

ZESPÓŁ ELEKTROWNI PAŃNÓW – ADAMÓW – KONIN SA

MANAGEMENT BOARD'S REPORT FROM OPERATIONS OF ZE PAK SA 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 financial data</i>	<i>zloty thousand</i> <i>12 months 2017</i> <i>period</i> <i>from 01.01.2017</i> <i>to 31.12.2017</i>	<i>zloty thousand</i> <i>12 months 2016</i> <i>period</i> <i>from 01.01.2016</i> <i>to 31.12.2016</i>	<i>euro thousand</i> <i>12 months 2017</i> <i>period</i> <i>from 01.01.2017</i> <i>to 31.12.2017</i>	<i>euro thousand</i> <i>12 months 2016</i> <i>period</i> <i>from 01.01.2016</i> <i>to 31.12.2016</i>
Net revenues from sales of products, goods and materials	1 477 055	1 622 180	347 976	370 725
Operating profit/loss	86 088	73 686	20 281	16 840
Profit/loss before tax	103 514	137 305	24 387	31 379
Net profit/loss for the period	90 637	131 407	21 353	30 031
Net cash flow from operating activities	173 618	96 249	40 902	21 996
Net cash flow from investing activities	34 003	23 102	8 011	5 280
Net cash flow from financing activities	(229 788)	(132 824)	(54 135)	(30 355)
Net cash flow together	(22 167)	(13 473)	(5 222)	(3 079)
Net profit per share (in zloty/euro per share)	1.78	2.59	0.42	0.59
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547
	<i>as of</i> <i>31.12.2017</i>	<i>as of</i> <i>31.12.2016</i>	<i>as of</i> <i>31.12.2017</i>	<i>as of</i> <i>31.12.2016</i>
Total assets	2 367 870	2 598 206	567 712	587 298
Fixed assets	2 021 250	2 219 586	484 608	501 715
Current assets	346 620	378 620	83 104	85 583
Equity	1 516 912	1 491 837	363 689	337 215
Share capital	101 647	101 647	24 371	22 976
Liabilities and provisions for liabilities	850 958	1 106 369	204 023	250 083
Long-term liabilities	203 524	344 005	48 796	77 759
Short-term liabilities	289 597	387 209	69 433	87 525
Book value per share (in zloty/euro per share)	29.85	29.35	7.16	6.63
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 concerning the profit and loss account and cash flow 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 balance sheet items 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, Energoinvest SERWIS sp. z o.o. in liquidation. All the above-mentioned companies are consolidated.

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 Pałnów 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: Pałnów II – equipped with a supercritical power unit, Pałnów 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 Pałnów 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.

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

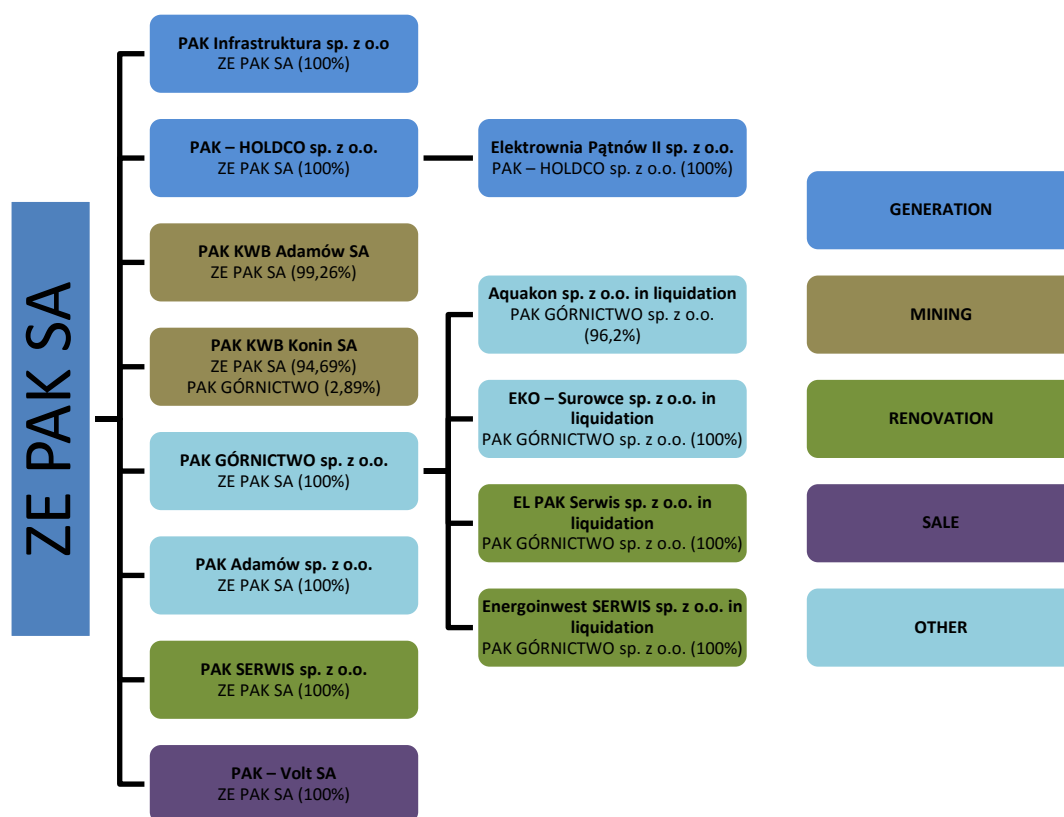


Table 1: Description of the Group's companies (excluding ZE PAK SA)

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%*
Energoinwest Serwis	62-510 Konin	Repair-construction service	100.00%*	100.00%*

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. and 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.

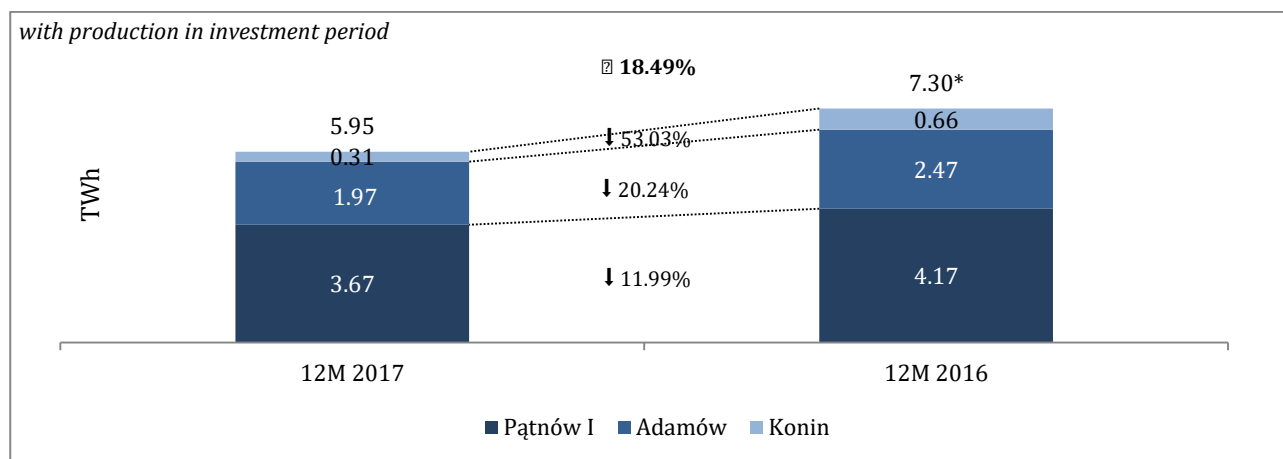
- On 16 October 2017 a new subsidiary has been set up – PAK Adamów Sp. z o.o., in which ZE PAK SA holds all the shares. The appointment of the new subsidiary company is related to preparation of the processes of terminating the activity of Elektrownia Adamów.

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

Operations of ZE PAK SA are focused in several areas. The main area is doubtlessly generation of electricity, 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 sale of heat. In 2017, ZE PAK SA 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 foreign partners.

The Company 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. Total electricity production in all power plants of the Company in 2017 was lower by 18.49% compared to the previous year.

