

ZESPÓŁ ELEKTROWNI PAŃNÓW – ADAMÓW – KONIN SA

MANAGEMENT BOARD'S REPORT FROM COMPANY'S OPERATIONS IN 2016

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

21 MARCH 2017

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1. SELECTED FINANCIAL DATA

<i>Selected financial data</i>	<i>zloty thousand</i>	<i>zloty thousand</i>	<i>euro thousand</i>	<i>euro thousand</i>
	<i>12 months of 2016 period from 01.01.2016 to 31.12.2016</i>	<i>12 months of 2015 period from 01.01.2015 to 31.12.2015</i>	<i>12 months of 2016 period from 01.01.2016 to 31.12.2016</i>	<i>12 months of 2015 period from 01.01.2015 to 31.12.2015</i>
Sales revenue of products, goods and materials	1 622 180	1 538 913	370 725	367 739
Operating profit/loss	73 686	(1 573 581)	16 840	(376 023)
Profit/Loss before tax	137 305	(1 520 196)	31 379	(363 266)
Net profit/loss for the period	131 407	(1 515 850)	30 031	(362 228)
Net cash flow from operating activities	96 249	110 768	21 996	26 469
Net cash flow from investing activities	23 102	(286 189)	5 280	(68 388)
Net cash flow from financing activities	(132 824)	185 171	(30 355)	44 248
Net cash flow	(13 473)	9 750	(3 079)	2 330
Net profit per share (in PLN/EUR per share)	2.59	(29.83)	0.59	(7.13)
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547
	<i>As of 31.12.2016</i>	<i>As of 31.12.2015</i>	<i>As of 31.12.2016</i>	<i>As of 31.12.2015</i>
Total assets	2 598 206	2 649 371	587 298	621 699
Fixed assets	2 219 586	2 184 042	501 715	512 505
Current assets	378 620	465 329	85 583	109 194
Equity	1 491 837	1 360 431	337 215	319 238
Share capital	101 647	101 647	22 976	23 852
Liabilities and provisions for liabilities	1 106 369	1 288 940	250 083	302 462
Long term liabilities	344 005	536 213	77 759	125 827
Short term liabilities	387 209	343 449	87 525	80 593
Book value per share (in PLN/EUR per share)	29.35	26.77	6.63	6.28
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:

- particular items of Profit & loss account and statement of cash flows – according to the exchange rate constituting an arithmetic average of average exchange rates set out by the National Bank of Poland at the last working day of every month of the reporting period starting from 1 January 2016 to 31 December 2016, which is 4.3757 euro/zloty and starting from 1 January 2015 to 31 December 2016, which is 4.1848 euro/zloty;
- particular items of the Balance sheet according to average euro/zloty exchange rate published by the National Bank of Poland as of 30 December 2016, which is 4.4240 euro/zloty and as of 31 December 2015, which is 4.2615 euro/zloty.

2. DESCRIPTION OF THE COMPANY AND OF 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, 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 w Warszawie SA (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 2016, the share capital of ZE PAK SA has been not changed. As of 31 December 2015 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 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.”), Przedsiębiorstwo Serwisu Automatyki i Urządzeń Elektrycznych EL PAK sp. z o.o. (hereinafter referred to as the “EL PAK sp. z o.o.”), EL PAK Serwis sp. z o.o., Aquakon sp. z o.o., Eko-Surowce sp. z o.o., Energoinvest SERWIS sp. z o.o., PAK Górnictwo sp. z o.o., PAK – HOLDCO sp. z o.o., PAK Infrastruktura sp. z o.o. Consolidation covers all the above-mentioned companies.

The companies which are of the biggest importance for the Group due to the scale of their operations are: ZE PAK SA and Elektrownia Pątnów II sp. z o.o., dealing with production of electricity and heat, and PAK KWB Adamów SA and PAK KWB Konin SA, dealing with lignite mining. Apart from the core business, the Group comprises also other

companies which perform e.g. construction and erection works, maintenance works, provide services, deal with production and trade to meet demand from and offer complex services for industry.

The production facilities of the Group include four lignite-fired power plants located in the central part of Poland in the Wielkopolskie voivodship. These are: Państw II which is equipped with a supercritical power unit, Państw I, Adamów and Konin equipped additionally with power unit with biomass fired boiler. Total installed gross power output of the production facilities of the Group was 2506 MWe as of 31 December 2016.

The Group's mining assets are concentrated in three companies: PAK KWB Konin SA, which currently operates on Józwin, Tomislawice and Drzewce open casts, PAK KWB Adamów SA, which operates on Adamów open casts as well as PAK Górnictwo sp. z o.o. which executes works related to identification of lignite deposits in the areas of Poniec-Krobia and Oczkowice in the southern Wielkopolskie Province.

Majority of the Group's sales revenue is derived from sale of electricity (both generated within the Group and purchased for resale). This is supplemented by revenues from sale of heat, certificates of Energy origin (green and red certificates) and from construction contracts. An additional sales revenue, which depends on the level of electricity prices on the market as well as the volume of generated electricity, is revenue from termination of long-term contracts for sale of electricity (Power Purchase Agreements), generated by Elektrownia Państw II sp. z o.o. Group having in its structure lignite mines, provides with an access to continuous supplies of lignite for its own power plants located in the direct vicinity of open pits. The vertically integrated Group allows for optimization of lignite inventories and supplies while coordinating lignite extraction with its requirements for this fuel. The requirements for biomass are satisfied by the suppliers of this raw material.

Structure of the ZE PAK Group as at 31 December 2015 presents Picture 1

The Company outside the Capital Group has shares in Zakłady Pomiarowo-Badawcze Energetyki Energopomiar Sp. z o.o. with registered office in Gliwice, providing measurement, research and consulting services related to the Energy market. ZE PAK SA has 1 share with a value of zloty 151 201.01 in the aforementioned company, comprising 2.81% of the total capital.

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

Picture 1: Structure of the Group as of 31 December 2016

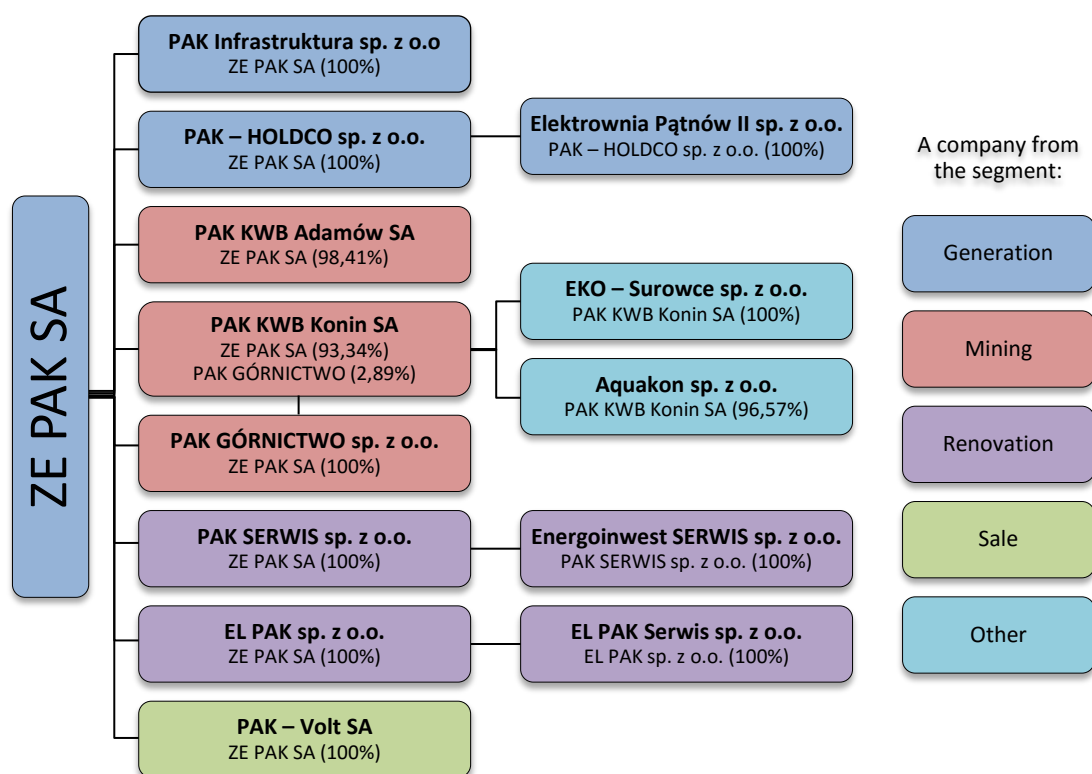


Table 1: Description of the Group's companies (excluding ZE PAK SA)

Entity	Registered office	Scope of operations	Group's share in the capital in percent	
			31.12.2016	31.12.2015
Przedsiębiorstwo Remontowe „PAK SERWIS” sp. z o.o.	62-510 Konin ul. Przemysłowa 158	Construction and repair services	100,00%	100,00%
Przedsiębiorstwo Serwisu Automatyki i Urządzeń „EL PAK” sp. z o.o.	62-510 Konin ul. Przemysłowa 158	Services related to industrial automatics and electric appliances maintenance	100,00%	100,00%
„Elektrownia Państw II” sp. z o.o.	62-510 Konin ul. Kazimierska 45	Electric energy production and distribution from the 464 MW power unit	100,00%*	100,00%*
„PAK – HOLDCO” sp. z o.o.	62-510 Konin ul. Kazimierska 45	Holding activity	100,00%	100,00%
„PAK Infrastruktura” sp. z o.o.	62-510 Konin ul. Kazimierska 45	General construction of engineering objects, not classified elsewhere	100,00%	100,00%
„PAK GÓRNICtwo” sp. z o.o.	62-510 Konin ul. Kazimierska 45	Exploration and recognition of lignite	100,00%	100,00%
Energoinwest Serwis sp. z o.o.	62-510 Konin ul. Spółdzielców 3	Construction and repair services	100,00%*	100,00%*
PAK Kopalnia Węgla Brunatnego Konin SA	62-540 Kleczew ul. 600-lecia 9	Lignite extraction	96,23%*	96,23%
PAK Kopalnia Węgla Brunatnego Adamów SA	62-700 Turek ul. Uniejowska 9	Lignite extraction	98,41%	98,41%
„Aquakon” sp. z o.o.	62-610 Sompolno Police	Mechanical services, repairs, reclamation of land, production and trade of mineral water	92,57%*	92,57%*
Eko-Surowce sp. z o.o.	62-540 Kleczew ul. 600-lecia 9	Vulcanization services, sale of lignite	96,23%*	96,23%*
PAK – Volt SA	00-834 Warszawa ul. Pańska 77/79	Trade of electricity	100,00%	100,00%
EL PAK Serwis sp. z o.o.	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 Organisational Department was established within the organisational 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 organisational structure of the Company, organisational division units that bring together organisational 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 organisational division unit. The members of the Management Board of ZE PAK SA co-operate, agree, and coordinate the actions regarding the

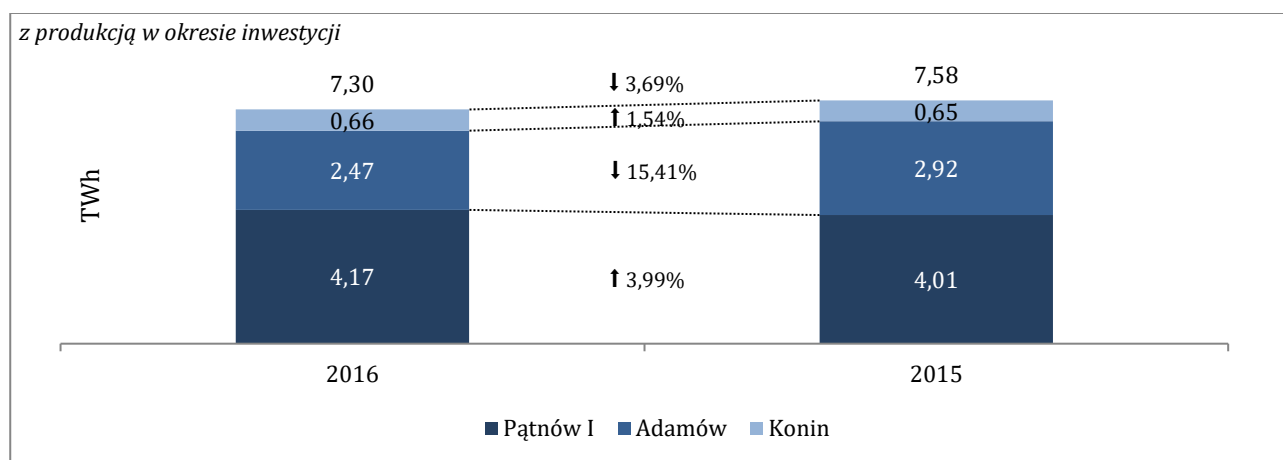
Company's matters as well as secure proper co-operation of the organisational division units and units managed by them. The areas of the Company's activity managed by individual members of the Management Board are defined by the Company's organisational regulations specifying the Company's organisation of the enterprise. In relation to the changes in the Management Board's composition, which took place on 3 March 2017, the internal division of competences between the currently incumbent members of the Management Board of ZE PAK SA will be made.

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

The Company's operations are focused in several areas. The main area is doubtlessly generation of and wholesale trading in electricity, which is supplemented by sales of energy certificates, operations undertaken to ensure an adequate amount of CO₂ allowances as well as generation and sales of heat. In 2015, the Company 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 fifth largest producer of electricity in Poland and second largest producer of electricity generated from lignite. The share of all of the Company's power plants in the entirety of electricity produced in Poland amounts to 5.0%¹. The net electricity production in the Pałnów I power plant was equal to 4.13 TWh in 2016, while in the Adamów, 2.47 TWh and in Konin 0.66 TWh. The total electricity production in all power plants of the Group in 2016 was lower by 3.69% in comparison to the year before. Total energy production in all the Company's power plants in 2016 was lower by 3.69% compared to the previous year. When taking into account the entire country, in 2016, there was a decrease in the energy production from brown coal at a comparable level, that is by c. 4.4%. In the ZE PAK SA, the production economics, operator's requirements, and geological conditions in the mines supplying the coal to the power plants decide primarily about the generation distribution in particular power plants. In 2016, in the Pałnów I power plant in 2016, the production increased slightly. In the Konin power plant, it remained at a similar level and in the Adamów it decreased.

Chart 1: Net electricity production*

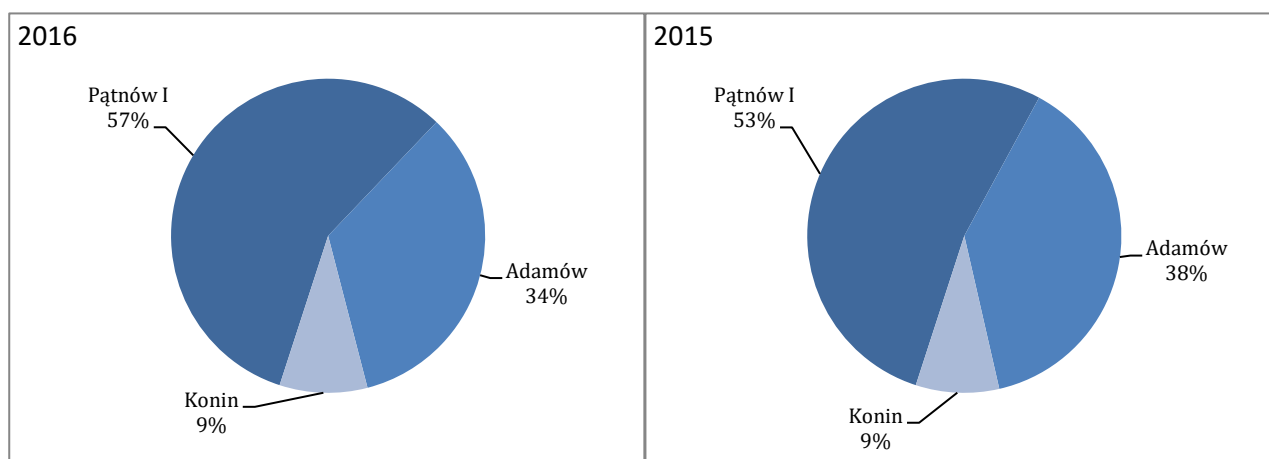


* Net electricity production together with the electricity production from the units 1 and 2 in the Pałnów I during the investment.

Source: internal data

¹ According to the Table: The 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, source PSE S.A. Total gross electricity generation in Poland in 2016 amounted to 162 626 GWh.

Chart 2: Structure of generation between power plants



Source: internal data

In 2016, the Company sold 8.07 TWh of electricity, i.e. approx. 0.7% less than in 2015.

The main direction of sales of electricity was the sale in the scope of bilateral contracts concluded with electricity trade companies conducting activities in the Polish market. This form of sales amounts to 64.4% of the electricity sales volume executed by the Company in 2016, including transactions with the final recipients that amounted to only 0.5% of the entire volume of electricity sales. The sale on the exchange market was 27.14% of the total sales volume. The electricity balancing market, on which the Company sold 8.46% of the total electricity sales volume, is the supplementation of the sales structure.

The electricity sales revenues (in total – generated and from the market) were 86.7% of the total revenue from the sales of the Company.

The number of green and red certificates obtained by the Company, due to the biomass unit as well as high efficiency cogeneration in heat production in 2016, is substantially higher than the number of certificates that the Company is obligated to present to the ERO President for redemption in order to fulfil the obligations imposed by the current regulations. Therefore, the excess certificates are to be sold, mainly on Towarowa Giełda Energii (Polish Power Exchange). In 2016, the Company generated 0.39 TWh of green certificates and 0.16 TWh of red certificates.

The heat generated in the Company's power plants is sold to local recipients. The main recipients include local heat power engineering companies as well as local industrial manufacturers. The Company covers almost the entire heat demand of Konin and Turek cities. In 2016, the Company's power plants sold 2,017 TJ of heat. The heat sales comprised c. 3.7% of the Company's total sales revenues. The service sales revenues (including for the Group's companies) were 9.3% of the total revenues in the past year.

The main raw material used by the Company for the production of energy is brown coal, which is extracted almost exclusively for the power plants' needs. This is because the brown coal extracted in Poland is a soft coal and its long-distance transport is not cost-effective due to the large contents of water. The extracted brown coal is delivered directly from open cast mines to the power plants nearby. Therefore, the extraction of brown coal in the ZE PAK Group is strictly related to the amounts of electricity produced by the power plants located near the mines.

In the Company, biomass is also used as raw material to produce energy, which is combusted in a boiler specially dedicated for this purpose in the Konin Power Plant.

