the Provincial Administrative Court in Poznań announced the decision repealing the decision of the Self-government Appeal Court of 25 March 2009 refusing to declare the invalidity of the environmental decision issued on 7 August 2007 by the Head of Wierzbinek Commune, related to the extraction of lignite from the Tomisławice open pit by PAK KWBK SA On 7 January 2013, PAK KWBK Konin SA submitted a cassation appeal from the described decision.

After the review on the hearing on 7 October 2014, the Supreme Administrative Court dismissed the cassation appeal of PAK Kopalnia Węgla Brunatnego Konin SA from the judgement of the Provincial Administrative Court in Poznań of 6 November 2012 repealing the decision of the Self-government Appeal Court in Konin of 25 March 2009 refusing the annulment of the environmental decision issued on 7 August 2007 by the Head of Wierzbinek Commune related to the extraction of lignite from Tomisławice open pit.

Dismissal of the cassation appeal of PAK Kopalnia Węgla Brunatnego Konin SA means that the judgement of the Provincial Administrative Court in Poznań of 6 November 2012 became legally binding and the case regarding the statement of invalidity of the environmental decision will be examined again by the Self-government Appeal Court. On 1 October 2015, the Self-government Appeal Court issued a decision to suspend the proceedings on the statement of invalidity of the environmental decision issued by the Head of Wierzbinek Commune in connection with the unfinished European Commission proceedings against the Polish government on breach of the provisions concerning the environment protection in connection with the lignite deposit in Tomisławice. In the case of a ruling on suspending the proceedings, a separate proceeding is under way.

The decision of the Supreme Administrative Court in Warsaw of 7 October 2014 does not invalidate the environmental decision issued by the Head of Wierzbinek Commune and does not halt the extraction and utilisation works at Tomisławice open pit. The environmental decision issued on 7 August 2007 by the Head of Wierzbinek Commune is still in legal transactions, and until the issue of a final judgement by the Self-government Appeal Court, it exerts legal effects.

Proceedings on an environmental decision on lignite deposit in Ościsłowo

On 13 March 2017, PAK KWB Konin SA received the decision of the Regional Director for Environmental Protection in Poznań ("RDOŚ in Poznań") of 10 March 2017, refusing the establishment of the environmental conditions for the investment titled: "Extraction of lignite and associated minerals from the Ościsłowo Open Pit." The decision of RDOŚ in Poznań is not final. PAK KWB Konin SA appealed accordingly to the General Directorate for Environmental Protection in Warsaw. The appeal included a request to revoke the appealed ruling in its entirety and determine the environmental conditions for the execution of the above-mentioned project. On 30 November 2017, General Director of Environmental Protection in Warsaw has decided to repeal a decision in its entirety (contested by PAK KWB Konin SA - a subsidiary of the Company) of the Regional Director for Environmental Protection in Poznań ("RDOŚ in Poznań") dated March 10, 2017, refusing to specify environmental conditions for the project entitled: " Extraction of lignite and associated minerals from Ościsłowo Open Pit" and forward the case for reconsideration by RDOŚ in Poznań.

PAK KWB Konin SA, by letter of December 18, 2017 filed an objection against the abovementioned decision of GDOŚ in Warsaw to the Provincial Administrative Court in Warsaw (WSA). In the opinion of PAK KWB Konin S.A. there were grounds for issuing a reformatory decision by GDOŚ in Warsaw, i.e. amending the contested decision of RDOŚ in Poznań and substantive decision in this matter, not referring the matter for reconsideration. The other party also opposed the WSA. Both objections were dismissed by the WSA. The verdict was passed on March 1, 2018. On April 12, 2018, PAK KWB Konin SA filed a cassation complaint with the Supreme Administrative Court in Warsaw against the verdict of the WSA in Warsaw of 1 March 2018.

At present, the case is being reconsidered by RDOŚ in Poznań, which informed about June 5, 2018 as the new date of settling the matter.

The proceedings for issuing the environmental decision were initiated on 16 September 2015.

34.2. Tax settlements

Tax settlements and other regulated areas of activities (for example, customs or foreign exchange matters) may be the subject of inspection of the administrative authorities entitled to impose high penalties and sanctions. The lack of reference to fixed legal regulations in Poland causes ambiguities and inconsistencies of the laws in force. Common differences in opinions as to the legal interpretation of the tax law, both inside national authorities, as well as between them and companies, cause uncertainty and conflicts. Such phenomena result in the significantly higher tax risk in Poland than these normally existing in the countries of a more developed tax system.

Tax settlements may be subject to inspection for a period of five years, starting from the end of the year of the tax payment. As a result of the conducted inspections, the current tax settlements of the Group may be increased by additional tax liabilities. In the Group's opinion, as of 31 December 2016 and 31 December 2015, appropriate provisions for the recognised and calculable tax risk were created.