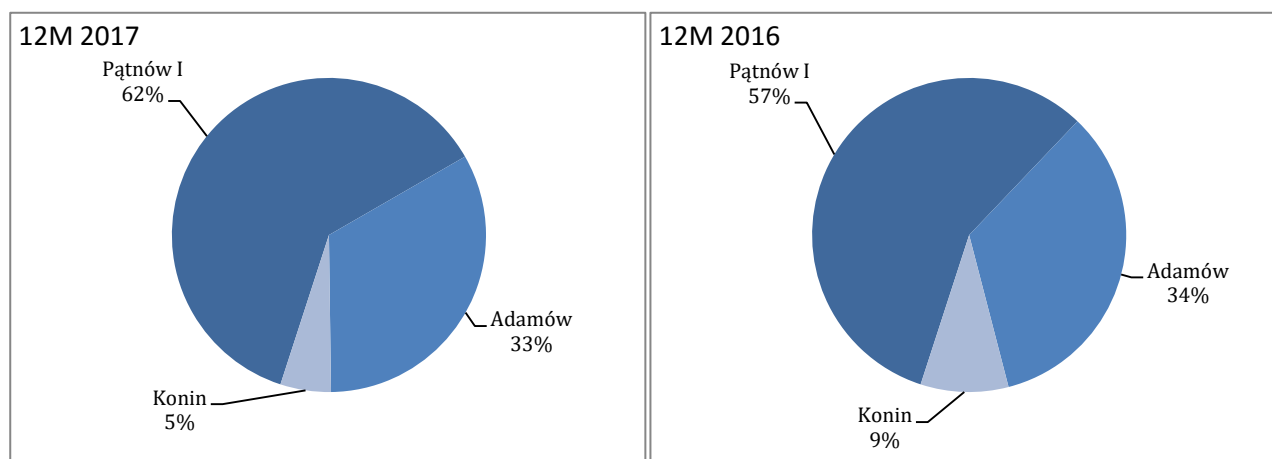
Chart 1: Net electricity production*



* 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 2: The structure of production divided into individual power plants



Source: internal data

The main direction of electricity sales in 2017 was sales in scope of bilateral contracts concluded with electricity trading companies operating on the Polish market. The transactions with final recipients represented only a small share in the total volume of electricity sales. The second largest direction of sales in terms of volume was the stock market. The balancing market for electricity was the supplement of the sales structure.

Revenues from the sale of electricity (total - generated and from resale, reduced by excise duty) accounted for 88.95% of the total revenues from the sale of the Company.

The heat generated in the Company's power plants is sold to local customers. The main customers are city heat energy enterprises and local industrial producers. In 2017, the Company covered almost the entire heat demand of Konin and Turek. In 2017, the Company's power plants sold 1 912 TJ of heat. Heat sales accounted for approximately 3.87% of the Company'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 level of electricity production from the biomass block. It is the continuing trend of low prices of green certificates, constituting a support system, among others for producers of electricity from biomass, it resulted mainly from the decision about a very low level of electricity production 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 Company 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 0.05% of the total revenue of the Company. Other sales revenues accounted for 7.13% of the total revenue generated by the Company in 2017 and mainly related to services provided to other entities of the Group.

The main raw material used by the Company for electricity 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.

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 within the accounting year

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 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.

Currently, there are two disputes in the Company, in which trade union organizations refer to the provisions of the Act on solving collective disputes.

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.

Significant events after balance sheet date

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

3.2. Significant agreements concluded within the accounting year

Significant agreements for the Company's activity

Because of the characteristics of the activity and the market, in which the ZE PAK SA 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 Company concludes framework agreements with particular counterparts setting out the basic terms and conditions of cooperation. On the other hand, the purchase / sale itself is made in separate transactions with reference to specific quantities using current market prices.

Agreements regarding the obtained credits and loans

The company did not sign any agreements regarding loans and advances received in 2017.

Agreements regarding the granted loans

The Company did not sign any agreements regarding granted loans in 2017.

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>2017</i>	
Granted guaranties	-	-
- 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

	<i>Zloty thousand</i>	<i>Euro thousand</i>
	<i>2017</i>	
Obtained guaranties	16 698	5 149
- from companies from the Group	-	-
Obtained sureties	-	-
- from companies from the Group	-	-

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

In 2017, no agreements were concluded between ZE PAK SA and affiliated companies on terms different from market ones.

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 Pańnów

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.

Key investments in the preparatory phase

Elektrownia Konin

The most important project implemented so far in the design phase at Konin Power Plant was the construction of a gas-steam block together with gas pipeline in the line Koło-Konin. It was assumed that this block will have a capacity of about 120 MWe and about 90 MWt and an additional peak boiler with a capacity of about 40 MWt (dedicated to the needs of heat supply for the city of Konin). Putting the block into operation was planned for mid-2020. However, due to the existing unfavourable external conditions, including uncertainty as to the shape of the cogeneration support system after 2018, on 29 September 2016, the Company terminated the contract with PSE SA for connecting a gas and steam unit in Konin Power Plant to the transmission network. In October, another contract was also terminated with the Energoprojekt-Katowice SA project office responsible for the design of the gas-steam block and gas pipeline in line between Koło-Konin. Despite the contracts terminated, this project is still in the company's investment program.

After many years of operation of the turbogenerator No. 6 at Konin Power Plant, it was upgraded in 2012, including it to the block system producing electricity based on the biomass combustion. During the modernization of the generator, its cooling medium was changed from hydrogen to air. After such a modernization, the generator was seriously damaged twice during operation; the main reason of the damage was elements of the modernized cooling system. In view of the above, the generator modernization contractor, referring to the current experience of modernization of generators carried out in recent years, after implementing its own calculation models, recommended that the active power load of generator no. 6 installed in Konin Power Plant should not exceed 50 MW. The last modernization works of the generator 6 cooling system ended in January 2017. After the modernization, ZE PAK SA asked the President of the Energy Regulatory Office to change the data in the concession for the generation of electricity in generation unit 1 of Konin Power Plant. The application concerns determination of the available and installed power for turbogenerator No. 6 at the level of 50 MWe (previously 55 MWe).

In the first half of 2016, study work was also started to prepare for the alternative solution of heat source reconstruction at Konin Power Station, which would ensure delivery of heat to Konin city after holdup of Konin Power Plant in June 2020 and failure to start the planned new gas and steam unit. The production of electricity and heat in cogeneration

would be based on the existing biomass boiler. As part of the implementation of the above-mentioned project, the promise of amending the concession for the production of electricity and heat in a dedicated biomass combustion installation has already been obtained from the Energy Regulatory Office.

In addition, in Konin Power Plant there is currently undergoing design work related to the development of the Essential Terms of Reference (SIWZ), which will be the basis for selecting the contractor for modernization of the TG-6 turbine in order to adapt it to the heating of network water supplied to the city of Konin.

3.4. Risk management

While conducting its operations, the Company is exposed to a series of risks, occurring actually, potentially or theoretically, existing in the industry as well as on the markets where it operates. These are factors having their source within the Company as well as in its environment. Taking into account the formalization of the risk-related sphere in the Company'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, ZE PAK SA did not issue or redeem securities.

4. MAIN BUSINESS RISK

The process of forecasting future results of ZE PAK SA must include a wide range of factors, actually, potentially, or theoretically, existent in the branch and markets, in which the Company conducts its activities. These are factors which originate both from the inside of the Company 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 Company's results include the following:

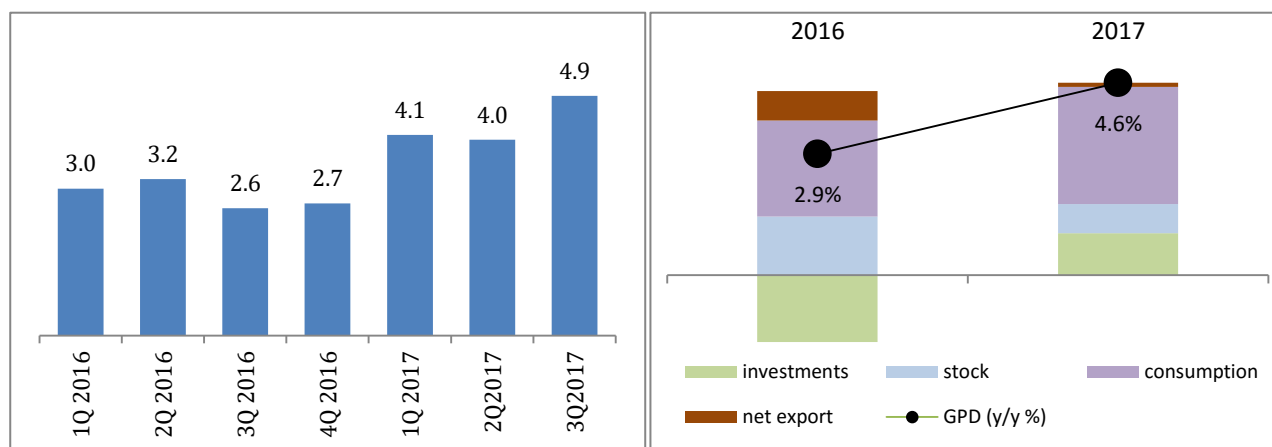
- macro-economic trends in the Polish economy and the demand for electricity;
- regulatory environment;
- electricity prices;
- prices and supply of certificates of origin;
- extraction and supply costs of coal and other fuel;
- CO₂ emission allowances costs;
- compensation for the stranded costs related to the termination of PPA of Elektrowni Pańków 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 analogous quarter of the previous year and yearly GDP dynamics by components