3. DESCRIPTION OF ACTIVITIES

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

Significant events in the accounting year

Agreement on financial support for PAK KWB Konin SA

In the course of the work related to preparing the description of the Company's and Capital Group's further strategy as well as final projections for banks granting a loan for the final stage of the 1-4 units modernisation in the Pańów Power Plant, the ZE PAK SA and PAK KWB Konin SA Management Boards decided to conclude the agreement for reaching the necessary decisions on providing financial support for the investment carried out by PAK KWB Konin SA that involves the opening of a new brown coal open pit, which is to secure uninterrupted supplies of coal for the purposes of the ZE PAK Capital Group's power plants. On 16 March 2016, a relevant agreement, which constitutes the first stage of setting the rules on developing the necessary decisions between the parties, including the conditions for granting financial support for construction of a new pit, was concluded. Further decisions will be taken after the PAK KWB Konin SA obtains a decision determining the environmental conditions for the construction of the Ościsłowo brown coal open pit and will be preceded by an economical and financial analysis of the project regarding opening of the new open pit. The final stage will be to conclude the relevant (final) agreement/agreements on financial support after obtaining the required corporate consents

Annex to credit facility agreement for modernisation of units in Pańów I power plant

On 30 June 2016, the Company, with a consortium of banks consisting of: mBank SA, Bank Gospodarstwa Krajowego, Bank Millennium SA, Bank Polska Kasa Opieki SA and Powszechna Kasa Oszczędności Bank Polski SA concluded an annex to the investment credit agreement in the amount of zloty 1 200 million, granted to finance the final stage of the modernisation of units in the Pańów I Power Plant.

In the annex, the parties agreed that the Company's decision to resign from the external funding for the modernisation of the units nos. 3 and 4 in Pańów I power plant, which was to be granted on the basis of the agreement, will not constitute a breach of the agreement. The deadline for full credit repayment was changed. The repayment is to take place by 20 March 2020 (previously 31 December 2023). The Company, under the agreement, used the amount of zloty 667 million and voluntarily released zloty 533 million of the unused amount for the modernisation of the units 3 and 4. The financial terms of the credit agreed with banks remained at levels which do not differ from the market rates. Other terms of the Credit are similar to those adopted for this type of agreement.

The Company planned to complete the modernisation process, whereas in accordance with earlier declarations, the Company expects to implement system solutions that will ensure the economic profitability of the investment. Due to the inability to determine the date of the introduction of the above-mentioned system solutions, the Company decided to resign from further maintenance of the unused credit amount, so as not to incur the associated costs.

Termination of long term heat delivery agreement

On 30 June 2016, the Company notified the Municipal District Heating Company – Konin sp. z o.o. ("MPEC") on termination of the Heat Sale Contract no. 93/MPEC/PAK/2005 concluded on 1 January 2005 between the Company and MPEC, the subject of which is the heat supply from the Company to the city of Konin, executed from the date contract conclusion. The contract will expire with a 4-year notice, effective on 30 June 2020.

The agreement was terminated by the Company due to the fact that the heat generation from the currently used source based on brown coal in the Konin power plant after 30 June 2020 year will not be possible due to the environmental requirements. Whereas adjusting the currently used source to the stricter requirements would result in expenses exceeding the economic effect, which would be gained thanks to this.

The company still wants to remain the heat supplier for the city of Konin and for this purpose, it conducts analytical as well as formal and legal works in order to develop an optimal project of launching a new heat source, replacing the existing carbon one, which could be the basis for the conclusion of a new contract with MPEC

Postpone the decision on the construction of steam-gas power unit in Konin

In September 2016 the Management Board of the Company decided that the decision on the investment project on the construction of CCGT with a capacity of 120 MWe and 90 MWt and an additional peak boiler with a capacity of 40

MWt in Konin Power Plant will not be taken this year. Due to the current external conditions affecting the economic efficiency of the planned project and, above all, uncertainty about the shape of the support system for gas cogeneration after 2018, and also because of the relationship between gas prices, prices of CO₂ allowances and electricity prices, the Management Board decided that the decision to implement the project in the current circumstances would involve too many risks, which could adversely affect achieved financial results in the future, the value of the Company and thus the interests of the shareholders. Construction of CCGT in Konin Power Plant is an investment reported to the National Investment Plan ("KPI"). The implementation of the project in the specified range and time was associated with the allocation of free CO₂ allowances in the amount of about 6.3 million tons. In the current situation of the absence of a decision to launch the project by the end of the year, the Company assumes that it will not be able to get free CO₂ allowances arising from the implementation of the project in the context of the current KPI.

Construction of CCGT in Konin Power Plant is still part of the investment plan of the Company, however, if it could be implemented, certain conditions are necessary which lend credence a positive impact of the project on the value of the Company.

Preparing for the completion of the energy production in the coal-fired units of the Adamów power plant

The end of electricity production by the coal-fired units of the Adamów power plant is set by the completion of the period of an exemption of an environmental nature resulting from the IED directive on industrial emissions, which was implemented into the Polish legislation. The power units in the Adamów power plant are covered by the derogation exemption period, whose end falls in January 2018. Therefore, preparatory actions for conducting the proceedings that include all the necessary activities related to the completion of the operation of the coal-fired units of the power plant are currently in progress. These proceedings must be conducted by the Company in accordance with the applicable legal provisions, in particular on the natural environment protection, and in such a way as to identify and reduce the associated possible economic and social risks for the Company and the region. The team of people responsible for the thematic study of the strategies of conduct in the following areas: environmental, legal, technical, and organisational was appointed specially for this purpose. In relation to the preparations to complete the production in the coal-fired units of the Adamów power plants, PAK KWB Adamów SA submitted a statement of resignation from the license no. 9/2003 for extraction of brown coal from the Koźmin deposit on 31 December 2016 to the Ministry of the Environment. Currently, PAK KWB Adamów SA supplies coal to the Adamów power plant from the exploited Adamów Open Pit.

Discussions between the Management Board and the social party

In the fourth quarter of 2015, the Management Board of the Company, having regard to the deteriorating external factors on the economic results of the energy generation segment, decided to temporarily suspend the financing of the employee pension fund ("EPF") in the Company as well as to reduce the statutory bonus attributable to the employed workers. At the same time, the Management Board offered the social party temporary suspension of the Corporate Collective Labour Agreement, as a whole or in part. The Management Board's proposals were not accepted by the social party.

The trade unions acting in ZE PAK SA reported, under the Act of 23 May 1991 on resolution of collective disputes, requests related to, among others, new components of the remuneration system, severance payments and work safety.

The Management Board refused to execute the trade unions' requests. The Management Board considered unacceptable the trade unions' requests on introducing the new components to the remuneration system, according to Article 4 paragraph 2 of the Act on resolution of collective disputes. The consequence of failure to take into account the requests includes the occurrence of a collective dispute between ZE PAK SA, as an employer, and the trade unions, as the representation of employees, since 8 February 2016. So far, no agreement on the collective dispute related to the requests reported by the letter of the trade unions of 8 February 2016 has been concluded.

On 12 May 2016, the Company's Management Board decided to liquidate the EPF, which was one of the topics of the talks conducted with the social party. The fund will be liquidated with a 12-month notice. In relation to the termination of the EPF, the Company applied to the PFSA to delete the fund from the employee pension funds. Currently, the administrative proceedings on deleting the fund are in progress.

On 18 January 2017, the trade unions operating in the Company filed another letter submitted under the Act of 23 May 1991 on resolution of collective disputes, containing requests regarding, among other, statutory bonus, return of the unpaid contributions to the EPF, and development of the support programme the Adamów power plant's employees. The Company's Management Board replied to the requests of the trade unions by presenting its position on individual requests along with invoking the relevant arguments in support of the taken position, by pointing to, among others, illegitimacy of the requests or the consequences of the regulation in the provisions of Article 4 of the Act on resolution of collective disputes concerning the inadmissibility of conducting a collective dispute. Currently, the talks between the Company's Management Board and the trade unions in relation to the requests applied by the letter of 18 January 2017 are in progress.

Significant events after the balance sheet date

On 13 March 2017, PAK KWB Konin SA received the decision of the Regional Director of Environmental Protection in Poznań (“RDOŚ in Poznań”) of 10 March 2017 refusing to determine the environmental conditions for the project titled: “Extraction of brown coal and associated minerals from the Ościsłowo Open Pit.” The decision of RDOŚ in Poznań is not final. The decision may be appealed against to the Chief Director of Environmental Protection via the RDOŚ in Poznań within 14 days after the date of delivery. PAK KWB Konin SA will appeal against the issued decision in an appropriate manner. According to the assessment of the Company’s Management Board, there are real premises to expect that the PAK KWB Konin SA’s appeal will be considered positively. According to the Company, the issued decision is devoid of substantive arguments and has not been supported by expert’s reports confirming the negative impact on the environment in the case of application of the solutions proposed by PAK KWB Konin SA.

As of the date of preparing this statement, in the Company’s Management Board opinion, the risk of not meeting the construction schedule and the commencement of exploitation of the Ościsłowo open pit is negligible; If, however, that risk materialises, the changes concerning the production plans of the Group in future years would be relevant, including a situation, in which they would have an effect on estimates of future expected cash flows generated by the generation assets of the Group.

3.2. Significant agreements concluded in the accounting year

Significant agreements for the Group’s activity

Because of the characteristics of the activity and the market, in which the ZE PAK SA 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, Company concludes framework agreements with particular counterparts setting out the basic terms and conditions of cooperation. Whereas purchase/sale alone are executed in separate transactions in relation to specific quantities using current market prices.

Apart from the standard agreements, concluded in the course of usual activities, such as the mentioned agreement of raw materials supply, energy sales, or CO₂ emission allowances purchase, in 2016 ZE PAK SA entered into following agreements with:

- PAK Serwis sp. z o.o., the multiannual repair and service of machinery agreement. The subject of the agreement are services in the field of service and mechanical repairs, provided by PAK Serwis sp. z o.o. for the Company aimed at maintaining the equipment used to generate electricity in optimal technical state. The agreement is valid in 2016-2021. The total estimated agreement value throughout its validity is zloty 277 million net.
- EL PAK sp. z o.o., the multiannual financing agreement for the provision of maintaining operation in ZE PAK SA’s power plants. The subject of the agreement are services in the field of maintaining operation of systems and electrical devices as well as I&C systems and equipment, provided by EL PAK sp. z o.o. for the Company aimed at maintaining the equipment used to generate electricity in optimal technical state. The agreement is valid in 2016-2021. The total estimated agreement value throughout its validity is zloty 115 million net.

Agreements regarding the obtained credits and loans

In 2016, ZE PAK SA signed the following agreements regarding credits and loans:

1. ZE PAK SA signed the Annex no. 3 to the Corporate Credit Agreement of 13 March 2014. On the basis of the Annex no. 3, the unused part of the A Credit was released (zloty 533,000 thousand) and the repayment period was reduced to 20 March 2020. The credit agreement with the consortium of banks comprising of: mBank, Bank Millennium, BGK, PKO BP and PEKAO SA.
2. ZE PAK SA signed with the PKO BP SA bank:
 - the Annex no. 19 extending the overdraft facility capital repayment date to 25 November 2017.
 - the Annex no. 20 concerning the commission from the unused amount of the overdraft facility capital. The available credit limit amounts to zloty 90,000 thousand. The interest rate according to the WIBOR rate amounts to 1M plus the bank’s profit margin.
3. ZE PAK SA signed with the PEKAO SA bank:
 - the Annex no. 11 reducing the overdraft facility capital limit to the amount of zloty 40,000 thousand and extending the credit repayment date to 30 November 2016.
 - the Annex no. 12 extending the overdraft facility capital repayment date to 30 November 2017.

The available credit limit amounts to zloty 40,000 thousand. The interest rate according to the WIBOR rate amounts to 1M plus the bank's profit margin.

Agreements regarding the granted loans

In 2016 the Company did not grant any loans.

Granted and obtained guarantees and sureties

Table 2: List of guarantees and sureties granted by Company as of 31 December 2016

	<i>zloty thousand</i>	<i>euro thousand</i>
	<i>31 December 2016</i>	
<i>Granted guarantees and sureties</i>		
Zespół Elektrowni Państw – Adamów – Konin SA		
1 Surety		
1.1 Surety for PAK KWB Konin for overdraft facility at BZ WBK Bank	65 000	
1.2 Surety for PAK KWB Konin for overdraft facility at Millennium SA	76 500	

Table 3: List of guarantees and sureties obtained by Company as of 31 December 2016

	<i>zloty thousand</i>	<i>euro thousand</i>
	<i>31 December 2016</i>	
<i>Obtained guarantees and surety</i>		
Zespół Elektrowni Państw – Adamów – Konin SA		
1 Guarantees		
1.1 Payment Guarantee	8 551	
1.2 Contract performance guarantee	36 958	
1.3 Advance return guarantee	5 929	

Insurance agreements

In 2016, the Annex no. 3 to the General Complex Insurance Agreement of the ZE PAK SA Group's Companies (ZE PAK SA, PAK KWB Konin SA and PAK KWB Adamów SA) was concluded on 31 March 2014 for the period from 1 April 2014 to 31 March 2017 with the consortium of Co-insurers comprised of: Sopockie Towarzystwo Ubezpieczeń Ergo Hestia SA, Towarzystwo Ubezpieczeń i Reasekuracji Warta SA, Towarzystwo Ubezpieczeń i Reasekuracji Allianz Polska SA and UNIQA Towarzystwo Ubezpieczeń SA – extending its validity period to 31 March 2019. The total insurance sum of fixed assets amounted to zloty 8.3 billion. The Policy Agreements include insurance coverage; property from any risk, loss of profit due to any risk, machinery and devices from damage, loss of profit due to machinery and device failure, electronic equipment from all risk, machinery, and devices from electric damage.

The agreements concluded with affiliates on conditions different than market conditions

In 2016, there were no agreements concluded on conditions different from market conditions between the affiliates of the ZE PAK Capital Group.

3.3. Investment programme execution

Key investments during execution

Pańnów power plant

The main purpose of disbursement of the investment expenses in 2016 was to finance the continuation of modernisation of the coal handling system in the Pańnów I Power Plant, which is to guarantee a process system with a large handling capacity for feeding the basic fuel to the boilers. By the end of 2016, about 90% of the subject scope of coal handling modernisation. The investment funds disbursed in 2016 were also intended to prepare the necessary tasks for the future operation of the generation assets.

In January 2016, the decisions of Powiat Inspectorate of Building Supervision [Powiatowy Inspektorat Nadzoru Budowlanego] in Konin on permits for use of the units 1 and 2 in the Pańnów I Power Plant became valid. The maximum power of each of the modernised units currently amounts to 222 MWe (previously 200 MWe). Both units generate electricity to the National Power System and provide the system services related to controllability of a generating unit in terms of power ranging from the technical minimum of 132 MWe to the permanent generating power of 222 MWe and the service of the unit's participation in defence and restoration of the National Power System, the so-called island operation. In 2016, in accordance with the contractual provisions, warranty measurements of achieving all of the units' guaranteed technical parameters were carried out. The basic effect of the modernisation was to increase the efficiency of the units from 33.5% to 37.5% and reduce gas emissions into the environment, to the following sizes:

- nitrogen oxides (NO_x) emissions reduction from 1.37 kg/MWh before modernisation to the adopted level of 0.74 kg/MWh;
- carbon dioxide (CO₂) emissions reduction from 1.17 Mg/MWh to the adopted level of 1.05 Mg/MWh;

Moreover, in 2016, the implementation of the IT system for keeping a unified database on real estates was completed. The aim of implementing the IT system for keeping a unified database covering all real estate possessed or managed by the ZE PAK SA Capital Group was achieving benefits both in the field of liabilities, costs and increasing the used assets efficiency as well as in the field concerning the expenses related with the economic use of the real estates, i.e. extracting brown coal, waste management, environmental impact management (especially water leachate) and land reclamation management.

Bearing in mind the current difficult situation on the domestic energy market, which affects mostly energy producers and is caused by external factors independent from the Company. In the first half of 2016, actions were taken to improve the efficiency in current activities' costs, including the costs of production assets maintenance, allowing to accomplish the Group's strategic goals. Changing economic and legal conditions in Poland, including the decrease in the profitability of energy production in coal-fired power plants, forced to verify the previously taken investment decisions expected for the units nos. 3 and 4. In 2016, re-analyses of the effectiveness of investment tasks expected for the units nos. 3 and 4 taking into account in particular, the current and expected economic, legal and technical conditions, including the assessment of viability of incurring the investment expenses related to the requirements concerning the BAT conclusions, which will be announced within the framework of the IED Directive. Considering the above fact, the decision on starting to implement the investment in the units 3 and 4 will be made after conducting the re-analysis of economic assumptions for the planned projects. Currently, uncertainty concerning the final form of the environment requirements currently prevents from making decisions related to the high investment expenses. It is reasonable to wait for the concrete form of regulations on emission standards, which have a significant impact on the assumptions adopted for the calculation of effectiveness of the planned investments. The scope of the planned system solutions aimed at creation of investment pulses for new power and modernisation of the already existed generation assets is of great importance in the context of the modernisation work execution on the units 3 and 4. The company carefully follows every proposal in this regard.

Key investments during the preparatory stage

The most important project implemented at the design stage in the Konin power plant was the construction of the gas-steam unit together with the Koło-Konin gas pipeline. It was assumed that this unit would have a power of approx. 120 MWe and approx. 90 MWt as well as an additional peak load boiler with a power of approx. 40 MWt (dedicated to the supply of heat for the city of Konin). The commissioning of the unit was planned for 2020. However, due to existing unfavourable external conditions, including the uncertainty about the shape of the support system for the co-generation after 2018, on 29 September 2016, the Company terminated an agreement with PSE SA to connect the gas-steam unit to the transmission system in the Konin power plant. In October, the agreement with the Energoprojekt-Katowice SA design office responsible for the design of the gas-steam unit and the Koło-Konin gas pipeline was terminated as well. Despite the terminated agreements, this project remains in the Company's investment program.

After many years of operation of the turbogenerator no. 6 in the Konin power plant, it was modernised in 2012, including it into the unit system producing the electricity based on biomass combustion. During the modernisation of the generator, its service fluid from the hydrogen to the air. After such modernisation, the generator had two serious failures, whose main cause was elements of the modernised cooling system. In view of the above, the generator modernisation contractor, referring to the current experience related with the generators' modernisation executed in recent years, after implementing own calculation models, recommended that value of the generator no. 6 installed in the Konin power plant's load with the active power does not exceed 50 MW. The recent modernisation works on the generator no. 6's cooling system finished in January 2017. After the finished modernisation, ZE PAK SA applied to the President of the Energy Regulatory Office to change the data in the licence for electricity generation of the generating unit no. 1 of the Konin power plant. The application concerns determining the output and installed power for the turbogenerator no. 6 at the level 50 MWe (formerly 55 MWe).

In the first half-year of 2016, studies preparing an alternative solution involving the reconstruction of heat sources in the Konin power plant, which would provide heat supplies to the city of Konin after immobilization the coal part of the Konin power plant in June 2020 and the absence of launching the planned new gas-steam unit, were started. The electricity and heat energy production in co-generation would be based on the existing biomass boiler. As part of the above project, the promises of an amendment to the licence for electricity and heat generation in the dedicated biomass co-combustion system in the was already obtained from the Energy Regulatory Office.

In addition, in the Konin power plant, the designing works related to the development of the Terms of Reference (ToR), which will be the basis for selecting the contractor of the TG-6 turbine's modernisation in order to adjust it to heating the district heating water fed to the city of Konin, are currently in progress.