In 2017, the audit of the corporate income tax for 2016 was carried out in the company Elektrownia Pątnów II sp. z o.o. In the opinion of Elektrownia Pątnów II sp. z o.o. all returns / repayments from Elektrownia Pątnów II sp. o.o. for Zarządca Rozliczeń SA arising from the LTC Act constitute tax deductible costs when the repayments are actually made. Elektrownia Pątnów II sp. z o.o. has the right to include these costs in the settlement for the tax year in which the settlement was / will be made to Zarządca Rozliczeń SA. This is determined by the regulation contained in art. 42 section 4 of the LTC Act. The company's above-mentioned opinion is also in line with broad court decisions in this area.

Having a different opinion the Director of National Treasury Department, who issued the individual interpretation considered the Company's position to be incorrect and stated that the repayments for Zarządca on the basis of the agreement made in 2014-2017 (within the scope of repayments) in 2017 (in scope of future, not made repayments), and other repayments from The Company for Zarządca, which validity will be based on LCT Act, constitute or will constitute the revenue costs on the day of incurring the costs, i.e. posting in accounting books.

On January 18, 2018, the Provincial Administrative Court in Poznań responded to the abovementioned complaint of Elektrownia Pątnów II sp. o.o., issued a verdict abrogating the contested Interpretations of the Director of the National Tax Information dated 20 April 2017. In the justification of the judgment, the WSA shared the position of Elektrownia Pątnów II sp. z o.o. that in the present case, contrary to the tax authority's position, general rules defining the day of tax deductible costs, which were set out in the Act on Corporate Income Tax (hereinafter 'u.p.d.o.p'), cannot be applied, in particular in art. 15. In the present case, the provision of Article 42 section 4 of the LTC Act as "Lex Specialis" to the provisions of the Law on u.p.d.o.p.

The verdict of the Provincial Administrative Court in Poznań confirmed that the Pątnów II Power Plant sp. Z o.o. proceeded correctly including all refunds / repayments from Elektrownia Pątnów II sp. o.o. to Zarządca Rozliczeń SA under the LTC Act to the tax deductible costs at the time of actual repayment.

For Elektrownia Pątnów II sp. Z o.o. the above sentence means lowering the tax risk and confirming the correct tax asset settlement for the years 2014-2016. The above verdict of the Provincial Administrative Court, at the same time, constitutes a security for the position of Elektrownia Pątnów II sp. z o.o., which disagreed with the result of the 2016 tax audit carried out in 2017 on the basis of income tax from legal persons.

In the minutes of the inspection of October 31, 2017, the Head of the Second Wielkopolska Tax Office in Kalisz shared the position expressed by the Director of the National Tax Information in the interpretation of 20 April 2017.

On November 14, 2017, Elektrownia Pątnów II sp. z o.o. raised objections to the aforementioned tax inspection protocol and disagreed with the position of the tax authorities, in the scope of the Tax Office's questioning of the manner of recognition as tax-deductible costs, expenses due to the return of funds to cover stranded costs by Zarządca Rozliczeń SA At the same time, Elektrownia Pątnów II sp. z o.o. indicated that the most reasonable solution would be to abstain from all actions in this case until a judicial decision on the complaint regarding the individual interpretation of tax law, issued by the Director of the National Tax Information dated 20 April 2017, was obtained.

On 27 March 2018, the Director of the National Tax Information filed a cassation complaint from the Judgment of the Provincial Administrative Court in Poznań of January 18, 2018.

With reference to the above, on 17 April 2018 Elektrownia Pątnów II sp. Z o.o. received the decision of the Head of the Second Wielkopolska Tax Office in Kalisz to initiate tax proceedings regarding the settlement of the corporate income tax for 2016.

As at the date of the report, Elektrownia Pątnów II sp. Z o.o. expects that in the next step, the Head of the Second Wielkopolska Tax Office in Kalisz will suspend the tax proceedings initiated in April 2018 pending resolution of the matter concerning the recognition by the Tax Office of the method of recognition in 2016 as tax deductible expenses, expenses due to the return of the Clearing Administrator funds to cover stranded costs.

(in thousand PLN)

35. Liability repayment securities

In order to protect the repayment of liabilities, the Group uses many forms of protections. Mortgages and registered pledges are the most common ones.

As of 31 December 2017 and 31 December 2016, the Group had liabilities protected with its assets and other protections of payment of liabilities:

Liabilities secured with the assets

Agreement	*Kind of security*	*31 December 2017 Security amount*	*currency*	*31 December 2016 Security amount*	*currency*
Syndicated loan agreement of 13 March 2014 for PLN 667 million for ZE PAK SA	Registered pledge on a collection of items Registered pledge on bank accounts Joint contractual mortgage established on real estate	Up to 2 040 000	PLN	Up to 2 040 000	PLN
Syndicated loan agreement dated 14 January 2011 for EUR 240 million for Pątnów II Power Plant	Registered and financial pledge on shares of ZE PAK in PAK Infrastruktura and PAK-HOLDCO Registered and financial pledge on shares of PAK-HOLDCO in Elektrownia Pątnów II Joint contractual mortgage established on the property of Pątnów II and PAK Infrastruktura Registered pledge on a collection of items Registered pledge on bank accounts	Up to 400 000 Up to 339 750	EUR PLN	Up to 400 000 Up to 339 750	EUR PLN
Multi-purpose line of November 20, 2013 for PLN 76.7 million for PAK KWB Konin	Registered pledge on fixed assets	Up to 153 400	PLN	Up to 100 500	PLN
	Mortgage on perpetual usufruct right	-		Up to 100 500	
Agreement of the guarantee line of June 8, 2007 for PAK Serwis	Registered pledge on fixed assets	Up to 5 674	PLN	-	PLN

