Energa

ENERGA SA Group

Consolidated financial statements prepared in accordance with the International Financial Reporting Standards as endorsed by the European Union for the year ended 31 December 2016

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Consolidated financial statements for the year ended 31 December 2016 (PLN millions)

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

	Note	Year ended 31 December 2016	Year ended 31 December 2015
Continuing operations			
Revenue	**11.1**	**10,181**	**10,804**
Cost of sales	**11.2**	(8,846)	(8,786)
Gross profit on sales		**1,335**	**2,018**
Other operating income	**11.5**	117	91
Selling and distribution expenses	**11.2**	(338)	(336)
General and administrative expenses	**11.2**	(318)	(344)
Other operating expenses	**11.6**	(309)	(149)
Financial income	**11.7**	54	59
Financial costs	**11.8**	(284)	(287)
Share in profit/(loss) of the entities measured by the equity method		(52)	-
Profit or loss before tax		**205**	**1,052**
Income tax	**12**	(58)	(212)
Net profit or loss for the period		**147**	**840**
Attributable to:			
Equity holders of the Parent Company		151	832
Non-controlling interest		(4)	8
Earnings or loss per share (in PLN)	**22**		
- basic		**0.36**	**2.01**
- diluted		**0.36**	**2.01**

31 December 2016 (PLN millions)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended 31 December 2016	Year ended 31 December 2015
Net profit for the period		**147**	**840**
Items that will never be reclassified to profit or loss		***26***	***(6)***
Actuarial gains and losses on defined benefit plans	**24.1**	33	(7)
Deferred tax		(7)	1
Items that are or may be reclassified subsequently to profit or loss		***39***	***23***
Foreign exchange differences from translation of foreign entities		4	-
Cash flow hedges	**28.7**	43	28
Deferred tax		(8)	(5)
Share in other comprehensive income of the entities measured by the equity method		(2)	-
Net other comprehensive income		**63**	**17**
Total comprehensive income		**210**	**857**
Attributable to:			
Equity holders of the Parent Company		214	849
Non-controlling interest		(4)	8

Consolidated financial statements for the year ended 31 December 2016 (PLN millions)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	As at 31 December 2016	As at 31 December 2015
ASSETS			
Non-current assets			
Property, plant and equipment	**13**	13,053	12,912
Intangible assets	**14**	383	395
Goodwill	**15**	26	143
Investments in joint ventures measured by the equity method	**16**	390	-
Deferred tax assets	**12.3**	396	260
Other non-current financial assets	**28.1**	166	60
Other non-current assets	**20.1**	101	103
		14,515	**13,873**
Current assets			
Inventories	**17**	472	513
Current tax receivables		111	47
Trade receivables	**28.5.1**	1,947	1,762
Portfolio of financial assets	**28.3.1**	2	322
Other current financial assets	**28.1**	15	38
Cash and cash equivalents	**19**	1,471	1,669
Other current assets	**20.2**	198	232
		4,216	**4,583**
TOTAL ASSETS		**18,731**	**18,456**

31 December 2016 (PLN millions)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION (cont.)

	Note	As at 31 December 2016	As at 31 December 2015
EQUITY AND LIABILITIES			
Equity			
Share capital	**21.1**	4,522	4,522
Foreign exchange differences from translation of a foreign entity		4	-
Reserve capital	**21.4**	1,018	447
Supplementary capital	**21.5**	728	661
Cash flow hedge reserve	**21.6, 28.7**	41	6
Retained earnings	**21.7**	2,464	3,134
Equity attributable to equity holders of the Parent Company		**8,777**	**8,770**
Non-controlling interest	**21.8**	**40**	**44**
		8,817	**8,814**
Non-current liabilities			
Loans and borrowings	**28.5.2**	3,086	2,475
Bonds issued	**28.5.2**	2,639	3,116
Non-current provisions	**24**	578	664
Deferred tax liabilities	**12.3**	593	591
Deferred income and non-current grants	**26**	515	531
Other non-current financial liabilities	**28.1**	6	25
		7,417	**7,402**
Current liabilities			
Trade liabilities		811	877
Current loans and borrowings	**28.5.2**	334	203
Bonds issued	**28.5.2**	78	76
Current income tax liability		3	2
Deferred income and grants	**26**	170	161
Short-term provisions	**24**	711	471
Other financial liabilities	**28.1**	157	193
Other current liabilities	**25**	233	257
		2,497	**2,240**
Total liabilities		**9,914**	**9,642**
TOTAL EQUITY AND LIABILITIES		**18,731**	**18,456**

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CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

		Equity attributable to equity holders of the Parent Company								
	Note	Share capital	Foreign exchange differences from translation of a foreign entity	Reserve capital	Supplementary capital	Cash flow hedge reserve	Retained earnings	Total	Non-controlling interest	Total equity
Note		**21.1**		**21.4**	**21.5**	**21.6, 28.7**	**21.7**		**21.8**	
As at 1 January 2016		**4,522**	**-**	**447**	**661**	**6**	**3,134**	**8,770**	**44**	**8,814**
Actuarial gains and losses on defined benefit plans	**24.1**	-	-	-	-	-	26	**26**	-	**26**
Foreign exchange differences from translation of foreign entities		-	4	-	-	-	-	**4**	-	**4**
Cash flow hedges	**28.7**	-	-	-	-	35	-	**35**	-	**35**
Share in other comprehensive income of the entities measured by the equity method		-	-	-	-	-	(2)	**(2)**	-	**(2)**
Net profit or loss for the period		-	-	-	-	-	151	**151**	(4)	**147**
Total comprehensive income for the period		**-**	**4**	**-**	**-**	**35**	**175**	**214**	**(4)**	**210**
Retained earnings distribution		-	-	571	67	-	(638)	**-**	-	**-**
Dividends	**23**	-	-	-	-	-	(203)	**(203)**	-	**(203)**
Purchase of shares in related parties		-	-		-	-	(4)	**(4)**	-	**(4)**
As at 31 December 2016		**4,522**	**4**	**1,018**	**728**	**41**	**2,464**	**8,777**	**40**	**8,817**
As at 1 January 2015		**4,522**	**-**	**447**	**607**	**(17)**	**2,957**	**8,516**	**37**	**8,553**
Actuarial gains and losses on defined benefit plans	**24.1**	-	-	-	-	-	(6)	**(6)**	-	**(6)**
Cash flow hedges	**28.7**	-	-	-	-	23	-	**23**	-	**23**
Net profit for the period		-	-	-	-	-	832	**832**	8	**840**
Total comprehensive income for the period		**-**	**-**	**-**	**-**	**23**	**826**	**849**	**8**	**857**
Retained earnings distribution		-	-	-	54	-	(54)	**-**	**-**	**-**
Dividends	**23**	-	-	-	-	-	(596)	**(596)**	**-**	**(596)**
Purchase of shares in subsidiaries		-	-	-	-	-	1	**1**	**(1)**	**-**
As at 31 December 2015		**4,522**	**-**	**447**	**661**	**6**	**3,134**	**8,770**	**44**	**8,814**

31 December 2016 (PLN millions)

CONSOLIDATED STATEMENT OF CASH FLOWS

	Note	Year ended 31 December 2016	Year ended 31 December 2015
Cash flows from operating activities			
Profit/(loss) before tax		**205**	**1,052**
Adjustments for:			
Share in loss of the entities measured by the equity method		52	-
Foreign currency (gains)/losses		11	(1)
Amortization and depreciation	**11.3**	957	916
Net interest and dividends		259	241
Loss on investing activities, including goodwill impairment allowance	**30**	611	66
Changes in working capital:			
Change in receivables	**30**	(127)	(235)
Change in inventories		41	(214)
Change in liabilities excluding loans and borrowings	**30**	(104)	(100)
Change in prepayments and accruals		(29)	(15)
Change in provisions	**30**	176	106
		2,052	**1,816**
Income tax paid		**(270)**	**(212)**
Net cash from operating activities		**1,782**	**1,604**
Cash flows from investing activities			
Disposal of property, plant and equipment and intangible assets		11	13
Purchase of property, plant and equipment and intangible assets		(1,580)	(1,602)
Proceeds from deposits above 3m		-	14
Establishment of deposits above 3m		-	(14)
Sale of participation units in the ENERGA Trading fund		320	442
Purchase of shares in entities measured by the equity method	**2.2.1**	(443)	-
Other		3	8
Net cash from investing activities		**(1,689)**	**(1,139)**
Cash flows from financing activities			
Proceeds from loans and borrowings		1,286	340
Repayment of loans and borrowings		(575)	(240)
Redemption of debt securities		(578)	-
Dividends paid	**23**	(203)	(596)
Interest paid		(204)	(220)
Other		(13)	(2)
Net cash from financing activities		**(287)**	**(718)**
Net increase/(decrease) in cash and cash equivalents		**(194)**	**(253)**
Cash and cash equivalents at the beginning of the period	**19**	**1,658**	**1,911**
Cash and cash equivalents at the end of the period	**19**	**1,464**	**1,658**

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ACCOUNTING PRINCIPLES (POLICIES) AND OTHER EXPLANATORY INFORMATION

1. General information

The ENERGA SA Group (the "Group") consists of **ENERGA Spółka Akcyjna** ("Parent Company", "Company") with its registered office in Gdańsk and its subsidiaries (see Note 2). The consolidated financial statements of the Group cover the year ended 31 December 2016 and contain appropriate comparative data.
The Parent Company is entered in the Register of Entrepreneurs of the National Court Register held by the District Court Gdańsk-Północ, 7th Commercial Division of the National Court Register under number KRS 0000271591.

The Parent Company's REGON statistical number is 220353024.

The primary activities of the Group are as follows:

1. distribution and sales of electricity and heat,
2. production of electricity and heat,
3. trading in electricity.

As at 31 December 2016, the Polish State Treasury is the Company's parent and ultimate controlling party of the ENERGA SA Group.

2. Composition of the Group and its changes

2.1. Composition of the Group at the end of the reporting period

As at 31 December 2016, the Group consists of ENERGA SA and the following companies:

No.	Company name	Registered office	Line of business	% held by the Group in share capital as at	
				31 December 2016	31 December 2015
	Distribution Segment				
1	ENERGA-OPERATOR SA	Gdańsk	distribution of electricity	100	100
2	ENERGA-OPERATOR Eksploatacja Elbląg Sp. z o.o.	Elbląg	grid operation	100	100
3	ENERGA-OPERATOR Eksploatacja Gdańsk Sp. z o.o.	Gdańsk	grid operation	100	100
4	ENERGA-OPERATOR Eksploatacja Kalisz Sp. z o.o.	Kalisz	grid operation	100	100
5	ENERGA-OPERATOR Eksploatacja Płock Sp. z o.o.	Płock	grid operation	100	100
6	ENERGA-OPERATOR Eksploatacja Słupsk Sp. z o.o.	Słupsk	grid operation	100	100
7	ENERGA-OPERATOR Eksploatacja Toruń Sp. z o.o.	Toruń	grid operation	100	100
8	ENERGA-OPERATOR Techniczna Obsługa Odbiorców Sp. z o.o.	Koszalin	technical customer service	100	100
9	Przedsiębiorstwo Budownictwa Elektroenergetycznego ENBUD Słupsk Sp. z o.o.	Słupsk	contracting and design	100	100
10	Energetyka Kaliska – Usługi Techniczne Sp. z o.o.	Kalisz	contracting and design	100	100
11	ZEP - Centrum Wykonawstwa Specjalistycznego Sp. z o.o.	Płock	contracting and design	100	100
12	Zakład Budownictwa Energetycznego Sp. z o.o.	Koszalin	contracting and design	100	100
13	ENERGA-OPERATOR Logistyka Sp. z o.o.	Płock	logistics and supply	100	100
14	Zakład Energetyczny Toruń - ENERGOHANDEL Sp. z o.o. w likwidacji (in liquidation)[1]	Toruń	supply	-	100
	Sales Segment				
15	ENERGA-OBRÓT SA	Gdańsk	trading in electricity	100	100