3.4. Risk management

While conducting its operations, the Company is exposed to a series of risks, occurring actually, potentially or theoretically, present in the industry as well as on the markets on which the Company operates. These are factors which originate both from the inside of the Company as well as from its environment. Taking into account the formalisation of the realm related to the risk in the Company's operations, the complex document titled "Principles of Risk Management for the ZE PAK S.A. Capital Group" ("Management Principles") was developed. The Management Principles were developed and introduced in order to define and specify the limits of risks present or which can occur in the ZE PAK S.A. Capital Group as well as to specify the mechanisms used to minimise risk exposure in the course of conducting operations in the energy sector and to minimise the effects of the risk, which due to the specificity of the ZE PAK S.A. Capital Group's primary production operations cannot be eliminated in its entirety.

The first stage was to specify the Group's companies, in the operations of which the risk with material significance for the operations of the entire group can be identified and then to use appropriate principles of procedure. The Companies significantly affecting the Group's primary operations are: ZE PAK S.A., EPII, PAK KWBK S.A., PAK KWBA S.A., PAK Centrum Usług Informatycznych Sp. z o.o., PAK Volt S.A. Other Companies in the Group do not directly affect the operational risks.

The Capital Group's business model and strategy were established pursuant to the aforementioned principles. The primary principle of the business model executed by the Group in the realm of its business operations: extraction, production and trade are to maximise the production and profit with simultaneous compliance with the risk minimisation principle. In order to achieve its business goals, the Group accepts to incur the risk, but only in the scope and pursuant to principles specified in the Management Principles. All types of business risks and situations resulting in exposure to risk are constantly minimised, provided that the Management Principles or the Board's decisions do not authorise specific deviations. The specific roles and the scope of liability for decisions and actions related to the executed market policy and strategy were distinguished in relation to the Group's capital structure and the organisational chart of particular companies. A special role, related to the compliance and proper application of the Management Principles, is played by the task team named the Risk Management Committee, which acts as a consultative body for the ZE PAK S.A.'s Board. The body was appointed by the Order of the President of the Company's Board. The main task of the Risk Management Committee is to recognise, identify and evaluate in substantive terms all economic risks with a value exceeding PLN 10 million, related to the business operations conducted by the Group.

The scope of the Group's risk management featured identification of specific areas of risks related to the execution of the established business goals:

- 1) raw material risks;
- 2) production risks;
- 3) market risks and related financial risks;
- 4) operational risks related to the operation of IT systems;

5) risk in the area of information security.

Each area of risk identified above included the identification of specific types of risks related a specific area. The type of a given risk was thoroughly described with specification of theoretical examples of its occurrence in the Group's operating activities. Each type of risk also features specific forms of action aiming at its minimisation or elimination, a specific benchmark was also assigned and the so called "key performance indicator", i.e. the minimum performance level, was specified wherever possible.

Directors and employees of organisational units allocated to a given area of risk are subject to inspection in the scope of compliance with the Management Principles, appropriately to their scope of operations. The management of the organisational units is responsible for the proper and compliant with the Management Principles execution of tasks by subordinate organisational units and individual positions. The Management Principles also include an in-depth description of the correct reporting process regarding the identified risk as well as the method of procedure in case of identifying the infringement of the principles described in the document.

According to the Management Principles, the compliance with the procedures and methods of procedure described in the document can be abandoned only in case of obtaining the approval of the ZE PAK S.A.'s Board expressed in writing. In such case a special procedure also described in the Management Principles is applied.

3.5. Description of use of emission earnings

In 2016 the Company did not issue any securities.

4. MAIN BUSINESS RISKS

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

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

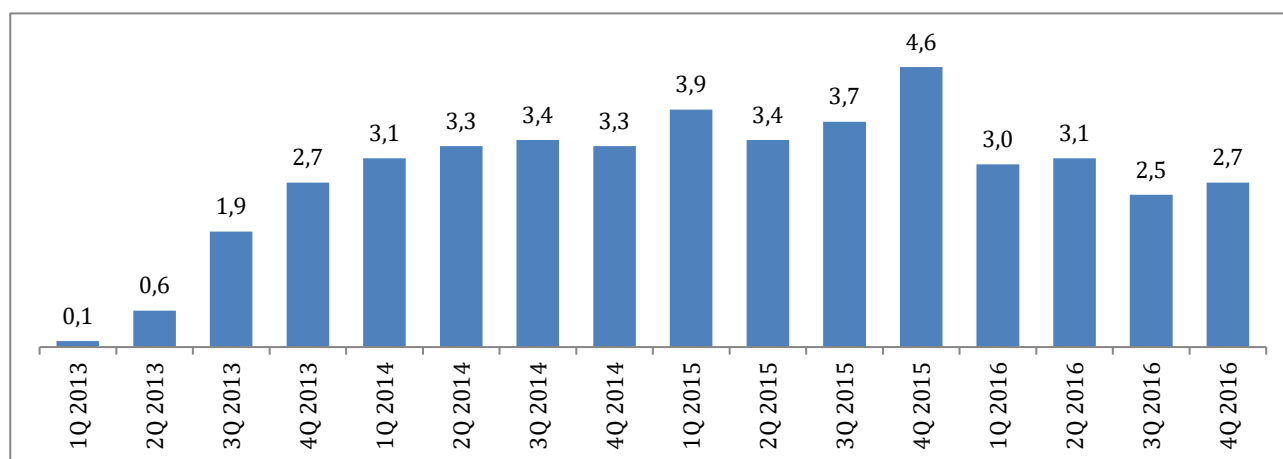
- macro-economic trends in the Polish economy and the demand for electricity;
- regulatory environment;
- electricity prices;
- prices and supply of certificates of origin;
- fuel costs and supplies,
- CO₂ emission allowances costs;
- seasonality and meteorological conditions;
- investment expenses; 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 Company'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 2016 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

When 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.

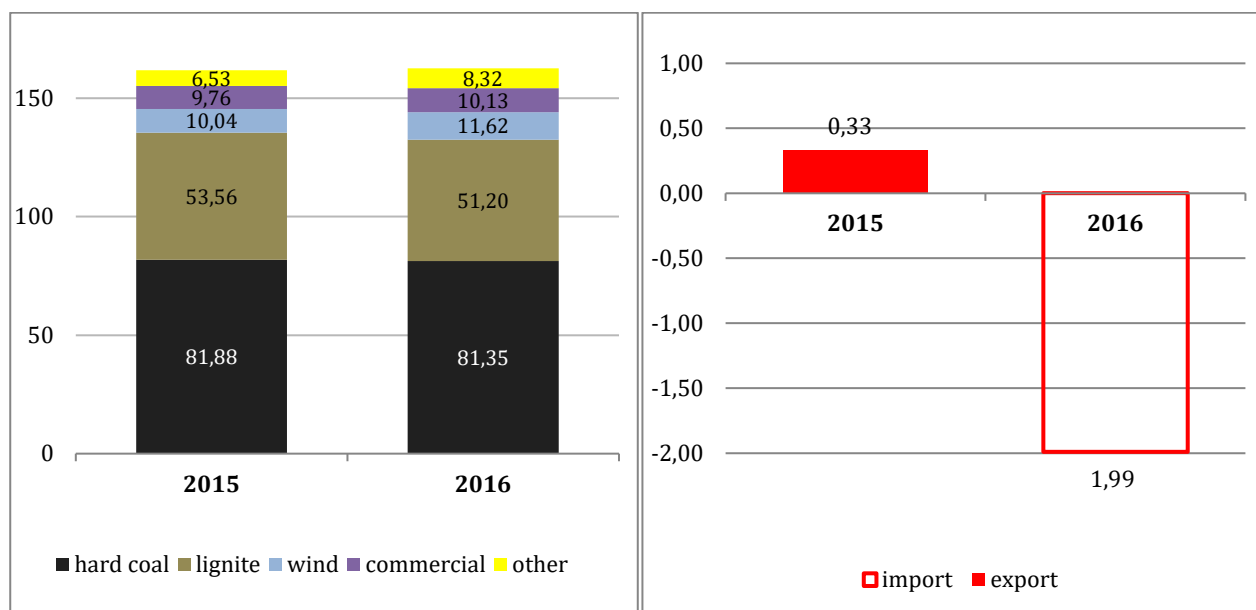
Chart 3: GDP dynamics (%) in relation to the analogous quarter of the previous year



Source: GUS data

According to the initial Central Statistical Office's estimation, the gross domestic product ("GDP") calculated in fixed prices from the previous year increased in real terms in 2016 by 2.8% in relation to the growth by 3.9% in 2015. At the beginning of 2016, forecasts regarding the growth were around 3.6-3.8%. However, they were revised downward many times throughout the year. By analysing the quarterly data, it can be noticed that the results for particular quarters of 2016 have been the lowest since the end of 2013. Consumption and investments, where we dealt with opposing trends, decided on the GDP dynamics in 2016 to the greatest extent. In the case of retail sales, the dynamics had been the highest for many years. There were many factors supporting consumer demand in 2016. The most important ones include: the decrease in the registered unemployment rate to the volume of 2.3% at the end of the year, significant dynamics of the increase in salaries, as well as the "500+" child benefit programme's effect. The cumulated impact of all these factors caused the demand stimulus positively influencing the consumption's contribution to the GDP dynamics for 2016. However, it must be noted that some of these factors, due to the base effect, may be a burden of the dynamics. The investments influenced the GDP in the opposite direction in 2016. Here, we also dealt with a combination of several factors that caused this effect. The most important ones include: lower inflow of EU funds related to a new prospect of the expenses of these funds, legislative changes in the area of taxation (e.g., VAT, the so-called "trade tax" or "bank tax") causing the uncertainty about their impact on economic activity, and significant, cyclic nature of the investments. Very low readings of the construction and assembly production indicator, which could reach -20% in particular months, may indicate the scale of this component's negative impact. However, in the case of investments, one can expect that some of the factors that negatively affected the dynamics in 2016 will reverse like the mentioned cyclic nature or the increased EU funding stream that, combined with the effect of a low base, will allow for the reconstruction of this GDP component in subsequent periods. It is worth only mentioning that the export's impact on the GDP dynamics in 2016 was very small but the increase in the inventory worked positively.

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



Source: own development based on the PSE data

The data concerning the functioning of the National Power System and the Balancing Market, presented by Polskie Sieci Elektroenergetyczne SA, show that the national electricity consumption² in 2016 was 164.6 TWh, and increased by 1.97% in comparison to the previous year. The increase in consumption was recorded in all the months of 2016 except for July, when a slight decrease was recorded. A stable rate of economic development, including the dynamics of the industrial production growth and weather conditions, also influenced the energy consumption in 2016. The greatest demand for power in 2016 was recorded on 15 December at approx. 5:00 p.m., at the level of the 25,576 MW³. In 2016, the total electricity production increased by 0.53%. Taking into account the entire year balance sheet, the decrease in generating the energy from two main (in terms of produced energy volume) raw materials, i.e. hard and brown coal, was recorded. The energy production from hard coal decreased by 0.65%, and from brown coal decreased by 4.41%. It is worth noting that the decrease in the production from brown coal concerned especially the first years of 2016 and was associated with repair works in one of large power plants. The dynamic generation growth from wind sources was recorded again, this time by 15.76% per year. The increase in generation from wind sources was commensurate with the increase in wind power plants' output capacity, which increased by 14.6% to 5,735.9 MW in 2016⁴. In the past year, there was a noticeable increase in gas generation by almost 37.8% compared to 2015. Electricity produced from hard coal was 50% of total electricity production, energy from brown coal – 31%, and wind turbines generated 7.1% of the total energy. On the other hand, the direction of foreign trade changed. In the past year, Poland was a net electricity importer, the import surplus over the export amounted to 1.99 TWh compared with 2015, when Poland was the net exporter of electricity in the amount of 0.33 TWh.

Regulatory environment

The entities conducting activities in the electricity market are subject to strict regulation, such as the Energy Law, the law on renewable energy sources ("res"), resolutions, as well as the directives of the European Commission and international conventions, regarding, among others, the environmental protection, and climactic changes (including CO₂

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

³ Based on the graph: Demand cycles on days, on which the minimum and maximum domestic power demand occurred included in PSE SA's website.

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

emissions), obligation of public sales of a part of the generated energy as well as the support of specific energy generation processes. 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.

In the past year, in the broadly understood regulatory environment important for the ZE PAK SA Group's activities, there were few significant changes that would significantly affect the Group's activities. Although works on several important issues were in progress, among which one must pay attention to the draft of solutions concerning the "power market" functioning principles, they were not completed by the end of 2016. The act regulating the principles of the power market's functioning is one of the key legislative acts for energy producers. In the author's concept, this act is to ensure the profitability of the new power units and the modernisation of the already existing units, without which the power system is threatened with power deficit. Due to the age of the currently operated power units, it is expected that in the following years, a significant part of the power plants built as early as in the 1960s and 1970s will have to be closed permanently. The modernisation of part of generating units (especially the 200 MW units) may prove to be a solution to the current problems, however the current energy wholesale prices are not favourable for undertaking big investment liabilities, to which repairs of the old units and the construction of the new ones are related. It is the power support mechanism that is to solve the problem of the lacking funds. In the assumptions presented during the past year, the power market is to be based on auctions. The producers of energy with the power of over 2 MW are to be certified and then allowed to participate in the auctions, providing the power in the system. Auction parameters are to be determined on the basis of the planned power demand forecast by the Polish Power Grid [in Polish: Polskie Sieci Elektroenergetyczne]. In the concept authors' intend, the principles regulating the selection process in auctions are to take into account "the state energy policy, adequacy of the applied parameters to the needs to the national power system, ensuring the safety of the national power system, as well as equal and non-discriminatory treatment." The funds for the implementation of the concept is to be ensured by the "power charge" added to the energy bill. The amount of the charge is to be calculated by the President of the Energy Regulatory Office on the basis of the regulation of the minister of energy, which will its parameters in detail. The provisions of the new law have already been prenotified by the European Commission ("EC"). Meanwhile, on 30 November 2016, the EC presented a draft document called "Clean Energy for All Europeans legislative proposals," whose provisions include the introduction of the CO₂ emission limit for publicly funded electricity producers, who would operate within the power market. The EC's proposals may complicate the process of determining the provisions of a bill. Currently, further works related to the provisions of the act on power market by the EC are in progress.

On 1 January 2016, after many years and subsequent concepts, the Law on res entered into force. However, the date of entry into force of part of the provisions were postponed by a half of year. On 1 July 2016, another amendment to the law on res entered into force. The amendment concerns mainly the chapter 4 of the law regulating the new principles of supporting green energy producers. At the end of 2016, the first auction for renewable energy sources producers was launched. Within the auction system, the specified amount of energy from res will be ordered in division by particular res technology baskets. The amended regulations emphasised rewarding technologies providing renewable energy generation mainly by a stable generation. The support principles for prosumers were also standardised. The new definition of prosumer allows the broader directory of entities, including not only households but also among others public sector institutions, to use the preferences. These preferences involve proposing a system, in which the so-called indulgence for the energy taken from the operator for putting the unconsumed energy excesses to the grid is entitled to the prosumers in place of the guaranteed tariffs system. Another new solution is the introduction of a separate obligation, within the framework of the so-called "res obligation" to purchase green electricity from biogas plants, which is to improve the financial situation of the biogas plant owners. The provisions of the law also introduce conditions improving development of the power engineering scattered within local energy cooperates and clusters. These entities are to take part in one of the auction system ranges. However, the Ministry of Energy admits that some of the provisions of the Law will require clarification in the subsequent amendments in 2017.

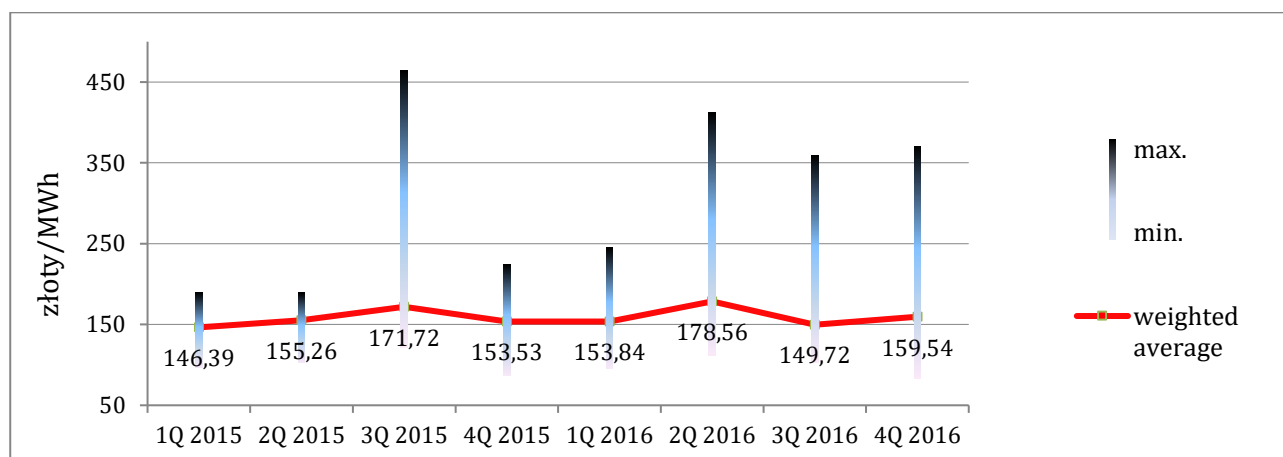
Electricity prices

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 addition, the Company practices the purchase of energy on the market of electricity (including the exchange market and balancing market) and re-sale to recipients.

In 2016, there was a significant decrease in the average price of energy in relation to the previous year. The weighted average of the quotations of the IRDN index (Next Day Market Forecast) on TGE (Polish Power Exchange), for 2016, stood at 160.71 zloty /MWh, which means an increase in relation to 2015 by 4.67 zloty /MWh, i.e. by about 3%. The growing number of periods with increased volatility of the price levels of electricity is characteristic for the past year. Whereas in 2015, because of the weather conditions and a considerable number of repairs of the power units, the increased volatility of the price levels occurred only in the third quarter (especially in August), in 2016 the increased volatility on the market occurred in the second, third, and fourth quarters. The factors influencing significantly the level of stock prices on the SPOT market remained the same, of which the most important are: the size of the wind generation

rate, the reserves in the National Power System, import transmission capacities available for the cross-border exchange, as well as weather conditions. According to the PSE data, at the end of 2016, there were 5735.9 MW⁵ of wind turbines' power installed in the system, which means an increase by approximately 730 MW, i.e. 14.6% year-on-year. The generation from wind resources increased at a similar pace. The energy produced from wind was 7.1%⁶ in 2016, while the year before, it was 6.2%. The increasingly larger share of unstable sources in the energy generation is one of the reasons the increase prices volatility. In 2016, this concerned especially the third and fourth quarters. In periods, when the generation from wind turbines is high, the energy prices are recorded at their minimums. At the same time, the low level of wind powers use contributes to the rapid growth of energy prices since the conventional powers with high production costs have to be used. Another factor, which significantly impacted on the price levels in 2016, was the reserves in the power system. The need for periodic repairs and modernisations causes that power units must be shut-down from the production for the time of executed works, and the reserve in the system is decreed. In a situation, when the amount of planned shut-downs is relatively large, and e.g. weather conditions justify the increased demand for power, the prices begin to increase. In the past year, in order to prevent repeating of the situation of August 2015, the part of the repairs was postponed to the second quarter. However, extremely high temperatures in June resulted in a very high demand for energy used for cooling in this period. It was the low level of the reserve in the system and weak wind in the second quarter caused that prices in this period were characterised by increased volatility and high levels. The highest quarterly weighted average price was recorded in the second quarter at the level of 178.56 zloty /MWh. The lowest quarterly weighted average price shaped at the level of 149.72 zloty /MWh in the third quarter. The prices of hard coal on the world markets in the past year, as opposed to 2015, trended higher. However, it did not translate largely into the prices offered by domestic coal producers for energy producers in 2016. The entire domestic hard coal extraction sector underwent significant changes in ownership in the past year. The greatest coal producers became affiliated with the greatest state energy companies. The impact of these transformations as well as acquisitions of significant foreign generating assets in Poland by the state companies did not have a major impact on the level of energy prices. The policy regarding the prices of hard coal supplies in the future and proceeding consolidation of the energy sector in Poland on the energy prices in the future years remain unknown.

