PGE Polska Grupa Energetyczna S.A.
Separate financial statements
for 2018

ended December 31, 2018

in accordance with IFRS EU (in PLN million)

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in accordance with IFRS EU (in PLN million)

STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended December 31, 2018	Year ended December 31, 2017
STATEMENT OF PROFIT OR LOSS			
REVENUE FROM SALES	4.1	**11,450**	**9,185**
Cost of goods sold	4.2	(10,634)	(8,436)
GROSS PROFIT ON SALES		**816**	**749**
Distribution and selling expenses	4.2	(17)	(17)
General and administrative expenses	4.2	(222)	(154)
Other operating income / (expenses)		(28)	(37)
OPERATING PROFIT		**549**	**541**
Financial income / (expenses)	4.3	(698)	4,008
GROSS PROFIT/(LOSS)		**(149)**	**4,549**
Current income tax	5.1	(60)	(16)
Deferred income tax	5.1	6	11
NET PROFIT/(LOSS) FOR THE REPORTING PERIOD		**(203)**	**4,544**
OTHER COMPREHENSIVE INCOME			
Items that may be reclassified to profit or loss:			
Measurement of hedging instruments	13.3	(138)	(48)
Deferred tax	5.1	26	9
Items that may not be reclassified to profit or loss:			
Actuarial gains and losses from valuation of provisions for employee benefits		6	-
Deferred tax		(1)	-
OTHER COMPREHENSIVE INCOME FOR THE REPORTING PERIOD, NET		**(107)**	**(39)**
TOTAL COMPREHENSIVE INCOME		**(310)**	**4,505**
NET PROFIT/(LOSS) AND DILUTED NET PROFIT/(LOSS) PER SHARE (IN PLN)	13.5	**(0.11)**	**2.43**

in accordance with IFRS EU (in PLN million)

STATEMENT OF FINANCIAL POSITION

	Note	As at December 31, 2018	As at December 31, 2017 *restated data*
NON-CURRENT ASSETS			
Property, plant and equipment	6	167	176
Intangible assets	7	1	3
Financial receivables	17.1.1	12,756	11,840
Derivatives and other assets measured at fair value through profit or loss	17.1.2	115	216
Shares in subsidiaries	8	32,024	32,568
Shares in subsidiaries, associates and jointly controlled entities	8.2	101	84
Deferred income tax assets	5.3.1	19	-
		45,183	**44,887**
CURRENT ASSETS			
Inventories	10	4	2
Income tax receivables		57	-
Trade and other receivables	17.1.1	5,550	2,636
Derivatives	17.1.2	231	54
Other current assets	11	51	220
Cash and cash equivalents	12	235	1,832
		6,128	**4,744**
TOTAL ASSETS		**51,311**	**49,631**
EQUITY			
Share capital	13.1	19,165	19,165
Reserve capital	13.2	19,872	15,328
Hedging reserve	13.3	(2)	110
Retained earnings	13.4	(201)	4,541
		38,834	**39,144**
NON-CURRENT LIABILITIES			
Non-current provisions	14,15	16	20
Loans, borrowings, bonds	17.1.3	5,628	7,714
Derivatives	17.1.2	24	5
Deferred income tax liabilities	5.3.2	-	13
Other liabilities	17.1	21	23
		5,689	**7,775**
CURRENT LIABILITIES			
Current provisions	14,15	9	2
Loans, borrowings, bonds, cash pooling	17.1.3	5,544	1,764
Derivatives	17.1.2	164	27
Trade and other liabilities	17.1.4	840	682
Income tax liabilities		-	176
Other non-financial liabilities	16	231	61
		6,788	**2,712**
TOTAL LIABILITIES		**12,477**	**10,487**
TOTAL EQUITY AND LIABILITIES		**51,311**	**49,631**

* *restatement of comparative data is described in note 3 of these financial statements.*

in accordance with IFRS EU (in PLN million)

STATEMENT OF CHANGES IN EQUITY

	Share capital	Supplementary capital	Hedging reserve	Retained earnings	Total equity
Note	*13.1*	*13.2*	*13.3*	*13.4*	
AS AT JANUARY 1, 2017	**19,165**	**13,730**	**149**	**1,594**	**34,638**
Net profit for the reporting period	-	-	-	4,544	**4,544**
Other comprehensive income	-	-	(39)	-	**(39)**
COMPREHENSIVE INCOME FOR THE PERIOD	**-**	**-**	**(39)**	**4,544**	**4,505**
Retained earnings distribution	-	1,598	-	(1,598)	**-**
Other changes	-	-	-	1	**1**
AS AT DECEMBER 31, 2017	**19,165**	**15,328**	**110**	**4,541**	**39,144**
Net loss for the reporting period	-	-	-	(203)	**(203)**
Other comprehensive income	-	-	(112)	5	**(107)**
COMPREHENSIVE INCOME FOR THE PERIOD	**-**	**-**	**(112)**	**(198)**	**(310)**
Retained earnings distribution	-	4,544	-	(4,544)	**-**
Other changes	-	-	-	-	**-**
AS AT DECEMBER 31, 2018	**19,165**	**19,872**	**(2)**	**(201)**	**38,834**

in accordance with IFRS EU (in PLN million)

STATEMENT OF CASH FLOWS

	Note	Year ended December 31, 2018	Year ended December 31, 2017 *restated data*
CASH FLOWS FROM OPERATING ACTIVITIES			
Gross profit / (loss)		**(149)**	**4,549**
Income tax paid		16	(105)
Adjustments for:			
Depreciation, amortisation and impairment losses		13	14
Interest and dividend, net	19.1	(133)	(2,869)
Profit / loss on investing activities	19.1	849	(1,144)
Change in receivables	19.1	(228)	(233)
Change in inventories		(2)	74
Change in liabilities, excluding loans and borrowings	19.1	175	466
Change in other non-financial assets	19.1	7	17
Change in provisions		11	31
Other		(1)	1
NET CASH FROM OPERATING ACTIVITIES		**558**	**801**
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, plant and equipment and intangible assets		(1)	(3)
(Purchase) / redemption of bonds issued by PGE Group companies	19.2	(2,101)	(2,142)
Sale of other financial assets		1	368
Purchase of subsidiaries	19.2	(284)	(4,351)
Purchase of other financial assets		(30)	(87)
Dividends received	19.2	46	2,872
Deposits with maturity over 3 months		-	(50)
Termination of deposits with maturity over 3 months	19.2	-	2,340
Origination / (repayment) of loans granted under cash pooling agreement	19.2	(202)	597
Loans granted		(612)	(366)
Interest received		360	66
Loans repaid		260	174
Other		-	-
NET CASH FROM INVESTING ACTIVITIES		**(2,563)**	**(582)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from loans, borrowings and issue of bonds	19.3	2,438	-
Repayment of credit, redemption of bonds	19.3	(1,700)	(17)
Dividends paid		-	-
Interest paid		(315)	(298)
Other		(16)	(3)
NET CASH FROM FINANCING ACTIVITIES		**407**	**(318)**
NET CHANGE IN CASH AND CASH EQUIVALENTS		**(1,598)**	**(99)**
Net exchange differences		-	-
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF PERIOD	12	**1,831**	**1,930**
CASH AND CASH EQUIVALENTS AT THE END OF PERIOD	12	**233**	**1,831**

* *restatement of comparative data is described in note 3 of these financial statements.*

in accordance with IFRS EU (in PLN million)

GENERAL INFORMATION, BASIS FOR PREPARATION OF FINANCIAL STATEMENTS AND OTHER EXPLANATORY INFORMATION

1. General information

1.1 Company operations

PGE Polska Grupa Energetyczna S.A. ("Company", "PGE S.A.") was founded on the basis of a notary deed of August 2, 1990 and registered in the District Court in Warsaw, XVI Commercial Department on September 28, 1990. The Company was registered in the National Court Register of the District Court for the capital city of Warsaw, XII Commercial Department, under no. KRS 0000059307. The Company's registered office is in Warsaw, ul. Mysia 2.

PGE S.A. is the parent company of the PGE Polska Grupa Energetyczna S.A. Group ("PGE Group", "Group") and prepares separate and consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS EU").

The State Treasury is the Company's principal shareholder.

The Company's core activities are as follows:

- trade in electricity and other energy market products
- oversight of head offices and holding companies
- provision of financial services to PGE Group companies
- provision of other services related to these activities

PGE S.A.'s business activities are conducted under appropriate concessions, including concession for electricity trading granted by the Energy Regulatory Office. The concession is valid until 2025. No significant assets or liabilities are assigned to the concession. According to the concession the annual fees are paid depending on the level of trading. In 2018 and in 2017, the Company's costs relating to the concession amounted to PLN 1 million.

Revenue from the sale of electricity and other energy market products is the only significant items in operating revenue. This revenue is generated on the domestic market. The Company's Management Board does not analyse its business based on segments as a result of which the Company does not report business or geographical segments.

PGE S.A.'s accounting books are maintained by subsidiary PGE Synergia sp. z o.o. (formerly PGE Obsługa Księgowo-Kadrowa sp. z o.o.).

Going concern

These financial statements are prepared under the assumption that the Company companies will continue to operate as a going concern in the foreseeable future. As at the date of approval of these financial statements, there is no evidence indicating that the Company will not be able to continue its operations as a going concern.

These financial statements comprise financial data for the period from January 1, 2018 to December 30, 2018 ("financial statements") and include comparative data for the period from January 1, 2017 to December 31, 2017.

1.2 Ownership structure

	State Treasury	Other shareholders	Total
As at January 1, 2018	57.39%	42.61%	100.00%
As at December 31, 2018	57.39%	42.61%	100.00%

The ownership structure as at particular reporting dates was prepared on the basis of data available to the Company.

According to information known to the Company as of the date on which these financial statements were prepared, the State Treasury was the only shareholder with at least 5% of votes at the general meeting of PGE S.A.

1.3 Composition of the Company's Management Board

During the year ended December 31, 2018 and on the date on which these financial statements were published, the Company's Management Board was as follows:

- Henryk Baranowski – President of the Management Board,
- Wojciech Kowalczyk – Vice-President of the Management Board,
- Marek Pastuszko – Vice-President of the Management Board,
- Paweł Śliwa – Vice-President of the Management Board,
- Ryszard Wasiłek – Vice-President of the Management Board,
- Emil Wojtowicz – Vice-President of the Management Board.

2. Basis for preparation of financial statements

2.1 Statement of compliance

These financial statements are prepared in accordance with IFRS EU. International Financial Reporting Standards (IFRS) comprise standards and interpretations, approved by the International Accounting Standards Board ("IASB") and International Financial Reporting Interpretation Committee ("IFRIC").

Included in these financial statements, in note 25, is the financial information referred to in art. 44 sec. 2 of the Energy Law dated April 10, 1997 (Official Journal from 2012 item. 1059 with amendments).

These financial statements are prepared under the historical cost convention, which was modified in relation to:

- Property, plant and equipment and intangible assets – property, plant and equipment and intangible assets that were owned by the Company at the date of transition to IFRS were measured at deemed cost as at that date. In addition, for certain property, plant and equipment and intangible assets impairment loss has been recognised.
- Financial instruments – selected categories of financial instruments are measured and presented in the statement of financial position at fair value. Details on the valuation of particular categories of financial instruments are presented in the description of the accounting principles applied.
- Impaired assets – presented in historical cost adjusted by impairment losses.

The accounting rules used in preparing these financial statements are described in detail in specific notes and were applied by the Company in a continuous manner for all of the presented periods, unless stated otherwise.

2.2 Presentation and functional currency

The functional currency of the Company and presentation currency of these financial statements is the Polish zloty ("PLN"). All amounts are in PLN million, unless indicated otherwise.

For the purpose of translation at the reporting date of items denominated in currency other than PLN the following exchange rates were applied:

	December 31, 2018	December 31, 2017
USD	3.7597	3.4813
EUR	4.3000	4.1709

in accordance with IFRS EU (in PLN million)

2.3 New standards and interpretations published, not yet effective

The following standards, changes in already effective standards and interpretations are not endorsed by the European Union or are not effective as at January 1, 2018:

Standard	Description of changes	Effective date
IFRS 14 *Regulatory Deferral Accounts*	Accounting and disclosure principles for regulatory deferral accounts.	Standard in the current version will not be effective in the EU
Amendments to IFRS 10 and IAS 28	Deals with the sale or contribution of assets between an investor and its joint venture or associate.	Postponed indefinitely
IFRS 16 *Leases*	The standard eliminates the classification of leases as either operating or finance lease in the lessee's accounts. All contracts which meet the criteria of lease will be recognized as finance lease.	January 1, 2019
Amendments to IFRS 9	These changes apply to the right of early repayment with negative fees.	January 1, 2019
IFRS 17 *Insurance contracts*	Defines a new approach to recognising revenue and profit/loss in the period in which insurance services are provided	January 1, 2021
IFRIC 23 *Uncertainty over income tax treatments*	This interpretation applies to establishing taxable revenue, tax base, unsettled tax losses, unused tax rebates and tax rates.	January 1, 2019
Amendments to IAS 28	This amendment concerns measurement of non-current investments in associates	January 1, 2019
Annual improvements to IFRS (cycle 2015-2017)	A collection of amendments dealing with: IFRS 3 - measurement of existing stake in a joint operation; IFRS 11 - no measurement of existing stake in a joint operation; IFRS 12 - income tax consequences of dividends; IAS 23 - borrowing costs when an asset is ready for its intended use.	January 1, 2019
Amendments to IAS 19	Amendments concern defined-benefit plans.	January 1, 2019
Amendments to the Conceptual Framework	These amendments aim to harmonise the Conceptual Framework	January 1, 2020
Amendments to IFRS 3	These changes clarify the definition of economic activity	January 1, 2020
Amendments to IAS 1 and IAS 8	The amendments concern the definition of 'material.'	January 1, 2020

The Company intends to adopt the above mentioned new standards, amendments to standards and IFRS interpretations published by the International Accounting Standards Board but not yet effective at the reporting date, when they become effective.

Impact of new regulations on the Company's future financial statements

IFRS 16 Leases

The new standard changes principles for the recognition of contracts which meet the criteria of lease. The main change is to eliminate the classification of leases as either operating leases or finance leases in the lessee's accounts. All contracts which meet the criteria of a lease will be recognised as a finance lease. Adoption of the standard will have the following effect:

- in the statement of financial position: increase of non-financial non-current assets and financial liabilities,
- in the statement of comprehensive income: decrease of operating expenses (other than depreciation/amortisation), increase of depreciation/amortisation and financial expenses.
- increase in net debt and net debt to EBITDA due to proportionally higher increase in financial liabilities than decrease in operating expenses other than depreciation

The Company analysed the potential impact of IFRS 16 on its future financial statements. The Company inventoried its contracts in order to identify those that contain a lease or a lease component in accordance with IFRS 16.

The following areas were identified as being influenced by IFRS 16:

- right of perpetual usufruct of land;
- tenancy, rental contracts.

As a result of this analysis, the Company concluded that the right to perpetual usufruct of land meets the definition of lease under IFRS 16. Tenancy and rental contracts meet the definition of lease but in their case the Company will use a practical solution, as referred to in paragraph C8 for leases the lease term of which ends prior to 12 months from the first day of use, i.e. January 1, 2019, and will recognise these leases as current leases.

The Company will implement the new IFRS 16 standard starting from financial statements prepared for periods beginning after January 1, 2019. The Company selected the option to implement this standard described in paragraph C5.b) of IFRS 16, i.e. retrospectively with the cumulative effect of initially applying the standard recognised at January 1, 2019 as adjustment of the opening balance of retained earnings.

in accordance with IFRS EU (in PLN million)

In accordance with the selected option, the Company will not restate comparative data. As at the moment IFRS 16 is implemented, it will recognise an asset consisting of the right to perpetual usufruct of land as an operating lease under IAS 17 in an amount equal to the lease liability, adjusted by the amounts of all prepayments and accrued lease payments relating to this lease and recognised directly in the statement of financial situation prior to the first day of application, in compliance with paragraph C8.b.ii).

Recognition of an asset for the right to perpetual usufruct of land will result in an estimated increase in perpetual usufruct assets and lease liabilities as at January 1, 2019, by approx. PLN 20 million. Impact on the net financial result for 2019 will be negligible.

The lessee's residual interest rate was used for measurement and it was assumed that the liability will be settled over the period for which the right was granted.

The aforementioned conclusions and estimates of the impact on future financial statements are subject to change.

Other standards

The other standards and amendments should not have a major impact on the Company's future financial statements.

2.4 Professional judgement of management and estimates

In the process of applying accounting rules with regards to the below issues, management has made judgements and estimates that affect the amounts presented in the financial statements, including in other explanatory information. The estimates were based on the best knowledge of the Management Board relating to current and future operations and events in particular areas. Detailed information on the assumptions made was presented below or in respective explanatory notes.

Recoverable amount of assets

The electricity market is the primary area of operations of the Company and PGE Group entities. Changes in this market may have a significant influence on the recoverable amount of power generating property, plant and equipment of the Company's subsidiaries. If impairment indicators specified in IAS 36 *Impairment of Assets* are identified, the Company estimates the recoverable amount of the respective shares owned.

The Company's impairment analysis of cash generating units is based on a number of significant assumptions concerning factors, some of which are outside the control of the Company. Any significant change in these assumptions will impact the result of future impairment tests and as a consequence may lead to significant changes to the financial position and results of the Company.

In 2018 the Company performed impairment tests of shares in PGE Obrót S.A., PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE Energia Ciepła S.A. and PGE Energia Odnawialna S.A. These tests are described in note 8.1 to these financial statements. Additionally, the Company periodically analyses impairment of non-current financial assets in accordance with IFRS 9 *Financial Instruments.*

Provisions

As described in note 14, the recognition of provisions requires estimates of the probable outflow of economic benefits and determination of the amount that shall be the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The most significant values concern provision for post-employment benefits. Provisions for employee benefits were estimated using actuarial methods.

Key actuarial assumptions related to the calculation of provisions as at the reporting date are as follows:

	As at December 31, 2018	As at December 31, 2017
Expected inflation rate (%)	2.3%-2.5%	1.8%
Discount rate (%)	3.0%	3.4%
Expected salary growth rate (%)	2.5%	1.8%
Employee turnover (%)	5.1%-8.4%	9.57%
Expected medical care costs growth rate (%)	2.3%-2.5%	1.8%
Expected Social Fund (ZFŚS) allowance growth rate (%)	3.6%	3.4%-5.0%

- The probability of employee attrition has been predicted on the basis of historical data related to Company's employee turnover ratio and statistical data on employee attrition in the industry.
- Mortality and survival probability have been adopted from the Life Expectancy Tables published by Central Statistical Office of Poland, assuming that the population of the Company's employees corresponds, in respect of mortality, to the average in Poland.
- Normal procedure of employees' retirement was assumed, in accordance with detailed rules included in the Law on State Social Insurance Pensions, with the exception of employees who meet the conditions required to early retirement.
- For discounting future benefit payments a discount rate of 3.0% was adopted (December 31, 2017: 3.4%), which corresponds to the profitability of long-term Treasury bonds listed on the Polish capital market.

Contingent liabilities

The recognition and measurement of provisions and contingent liabilities requires that the Company estimates the probability of occurrence of potential liabilities. If the occurrence of an unfavourable future event is probable, the Company recognizes a provision in the appropriate amount. If the occurrence of an unfavourable future event is estimated by the Company as not probable but possible, the contingent liability is recognised. Conditional liabilities are described in note 20.1 of these financial statements.

Impairment of receivables

As at the reporting date, the Company recognise the impairment for expected credit losses in an amount equal to full lifetime expected credit losses.

The Company applies the following rules for recognition and valuation of impairment losses on financial assets:

- for trade receivables from significant clients that are subject to a credit risk assessment procedure, the Company estimates expected credit losses based on a model used to evaluate this risk on the basis of ratings assigned to counterparties; ratings have a likelihood of default assigned, which is adjusted to reflect impact of macroeconomic factors;
- for receivables from mass or clients not covered by the credit risk assessment procedure, the Company estimates expected credit losses based on an analysis of the likelihood of credit losses in each age bracket;
- in justified cases, the Company might estimate the amount of an impairment loss on an individual basis.

Revision of impairment losses on trade and other receivables is described in note 18.3.1 of these financial statements.

Uncertainty concerning tax settlements

Regulations concerning tax on goods and services, corporate income tax and burdens related to social insurance are subject to changes. These frequent changes result in a lack of reference points, inconsistent interpretations and few precedents that can be applied. The existing regulations also contain uncertainties that result in differing opinions as to legal interpretation of tax regulations both between state organs and between state organs and companies.

Tax settlements and other activity areas are conditioned by regulations (customs or currency controls) and can be subject to controls of respective authorities that are authorised to issue fines and penalties, and all additional tax liabilities resulting from such audits must be paid with high interest. This means that tax risk in Poland is higher than in countries with more stable tax systems.