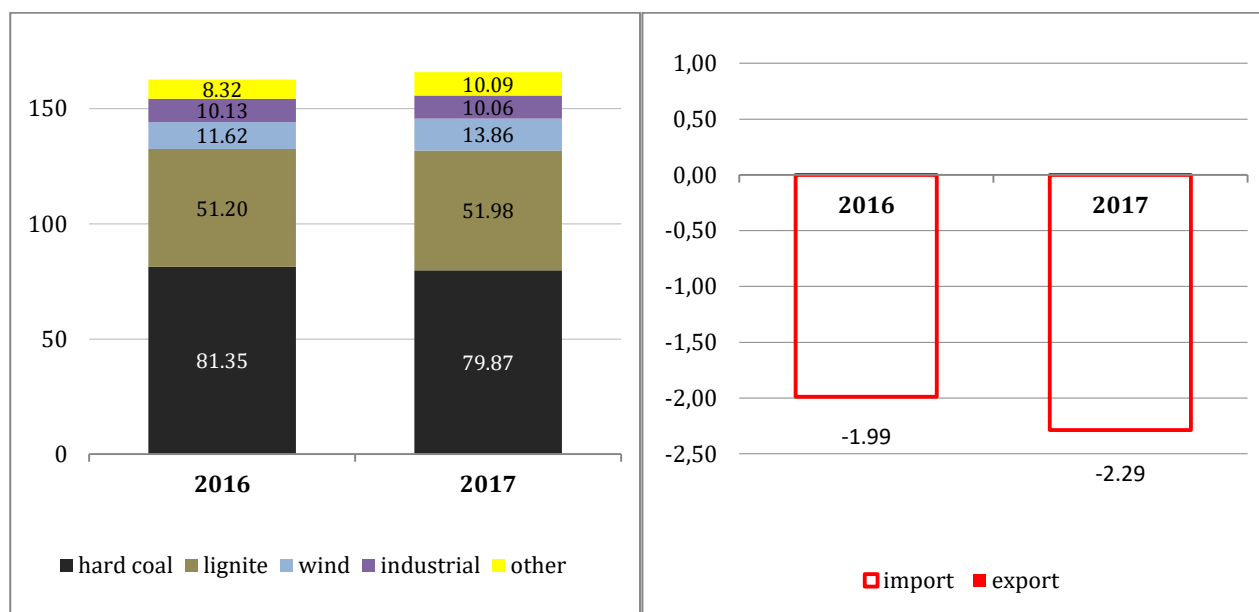


Source: GUS data

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 elaboration 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 consumption¹ 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 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 MW² – 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%. The annual increase in wind generation by 19.2% was recorded once again. 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 MW³. 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

¹ 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.

² 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.

³ 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.

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, NO_x, 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. Lack of amendment to 31 July this year according to the Ministry of the Environment would imply a penalty imposed on Poland by the European Commission and a loss of some European funds, among others for flood prevention. The provisions of the amended law will come 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 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 Company 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.

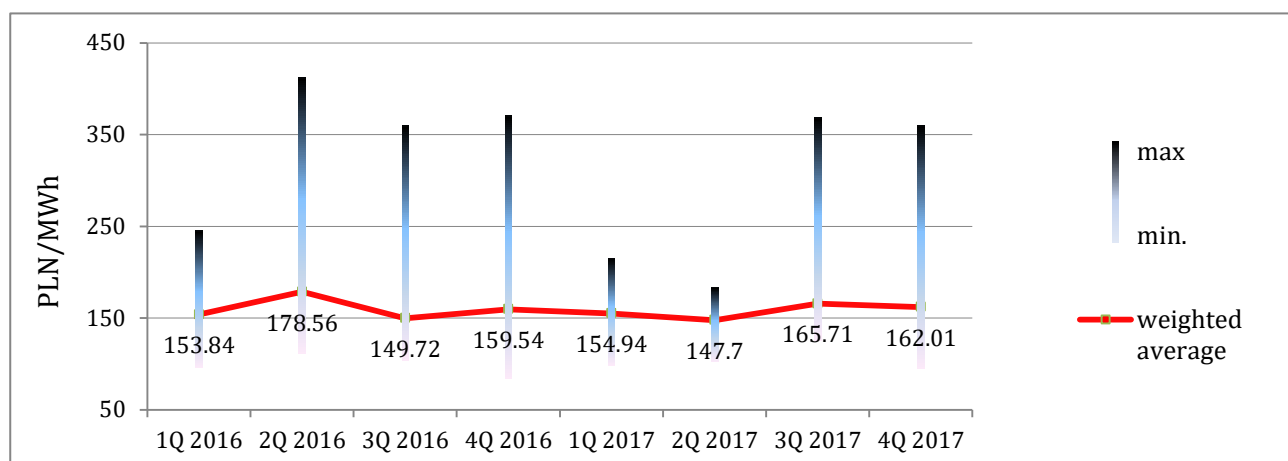
In 2017, the weighted average energy price decreased in relation to the previous year. The weighted average of the IRDN (Day-Ahead Market Index) on the Polish Power Exchange (PPE) for 2017 was at the level of 155.56 PLN / MWh, which means a decrease in relation to 2016 by 5.15 PLN / MWh, i.e. by 3.2%. 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 caused 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 MW⁴ of wind turbine power, which means a symbolic increase of only about 38.4 MW, but due to excellent wind conditions, especially in the third and fourth quarter, the increase in electricity production from wind farms amounted to 19.2%⁵. 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 12%⁶. 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.

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

⁵ 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."

⁶ 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.

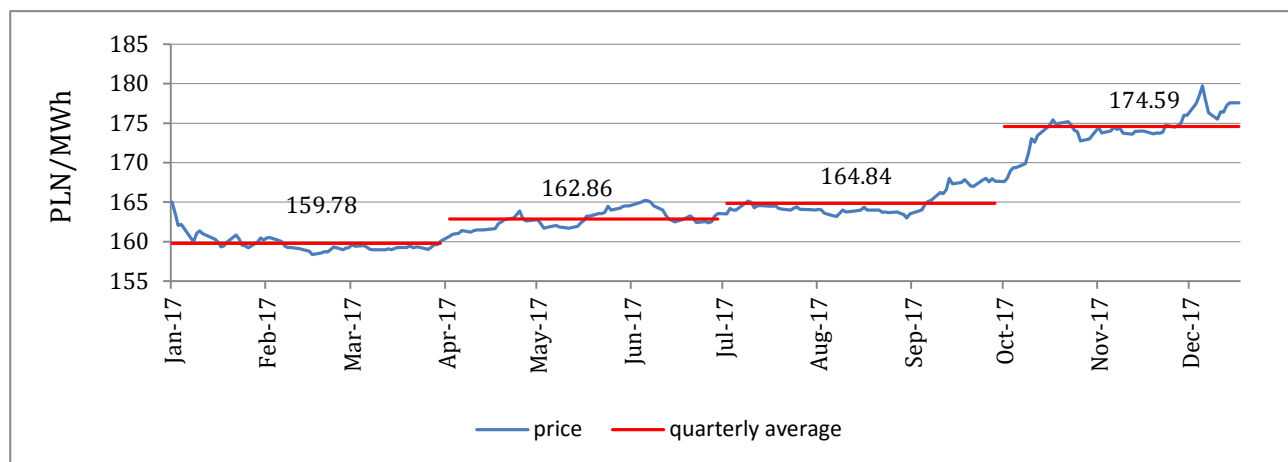
Chart 5: Electricity prices (IRDN)



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.