Chart 5: Electricity prices (IRDN)



Source: own development based on the TGE data

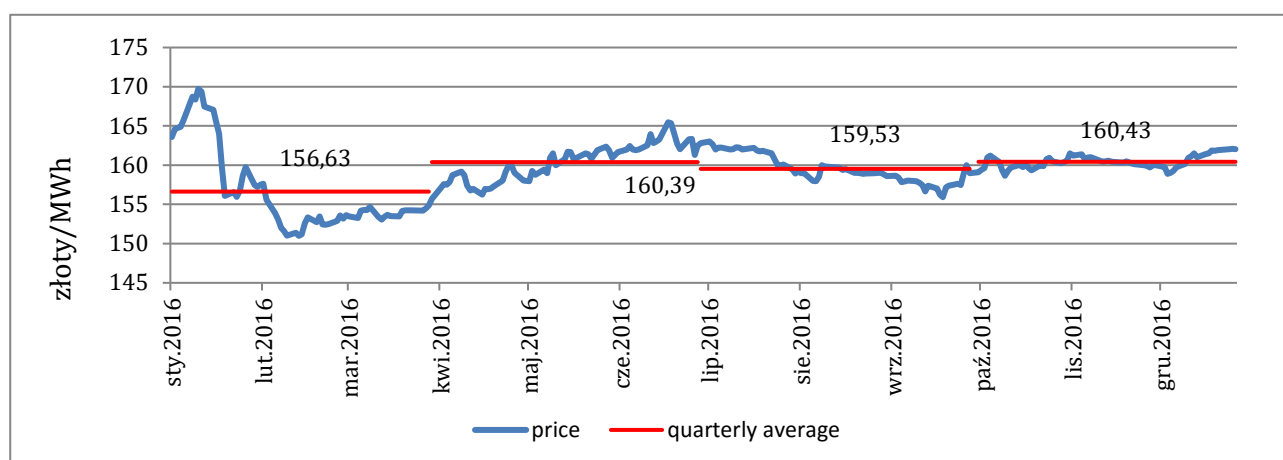
On the futures market of the electricity of the Polish Power Exchange, the most liquid instrument, the annual contract BASE_Y-17, was being quoted at relatively high levels in January 2016, along with the higher prices on the spot market. In a later period, the prices decrease dynamically, reaching its annual minimum at 151 zloty /MWh in mid-February. From this moment, the contract prices had been steadily growing since the mid-year but they did not reach the maximum recorded in January at the level close to 170 zloty /MWh. In the second part of the year, the prices were fluctuating within a relatively narrow range between 156 and 164 zloty /MWh. By analysing the quarterly arithmetic averages of the BASE_Y-17 contract's price, it is easy to note that, except for the first quarter of 2016, in other quarters,

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

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

the price is almost flat and close to 160 zloty /MWh. It can be concluded that the increased volatility and price signals from the spot market, except for the first quarter, did not affect the futures market very much in 2016.

Chart 6: The price of the futures contract for the supply of electricity (base) for 2017



Source: own development based on the TGE data

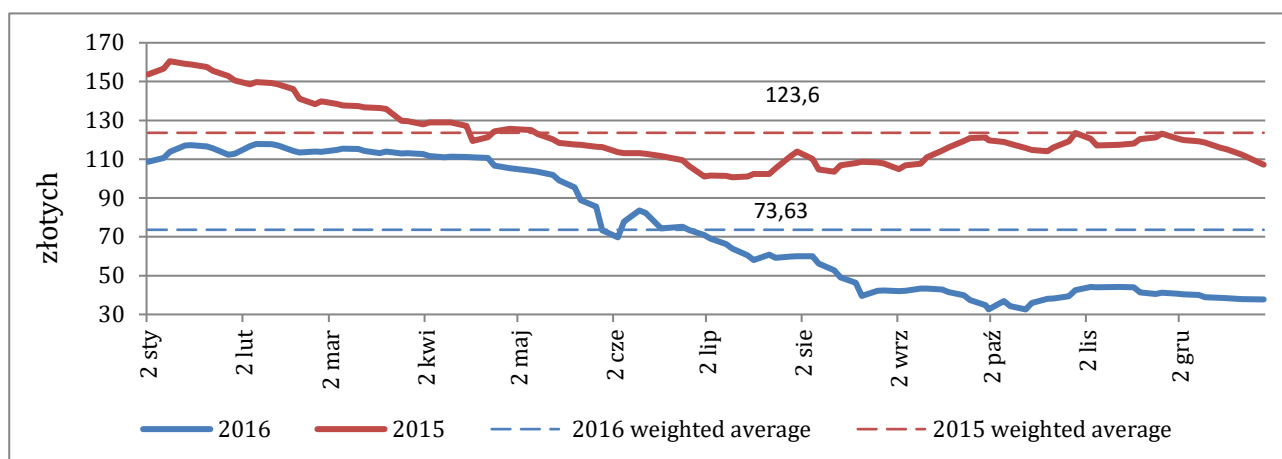
Certificates of origin

Due to the fact that a part of the electricity generated in ZE PAK SA derives from the combustion of biomass (forest and agricultural) and the production of heat includes high-efficiency co-generation, a producer is entitled to green and red certificates, provided that it fulfils specific regulatory requirements. The number of obtained certificates of origin is significantly higher than the number of certificates that the Company is obligated to present for redemption, thus it is possible to dispose of their excess to other market participants.

2016 was another year of dynamic decrease in the price of green certificates. In 2016, like in 2015, the highest levels were recorded in the first quarter. Later, a gradual decline or stagnation at low levels occurred. The weighted average price of green certificates in 2016 shaped at the level of zloty 73.63,⁷ which means a decrease in relation to the average of 2015 by zloty 49.97, i.e. by as much as 40%. The price minimum recorded in October amounted to zloty 32.57 per certificate. The causes of deep decreases of the green certificates prices remain similar as in the previous periods. The huge oversupply of production in relation to the demand, which is the derivative of the coefficient of the obligation to redeem the certificates of origin, causes that the prices reach even lower levels. The green energy producers pinned some their hopes on the new law on res. Although it did not enter into force in its entirety on 1 January 2016, however, provisions limiting support for installation of biomass co-combustion to some extent and eliminating the support of the so-called “large” hydrological systems producing energy have been already in force since the beginning of 2016. The provisions of the new law on res also provided an increase in the coefficient of the obligation to redeem the certificates of origin. However, the dynamic process of wind powers growth in 2015 and 2016, and hence the increasing number of green certificates generated from the increasing amounts of energy generated from the wind prevented the inhibition of the process of the dynamic decrease in the prices of green certificates of origin.

⁷ The weighted average of the PMOZE_A instrument quotations on the Polish Power Exchange.

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



Source: own development based on the TGE data

Fuel costs and supplies, coal extraction costs

Fuel costs is the most important part of the costs related to the electricity and heat generation in companies of the ZE PAK SA. The prices of fuel largely determine the competitiveness of particular electricity production processes. The ZE PAK SA power plants produce most of their electricity from lignite, 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 lignite mines, PAK KWB Konin SA and PAK KWB Adamów SA, which are the suppliers of lignite to the ZE PAK SA power plants, satisfy the demand of generation assets for this basic fuel. Therefore, the ZE PAK does not rely on external suppliers and eliminates the exposure to potential fluctuations of lignite prices. Nevertheless, the Company is exposed to the fluctuations in prices of other fuels used (mainly biomass) and part of the costs related to the extraction of lignite depends on the factors which remain outside the direct control of the Company.

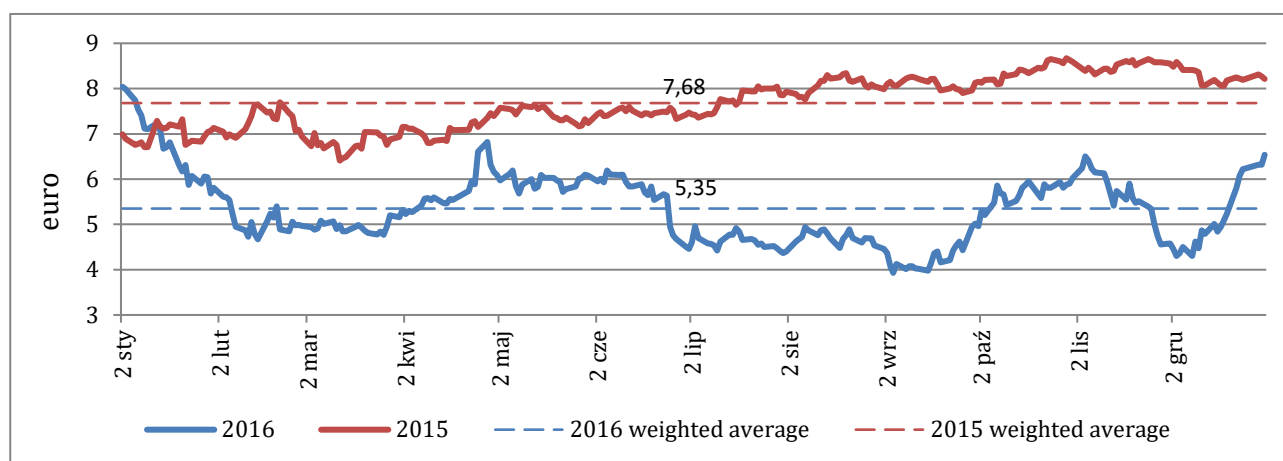
The deposits exploited by the Group's mines have specified richness. The opportunity to achieve the expected level of electricity production in the long term is partially dependent on the ability of extracting from the currently exploited deposits and launching the exploitation of new brown coal deposits, 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 licence 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 production of electricity and heat from conventional sources are associated with the need to bear 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 brown coal, the impact of emitted quantities of CO₂ (EUA) and the price of emissions allowances is of great importance to the activities results. The results largely depend also on the amount of free-of-charge CO₂ emission allowances granted in a given period. The number of allowances possible to be obtained for power engineering were specified in article 10c of the ETS directive and the amounts that can be physically obtained by particular systems depend on the expenses incurred for investments, which are recorded in the National Investment Plan. The Group is obligated to purchase the other part of the missing allowances on the free market. ZE PAK SA also uses a small amount of free allowances from the article 10a of Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 (EUAs for the needs of heat generation). In 2016, the Group received a very small amount of CO₂ free emission allowances oscillating in the range of 100 thousand EUAs, most of which results from the allocation for heat generation. Therefore, practically the entire amount emission allowances needed for the ZE PAK SA Group had to be purchased on the primary (auctions) and secondary markets (ICE exchange and bilateral contracts).

The quotations of CO₂ emission allowances in 2016 differed significantly from the levels quoted year earlier. The average price of emission allowances in 2016 shaped at the level of 5.35 EUR/EUA⁸, which is a significant decrease by EUR 2.33, i.e. 30% in relation to the average price of 2015. The EUAs quotations are sensitive to two types of factors – the ones that arise from the relationship between the supply and the demand on the unit and the political factors. In 2016, factors of a fundamental nature were favourable to rather decreases of quotations of the units allowing to emit CO₂. The existing oversupply in relation to the needs arising from the need to cover the emitted CO₂ amounts with the units is favourable to periodic decreases in prices. In addition, especially in the first quarter of 2016, the correlation of the EUA market with the prices of energy resources, which were getting cheaper in that period, was visible. Another factor limiting the demand for EUAs in 2016 was the amount of energy produced from res growing faster in relation to the forecasts of the past (especially fast in some countries of Western Europe). Political factors affected the prices of EUAs in 2016 in two ways. Such events as the outcome of the referendum in the United Kingdom meaning that this country leaves the European Union affected the dynamic decrease in the EUAs prices in the mid-year especially strongly. The United Kingdom's leaving the European Union sew doubts regarding the nature of the participation of this country in the ETS system and the shape of this system in the future in the light of significant changes that affect the EU. In turn, a factor catalysing the periodic increases in the EUAs prices in 2016 was constant efforts of some countries included in the ETS aimed at reforming this system that, in its initiators' concept, would lead to a significant increase in the EUAs prices by limiting the quantity of units available on the market in the future periods. The EUAs prices recorded the highest levels, a little above EUR 8, at the very beginning of 2016. In the subsequent months, the EUAs prices were subject to consecutive increase and decrease waves. The price minimum was reported at the beginning of September at the level just below EUR 4.

Chart 8: Price of the futures contract for the supply of EUA



Source: own development based on the 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.

Regardless of the factors described above, meteorological conditions become more and more important for the level of the Company's production. So far, the Company has not been significantly subject to seasonality of demand. Due to the low cost of the units' operation was executed continuously (at base) for almost entire year. Currently, given the increasing share of RES in the segment of energy producers, primarily wind sources, at estimating the volume of the Company's generation, weather conditions become more and more important, with a particular focus on wind conditions. Statistically, the first and fourth quarters are periods with the best wind conditions. It should be taken into account that on periods when wind conditions are very good and the wind turbines' generation is high, the demand for Company's production may be subject to periodic deductions.

⁸ The arithmetic mean of the day-end levels for quotations of EUAs on ICE.

Investment expenses

The activities in the lignite extraction and energy production sector requires substantial investment expenses. The Company's generation assets require periodical renovations and on-going modernisation, both due to the increasing strictness of requirements in the scope of environmental protection as well as the need for improvement of electricity production effectiveness. The level of investment expenses had major impact, and according to expectations will still have major impact, on the results of the operating activities, level of debt and cash flows. Delays in execution, changes of the investment programme, and excess in the budget can have severe impact on the investment expenses incurred in the future, as well as on the results, financial position, and perspectives of development. Moreover, the part of the Company's planned investment projects reported to the National Investment Plan involves the allocation of free units allowing for CO₂ emission. However, in the case of failure to implement these investments, the ability to use the free allocation is prevented as well. The topic of the Company's investment plans and the execution of current tasks is more widely discussed in points 3.3 and 7 of this statement.

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:

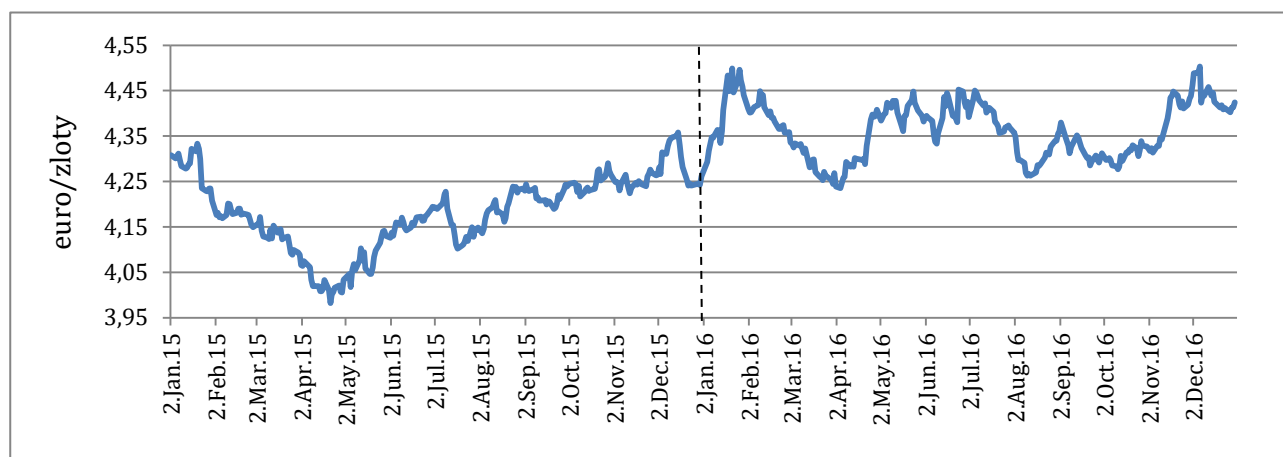
- ZE PAK SA use debt financing based on a variable interest rate;
- transactions related to the purchase of EUAs are settled in EUR.

In 2016, the Company did not apply the instruments to mitigate risks arising from changes in exchange rates, with the exception of secure of the EUR exchange rate for part of the flows related to the purchase of units allowing for CO₂ emission. To secure the exchange rate, the forward transactions with settlement date in December 2016 and January 2017 were applied. Management Board is constantly monitoring the financial position and market situation and can make the decision to use financial instruments limiting the exchange rate risk, if needed. According to the Risk Management Principles adopted in the ZE PAK SA Group, possible transactions will have a form of security and will be adapted to the secured item in terms of volume and maturity date. The decision on the choice of the security instrument will also include the following: price, market liquidity, product simplicity, easiness of quotation and accounting as well as flexibility.

Exposure of the Company to risk caused by the changes of interest rates mainly concerns long-term financial liabilities related to the financing of investments in ZE PAK SA. The Company uses financial liabilities, mostly variable rate credits and loans. The Company did not use any instrument hedging interest rates. However similar as in case of exchange rate, according to Risk Management Rules in ZE PAK Group, such instruments might be used in future only to protect hedge interest rate and should be matched with hedged position.

The EUR/PLN exchange rate recorded higher values than in the previous year over the almost entire 2016. The consecutive waves weakening and strengthening of zloty caused that the exchange rate fluctuated within the range, closing to 4.25 and 4.5 several times. It recorded its minimum at the level of 4.2355 at the beginning of April and the maximum at the level of 4.5035 at the beginning of December.

Chart 9: euro/zloty exchange rate



Source: own development based on NBP average exchange rate tables

5. DESCRIPTION OF THE FINANCIAL AND ECONOMIC SITUATION

5.1. Principles of development of the financial statement

Zespół Elektrowni Państw – Adamów – Konin SA [Państw-Adamów-Konin Power Plant Group Joint-stock Company] develops the standalone financial statement on the basis of the Accounting Act of 29 September 1994.

The financial statement was developed with the assumption of continuing business activity by the Company in the foreseeable future. On the date of development of the financial statement, there are no reported circumstances indicating any risk to the continuation of the Company's activity.