As a consequence, the amounts presented and disclosed in financial statements may change in the future as a result of a final decision by a tax control organ.

General Anti-Avoidance Rules (GAAR) are in effect in Poland since 2016. GAAR is intended to prevent the formation and use of artificial legal structures created in order to avoid paying tax in Poland. GAAR defines tax avoidance as an activity performed primarily to obtain a tax benefit contrary under the circumstances to the subject and aim of the tax law. According to GAAR, such an activity does not result in a tax benefit if it is artificial. All proceedings regarding unjustified division of operations, involving intermediaries despite a lack of economic justification, mutually offsetting elements or other similar activities may be treated as a condition for the existence of artificial activities subject to GAAR. These new regulations will require a much greater judgement in assessing the tax effects of transactions.

The Company recognises current and deferred income tax assets and liabilities using IAS 12 Income tax based on profit (tax loss), tax base, unsettled tax losses, unused tax exemptions and tax rates, taking into account assessment of uncertainties related to tax settlements. If there is uncertainty over where or not and in what scope the tax authority will accept tax accounting for transactions, the Company recognises these settlements taking into account an uncertainty assessment.

in accordance with IFRS EU (in PLN million)

3. Changes in accounting and data presentation principles

New standards and interpretations which became effective on January 1, 2018

The accounting principles applied in preparing these financial statements are consistent with those applied in preparing the Company's financial statements for 2017, except as stated below. The following amendments to IFRSs are applied in these financial statements according to their effective dates. Amendments relating to IFRS 9 and IFRS 15 are described below. The other amendments did not have material impact on the presented and disclosed financial information or were not applicable to the Company's transactions;

- Amendments to IFRS 2 - Classification and measurement of share-based payment transactions
- Amendments to IFRS 4 - Application of IFRS 9 Financial instruments jointly with IFRS 4 Insurance contracts
- Amendments resulting from IFRS annual improvement cycle 2014-2016 - amendments to IFRS 1, IAS 28;
- Amendments to IAS 40 - Classification of properties: i.e. transfer from investment property to other groups of assets;
- Amendments to IFRIC 22 - Guidelines specifying determination of the date of a transaction and related spot foreign exchange rate to be used in case foreign currency payments are made.

The Company decided not to apply early any other standards, interpretations or amendments that were published but are not yet effective in light of EU regulations.

IFRS 9 *Financial Instruments*

IFRS 9 replaced IAS MSR 39 *Financial instruments: recognition and measurement* and is effective for annual periods beginning as at or after January 1, 2018. IFRS addressed three areas related to financial instruments: classification and measurement, impairment and hedge accounting.

After analysis, the Company decided not to implement the changes resulting from IFRS 9 as regards hedge accounting from January 1, 2018.

The Company applied IFRS 9 from January 1, 2018, without restating its comparative data.

The Company analysed the business model as at the first date of application of IFRS 9, i.e. January 1, 2018, and subsequently applied retrospectively, regardless of what business model was used in previous reporting periods on these assets for which recognition had not ceased prior to January 1, 2018. Based on the facts and circumstances at initial recognition of a financial assets, the Company assessed whether contractual cash flows concerning a given instrument cover solely payments of principal and interest on the principal amount outstanding - the Solely Payments of Principal and Interest (SPPI) test.

If the Company applied IFRS 9 in its financial statements for 2017, impairment losses on financial assets as at December 31, 2017, would be approx. PLN 4 million higher. Equity as at December 31, 2017 would have decreased by about PLN 4 million gross (no impact on deferred tax).

Due to the insignificant impact of the new standard, its effects were not recognised as retained earnings as of January 1, 2018. Starting from January 1, 2018, the Company recognises expected credit losses in accordance with IFRS 9 requirements.

Changes in the classification of financial instruments resulted in the change of name of several items from the statement of financial position but not amounts were reclassified between items.

Financial Instruments	Classification of instruments under IAS 39	Classification of instruments under IFRS 9
ASSETS		
Trade and other financial receivables	Loans and receivables	Measured at amortised cost
Cash and cash equivalents	Cash and cash equivalents	Measured at amortised cost
Available-for-sale financial assets and shares measured at fair value through profit or loss	Financial assets carried at fair value through profit or loss	Carried at fair value through profit or loss
Derivative financial instruments	Hedging derivatives	Hedging derivatives
EQUITY AND LIABILITIES		
Loans, borrowings, bonds and leases	Financial liabilities at amortised cost	Financial liabilities at amortised cost
Trade and other financial liabilities	Financial liabilities at amortised cost	Financial liabilities at amortised cost
Derivative financial instruments	Financial liabilities at fair value through profit or loss	Carried at fair value through profit or loss
Derivative financial instruments	Hedging derivatives	Hedging derivatives

IFRS 15 *Revenue from Contracts with Customers*

IFRS 15 repeals IAS 11 *Construction Contracts*, IAS 18 *Revenue* and related interpretations and applies to all contracts with customers, with the exception of those that fall under the scope of other standards. The new standard establishes the Five Step Model for recognising revenue from contracts with customers. According to IFRS 15, revenue is recognised in the amount that - according to the entity's expectations - is due in exchange for delivery of the goods or services to the customer.

The Company analysed the largest contracts with its customers in order to identify those that include provisions which could potentially have an impact on the moment of revenue recognition and the level of revenue in the given reporting period, in particular concerning: contracts for the sale of electricity and gaseous fuel, multi-component contracts, mutually linked contracts and contracts containing the entity's commitment to deliver products or services to the client by another entity (intermediary vs principal), variable remuneration, trade bonuses as well as contractual penalties and bonuses.

in accordance with IFRS EU (in PLN million)

Based on this analysis, the Company found that it is an intermediary in gaseous fuel transmission services. The recognition of revenue and costs concerning these services in the financial statements for 2018, would have caused a decrease in operating revenue and costs by less than PLN 2 million.

Based on analyses, the Company considers that on initial application, i.e. in the periods beginning on January 1, 2018, IFRS 15 will not have a significant impact on the moment of recognition and level of revenue identified in the Company's financial statements.

The Company decided not to apply early any other standards, interpretations or amendments that were published but are not yet effective.

Changes in applied accounting principles

Change in presentation of employee benefits concerning accrued leave and bonuses

In the present period, the Company decided to change the way in which it presents employee benefits concerning accrued leave, bonuses and similar from the "provisions" to the "other non-financial liabilities."

The Company restated its comparative data presented in the statement of financial position. The restatement is presented in the table below.

	As at December 31, 2017 *published data*	Change in presentation	As at December 31, 2017 *restated data*
CASH FLOWS FROM OPERATING ACTIVITIES			
Adjustment for items, including:			
Change in liabilities, excluding loans and borrowings	496	(30)	**466**
Change in provisions	1	30	**31**
NET CASH FROM OPERATING ACTIVITIES	**497**	**-**	**497**

	As at December 31, 2017 *published data*	Change in presentation	As at December 31, 2017 *restated data*
CURRENT LIABILITIES, including:			
Current provisions	33	(31)	2
Other non-financial liabilities	30	31	61
TOTAL CURRENT LIABILITIES	**2,712**	**-**	**2,712**
TOTAL EQUITY AND LIABILITIES	**49,631**	**-**	**49,631**

EXPLANATORY NOTES TO THE FINANCIAL STATEMENTS
EXPLANATORY NOTES TO THE STATEMENT OF COMPREHENSIVE INCOME

4. Revenue and expenses

4.1 Revenue from sales

ACCOUNTING RULES

Revenue from contracts with customers - accounting policy applied up from January 1, 2018

Revenue is recognised so as to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

Revenue is recognised when the performance obligation concerning the goods and services is met (or is in the process of being met) by delivery to the customer. The product is delivered when the customer obtains control over it.

The entity recognises revenue from a contract with a customer only if all of the following criteria are met:

- the parties have executed a contract (in written or verbal form or in accordance with customary trade practices) and are obligated to perform their duties;
- the entity is able to identify the rights of each of the parties with regard to the goods or services that are to be transferred;
- the entity is able to identify terms of payment for the goods or services that are to be transferred;
- the contract has commercial substances;
- it is probable that the consideration to which the entity is entitled to in exchange for the goods or services will be collected.

Upon contract execution, the entity analyses the goods or services covered by the contract with the customer and identifies as a performance obligation all commitments to provide the customer with:

- goods or services (or packages of goods or services) that are distinguishable; or
- groups of separate goods or services that are essentially the same and in the transfer to the client is the same.

The Company recognises revenue when the performance obligation concerning the goods and services is met (or is in the process of being met). The transfer of the asset occurs when the customer obtains control over the asset, i.e. gains the ability to directly manage the asset and obtain largely all other benefits from it.

The Company transfers control over goods or services over time and thus satisfies the performance obligation and recognises revenue over time if one of the following conditions is met:

- the customer receives and derives benefits from the Company's consideration as the Company provides the consideration;
- as a result of the Company's consideration a new or improved asset is created (e.g. production in progress) and control over this asset - as it is created or improved - is exercised by the customer; or
- as a result of the Company's consideration no new asset is created for alternative use by the Company and the Company has an enforceable title to pay for the consideration provided thus far.

For each performance obligation over time, the entity recognises revenue over time, measuring the degree of performance of this obligation. The aim of this measurement is to establish progress in performing this obligation to transfer control over goods or services promised to the client (i.e. degree of obligation performance).

Once a performance obligation is provided (or is in the process of being provided), the entity recognised as revenue an amount equal to the transaction price that was assigned to this performance obligation. The transaction price takes into account part or all of the amount of estimated variable consideration only in as far as there is high likelihood that there will not be a reversal of a significant portion of the amount formerly recognised in accumulated revenue when the amount of variable consideration is no longer uncertain.

In order to determine the transaction price, the entity takes into account contractual terms and the customary trade practices. Transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties.

When another party is involved in providing goods or services to a customer, the entity shall determine whether the nature of its promise is a performance obligation to provide the specified goods or services itself (i.e. the entity is a principal) or to arrange for the other party to provide those goods or services (i.e. the entity is an agent).

The entity specifies whether it is the commissioning party or intermediary for each good or service promised to the customer. A specific product or service is a separate product or service (or a group of separate products or services) that are to be delivered to the customer. If the contract with a customer contains more than one specific product or service, the entity might be a principal for some of the products or services and an agent for others.

An entity is a principal if the entity controls a promised good or service before the entity transfers the good or service to a customer.

When an entity that is a principal satisfies a performance obligation, the entity recognises revenue in the gross amount of consideration to which it expects to be entitled in exchange for those goods or services transferred.

An entity is an agent if the entity's performance obligation is to arrange for the provision of goods or services by another party. An entity that is an agent does not control the specific good or service provided to another party prior to delivery to the customer. When an entity that is an agent satisfies a performance obligation, the entity recognises revenue in the amount of any fee or commission to which it expects to be entitled in exchange for arranging for the other party to provide its goods or services. An entity's fee or commission might be the net amount of consideration that the entity retains after paying the other party the consideration received in exchange for the goods or services to be provided by that party.

in accordance with IFRS EU (in PLN million)

Revenue from sales - accounting policy used in force December 31, 2017

Revenue was measured at the fair value of the consideration received or due. Revenue was recognised after deducting value added tax (VAT), excise tax and other sales-based taxes as well as discounts. When recognising revenue, the criteria specified below were also taken into account.

Revenue from sale of goods and merchandise

Revenues from the sale of goods and merchandise were recognised when related risks and rewards have been transferred and when the amount of revenue can be reliably measured and costs incurred can be reliably estimated. In particular, revenues from the sale of electricity were recognised at the time of delivery.

Revenue from the sale of goods and products mainly included:

- amounts receivable from: wholesale and retail sales of electricity, sales of heat energy, gas, lignite, certificates of energy origin from renewable energy sources, certificates of production of energy in high efficiency cogeneration plants, greenhouse gas emission rights, distribution and transmission services and other services relevant to core business,
- amounts receivable from sales of materials and merchandise not mentioned above.

Revenue from sale of services

Revenue from services rendered was recognised when the service is performed. Revenue from the provision of unfinished long-term services in the period from contract date to reporting date - after subtracting revenue recognised in previous reporting period - was determined proportionally to the services' status, if this status could have been determined reliably.

If the results of a contract could not have been reliably estimated, revenue was recognised only up to the amount of costs incurred that the Company expected to recover.

The following table shows revenue from contracts with customers divided into categories that reflect the manner in which economic factors influence the nature, amount and payment deadline and the uncertainty of revenue and cash flows.

Type of good or service	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2018
Total Revenue from Contracts with Customers					
Revenue from sale of goods, including:	**2,507**	**2,273**	**2,550**	**3,253**	**10,583**
Sale of electricity	*2,185*	*2,134*	*2,229*	*2,287*	***8,835***
Sale of gas	*253*	*84*	*87*	*107*	***531***
Other sales of goods and materials	*69*	*55*	*234*	*859*	***1,217***
Revenue from sale of services	**210**	**189**	**230**	**238**	**867**
TOTAL REVENUE FROM SALE*	**2,717**	**2,462**	**2,780**	**3,491**	**11,450**

*The total revenue amount includes approx. PLN 2 million in sales transactions for which the value was not ultimately established as at the end of the reporting period.

Timing of transfer of goods or services	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2018
Total Revenue from Contracts with Customers					
Revenue from sale of goods or services provided to the customer over time	*2,648*	*2,407*	*2,546*	*2,632*	*10,233*
Revenue from sale of goods or services provided to the customer at a point in time	*69*	*55*	*234*	*859*	***1,217***
TOTAL REVENUE FROM SALES	**2,717**	**2,462**	**2,780**	**3,491**	**11,450**

The Company operates mainly in Poland. Sales to foreign customers in 2018 and in 2017 reached PLN 204 million and PLN 230 million respectively and concerned mainly electricity and gas.

In 2018, the Company recognised revenue from considerations satisfied in previous periods resulting from adjustments of the amounts of electricity sales on the balancing market made in previous years. The total amount of revenue from these adjustments was PLN 1.6 million.

Type of good or service	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2017*
REVENUE FROM SALES					
Revenue from sale of goods, including:	**2,230**	**2,047**	**2,057**	**2,220**	**8,554**
Sale of electricity	*2,003*	*1,748*	*1,910*	*1,961*	***7,622***
Sale of energy origin rights	*10*	*-*	*19*	*20*	***49***
Sale of gas	*157*	*139*	*88*	*215*	***599***
Other sales of goods and materials	*60*	*160*	*40*	*24*	***284***
Revenue from sale of services	**170**	**144**	**156**	**161**	**631**
TOTAL REVENUE FROM SALES	**2,400**	**2,191**	**2,213**	**2,381**	**9,185**

*The Company applied IFRS 15 for the first time in 2018. In accordance with the standard's implementation method, the Company did not restate comparative data.

in accordance with IFRS EU (in PLN million)

The y/y increase in revenue from electricity sales in 2018 results from higher turnover volume and higher sales prices, mainly in transactions with PGE Obrót S.A. Sales to PGE Obrót S.A. are conducted in order to satisfy retail client demand for electricity.

The decline in revenue from the sale of natural gas in 2018 resulted from a decrease in gas sales volumes on the exchange and to entities outside PGE Group.

Growth in revenue from the sale of other goods and materials in 2018 resulted from higher sales of CO_2 emission allowances to PGE Group companies. The growth in revenue from the sale of CO_2 emission allowances resulted from both an increase in sales prices and sales volumes.

Revenue from the sale of services mainly concern services provided to PGE Group subsidiaries and cover electricity trade and supply, fuel deliveries, licences and support services.

Information concerning key clients

The Company's main counterparties are PGE Group subsidiaries. In 2018, sales to PGE Obrót S.A. accounted for 68% of revenue from sales, while sales to PGE Górnictwo i Energetyka Konwencjonalna S.A. accounted for 16%. In 2017, sales to these companies accounted for 71% and 9%, respectively.

4.2 Costs by nature and function

ACCOUNTING RULES

Cost of goods sold

Cost of goods sold includes: value of electricity, certificates of origin for energy, gas sold and other goods and materials at acquisition prices.

Costs that can be directly attributable to revenues recognised by the Company are recognised in profit or loss for the reporting period in which the revenues were recognised.

Costs that can only be indirectly attributed to revenues or other economic benefits recognised by the Company, are recognised in the profit or loss in the reporting periods to which they relate, in accordance with accrual basis of accounting, taking into account the principles of measurement of property, plant and equipment and inventories.

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2018
COSTS BY NATURE					
Depreciation, amortisation	3	4	3	3	**13**
External services	13	14	15	20	**62**
Employee benefits expenses	30	28	31	38	**127**
Other costs by nature	16	23	20	24	**83**
TOTAL COSTS BY NATURE	**62**	**69**	**69**	**85**	**285**
Distribution and selling expenses	(5)	(4)	(5)	(3)	**(17)**
General and administrative expenses	(49)	(55)	(51)	(67)	**(222)**
Cost of goods and materials sold	2,504	2,269	2,547	3,268	**10,588**
COST OF GOODS SOLD	**2,512**	**2,279**	**2,560**	**3,283**	**10,634**

	Q1 *unaudited*	Q2 *unaudited*	Q3 *unaudited*	Q4 *unaudited*	Year ended December 31, 2017
COSTS BY NATURE					
Depreciation, amortisation	4	3	4	3	**14**
External services	13	17	15	13	**58**
Employee benefits expenses	27	28	25	32	**112**
Other costs by nature	16	14	18	25	**73**
TOTAL COSTS BY NATURE	**60**	**62**	**62**	**73**	**257**
Distribution and selling expenses	(5)	(5)	(3)	(4)	**(17)**
General and administrative expenses	(35)	(37)	(37)	(45)	**(154)**
Cost of goods and materials sold	2,175	1,997	2,009	2,169	**8,350**
COST OF GOODS SOLD	**2,195**	**2,017**	**2,031**	**2,193**	**8,436**

The increase in the value of goods and materials sold in 2018, comparing to 2017, is largely the effect of higher revenue from sales, as described above, and higher prices on the wholesale market.

in accordance with IFRS EU (in PLN million)

4.2.1 Depreciation, amortisation and impairment losses

	Depreciation, amortisation					
	Year ended December 31, 2018			Year ended December 31, 2017		
	Property, plant and equipment	Intangible assets	TOTAL	Property, plant and equipment	Intangible assets	TOTAL
Cost of goods sold	4	1	**5**	4	2	**6**
Distribution and selling expenses	-	-	**-**	-	1	**1**
General and administrative expenses	7	1	**8**	6	1	**7**
TOTAL	**11**	**2**	**13**	**10**	**4**	**14**

4.2.2 External services

	Year ended December 31, 2018	Year ended December 31, 2017
Trading commissions	13	10
IT services	24	20
Consulting services	13	16
Transmission services	2	3
Other	10	9
TOTAL EXTERNAL SERVICES	**62**	**58**

4.2.3 Employee benefits expenses and employment structure

	Year ended December 31, 2018	Year ended December 31, 2017
Payroll	96	86
Social security expenses	14	13
Change in provisions for employee benefits	5	(1)
Other employee benefits	12	14
TOTAL EMPLOYEE BENEFITS EXPENSES, INCLUDING:	**127**	**112**
Included in costs of goods sold	22	25
Included in distribution and selling expenses	7	6
Included in general and administrative expenses	98	81

As at December 31, 2018, the Company had 614 employees (full-time equivalent), compared to 525 at December 31, 2017.

4.2.4 Other expenses by nature

	Year ended December 31, 2018	Year ended December 31, 2017
Sponsoring and advertising	58	51
Management remuneration	8	7
Taxes and fees	4	4
Other	13	11
TOTAL EXTERNAL SERVICES	**83**	**73**

in accordance with IFRS EU (in PLN million)

4.3 Financial income and financial expenses

ACCOUNTING RULES

Financial income and financial expenses

Interest income and expenses are recognised over the respective period using the effective interest method in relation to the net amount of the financial instrument at the reporting date.
Dividends are recognised when the shareholders' right to receive payments is established.

	Year ended December 31, 2018	Year ended December 31, 2017
NET FINANCIAL INCOME / (EXPENSES) FROM FINANCIAL INSTRUMENTS		
Dividends	46	2,872
Interest	100	42
Revaluation of financial instruments, including:	(43)	63
CO2 emission rights	*(40)*	*31*
Other derivatives	*(3)*	*32*
Reversal/(recognition) of impairment allowances	(799)	1,036
Foreign Exchange differences	-	(4)
Gain on disposal of investment	1	-
TOTAL NET FINANCIAL INCOME / (EXPENSES) FROM FINANCIAL INSTRUMENTS	**(695)**	**4,009**
NET OTHER FINANCIAL: INCOME / (EXPENSES)		
Interest expenses, including effect of unwinding the discount	(1)	(1)
Other	(2)	-
TOTAL NET OTHER FINANCIAL INCOME / (EXPENSES)	**(3)**	**(1)**
TOTAL NET FINANCIAL INCOME / (EXPENSES)	**(698)**	**4,008**

In 2018, the Company reported dividend income mainly from PGE Obrót S.A. (PLN 28 million), and in the comparative period PLN 2,019 million from PGE GiEK S.A. and PLN 808 million from PGE Dystrybucja S.A.

