

**ZESPÓŁ ELEKTROWNI PAŃNÓW – ADAMÓW – KONIN SA
CAPITAL GROUP**

**MANAGEMENT BOARD'S REPORT
FROM THE CAPITAL GROUP'S OPERATIONS IN 2017**

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

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1. SELECTED FINANCIAL DATA

<i>Selected consolidated financial data</i>	<i>zloty thousand</i>	<i>zloty thousand</i>	<i>euro thousand</i>	<i>euro thousand</i>
	<i>12 months 2017 period from 01.01.2017 to 31.12.2017</i>	<i>12 months 2016 period from 01.01.2016 to 31.12.2016</i>	<i>12 months 2017 period from 01.01.2017 to 31.12.2017</i>	<i>12 months 2016 period from 01.01.2016 to 31.12.2016</i>
Sales revenue	2 443 075	2 704 711	575 559	618 121
Operating profit/loss	290 092	371 433	68 342	84 885
Profit/loss before tax	258 633	307 878	60 931	70 361
Net profit/loss for the period	183 544	250 286	43 241	57 199
Net profit attributable to equity holders of the parent	183 243	247 674	43 170	56 602
Total comprehensive income	186 204	258 880	43 867	59 163
Net cash flow from operating activities	478 798	536 051	112 799	122 506
Net cash flow from investing activities	(57 624)	(183 708)	(13 576)	(41 984)
Net cash flow from financing activities	(447 250)	(387 014)	(105 367)	(88 446)
Net increase / (decrease) in cash and cash equivalents	(26 076)	(34 671)	(6 143)	(7 924)
Net profit per share (in zloty/euro per share)	3.61	4.87	0.85	1.11
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547
	<i>as of 31.12.2017</i>	<i>as of 31.12.2016</i>	<i>as of 31.12.2017</i>	<i>as of 31.12.2016</i>
Total assets	4 455 712	4 801 300	1 068 286	1 085 285
Fixed assets	3 447 776	3 702 058	826 626	836 812
Current assets	1 006 898	1 099 242	241 410	248 472
Total equity	2 264 272	2 143 658	542 874	484 552
Share capital	101 647	101 647	24 371	22 976
Share capital attributable to equity holders of the parent	2 264 272	2 143 658	542 874	484 552
Total liabilities	2 191 440	2 657 642	525 412	600 733
Long-term liabilities	1 191 958	1 389 715	285 780	314 131
Short-term liabilities	999 482	1 267 927	239 632	286 602
Book value per share (in zloty/euro per share)	44.55	42.18	10.68	9.53
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547

Above financial data were converted into EUR according to the following exchange rates:

- data on the statement of comprehensive income and the statement of cash flows according to the arithmetic average of the average NBP exchange rates from each last business day of the month of the financial period from January 1, 2017 to December 31, 2017, which is EUR/PLN 4.2447, and from January 1, 2016 to December 31, 2016, which is EUR/PLN 4.3757.
- data on individual items of the statement of financial position according to the average exchange rate of the EUR/PLN specified by the NBP as at December 29, 2017, i.e. EUR/PLN 4.1709, and as at December 30, 2016, i.e. EUR/PLN 4.4240.

2. DESCRIPTION OF THE COMPANY AND THE CAPITAL GROUP

2.1. Basic information on the Company and the Capital Group

Basic information on the Company

Zespół Elektrowni Pątnów – Adamów – Konin SA (hereinafter referred to as ZE PAK SA or Company) operates in the form of a joint-stock company, pursuant to the regulations of the Code of Commercial Companies as well as other regulations of the generally applicable Polish law. The Company was established as result of transformation of Zespół Elektrowni Pątnów – Adamów – Konin state-owned company with registered office in Konin into a company wholly owned by the State Treasury under the business name of Zespół Elektrowni „Pątnów – Adamów – Konin” Spółka Akcyjna. The deed of transformation was signed on 29 December 1994 in the presence of the notary public Elżbieta Brudnicka from the Notarial Office in Warsaw. On 31 December 1994, the Company was entered into the commercial register section “B” by the District Court in Konin under number RHB 847. Based on the decision of the District Court in Poznań, 22nd Commercial Department of KRS dated 21 June 2011, the Company was entered into the Register of Entrepreneurs. Currently the Company is entered into the Register of Entrepreneurs kept by the District Court Poznań Nowe Miasto i Wilda, IX Commercial Department, under the KRS number 0000021374. The Company was established for an unlimited period of time.

Name:	Zespół Elektrowni „Pątnów – Adamów – Konin” Spółka Akcyjna
Legal status:	stock company
Abbreviated name:	ZE PAK SA
Registered office and address:	ul. Kazimierska 45, 62-510 Konin, Polska
Telephone number:	+48 63 247 30 00
Fax number:	+48 63 247 30 30
Website:	www.zepak.com.pl
Email address:	zepak@zepak.com.pl
KRS number:	0000021374
REGON number:	310186795
NIP number:	665-000-16-45

According to the Company’s Articles of Association, the primary subject of the Company’s operations is the production and sales of electricity as well as the production and sales of heat. The Company produces energy from conventional sources as well as by biomass combustion. The Company can conduct operations within the territory of the Republic of Poland as well as abroad.

The Company’s shares are listed on the regulated market operated by Giełda Papierów Wartościowych SA w Warszawie (Warsaw Stock Exchange). The Company’s shares are dematerialised and marked by Krajowy Depozyt Papierów Wartościowych SA (National Depository for Securities) with the following stocks code: ISIN PLZEPAK00012.

In 2017, the share capital of ZE PAK SA has been not changed. As of 31 December 2017 amounts to zloty 101 647 094.00 and is divided into 50 823 547 bearer shares class A with a face value of zloty 2.00 each, which represent 50 823 547 votes at the Company’s General Meeting, comprising 100% of the total votes at the Company’s General Meeting.

The Company has no branches (establishments).

Basic information about the Capital Group

As of 31 December 2016 the ZE PAK Capital Group (hereinafter referred to as the “Group”, “Capital Group” the “ZE PAK SA Group”) is composed of a dominant entity Zespół Elektrowni Pątnów – Adamów – Konin SA (hereinafter referred to as “ZE PAK SA” or “Company”) and thirteen subsidiaries i.e. Elektrownia Pątnów II sp. z o.o., PAK – Volt SA, PAK Kopalnia Węgla Brunatnego Adamów SA (hereinafter referred to as the “PAK KWB Adamów SA”), PAK Kopalnia Węgla Brunatnego Konin SA (hereinafter referred to as the “PAK KWB Konin SA”), Przedsiębiorstwo Remontowe PAK SERWIS sp. z o.o. (hereinafter referred to as the “PAK SERWIS sp. z o.o.”), PAK Górnictwo sp. z o.o., PAK – HOLDCO sp. z o.o., PAK Infrastruktura sp. z o.o., PAK Adamów sp. z o.o., EL PAK Serwis sp. z o.o. in liquidation, Aquakon sp. z o.o. in liquidation, Eko-Surowce sp. z o.o. in liquidation, Energoinwest SERWIS sp. z o.o. in liquidation. All the above-mentioned companies are consolidated.

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The companies of the biggest importance for the Group due to their scale of activity are: ZE PAK SA, dealing with production of electricity and heat, Elektrownia Pańków II sp. z o.o., dealing with production of electricity, and PAK KWB Adamów SA and PAK KWB Konin SA, dealing with lignite mining. In addition to companies from the aforementioned main areas of activity, the Group also includes other companies that deal, among others, with the execution of construction and assembly works, maintenance works, service, production and trade activities aimed at satisfying the needs and comprehensive industry service.

The production facilities of the Group include three lignite-fired power plants located in the central part of Poland in Wielkopolskie voivodship. These are: Pańków II – equipped with a supercritical power unit, Pańków I and Konin – equipped additionally with power unit with a boiler dedicated to biomass firing. Total installed gross power output of the production facilities as at the date of this report is 1896 MW.

The Group's main mining assets are concentrated in two companies: PAK KWB Konin, which currently operates on Józwin, Tomisławice and Drzewce open casts, PAK KWB Adamów operating on Adamów open cast.

Majority of the Group's sales revenue is derived from sale of electricity. This is supplemented by revenues from sale of heat, contracts for construction repair services and certificates of Energy origin.—An additional source of sales revenues, depending on the level of production costs, energy prices on the market and production volume, are revenues from the termination of long-term contracts (Power Purchase Agreements) for the sale of electricity, generated by Elektrownia Pańków II sp. z o.o. The Group, having lignite mines in its structure, provides power plants with an access to uninterrupted lignite supplies for own production installations located in the immediate vicinity of the mines. The vertically integrated Group enables optimization of coal inventories and supplies by coordinating coal mining with the demand for this fuel. The demand for biomass is covered on the basis of contracts concluded with suppliers.

The structure of ZE PAK SA Group as at December, 31 2017 is presented at Picture 1.

Apart from the Capital Group, the Company owns shares in Zakłady Pomiarowo-Badawcze Energetyki Energopomiar sp. z o.o. with headquarters in Gliwice and providing measurement, research and consultancy services regarding, among others power engineering. ZE PAK SA holds one share in the aforementioned company with the value of PLN 151 201.01, which constitutes 2.81% of the total capital.

The main shareholder makes the Group affiliated with other entities, in which Zygmunt Solorz holds substantial direct or indirect share.

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Picture 1: Structure of the Group as of December, 31 2017

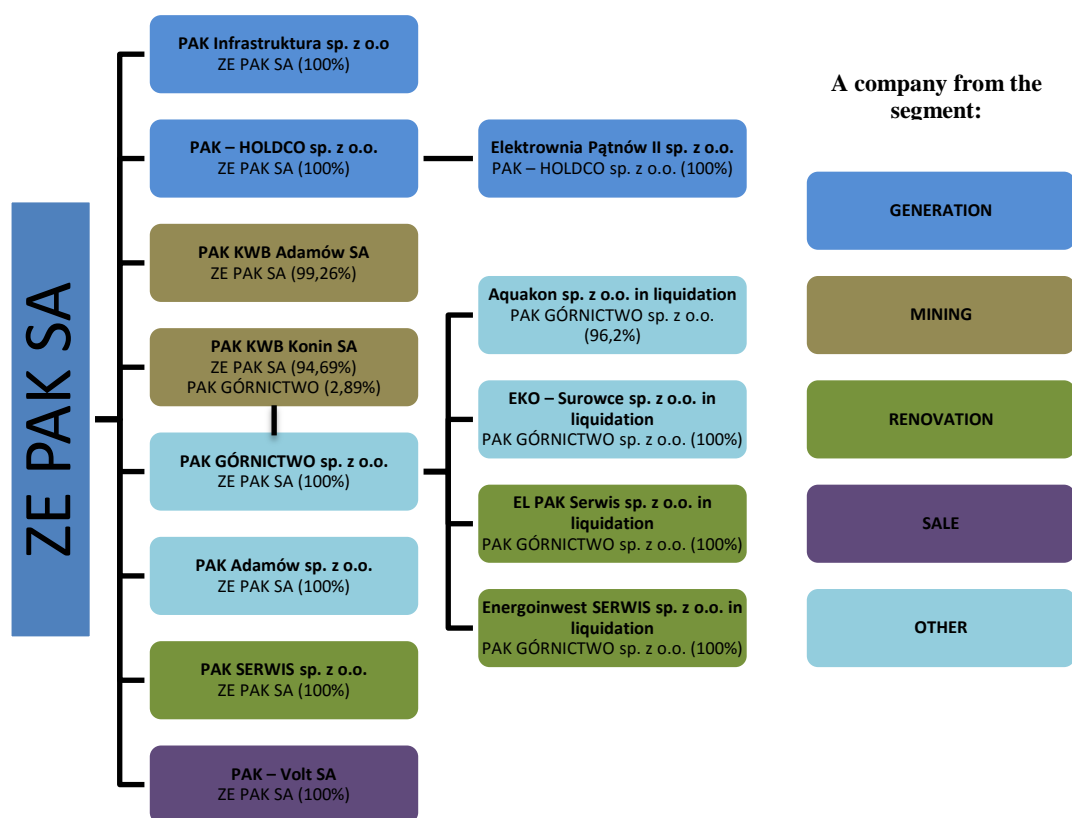


Table 1: Description of the Group's companies (excluding ZE PAK SA)

Entity	Registered office	Scope of operations	Group's share in the capital in %	
			31.12.2017	31.12.2016
„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 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%
Przedsiębiorstwo Remontowe „PAK SERWIS” sp. z o.o.	62-510 Konin ul. Przemysłowa 158	Construction and repair services	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%
PAK – Volt SA	00-834 Warszawa ul. Pańska 77/79	Trade of electricity	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 Adamów sp. z o.o.	62-510 Konin Ul. Kazimierska 45	Buying and selling real estate	100.00%	-
„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%*
Energoinvest Serwis	62-510 Konin	Repair-construction service	100.00%*	100.00%*

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sp. z o.o. in liquidation	ul. Spółdzielców 3			
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%*

* *Entities with partial or total indirect share via other companies from ZE PAK Group.*

2.2. Basic rules and changes to basic rules of ZE PAK SA Capital Group management

In order to provide appropriate solutions for key issues related to management of the Capital Group, in which ZE PAK SA is the parent company and, at the same time, the owner of capital, seeking a satisfactory return on the funds engaged, a separate Legal and Organizational Department was established within the organizational structure of the Company. The main task of this Department is supervision over the operations of the ZE PAK Capital Group and other companies in which the Company holds shares. This unit coordinates the consistency of the operations of all entities in the Group and monitors their compliance with the legal regulations in force as well as the interests of the whole Capital Group. The Department is subject to direct sovereignty of Vice President of the Management Board involved in Corporation issues.

According to the policy of the Group, in the key subsidiaries, the members of the Management Boards ZE PAK SA are Members of these companies Management Boards, and in other companies of the Group are members of the Supervisory Boards. In addition, in order to ensure proper functioning of the corporate governance body, the Management Board of ZE PAK SA recommends to the Supervisory Board of ZE PAK SA, the candidature of other Supervisory Board members of the Group companies.

In the organizational structure of the Company, organizational division units that bring together organizational units of the Company (departments, offices, divisions, etc.) managed by individual members of the Management Board of ZE PAK SA are created. The Supervisory Board divides internally the competencies among the members of the Management Board by entrusting a Management Board member with a specific organizational division unit. The members of the Management Board of ZE PAK SA co-operate, agree, and coordinate the actions regarding the Company's matters as well as secure proper co-operation of the organizational division units and units managed by them. The areas of the Company's activity managed by individual members of the Management Board are defined by the Company's organizational regulations specifying the Company's organization of the enterprise.

In the past year the following changes in the Group's structure have been recorded:

- As a result of the repurchase process of a part of shares from eligible employees and the transfer of shares of bought back shares from the State Treasury, the share of companies from ZE PAK SA in PAK KWB Konin SA shareholding increased to 97.58% and in PAK KWB Adamów SA up to 99.26%.

- On May 9th, 2017 PAK Górnictwo sp. z o.o. signed agreements with PAK KWB Konin SA, PAK Serwis sp. z o.o. an EL PAK sp. z o.o. as a result of which this company 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 these four acquired companies adopted resolutions on the dissolution of companies and the opening of 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. This change in the Group's structure is also a consequence of the consolidation of auxiliary activities to the Group's main segments.

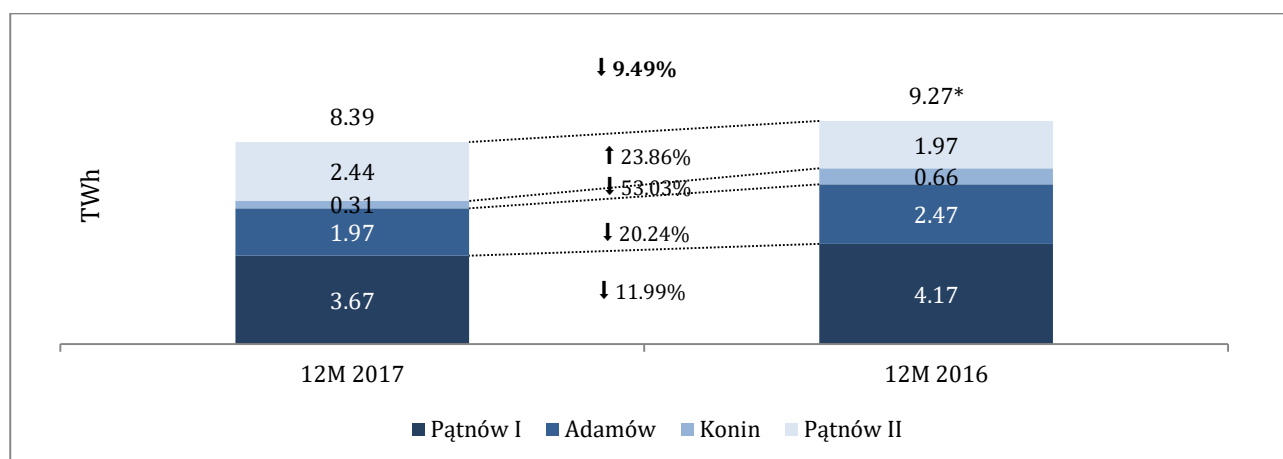
- On 16 October 2017 a new subsidiary has been set up – PAK Adamów Sp. z o.o., in which ZE PAK SA holds all the shares. The appointment of the new subsidiary company is related to preparation of the processes of terminating the activity of Elektrownia Adamów.

2.3. Basic products, goods, services, markets and sources of supply characteristics

The Company's operations are focused in several areas. The main area is doubtlessly generation of electricity, lignite extraction, electricity wholesale trading, which is supplemented by sales of energy certificates, operations undertaken to ensure an adequate amount of CO2 allowances as well as generation and sales of heat. In addition, the Group also includes other companies, which are engaged, among others, in: carrying out construction and assembly works, maintenance works, services, production and trade operations for the purpose of satisfying their own needs as well as providing comprehensive services to the industry. In 2017, the Group mainly conducted its operations in the Polish market. The only exception included operations related to transactions regarding the CO2 allowances, which were executed between ZE PAK and EPII as well as foreign partners.

The Group is the fourth largest producer of electricity in Poland and bases its production mainly on lignite. The net electricity production in Pałnów I power plant in 2017 reached 3.67 TWh, in Adamów power plant 1.97 TWh, in Konin power plant 0.31 TWh and in Pałnów II power plant 2.44 TWh. Total net energy production in all power plants of the Group in 2017 was lower by 9.49% compared to the previous year. In ZE PAK SA Group, the distribution of generations in individual power plants is primarily determined by the economics of production, operator requirements and geological conditions in the mines supplying coal to the power plant.

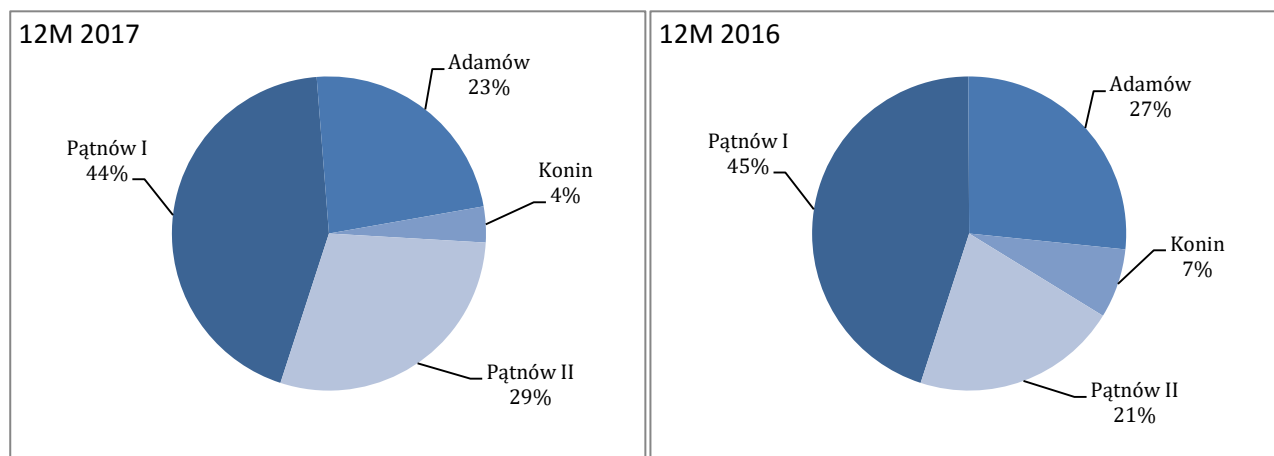
Chart 1: Net electricity production*



* Net electricity production together with the electricity production from the units 1 and 2 in Pałnów I during investment in I quarter 2016 in the amount of 0.03 TWh.

Source: internal data

Chart 1: The structure of production divided into individual power plants

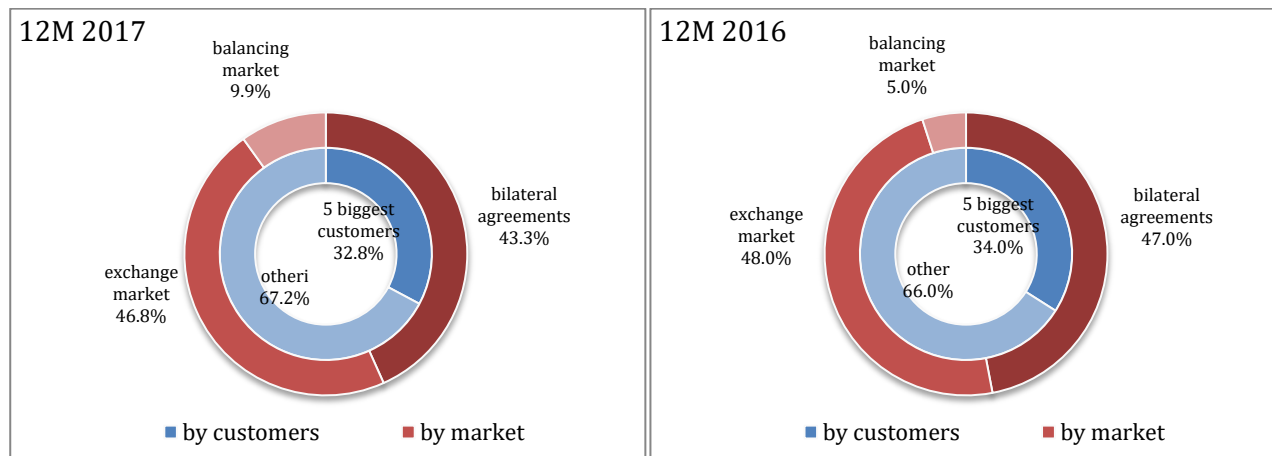


Source: Internal data

In 2017, the Group sold 11.76 TWh of electricity, i.e. nearly 12.95% less than in 2016.

The main direction of electricity sales in 2017 was sales on the stock market, which accounted for 46.8% of the total volume of energy sold¹. As part of bilateral contracts concluded mainly with electricity trading companies operating on the Polish market, the Group's companies sold 43.3% of the yearly energy sales volume realized in 2017, of which the Group's five largest counterparties accounted for 32.8% of total sales, while transactions with final customers accounted for 3.0% of the total volume of electricity sales. The structure of sales is supplemented with the electricity balancing market, where the Group companies sold 9.9% of the total volume of electricity sales last year.

Chart 2: Electricity sale structure by customers (internal ring) and by market (external ring)



Source: internal data

Revenues from the sale of electricity (total - generated and from turnover, reduced by excise duty) accounted for 85.56% of the total revenues from the sale of the Group, while revenues from the received compensations to cover the so-called "Stranded costs" in Elektrownia Pątnów II constituted 7.42% of the Group's sales revenues.

The heat generated in the Group's power plants is sold to local customers. The main customers are city heat energy enterprises and local industrial producers. In 2017, the Group covered almost the entire heat demand of municipal thermal energy companies in Konin and Turek. Last year, the Group's power plants sold 1,912 TJ of heat. Heat sales accounted for approximately 2.34% of the Group's total sales revenues.

In 2017, revenues from the sale of rights of origin were exceptionally low compared to previous years. The low revenues from this source were mainly caused by the very slight production of energy from the biomass block. The continuing trend of low prices of green certificates, constituting a support system, among others for producers of energy from biomass, caused a decision about a significant decrease in production of energy from this source. The company sold some of the certificates received for the previous periods, however their market price was usually lower than the one at which they were booked at the time of manufacture. The sale of red certificates related to energy and heat production in cogeneration determined the positive balance of revenues from the sale of property rights. In 2017, the Group generated 0.15 TWh of red certificates. The share of revenues from the sale of property rights from energy certificates of origin in 2017 accounted for only 0.03% of the total revenue of the Group.

From significant sources supplementing the revenue structure, it is worth mentioning the activities related to the execution of construction and assembly works. PAK Serwis sp. z o. o., one of the Group's companies, deals with the implementation of such tasks for the needs of the Group and external entities. The main external customers are entities from the industrial construction sector and the electricity generation and distribution sector. Revenues obtained from this service provided to external entities in 2017, accounted for 3.39% of the total revenue of the Group's sales. The remaining activity generated 1.26% of total revenues in the previous year.

¹ Elektrownia Pątnów II sp. z o. o., as an electricity producer entitled to receive compensations to cover the so-called "stranded costs" under the term of "the Act 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," in accordance with the provisions of the Energy Law, is obliged to sell the entire generated electricity on the exchange market or by way of an open tender. However, by decision of the President of the Energy Regulatory Office, Elektrownia Pątnów II sp. z o. o. has been exempted from the obligation of public sale in relation to 60% of the net electricity generated by the Pątnów II Power Plant until the end of 2019.

The main raw material used by the Group for energy production is lignite, which is extracted almost exclusively for the needs of the power plant. This is mainly due to the fact that lignite coal extracted in Poland is soft coal, and its long-distance transport is not viable due to its high water content. The extracted lignite coal is delivered directly from open pit mines to nearby power plants. For this reason, lignite mining in the ZE PAK SA Group is closely correlated with the amount of electricity generated by power plants located in the vicinity of the mines.

Practically, the whole amount of coal mined in both mines is delivered to the power plants of the ZE PAK SA Capital Group; an insignificant amount (less than 1%) is used for the needs of the mines or sold to other recipients.

In the Group, biomass is also used as a raw material for energy production – it is burned in a boiler dedicated to this purpose and located in Elektrownia Konin. However, last year, as a result of unfavourable trends on the green certificates market, production from the biomass block was stopped.

3. DESCRIPTION OF ACTIVITIES

3.1. Significant events in the accounting year as well as events after the balance sheet date affecting the current and future activities

Significant events in the accounting year

The process of obtaining formal permits in order to launch Ościsłowo open pit

As part of the activities aimed at ensuring the raw material for the Group's generation assets, project works on prospective lignite deposits are continued. PAK KWB Konin SA carries out the activities aimed at getting all the necessary decisions and documents allowing for obtaining a permit to grant a mining concession to the company. The current activities are concentrated on Ościsłowo open pit. The planned open pit is to provide coal necessary for energy generation in Elektrownia Pątnów II and renovated blocks in Elektrownia Pątnów I. Before getting the mining concession a number of formal and legal consents as well as documents specifying the way of conducting the mining operations, its scope and impact on the surroundings of the planned investment must be obtained. An environmental decision is one of them. An institution authorized to issue an environmental decision for the project "Extraction of lignite and associated minerals from the Ościsłowo Open Pit" is Regional Director for Environmental Protection in Poznań ("RDOŚ in Poznań"). On 16 September 2015, proceedings against this authority regarding the issue of an environmental decision for Ościsłowo open pit were initiated. As part of the documentation necessary in the proceedings, inter alia, a report on the environmental impact of Ościsłowo open pit and expert opinion on the impact of the designed open-pit on uniform surface and underground waters as well as protected areas were prepared. PAK KWB Konin SA with due diligence provides data and supplements the documentation necessary for the proper conduct of the proceedings. The date of issuing the environmental decision has been postponed several times. On March, 10 2017 RDOŚ in Poznań made a decision refusing the establishment of the environmental conditions for the investment. The decision of RDOŚ in Poznań was not final and PAK KWB Konin SA appealed accordingly to the General Directorate for Environmental Protection in Warsaw within the time allowed by law. 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. In the opinion of the Management Board of the Company, there are real reasons to expect that the final decision will be positive if the solutions proposed by PAK KWB Konin SA are applied. On November 30, 2017, General Director of Environmental Protection 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 the letter of December 18, 2017 filed an objection against the abovementioned decision of RDOŚ 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 RDOŚ in Warsaw, i.e. amending the contested decision of RDOŚ in Poznań and substantive decision in this matter, and not referring the matter for reconsideration. The participant in the opposition proceedings to construct the open pit Ościsłowo also appealed to the Provincial Administrative Court. Both objections were dismissed by the WSA. The judgement was issued 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.

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

Another condition necessary for the implementation of the project is the change of the local spatial development plan in the area to be covered by the planned outcrop. Decisions in this respect are taken by the self-governments of the three communes in which the Ościsłowo deposit is planned to be exploited. In December 2016, the Minister of Agriculture issued the approval for dedicating the agricultural lands of Ślesin and Skulsk communes in the area of the construction of the Ościsłowo brown coal open pit for non-agricultural purposes. Also in December 2016, media reports on an archaeological discovery on the part of the land for the planned open pit were published. On September 26, 2017, Wielkopolski Voivodship Monument Conservator initiated administrative proceedings regarding the entry of the archaeological site "Góry stan. 24, AZP area 52-40 / 193 - a multiphase cemetery", i.e. a burial ground of cell-less funerary culture tombs from the Neolithic period and a burial mound of the Lusatian culture from the Bronze Age. The area covered by the protection and its scope may prove to be important from the perspective of the implementation of the investment. On February 9, 2018, Wielkopolska Voivodship Conservator in Poznań issued a decision on the entry of the archaeological site "Góry stan. 24, AZP area 52-40 / 193 - multiphase cemetery" in the village of Góry, gm. Wilczyn area Konin. However, this decision has not become legally binding as a result of appealing to the Minister of Culture and National Heritage by one of the parties to the proceedings. It is worth noting that in the past, on the other open pits exploited by the mines, archaeological and excavation works took place many times. PAK KWB Konin SA cooperated in the past and is going to cooperate in such cases with all relevant institutions.