The accounting principles (policy) used in the development of the financial statement are presented in point II.6 of the Introduction to the Financial Statement of ZE PAK SA for the year concluded on 31 December 2016.

5.2. Specification of the basic economic and financial values

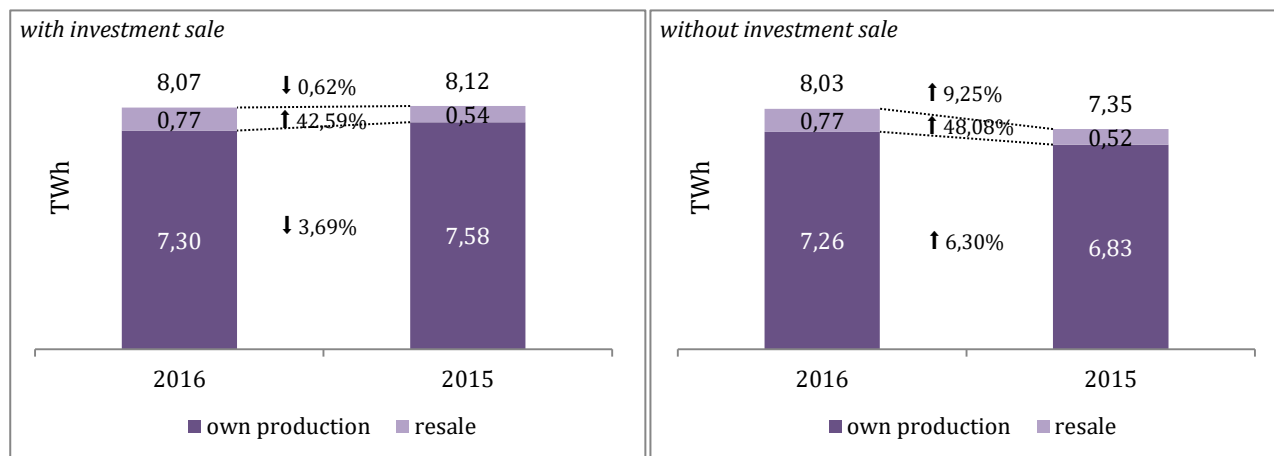
Income statement

In 2016, net revenue from products, goods and materials sales in 2016 amounted to PLN 1 622 180 thousand and it increased by PLN 83 267 thousand in relation to 2015, i.e. by 5.41%. The revenue increased mainly because of the electricity sales revenue higher by PLN 85 067 thousand, i.e. by 6.43% due to the increase in the energy sales volume by 0.68 TWh, i.e. by 9.24%, despite a lower average price of electricity sales by 4.52 PLN/MWh. The lower property rights sales revenue from certificates of origin was the result of a decline in market prices of green certificates and the sales of green certificates inventory at a price that was lower at the time of their sale than the price, at which they were valued, which impacted the reduction of the achieved sales revenue. The Company achieved service sale revenues that was higher by PLN 32 571 thousand, i.e. by 27.42%. The main reason for the increase in revenue was higher revenue related to services provided for Elektrowni Państw II sp. z o.o., including among others the major overhauls of the unit with the power of 464 MW.

Table 4: Specification of consolidated sales revenues

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2015</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Revenues from the sales of products	1 490 122	1 441 309	48 813	3.39
Products sales revenues, including:	1 338 772	1 322 529	16 243	1.23
– Electricity	1 277 384	1 228 074	49 310	4.02
– Property rights on energy certificates of origin	812	33 547	(32 735)	(97.58)
– Heat	60 575	60 907	(332)	(0.55)
Service sales revenues	151 351	118 780	32 571	27.42
Goods and materials sales revenues	132 058	97 604	34 454	35.30
Goods sales revenues (electricity)	129 630	93 873	35 757	38.09
Material sales revenues	2 428	3 731	(1 303)	(34.92)
Sales revenues, including:	1 622 180	1 538 913	83 267	5.41
Electricity (products and goods)	1 407 014	1 321 947	85 067	6.43

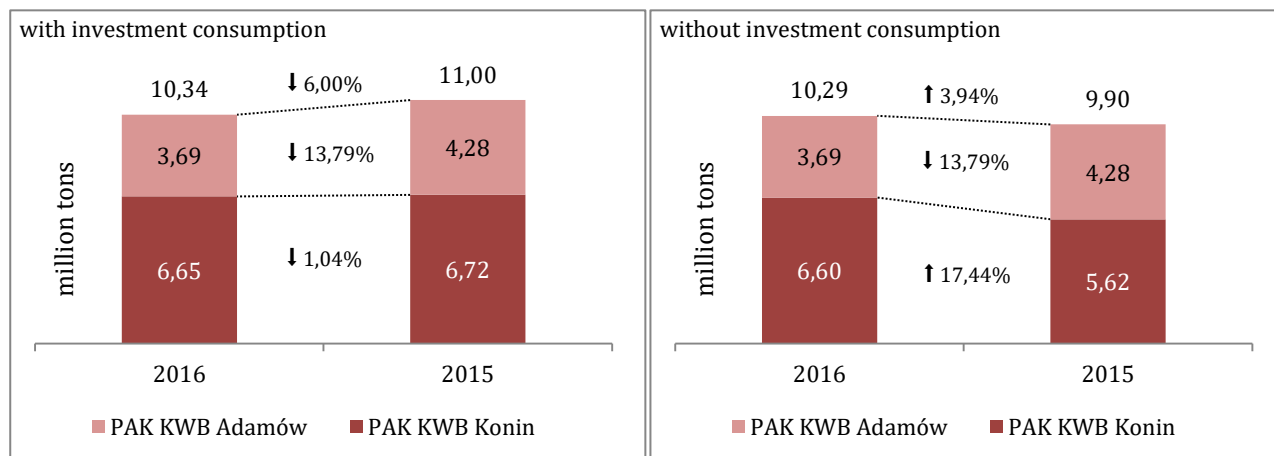
Chart 10: Sale of electricity*



* On the chart on the right, the sales of electricity from units 1 and 2 in the Pątnów I power plant in the period of the investment, from which the achieved revenues decreased the value of the incurred investment expenses, were not shown.

Source: internal data

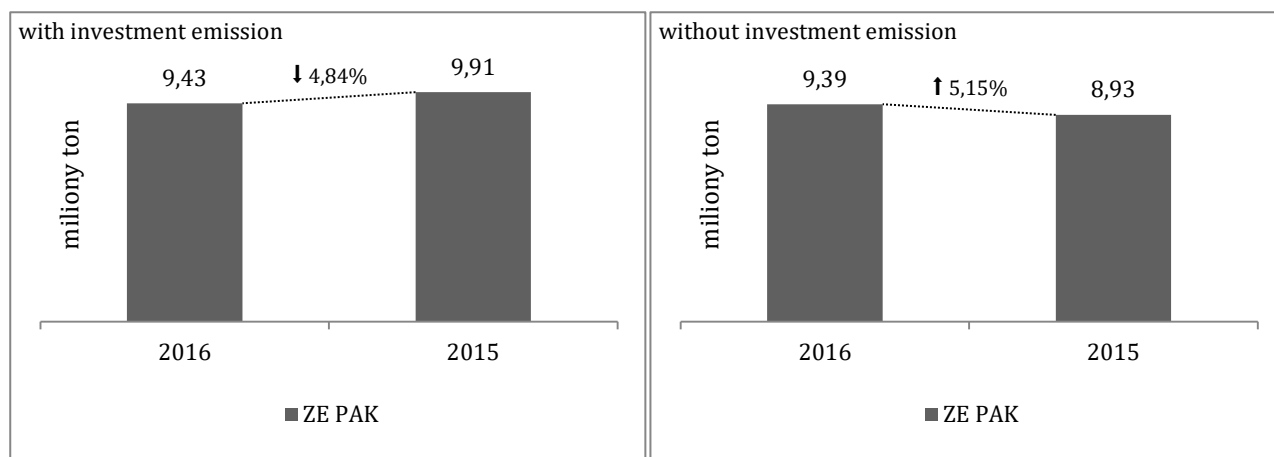
Chart 11: Lignite consumption*



* On the chart on the right, the coal consumption for units 1 and 2 in the Pątnów I power plant in the period of the investment, whose costs increased the value of the incurred investment expenses, were not shown.

Source: internal data

Chart 12: Emission of CO₂*



* On the chart on the right, the CO₂ emission from units 1 and 2 in the Pątnów I power plant in the period of the investment, whose costs increased the value of the incurred investment expenses, were not shown.

Source: internal data

The cost of production of the sold products amounted to PLN 1 389 927 thousand in 2016 and in relation to 2015, it is lower by PLN 76 795 thousand, i.e. by 5.24%. The decrease in cost was mainly the result of lower depreciation, lower fuel costs for electricity production, and lower costs of employee benefits.

The value of goods and materials sold in 2016 amounted to PLN 119 595 thousand and was higher in comparison with the previous year by PLN 30 719 thousand, i.e. by 34.56%, mainly as a result of a lower volume of purchased electricity for re-sale by 0.25 TWh.

Selling costs amounted to PLN 3 100 thousand in 2016 and were lower by PLN 452 thousand, i.e. by 12.73%.

Overheads in 2016 amounted to PLN 30 194 thousand and were lower than these incurred last year by PLN 5 669 thousand, i.e. by 15.81% because of the lower employee benefits costs.

A detailed analytical presentation of costs by type is included in Table 6

Table 5: Selected items from the income statement

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2015</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Net products, goods and materials sales revenues, including:	1 622 180	1 538 913	83 267	5.41
– Net revenues of the products sales	1 490 122	1 441 309	48 813	3.39
– Net revenues resulting from the goods and materials sales	132 058	97 604	34 454	35.30
Costs of sold products, goods, and materials, including:	1 509 522	1 555 598	(46 076)	(2.96)
– Cost of manufacturing of the sold products	1 389 927	1 466 722	(76 795)	(5.24)
– Value of sold goods and materials	119 595	88 876	30 719	34.56
Gross profit (loss) on sales	112 658	(16 685)	129 343	-
Selling costs	3 100	3 552	(452)	(12.73)
Overheads	30 194	35 863	(5 669)	(15,81)
Sales profit (loss)	79 364	(56 100)	135 464	-
Other operating revenues	6 993	1 679	5 314	316.50
Other operating costs	12 671	1 519 160	(1 506 489)	(99.17)
Profit (loss) on operating activities	73 686	(1 573 581)	1 647 267	-
Financial revenues	86 676	87 283	(607)	(0.70)
Financial costs	23 057	33 898	(10 841)	(31.98)
Gross profit (loss)	137 305	(1 520 196)	1 657 501	-
Income tax	5 898	(4 346)	10 244	-
Net profit (loss)	131 407	(1 515 850)	1 647 257	-

Other operating revenues amounted to PLN 6 993 thousand in 2016. The higher revenues are primarily the result of the revaluation of the provisions for employee benefits and receiving higher compensations from insurers and the higher value of grants.

Other operating costs amounted to PLN 12 671 thousand in 2016. This value consists of impairment write-downs against green certificates inventory in the amount of PLN 9 845 thousand.

In 2016, the Group generated profit on operating activities in the amount of PLN 73 686 thousand.

Financial revenues in 2016 amounted to PLN 86 676 thousand and were higher than these of the last year by PLN 607 thousand, i.e. by 0.70%. As in the previous year, the largest item were the dividends received from the subsidiaries, which amounted to PLN 78 722 thousand.

Financial costs in 2016 amounted to PLN 23 057 thousand and in relation to the last year, they decreased by PLN 10 841 thousand, i.e. 31.98% despite that in the Company, the interest expenses increased by PLN 15 943 thousand, which was related to the commencement of accounting the cost of the credit for modernisation of the units in the Pałnów I power plant for the burden of the financial result because of the impairment write-downs in the amount of PLN 28 200 thousand for the shares in the subsidiary PAK GÓRNICZWO sp. z o.o.

Table 6: Costs by type

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2015</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Depreciation	36 925	83 263	(46 338)	(55.65)
Use of materials and energy	758 536	780 702	(22 166)	(2.84)
Foreign services	182 900	182 972	(72)	(0.04)
Taxes and charges, including:	323 851	322 541	1 310	0.41
– excise tax	797	743	54	7.27
– CO ₂ emission costs	248 789	247 952	837	0.34
Salaries	92 778	111 674	(18 896)	(16.92)
Social security and other benefits	24 287	26 889	(2 602)	(9.68)
Other costs by type	8 570	11 542	(2 972)	(25.75)
Value of sold goods and materials	119 595	88 876	30 719	34.56
Total costs by type	1 547 442	1 608 459	(61 017)	(3.79)

In 2016, the Company took a gross profit in the amount of PLN 137 305 thousand. At the nett level, the profit amounted to PLN 131 407 thousand

Balance sheet

Total balance sheet of the Company amounted to PLN 2 598 206 thousand as of 31 December 2016 and decreased in comparison to the state as of 31 December 2015 by PLN 51 165 thousand, i.e. by 1.93%.

Fixed assets decreased by PLN 35,544 thousand, i.e. by 1.63%. The greatest changes occurred in the following items:

- intangible assets, which increased by net PLN 78 274 thousand, due to the activities related to the purchase of CO₂ emission allowances;
- tangible fixed assets, which increased by net PLN 21 376 thousand, as a result of a higher level of depreciation write-downs related to the executed investment expenses (during the year, as a result of completing the investment in the modernisation of the units in the Pańków I power plant, the fixed assets under construction item was decreased and the fixed assets was increased);
- long-term investments which decreased by PLN 17 478 thousand, i.e. by 1.45%, primarily as a result of the repayment of loans granted to the subsidiaries).

Current assets decreased by PLN 86 709 thousand, i.e. by 18.63%. The largest decrease occurred in the green certificate inventory item, which decreased by PLN 50 857 thousand as a result of the sale of the part of the certificates in 2016, as well as a lower valuation of the unsold certificates (the price applied to the valuation at the end of 2016 amounted to 37.76 PLN/MWh in comparison to 116.84 PLN/MWh in 2015).

The equities as of 31 December 2016 amounted to PLN 1 491 837 thousand. Compared to the completion of the previous year, they increased by PLN 131 406 thousand, i.e. by 9.66%, being the result of the generated net profit.

Level of provisions at the end of 2016 amounted to PLN 347 396 thousand and was lower in comparison to the state of the previous year by PLN 27 374 thousand. The largest change occurred in the “other provisions” item and involved a decrease in the CO₂ emission allowances provision by PLN 31 946 thousand.

The total liabilities at the end of the 2016 in relation to the previous year decreased by PLN 148 448 thousand, i.e. by 16.88%, including the long-term liabilities that decreased by PLN 192 208 thousand and the short-term liabilities that increased by PLN 43 760 thousand. The largest decrease in liabilities in the amount of PLN 113 146 thousand occurred in the “credits and loans” item and was mainly associated with the service of the credit for financing the modernisation of the units in the Pańków I Power Plant.

Table 7: Selected items from assets

	<i>zloty thousand</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>31 December 2015</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Fixed assets	2 219 586	2 184 042	35 544	1.63
Intangible and legal assets	368 132	289 858	78 274	27.00
Tangible fixed assets, including:	662 844	684 220	(21 376)	(3.12)
1. Fixed assets	617 868	392 252	225 616	57.52
2. Fixed assets under construction	41 067	287 639	(246 572)	(85.72)
3. Advances on fixed assets in construction	3 909	4 329	(420)	(9.70)
Long-term receivables	0	0	0	-
Long-term investments	1 187 862	1 205 340	(17 478)	(1.45)
Long-term accruals and prepayments	748	4 624	(3 876)	(83.82)
Current assets	378 620	465 329	(86 709)	(18.63)
Inventory, including:	53 915	104 156	(50 241)	(48.24)
1. Materials	39 602	38 536	1 066	2.77
2. The goods	13 959	64 816	(50 857)	(78.46)
3. Advances for deliveries	354	804	(450)	(55.97)
Short-term receivables	137 373	153 828	(16 455)	(10.70)
Short-term investments	186 022	206 163	(20 141)	(9.77)
1. Short-term financial assets, including:	186 022	206 163	(20 141)	(9.77)
– in the affiliates	16 125	23 174	(7 049)	(30.42)
– in other entities	296	0	296	-
– cash means and other pecuniary assets	169 601	182 989	(13 388)	(7.32)
2. Other short-term investments	0	0	0	-
Short-term accruals and prepayments	1 310	1 182	128	10.83
Unpaid share capital (basic)	0	0	0	-
Own shares	0	0	0	-
Total assets	2 598 206	2 649 371	(51 165)	(1.93)

Table 8: Selected items from liabilities

	<i>zloty thousand</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>31 December 2015</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Equity	1 491 837	1 360 431	131 406	9.66
Stated capital	101 647	101 647	0	-
Supplementary capital	1 028 647	2 542 060	(1 513 413)	(59.53)
Revaluation capital	227 498	227 531	(33)	(0.01)
Other reserve capital	3 472	5 877	(2 405)	(40.92)
Profit (loss) from previous years	(834)	(834)	0	-
Net profit (loss)	131 407	(1 515 850)	1 647 257	-
Net write-offs during the financial year (negative value)	0	0	0	-
Liabilities and provisions for liabilities	1 106 369	1 288 940	(182 571)	(14.16)
Provisions for liabilities	347 396	374 770	(27 374)	(7.30)
1. Deferred income tax provision	68 806	62 920	5 886	9.35
2. Provisions for pensions and similar benefits.	9 922	11 598	(1 676)	(14.45)
3. Other reserves	268 668	300 252	(31 584)	(10.52)
Long-term liabilities	344 005	536 213	(192 208)	(35.85)
1. Towards related entities	254	254	0	-
2. Towards other entities of which entity has capital engagement	0	0	0	-
3. Towards other entities	343 751	535 959	(192 208)	(35.86)
– credits and loans	343 295	535 127	(191 832)	(35.85)
– other	0	241	(241)	(100.00)
Short-term liabilities	387 209	343 449	43 760	12.74
1. Towards related entities	32 405	85 016	(52 611)	(61.88)
2. Towards other entities of which entity has capital engagement	0	0	0	-
3. Towards other entities, including:	350 650	253 698	96 952	38.22
– credits and loans	158 629	79 943	78 686	98.43
– trade liabilities:	53 247	15 635	37 612	240.56
– advance payments received for deliveries and services	50	124	(74)	(59.68)
– due to taxes. customs duty. social security and other benefits	68 521	83 113	(14 592)	(17.56)
– remunerations	4 314	4 067	247	6.07
– other	65 750	70 681	(4 931)	(6.98)
4. Special funds	4 154	4 735	(581)	(12.27)
Accruals and prepayments	27 759	34 508	(6 749)	(19.56)
Total liabilities	2 598 206	2 649 371	(51 165)	(1.93)

Cashflow statement

In 2016, the Company made a positive cash flow balance on operating activities in the amount of PLN 95 238 thousand despite higher expenses related to the purchase of CO₂ emission allowances by PLN 151 295 thousand.