Consolidated financial statements for the year ended 31 December 2016 (PLN millions)

No.	Company name	Registered office	Line of business	% held by the Group in share capital as at	
				31 December 2016	31 December 2015
16	ENERGA Obsługa i Sprzedaż Sp. z o.o.	Gdańsk	customer service	100	100
17	ENERGA Oświetlenie Sp. z o.o.	Sopot	lighting services	100	100
18	ENERGA SLOVAKIA s.r.o.	Bratislava	trading in electricity	100	100
19	Enspirion Sp. z o.o. (formerly: ENERGA Innowacje Sp. z o.o.)	Gdańsk	organization and management of development of innovative power projects	100	100
20	EOB PGK1 Sp. z o.o.	Gdańsk	financing services	100	100
21	EOB PGK2 Sp. z o.o.	Gdańsk	financing services	100	100
	Generation Segment				
22	ENERGA Wytwarzanie SA	Gdańsk	production of energy	100	100
23	ENERGA Elektrownie Ostrołęka SA	Ostrołęka	production of energy	89.64	89.64
24	ENERGA Kogeneracja Sp. z o.o.	Elbląg	production of energy	100	100
25	ENERGA Ciepło Ostrołęka Sp. z o.o.[1]	Ostrołęka	distribution of heat	100	99.99
26	ENERGA Serwis Sp. z o.o.	Ostrołęka	repairs and maintenance services	94.81	94.81
27	ENERGA Ciepło Kaliskie Sp. z o.o.	Kalisz	distribution of heat	91.24	91.24
28	ENERGA Invest SA	Gdańsk	investment project management	100	100
29	ZEC Żychlin Sp. z o.o.[1]	Żychlin	distribution of heat	-	100
30	Elektrownia Ostrołęka SA	Ostrołęka	production of energy	100	100
31	AEGIR 4 Sp. z o.o.	Gdańsk	production of energy	100	100
32	BORA Sp. z o.o.	Gdańsk	production of energy	-	100
33	Ekologiczne Materiały Grzewcze Sp. z o.o.	Gdańsk	consulting activity	-	100
34	Elektrownia CCGT Gdańsk Sp. z o.o.	Gdańsk	production of energy	100	100
35	Elektrownia CCGT Grudziądz Sp. z o.o.	Grudziądz	production of energy	100	100
	Others Segment				
36	ENERGA Centrum Usług Wspólnych Sp. z o.o.	Gdańsk	accounting, payroll and administrative services	100	100
37	ENERGA Finance AB (publ)	Stockholm	financing activity	100	100
38	ENERGA Informatyka i Technologie Sp. z o.o.	Gdańsk	information and communication technologies	100	100

Consolidated financial statements for the year ended 31 December 2016 (PLN millions)

No.	Company name	Registered office	Line of business	% held by the Group in share capital as at	
				31 December 2016	31 December 2015
39	RGK Sp. z o.o.	Gdańsk	financing services and property management	100	100
40	ENSA PGK1 Sp. z o.o.	Gdańsk	financing services	100	100
41	ENSA PGK2 Sp. z o.o.	Gdańsk	financing services	100	100
42	ENSA PGK3 Sp. z o.o.	Gdańsk	financing services	100	100
43	ENSA PGK4 Sp. z o.o.	Gdańsk	financing services	100	100
44	ENSA PGK5 Sp. z o.o.	Gdańsk	financing services	100	100
45	ENSA PGK6 Sp. z o.o.	Gdańsk	financing services	100	100
46	ENSA PGK7 Sp. z o.o.	Gdańsk	financing services	100	100
47	ENSA PGK8 Sp. z o.o.	Gdańsk	financing services	100	100

[1] See description in note 2.2.

Additionally, as at 31 December 2016 the Group holds a 16.6% stake in Polska Grupa Górnicza Sp. z o.o. ("PGG"), a joint venture with its registered office in Katowice (see description in note 2.2.).

2.2. Changes in the composition of the Group and investments in joint ventures in the reporting period

2.2.1. Polska Grupa Górnicza

On 28 April 2016, the subsidiary ENERGA Kogeneracja Sp. z o.o. signed an Investment Agreement ("Agreement") defining the terms and conditions of the financial investment in Polska Grupa Górnicza Sp. z o.o. As part of the investment in PGG, ENERGA Kogeneracja Sp. z o.o. undertook to make payments to the newly-issued shares in PGG in the total amount of PLN 500 m, which will ultimately allow the company to subscribe for 17.1% of PGG's share capital (the number of shares corresponds to the number of voting rights). As at the end of the current reporting period, the following capital contribution has been made:

- PLN 361 m – on 5 May 2016, resulting in the 15.7% stake held in PGG's share capital,
- PLN 83 m – on 3 November 2016, raising the stake in PGG's share capital to 16.6%.

The last tranche of the capital contribution in the amount of PLN 56 m was made on 1 February 2017 in accordance with the Agreement (which raised the stake held in PGG's share capital to 17.1%). Disbursement of the individual tranches was conditional upon, among others, the absence of default on the terms and conditions of the bonds issued by PGG.

PGG is in the business of coal production and it offers access to extensive resources of energy fuels, which may be used by the Group's production entities. The registered office of PGG is in Katowice.

The Investment Agreement provides for a number of mechanisms, which enable investors to monitor PGG's financial standing on an ongoing basis, including fulfillment of its business plan and undertaking of optimization activities, among others when market conditions change to the worse. These rights are exercised by PGG's Supervisory Board, while according to the Agreement, each shareholder in PGG has the right to appoint, dismiss and suspend one Supervisory Board member (as a personal entitlement), while there are 6 Supervisory Board members in total.

Additionally, PGE Górnictwo i Energetyka Konwencjonalna S.A., ENERGA Kogeneracja Sp. z o.o., PGNiG TERMIKA S.A. and Fundusz Inwestycji Polskich Przedsiębiorstw Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych [Polish Corporates Closed-End Mutual Fund] (hereinunder jointly referred to as "New Investors" signed a memorandum of agreement regarding PGG ("Memorandum of Agreement"). The purpose of the Memorandum of Agreement is to increase control of New Investors over PGG, since they jointly hold the majority of votes at PGG's Shareholder Meeting. The Memorandum of Agreement assumes, among others, that a joint position will be agreed upon when the key decisions are made by PGG's General Meeting and its Supervisory Board.

On 29 June 2016, the Office of Competition and Consumer Protection issued his approval for the concentration involving acquisition of joint control over PGG by the New Investors based on the Memorandum of Agreement.

Because of the aforementioned powers of the New Investors, the investment in PGG is treated as a joint venture and measured by the equity method.

PGG is a privately held company and therefore there are no market quotes for its share prices.

2. Composition of the Group and its changes (cont.)

Following the analyses and valuations of the acquired assets and liabilities, the fair value of PGG's identifiable assets, liabilities and contingent liabilities was determined. The purchase price including transaction cost of PLN 3 m was also determined. The calculation of goodwill is presented in the table below.

Settlement of the acquisition transaction	
Group's share in identifiable net assets	361
Share purchase price plus transaction costs	364
Goodwill	**3**

2.2.2. Other changes in the composition of the Group

As of 6 April 2016, ENERGA Kogeneracja Sp. z o.o. became the only shareholder of ENERGA Ciepło Ostrołęka Sp. z o.o. by purchasing 3 shares from a shareholder, a natural person.

On 1 February 2016, ENERGA Kogeneracja Sp. z o.o. (acquiring company) merged with ZEC Żychlin Sp. z o.o. Sp. z o.o. (acquired company) without increasing the share capital of the acquiring company. Following the merger, ZEC Żychlin Sp. z o.o. was deleted from the National Court Register.

On 25 January 2016, the Court of Registration removed Zakład Energetyczny Toruń - ENERGOHANDEL Sp. z o.o. w likwidacji (in liquidation) from the National Court Register.

3. Composition of the Parent Company's Management Board

In the period from 1 to 3 January 2016, the Management Board of the Parent Company was as follows:

- Roman Pionkowski – President of the Management Board,
- Seweryn Kędra – Vice-President of the Management Board for Financial Matters.

On 29 December 2015, the Company's Supervisory Board adopted a resolution to appoint as of 4 January 2016 the Company's Management Board for the 5th term of office comprised of:

- Dariusz Kaśków – President of the Management Board,
- Mariusz Rędaszka – Vice-President of the Management Board for Financial Matters,
- Roman Pionkowski – Vice-President of the Management Board for Development Strategy, dismissed as of 26 February 2016.

On 1 February 2016, the Company's Supervisory Board adopted a resolution to appoint Mr. Grzegorz Ksepko to the Company's Management Board as of 1 February 2016 to serve as the Vice-President of the Management Board for Corporate Matters.

On 19 March 2016, the Company's Supervisory Board adopted a resolution to appoint to the Company's Management Board as of 21 March 2016: Ms. Mariola Zmudzińska to serve as the Vice-President of the Management Board for Investor Relations and Mr. Przemysław Piesiewicz to serve as the Vice-President of the Management Board for Development Strategy.

On 17 January 2017, the Company's Supervisory Board adopted a resolution to delegate Mr. Jacek Kościelniak to act as the President of the Management Board. At the same time, Mr. Dariusz Kaśków, the previous President of the Management Board, Mr. Mariusz Rędaszka, the Vice-President of the Management Board for Financial Matters and Mr. Przemysław Piesiewicz, the Vice-President of the Management Board for Development Strategy, were dismissed from their functions.

On 10 February 2017, the Company's Supervisory Board adopted a resolution to appoint the following to the Management Board: Mr. Daniel Obajtek (as President of the Management Board), Ms. Alicja Klimiuk (as Vice-President of the Management Board for Operations), Mr. Jacek Kościelniak (as Vice-President of the Management Board for Financial Matters).

On 16 February 2017, the Company's Supervisory Board adopted a resolution to dismiss from the Company's Management Board Ms. Mariola Zmudzińska, who served as the Vice-President of the Management Board for Investor Relations.

4. Approval of the financial statements

These consolidated financial statements were approved for publication by the Company's Management Board on 29 March 2017.

5. Basis for preparation of the financial statements

These consolidated financial statements have been prepared on the historical cost basis except for financial instruments measured at fair value through profit or loss and hedging derivatives.

These consolidated financial statements are presented in millions of zloty ("PLN m").

These consolidated financial statements have been prepared based on the assumption that the Group would continue as a going concern in the foreseeable future.

As at the date of these financial statements there is no evidence indicating significant uncertainty as to the ability of the Group to continue its business activities as a going concern.

5.1. Statement of compliance

These consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards ("IFRS") and IFRS approved by the European Union ("IFRS EU").

IFRS include standards and interpretations approved by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC").

5.1 Statement of compliance (cont.)

The Management Board of the Parent Company used its best knowledge in the application of standards and interpretations as well as measurement methods and principles for the individual items of the consolidated financial statements of the ENERGA SA Group in accordance with IFRS EU as at 31 December 2016. All the tables and explanations have been prepared with due care.

5.2. Functional and presentation currency

The functional currency of the Parent Company and other Polish companies covered by these consolidated financial statements and the presentation currency of these consolidated financial statements is the Polish zloty except for ENERGA SLOVAKIA s.r.o. and ENERGA Finance AB (publ) where the functional currency of their financial statements is euro. For the purpose of these financial statements, the underlying accounts of the above-mentioned companies have been translated into PLN as follows: data in the statement of financial position, except equity - exchange rates at the reporting date; equity - exchange rates at the date of transaction and data in the statement of profit or loss - at the weighted average exchange rate for the financial period. Exchange differences from translation were captured in other comprehensive income.