Other securities of liabilities

Guarantees given

Kind of security	*31 December 2017 Security amount*	*currency*	*31 December 2016 Security amount*	*currency*
Guarantees of good performance of the contract	14 500	PLN	14 581	PLN
Guarantees to remove defects and faults	4 135 419	PLN EUR	4 264 279	PLN EUR
Payment guarantees	145	PLN	131	PLN

(in thousand PLN)

Guarantee of advance payment	1 329	PLN	5 658	PLN

In addition, the Group uses as collateral the repayment of liabilities, assignments from sales contracts, assignment from insurance policies, power of attorney to bank accounts and a statement on submission to enforcement.

In addition, intra-group guarantees are used in the Capital Group as collateral for repayment of liabilities.

The table below shows the sum of granted guarantees.

	31 December 2017	*currency*	*31 December 2016*	*currency*
Intra-Group Guarantees	50 000	PLN	143 500	PLN

36. Obtained guaranties and sureties

Kind of security	*31 December 2017* *Security amount*	*currency*	*31 December 2016* *Security amount*	*currency*
Guarantees of good performance of the contract	19 752	PLN	44 036	PLN
Guarantees to remove defects and faults	-	EUR	34	EUR
	2 245	PLN	2 889	PLN
Payment guarantees	18	EUR	-	EUR
Guarantee of advance payment	32 004	PLN	47 512	PLN
Guarantees of good performance of the contract	5 149	EUR	-	EUR
Guarantees to remove defects and faults	2 399	PLN	6 958	PLN

The Group has sureties received, these are only intra-group guarantees.

The value of guarantees received is in line with the value of sureties granted described in Note 35.

37. Information about related entities

The following table presents total amounts of transactions concluded with affiliates for the current and next financial years:

Related entity		*Sales to related entities*	*Purchase from related entities*	*Receivables from related entities*	*Liabilities towards related entities*
Elektrim SA	2017	-	120	-	-
	2016	-	121	-	-
Megadex Serwis Sp. z o.o.	2017	3	-	-	-
	2016	1	47 182	210	5 432
Polkomtel sp. z o.o.	2017	128 970	3 979	16 859	475
	2016	120 642	4 530	15 400	891
Laris Investments sp. z o.o.	2017	463	821	251	-
	2016	501	974	217	22

(in thousand PLN)

CPE sp. z o.o.	2017	-	1 089	-	11
	2016	-	-	-	-
Plus Flota sp. z o.o.	2017	-	628	-	357
	2016	-	-	-	-
Total	**2017**	**129 436**	**6 637**	**17 110**	**843**
	2016	**121 144**	**52 807**	**15 827**	**6 345**

37.1. Loan granted to a member of the Management Board

Both in the financial year ended 31 December 2017 and in the one ended 31 December 2016, the Parent Company did not grant any loans and similar benefits to members of the management and supervisory staff.

37.2. Other transactions involving members of the Management Board

Both in the financial year ended 31 December 2017 and in the one ended 31 December 2016, there were no transactions with members of management and supervisory staff.

37.3. Remuneration of Chief executive Staff of the Group

37.3.1. Remuneration paid or payable to the members of the Management Board and to the members of the Supervisory Council of the Group

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Management Board of the parent company		
Short-term employee benefits	2 400	2 989
Benefits for termination of the contract of employment	-	28
Supervisory Board of the parent company		
Short-term employee benefits	993	1 095
Management Boards of subsidiaries		
Short-term employee benefits	4 235	5 453
Post-employment benefits	19	-
Benefits for termination of the contract of employment	105	-
Supervisory Board of subsidiaries		
Short-term employee benefits	16	14
Total	7 768	9 579

37.3.2. Remuneration paid or entitled to other members of the main management

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Short-term employee benefits	14 701	15 389
Jubilee awards	-	96
Post-employment benefits	15	7

(in thousand PLN)

Benefits for termination of the contract of employment	317	247
Total amount of remuneration paid to the chief executive staff (except for members of the Management Board and the Supervisory Board)	15 033	15 739

38. Information about the remuneration of the statutory auditor or the entity entitled to audit accounts

The following table presents the remuneration of an entity entitled to audit accounts paid or due to the year ended 31 December 2017, and for the year ended 31 December 2016, divided into types of services:

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Compulsory examination and unit review and consolidated financial statements	194	212
Other services	23	104
Total	217	316

39. Goals and rules of financial risk management

Apart from derivatives, the main financial instruments, used by the Group, consist of bank credits, loans granted from affiliates and other institutions, funds, and short-term deposits. The main goal of these financial instruments is to obtain funds for the Group's activities. The Group also has other financial instruments, such as receivables and liabilities due to supplies and services created directly within its conducted activities.