The cash operation balance on investment activities was positive and amounted to PLN 23 102 thousand. Its height mainly consisted of expenses on investments in fixed assets in the amount of PLN 85 608 thousand, which primarily consisted of expenses on the modernisation of the units in the Pańków I Power Plant, as well as inflows from dividends in the amount of PLN 78 778 thousand and the inflows from the loans and debentures in the amount of PLN 24 644 thousand.

The cash operation balance on financial activities was negative and amounted to PLN 132 824 thousand. In 2016, the cash flow from financial activities was almost entirely related to the service of financial debt.

Cash decreased by PLN 13 473 thousand throughout 2016 and amounted to PLN 169 516 thousand at the end of the year.

Table 9: Selected items of the cash flow statement

	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2016</i>	<i>zloty thousand</i> <i>12 months period</i> <i>ended</i> <i>31 December 2015</i>	<i>zloty thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Cash flows on operating activities				
Gross profit (loss)	131 407	(1 515 850)	1 647 257	-
Total adjustments	(35 158)	1 626 618	(1 661 776)	-
1. Depreciation	36 925	83 263	(46 338)	(55,65)
2. Profits (losses) on foreign exchange	(2 936)	183	(3 119)	-
3. Interest and shares in profits (dividends)	(61 139)	(83 276)	22 137	(26,58)
4. Profit (loss) on investment activities	(263)	1 531 702	(1 531 965)	-
5. Change in provisions	254 761	252 684	2 077	0,82
6. Change in inventory	50 241	76 363	(26 122)	(34,21)
7. Change in receivables	14 861	(2 940)	17 801	-
8. Change in short-term liabilities, with the	35 720	(24 098)	59 818	-
9. Change in the status of interim settlements	(2 682)	2 088	(4 770)	-
10. Other adjustments	(360 646)	(209 351)	(151 295)	72,27
Net cash flow from operating activities	96 249	110 768	(14 519)	(13,11)
Cash flows on investment activities				
Income	108 710	102 562	6 148	5,99
1. Disposal of intangible and legal assets as well as tangible assets	1 613	180	1 433	796,11
2. From financial assets, including:	107 097	102 382	4 715	4,61
– in the affiliates	107 041	102 332	4 709	4,60
– in other entities	56	50	6	12,00
– dividends and shares in profits	56	50	6	12,00
– interest	0	0	0	-
Expenses	85 608	388 751	(303 143)	(77,98)
1. Acquisition of intangible and legal assets as well as tangible assets	85 608	356 342	(270 734)	(75,98)
2. For own financial assets, including:	0	32 409	(32 409)	(100,00)
– in the affiliates	0	32 409	(32 409)	(100,00)
Net cash flow from investment activities	23 102	(286 189)	309 291	-
Cash flows on financial activities				
Income	0	312 000	(312 000)	(100,00)

1. Credits and loans	0	312 000	(312 000)	(100,00)
Expenses	132 824	126 829	5 995	4,73
1. Dividends paid and other payments to shareholders	0	60 988	(60 988)	(100,00)
2. Repayment of credits and loans	111 877	48 319	63 558	131,54
3. Payments of financial lease agreement liabilities	130	109	21	19,27
4. Interest	20 757	17 148	3 609	21,05
5. Other financial expenses	60	265	(205)	(77,36)
Net cash flow from investment activities	(132 824)	185 171	(317 995)	-
Total cash flow	(13 473)	9 750	(23 223)	-
Cash flow change in the balance sheet, including:	(13 388)	9 207	(22 595)	-
cash flow change related to foreign exchange differences	85	(543)	628	-
Cash opening balance	182 989	173 239	9 750	5,63
Closing balance of cash, including:	169 516	182 989	(13 473)	(7,36)
restricted cash	4 524	4 825	(301)	(6,24)

Financial indexes

Making the net profit for 2016 in the amount of PLN 131 407 thousand, compared to the loss for the past year in the amount of PLN 1 515 850 thousand, caused that all the profitability indexes became positive.

The overall debt index illustrating the ratio of liabilities to total assets amounted to 0.43 at the end of 2016 and was slightly lower than at the end of 2015. The reduction of the index results from the debt level of the Company. The index value indicates that liabilities comprise 43% of the Company's assets.

The current liquidity index, which informs about the degree of current liability coverage with current assets, was equal to 0.98 at the end of 2016. The purchases of the CO₂ emission allowances for 2017 significantly influenced the deterioration of the index.

Table 10: Indexes

		2016	2015	Change	% Dynamics
ROE	%	8,81	(111,42)	120,23	-
ROA	%	5,06	(57,22)	62,28	-
Net sales profitability	%	8,10	(98,50)	106,60	-
General debt index	<i>x times</i>	0,43	0,49	(0,06)	(12,24)
Current liquidity index	<i>x times</i>	0,98	1,35	(0,37)	(27,41)

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

The financial results of the Company, as an entity focused on activities in the field of electricity generation, selling its product on the free wholesale electricity market, including the Polish Power Exchange, are fully subject to and depend on the behaviours of all participants of this market. These, in turn, depend largely on the proposed or newly introduced legislative changes influencing the domestic electricity market. The price of electricity in the wholesale market is created by all the entities participating in the market trade and a single participant, even the one with a relatively big share in the market, is not able to affect its level on his or her own.

From the electricity producer's point of view, evaluating the environment in terms of both facts and regulations, some particularly important phenomena in the last year that may also affect the Company's results in the future, should be taken into account:

By judging from the producer's point of view, it is important to take into account some particularly important phenomena in the last year:

- continuing increase of power in National Power System (KSE) in the segment of wind turbines,
- Poland's participation in the interconnection projects, aimed at the construction of the common European market in the Price Coupling of Regions model,
- intensified works on the project on the rules of the "power market" functioning
- entry into force of Law on renewable energy sources;
- intensification of works on adjusting the wholesale electricity market to MIFID2 directive.

The Company generates most of its revenues from the production and sales of electricity, therefore, the price at which it sells electricity is very important for the results of its activities. By analysing the current market trends in the context of the level of electricity prices on wholesale energy markets, it is important to look at, above all, prices quoted on the Polish Power Exchange, which, as the most transparent, are the basis of establishing price conditions in the bilateral agreements concluded on a bilateral bidding market (OTC market). The growing number of periods with increased volatility of the price levels of electricity is characteristic for 2016. The factors significantly influencing the level of stock prices on the SPOT market remained the same, the most important of which are: wind generation volume, condition of the reserves in the National Power System (KSE), as well as industrial capacity volume available for the cross-border exchange, and weather conditions. In the previous year, June occurred to be the most expensive in the SPOT market, and its combination of the above mentioned factors, which include low reserves in the National Power System, caused by the repair campaign of units and a number of unplanned shut downs of generation units, and also weather conditions characterised by weak winds and high temperatures, caused that the weighted average price of BASE product in the Day Ahead Market of the Polish Power Exchange in June was 222.84 zloty /MWh, when the last example, where the average price in the Day Ahead Market exceeded 200 zloty /MWh, on a monthly basis, included November 2014⁹.

By analysing the quarterly arithmetic means of the price of BASE_Y-17 agreement, which is the most liquid instrument in the TGE SA futures market last year, it is possible to note that the price is flat and similar to the level of 160 zloty /MWh. From the perspective of transparency, the fact that the trade volume in the TGE SA futures market decreased in 2016 by 38.7% in relation to 2015 is alarming, and as the quotation from the beginning of 2017 shows, the volume size is subject to the further decrease. The causes should be found, on the one hand, in termination of the large part of PPA, and thus, the decrease in performing the obligation of public sale on the stock market, and on the other hand, in the upcoming date of entry into force of the so-called MiFID2 package (3 January 2018), with which, in accordance with the position presented by European and Polish supervisory authorities, the functioning of the Commodity Futures Market (RTT), carried out by Polish Power Exchange in its present form, will not be possible. In accordance to the above fact, TGE SA faces the need of adjusting to the changes resulting from MiFID2 package, by implementing new products and services for the market participants, which from the perspective of participation in the stock exchange by the Company, will certainly generate additional costs of organisational and legal regulations. To sum up, it can be added that the carried-out analyses result in the fact that regardless of the level of exchange quotations, the Company's power plants still remain in the Company of producers participating in covering the demand and balancing the National Power System.

One should take a closer look at the changes in the regulatory environment among the factors influencing the price of property rights. Since 30 April 2014, the amendment to the Energy Law, prolonging the support system for the energy production in peak load co-generation systems (simultaneously generating electricity and heat) until the end of 2018 has been in force. There are no projects in a continuation of the co-generation system support after 2018, and the Company does not have knowledge on the works of Ministry of Energy on possible extension of the support system, however, it is obvious that the works on the continuation of the support system after 2018, which were carried out in the previous year due to the initiative of the Polish Association of Professional Heat and Power Plants and the Chamber of Commerce Polish District Heating, are in progress. Moreover, they assumed a support model consistent with the mechanism already implemented in the act on RES, based on auctions, but not only to the extent of additional bonuses for new heat producers in co-generation. The issue on the obligation of the EU countries to support the co-generation is included in the efficiency directive No. 2012/27/EU of 25 October 2012 containing the chapter on achieving the efficiency improvement through the co-generation support. Currently, "red certificates" obtained by ZE PAK SA., due to the lack

⁹ Polish Power Exchange (TGE) message from the website www.tge.pl.

of a possibility of transferring between settlement periods (“bankability”) are sold on an ongoing basis at the exchange price, which is around the cost of a compensatory fee after the resumption of the system.

Constant changes, which have an effect on the situation of the domestic energy producers, entitled to obtain these certificates of origin, also take place in the broadly understood legal and market environment affecting the prices of the certificates of origin from RES (green certificates). The weighted average price of green certificates in 2016 was at the level of zloty 73.63, and the minimum price recorded in October was zloty 32.57 per certificate. The causes of deep decreases in prices of green certificates remain similar to the previous periods and they are associated with the production oversupply in relation to the demand. On 1 July 2016, the Law on RES, in terms of chapter 4, came into force, introducing new principles and obligations for renewable energy, including, among others, introduction of the auction system divided into two power capacity baskets, and systems with an installed capacity of over 50 MW will be excluded from auction procedures. In case of the biomass unit participation in the auction, and assuming its win, the Company could potentially gain revenues from electricity generation from the biomass unit higher than the currently obtained from the support system of green certificates. In addition, the Law introduces new RES fees to cover the costs arising from the provisions of the new act in the amount of 2.51 zloty /MWh in 2016, calculated per volume of sales to end recipients, and determines the level of fulfilling the obligation of redemption of green certificates in 2016 to 14.35%, at the same time, introducing the obligation of redemption of the so-called blue certificates, derived from the production on agricultural biogas, in the amount of 0.65% in relation to the sale of electricity to end recipients. The act also gave the possibility for the Minister of Economy to progressively introduce the obligation of redemption of green certificates to 20%. However, the obligation of redemption of green certificates at the level of 15.4%, and blue certificates at the level of 0.60% was established for 2017. In addition, on 1 October 2016, the Act on energy efficiency, which remodeled the market of the so-called “white certificates” came into force. The new act introduced three types of efficiency certificates, dividing them into: certificates issued on the basis of this act – valid to the end of 2017, certificates resulting from the investments performed in 2014-2016, which the Company applied for in 2016 (which was allowed by the new act) and certificates issued on the basis of the new act, obtained on the basis of the efficiency investments after 1 October 2016. If the President of ERO provides the Company with white certificates, the issue of which was requested by the Company, then, the excess of certificates, more than those that the Company is obliged to redeem, can be sold in the market in the year of their issue, because white certificates, which will be obtained by the Company, are not “bankable,” therefore, it will not be possible to hold them for the next redemption periods.

The market of CO₂ emission allowances is a market, which is currently the most exposed to fluctuations in the exchange rate due to political conditions. Since September 2015, negotiations on the EU Climate Package after 2020 have been in progress. The form of the discussion on the future of EU ETS system significantly affected the volatility of prices on the carbon market in 2016. The political factors affected EUA prices in 2016 in two ways, i.e. results of the referendum on “Brexit” influenced a dynamic decrease in EUA prices in June, while the efforts of some countries covered by ETS, aimed at the reform of this system, which according to its initiators would lead to a significant increase in EUA prices by reducing their supply in future periods, resulted in periodic increases. The December voting of the European Parliament’s Committee on Environment (ENVI) on the European Commission’s project related to the reform of ETS system after 2020 was particularly important. Subsequently, as soon as the European Parliament and the Council of Europe formalise their positions, a trilateral dialogue on ETS reform will be started between the European Commission, European Parliament, and the Council of Europe. The causes of the downward trends must be sought in the reduction of energy commodity quotations, i.e. crude oil, electricity, or natural gas as well as the increasing correlation of EUA allowances’ prices with the prices on commodity markets, and in the fast-growing share of RES sources in electricity generation in some countries of the Western Europe, reducing the demand for the emission allowances on the side of the conventional producers in these countries. Currently, due to events, such as the United Kingdom’s leave process from the EU and the US election results, it is possible to consider the stabilisation of prices at the current levels in the near future, and in turn, the argument for the increase in prices, can include the energy policy to 2050 “Klimaschutzplan 2050”, adopted by the German government, which is the main driving force of decarbonisation in the European Union.

ZE PAK SA will receive a very small amount of CO₂ free emission allowances for 2016, oscillating within 100 thousand of EUAs, most of which results from the allocation for heat generation. Therefore, practically the entire amount emission allowances needed for the ZE PAK SA must be purchased on the primary (auctions) and secondary markets (ICE exchange and bilateral contracts). Since 2015, the volume of free emission allowances received by the Company has differed significantly from the number of free units received in previous years, and the allocations received by other major energy producers in Poland. Hence, the issue of CO₂ emission allowances is crucial for predicting the financial results of the Company in the coming years.

The factor affecting the Polish power engineering sector is “aging” of the currently functioning generating units. The installed power, age and efficiency of the units will have a fundamental impact on ensuring safe and stable operation of the National Power System, as these units are still the regulatory and controllable provision. When in August 2015,

energy in the Polish power system run out, for the first time in 25 years, the recipients felt the effects of the lack of system solutions. In addition, PSE SA warns that supply restrictions may repeat periodically, and after 2020, it will be possible to feel the serious effects of the lack of power. In order to improve the country's energy security, it was decided to implement the power market solutions. In March 2016, the works on introduction of the power market in Poland were started. On 4 July 2016, the consultation of the prepared power market concept was initiated, and on 30 September, the consultation report and functional solutions of the power market after changes appeared on the websites of the Ministry of Energy. On 16 November 2016, pre-notification of records in the European Commission was performed, and on 2 December 2016, a bill on the power market was directed to inter-ministry and social consultations. On 10 January 2017, the Economic Committee of the Council of Ministers supported the planned change in the market's model from a single commodity market to a dual-commodity market. The measures for introduction of the power market do not change operational conditions of the Company on the energy market until 2020, but they are the basis for strengthening transitional power mechanisms, which are aimed at providing the systemic energetics with the power market. In the context of the power market, it is worth mentioning the so-called "Winter Package" ["Pakiet Zimowy"] published by EC on 30 November 2016. The proposals included in it are intended to create the rules for emergence of the European energy market. The proposals on amendments of existing regulations and European directives were presented there. It should be noted that final provisions offered by the Winter Package, in the perspective after one day of its entry into force (estimated date for implementation is two years) can have a major impact on the form of the activity carried out by the Company, and thus, on its future financial results.

5.4. Unusual events affecting the obtained financial results

There was no unusual events affecting assets, liabilities, equity, financial results or cash flow in 2016.

6. MANAGEMENT OF FINANCIAL ASSETS

6.1. Evaluation of financial assets management

ZE PAK SA 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's Companies execute current monitoring and analyses of the maturity dates of receivables and liabilities as well as adjust the deadlines and bank account balances to the amounts of cash flows. The excess cash is managed by investing in safe instruments of the financial market, which mainly include bank deposits.

6.2. Evaluation of investment plan execution

The 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 SA, 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 of several of them, the Company does not exclude adjustments or significant changes in the executed strategy.

7. SIGNIFICANT FACTORS AND DEVELOPMENT PROSPECTS

Directional activities designated by the Company's strategy

ZE PAK SA conducts systematic analyses of price trends, mechanisms supporting different technologies of electricity and heat generation and mega trends related to the Company's activity area. The aim is to optimise the investment plans for objective matters and work schedules of generation devices. The obtained results allow to develop a model of long-

term functioning in conditions, which indicate negative trends for coal energy covering the risks arising from increasingly aggravating environmental regulations, as well as anticipated changes in the Polish energy mix.

Environmental requirements determined by the EU and Polish law provisions directly contribute to the Company's production capacity. The decision was taken that the technically depleted generation devices, in case of which the analyses did not demonstrate purposefulness of their modernisation, will be gradually withdrawn. The method of operation during the transitional period was closely matched to their capabilities by choosing a dedicated exemption:

- The Adamów Power Plant, included in a derogatory mechanism of a limited exemption in the entire operation period, obtained the right to function with the current emission standards for 17.5 thousand hours counted from 1 January 2016. It means that in case of uninterrupted work in January 2018, the power plant will be inactivated. Currently, the preparatory activities for the process of closing the activity in accordance with the applicable legal regulations and maximum limitation of risks arising from this process, which is unprecedented in the Polish energy sector, are in progress.
- The Konin Power Plant – the coal part – may function until mid-2020, as it was included in other derogatory mechanism, i.e. Transitional National Plan, under provisions of which it will be obligated to remain within the annually allocated pollutant emission ceilings.

The remaining coal assets were partially upgraded and will operate until 2030, subject to adjustment of extraction and protection of relevant coal resources by PAK KWB Konin SA.

The Company is aware of the changes, especially the ones in the legislation and legal area, which take place in its surroundings. The legal regulations aiming at reducing emissions of CO₂ and other gases (SO₂, NO_x), as well as regulations regarding the renewable energy source sector comprise significant challenges for the Group's companies. New environmental regulations, appearing in 2021, resulting from the implementation of BAT conclusions (Best Available Technology), extend the catalogue of limited pollutions. The currently implemented – in collaboration with the renowned design office – analyses will allow to assess the need for undertaking investment measures in order to obtain compliance with the requirements and a scope of possible exemptions.

In the Pańków Power Plant, the achievement of assumed effects of the completed modernisation of units 1 and 2 was confirmed with the use of guarantee tests. The modernisation of units 3 and 4, which includes replacement or modernisation of elements crucial for the operation of units, and operational safety improvement, was analysed in terms of the question if the legal regulations for the power market implementation and the maintenance programme implementation for 200 MW units provide profitability of these investments.

PAK KWB Konin SA and PAK KWB Adamów SA: The continuation of investment expenses for works related to development of the documentation necessary for submission of the application for obtaining licences for extracting minerals from the local perspective deposits. Furthermore, the investment programme assumes the continuation of current expenses for the maintenance of the currently operated open pits of Drzewce, Józwin, Tomisławice, and Adamów.