Relations between the Management Board and a social side

On January 18, 2017, trade unions operating in the Company filed a letter in accordance with the Act of May 23, 1991 on the resolution of collective disputes, including demands on, inter alia, the statutory bonus, the reimbursement of unpaid contributions to the employee pension scheme and the development of a support program for employees of the Adamów power plant. The Management Board of the Company responded to requests made by trade unions, presenting its position regarding individual demands together with the appointment of relevant arguments to justify the position taken, indicating, inter alia, for the unjustified demands or consequences of regulations contained in the provisions of art. 4 of the **Act on the resolution of collective disputes regarding the inadmissibility of a collective dispute.**

On July 26, also unions operating in the mines initiated a collective dispute at PAK KWB Konin SA in response to organizational and restructuring changes carried out in the Capital Group. At present, there are 4 collective disputes in the Group between trade union organizations and the Management Boards of individual Group companies.

The end of production at Elektrownia Adamów

On January, 1st, 2018, Elektrownia Adamów, being a part of Zespół Elektrowni Państw-Adamów-Konin SA, was closed. Five power units with a capacity of 120 MW each were producing electricity for the need of National Power System as well as they were supplying heat to local customers. The power plant stopped the production due to the environmental requirements. The installation in Elektrownia Adamów used derogation from the IED Environmental Directive in the scope of 17.5 thousand working hours, beginning from January 1st, 2016. Efforts were made to extend the operation of the power plant until the depletion of local lignite deposits, nevertheless, the decision of European Commission was negative.

Majority of the staff working in Elektrownia Adamów, i.e. 120 employees signed agreements regulating the end of their work in ZE PAK SA. About 25 people are still employed at Elektrownia Adamów to handle technical processes that will have to be sustained for some time. 33 employees have been transferred to other power plants of the Group - these are mainly people who due to the approaching time of acquiring pension rights are in the so-called "Protective period". The remaining group of about 60 employees did not use the possibility to sign the agreement voluntarily or as a result of failure to meet the conditions required in the offered agreement.

Significant events after the balance sheet date

In the period after the balance sheet date no significant events for the Group's operation were identified.

3.2. Significant agreements concluded in the accounting year

Significant agreements for the Group's activity

Because of the characteristics of the activity and the market, in which the ZE PAK SA Capital Group operates, the basic agreements concluded with main suppliers and recipients in the course of usual activities are of a standard nature. The agreements of the supply of the main raw material, which is brown coal, are of a multiannual nature and the suppliers are subsidiaries of ZE PAK SA. In the area of the electricity sales and purchase of CO₂ emission allowances, the Group's companies conclude framework agreements with particular counterparts setting out the basic terms and

conditions of cooperation. Whereas purchase/sale alone are executed in separate transactions in relation to specific quantities using current market prices.

Agreements regarding the obtained credits and loans

In 2017, ZE PAK SA Group's companies signed the following agreements regarding credits and loans:

1. Elektrownia Pańków II sp. z o.o. signed an annex to the syndicated loan agreement for EUR 240 million dated 14 January 2011 and the agreements on the bank accounts dated 14 January 2011. On the basis of the Annex, the amount of held reserves securing the repayment of debt was reduced and currency hedging transactions were permitted. The Parties to the annex were: Elektrownia Pańków II sp. z o.o., ZE PAK SA, PAK-Holdco sp. z o.o. and PEKAO SA, mBank SA and Bank EBRD.
2. PAK KWB Konin SA signed Annex No. 6 with Alior Bank SA extending the repayment date of the loan – multi-purpose line by 29 June 2017. Available credit limit is PLN 46 700 thousand. The interest rate is based on the WIBOR 1M rate plus the bank's margin.
3. PAK KWB Konin SA signed Annex 7 with Alior Bank SA extending the repayment date of the loan - multi-purpose line until 30 May 2018 for credit products and until 31 December 2018 for guarantee products. The available credit limit has been increased to PLN 76 700 thousand and divided into a sublimit for overdraft facility up to PLN 66 700 thousand and a sublimit for guarantees up to PLN 10 000 thousand. The interest rate on the overdraft facility is based on the WIBOR 1M rate plus the bank's margin.
4. PAK KWB Konin SA signed Annex No. 10 with Bank Zachodni WBK SA extending the repayment date of the loan by 30 June 2018. The available credit limit for financing current business operations is PLN 50 000 thousand. The interest rate is based on the WIBOR 1M rate plus the bank's margin.
5. PAK KWB Konin SA signed Annex No. 2 to the contract for bonds with PKO BP, extending the program until December 31, 2019.
6. PAK SERWIS sp. o.o. signed annexes No. 5 and 6 with PEKAO SA to the multi-purpose credit limit agreement extending the term of the agreement until November 30, 2018. The multi-purpose credit limit available is PLN 20 000 thousand. The interest rate is based on the WIBOR 1M rate plus the bank's margin.
7. PAK SERWIS sp. o.o. signed a debt limit agreement with Raiffeisen Bank Polska SA The validity period for the overdraft facility is July 31, 2018, for the revolving loan - November 15, 2018. The available limit is: PLN 5 000 thousand for all overdrafts, revolving loans, guarantees in zloty and other currencies, the maximum limit for guarantees is PLN 4 152 thousand.

Agreements regarding the granted loans

On 19 and 27 April 2017 PAK Infrastruktura sp. o.o. from ZE PAK SA Capital Group signed two loan agreements for another company from the Group, i.e. Energoinwest Serwis sp. o.o. The amount of each loan was PLN 1 500 thousand. The loans are to be repaid in instalments, the final repayment date of both loans is 30 April 2022. The loan interest rate was determined on market terms. In connection with the takeover of Energoinwest Serwis sp. o.o. through PAK Górnictwo sp. o.o. obligations resulting from loan agreements have been transferred to PAK Górnictwo sp. o.o.

Granted and obtained guaranties and sureties

Table 2: List of guaranties and sureties granted in 2017

	<i>zloty thousand</i>	<i>euro thousand</i>
	<i>31 December 2017</i>	
Granted guaranties	10 357	201
- for companies from the Group		
Granted sureties	50 000	-
- for companies from the Group	50 000	-

Table 3: List of guaranties and sureties obtained in 2017

	zloty thousand	euro thousand
	31 December 2017	
Obtained guaranties	25 469	5 167
- from companies from the Group	-	-
Obtained sureties	50 000	-
- from companies from the Group	50 000	-

The agreement concluded between affiliated companies on terms different from market terms

In 2017, in the ZE PAK SA Capital Group, there were no agreements concluded between affiliated companies on terms different from market terms.

3.3. Investment programme execution

Key investments during execution

Currently, ZE PAK SA Group does not implement any large investment projects. Investment activity focuses primarily on the implementation of the necessary tasks to ensure the maintenance of current efficiency and more efficient use of production and mining assets. Investment expenditures expended in 2017 concerned the preparation and implementation of tasks necessary for the day-to-day operation.

Elektrownia Pańków

The main purpose of disbursement of the investment expenses in 2017 was to finance the continuation of modernisation of the coal handling system, which is to guarantee a process system with a large handling capacity for feeding the basic fuel to the boilers. By the end of 2017, almost the entire range of modernization of coal handling system was completed. The task of sealing the wall between the boiler room and the engine room over the modernized blocks 1 and 2 was also continued. The task is to reduce dust from the boiler room towards the engine room, improve the structural and fire safety of facilities, improve safety and hygiene aspects of crew work. In the past year, the implementation of the task consisting in reconstruction of sewage management in the engine room building of modernized units 1 and 2, whose purpose is to organize water management in the engine room building, has been started. The deadline for completion of all described tasks is planned in the first half of 2018.

Elektrownia Konin

According to the declarations, the Company started to implement a task, the effect of which is to be the possibility to produce both electricity and heat from the biomass unit at the Konin power plant. For this purpose, the contractor of the investment undertaking the task in the "turnkey" formula was selected, and in the second half of 2017 the task was commenced. The implementation of the assumed concept will enable the heating of network water fed to the city of Konin using the steam produced by the biomass block. This block will become a source of RES producing electricity for the National Power System and thermal energy for heating the city of Konin. The planned date of commissioning the modernized TG-6 turbine along with the new auxiliary systems was set for the first quarter of 2018. As part of the implementation of the above-mentioned project, the Energy Regulatory Office was also requested to change the concession for the production of electricity and heat in cogeneration for Konin power plant.

PAK KWB Konin SA i PAK KWB Adamów SA

In the mining segment, PAK KWB Konin SA, as a part of the Capital Group, carried out investment tasks on active outcrops aimed at maintaining production capacity. On Józwin, Drzewce and Tomisławice open pits there are carried out the works related to the need to build drainage systems resulting from the progress of mining operations and the need to prepare the area for future exploitation. The largest expenditures were incurred for the purchase of land on Józwin and Tomisławice pits, and the construction of a drainage and electricity supply system on these pits. At PAK KWB Adamów SA, a bulldozer designed for the reclamation of Kozmin mine was purchased.

3.4. Risk management

While conducting its operations, the Group is exposed to a series of risks, occurring actually, potentially or theoretically, existing in the industry as well as on the markets where the Group's companies operate. These are factors having their source within the Group as well as and in its environment. Taking into account the formalization of the risk-related sphere in the Group's operations, a comprehensive document was created, entitled "Risk Management Principles for the ZE PAK SA Capital Group" ("Management Principles"). The principles of Management have been developed and implemented in order to define and determine the risks limits occurring or likely to occur in the ZE PAK SA Capital Group and to determine mechanisms for minimizing risk exposure in the course of conducting operations in the energy and mining sectors and minimizing the effects of risk, which due to the specific nature of the core business of the ZE PAK SA Capital Group, cannot be completely eliminated.

The first stage was to determine the Group companies in which activities can identify risks of material importance for the operation of the entire Group, and then apply the appropriate rules of conduct. The following entities have a significant impact on the Group's core business: ZE PAK SA, Państw II sp. Z o.o., PAK KWB Konin SA, PAK KWB Adamów SA, and PAK - Volt SA. Other Group's companies do not have a direct impact on operational risks.

Business model and strategy of the Capital Group were determined within the principles mention earlier. The leading principle of the business model implemented by the Group in the area of business operations (mining, production and trade) is to maximize production and profit while respecting the principle of risk minimization. In order to achieve the business goals, the Group allows for incurring risk, but only to the extent and on the principles set out in the Management Rules. All kinds of the business risk and the situations resulting in the exposure to the risk are constantly minimized, unless the Management Rules or the Management decisions clearly allow for specific deviations. Relating to the structure of the Capital Group and organizational charts of particular subsidiaries, specific roles and scope of responsibility for decisions and activities connected with the realized strategy and market policy have been determined and extracted. A special role, strictly related to the observance and correct application of the Rules of Management, is performed by a task team, called the "Risk Management Committee", acting as an advisory and consultative body of the Management Board of ZE PAK SA. The team was appointed by the Ordinance of the President of the Management Board. The main tasks of the Risk Management Committee are identification and substantive assessment of all economic risks worth more than PLN 10 million related to the Group's business operations.

As part of risk management, the Group identified certain areas of risks related to the implementation of the assumed business objectives:

- 1) raw material risks;
- 2) production risks;
- 3) market risks and associated financial risks;
- 4) operational risks related to the operation of IT systems;
- 5) risk in the area of information security.

For each area of risk identified above, specific types of risks have been identified for a strictly specific area. The risk type has been described comprehensively, including the theoretical examples of its occurrence in the operational activity of the Group. For each type of risk, specific forms of action were also developed in order to minimize or exclude it; an appropriate measure was also assigned and, where possible, so-called "Key performance indicator", i.e. the minimum level of performance was determined.

The managers and employees of organizational units assigned to particular risk area are the subject to control, in scope of compliance with the Management Principles, in accordance with their scope of activity. The management of organizational units is responsible for correct and compliant with the Management Rules performance of tasks by subordinate units and independent positions. The Management Rules also describe the detailed process of correct reporting on the identified risk as well as how to proceed in case of identifying a violation of the principles described in the document.

According the Management Principles, the compliance with the procedures and ways of proceeding described in the document can be abandoned only after obtaining the written approval of ZE PAK SA Management Board. In such a situation a special procedure, described also in in the Management Principles, is applied.

3.5. Description of use of emission earnings

In 2017, PAK KWB Konin SA, a company subject to consolidation within the Capital Group, made nine issues of bonds - the total amount of bonds issued in 2017 amounted to PLN 130 000 thousand, the bonds were fully covered by the companies from the Group. The proceeds from the issue of bonds were used to finance the current operations of PAK KWB Konin SA.

The total amount of bonds purchased in 2017 by PAK KWB Konin SA amounted to PLN 130 000 thousand, and the entire purchase covered bonds acquired by the Group companies.

4. MAIN BUSINESS RISKS

The process of forecasting future results of Zespół Elektrowni Pątnów-Adamów- Konin SA Capital Group must include a wide range of factors, actually, potentially, or theoretically, existent in the branch and markets, in which the Group conducts its activities. These are factors which originate both from the inside of the Group as well as from its environment. In the opinion of the Board, they can be divided into factors, which occur constantly in all periods as well as those, which occur incidentally in the period, which is concerned by a given periodical report.

The most important factors with constant impact on the Group's results include the following:

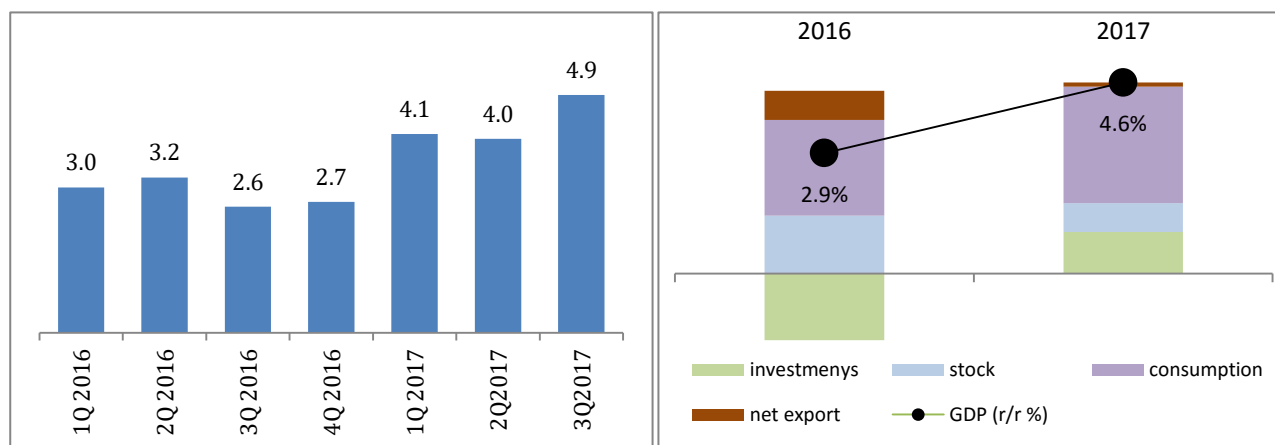
- macro-economic trends in the Polish economy and the demand for electricity;
- regulatory environment;
- electricity prices;
- prices and supply of certificates of origin;
- extraction and supply costs of coal and other fuel;
- CO₂ emission allowances costs;
- compensation for the stranded costs related to the termination of PPA of Elektrowni Pątnów II sp. z o.o.;
- seasonality and meteorological conditions;
- investment expenses; in particular, these entitling to obtain free CO₂ emission allowances;
- EUR/PLN exchange rate, the level of interest rates.

Moreover, important factor that may have a significant impact on the Group's financial results in the coming quarters are the results of the value impairment test of assets. In accordance with IAS 36, the value impairment test of assets is carried out after the occurrence of certain conditions. The last tests were carried out on 31 December 2017 and their result did not justify the change of the asset components value. The used valuation models of assets show sensitivity to a range of parameters, among others, the ones described in this section. Therefore, in the face of deterioration of the operational perspectives, both the market ones and those having its origin in the legal conditions, the assumptions for the valuation models of assets can change, and consequently the value impairment tests results may cause the necessity of verifying the value of the amount of the write-downs against the asset components. Another analysis of the reasons justifying the potential necessity to conduct the value impairment tests of the asset components will be executed at the end of the next reporting period.

Macro-economic trends in the Polish economy and the demand for electricity

While conducting activities within the territory of Poland and obtaining most revenues from the sale of electricity, it is necessary to take into consideration the macro-economic trends in the Polish economy. A very significant factor is the increase in the real GDP and industrial production in Poland, the development of the service sector as well as the increase in individual consumption. All the aforementioned factors significantly affect the demand for electricity and its consumption.

Chart 3: GDP dynamics (%) in relations to analogous quarter of the previous year and yearly GDP dynamics by components

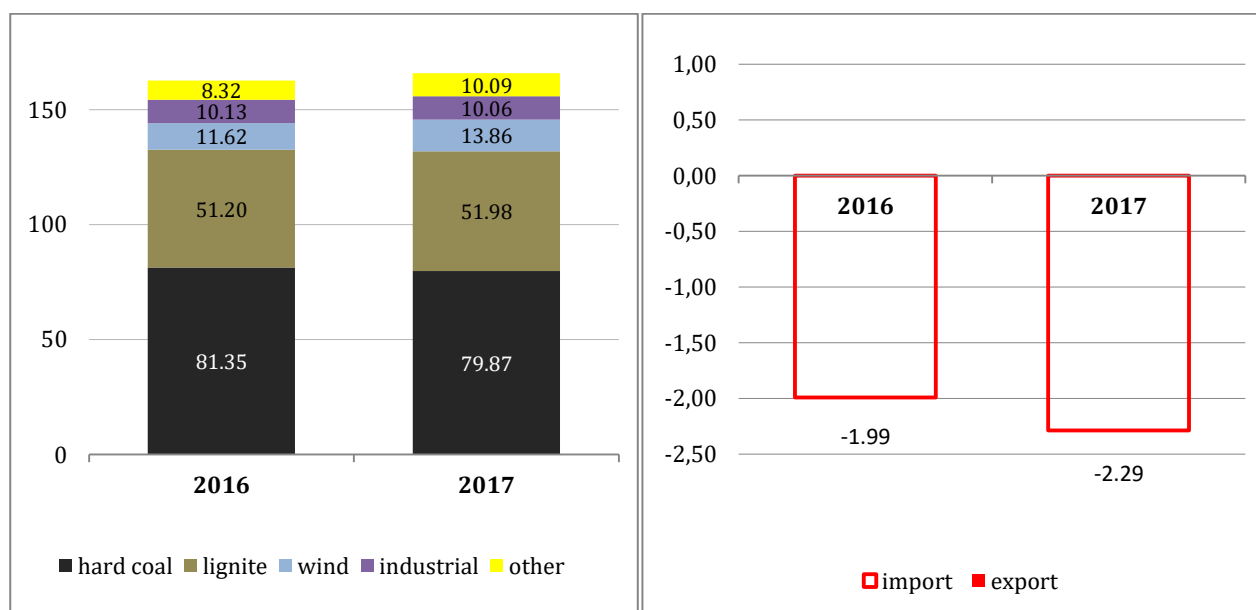


Source: GUS data

According to the initial estimates of the Central Statistical Office (GUS), gross domestic product ("GDP") calculated in fixed prices of the previous year increased in real terms in 2017 by 4.6%, compared to an increase of 2.9% in 2016. Taking into account the dynamics of GDP in the third and fourth quarter of 2017, this annual result was not a surprise. However, the first half of the year did not announce such high dynamics, also the forecasts for growth in 2017 were increasing along the following quarters. Dynamics of last year was the highest in six years (since 2011). The GDP growth in 2017 was again largely determined by consumption. Household expenditures increased by 4.8%, after an increase of 3.9% in 2016, as a result of which the contribution of consumption to the GDP growth rate amounted to 2.8%. Investments, although they increased in 2017 by 5.4%, after a breakdown of 7.9% a year earlier, their contribution to GDP growth was 1%.

The factors supporting consumer demand in 2017 remained similar as in the previous year, the most important are: a drop in the registered unemployment rate to 6.6% at the end of 2017 from 8.2% recorded at the end of 2016 and a significant increase in wages. The cumulative impact of these factors caused a demand impulse that positively influences the contribution of consumption to GDP growth in 2017. The strength of consumption in 2017 is additionally confirmed by the high base effect of the 2016 readings. In contrast to the previous year, in 2017, the component regarding fixed capital formation positively affected GDP dynamics. The increase in this component could be influenced by a certain cyclical nature of investment processes, less legislative uncertainty and the launch of investment programs by the public sector. In the case of investments, the low base effect from the previous year acted in favour of dynamics. However, it should be remembered that the low contribution of investment to GDP growth as compared to a relatively high consumption contribution may in future periods reduce the growth potential. It is worth mentioning that the impact of net exports on GDP growth in 2017 was much lower than in the previous year, which can be somehow related to the strengthening of the zloty in the second half of the year. The impact of change in inventories was positive, however, less than a year earlier.

Chart 4: Structure of electricity production and the balance of the electricity exchange with foreign countries (gross amounts) – TWh



Source: own development based on PSE data

The data concerning the functioning of the National Power System and the Balancing Market, presented by Polskie Sieci Elektroenergetyczne SA, show that the national electricity consumption² in 2017 was 168.14 TWh and increased by 2.13% in comparison to the previous year. The increase in consumption was recorded in all the months of 2017, with the exception of June and December, when slight decrease were recorded. Acceleration of the pace of economic

² Based on the Table: Structure of electricity production in domestic power plants, the amounts of exports of electricity and domestic electricity consumption – monthly and cumulative amounts from the beginning of the year – gross amounts included in PSE SA's website.

development, including the dynamics of industrial production growth and atmospheric conditions, especially in the first half of the year, influenced the energy consumption in 2017. The greatest demand for power in 2017 was recorded on 9 January at approx. 5:30 p.m., at the level of 26.231 MW³ – simultaneously, it was the highest level of demand for power in the history of National Power System. In 2017 the total electricity production increased by 1.98%. Taking into account the entire year balance sheet, there was recorded the decrease of generating energy from the main raw material (in terms of produced energy volume), i.e. the hard coal by 1.82%. The electricity production from lignite coal increased by 1.52%. **Once again, the generation of wind farms increased by 19.2% annually.** The increase in generation from wind sources resulted mainly from better wind conditions, because the increase in the reachable capacity of wind farms was much lower and in 2017 amounted to 0.67% to 5 774.3 MW⁴. In the past year, the generation of gas increased by nearly 24.16% compared to 2016. Electricity produced from hard coal accounted for 48.15% of total electricity production, energy from lignite coal 31.34% and wind turbines generated 8.35% of total energy. The direction of foreign exchange has not changed. Last year Poland was again a net electricity importer, the surplus of imports over exports amounted to 2.29 TWh.

Regulatory environment

Entities operating on the power market are subject to strict regulations, such as, e.g., the Energy Law, the act on renewable energy sources ("RES"), regulations regarding the obligation of selling a part of generated power to the public, as well as supporting defined power generation technologies, and the regulations and directives of the European Commission and international conventions, on, i.e., environmental protection and climate change (including CO₂ emissions). It is also necessary to take into consideration the regulations of the tax law as well as interpretations and recommendations issued by the Energy Regulatory Office.

On April 28, 2017, representatives of the European Union Member States voted for new standards to tighten emission standards for industry (so-called BREF / BAT), which will have a significant impact on the future of conventional power plants. Poland and several other countries were against the so-called BAT conclusions. Adaptation of large industrial installations, including those generating energy and heat, to new, more stringent emission standards for SO₂, NOX, dusts and permissible mercury levels introduced for the first time, plus the admissible average annual levels of hydrogen chloride, hydrogen fluoride and ammonia, in the absence of derogation from the conclusions BAT will be associated with expensive investments. Power generation installations will have to adapt to the new emission requirements within 4 years from the date of publication of the decision adopting the regulations, i.e. until the end of July 2021. Both the costs and the schedule of adjustment investments for installations subject to restrictions will be a huge challenge for the Polish energy system in the coming years.

The Water Law Act was adopted by the Sejm (Lower House of the Parliament) on 18 July 2017 and concluded by the President on 3 August. The provisions of the Act govern the rules of using water resources and define fees associated with using these resources. The new burden arising from the act will apply to the largest agricultural farms and the power sector, as well as the industries using large amounts of waters. Water intake up to 5k litres per day is to be free of charge. Up till now, there have been no applicable pricing systems for water for cooling purposes in thermal power plants and generation hydro plants. Under the new regulations, in the case of the power sector, the fee for using water resources shall be PLN 0.70 per m³ of the difference between the volume of underground waters consumed for these purposes and the volume of water from cooling systems of the power plants or CHPPs, introduced to the waters or the ground. Another rate applies to surface waters - it is PLN 0.35 per m³ of the difference between the volume of underground waters consumed for these purposes and the volume of water from cooling systems of the power plants. The rate for the so-called cooling waters, coming from cooling systems of the power plants, which are, e.g., later sent to rivers, shall be: PLN 0.68 if the water temperature is above 26 degrees Celsius and does not exceed 32 degrees; PLN 1.36 if it is higher than 32 degrees and does not exceed 35 degrees; PLN 4.24 if it exceeds 35 degrees. According to a declaration from the Ministry of Environment, passing the new law will enable meeting the prerequisites of the EU Water Framework Directive. The provisions of the revised law entered into force at the beginning of 2018.

On 14 August 2017, the Polish President signed an amendment to the Act on renewable energy sources. A major change in the new regulations is the withdrawal from a fixed value of the so-called replacement fee, previously at PLN 300.03/MWh and binding it with market prices of energy certificates of origin - green certificates and blue

³ Based on the Table: Requirements run on days where there was a minimum and maximum domestic demand for power available on the PSE SA website.

⁴ Based on the Table: Balance of power at the morning rush hour of domestic demand for power in the average values of working days in a month included in PSE SA's website.

certificates. The fee is supposed to be at 125% of the weighted average price of given certificates from the previous year, but not more than PLN 300.03/MWh.

On December 29, 2017, the President signed the Power Market Act. The act regulating the functioning of the power market is one of the key legal acts for energy producers. According to the authors, this act is to ensure the profitability of construction of new power units and modernization of existing units, without which the energy system is in danger of a power deficit. Due to the age of currently operated power units, it is to be expected that in the next years, a significant part of the power plants built in the 1960s and 1970s will have to be shut down. Modernization of a part of generating units (especially 200 MW class blocks) may be a solution for the current problems, however current wholesale energy prices are not conducive to making large investment commitments associated with old repairs and construction of new units. The solution to the problem of missing resources is to be the power support mechanism. The power market introduces support in the form of additional remuneration - power payments - for generation sources for the fact that within the time specified in the contract, if necessary, for example energy shortage, will have sufficient power. So they can provide the energy they need. Such an additional source of income is to be an impulse for energy producers to willingly finance the modernization or construction of new capacities. Offers for the amount of expected remuneration for power will be selected in special auctions, which will start in December 2018. Exceptionally, three auctions should take place then - for the power in the following years: 2021, 2022, and 2023. From 2019, one auction will be held annually - for a five-year power reservation. Auctions will win the cheapest offers with maximum consideration for technological neutrality. Similarly, offers of domestic bidders will be considered, but also - at a certain level - foreign sources, as well as DSR services, i.e. limiting energy consumption and demanded power. The project assumes that the greater the investment into the generating source, the longer the power contract it can receive. Longer contracts will also be awarded to units with low CO₂ emissions and providing enough heat for municipal heating systems. On 27 February 2018, the European Council officially approved the reform of the EU Emissions Trading Scheme (EU ETS) for the period after 2020. In the opinion of their initiators, subsequent reforms of the EU ETS system, through interference with the market system model, contribute to the achievement of the assumed goals of reduction of greenhouse gas emissions by 2030. The most important proposition assumes: the total emissions ceiling is to be reduced every year by 2.2% (linear reduction factor - LRF), moreover the rate of reduction can be increased once again in 2024, after prior examination of the effectiveness of the implemented mechanisms. By the end of 2023, the number of allowances transferred to the market stability reserve (Market Stability Reserve, MSR) is expected to double temporarily, and in 2023 a new mechanism limiting the validity of allowances in the market stability reserve to a certain level will enter into force. After the reform, MSR is to absorb up to 24% of the excess of emission allowances every year for the first four years of the reformed system. The provisions of the new EU ETS Directive are to be regularly reviewed. The Council's decision closes the legislative process on the new EU ETS directive. The next step is publication in the EU official journal. The new regulations will come into force after 20 days.

Electricity prices

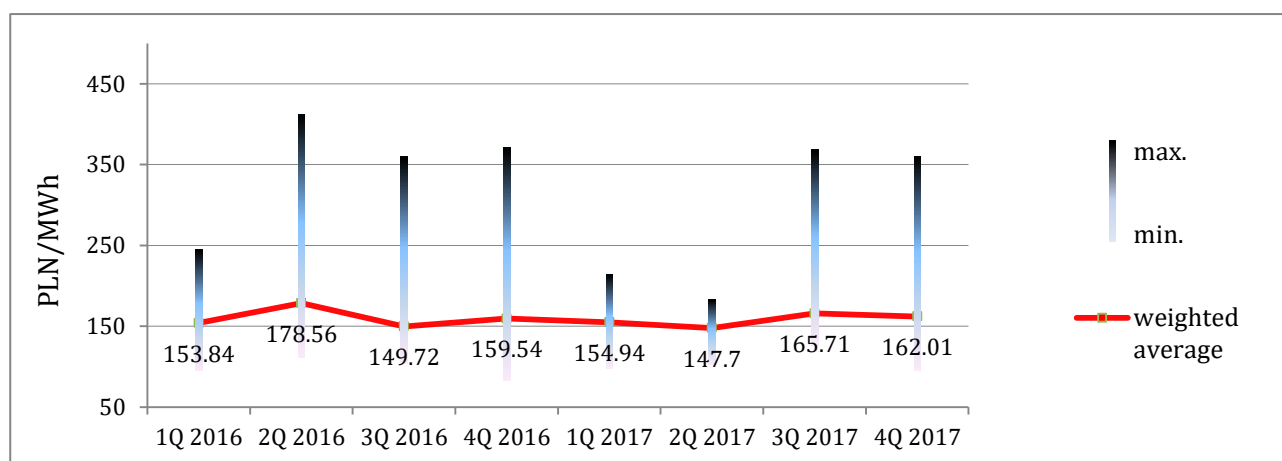
The Group generates most of its revenues from the production and sales of electricity, therefore the price for which it sells electricity is very important for the results of its activities.