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



Source: Own elaboration based on TGE data

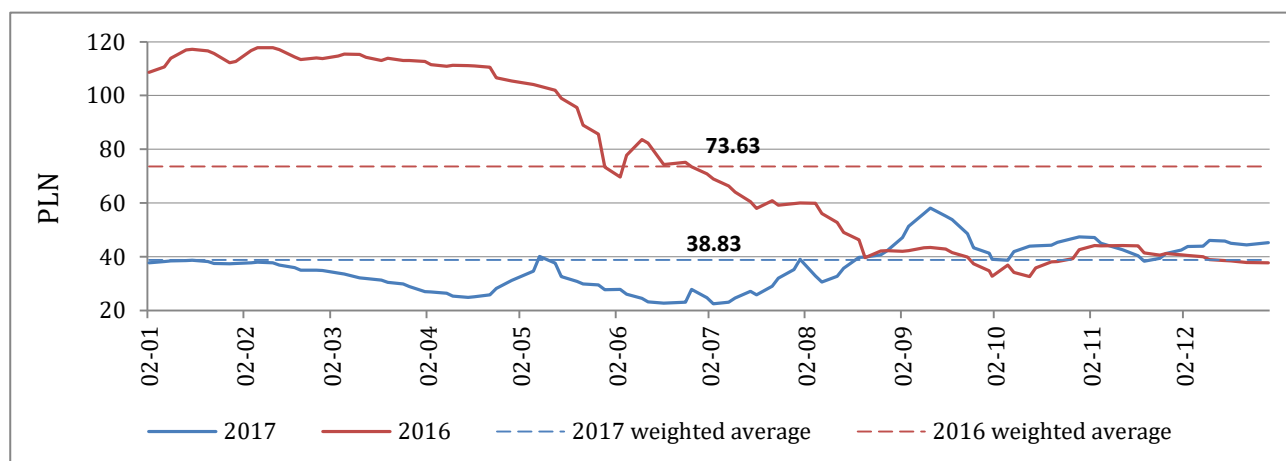
Certificates of origin

Due to the fact that one of the power units at ZE PAK SA is dedicated for combusting biomass (forest and agricultural), and in addition, high-efficiency co-generation in order to generate heat is used, 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 electricity



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 ZE PAK SA. The prices of fuel largely determine the competitiveness of particular electricity production processes. ZE PAK SA 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

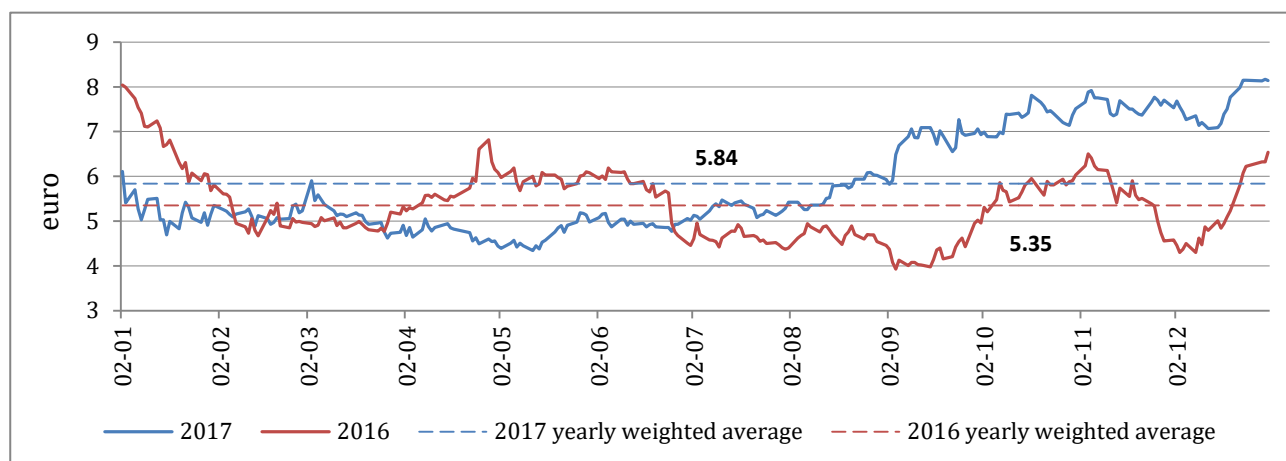
Group's generating assets. The opportunity to start the extraction from the prospective coal deposits in the future may be limited by many factors beyond the control of the Group. The main risk factors include: failure to obtain the necessary licenses, adverse settlements of the local government authorities 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 Company 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 ZE PAK SA 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

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 Company's production level. In the past, the operations of the Company 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 electricity production sector require significant investment expenditures. The Company'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 Company, 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 Company 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:

- Transactions connected with EUA purchase are settled in EURO,
- ZE PAK SA uses debt financing based on a variable interest rate.

In 2017, the Company 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. Management Board monitors 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 Company'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. The company benefits from financial liabilities, mainly loans and credits with variable interest. The company does not use instruments hedging the interest rate. However, as in the case of the exchange rate, in accordance with the Risk Management Principles adopted in the ZE PAK Group, such instruments may be used in the future only to hedge the interest rate and should be adjusted to the hedged position in terms of volume and maturity date.

5. DESCRIPTION OF THE FINANCIAL AND ECONOMIC SITUATION

5.1. Principles of development of the financial statement

Zespół Elektrowni Państw – Adamów – Konin SA develops the financial statement on the basis of the Act of Accountancy of 29 September 1994.

The financial statements have been prepared on the assumption that the Company will continue as a going concern in the foreseeable future. As at the date of preparation of the financial statements, there are no circumstances indicating a threat to the continued operation of the Company.

The accounting principles (policy) applied to the preparation of the financial statements, are presented in item 6 of the Introduction to the Financial Statements of ZE PAK SA for the period of 12 months ended on 31 December 2017.

5.2. Specification of the basic economic and financial values

Profit and loss account

Net revenues from sales of products, goods and materials in 2017 amounted to PLN 1 477 055 thousand and in relation to 2016 they decreased by PLN 145 125 thousand, i.e. by 8.95%. The drop in revenues from the sale of electricity from own production and from resale (minus excise duty) in 2017 compared to the previous year amounted to PLN 93 136 thousand, i.e. 6.62%. The lower volume of electricity sales resulted from lower sales of electricity from own production, sales of electricity from resale increased. The volume of electricity sales from own production decreased by 1.31 TWh to 5.95 TWh, while the volume of electricity from resale increased by 0.47 TWh to 1.24 TWh. There was an increase in the electricity sale price obtained, calculated as revenues from electricity sales (own sales, resale and system services) divided by a volume of 7.66 PLN / MWh. The higher sale price achieved did not manage to offset the loss of revenues which caused a drop in volume.

In 2017, lower revenues from sales of thermal energy were realized, i.e. by PLN 3 371 thousand. The decrease was caused by a lower realized sales volume.

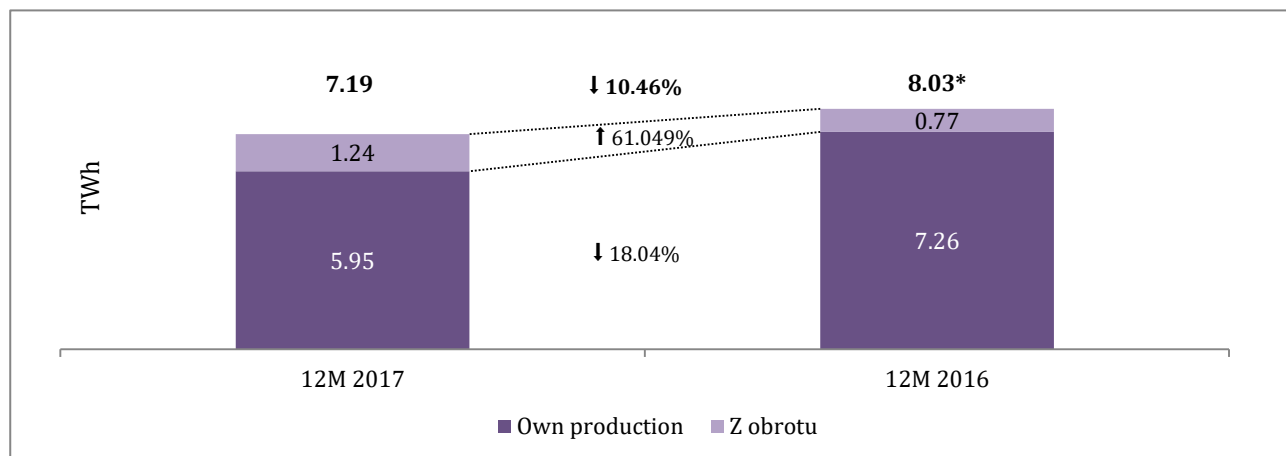
Revenues from the sale of property rights from certificates of origin in 2017 amounted to PLN 684 thousand. In 2016, PLN 812 thousand was recorded on this account. Revenues obtained from energy certificates in 2017 mainly concerned red certificates, as due to very small biomass production, the Company 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.