6. Material items subject to judgment and estimates

In the process of applying the accounting policies, one of the most important factors next to accounting estimates was the professional judgment of the management, which affected the amounts stated in the consolidated financial statements, including the notes. The assumptions adopted for the purposes of those estimates are based on the best knowledge of the Management Board regarding the current and future actions and events in individual areas. Detailed information on the assumptions is presented in the relevant notes in these consolidated financial statements.
The key assumptions for the future and other main sources of uncertainty occurring as at the end of the reporting period, which entail a significant risk of considerable adjustment of the carrying amount of assets and liabilities in the next financial year, are presented below.

Impairment of property, plant and equipment, intangible assets and goodwill

The Group assesses whether there is any evidence of impairment of the Cash Generating Units ("CGU") and individual assets.

This analysis covers external factors, including technological, market, economic or legal changes in the environment in which we conduct our business or on the markets where we use the Group's assets to serve our clients, as well as internal factors associated with the physical condition of property, plant and equipment components and changes in the way they are used. If we find any such evidence, we carry out an asset impairment test following the rules described in Note 9.8. Information on the impairment tests that we have conducted is presented in Notes 13 and 15.

Measurement of provisions

Provisions for employee benefits (provision for pensions and similar benefits, jubilee bonuses, energy tariff, additional allowances for the Company Social Benefit Fund to which employees of Group companies are entitled after their employment period) are estimated using actuarial methods.

Other provisions are measure according to the best estimation of expenditures necessary to fulfill the existing duties. If the time value of money is important then the provision is equal to the present value of expenditures expected to be necessary to fulfill this duty.

Detailed information about the accepted assumptions and provisions recognized are presented in Note 24.

Depreciation rates

Depreciation rates and charges are determined on the basis of the anticipated useful life of a property, plant and equipment component or intangible asset and estimates regarding their residual value. Every year, Group companies revise the assumed periods of useful life, based on the current estimates. The revision carried out in 2015 had no significant influence on the costs of the current period.

Energy price paths

Energy price paths developed by independent industry experts are an important element of the estimation of value in use of cash generating centers in the generation segment. They are also used to estimate provisions for post-employment benefits in the form of employee energy tariffs. The Group uses expert price path reports, which include pricing projections for the Polish market. Detailed information about the analysis of sensitivity to changes in the paths is disclosed in Notes 13 and 24.

Deferred tax asset

Deferred tax assets are measured using the tax rates that will be applied at the moment when the asset is utilized, based on the tax regulations in force on the end of the reporting period. The Group recognizes a deferred tax asset based on the assumption that tax profit would be recorded in the future, allowing the Group to use the asset. This assumption may prove to be unjustified if tax results deteriorate in the future. Details on the deferred tax asset are provided in Note 12.3.

Fair value of financial instruments

The fair value of financial instruments, for which no active markets exist, is measured by using appropriate valuation techniques. The Group applies professional judgment to the selection such appropriate methods and assumptions. The method used to determine fair value of individual financial instruments is presented in Note 28.3.

Estimation of revenues on sales of electricity and distribution services

Meter readings of electricity sold to retail customers are made in periods different from reporting periods. Therefore, the entities comprising the Group make estimations of electricity and distribution services sold as at every last day of the reporting period, for the period not covered by meter readings. The amount of revenues recognized as at 31 December 2016 on the basis of the estimations was PLN 371 m (PLN 644 m as at 31 December 2015).

6. Material items subject to judgment and estimates (cont.)

Impairment losses on receivables

As at the end of the reporting period, the entity evaluates whether there is objective evidence of impairment of a receivable or a group of receivables. If a recoverable amount of an asset is lower from its carrying amount then the entity recognizes an impairment loss bringing it down to the present value of planned cash flows. Impairment losses are recognized based on the age analysis of receivables and an analysis of the financial standing of the individual debtors. The amounts of the impairment losses on receivables are provided in Note 28.5.1.

7. Changes in estimates

During the periods covered by these consolidated financial statements, no changes were made in the scope or methods used in determining significant estimates. The changes in the amounts of the estimates resulted from events that occurred during the reporting periods.

8. New standards and interpretations

The accounting policies of the Group are applied on a continuous basis.

8.1. Standards and interpretations adopted for the first time in 2016

The following amendments to the existing standards published by the International Accounting Standards Board (IASB) and endorsed in the EU came into force in 2016:

- Amendments to IFRS 10 “Consolidated Financial Statements”, IFRS 12 “Disclosure of Interests in Other Entities” and IAS 28 “Investments in Associates and Joint Ventures” - Investment Entities: Applying the Consolidation Exception (applicable to annual periods beginning on or after 1 January 2016),
- Amendments to IAS 19 “Employee Benefits” – Defined Benefit Plans: Employee Contributions - endorsed in the EU on 17 December 2015 (applicable to annual periods beginning on or after 1 February 2015),
- Amendments to various standards “Annual Improvements to IFRS (2010-2012 cycle)” – changes introduced during the annual cycle of improvements to IFRS (IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38) aimed mainly at removing inconsistencies agreeing on the wording - endorsed in the EU on 17 December 2015 (applicable to annual periods beginning on or after 1 February 2015),
- Amendments to IFRS 11 “Joint Arrangements” (applicable to annual periods beginning on or after 1 January 2016),
- Amendments to IAS 16 “Property, Plant and Equipment” and IAS 38 “Intangible Assets” – Acceptable methods of depreciation and amortization (applicable to annual periods beginning on or after 1 January 2016),
- Amendments to IAS 16 “Property, Plant and Equipment” and IAS 41 “Agriculture – Bearer Plants” (applicable to annual periods beginning on or after 1 January 2016),
- Amendments to IAS 27 “Separate Financial Statements” – Equity Method in Separate Financial Statements (applicable to annual periods beginning on or after 1 January 2016),
- Amendments to various standards “Annual Improvements to IFRS (2012-2015 cycle)” – changes introduced during the annual cycle of improvements to IFRS (IFRS 5, IFRS 7, IAS 19 and IAS 34) aimed mainly at removing inconsistencies agreeing on the wording (applicable to annual periods beginning on or after 1 January 2016),
- Amendments to IAS 1 “Presentation of Financial Statements” – Disclosure Initiative (applicable to annual periods beginning on or after 1 January 2016).

These amendments to the standards have had no significant impact on the Group's accounting policies applied so far.

8.2. Standards and interpretations already published and endorsed in the EU, which have not come into effect

- IFRS 15 “Revenue from Contracts with Customers” (applicable to annual periods beginning on or after 1 January 2018),
- IFRS 9 “Financial Instruments” (applicable to annual periods beginning on or after 1 January 2018).

New standards IFRS 9 “Financial Instruments”, IFRS 15 “Revenue from Contracts with Customers” introduce significant changes as compared to the currently applicable standards. Following a tentative analysis, the Group anticipates that the changes will affect, among others, the calculation methodology for impairment losses on financial assets and may change the time of recognition of the fees for connection to the distribution network.

8.3. Standards and interpretations adopted by the IASB but not yet endorsed in the EU

IFRS as endorsed in the EU do not currently differ from the regulations adopted by the International Accounting Standards Board, with the exception of the following standards, amendments to standards and interpretations, which as at the date of approving these financial statements have not yet been adopted for application:

- IFRS 14 “Regulatory Deferral Accounts” (applicable to annual periods beginning on or after 1 January 2016),
- IFRS 16 “Leases” (applicable to annual periods beginning on or after 1 January 2019),
- Amendments to IFRS 10 “Consolidated Financial Statements” and IAS 28 “Investments in Associates and Joint Ventures” - Sales or contributions of assets between an investor and its associate/joint venture (no effective date specified),
- Amendments to IAS 12 “Income Taxes” – Detailed regulation of the recognition of deferred tax assets for unrealized losses (applicable to annual periods beginning on or after 1 January 2017).
- Amendments to IAS 7 “Statement of Cash Flows” – Disclosure Initiative (applicable to annual periods beginning on or after 1 January 2017),
- Amendments to IFRS 2 “Share-based Payment” – Classification and Measurement of Share-based Payment Transactions (applicable to annual periods beginning on or after 1 January 2018),
- Amendments to IFRS 4 “Insurance Contracts” – Applying changes introduced by IFRS 9 “Financial Instruments” (applicable to annual periods beginning on or after 1 January 2018),
- Explanations for IFRS 15 “Revenue from Contracts with Customers” (applicable to annual periods beginning on or after 1 January 2018),

8. New standards and interpretations (cont.)

- Amendments to IAS 40 "Investment Property" – Transfers of Investment Property to other asset groups (applicable to annual periods beginning on or after 1 January 2018),
- IFRIC 22 interpretation: "Foreign Currency Transactions and Advance Consideration" (applicable to annual periods beginning on or after 1 January 2018),
- Improvements to IFRSs (2014-2016 cycle) – Amendments to IFRS 1, IAS 28 (applicable to annual periods beginning on or after 1 January 2018) and IFRS 12 (applicable to annual periods beginning on or after 1 January 2017).

The new standard IFRS 16 "Leases" changes the rules for recognizing agreements that satisfy the definition of a lease. From the Group's point of view, the main change is the requirement to recognize the right to use an asset and a financial liability in the lessee's statement of financial position – both in the case of agreements that meet the criteria of finance leases and operating leases. This change will increase the value of assets and liabilities. The Group has not yet made a detailed estimation of the impact that the new standard will exert on the consolidated financial statements.

The Group does not expect the remaining amendments to IFRSs mentioned above to have a material influence on its financial statements.

9. Significant accounting policies

The key accounting policies used by the Company are presented below. The policies have been applied continuously.

9.1. Principles of consolidation

This consolidated financial statements includes the financial statements of ENERGA SA and financial data of its subsidiaries prepared in each company for the year ended 31 December 2016.

Subsidiaries are consolidated in the period from the date the Group took control over them and they cease to be consolidated on the date such control ceases. Control is exerted by the Parent Company when, because of its investment, it is subject to exposure to varying returns, or if it holds rights to the variable returns and can also influence those returns by effecting control over the subsidiary.

The Group also considers whether to treat the part of the entity where the investment was made as a separate entity (a silo). If the Group controls the recognized separate entity then it consolidates the part of the entity where the investment was made.

The Group settles transactions to purchase subsidiary undertakings by using the acquisition method. A payment transferred within the framework of the transaction is determined as the fair value of transferred assets, accepted obligations towards previous owners of the entity being acquired and equities issued by the acquiring entity.

The identifiable assets and liabilities of the acquired entity are measured as at the acquisition date at fair value. Non-controlling interest in an acquired entity is recognized at the amount of the proportionate percentage (corresponding to the non-controlling interest) of the identifiable, recognized net assets of the acquired entity. The goodwill that is created in a purchase transaction is calculated in accordance with the rules presented in Note 9.7.

The costs related to the purchase of a subsidiary entity are recognized as the costs of the period.

Unrealized profits from transactions concluded within the Group are eliminated in their entirety. Unrealized losses are ignored, unless they constitute a proof of impairment.

Purchase or sale of minority interest, when control is not acquired or lost, is recognized as a transaction between shareholder and settled through equity.

9.2. Business combinations of entities under common control

Business combinations of entities under common control are settled by summing up the various line items of the relevant assets and liabilities as well as the revenues and expenses of the merged companies, after first converting their values using uniform measurement methods and making the relevant exclusions. In the case of the acquired company, all the balance sheet and profit and loss items included in the financial statements of that company are added up in the amounts presented in the Group's consolidated financial statements. The share capital of the company whose assets are transferred to another company, or of the companies that are stricken from the commercial register as a result of the business combination, is subject to exclusion. After effecting this exclusion, the pertinent line items of the equity of the company to which the assets of the merged companies or of the newly-formed company are transferred, are adjusted by the difference between the sum total of assets and liabilities and equity. All the account balances and transactions between the merging entities, including the profits or losses on business operations executed prior to the business combination and included in the assets and liabilities and equity undergoing combination are also subject to exclusion.