In 2017, the weighted average energy price decreased in relation to the previous year. The weighted average of the IRDN (Day-Ahead Market Index) on the Polish Power Exchange (PPE) for 2017 was at the level of 155.56 PLN / MWh, which means a decrease in relation to 2016 by 5.15 PLN / MWh, i.e. by 3.2%. Characteristic is the fact that only for the second quarter the weighted average price was higher in 2016 than in 2017, in the remaining quarters the 2017 quotations were higher. However, the difference in the weighted average price between the second quarter of 2016 and 2017 was exceptionally large, i.e. 30.86 PLN / MWh. It was the second quarter that was the period of increased volatility and high prices in 2016, while in 2017 it was characterized by the lowest prices and low volatility. In 2017, the second half of the year brought higher price levels and greater volatility. The factors significantly influencing the level of stock exchange quotations on the SPOT market remained the same, and the most important ones among them are: the size of wind generation, the state of the reserve in the PPS system, the volume of transmission capacities available for cross-border exchange, and weather conditions. According to PSE data, on January 9, 2017 the highest power demand in the history of the National Power System was recorded at the level of 26,231 MW. However, even such a high demand did not disturb the system operation mode and did not cause extremely high prices, because the system was well balanced in this period. The year 2017 was not characterized by such a large dynamics of the increase in installed wind power as the previous two years. At the end of 2017, in the system there was installed 5 774.3 MW⁵ of wind turbine power, which means a symbolic increase of only about 38.4 MW, but due to excellent wind conditions,

⁵ Based on the Table: Balance of power at the morning rush hour of domestic demand for power in the average values of working days in a month included in PSE SA's website

especially in the third and fourth quarter, the increase in electricity production from wind farms amounted to 19.2%⁶. It is worth noting, however, that last year the power installed in the system increased due to new conventional units. The steam and gas block in Włocławek with the power of 463 MW and the largest in Poland block for hard coal with the power of 1075 MW in Kozienice are the largest of the units that joined the National Power System in the past year. In 2018, it is expected that the works in Płock will be finalized, a 600 MW gas and steam block and possibly the first coal block in Opole (900 MW), although in this case delays in the schedule were reported. Another factor that influenced the market prices of electricity in the past year, especially in the second half of it, was the increase in the prices of raw materials, including hard coal, the main raw material used to produce energy in Poland, and the increase in prices for CO2 emission permits. Despite the fact that last year coal prices in Poland did not grow as dynamically as on global markets, in 2017 on the basis of the Polish Energy Market Index in sales to the professional and industrial power industry there was an increase by almost 12%⁷. In the second half of the year, the price of CO2 emission allowances also increased (more detailed discussion under "CO2 allowances costs" below). It was these two factors mentioned above that probably caused an increase in electricity prices in the second half of 2017. The highest quarterly weighted average price in 2017 was reported in the third quarter at 165.71 PLN / MWh.

Chart 5: Energy prices (IRDN)



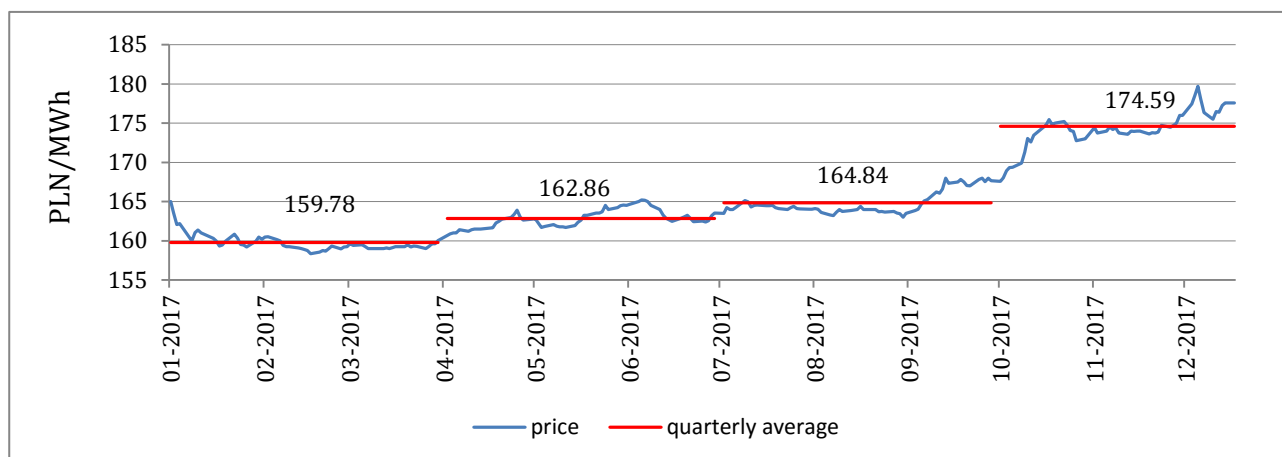
Source: Own elaboration based on TGE data

On the forward electricity market of the Polish Power Exchange, the most liquid instrument, the annual BASE_Y-18 contract, with time passed was recorded at increasingly higher levels. The highest dynamics of growth could be observed at the turn of the third and fourth quarter. It is easy to notice a certain correlation with the spot market, where also higher levels were observed in the second half of the year. The factors determining the increases in both markets were similar. Higher and higher quotations of energy raw materials, including hard coal, growing quotation of emission allowances and expectations for this trend to continue in the next year.

⁶ Based on the PSE data "Structure of electricity generation in domestic power plants, the amounts of exports of electricity and domestic electricity consumption – monthly and cumulative amounts from the beginning of the year – gross amounts."

⁷ Based on the Quotations of PSCMI 1 / Q of the Polish Power Market Index 1 for sale to professional and industrial power plants available on the ARP SA website.

Chart 6: The price of the futures contract for the supply of electricity (band) for 2018



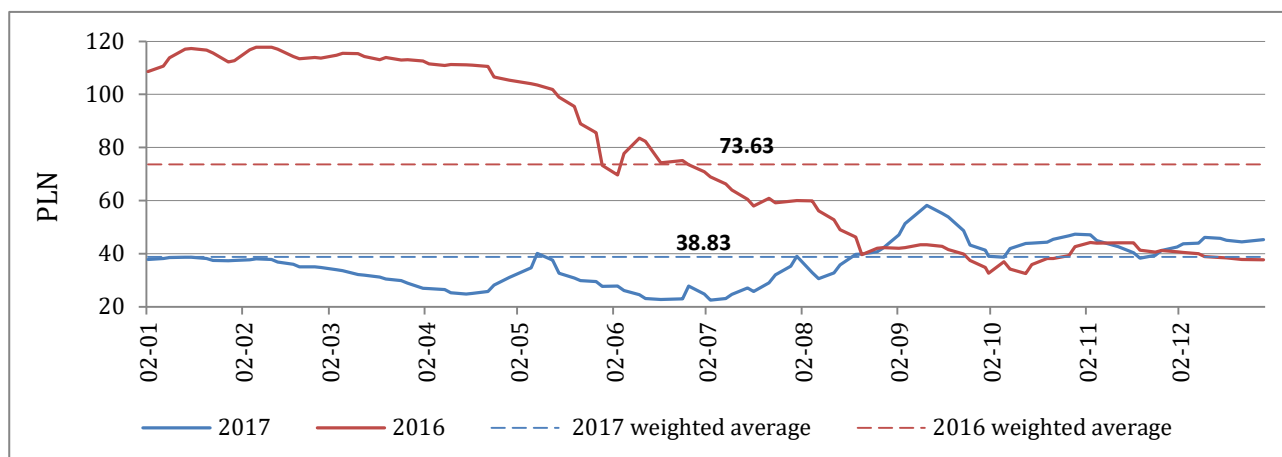
Source: Own elaboration based on TGE data

Certificates of origin

Due to the fact that one of the power units at ZE PAK SA is dedicated to combusting biomass (forest and agricultural), and in addition, the Group utilizes high-efficiency co-generation in order to generate heat, a producer is entitled to green and red certificates, provided certain regulatory requirements are met. The number of obtained certificates of origin depends on the level of generation from a given sources and is usually higher than the number, which the Company is obliged to present for redemption, which in the case of a surplus allows to sell specific volumes to other market participants. However, biomass unit generation largely depends on the green certificates market price levels. During periods, when the total generated biomass energy and green certificate prices do not ensure reaching the assumed financial effect, the generation may be decreased or halted, which also automatically decreases the amount of generated green certificates. In the case of a shortage, the certificates must be purchased on the market.

2017 year on the market of property rights resulting from certificates of origin from renewable energy was slightly different from the previous two years when quotations of green certificates were almost constantly falling. In the past year, there have been symptoms indicating a break in this lasting downward trend. While prices continued to decline until April, a rather dynamic rise was recorded in the middle of the second quarter. The price increase was admittedly short-lived, because prices soon started to fall again, setting a minimum annual listing at the level of PLN 22.46 / MWh. However, another growth impulse initiated in the third quarter has already managed to raise prices in a sustainable manner. Stopping the long-term downward trend on the green certificates market in 2017 can be combined with the expectations of market participants on legislative solutions that, in the assumption of their creators, would lead to eliminate the oversupply that has been accompanying the market for several years. There are two events worth mentioning, being important for the market in 2017. The latest amendment to the Act on Renewable Energy Sources provides that the substitute fee, which is an alternative to the redemption of green certificates of energy origin, will depend on market quotations of green certificates and its value will be equal to 125% of the weighted average market price of certificates of origin from the previous year, but no more than 300.03 PLN/MWh. In August, the Ministry of Energy announced the obligation of RES for 2018 at the level of 17.5% for energy from all renewable sources except for agricultural biogas, as well as 0.5% for energy from agricultural biogas and the obligation for 2019, for energy from all renewable sources, with the exception of agricultural biogas plants 18.5%, and the obligation for energy coming from agricultural biogas plants at the level of 0.5%. In the fourth quarter, however, declines returned to the market. The reduction of the excess number of certificates on the market was certainly not supported by the high wind generation in the third and fourth quarters, which, despite similar installed capacity, significantly increased in relation to the same period of the previous year. The average weighted price of green certificates in 2017 was at 38.83 PLN / MWh, which means a decrease of 34.8 PLN / MWh, or 47.26% compared to the weighted average price for 2016.

Chart 7: Average price of certificate of origin for RES produced energy



Source: own development based on the TGE data

Fuel costs and supplies, coal extraction costs

A fuel cost is the most important part of the costs related to the electricity and heat generation in companies of the ZE PAK SA Group. The prices of fuel largely determine the competitiveness of particular electricity production processes. The ZE PAK SA Group's power plants produce most of their electricity from brown coal, but they also use forest and agricultural biomass. Furthermore, heavy and light heating oil is used in minimum quantities for heating purposes in the process of electricity production.

Two brown coal mines, PAK KWB Konin SA and PAK KWB Adamów SA, which are the suppliers of brown coal to the ZE PAK SA Group's power plants, satisfy the demand of generation assets for this basic fuel. Therefore, the ZE PAK Group does not rely on external suppliers and eliminates the exposure to potential fluctuations of brown coal prices. Nevertheless, the Group is exposed to the fluctuations in prices of other fuels used (mainly biomass) and part of the costs related to the extraction of brown coal depends on the factors which remain outside the direct control of the Group.

The deposits exploited by the Group's mines have specified richness. The opportunity to achieve the expected level of electricity production in the long term is partially dependent on the ability of extracting from the currently exploited deposits and launching the exploitation of new brown coal deposits, which would be economically viable. As part of activities to ensure the raw material for the Group's generation assets, PAK KWB Konin executed designing works at the perspective brown coal deposits. In order to develop the perspective deposits, it is necessary to obtain all necessary formal approvals and permits, culminated with obtaining a license to extraction. The process of obtaining approvals and permits is a multi-step and stretched in time. In view of the above, there is a risk of delays and postponements in the schedule of developing subsequent deposits which, in turn, may entail risks of interruptions of coal supplies for the Group's generating assets. The opportunity to start the extraction from the prospective coal deposits in the future may be limited by many factors beyond the control of the Group. The main risk factors include: failure to obtain the necessary licenses, adverse settlements of the local government authorities in terms of shaping the special policy, lack of opportunity to obtain adequate financing

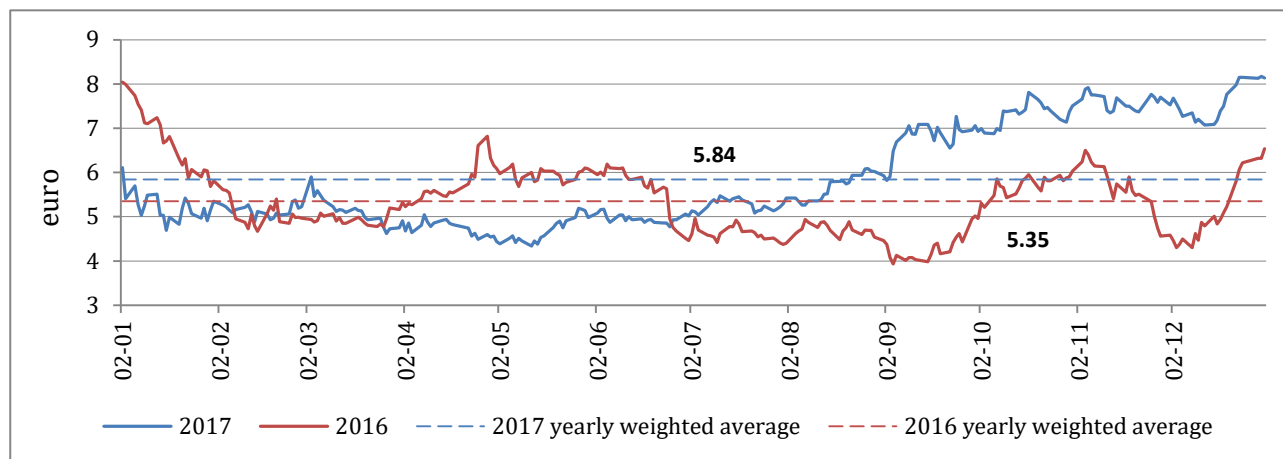
CO₂ emission allowances costs

The activities in the scope of generating electricity and heat from conventional sources are associated with the need to incur the CO₂ emission costs. In view of the fact that these costs represent an important item in the structure of the costs incurred by the producers of energy from lignite, the impact of emitted quantities of CO₂ and the price of CO₂ emission allowances (EUA) is of great importance to the activities' results. In 2017, the Group received a small amount of free CO₂ emission allowances, i.e. 83 317 EUA, resulting from the allocation for heat generation. Therefore, practically the entire volume of emission allowances needed for the ZE PAK SA Group will have to be purchased on the primary (auctions) and secondary (ICE, EEX and bilateral contracts) markets.

The course of price quotations for CO₂ emission allowances in 2017 can be divided into two periods. The first half of the year is a consolidation of quotations limited from the bottom by the minimum level of quotations in 2017, i.e. EUR 4.34. The second half of the year is a clear upward trend. The factors supporting the demand for energy from conventional sources in Europe (and thus the demand for CO₂ emission rights) were low temperatures in January, relatively high temperatures and a lower amount of precipitation in the summer. Weather conditions caused greater

intensity of use of coal-fired power plants, and thus contributed to the increase in demand for EUA. The second factor favouring the demand for EUA, especially in the first months of 2017, was the situation of the nuclear power sector in France where the announcements of the necessary withdrawal of power units caused increased demand for energy produced, among others, from coal in neighbouring countries. The third factor supporting the upward trend, especially in the second half of 2017 were purely political reasons, joint calls from representatives of the government administration of France and Germany to quickly complete work on changes to the current EU ETS CO₂ trading system, which, as a consequence, by interference in the market mechanism, would according to the authors of this plan, increase the price of emission rights. Poland as a party participating in the work on changes in the CO₂ trading system was opposed to too radical steps that could affect the price increase of emission allowances and, consequently, also of energy prices. The arithmetic average of EUA quotations in 2017 was EUR 5.84, which means an increase of EUR 0.49, i.e. 9.16% compared to the 2016 arithmetic average.

Chart 8: The price of a forward contract for the delivery of EUA



Source: Own elaboration based on ICE data

Compensation for the stranded costs related to the termination of the „Long-term Contract” („PPA”)

The long-term contract for the sale of power and electricity (PPA) was concluded between Elektrownia Pańków II sp. z o.o. and Polskie Sieci Elektroenergetyczne SA. The contract was a long-term agreement in the scope of supply of electricity according to the established price formula.

Due to the early termination (on 1 April 2008) of PPA of Elektrownia Pańków II sp. z o.o., 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, Elektrownia Pańków II sp. z o.o. is entitled to receive sufficient compensation. The amount of compensation is estimated according to an applicable formula specified in the Act. Elektrownia Pańków II sp. z o.o. is covered by the said act by the end of 2025.

Seasonality and meteorological conditions (including mainly wind conditions)

The demand for electricity and heat, especially among consumers, is subject to season fluctuation. So far, the practice showed that the consumption of electricity was higher in the winter (mainly due to low temperatures and shorter days) and lowered in the summer (due to the summer period, higher ambient temperatures, and a longer day). In the last couple of years, there is an increase in the demand for electricity in the summer, which is caused mostly by the rising number of used cooling devices and air conditioning.

Irrespective of the factors described above, meteorological conditions are becoming more and more important for the Group's production level. In the past, the operations of the Group were not subject to significant seasonality of demand, due to low costs, the work of blocks was carried out continuously (in the basis) for almost a whole year. Currently, taking into account the growing share of RES in the energy generation segment, including primarily wind sources, weather conditions are becoming more and more important in the estimation of the Group's production volume, with particular regard to wind conditions. Statistically, periods of the best wind conditions are the first and the fourth quarter. It should be taken into account that in periods when wind conditions are extremely good and the production of wind turbines is high, the demand for the Group's production may be subject to periodic reductions, similarly in periods of lower wind production can increase.

Investment expenses

Activities in the coal mining and energy production sector require significant investment expenditures. The Group's generation assets require periodic renovations and ongoing modernizations, both due to the tightening of environmental protection requirements and the need to increase the efficiency of electricity production. The level of investment outlays had a material impact, and, according to expectations, it may still have a significant impact on the results of operating activities, the level of indebtedness and cash flow. Delays in implementation, changes in the investment program and exceeding the budget may have a serious impact on future capital expenditures as well as on results, financial situation and development prospects. In addition, some of the investment projects planned by the Group, reported to the National Investment Plan, involve the allocation of free units authorizing to CO₂ emissions, however, if these investments are not implemented, the ability to use the free allocation is also prevented.

EUR/PLN exchange rate, the level of interest rates

Despite the fact that the Group conducts its activities in Poland, where it incurs costs and gains revenues in zloty, there is a couple of significant factors which make the financial results dependent on the exchange rate of EUR/PLN and the level of WIBOR and EURIBOR interest rates. The most important factors include:

- a significant part of the debt (that is the corporate credit taken by Elektrownia Państw II sp. z o.o.) is denominated in EUR, which means that the depreciation of the value of zloty in relation to EUR has negative impact on financial results, because it increases the financing costs in zloty related to the foreign currency debt, whereas the depreciation of the value of EUR in relation to zloty has positive impact on financial results, because it decreases the financial costs in zloty related to the debt in foreign currency;
- transactions connected with EUA purchase are settled in EURO;
- The company from the renovation segment periodically provides services to foreign contractors earning revenues in EUR,
- ZE PAK SA and Elektrownia Państw II sp. z o.o. use debt financing based on a variable interest rate.

In 2017, two Group's companies used instruments to limit the risk resulting from changes in foreign exchange rates. ZE PAK SA hedged the euro exchange rate for some of the 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 Państw II sp. 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. Currency risk in the case of revenues from construction services is partially offset by costs incurred in the same currency with respect to the same contracts. Management Boards monitor the financial situation and market situation on an ongoing basis, and may, if necessary, decide on the necessity of using financial instruments to hedge against exchange rate risk. In accordance with the principles applied in the ZE PAK SA Group, any transactions will be hedging and will be matched to the hedged item in terms of volume and maturity date. The decision on the choice of the hedging instrument will also include: price, market liquidity, product simplicity, ease of valuation and accounting, and flexibility. The Group's exposure to the risk caused by changes in interest rates relates primarily to long-term financial liabilities related to the financing of investments in ZE PAK SA and Elektrownia Państw II sp. Z o.o. The Group has financial liabilities, mainly loans and loans with variable interest. In order to minimize the interest rate risk, the Group has concluded interest rate swaps (interest rate swaps), under which it agrees to exchange, at specified intervals, the difference between the amount of interest accrued at a fixed and variable interest rate on the agreed principal amount. These transactions are aimed at securing the incurred financial liabilities and relate to the syndicated loan of Elektrownia Państw II sp. o.o. based on the variable EURIBOR rate. IRS instruments were used for hedging.

5. DESCRIPTION OF THE FINANCIAL AND ECONOMIC SITUATION

5.1. Principles of development of the financial statement

The Group develops the financial statements on the basis of the International Financial Reporting Standards approved by the European Union. The above standards, known collectively as International Financial Reporting Standards (IFRS), also include the International Accounting Standards (IAS) and Interpretations issued by the Standing Interpretations Committee and the International Financial Reporting Interpretations Committee.

The significant principles of accounting used in the Group's Consolidated Financial Statement are discussed in note no. 10 of the Group's Consolidated Financial Statement for 2017.

5.2. Specification of the basic economic and financial values

Consolidated profit and loss account and the consolidated income statement

Sales revenues in 2017 amounted to PLN 2 443 075 thousand and in comparison to 2016 decreased by PLN 261 636 thousand, i.e. 9.67%.

The largest drop in revenues in 2017 occurred as part of revenues from the sale of electricity. The drop in revenue from the sale of electricity from own production and from resale (minus excise duty) in 2017 compared to the previous year amounted to PLN 257 128 thousand, i.e. 10.95%. The lower volume of electricity sales resulted from both lower sales of electricity from own production and sales of electricity from trading. The volume of electricity sales from own production decreased by 0.84 TWh to 8.39 TWh, while the volume of energy from trading decreased by 0.87 TWh to 3.37 TWh. On the other hand, there was an increase in the energy sales price, calculated as revenues from energy sales (own sales, turnover and system services) divided by the sales volume, to the level of 177.78 PLN / MWh, i.e. by 2.05%. Higher sales prices achieved did not manage to offset the loss of revenues which caused a drop in volume.

Revenue from the LTC solution (long-term sale of power and electricity) in 2017 amounted to PLN 181 335 thousand (including PLN 58 303 thousand adjustment), while in 2016 it amounted to PLN 207 158 thousand (including PLN 88 353 thousand adjustment). The advances in both years were at a similar level, i.e. PLN 123 028 thousand and PLN 118 805 thousand, respectively, hence the difference in the amount of income obtained is the result of the amount of the adjustment. The adjustment for 2017 was calculated at a lower level compared to 2016 due to the company's achievement in 2017 of higher revenues from sales of energy and system services and incurring lower costs within the meaning of the Act of 29 June 2007 on the rules for covering costs incurred by generators due to the early termination of long-term contracts for the sale of power and electricity.

In 2017, lower revenues from sales of thermal energy were realized, i.e. by PLN 3 366 thousand. The decrease was caused by a lower realized sales volume by 105.85 GJ, i.e. by 5.25%.

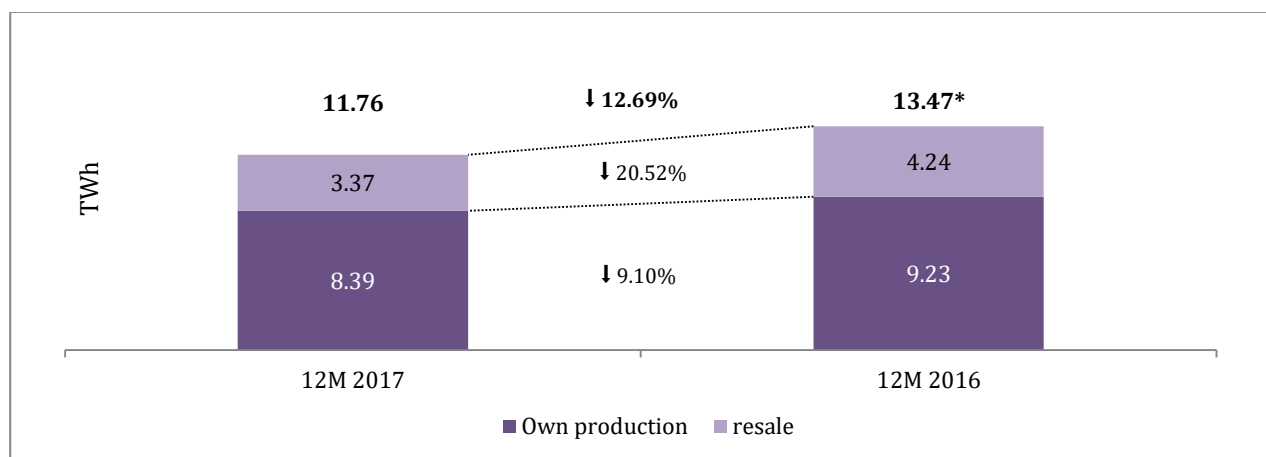
Revenues from the sale of property rights from certificates of origin in 2017 amounted to PLN 700 thousand. In 2016, PLN 812 thousand was recorded on this account. Revenues obtained from energy certificates in 2017 mainly concerned red certificates, as due to very small biomass production, the Group generated trace amounts of green certificates, additionally part of the green certificates stock was sold (in the first half of 2017) at prices lower than their prices at the end of 2016, which caused an additional cost and resulted in lowering the sales revenue.

Revenues from construction services contracts in 2017 in relation to revenues earned in the previous year increased by PLN 23 400 thousand, i.e. by 39.32%. The main reason was the increase of contractual commitment of PAK Serwis to external customers in the implementation of investments in the energy sector.

Table 4: Specification of consolidated sales revenues

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2017</i>	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Revenues from the sale of electricity from own production (reduced by excise duty)	1 510 809	1 609 762	(98 953)	(6.15)
Revenues from the sale of electricity from resale on the market	579 571	737 746	(158 175)	(21.44)
LTC compensations	181 335	207 158	(25 823)	(12.47)
Construction agreements	82 906	59 506	23 400	39.32
Heat	57 175	60 541	(3 366)	(5.56)
Property rights from certificates of origin of energy	700	812	(112)	(13.79)
Other revenues	30 579	29 186	1 393	4.77
Total	2 443 075	2 704 711	(261 636)	(9.67)

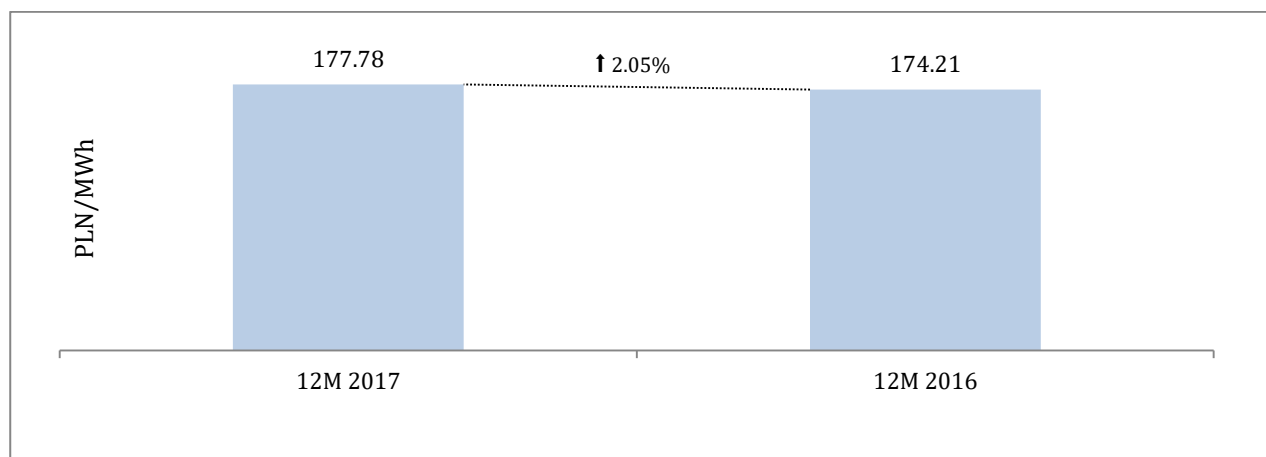
Chart 9: Sale of electricity



* In addition to the values presented in the chart, in 2016, 0.04 TWh of electricity was sold as part of the production of units 1 and 2 in Pątnów I power plant during the investment period.

Source: Internal data

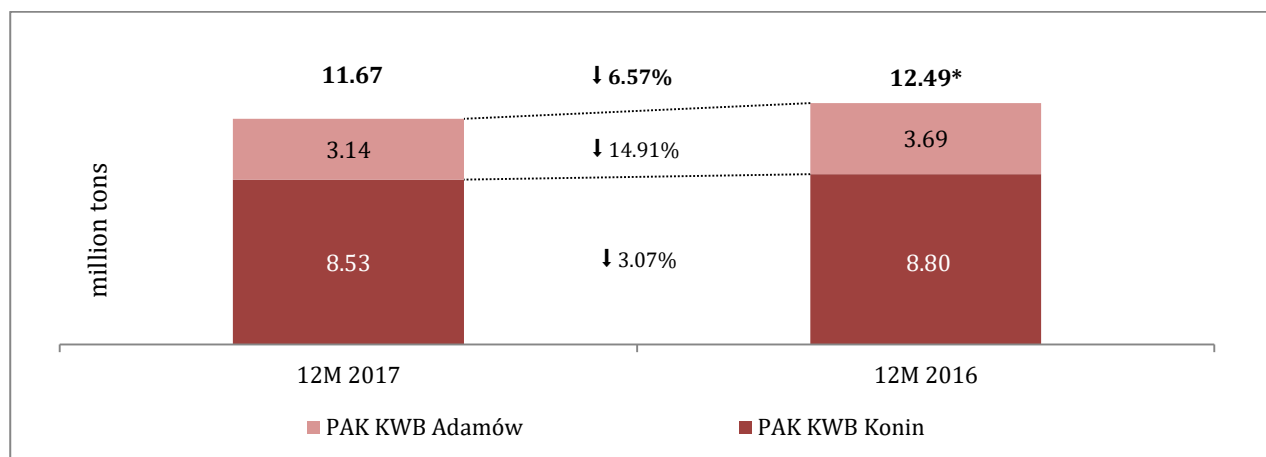
Chart 10: Average electricity prices*



* Average price, calculated as electricity sales revenues (own production with system service as from resale) divided by the sales volume.