Under the heading 'Recognition / (reversal) of impairment allowances,' in the current reporting period the Company mainly presents the recognition of impairment for expected credit losses concerning PGE Obrót S.A. and PGE Sweden AB shares and the reversal of impairment for expected credit losses concerning PGE Obrót S.A. shares in the comparative reporting period, which is further described in note 8.1 to these financial statements.

Interest income relates mainly to bonds issued by subsidiaries and cash deposits.

Revaluation of financial instruments includes an ineffective portion of CCIRS hedging transaction valuation designated as hedging instruments in the cash-flow hedge accounting and total valuation of other derivatives.

Interest expenses mainly relate to bonds issued and credit and loans, as described in note 17.1.3 of these financial statements.

4.3.1 Valuation of transactions related to trading in CO_2 emission allowances

As described in note 4.3 of these financial statements, income and expenses recognised under the heading "Revaluation of financial instruments" comprise the result on transactions related to CO2 emission rights (so-called trading book).

The following table illustrates the effects of particular items related to the CO2 emission rights on the financial income and expenses.

	Year ended December 31, 2018	Year ended December 31, 2017
Income		
Valuation of commodity forwards	-	46
Valuation of futures	147	-
Profit on sale of CO_2 emission rights outside PGE Group	8	-
Revaluation of emission allowances	-	8
TOTAL INCOME RELATED TO TRADE IN CO2 EMISSION RIGHTS	**155**	**54**
Expenses		
Measurement of commodity forwards	(170)	-
Measurement of currency forwards	(25)	(20)
Loss on sale of CO_2 emission rights outside PGE Group	-	(3)
TOTAL EXPENSES RELATED TO TRADE IN CO2 EMISSION RIGHTS	**(195)**	**(23)**
Income / (expenses) from revaluation of financial instruments related to trading in CO2 emission rights	**(40)**	**31**

in accordance with IFRS EU (in PLN million)

5. Income tax

ACCOUNTING RULES

Taxes

Income tax recognised in profit or loss comprises current income tax and deferred income tax. Recognised are actual fiscal charges for the reporting period calculated by the Company in accordance with regulations of the Corporate Income Tax Act and the change in deferred tax assets and deferred tax liabilities other than the ones charged or credited directly to equity.

Due to temporary differences between the carrying amount of a given asset or liability and its tax base and tax loss that is recoverable in the future, the Company recognises deferred income tax liabilities and assets.

The value of a deferred tax asset and deferred tax liability in the statement of financial position is verified at each reporting date. Deferred income tax assets and deferred income tax liabilities are classified as non-current. The Company offsets deferred tax asset and liabilities.

The Company reduces the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable profit will be available to allow deferred tax asset to be utilised partially or entirely.

5.1 Tax in the statement of comprehensive income

The key elements of income tax expense for the years ended December 31, 2018 and December 31, 2017 are as follows:

	Year ended December 31, 2018	Year ended December 31, 2017
INCOME TAX RECOGNISED IN STATEMENT OF PROFIT OR LOSS		
Current income tax PGE S.A.	125	19
Benefits from tax group settlements	(65)	(7)
Adjustments related to settlement of current income tax of previous years	-	4
Total current income tax	**60**	**16**
Deferred income tax	(6)	(11)
INCOME TAX EXPENSE RECOGNISED IN STATEMENT OF PROFIT OR LOSS	**54**	**5**
INCOME TAX EXPENSE RECOGNISED IN OTHER COMPREHENSIVE INCOME		
From valuation of hedging instruments	(26)	(9)
From actuarial gains and losses from valuation of provisions for employee benefits	1	-
INCOME TAX EXPENSE RECOGNISED IN OTHER COMPREHENSIVE INCOME (EQUITY)	**(25)**	**(9)**

Rules regarding settlements between companies forming the PGE tax group ("TG PGE") are described in note 22 of these financial statements.

Adjustments related to settlement of current income tax from previous years concern mainly final settlement of the tax group for the previous year. The differences arise from sales of electricity for the previous year invoiced in the first quarter of the current year, previously recognised based on estimates.

in accordance with IFRS EU (in PLN million)

5.2 Effective tax rate

A reconciliation of the calculation of income tax on profit before tax at the statutory tax rate and income tax calculated according to the effective tax rate of the Company is as follows:

	Year ended December 31, 2018	Year ended December 31, 2017
PROFIT / (LOSS) BEFORE TAX	**(149)**	**4,549**
Income tax according to Polish statutory tax rate of 19%	(28)	864
ITEMS ADJUSTING INCOME TAX		
Adjustments related to settlement of current income tax of previous years	-	4
Adjustments concerning deferred income tax from previous years	(1)	
Tax losses of companies belonging to the tax group	(65)	(7)
Non-taxable income	(9)	(841)
Costs not recognised as tax-deductible costs	156	26
Other	1	(41)
TAX AT EFFECTIVE TAX RATE (Income tax (expense) as presented in the financial statements)	**54**	**5**
EFFECTIVE TAX RATE	**(36.2%)**	**0.1%**

In accordance with the agreements within PGE's tax group, when the company belonging to the tax group incurs tax loss, the respective tax benefits are transferred to the representing company, PGE S.A.

Non-taxable income refers mainly to dividend income which is not included in the calculation of current income tax base (tax amount: PLN 9 million in 2018 and PLN 546 million in 2017) and the reversal of impairment of PGE Obrót S.A. shares (tax value of PLN 245 million).

In the item 'Non-deductible costs,' the Company recognised impairment of PGE Obrót S.A. and PGE Sweden AB shares (tax value of PLN 153 million).

5.3 Deferred tax in the statement of financial position

5.3.1 Deferred income tax assets

	As at December 31, 2018	As at December 31, 2017
Difference between tax value and carrying amount of financial liabilities	28	20
Difference between tax value and carrying amount of financial assets	59	21
Provisions for employee benefits	9	10
Other	5	-
DEFERRED TAX ASSETS	**101**	**51**

The Company does not recognise deferred tax asset related to difference between tax value and carrying amount of shares in subsidiaries. Negative temporary differences connected with the recognition of impairment losses on shares in subsidiaries would be PLN 4,605 million, which would have a PLN 875 million impact on tax.

5.3.2 Deferred tax liabilities

	As at December 31, 2018	As at December 31, 2017
Difference between tax value and carrying amount of property, plant and equipment	19	20
Difference between tax value and carrying amount of other financial assets	63	41
Other	-	3
DEFERRED TAX LIABILITIES	**82**	**64**
AFTER OFF-SET OF BALANCES THE COMPANY'S DEFERRED TAX IS PRESENTED AS:		
Deferred tax assets	19	-
Income tax liabilities	-	13

in accordance with IFRS EU (in PLN million)

EXPLANATORY NOTES TO THE STATEMENT OF FINANCIAL POSITION

6. Property, plant and equipment

ACCOUNTING RULES

Property, plant and equipment

Property, plant and equipment are assets:

- held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and
- expected to be used for more than one year.

After initial recognition, an item of property, plant and equipment is measured at carrying amount, i.e. initial value (or deemed cost for items of property, plant and equipment used before the transition to IFRS) less any accumulated depreciation and any impairment losses. Initial value comprises purchase price including all costs directly attributable to the purchase and bringing the asset into use. The cost comprises estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having it used for purposes other than to produce inventories.

The depreciable amount is the cost of an asset less its residual value. Depreciation commences when the asset is available for use. Depreciation is based on a depreciation plan reflecting the future useful life of the asset. The depreciation method used reflects the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

The following useful lives are adopted for particular groups of property, plant and equipment:

Group	Average remaining amortisation period in years	Applied total depreciation periods in years
Buildings and structures	18	2-31
Machinery and equipment	6	1-39
Vehicles	2	1-10
Other property, plant and equipment	2	1-15

	As at December 31, 2018	As at December 31, 2017
Buildings	156	163
Other property, plant and equipment	11	13
NET VALUE OF PROPERTY, PLANT AND EQUIPMENT	**167**	**176**

In the reporting and comparative period, the Company did not purchase nor sold any significant property, plant and equipment.

7. Intangible assets

ACCOUNTING RULES

Intangible assets

An intangible asset is an identifiable non-monetary asset without physical substance, such as:

- economic rights acquired by the Company and recognised in non-current assets, with an economic useful life exceeding one year, intended to be used by the Company,
- development costs,
- goodwill excluding internally generated goodwill,
- acquired right of perpetual usufruct of land.

As at the date of initial recognition, an intangible asset is measured at acquisition cost or production cost with respect to development costs. After initial recognition, an intangible asset shall be carried at its cost less accumulated amortization and accumulated impairment losses. The cost of an internally generated intangible asset, excluding development costs, is not capitalised and is recorded in profit or loss for the period when the related cost was incurred.

The Company assesses whether the useful life of intangible assets is definite or indefinite. If the useful life is definite, the Company estimates the length of the useful period, the volume of production or other measures as the basis to define the useful life. An intangible asset is regarded as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the Company.

The amortisable amount of an intangible asset with a definite useful life shall be allocated on a systematic basis over its useful life. Amortisation starts when the asset is available for use.

The following useful lives are adopted for intangible assets:

Group	Average remaining amortisation period in years	Applied total amortisation period in years
Acquired patents and licences	1	1-11

Intangible assets consist mainly of software and licences. As at December 31, 2018, no impairment risk regarding these assets was identified.

8. Shares in subsidiaries

ACCOUNTING RULES

Shares in subsidiaries, jointly controlled entities and associates

Subsidiaries are those companies whose financial and operational policies are managed by the Company in order to derive economic benefits from their operations. This involves holding the majority of total votes in decision-making bodies of these organisations. To determine whether the Company has control over the given organisation, existence and impact of potential voting rights that can be realized or converted at any time are considered.

A jointly controlled entity is an organization in which the division of control over the business as specified in the agreement requires unanimity of controlling parties with respect to strategic financial and operational decisions.

An associate is a business organization, including a partnership (such as a civil partnership) upon which the investor has significant influence and which is not a wholly or partially owned subsidiary. "Significant influence" is defined in IAS 28 as the right to participate in the financial and operating policy decisions of the investee but does not refer either to control or joint control over those policies.

Shares in subsidiaries, jointly controlled entities and associates held by the Company are measured at historical acquisition cost in accordance with IAS 27 *Separate financial statements*. If there is an objective evidence of impairment of these assets, the amount of impairment is measured as the difference between the carrying value of the asset and the estimated recoverable amount.

in accordance with IFRS EU (in PLN million)

Shares in subsidiaries are recognised at cost less accumulated impairment losses.

	Registered office	Stake as at December 31, 2018	As at December 31, 2018	Stake as at December 31, 2017	As at December 31, 2017
COMPANIES BELONGING TO TG PGE 2015					
PGE GiEK S.A.	Bełchatów	100.00%	15,437	100.00%	15,437
PGE Dystrybucja S.A.	Lublin	100.00%	10,595	100.00%	10,611
PGE Obrót S.A.	Rzeszów	100.00%	1,647	100.00%	2,406
PGE Energia Odnawialna S.A.	Warsaw	100.00%	1,349	100.00%	1,349
PGE Systemy S.A.	Warsaw	100.00%	131	100.00%	140
ELBEST sp. z o.o.	Bełchatów	100.00%	101	100.00%	101
PGE Dom Maklerski S.A.	Warsaw	100.00%	97	100.00%	97
PGE Ventures sp. z o.o	Warsaw	100.00%	68	100.00%	21
BETRANS sp. z o.o.	Bełchatów	100.00%	35	100.00%	35
ELMEN sp. z o.o.	Rogowiec	100.00%	23	100.00%	23
PGE Nowa Energia sp. z o.o	Warsaw	100.00%	15	100.00%	15
PGE Centrum sp. z o.o.	Warsaw	100.00%	14	100.00%	8
BESTGUM sp. z o.o.	Rogowiec	100.00%	12	100.00%	13
MEGAZEC sp. z o.o.	Bydgoszcz	100.00%	10	100.00%	10
PGE Inwest 5 sp. z o.o. (currently PGE Baltica sp. z o.o.)	Warsaw	100.00%	9	100.00%	<1
ELBIS sp. z o.o.	Rogowiec	100.00%	8	100.00%	8
Ramb sp. z o.o.	Piaski	100.00%	7	100.00%	7
MegaSerwis sp. z o.o.	Bogatynia	100.00%	7	100.00%	7
PGE Synergia sp. z o.o. (formerly PGE Obsługa Księgowo-Kadrowa sp. z o.o.)	Warsaw	100.00%	6	100.00%	6
ELTUR SERWIS sp. z o.o.	Bogatynia	100.00%	5	100.00%	-
PGE Inwest 13 S.A.	Warsaw	100.00%	1	100.00%	1
ELBEST Security sp. z o.o.	Warsaw	100.00%	<1	100.00%	<1
7 limited liability companies named PGE Inwest 2;8 to 12;14	Warsaw	100.00%	<1	100.00%	<1
TOP Serwis sp. z o.o.	Bogatynia	-	-	100.00%	5
COMPANIES NOT BELONGING TO TG PGE 2015					
PGE Energia Ciepła S.A.	Warsaw	100.00%	2,005	99.52%	1,992
PGE EJ 1 sp. z o.o.	Warsaw	70.00%	155	70.00%	113
PGE Sweden AB (publ)	Stockholm	100.00%	72	100.00%	112
PGE Towarzystwo Funduszy Inwestycyjnych S.A.	Warsaw	100.00%	24	100.00%	24
PGE Trading GmbH	Berlin	100.00%	23	100.00%	23
Elektrownia Wiatrowa Baltica 1 sp. z o.o.	Warsaw	100.00%	17	-	-
Elektrownia Wiatrowa Baltica 2 sp. z o.o.	Warsaw	100.00%	65	-	-
Elektrownia Wiatrowa Baltica 3 sp. z o.o.	Warsaw	100.00%	85	-	-
Energopomiar sp. z o.o.*	Gliwice	-	-	22.73%	3
PGE Inwest 16 sp. o.o.	Warsaw	100.00%	1	100.00%	1
3 limited liability companies named PGE Inwest 17, 18, 19	Warsaw	100.00%	<1	100.00%	<1
TOTAL			**32,024**		**32,568**

**In 2017 Energopomiar sp. z o.o. was subsidiary in GK PGE, as overall share of PGE S.A. and other GK PGE companies exceeded 50%. During 2018 partial sale of shares took place, and Energopomiar became an associate and is no longer presented in above table..*

Significant changes in the structure of subsidiaries that took place in 2018:

- On February 26, 2018, a resolution was adopted to merge Przedsiębiorstwo Usługowo-Produkcyjne ELTUR-SERWIS Sp. z o.o. (the acquiring company) with Przedsiębiorstwo Usługowo-Produkcyjne „TOP SERWIS" sp. z o.o. (the acquired company). The merger was registered at the National Court Register on April 12, 2018.
- On March 7, 2018 and May 7, 2018, PGE S.A. purchased 3,285 and 2,970 shares of PGE Energia Ciepła S.A. respectively in a mandatory squeeze out procedure pursuant to art. 418[1] of the Polish Commercial Companies Code. On May 18, 2018, PGE S.A. purchased 336,473 shares of PGE Energia Ciepła S.A. in a mandatory squeeze out procedure pursuant to art. 418 of the Polish Commercial Companies Code. As a result of these transactions, PGE S.A. currently holds a 100% interest in PGE Energia Ciepła S.A. The price paid for the shares was PLN 13 million.
- On August 31, 2018, an agreement was executed pursuant to which PGE Polska Grupa Energetyczna S.A. purchased from PGE Energia Odnawialna S.A. all shares in Elektrownia Wiatrowa Baltica-1 sp. z o.o., Elektrownia Wiatrowa Baltica-2 sp. z o.o. and Elektrownia Wiatrowa Baltica-3 sp. z o.o. The shares were transferred on September 3, 2018.

Furthermore, on October 18, 2018, the Extraordinary General Meetings of PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Energia Ciepła S.A. adopted resolutions to divide PGE Górnictwo i Energetyka Konwencjonalna S.A. (divided company) by transferring the following PGE Górnictwo i Energetyka Konwencjonalna S.A. branches to PGE Energia Ciepła S.A.:

- Elektrociepłownia Kielce,
- Elektrociepłownia Gorzów,
- Elektrociepłownia Rzeszów,
- Elektrociepłownia Lublin Wrotków,
- Elektrociepłownia Zgierz,
- Zespół Elektrociepłowni Bydgoszcz.

The division was registered at the National Court Register on January 2, 2019.

8.1 Analysis of value of non-current financial assets

In the previous reporting period, the Company recognised an impairment loss on PGE EJ1 sp. z o.o. shares of PLN 105 million. The reason for this impairment loss was a substantial difference between the book value of PGE EJ1 sp. z o.o. shares in PGE S.A.'s accounts and the value of this company's equity.

In the previous reporting period, the Company recognised an impairment loss on its stake in subsidiary ELTUR SERWIS sp. z o.o., amounting to PLN 23 million, due to its economic and financial situation.

In previous reporting periods, the Company recognised an impairment loss on shares in AWSA Holland II BV of PLN 115 million.

Moreover, PGE S.A. holds bonds issued by Autostrada Wielkopolska S.A., which were fully written-off due to a loss of value.

Impairment analysis of PGE Energia Odnawialna S.A., PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Energia Ciepła S.A.

In 2018, PGE Group analysed assumptions and identified drivers that could have substantial impact on changes in the value of its generating assets and as a result have an impact on the value of PGE S.A.'s stakes in PGE Energia Odnawialna S.A., PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Energia Ciepła S.A. Key changes in the regulatory environment are as follows:

- entry into force on December 14, 2018, of the Act on promotion of electricity produced in high-efficiency cogeneration. A reduction of support for gas-fired generating units after 2018 vs assumptions adopted in 2017 was introduced alongside inclusion of hard coal-fired generating units in the support system,
- positive regulatory changes concerning wind farm maintenance costs in the Renewables segment due to legislative changes in respect of the act of May 20, 2016, on investments in wind farms ("Act") resulting from the entry into force of the act of June 7, 2018, on amendment of the act on renewables and certain other acts ("Renewables Act"). In particular, the Renewables Act introduces a change in the definition of wind farm by re-introducing the wording contained in the act of July 7, 1994 - Construction Law. In accordance with the justification in the Renewables Act, this should clear up interpretation doubts with regard to property tax bases for wind farms, which arose after January 1, 2017. Given the change in the Act in the above scope, wind farms are no longer considered entirely as structures, which translates into lower property tax expenses. Tax base changes are in effect retrospectively, from January 1, 2018.
- execution on December 18/19, 2018, of an agreement between the representatives of EU member states and the European Parliament on Capacity Market regulations and subsequent approval of the agreement on January 18, 2019 by EU member state ambassadors. Comparing to previous assumptions, the key change in the new regulations is rejection from the Capacity Market from July 1, 2025 of units that do not meet the emission criterion of 550g CO_2/kWh of electricity produced (except for multiannual contracts executed in main auctions for 2021-2024), which in practice removes coal-based units from the Capacity Market after 2024.

Given the above, PGE S.A. has carried out impairment tests on its stakes in PGE Energia Odnawialna S.A. and PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Energia Ciepła S.A. These tests were conducted on cash generating unit basis by establishing their recoverable amounts. The recoverable value of the analysed assets was estimated on the basis of discounted net cash flow method which relied on the financial projections prepared for the assumed useful life of the particular CGU. According to the Company, financial projections longer than five years are justified because the property, plant and equipment items used by the tested entities have significant longer useful lives and also due to significant and long-term effects of projected changes in the regulatory environment.

Macroeconomic assumptions

The key price assumptions, i.e. the prices of electricity, CO_2 emission allowances, hard coal, gas, and assumptions related to production at most of the Group's installations were derived from a study prepared by an independent expert, basing on the current market situation for the first three years of the forecast.

Electricity price forecasts expect a major increase in 2019, comparing to 2018, followed by stability until 2022 and several-percent growth in subsequent years.

Price forecasts for CO_2 emission allowances see dynamic market price growth in successive years covered by the forecast.

Hard coal price forecasts expect strong growth in 2019, comparing to 2018, followed by stability until 2022 and several-percent growth in subsequent years.

Gas price forecasts see average annual growth in the period to 2022 at approx. 7% and growth of approx. 4% annually in the years thereafter.