The Group also concluded transactions with the use of derivatives, above all, the contracts for a change in interest rates (interest rate swaps). The goal of these transactions includes the interest rate risk management arising within the Group's activities, and resulting from financing resources used by it.

The rule which is applied by the Group currently and through the whole period included in the statement is non-conducting of the exchange of financial instruments.

The main kinds of the risk resulting from the Group's financial instruments include the interest rate risk, liquidity risk, foreign currency risk, and credit risk. The Management Board verifies and consults the rules of management of each of these kinds of risk – these rules were discussed shortly below. The Group also monitors the market price risk regarding all its held financial instruments.

39.1. Interest rate risk

Exposure of the Group to risk caused by the changes of interest rates mainly concerns long-term financial liabilities.

The Group uses financial liabilities, mostly variable rate credits and loans.

In order to minimise interest rate risk, the Group concluded contract for interest rates change (interest rate swaps), within which it agreed to change, within specified time intervals, the difference between the amount of interests calculated according to the fixed and the variable rate of the agreed main amount. The transactions are to protect incurred financial liabilities.

Interest rate risk – the sensitivity gap

In the interest rate sensitivity gap analysis, the Group uses yield curve shift by potential possible change of benchmark interest rates during the coming year. For the needs of the interest rate sensitivity gap analysis, average levels of benchmark interest rates in a given year were used. The scale of potential interest rate sensitivity gap was estimated on the basis of volatilities implied of ATMF options for the interest rate quoted on the inter-bank market for foreign currencies, for which the Group has the exposition to interest rate risk from the balance sheet date.

(in thousand PLN)

	31 December 2017		***Interest rate risk sensitivity study as of 31 December 2017***							
			WIBOR				***EURIBOR***			
Classes of financial instruments			***WIBOR + 44***		***WIBOR - 44***		***EURIBOR + 10.05***		***EURIBOR - 10.05***	
	Carrying amount	***value at risk***	***Profit/loss***	***Other comprehensive income***	***Profit/loss***	***Other comprehensive income***	***Profit/loss***	***Other comprehensive income***	***Profit/loss***	***Other comprehensive income***
Other financial assets	46 099	43 995	37	-	(37)	-	36	-	(36)	-
Trade and other receivables	253 261	-	-	-	-	-	-	-	-	-
Derivative financial instruments	-	-	-	-	-	-	-	-	-	-
Cash and cash equivalents	322 201	322 201	1 249	-	(1 249)	-	38	-	(38)	-
Interest-bearing loans and borrowings	(652 038)	(652 038)	(1 820)	-	1 820	-	(239)	-	239	-
Trade payables and other financial liabilities	(151 562)	-	-	-	-	-	-	-	-	-
Derivative financial instruments	(5 009)	(5 009)	-	-	-	-	-	125	-	(125)
Total	**(187 048)**	**(290 851)**	**(534)**	**-**	**534**	**-**	**(165)**	**125**	**165**	**(125)**

(in thousand PLN)

	31 December 2016		**Interest rate risk sensitivity study as of 31 December 2016**							
			WIBOR				***EURIBOR***			
Classes of financial instruments			***WIBOR + 62***		***WIBOR - 62***		***EURIBOR + 18.92***		***EURIBOR – 18.92***	
	Carrying amount	***Value at risk***	***Profit / loss***	***Other comprehensive income***	***Profit / loss***	***Other comprehensive income***	***Profit / loss***	***Other comprehensive income***	***Profit / loss***	***Other comprehensive income***
Other financial assets	89 262	86 834	68	-	(68)	-	143	-	(143)	-
Trade and other receivables	246 025	-	-	-	-	-	-	-	-	-
Derivative financial instruments	296	-	-	-	-	-	-	-	-	-
Cash and cash equivalents	350 101	350 101	1 399	-	(1 399)	-	235	-	(235)	-
Interest-bearing loans and borrowings	(1 009 809)	(1 009 809)	(3 861)	-	3 861	-	(732)	-	732	-
Trade payables and other financial liabilities	(307 731)	-	-	-	-	-	-	-	-	-
Derivative financial instruments	(10 053)	(10 053)	-	-	-	-	-	587	-	(587)
Total	**(641 909)**	**(582 927)**	**(2 394)**	-	**2 394**	**-**	**(354)**	**587**	**354**	**(587)**

39.2. Currency risk

The Group is exposed to currency risk due to concluded transactions. Such a risk relates to liabilities due to loans and advances. In 2017, two companies of the Group applied instruments to limit the risk resulting from changes in foreign exchange rates. ZE PAK SA hedged the euro exchange rate for a part of cash flows related to the purchase of CO2 emission allowances. To hedge the exchange, forward transactions were made with the settlement date in March 2018. The Pątnów II power plant secured the euro exchange rate for a part of the flows related to the repayment of the consortium loan instalment, also applying a forward transaction with the settlement date in April 2018. Potential possible changes in exchange rates have been calculated on the basis of the annual volatilities implied for currency options quoted on the interbank market for a given currency pair from the balance sheet date.