Key investment projects during the preparatory stage in 2016-2019:

- In the Konin Power Plant: The construction of a gas and steam unit with a power of approx. 120 MWe and approx. 90 MWt, as well as an additional gas-fired back-up peak load boiler with a power of approx. 40 MWt, dedicated to the supply of heat for the city of Konin. In the past year, the promise of an amendment to the license, including the above-mentioned unit with the term until the end of the first half of 2020, was obtained from the Energy Regulatory Office. The document provides confirmation of the "incentive effect" fulfilment – i.e. It was considered that the investment would not be implemented without support for electricity generation within the framework of peak load co-generation. However, such help is implemented as part of separate regulations. However, due to existing unfavourable external conditions, including uncertainty in terms of the support system form for co-generation after 2018, which affects economic efficiency of the project, the Company cancelled the carried-out tender for acquiring a contractor of the project.
- In the previous year, ZE PAK SA terminated the agreement for the heat supply from the coal part, the provisions of which will cease at the end of June 2020. At the same time, ZE PAK SA started studies for the project involving the heat supply for the city of Konin from the biomass unit.
- In the Adamów Power Plant: The construction of the peak load gas-steam unit generating electricity in condensation with a capacity of c. 400 MWe (the unit's size may be subject to optimisation). The strategic investment programme for ZE PAK SA, which takes into consideration the Polish Energy Policy's assumption in effect in 2008, was developed in a period prognosticating advantageous conditions for investments in gas-fired devices. So far, the Polish economy has not created advantageous conditions for the construction of the designed steam and gas unit for the Adamów Power Plant. ZE PAK SA, in close co-operation with the General Design Engineer – Energoprojekt Katowice – using professional tools, has conducted tests and analyses of the volume of energy generation from the new unit in particular years, after commissioning of the coal and gas

units in the country, for which the decisions on construction were already made. The results of these tests confirm that the significant demand for energy from the designed steam and gas unit in the Adamów Power Plant will occur as late as after 2025. In this situation, the decisions on the development of this project were suspended. ZE PAK SA systematically examines the extent to which the designed mechanism of the power market will ensure satisfactory conditions for investors. Currently, the works on the act on Power Market, which makes it possible to reward the manufacturer, determined by auction, for readiness for energy generation to the request of PSE SA, are in progress.

In accordance with the implemented policy and market practice adopted by other companies from the power engineering sector, more investment projects are analysed and prepared than actually implemented ones. In the future, decisions on the implementation of other projects than those mentioned above, provided for in the documents defining the Company's strategy, may be made.

8. SPECIFICATION OF THE SHAREHOLDING STRUCTURE

8.1. Shareholding structure

As of 31 December 2016, the Company's share capital amounted to zloty 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 Company's General Meeting according to the Company's knowledge as of 31 December 2016.

*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 2015 and as of the day of this statement**

<i>Shareholder</i>	<i>shares.</i> <i>Number of shares and corresponding number of votes at the General Meeting</i>	<i>%</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 sp. z o.o.</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 the Company's knowledge on the basis of notifications submitted by the shareholders..*

The structure of the Company's shareholders was presented according to the Company's knowledge on the basis of notifications submitted by the shareholders.

The Company is not aware of any agreements which would result in future changes in the shareholding structure of the current shareholders.

8.2. Acquisition of own shares

The Company did not acquire own shares in 2016.

8.3. Shares of the ZE PAK Capital Group entities belonging to the supervising and managing persons

The below table presents the Company's share holdings (direct and indirect), as well as affiliates' share holdings of management personnel as of 31 December 2015 and as of the date of development of this statement.

Table 12: Company's share holdings as well as affiliates' share holdings by management personnel as of 31 December 2016

<i>Name and surname</i>	<i>ZE PAK SA shares.</i>		<i>Affiliate shares</i>	
	<i>quantity</i>	<i>face value</i>	<i>quantity</i>	<i>face value</i>
Adam Kłapszta	0	0	0	0
Aneta Lato-Żuchowska	0	0	0	0
Zygmunt Artwik	0	0	0	0
Katarzyna Sobierajska	0	0	0	0
Tomasz Zadroga	0	0	0	0

Table 13: Company's share holdings as well as affiliates' share holdings by management personnel as of the day of this statement

<i>Name and surname</i>	<i>ZE PAK SA shares.</i>		<i>Affiliate shares</i>	
	<i>quantity</i>	<i>face value</i>	<i>quantity</i>	<i>face value</i>
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 share holdings (direct and indirect), as well as affiliates' share holdings of supervising personnel as of 31 December 2015 and as of the date of development of this statement.

Table 14: Company's share holdings as well as affiliates' share holdings by supervisory personnel.

<i>Name and surname</i>	<i>ZE PAK SA shares.</i>		<i>Affiliate shares</i>	
	<i>quantity</i>	<i>face value</i>	<i>quantity</i>	<i>face value</i>
Tomasz Szelaĝ	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

9. DECLARATION OF COMPLIANCE WITH THE CORPORATE GOVERNANCE RULES

Declaration of compliance with the corporate governance rules is presented in accordance with § 91 paragraph 5 (4) of the Resolution of the Minister of Finances of 19 February 2009 on the current and periodical information submitted by issuers of stocks as well as conditions for the recognition as equally important of information required by the regulations of the law of a country which is not a Member State.

9.1. Set of corporate governance rules applied

In 2016, the Company is subject to corporate governance rules described in the "Best Practice for WSE Listed Companies 2016" (Best Practice) adopted by resolution of the WSE Supervisory Council of 13 October 2015. Best Practice came into force on 1 January 2016.

The Company's Management Board, within the competencies granted to it by the Articles of Association and the generally binding legal regulations, exercises due care in order to ensure the Company's compliance with the Best Practice to the greatest extent possible. The number and scope of principles, which were not applied in 2015, was at the same level as in previous year. The Company's Management Board makes all exceptional efforts in order for the Company's information policy towards investors, both individual and institutional, comprising the execution of guidelines included in the Best Practice, to be compliant with the expectations. Furthermore, due to reasons beyond the Company's control, not all principles included in the Best Practice are applied.

The Code 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 Best Practice the Company published information about status of application of Best Practice by the Company at the following address:

(http://ri.zepak.com.pl/upload/files/EN_GPW_dobre_praktyki_PAK.pdf)

9.2. Set of rules which Company has not complied with

Presented below are corporate governance rules, which the Company has not complied with in its activities in 2016, together with an explanation of the Company's position for each specific departure.

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, responsibility of the position and work effects.

Recommendation VI.R.2. Best Practice:

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

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

There is no comprehensive, formal remuneration policy in the Company. However link with such factors as short- and long-term goals, long-term interests and results are taken into consideration in establishing remuneration of governing bodies and key managers. The company does not discriminate on whatever ground in process of establishing remuneration on any position.

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

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

The development of the Company's financial statements as well as the Group's consolidated financial statements is executed in an orderly manner, pursuant to the organisational 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 the Company’s Accounting and Reporting Department, who, together with the Principal Accountant, develop 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 May 2015 as amended.

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 to determine 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 authorised employees only in the scope of their responsibilities and activities.

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

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

9.4. Shareholders with significant blocks of shares

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

*Table 15: Shareholders holding, either directly or indirectly, significant blocks of shares in accordance with the Company's knowledge as of 31 December 2015 and as of the day of submission 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 sp. z o.o., Trigon XIX Fundusz Inwestycyjny Zamknięty, Argumenol Investment Company Limited.	26 200 867	51,55%	26 200 867	51,55%
Nationale-Nederlanden Otwarty Fundusz Emerytalny	5 068 410	9,97%	5 068 410	9,97%
Towarzystwo Funduszy Inwestycyjnych PZU SA	3 081 567	6,06%	3 081 567	6,06%
OFE PZU „Złota Jesień”	2 664 378	5,24%	2 664 378	5,24%

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

9.5. Holders of stocks giving special control rights

As of 31 December 2016 and as of the date of development of this statement, the Company has not issued stocks giving special control rights.

9.6. Limitations in the execution of the right of ballot

According to the Company's Articles of Association and other internal documents of the Company as of 31 December 2016 and as of the date of development of this report, there are no limitations regarding the execution of the right of ballot.

9.7. Limitations regarding the transfer of right of ownership to stocks

As of 31 December 2016 and as of the date of development of this statement, the Company does not include any limitations regarding the transfer of right of ownership to Company's stocks.

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

Management Board

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

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

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

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

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

Supervisory Board

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

The composition of the Board should include two members who fulfil the independence criteria projected for an independent Board member within the meaning of the Commission's Recommendation of 15 February 2005 regarding the role of non-executive directors or directors acting as members of supervisory Boards in stock exchange listed

companies and the (supervisory) Board's committee (2005/16/EC) with consideration of Good Practices of the Warsaw Stock Exchange Listed Companies ("Independent Supervisory Board Members"). A candidate for the Independent Supervisory Board Members provides the Company, prior to his/her appointment as a Board member, with a written declaration on the fulfilment of the independence criteria.

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.

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

Management Board

The Company's Board composition was as follows at the beginning of the accounting year of 2016:

- 1) Wojciech Piskorz – the Member of the Supervisory Board delegated to temporarily act as the President of the Board,
- 2) Aneta Lato-Żuchowska – Vice-President of the Board,
- 3) Zygmunt Artwik – Vice-President of the Board,
- 4) Adrian Kaźmierczak – Vice-President of the Board,
- 5) Tomasz Zadroga – Vice-President of the Board.

During the meeting on 11 February 2016, the Company's Supervisory Board adopted a resolution on the appointment of Mr Aleksander Grad to the composition of the Company's Management Board on 18 February 2016 and entrusted him with the function of the President of the Management Board. Since 18 February 2016, the composition of the Management Board has been as follows:

- 1) Aleksander Grad – President of the Board,
- 2) Aneta Lato-Żuchowska – Vice-President of the Board,
- 3) Zygmunt Artwik – Vice-President of the Board,
- 4) Adrian Kaźmierczak – Vice-President of the Board,
- 5) Tomasz Zadroga – Vice-President of the Board.

At the meeting on 8 April 2016, the Company's Supervisory Board adopted a resolution on the appointment of Mr Adam Kłapszta to the composition of the Company's Management Board and entrusted him with the function of the Vice-President of the Management Board. After this change, the Company's Management Board composition was as follows:

- 1) Aleksander Grad – President of the Board,
- 2) Aneta Lato-Żuchowska – Vice-President of the Board,
- 3) Zygmunt Artwik – Vice-President of the Board,
- 4) Adrian Kaźmierczak – Vice-President of the Board,
- 5) Tomasz Zadroga – Vice-President of the Board,
- 6) Adam Kłapszta – Vice-President of the Board.

On 17 June 2016, Mr Aleksander Grad resigned from the position of the President of the Management Board and a member of the Management Board of the Company. In view of the above, the Company's Supervisory Board started the procedure of selecting the new President of the Management Board. Until the completion of this procedure, the Supervisory Board has delegated the directing of the Management Board works to Mr Adam Kłapszta, the Vice President of the Company's Management Board, who has been acted as the President of the Management Board since 17 June 2016.

On 26 October 2016, Mr Adrian Kaźmierczak resigned from the position as the Vice-President of the Company's Management Board. In view of the above, at the meeting held on 26 October 2016, the Company's Supervisory Board

appointed Ms Katarzyna Sobierajska as the Vice-President of the Management Board. Since 26 October 2016, the Company's Management Board has operated in the following composition:

- 1) Adam Kłapszta – Vice-President of the Board, acting President of the Board,
- 2) Aneta Lato-Zuchowska – 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 Company's Management Board was entrusted to Mr Adam Kłapszta. At the same time, during the same meeting of the Supervisory Board, Ms Katarzyna Sobierajska and Mr Tomasz Zadroga submitted resignations from the positions of the Vice-Presidents of the Company's Management Board as of 3 March 2017, the Company's Supervisory Board also appointed Ms Elżbieta Niebisz to the position of the Vice-President of the Management Board. Since 3 March 2017, the Company's Management Board has operated in the following composition:

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

Supervisory Board

The Company's Supervisory Board composition undergone the following changes during the reporting period.

The ZE PAK SA's Supervisory Board composition was as follows at the beginning of the accounting year of 2016:

- 1) Zygmunt Solorz – President,
- 2) Henryk Sobierajski – Vice-President,
- 3) Wojciech Piskorz – Secretary,
- 4) Leszek Wysłocki,
- 5) Lesław Podkański,
- 6) Ludwik Sobolewski,
- 7) Wiesław Walendziak.

On 17 November 2015, the Company's Supervisory Board, in accordance with Article 383 § 1 of the Code of Commercial Companies, delegated Mr Wojciech Piskorz, the Member of the Supervisory Board, to temporarily act as the President of the Company's Management Board for a period not longer than 3 months. Therefore, for the time of the above-mentioned delegation, the rights and duties of Mr Wojciech Piskorz arising from the participation in the Supervisory Board were suspended. The delegation lasted until 17 February 2016.

On 28 June 2016, the Ordinary General Meeting appointed Mr Tomasz Szelaż to the composition of the Supervisory Board. The resolution on the appointment became effective upon its adoption. Since that time, the Company's Supervisory Board was held in the composition:

- 1) Zygmunt Solorz – President,
- 2) Henryk Sobierajski – Vice-President,
- 3) Wojciech Piskorz – Secretary,
- 4) Leszek Wysłocki,
- 5) Lesław Podkański,
- 6) Ludwik Sobolewski,
- 7) Wiesław Walendziak,
- 8) Tomasz Szelaż.

On 26 October 2016, the Chairman of the Supervisory Board, Mr Zygmunt Solorz resigned from the membership in the Company's Supervisory Board with immediate effect.

Due to the resignation of Mr Zygmunt Solorz, the Supervisory Board selected Mr Tomasz Szelaż, from its members, to the position of the Chairman of the Supervisory Board.

Since 26 October 2016, the composition of the Supervisory Board has been as follows:

- 1) Tomasz Szelaż – President,
- 2) Henryk Sobierajski – Vice-President,
- 3) Wojciech Piskorz – Secretary,
- 4) Leszek Wysłocki,

- 5) Lesław Podkański,
- 6) Ludwik Sobolewski,
- 7) Wiesław Walendziak.

The Supervisory Board members that fulfil the independence criteria include Mr Ludwik Sobolewski and Mr Lesław Podkański.

In the execution of their code and statutory obligations, in 2016, the Supervisory Board held eight sessions adopting a total of 52 resolutions. The Supervisory Board executed its statutory obligation of holding a session 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) approval of the Company's budget for 2016 and control of its implementation, in particular, the conditions in the field of energy generation and the results achieved by the Company from the sale of own and foreign electricity, including the one generated from renewable energy sources,
- 4) giving an opinion on the applications submitted by the Management Board in regard to cases related to the Company's current activities;
- 5) changes in the composition of the Management Board of ZE PAK SA.;
- 6) design project of a gas-steam unit in the Konin Power Plant.

In the financial year of 2016, the ZE PAK SA. Supervisory Board's Audit Committee held three meetings. During the held meetings, the ZE PAK SA. Supervisory Board's Audit Committee discussed with a statutory auditor, among others, the results of financial statements' audits for 2015 and the review of interim financial statements for 2016. The Audit Committee also dealt with the issue of selection of the entity authorised to audit financial statements prepared for 2016 and issues related to risk management and functioning of an internal audit in the Company.

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

General Meeting

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

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

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

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

The basic competencies of the General Meeting include:

- 1) examination and approval of the Board's report on the Company's activities, as well as the financial statement for the previous accounting year, as well as acknowledgement of the fulfilment of duties by the Company's body members,
- 2) division of profit and loss coverage,
- 3) change in the subject of the Company's activities,
- 4) amendments to the Company's Articles of Association,
- 5) increase or decrease in the share capital,
- 6) authorisation of the Board to acquire own shares for the purpose of redemption,

- 7) appointment and dismissal of Council members,
- 8) establishment of the remuneration of Council members,
- 9) Company merging, division and transformation,
- 10) Company termination and liquidation,
- 11) emission of convertible bonds or bonds with right of priority and subscription warrants,
- 12) sale or lease of the company or its organised part as well as establishment of a limited property right for them,
- 13) establishment and cancellation of the Company's capitals and funds,
- 14) conclusion by the Company of a credit, loan, surety agreement, or a similar agreement with a member of the Company's Board, Supervisory Council, proxy or liquidator, or for any of this personnel,
- 15) conclusion by an affiliate of a credit, loan, surety agreement or a similar agreement with a member of the Company's Board, Supervisory Council, proxy or liquidator, or for any of this personnel,
- 16) any provisions regarding claims the remedy of damage done during the Company's establishment or executing management or supervision, and
- 17) use of the share capital.

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

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

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

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

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

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

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

9.11. Description of the amendments to the Company's Articles of Association

Amendments to the Company's Articles of Association, in accordance with the Code of Commercial Companies and provisions of the Company's Articles of Association, 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 articles of association, or to introduce editorial changes specified in the General Meeting's resolution. Amendments to the Articles of Association are binding since the moment of entry into the register of entrepreneurs.

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

In the Zespół Elektrowni Pańńów-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. Moreover, the key managers were also entitled to the annual award (bonus), the amount of which is divided into a discretionary part, whose granting depends on the Management Board's assessment of the degree of individual tasks' implementation, and a coefficient part depending on the achievement of a specific economic coefficient. Since 1 January 2016, the bonus has been replaced with 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 16: Information on the value of remuneration paid by the Company as well as the Company's subsidiaries to all acting Board members in 2016

<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>
Zygmunt Artwik	689,0	2,7	691,7	2,7
Aleksander Grad	686,4	0,6	687,0	424,9
Adrian Kaźmierczak	512,6	1,8	514,4	25,9
Adam Kłapszta	155,2	0,7	155,9	0,7
Aneta Lato-Żuchowska	321,0	2,8	323,8	2,4
Wojciech Piskorz	0,0	1,6	1,6	1,6
Katarzyna Sobierajska	0,0	260,0	260,0	20,0
Tomasz Zadroga	540,0	3,8	543,8	3,8
total	2 904,2	274,0	3 178,2	482,0

* *The variable remuneration components included: awards and bonuses, severance pays for dismissal of the Board, equivalents for holiday, a post-retirement benefit and remunerations for participation in meetings of the supervisory boards*

Table 17: Information on the value of non-cash benefits paid by the Company as well as the Company's subsidiaries to all acting Board members in 2016

<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>
Zygmunt Artwik	1,2	0,0	1,2
Aleksander Grad	0,4	0,0	0,4
Adrian Kaźmierczak	23,2	0,0	23,2
Adam Kłapszta	0,6	0,0	0,6
Aneta Lato-Żuchowska	0,6	0,0	0,6
Wojciech Piskorz	0,0	0,0	0,0
Katarzyna Sobierajska	0,3	0,6	0,9
Tomasz Zadroga	1,1	0,0	1,1
total	27,4	0,6	28,0

The total amount of remuneration, understood as the value of remuneration, prizes and benefits received in cash, in kind or in any other form, paid by the Company and the Company's subsidiaries to the Management Board members in 2016 amounted to zloty 3,206.2 thousand. The given amount must be treated as the gross value of remunerations paid or to be paid in the period from 1 January to 31 December 2016.

The members of the ZE PAK SA. Supervisory Board are remunerated on the basis of the Resolution No. 4 of the Extraordinary General Meeting of 21 February 2013, which fixed the monthly salary for the Chairperson of the Supervisory Board in the amount of zloty 15 thousand, and for other members in the amount of zloty 10 thousand.