The company obtained lower revenues from sales of services by PLN 48 535 thousand, i.e. by 32.07%. The main reason for the decrease in revenues was lower revenues related to services provided to Państw II Power Plant sp. o.o.

Table 4: Specification of sales revenues

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2017</i>	<i>zloty thousand</i> <i>12months 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 sales of products	1 260 372	1 490 122	(229 750)	(15.42)
Products sales revenues, including:	1 157 556	1 338 772	(181 216)	(13.54)
– Electricity	1 099 668	1 277 384	(177 716)	(13.91)
– Property rights on energy certificates of origin	684	812	(128)	(15.76)
– Heat	57 204	60 575	(3 371)	(5.57)
Service sales revenues	102 816	151 351	(48 535)	(32.07)
Goods and materials sales revenues	216 683	132 058	84 625	64.08
Goods sales revenues (electricity)	214 211	129 630	84 581	65.25
Material sales revenues	2 472	2 428	44	1.81
Sales revenues, including:	1 477 055	1 622 180	(145 125)	(8.95)
Electricity (products and goods)	1 313 879	1 407 014	(93 135)	(6.62)

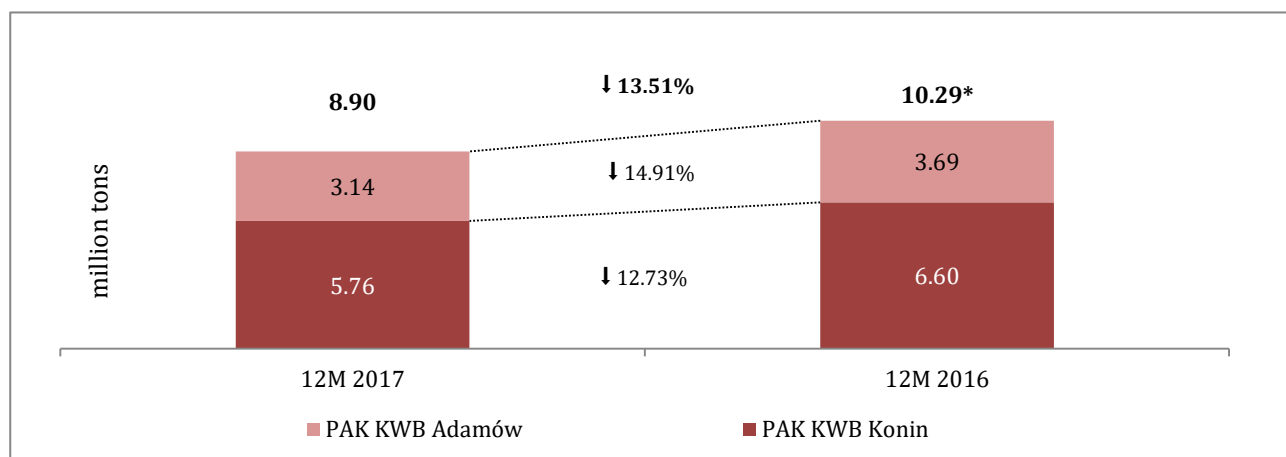
Chart 9: Sale of electricity



* 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

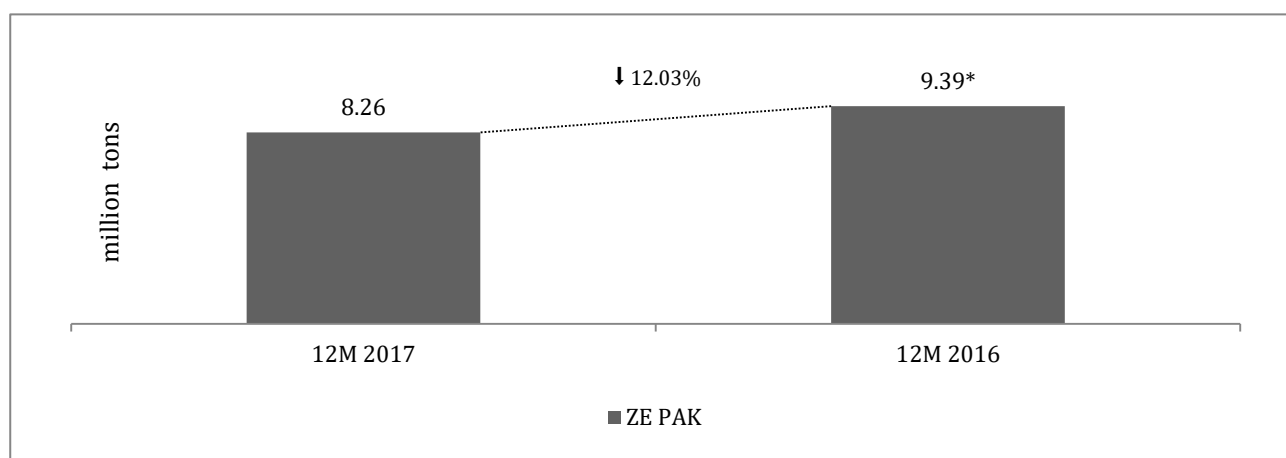
Chart 10: Lignite consumption



* 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 Pątnów I Power Plant in the investment period.

Source: Internal data

Chart 11: CO₂ emission



* 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 Pątnów I Power Plant in the investment period, within 12 months of 2016.

Source: Internal data

The production cost of products sold in 2017 amounted to PLN 1 181 760 thousand and compared to 2016 it was PLN 208 167 thousand lower, i.e. by 14.98%. The reduction in the cost was mainly caused by lower production, which resulted in lower costs of fuel for production (coal and biomass) and a lower amount of CO2 emission allowances necessary to acquire.

The value of goods and materials sold in 2017 amounted to PLN 170 505 thousand and was higher, as compared to the previous year, by PLN 50 910 thousand, i.e. by 42.57% as a result of the higher volume of electricity purchased for resale by 0.47 TWh.

Selling costs in 2017 amounted to PLN 2 944 thousand and were lower by PLN 156 thousand, i.e. by 5.03%.

General administrative expenses in 2017 amounted to PLN 35 713 thousand and were higher than those incurred in the previous year by PLN 5 519 thousand, i.e. by 18.28%. One of the main reasons for the increase was posting in this item the costs of employee benefits related to compensations resulting from agreements signed with the employees of Adamów power plant, which ended its operation at the beginning of January 2018.

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

Table 5: Selected items from profit and loss account

	<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>
Net products, goods and materials sales revenues, including:	1 477 055	1 622 180	(145 125)	(8.95)
– Net revenues of the products sales	1 260 372	1 490 122	(229 750)	(15.42)
– Net revenues resulting from the goods and materials sales	216 683	132 058	84 625	64.08
Costs of sold products, goods, and materials, including:	1 352 265	1 509 522	(157 257)	(10.42)
– Cost of manufacturing of the sold products	1 181 760	1 389 927	(208 167)	(14.98)
– Value of sold goods and materials	170 505	119 595	50 910	42.57
Gross profit (loss) on sales	124 790	112 658	12 132	10.77
Selling costs	2 944	3 100	(156)	(5.03)
Administrative costs	35 713	30 194	5 519	18.28
Sales profit (loss)	86 133	79 364	6 769	8.53
Other operating revenues	3 260	6 993	(3 733)	(53.38)
Other operating costs	3 305	12 671	(9 366)	(73.92)
Profit (loss) on operating activities	86 088	73 686	12 402	16.83
Financial revenues	41 527	86 676	(45 149)	(52.09)
Financial costs	24 101	23 057	1 044	4.53
Gross profit (loss)	103 514	137 305	(33 791)	(24.61)
Income tax	12 877	5 898	6 979	118.33
Net profit (loss)	90 637	131 407	(40 770)	(31.03)

Other operating revenues in 2017 amounted to PLN 3 260 thousand. The lower revenues are primarily the effect of lower claims from insurers and the lack of 2017 profits from actuarial revaluation that occurred a year earlier.