The Group identifies the exposure to EUR/PLN exchange rate changes. The below table presents the gross financial result sensitivity for exchange rate changes rationally possible to occur, assuming non-variability of other risk factors for these classes of financial instruments exposed to the exchange rate change risk.

(in thousand PLN)

	31 December 2017		*Analysis of sensitivity to interest rate risk as of 31 December 2017*			
			EUR/PLN			
Classes of financial instruments			**EUR/PLN + 6.2%**		**EUR/PLN - 6.2%**	
			4.4295		**3.9123**	
	Carrying amount	*Value at risk*	*Profit/loss*	*Other comprehensive income*	*Profit/loss*	*Other comprehensive income*
Other financial assets	46 099	35 630	2 209	-	(2 209)	-
Trade and other receivables	253 261	-	-	-	-	-
Derivative financial instruments	-	-	-	-	-	-
Cash and cash equivalents	322 201	38 235	2 371	-	(2 371)	-
Interest-bearing loans and borrowings	(652 038)	(238 271)	(14 773)	-	14 773	-
Trade payables and other financial liabilities	(151 562)	(1 860)	(115)	-	115	-
Derivative financial instruments	(5 009)	-	-	-	-	-
Total	**(187 048)**	**(166 266)**	**(10 308)**	**-**	**10 308**	**-**

(in thousand PLN)

	31 December 2016		**Analysis of sensitivity to interest rate risk as of 31 December 2016**			
			EUR/PLN			
Classes of financial instruments			**EUR/PLN + 7.75%**		**EUR/PLN – 7.75%**	
			4.7669		**4.0811**	
	Carrying amount	***Value at risk***	***Profit / loss***	***Other comprehensive income***	***Profit / loss***	***Other comprehensive income***
Other financial assets	89 262	75 813	5 875	-	(5 875)	-
Trade and other receivables	246 025	3 754	291	-	(291)	-
Derivative financial instruments	296	-	-	-	-	-
Cash and cash equivalents	350 101	124 422	9 643	-	(9 643)	-
Interest-bearing loans and borrowings	(1 009 809)	(387 123)	(30 002)	-	30 002	-
Trade payables and other financial liabilities	(307 731)	(60 927)	(4 722)	-	4 722	-
Derivative financial instruments	(10 053)	-	-	-	-	-
Total	**(641 909)**	**(244 061)**	**(18 915)**	**-**	**18 915**	**-**

39.3. Commodity prices risk

The company is exposed to influence and the adverse impact of risk factors associated with the volatility of cash flows and financial results due to the changes in the prices of commodity prices. Exposure to the commodity prices risk is reflected by the volume of purchases of basic raw materials, which are mostly lignite and biomass of wood and agricultural origin.

The volume and costs of consumption of the main raw materials are presented in the table below:

	2017		*2016*	
	Volume (tons)	*Consumption cost (in PLN thousand)*	*Volume (tons)*	*Consumption cost (in PLN thousand)*
Fuel				
Lignite	11 666 228	763 820	12 549 649	755 463
Forestry biomass	3 917	499	367 137	51 962
Agricultural biomass	908	189	94 785	22 876
Fuel oil	12 203	19 079	13 963	19 473
Sorbent	159 761	13 084	235 717	17 643

39.4. Credit risk

The credit risk is a potential credit event, which may be materialised in the form of the following factors: the counterparty’s insolvency, partial repayment of receivables, significant delay in repayment of receivables, or another not predicted derogation from contractual terms.

The Group concludes transactions only with reputable companies of good credit rating. All clients who want to use trade credit terms, are subject to procedures of initial verification. Moreover, thanks to current monitoring of receivables, the Group’s exposure to the risk of unrecoverable receivables is insignificant.

The main recipients of electricity include the companies with a significant position in the electricity trade sector, such as Energa Obrót, ENEA Trading, Tauron Polska Energia, Alpiq Energy, InterEnergia and PSE Operator. The transactions concluded on the exchange market are settled on a day-to-day basis by the Towarowa Giełda Energii SA Company, which minimises the credit risk.

In relation to other financial assets of the Group, such as funds and their equivalents, financial assets available for sale, and some derivatives, the Group’s credit risk occurs as a result of incapability of payment by the other party of the agreement, and the maximum exposure to this risk is equal to the balance sheet value of these derivatives.

39.5. Liquidity risk

The Group monitors risk to a shortage of funds by means of the tool for periodic planning of liquidity. This tool takes into account maturity dates of both investment and financial assets (e.g. receivables accounts, other financial assets), as well as projected cash flows from operating activities.