9.3. Investments in joint ventures

A joint venture is a joint contractual arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

Investments in joint ventures are recognized using the equity method after deducting impairment losses, if any. Application of the equity method involves the initial recognition of the investment at purchase price plus transaction costs. The Group's share in the profit or loss of the entities measured by the equity method (calculated taking into account the impact of the fair value measurement as at the investment purchase date) starting from the purchase date is recognized in the Group's profit or loss, while its share in other comprehensive income of such an entity, starting from the purchase date, is recognized in the Group's other comprehensive income. Unrealized gains and losses on account of transactions between the investor and the joint venture are eliminated in the amount corresponding to the investor's share in such gains/losses.

31 December 2016 (PLN millions)

9. Significant accounting policies (cont.)

9.4. Conversion of items in foreign currencies

Transactions denominated in currencies other than the Polish zloty are converted on initial recognition into Polish zloty using the exchange rate applicable on the date of the transaction. At the end of the reporting period:

- cash is converted using the closing exchange (it is assumed that the closing exchange rate is the average exchange rate set for the currency by the National Bank of Poland for the day),
- non-cash items measured at historical cost in a foreign currency are converted using the exchange rate in effect on the initial transaction date (exchange rate of the company's bank), and
- non-cash items measured at fair value in a foreign currency are converted using the exchange rate from the date the fair value is determined.

Exchange differences resulting from this conversion are recognized respectively as financial income (cost) items or, in the cases identified in the accounting principles (policies), they are capitalized as assets. Foreign exchange gains/losses on non-cash items such as equity instruments measured at fair value through profit or loss are recognized as changes in fair value.

Assets and liabilities of foreign entities consolidated by the full method are converted to the Group's presentation currency at the rate in effect on the end of the reporting period and their statements of profit or loss are converted at the average weighted exchange rate for the reporting period. Foreign exchange gains/losses resulting from such a conversion are posted directly to other comprehensive income. When a foreign entity is sold, the accumulated deferred exchange differences recognized in other comprehensive income relating to that foreign entity are recognized in the statement of profit or loss.

The following exchange rates were used for measurement purposes at the end of the reporting period:

Exchange rate applicable on the last day of the period		
Currency	**31 December 2016**	**31 December 2015**
EUR	4.4240	4.2615

The weighted average exchange rates for each respective reporting period were as follows:

Average exchange rate in the period		
Currency	**1 January - 31 December 2016**	**1 January - 31 December 2015**
EUR	4.3757	4.1848

9.5. Property, plant and equipment

Property, plant and equipment is measured at net value, i.e. the initial value (or at cost assumed for property, plant and equipment used before transition to IFRS EU) less accumulated depreciation and impairment losses. The initial value of property, plant and equipment includes their cost price plus all the costs directly related to the purchase and bringing the asset to the condition necessary for its use. The cost also includes the expected cost of dismantling the property, plant and equipment, removal and restoration of the asset's location to its initial condition; the obligation to incur this cost arises upon installation of the asset or its use for purposes other than the production of inventories. The costs of purchase or manufacturing costs are capitalized until the asset is adapted to the place and conditions needed to begin its operation.

As at the date of purchasing a component of property, plant and equipment, all relevant elements with different useful lives comprising the asset are identified and separated (components). Property, plant and equipment also includes costs of general overhauls, periodic inspections, provided that their value is significant, and cost of replacement of major parts.

Depreciation charges are calculated on the basis of purchase price/manufacturing cost of the property, plant and equipment component less its residual value. Depreciation commences in the month following the month in which the asset becomes available for use. Property, plant and equipment is depreciated based on a depreciation plan defining the expected useful life of the property, plant and equipment item. The depreciation method used reflects the manner in which the business consumes economic benefits provided by the asset.

Depreciation is calculated by the straight-line method for the estimated period of the asset's useful life, i.e. for respective groups of property, plant and equipment:

• Buildings, premises and civil and marine engineering facilities, of which:	5 - 100 years
– Buildings	10 - 100 years
– Premises and civil and marine engineering facilities	5 - 50 years
• Machinery and technical equipment	3 - 50 years
• Vehicles	3 - 14 years
• Office equipment, of which:	1 - 15 years
– Computer hardware	1 - 5 years
– Other	1 - 15 years
• Other property, plant and equipment	2 - 15 years

Depreciation methods, rates and residual values of property, plant and equipment are reviewed at least once a year at the end of each financial year. Any changes resulting from such reviews are recognized as changes of estimates, with possible adjustments of depreciation charges accounted for on a prospective basis.

9. Significant accounting policies (cont.)

A property, plant and equipment item may be removed from the statement of financial position after its disposal or when no economic benefits are expected from further usage of such asset. All gains or losses arising from derecognition of an asset (calculated as a difference between the possible net sale price and the carrying amount of the item) are posted to the statement of profit or loss in the period when such derecognition took place.

9.6. Intangible assets

The Group's intangible assets include identifiable non-cash assets, which have no physical form, including right of perpetual usufruct to land purchased for cash or as part of business combinations (right of perpetual usufruct to land received free of charge is treated as an operating lease and recognized off the balance sheet).

Intangible assets are carried at purchase price or production cost, less accumulated amortization and impairment losses.

Outlays incurred for intangible assets developed in-house, with the exception of the outlays incurred for development work, are not converted into assets and are recognized in the cost of the period in which they were incurred.

Intangible assets with a limited useful life are subject to straight-line amortization throughout their useful lives and subjected to impairment tests each time when there are prerequisites indicating their impairment. Amortization commences in the month following the month in which the asset is available for use. The amortization period and method applied to intangible assets with limited useful lives must be reviewed at least at the end of each reporting period. Any changes in the expected useful life or in the expected consumption of economic benefits from the asset are recognized by changing the amortization period or method accordingly and treated as changes to estimated amounts.

Gains or losses arising from derecognition of intangible assets from the statement of financial position are measured as the difference between net proceeds from their sale and the carrying amount of the asset and are posted to the statement of profit or loss upon derecognition.

9.7. Goodwill

Goodwill from acquisition of a business is initially recognized at purchase price constituting the surplus of the price paid for shares in the acquired business plus the value of non-controlling interest, over the net fair value of identifiable assets, liabilities and contingent liabilities. On initial recognition, goodwill is recognized at purchase price less all the accumulated impairment losses.

Goodwill is not amortized. The impairment test is carried out once a year, or more frequently if necessary.

As at the date of acquisition, the acquired goodwill is allocated to each cash generating unit (or groups of units) which may benefit from merger synergies. An impairment loss is determined by estimating the recoverable amount of the cash generating unit to which the given goodwill has been allocated. If the recoverable amount of a cash generating unit is lower than its carrying amount then an impairment loss is recognized.

9.8. Impairment of non-financial non-current assets

At the end of every reporting period, the Group determines whether there is any evidence of impairment of any non-financial non-current asset. If such evidence is found or when an annual impairment test must be carried out, the Group estimates the recoverable amount of such asset or cash generating unit ("CGU") to which such asset is allocated.

Recoverable amount of an asset or a cash generating unit is equal to either: its fair value less the cost to sell such asset or cash generating unit, or its value in use, whichever is higher. Recoverable amount is determined for individual assets, unless the asset does not by itself generate any cash proceeds, which are mostly independent from those generated by other assets or asset groups. If the carrying amount of an asset is greater than its recoverable amount, impairment occurs and the value is written off to match the calculated recoverable amount.

When estimating the value in use, the forecast cash flows are discounted to their present value using the discount rate before the effects of taxation are taken into account, which reflects the current market estimation of time value of money and risk typical for a given asset. Impairment losses on assets used in the continuing activity are recognized in those cost categories, which correspond to the function of the impaired asset.

When estimating the fair value amount less selling cost, the Group takes into account the capacity of the market player to achieve economic benefits through the highest and most effective use of the asset or its sale to another market player, who would ensure such highest and most effective use of that asset.

The previously recognized impairment allowance is reversed only when the estimated values used to determine the recoverable amount of the asset changed since the last impairment loss was recognized. In such a case, the carrying amount of the asset is increased to its recoverable amount. The increased amount must not exceed the carrying amount of the asset which would be calculated (after deducting depreciation) if the impairment loss had not been applied at all to such asset in previous years. A reversal of an asset impairment loss is recognized immediately as income in the statement of profit or loss.

9.9. External financing expenses

External financing expenses are capitalized as a portion of the cost of constructing property, plant and equipment. External financing expenses consist of: interest and gains or losses on foreign exchange differences up to the amount corresponding to the interest cost adjustment.

The capitalization of financing expenses commences when measures are taken that are necessary to prepare an asset for usage, capital expenditures and external financing costs are incurred for a given asset. When an investment in an asset is discontinued for a longer period, the capitalization of external financing expenses is suspended. Capitalization is stopped when all the measures required to adapt an asset for usage are in principle concluded.

9. Significant accounting policies (cont.)

Capitalization applies to the current expenses of special-purpose loans and borrowings less the revenues from temporarily investing surplus funds and the pertinent portion of the current expenses of general loans and borrowings, when the expenditures for property, plant and equipment exceed the value of special-purpose loans and borrowings. General financing expenses are capitalized in an amount equal to the product of the capitalization rate and the surplus expenditures for property, plant and equipment above special-purpose financing. The capitalization rate is determined as the weighted-average of external financing expenses pertaining to the loans and borrowings constituting the Group's liabilities other than special-purpose loans and borrowings. The amount of external financing expenses capitalized in a period does not exceed the amount of external financing expenses incurred in the period.

9.10. Inventories

Inventories include:

- assets designated for sale in the regular course of business activity,
- in production for sale, or
- assets taking the form of raw materials used in the manufacturing process or in the provision of services.
- as well as certificates of origin and CO_2 emission allowances.

Inventories are measured at the lower of: purchase price (manufacturing cost) and net realizable value. The purchase prices applied to the valuation at the end of the reporting period cannot be higher than the net realizable value of those assets. The net realizable value is a difference between the estimated sale price in the regular course of business activity and the estimated cost of completion and costs necessary to make the sale.

The Group measures consumption of materials which are identical or considered identical due to similarity of their type and purpose, as follows:

- coal and CO_2 emission allowances – according to the FIFO method,
- materials purchased to fulfill orders – using a detailed price identification method,
- other inventories – using the weighted average method.

Certificates of origin

The certificates of origin of electricity generated by the Group in the reporting period are measured on initial recognition at fair value on the date of recognition of that asset, i.e. the date when energy is generated from renewable sources or in the co-firing process, and recognized in sales revenues. Fair value is defined as the average weighted price of the certificates of origin from a given month, determined on the basis of listings on the Polish Power Exchange.

The certificates of origin which are purchased are measured at purchase price.

CO_2 emission allowances

The acquired CO_2 emission allowances are measured at purchase price. The CO_2 emission allowances received free of charge are measured at zero value and registered off-balance sheet.

9.11. Cash and cash equivalents

Cash and cash equivalents include:

- cash on hand and on current bank accounts,
- other cash, including bank deposits with maturities no longer than 3 months.

The balance of cash and cash equivalents shown in the consolidated statement of cash flows consists of the aforementioned cash and other cash less outstanding current account overdrafts.

Bank deposits with initial maturities exceeding 3 months are presented by the Group as deposits.

Cash is measured at par value. Other cash assets are measured according to the rules applicable to financial instruments.

9.12. Other assets

Other non-financial assets recognized by the Group include also receivables on account of public and legal settlements (except for settlements on account of corporate income tax, presented as a separate item in the statement of financial position), surplus of assets over liabilities of the Company Social Benefit Fund and advances paid for future purchases of property, plant and equipment, intangible assets and inventories as well as biological assets. Advances are presented in line with the type of assets to which they refer – as non-current or current assets respectively. As non-pecuniary assets, advances are not discounted.

Accruals and deferred income

Prepayments are recorded at the level of incurred and reliably measured expenses that refer to future periods and will bring future economic benefits to the entities.

Prepayments may be written off in proportion to the passage of time or benefits received. The time and manner of settlement is justified by the nature of the cost being settled, in keeping with the conservative valuation principle.

At the end of a reporting period, the Group reviews prepayments to find whether the degree of certainty that the entity will achieve economic benefits after the elapse of the reporting period is sufficient to recognize the item as an asset component.