Other operating expenses in 2017 amounted to PLN 3 305 thousand, which means a decrease by PLN 9 366 thousand compared to the previous year. The decrease can be explained by the lack of an impairment of green certificates in 2017.

In 2017, the Company generated operating profit in the amount of PLN 86 088 thousand.

Financial revenues in 2017 amounted to PLN 41 527 thousand and were lower than those recorded in the previous year by PLN 45 149 thousand, i.e. 52.09%. The lower dividends received from subsidiaries had the greatest impact on the decline in financial revenues.

Financial expenses in 2017 amounted to PLN 24 101 thousand and in relation to 2016 they increased by PLN 1 044 thousand, i.e. 4.53%. In 2017, as in the previous year, this item mainly consisted of interest on financial liabilities.

Table 6: 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>12months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Depreciation	38 333	36 925	1 408	3.81
Use of materials and energy	617 823	758 536	(140 713)	(18.55)
External services	152 381	182 900	(30 519)	(16.69)
Taxes and charges, including:	288 532	323 851	(35 319)	(10.91)
– excise tax	768	797	(29)	(3.64)
– CO ₂ emission costs	221 792	248 789	(26 997)	(10.85)
Salaries	91 163	92 778	(1 615)	(1.74)
Social security and other benefits	24 991	24 287	704	(2.90)
Other costs by type	7 072	8 570	(1 498)	(17.48)
Value of sold goods and materials	170 505	119 595	50 910	42.57
Total costs by type	1 390 800	1 547 442	(156 642)	(10.12)

In 2017, the Company generated a gross profit of PLN 103 514 thousand. At the net level, the profit was PLN 90 637 thousand.

Balance sheet

The balance sheet total of the Company as at December 31, 2017 amounted to PLN 2 367 870 thousand and, as compared to the balance as at December 31, 2016, it decreased by PLN 230 336 thousand, i.e. by 8.87%.

Fixed assets decreased by PLN 198 336 thousand, i.e. by 8.94%. The largest changes concerned the following positions:

- intangible assets, which decreased by PLN 171 255 thousand as a result of settlement of CO₂ emission allowances in 2017;
- tangible fixed assets, which decrease by net PLN 15 119 thousand, as a result of higher level of depreciation write-offs on realized investment outlays;
- long-term investment, which decreased by PLN 11 765 thousand, i.e. by 0.99%, mainly as a result of repayment of loans granted to a subsidiary.

Current assets decreased by PLN 32 000 thousand, i.e. by 8.45%. The decrease in current assets was a consequence of the decrease in the level of cash as a result of repayment of financial debt.

Equity as at December 31, 2017 amounted to PLN 1 516 912 thousand, and compared to the end of 2016 it increased by PLN 25 757 thousand, i.e. by 1.68%, 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. On the other hand, the lower net profit generated during the year was unfavourable as compared to the one generated in the previous year.

The level of provisions at the end of 2017 amounted to PLN 329 940 thousand and was lower as compared to the previous year by PLN 17 456 thousand. The largest change took place in the item "other reserves" and concerned the reduction of the provision for CO₂ emission allowances. Its decrease was mainly caused by the lower amount of emission allowances needed to cover the 2017 issue.

Total liabilities as at the end of 2017 as compared to the end of 2016 decreased by PLN 238 093 thousand, i.e. by 32.56% - long-term liabilities decreased by PLN 140 481 thousand, and short-term liabilities decreased by PLN 97 612 thousand. The largest drop in liabilities related to the item "loans and borrowings" and was related to servicing the loan for financing the modernization of blocks in Państw I Power Plant.

Table 7: Selected items from assets

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2017</i>	<i>zloty thousand</i> <i>12months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Fixed assets	2 021 250	2 219 586	(198 336)	(8.94)
Intangible and legal assets	196 877	368 132	(171 255)	(46.52)
Tangible fixed assets, including:	647 725	662 844	(15 119)	(2.28)
1. Fixed assets	582 725	617 868	(35 143)	(5.69)
2. Fixed assets under construction	64 302	41 067	23 235	5.,58
3. Advances on fixed assets in construction	698	3 909	(3 211)	(82.14)
Long-term receivables	0	0	0	-
Long-term investments	1 176 097	1 187 862	(11 765)	(0.99)
Long-term accruals and prepayments	551	748	(197)	(26.34)
Current assets	346 620	378 620	(32 000)	(8.45)
Inventory, including:	41 617	53 915	(12 298)	(22.81)
1. Materials	39 601	39 602	(1)	0.0
2. The goods	1 985	13 959	(11 974)	(85.78)
3. Advances for deliveries	31	354	(323)	(91.24)
Short-term receivables	138 406	137 373	1 033	0.75
Short-term investments	166 063	186 022	(19 959)	(10.73)
1. Short-term financial assets, including:	166 063	186 022	(19 959)	(10.73)
– in the affiliates	18 714	16 125	2 589	16.06
– in other entities	0	296	(296)	100.00
– cash and other monetary assets	147 349	169 601	(22 252)	(13.12)
2. Other short-term investments	0	0	0	-
Short-term accruals and prepayments	534	1 310	(776)	(59.24)
Unpaid share capital (basic)	0	0	0	-
Own shares	0	0	0	-
Total assets	2 367 870	2 598 206	(230 336)	(8.87)

Table 8: Selected items from liabilities

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2017</i>	<i>zloty thousand</i> <i>12months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Equity	1 516 912	1 491 837	25 075	1.68
Stated capital	101 647	101 647	0	-
Supplementary capital	1 094 493	1 028 647	65 846	6.40
Revaluation capital	227 497	227 498	(1)	-
Other reserve capital	3 472	3 472	0	-
Profit (loss) from previous years	(834)	(834)	0	-
Net profit (loss) from previous years	90 637	131 407	(40 770)	(31.03)
Net write-offs during the financial year (negative value)	0	0	0	-
Liabilities and provisions for liabilities	850 958	1 106 369	(255 411)	(23.09)
Provisions for liabilities	329 940	347 396	(17 456)	(5.02)
1. Deferred income tax provision	79 212	68 806	10 406	15.12
2. Provisions for pensions and similar benefits.	10 398	9 922	476	4.80
3. Other reserves	240 330	268 668	(28 338)	(10.55)
Long-term liabilities	203 524	344 005	(140 481)	(40.84)
1. Towards related entities	0	254	(254)	(100.00)
2. Towards other entities of which entity has capital engagement	0	0	0	-
3. Towards other entities	203 524	343 751	(140 227)	(40.79)
– credits and loans	201 035	343 295	(142 260)	(41.44)
– other financial liabilities	489	456	33	7.23
– other	2 000	0	2 000	-
Short-term liabilities	289 597	387 209	(97 612)	(25.21)
1. Towards related entities	29 736	32 405	(2 669)	(8.24)
2. Towards other entities of which entity has capital engagement	0	0	0	-
3. Towards other entities, including:	255 659	350 650	(94 991)	(27.09)
– credits and loans	153 684	158 629	(4 945)	(3.12)
– trade liabilities:	21 586	53 247	(31 661)	59.46
– advance payments received for deliveries and services	0	50	(50)	(100.00)
– due to taxes, customs duty, social security and other benefits	60 402	68 521	(8 119)	(11.85)
– remunerations	5 644	4 314	1 330	30.83
– other	13 382	65 750	(52 368)	(79.65)
4. Special funds	4 202	4 154	48	1.16
Accruals and prepayments	27 897	27 759	138	0.50
Total liabilities	2 367 870	2 598 206	(230 336)	(8.87)

Cash flow statement

In 2017, the Company generated a positive balance of cash flows from operating activities in the amount of PLN 173 618 thousand. The balance of cash flows from operating activities in 2017 was higher by PLN 77 369 thousand as compared to the corresponding balance in 2016 - the main reason was lower expenses for the acquisition of CO2 emission allowances in 2017.

The balance of cash transactions on investing activities was positive and amounted to PLN 34 003 thousand. Attention is paid to significantly lower than in 2016 expenditure on investments in fixed assets. Dividend income was also lower, however, the balance of decrease was lower than in the case of expenditure on investments in fixed assets.

In 2017, similarly as in 2016, no inflows in financial activity were obtained. Expenses amounted to PLN 229 788 thousand and were higher by 73.00% from last year. In 2017, in addition to expenditure on servicing financial debts, a dividend was paid to shareholders in the amount of 1.29 PLN / share.

Cash in 2017 decreased by PLN 22 167 thousand and at the end of the year amounted to PLN 147 349 thousand.