The goal of the Group is maintenance of balance between continuity and flexibility of financing through use of various resources of financing, such as overdraft facilities, bank credits, debentures, preferred shares, financial lease agreements, and lease agreements with purchase option.

The tables below present financial liabilities of the Group as of 31 December 2017 and 31 December 2016 according to the maturity date based on contractual non-discounted payments.

(in thousand PLN)

31 December 2017	*Less than 3 months*	*3 - 12 months*	*1 - 5 years*	*Over 5 years*	*Total*
Interest bearing loans and borrowings	75 064	281 629	321 592	-	678 285
Trade payables and other financial liabilities	64 728	81 688	5 146	-	151 562
Derivative financial instruments	39 176	25 618	812	-	65 606
	178 968	**388 935**	**327 550**	**-**	**895 453**

31 December 2016	*Less than 3 months*	*3 - 12 months*	*1 - 5 years*	*Over 5 years*	*Total*
Interest bearing loans and borrowings	100 041	329 180	634 191	-	1 063 412
Trade payables and other financial liabilities	240 997	61 665	5 069	-	307 731
Derivative financial instruments	14 446	3 716	3 973	-	22 135
	355 484	**394 561**	**643 233**	**-**	**1 393 278**

Derivative instruments indicated in above tables were presented in gross values of non-discounted payments. However, these contracts can be settled either in gross values, or net amounts.

The tables shown below present agreements of these values to balance sheet values of derivative instruments:

(in thousand PLN)

31 December 2017	*On demand*	*Less than 3 months*	*3 – 12 months*	*1 – 5 years*	*Over 5 years*	*Total*
Inflows	-	(102)	(203)	(55)	-	(360)
Outflows	-	950	1 983	812	-	3 745
Net amounts	-	(1 052)	(2 186)	(867)	-	(4 105)
Discounted using appropriate interbank rates	**-**	**(1 949)**	**(2 190)**	**(870)**	**-**	**(5 009)**

31 December 2016	*On demand*	*Less than 3 months*	*3 – 12 months*	*1 – 5 years*	*Over 5 years*	*Total*
Inflows	-	(154)	(365)	(302)	-	(821)
Outflows	-	1 516	3 716	3 973	-	9 205
Net amounts	-	(1 670)	(4 081)	(4 275)	-	(10 026)
Discounted using appropriate interbank rates	**-**	**(1 671)**	**(4 088)**	**(4 294)**	**-**	**(10 053)**

(in thousand PLN)

40. Financial instruments

40.1. Balance sheet value and fair value of particular classes of financial instruments

The table shown below presents a comparison between balance sheet values and fair values of all financial instruments of the Group, divided into particular classes and categories of assets and liabilities according to IAS 39.

		Balance sheet value			
Financial assets	Category according to 39	*31 December 2017*	*31 December 2016*	*31 December 2017*	*31 December 2016*
Other financial assets	PiN	46 099	89 262		
Trade receivables and other receivables	PiN	253 261	246 025		
Derivative financial instruments	WwWGpWF	-	296		
Cash and cash equivalents	UdtW	322 201	350 101		
Financial liabilities					
Interest-bearing bank credits and loans, including:		652 038	1 009 809		
long term	PZFwgZK	302 465	587 851		
short term	PZFwgZK	349 573	421 958		
Liabilities due to supplies and services and other financial liabilities	PZFwgZK	151 562	307 731		
Derivative financial instruments		5 009	10 053		

Used abbreviations:

UdtW – *Financial assets maintained to the maturity date,*

WwWGpWF – *Financial assets/liabilities evaluated in the fair value by the financial result,*

PiN – *Loans and receivables*

DDS – *Financial assets available for sale,*

PZFwgZK – *Other financial liabilities evaluated according to the depreciated cost.*

(in thousand PLN)

As of 31 December 2016 and 31 December 2015, the Group had following financial instruments evaluated in the fair value:

	31 December 2017	*Level 1*	*Level 2*	*Level 3*
Derivatives hedging assets	-	-	-	-
Derivatives hedging liabilities	-	-	5 009	-

	31 December 2016	*Level 1*	*Level 2*	*Level 3*
Derivatives hedging assets	-	-	296	-
Derivatives hedging liabilities	-	-	10 053	-

The fair value of financial instruments other than derivatives as at December 31, 2017 and December 31, 2016 did not deviate significantly from the carrying amounts, mainly due to the fact that for short-term instruments the effect of discounting is not material and the fact that the transactions are concluded at market conditions; for this reason, the fair value of these instruments has been presented at the carrying amount.

The valuation of interest-bearing loans and credits after the initial recognition is carried out according to the depreciated cost method, taking into account the contractual costs related to obtaining a given loan or borrowing as well as discounts and earned bonuses.

As at December 31, 2017, Interest Rate Swap derivatives and forward transactions for currency purchase were valued at fair value. The Interest Rate Swap valuation methodology is presented in note 40.3. For the purposes of valuing foreign exchange contracts, the difference between discounted future cash flows is calculated between the forward price on the valuation day and the transaction price, according to quotations prepared by the relevant bank, multiplied by the nominal value of the contract in a foreign currency. The valuation of these instruments has been classified to level 2 of the fair value measurement hierarchy.