Source: Internal data

Chart 11: Lignite consumption

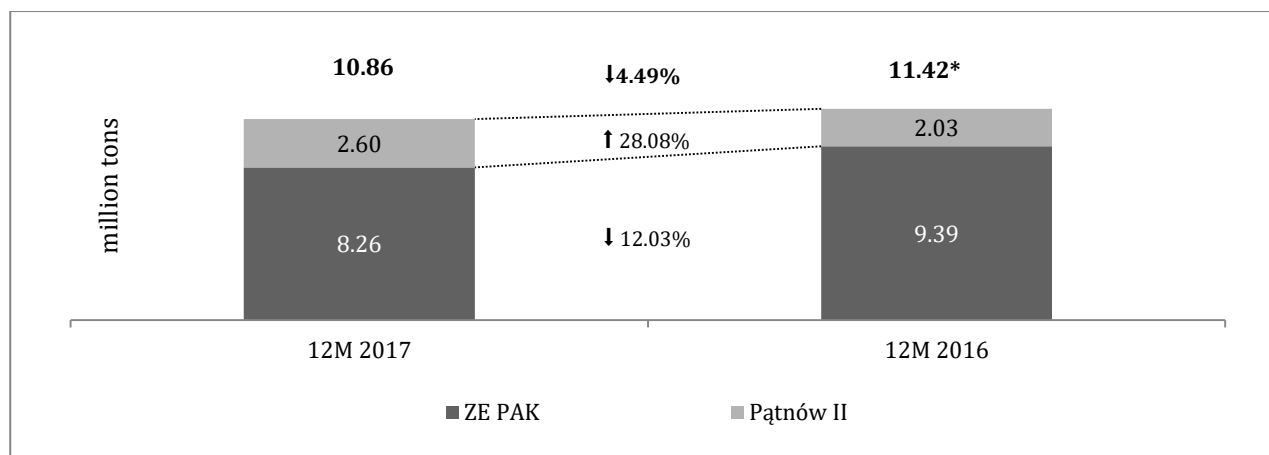


* Apart from the values presented in the chart, additionally 0.05 m tonnes of coal were consumed within 12 months of 2016 for the needs of units 1 and 2 at the Pątnów I Power Plant in the investment period.

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Source: Internal data

Chart 12: CO₂ emissions



* Apart from the values presented in the chart, additionally 0.04 m tonnes of CO₂ were emitted in the course of generation in units 1 and 2 at the Pańków I Power Plant in the investment period, within 12 months of 2016.

Source: Internal data

Table 5: Selected items from the consolidated profit and loss account

	zloty thousand 12 months period ended 31 December 2017	zloty thousand 12 months period ended 31 December 2016	zloty thousand change	%
				dynamics
Sales revenues	2 443 075	2 704 711	(261 636)	(9.67)
Cost of goods sold	(2 035 396)	(2 241 353)	205 957	(9.19)
Gross profit (loss) on sales	407 679	463 358	(55 679)	(12.02)
Other operating revenues	11 324	26 461	(15 137)	(57.20)
Selling costs	(4 258)	(4 360)	(102)	(2.34)
Administrative expenses	(119 467)	(108 634)	(10 833)	9.97
Other operating costs	(5 186)	(5 392)	206	(3.82)
Profit (loss) on operating activities	290 092	371 433	(81 341)	(21.89)
Financial revenues	16 193	9 117	7 076	77.61
Financial costs	(47 652)	(72 672)	25 020	(34.43)
Gross profit (loss)	258 633	307 878	(49 245)	(15.99)
Income tax (tax load)	(75 089)	(57 592)	(17 497)	30.38
Net profit (loss)	183 544	250 286	(66 742)	(26.66)
Net other comprehensive income	2 660	8 594	(5 934)	(69.05)
Total income for the period	186 204	258 880	(72 676)	(28.07)
EBITDA*	511 905	593 587	(81 682)	(13.76)

* The Company defines and estimates EBITDA as the profit/(loss) on operating activities (estimated as the net profit/(loss) for the accounting year corrected by the (i) income tax (tax load), (ii) financial revenues as well as (iii) financial costs) corrected by the depreciation (shown in the income statement) as well as impairment write-downs against tangible assets, intangible assets as well as mining assets.

The cost of sales in 2017 amounted to PLN 2 035 396 thousand and, as compared to the previous year, it decreased by PLN 205 957 thousand, i.e. by 9.19%.

The following factors contributed the most to the decrease in own cost: lower value of electricity purchased for trading, lower costs of materials consumption due to lower production (in particular, production from a biomass boiler) and lower employee benefits costs resulting from lower average employment in the period. In 2017, the lack of significant impairment losses on inventories also had a positive effect, which increased the cost base in 2016. The lower amortization value seen in 2017 in relation to the previous year results from the inactivation of one of the outcrops in 2016 and the ending of depreciation of the overburden in one of the mines in March, this effect would be even more

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visible, but it was partially offset by higher depreciation of the block at Pańków II Power Plant in 2017 (following the capital renovation in the 4th quarter of 2016). In 2017, a lower cost of mining damage was also recorded in other types of costs. On the other hand, higher external services were influenced by higher external services as a result of greater involvement of one of the service companies in the implementation of contracts for external customers, higher service costs (in 2016 some of these costs were activated in the overhaul component during the capital overhaul at Pańków II power plant). The costs of CO2 emissions decreased in 2017 as compared to 2016 as a result of both lower volume of energy produced and a slightly lower average unit price of emission allowances. In 2017, in comparison to the previous year, a revaluation write-down was made for fixed assets under construction, a write-down related to one of the machines at PAK KWB Adamów SA and its cause was a change in the economic prospects for mine operation following the end of Adamów power plant operation. Additionally, the amount of the cost of sales in 2017 was adversely affected by the necessity of a one-off increase in the reclamation provision, which was announced by the Company in October. Own cost of sale was charged to the part of the reserve, which related to currently exploited opencasts, while the remaining part of the reserve, concerning the areas where the operation was completed, increased general administrative costs.

The detailed analytical approach to costs by type is provided in Table 6.

Other operating revenues in 2017 amounted to PLN 11 324 thousand and were lower than in 2016 by PLN 15 137 thousand, i.e. 57.20%. In 2017, one of the companies completed the settlement of leaseback transactions, therefore the revenues resulting from the surplus of the contract value over the net value of the leased asset were settled only for a part of the year. Additionally, in 2016, provisions for, among others, coal allowance, which inflated the value of other operating income once.

Other operating expenses in 2017 amounted to PLN 5 186 thousand and their level did not differ significantly from the level from 2016.

Selling costs in 2017 amounted to PLN 4 258 thousand and were lower by PLN 102 thousand, i.e. by 2.34% on sales costs recorded in 2016.

General administrative expenses in 2017 amounted to PLN 119 467 thousand and were higher than in the previous year by PLN 10 833 thousand, i.e. by 9.97%. The increase in general administrative expenses in 2017 is to a large extent the result of classifying to this item part of the costs resulting from the increase in the reclamation provision, about which the Company informed in October. The general administrative expenses related to this part of the increase in the reserve, which refers to unexploited outcrops. The increase in general and administrative expenses also resulted from the lower base effect in 2016 due to the provision for the employee bonus in one of the companies terminated at that time. An additional factor was the inclusion of this part of employee benefits costs, which resulted from agreements concluded with the employees of Adamów power plant, which ended its activities in January 2018.

In 2017, the Group generated operating profit in the amount of PLN 290 092 thousand.

Financial revenues in 2017 amounted to PLN 16 193 thousand and were higher than those recorded in 2016 by PLN 7 076 thousand, i.e. 77.61%. The appreciation of zloty against euro in the previous year had the greatest impact on the increase in financial income due to the impact on the valuation of credit liabilities in the company Elektrownia Pańków II sp. z o.o.

Financial expenses in 2017 amounted to PLN 47 652 thousand and in comparison to the previous year decreased by PLN 25 020 thousand, i.e. 34.43%. Two reasons have contributed to the decline in financial costs: the first is the lack of exchange-rate expenses in 2017 that were recorded a year earlier, and the second reason is the lower interest expenses related to the decreasing Group debt.

In 2017, the Company generated a gross profit of PLN 258 633 thousand, which means a decrease by 15.99% compared to 2016. At the net level, the profit was PLN 183 544 thousand, by PLN 66,742 thousand, or 26.66% less than a year earlier.

Table 6: Consolidated costs by type

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2017</i>	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Depreciation	199 648	221 699	(22 051)	(9.95)
Fixed assets – write offs	22 165	455	21 710	-
Inventory – write-offs	(852)	10 188	(11 040)	-
Materials consumption	252 602	336 435	(83 833)	(24.92)

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External services	112 451	66 041	46 410	70.27
Taxes and fees excluding excise tax	201 592	204 688	(3 096)	(1.51)
CO ₂ allowances costs	289 942	311 328	(21 386)	(6.87)
Employee benefits costs	461 291	488 005	(26 714)	(5.47)
Other costs by type	39 350	48 354	(9 004)	(18.62)
Value of sold goods and materials and of sold energy purchased from trade	555 156	747 216	(192 060)	(25.70)
Total	2 133 345	2 434 409	(301 064)	(12.37)

Consolidated statement of financial position

The balance sheet total as at December 31, 2017 amounted to PLN 4 455 712 thousand and, as compared to the balance as at December 31, 2016, it decreased by PLN 345 588 thousand, i.e. by 7.20%.

Fixed assets as at 31 December 2017 amounted to PLN 3 447 776 thousand. In comparison to the last day of 2016, they decreased by PLN 254 282 thousand, i.e. by 6.87%. The biggest decrease concerned:

- the item of intangible assets, which decreased by PLN 112 603 thousand as a result of the settlement in 2017 of CO₂ emission allowances, which at the end of 2016 were classified as long-term,
- items of tangible fixed assets which decreased by PLN 110 411 thousand as a result of the difference between the amount of investment outlays and the amortization write-off in the period under consideration. Additionally, at the end of the year, a revaluation write-off was made for the value of fixed assets under construction at PAK KWB Adamów SA.

Current assets as at December 31, 2017 amounted to PLN 1 006 898 thousand. In comparison with the last day of 2016, they decreased by PLN 92 344 thousand, i.e. 8.40%. The largest change took place in the position of other short-term financial assets, which decreased by PLN 40 101 thousand. The decrease was related to changes in one of the loan agreements, which allowed the release of some of the collateral held previously in the form of deposits. The VAT receivables disclosed under other non-financial short-term assets also decreased.

Equity as at December 31, 2017 amounted to PLN 2 264 273 thousand, compared to the end of 2016 increased by PLN 120 615 thousand, i.e. by 5.63%, being the result of an increase by this part of the profit from the previous year, which was not paid in the form of a dividend and earned net profit during the current year.

Liabilities as at 31 December 2017 amounted to PLN 2 191 440 thousand, which means that during the year they decreased by PLN 466 202 thousand, i.e. by 17.54%. The biggest changes took place in the following positions:

- loans and credits, which decreased by PLN 357 771 thousand;
- trade liabilities which decreased by PLN 85 990 thousand and other short-term financial liabilities, which decreased by PLN 70 256 thousand mainly as a result of repayment of the liability of Elektrownia Pańków II sp. z o.o. related to the settlement of overpayment for compensation for terminating PPAs in previous years.

Table 7: Selected items from consolidated assets

	<i>zloty thousand</i> 31 December 2017	<i>zloty thousand</i> 31 December 2016	<i>zloty thousand</i> change	<i>%</i> dynamics
<i>Fixed assets</i>				
Tangible fixed assets	3 280 835	3 391 246	(110 411)	(3.26)
Investment property	2 365	2 337	28	1.2
Intangible assets	6 679	119 282	(112 603)	(94.40)
Assets concerning stripping and other mining assets (long-term)	72 536	80 524	(7 988)	(9.92)
Other long-term financial assets	10 311	11 945	(1 634)	(13.68)
Other long-term non-financial assets	2 122	5 726	(3 604)	(62.94)
Deferred tax assets	72 928	90 998	(18 070)	(19.86)
Total fixed assets	3 447 776	3 702 058	(254 282)	(6.87)
<i>Current assets</i>				
Short-term intangible assets	261 654	273 036	(11 382)	(4.17)
Inventory	97 758	105 296	(7 538)	(7.16)

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Deliveries and services receivables and other receivables	253 261	246 025	7 236	2.94
Income tax receivables	17 731	10 227	7 504	73.37
Derivative short-term financial instruments	-	296	(296)	(100.00)
Other short-term financial assets	35 788	77 317	(41 529)	(53.71)
Other short-term non-financial assets	11 425	28 776	(17 351)	(60.30)
Long-term contract receivables due from ordering parties	7 080	8 168	(1 088)	(13.32)
Cash and cash equivalents	322 201	350 101	(27 900)	(7.97)
Total current assets	1 006 898	1 099 242	(92 344)	(8.4)
Fixed assets classified as held for sale	1 038	-	1 038	100
TOTAL ASSETS	4 455 712	4 801 300	(345 588)	(7.20)

Table 8: Selected items from consolidated equity & liabilities

	<i>zloty thousand</i> <i>31 December 2017</i>	<i>zloty thousand</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
<i>Equity</i>				
Issued capital	101 647	101 647	-	-
Supplementary capital	1 094 493	1 028 647	65 846	6.4
Capital from the revaluation of the derivative instrument quotation	(2 678)	(7 084)	4 406	(62.20)
Other reserve capitals	3 472	3 472	-	-
Retained profits / Uncovered losses	884 095	769 302	114 793	14.92
Net profit (loss)	183 243	247 674	(64 431)	(26.01)
Equity of the majority shareholders	2 264 272	2 143 658	120 614	5.62
Total equity	2 264 273	2 143 658	120 614	5.62
<i>Long-term liabilities</i>				
Interest credits and loans	302 465	587 851	(285 386)	(48.55)
Long-term employee benefits	48 166	48 587	(421)	(0.87)
Long-term delivery and service liabilities and other financial liabilities	5 146	5 069	77	1.52
Long-term derivative financial instruments (liabilities)	870	4 294	(3 424)	(79.74)
Long-term subsidies	44 509	43 302	1 207	2.79
Other long-term provision as well as prepayments and accruals	364 852	312 253	52 599	16.84
Deferred income tax provision	432 900	388 359	44 541	11.47
Total long-term liabilities	1 198 908	1 389 715	(190 807)	(13.72)
<i>Short-term liabilities</i>				
Short-term delivery and service liabilities and other financial liabilities	146 416	302 662	(156 246)	(51.62)
Current part of interest credits and loans	349 573	421 958	(72 385)	(17.15)
Short-term derivative financial instruments (liabilities)	4 139	5 759	(1 620)	(28.13)
Other non-financial liabilities	107 387	116 431	(9 044)	(7.77)
Income tax liabilities	1 092	166	926	557.83
Short-term employee benefits	5 457	6 503	(1 046)	(16.08)
Short-term subsidies	1 507	6 670	(5 163)	(77.41)
Long-term contract receivables due to ordering parties	5 626	3 990	1 636	41.00
Other short-term provisions as well as prepayments and accruals	371 335	403 788	(32 453)	(8.04)
Total short-term liabilities	992 532	1 267 927	(275 395)	(21.72)
Total liabilities	2 191 440	2 657 642	(466 202)	(17.54)

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TOTAL equity & liabilities	4 455 712	4 801 300	(345 588)	(7.20)
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Consolidated cash flow statement

In 2017, the Group generated a positive balance of cash flows from operating activities in the amount of PLN 478 798 thousand, which was PLN 57 253 thousand lower than in the previous year. The main reasons that affected the lower balance, alongside the lower earnings, were:

- reduction of liabilities (not related to loans and credits) mainly as a result of repayment of the liability of Elektrownia Pańków II sp. z o.o. related to the settlement of overpayment for compensation for termination of PPAs in previous years,
- a smaller decrease in inventories than in the previous year mainly due to their low level because no green certificates were obtained due to lack of production from the biomass block,
- positive exchange differences as a result of the strengthening of the zloty against the euro.

The balance of cash transactions on investing activities amounted to minus PLN 57 624 thousand and, as compared to the previous year, it decreased by PLN 126 084 thousand. The decrease in the balance was mainly due to lower expenditure on the acquisition of tangible fixed assets and the release of some of the collateral previously held in the form of deposits.

The balance of cash transactions as part of financing activities amounted to minus PLN 447 250 thousand and was higher than the one recorded in the previous year by PLN 60 236 thousand. The difference was determined by the dividend paid in 2017.

Cash in 2017 decreased by PLN 26 077 thousand and at the end of the year amounted to PLN 322 570 thousand.

Table 9: Selected items from the consolidated cash flow statement

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2017</i>	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Cash flows on operating activities				
Gross profit (loss)	258 633	307 878	(49 245)	(15.99)
Item adjustments	220 165	228 173	(8 008)	(3.51)
Net cash on operating activities	478 798	536 051	(57 253)	(10.68)
Cash flows on investment activities				
Sale of tangible and intangible assets	3 478	3 723	(245)	(6.58)
Acquisition of tangible and intangible assets	(98 272)	(195 352)	97 080	(49.69)
Expenses and income related to other financial assets	1 451	7 773	(6 322)	(81.33)
Acquisition of other financial assets	35 630	-	35 630	-
Received dividends	208	60	148	246.67
Received interest	5	6	(1)	(16.67)
Other	(124)	82	(206)	-
Net cash on investment activities	(57 624)	(183 708)	126 084	(68.63)
Cash flows on financial activities				
Repayment of financial leasing liabilities	(7 012)	(15 038)	8 026	(53.37)
Credits, loans and debt stocks income	-	12 295	(12 295)	(100.00)
Repayment of credits, loan and debt stocks	(340 837)	(334 211)	(6 626)	1.98
Paid-out dividends	(65 562)	-	(65 562)	-
Paid interest	(33 373)	(48 632)	15 259	(31.38)
Other	(466)	(1 429)	962	(67.37)
Net cash on financial activities	(447 250)	(387 015)	(60 236)	15.56
Increase (decrease) in net cash and its equivalents	(26 076)	(34 672)	8 596	(24.79)
Cash opening balance	348 646	383 318	(34 672)	(9.05)
Closing cash balance	322 570	348 647	(26 077)	(7.47)

Financial indexes

The lower net profit in 2017 had a negative impact on all profitability ratios, which is particularly evident in the case of ROE in relation to the increase in equity during the year, and less in the case of other ratios due to the simultaneous decrease in assets as well as sales revenues.

The total debt ratio reflecting the ratio of liabilities to total assets once again decreased as a result of reducing the level of debt to a greater degree than the reduction in the total assets. The value of the indicator indicates that liabilities constitute 49% of owned assets.

The value of the current liquidity ratio, informing about the degree of coverage of current liabilities with short-term current assets, increased to 1.01, which means that at the end of 2017 the liquidity situation was better than at the end of the previous year.

Table 10: Indexes

		2017	2016	change	% dynamics
ROE	%	8.11	11.68	(2.02)	(17.29)
ROA	%	4.12	5.21	(0.26)	(4.99)
Net sales profitability	%	7.51	9.25	(0.14)	(1.51)
General debt index	x	0.49	0.55	(0.06)	(10.91)
Net debt / EBITDA	x	0.58	1.00	(0.42)	(42.00)
Current liquidity index	x	1.01	0.87	0.14	16.09

5.3. Specification of factors affecting the current and future financial results

The Group's financial results, as an entity focused on the generation and sale of electricity produced on the open wholesale market, are fully dependent on the behaviour of other market participants who, to a greater or lesser extent, depending on their market share, affect the level of shaped prices. Market behaviours of participants in the wholesale energy market are in turn stimulated by legislative actions in the area of broadly understood energy policy, conducted both at the national and EU level as well as at the level of the global economy.

Recently, the energy sector has experienced a number of changes, but also in the near future there is no shortage of announcements that may have a significant impact on the shape and principles of functioning of the broadly understood energy market. In this context, we can mention, for example, the current package of EU regulations, affecting current EU and national legal acts. Energy package known to participants in the energy market under the name "Clean energy for all Europeans" (Winter Package) can fundamentally affect national legislation in the energy sector. The findings related to the shape of these regulations are particularly important from the point of view of the law introducing the power market in Poland, which the Polish parliament adopted in early December 2017. The Polish power market was constructed in such a way that it would be technologically neutral and ensure the participation of domestic generators based on production on every technology, as well as entities offering power demand reduction services, as well as foreign entities. From the point of view of the Group's operations, the power market in its assumptions is a support mechanism primarily for energy companies, designed to stimulate investments in the modernization of existing units and construction of new generation units, because today's energy prices on the wholesale market are low enough that they do not provide return on capital employed in any of the available manufacturing technologies. In addition, the RES support system operating on the market, whose main beneficiary in Poland is primarily wind farms, displaces the oldest coal blocks from the market, which due to the lack of new investments in generation units centrally disposed by the Transmission System Operator ("TSO"), results in the risk of a power shortage in the National Power System ("NPS").

Therefore, when assessing the market and regulatory environment of the producer and seller of electricity, several phenomena that are particularly important in the last year should be taken into account, the effects of which may also affect the Group's results in the future:

- limitation of power increase in NPS in the wind turbines segment;
- intensified work on the project concerning the rules of the power market, concluded with the adoption of the Power Market Act;
- work on the amendment to the Act on renewable energy sources, removing collisions of the currently binding act with European law and establishing such a support system for RES, which will be fully acceptable by the European Commission;

- work on the energy strategy of Poland until 2030, which is to determine the new shape of the target energy mix for Poland, including assumptions for lignite coal mining;
- work on the new support system for Energy production in cogeneration;
- intensified work on adjusting of the wholesale energy market to MIFID II directive;
- issue by the European Commission of a Regulation on BAT conclusions, designating a 4-year adjustment period for the installation, i.e. until August 2021;
- work on the Winter Package, introducing among others new restrictions on CO2 emissions and assuming an increase in the share of renewable energy sources in electricity production;
- intensified work on the reform of the CO2 emission allowance trading system (EU ETS) after 2020;
- Poland's participation in inter-operator projects aimed at building a common European market in the "Price Coupling of Regions" model.

The Group generates the majority of revenues from generation and sale of electricity, therefore the price for which it sells electricity is very important for the results of its operations. Analysing the current market trends in the context of electricity prices on wholesale energy markets, one should take a close look at prices quoted on the Polish Power Exchange ("PPE"), which as the most transparent, form the basis for determining pricing conditions in bilateral agreements concluded on bilateral offer market (OTC market). The factors significantly influencing the level of stock exchange quotations on the SPOT market have remained the same for the past years, the most important of them are: the size of wind generation, the state of the reserve in the PPS system, the volume of transmission capacities available for cross-border exchange, and weather conditions (broader description of trends on the spot and on-time energy market, you can find in point 4 "Basic risk factors of operations - Electricity prices" of this report). A phenomenon characteristic for the past year from the point of view of price transparency is the fact that the volume of trade on TGE fell last year by 11.8% compared to 2016 (the volume of trade in electricity on the PPE in 2017 was 111.65 TWh)⁸. The probable cause can be seen in the prospect of entry into force of the so-called MIFID II package binding on the participants of the wholesale electricity market (January 3, 2018), and the lack of implementation of its provisions into the Polish legal order, which caused a lot of uncertainty to arouse the formal status of futures contracts (classification - commodity or financial instrument), concluded at PPE in 2017 and being the subject of delivery in 2018 that in the light of today's positions of both the Polish Financial Supervision Authority ("PFSA") and PPE, in the year of supply 2018, due to the delayed implementation, remains unchanged. After the entry into force of the Act on Trading in Financial Instruments implementing MIFID II to Polish law, in accordance with the provisions of the currently published bill and positions presented by PPE, it will be able to operate on unchanged terms for 12 months, during which time efforts will be made to obtain the status OTF (organized trading platform). Without the final product qualification, this will be possible only after PPE publishes the trading conditions for these instruments and the change of PPE's trading regulations (in other words after the KNF approves the market model), it is difficult to predict at this time whether and how changes in the functioning of PPE will affect level of quoted prices and liquidity of the electricity market. One of the factors that mostly determines the competitiveness of an energy company producing lignite based on coal, apart from the costs of coal and auxiliary fuels, is the price of CO2 emission rights ("EUA"), which the issuer is obliged to redeem in the amount corresponding to the volume of CO2 emissions to the atmosphere. Currently, the Company receives very small amounts of CO2 emission allowances free of charge, resulting from the allocation for heat production, therefore, virtually all the allowances needed by the Group must be purchased on the primary market (auctions) and secondary (ICE, EEX and bilateral contracts). The level of prices at which the Group acquires CO2 emission rights, was in previous years and will continue to be of great importance for the future financial results of the Group. The Emission Allowances Market is the market which is currently the most exposed to price changes caused by political decisions resulting from the directions of the debate on the shape of the reform of the European Emissions Trading System (EU ETS) lasting for several years. The main assumptions of the EU ETS reform were set by the European Council in the conclusions of October 2014. On this basis, in July 2015 the European Commission proposed a draft directive, and after a series of legislative actions in February 2018, the European Council officially approved the reform of the EU Emissions Trading Scheme for the period after 2020 (more on the approved changes in the European system of trading in allowances for EU ETS issues can be read in point 4 "Basic risk factors of operations - Regulatory environment" of this report). It should be emphasized that any changes that are supposed to affect the increase of the cost of CO2 emissions will also have an impact on raising the cost of energy production. However, not all manufacturers are equally exposed to the impact of this factor. The degree of this impact is determined by the emissivity factor of a given producer and the possible number of free emission rights, which are granted e.g. in the case of investments declared in the National Investment Plan.

⁸ PPE statement from www.tge.pl

Another factor that will undoubtedly affect the future financial results of the Group is the final determination of the shape of the Polish power market with the European Commission. The Act of 8 December 2017, adopted after a long time of intense work and expectations, was officially approved by the EC on February 9, 2018, which in its decision confirmed that the assumptions of the Polish power market are in line with EU rules on the rules for granting aid public. Revenues from the capacity market for all its participants will start only with the start of the first year of supply on the capacity market, i.e. in 2021. If the Group's generation units win power auctions, the Group will receive payments resulting from performance of power obligations as a payment for a constant readiness to supply power to the network. If the generating units belonging to the Group do not take part in the auctions or do not win the auctions, the Group still has a share in the secondary power market, where it can buy back power obligations contracted through auction by other entities. However, it should be remembered that the capacity market is not only additional payments for entities participating in it, but also financial penalties, for those who do not perform or do not fully perform contracted obligations. The effectiveness and potential of the capacity market will largely be determined by the parameters of the first auctions, which will cover not only the network demand for power, but also minimum exit prices for individual production technologies, the size of penalties, initial auction price, number of rounds and the price drop step in a particular round. The parameters for the auctions to be carried out in the last quarter of 2018 will be announced by the Ministries of Energy ("ME"), in accordance with the Act, in August 2018. Bearing in mind the above, the Group is currently preparing to participate in the capacity market and is working on the assumptions of the strategy in this respect.

In the context of the capacity market one should also mention the provisions of the Winter Package being processed by the European Commission since 2016, which consists of a number of regulations and directives, whose currently consulted provisions provide for, inter alia, introduction of a strict CO2 emission limit (EPS 550) for publicly funded electricity generators who would operate under capacity markets introduced in individual EU Member States. Conversations, so-called The "trilogue" between the European Commission, the Council of Europe and the European Parliament regarding market documents will probably start in the second half of 2018, so it can legitimately be assumed that the legislative procedure for documents comprising the Winter Package should not end before Poland's 2018 the first power auctions with deliveries for 2021-2023. However, due to the fact that the proposals for the Winter Package assume reviews of existing power mechanisms and the requirement to adapt them to the regulations included in the Winter Package, the final provisions that will be included in the package may affect the rules of the power market in Poland and other EU member states in the near future, and thus may have a large impact on the shape of the Group's operations and its future financial results.

The future shape of Poland's energy mix will be of great significance for the Group's business framework, it should be mentioned that the strategy currently being prepared by the Government is to take into account sectoral assumptions for lignite coal mining. As at the date of publication of this report, there is no official document announced by the ME of a comprehensive program for lignite mining, which is to be one of the foundations of the document for the overall energy policy of Poland until 2030. However, based on the information and statements of ME representatives, it is known that at least 50-60% of electricity will be produced from lignite and black coal and that ME assumes a development scenario and declares the emergence of new lignite opencasts, which is of particular importance for the Group due to its the prolonging process of obtaining a concession for the construction of a new lignite open pit on the Ościsłowo deposit.

5.4. Unusual events affecting the obtained financial results

The results achieved by the Group in 2017 were affected by the following one-off events:

- increase in the reclamation reserve. The provision is related to the exploitation of lignite deposits and concerns the estimated cost of reclamation of areas covered by mining operations after its completion. The basis for increasing the reserve was a report on the costs of reclamation and management of excavations and post-mining areas, prepared by an independent adviser. Preparation of documentation was commissioned due to the need to update the assumptions taken into account when estimating the costs associated with the reclamation of land used. The costs of which the established provisions relate will be borne by PAK KWB Konin SA after the exploitation of the outcrops, i.e. after 2020 and 2030 respectively. The increase in the provision had an impact on the consolidated results of the ZE PAK SA Group, i.e. the net result was reduced by PLN 37 554 thousand
- decrease in deferred tax assets charging the consolidated net result by PLN 19 385 thousand. Change in the balance of deferred tax assets results from the inability to settle them with current financial projections for PAK KWB Adamów SA.
- creation of a write-down of fixed assets under construction in the amount of PLN 22 165 thousand. The write-down results from the update of financial projections for PAK KWB Adamów SA and is related to the change in the economic perspective of the mine's operating efficiency resulting among others, from the closing of Elektrownia Adamów.

6. MANAGEMENT OF FINANCIAL ASSETS

6.1. Evaluation of financial assets management

Companies in the ZE PAK Capital Group have sufficient cash resources to conduct business operations and constantly execute both all their operational liabilities and liabilities resulting from concluded financial and investment agreements. The Group manages its current financial resources in a flexible manner by using cash liquidity analysis models and planning future cash flows on the basis of short-term and long-term financial forecasts developed periodically. By using the aforementioned tools, the Group's Companies execute current monitoring and analyses of the maturity dates of receivables and liabilities as well as adjust the deadlines and bank account balances to the amounts of cash flows. The excess cash is managed by investing in safe instruments of the financial market, which mainly include bank deposits.

6.2. Evaluation of investment plan execution

The Group has its own functioning strategy and an investment plan adjusted to it. The investment plans take into consideration the current conditions in legislation and law, as well as economy and technology. The adopted manner of execution of the planned investments is mainly based on the use of resources obtained from current operations as well as external financing. During financing planning, the Group's Companies take into consideration a series of existing or future factors which can significantly affect the executed program. The projected financing structure of particular investment plans also takes into consideration the levels of a series of financial indexes, such as the debt or liquidity index, in a way which allows obtaining their optimal levels. In the view of the ZE PAK CG, the currently adopted investment plans are possible to execute with the use of the possessed and potential resources. It is however necessary to note that the Group is constantly monitoring the factors which have the biggest impact on the executed investment program and in case of substantial changes in either one of several of them, the Group does not exclude adjustments or significant changes in the executed strategy.