The forecast for prices of property rights concerning certificates of origin was drafted by PGE S.A.'s team of in-house experts, based on a demand-supply balance and expected regulatory changes in renewables property rights area. It was assumed that auctions will be the dominant support mechanism. Forecast for the prices of property rights concerning the origin of energy from renewable sources see a down trend, resulting mainly from a reduction in potentially excessive support in a situation of dynamically increasing electricity prices for units within the green certificate system. For production covered by contracts the prices and settlement terms used in these contracts during their validity were adopted.

Capacity-market revenue forecast for 2021-2023 is based on the results of main auctions for these delivery periods, taking into account the mechanisms of the agreement to re-allocate revenue within PGE Group companies. The forecast after 2024 was developed by a team of experts at PGE S.A., based on assumptions concerning estimated future cash flows for generation units, on the basis of completed auctions. From July 1, 2025, removed from the Capacity Market are units that fail to meet the 550 g CO_2 emission criterion, except for units covered by multiannual contracts executed in main auctions for years 2021-2024.

Revenue from regulatory system services was based on existing bilateral agreements with PSE S.A.

Unit availability was estimated based on repair plans, taking into account statistical failure rates.

Detailed assumptions regarding the tested companies

Presented below are the key assumptions having impact on estimates of the useful value of PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Energia Ciepła S.A.:

- receipt of a quantity of free-of-charge CO_2 emission allowances for the purposes of electricity generation for 2018-2020 for specific cash generating units in accordance with Poland's application for a transition allocation of free emission allowances for the modernisation of electricity generation activities pursuant to art. 10c sec. 5 of directive 2003/87/EC of the European Parliament and the Council (derogation application), which meets the requirements of Commission Decision of July 13, 2012. As regards heat generation, free-of-charge allowances were taken into account in accordance with the list of quantities of CO2 emission allowances allocated for heat for 2013-2020 published by the Environment Ministry,
- take into account the allocation of free CO_2 emission allowances in the period 2021-2030 only for system district heating and high-efficiency cogeneration, based on the 2020 level and assuming annual reduction,
- assumption for conventional plants that during the residual period there will be support from the capacity market or equivalent, only for units that meet the emission criterion of 550 g CO_2 of electricity produced.
- take into account the support system for high-efficiency cogeneration for gas units over the entire forecast period and in the residual period,
- take into account work cost optimisation resulting from current work plans, among other things,
- maintain production capacities as a result of replacement-type investments,
- take into account development investments for which construction work has begun,
- adopt WACC for the projection period at 7.29%.

Presented below are the key assumptions having impact on estimates of the useful value of PGE Energia Odnawialna S.A.:

- production of electricity and property rights was estimated based on historic data and expert estimates prepared for investment purposes, adjusted by the availability of units;
- recognition of cash flows concerning contractual penalties and damages awarded in disputes with Enea S.A. and Energa Obrót S.A. in amounts resulting from the contracts or calculated as the difference between the contract prices of property rights and market prices;
- decline in property tax expenses from 2018; In accordance with the assumptions adopted for the impairment tests as at December 31, 2017, the lower property tax base was adopted starting from 2019.
- maintain production capacities as a result of replacement-type investments,
- adopt WACC for the projection period at 7.29%.

The tests did not indicate the necessity to recognise an impairment loss on the shares of PGE Energia Odnawialna S.A., PGE Energia Ciepła S.A. and PGE Górnictwo i Energetyka Konwencjonalna S.A. The recoverable value of these stakes exceeds their book value indicated in these financial statements.

in accordance with IFRS EU (in PLN million)

Impairment test at PGE Obrót S.A.

Significant increase in electricity volatility prices on the wholesale market in 2018. These prices have not stabilised yet. As a result of this situation, PGE Obrót S.A. is expected in the foreseeable future to generate lower margins than planned.

Moreover, on December 28, 2018, an act amending the act on excise duty and certain other acts ("Act") was adopted. The Act aims to stabilise electricity prices for final customers in 2019. In accordance with the new regulations, the excise duty on electricity is reduced from PLN 20 to PLN 5 per MWh. The transition fee, paid each month by electricity customers, is reduced by 95%. , paid monthly by energy final consumers.

On February 21, 2019, the Polish parliament adopted an updated version of the Act. The updated Act indicates that the electricity prices for final customers in 2019 must correspond to the prices indicated in the tariff approved by the URE President on December 31, 2018. Where electricity prices for 2019 were determined in a manner other than tariff, including in individually negotiated contracts or through a tender, then the prices for 2019 may not be higher than those applied on June 30, 2018. The Act was adopted by the Senate on February 26, 2019, and was signed by the President on March 1, 2019. The above legislative changes are a response and an attempt to ease the effects of dynamic growth in electricity prices on the wholesale market, mainly due to growth in the prices of CO_2 allowances. Price growth on the wholesale market translates into growth in prices for final customers in subsequent periods.

At the same time, it is expected that the Act's provisions will be neutral from the viewpoint of trading companies. Companies selling electricity to final customers will be able to apply for reimbursement of lost revenue in the form of compensation. As at the date on which these financial statements were prepared, no detailed information is yet available as to how PGE Obrót S.A. will receive these compensations because implementing regulations for the Act have not yet been published.

Given the fact the Company's capitalisation remains below its book value, the rising electricity prices on the wholesale market and the regulatory changes, the Company conducted an impairment test on equity. The test was conducted in line with IAS 36 using the discounted cash flows method. A five-year cash flow model for PGE Obrót S.A. was used in developing the projects. The key assumptions used in the valuation were as follows:

- increase in overall sales volume in 2023 by approx. 3.9% compared to 2018,
- the price assumptions, i.e. the prices of electricity, were derived from a study prepared by an independent expert, basing on the current market situation for the first three years of the forecast,
- lower forecast margins on electricity in 2019-2020 due to higher costs to purchase electricity,
- change in margin after 2020, calculated on the basis of historic data, taking into account a down trend in 2021-2023,
- correlation between electricity prices in sales to retail customers with wholesale prices and impact on their level resulting from a change in the obligation to redeem property rights as well as changes in the prices of property rights,
- full coverage of lost revenue due to reduced electricity prices for final customers in 2019 with compensations,
- adopt WACC for the projection period at 7.29%.

The higher sales volume and margins for 2021-2023 adopted for these tests were estimated on the assumption that PGE Obrót S.A. will strengthen its position on the electricity sales market. In 2018, as a result of considerable volatility of prices on the wholesale market, many companies engaged in trade of electricity ceased their activities and terminated their sales contracts with customers.

The balance sheet value of PGE Obrót S.A. shares in the Company's accounts amounted to PLN 2,406 million. As a result of an impairment test, the value of PGE Obrót S.A. shares was estimated at PLN 1,647 million, in connection with which PGE S.A. recognised an impairment loss of PLN 759 million. The need to recognise this impairment loss is dictated mainly by rising electricity prices on the wholesale market from 2018, which translates into lower forecast margins for years 2019-2020.

Sensitivity analysis

The results of a sensitivity analysis showed that the largest impact on the value of shares have changes in assumptions concerning the weighted average cost of capital and stand-alone margins. Presented below is the estimated impact of changes in key assumptions on changes in impairment losses on PGE Obrót S.A. shares as at December 31, 2018.

Parameter	Change	Impact on impairment loss	
		Increase in impairment loss	Decrease in impairment loss
Change in stand-alone margin	1%	-	99
	-1%	99	-
Change in WACC	+ 0.5 p.p.	214	-
	- 0.5 p.p.	-	262

in accordance with IFRS EU (in PLN million)

8.2 Shares in subsidiaries, associates and jointly controlled entities

	As at December 31, 2018	As at December 31, 2017
Polimex Mostostal S.A.	81	81
ElectroMobility Poland S.A.	18	3
Energopomiar Sp. z o.o.	2	-
Total	**101**	**84**

9. Joint ventures

The Company did not participate in joint ventures in 2018 and 2017.

10. Inventories

ACCOUNTING RULES

Inventories

Inventories are assets held for sale in the ordinary course of business, in the process of production for such sale, or in the form of materials or supplies to be consumed in the production process or in providing services.

Inventories comprise:

- energy origin rights – purchased rights of origin for energy produced from renewable energy sources, rights of origin for energy relating to energy generated in cogeneration and rights to energy efficiency certificates,
- goods (especially CO_2 emission allowances intended for re-sale).

Inventories are measured at the lower value of the following two: acquisition cost or inventory cost and net realisable value. CO_2 emission allowances acquired in order to realise profits from fluctuations in market prices are measured at fair value less costs of disposal.

	As at December 31, 2018			As at December 31, 2017		
	Historic cost	Impairment	Net value	Historic cost	Impairment	Net value
Other CO_2 emission allowances	4	-	4	2	-	2
TOTAL INVENTORIES	**4**	**-**	**4**	**2**	**-**	**2**

	Year ended December 31, 2018	Year ended December 31, 2017
REVALUATION ADJUSTMENTS OF INVENTORIES AS AT JANUARY 1	**-**	**(8)**
Fair value measurement of CO_2 emission allowances	-	8
REVALUATION ADJUSTMENTS OF INVENTORIES AS AT DECEMBER 31	**-**	**-**

11. Other current assets

ACCOUNTING RULES

Other assets (including prepayments)

The Company recognises an asset as a prepayment under the following conditions:

- an expense was incurred in the past in relation to operating activity,
- it can be reliably measured,
- it refers to future reporting periods.

Prepayments are recognised at reliably measured amounts, relate to future periods and will generate future economic benefits.

Other assets include in particular state receivables, advances for deliveries and services and dividend receivables.

in accordance with IFRS EU (in PLN million)

	As at December 31, 2018	As at December 31, 2017
Receivables from tax group	8	170
Advance payments	37	32
VAT receivables	-	13
Other	6	5
TOTAL	**51**	**220**

PGE S.A. is the representative entity in its tax group, which covers the Company and some of its subsidiaries. Rules regarding settlements between companies are described in note 22 of these financial statements.

Advance payments consist mainly of funds transferred to the subsidiary PGE Dom Maklerski S.A. for the purchase of electricity and gas of PLN 37 million in the current reporting period as compared to PLN 32 million in the comparative period.

12. Cash and cash equivalents

ACCOUNTING RULES

Cash and cash equivalents

Cash comprises cash on hand and demand deposits.

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Short-term deposits are made for different periods, from one day up to one month, depending on the Company's needs for cash, and are deposited at individually agreed interest rates.

Cash in bank accounts accrues interest based on variable interest rates the level of which depends on the interest on overnight bank deposits

The balance of cash and cash equivalents comprise the following positions:

	As at December 31, 2018	As at December 31, 2017
Cash on hand and cash at bank	211	732
Overnight deposits	-	1
Short-term deposits	-	1,099
Cash in VAT accounts	24	-
TOTAL	**235**	**1,832**
Exchange differences on cash in foreign currencies	(2)	(1)
Cash and cash equivalents presented in the statement of cash flows	**233**	**1,831**
Undrawn borrowing facilities as at December 31	7,290	4,360
including overdraft facilities	*932*	*2,000*

Cash includes PLN 24 million in restricted cash in the form of funds on VAT accounts and PLN 3 million in the form of received collateral.

A detailed description of credit agreements is presented in note 17.1.3 of these financial statements.

13. Equity

ACCOUNTING RULES

Equity

Equity is stated at nominal value, classified by type and in accordance with legal regulations and the Company's Articles of Association.

Share capital in these financial statements is presented at the value specified in the Articles of Association and registered in the Court Register.

Declared, but not contributed, share capital contributions are recognised as outstanding share capital contributions as negative value.

The objective of equity management is to ensure a secure and effective financing structure that takes into account operational risk, investment expenditures and the interests of shareholders and debt investors. Equity management takes places at Group level.

In accordance with common practice, the Company monitors the net debt to EBITDA ratios at PGE Group level, as described in note 20 to the consolidated financial statements. Net debt is understood as short- and long-term financial debt (interest-bearing credit and loans, bonds and other debt instruments as well as finance lease liabilities), less cash and cash equivalents and short-term deposits. Restricted cash is not included in calculating net debt.

in accordance with IFRS EU (in PLN million)

The Company's aim is to maintain its investment grade credit ratings. However, given the on-going investment programme, financial leverage is expected to increase in the coming years. The net debt to EBITDA ratio is a central element of the Company's financial forecasts and plans.

13.1 Share capital

	As at December 31, 2018	As at December 31, 2017
1,470,576,500 Series A ordinary Shares with a nominal value of PLN 10.25 each	15,073	15,073
259,513,500 Series B ordinary Shares with a nominal value of PLN 10.25 each	2,660	2,660
73,228,888 Series C ordinary Shares with a nominal value of PLN 10.25 each	751	751
66,441,941 Series D ordinary Shares with a nominal value of PLN 10.25 each	681	681
Total share capital	**19,165**	**19,165**

All of the Company's shares are paid up.

After the reporting date and until the date of preparation of the foregoing financial statements there were no changes in the value of the Company's share capital.

Shareholder rights - State Treasury rights concerning the Company's activities

The Company is a part of the PGE Polska Grupa Energetyczna S.A. Group, to which State Treasury holds special rights as long as it remains a shareholder.

Special rights of the State Treasury that are applicable to the PGE Group entities derive from the Act of March 18, 2010 on special rights of the Minister of Energy and their performance in certain companies and groups operating in the electricity, oil and gaseous fuels sectors (Official Journal from 2016, item 2012). The aforesaid Act specifies the particular rights entitled to the Minister of Energy related to companies and groups operating in the electricity, oil and gaseous fuels sectors whose property was disclosed within the register of buildings, installations, equipment and services included in critical infrastructure.

Based on this act the Minister of Energy has the right to object to any resolution or legal action of the Management Board that relates to the ability to dispose of a part of Company's property, which may result in threat to functioning, continuity of operations and integrity of critical infrastructure.

The objection can also be expressed against any resolution adopted that relates to:

- Liquidation of the Company,
- Changes of the use or discontinuance of exploitation of the Company's asset, which is a component of critical infrastructure,
- Change in the scope of activities of the Company,
- Sale or lease of the enterprise or its organised part or establishment of legal restrictions,
- Approval of operational and financial plan, investment plan, or long-term strategic plan,
- Movement of the Company's seat abroad,

if the enforcement of such a resolution would result in an actual threat to functioning, continuity of operations and integrity of the critical infrastructure. The objection is expressed in the form of an administrative decision.

13.2 Reserve capital

Supplementary capital results from statutory allocation of profits generated in previous reporting periods, from surplus of profit distribution in excess of the value of statutory allocations, as well as from merger of PGE S.A. with its subsidiaries.

According to regulations of the Commercial Code, joint stock companies are obliged to create reserve capital to cover potential losses. At least 8% of the profit for the reporting year recognised in the separate financial statements of the Company is transferred to supplementary capital, until this supplementary amounts to at least one third of share capital. The part of supplementary capital which amounts to one third of share capital can only be used to cover losses recognised in the separate financial statements and cannot be distributed for other purposes. The General Meeting decides on the use of supplementary capital and other capital reserves.

Reserve capital subject to distribution to shareholders amounted to PLN 13,484 million as at December 31, 2018 and to PLN 8,940 million as at December 31, 2017.

in accordance with IFRS EU (in PLN million)

13.3 Hedging reserve

Change in the revaluation reserve concerning cash flow hedge accounting implemented:

	Year ended December 31, 2018	Year ended December 31, 2017
AS AT JANUARY 1	**110**	**149**
Change in hedging reserve, including:	**(138)**	**(48)**
Deferral of changes in fair value of hedging financial instruments in the part considered as effective hedge	(44)	(218)
Accrued interest on derivatives transferred from hedging reserve and recognised in interest expense	(10)	4
Currency revaluation of CCIRS transaction transferred from hedging reserve and recognised in the result on foreign exchange differences	(84)	166
Ineffective portion of changes in fair value of hedging derivatives recognised in profit or loss	-	-
Deferred tax	**26**	**9**
HEDGING RESERVE INCLUDING DEFERRED TAX	**(2)**	**110**

13.4 Retained earnings and limitations on payment of dividend

Retained earnings which are not subject to distribution are amounts that cannot be paid in the form of dividends.

	As at December 31, 2018	As at December 31, 2017
Retained earnings not subject to distribution - profits / losses recognised in other comprehensive income	2	(3)
Retained earnings subject to distribution	-	4,544
Net loss	(203)	-
TOTAL RETAINED EARNINGS PRESENTED IN THE STATEMENT OF FINANCIAL POSITION	**(201)**	**4,541**

The Company assumes, that the net loss for the year ended December 31, 2018 in amount of PLN 203 million will be covered with the profit from the following years.

For information regarding limitations in payment of dividends from reserve capital please refer to note 13.2 of these financial statements. As at December 31, 2018 there were no other restrictions on dividend payments.

13.5 Earnings per share

ACCOUNTING RULES

Earnings per share

Earnings per share for each period is calculated by dividing profit or loss attributable to ordinary equity holders of the Company by the weighted average number of shares outstanding during the reporting period.
The Company calculates diluted earnings per share by dividing profit or loss attributable to ordinary equity holders of the Company (after deduction of interest on redeemable convertible preference shares) by the weighted average number of shares outstanding during the period (adjusted by the number of dilutive options or dilutive redeemable convertible preference shares).

During current and comparative reporting period there was no dilutive effect on earnings per share.

	Year ended December 31, 2018	Year ended December 31, 2017
NET PROFIT/(LOSS)	**(203)**	**4,544**
NET PROFIT / (LOSS) ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY USED TO CALCULATE EARNINGS PER SHARE	**(203)**	**4,544**
Number of ordinary shares at the beginning of the reporting period	1,869,760,829	1,869,760,829
Number of ordinary shares at the end of the reporting period	1,869,760,829	1,869,760,829
WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES USED TO CALCULATE EARNINGS PER SHARE	**1,869,760,829**	**1,869,760,829**
NET PROFIT/(LOSS) AND DILUTED NET PROFIT/(LOSS) PER SHARE (IN PLN)	**(0.11)**	**2.43**

in accordance with IFRS EU (in PLN million)

13.6 Dividends paid and recommended for payment

On May 11, 2017 the Company's Management Board decided to change its dividend policy. In light of the need to finance an ambitious growth programme and with a view towards reducing debt growth, the Company's Management Board recommended the suspension of dividends from profit for years 2016, 2017 and 2018.
After this period, the Company's Management Board intends to recommend to the General Meeting dividend payments to shareholders amounting to 40-50% of consolidated net profit attributable to the parent's shareholders, adjusted for impairment of tangible and intangible assets.

14. Provisions

ACCOUNTING RULES

Provisions

The Company recognises provisions when there is present obligation (legal or constructive) that arises from past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. When the effect of the time value of money is significant, the amount of a provision is the present value of the expenditures expected to be required to settle the obligation. The discount rate is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The discount rate does not reflect risks for which future cash flow estimates have been adjusted.

Provision for post-employment benefits

The Company's employees are entitled to the following post-employment benefits:

- retirement and pension benefits – paid once when the employee retires or becomes a pensioner,
- post-mortem severance,
- cash equivalent related to energy tariff for employees of power industry,
- benefits from the Social Fund,
- medical benefits.

Until December 31, 2017, the Company's employees were also entitled to receive jubilee awards that are paid after an employee has worked for a specified period of time. The amount of awards paid depended on the period of service and the average remuneration of the employee.
The Company recognises a provision for future obligations relevant to past service costs and jubilee awards for the purpose of assigning costs to the periods in which they are incurred. The provision raised is recognised as an operating expense in the amount corresponding with accrued future employees' benefits. The present value of these obligations is measured by an independent actuary.
Actuarial gains and losses arising from the change of actuarial assumptions (including change in discount rate) and ex post actuarial adjustments are recognised in other comprehensive income.

The carrying amount of provisions is as follows:

	As at December 31, 2018		As at December 31, 2017	
	Non-current	Current	Non-current	Current
Post-employment benefits	16	1	20	2
Other	-	8	-	-
TOTAL PROVISIONS	**16**	**9**	**20**	**2**

Changes in provisions

Year ended December 31, 2018	Post-employment benefits	Other
AS AT JANUARY 1, 2018	**22**	**-**
Current employment costs	1	-
Adjustment of discount rate and other assumptions	(7)	-
Other changes	1	8
AS AT DECEMBER 31, 2018	**17**	**8**

In 2018, the Company created a provision for risk associated with additional costs related to PGE Group's debt financing programmes.