Table 9: Selected items of the cash flow statement

	<i>zloty thousand</i> 12 months period ended 31 December 2017	<i>zloty thousand</i> 12 months period ended 31 December 2016	<i>zloty thousand</i> change	%
				<i>dynamics</i>
Cash flows on operating activities				
Gross profit (loss)	90 637	131 407	(40 770)	(31.03)
Total adjustments	82 981	(35 158)	118 139	-
1. Depreciation	38 333	36 925	1 408	3.81
2. Profits (losses) on foreign exchange rates	2 819	(2 936)	5 755	-
3. Interest and shares in profits (dividends)	(21 035)	(61 139)	40 104	(65.59)
4. Profit (loss) on investment activities	1 092	(263)	1 355	-
5. Change in provisions	232 733	254 761	(22 028)	(8.65)
6. Change in inventory	12 298	50 241	(37 943)	(75.52)
7. Change in receivables	(1 033)	14 861	(15 894)	(106.95)
8. Change in short-term liabilities, with the exception of loans and credits	(44 319)	(24 231)	(20 088)	82.90
9. Change in accruals	1 111	(2 682)	3 793	-
10. Other adjustments	(139 018)	(300 695)	161 677	(53.77)
Net cash flow from operating activities	173 618	96 249	77 369	80.38
Cash flows on investment activities	0	0	0	-
Income	53 806	108 710	(54 904)	(50.51)
1. Disposal of intangible and legal assets as well as tangible assets	56	1 613	(1 557)	(96.53)
2. From financial assets, including:	53 750	107 097	(53 347)	(49.81)
– in the affiliates	53 550	107 041	(53 491)	(49.97)
– in other entities	200	56	144	257.14
– dividends and shares in profits	200	56	144	257.14
Expenses	19 803	85 608	(65 805)	(76.87)
1. Acquisition of intangible and legal assets as well as tangible assets	10 354	85 608	(75 254)	(87.91)
2. For own financial assets, including:	9 449	0	9 449	-
– in the affiliates	9 449	0	9 449	-
Net cash flow from investment activities	34 003	23 102	10 901	47.19
Cash flows on financial activities	0	0	0	-
Income	0	0	0	-
1. Credits and loans	229 788	132 824	96 964	73.00

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Expenses	65 562	0	65 562	-
1. Dividends paid and other payments to shareholders	148 543	111 877	36 666	32.77
2. Repayment of credits and loans	142	130	12	9.23
3. Payments of financial lease agreement liabilities	15 541	20 757	(5 216)	(25.13)
4. Interest	0	60	(60)	(100.00)
Net cash flow from financial activities	(229 788)	(132 824)	(96 964)	73.00
Total cash flow	(22 167)	(13 473)	(8 694)	64.53
Cash flow change in the balance sheet, including:	(22 252)	(13 388)	(8 864)	66.21
cash flow change related to foreign exchange rates	(85)	85	(170)	-
Cash opening balance	169 516	182 989	(13 473)	(7.36)
Closing balance of cash, including:	147 349	169 516	(22 167)	(13.08)
restricted cash	3 533	4 524	(991)	(21.91)

Financial indexes

At the end of 2017, lower profitability ratios were noted. This applies to the largest extent to ROE due to two reasons, i.e. lower net profit in 2017 and higher equity. In the case of ROA and profitability of sales, the lower net profit was accompanied by a lower value of assets and lower sales revenues.

The overall debt ratio dropped to 0.36 due to a greater decline in the level of debt in relation to the reduction in total assets.

The value of the current liquidity ratio, informing about the coverage of current liabilities with short-term current assets, strongly increased to the level of 1.20, which means an improvement in the liquidity situation compared to the end of 2016.

Table 10: Indexes

		2017	2016	Change	Dynamics
ROE	%	5.98	8.81	(2.83)	(32.12)
ROA	%	3.83	5.06	(1.23)	(24.31)
Net sales profitability	%	6.14	8.10	(1.96)	(24.20)
General debt index	x	0.36	0.43	(0.07)	(16.28)
Current liquidity index	x	1.20	0.98	0.22	22.45

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

The Company'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 Company'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 Company 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)⁷. 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 determine 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

⁷ PPE statement from www.tge.pl

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 Company acquires CO₂ emission rights, was in previous years and will continue to be of great importance for the future financial results of the Company. 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.

Another factor that will undoubtedly affect the future financial results of the Company 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 Company's generation units win power auctions, the Company 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 Company 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 Company 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 Company'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.

4.4. Unusual events affecting the obtained financial results

In 2017, there were no unusual events having a significant impact on assets, liabilities, equity, net financial result or cash flows.

5. MANAGEMENT OF FINANCIAL ASSETS

5.1. Evaluation of financial assets management

The company has 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 Company 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 Company executes 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.

5.2. Evaluation of investment plan execution

The Company has its own development 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 Company takes 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, 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 Company is constantly monitoring the factors which have the biggest impact on the executed investment program and in case of substantial changes in either one or several of them, the Company will make certain adjustments or significant changes in the executed strategy.

6. SIGNIFICANT FACTORS AND DEVELOPMENT PROSPECTS

Directional activities designated by the Company'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 Company'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 Company'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 Pałnów

The coal assets in Pałnów I power plant have been partially modernized (units 1 and 2 with a capacity of 222MW 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 Ościśłowo open pit. At present, the environmental decision issue is being reconsidered by the Regional Directorate for Environmental Protection in Poznań.

7. SPECIFICATION OF THE SHAREHOLDING STRUCTURE

7.1. 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.

*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**

<i>Shareholder</i>	<i>shares.</i>	<i>%</i>
	<i>Number of shares and corresponding number of votes at the General Meeting</i>	<i>Share [%] in the total number of shares/votes</i>
Zygmunt Solorz (indirectly) through:	26 200 867	51.55
– <i>Elektrim SA</i>	<i>196 560</i>	<i>0.39</i>
– <i>Embud 2 sp. z o.o. S.K.A.</i>	<i>592 533</i>	<i>1.16</i>
– <i>Trigon XIX Fundusz Inwestycyjny Zamknięty</i>	<i>10 004 001</i>	<i>19.68</i>
– <i>Argumenol Investment Company Limited</i>	<i>15 407 773</i>	<i>30.32</i>

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.

7.2. Acquisition of own shares

The Company did not acquire own shares in 2017.

7.3. 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 Szelaǳ	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
Lesław Podkański	0	0	0	0
Sławomir Zakrzewski	0	0	0	0

7.4. 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.

8. 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.

8.1. 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

8.2. Set of rules which the Company has not applied 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.

8.3. Description of the main characteristics of internal control and risk management systems in relations 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.

8.4. 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.*

8.5. 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.

8.6. 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.

8.7. 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.

8.8. 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,
- 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.

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.

8.9. 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 Szeląg – 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 Szeląg,
- 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 Szeląg 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 Szeląg – Deputy of the Chairman,
- 3) Wojciech Piskorz – Secretary,
- 4) Henryk Sobierajski,
- 5) Leszek Wysłocki,
- 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 Szelağ.

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 Pańńów-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 Pańńów-Adamów-Konin SA" and "The policy of selecting an audit firm for the purpose of carrying out a statutory audit of Zespół Elektrowni Pańńów-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.

8.10. 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.

8.11. 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.

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

In Zespół Elektrowni Państw-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.

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 Value of (gross) remuneration paid by the Company</i>	<i>zloty thousand Value of (gross) remuneration paid by the Company's subsidiaries</i>	<i>zloty thousand 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 Total estimated value of non- cash benefits granted by the Company</i>	<i>zloty thousand Total estimated value of non- cash benefits granted by the Company's subsidiaries</i>	<i>zloty thousand 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>złoty thousand</i> <i>Value of (gross) remuneration paid by the Company and the Company's subsidiaries</i>	<i>złoty thousand</i> <i>Total estimated value of non-cash benefits granted by the Company and the Company's subsidiaries</i>	<i>złoty 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.

9. 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 52 of this report.

10. STATEMENT OF ZESPÓŁ ELEKTROWNI PĄTNÓW – ADAMÓW – KONIN SA MANAGEMENT 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 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.

10.1. Description of business model

ZE PAK SA is a producer of electricity operating on the Polish market and an important element of national power engineering system. In accordance with the Company's Articles of Association, the Company's primary business is the generation and sale of electricity as well as the production and sale of heat. The company generates electricity from conventional sources and by burning biomass. The company operates mainly on the territory of the Republic of Poland. ZE PAK SA 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 power plants in the immediate vicinity of the mines.