Table 18: Information on the value of paid remuneration as well as the value of non-cash benefits paid by the Company as well as the Company's subsidiaries to all acting Supervisory Board members in 2016

<i>Name and surname of Supervisory Board member</i>	<i>zloty thousand</i> <i>Value of (gross) remuneration paid by the Company and the Company's subsidiaries</i>	<i>zloty thousand</i> <i>Total estimated value of non-cash benefits granted by the Company and the Company's subsidiaries</i>	<i>zloty thousand</i> <i>In total:</i>
Zygmunt Solorz	162,9	0,0	162,9
Henryk Sobierajski	120,0	0,0	120,0
Wojciech Piskorz*	198,8	0,0	198,8
Leszek Wysocki	120,0	0,0	120,0
Lesław Podkański	120,0	0,0	120,0
Wiesław Walendziak	120,0	0,0	120,0
Ludwik Sobolewski	120,0	0,0	120,0
Tomasz Szeląg	57,1	0,0	57,1
total	1 018,8	0,0	1 018,8

* Together with remuneration for temporary secondment to act in the Company's Management Board.

The total amount of remuneration, understood as the value of remuneration, prizes and benefits received in cash, in kind or in any other form, paid by the Company and the Company's subsidiaries to the Supervisory Board in 2016 amounted to zloty 1,018.8 thousand. The given amount must be treated as the gross value of remunerations paid or to be paid in the period from 1 January to 31 December 2016.

10. GROUP'S SOCIAL RESPONSIBILITY

10.1. Involvement in environmental issues

Electricity production from lignite is inevitably related to interference in the natural environment. On the other hand, one of the main goals of the ZE PAK SA is the minimisation or prevention, if possible, of negative effects on the environment. The activities conducted by the Company affect the natural environment, especially by the emission of contaminants into the air, production and processing of wastes, utilisation of waters, and introduction of sewage wastes into waters or the soil. This impact is regulated by the current regulations on environmental protection. In relation to the conducted activities, the ZE PAK SA has a series of environmental approvals, including integrated approvals which regulate the operational and environmental aspects of the main and auxiliary systems. Furthermore, the Company has approvals for the utilisation of systems which are not embraced by the integrated approvals, including approvals subject to the Water Act Law and approvals for the production and processing of wastes. The Company fulfils the obligations in the scope of reporting to applicable offices, as well as make timely charges relating to the economical use of the environment.

Air protection

In 2016, general annual and monthly emission values of major pollutions into the air: SO₂, NO_x and dust from fuel combustion systems in ZE PAK SA did not exceed the applicable levels specified in the IPPC Permits, with the exception of the average monthly dust concentrations in the Adamów Power Plant. Excesses of the standard of dust emission in the Adamów Power Plant were caused by the combustion of poor quality lignite with the higher ash and sand content. Electrostatic precipitators installed in the Adamów Power Plant, in accordance with the assumptions, should dispose ashes from fumes from combustion of the lignite with the ash content with sand at a certain level. PAK Kopalnia Węgla Brunatnego Adamów SA is in the last stage of operation. The Adamów Power Plant does not have the possibility of changing a supplier of coal in quantities that ensure its safe and stable operation in the national power system, and providing the heat supply to the city. Due to limitations in 2016 related to the supply of low-sulphur coal by PAK Kopalnia Węgla Brunatnego Adamów SA to the Adamów Power Plant, the standard of the emission of carbon dioxide was increased in the number of hours compliant with the environmental law.

In 2016, the 8-year operation period of the Pątnów II Power Plant, after which the first major overhauls of the system devices were started, ended.

Systems for continuous monitoring of dust and gas pollutions' emissions are installed on flue stacks of all fuel combustion systems in the Group. On the basis of the annual settlement of meeting emission standards, it should be stated that:

- in the Pątnów I Power Plant – there were no excesses of concentration limits of SO₂, NO_x and dust (at the operation of two flue gas desulphurisation systems),
- in the Adamów Power Plant – excesses of permissible values of 48-hour dust concentrations (151 times) and average monthly concentrations. The projected fine is the amount of zloty 1.4 million,
- in the Konin Power Plant: there were no excesses of concentration limits of SO₂, NO_x and dust in the boiler part and the boiler combusting biomass,

The Company's power plants pass their emission reports for 2016 of four fuel combustion systems on time to the National Centre of Emission Balancing and Management within meeting the reporting obligations. While pollutant release and transfer registers (PRTR) from all the Companies's power plants are submitted to the Chief Inspectorate of Environmental Protection. Within the Central Statistical Office's reporting, on the CSO's reporting portal, reports for 2016 for particular power plants were generated. Schedules of charges for 2016 submitted to the Marshal Office of the Wielkopolska Province also include a list of additional pollutions emitted from the systems' flue stacks fixed installation as a result of specialised tests that were undertaken in 2010-2015.

In connection with ZE PAK SA joining the Transitional National Plan (PPK) for 6 boilers of the Pątnów I Power Plant and 4 boilers of the Konin Power Plant in terms of SO₂, NO₂ and dust in the period from 1 January 2016 to the expiry of the settlements within the Transitional National Plan, but not later than until 30 June 2020, the balancing of annually allocated emission ceilings. The amount of the emission of SO₂, NO₂ and dust from resources of the Pątnów I Power Plant and Konin Power Plant for 2016 is settled in accordance with the Transitional National Plan and is within the acceptable amounts.

From 1 January 2016, the Adamów Power Plant for all 5 boilers started the time limit for the source use amounting to 17,500 hours to 31 December 2023 or in a shorter period, if it is used before 31 December 2023. In 2016, the total time of using the source was 8,734 hours.

ZE PAK SA conducts the analytical works, which allow to determine the scope of modernisation works in the power plants upon the entry into force of BAT Conclusions, are in progress. The expected validity period of these requirements is the period after 2020.

The monitoring of the air pollutant immission in the area of the impact of the Companies's power plants is also conducted. It is executed through measurements in two automatic measuring stations in the vicinity of the Pątnów I, Konin and Adamów Power Plants. In 2016, no significant excesses of the tested factors' permissible values were recorded. The comparison of the atmospheric air condition around the Company's power plants and the level of air pollution in the areas monitored by the Provincial Environmental Protection Inspectorate of Wielkopolska's stations do not show any deviations.

Water and waste water management

The Pątnów I and Konin Power Plants use the string of natural glacial lakes connected with canals and pumping stations, as a cooling system. The Adamów Power Plant, due to the lack of natural water reservoirs, is equipped with cooling towers. Konin lakes are a team of water reservoirs which consists of the following lakes: Gosławskie, Pątnowskie, Wąsowsko-Mikorzyńskie, Ślesińskie and Licheńskie. These lakes are an example of many anthropogenic impacts. In addition to the impact of power engineering, the lakes are also subject to the impact of open-pit mining, fishing and tourism. ZE PAK SA conducts constant monitoring of the waters of Konin lakes and on the basis of these studies, where appropriate, undertakes actions preventing the negative impacts of own activities. The monitoring conducted for many years also allows to thoroughly observe changes in the observed environment. Within each of the power plants, there are deep water wells that supply drinking water to the personnel. Until 2014, in the Pątnów I Power Plant, deep underground water was also used for process purposes – the production of demi water. Starting from 2015, demi water has been already produced in a modern demineralisation station, where surface water is a raw material. The performance of the station allows to meet the needs of both the Pątnów II and Pątnów Power Plants. This is of enormous importance taking into account the economical use of groundwater resources. Each of the ZE PAK SA power plants have its own domestic and industrial waste water treatment plant. Treated waste water is discharged to the receivers and their parameters are regularly examined. In 2016, no excesses of permissible parameters of discharged and treated waste water were recorded. Waste process water, which is difficult to treat in the treatment plant, is managed in the internal system of power plants for, among others, the production of fly ash suspension. Then, the

mutual neutralisation takes place without a negative impact on the environment. In the summer, the plant particularly takes care of not exceeding temperatures in the waters of lakes and canals, included in the cooling system.

The legislature, through legal acts and standards specified in them, affects the shape of the company's activity, specifying the permissible concentration and volumes of pollutants and introducing charges for using the environment in accordance with the "polluter pays" principle. By taking the above into account and promoting a high level of environmental awareness, the Company undertakes preventive measures in order to reduce the negative impact on the soil and water environment to a minimum.

Waste

Technological processes (fuel combustion, vent gas treatment and water treatment processes) are the source of generated waste in the ZE PAK SA. Other types of waste – mainly after repair – are produced in small quantities. Firstly, the produced waste is directed to be used in the waste recovery operations to the external recipients or it is used by the Group on its own areas (e.g. for shot peening, reclamation of closed parts of waste landfills). Despite the significant increase in the quantity of sold waste, a part of waste generated in the Group is still disposed on own waste landfills:

- combustion waste landfill, the Gosławice Open Pit with the Linowiec vaporiser,
- northern combustion waste landfill, the Pańków Open Pit,
- combustion and solid waste landfill, the Western Open Pit,
- solid waste landfill, the Pańków Open Pit,

The waste, sold to external recipients, is mainly used in the construction and road engineering. In 2016, the Group sold over 326 thousand tonnes of combustion waste and over 286 thousand tonnes of synthetic gypsum (flue gas desulphurisation waste). The combustion and flue gas desulphurisation waste generated in ZE PAK SA meet the requirements of environmental protection and does not endanger human life and health, which was confirmed by tests in the field of physico-chemical, toxicological and ecotoxicological properties executed for the needs of registration of substances in accordance with the REACH regulation's requirements.

On waste landfills operated by ZE PAK SA, in 2016, monitoring of the groundwater, surface and supernatant water quality with the frequency specified in the IPPC permits was conducted. The monitoring was carried out in the network of basic and supplementary monitoring. Within the monitoring of waste landfills, annual assessment of the stability of slopes and the subsidence volume was conducted. Most of the monitored slopes proved to be stable.

In 2016, ZE PAK SA also completed the reclamation of the closed section of the solid waste landfill, the Pańków Open Pit. The total area under reclamation was 11.836 ha. For the part of the area of 9.23 ha, an afforestation reclamation direction was adopted, however, for the area part of 2.606 ha, a special direction (stockyard) was adopted. In 2016, ZE PAK SA also continued the reclamation of the closed section of the combustion waste landfills, the Gosławice Open Pit, and the works were carried out in this landfill with the area of 30 8353.

Noise

Within the obligation of monitoring noise emitted into the environment imposed by the IPPC permits for the fuel combustion systems in the Group's power plants in 2016, measurements of noise from the Adamów Power Plant's and Konin Power Plant's areas. The noise measurements from the Adamów and Pańków II Power Plants' area were not performed. The current measurements are from 2015. The conducted measurements showed no excess of permissible values of the noise level in the environment specified by the IPPC permit, both during the day and night. The monitoring of noise emitted into the environment in the Group's mines is conducted in accordance with applicable regulations. On the basis of the results of these measurements, if necessary, the measures to prevent negative impacts of mining activities are taken.

Inspection, verification of IPPC permits and new legal requirements

In 2016, the Provincial Inspectorate of Environmental Protection in Poznań – Delegation in Konin ("WIOŚP") conducted 5 inspections in the Company's power plants, however, the State County Sanitary Inspectorate in Konin carried out inspections within the framework of control and review monitoring of ground water from the deep-water wells of the Pańków Power Plant and Konin Power Plant. As their result, no fines were imposed on ZE PAK SA. The post-inspection recommendations were implemented.

Last year, the Marshal Office of the Wielkopolska Province conducted an analysis of the IPPC Permit for the fuel combustion system in the Konin and Pańków Power Plants. The analysis of the IPPC permit was conducted in accordance with Article 216 paragraph 1 of the Act of 27 April 2001, Environmental Protection Law, pursuant to which the authority, competent to issue a permit, analyses the issued IPPC permit at least once every five years. As a result of the carried-out analysis of the IPPC permit, there were no post-inspection recommendations, which oblige to the change of the IPPC permit, imposed on ZE PAK SA. Other recommendations resulting from the carried-out verification had a nature of minor comments and focused on the noise emission to the environment.

The European Chemicals Agency (“ECHA”), under the REACH regulation, continued the verification process of the registration documentation concerning generated ash and gypsum submitted by ZE PAK SA in 2016. Within the verification, it was not necessary to conduct additional tests for the registered substances. In 2016, the Company, in accordance with the ECHA recommendation, updated the registration dossier for the registered gypsum.

Environmental management system – ISO 14001

The ZE PAK SA, within its operation, tries to meet the highest standards. This also applies to environmental protection issues. Any tools to support activities in this field are subject to inspection and verification in terms of achieved performance. In the assessment of the Management Board of the Company, standards implemented in over 80% of the systems operated by the Company in accordance with the requirements of the environmental standard ISO 140001 are the one of the most important elements of quality control system

10.2. Employment and employee issues

The below table presents the specification of the average employment rate in 2015-2016.

Table 19: Specification of the average employment rate ZE PAK SA

	2016 <i>full time</i>	2015 <i>Full time</i>	<i>Full time</i>	<i>change full time</i>
Management Board of a parent company	5	4	1	25.0
Administration	40	44	-4	-9.1
Operational	1 258	1 303	-45	-3.4
Total	1 303	1 351	-48	-3.5

Source: internal data

Employment in both compared periods decreased by 48 jobs, i.e. by about 3.5%.

In terms of education, the largest group among employees is people with secondary education.

Table 20: Structure of education of the ZE PAK SA employees (in persons), status at the end of 2016

<i>Education level</i>	<i>Number of employees</i>
University education (bachelor's degree, master's degree, postgraduate studies, PhD, professors)	490
Secondary education (general upper secondary school, technical upper secondary school, post-secondary non-tertiary schools)	496
Vocational education (basic vocational, vocational training)	231
Elementary education (primary school, lower secondary school)	79
Total	1 296

Source: internal data

The largest group among employees are people aged 51-55. Women make up 15.6% of the Company's crew. The structure of the crew is largely determined by the type of activity it carries. The energy sector is an area that requires a lot of hard work.

Table 21: Structure of gender and age of the ZE PAK SA employees (in persons), status at the end of 2016

<i>Age</i>	<i>Female</i>	<i>Male</i>	<i>Total</i>
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below 30 years	13	100	113
31-40 years	40	143	183
41-45 years	19	152	171
46-50 years	23	235	258
51-55 years	56	235	291
56-60 years	42	179	221
above 60 years	9	50	59
Total	202	1 094	1 296

Source: internal data

Due to the specificity of the fields, in which the Company operates, special attention is paid to issues regarding the Occupational Health & Safety. The great importance is attached to employing persons with proper qualifications for the execution of tasks entrusted to them. The Company provides its employees with equipment and machines of proper parameters and attestation, allowing for effective and safe execution of their responsibilities. The number of people injured in 2016 at work was at the same level as in 2015, 4 accidents. Last year, one accident, which belongs to the “fatal and serious” category.

10.3. Involvement in social issues

The ZE PAK SA does not limit its employees in their rights related to the possibility of free association. The number of operating company and inter-company trade union organisations is 7, and at the end of 2016, they affiliated a total of approx. 1 2016 members.

The energy sector poses very high qualification requirements to its employees, in particular, in two fields. The first one is related to the specificity and technology of electricity and heat generation, which are strictly regulated by specialised instructions, which guarantee correctness and safety of production processes. The second is the need to ensure the continuous training of employees, which will make it possible to keep up with the continuous technology development in the sector. There is also specialist training in other fields and the overall development of the qualification level of employees. The training in the ZE PAK SA constitutes one of the methods for influencing the development. It is mainly related to the fact that the employees, who develop, acquire new qualifications, and then, they will use them in in activities, which contributes to measurable effects. They are encouraged to put the obtained knowledge, skills, and greater creativity into effect. Within the framework of the continuous development of competence, the employees are sent to different types of training, among others: mandatory, specialised industry conferences and different kinds of other meetings. In 2016, the training carried out in the ZE PAK SA was mainly related to the energy law, environmental protection, as well as the trainings for engineers, trainings on human resources and finance, and periodic first aid trainings.

The ZE PAK SA perceives its functioning in the environment, taking into account all the standards and expectations relevant to its employees, local community as well as other stakeholder groups. The rules applied in the Company definitely exclude any forms of harassment, forced labour or employment of minors. The great attention is paid to prevention of the occurrence of any possible types of corruption or e.g. unequal treatment of the Company's business trade partners. The internal rules and adopted standards prevent from making activities commonly regarded as unethical in this scope.

Within the framework of shaping appropriate relations with the external environment and taking into account financial and organisational possibilities, the Company tries to support initiatives and projects, which have positive effects for the local community or those with a greater range. In 2016, the Group financially supported one project, i.e. International Children's Song and Dance Festival in Konin [“Międzynarodowy Dziecięcy Festiwal Piosenki i Tańca w Koninie”]. For many years, the Company cooperates in funding the diplomas and prizes for the festival participants

11. OTHER INFORMATION

11.1. Significant court proceedings

In 2016, Zespół Elektrowni Państw – Adamów – Konin SA was not a party in any proceedings pending before a court, a body competent for arbitration proceedings or a public administration body, whose single or total value would exceed 10% of equity of ZE PAK SA, except the ones specified below.

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.

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 (Polish Journal of Laws of 1997; Dz.U. no. 137, item 926, as amended), 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 zloty 626 000 thousand, 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, as well as the Supreme Administrative Court.

In relation to the decisions of the Administrative Courts in the cases of other energy companies in the subject of the overpaid excise tax, ZE PAK SA, in cooperation with a tax advisor, analysed the resolution I GPS 1/11 of the Supreme Administrative Court of 22 June 2011, where the Supreme Administrative Court recognised that the pass-through of the tax load to the price excludes the possibility of refunding the overpayment. The justification of the resolution allows for the assumption of the risk that tax authorities will dismiss any claims regarding the refunding of overpayments indicating that the tax proceeding is not appropriate for such type of claims. In such case, it is possible to seek them under civil law, as a result of which expiration (on the grounds of civil law this term is 3 years) becomes a significant issue. In relation to the above fact, on 10 February 2012, ZE PAK SA submitted to the District Court of Warszawa Śródmieście a summons for the State Treasury for a conciliatory hearing for the amount of approx. zloty 626 406 thousand and thus stopped the statute of limitation. 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 included 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.
- 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

The Company will take further actions depending on the provisions of the issued decisions.

Other legal proceedings have been described in the consolidated financial statement of the Group in point III.6.s).

11.2. Significant achievements in the field of research and development

As of the date of this report, the ZE PAK SA does not conduct research and development works, which would have material relevance for the Company. Furthermore, the Company has not assigned major financial expenses for research and development works.

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 17 August 2016.

The information regarding the remuneration of the entity authorised to the audit of financial statements was presented in section 38 of the Group's consolidated financial statement for 2016

11.4. Financial forecasts

The Capital Group has not published the financial forecasts. The Group does not intend to present forecasts for 2017.

SIGNATURES OF THE MANAGEMENT BOARD MEMBERS:

Adam Kłapszta

Aneta Lato-Żuchowska

Zygmunt Artwik

Elżbieta Niebisz