Year ended December 31, 2017	Post-employment benefits	Jubilee awards	Total
AS AT JANUARY 1, 2017	**22**	**2**	**24**
Benefits paid / Provisions used	-	(2)	**(2)**
AS AT DECEMBER 31, 2017	**22**	**-**	**22**

in accordance with IFRS EU (in PLN million)

Based on data received from the actuary, the Company estimates that the influence of changes in assumptions on the value of provisions for post-employment benefits would be as follows:

- should the discount rate be higher by 1 percentage point (p.p.), the provision would decrease by PLN 2 million, and should the discount rate be lower by 1 p.p., the provision would increase by PLN 3 million.
- should the growth rates be higher by 1 p.p., the provision would increase by PLN 3 million, and should the rates be lower by 1 p.p., the provision would decrease by PLN 2 million.

15. Post-employment benefits

The amount of provisions for post-employment benefits recognised in the financial statements results from the valuation prepared by an independent actuary.

The carrying amount of provisions for employee benefits:

	As at December 31, 2018		As at December 31, 2017	
	Non-current	Current	Non-current	Current
Retirement, pension and post-mortem benefits	2	-	1	1
Energy tariff	9	1	8	1
Social Fund	1	-	7	-
Medical benefits	4	-	4	-
TOTAL EMPLOYEE BENEFITS	**16**	**1**	**20**	**2**

16. Other non-financial liabilities

The main components of non-financial liabilities as at respective reporting dates are as follows:

	As at December 31, 2018	As at December 31, 2017
Liabilities due to settlements in the tax group	174	25
VAT liabilities	13	-
Employee bonuses (annual, quarterly)	18	18
Unused holiday leave	4	4
Awards for Management Board	11	8
Estimated liabilities concerning other employee benefits	5	1
Other	6	5
TOTAL OTHER LIABILITIES	**231**	**61**

PGE S.A. is the representative entity in its tax group, which covers the Company and most of its subsidiaries. Rules regarding settlements between companies are described in note 22 of these financial statements.

EXPLANATORY NOTES TO FINANCIAL INSTRUMENTS

17. Financial Instruments

ACCOUNTING RULES

Classification and measurement

Financial assets are subject to classification in the following categories of financial instruments:

- measured at amortised cost;
- measured at fair value through other comprehensive income ("FVTOCI");
- measured at fair value through profit or loss ("FVTPL").

The classification of financial assets is based on the business model and characteristics of cash flows.

A debt instrument is measured at amortised cost if both of the following conditions are met:

- the objective of the entity's business model is to hold the financial asset to collect the contractual cash flows;
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI test).

A debt instrument is measured at FVTOCI if both of the following conditions are met:

- the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets;
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI test).

All other debt instruments if do not met above conditions are measured at fair value through profit or loss (FVTPL).

All equity investments are to be measured at fair value. If an equity investment is not held for trading, the Company can make an irrevocable election at initial recognition to measure it at FVTOCI. For equity instruments held for trading, changes in fair value are recognised in profit or loss.

All standard transactions to purchase or sell financial assets are recognised at the transaction date, i.e. at the date on which the entity committed to purchase the asset. Standard transactions to purchase or sell financial assets are purchase or sale transactions in which the asset delivery deadline is explicitly stated by law or customs in a given market.

An impairment model is based on expected credit losses and its scope covers the following:

- Financial assets measured at amortised cost;
- Financial assets measured at FVTOCI;
- Loan commitments when there is a present obligation to extend credit;
- Financial guarantee contracts to which IFRS 9 is applied;
- Lease receivables within the scope of IAS 17;
- Contract assets within the scope of IFRS 15.

The Company classified financial liabilities in one of the following categories:

- measured at amortised cost;
- measured at fair value through profit or loss.

Financial instruments - accounting policy used until December 31, 2017

In accordance with IAS 39, financial assets were classified into the following categories:

- Held-to-maturity investments;
- Financial assets at fair value through profit or loss;
- Loans and receivables;
- Available-for-sale financial assets.

Financial assets carried at fair value through profit or loss

An asset constituting a financial asset carried at fair value through profit or loss had to meet one of the following conditions:

- was qualified as held for trading. Financial assets were classified as held for trading if they were:
  - acquired principally for the purpose of selling in the near term,
  - part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking, or
  - derivatives, except for a derivative that is a designated and effective hedging instrument.
- Was classified to this category at acquisition. Every financial asset that falls under IAS 39 might have been reclassified at acquisition to a portfolio measured at fair value with changes recognised in profit or loss except for equity instruments that have no prices quoted on an active market and their fair value cannot be reliably established.

These instruments were measured at fair value as at the reporting date. Gain or loss on financial assets classified to the FVP portfolio were recognised in the financial result and were not decreased by interest.

Loans and receivables

Loans and receivables were financial assets other than derivatives with identified or identifiable payments, not listed on an active market. They were classified as current assets if their maturities did not exceed 12 months from the reporting date. Loans and receivables with maturity exceeding 12 months were classified as non-current assets. Loans and receivables were recognised at amortised cost.

Trade receivables were measured at least at each reporting date in the amount due, i.e. at the nominal value increased by applicable penalty interest, in accordance with the principle of prudence, i.e. less applicable impairment allowances. Impairment allowances on receivables were recognised as other operating expenses or finance expenses . Non-current receivables were recognised at present value (discounted).

Available-for-sale assets

All other financial assets were available-for-sale financial assets. Financial assets available for sale were recognised at fair value as at each reporting date. The fair value of an instrument which does not have a quoted market price was estimated with regards to another instrument of similar characteristics or based on future cash flows relevant to an investment asset (measurement using discounted cash flow method).

Positive and negative differences between fair value of available-for-sale financial assets (if their price is determinable on a regulated active market or if the fair value may be estimated by some other reliable method) and cost, net of deferred tax, were recognised in other comprehensive income, except for:

- impairment losses,
- exchange gains and losses arising on monetary assets,
- interest recognised using the effective interest rate method.

Dividends from equity instrument in the AFS portfolio were recognised in profit or loss on the date that the entity's right to receive payment is established.

17.1 Description of significant items within particular classes of financial instruments

17.1.1 Trade and other financial receivables

ACCOUNTING RULES

Financial receivables

Financial receivables are measured at least at each reporting date in the amount due, i.e. at the nominal value increased by applicable penalty interest, in accordance with the principle of prudence, i.e. less applicable impairment allowances. Impairment allowances on receivables are recognised as other operating expenses or finance expenses. Non-current receivables are measured at present (discounted) value.

For trade receivables, the Company measures impairment for expected credit losses in an amount equal to the expected credit losses throughout the entire term of the instrument.

The Company measures financial assets at amortised cost using the adopted business model.

in accordance with IFRS EU (in PLN million)

	As at December 31, 2018		As at December 31, 2017	
	Non-current	Current	Non-current	Current
Trade receivables	-	844	-	758
Bonds acquired	12,582	571	10,912	130
Cash pooling receivables	-	1,204	-	134
Loans granted	174	2,790	928	1,614
Other financial receivables	-	141	-	-
TOTAL FINANCIAL RECEIVABLES	**12,756**	**5,550**	**11,840**	**2,636**

Trade receivables

Trade receivables of PLN 844 million relate mainly to the sale of electricity and services to subsidiaries in PGE Group. As at December 31, 2018, the balance of the three most important customers, i.e. PGE Obrót S.A., PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Dom Maklerski S.A., accounted for 85% of total trade receivables.

Additional information relating to trade receivables is presented in note 18.3.1 of these financial statements.

Bonds acquired

	As at December 31, 2018		As at December 31, 2017	
	Non-current	Current	Non-current	Current
BONDS ACQUIRED - ISSUER				
PGE Górnictwo i Energetyka Konwencjonalna S.A..	11,525	365	9,685	94
PGE Energia Odnawialna S.A.	1,057	206	1,227	36
TOTAL BONDS ACQUIRED	**12,582**	**571**	**10,912**	**130**

PGE S.A. acquires bonds issued by entities belonging to PGE Group. Cash obtained from the issue of bonds is used for financing investments, repayment of financial liabilities as well as for financing current operations.

From January 1, 2018 all transactions are on market terms.

Bonds with maturities not exceeding 12 months from the reporting date are classified as current assets, while bonds with maturities exceeding 12 months from the reporting date are classified as non-current assets, however this classification depends not only on maturity but also on the Company's intentions with regard to roll-over.

Intra-group bonds maturing in less than one year that are expected to be rolled over are classified as non-current instruments. This classification reflects the character of cash management in mid- and long-term.

The final bond buy-back deadline is set at 2025 for PGE Górnictwo i Energetyka Konwencjonalna S.A. and 2020 for PGE Energia Odnawialna S.A.

Cash pooling receivables

In 2014, in order to centralize the management of financial liquidity in PGE Group, agreements for real cash pooling services were executed between 16 companies of PGE Group and each bank separately, i.e. with Powszechna Kasa Oszczędności Bank Polski S.A. and Polska Kasa Opieki S.A. PGE S.A. coordinates the cash pooling service in PGE Group. This means, among others, that certain entities settle with the Company and the Company settles with banks. In connection to the above, balances with related parties participating in cash pooling are reported in financial receivables and financial liabilities of PGE S.A.

Loans granted

	As at December 31, 2018		As at December 31, 2017	
	Non-current	Current	Non-current	Current
LOANS GRANTED - BORROWER				
PGE Energia Ciepła S.A.	-	2,771	542	1,614
PGE Dystrybucja S.A.	-	-	243	-
PGE Systemy S.A.	110	6	106	-
PGE EJ 1 sp. z o.o.	56	-	21	-
PGE Trading GmbH	-	13	12	-
Bestgum sp. z o.o.	5	-	4	-
Betrans sp. z o.o.	3	-	-	-
TOTAL LOANS GRANTED	**174**	**2,790**	**928**	**1,614**

The loan repayment deadline is in 2019-2022.

in accordance with IFRS EU (in PLN million)

17.1.2 Derivatives and other assets measured at fair value through profit or loss

ACCOUNTING RULES

Derivatives and hedging instruments

The Company uses derivatives in order to hedge against interest rate risk and exchange rate risk, mostly forwards, futures and interest rate swaps (IRS) as well as CCIRSs. Such derivatives are measured at fair value. Depending on whether the valuation of a derivative is positive or negative, it is recognised as a financial asset or financial liability, respectively.
The gain or loss resulting from the change in fair value of a derivative not qualifying for hedge accounting, is recognised directly in profit or loss.
The fair value of currency forward contracts is estimated with reference to current forward rates for contracts of similar maturity. Fair value of interest rate swaps is estimated with reference to the market value of similar financial instruments.

All derivatives are recognised in the Company's financial statements at fair value.

	As at December 31, 2018			
	Recognised in profit or loss	Recognised in other comprehensive income	Assets	Liabilities
DERIVATIVES AT FAIR VALUE THROUGH PROFIT OR LOSS				
Commodity forwards	(162)	-	-	116
Futures	147	-	147	-
Currency forwards	(25)	-	4	48
IRS hedges	8	-	-	-
Options	(12)	-	12	-
HEDGING DERIVATIVES				
CCIRS hedges	98	(29)	113	-
IRS hedges	(4)	(109)	4	24
OTHER assets measured at fair value through profit or loss				
Investment fund participation units	1	-	66	-
TOTAL DERIVATIVES AND OTHER RECEIVABLES MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS	**51**	**(138)**	**346**	**188**
non-current			115	24
current			231	164

	As at December 31, 2017			
	Recognised in profit or loss	Recognised in other comprehensive income	Assets	Liabilities
DERIVATIVES AT FAIR VALUE THROUGH PROFIT OR LOSS				
Currency forwards	46	-	54	-
Commodity forwards	(20)	-	-	19
IRS transactions	15	-	-	8
Options	17	-	24	-
HEDGING DERIVATIVES				
CCIRS hedges	(168)	(19)	44	-
IRS hedges	(3)	(29)	98	5
OTHER assets measured at fair value through profit or loss				
Investment fund participation units	-	-	50	-
TOTAL DERIVATIVES AND OTHER RECEIVABLES MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS	**(113)**	**(48)**	**270**	**32**
non-current			216	5
current			54	27

in accordance with IFRS EU (in PLN million)

Commodity and currency forwards

Commodity and currency forward transactions mainly relate to trade in CO_2 emission allowances.

IRS transactions

In the previous reporting periods, the Company concluded IRS transactions to hedge interest rates on credit facilities totalling PLN 5,130 million. To recognise these IRS transactions, the Company uses hedge accounting. The impact of hedge accounting on equity is presented in note 13.3 to these financial statements.

In 2014, PGE S.A. concluded IRS transactions hedging the interest rate on issued bonds with a nominal value of PLN 1,000 million. Payments arising from IRS transactions are correlated with interest payments on bonds. Changes in fair value of IRS transactions are fully recognised in profit or loss.

The company bought back the bonds in the present period, and the hedging IRS transaction was settled.

CCIRS hedges

In June and August 2014, in connection with loans received from PGE Sweden AB (publ) disclosed in note 17.1.3 of these financial statements, PGE S.A. concluded CCIRS transactions, hedging both the exchange rate and interest rate. In these transactions, banks - counterparties pay PGE S.A. interest based on a fixed rate in EUR and PGE S.A. pays interest based on a fixed rate in PLN. The nominal value, payment of interest and repayment of nominal value in CCIRS transactions are correlated with the relevant conditions arising from loan agreements.

To recognise these CCIRS transactions, the Company uses hedge accounting. The impact of hedge accounting on equity is presented in note 13.3 of these financial statements.

Options

On January 20, 2017 PGE S.A. purchased a call option to purchase shares of Polimex-Mostostal S.A. from Towarzystwo Finansowe Silesia Sp. z o.o. The option was valued using the Black-Scholes method. The option exercise dates are: July 30, 2020, July 30, 2021 and July 30, 2022.

Investment fund participation units

In 2018, the Company purchased investment certificates from FIZAN PGE Ventures. The value of these certificates as at the reporting date was PLN 15 million. In 2017 the Company purchased participation units from PGE TFI S.A. in three sub-funds. The value of these units as at the reporting date was PLN 51 million.

Presented below are the terms of the derivative instruments and other assets measured at fair value through profit or loss.

	As at December 31, 2018		As at December 31, 2017		
	Value in financial statements in PLN	**Instrument's nominal value in original currency**	**Value in financial statements in PLN**	**Instrument's nominal value in original currency**	**Maturity as at December 31, 2018**
Currency forward - EUR	4	203	-	-	by December 2021
Commodity forward sale EUA - EUR	-	-	54	763	
Commodity forward purchase EUA - EUR		-		194	
Futures purchase EUA - EUR	147	144	-	-	by December 2020
Futures sale EUA - EUR		5	-	-	by December 2020
CCIRS - EUR to PLN	113	514	44	514	by June 2019
		144		144	by July 2029
IRS - interest rate PLN	4	-	98	3,630	
		1,000		1,000	by December 2027
Options	12	6	24	6	by July 2022
Fund participation units	66	65	50	50	n/a
FINANCIAL ASSETS	**346**	**-**	**270**	**-**	
Currency forward - EUR	48	1,222	19	193	by March 2020
Commodity forward sale EUA - PLN	116	5,762	-	-	by December 2022
Commodity forward purchase EUA - EUR		1,164	-	-	by December 2020
Commodity forward sale EUA - EUR		19	-	-	by March 2020
Commodity forward purchase EUA - PLN		63	-	-	by March 2019
IRS - interest rate PLN	24	500	13	500	by December 2027
		3,630	23	1,000	by June 2018
FINANCIAL LIABILITIES	**188**	**-**	**32**	**-**	

in accordance with IFRS EU (in PLN million)

17.1.3 Loans, borrowings, bonds, cash pooling

	As at December 31, 2018		As at December 31, 2017	
	Non-current	Current	Non-current	Current
Credit liabilities	5,022	1,866	5,019	129
Loans received	606	2,232	2,695	59
Bonds issued	-	-	-	1,000
Cash pooling liabilities	-	1,446	-	576
TOTAL LOANS, BORROWINGS, BONDS AND CASH POOLING	**5,628**	**5,544**	**7,714**	**1,764**

Bank credit

Lender	Type of financing	Execution date	Maturity date	Limit in currency	Currency	Interest rate	Liability as at December 31, 2018	Liability as at December 31, 2017
Bank Gospodarstwa Krajowego	general-purpose credit facility	2014-12-17	2027-12-31	1,000	PLN	Variable	1.001	1.001
Bank Gospodarstwa Krajowego	general-purpose credit facility	2015-12-04	2028-12-31	500	PLN	Variable	500	500
Bank consortium	general-purpose credit facility	2015-09-07	2023-09-30	3,630	PLN	Variable	3.648	3.647
Bank consortium	general-purpose credit facility	2015-09-07	2019-04-30	1,870	PLN	Variable	1.171	-
European Investment Bank	credit facility for grid modernisation	2015-10-27	2032-10-26	1,500	PLN	Variable	-	-
European Investment Bank	credit facility for CHP construction	2015-10-27	2032-10-26	490	PLN	Variable	-	-
European Bank for Reconstruction and Development	financing for selected investment tasks	2017-06-07	2028-06-06	500	PLN	Variable	-	-
Revolving credit facility	general-purpose credit facility	2018-09-17	2023-12-17	4,100	PLN	Variable	-	-
Bank Pekao S.A.	Current-account overdraft facility	2018-07-05	2021-07-03	500	PLN	Variable	148	-
PKO BP S.A.	Current-account overdraft facility	2018-04-30	2020-04-29	500	PLN	Variable	-	-
Bank Gospodarstwa Krajowego	Current-account overdraft facility	2018-06-01	2021-05-31	500	PLN	Variable	420	-
Total bank credit							**6,888**	**5,148**

The value of overdraft facilities at the Company's disposal amounted to PLN 932 million as at December 31, 2018 and PLN 2,000 million as at December 31, 2017. The aforesaid overdraft facilities are available until July 2021.

In the period covered by these financial statements there were no cases of default on repayment or breach of other terms of credit agreements.

Loans received

Lender	Type of financing	Execution date	Maturity date	Limit in currency	Currency	Interest rate	Liability as at December 31, 2018	Liability as at December 31, 2017
PGE Sweden AB	general-purpose loan	2014-06-10	2019-06-05	210	EUR	Fixed	904	877
PGE Sweden AB	general-purpose loan	2014-06-10	2019-06-05	300	EUR	Fixed	1,292	1,253
PGE Sweden AB	general-purpose loan	2014-06-10	2019-06-05	4	EUR	Fixed	17	17
PGE Sweden AB	general-purpose loan	2014-08-27	2029-07-31	43	EUR	Fixed	189	184
PGE Sweden AB	general-purpose loan	2014-08-27	2029-07-31	100	EUR	Fixed	436	423
Total loans received							**2,838**	**2,754**

The Company recognises loans of EUR 660 million (PLN 2,838 million) from subsidiary PGE Sweden AB (publ).

In 2014, PGE S.A. and PGE Sweden AB (publ) established a Euro Medium Term Note Program, in which PGE Sweden AB (publ) may issue Eurobonds up to EUR 2 billion with a minimum maturity of 1 year. In 2014, PGE Sweden AB (publ) issued Eurobonds in the total amount of EUR 638 million. The subsidiary allocated the funds raised under this program to grant a loan to its parent company.

in accordance with IFRS EU (in PLN million)

Domestic market bond issues

During the reporting period, the Company had the ability to finance its own operations through two bond issue programs:

- The bond issue program for the amount of PLN 5 billion directed towards investors from the Polish capital market. In 2013, the first non-public issuance of 5-year bonds under this program took place, the coupon bearer bonds with a variable interest rate. The nominal value of the issue was PLN 1 billion and the maturity of the bonds is June 27, 2018. On August 29, 2013, the bonds were floated in the Alternative Trading System organised by BondSpot S.A. and Giełda Papierów Wartościowych w Warszawie S.A. (Warsaw Stock Exchange). The Company bought back the bonds on time.
- A bond issue program for the amount of PLN 5 billion dedicated to entities within PGE Group.

Cash pooling liabilities

The launch of real cash pooling is described in note 17.1.1 of these financial statements.