In 2017, the generation assets of ZE PAK SA included three power plants, i.e.: Pątnów I, Konin – equipped with the biomass-fired boiler unit, and Adamów (Elektrownia Adamów ended its operation in January 2018).

10.2. Social issues

Management approach

The policy and management approach of ZE PAK SA 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 generating operations in the units that belong to ZE PAK SA and dependent on the specifics of the particular object. Each time, the Company 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 Company's management approach to social issues is conditioned by the nature of its 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 to the risk.

The Company's influence on the environment is multidimensional. From the point of view of general public, ZE PAK SA is an important supplier of energy for the Polish economy and Polish society. Nevertheless, the final customers are not the main clients of the Company but the trading companies operating on the wholesale electricity market. For this reason, the ZE PAK SA aims at ensuring stable electricity supply at a competitive price to other technologies. ZE PAK SA 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 Company's plants, where the production of electricity and heat is conducted. The production of electricity have an 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:

- emissions of compounds accompanying the combustion of coal, e.g. CO₂, SO₂, NO_x,

- dust emission,
- noise generation (e.g. due to the operation of power block turbines),
- waste generation (in the process of lignite combustion and flue gas cleaning),
- possible leaks of oil, mazout, acids, 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.

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 ślesieńskie” includes the following lakes: Gosławskie, Pańnowskie, Wąsowsko-Mikorzyńskie, Licheńskie and Ślesieńskie, which are included in the cooling circulation of Pańnow, Pańnow 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 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.

ZE PAK SA 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 Company paid over PLN 91.6 million (PLN 87.0 million in 2016), of which PLN 75.8 million (in 2016 it was over PLN 80.8 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 Company allocated employee benefits to PLN 91.2 million in 2017 and PLN 92.8 million in 2016).

The management approach of ZE PAK SA 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 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, ZE PAK SA, 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 Company 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 Company'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 ZE PAK SA 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.

As an example there can be given periodical burdens, e.g. 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 Company 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 Company's PR department performs press articles explaining the rules of exploitation of lignite open mines and reclamation of post-mining sites. The inhabitants of the nearest neighbourhood of the plant are often the Company'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. 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 Company 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 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 Company's involvement in spectacular projects is not meant to get publicity but to reach the nearest communities and non-governmental organizations from the region. 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 Company.

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
Total amount of taxes and para-taxes paid - altogether	PLN 91.6 m	PLN 87.0 m
Total amount of taxes and para-taxes paid – for local administration	PLN 75.8 m	PLN 80.8 m

10.3. Employee issues

Management approach

In the area of human resources management, ZE PAK SA 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; Staff Council is also operating. The Unions are also operating in ZE PAK SA. In the matters specified by the law the management of ZE PAK SA informs and consults 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 Company complies with the labour law and requires proper behaviour in relations between the employees as well as between the employees and their superiors.

Corporate collective labour agreement, obligatory in ZE PAK SA in the reporting period, contains 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.

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).

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.

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-medical 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 Pańków 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.

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 it is necessary to guarantee the employment at an appropriate level, by positioning the Company as an attractive employer 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	191	1019	1210	178	943	1121
Work contract for an definite period	11	75	86	8	50	58
Work contract for a trial period	0	0	0	0	0	0
Civil-law agreement	12	3	3	0	0	0

- 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	15	57	72	17	48	65
Non-managerial position	187	1037	1224	169	945	1114
<i>By education</i>						
Higher (bachelor, master, postgraduate, doctorate, professor)	125	365	490	119	328	447

ZESPÓŁ ELEKTROWNI PAŃNÓW – ADAMÓW – KONIN SA
MANAGEMENT BOARD'S REPORT FROM OPERATION OF ZE PAK SA IN 2017

Medium (high school, technical college, college, post-secondary)	72	424	496	63	390	453
Professional (basic, learning a profession)	4	227	231	3	208	211
Basic (elementary, junior high)	1	78	79	1	67	68
<i>By age</i>						
Up to 30 years old	13	100	113	10	67	77
31 to 40 years old	40	143	183	32	124	156
41 to 50 years old	42	387	429	44	320	364
Over 50 years old	107	464	571	100	482	582
Total	202	1094	1296	186	993	1179

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	7	17	24	1	0	1
31 to 40 years old	4	9	13	2	0	2
41 to 50 years old	4	4	8	2	0	2
Over 50 years old	1	5	6	2	1	3
Total	16	35	51	7	1	8

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	4	3	7	2	20	22
31 to 40 years old	1	9	10	2	17	19
41 to 50 years old	2	6	8	3	17	20
Over 50 years old	15	37	52	15	49	64
Total	22	55	77	22	103	125

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

Amount	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:	2	4

– light	2	3
– serious	-	-
– fatal	-	1
Number of lost days	100	179
Frequency ratio of injured in total accidents (per 1000 insured)	1,5	3
Frequency ratio of injured in serious and fatal accidents (per 1000 insured)	-	0.739

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	123	163
Dust	59	60
Insufficient lighting	324	350
Energy expenditure	44	44
Nuisance at work – night shift work	785	859

10.4. 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 system covering the environmental issues, relating to the process of electricity and heat production with all the auxiliaries, identified environmental aspects, threats, legal and other requirements and containing the environmental policies with particular procedures periodically reviewed and optimized. Certified management system as well as Corporate Social Responsibility Strategy of ZE PAK SA Capital Group for the years 2017-2020 aims at providing stable and safe electricity production 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).

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. In case of producing electricity 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.

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 in recent years, the efficiency of generation (and thus the efficiency of fuel use) increased on this plant, and on the other hand, the emissivity decreased, including CO₂ mass per unit of electricity produced. Such approach also allowed reducing 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 Company.

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.

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 Pańków 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 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 Company's 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, Pańnowskie, Ślesińskie, 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 Pańków I 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 Pańków I 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.

Economical groundwater management

Technologies used to build the 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 Pańków 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, Pańków 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, Pańków 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 Pańków 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 Państw 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, in 2017, noise measurements were taken from the area of Konin power plant. No measurements were taken from Adamów and Państw 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 Power Plant both at daytime and at night.

Inspections

In 2017 the Voivodship Inspectorate for Environment Protection in Poznań, Delegation in Konin, inspected Elektrownia Państw I, and Elektrownia Konin:

- Elektrownia Państw I – inspection of sources covered by the Transitional National Plan at the request of GIEP (General Inspection of Environment Protection).
- 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 Państw I is in the group of plants where increased risk of major industrial accidents may occur.

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 ZE PAK SA 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 ZE PAK SA, 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 per production unit	1.23	1.19	1.15	1.09

**excluding elektrownia Adamów*

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

	2017	2017*	2016	2016*
SO ₂ emission in ZE PAK SA per production unit	2.65	1.10	2.36	1.05
NO _x emission in ZE PAK SA per production unit	1.83	1.47	1.77	1.39
Dust emission in ZE PAK SA per production unit	0.37	0.13	0.37	0.13

** excluding elektrownia Adamów*

10.5. 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 Company, there is operating the Employees' Council selected on the basis of applicable regulations. There are also a number of trade union organizations operating under the Trade Unions Act. The Management Board of the Company informs and consults 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 PAK 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 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 Company but also the national energy system.

Regarding the risk of disrespect for individual rights, such cases can not only expose ZE PAK SA 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 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
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/d
Unionization ratio	52,25%	49,77%
Number of disputes in which trade union organizations refer to the provisions of the Act on the resolution of collective disputes	2	1
Number of work days lost due to strike actions	0	0

10.6. 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 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 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" determines 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 ZE PAK SA 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 ZE PAK SA also regulate the issues of supplier selection. 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 purchasing area is a 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 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, 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 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 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

11. OTHER INFORMATION

11.1. Significant court proceedings

In 2017 Zespół Elektrowni Pątnów - Adamów - Konin SA was 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.

11.2. Significant achievements in the field of research and development

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

11.3. 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 36 of ZE PAK SA financial statement for 2017 for a period of 12 months ended 31 December 2017..

11.4. Financial forecasts

The Company has not published financial forecasts and is not going to present the forecast for 2018.

Konin, 19 April 2018

Adam Klapszta
President of the Board

Aneta Lato-Żuchowska
Vice President of the Board

Zygmunt Artwik
Vice President of the Board

Elżbieta Niebisz
Vice President of the Board