9.13. Assets classified as held for sale

Non-current assets and groups to be sold are classified by the Group as held for sale, if their carrying amount is recovered as a result of a sale transaction rather than from their continued use. This condition is deemed satisfied only when the sale transaction is very probable and the asset (or group to be sold) is available for immediate sale in its current condition (according to generally accepted commercial terms). Classification of an asset as designated for sale assumes an intention to make a sale transaction within one year from the change in classification.

9. Significant accounting policies (cont.)

If the Group intends to make a disposal leading to a loss of control over a subsidiary, all the assets and liabilities of that subsidiary are classified as held for sale if all of the above criteria are met and regardless of whether the Group retains any non-controlling stakes after the disposal.

Non-current assets and groups to be sold classified as held for sale are measured at the lower of initial carrying amount or fair value, less cost to sell.

9.14. Equity

Equity is carried at par value, broken down into types and according to the principles set forth by the law and by the Parent Company's articles of association.

In the consolidated financial statements, share capital is recognized at the amount stated in the Parent Company's articles of association.

Retained earnings include net result of the current year, results carried forward from previous years, reserve capital and supplementary capital of subsidiaries, arising after the acquisition of control, IFRS transition adjustments and adjustments tied to a change in interests held in subsidiaries after the parent company acquired control over them.

9.15. Provisions for employee benefits

In accordance with the regulations applicable in the individual companies, Group employees are eligible for certain benefits after their employment period and other long-term employee benefits - jubilee bonuses.

The group recognizes provisions for employee benefits in order to allocate costs to the pertinent periods. The present value of those liabilities at the end of each reporting period is calculated by an actuary using the projected unit credit method. The liabilities are calculated as discounted future payments adjusted for employee turnover, and refer to the period up to the end of the reporting period. Demographic information and information on staff turnover are based on historical information.

Provisions for pensions and other post-employment defined benefit plans

The Group recognizes provisions for the following post-employment benefits:

- pension and similar benefits are paid once, upon retirement/qualification for disability award,
- cash equivalent resulting from employee tariff for energy industry employees.
- benefits from the Company Social Benefit Fund.

Provisions established are recognized in the statement of profit or loss (as operating expenses or financial costs, respectively – discount unwinding), except for actuarial gains and losses. Gains and losses on actuarial calculations are recognized fully in other comprehensive income.

Provision for jubilee bonuses

Employees of Group companies are eligible to jubilee bonuses paid out after they reach certain lengths of employment.

Provisions established for jubilee bonuses are recognized fully in the statement of profit or loss (as operating expenses or financial costs, respectively – discount unwinding).

Provision for employee restructuring

In the previous reporting periods, voluntary departure programs (“PDO”) and individual termination rules (“ZIO”) were launched in Group companies. As employment restructuring provisions, the Group recognizes primarily the provisions for benefits for employment termination under a voluntary employment termination program and other employment restructuring measures, based on the expected number of employees to terminate work for Group companies and estimated value of severance awards or compensation. Provisions are recognized when the interested parties are notified about the main elements of the restructuring plan.

9.16. Other provisions

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable that settlement of the obligation by the Group will require an outflow of economic benefits and a reliable estimate can be made of the amount of the obligation. Recognized provisions are classified as operating expenses, other operating expenses, financial costs, as required by the circumstances.

If the time value of money is important then the provision is equal to the present value of expenditures expected to be necessary to fulfill this duty. A pre-tax discount rate is used that reflects the current market assessments of the time value of money and the risks specific to the liability. The discount rate is not adjusted for risk, since the estimates of future cash flows have been adjusted. If a discounting-based method has been used then an increase in the provision associated with passage of time is recognized as financial costs.

Provision for land reclamation and for property, plant and equipment liquidation costs

The provision for land reclamation and future costs of property, plant and equipment liquidation is established in the circumstances where the provisions of law require such assets to be dismantled and removed when they are no longer used and restore their locations to their previous state. The increase of the provision related to the passage of time (discount unwinding) is recognized in financial costs. The change in provision resulting from a change of the discount rate or the estimated reclamation/liquidation costs adjusts the value of the property, plant and equipment to which the provision refers.

9. Significant accounting policies (cont.)

Provision for liabilities for gas emissions

The provision for gas emissions is recognized gradually over the annual reporting period, based on actual CO_2 emissions, while taking into account the free emission allowances according to the following rules and order:

- in the part covered by the awarded free allowances (pro rata to the total quantity of free emission allowances awarded for the year) - at zero.
- in the part covered by acquired allowances - at purchase price,
- in the part not covered by allowances held or receivable - based on the contracted allowance purchase prices and then based on market prices of those allowances at the end of the reporting period.

Provision for redemption of certificates

The provision for redemption of certificates of origin of electricity generated from renewable energy sources, certificates of origin of electricity generated in the cogeneration process and energy efficiency credits, is recognized:

- in the part covered by the certificates of origin held at the end of the reporting period – at the value of certificates held,
- in the part not covered by the certificates of origin held at the end of the reporting period – at the value of contracted property rights and the market value of certificates needed to fulfill the obligation at the end of the reporting period or at the amount of the substitution fee.

9.17. Other liabilities

Other non-financial liabilities include in particular public tax liabilities and liabilities on account of received advance payments to be settled by deliveries of goods, services or property, plant and equipment.

Other non-financial liabilities are recognized at the amount of the required payment.

9.18. Accrued costs and deferred income

Accrued costs

Accrued costs are liabilities payable for goods or services received/provided but not paid for, billed or formally agreed with the supplier, including amounts due to the employees. Even though it is sometimes necessary to estimate the amount or payment term of the accruals, the degree of uncertainty is in general considerably lower than in the case of provisions.

Accrued costs, measured at the amount of reliably estimated and probable liabilities due in the current reporting period, resulting in particular from benefits provided to the Group by external contractors, is reported in the statement of financial position as trade liabilities.

Deferred income

Deferred income is recorded in keeping with the principle of conservative valuation and of commensurability of income and expenses. Deferred income includes:

- equivalents of funds received or due from contractors for benefits to be delivered in subsequent reporting periods,
- cash received in the form of a grant to finance a purchase or production of property, plant and equipment. These are settled by gradually increasing other operating income by an amount corresponding to depreciation on these assets, in the part financed by the mentioned cash.
- property, plant and equipment accepted free of charge and intangible assets. These revenues are recorded in other operating income and also in depreciation charges on non-current assets received,

As deferred income, the Group also posts revenues on the connection of customers to the grid, i.e. the “connection fees” received before 1 July 2009. Connection fees received after that date are recognized fully in the period’s revenues.

9.19. Grants

Grants are recognized when there is sufficient certainty that the Group will meet the conditions associated with such grants and that the grants will be received.

Grants related to assets are captured in deferred income and then written off regularly to the period’s revenues for the estimated period of economic life of the related asset.

If the Group receives a loan or borrowing on preferential terms then, on initial recognition, such financial instrument is measured at fair value equal to the value of discounted cash flows, using market interest rates for similar instruments. The difference between the valuation amount calculated using this method and at amortized cost is recognized in the statement of financial position as a grant and amortized on a straight-line basis during the repayment period of the liability, charged to other operating income in the statement of profit or loss.

9.20. Lease

Group as a lessee

Financial lease agreements, which transfer to the Group essentially the entire risk and benefits derived from the possession of the leased item, are recognized in the statement of financial position as at the lease commencement date, at the lower of: fair value of the property, plant and equipment component which constitutes the leased item, or the present value of minimum leasing fees. Leasing fees are allocated between financial costs and reduction of principal lease debt balance, in the manner that allows us to receive a fixed interest rate on the outstanding debt. Financial costs are posted directly to the statement of profit or loss.

Property, plant and equipment used under financial lease agreements are depreciated for the shorter of the two periods: estimated useful life of the asset or the term of the lease, if there is no certainty that the lessee obtains the ownership title before the end of the term of lease.

9. Significant accounting policies (cont.)

Lease agreements under which the lessor retains essentially all the risks and all the benefits derived from possession of the leased item are classified as operating lease agreements. Leasing fees under operating lease contracts and the subsequent leasing installments are recognized as expenses in the statement of profit or loss using the straight-line method throughout the term of lease.

Group as a lessor

Lease agreements under which the Group retains essentially all the risks and all the benefits derived from possession of the leased item are classified as operating lease agreements (see Note 33.2). Leasing payments are recognized as revenues in the statement of profit or loss using the straight-line method throughout the term of lease.

9.21. Financial instruments

9.21.1. Financial assets

The Group identifies the following categories of financial assets:

- Financial assets held to maturity
- Financial assets at fair value through profit or loss,
- Granted loans and receivables,
- Assets available for sale.

Financial assets held to maturity

Assets held to maturity include financial assets with specified or determinable payments and a set maturity date, which the Group intends and is able to hold until such time. Financial assets held to maturity are measured at amortized cost using the effective interest rate method.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss must meet one of the following conditions:

a) they are classified as 'held for trading'. Financial assets are classified as held for trading if:
   - they have been purchased primarily for sale in the near future,
   - they are part of the portfolio of specified financial instruments managed together where there is high probability that gains would be achieved in the short term, or
   - they are derivatives, except for derivatives under hedge accounting,

b) they have been classified as such upon purchase. Upon purchase, a financial asset may be classified as measured at fair value, with any changes in value recognized through profit or loss (except for equity securities whose prices are not quoted on an active market and whose fair value cannot be measured reliably) if the following criteria are satisfied:
   - such classification eliminates or materially reduces inconsistencies in treatment, when both measurement and the rules for recognizing losses or gains are subject to other regulations; or
   - assets are part of a group of financial assets managed and measured based on their fair value in accordance with a documented risk management strategy; or
   - such financial assets contain embedded derivatives, which should be recognized separately.

The Group classifies as financial assets at fair value through profit or loss, in particular the participation units in the ENERGA Trading SFIO mutual fund (“Fund”). At the end of a reporting period (month) the Group measures the value of participation units in the Fund as the product of the number of participation units held and the value of a single participation unit.

Measurement is done by the fund management company.

Financial assets in this category are initially measured at fair value. After initial recognition, the gains/losses on restatement to fair value are posted in profit or loss.

Loans and receivables

Loans granted and receivables include financial assets with determined or determinable payments, not listed on an active market, which are not classified as derivative instruments. Loans and receivables are initially measured at fair value plus transaction costs and after initial recognition they are measured at amortized cost.

Assets available for sale

All the remaining financial assets are assets available for sale. Assets available for sale are measured at fair value at the end of each reporting period, gains and losses on restatement to fair value (which do not constitute impairment) are recognized in other comprehensive income. The fair value of investments with no listed market price is determined in reference to the current market value of another instrument with generally the same features or based on the expected cash flows from the asset comprising the investment (discounted cash flow valuation).

9.21.2. Impairment of financial assets

At the end of each reporting period, the Group evaluates whether there exists objective evidence of impairment of a financial asset or a group of financial assets. Such important objective evidence considered by the Group includes primarily: serious financial difficulties of the debtor, litigation against the debtor, significant or persisting decline of fair value below the purchase price, material adverse change in the economic, legal or market environment of the issuer of the financial instrument.

Assets recognized at amortized cost

If there exists objective evidence that a loss has been incurred on impairment of loans granted and receivables measured at amortized cost then the Group recognizes an impairment loss equal to the difference between the carrying amount of the financial asset and the present value of estimated future cash flows (excluding future losses on defaulted receivables, which have not yet been incurred), discounted using the initial effective interest rate (i.e. one determined on initial recognition). The amount of loss is recognized in the statement of profit or loss.

9. Significant accounting policies (cont.)

If impairment loss is reduced in the next period and the reduction may be objectively tied to an event occurring after the impairment loss was recognized then the previous impairment loss is reversed. A reversal of an impairment loss is recognized in the statement of profit or loss, provided however that the carrying amount of the asset on the reversal date must not exceed its amortized cost.