Currency position and interest rates

As at December 31, 2018

Currency	Reference rate	Value in currency	Value in PLN	Final repayment deadline
PLN	Variable	1,171	1,171	April 2019
	Variable	1,001	1,001	December 2027
	Variable	500	500	December 2028
	Variable	3,648	3,648	September 2023
	Variable	1,446	1,446	5-year programme
	Variable	568	568	July 2021
TOTAL PLN		**8,334**	**8,334**	
EUR	Fixed	517	2,213	June 2019
	Fixed	145	625	July 2029
TOTAL EUR		**662**	**2.838**	
TOTAL LOANS, BORROWINGS, BONDS, CASH POOLING			**11,172**	

As at December 31, 2017

Currency	Reference rate	Value in currency	Value in PLN	Final repayment deadline
PLN	Variable	3,647	3,647	September 2023
	Variable	1,001	1,001	December 2027
	Variable	1,000	1,000	indefinite program, maturity date of the tranche issued- June 2018
	Variable	500	500	December 2028
	Variable	576	576	5-year programme
	Fixed	-	-	
TOTAL PLN		**6,724**	**6,724**	
EUR	Variable	-	-	
	Fixed	515	2,147	June 2019
	Fixed	145	607	July 2029
TOTAL EUR		**660**	**2,754**	
TOTAL LOANS, BORROWINGS, BONDS, CASH POOLING			**9,478**	

The following table illustrates changes in interest-bearing debt in the years ended December 31, 2018 and 2017:

	Year ended December 31, 2018	Year ended December 31, 2017
AS AT JANUARY 1	**9,478**	**9,558**
CHANGE IN OVERDRAFTS	**568**	**-**
CHANGE IN CASH POOLING LIABILITIES	**870**	**103**
CHANGE IN OTHER LOANS, BORROWINGS AND BONDS, including:	**256**	**(183)**
Drawn loans and borrowings / issued bonds	1,870	-
Accrued interest	213	215
Repayment of loans and borrowings / redemption of bonds	(1,700)	(17)
Interest repayments	(212)	(215)
Exchange differences	85	(166)
AS AT DECEMBER 31	**11,172**	**9,478**

in accordance with IFRS EU (in PLN million)

17.1.4 Other financial liabilities measured at amortised cost

ACCOUNTING RULES

Liabilities

Liabilities are the Company's present obligations, arising from past events, settlement of which will cause an outflow of resources embodying economic benefits from the Company.

The Company divides liabilities into the following categories:

- financial liabilities at fair value through profit or loss,
- other financial liabilities measured at subsequent reporting dates at amortized cost,
- non-financial liabilities.

When the effect of the time value of money is significant, liabilities are presented at discounted value.

	As at December 31, 2018		As at December 31, 2017	
	Non-current	Current	Non-current	Current
Trade liabilities	-	689	-	673
Other	21	151	23	9
TOTAL OTHER FINANCIAL LIABILITIES	**21**	**840**	**23**	**682**

Trade liabilities

Trade liabilities relate mainly to purchase of electricity and gas.

Other financial liabilities

In the item Other, the Company mainly presents settlements with exchanges, related mostly to the purchase of CO_2 emission allowances and future payments to the Polish National Foundation.

17.2 Fair value of financial instruments

The book value of financial receivables and payables measured at amortised cost, except for loans from PGE Sweden AB (publ), constitutes a rational approximation of their fair value.

In the case of loans received from PGE Sweden AB (publ), PGE S.A. estimates their fair value at PLN 2,915 million (as compared to PLN 2,838 million of the carrying amount). The fair value was determined using the estimated credit risk of PGE S.A. It is Level 2 of fair value hierarchy.

17.3 Fair value hierarchy

Derivatives

The Company measures derivatives at fair value using valuation models for financial instruments based on publicly available exchange rates, interest rates, discount curves for currencies (valid also for commodities, prices of which are denominated in those currencies) derived from active markets. The fair value of derivatives is determined based on discounted future cash flows from transactions, calculated on the difference between the forward rate and transaction price. Forward exchange rates are not modelled as separate risk factors, but are derived from the spot rate and appropriate forward interest rate for foreign currencies in relation to PLN.

In the category of financial assets and financial liabilities at fair value through profit or loss, the Company presents financial instruments related to greenhouse gases emission rights – currency and commodity forwards and IRS hedging transaction changing variable interest rate in PLN to fixed interest rate in PLN (Level 2).

In addition, the Company presents CCIRS derivative that hedges foreign exchange rate and interest rate (Level 2).

FAIR VALUE HIERARCHY	As at December 31, 2018		As at December 31, 2017	
	Level 1	Level 2	Level 1	Level 2
Currency forwards	-	4	-	-
Commodity forwards	-	-	-	54
Measurement of CCIRS transactions	-	113	-	44
Futures	-	147	-	-
Measurement of IRS transactions	-	4	-	98
Options	-	12	-	24
Fund participation units	-	66	-	50
Financial assets	**-**	**346**	**-**	**270**
Currency forwards	-	48	-	19
Commodity forwards	-	116	-	-
Measurement of IRS transactions	-	24	-	13
Financial liabilities	**-**	**188**	**-**	**32**

During the current and comparative reporting periods, there have been no transfers of financial instruments between the first and the second level of fair value hierarchy.

in accordance with IFRS EU (in PLN million)

Financial instruments not quoted on active markets, for which fair value cannot be estimated reliably

PGE S.A. holds significant amount of shares in entities not quoted on active markets. For shares in entities that are not quoted on the stock exchange, there is no active market nor the possibility to use measurement techniques that will give reliable values. These assets are measured at purchase prices less impairment.

17.4 Collateral for repayment of receivables and liabilities

The Company uses a variety of collateral and its combinations. The most frequently used are execution statements. Additionally, the Company uses the power of attorney to the bank accounts and assignment of receivables. As a rule, there is no collateral on subsidiaries' liabilities towards PGE S.A.

As at December 31, 2018 and December 31, 2017, Company's assets are not encumbered as collateral for the repayment of the Company's liabilities and contingent liabilities.

17.5 Statement of comprehensive income

The table below presents the combined effect of the various categories of the financial instruments on the financial income and financial expenses.

Year ended December 31, 2018	Hedging derivatives	Derivatives measured at fair value through profit or loss	Cash and cash equivalents	Shares and other equity instruments within the Group	Shares and other equity instruments outside the Group	Loans and receivables	Financial liabilities at amortised cost	TOTAL
Dividends	-	-	-	45	1	-	-	**46**
Interest income / (expenses)	9	-	14	-	-	414	(337)	**100**
Exchange differences	85	-	(2)	-	-	1	(84)	**-**
Revaluation of financial instruments/Reversal of impairment allowances for expected credit losses	-	161	-	-	-	-	-	**161**
Revaluation of financial instruments/Recognition of impairment allowances for expected credit losses	(1)	(203)	-	(799)	-	-	-	**(1,003)**
Gain on disposal of investment	-	-	-	-	1	-	-	**1**
TOTAL PROFIT/ (LOSS)	**93**	**(42)**	**12**	**(754)**	**2**	**415**	**(421)**	**(695)**

YEAR ENDED DECEMBER 31, 2017	Hedging derivatives	Derivatives measured at fair value through profit or loss	Cash and cash equivalents	Shares in subsidiaries	Loans and receivables	Financial liabilities at amortised cost	TOTAL
Dividends	-	-	-	2,872	-	-	**2,872**
Interest income / (expenses)	(4)	-	62	-	306	(322)	**42**
Exchange differences	(166)	-	(4)	-	(2)	168	**(4)**
Revaluation of financial instruments/Reversal of impairment allowances for expected credit losses	-	63	-	1,289	-	-	**1,352**
Revaluation of financial instruments/Recognition of impairment allowances for expected credit losses	(1)	-	-	(164)	(88)	-	**(253)**
TOTAL PROFIT/ (LOSS)	**(171)**	**63**	**58**	**3,997**	**216**	**(154)**	**4,009**

The recognition and reversal of impairment allowances for expected credit losses concerning shares in the current and comparative reporting period are described no notes 4.3 and 8.1 to these financial statements.

18. Objectives and principles of financial risk management

The main goal of financial risk management at PGE Group is to support the process of creating value for shareholders and to implement business strategies of the Group through maintaining the financial risk at the level acceptable for the Group management. Responsibility for managing financial risk lies with the Management Board of PGE S.A. The Management Board specifies risk appetite, understood as an acceptable level of deterioration of PGE Group's financial results, taking into consideration its current and planned economic and financial situation. The Management Board also decided on the allocation of risk appetite to specific business areas.

The organisation of the financial risk management function is based on the principle of independence of an entity responsible for measurement and control of risk vs business entities (risk owners) responsible for taking and managing the risk on an ongoing basis. Risk reports are submitted directly to the Risk Committee, Audit Committee and the Management Board of PGE S.A.

The Company has a Risk Committee that exercises oversight of the financial and corporate risk management process at PGE Group. The Risk Committee monitors exposure levels, sets limits for significant financial risks, accepts methodologies in financial risk resulting from trade and finance activities, permits expansions of activities in new business areas and makes key decisions regarding risk management.

Financial risk is managed at Group level as a whole, with the Company having a leading role, being a centre of competence in this area, and managing the process in an integrated manner. Exposures to risk generated by business areas are examined on a comprehensive basis, taking into account interdependencies, the possibility of using natural hedging effects and the overall impact on PGE Group's risk profile and financial situation.

The financial risk management model includes:

- collection and consolidation of data on exposure to particular categories of financial risk,
- calculation of Value-at-Risk and Profit-at-Risk for specific risk factors and overall for all risk factors;
- management of the PGE Group's consolidated exposure in relation to capital at risk and risk limits established based on it (including the identification and implementation of hedging strategies).

In key areas of financial risk, the Company has implemented internal regulations for managing these risks.

The Company is exposed to a variety of financial risks:

- market risk (commodity risk, interest rate risk, currency risk);
- liquidity risk;
- credit risk.

The Company's exposure to specific financial risks depends on the scope of activities in commodity and financial markets.

18.1 Market risk

Market risk covers commodity risk, interest rate risk, currency risk.

The main objective of managing market risk is to retain a level of risk resulting from trade and finance activities at an acceptable level and to support business strategy and maximisation of the Group's value for shareholders.

The Company's procedures for managing specific market risk categories in trade and finance activities specify the following:

- objective, scope and rules for managing risk;
- responsibility for managing risk;
- management and operational processes within risk management in trade activities on electricity markets and electric product markets and as regards finance activities;
- ways of identifying sources of exposure to risk;
- methods for measuring and monitoring exposures to risk;

The Company's market risk management rules also specify ways to set risk appetite, limit exposures to market risk based on Profit-at-Risk and Value-at-Risk and mechanisms for limiting risk when limits are exceeded

18.1.1 Commodity risk

Commodity risk is related to the possibility that financial results deteriorate as a result of changes in commodity prices.
The Company's exposure to commodity risk mainly concerns the following commodity markets:

- electricity
- CO_2 emission allowances
- natural gas

The Company has a strategy for hedging key exposures in trading electricity and related products over a 5-year horizon. The level of hedging for an open position is set taking into account risk appetite, results of monitoring the risk of electricity and related product prices, liquidity of specific markets as well as the financial situation of the Company and the Group and the Group's strategic objectives

18.1.2 Interest rate risk

Interest rate risk is related to the possibility that financial results deteriorate as a result of changes in interest rates.
The Company is exposed to interest rate risk as a result of financing their operating and investment activities with interest bearing indebtedness at variable interest rates, mainly in the form of credit facilities, loans and bonds issued in domestic or foreign currency and through investments in financial assets at variable interest rates.
The Company controls interest rate risk through a system of limits relating to the maximum potential loss due to changes in interest rates. The interest rate risk measure is based on the Value at Risk methodology.
Moreover, the Company sets out hedging strategies for interest rate risk using hedging ratios subject to approval by PGE S.A.'s Risk Committee and Management Board. The hedging strategy and level of interest rate risk are subject to monitoring and are regularly reported to the Risk Committee.
The Company executes derivative transactions concerning instruments that are based on interest rates only in order to hedge identified risk exposures. Regulations applicable to PGE Group do not permit derivative transactions based on interest rates for the purposes of speculative transactions that would be intended to generate additional earnings resulting from changes in interest rates while exposing the Company to a risk of potential losses.
Bonds issued in the amount of PLN 1 billion under the Bonds issue program of PLN 5 billion that was described in note 17.1.3 of these financial statements, are interest-bearing bonds at a variable rate in PLN. Payments relating to those bonds are hedged by IRS transactions, described in note 17.1.2.
Loans received from a subsidiary PGE Sweden AB (publ) are interest bearing loans at a fixed interest rate in EUR. Payments for these loans are hedged by CCIRS transactions described in note 17.1.2.

in accordance with IFRS EU (in PLN million)

In addition, the Company holds long-term bank credit of PLN 1.5 billion under the terms of Credit Agreement signed on December 17, 2014 with Bank Gospodarstwa Krajowego and syndicated loan (term loan facility tranche) of PLN 3.63 billion under the terms of Credit Agreement signed on September 7, 2015. These credit facilities are based on variable interest rates in PLN. Payments related to bank credits are hedged with IRS hedge instruments, described in note 17.1.2.
The Company's exposure to interest rate risk and concentration of this risk by currency:

		Type of interest	As at December 31, 2018	As at December 31, 2017
Derivatives - assets exposed to interest rate risk	PLN	Fixed	-	-
		Variable	16	122
	EUR	Fixed	-	-
		Variable	264	98
Loans granted, bonds acquired and cash exposed to interest rate risk	PLN	Fixed	15,989	15,185
		Variable	1,381	311
	EUR	Fixed	185	55
		Variable	-	-
Derivatives – liabilities, exposed to interest rate risk	PLN	Fixed	-	-
		Variable	(24)	(13)
	EUR	Fixed	-	-
		Variable	(164)	(19)
Loans received, bonds issued exposed to interest rate risk	PLN	Fixed	-	-
		Variable	(8,334)	(6,724)
	EUR	Fixed	(2,838)	(2,753)
		Variable	-	-
Net exposure	**PLN**	**Fixed**	**15,989**	**15,185**
		Variable	**(6,961)**	**(6,304)**
	EUR	**Fixed**	**(2,653)**	**(2,698)**
		Variable	**100**	**79**

Interest rates on variable interest rate financial instruments are updated in periods shorter than one year. Interest rates on fixed interest rate financial instruments are fixed throughout the whole period until maturity of these instruments.

in accordance with IFRS EU (in PLN million)

18.1.3 Currency risk

Currency risk is related to the possibility that financial results deteriorate as a result of changes in currency prices.

The main sources of exposure to currency risk are presented below:

- loans and borrowings denominated in foreign currencies;
- sales of electricity denominated in foreign currencies (export);
- sales and purchases of CO_2 emission allowances denominated in or indexed to foreign currencies;
- financial assets with deposit characteristics denominated in foreign currencies,
- foreign subsidiaries,
- other operating flows denominated in or indexed to foreign currencies

The Company controls currency risk through a system of limits relating to the maximum potential loss due to changes in currencies. The currency risk measure is based on the Value at Risk methodology.

Moreover, the Company sets out hedging strategies for currency risk using hedging ratios subject to approval by the Company's Risk Committee and Management Board. The hedging strategy and level of currency risk are subject to monitoring and are regularly reported to the Risk Committee.

The Company executes derivative transactions concerning instruments that are based on currency only in order to hedge identified risk exposures. Regulations applicable to PGE Group do not permit derivative transactions based on currencies for the purposes of speculative transactions that would be intended to generate additional earnings resulting from changes in currencies while exposing the Company to a risk of potential losses.

The Company's exposure to currency risk broken down into classes of financial instruments:

	Total value in financial statements in PLN	CURRENCY POSITION AT DECEMBER 31, 2018	
		EUR	PLN
FINANCIAL ASSETS			
Trade and other financial receivables, including:	18,305	47	203
Trade receivables	*844*	*11*	*49*
Loans granted	*174*	*3*	*13*
Other financial receivables	*141*	*33*	*141*
Cash and cash equivalents	235	40	172
Derivatives, including:	346	868	3,732
Carried at fair value through profit or loss	*151*	*169*	*726*
CCIRS hedges	*113*	*699*	*3,006*
FINANCIAL LIABILITIES			
Loans, borrowings, bonds, including:	(11,172)	(660)	(2,838)
Loans received	*(2,838)*	*(660)*	*(2,838)*
Trade and other payables, including:	(861)	(34)	(145)
Trade liabilities	*(689)*	*(1)*	*(4)*
Other financial liabilities	*(172)*	*(33)*	*(141)*
Derivatives measured at fair value through profit or loss	(188)	(77)	(331)
NET CURRENCY POSITION		**184**	**793**

The book value of derivatives constitutes their fair value measurement. The value of exposure to currency risk for forwards constitutes their nominal value in currency. The value of exposure to risk currency for CCIRS constitutes a value in the currency of discounted cash flows in the currency leg.

in accordance with IFRS EU (in PLN million)

	Total value in financial statements in PLN	CURRENCY POSITION AT DECEMBER 31, 2017	
		EUR	PLN
FINANCIAL ASSETS			
Trade and other financial receivables, including:	14,476	4	15
Trade receivables	*758*	*1*	*3*
Loans granted	*928*	*3*	*12*
Cash and cash equivalents	1,832	10	41
Derivatives, including:	270	724	3,020
Carried at fair value through profit or loss	*54*	*13*	*54*
CCIRS hedges	*44*	*711*	*2,966*
FINANCIAL LIABILITIES			
Loans, borrowings, bonds, including:	(9,478)	(660)	(2,754)
Loans received	*(2,754)*	*(660)*	*(2,754)*
Trade and other payables, including:	(705)	(1)	(2)
Trade liabilities	*(673)*	*(1)*	*(2)*
Derivatives measured at fair value through profit or loss	(32)	(193)	(805)
NET CURRENCY POSITION		**(116)**	**(485)**

The book value of derivatives constitutes their fair value measurement. The value of exposure to currency risk for forwards constitutes their nominal value in currency. The value of exposure to risk currency for CCIRS constitutes a value in the currency of discounted cash flows in the currency leg.

18.2 Liquidity risk

Liquidity risk concerns a situation in which the company is unable to meet its liabilities (current or non-current) when they become due.

The main objective of liquidity risk management at PGE Group is to ensure and maintain the companies' ability to meet their existing and future financial liabilities, taking into account the cost to obtain liquidity. Liquidity risk management at PGE Group involves planning and monitoring short- and long-term cash flows from operating, investing and financing activities and taking action intended to secure funds for the activities of PGE S.A. and its subsidiaries, while limiting the cost of these actions.

Periodic planning and monitoring of liquidity makes it possible to secure funds for any liquidity gaps by allocating funds among PGE Group companies (cash pooling) as well as using external financing, including overdrafts.

Liquidity risk management in the long term allows PGE Group to define its borrowing capacity and supports decisions regarding the financing of long-term investments.

PGE Group has a central financing model in which, as a rule, agreements relating to external financing are executed by PGE S.A. PGE Group subsidiaries use various sources of intra-group financing such as loans, bonds, bank account consolidation agreements and real cash pooling agreements.

The Company has an active policy of investing free cash. The Company monitors its financial surpluses and forecasts future cash flows and then on this basis implements an investment strategy for its free cash.

In the case of cash shortages, the Company uses the following financing sources:

- overdrafts, term loans, working capital loans;
- bank accounts consolidation agreements (real cash-pooling);
- bond issues addressed to external investors;
- bonds issues addressed to PGE Group subsidiaries.

in accordance with IFRS EU (in PLN million)

Maturities of financial liabilities based on contractual non-discounted payments:

As at December 31, 2018	Carrying amount	Total payments	Under 3 months	From 3 to 12 months	From 1 year to 5 years	Over 5 years
Bank credit	**6,888**	**7,456**	1,783	87	4,717	869
Loans received	**2,838**	**3,061**	10	2,241	77	733
Cash pooling liabilities	**1,446**	**1,446**	1,446	-	-	-
Trade and other financial liabilities measured at amortised cost	**861**	**861**	691	149	21	-
Derivatives measured at fair value through profit or loss	**188**	**188**	5	10	173	-
TOTAL	**12,221**	**13,012**	**3,935**	**2,487**	**4,988**	**1,602**

As at December 31, 2017	Carrying amount	Total payments	Under 3 months	From 3 to 12 months	From 1 year to 5 years	Over 5 years
Bank credit	**5,148**	**5,849**	43	87	3,157	2,562
Loans received	**2,754**	**3,027**	9	50	2,239	729
Bonds issued	**1,000**	**1,013**	-	1,013	-	-
Cash pooling liabilities	**576**	**576**	576	-	-	-
Trade and other financial liabilities measured at amortised cost	**705**	**710**	678	-	32	-
Derivatives measured at fair value through profit or loss	**32**	**32**	1	13	22	(4)
TOTAL	**10,215**	**11,207**	**1,307**	**1,163**	**5,450**	**3,287**

18.3 Credit risk

Credit risk is connected with a potential credit event that can occur, such as insolvency of a customer, partial payment of a receivable, significant delay in receivable payment or other breaches of contract conditions (in particular the lack of delivery and acceptance of the goods as agreed in the contract and the possible non-payment for damages and contractual penalties).

The Company is exposed to credit risk arising in the following areas:

- Basic activities – the credit risk results from, among others, purchases and sales of electricity, energy origin rights, gas, hard coal and CO_2 emission allowances. This relates primarily to the possibility of a default of the other party of transaction, if fair value of the transaction is positive from the point of view of the Company;
- Investing free cash – the credit risk results from investing free cash of PGE S.A. in securities bearing credit risk, i.e. financial instruments other than those issued by the State Treasury.