7. SIGNIFICANT FACTORS AND DEVELOPMENT PROSPECTS

Directional activities designated by the Group's strategy

Directions determined by the strategy of ZE PAK SA Capital Group are determined based on a systematic analysis of a wide range of factors, such as: price trends, mechanisms supporting various technologies of electricity and heat generation, etc. and a wider view covering the dominant trends related to the Group's area of operations. The goal is to optimize investment plans in terms of material and work schedules of manufacturing devices. The obtained results allow developing a long-term model of functioning in conditions of visible unfavourable trends for coal-based energy, including threats resulting from more stringent environmental regulations, as well as anticipated changes in the energy mix of Poland.

Ecological requirements determined by EU and Polish law translate directly into the Group's production potential. According to the decisions taken, technically depleted production facilities, for which the analyses will not demonstrate the expediency of modernization, will be gradually withdrawn. The mode of operation during the transitional period must be closely matched to their capabilities by choosing a dedicated derogation.

The company is aware of changes, especially those from the legislative and legal area that occur in the environment. Legal regulations aiming at reducing CO₂ emissions, other gases (SO₂, NO_x) as well as the regulations regarding the renewable energy sector are important challenges for the Group companies. The new environmental regulations, coming from 2021 resulting from the implementation of the BAT (Best Available Technology) conclusions, expand the catalogue of limited pollutants. Conducted, in cooperation with a renowned design office, analyses allow the assessment of the necessity to undertake investment activities to obtain compliance with the requirements and scope of possible exceptions.

1) Elektrownia Adamów

A power plant covered by the derogation mechanism of a limited derogation (17 500 hours counted from January 1, 2016) on January 1, 2018 ended its operations. Documents required by law were prepared for regulatory authorities and the possibility of auxiliary economies was secured to the extent necessary. In the past year, the Company informed about the potential sale of assets related to Adamów power plant.

Another scenario considered in the context of the Adamów power plant is the return to analyses for the construction of a high-efficiency gas-steam block generating electricity in condensation with a capacity of approximately 400 MWe (block size can be optimized). However, from the current perspective, such a scenario is possible only after 2020. Current forecasts confirm that only after 2025 there may be a significant demand for energy from the designed steam and gas block. In this situation, decisions about the development of this project were suspended. ZE PAK SA investigates on an ongoing basis how far the statutory power market mechanism - approved in 2017 will ensure satisfactory conditions for investors.

2) Elektrownia Konin

At the end of last year, the termination of the contract for the supply of heat for the city of Konin was extended for 2 consecutive years, i.e. until mid-2022. The company also performed the adaptation of the biomass block as the source of the basic heat supply to the city. Currently, used for the production of heat, the carbon part, with restrictions resulting from the profitability of production, may function until mid-2020, as it has been covered by a derogatory mechanism, i.e. the Transitional National Plan. According to the current assumptions, the coal part from June 2020 to June 2022 is to be used as reserve power securing heat production based on the biomass block, in emergency situations and planned repairs with the scope of work up to 500 hours per year.

At Konin power plant, a scenario for the construction of a gas and steam unit with a capacity of approximately 120 MWe was also considered. However, due to the current low economic efficiency of the project, the Company annulled the tender for obtaining a contractor for the investment. The return to analyses is probable after 2020, taking into account other conditions for the operation of the energy industry resulting from the entries, e.g. Winter package.

3) Elektrownia Państwów

The coal assets in Państwów I power plant have been partially modernized (units 1 and 2 with a capacity of 222 MW each) and will operate at the current level of production until 2030, under the condition of the adjustment of extraction and securing adequate coal resources by PAK KWB Konin SA. In the context of coal supplies for modernized assets, the most important is the continuation of the procedure for granting a concession for extracting minerals from Ościsłowo open pit. At present, the environmental decision issue is being reconsidered by the Regional Directorate for Environmental Protection in Poznań.

Modernization of units 3 and 4, including replacement or modernization of elements decisive for block efficiency and improvement of operational safety, has been analysed, and a decision was made to withdraw the blocks without modernization. In the event of the successful conclusion of the concession procedure for Ościsłowo open pit, the company is also considering the peak work of block 5 after 2020.

According to the policy and market practice adopted by other companies in the energy sector, more investment projects are analysed and prepared than actually implemented, in the future decisions on the implementation of other projects than those mentioned above, provided for in the documents defining the Group's strategy, may be taken.

Regardless of investment plans, one of the areas of implementation of the Group's strategy is progressive integration in particular segments. Ultimately, the activities assume the existence of two main segments, i.e. the consolidated mining segment and the generation segment. In the case of ancillary activities, the Group aims at the maximum concentration of competences in order to increase the flexibility of the auxiliary segment and to optimize the management structure and cost structure. The Group strives to achieve maximum benefits through the synergy effect in the entire technological chain.

8. SPECIFICATION OF THE SHAREHOLDING STRUCTURE

8.1. Shareholding structure

As of 31 December 2017, the Company's share capital amounted to PLN 101 647 094.00 and consisted of 50 823 547 shares with a face value of zloty 2.00 each.

The below table includes the specification of shareholders holding either directly or indirectly through subsidiaries, at least 5% of the total number of votes at the General Meeting of the Company according to information held by the Company based on the notifications of purchase / sale of the Company's shares, as at December 31, 2017 and as at preparation of this report.

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*Table 11: Description of shareholders holding, either directly or indirectly through subsidiaries, at least 5% of the total number of votes at the Company's General Meeting as of 31 December 2017 and as of the day of this statement**

Shareholder	shares. Number of shares and corresponding number of votes at the General Meeting	% Share [%] in the total number of shares/votes
Zygmunt Solorz (indirectly) through:	26 200 867	51.55
– Elektrim SA	196 560	0.39
– Embud 2 sp. z o.o. S.K.A.	592 533	1.16
– Trigon XIX Fundusz Inwestycyjny Zamknięty	10 004 001	19.68
– Argumenol Investment Company Limited	15 407 773	30.32
Nationale-Nederlanden OFE	5 068 410	9.97
Towarzystwo Funduszy Inwestycyjnych PZU SA	3 081 567	6.06
OFE PZU „Złota Jesień”	2 664 378	5.24

* According to information possessed by the Company based on the delivered notices of purchase / sale of shares.

The company has no knowledge of any agreements that may result in future changes in the proportions of shares held by the current shareholders.

8.2. Acquisition of own shares

The Company did not acquire own shares in 2017.

8.3. Shares of entities from ZE PAK SA Capital Group in the possession of supervising and managing persons

The below table presents the Company's shareholdings (direct and indirect), as well as shareholdings of the management personnel of its affiliates as of 31 December 2017 and as at the date of this report.

Table 12: The ownership of the Company's shares / stocks in entities related to the Company by the management as at December 31, 2017 and as at the date of the report.

Name and surname	ZE PAK SA shares.		Affiliate shares	
	quantity	face value		quantity
Adam Kłapszta	0	0	0	0
Aneta Lato-Żuchowska	0	0	0	0
Zygmunt Artwik	0	0	0	0
Elżbieta Niebisz	0	0	0	0

The below table presents the Company's shareholdings (direct and indirect), as well as shareholdings of the supervising personnel of its affiliates as of 31 December 2015 and as at the date of this report.

Table 13: The ownership of the Company's shares / stocks in entities related to the Company by the supervising personnel as at December 31, 2017 and as at the date of the report.

Name and surname	ZE PAK SA shares.		Affiliate shares	
	quantity	face value		quantity
Tomasz Szelaąg	0	0	0	0
Henryk Sobierajski	0	0	0	0
Wojciech Piskorz	0	0	0	0
Leszek Wysłocki	0	0	0	0
Wiesław Walendziak	0	0	0	0
Ludwik Sobolewski	0	0	0	0

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Lesław Podkański	0	0	0	0
Sławomir Zakrzewski	0	0	0	0

8.4. Control of employee share option plan

The Company does not have an employee share program, therefore there is no control system of the employee share program in the Company.

9. DECLARATION OF COMPLIANCE WITH THE CORPORATE GOVERNANCE RULES

Declaration of compliance with the corporate governance rules is presented in accordance with § 91 paragraph 5 (4) of the Resolution of the Minister of Finances of February, 19, 2009 on the current and periodical information provided by issuers of stocks as well as conditions for recognizing as equivalent information required by the laws of a non-member state.

9.1. Set of corporate governance rules applied

In 2017, the Company was subject to corporate governance principles contained in the „Best Practice for WSE Listed Companies 2016” (Best Practice) adopted by resolution of the WSE Supervisory Council of October 13, 2015. Best Practice came into force on January 1, 2016.

The Management Board of the Company, within the scope of competences conferred upon it by the Statute and generally binding legal regulations, exercises due diligence in order to ensure the Company's compliance with the widest possible range of Best Practices. The number and scope of principles that the Company has not complied with are described in detail in the item below. The Management Board of the Company makes special efforts to ensure that the Company's information policy towards individual as well as institutional investors, being the implementation of the guidelines contained in the Good Practices, was in line with their expectations. Furthermore, for reasons beyond the Company's control, not all rules contained in Good Practices are applied.

The collection of Best Practices is published on the website of the Warsaw Stock Exchange at the following address:

https://static.gpw.pl/pub/files/PDF/inne/GPW_1015_17_DOBRE_PRAKTYKI_v2.pdf.

According to the Best Practice principles the Company published A statement on the company's compliance with the corporate governance recommendations and principles contained in Best Practice at the following address:

http://ri.zepak.com.pl/upload/files/PL_GPW_dobre_praktyki_PAK.pdf

9.2. Set of rules which Company has not complied with

The following are the corporate governance principles that the Company has not applied with as part of its operations in 2017, with an explanation of the position of the Company in each specified derogation.

Principle I.Z.1.20. Best Practice

A Company should operate a corporate website and publish on it, in a legible form and in a separate section, in addition to information required under the legislation: an audio or video recording of a general meeting.

Reasons for non-compliance with the principle I.Z.1.20. of Best Practice:

Taking into consideration the Company's experience, according to which most of the Company's capital share is represented in the deliberations of the general meeting as well as the fact that the recording of the course of the general meeting could be involved with substantial costs and potential difficulties of organizational, technical and legal nature, the company does not record and broadcast the course of the general meeting. In case of notification about a need of recording general meeting announced by bigger group of shareholders, the company will consider such possibility.

Recommendation IV.R.2. Best Practice

If justified by the structure of shareholders or expectations of shareholders notified to the company, and if the company is in a position to provide the technical infrastructure necessary for a general meeting to proceed efficiently using

electronic communication means, the company should enable its shareholders to participate in a general meeting using such means, in particular through:

- 1) real-life broadcast of the general meeting;
- 2) real-time bilateral communication where shareholders may take the floor during a general meeting from a location other than the general meeting;
- 3) exercise of the right to vote during a general meeting either in person or through a plenipotentiary.

Reasons for non-compliance with the recommendation IV.R.2. Best Practice:

According to the Company's assessment, current shareholders structure does not justify real-life broadcast of the general meeting and real-time bilateral communication where shareholders may take the floor during a general meeting from a location other than the general meeting. Taking into consideration the Company's experience, according to which most of the company's capital share is represented in the deliberations of the general meeting as well as the fact that the recording and broadcasting of the course of the general meeting could be involved with substantial costs and potential difficulties of organizational, technical and legal nature, the Company does not record and broadcast the course of the general meeting. So far the Company did not receive shareholder's notifications of general meeting broadcasting. In case of such a notification announced by bigger group of shareholders, the Company will consider recording and broadcasting of general meeting. Exercise of the right to vote during a general meeting either in person or through a plenipotentiary is a usual practice on general meeting of the Company. According to the Company's assessment, not in full use of above mentioned recommendation does not adversely affect the achievement of the objective described in the section IV of the code of best practices.

Principle IV.Z.2. Best Practice

If justified by the structure of shareholders, companies should ensure publicly available real-time broadcasts of general meetings.

Reasons for non-compliance with the principle IV.Z.2. Best Practice:

According to the Company's assessment, current shareholders structure does not justify real-life broadcast of the general meeting. Taking into consideration the Company's experience, according to which most of the Company's capital share is represented in the deliberations of the general meeting as well as the fact that the recording and broadcasting of the course of the general meeting could be involved with substantial costs and potential difficulties of organizational, technical and legal nature, the Company does not record and broadcast the course of the general meeting. So far the Company did not receive shareholder's notifications of general meeting broadcasting. In case of such a notification announced by bigger group of shareholders, the Company will consider recording and broadcasting of general meeting.

Recommendation VI.R.1. Best Practice

The remuneration of members of the company's governing bodies and key managers should follow the approved remuneration policy.

Reasons for non-compliance with the recommendation VI.R.1. Best Practice:

There is no comprehensive, formal remuneration policy in the Company. Remuneration of the members of the supervisory board are established by the general meeting, remuneration of the members of the management board are established by the supervisory board and there is a document in the company describing remuneration rules of the key managers. In any case such factors are taken into consideration: competence, experience, and responsibility of the position and work effects.

Recommendation VI.R.2. Best Practice:

The remuneration policy should be closely tied to the company's strategy, its short- and long-term goals, long-term interests and results, taking into account solutions necessary to avoid discrimination on whatever grounds.

Reasons for non-compliance with the recommendation VI.R.2. Best Practice:

There is no comprehensive, formal remuneration policy in the Company. However link with such factors as short- and long-term goals, long-term interests and results are taken into consideration in establishing remuneration of governing

bodies and key managers. The company does not discriminate on whatever ground in process of establishing remuneration on any position.

9.3. Description of the main characteristics of internal control and risk management systems in relation to the process of financial statement and consolidated financial statement development

The process of development of the Company's financial statements as well as the Capital Group's consolidated financial statements takes place with the use of internal control and risk management mechanisms, such as: Company's internal procedures, management mechanisms of IT systems used for registration of economic activities and development of financial statements, as well as protection mechanisms of data and systems, principles of supervision over preparation of financial statements, principles of verification and assessment of statements, the internal audit and other control elements.

The development of the Company's financial statements as well as the Group's consolidated financial statements is executed in an orderly manner, pursuant to the organizational structure of the Company and Group. The management accounting tools and IT systems implemented in the Company and Group for the purpose of registration of economic events in books of account provide the basis for the evaluation that the Company's financial statements and the Group's consolidated financial statements reliably and clearly present the Company's and Group's financial and economic situation.

The basic regulations in the scope of development of financial statements include: the Company's accounting policy in accordance with the Accounting Act of 29 September 1994, International Financial Reporting Standards ("IFRS"), approved by the European Union, the procedure of closing the books of account of companies including the Capital Group, as well as the financial statement and consolidated financial statement development requirements imposed by the Warsaw Stock Exchange.

As of the date of development of this statement, the Company did not make a decision on keeping the books of account in the Group according to the International Financial Reporting Standards ("IFRS"). Therefore, the process of development of financial statements in the Group takes place in two stages. Firstly, all the companies of the Group develop their own individual statements pursuant to the Polish accounting standards. These statements are studied if they meet the conditions specified in the Accounting Act. Then, the companies transform the individual statements on the basis of the accounting policy, determined for the Group, in accordance with the International Financial Reporting Standards ("IFRS") using the so-called sheets of transition into financial statements in the IFRS standards. Such prepared individual statements are the basis for development of the Group's consolidated financial statement. Only in case of ZE PAK SA, there is an automatic process of importing data from SAP ERP system to SAP BPC consolidation system.

The Group's consolidated statement is developed with the use of SAP BPC IT system. The separated central unit in the parent company (i.e. ZE PAK SA) merged with accounting departments in individual subsidiaries functions within the framework of the system. The consolidation process is started with the central unit opening access for companies to enter data into the system, the subsidiaries have the possibility of access to its back data at any time, but without the possibility of their adjustment. The central unit constantly monitors the entry of data by the companies, and then, after entering individual data, it starts the consolidation process. This process is based on defined business rules, which determine the content of consolidation adjustments. Furthermore, the consolidation process allows for entering manual adjustments by the central unit. The result of the consolidation process completion includes a complete package of the financial statement together with explanatory notes in Excel files, which is then exported to Word file after verification.

The Management Board is responsible for the Company's internal control system and for its effectiveness in the process of development of financial statements and periodical reports developed and published in accordance with the Regulation of the Minister of Finance dated 19 February 2009 on current and periodic information provided by issuers of securities and conditions for recognizing as equivalent to the information required by the law of a non-member state.

The substantive supervision over the process of development of the Company's and Group's financial statements and periodical reports is executed by a member of the Management Board responsible for financial issues. The organisation of works related to the development of financial statements is the responsibility of the Director of Finance who, together with the Principal Accountant, develops the work schedule including in the development of statements.

The Company's effective internal control and risk management systems related to the process of financial reporting is ensured thanks to the following aspects:

- development of procedures specifying the principles and division of responsibility in the development process of financial statements,
- specification of the scope of reporting pursuant to the mandatory provisions of the Accounting Act and International Financial Reporting Standards,
- implementation and execution of supervision over the use by the Capital Group's companies of coherent accounting principles as well as
- semi-annual inspections and annual audits of the financial statements of ZE PAK SA. and Capital Group by an independent statutory auditor.

The annual and semi-annual financial statements are subject to the independent auditing and inspection by the independent statutory auditor, who gives an opinion on the reliability and clarity of such a statement as well as correctness of books of account comprising the basis for the statement development.

The choice of a statutory auditor is made by the Supervisory Board, from a group of reputable auditing companies, which guarantee high service standards and the required independence.

The audits of financial statements are carried out:

- in accordance with the provisions of Chapter 7 of the Accounting Act of 29 September 1994,
- in accordance with the National Standards of Auditing within the meaning of the International Standards on Auditing, adopted by the resolution of the National Chamber of Statutory Auditors of 10 February 2015 as amended and the resolution of the KRBR of 7 July 2017.

In particular, the audits include verification of correctness of the accounting rules used by the Company and Group, verification of significant estimates, checking – in a random manner – of accounting evidence and records, which the amounts and information included in the financial statement result from, as well as comprehensive assessment of the financial statement.

The Company's and Group's financial results are regularly monitored during the financial year and are subject to periodical evaluation made by the Supervisory Board. During regular sessions of the Supervisory Board, the Company's Management Board provides information regarding the current financial situation of the Company and ZE PAK SA Group.

The Company's and Group's task is to develop a financial statement, including numerical data and wordy clarifications, which:

- reliably and clearly presents all information which are significant for the evaluation of the financial and economic situation for a given day, as well as the financial result for a given period,
- was properly developed in all the significant aspects, that is, in accordance with the accounting rules resulting from the International Financial Reporting Standards, as well as the related interpretations published in the form of the European Commission regulations, and according to the requirements of the Accounting Act and executive regulations issued on its basis, as well as on the basis of correctly kept books of account,
- is compliant with the regulations and provisions of the Company's Articles of Association, which affect the financial statement content.

The Company has the documentation, which describes its adopted accounting principles, specified in Article 10 of the Accounting Act. The applied principles of cost accounting, quotation of assets and liabilities as well as determination of the financial result are pursuant to the Accounting Act and the International Financial Reporting Standards.

The Management Board is responsible for the correct keeping of the Company's and Group's accounting. The Company keeps the books of account within the integrated SAP ERP IT system. This system, like the above SAP BPC consolidation system of statements, provides the division of competence, coherence of activity entries in the books, as well as control between the main book of account and the auxiliary books. The conducted registration allows determining the financial result, VAT tax, and other budget liabilities. The account registration ensures correctness and completeness of entries. The chronology of economic events is kept. Entries in the books of account reflect the actual state, and data are entered in a complete and correct manner, on the basis of accounting records qualified for entry. The continuity of entries and correctness of the applied procedures are ensured. The accounting records meet the requirements of the Accounting Act. The books of account are kept in the Company's registered office. There is a possibility to modify the system operation in order to ensure the adequacy of technical solutions to the changing accounting principles and legal standards. The system includes the documentation both in the part related to end users as well as in the technical part. The system's documentation is subject to periodical verification and updating. The Company implemented organisational and system solutions in the scope of ensuring proper use and protection of data access protection systems as well as hardware. The access to the financial registration system resources is limited with

proper entitlements, which are provided to authorized employees only in the scope of their responsibilities and activities.

The internal audit, the aim of which is to carry out independent and objective assessment of the risk management and internal control systems, functions in the Company. The internal audit is conducted on the basis of the auditing regulations. The audit executes planned and temporary auditing tasks both in the parent company as well as in the Group's companies. The audit plans are developed on the basis of the risk analyses. The audit results are reported to the Company's Management Board. Information on the internal audit activity also constitutes the subject of analyses of the Audit Committee.

As part of the control activity, the periodical management reporting is subject to evaluation in terms of presented information, especially, in the context of the analysis of deviations from the assumptions adopted in the financial plans.

9.4. Shareholders with significant blocks of shares

The below table presents the shareholders with significant blocks of shares, in accordance with the Company's knowledge, based on the notifications submitted to the Company.

*Table 14: Shareholders owning directly or indirectly significant blocks of shares in accordance with the information available to the Company based on the notifications of purchase / sale of the Company's shares, as at December 31, 2017 and as at the date of this report.**

<i>Shareholder</i>	<i>Number of shares</i>	<i>Percentage share in the share capital</i>	<i>Number of votes</i>	<i>Percentage share in the share capital</i>
Zygmunt Solorz (indirectly) through: Elektrim SA, Embud 2 sp. z o.o. S.K.A., Trigon XIX Fundusz Inwestycyjny Zamknięty, Argumenol Investment Company Limited.	26 200 867	51.55%	26 200 867	51.55%
Nationale-Nederlanden Otwarty Fundusz Emerytalny	5 068 410	9.97%	5 068 410	9.97%
Towarzystwo Funduszy Inwestycyjnych PZU SA	3 081 567	6.06%	3 081 567	6.06%
OFE PZU „Złota Jesień”	2 664 378	5.24%	2 664 378	5.24%

** according to the Company's knowledge on the basis of notifications submitted by the shareholders.*

9.5. Holders of stock giving special control rights

As of 31 December 2017 and as of the date of development of this statement, the Company has not issued stocks giving special control rights.

9.6. Limitations in the execution of the right of ballot

According to the Company's Articles of Association and other internal documents of the Company as of 31 December 2017 and as of the date of development of this report, there are no limitations regarding the execution of the right of ballot.

9.7. Limitations regarding the transfer of right of ownership of stock

As of 31 December 2017 and as of the date of development of this statement, the Company does not include any limitations regarding the transfer of right of ownership to Company's stocks.

9.8. Principles for the appointment and dismissal of management and supervisory personnel

Management Board

The Management Board is comprised of 3 to 6 members appointed for joint term. The composition of the Management Board includes: President of the Board, Vice-Presidents, as well as other members of the Board. The number of Board members and their functions are specified by the Supervisory Council. The Management Board's term is five years. The Board's President, Vice-Presidents, as well as other members are appointed and dismissed by the Supervisory Council during a secret ballot. The Board's President, Vice-Presidents, as well as other members can also be dismissed or suspended in duties during the General Meeting.

The Board administers the Company's cases and represents the Company. The Board acts pursuant to the Board's Regulations which specifically determine the Board's action mode. The Regulations are established by the Board and approved by the Supervisory Council by way of a resolution.

The Board's resolutions are required for cases exceeding common management, which especially include:

- 1) resolution and changes in the organisational regulations which specify the organisation of the Company's entrepreneurship,
- 2) contracting credits and loans,
- 3) proxy establishment,
- 4) granting credit guarantees and sureties,
- 5) acquisition and disposal of property, right of perpetual usufruct or share in property or perpetual usufruct.
- 6) decisions in cases, the value of which exceeds zloty 500 000.00. The value of transactions expressed in foreign currencies is subject to conversion according to the average exchange rate of the National Bank of Poland (NBP) of the date of resolution passing.

The Board's resolutions are also required for cases in which the Board addresses the General Meeting and the Supervisory Board.

Supervisory Board

The Supervisory Board is comprised of 5 to 14 members appointed for joint term. The Board's term is five years. The members of the Supervisory Board are appointed and dismissed during the General Meeting. The General Meeting, prior to the appointment of the Board's members for a new term, specifies the number of members of the Board. The Board appoints the President, Secretary, Vice-President or, if deemed reasonable, two Vice-Presidents, among its members in a secret ballot.

The composition of the Board should include two members who fulfil the independence criteria projected for an independent Board member within the meaning of the Commission's Recommendation of 15 February 2005 regarding the role of non-executive directors or directors acting as members of supervisory Boards in stock exchange listed companies and the (supervisory) Board's committee (2005/16/EC) with consideration of Good Practices of the Warsaw Stock Exchange Listed Companies ("Independent Supervisory Board Members"). A candidate for the Independent Supervisory Board Members provides the Company, prior to his/her appointment as a Board member, with a written declaration on the fulfilment of the independence criteria.

In accordance with the Act of 11 May 2017 on statutory auditors, audit firms and public supervision (Journal of Laws, item 1089), the Company has the status of a public interest entity within the meaning of this Act, and therefore it should have an Audit Committee. The audit committee consists of at least 3 members. At least one member of the audit committee has the knowledge and skills in the field of accounting or auditing of financial statements. According to the said Act, the majority of the audit committee members, including its chairman, must meet the criteria of independence from a given public interest entity.

The Board supervises the Company's activities in all areas of its operation.

The Board's rights especially include:

- 1) approval of the Board's Regulations and giving opinion on the organisational regulations, which specify the organisation of the Company's entrepreneurship,
- 2) conclusion, termination, and amending agreements with the Board members, as well as establishment of the Board's remuneration principles and the remuneration amounts for the Company's Board members,

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- 3) appointment and dismissal of the Board's President, Vice-Presidents, as well as other Board members in a secret ballot,
- 4) suspension in duties due to significant reasons, in a secret ballot, of the Board's President, Vice-Presidents, as well as other Board members, or the entire Management Board,
- 5) delegation of a Board member or members for temporary execution of Board member activities in case of suspension of Board members or the entire Management Board,
- 6) selection of the entity authorised to audit the Company's financial statements,
- 7) evaluation of the Board's report from the Company's activities or financial statement for the previous accounting year,
- 8) evaluation of the Board's conclusion regarding the division of profit or loss coverage,
- 9) submission to the General Meeting of the written annual report on the results of evaluations specified in paragraph 7 and 8,
- 10) submission to the General Meeting of the annual brief evaluation of the Company's situation, as well as the annual report on the Board's work,
- 11) giving opinion on cases submitted by the Board and comprising the subject of the General Meeting's resolutions,
- 12) approval of the Company's and ZE PAK Capital Group's perennial activity programs, including the Company's and ZE PAK Capital Group's activity strategies, developed by the Board, and
- 13) approval of the Company's annual activity programs, as well as the Capital Group's annual activity programs, especially including production plans and revenues, type cost plans, unit cost plans, remuneration plans, investment plans, as well as renovation and maintenance service plans.

The Board's competencies also include giving the Board an approval:

- 1) to participate in other companies and disposal of shares in other companies,
- 2) to establish foreign branches,
- 3) to make advanced payments for dividends,
- 4) for the Company to execute activities which result in incurring liabilities, except for:
 - a. activities provided in the Company's annual activity program approved by the Board,
 - b. activities resulting in incurring liabilities with a value of up to zloty 1 000 000, including granting sureties or guarantees as well as suretyship,
- 5) acquisition and disposal of property, right of perpetual usufruct or share in property or perpetual usufruct with a value exceeding zloty 1 000 000,
- 6) conclusion by the Company and an affiliate of a major agreement within the meaning of the regulations regarding the current and periodical information provided by issuers of stocks accepted for trade in a regulated market, excluding typical agreements concluded by the Company pursuant to market conditions, within the conducted operational activities,
- 7) designation by the Board of personnel acting in the bodies of companies or other entities in which the Company has a direct or indirect share, as well as
- 8) establishment by the Board of the manner of ballot execution during the General Meeting or the Meeting of Partners in companies, in relation to which the Company is a parent company or an affiliate within the meaning of the Code of Commercial Companies, in the following cases:
 - a. disposition and lease of the company's entrepreneurship or its organised part, establishment of a limited property right for them, as well as execution of other activities related to the acquisition or administration of the company's asset components which comprise the subject of the General Meeting's or Meeting of Partners' deliberations,
 - b. company's termination or liquidation,
 - c. amendment of the company's articles of association or deed
 - d. company's merger, division or transformation, as well as
 - e. increase or decrease in the company's share capital.

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Pursuant to the Board's application, the Supervisory Board grants Board members the approval to take positions in the bodies of companies, in which the Company holds shares, as well as for the collection of remuneration for acting in these positions.

9.9. Composition, its changes as well as description of the management and supervisory bodies

Management Board

The 2017 financial year began in the following composition:

- 1) Adam Kłapszta – Vice-President of the Board, acting President of the Board,
- 2) Aneta Lato-Żuchowska – Vice-President of the Board,
- 3) Zygmunt Artwik – Vice-President of the Board,
- 4) Katarzyna Sobierajska – Vice-President of the Board,
- 5) Tomasz Zadroga – Vice-President of the Board.

On 3 March 2017, by the resolution of the Company's Supervisory Board, the function of the President of the Management Board was entrusted to Mr. Adam Kłapszta. Simultaneously, at the same Supervisory Board meeting, Ms. Katarzyna Sobierajska and Mr. Tomasz Zadroga submitted their resignation from the positions of the Vice-Presidents of the Company's Management Board on March 3, 2017. The Supervisory Board of the Company also appointed Ms. Elżbieta Niebisz as the Vice-President of the Management Board.

Since 3 March 2017, the Management Board of the Company has been operating in the following composition:

- 1) Adam Kłapszta – President of the Board,
- 2) Aneta Lato-Żuchowska – Vice-President of the Board,
- 3) Zygmunt Artwik – Vice-President of the Board,
- 4) Elżbieta Niebisz – Vice-President of the Board.

Supervisory Board

There were the following changes in the composition of the Supervisory Board in the reported period:

The 2017 financial year the Supervisory Board of ZE PAK SA started in the following composition:

- 1) Tomasz Szelaĝ – Chairman,
- 2) Henryk Sobierajski – Deputy of the Chairman,
- 3) Wojciech Piskorz – Secretary,
- 4) Leszek Wysłocki,
- 5) Lesław Podkański,
- 6) Ludwik Sobolewski,
- 7) Wiesław Walendziak.