Financial assets available for sale

If there exists objective evidence that a financial asset available for sale has been impaired then the amount equal to the difference between the purchase price of that asset (less any principal repayments and, in the case of financial assets measured at amortized cost using the effective interest rate method, also amortization) and its present fair value, less any impairment losses previously recognized for this asset in the statement of profit or loss, is derecognized from equity and transferred to the statement of profit or loss. If the fair value of a debt instrument available for sale increases in the following period and the increase can be objectively tied to an event following the recognition of the impairment loss in the statement of profit or loss, the amount of the reversed charge is recognized in the statement of profit or loss. Impairment losses on equity instruments classified as available for sale cannot be reversed in the statement of profit or loss.

9.21.3. Financial liabilities

The Group identifies financial liabilities measured at amortized cost

Financial liabilities held at amortized cost include primarily trade liabilities, bank loans, borrowings and debt securities. On initial recognition, they are recognized at fair value less costs of with obtaining the loan or borrowing. After initial recognition, they are measured at amortized cost using the effective interest rate method.

When calculating amortized cost, the cost of obtaining the loan or borrowing must be taken into account, as well as any discounts and bonuses obtained in connection with the liability.

Revenues and costs are recognized in the statement of profit or loss upon derecognition of the liability from the statement of financial position and also as a result of a settlement using the effective interest rate method.

The Group derecognizes a financial liability from its statement of financial position if the liability has expired, i.e. when the obligation defined in the respective agreement has been performed, has been canceled or has expired.

9.21.4. Hedge accounting

Hedging derivatives and hedge accounting

The Group may decide to designate selected derivatives as hedges under cash flow hedge accounting under any identified hedge relationship. The Group allows the use of cash flow hedge accounting only if certain criteria are met, i.e.:

- at the inception of the hedge the Group formally designates and documents the hedging relationship and the risk management objective as well as strategy for undertaking the hedge. The documentation includes the identification of the hedging instrument, the hedged position, the nature of risk and the method for a current assessment of the effectiveness of the hedge in offsetting the risk of changes in cash flows associated with the hedged risk;
- the hedge is expected to be highly effective in offsetting changes in cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship;
  the planned transaction, which is the subject of the hedge, must be highly probable and must be exposed to variations in cash flows that could ultimately affect the statement of profit or loss.
- effectiveness of the hedge can be reliably assessed, i.e. cash flows related to the hedged position resulting from the hedged risk and the fair value of the hedge can be reliably measured;
- the hedge is assessed on an ongoing basis and determined to have been highly effective throughout the reporting periods for which the hedge was designated.

Applicable accounting principles for derivatives designated as hedges under cash flow hedge accounting

Changes in the fair value measurement of derivative financial instruments designated as cash flow hedges, to the extent they are an effective hedge, are recognized in other comprehensive income, whereas any ineffective portion of the hedge is recognized in the statement of profit or loss.

The accumulated amounts of hedging instrument revaluation to fair value, previously recognized in the cash flow hedge reserve, are recognized in the statement of profit or loss in the period or periods when the hedged position affects the statement of profit or loss.

The Group ceases to use the cash flow hedge accounting principles in the event of one or more of the following events:

- The hedging instrument expires or is sold, terminated or exercised (for this purpose, the replacement or rollover of a hedging instrument into another hedging instrument is not an expiration or termination if such replacement or rollover is part of the entity's documented hedging strategy). In this case, the cumulative gain or loss on the hedging instrument, which is posted to other comprehensive income in the period when the hedge was effective remains recognized separately in equity until the planned transaction occurs;
- the hedge no longer meets the hedge accounting criteria. In this case, the cumulative gain or loss on the hedging instrument, which is posted to other comprehensive income in the period when the hedge was effective, remains recognized separately in equity until the planned transaction occurs;
- the planned transaction is no longer expected to occur, in which case any related cumulative gain or loss on the hedging instrument, which is posted to other comprehensive income in the period when the hedge was effective, is recognized in the statement of profit or loss. A planned transaction, which is no longer highly probable, may still be expected;

9. Significant accounting policies (cont.)

- The Group cancels any hedging relationship. For hedges of planned transactions, the cumulative gain or loss on the hedging instrument posted to other comprehensive income in the period when the hedge was effective remains recognized in a separate equity item until the planned transaction occurs or is no longer expected to occur. If the transaction is no longer expected to occur, the cumulative gain or loss that was recognized directly in equity is recognized in the statement of profit or loss.

Presentation

In connection with the use of cash flow hedge accounting, the Group applies the following presentation:

- the effective portion of any change in the valuation of hedges is posted to other comprehensive income and accumulated in revaluation reserve,
- interest on hedges is presented in the same item of the statement of profit or loss, which presents interest result on the hedged position,
- any revaluation of hedges is presented in the same line of the statement of profit or loss in which the revaluation of the hedged position is presented,
- the ineffective portion of changes in the valuation of hedging instruments is recognized in the result on financial instruments held for trading.

9.22. Income tax

Income tax recognized in the statement of profit or loss includes the actual tax liability for the reporting period and a change in deferred tax assets and deferred tax liabilities which are not recognized in equity or other comprehensive income.

Current tax liability

The actual tax liability for the reporting period is calculated by Group companies according to the applicable provisions of the corporate income tax act.

For companies comprising a tax capital group (see Note 12.4), income tax is calculated on income earned in the fiscal year equal to the surplus of aggregated income of all companies comprising the group over their aggregate losses.

Deferred tax

In connection with temporary differences between the value of assets and liabilities carried in accounting ledgers and their tax value and taxable loss that may be deducted in the future, the entity calculates and recognizes deferred income tax assets and liabilities.

The deferred tax liability is established for all positive temporary differences except for cases where the deferred income tax liability follows from:

- initial recognition of goodwill or an asset or liability in a transaction that is not a business combination, not affecting, at the moment of the transaction, either gross financial result before tax or taxable income (loss); and
- positive temporary differences connected with investments in subsidiaries and associates, and interests in joint ventures, in which it is possible to control the reversal of the temporary differences and it is probable that those differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized with respect to all negative temporary differences to the extent to which it is probable that there will be sufficient taxable profits against which to deduct the negative temporary differences, except for:

- cases where a deferred income tax asset results from an initial recognition of an asset or liability under a transaction other than business combination, which at the moment of the transaction has no effect on financial result before tax or taxable profit (loss); and
- negative temporary differences connected with investments in subsidiaries and associates, and interests in joint ventures, where deferred income tax assets are recognized only to the extent that it is probable that those temporary differences will be reversed in the foreseeable future and that there will be sufficient taxable profits against which to utilize the benefits of the negative temporary differences.

Deferred tax assets and liabilities are presented in the statement of financial position, after netting at the level of individual entities of the ENERGA Group.

9.23. Revenue

Sales revenues are recognized at the amount at which it is probable that the Group will obtain economic benefits tied to a specific transaction and where the amount of revenues may be measured reliably. Revenues are recognized net of value added tax (VAT), excise tax and other sales taxes or fees and discounts and rebates.

Sales of products and goods for resale are recognized when the significant risk and benefits stemming from ownership title of merchandise and products have been surrendered to the buyer and when recovery of the due amount is probable and when the amount of revenues may be measured reliably and incurred costs may be reliably estimated.

Revenues on sales of electricity distribution services and on sales of electricity to end users

The sale of electricity distribution services or electricity occurs at the moment when the electricity distribution service or electricity is delivered to the customer, which is recorded by an electricity meter. In practice, the sale occurs on the date of reading a metering and billing system.

If no actual meter reading was performed in the billing period then revenues are determined through estimation based on average daily consumption of electricity in the previous billing periods. Revenues are calculated using the price lists applicable in the period.

9. Significant accounting policies (cont.)

Revenues on electricity sales on the wholesale market

Wholesale electricity transactions are conducted when a supplier and a buyer declare to the Transmission System Operator (TSO) the quantity of electricity that the Group is contractually obligated to supply or ensure its supply (by purchasing electricity on the Balancing Market) and the buyer is obligated to accept in each hourly period. When a production unit generates electricity without a bilateral transaction signed (with a buyer) then the electricity is sold on the Balancing Market (to the TSO). TSO as a guarantor of volumes, ensures reliability of data in respect to the quantity of electricity supplied.

9.24. Operating expenses

Cost of sales is comprised of the following:

- cost of manufacturing products and providing services incurred in a reporting period, adjusted for a change in products and adjusted for the cost of manufacturing products for own needs,
- value of electricity and materials sold, at purchase prices,
- recognition/reversal of impairment losses on property, plant and equipment, intangible assets, receivables and inventories,

Selling and distribution expenses include expenses related to customer service and customer acquisition as well as marketing and advertising expenses.

General and administrative expenses include expenses related to the governance and administration of the Group as a whole and the companies comprising the Group.

9.25. Other operating income and expenses

Other operating income and expenses include in particular items associated with:

- disposals of property, plant and equipment, intangible assets,
- recognition and reversal of provisions, except for provisions tied to financial operations or recognized in operating expenses,
- giving or receiving assets, including cash, free of charge, also as a donation,
- with damages, penalties and fines and other costs not associated with ordinary operations.

9.26. Financial income and costs

Financial income and costs include in particular income and costs associated with:

- disposal of financial assets,
- restatement of financial instruments, excluding financial assets available for sale, for which the effects of restatement are recognized in other comprehensive income,
- revenues from profit-sharing in other entities,
- interest,
- change in provision resulting from the approaching date of incurring the cost (unwinding discount effect),
- exchange differences resulting from operations performed during the reporting period and book valuation of assets and liabilities at the end of the reporting period, except for exchange differences recognized in the initial value of property, plant and equipment, to the extent they are recognized as adjustment of interest cost and exchange differences from measurement of equity instruments denominated in foreign currencies and classified in the available-for-sale portfolio,
- other items related to financing activity.

Interest income and interest expense are recognized gradually as they accrue (taking the effective interest rate method into account) in relation to the net carrying amount of the financial instrument and in line with the materiality principle.

Dividends are recognized when the title of shareholders to receive them are determined.

9.27. Earnings per share

Earnings per share for each period are calculated by dividing the net profit allocated to shareholders of the Parent Company for the period by the weighted average number of shares in the reporting period. In the case of a split or reverse split of shares, the number of shares after the split or reverse split is applied to the calculation retrospectively.

9.28. Statement of cash flows

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

NOTES ON OPERATING SEGMENTS

10. Operating segments

The Group presents segment information in accordance with IFRS 8 Operating Segments for the current and for comparative reporting periods. The Group is organized and managed within operating segments, which are divided according to the types of products offered. The Group's disclosures are made for the following operating segments:

- Distribution – distribution of electricity by ENERGA-OPERATOR SA (Distribution System Operator), as well as operations directly associated with the distribution operations conducted by other Group companies;
- Generation – production of electricity from conventional and renewable sources, production and distribution of heat and maintenance and repair activity, related directly to the production of energy;
- Sales - trading in electricity (wholesale trading and retail sales) and lighting services.
- Other - shared services centers in the accounting, HR and salary, administration and ITC areas as well as financing activity and real estate management areas. The Parent Company has also been classified as belonging to the other segment.

The key measures used by the ENERGA SA Management Board to assess the performance of the segments is net profit and EBITDA, i.e. operating profit /(loss) (calculated as the profit /(loss) before tax adjusted by the share of profit/(loss) of an entity measured by the equity method, financial income and financial costs) plus depreciation and amortization and impairment losses on non-financial non-current assets. The EBITDA calculation method changed in the current reporting period. In the previous periods, EBITDA was not adjusted for impairment losses on non-financial non-current assets. This modification chiefly aims to enhance transparency and simplify analyses by ensuring comparability for the key parameter in the industry in which the Group operates. Comparative data have been restated accordingly.

The rules applied to the determination of segment results and measure the segment's assets and liabilities are consistent with the rules used to prepare the consolidated financial statements. The share in the result of the entities measured by the equity method is recognized in consolidation eliminations and adjustments.