Maximum credit risk exposure resulting from financial assets is equal to the carrying value of these items.

	Year ended December 31, 2018	Year ended December 31, 2017
Trade receivables	844	758
Loans and receivables	17,462	13,718
Cash and cash equivalents	235	1,832
Derivatives - assets	346	270
MAXIMUM EXPOSURE TO CREDIT RISK	**18,887**	**16,578**

In addition, in accordance with IFRS 9, value exposed to credit risk constitute sureties to the bank payment guarantee issued for PGE Górnictwo i Energetyka Konwencjonalna S.A. at the total value of PLN 218 million at the reporting date (PLN 391 million in the corresponding period).

in accordance with IFRS EU (in PLN million)

18.3.1 Trade and other financial receivables

Trade receivables typically have a 2-3-week payment deadline. In 2018, received payment for receivables on average after 26 days. Trade receivables relate mainly to receivables for energy sold. According to the management, due to current control over trade receivables, there is no additional significant credit risk that would exceed the level reflected by impairment on receivables.

The Company reduces and controls the credit risk related to trade transactions. In the case of trade transactions which due to high value may generate substantial loss in case of failure of business partner to comply with the agreement, the assessment of contractor is carried out before the transaction is conducted, taking into account contractor's financial analysis, its credit history and other factors. Based on the assessment, an internal rating is recognised or the Company uses a rating determined by an independent reputable agency. A limit for the contractor is set based on the rating. Entering into contracts that would increase exposure above the limit, requires in principle the collateral in line with rules pertaining to credit risk management. The level of used limit is regularly monitored and if it is substantially exceeded, units responsible for contractor's risk are obliged to undertake measures to eliminate them. The Company regularly monitors the payment of receivables and uses a system for early recovery. It also cooperates with credit bureaus.

Credit risk relating to trade receivables by geographical region is presented in the table below:

	DECEMBER 31, 2018		DECEMBER 31, 2017	
	Receivables balance	% share	Receivables balance	% share
Poland	795	94.2%	688	90.8%
Netherlands	-	-	59	7.8%
Germany	-	-	3	0.4%
Great Britain	49	5.8%	3	0.4%
Other	-	-	5	0.6%
TOTAL	**844**	**100.0%**	**758**	**100%**

The majority of sales transactions and trade receivables balances relate to related parties within the PGE Group, as well as large Polish entities from the electricity market. Information on transactions with related parties is presented in note 24 of these financial statements.

Ageing of receivables and impairment for expected credit losses

Certain financial assets were covered by impairment allowances for future credit losses as of December 31, 2018.

The change in allowances accounts for these classes of financial instruments is presented in the table below:

2018	Trade receivables	Loans granted	Cash pooling receivables	Bonds acquired	Other financial receivables
Impairment allowance for expected credit losses as at January 1	**(3)**	**-**	**-**	**(386)**	**(25)**
Recognition of impairment losses	(18)	-	-	-	-
Impairment allowance for expected credit losses as at December 31	**(21)**	**-**	**-**	**(386)**	**(25)**
Value of the item before impairment	**865**	**2,964**	**1,204**	**13,539**	**166**
Net value (carrying amount)	**844**	**2,964**	**1,204**	**13,153**	**141**

in accordance with IFRS EU (in PLN million)

2017	Trade receivables	Loans granted	Cash pooling receivables	Bonds acquired	Other financial receivables
Impairment allowance for expected credit losses as at January 1	**(3)**	**-**	**-**	**(297)**	**(25)**
Recognition of impairment losses	-	-	-	(89)	-
Impairment allowance for expected credit losses as at December 31	**(3)**	**-**	**-**	**(386)**	**(25)**
Value of the item before impairment	**761**	**2,542**	**134**	**11,428**	**25**
Net value (carrying amount)	**758**	**2,542**	**134**	**11,042**	**-**

Trade and other receivables and other loans and receivables

	DECEMBER 31, 2018			DECEMBER 31, 2017		
	Gross value	Impairment	Net carrying amount	Gross value	Impairment	Net carrying amount
Receivables before due date	**18,648**	**(389)**	**18,259**	**14,844**	**(389)**	**14,445**
Past due <30 days	*58*	*(12)*	*46*	*21*	*-*	*21*
Past due 30-90 days	*6*	*(6)*	-	-	-	-
Past due 90-180 days	*1*	-	**1**	-	-	-
Past due 180-360 days	-	-	-	-	-	-
Past due >360 days	*26*	*(26)*	-	*25*	*(25)*	-
RECEIVABLES PAST DUE, TOTAL	**91**	**(44)**	**47**	**46**	**(25)**	**21**
TOTAL LOANS AND RECEIVABLES	**18,739**	**(433)**	**18,306**	**14,890**	**(414)**	**14,476**

18.3.2 Deposits, cash and cash equivalents

The Company manages credit risk related to cash and cash equivalents by diversification of banks in which surpluses of cash are allocated. All entities with which the Company concludes deposit transactions with operate in the financial sector. These can only be banks registered in Poland or divisions of foreign banks with high investment level ratings, adequate indicator of solvency and equity as well as strong, stable market position.

18.3.3 Derivatives

All entities with which the Company concludes derivative transactions with operate in the financial sector. These are banks with investment ratings, adequate equity and strong, stable market position. As at the reporting date, the Company was party to the derivative transactions, described in detail in note 17.1.2 to these financial statements.

18.3.4 Guarantees and sureties issued

Guarantees and sureties issued by the Company are presented in note 20 to these financial statements.

18.4 Market (financial) risk - sensitivity analysis

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

- Interest rate risk
- Currency risk

Currently, the Company is exposed mainly to currency risk related to foreign exchange rates between EUR/PLN. Furthermore, the Company is exposed to interest rate risk related to referential interest rates of PLN. The Company uses a scenario analysis for the purpose of analysing sensitivity to changes of market risk factors. The Company uses experts' scripts reflecting the subjective opinion on the Company in relation to future fluctuations of individual market risk factors.

The scenario analysis presented in this point is intended to analyse the influence of changes in market risk factors on the financial results of the Company. Only those items that can be defined as financial instruments are subject to the analysis of interest and currency risk.

In sensitivity analysis related to interest rate risk, the Company applies parallel shift of interest rate curve related to a potential possible change of referential interest rates during the following year.

In case of sensitivity analysis of interest rates' fluctuations, the effect of risk factors' changes could be recorded in the statement of comprehensive income as income or expenses or as revaluation of financial instruments measured at fair value.

The sensitivity analysis related to all types of market risks the Company is exposed to as at the reporting date, indicating the potential influence of changes of individual risk factors by class of financial assets and liabilities on profit before tax is presented below.

in accordance with IFRS EU (in PLN million)

Sensitivity analysis for currency risk

The table below presents the sensitivity of profit before tax and equity to reasonably possible changes in foreign currency exchange rates, under the assumption of stability of other risk factors for these classes of financial instruments exposed to currency risk.

FINANCIAL INSTRUMENTS BY CLASS	SENSITIVITY ANALYSIS FOR CURRENCY RISK AS AT DECEMBER 31, 2018			
	Carrying amount in PLN	Value at risk in PLN	EUR/PLN Impact on financial result / equity	
			+10%	-10%
Trade and other financial receivables	18,306	203	20	(20)
Cash and cash equivalents	235	172	17	(17)
Derivatives - assets	151	726	72	(72)
CCIRS hedges	113	3,006	283	(283)
Loans, borrowings, bonds	(11,172)	(2,838)	(284)	284
Trade and other financial payables	(861)	(145)	(15)	15
Derivatives - liabilities	(188)	(331)	(33)	33
Impact on financial result			**60**	**(60)**
CCIRS hedges	113	3,006	18	(18)
Impact on revaluation reserve			**18**	**(18)**

FINANCIAL INSTRUMENTS BY CLASS	SENSITIVITY ANALYSIS FOR CURRENCY RISK AS AT DECEMBER 31, 2017			
	Carrying amount in PLN	Value at risk in PLN	EUR/PLN Impact on financial result / equity	
			+10%	-10%
Trade and other financial receivables	14,476	15	2	(2)
Cash and cash equivalents	1,832	41	4	(4)
Derivatives - assets	54	54	5	(5)
CCIRS hedges	44	2,966	274	(274)
Loans, borrowings, bonds	(9,478)	(2,753)	(275)	275
Trade and other financial payables	(705)	(2)	-	-
Derivatives - liabilities	(32)	(805)	(81)	81
Impact on financial result			**(71)**	**71**
CCIRS hedges	44	2,966	22	(22)
Impact on revaluation reserve			**22**	**(22)**

in accordance with IFRS EU (in PLN million)

Sensitivity analysis for interest rate risk

The table below presents the sensitivity of profit before tax and equity to reasonably possible changes in interest rates, under the assumption of stability of other risk factors for these classes of financial instruments that are exposed to interest rate risk:

FINANCIAL ASSETS AND LIABILITIES	SENSITIVITY ANALYSIS FOR INTEREST RATE RISK AS AT DECEMBER 31, 2018					
	Carrying amount in PLN	Value at risk in PLN	WIBOR Impact on financial result / equity		EURIBOR Impact on financial result / equity	
			+50bp	–50bp	+25bp	–25bp
Trade and other receivables	18,306	1,381	7	(7)	-	-
Derivatives - assets	346	163	1	(1)	-	-
Loans, borrowings, bonds, cash pooling	(11,172)	(8,334)	(42)	42	-	-
Derivatives - liabilities	(188)	(48)	-	-	-	-
Impact on financial result			**(34)**	**34**	**-**	**-**
CCIRS hedges	113	113	35	(36)	(20)	21
IRS hedges - assets	4	4	24	(24)	-	-
IRS hedges - liabilities	(24)	(24)	82	(82)	-	-
Impact on revaluation reserve			**141**	**(142)**	**(20)**	**21**

Value of derivatives exposed to interest rate risk is fair value of those instruments (carrying amount). Sensitivity analysis for CCIRS and IRS derivatives was carried out using the valuation change due to the shift of interest rates curves for particular currency.

FINANCIAL ASSETS AND LIABILITIES	SENSITIVITY ANALYSIS FOR INTEREST RATE RISK AS AT DECEMBER 31, 2017					
	Carrying amount in PLN	Value at risk in PLN	WIBOR Impact on financial result / equity		EURIBOR Impact on financial result / equity	
			+50bp	–50bp	+25bp	–25bp
Trade and other receivables	14,476	311	2	(2)	-	-
Derivatives - assets	270	78	-	-	-	-
Loans, borrowings, bonds, cash pooling	(9,478)	(6,724)	(34)	34	-	-
Derivatives - liabilities	(32)	(27)	-	-	-	-
Impact on financial result			**(32)**	**32**	**-**	**-**
CCIRS hedges	44	44	46	(48)	(27)	27
IRS hedges - assets	98	98	109	(113)	-	-
IRS hedges - liabilities	(5)	(5)	(12)	16	-	-
Impact on revaluation reserve			**143**	**(145)**	**(27)**	**27**

Value of derivatives exposed to interest rate risk is fair value of those instruments (carrying amount). Sensitivity analysis for CCIRS and IRS derivatives was carried out using the valuation change due to the shift of interest rates curves for particular currency.

18.5 Hedge accounting

ACCOUNTING RULES

Hedge accounting

Changes in fair value of derivative financial instruments designated as cash flow hedges CCIRS (Cross Currency Interest Rate Swap) and IRS (Interest Rate Swap) are recognised in hedging reserve in the portion determined to be an effective hedge, while the ineffective portion of the hedge is recognised in profit or loss.

The accumulated changes in fair value of hedging instrument, previously recognised in hedging reserve are transferred to profit or loss in the period or periods in which the hedged item affects profit or loss. Alternatively, if the hedge of a planned transaction results in the recognition of non-financial assets or non-financial liabilities, the Company excludes the amount from equity and includes it in the initial cost or other carrying amount of a non-financial asset or liability.

In June and August 2014, in connection with loans received from PGE Sweden AB, PGE S.A. concluded CCIRS transactions, hedging both exchange rates. In these transactions, banks - counterparties pay PGE S.A. interest based on a fixed rate in EUR and PGE S.A. pays interest based on a fixed rate in PLN. The nominal value, payment of interest and repayment of nominal value in CCIRS transactions are correlated with the relevant conditions arising from loan agreements. To recognise these transactions, the Company uses hedge accounting.

Hedge accounting is also applied to the IRS transactions hedging interest rate due to the financial liabilities under credit agreements such as the Credit Agreement with a syndicate of banks signed on September 7, 2015 and Credit Agreement with Bank Gospodarstwa Krajowego signed on December 17, 2014. In these transactions, banks - counterparties pay PGE S.A. interest based on a fixed rate in EUR and PGE S.A. pays interest based on a fixed rate in PLN.

The impact of hedge accounting on the revaluation reserve is presented in note 13.3 to these financial statements.

in accordance with IFRS EU (in PLN million)

EXPLANATORY NOTES TO THE STATEMENT OF CASH FLOWS

19. Statement of cash flows

ACCOUNTING RULES

Statement of cash flows

The statement of cash flows is prepared using the indirect approach.

Presented below is the analysis of the most significant items of cash flow statement.

19.1 Cash flows from operating activities

Interest and dividends

	Year ended December 31, 2018	Year ended December 31, 2017
Dividend receivables	(46)	(2,872)
Interest on purchased bonds	(325)	(283)
Interest on issued bonds	12	25
Interest on loans received	61	60
Interest and commission on bank credit	141	137
Other	24	64
TOTAL INTEREST AND DIVIDENDS	**(133)**	**(2,869)**

(Profit) / loss on investing activities

	Year ended December 31, 2018	Year ended December 31, 2017
Matching cost measurement of derivatives	52	(114)
Recognition and reversal of impairment losses on financial assets	799	(1,036)
Other	(2)	6
Total (profit) / loss on investing activities	**849**	**(1,144)**

Change in receivables

	Year ended December 31, 2018	Year ended December 31, 2017
Change in trade and other receivables	(3,830)	(2,876)
Adjustment for changes in loans issued (including cash pooling)	1,492	1,950
Adjustment for changes in purchased bonds	2,110	2,992
Adjustment for deposits with maturities over 3 months	-	(2,299)
Other	-	-
TOTAL CHANGE IN LOANS AND RECEIVABLES	**(228)**	**(233)**

Change in liabilities, excluding loans and borrowings

	Year ended December 31, 2018	Year ended December 31, 2017
Change in trade and other financial payables	16	489
Change in other non-financial liabilities	167	(153)
Change in financial liabilities at fair value through profit or loss	-	27
Change in other financial liabilities	143	-
Adjustment for changes in tax liabilities due to share capital increase	-	110
Adjustment for change sin settlements in tax group	(148)	(7)
Other	(3)	-
TOTAL CHANGE IN LIABILITIES, EXCLUDING LOANS AND BORROWINGS	**175**	**466**

Change in other non-financial assets

	Year ended December 31, 2018	Year ended December 31, 2017
Change in other current assets	169	(140)
Adjustment for change sin settlements in tax group	(161)	158
Other	(1)	(1)
TOTAL CHANGE IN OTHER CURRENT ASSETS	**7**	**17**

19.2 Cash flows from investing activities

Purchase and redemption of bonds issued by PGE Group companies

PGE S.A. acquires bonds issued by entities belonging to PGE Group. Cash obtained from the issue of bonds is used for financing investments, repayment of financial liabilities as well as for financing current operations. Detailed description in note 17.1.1.

Sale of other financial assets

In 2017, the Company executed an agreement to sell 100% of shares in Exatel S.A. for PLN 368 million.

Purchase of subsidiaries

In 2017, the Company mainly purchased EDF's assets for PLN 4.227 million.

Release of deposits with maturity over 3 months

In 2017, the Company concluded deposits with maturity over 3 months in the total amount of PLN 2,340 million.

Dividends received

The total sum of dividends received consists mainly of dividends from PGE Obrót S.A. (PLN 28 million) and in the comparative period PLN 2,019 million from PGE GiEK S.A. and PLN 808 million from PGE Dystrybucja S.A.

Cash flows under cash pooling

As described in note 17.1.1, PGE S.A. serves as coordinator for PGE Group's cash pooling services. This means, among others, that certain entities settle with the Company and the Company settles with banks. In connection with the above, balances with related parties participating in cash pooling are reported in the Company's financial receivables and liabilities.

19.3 Cash flows from financing activities

Proceeds from credit facilities

In the present reporting period, the Company incurred credit facilities worth PLN 2,438 million in total.

Repayment of credit facilities, redemption of bonds

In the present reporting period, the Company bought back bonds worth PLN 1,000 million and repaid a revolving credit facility amounting to PLN 700 million.

in accordance with IFRS EU (in PLN million)

OTHER EXPLANATORY NOTES

20. Contingent liabilities and receivables. Legal claims

20.1 Contingent liabilities

	As at December 31, 2018	As at December 31, 2017
Bank guarantee liabilities	12,408	11,052
Other contingent liabilities	1	33
Total contingent liabilities	**12,409**	**11,085**

Guarantee for PGE Sweden AB (publ) liabilities

Due to establishment of the Eurobonds program in 2014, an agreement was concluded for the issue of guarantee by PGE S.A. for the liabilities of PGE Sweden AB (publ). The guarantee was granted to the amount of EUR 2,500 million (PLN 10,750 million) and will be valid until December 31, 2041. As at December 31, 2018, PGE Sweden AB (publ)'s liabilities due to bonds issued amounted to EUR 642 million (PLN 2,761 million), as at December 31, 2017 liabilities amounted to EUR 642 million (PLN 2,682 million).

Surety for PGE GiEK S.A.'s liabilities

In January 2014, the Company granted three sureties to the bank payment guarantee issued for PGE Górnictwo i Energetyka Konwencjonalna S.A. at the total value of PLN 218 million at the reporting date (PLN 391 million in the corresponding period). Granting sureties is related to the investment conducted by PGE GiEK S.A. relating to the construction of the new power units in Elektrownia Opole.

20.2 Other significant issues related to contingent liabilities

Standby commitments to ensure financing of new investments for PGE Group companies

Due to planned strategic investments in PGE Group, the Company committed to its subsidiaries, in the form of standby commitments, to ensure financing of the planned investments. The standby commitments relate to specific investments and may be used only for such purposes. As at the reporting date, the approximate value of future investment commitments related to these projects amounts to about PLN 2.6 billion. As at December 31, 2018 and December 31, 2017, the estimated value of the standby commitments amounts to approx. PLN 15 billion.

20.3 Other legal claims and disputes

Compensation for conversion of shares

Former shareholders of PGE Górnictwo i Energetyka S.A. are presenting to the courts motions to summon PGE S.A. to a conciliation hearing concerning payment of compensation for incorrect (in their opinion) determination of the exchange ratio of shares of PGE Górnictwo i Energetyka S.A. into shares of PGE S.A. during a consolidation process that took place in 2010. The total value of claims resulting from summons to a conciliation hearing directed by the former shareholders of PGE Górnictwo i Energetyka S.A. amounts to over PLN 10 million.

Regardless of the above, on November 12, 2014 Socrates Investment S.A. (an entity which purchased claims from former PGE Górnictwo i Energetyka S.A. shareholders) filed a lawsuit to impose a compensation in the total amount of over PLN 493 million (plus interest) for damages incurred in respect of incorrect (in their opinion) determination of the exchange ratio of shares in the merger of PGE Górnictwo i Energetyka S.A. and PGE S.A. The Company filed a response to the lawsuit. Currently the proceedings before the court of first instance are in progress. A hearing concerning appointment of an expert was held on November 20, 2018. The next court hearing has not been scheduled.

Moreover, a similar claim was raised by Pozwy sp. z o.o., a buyer of claims from the former shareholders of PGE Elektrownia Opole S.A. Through a lawsuit filed at the District Court in Warsaw against PGE GiEK S.A., PGE S.A. and PwC Polska sp. z o.o. ("Defendants"), Pozwy sp. z o.o. demanded from the Defendants, in solidum, or jointly damages for Pozwy sp. z o.o. totalling over PLN 260 million with interest for allegedly incorrect (in its opinion) determination of exchange ratio for PGE Elektrownia Opole S.A. shares for PGE Górnictwo i Energetyka Konwencjonalna S.A. shares in a merger of these companies. This lawsuit was delivered to PGE S.A. on March 9, 2017, and the deadline for responding to it was set by the court as July 9, 2017. The following companies: PGE S.A. and PGE GiEK S.A. submitted a response to the claim on July 8, 2017. On September 28, 2018, the District Court in Warsaw ruled in the first instance - the lawsuit by Pozwy sp. z o.o. against PGE S.A., PGE GiEK S.A. and PWC Polska sp. z o.o. was rejected. Pozwy sp. z o.o. appealed the District Court's ruling.