On June 28, 2017, the Ordinary General Meeting of the Company appointed the Supervisory Board for a new, i.e. 7th term of office. 7 members were appointed to the Supervisory Board of the 7th term, i.e.:

- 1) Tomasz Szelaĝ,
- 2) Wojciech Piskorz,
- 3) Henryk Sobierajski,
- 4) Leszek Wysłocki,
- 5) Wiesław Walendziak,
- 6) Lesław Podkański,
- 7) Sławomir Sykucki.

At the meeting on June 29, 2017, the Supervisory Board of the Company chose:

- 1) Wiesław Walendziak as the Chairman of the Supervisory Board,
- 2) Tomasz Szelaĝ as the Deputy of the Chairman of the Supervisory Board,
- 3) Wojciech Piskorz as the Secretary of the Supervisory Board.

On October 21, 2017, the Extraordinary General Meeting of the Company appointed Mr. Sławomir Zakrzewski to the Supervisory Board. Since October 21, 2017, the Supervisory Board has been working in the following composition:

- 1) Wiesław Walendziak – Chairman,
- 2) Tomasz Szelaĝ – Deputy of the Chairman,

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- 3) Wojciech Piskorz – Secretary,
- 4) Henryk Sobierajski,
- 5) Leszek Wysocki,
- 6) Sławomir Zakrzewski,
- 7) Lesław Podkański,
- 8) Sławomir Sykucki.

The members of the Supervisory Board meeting the criteria of the independence are Mr. Lesław Podkański and Mr. Sławomir Zakrzewski.

In performing its code and statutory duties, the Supervisory Board held 12 meetings in 2017, adopting a total of 64 resolutions. The Supervisory Board performed the statutory duty to hold a meeting in each quarter.

In the reporting period, the Supervisory Board collectively supervised the Company's activity in all areas of its operation. The Supervisory Board focused on the following issues:

- 1) evaluation of statements developed for the financial year of 2015,
- 2) giving an opinion on the Company's new organisational structure,
- 3) appointing the Audit Committee within the new, i.e. 7th term of the Supervisory Board,
- 4) giving consent for the Company to perform actions resulting in incurring liabilities with a value of over PLN 1 million,
- 5) giving opinions on applications submitted by the Management Board regarding matters related to the current operations of the Company,
- 6) changes in the Management Board of ZE PAK SA,
- 7) supervising activities related to heat supply to Miejskie Przedsiębiorstwo Energetyki Ciepłej – Konin Sp. z o.o.,
- 8) supervising works related to the end of coal blocks operation at Elektrownia Adamów,
- 9) approval of activities related to the ongoing restructuring process in ZE PAK SA Capital Group,
- 10) current discussion of the situation related to the course of the construction project of the open-pit construction of Ościsłowo, in particular obtaining a decision on environmental conditions for this investment.

On October 21, 2017, the Supervisory Board of the 7th term of office appointed the Audit Committee in the following composition:

- 1) Sławomir Zakrzewski,
- 2) Lesław Podkański,
- 3) Tomasz Szeląg.

In the financial year 2017, the Audit Committee of the Supervisory Board of ZE PAK SA held 5 meetings. At the meeting on October 23, 2017, the Audit Committee of the Supervisory Board of ZE PAK SA, functioning within the 7th term of the Council, proceeded to elect the Chairman of the Committee. Members of the Committee elected Mr. Lesław Podkański as the Chairman. Additionally, during the meetings held, the Audit Committee of the Supervisory Board of ZE PAK SA discussed with the auditor, among others, results of audits of financial statements for 2016 and review of interim financial statements for 2017. As part of the work carried out in 2017, the Audit Committee adopted such documents as: "Policy of providing Zespół Elektrowni Państw-Adamów-Konin SA by the auditing company conducting the research, by entities related to this auditing company and by a member of the auditing company's network of permitted non-audit services", "The procedure for selecting an audit firm for the purpose of carrying out a statutory audit of Zespół Elektrowni Państw-Adamów-Konin SA" and "The policy of selecting an audit firm for the purpose of carrying out a statutory audit of Zespół Elektrowni Państw-Adamów-Konin SA". The Audit Committee also dealt with the matter of indicating the Person Being responsible for the implementation of the selection procedure for the audit company for the purposes of conducting the statutory audit ZE PAK SA for the years 2018-2019.

9.10. Procedure and basic powers of the General Meeting as well as description of shareholders' rights and their exercise

General Meeting

The General Meeting is held in cases specified in the Code of Commercial Companies and in the Company's Articles of Association. The General Meeting is held in principle by the Company's Board and deliberates, and an ordinary or extraordinary meeting. In case of summoning the General Meeting by an entity or body other than the Company's Board, the Board is obligated to cooperate with the entity or body in order to execute any activities specified by the law as necessary to summon, organise, and execute the General Meeting. Since the first day of listing of the Company's shares in the regulated market of the Warsaw Stock Exchange Joint-stock Company, the General Meetings can take place with the use of electronic communication resources. The decision on arranging the General Meeting using electronic communication devices is made by the Company's Supervisory Council.

The General Meeting takes place in Warsaw or in the Company's registered office.

The ZE PAK SA's General Meeting is summoned by notification placed on the Company's website and in a manner specified for provision of current information in accordance with the regulations on public bidding and conditions for introducing financial instruments to the organised trade system and on public companies.

The materials made available to shareholders in relation to the General Meeting, including drafts of resolutions proposed for passing, as well as other important materials are made available by the Company on the <http://ri.zepak.com.pl/> website.

The basic competencies of the General Meeting include:

- 1) examination and approval of the Board's report on the Company's activities, as well as the financial statement for the previous accounting year, as well as acknowledgement of the fulfilment of duties by the Company's body members,
- 2) division of profit and loss coverage,
- 3) change in the subject of the Company's activities,
- 4) amendments to the Company's Articles of Association,
- 5) increase or decrease in the share capital,
- 6) authorisation of the Board to acquire own shares for the purpose of redemption,
- 7) appointment and dismissal of Council members,
- 8) establishment of the remuneration of Council members,
- 9) Company merging, division and transformation,
- 10) Company termination and liquidation,
- 11) emission of convertible bonds or bonds with right of priority and subscription warrants,
- 12) sale or lease of the company or its organised part as well as establishment of a limited property right for them,
- 13) establishment and cancellation of the Company's capitals and funds,
- 14) conclusion by the Company of a credit, loan, surety agreement, or a similar agreement with a member of the Company's Board, Supervisory Council, proxy or liquidator, or for any of this personnel,
- 15) conclusion by an affiliate of a credit, loan, surety agreement or a similar agreement with a member of the Company's Board, Supervisory Council, proxy or liquidator, or for any of this personnel,
- 16) any provisions regarding claims the remedy of damage done during the Company's establishment or executing management or supervision, and
- 17) use of the share capital.

The active right to participate in the General Meeting is available to persons being the shareholders, 16 days prior to the General Meeting. The condition of admitting a shareholder to participate in the General Meeting is the submission of a registered certificate regarding the right to participate in the General Meeting, which is issued by the entity that keeps the stocks account.

The shareholder participates in the General Meeting's deliberations and executes the right of ballot in person or via an authorised representative.

The shareholder who represents at least 1/20 of the Company's share capital is entitled to request specific cases to be included in the Company's General Meeting agenda. The request should be reported to the Company's Board no later than 21 days prior to the Company's General Meeting.

The shareholder, who requests to include specific cases in the General Meeting's agenda, should demonstrate the possession of the proper number of shares at the date of request submission, including a deposit certificate to the request, issued by the entity keeping the stocks account.

The shareholder representing at least 1/20 of the Company's share capital can submit resolution drafts regarding the cases introduced into the General Meeting's agenda, or cases, which are to be introduced into the agenda in a written or electronic form prior to the date of the General Meeting.

Each of the shareholders authorised to participate in a general meeting can provide the resolution drafts regarding the cases introduced into the agenda during the Company's General Meeting.

The General Meeting's resolutions are passed with a majority of 75% votes, provided that the Code of Commercial Companies does not specify otherwise. Each Company's share entitles to a single vote at the General Meeting.

9.11. Description of principles of changes in the Company's statute

Changes to the Company's statute, in accordance with the Code of Commercial Companies and provisions of the Company's Statute, require the General Meeting to pass a suitable resolution and an entry into the register of entrepreneurs. The General Meeting can authorise the Company's Supervisory Council to develop a uniform text of the amended statute, or to introduce editorial changes specified in the General Meeting's resolution. Amendments to the Statute are binding since the moment of entry into the register of entrepreneurs.

9.12. Information on the remuneration system and the amount of management and supervisory staff's remuneration

In Zespół Elektrowni Pątnów-Adamów-Konin SA. company, the remuneration system is based on the Corporate Collective Labour Agreement for ZE PAK SA employees as of 24 September 1993 (CCLA). Only members of the Management Board, the principal accountant and key managers are not subject to the CCLA's provisions.

The basic components of remuneration for the employees contained in the CCLA include an individual monthly basic salary, a monthly statutory bonus, an annual bonus, a post-employment benefit and allowances. The employees are also entitled to receive awards from the president's fund and social benefits.

The Management Board determines the principles of remuneration of key managers in individual agreements. The basic component of remuneration is the basic salary. The key managers can receive a discretionary award granted by the Management Board's decision. The key managers are also entitled to some components of the CCLA.

The members of the ZE PAK SA Management Board are paid on the basis of the provisions of individual management agreements, the content of which is formed by the Supervisory Board of the Company. There are no other additional regulations or other documents creating the rules of the Management Board's remuneration. The members of the Management Board are entitled to a monthly salary. They can also be granted a discretionary award. In case of dismissal from the Management Board composition, the payment of a severance pay in the amount of a six-month salary is provided. The severance pay is not entitled if the dismissal occurs for reasons concerning the dismissed member of the Management Board, particularly for the reasons set forth in Article 52 of the Labour Code.

The Company does not have a motivational or bonus program based on the Company's capital.

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Table 15: Information on the amount of remuneration paid in 2017 by the Company and its subsidiaries to all Management Board members performing their functions in 2017

<i>The Board's member name and surname</i>	<i>zloty thousand</i> <i>Value of (gross) remuneration paid by the Company</i>	<i>zloty thousand</i> <i>Value of (gross) remuneration paid by the Company's subsidiaries</i>	<i>zloty thousand</i> <i>In total: including variable elements of remuneration*</i>	<i>zloty thousand</i>
Adam Kłapszta	550.00	63.60	613.60	200.00
Aneta Lato-Żuchowska	493.00	94.10	587.10	140.40
Zygmunt Artwik	736.00	1.20	737.20	100.40
Elżbieta Niebisz	114.00	394.70	508.70	30.40
Katarzyna Sobierajska	86.40	270.90	357.30	20.00
Tomasz Zadroga	340.90	0.40	341.30	200.00
Total	2 320.30	824.90	2 591.80	691.20

* *The variable remuneration components include: awards and bonuses, severance pay for dismissals from the Management Board, holiday equivalents, retirement benefits and remuneration for participation in meetings of supervisory boards.*

Table 16: Information on the amount of non-cash benefits in 2017 granted by the Company and its subsidiaries to all Management Board members performing functions in 2017

<i>The Board's member name and surname</i>	<i>zloty thousand</i> <i>Total estimated value of non-cash benefits granted by the Company</i>	<i>zloty thousand</i> <i>Total estimated value of non-cash benefits granted by the Company's subsidiaries</i>	<i>zloty thousand</i> <i>In total:</i>
Adam Kłapszta	0.80	-	0.80
Aneta Lato-Żuchowska	0.70	-	0.70
Zygmunt Artwik	1.10	-	1.10
Elżbieta Niebisz	1.60	2.00	3.60
Katarzyna Sobierajska	0.20	0.60	0.80
Tomasz Zadroga	0.03	-	0.03
Total	4.43	2.60	7.03

The total amount of remuneration, understood as the value of remuneration, bonuses and benefits received in cash, in kind or in any other form, paid by the Company and subsidiaries of the Company to the Management Board members in 2017 amounted to PLN 3 152.23 thousand. The given amount should be treated as the gross value of remuneration paid or due in the period from 1 January to 31 December 2017.

Members of the Supervisory Board of ZE PAK SA are remunerated on the basis of Resolution No. 32 of the Ordinary General Meeting of June 28, 2017, which fixed the monthly remuneration for the chairman of the Supervisory Board in the amount of PLN 15 000 and for other members in the amount of PLN 10 000.

Table 17: Information on the amount of remuneration paid and the value of non-cash benefits in 2017 by the Company and its subsidiaries, as a member of the Supervisory Board, all members of the Supervisory Board performing their functions in 2017

<i>Name and surname of Supervisory Board member</i>	<i>zloty thousand</i> <i>Value of (gross) remuneration paid by the Company and the Company's subsidiaries</i>	<i>zloty thousand</i> <i>Total estimated value of non-cash benefits granted by the Company and the Company's subsidiaries</i>	<i>zloty thousand</i> <i>In total:</i>
Wiesław Walendziak	145.50	0.00	145.50
Tomasz Szelaąg	154.50	0.00	154.50
Wojciech Piskorz	121.10	1.10	122.20
Henryk Sobierajski	120.00	0.00	120.00
Leszek Wysłocki	120.00	3.30	123.30
Lesław Podkański	120.00	0.00	120.00
Ludwik Sobolewski	71.50	0.00	71.50
Sławomir Sykucki	240,00	0.00	240,00
Sławomir Zakrzewski	13.20	0.00	13.20
Total	1 105.80	4.40	1 110.20

The total amount of remuneration, understood as the value of remuneration, bonuses and benefits received in cash, in kind or in any other form, paid out by the Company and subsidiaries of the Company to the members of the Supervisory Board in 2017 amounted to PLN 1 110.20. The given amount should be treated as the gross value of remuneration paid or due in the period from 1 January to 31 December 2017.

10. STATEMENT ON THE DIVERSITY POLICY

With reference to §91 paragraph 5 point 4 lit. 1 of the Regulation of the Minister of Finance of 19 February 2009 on current and periodic information the Company declares that in ZE PAK SA Group and in ZE PAK SA no separate document describing the diversity policy has been adopted. At the same time, management solutions related to the issue of diversity management were adopted.

The objectives related to diversity management, in particular with regard to the age structure of employees, were adopted in the Group together with the Corporate Social Responsibility Strategy of ZE PAK SA Capital Group for the years 2017-2020. The restructuring process, lasting for years, meant that most vacancies were filled on the basis of internal recruitment (as part of transfers between departments and companies). A side effect of actions aimed at reducing redundancies and concentrating in the recruitment process on persons already employed in the Group's companies was the lack of a significant inflow of young employees, and as a result, the average age of employees increased. At some point, this may result in significant retirements and staff shortages. Therefore, ZE PAK SA Group actively monitors changes in the age structure of employees in order not to allow the adverse consequences of losing a large part of experienced employees without proper preparation of their successors.

Simultaneously, the Code of Ethics adopted at the end of 2017 in ZE PAK SA includes diversity policy, guaranteeing equal treatment regardless of gender, age, worldview, religion, political views, etc. The document is a tool for reporting potential incidents related to discrimination on any background. It is planned to implement analogous solutions in the subsequent companies of the Group.

As of today, in the Company's opinion such solutions are sufficient.

Numerical data referring to diversity can be found in the Statement on non-financial information for 2017 in the subsection "Employee issues", page 57 of this report.

11. STATEMENT OF ZESPÓŁ ELEKTROWNI PAŃNÓW-ADAMÓW-KONIN SA CAPITAL GROUP ON NON-FINANCIAL INFORMATION FOR 2017

In the process of preparing an approach to non-financial reporting, including preparation of this statement, ZE PAK SA Group has worked on the basis of the best global practices in this field, for instance using the approach for defining the significant contents, information as well as the indicators suggested, among others, by:

- PN-ISO 26000 standard,
- GRI G4 guidelines / GRI Standards,
- RI G4 Sectoral Supplements in the field corresponding to the mining and power engineering

Nevertheless, this statement might not be considered as the one developed in accordance with GRI G4, GRI Standards or any other comprehensive standard.

The reporting process itself was preceded by the development of strategy for Corporate Social Responsibility of ZE PAK SA Group, where the approach suggested by PN-ISO 26000 was maintained, i.e. in the first step of works, during the internal conferences, in which the members of interdisciplinary team appointed by ZE PAK SA Management took part, the significant areas of responsibility and crucial groups of stakeholders were defined. The defined significant areas became appropriately a starting point to determine the crucial aspects to which particular emphasis has been placed in the statement, in the fields of social, employee, environmental protection, human rights and counteracting corruption issues.

11.1. Description of business model

ZE PAK SA Capital Group („ZE PAK SA Group”, „Group”) is a significant producer of energy on the Polish market and an important element of national power engineering system. The vast majority of its revenues are generated from the sale of produced electricity. The Group is operating on the basis of the integrated business model. With its own coal lignite mines, it extracts it and using mainly this fuel it is generating electricity and heat in nearby power plants. Simultaneously, there are entities functioning within the group, in the form of separated companies responsible for the support functions (e.g. sale, renovation, maintenance, etc.).

The companies of the greatest importance to the ZE PAK SA Group due to their scale of operations are: Zespół Elektrowni Pańńów-Adamów-Konin SA ("ZE PAK SA") - dealing with the production of electricity and heat, Elektrownia Pańńów II sp. z o.o. - dealing with the production of electricity, and PAK KWB Adamów SA and PAK KWB Konin SA dealing with lignite mining. Beside the companies from the main areas of activity, there are also other companies that, among others, are dealing with implementation of construction and assembly works, maintenance, service, production and trade activities aimed at satisfying the needs and comprehensive industry service. In 2017 generation assets of the Group included four lignite-fired power plants located in the centre of Poland, in Wielkopolska voivodship. There are: Pańńów II - equipped with the power unit of supercritical parameters, Pańńów I and Konin – equipped with the biomass-fired boiler unit, and Adamów (Elektrownia Adamów was closed in January 2018). The Group's basic production assets are concentrated mainly in two companies: PAK KWB Konin SA, which currently operates in Jóźwin, Tomisławice and Drzewce opencast mines, and PAK KWB Adamów SA exploiting Adamów opencast mine.

11.2. Social issues

Management approach

The policy and management approach of the ZE PAK SA Group to social issues were set out in the Strategy for Corporate Social Responsibility of the ZE PAK SA Capital Group for 2017-2020 adopted in 2017. Simultaneously, the approach presented in the Strategy is reflected in other internal regulations. The management approach is also determined in administrative decisions that allow conducting the mining and generating operations in the units that belong to ZE PAK SA Group and dependent on the specifics of the particular object. Each time, the Group is trying to work out the optimal solutions in this respect, based on social consultations as well as in accordance with the applicable law.

The Group's management approach to social issues is conditioned by the nature of its companies' influence on the environment. Particularly in the areas where the influence is or might be negative and can be associated with specific burdens for people, the management approach aims at eliminating, limiting or compensating for these burdens, and consequently limiting the exposure of the Group to the risk.

The Group's influence on the environment is multidimensional. From the point of view of general public, ZE PAK SA Group is an important supplier of energy for the Polish economy and Polish society. Nevertheless, the final customers are not the main clients of the Group but the trading companies operating on the wholesale electricity market. For this reason, the ZE PAK SA Group aims at ensuring stable electricity supply at a competitive price to other technologies. The ZE PAK SA Group has a much wider range of impact on the environment from the point of view of the local community, i.e. understood as a community living in the immediate neighbourhood of the Group's plants, where the production of electricity and heat and lignite coal mining is conducted. The exploitation of lignite deposit and production of energy have the great impact on the natural environment (see: Environmental issues), and consequently social environment too. Dealing with the negative influence on the natural as well as social environment, it is necessary to mention, first of all, about the danger and burdens associated with:

- an influence on the land surface (opencast mining of minerals results from the transformation of the land surface; in the place of the originally used land, spatial field forms (excavation, heap) and accompanying infrastructure are created (conveyors, transport routes, facilities),
- an influence on the surface water (inter alia reducing the flow in watercourses under the influence of the mine and increasing the flow in the watercourses due to discharging water from underground drainage and surface pits),
- an influence on the groundwater (formation of the so-called depression funnel due to the drainage of open-cast mines),
- noise emission (basic machines related to the operation of the overburden and its dumping, basic machines mining coal, coal and overburden conveyors, road transport),
- an impact of mine objects on atmospheric air (dust emission: technological (mechanical), i.e. associated with mechanical mining and transport of the raw material with conveyor belts; climatological, i.e. related to wind erosion of vegetation-free areas; organized emissions of pollutants into the air from the boiler room providing heat for social facilities mine),
- an influence on valuable natural area (in case when the valuable natural area is located in the zone of influence),
- hazards associated with electromagnetic fields.

It is worth mentioning here, that the above mentioned influence is not only negative. Konin energy basin has a unique, cooling system, based on water cycle. A common name of "jeziora ślesińskie" includes the following lakes: Gosławskie, Państwskie, Wąsowsko-Mikorzyńskie, Licheńskie and Ślesińskie, which are included in the cooling circulation of Państw, Państw II and Konin power plants. All the lakes are connected by a channel system of total length of about 26 km and they are forming a closed circulation where the water flow is regulated by culverts and pumping stations. The discharge of waste heat to nearby lakes obviously influenced their ecosystems, but also made these reservoirs especially valuable for fishing and fish farming. Higher temperature of water and its large flow in the channels and lakes caused that in the area of cooling system the breeding fish ponds were located there. Fishing farms operating here are not only the largest producers of sturgeon fish in Poland (Siberian sturgeon, Russian sturgeon, sterlet), but also other species of fish such as European catfish, rainbow trout, amur, silver carp, catfish, carp or ornamental fish. By the use of waters with increased thermic for reproduction, breeding and breeding of thermophilic fish, they are an important producer of fry in the domestic market. The cooperation with ZE PAK SA Group makes the warm water to flow directly through the ponds providing optimal conditions for development of fry and adult fish. One of the farms is taking the water for breeding from Elektrownia Konin precooling water tank and the production is strictly dependent on the conditions made by the power plant, water temperature and its cleanliness, etc. For this reason there is a constant communication and information flow between the fish farms and the power plants. In addition to some of the largest fishing farms in Poland, these areas are known among anglers. Supporting such economic activities, as well as all other forms of social involvement allows compensating partially to social environment the burdens related to the activities of ZE PAK SA Group.

ZE PAK SA Group may also be a welcome member of the community, due to significant direct and indirect economic impact. Money transfers in the form of taxes and para-taxes (license fees, concessions, etc.) to a large extent feed budgets of local governments. For example, in 2017, the Group's companies paid over PLN 247.9 million (PLN 264.1 million in 2016), of which PLN 170.6 million (in 2016 it was over PLN 158.1 million) increased budgets of local governments. These means allow the communities to realize investment projects, finance health care and education, etc. Simultaneously, thanks to the salaries of employees who are mostly recruited from local communities, the so-called multiplier effects are started and the local economy is stimulated, including sectors not directly related to lignite mining and energy (the Group's companies allocated employee benefits to PLN 461 million in 2017 and PLN 488 million in 2016).

The management approach of ZE PAK SA Group concentrates mainly on ensuring production continuity and stability while ensuring at the same time the safety for natural and consequently social environment. Such management approach was set out in the Strategy for Corporate Social Responsibility for 2017-2020 adopted in 2017 and it assumes providing effective mechanisms reducing to minimum the threat of anomalies and gaps occurring resulting in over-normative impact on the environment in the mining or manufacturing process. Consequently, it assumes providing mechanisms guaranteeing the stable operation of the plants, which is not disturbed by interruption in production or mining that would be caused by social factors. These aspects also relate to policies accompanying management systems and internal regulations that ensure compliance with laws and administrative permits related to specific manufacturing facilities and installations.

The other dimension of impact on social environment is connected with the economical use of waste heat, which accompanies the electricity production. A part of heat has been used for years for heating purposes, inter alia by Miejskie Przedsiębiorstwo Energetyki Ciepłej in Konin. Such approach is extremely rational from the social as well as environmental point of view. Nevertheless, due to restructuring of power plants, the heat production from the current source based on the lignite from Konin power plant, after June 30, 2020 will not be possible because of the environmental requirements. However, the Group, wishing to remain a supplier of heat for the local community, conducts analytical and formal-legal work for this purpose to develop an optimal project for starting a new source of heat based on a biomass block that could form the basis for a new heat supply contract. The Group is interested in constructive dialogue, giving a chance to develop the solutions satisfying for the parties and economically viable, that would ensure safe heat supply for Konin residents. Nevertheless, as noted, the solutions must be profitable at the same time, in order to protect the obvious interest of the residents, as well as the shareholders'.

The management approach and, consequently, the implemented activities directly or indirectly address the risks associated with the loss of favour of the local community, and thus contribute to the prevention of events that could disrupt the stable operation of mining and manufacturing plants, and consequently negatively affect the Group's financial results. When it comes to aspects of influence on the natural environment, which at the same time are the source of potential burdens for the local society, they were widely described in the further part of the report (see: Social issues). They constitute the element of environmental management, having parallel consequences for local society. The approach to them was also described in other internal regulations as well as in the administrative decisions regulating the environmental issues. This description is limited to the characteristic of the Group's approach to these aspects which concerns only the human beings. Though, all of them focus on the activities which aim at monitoring and reducing the negative influence.

For instance, in the areas that are to be under extraction, as well as directly adjacent with the area designed for extraction, real estate buyouts are made. Most often they are agricultural lands but also the buildings or constructions. Assessments of the influence, i.e. whether the real estate adjacent to the opencast mine is going to be the subject to buyout, are set individually. The individual approach is justified by the fact that in such aspect the significant roles are played by emotional factors, for instance, associated with getting used to this place. In addition to those who may be reluctant to resell the property, there are also those who would like to sell it, although in the opinion of the investor's experts, the scale of impact will not be sufficient to justify the necessity of buying. In extreme cases, there may be disputes that eventually find their final in the court. Nevertheless, the Group's intention is to carry out the described processes in a way reducing the negative emotions, because it may influence subsequent projects of this type.

Lignite deposits in the operation area of the Group have their specific characteristics and wealth. The company does not use one deposit, but over the years it is forced to launch further opencast mines. Therefore, at the same time a process of reclamation of previously exploited pits, exploitation of current outcrops and preparatory processes for the next ones take place. Currently, PAK KWB Konin SA is applying for a mining concession for Ościsłowo open pit. The coal supplied from this outcrop is to secure supplies for the modernized blocks at Pańków I and Pańków II power plants. These are the most efficient generation assets of the Group for modernization of which, significant expenditures have already been incurred. The process of launching a new lignite mine is a multi-stage process and its implementation requires special care. It should be borne in mind that in processes related to obtaining formal consents before public administration authorities, there are usually various associations and organizations that aim to fight specific types of activities (e.g. they deny the use of lignite as a rule, and thus, the operation of opencast mining). In the current pending proceedings concerning the determination of environmental conditions for the project entitled: "Extraction of lignite coal and accompanying minerals from Ościsłowo open-pit" (more detailed description in the Management Board's report on pages 11 and 12) the parties also have several organizations opposed to the location of new lignite opencast mine. It is worth mentioning that, on the other hand, the trade unions or some local opinion leaders pay a lot of attention to the supporters.

As mentioned earlier, as a result of mining operations, socially annoying phenomena may occur. In case of occurrence of such situations the Group tries to compensate by paying out appropriate damages in justified cases. Damage can be divided into direct and indirect. Direct damage is usually associated with mining plant operations and the progress of exploitation fronts. They include reconstruction and construction of new roads, power lines, water supply networks and

other technical infrastructure as well as road repairs, on which the mine transport moves and in particular cases the transfer of sacral culture objects, e.g. chapels, churches, cemeteries. Due to direct damage, the companies from the Group's mining segment in 2017 paid PLN 8 855 thousand, while in 2016 it was PLN 16 927 thousand, respectively. It is worth noting that in each case the payment of compensation for direct damages occurred by way of a settlement or agreement. Apart from direct damage, there are also indirect damages connected, for example, with the lowering of the groundwater level in the areas adjacent to the mines. However, drainage of water from the outcrop to watercourses can lead, for example, to raising their level. Water shortage as well as its excess can mean adverse effects, for example, on agricultural production, which the Group tries to compensate by paying reasonable compensation in justified cases. Owners of compensated land receive written notifications with a proposal for the amount of compensation due to the mine's impact. In the case of acceptance, an out-of-court settlement is signed with the owner, with a waiver of claims after payment of compensation. Only a few cases of mining damage are subject to resolution by ordinary courts. Practice indicates that in the vast majority (about 80-90%) of compensation cases, out-of-court settlements are made, in the remaining part by way of court settlement or court ruling. In 2017, only PLN 52.37 thousand out of PLN 2,189 thousand - the total amount of indirect damages was paid as a result of a court judgment, and in the case of the remaining part, a settlement was reached. In 2016, the whole of 1,994 thousand PLN was paid as part of the settlement.

In case of other periodical burdens, for example intensified noise associated with the renovation or modernization works on the generating objects (such works give rise to the necessity of blowing the boiler's installation under very high pressure, in order to remove even the filings from the installation, which could damage it, and that is quite loud), the Group informs local society, through mass media, about such burdens by giving the information to local media or local offices. The same happens with any other burdens (e.g. in road traffic connected with the transport of oversized equipment, the intensification of dusting or dew from chimneys. Consequently, they do not arouse controversy, and the plant can count on the forbearance of the inhabitants of the immediate area. Within the education activities directed to external society, the Group's PR department performs press articles explaining the rules of exploitation of lignite open mines and reclamation of post-mining sites. As mentioned earlier, the inhabitants of the nearest neighbourhood of the plant are often the Group's employees. Thus, although the external communication is described here, the appropriate internal communication is significant and the employees themselves are the ambassadors of ZE PAK SA Group. In case of communication activities, in situations like those described above, an equally important role can be played here by internal communication. Here, however, a wider spectrum of information transfer is possible: some activities can be better and more precisely explained, using e.g. "Kontakt" - a monthly e-magazine of the Capital Group.

The Group also declares its support for local initiatives, although due to the savings program it has been less recently than in previous years. ZE PAK SA Group aims at supporting local society by social commitment, so as to compensate the burdens associated with the operation of the plant, in a part which cannot be eliminated or limited.