Transactions between segments are settled on market terms.

The Group does not present information by geographic segments since its operations conducted for international clients and its international assets do not have a significant impact on the Group's results.

The tables below show the breakdown of revenues and expenses for the period from 1 January to 31 December 2016 and assets and liabilities as at 31 December 2016, by individual reporting segments, together with appropriate comparative information.

31 December 2016 (PLN millions)

10. Operating segments (cont.)

Year ended 31 December 2016 or as at 31 December 2016	Distribution	Sales	Generation	Other	Total	Consolidation eliminations and adjustments	Total activity
Revenues							
Sales to external clients	4,096	5,267	812	6	**10,181**	-	**10,181**
Inter-segment sales	47	359	328	145	**879**	(879)	**-**
Total segment revenues	**4,143**	**5,626**	**1,140**	**151**	**11,060**	**(879)**	**10,181**
EBITDA	**1,720**	**40**	**315**	**(47)**	**2,028**	**(1)**	**2,027**
Amortization and depreciation	736	39	183	18	**976**	(19)	**957**
Impairment losses on non-financial non-current assets	-	4	573	6	**583**	-	**583**
Operating profit or loss	**984**	**(3)**	**(441)**	**(71)**	**469**	**18**	**487**
Net finance income/expense	(114)	4	41	842	**773**	(1,003)	**(230)**
Share in profit/(loss) of the entities measured by the equity method	-	-	-	-	**-**	(52)	**(52)**
Profit or loss before tax	**870**	**1**	**(400)**	**771**	**1,242**	**(1,037)**	**205**
Income tax	(167)	(3)	97	15	**(58)**	-	**(58)**
Net profit or loss	**703**	**(2)**	**(303)**	**786**	**1,184**	**(1,037)**	**147**
Assets and liabilities							
Cash and cash equivalents	4	42	2	1,423	**1,471**	-	**1,471**
Total assets	**13,393**	**2,803**	**4,163**	**14,639**	**34,998**	**(16,267)**	**18,731**
Financial liabilities	4,825	5	1,057	6,017	**11,904**	(5,767)	**6,137**
Total liabilities	**7,072**	**2,069**	**1,590**	**7,280**	**18,011**	**(8,097)**	**9,914**
Other segment information							
Capital expenditures	1,263	92	248	77	**1,680**	(113)	**1,567**

Consolidated financial statements for the year ended 31 December 2016 (PLN millions)

10. Operating segments (cont.)

Year ended 31 December 2015 or as at 31 December 2015	Distribution	Sales	Generation	Other	Total	Consolidation eliminations and adjustments	Total activity
Revenues							
Sales to external clients	4,199	5,570	1,031	4	**10,804**	-	**10,804**
Inter-segment sales	56	170	353	170	**749**	(749)	**-**
Total segment revenues	**4,255**	**5,740**	**1,384**	**174**	**11,553**	**(749)**	**10,804**
EBITDA	**1,688**	**173**	**392**	**(25)**	**2,228**	**(12)**	**2,216**
Amortization and depreciation	711	34	168	18	**931**	(15)	**916**
Impairment losses on non-financial non-current assets	-	1	17	2	**20**	-	**20**
Operating profit or loss	**977**	**138**	**207**	**(45)**	**1,277**	**3**	**1 280**
Net finance income/expense	(137)	16	(62)	885	**702**	(930)	**(228)**
Profit or loss before tax	**840**	**154**	**145**	**840**	**1,979**	**(927)**	**1,052**
Income tax	(173)	(35)	(30)	27	**(211)**	(1)	**(212)**
Net profit or loss	**667**	**119**	**115**	**867**	**1 768**	**(928)**	**840**
Assets and liabilities							
Cash and cash equivalents	708	115	227	619	**1,669**	-	**1,669**
Total assets	**12,259**	**2,461**	**4,589**	**12,811**	**32,120**	**(13 664)**	**18,456**
Financial liabilities	3,670	255	1,512	5,835	**11,272**	(5,402)	**5,870**
Total liabilities	**5,994**	**1,580**	**2,052**	**6,076**	**15,702**	**(6,060)**	**9,642**
Other segment information							
Capital expenditures	1,123	58	392	48	**1,621**	(38)	**1,583**

31 December 2016 (PLN millions)

NOTES TO CONSOLIDATED STATEMENT OF PROFIT OR LOSS

11. Revenues and expenses

11.1. Revenue

	Year ended 31 December 2016	Year ended 31 December 2015
Revenues on sales of products and goods for resale and materials, including:	**5,892**	**6,424**
Electricity	5,686	6,112
Certificates of origin	-	205
Gas	216	90
Other products, goods for resale and materials	288	276
Excise tax	(298)	(259)
Revenues on sales of services, including:	**4,289**	**4,380**
Distribution and transit services	3,904	3,923
Customer connection fees	62	97
Rental income	80	85
Other services	243	275
TOTAL	**10,181**	**10,804**

11.2. Costs by nature

	Year ended 31 December 2016	Year ended 31 December 2015
Depreciation and amortization of property, plant and equipment, intangible assets and investment properties	957	916
Impairment losses on property, plant and equipment, intangible assets and investment property (including advances paid)	466	20
Consumption of materials and energy, including:	651	832
Fuel consumption	*267*	*448*
External services, including:	1,400	1,434
Transmission and transit fees	*950*	*933*
Taxes and fees	393	377
Employee benefit expenses	873	913
Impairment loss on inventories	5	-
Impairment loss on trade receivables	62	40
Other costs by nature	72	76
Change in product inventories	(5)	(5)
Cost of producing services for own needs	(90)	(97)
Cost of products and materials sold	4,718	4,960
Total operating expenses	**9,502**	**9,466**
incl.:		
Cost of sales	8,846	8,786
Selling and distribution expenses	338	336
General and administrative expenses	318	344

31 December 2016 (PLN millions)

11. Revenues and expenses (cont.)

11.3. Cost of depreciation and impairment losses recognized on non-financial non-current assets in the statement of profit or loss

	Year ended 31 December 2016	Year ended 31 December 2015
Items included in cost of sales:	**1,390**	**902**
Depreciation of property, plant and equipment	848	810
Impairment loss on property, plant and equipment	460	18
Amortization of intangible assets	75	71
Depreciation of investment property	1	1
Impairment losses on investment property	6	2
Items included in selling and distribution expenses:	**12**	**14**
Depreciation of property, plant and equipment	5	6
Amortization of intangible assets	7	8
Items included in general and administrative expenses:	**21**	**20**
Depreciation of property, plant and equipment	8	9
Amortization of intangible assets	13	11

11.4. Employee benefit expenses

	Year ended 31 December 2016	Year ended 31 December 2015
Wages and salaries	670	635
Social security contributions	126	123
Post-employment benefits and jubilee bonuses	(44)	34
Other employee benefit expenses, including:	121	121
Energy tariff - current costs	11	11
Company Social Benefit Fund - charges for the current financial year	30	30
Employee Pension Plan	38	36
Employee training	10	12
Expenses related to health and safety	7	7
Other	25	25
TOTAL	**873**	**913**

11.5. Other operating income

	Year ended 31 December 2016	Year ended 31 December 2015
Penalties, fines, compensations received	62	35
Grants	22	18
Reversal of provisions (e.g. court cases)	18	17
Revenues related to illegal energy consumption	7	5
Surplus of revenues on reversal of actuarial provisions over headcount restructuring expenses	-	6
Infrastructure acquired free of charge	4	3
Other	4	7
TOTAL	**117**	**91**

31 December 2016 (PLN millions)

11. Revenues and expenses (cont.)

11.6. Other operating expenses

	Year ended 31 December 2016	Year ended 31 December 2015
Goodwill impairment allowance	117	-
Cost of remedying losses arising from unexpected events	29	38
Donations	11	3
Compensations	24	14
Loss on disposal/liquidation of property, plant and equipment/intangible assets	27	46
Recognition of provisions	88	33
Costs related to illegal energy consumption	6	7
Litigation expenses	4	3
Other	3	5
TOTAL	**309**	**149**

11.7. Financial income

	Year ended 31 December 2016	Year ended 31 December 2015
Income on financial instruments, including:	**53**	**58**
Interest income	53	58
Other financial income	**1**	**1**
TOTAL	**54**	**59**

11.8. Financial costs

	Year ended 31 December 2016	Year ended 31 December 2015
Costs of financial instruments, including:	**244**	**264**
Interest expenses	237	261
Foreign exchange differences	7	3
Other financial costs, of which:	**40**	**23**
Actuarial and other interest	21	19
Other	19	4
TOTAL	**284**	**287**

31 December 2016 (PLN millions)

12. Income tax

12.1. Tax liabilities

The key components of the tax liability for the year ended 31 December 2016 are as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Statement of profit or loss		
Current income tax expense	(210)	(181)
Adjustments to income tax for prior years	3	(8)
Deferred tax	149	(23)
Tax expense recognized in the statement of profit or loss	**(58)**	**(212)**
Statement of comprehensive income		
Deferred tax	(15)	(4)
Tax expense recognized in the statement of comprehensive income	**(15)**	**(4)**

With regard to income tax, the Group was principally subject to the general regulations in 2016. Except for the ENERGA Tax Group (see description in Note 12.4), there were no other occurrences that would require calculation of tax liabilities using methods different from the general regulations in this respect.

The expiration date of the right to settle a tax loss by ENERGA Group companies is no later than 31 December 2020.

As at 31 December 2016, the total amount of temporary differences related to investments in subsidiaries, for which no deferred tax liabilities have been recognized, is PLN 2,444 m.

12.2. Reconciliation of effective tax rate

Reconciliation of income tax calculated on financial result before tax using the statutory tax rate to income tax calculated according to the Group's effective tax rate is as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Profit before tax on continuing operations	**205**	**1,052**
Loss before tax on discontinued operations and disposal of assets classified as held for sale	-	-
Profit before tax	**205**	**1,052**
Tax at Poland's statutory rate of 19%	**(39)**	**(200)**
Adjustments to income tax for prior years	3	(8)
Tax impact of permanently non tax-deductible expenses	(28)	(16)
Tax on the share in the loss of the entities measured by the equity method	(10)	-
Tax impact on permanently non-taxable income	29	2
Tax losses	(4)	11
Temporary differences for which no deferred tax asset was recognized	(9)	(1)
Tax at the effective tax rate in the statement of profit or loss	**(58)**	**(212)**

Current tax liability is calculated on the basis of the applicable tax regulations. Application of those regulations causes differences between the tax profit (loss) and accounting net profit (loss) because of non-taxable revenues and non-deductible expenses and items of income or expense which are never taxable. Tax liabilities are calculated on the basis of tax rates applicable in the given financial year. A 19% tax rate was used in 2016 and 2015. Current regulations do not provide for differentiated tax rates for future periods.

Both the fiscal year and the reporting period of these financial statements are the same as the calendar year.

31 December 2016 (PLN millions)

12. Income tax (cont.)

12.3. Deferred tax

The deferred tax results from the following items:

	As at 31 December 2016	As at 31 December 2015
Deferred tax assets	**696**	**520**
On the difference between the tax and carrying value of property, plant and equipment, intangible assets and inventories	236	149
On the difference between the tax and carrying value of financial assets and liabilities	97	51
Power infrastructure received free of charge and connection fees received	63	65
On provisions for post-employment benefits	67	76
On provisions for jubilee bonuses	40	50
On provisions for redemption of certificates of origin	76	47
On provisions for reclamation and decommissioning costs of property, plant and equipment	9	7
On provision gas emission liabilities	8	6
Unpaid employee salaries and benefits	4	4
On other provisions	46	36
Accrued expenses	33	15
Tax losses	5	7
Other	12	7
Set-off	**(300)**	**(260)**
Deferred tax assets after set-off	**396**	**260**

	As at 31 December 2016	As at 31 December 2015
Deferred tax liability	**893**	**851**
On the difference between the tax and carrying value of property, plant and equipment and intangible assets	799	758
accrued revenues	40	48
On the difference between the tax and carrying value of energy certificates	4	13
On the difference between the tax and carrying value of financial assets and liabilities	49	28
Other	1	4
Set-off	**(300)**	**(260)**
Deferred tax liability after set-off	**593**	**591**

The Group did not include in the balance sheet the deferred income tax asset on the value of outstanding tax losses incurred in 2011 - 2016 for the total amount of PLN 33 m.