PGE Group companies do not recognise the claims being raised by Socrates Investment S.A., Pozwy sp. z o.o. and other shareholders requesting conciliatory settlements. According to PGE S.A., these claims are groundless and the entire consolidation process was conducted fairly and properly. The value of the shares, which were subject to the process of consolidation (merger), was established by an independent company PwC Polska sp. z o.o. Additionally, merger plans of the companies mentioned above, including the exchange ratios were examined for accuracy and reliability by an expert appointed by the registration court; no irregularities were found. Then, the court registered the mergers of the companies mentioned above.

The Company has not recognised provisions for these claims.

Claims for annulment of General Meeting resolutions

On March 15, 2017, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking annulment of resolution 4 of the Company's Extraordinary General Meeting held on September 5, 2016. The Company filed a response to the lawsuit.

Having examined the shareholder's claim at a closed-door hearing on October 11, 2017, the District Court in Warsaw ruled to refer the case for mediation.

PGE S.A. decided not to agree to mediation. On March 15, 2018, the District Court in Warsaw issued a judgement dismissing the shareholder's claim in its entirety. The ruling is final.

On January 29, 2019, PGE S.A. received a copy of a lawsuit filed to the District Court of Warsaw by one of its shareholders. In the lawsuit, the shareholder is seeking annulment of resolutions 7, 9 and 20 of the Company's Ordinary General Meeting held on July 19, 2018. On February 28, 2019 the Company submitted a response to the lawsuit.

21. Leases

21.1 Operating lease liabilities – the Company as a lessee

The Company executes tenancy and rental contracts, which in accordance with IAS 17 *Leases* meet the definition of operating lease contract. The Company uses rights of perpetual usufruct of land. Future minimum lease payments concerning irrevocable operating leases amount to PLN 67 million as at December 31, 2018, while lease payments recognised as costs in 2018 amounted to PLN 2 million.

21.2 Operating lease receivables – the Company as lessor

The Company executes tenancy contracts, mainly for office space, which in accordance with IAS 17 *Leases* meet the definition of operating lease. Future minimum lease payments concerning irrevocable operating leases amount to PLN 5 million as at December 31, 2018, while lease payments recognised as revenue in 2018 amounted to PLN 5 million.

22. Tax settlements

Tax obligations and rights are specified in the Constitution of the Republic of Poland, tax regulations and ratified international agreements. According to the tax ordinance, tax is defined as public, unpaid, obligatory and non-returnable cash liability toward the State Treasury, provincial or other regional authorities resulting from the tax regulation. Taking into account the subject criterion, current taxes in Poland can be divided into five groups: taxation of incomes, taxation of turnover, taxation of assets, taxation of activities and other, not classified elsewhere.

From the point of view of business entities, the most important is the taxation of incomes (corporate income tax), taxation of turnover (value added tax, excise tax) followed by taxation of assets (real estate tax and vehicle tax). Other payments classified as quasi – taxes must also be mentioned Among these there are social security charges.

Basic tax rates were as follows in 2018: corporate income tax rate – 19%, for smaller enterprises a 15% rate is possible; basic value added tax rate – 23%, reduced: 8%, 5%, 0%, furthermore some goods and products are subject to a VAT tax exemption.

The tax system in Poland is characterized by a significant changeability of tax regulations, their high complexity, high potential fees for commitment of a tax crime or violation. Tax settlements and other activity areas are conditioned by regulations (customs or currency controls) and can be subject to controls of respective authorities that are entitled to issue fines and penalties with penalty interest. Controls may cover tax settlements for the period of 5 years after the end of calendar year in which the tax was due.

Tax group

An agreement for a tax group named PGK PGE 2015, for which PGE S.A. is the representative, was signed on September 18, 2014, for a period of 25 years.

Companies included in the tax group must meet a number of requirements covering: appropriate level of equity, parent's stake in PGK companies of at least 75%, lack of capital ties between subsidiaries, no tax arrears, share in total revenue of at least 2% (counted at tax group level), and execution of transactions with related parties from outside the tax group only on market terms. Violating these requirements would mean the dissolution of the tax group and loss of its taxpayer status. When the tax group is dissolved, each of its member companies becomes an individual payer of corporate income tax.

Changes in corporate income tax in effect from January 1, 2018

As a result of changes in legislation, starting from 2018 taxpayer revenue is divided into two sources: economic (operating) activities and capital gains. This means that each source of revenue will be settled separately and that companies may not offset losses incurred in one source using revenue from the other source. The capital gains source includes: dividends, income obtained as a result of mergers of de-mergers, in-kind contributions, share disposals, disposal of debt claims, income from property rights (authors' rights, licences) and income from securities.
The introduction of two income sources did not affect the Company's tax burden for 2018.

VAT split payment mechanism

Starting from July 1, 2018, a VAT split payment mechanism will be introduced. This solution is intended to seal off the tax system by separating VAT amounts from bank transfers being made by buyers of products and services and directing these to sellers' dedicated VAT accounts. Funds collected in these VAT accounts may only be used for VAT settlements concerning invoices received and VAT settlements with the tax office. Using split VAT payments is the buyer's right but not an obligation.

in accordance with IFRS EU (in PLN million)

PGE S.A. uses funds received from counterparties in VAT accounts to pay its liabilities that contain VAT. The level of funds in these VAT accounts at a given date depends mainly on how many of the Company's counterparties decide to use this mechanism and the relation between receivables and liabilities payment dates. According to the Company's estimates, the average level of cash in VAT accounts might be in the range of PLN 10-40 million. As at December 31, 2018, the cash balance in these VAT accounts totalled PLN 24 million.

23. Information on related parties

The State Treasury is the dominant shareholder of the PGE Group and as a result State Treasury companies are recognised as related entities. The Company closely monitors transactions with key State Treasury subsidiaries. The total value of transactions with such entities is presented in the table below in the column "other related parties".

Transactions with related entities are concluded based on market prices for provided goods, products and services or are based on the cost of manufacturing. Exceptions to this rule were:

- bonds issued by subsidiaries belonging to the tax group with interest rates below market rates, described in note 17.1.1 of these financial statements. From January 1, 2018 all transactions are on market terms,
- tax losses settlements within the tax group, described in notes 5.2 and 22 of these financial statements.

23.1 Transactions with related parties

Year ended December 31, 2018

	Subsidiaries	Other PGE Group related parties	Other related parties	Third parties	*TOTAL*
STATEMENT OF COMPREHENSIVE INCOME					
Revenue from sales	10,558	-	131	761	*11,450*
Other operating revenue / (expenses)	7	-	-	(35)	**(28)**
Financial income / (expenses)	(419)	1		(280)	**(698)**
Operating costs	8,245	-	255	2,373	**10,873**

Year ended December 31, 2017

	Subsidiaries	Other PGE Group related parties	Other related parties	Third parties	**TOTAL**
STATEMENT OF COMPREHENSIVE INCOME					
Revenue from sales	7,975	-	339	871	**9,185**
Other operating income / (expenses)	3	(2)	(34)	(4)	**(37)**
Financial income / (expenses)	4,236	(89)	-	(139)	**4,008**
Operating costs	7,156	-	295	1,156	**8,607**

The Company recognises revenues from sales to related parties in the PGE Group mainly related to sales of electricity, gas, energy origin rights and CO_2 emission allowances.

Financial income relates primarily to dividends and interest on bonds.

Operating costs relate to the value of sales of materials and goods.

The Company concludes significant transactions on the energy market via Towarowa Giełda Energii S.A. (Polish Power Exchange). Due to the fact that this entity only deals with the organization of trading, purchases and sales transacted through this entity are not recognised as transactions with related parties.

in accordance with IFRS EU (in PLN million)

23.2 Balances with related parties

As at December 31, 2018

ASSETS	Subsidiaries	Other PGE Group related parties	Other related parties	Third parties	TOTAL
Loans and receivables:	**18,262**	**-**	**10**	**34**	**18,306**
Bonds acquired	13,153	-	-		13,153
Trade receivables	800	-	10	34	844
Other loans and financial receivables	4,309	-	-	-	4,309
Shares in subsidiaries	**32,024**	**-**	**-**	**-**	**32,024**
Shares in subsidiaries, associates and jointly controlled entities	**-**	**101**	**-**	**-**	**101**
Derivatives - assets	**-**	**-**	**-**	**346**	**346**
Other current assets	**45**	**-**	**-**	**6**	**51**

As at December 31, 2017

ASSETS	Subsidiaries	Other PGE Group related parties	Other related parties	Third parties	TOTAL
Loans and receivables:	**14,348**	**-**	**24**	**104**	**14,476**
Bonds acquired	11,042	-	-	-	11,042
Trade receivables	630	-	24	104	758
Other loans and financial receivables	2,676	-	-	-	2,676
Shares in subsidiaries	**32,568**	**-**	**-**	**-**	**32,568**
Shares in subsidiaries, associates and jointly controlled entities	**-**	**84**	**-**	**-**	**84**
Derivatives - assets	**-**	**-**		**270**	**270**
Other current assets	**202**	**-**	**-**	**18**	**220**

As at December 31, 2018

	Subsidiaries	Other related parties	Third parties	TOTAL
LIABILITIES				
Derivatives - equity and liabilities	**-**	**-**	**188**	**188**
Financial liabilities measured at amortised cost:	**4,918**	**29**	**7,086**	**12,033**
Interest bearing loans and borrowings	*2,838*	-	*6,888*	*9,726*
Cash pooling liabilities	*1,446*	-	-	*1,446*
Trade liabilities	*634*	*29*	*26*	*689*
Other financial liabilities	-	-	172	172

As at December 31, 2017

	Subsidiaries	Other related parties	Third parties	TOTAL
LIABILITIES				
Derivatives - equity and liabilities	**-**	**-**	**32**	**32**
Financial liabilities measured at amortised cost:	**3,902**	**35**	**6,246**	**10,183**
Bonds issued	-	-	*1,000*	*1,000*
Interest bearing loans and borrowings	*2,753*	-	*5,149*	*7,902*
Cash pooling liabilities	*576*	-	-	*576*
Trade liabilities	*543*	*35*	*95*	*673*
Other financial liabilities	30	-	2	32

Standby commitments and sureties granted to PGE S.A.'s subsidiaries are described in note 20 of these financial statements.

23.3 Management remuneration

The key management personnel comprises the Management Board and the Supervisory Board.

PLN 000s	Year ended December 31, 2018	Year ended December 31, 2017
Short-term employee benefits (salaries and salary related costs)	8,543	8,046
Post-employment and termination benefits	-	168
TOTAL REMUNERATION OF KEY MANAGEMENT PERSONNEL	**8,543**	**8,214**

PLN 000s	Year ended December 31, 2018	Year ended December 31, 2017
Management Board	7,858	7,454
Supervisory Board	685	760
TOTAL REMUNERATION OF KEY MANAGEMENT PERSONNEL	**8,543**	**8,214**

Members of the Company's Management Board are employed on the basis of civil law contracts for management (so called management contracts). In note 4.2 Costs by nature and type, this remuneration is presented in the item other costs by type.

24. Remuneration for the entity authorised to audit financial statements

Ernst & Young Audyt Polska sp. z o.o. sp.k. is the entity authorised to audit the separate financial statements of PGE S.A. for 2018 and 2017 and consolidated financial statements of PGE Group for 2018 and 2017, based on an agreement executed on July 17, 2017.

KPMG Audyt sp. z o.o. sp.k. was the entity conducting a review of semi-annual separate financial statements and semi-annual consolidated financial statements for 2017, based on an agreement executed on November 4, 2014.

PLN 000s	Year ended December 31, 2018	Year ended December 31, 2017
Audit of annual separate financial statements and PGE Group's annual consolidated financial statements	381	390
Other assurance services, including review of semi-annual financial statements	142	79
Total amount of remuneration	**523**	**469**

25. Disclosures resulting from art. 44 of the Energy Law regarding specific types of activities

Article 44 of the Energy Law imposes an obligation on the energy companies to prepare regulatory financial statements with a balance sheet (statement of financial position) and the statement of profit or loss for the reporting periods separately for each type of business activity related to the following areas:

- supply of gaseous fuels or energy, including fixed costs, variable costs and revenues separately for the generation, transmission, distribution and trade in gaseous fuels or energy, gaseous fuel storage and liquefaction of natural gas or re-gasification of liquefied natural gas, also in relation to groups of recipients specified in the tariff;
- unrelated to the activities listed above.

25.1 Principles for allocation to different types of activities

The section below presents the types of activities referred to in art. 44 of the Energy Law and principles for allocation of revenues, expenses, assets and liabilities resulting from these types of activities.

25.1.1 Description of separate types of activities

The Company has identified the following types of activities pursuant to art. 44 point 1 of the Energy Law:

- trade in electricity
- trade in gaseous fuels
- other activities

25.1.2 Rules for allocation of revenues, expenses, assets and liabilities

Selected items in the statement of comprehensive income and statement of financial position are assigned by the Company to certain types of activities based on the accounting records:

- revenue from sale
- cost of goods sold
- selling and distribution costs
- general and administrative expenses
- financial income and financial expenses
- trade receivables
- trade payables
- derivatives
- inventories
- provisions, except for employee benefit provisions

Selected items in the statement of financial position are assigned by the Company to certain types of activities with the use of allocation keys:

- property, plant and equipment as well as intangible assets in proportion to the depreciation/amortisation costs,
- provisions for employee benefits and liabilities arising from wages, personal income tax and social insurance in proportion to the costs of employee benefits,
- VAT liabilities in proportion to revenues from sales.

Selected items in the statement of comprehensive income and statement of financial position are not assigned to certain types of activities as they pertain to all activities of the entity. The main unallocated items include:

- deferred tax assets and liabilities
- loans and receivables other than trade receivables
- interest-bearing loans, borrowings, bonds
- shares in subsidiaries and financial assets available for sale
- income tax receivables and liabilities
- cash and cash equivalents
- equity, except for profit for the reporting period
- income tax in statement of profit or loss

Unallocated items are presented together with other activities.

in accordance with IFRS EU (in PLN million)

25.2 Breakdown by type of business activity

STATEMENT OF PROFIT OR LOSS FOR THE YEAR ENDED DECEMBER 31, 2018

	Trade in electricity	Total trade	Other activities and unallocated items	Total
REVENUE FROM SALES	**9,073**	**533**	**1,844**	**11,450**
Cost of goods sold	(8,843)	(540)	(1,251)	**(10,634)**
GROSS PROFIT ON SALES	**230**	**(7)**	**593**	**816**
Distribution and selling expenses	(13)	(4)	-	**(17)**
General and administrative expenses	(62)	-	(160)	**(222)**
Other operating income / (expenses)	-	-	(28)	**(28)**
OPERATING PROFIT	**155**	**(11)**	**405**	**549**
Financial income / (expenses)	-	-	(698)	**(698)**
GROSS LOSS	**155**	**(11)**	**(293)**	**(149)**
Income tax	-	-	(54)	**(54)**
Net loss for the reporting period	**155**	**(11)**	**(347)**	**(203)**

In Note 4.1 Revenues from sales of each activity are presented in revenues from sales of goods and revenues from sales of services.

STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 2018

	Trade in electricity	Total trade	Other activities and unallocated items	Total
NON-CURRENT ASSETS				
Property, plant and equipment	6	1	160	167
Intangible assets	-	-	1	1
Financial receivables	-	-	12,756	12,756
Derivatives and other assets measured at fair value through profit or loss	-	-	115	115
Shares in subsidiaries	-	-	32,024	32,024
Shares in other related parties	-	-	101	101
Deferred income tax assets	-	-	19	19
	6	**1**	**45,176**	**45,183**
CURRENT ASSETS				
Inventories	-	-	4	4
Income tax receivables	-	-	57	57
Derivatives	-	-	231	231
Trade and other receivables	648	47	4,855	5,550
Other current assets	23	13	15	51
Cash and cash equivalents	-	-	235	235
	671	**60**	**5,397**	**6,128**
TOTAL ASSETS	**677**	**61**	**50,573**	**51,311**

in accordance with IFRS EU (in PLN million)

STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 2018

	Trade in electricity	Total trade	Other activities and unallocated items	Total
Net loss for the reporting period	155	(11)	(347)	(203)
Other equity	-	-	39,037	39,037
TOTAL EQUITY	**155**	**(11)**	**38,690**	**38,834**
NON-CURRENT LIABILITIES				
Non-current provisions	1	-	15	16
Loans, borrowings, bonds, cash pooling	-	-	5,628	5,628
Derivatives	-	-	24	24
Other financial liabilities	-	-	21	21
	1	**-**	**5,688**	**5,689**
CURRENT LIABILITIES				
Current provisions	-	-	9	9
Loans, borrowings, bonds, cash pooling	-		5,544	5,544
Trade and other liabilities	628	18	194	840
Derivatives	-	-	164	164
Other non-financial liabilities	2	-	229	231
	630	**18**	**6,140**	**6,788**
TOTAL LIABILITIES	**631**	**18**	**11,828**	**12,477**
TOTAL EQUITY AND LIABILITIES	**786**	**7**	**50,518**	**51,311**

STATEMENT OF PROFIT OR LOSS FOR THE YEAR ENDED DECEMBER 31, 2017

	Trade in electricity	Total trade	Other activities and unallocated items	Total
REVENUE FROM SALES	**7,622**	**605**	**958**	**9,185**
Cost of goods sold	(7,423)	(595)	(418)	**(8,436)**
GROSS PROFIT ON SALES	**199**	**10**	**540**	**749**
Distribution and selling expenses	(12)	(5)	-	**(17)**
General and administrative expenses	(39)	(1)	(114)	**(154)**
Other operating income / (expenses)	-	-	(37)	**(37)**
OPERATING PROFIT	**148**	**4**	**389**	**541**
Financial income / (expenses)	-	-	4,008	**4,008**
GROSS PROFIT	**148**	**4**	**4,397**	**4,549**
Income tax	-	-	(5)	**(5)**
NET PROFIT FOR THE REPORTING PERIOD	**148**	**4**	**4,392**	**4,544**

STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 2017

	Trade in electricity	Total trade	Other activities and unallocated items	Total
NON-CURRENT ASSETS				
Property, plant and equipment	31	2	143	176
Intangible assets	1	-	2	3
Financial receivables	-	-	11,840	11,840
Derivatives and other assets measured at fair value through profit or loss	-	-	216	216
Shares in subsidiaries	-	-	32,568	32,568
Shares in other related parties	-	-	84	84
	32	**2**	**44,853**	**44,887**
CURRENT ASSETS				
Inventories	-	-	2	2
Derivatives	-	-	54	54
Trade and other receivables	560	99	1,977	2,636
Other current assets	15	17	188	220
Cash and cash equivalents	-	-	1,832	1,832
	575	**116**	**4,053**	**4,744**
TOTAL ASSETS	**607**	**118**	**48,906**	**49,631**

in accordance with IFRS EU (in PLN million)

STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 2017

	Trade in electricity	Total trade	Other activities and unallocated items	Total
Net profit for the reporting period	148	4	4,392	4,544
Other equity	-	-	34,600	34,600
TOTAL EQUITY	**148**	**4**	**38,992**	**39,144**
NON-CURRENT LIABILITIES				
Non-current provisions	5	-	15	20
Loans, borrowings, bonds, cash pooling	-	-	7,714	7,714
Derivatives	-	-	5	5
Deferred income tax liabilities	-	-	13	13
Other financial liabilities			23	23
	5	**-**	**7,770**	**7,775**
CURRENT LIABILITIES				
Current provisions	8	-	25	33
Loans, borrowings, bonds, cash pooling	-	-	1,764	1,764
Trade and other liabilities	546	95	41	682
Derivatives			27	27
Income tax liabilities	-	-	176	176
Other non-financial liabilities	-	-	30	30
	554	**95**	**2,063**	**2,712**
TOTAL LIABILITIES	**559**	**95**	**9,833**	**10,487**
TOTAL EQUITY AND LIABILITIES	**707**	**99**	**48,825**	**49,631**

26. Significant events during and after the reporting period

26.1 Events after the reporting period

Until the date on which these financial statements were approved, no significant events took place after the end of the reporting period the impact or disclosure of which is not included in these financial statements.

27. Approval of financial statements

These financial statements were approved for publication by the Management Board on March 8, 2019.

Warsaw, March 8, 2019

Signatures of members of the Management Board of PGE Polska Grupa Energetyczna S.A.

President of the Management Board	**Henryk Baranowski**	
Vice-President of the Management Board	**Wojciech Kowalczyk**	
Vice-President of the Management Board	**Marek Pastuszko**	
Vice-President of the Management Board	**Paweł Śliwa**	
Vice-President of the Management Board	**Ryszard Wasiłek**	
Vice-President of the Management Board	**Emil Wojtowicz**	
Signature of person responsible for drafting these financial statements	Michał Skiba Director, Reporting and Tax Department	