The Group's involvement in spectacular projects is not meant to get publicity but to reach the nearest communities and non-governmental organizations from the region. PAK KWB Konin, for instance gave a number of donations last year, largely factual, e.g. in the form of earth or sand for Ślesin and Wierzbinek community and for Roman Catholic parish in Połajewo in the amount of ca. PLN 80 thousand gross; in the form of 7000 bottles of "Licheńska" water (produced by one of Group's subsidiaries) for communal harvest festivals in Kobylanki, Zakrzewek, Rudzica and Osiek Mały; for organization of the First Running Festival of Skulsk Commune on "Szlak Wielkiej Pętli Wielkopolski"; in the form of Christmas packages for the Special Educational Centre of Janusz Korczak in Konin and Sociotherapy Centre No. 4 in Konin. PAK KWB Konin also gave, along with the loading, a 42-ton boulder for "LEDNICA 2000" Association for the monument on the grave of Father Jan Góra and a 6-ton erratic boulder for the municipality of Świnice Warckie for placement of a plaque commemorating the air battle between Polish and German aircraft. For the Deep Diving Dive Centre, two excavator digger shovels were donated and for the commune of Osiek Mały a service was performed in the form of sludge and silt loading by wheel loader and transport carried out by dump trucks - the works were related to the clean-up of the lake shoreline in Łuczywno. On the occasion of Barbórka, the mine donates every year to Sailing Club operating at PAK KWB Konin for the organization of the Winter Regatta of Barbórka and the Runner Club "Aktywni Konin", organizer of the Run for the Miners' Lamp. There are the meetings organized in educational institutions, the miners meet children in schools and kindergartens, the company's employees perform presentations about mine work, mining traditions. Also the brass bands operating at both mines organize musical meetings with children from schools and kindergartens - the prepared program concerns the history of the mine, mining traditions and work of the orchestra, and it is combined with the presentation of musical instruments and a short concert. Such meetings are free and they are very popular within educational institutions. The bands participate in state and church celebrations. Simultaneously, thanks to the support of the mines, PAK KWB Konin teams took part in: X National Volleyball Tournament for the Cup of the Mayor of Miasto i Gmina Kleczew, volleyball tournament organized as part of the Great Orchestra of Christmas Charity in Konin, volleyball tournament in Kazimierz Biskupi, Polish National Football Tournament of Non-attached Members for the Cup of Director PGE GiEK S.A. in Bełchatów, "Runmageddon" training in Lubstów (organized on the reclaimed area of Lubstów open-cast mine) in Sompolno commune, Runmageddon in Poznań and the Polish National Darts Masters Tournament. PAK KWB Adamów takes part in the event called "All of Poland Reads to Kids" prepared by the centre's educators in Stemplew - text is reading by a miner in gala uniform. Every year before Christmas the

miners' employees take part in Christmas Eve in orphanage in Nowy Świat, the company gives the children gifts and sweets. Throughout the year the company is visited by the tour groups from the various regions of Poland: from schools, workplaces and associations. Sightseeing of the mine is free of charge. In 2017, within prosocial activities, ZE PAK SA supported financially the 38th International Kids Song and Dance Festival in Konin, organization of the Sailing Regatta for the Cup of the President of ZE PAK SA and celebrations of the 40th anniversary of the Association of Polish Electrical Engineers in Konin. A donation was also made to the Camaldolese Hermit Congregation of the Crown Mountain - the Five Martyrs hermitage in Bieniszew. Traditionally, ZE PAK SA supports Polsat Foundation activities, one of the biggest non-governmental organizations operating in the area of Poland, which for over twenty years has been directing its help to sick children and their parents.

The significant role in the life of local society is played by Konin lakes mentioned earlier, which are on one hand the source of revenue for unique (on national scale) fish farms, and on the other hand they attract a number of amateur anglers. For this reason, the contribution of ZE PAK SA employees who are privately engaged in the life of the fishing community is worth mentioning here. In addition to other fishing clubs of Polish Angling Associations operating in this area, there are two in ZE PAK power plants associating their employees. The members of one of them are taking care of the mentioned earlier precooling tank of Elektrownia Konin - they organize annual spring action of cleaning the edge of the water reservoir and restocking with various fish species. There are also season fishing competitions with youths' participation organized by the anglers from PAA clubs. It aims at promoting fishing sport among young residents of the region and it helps acquiring new members to fishing clubs, as well as it builds a positive attitude among the participants of mentioned sport, cultural and social events towards the activity of the Group.

Associated business risk

Business risk that may have negative influence on the Group's results and development, and being associated with the area of social influence, results directly from the character of its influence (e.g. disturbing the hydrology balance or noise mentioned earlier). They constitute inconvenience and may also be a source of material damage of the third parties. This can lead to disputes with the society and thus loss of its positive attitude for present and further projects, including so-called social licence to operate. It can cause the increase of complaints directed by the society to administration bodies, initiating the proceedings against the plants and legal and financial sanctions, in case of confirming the allegations. Ineffective dialogue, for example on damages or land purchase, may also mean civil proceedings for damages. A particular threat is the loss of public trust and a negative opinion about the plant as an unreliable investor, which can definitely hinder the acquisition of further permits and concessions (e.g. for lignite mining in new areas). This, in turn, may cause a greater risk associated with the new investment and less favour of investors and lenders, and thus difficulties in raising capital.

It is worth mentioning here that the employees of the plants are recruiting from local communities. As a consequence, these groups are not separate and any possible animosities with the local community related to, for example, inconvenience, will indirectly affect the culture of the organization and the work atmosphere, and vice versa: all important incidents on the employer-employee line may result and are resulting in specific consequences in relations with local community. The same person may appear in several roles, i.e. an employee, a resident of a local community adjacent to a plant, which is exposed to nuisance related to noise for example, as well as being the owner of a real estate that is seeking compensation or redemption.

Key indicators

	2017	2016
Number of environmental failures resulting in serious contamination	0	0
Amount of indemnities paid as a result of court verdict in relation to the amount of damages paid out by the Group as a result of a settlement or agreement	0.5%	0%
Total amount of taxes and para-taxes paid - altogether	PLN 247.9 m	PLN 264.1 m
Total amount of taxes and para-taxes paid – for local administration	PLN 170.6 m	PLN 158.1 m

11.3. Employee issues

Management approach

In the area of human resources management, the ZE PAK SA Group has formal solutions defining the relationships between the employer and employees, resulting from the polish law, inter alia work regulation resulting from the

Labour Code, corporate collective labour agreement resulting from the Labour Code, Company Social Benefits Fund resulting from the act of Social Benefits Funds, in the companies not covered by the provisions of CSBF the remuneration regulations are obligatory. The companies meeting the statutory criteria have their own Staff Councils. The Unions are also operating in ZE PAK SA Group. In the matters specified by the law the management of ZE PAK SA and other companies inform and consult the decisions with the employee representatives.

Simultaneously, apart from formalized solutions resulting from specific legal provisions or adopted voluntarily (e.g. recruitment procedure), current operational activity is based on a series of solutions and customary forms of behaviour that do not require rigid formalization in the managers' opinion, and at the same time they guarantee the management that is effective and consistent with legal norms and standards of social coexistence. The Group's companies comply with the labour law and they require proper behaviour in relations between the employees as well as between the employees and their superiors.

Corporate collective labour agreements, obligatory in ZE PAK SA Groups in the reporting period, contain the principles of employment and remuneration of the employees. On the other hand, the regulations of the Company Social Benefits Fund define the rules of using and financing of social activity and housing for the benefits of the employees and their family members. The records in both documents are implemented by the managing units although at the same time there are collective disputes concerning the employee remuneration.

Meanwhile, in companies such as PAK –Volt SA (trading in electricity, office work) significant from the point of view of the generated revenues, but with very little employment and work specificity without any significant health and safety risk, formalization of labour relations and related procedures are minimal and limited to legal requirements.

Basic aspects associated with the human resources management have been determined in the Strategy for Corporate Social Responsibility of the ZE PAK SA Capital Group for 2017-2020.

Health and Safety at Work

Similarly to earlier areas, the most significant ways of activities associated with the health and safety risk management have been described in the Strategy for Corporate Social Responsibility of ZE PAK SA Capital Group for 2017-2020. Simultaneously, it is important to remember about the obligatory certified management systems covering the issues of security management, including:

- the process of electricity and heat production with all the auxiliaries, identified environmental aspects, threats, legal and other requirements (ZE PAK SA – according to PN-N 18001, OHSAS 18001),
- works in scope of installations, renovations and service of power engineering and industry equipment, industry construction services, management of investments in power engineering and industry, as well as modernization and maintenance of automation and electrical systems in power engineering (Przedsiębiorstwo Remontowe PAK Serwis Sp. z o.o. – according to PN-N 18001, OHSAS 18001).

Their goal and the objective of the Corporate Social Responsibility Strategy of ZE PAK SA Capital Group for the years 2017-2020 is to minimize the level of accidents, with particular emphasis on the elimination of events with severe and fatal consequences and undertaking organizational and technical measures aimed at eliminating or reducing the exposure of workers to harmful factors occurring in the work environment like noise and pollution to a level compliant with the standard. Simultaneously, selected management aspects, falling within a broader scope of environmental management, are regulated by internal principles and ordinances.

Mining

The mining part is the only one from three main areas where certified management system according with PN-N 18001 and OHSAS 18001 was not implemented. The management of health and safety risk works on the basis of Ordinances of the President and Ordinances of Manager of mining plant. For example, for PAK KWB Konin SA there are the following ordinances:

- 15/2001 on providing the employees of the Company by the employer with eyeglasses that correct the eyesight,
- 4/2002 on informing employees of occupational risk related to the work performed,
- 16/2003 regarding the index of works which should be performed by at least two employees,
- 20/2003 regarding the index of works requiring the particular employees' psychophysical predispositions, organization and conducting of psychological tests,
- 4/2004 regarding establishment of Health and Safety Work Commission,
- 7/2005 regarding minimum requirements concerning health and safety work in scope of using the machinery and equipment by the employees,

- 29/2007 regarding a list of works particularly hazardous or high physical or mental effort, which may not exceed 8 hours a day by a night worker,
- 27/2009 on nuclear safety, radiological protection, employee health protection and quality assurance program,
- 29/2010 regarding safety exploitations of scaffolding ,
- 28/2012 on the list of harmful, burdensome and dangerous works and the rules of granting cash and preventive meals on this account,
- 24/2013 on defining the type of particularly hazardous works in PAK KWB Konin SA,
- 36/2013 on determining places and workplaces and works requiring wearing protective helmets and the rules for their use in accordance with the company standard ZN-003: 2007,
- 29/2014 on determining places and workplaces requiring wearing appropriate personal protective equipment,
- 30/2014 on the organization of medical assistance in PAK KWB Konin SA.
- 31/2014 regarding the supply the employees with water and soft drinks,
- 49/2014 regarding the proceedings in case of accidents at work and dangerous events in PAK KWB Konin SA,
- 5/2015 regarding the form and principles of in-house training in the area of health and safety at work in PAK KWB Konin SA,
- 18/2015 on the principles of clothing, work and protective footwear as well as personal protection and hygiene,
- 7/2016 on introducing an updated „PAK KWB Konin SA Safety Document”,
- 4/2017 on the prohibition of smoking cigarettes, including smoking of innovative tobacco products and smoking of electric cigarettes in rooms, facilities and means of transport of PAK KWB Konin SA,
- 8/2017 on initial, periodic and control medical examinations.

Typical threats accompanying opencast lignite coal mining should be divided into natural and traumatic hazards. The last ones, potentially connected with the machines work, particularly their rotating elements, dangerous in consequences but they happen very rarely, mostly due to the activities of health and safety service and the employees' awareness. In recent years, in practice, if there were accidents, these were light accidents: dislocations, sprains and occasional fractures. As for the natural hazards, they can be divided into landslide (scarp escaping), methane (emergence of gas in drainage wells), fire and water (associated with: atmospheric precipitation, neighbourhood of natural reservoirs and watercourses or watercourses in the excavation).

Regarding the activities carried out in 2017 to improve the health and safety conditions in the area of extraction, in accordance with the adopted annual plan in PAK KWB Konin SA, cabin operators of basic machines (excavators, stackers) were repaired, which allowed reducing the noise level in the cabins. The change of seats for basic machine operators allowed reducing the level of exposure to vibrations. The platform for filling the excavator poles on Drzewce opencast contributed to the improvement of safety while performing welding works in the polygon chamber. The safety was also improved by the assembly of the entrance to one of the tapes from the platform of the operator's cabin.

Simultaneously, the renovations carried out in 2017 including replacement of shower cabins in the bath, painting of office and social rooms and renovation of shelters (windows, heaters, insulation, partial replacement of external sheet, chairs) improved sanitary and hygienic conditions in PAK KWB Konin.

Comfort of work was also improved by purchase of rain clothes, shoe protectors, replacement of flashlights, as well as purchase of new equipment and power tools.

Generation

In the generation area of ZE PAK SA, as mentioned earlier, the management of health and safety work is based on the integrated management system compliant with PN-N 18001 and OHSAS 18001. Simultaneously, the activities in the area of health and safety are regulated by the President's Ordinances, referring to wider aspects but covering health and safety matters as well, including:

- 42/2000 regarding eyeglasses correcting sight while working on screen monitors,
- 50/2000 on medical examination and psychological tests and preventive health care for ZE PAK SA employees,
- 47/2001 on carrying to risk assessment of identified threats at all workplaces in ZE PAK SA,
- 30/2002 regarding implementation of pre-medic rescue system in The Capital Group of ZE PAK SA,
- 47/2002 on accidents on the way to and from work,
- 51/2003 on the register of suspected occupational diseases and the register of occupational diseases,
- 5/2005 regarding occupational accidents and accidents treated equally as occupational accidents,
- 12/2005 on the workplaces and the rules of issuing supportive meals and drinks,

- 19/2005 on the training in the area of health and safety at work,
- 5/2006 on the inspection of machines in terms of compliance with the minimum health and safety requirements for the use of machines by workers at work,
- 11/2010 regarding the establishment of the Safety and Health at Work Committee, hereinafter referred to as the "Health and Safety Commission" at the Management Board of ZE "PAK" SA, hereinafter referred to as the "Employer",
- 29/2011 on the rules for determining the qualifications of persons dealing with the operation of equipment, installations and networks by qualification commissions appointed by ZE PAK,
- 5/2014 on the implementation of the "Instruction for the organization of operating works at energy devices in ZE PAK SA that pose a potential threat to human health or life", including the "Instruction for the safe conduct of fire hazardous work in rooms at risk of fire or explosion and the management of technical gases in the area Pałnów Power Plant" and "Document for securing workstations against explosion",
- 22/2016 on the list of particularly dangerous works, related to high physical or mental effort, which, due to the necessity to ensure work safety and health protection of employees, may be performed by a working person not more than 8 hours a day, hereinafter referred to as the "list of works",
- 21/2017 on the rules and standards for the allocation of clothing and footwear, personal protective equipment and personal hygiene measures for employees of ZE PAK SA.

Significant documents and procedures are here: Exploitation Manuals of Power Devices (they are the elementary documents on the basis of which the safe operation of devices is carried out), business order of the power plant's director, including e.g. No. 5/2017 regarding application at the Pałnów Power Plant "Instruction on the organization of operating works at power units at ZE PAK SA that pose a potential threat to health and human life".

Identification of threats at workplaces is the element of ZE PAK SA operation in reference to products and services that may affect the working environment. The threats identification results are included in the process of planning by establishing the particular purposes with reference to health and safety at work. In order to define the ZE PAK SA affection to working environment the following activities are carried out at workplaces: initial health and safety review, recognition of the source of the threat, identification of threat, controlling of defined workplaces. Occupational risk that includes typical operating conditions, retention and start-up, as well as potential and significant influences accompanying justified emergency situations is assessed. The scope of tests and measurements at workplaces is determined and the measurement results are analysed.

Annual analysis show that repairs and renovations carried out over the years, and most of all decommissioning of old and construction of new devices and installation, including generation units, in addition to improvement of production efficiency and reduction of negative influence on natural environment, undoubtedly contribute improvement of employees working conditions and technical safety at work through elimination or reduction of danger to health and life of the employees.

Regarding the occupational risk assessment, the factor causing noise pollution above the maximum permissible intensities are the elements such as gears, motors, clutches, etc. The maximum permissible dust concentrations, on the other hand, are exceeded in the case of lignite transporting devices. Another group of threats are dangerous factors, and their influence on the employee may cause injuries or even death. The most important factors of this group are: high temperature, high pressure, electric current, explosive atmosphere and machines' movable components. The factors related to the nuisance of work include excessive physical load, insufficient lighting and night employment.

The controls of working conditions as well as compliance with health and safety rules and regulations are carried out systematically by Health and safety service, and the recommendations are issued for these controls.

In 2017 minor works increasing health and safety level in the power plants were carried out, and they related, among others to the inspection and supplementation of the markings in the pipeline of heavy oil as well as acid and lye, repair of the insulation of the hot air duct of one of the boilers and repair of the stretch of the pavement on the roof at Pałnów Power Plant. On the other hand, in Konin Power Plant, the planned works were related to the construction of the demolished sound absorbing cover of one of the pumps, the adjustment of safety barriers to the source of ionizing radiation on the boiler biomass tank and the replacement of the sheet covering the brine tank at the Demineralization Station. At Adamów Power Plant, it was decided to replace and repair seats in the cabins of silence, replace the air conditioner, light up selected points of water readings and adjust the markings.

Service

In the service area (PAK Serwis Sp. z o.o.) the risk assessment includes all the workplaces, stationary as well as extramural ones. The risk assessment is carried out once for three years and each time, in case of any changes, reported

at workplaces or after an accident. Health and safety department keeps a register of all the workplaces being the subject to occupational risk assessment.

The so-called last minute risk analysis is carried out as well - before the work starts the employees identify the potential threats at their workplaces and assess the degree of risk. In this way the works and areas of operation associated with the significant threats are being identified. For each and every significant threat the way of procedure and supervising is determined, providing compatibility with legal and other regulations of health and safety.

Due to the current health and safety management the following procedures are of the special importance:

- „Training in scope of health and safety and environment protection”,
- „Identification of threats and occupational risk assessment”,
- „Health and safety and environment monitoring”,
- „Serious failures”,
- „Organization of works of significant threats”,
- „Accidents and occupational disease investigation”.

Annual analyses show that most of the accidents in service work result from the improper behaviour of the employees, i.e. by failure to exercise due caution and concentration on the performed activity. The most common cause of potentially accidental events, on the other hand, is the failure to carry out the risk assessment before the task starts (LMRA – last minute risk analysis). The noise and industrial dust are the basic factors associated with the work environment, and the factor related to the nuisance of work is a forced body position. Within post-accidental prophylaxis the employees are acknowledged with the circumstances and reasons of the accidents, additional instructions are given, and the information on accidents are provided to the services of ZE PAK SA (in these cases where the cause related to energy devices was found). Sometimes, it is also possible to impose administrative fines on the person supervised, in relation to whom non-compliance with health and safety regulations was proven, in connection with the accident. The employees of the Health and safety Office carry out inspections in the scope of compliance with health and safety rules and regulations, as a result of which, in the most common cases, the so-called non-compliance card and applications for imposing a penalty are given out. In the prepared business notes or protocols after the inspections carried out, the most common recommendations regarding disorder at the workplace and improper technical condition of the work means are registered.

Ancillary activity

In PAK Górnictwo Sp. z o.o. due to consolidation in the course of the reporting period under one company's activities previously covered by several entities and the related extension of the scope of activity, the majority of formal documents related to management, including occupational safety and health management, were developed and adopted in 2017 (the company has been operating since August 1, 2017 and has acquired the following companies: Energoinwest SERWIS Sp. Z o. o., Aquakon Sp. z o.o., Eko Surowce Sp. z.o.o and EL PAK Serwis Sp. z o.o.). In order to systemise the formal approach to health and safety due to the changed scale and scope of activities, the following, among others, were adopted:

- Manual of supervision over measurement of factors in the work environment
- Regulation No. 33/2017 on the handling of chemical substances in work processes
- Regulation No. 24/2017 on preventive health care
- Regulation No. 25/2017 regarding the acceptance of the control regulations carried out by the Health and Safety Service
- Regulation No. 26/2017 regarding the adoption of the risk assessment and documentation procedure
- Regulation No 28/2017 on industrial accidents, accidents treated on an equal footing with accidents at work and accidents on the way to and from work
- Regulation No. 31/2017 on the allocation of work and protective clothing, personal protective equipment and personal hygiene
- Regulation No. 36_2017 regarding the appointment of the Safety and Hygiene Work Commission at PAK Górnictwo Sp. z o.o.
- Regulation No. 38/2017 regarding the acceptance of the Instruction for Supervision of Measurement of Factors in PAK Górnictwo Sp. z o.o. Work Environment
- Regulation No. 43/2017 on the rules of issuing supportive meals and drinks

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- Regulation No. 27/2017 on the prohibition of smoking cigarettes, smoking of innovative tobacco products and electronic cigarettes within premises and means of transport in PAK Górnictwo Sp. z o.o.
- Regulation No. 52/2017 on detailed training rules in the field of health and safety
- Regulation No. 39/2017 on the rules for the allocation of work and protective clothing, personal protective equipment and personal hygiene for "PAK Górnictwo" Sp. z o.o. employees

Associated business risk

Among the risks associated with the employee issues there are several categories to be distinguished. In all the areas of functioning of ZE PAK SA Group it is necessary to guarantee the employment at an appropriate level, by positioning the Group's companies as attractive employers in the region. An attractive remuneration level compared to those offered by other local employers has allowed, on the one hand acquiring new people, and on the other, to connect them with the company, preventing the outflow of qualified employees. Simultaneously, the restructuring process that has been going on for many years caused that most vacancies were filled on the basis of the internal recruitment (shifts between departments and subsidiaries). However, such solutions have some disadvantages, i.e. no significant inflow of young employees from outside. Concentration on the people employed in the Group's companies, in the restructuring process, causes that the age average of the employees is increasing. Aging of the crew will then lead to an increase the number of people retiring. The prolonged collective disputes regarding the principles of remunerating employees may consequently cause social unrest and strengthened relations with trade unions, which is another risk factor.

Another dimension of risk associated with the employees is the one of health and safety aspect. It is strongly dependent on the threats on particular workplaces and all the activities in the area of health and safety management concentrate on eliminating and reducing the threats and minimisation of accidents' consequences, if there are any.

Key indicators

- a. Employment structure at the end of the year by type of contract (in persons at the end of subsequent periods)

	2017			2016		
	women	men	total	women	men	total
<i>By type of contract</i>						
Work contract for an indefinite period	495	4640	5135	545	5087	5632
Work contract for an definite period	25	472	497	46	505	551
Work contract for a trial period	0	15	15	1	13	14
Civil-law agreement	12	117	129	13	135	148

- b. Employment structure at the end of the year by type of position, education and age (in persons at the end of subsequent periods). The structure does not include the civil law agreement employees.

	2017			2016		
	women	men	total	women	men	total
<i>By type of position</i>						
Managerial position	53	244	297	63	287	350
Non-managerial position	467	4 883	5 350	529	5 319	5 848
<i>By education</i>						
Higher (bachelor, master, postgraduate, doctorate, professor)	298	1 129	1 427	328	1 203	1 531
Medium (high school, technical college, college, post-secondary)	186	1 919	2 105	216	2 180	2 396
Professional (basic, learning a profession)	26	1 756	1 782	36	1 897	1 933
Basic (elementary, junior high)	10	323	333	12	326	338

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<i>By age</i>						
Up to 30 years old	31	521	552	46	653	699
31 to 40 years old	73	851	924	97	908	1 005
41 to 50 years old	146	2 242	2 388	151	2 483	2 634
Over 50 years old	270	1 513	1 783	298	1 562	1 860
Total	520	5 127	5 647	592	5 606	6 198

c. Newly employed during the year (in persons in the given period)

	2017			2016		
	women	men	total	women	men	total
Up to 30 years old	1	36	37	11	101	112
31 to 40 years old	2	32	34	5	49	54
41 to 50 years old	2	38	40	9	50	59
Over 50 years old	5	9	14	2	29	31
Total	10	115	125	27	229	256

d. Leaving work during the year (in persons in the given period)

	2017			2016		
	women	men	total	women	men	total
Up to 30 years old	3	73	76	6	124	130
31 to 40 years old	7	80	87	7	135	142
41 to 50 years old	6	145	151	7	205	212
Over 50 years old	40	154	194	27	260	287
Total	56	452	508	47	724	771

e. Diversity in the boards of the Company (in persons at the end of subsequent periods)

<i>Amount</i>	2017	2016
<i>Management of ZE PAK SA:</i>		
– Total	4	5
– Women	2	2
– Men	2	3
<i>Supervisory Board of ZE PAK SA:</i>		
– Total	8	7
– Women	0	0
– Men	8	7

f. Accidents at work

	2017	2016
Total number of accidents (injured), including:	62	54
– Light	62	53
– Serious	-	-

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– fatal	-	1
Number of lost days	4 573	3 321
Frequency ratio of injured in total accidents (per 1000 insured)	9.6	7.5
Frequency ratio of injured in serious and fatal accidents (per 1000 insured)	-	0.138

g. Number of employees exposed to health harmful factors and those connected with the work burdens (in persons at the end of subsequent periods)

	2017	2016
Noise	286	286
Dust	67	106
Insufficient lighting	324	350
Energy expenditure	1 358	1 097
Nuisance at work – night shift work	3 387	3 057

11.4. Environmental issues

Management approach

Similarly to other areas, the foundation of policies and ZE PAK SA management's approach to environmental issues were defined in the Strategy for Corporate Social Responsibility of ZE PAK SA Capital Group for 2017-2020. Simultaneously, it is important to remember about the obligatory certified management systems covering the environmental issues, including:

- the process of electricity and heat production with all the auxiliaries, identified environmental aspects, threats, legal and other requirements (ZE PAK SA),
- works in scope of installations, renovations and service of power engineering and industry equipment, industry construction services, management of investments in power engineering and industry, as well as modernization and maintenance of automation and electrical systems in power engineering (Przedsiębiorstwo Remontowe PAK Serwis Sp. z o.o.).

They contain the environmental policies of selected companies with particular procedures periodically reviewed and optimized. Their goal and the objective of the Corporate Social Responsibility Strategy of ZE PAK SA Capital Group for the years 2017-2020 is to provide stable and safe lignite mining, energy production and service and modernization work for the environment.

Simultaneously, selected management aspects, falling within a broader scope of environmental management, are regulated by internal principles and ordinances. They often reflect the legal provisions obligatory not only in the country, but also relating to a specific project, object or installation. The latter, i.e. environmental impact reports, and their detailed description of the foreseen activities of the planned project on the environment, constitute in itself an obligatory reference point for the managers of particular facilities and installations. This approach is extremely important. It should be realized that not universal management systems, but environmental impact reports, on the one hand refer to the specificity of the conditions of a given investment, and on the other, unlike many other procedural solutions, they are created through dialogue and open consultations with the environment. Therefore, solutions minimizing the impact on the natural environment are developed with the participation of stakeholders (local government, administration, local community, environmental organizations). They also recognize the unique specificity of each place, which is important, for example, in the case of opencast mines because even if they are located close to each other, the prevailing conditions (e.g. geological, hydrological, location of human settlements) will be at most similar but not identical. Therefore, the approach to environmental management and limiting the negative impact on the natural environment may also be similar, but not identical.

The starting point for policy and procedures based on it is the nature of the impact of business operations on the natural environment. It is associated with identified risks, to which specific and constantly improved procedures and technological solutions correspond. Defining briefly the nature of the impact on the environment, they should be divided into the impact associated with mining (lignite mining) and energy production.

In case of open pit mines, basic aspects of influence on natural environment are the following:

- impact on the surface area (opencast mining of minerals consists in the transformation of the land surface, instead of the land that was originally used, spatial terrain forms (excavation, heap) and accompanying infrastructure (conveyors, transport routes, facilities),
- impact on surface waters (including reduction of flow in watercourses under the influence of the mine's operation and increase of flow in watercourses due to discharge of water coming from underground drainage and surface opencast),
- impact on groundwater (formation of the so-called depression funnel due to the drainage of open-cast mines),
- noise emission (basic machines related to the operation of the overburden and its dumping, basic machines mining coal, coal and overburden conveyors, road transport),
- influence of mining objects on the atmospheric air:
 - dust emission: technological (mechanical), i.e. associated with mechanical mining and transport of the raw material with conveyor belts; climatological, i.e. related to wind erosion of vegetation-free areas;
 - organized emissions of pollutants into the air from the boiler room providing heat for social facilities mine,
- an influence on valuable natural area (in case when the valuable natural area is located in the zone of influence),
- hazards associated with electromagnetic fields.

In case of producing energy in conventional lignite power plants the following aspects of influence on the environment are to be distinguished:

- emissions of compounds accompanying coal combustion, e.g. CO₂, SO₂, NO_x
- dust emissions,
- noise generation (e.g. due to the operation of power unit turbines),
- waste generation (in the process of lignite combustion and flue gas cleaning),
- possible oil leaks, mazout and acids spills, resulting in local contamination of the ground and water environment,
- heating of surface waters, lakes (due to the use of lake surface waters in the cooling process),
- leakage of ash pulp or supernatant water to the soil and water environment,
- emission of industrial wastewater,
- emission of electromagnetic fields,
- terrorist threat that may result in environmental contamination.

In the mining area, the majority of the key activities, aiming at preventing, limiting or compensating nature of negative environmental impact, are initially planned at the stage of environmental analyses and creating a report of influence on the environment. In addition to technical and engineering solutions (appropriate formation of the dump, planning solutions to minimize the effects of disruption of water relations due to the drainage of opencasts, etc.), impact norms are defined in specific environmental aspects and environmental monitoring is carried out throughout the entire life cycle of the opencast mine. The monitoring of the level of water in wells, watercourses and water reservoirs, the quantity and quality of water discharged to receivers (water and ground), the extent of the depression funnel, dust emissions, noise level etc., is carried out as well.

From the procedural side, the situation in the manufacturing area looks quite similar. On the one hand, the existing production installations, which have been in operation for many years, have been modernized and retrofitted with technological solutions connected, above all, with adjusting them to the increasingly tightening environmental standards. As a result of the modernization of two blocks at Pańków power plant and the construction of the third one (Pańków II power plant) in recent years, the efficiency of generation (and thus the efficiency of fuel use) increased on those plants, and on the other hand, the emissivity decreased, including CO₂ mass per unit of electricity produced. Such approach also allowed reducing radically the emission of harmful nitrogen, sulphur oxides and dust to the atmosphere. At the beginning of 2018, Adamów power plant finished its work. The power plant has previously used derogation from the IED Environmental Directive in the scope of 17.5 thousand working hours, i.e. during the derogation period it was applicable to the size of the permissible emission of pollutants to the air, which were defined in the integrated permit as binding on 31 December 2015. In practice, this should result in a decrease in the average level of emissions per unit of electricity produced by the Group.