In the period ended 31 December 2017 and the one ended 31 December 2016, there were no shifts between the level 1 and the level 2 of the fair value hierarchy, and none of instruments was shifted to the level 3 of the fair value hierarchy

(in thousand PLN)

40.2. Items of revenue, costs, profits and losses included in the income statement divided into categories of financial instruments

12 month period ended 31 December 2017

	Revenues /(costs) due to interests (including effect of valuation with depreciated cost)	*Profits / (losses) due to exchange rate differences*	*Redemption / (creation) of impairment write-downs*	*Profits/(losses) due to derivative instruments*	*Other*	*Total*
Financial assets						
Cash and cash equivalents	3 179	(1 956)	-	-	-	1 223
Other short-term financial assets	1	(10 020)	-	-	(10)	(10 029)
Deliveries and services receivables	33	(38)	(16)	-	80	59
Other receivables	315	-	-	-	-	315
Derivative instrument	-	-	-	368	-	368
Financial liabilities						
Credit and loan liabilities (long- and short-term ones)	(26 065)	24 190	-	-	(527)	(2 402)
Deliveries and services liabilities	(143)	202	-	-	-	59
Other financial liabilities (without instruments)	(226)	-	-	-	-	(226)
Derivative instruments	-	-	-	(7 404)	-	(7 404)
Other liabilities	(793)	1	(11 166)	-	(1 273)	(13 231)
Total	(23 699)	12 379	(11 182)	(7 036)	(1 730)	(31 268)

(in thousand PLN)

12 month period ended 31 December 2016

	Revenues /(costs) due to interests (including effect of valuation with depreciated cost)	*Profits / (losses) due to exchange rate differences*	*Redemption / (creation) of impairment write-downs*	*Profits/(losses) due to derivative instruments*	*Other*	*Total*
Financial assets						
Cash and cash equivalents	4 724	1 355	-	-	-	6 079
Other short-term financial assets	11	2 753	1	-	(33)	2 732
Deliveries and services receivables	113	(34)	(113)	-	-	(34)
Other receivables	72	49	-	-	45	166
Derivative instrument	-	-	-	1 306	-	1 306
Financial liabilities						
Credit and loan liabilities (long- and short-term ones)	(34 703)	(16 607)	-	-	(4 049)	(55 359)
Deliveries and services liabilities	(80)	(296)	-	-	-	(376)
Other financial liabilities (without instruments)	(632)	-	-	-	-	(632)
Derivative instruments	-	-	-	(7 379)	-	(7 379)
Other liabilities	(2 250)	(3)	(9 650)	-	(1 047)	(12 950)
Total	(32 745)	(12 783)	(9 762)	(6 073)	(5 084)	(66 447)

(in thousand PLN)

40.3. Interest rate risk

The below table presents the interest rate gap constituting the Group's exposure to interest rate risk and concentration of this risk divided into currencies and kind of interest rate taking into account the effect of protection transactions Interest Rate Swap exchanging the stream of cash interest payments based on the variable EURIBOR rate for the fixed rate in EUR.

	Type of interest rate	*Carrying amount as of 31 December 2017*	*Carrying amount as of 31 December 2016*
Financial assets at interest rate risk – PLN	Fixed	-	-
	Variable	292 331	236 701
Financial assets at interest rate risk – Other currencies	Fixed	-	-
	Variable	73 866	200 708
Financial liabilities at interest rate risk - PLN	Fixed	-	-
	Variable	413 767	622 686
Financial liabilities at interest rate risk – Other currencies	Fixed	118 839	193 703
	Variable	119 432	193 420
Net exposure -PLN	Fixed	-	-
	Variable	(121 436)	(385 985)
Net exposure - other currencies	Fixed	(118 839)	(193 703)
	Variable	(45 566)	6 815

Interest rate of financial instrument of variable interest rate is updated in periods shorter than one year. Interests on financial instruments of the fixed interest rate are fixed through the whole period to the date of maturity of these instruments. Other financial instruments of the Group not included in the above tables are not subject to interest and they are not subject to interest rate risk.

40.3.1. Hedging

The Group secures interest rate risk related to the incurred corporate credit denominated in EUR of variable interest rate based on the EURIBOR 3M benchmark interest rate using derivative transactions. The instrument securing exposure to interest risk rate is the Interest Rate Swap transaction, within which the Groups exchanges stream of cash interest payments based on the variable EURIBOR 3M rate for payments of fixed interest rate at 3.1050%. The Groups indicates designated derivative instruments as protecting instruments in the model of cash flow security, and includes them in accordance with protections accounting rules.

In the tables shown below, basic parameters of derivative transaction indicates as security instruments, including periods, when cash flows due to cash flow securities and when they will influence the financial result, as well as their fair value in zloty as of 31 December 2017 and 31 December 2016 are presented.