Similarly to the mining area, key environmental impact parameters during electricity production are monitored, often in a continuous mode. The cases of reports about potential irregularities are checked in a similar manner.

Mining area

In the last year, opencast mines managed by PAK KWB Adamów SA and PAK KWB Konin SA carried out:

- quantity and quality monitoring of groundwater and surface water,

- nature monitoring, particularly valuable areas,
- technical and biological reclamation,
- investments, primarily related to hydro-technical constructions, in accordance with the administrative decisions obtained.

At PAK KWB Adamów SA in 2017, the following were made, among others: groundwater monitoring (in piezometers, farm and drainage wells), surface water monitoring (flow tests in river channels in the area of impact) and monitoring of vegetation in Warta River interval (determining the impact of Koźmin opencast on the variability of water conditions and vegetation of "Natura 2000" area), as part of natural compensation, the area of the "island" was mowed in the fork of Warta and Ner rivers. In PAK KWB Konin SA there were made, among others: monitoring of birds, natural habitats and plant species in the vicinity of Tomisławice open pit, monitoring of the impact of Drzewce open-pit on water-marsh birds being the subject of a special bird protection area in Central Warta Valley. The water environment of PAK KWB Konin SA open pit was monitored for the outlets of Tomisławice, Józwin, Drzewce and open pit areas where the exploitation was already completed, i.e. Kazimierz and Lubstów. In the past year, as part of the natural compensation and care for creating the friendliest conditions, among other things 15 artificial floating platforms for the black tern on the old river bed in the Central Warta Valley (Drzewce open pit) have been installed.

In the areas where the exploitation of the fields has already been completed, technical and biological reclamation are carried out in the water, forest, agricultural, recreational and other areas. For instance, in 2017 a technical reclamation was carried out on 223 hectares, biological reclamation on 750 hectares. As part of the biological reclamation over 373.5 thousand trees and shrubs were planted. At PAK KWB Adamów SA, among others, there were completed the works on sacking "Głowa" reservoir and technical reclamation of areas adjacent to the reservoir. In PAK KWB Konin SA, among other things, a decision was made to complete the water reclamation of Lubstów reservoir on the former grounds of Lubstów with an area of 33 ha, and flooded part of Kleczew water reservoir in the excavation pit of Kazimierz Północ with an area of 177 ha was reported for acceptance.

The mines were also inspected by the Voivodship Inspectorate for Environmental Protection (environmental compliance control regarding Adamów and Tomisławice open pits), Regional Water Management Board in Poznań (control of Tomisławice open water drainage system), District Mining Office in Poznań (control of Noteć river flows, control of reclamation performance) and the Powiat Eldership in Konin and Turek (control of the obligation to reclaim). The inspection bodies did not identify any deficiencies, therefore no post-inspection orders were issued and no fines were imposed.

Generation area

In the generation area in 2017 the activities were concentrated traditionally on the aspects associated with air protection (emissions, nuisance), water and wastewater management (lakes monitoring, sewage and groundwater management), waste management, noise emission to the environment.

Air protection: emissions and nuisance

During the year the quantities of pollution emissions in particular power plants were monitored in terms of meeting obligatory emission standards. The correct operation of continuous measurement systems were supervised, functioning of procedures was coordinated (QAL3 – quality assurance procedures during the exploitation of exhaust emission monitoring system in ZE PAK SA in accordance with PN-EN 14181). Emission limits of particular contamination such as SO₂, NO_x and dust for Państw I and Konin power plants covered by TNK (Transitional National Plan) derogation were monitored, calculated and reported. The conditions determined in natural derogation of 17 500h for Elektrownia Adamów were monitored. The correct operations of protective devices reducing emission of pollutants into the air were supervised. The production process in aspect of meeting air pollution emissions' standards and limits was coordinated (optimization of combustion process in Państw II Power Plant). The tasks were realized under PRTR (National Register of Pollution Release and Transfer) by pollution measurements and reporting as well as by paying the fees. Financial commitments were made for the emission of pollutants into the air as part of its operations, i.e. environmental and penalty fees as well as in the scope of reporting pollutant emissions to the air.

Due to the emission influence on the immediate surroundings, the purity of the atmospheric air in the area of operations of the Groups power plants is also monitored. In 2017 no significant differences between the levels of substances tested and those measured by the stations of Voivode Inspectorate of Environment Protection were found. In 2017, measurement data collection system of air monitoring was renovated and adjusted to the current standards.

Lakes monitoring

Anthropogenic activities contributed to the creation of an aquatic ecosystem characteristic only for heated lakes in the area of Konin (Gosławskie, Państwskie, Ślesieńskie, Licheńskie, Wąsowsko - Mikozyńskie). However, Konin power

plants do not treat lakes only as an available source of water intake for cooling and a receiver of heated water, but they take measures to improve their purity and therefore carry out continuous monitoring.

Cooling system of Państw I, Państw II and Konin power plants works in the conditions changing during the year. The following parameters are changeable:

- the amount of circulating water,
- the temperature of drop water,
- the levels of water in the lakes,
- use the lakes for cooling (only „close” or “distant” circulation).

All the above mentioned parameters are covered by a constant monitoring. Systematic control of thermic conditions in the lakes and in the channels of cooling circuit of Państw I, Państw II and Konin power plants is run by ZE PAK SA on the principles determined in the integrated permit. This control includes:

- temperature measurements of Surface water in 24 points important for protection of lakes and operation of cooling circuit; the measurements are taken at least once a month (in the cold period) and more often (even every day) in the summer period (depending on the temperature of the air),
- continuous, automatic temperature measurement on the lakes' shots – Pańnowskie and Gosławskie,
- continuous, automatic temperature measurement of water on power plant discharges.

All the objects of cooling system are equipped with the network of control and measurement benchmarks. Measurements of water levels and flows are carried out in order to control the proper functioning of the entire cooling circuit. They are, among others, water level gauges, mounted on water intake and discharge ditches and on lakes. Fluctuations in water levels in lakes depend on a number of factors, mainly of natural character. However, the possibility of using water to cool the working blocks depends on its quantity and temperature. In all the lakes and channels included in the cooling circuit, physicochemical monitoring of water is also performed once a month.

Sewage management

Wastewater generated in power plants is treated in factory sewage treatment plants and after obtaining parameters compliant with applicable regulations, it is discharged to the receivers. However, for many years, in order to prevent lake water pollution, the power plants have been taking actions aiming at using the sewage in internal systems. Thus, wastewater from exhaust gas treatment installations, oily sewage from cleaning industrial floor and filter wastewater from a drinking water treatment plant are used for the production of ash and slag pulp, and therefore there is no need to use lake water as a transport medium for this purpose. Additionally, the lakes are not polluted with chemical substances. In 2017 there were performed some renovations, concerning the management of wastewater from Państw II power plant water demineralization station in flue gas desulphurization station. Wastewater was directed both to top up process water in absorbers as well as to sorbent preparation tanks (lime milk). The quality of sewage (their physical composition) does not have a negative influence either on the processes taking place in absorbers or on the sorbent quality, perfectly replacing water from Gosławskie lake. Wastewater management in the independent directions brings the possibility of their continuous and comprehensive collection. The above described solution allowed reducing the surface water intake from Gosławskie lake and caused no discharge of industrial wastewater to the environment. It causes financial as well as environmental savings.

Economical groundwater management

Technologies used to build the Group's power plants allowed for the use of deep water for technological purposes. On the basis of such technology, the station of demineralization water production in Państw I power plant was operating for many years. The plant was taking huge amounts of groundwater in order to produce demineralization water necessary for production of electricity. The current environmental regulations require such practices to be stopped in order not to diminish the aquifer. Therefore, Państw I power plant undertook to bring and use demineralised water produced in a modern, membrane-based treatment station. This station is supplied with surface water from Gosławskie Lake. This contributed to significant savings in groundwater intakes. Sewage from this station does not go into the environment, but is used in the internal system.

Wastes

In ZE PAK SA, the main stream of generated waste is furnace waste (ashes) and solid waste from calcium methods of flue gas desulphurization (gypsum). Waste generated in the first place is managed by external companies as part of waste recovery. On the basis of the volatile ash produced, mixtures for road foundations and road binders are mainly made. On the other hand, waste from flue gas desulfurization is directed mainly to the production of gypsum products,

drywall and cement plants. In 2017, over 325.5 thousand tons of furnace waste and 268 thousand tons of waste from calcium flue gas desulphurisation were sold. The remaining quantities of waste generated are directed to landfills belonging to the Company. The furnace waste and waste from flue gas desulphurisation produced in ZE PAK SA meet the requirements of environmental protection and do not threaten human life and health, which was confirmed by research in the field of physicochemical, toxicological and Eco toxicological properties performed for the registration of substances in accordance with REACH requirements.

At landfills managed by ZE PAK SA in 2017, monitoring of the quality of groundwater and surface water as well as supernatant water was carried out, with the frequency specified in the integrated permits and instructions for running landfills, i.e. once a quarter. Currently, ZE PAK SA has 4 landfills and all of them were exploited in 2017 on the following:

- solid waste landfill, Pątnów opencast (landfill for inert waste),
- landfill site for Zachodnia opencast with a vaporizer - so-called Wschodnia outcrop and landfill site (landfill for non-hazardous and inert waste),
- northern landfill site for Pątnów open pit (landfill for non-hazardous and inert waste),
- landfill of furnace waste in Gosławice open pit along with Linowiec vaporizer (landfill for non-hazardous and inert waste).

Monitoring was carried out in the primary and supplementary monitoring networks. Monitoring of groundwater quality is performed in a network of piezo metric wells located in the vicinity of landfills. In the last 3 years, new hydrogeological documentations have been developed for all landfills describing the hydrogeological conditions around landfills along with recommendations for groundwater monitoring. For some facilities it was necessary to make new openings, liquidate old ones, which required changes in existing permits and instructions for running the landfills. In 2017, this process was completed and currently the monitoring is already being carried out in the updated monitoring network. The quality of the groundwater tested in piezometers and deep wells in 2017 fluctuated in classes from I to V. Supernatant waters occurring in landfills (used for hydro transport of furnace wastes) were characterized by high mineralization, high electrolytic conductivity, high pH and total hardness. In addition, as a part of the monitoring of landfills, an annual assessment of slope stability and subsidence is also carried out. Most of the monitored slopes surveyed in 2017 proved to be stable.

ZE PAK SA also conducts reclamation of unused parts of landfills on an ongoing basis. In 2017, the reclamation of the closed part of the furnace waste yard of the Gosławice open pit was continued. The total area in which reclamation works were carried out last year amounted to over 30.8 ha.

As part of the protection of the earth's surface, ground and soil studies were also carried out. In 2017, samples were taken from various depth intervals and the content of heavy and petroleum metals was determined at Pątnów I power plant. Sampling sites were selected in locations where there is the highest risk of soil and water contamination, i.e. near storage and use of environmental hazardous substances.

Noise

As part of the obligation to monitor noise emitted to the environment, imposed by integrated permits for the fuel combustion installations in ZE PAK SA and Elektrownia Pątnów II Sp. z o.o., in 2017, noise measurements were taken from the area of Konin and Pątnów II power plants. No measurements were taken from Adamów and Pątnów I power plant because the measurements from 2015 and 2016 are valid.

Measurements made in the past year showed that there was no exceeding of the permissible values of noise in the environment, imposed by the integrated permit for Konin and Pątnów II Power Plant both at daytime and at night.

Inspections

In 2017 the Voivodship Inspectorate for Environment Protection in Poznań, Delegacy in Konin, inspected Elektrownia Pątnów I, Elektrownia Pątnów II and Elektrownia Konin:

- Elektrownia Pątnów I – inspection of sources covered by the Transitional National Plan at the request of GIEP (General Inspection of Environment Protection).
- Elektrownia Pątnów II – inspection of compliance with environmental protection requirements by operators of installations requiring an integrated permit.
- Elektrownia Konin – inspection of sources covered by the Transitional National Plan at the request of GIEP.

As a result of the activities carried out, no necessity to order any post-inspection activities was found.

Programs for the prevention of major industrial accidents

In 2017, programs for the prevention of major industrial accidents were updated in terms of type, amount and hazardous substances location as well as description of technological installations in the power plants. On the base of performed update of hazardous substances quantity, only Elektrownia Pańków I is in the group of plants where increased risk of major industrial accidents may occur.

Other

In PAK Górnictwo Sp. z o.o. due to the consolidation of activities carried out in the past year (within one company) previously covered by several entities, the majority of formal documents related to management, including environmental management, were formally developed and adopted in 2017. The following were adopted, among others:

- Regulation No. 34/2017 of the President of the Management Board - Chief Executive Officer of PAK Górnictwo Sp. z o.o. on determining the amount of fees for using the environment in PAK Górnictwo Sp. z o.o.
- Regulation No. 37/2017 of the President of the Management Board – Chief Executive Officer of PAK Górnictwo Sp. z o.o. on waste management and related Instruction on waste management and disposal.

Administrative decisions issued in connection with taking over the functions of other business entities of the Group (including water abstraction, collection and waste production) are also of key importance. The issue of water abstraction is connected with the takeover of the activity previously carried out by Aquakon Sp. z o.o. and the collection of groundwater from chalk deposits from two deep wells (production of mineral water). Another important aspect of the environmental impact is the collection and production of waste. It is mainly about waste generated in service and repair workshops and maintenance workshops, a conveyor belt regeneration hall, a repairs hall, and a bottling plant.

On the other hand, **PAK - Volt SA** (electricity trading, office work) a company significant in terms of generated revenues, should be considered irrelevant as regards the impact of the entire Group on the natural environment.

Associated business risk

The particular aspects of influence on the natural environment, described above, give rise to specific threats to business, reducing environmental resources at the same time. Each of the aspect described above, in certain situations (e.g. breakdown resulting in contamination or over-normative emissions), can cause image losses, social conflicts and loss of social allowance for operation, legal sanctions, imposing of penalty or other decisions resulting in reducing the profits, or finally incurring additional costs for environment protection. As a consequence, it may cause, for example, the disturbance in production stability (the need to temporarily shut down some part of the production installation), decrease of revenues (decrease in production) or increase of costs (e.g. the need to remove the consequences of a failure, but also additional fees and penalties related to emissions to the environment, including greenhouse gas emissions).

For this reason, as it was adopted in the Strategy for Corporate Social Responsibility of the ZE PAK SA Capital Group for 2017-2020, the policy and the procedures accepted by the Group, focus on:

- providing effective mechanisms reducing to minimum the threat of anomalies and gaps occurring resulting in over-normative impact on the environment in the mining or manufacturing process.
- reducing the emission to atmosphere to minimum by optimal shaping of the use of generation capacities existing in ZE PAK and ensuring the minimization of the risk of exceeding emissions of gaseous pollutants into the atmosphere.

Key indicators

Due to the fact that at the beginning of 2018 Adamów power plant ceased its operations, apart from cumulative data for the Group, data excluding the impact of Adamów power plant are also presented (columns marked '*'). Due to the fact that the termination of Adamów power plant operation does not significantly affect the ratios in other areas described in this statement, only in the case of indicators related to the issue, this solution was used for purposes of maintaining comparability in subsequent periods.

a. CO₂ emission (thousands of tons/TWh)

	2017	2017*	2016	2016*
CO ₂ emission in ZE PAK SA Group per production unit	1.16	1.12	1.11	1.06

ZESPÓŁ ELEKTROWNI PAŃNÓW – ADAMÓW – KONIN SA CAPITAL GROUP
MANAGEMENT BOARD'S REPORT
FROM THE CAPITAL GROUP'S OPERATIONS IN 2017

**excluding elektrownia Adamów*

b. SO₂, NO_x and dust emission to the atmosphere (thousands of tons /TWh)

	2017	2017*	2016	2016*
SO ₂ emission in ZE PAK SA Group per production unit	2.03	0.86	2.00	0.93
NO _x emission in ZE PAK SA Group per production unit	1.53	1.22	1.58	1.24
Dust emission in ZE PAK SA Group per production unit	0.27	0.09	0.29	0.10

** excluding elektrownia Adamów*

c. Violation of environmental standards (%)

Emitted amount resulting from exceeding the standards in relation to the total amount of emissions

	2017	2017*	2016	2016*
SO ₂	5.41	0.06	0.00	0.00
NO _x	0.00	0.00	0.00	0.00
Dust	15.59	0.00	13.52	0.00

** excluding elektrownia Adamów*

d. Summary of the data on the size of the areas where the technical reclamation was carried out and areas where biological reclamation and seeding are still being carried out, as well as the areas for which the decision on the properly completed reclamation have been made (hectares)

	2017	2016
Technical reclamation	223	220
Biological reclamation (in progress)	750	651
Biological reclamation (completed)	90	173

e. Share of land for which decisions on completion of reclamation were made for land excluded from agricultural and forestry production in mines (%)

	2017	2016
	148	81

11.5. Issues of respect for human rights

Management approach

While analysing the issues associated with the respect for human rights, there are two significant aspects that are to be distinguished: the right to associate and strike as well as the respect for the inalienable rights of the individual.

As already mentioned earlier, in the Group's companies meeting the statutory criteria, there are operating the Employees' Councils selected on the basis of applicable regulations. There are also a number of trade union organizations operating under the Trade Unions Act. The Management Boards of the Group's companies inform and consult all the decisions in matters specified by the law with employees' representatives (Employees' Council, trade unions). In the opinion of managers, freedom of association in trade unions and related rights are assured.

In the aspect referring to an individual and ensuring its respect, which means the respect for variety and simultaneous lack of any form of discrimination, beside the respect and enforcement of legal regulations that guarantee such a

respect (e.g. Labour Code), in 2017 ZE PAK⁹ adopted The Code of Ethics. Not only does it guarantee the aforementioned rights of an individual, but it is also a tool in itself that allows for the resolution of potential conflicts of interest. It contains a mechanism for both resolving doubts as well as reporting suspicions about potential behaviour that violates the provisions of the Code. It is worth mentioning that the Code of Ethics also condemns other behaviours that violate human rights, such as child labour, forced labour or slave labour.

Associated business risk

The disrespect for human rights, including aforementioned right to associate and strike, would mean not only the breach of national law (and sanctions in consequence), but also could lead to unnecessary escalation of conflicts on the employer-employees line. Despite the existing differences of opinion, manifesting, for example, with a collective dispute, the managers of ZE PAK SA Group appreciate the role of trade unions. Theoretical tightening of disputes, while not having a dialogue, can lead to strike actions and threaten the stability of production. Trade unions and the management, despite disputes and different assessment of the situation (e.g. in terms of short and long-term approach), are constructively oriented and aware of the economic consequences of a possible imbalance in the stability of energy supplies. Such consequences could concern not only the Group but also the national energy system.

Regarding the risk of disrespect for individual rights, such cases can not only expose ZE PAK SA Group to litigations and necessity to pay compensations, but they are primarily a real threat for organisation culture, work atmosphere and the same its effectiveness. They are also associated with the risk of losing valuable employees or, through discrimination, the impossibility of making full use of their potential (e.g. promotion of people with lower competences, while inhibiting the promotion of discriminated people).

All the cases of disrespect for human rights in ZE PAK SA Group also mean a measurable reputational risk, and then, with the escalation of this type of phenomena it can affect the loss of social consent for acting.

Key indicators

	2017	2016
the number of cases of reporting suspicion of unethical behaviour under the mechanisms provided for by the Code of Ethics for violation of individual rights	2	n/a
Unionization ratio	47.74%	47.92%
Number of collective disputes	4	4
Number of work days lost due to strike actions	0	0

11.6. Issues related to counteracting corruption

Management approach

One of the purposes of ZE PAK SA Capital Group Strategy for Corporate Social Responsibility adopted in 2017 is providing high quality and constantly improved management system that in the process of taking decisions would include the social and environmental aspects. One of many solutions of such management system is counteracting potential corruption and other unacceptable unethical phenomena. The threat of such phenomena depends, among others, on the exposure to the risk of corruption behaviour (e.g. a range of realized investments and projects), organizational culture and ethical values as well as the effectiveness of inspecting system.

The range of contracts concluded and investments undertaken depends on the factors other than the threat of corruption phenomena. It is frequently a consequence of adopted strategy of development, and therefore from the managing point of view in terms of counteracting corruption, it should be treated as an independent factor. The other thing is the way of realizing contracts, including for instance the way of choice, evaluation and selection of suppliers and subcontractors. Regarding the choice, this issue is regulated in ZE PAK SA Groups by the procedures of management systems.

The factor influencing the degree of danger of such type phenomena is a proper organizational culture, i.e. the culture based on ethical values and such institutional solutions that provide the employees with the implements enabling them to determine and distinguish the behaviours within the company that are right and the ones that are not. The promotion of ethical values allows resolving potential conflicts of interest or doubts in this regard, as well as reporting suspicions

⁹ It is planned to implement analogous solutions in subsequent companies of the Capital Group.

about potential unaccepted behaviours, including those of bearing the signs of corruption. For this reason, while implementing the provisions of the Strategy for Corporate Social Responsibility for years 2017-2020, the Management of ZE PAK SA decided to adopt the Code of Ethics in 2017.

Another aspect, worth attention while analysing the system of counteracting corruption is the internal system of inspection. "Rules of Internal Audit of Zespół Elektrowni Pątnów-Adamów-Konin SA" and "Rules of Internal Supervision of PAK KWB Konin SA" determine the rules of organizing and functioning of internal audit that provides the systematic and methodological approach to evaluation and improvement of the effectiveness of supervision as well as management of risk and organization processes. They include the research and evaluation of activities of organizational units and the Group's subsidiaries in terms of thriftiness, legality, advisability, reliability and transparency of documentation (processes). The inspection activities aim at disclosure of unused business provisions, detection of irregularities and abuse in the operations of organizational units, determination of causes and effects of irregularities found and persons responsible for them, as well as elaboration of conclusions and post-audit recommendations. Among the irregularities and abuse there are also all activities that may be characterized by bribery and corruption.

The internal inspection system includes: self-control of the correctness of work performance, functional and institutional control (implemented by the internal audit unit). As part of the institutional control, the internal audit unit checks the activity of the organization as a whole, responding to the needs reported by the Management Board and the Supervisory Board in accordance with the audit regulations (among others, evaluates the coordination of activities between workstations and organizational units, evaluation of the creation system and documentation flow and information, etc.) with a frequency depending on the identified risk areas and the level of risk significance, as well as the role of control in its reduction. In this context, the activities of the internal control unit supplement the basic control and ongoing supervision and are aimed at revealing weaknesses or gaps in the organization and functioning of the internal control system. Controls are planned (in accordance with the annual plan approved by the Management Board), ad hoc (at the request of the Management Board or the Supervisory Board) and the one of checking nature.

The purchasing procedures described in the management systems applicable in the companies of the ZE PAK SA Group also regulate the issues of supplier selection. In the case of generation area, ZE PAK SA has implemented the Integrated Management System, under which in Sector 5.3 "Product / service support" applies, among others two procedures 5.3 - 01 "Supplier assessment" and 5.3 - 02 "Identification and traceability". The basic condition in the selection of suppliers is that they should be specialist suppliers, meeting agreed technical and commercial conditions and guaranteeing 100% reliability of deliveries. In addition, suppliers whose products decide directly on the quality of electricity and heat are subject to qualifications based on ongoing cooperation with suppliers, delivery control and periodic evaluation, among others, through their auditing as well as updates of the list of qualified suppliers. The management system also introduces "Supplier assessment sheets". In addition to the obvious factors such as the quality of deliveries, the level and stability of prices and payment conditions, for example, timeliness, or the fact that suppliers have certified management systems are taken into account.

Simultaneously, the purchase process itself has been defined in ZE PAK SA by the "Rules of Supplier Selection". The process is supported by the electronic purchase platform which eliminates some of the threats, for instance, it prevents from getting acquainted with offers submitted before the deadline. Thus, it eliminates the risk that dishonest employee could provide the information of competitive bids to the supplier who is still working on the offer. It is worth mentioning here, that the purchase process is based on the electronic auction option, which is carried out in real time, and this limits the possibility of unethical contact with a potential supplier. Moreover, until the auction closes, employees are not able to observe its progress, i.e. offers submitted by individual tenderers. They can read them only after the auction process is closed. ZE PAK SA makes purchases in the area of generating electricity.

The purchase for mining area are made by PAK KWB Konin (including the purchase for PAK Górnictwo Sp. z o.o.) and by PAK Serwis Sp. z o.o. for service area. Nevertheless, although each of the areas makes purchases on the basis of their own regulations, they are very similar to each other as to the shape of the process itself. They use the same tools, including the same electronic purchase platform. Approximately, the purchase procedure is initiated by a substantive unit that reports a specific purchase need. After obtaining relevant approvals justifying the future purchase, a commission which defines the purchase criteria is appointed¹⁰. The commission makes an assessment of the collected offers and points out the recommended supplier. In the next step, negotiations are conducted, and finally the accepted offer is directed to implementation. From the perspective of transparency, the important thing is that the information on planned purchases (i.e. request for quotations and tender inquiries) is published on the electronic purchase platform as well as on the website, and the purchases themselves are usually open tenders. Simultaneously, all areas, including the aforementioned purchasing area, are subject to be controlled by internal audit staff, also in terms of the potential occurrence of corruption-related phenomena. Controls may be planned as well as ad hoc inspections. The employees of

¹⁰ In case of mining area the members of commission are appointed right after the collection of the bids.

the internal audit unit have an access to all information and reports necessary to perform the control activities in a reliable and objective way. Auditors are therefore obliged to inform the auditing manager on an ongoing basis about the course of the audit and the difficulties encountered in the implementation of the audit tasks. Auditing manager presents an assessment of the implementation of the audit's objective to the Management or the Supervisory Board. The auditors are authorized to: enter all the objects and rooms of the audited unit; inspect all recording devices, plans, reports, protocols and business memos or correspondence as well as other documents and materials associated with the controlled unit operation; periodical assisting at all activities of controlled unit; request for clarification and any information (oral or written) related to the subject of the control, from the manager and other employees of the controlled unit; requesting the head of the audited entity to perform partial or complete inventory of certain assets at the indicated date and to commission calculations, draw up lists, analytical statements, copies, extracts, etc.; receiving declarations from employees and other persons in matters related to the activity of the controlled entity; determine the real states by means of measurements, situational sketches as well as photo and recordings etc.; take necessary actions to secure evidence and property in case of irregularities; request the management of the audit with an application for the appointment of experts, in case of a justified need to make an expert report; ask the head of the controlled entity to provide all means necessary for a smooth inspection and for the effective implementation of conclusions resulting from the audit findings; performing control activities at the time selected by the inspector and extending the subject of controls in justified cases without obtaining additional consent of the manager of the control. The manager of the controlled unit is obliged to provide the auditor with the appropriate working conditions and technical assistance necessary for the efficient control.

If there are any circumstances threatening for human health or life, or any other resulting in the loss of goods due to the mismanagement, negligence, prodigality or an offense found during the inspection, the auditor makes a written request to a manager of the controlled unit, obliging him to take immediate action in order to eliminate such incidents. The auditor informs immediately audit management unit and secures the evidence documents and items of mismanagement or an offense. Then, after receiving the legal advice, a person managing the audit takes a decision to inform law enforcement authorities.

Simultaneously, each employee of ZE PAK SA Group, in the case of suspicion of any unethical behaviour, including those of bearing the marks of corruption, has not only the possibility but obligation as well to report information using the mechanisms provided by the Code of Ethics. For this purpose, the employee can contact the superior or the person indicated by the Management and acting as Ethics Spokesman. Such a notification is analysed, and an employee who has reported the information cannot be in danger of any consequences and will be protected from any retaliation, even if the information was not confirmed but was reported in good faith.

Associated business risk

The risk of corruption behaviours accompanies every enterprise, and the cases of making decisions by corrupt employees lead, among others, to suboptimal choices in purchasing processes, in terms of price increase, as well as, for example, improper quality of products or services, untimely delivery or performance of services, or the consent of a corrupt employee to other, inappropriate contractor behaviour (e.g. breaking regulations, failure to carry out warranty repairs, etc.). Undoubtedly, the corruption and bribery can take a number of other forms, and may be connected with giving benefits by the employees to officials for issuing favourable decisions, etc. As a consequence, the organization may be exposed to threats related to unjustified increase of costs as well as, for example, huge image losses.

Simultaneously, in terms of assessing the exposure of ZE PAK SA Group to the risk of corruption, a relatively small scale of high-value orders is important. Unlike many other electricity generators, the business model of the ZE PAK SA Group is based on a strongly integrated value chain, i.e. energy production is based on its own raw material resources. Thus, the supply of raw materials takes place inside the organization (understood as a capital group), and not from external entities. Service work is also performed in many cases by entities from the ZE PAK SA Group. As a consequence, purchases of products and services from the outside are limited to minimum, and that contributes to the reduction of risk, although it does not eliminate it. The risk of corruption may increase in the case of significant investments (e.g. construction or modernization of power units or opencast mines). However, in 2017 no large investments or upgrades were made.

Key indicators

	2017	2016
Number of suspicions of corrupt behaviour reported to law enforcement authorities	0	0
Number of people convicted by a valid sentence for a corruption offense	0	0

12. OTHER INFORMATION

12.1. Significant court proceedings

In 2017 Zespół Elektrowni Pątnów - Adamów - Konin SA and companies consolidated within the Group were not a party in proceedings pending before court, competent arbitration authority or public administration authority, whose single or total value would exceed 10% of the equity of ZE PAK SA except as described below.

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. Currently, the Company is expecting the determination of hearing dates before 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 Pańków 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 Pańków 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 KWB 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 KWB SA. On 7 January 2013, PAK KWB 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.

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.

Other court cases are described in the consolidated financial statements of the Group in point 34.1.

12.2. Significant achievements in the field of research and development

As at the date of this report, the companies from the ZE PAK SA Capital Group do not conduct research and development works that would be of significant importance to the Group. In addition, during the past year, the Group did not make any significant financial outlays for research and development.

12.3. Information on the auditing of the financial statement

The Agreement on the Company's financial statement audit and the Group's consolidated financial statement with the entity entitled to audit financial statements, i.e. Ernst & Young Audyt Polska, a limited liability company, a limited partnership, with its registered office in Warsaw, Rondo ONZ 1, was concluded on 19 June 2017.

The information regarding the remuneration of the entity authorised to the audit of financial statements was presented in section 38 of the Group's consolidated financial statement for 2017.

12.4. Financial forecasts

The Capital Group did not publish financial forecasts for 2017 and it will not present the forecast for 2018.

Konin, 19 April 2018

Adam Kłapsza
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