Instrument type	*Nominal value in the transaction currency [euro]* 31 December 2017*	*Fair value in zloty 31 December 2017*	*Expected duration of hedged item's realisation 31 December 2017*
IRS transaction	28 492	(4 112)	in quarterly periods, in January, April, July, and October each year, until the date of maturity of IRS, i.e. July 2019

** the nominal values depreciated in accordance with the credit repayment schedule*

Instrument type	*Nominal value in the transaction currency [euro]* 31 December 2016*	*Fair value in zloty 31 December 2016*	*Expected duration of hedged item's realisation 31 December 2016*
IRS transaction	43 785	(10 053)	in quarterly periods, in January, April, July, and October each year, until the date of maturity of IRS, i.e. July 2019

** the nominal values depreciated in accordance with the credit repayment schedule*

The change in the fair value of cash flow securities transferred onto the equity is presented below:

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Opening balance	(6 883)	(14 742)
Effective part of profits / losses on a security instrument	6 352	585
Amounts charged to the income statement, including:	2 776	(7 274)
− adjustment of costs of interest	2 776	(7 274)
− adjustment under ineffective hedging	-	-
Closing balance	(3 307)	(6 883)
Deferred tax assets – recognized in the revaluation reserve	628	1 308
Closing balance including deferred tax	(2 679)	(5 575)

In 2017, two companies of the Group applied instruments to limit the risk resulting from changes in foreign exchange rates. ZE PAK SA hedged the euro exchange rate for a part of cash flows related to the purchase of CO2 emission allowances. To hedge the exchange, forward transactions were made with the settlement date in December 2017 and March 2018. Elektrownia Pątnów II sp. z o.o. hedged the euro exchange rate for a part of the flows related to the repayment of the syndicated loan instalment, also applying a forward transaction with the settlement date in April 2018.

Type of concluded transactions	*Currency cross*	*Transaction amount (nominal value in euro thousand) 31 December 2017*	*Net market value (fair value in zloty thousand) 31 December 2017*	*Maturity*
Purchase of EUR transaction (forward)	(EUR/PLN)	8 936	(805)	March 2018
Purchase of EUR transaction (forward)	(EUR/PLN)	5 600	(92)	April 2018

The Group also hedges the risk of changes in prices of CO2 emission allowances by using forward transactions to purchase allowances for its own needs. The tables below present a summary of forward transactions active as at December 31, 2017 and December 31, 2016.

31 December 2017

Type of concluded transactions	*Number of purchased allowances*	*Total value of transactions in EUR thousand*	*Currency of transactions*	*Maturity*
Forward transactions	2 622 000	17 224	EUR	Up to 1 year
Forward transactions	300 000	2 242	EUR	Up to 2 years

31 December 2016

Type of concluded transactions	*Number of purchased allowances*	*Total value of transactions in EUR thousand*	*Currency of transactions*	*Maturity*
Forward transactions	3 997 000	30 180	EUR	Up to 1 year

41. Capital management

The main goal of the management of the Group's capital is maintenance of good credit rating and safe equity ratios, which would support the Group's operating activities and increased the values for its shareholders.

The Group manages the capital structure, and, as a result of changes of economic conditions, introduces amendments to it. In year, ended 31 December 2017 and 31 December 2016, there were no introduced amendments to goals, rules and processes applying in this area.

The Group monitors the balance of its capitals using the leverage ratio, which is calculated as a relation of net debt to the sum of capitals enlarged with net debt. The Group includes interest bank credits and loans, liabilities due to supplies and services, and other liabilities, decreased by the cash and cash equivalents in the net debt. The capital includes the equity decreased by reserve capitals due to unrealised net profits.

	31 December 2017	*31 December 2016*
Interest-bearing credits and loans	652 038	1 009 809
Derivative financial instruments (liabilities)	5 009	10 053
Trade liabilities and other financial liabilities	151 562	307 731
Minus cash and its equivalents	322 201	350 101
Net debt	486 408	977 492
Equity	2 264 272	2 143 658
Capitals from revaluation of security instruments	(2 678)	(7 084)
Total capital	2 266 950	2 150 742
Net capital and debt	**2 753 358**	**3 128 234**
Leverage ratio	17,67%	31,25%

(in thousand PLN)

42. Employment structure

The average employment in the Group for the years ended 31 December 2017 and 31 December 2016 was developing as follows:

	12 months period ended 31 December 2017	*12 months period ended 31 December 2016*
Management Board of the parent company	4	5
Management Boards of the Group's entities	14	23
Administration	304	377
Sales department	108	62
Production division	5 053	5 278
Other	464	616
Total	5 946	6 362

43. Significant events after the balance sheet date

After the balance sheet date to the date of preparation of these annual financial statements for 2017, there were no significant events except those described in the additional explanatory notes.

Adam Kłapszta /President of the Board/	*Aneta Lato-Żuchowska /Vice President of the Board/*	*Zygmunt Artwik / Vice President of the Board /*	*Elżbieta Niebisz / Vice President of the Board /*	*Aneta Desecka /Chief Accountant/*