31 December 2016 (PLN millions)

12. Income tax (cont.)

Changes in deferred tax assets and liabilities are presented in the table below:

	Year ended 31 December 2016	Year ended 31 December 2015
Deferred tax assets		
At the beginning of the reporting period	**520**	**513**
Increases	185	82
recognized in profit or loss	185	72
recognized in other comprehensive income	-	7
reinstatement of assets held for sale		3
Decreases	(9)	(75)
recognized in profit or loss	(2)	(75)
recognized in other comprehensive income	(7)	-
At the end of the reporting period	**696**	**520**
Set-off	**(300)**	**(260)**
Deferred tax asset at the end of the reporting period	**396**	**260**
Deferred tax liability		
At the beginning of the reporting period	**851**	**820**
Increases	88	79
recognized in profit or loss	80	68
recognized in other comprehensive income	8	11
Decreases	(46)	(48)
recognized in profit or loss	(46)	(48)
At the end of the reporting period	**893**	**851**
Set-off	**(300)**	**(260)**
Deferred tax liability at the end of the reporting period	**593**	**591**

12.4. ENERGA Tax Group

On 27 January 2015, ENERGA SA and its related entities: ENERGA-OPERATOR SA, ENERGA-OBRÓT SA, ENERGA Wytwarzanie SA, ENERGA Informatyka i Technologie Sp. z o.o., ENERGA Centrum Usług Wspólnych Sp. z o.o., RGK Sp. z o.o., ENSA PGK1 Sp. z o.o., ENSA PGK2 Sp. z o.o., ENSA PGK3 Sp. z o.o., ENSA PGK4 Sp. z o.o., ENSA PGK5 Sp. z o.o., ENSA PGK6 Sp. z o.o., ENSA PGK7 Sp. z o.o., ENSA PGK8 Sp. z o.o., EOB PGK1 Sp. z o.o. and EOB PGK2 Sp. z o.o. entered into a tax capital group agreement under the name of ENERGA Tax Group (PGK ENERGA). The agreement was registered by the Head of the Pomorski Tax Authority on 27 February 2015. ENERGA SA was selected as the company representing the ENERGA Tax Group in respect to the duties arising from the Corporate Income Tax Act and the Tax Ordinance Act.

The launch date of ENERGA Tax Group's activity was 1 May 2015. The agreement was concluded for 3 fiscal years, that is until 31 December 2017. In PGK, tax is calculated on income earned in the fiscal year equal to the surplus of aggregated income of all companies comprising the group over their aggregate losses.

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NOTES TO CONSOLIDATED STATEMENT OF FINANCIAL POSITION

13. Property, plant and equipment

	Own land	Buildings, premises and civil and marine engineering facilities	Plant and equipment	Vehicles	Other property, plant and equipment	Property, plant and equipment under construction	Total
Gross value							
As at 1 January 2016	**153**	**11,616**	**5,236**	**288**	**767**	**1,113**	**19,173**
Direct purchase	4	-	1	4	-	1,471	**1,480**
Settlement of property, plant and equipment under construction	-	769	673	10	75	(1,527)	**-**
Sale, disposal	-	(7)	(4)	(5)	(11)	-	**(27)**
Liquidation	-	(55)	(50)	(3)	(2)	(1)	**(111)**
Received free of charge	-	5	-	-	-	-	**5**
Reclassification between groups	-	(8)	8	-	-	-	**-**
Capitalized financing expenses	-	-	-	-	-	2	**2**
Provision for land reclamation and liquidation costs	-	10	-	-	-	-	**10**
Other changes	-	(2)	(1)	-	-	5	**2**
As at 31 December 2016	**157**	**12,328**	**5,863**	**294**	**829**	**1,063**	**20,534**
Accumulated depreciation and impairment losses							
As at 1 January 2016	**-**	**(3,839)**	**(1,704)**	**(182)**	**(370)**	**(166)**	**(6,261)**
Depreciation for the period	-	(451)	(297)	(29)	(84)	-	**(861)**
Increase in impairment losses	-	(172)	(300)	-	(1)	(104)	**(577)**
Decrease in impairment losses	-	5	3	-	-	110	**118**
Sale, disposal	-	3	3	5	10	-	**21**
Liquidation	-	31	42	3	2	-	**78**
Other changes	-	3	(2)	-	-	-	**1**
As at 31 December 2016	**-**	**(4,420)**	**(2,255)**	**(203)**	**(443)**	**(160)**	**(7,481)**
Net value as at 1 January 2016	**153**	**7,777**	**3,532**	**106**	**397**	**947**	**12,912**
Net value as at 31 December 2016	**157**	**7,908**	**3,608**	**91**	**386**	**903**	**13,053**

31 December 2016 (PLN millions)

13. Property, plant and equipment (cont.)

	Own land	Buildings, premises and civil and marine engineering facilities	Plant and equipment	Vehicles	Other property, plant and equipment	Property, plant and equipment under construction	Total
Gross value							
As at 1 January 2015	**141**	**10,902**	**4,730**	**270**	**645**	**1,086**	**17,774**
Direct purchase	-	-	2	1	-	1,473	1,476
Settlement of property, plant and equipment under construction	12	767	514	19	125	(1,437)	**-**
Sale, disposal	-	(18)	(3)	(6)	(4)	-	**(31)**
Liquidation	-	(39)	(20)	-	(3)	(18)	**(80)**
Received free of charge	-	7	1	-	-	-	**8**
Transfer from assets classified as held for sale	-	1	7	3	4	-	**15**
Capitalized financing expenses	-	-	-	-	-	10	**10**
Other changes	-	(4)	5	1	-	(1)	**1**
As at 31 December 2015	**153**	**11,616**	**5,236**	**288**	**767**	**1,113**	**19,173**
Accumulated depreciation and impairment losses							
As at 1 January 2015	**-**	**(3,422)**	**(1,441)**	**(154)**	**(293)**	**(149)**	**(5,459)**
Depreciation for the period	-	(437)	(276)	(32)	(80)	-	**(825)**
Increase in impairment losses	-	(1)	-	-	-	(17)	**(18)**
Sale, disposal	-	4	3	6	4	-	**17**
Liquidation	-	16	15	-	3	-	**34**
Transfer from assets classified as held for sale	-	-	(5)	(2)	(4)	-	**(11)**
Other changes	-	1	-	-	-	-	**1**
As at 31 December 2015	**-**	**(3,839)**	**(1,704)**	**(182)**	**(370)**	**(166)**	**(6,261)**
Net value as at 1 January 2015	**141**	**7,480**	**3,289**	**116**	**352**	**937**	**12,315**
Net value as at 31 December 2015	**153**	**7,777**	**3,532**	**106**	**397**	**947**	**12,912**

13. Property, plant and equipment (cont.)

In connection with changes occurring in its market and regulatory environment in 2016, such as the declining prices of certificates of origin of energy, persisting low prices for electricity in forward and SPOT contracts, introduction of the Act on wind farm investments and the new Group Strategy and the Long-Term Plan of Strategic Investments coming into force, the Group has identified certain indications, which may result in a decline of recoverable amount of property, plant and equipment of the companies in the Generation Segment.

The impairment tests for cash generating units ("CGUs") were performed using the income method, determining the value in use based on the discounted value of estimated cash flows from operating activities, taking into account, among others, the following assumptions:

- price forecasts have been adopted for electricity, coal, CO_2 allowances and for certificates of origin, based on a report on the Polish market prepared for the Group by an independent agency in October 2016; the forecast was prepared with the timeframe until 2035;
- assumptions adopted for costless CO_2 emission allowances for 2015-2021 as specified in the Regulation of the Council of Ministers of 31 March 2014 (Item 439) and 8 April 2014 (Item 472),
- assumptions made for capital expenditures at the levels allowing for maintenance of the production capacity of the existing non-current assets after replacement investments, including capital expenditures to adjust industrial emission levels to the requirements of the Industrial Emission Directive 2010/75/EU of the European Parliament and of the Council of 24 November 2010,
- support maintained for production of energy from the existing renewable sources in accordance with the Renewable Energy Sources Act of 20 February 2015 and the Act of 22 June 2016 Amending the Renewable Energy Sources Act and Certain Other Acts,
- support system maintained for high-efficient cogeneration throughout the forecast period,
- Operating Reserve maintained throughout the forecast period,
- the length of forecasts for the individual CGUs has been adopted in such a way to ensure that the cash flow used to calculate residual value was as similar as possible to the cash flows expected in the coming years.

Wind farms ("CGU Karcino, CGU Karścino, CGU Bystra, CGU Myślino, CGU Parsówek")

The impairment tests for the wind farms were conducted as at 31 March 2016 and as at 31 May 2016. The value in use was calculated on the basis of financial projections for the full useful life period of the wind farms, that is 25 years. The discount rates set on the basis of the pre-tax weighted-average cost of capital (WACC), used for the calculation, fell within the range from 6.76% to 7.52% (on average 6.13% after tax).

Based on the results of the tests, it was determined that impairment losses on the wind farms must be recognized in the amount of PLN 324 m (mainly Plant and equipment). The recoverable amount was estimated at the level of PLN 521 m. The tests conducted on a group of CGUs (Karcino, Karścino, Bystra) have also shown the necessity to write down the entire goodwill coming from the acquisition of the wind farm portfolio in 2013, in the amount of PLN 117 m.

The tests were conducted again as at 30 November 2016 and based on the tests, no need was found to recognize additional impairment losses.

Wind projects

The impairment tests for the wind farms were conducted as at 31 May 2016. The value in use was calculated for wind projects on the basis of financial projections for the full useful life period of the projected farms, that is 25 years, assuming that the auction system comes into effect. The standard projection period of 5 years was extended to 25 years enabling a more reliable valuation of the units, the useful life of which is known and predictable. The discount rates set on the basis of the pre-tax weighted-average cost of capital (WACC) used for the calculation fell within the range from 7.03% to 8.29%. Based on the results of the tests, it was determined that impairment losses on the tested wind projects must be recognized in the amount of PLN 31 m.

Moreover, after the Act on wind farm investments came into effect and the minimum distance between a wind farm and residential buildings was introduced, it was determined that the remaining wind projects cannot be executed. Accordingly, an impairment loss was recognized for these projects in the amount of PLN 68 m. The recoverable amount was estimated at the level of PLN 39 m.

Impairment losses decreased the value of property, plant and equipment under construction. After impairment losses, the value of the projected wind farms amounts to PLN 12 m.

Photovoltaic farms ("CGU PV Delta, PV Czernikowo")

The impairment tests for the photovoltaic farms were conducted as at 31 March 2016. The value in use was calculated on the basis of financial projections for the full useful life period of the farms, that is 25 years. The standard projection period of 5 years was extended to 25 years enabling a more reliable valuation of the units, the useful life of which is known and predictable. The discount rates set on the basis of the pre-tax weighted-average cost of capital (WACC), used for the calculation, fell within the range from 6.69% to 6.71% (on average 5.73% after tax).

Based on the results of the tests, it was determined that impairment losses must be recognized on the photovoltaic farms in the amount of PLN 11 m (mainly Plant and equipment). The recoverable amount was estimated at the level of PLN 14 m.

The tests were conducted again as at 30 November 2016 and based on the tests, no need was found to recognize additional impairment losses.

13. Property, plant and equipment (cont.)

Ostrołęka B Power Plant ("CGU Ostrołęka B")

The impairment test for CGU Ostrołęka B was conducted as at 30 November 2016. The value in use was calculated on the basis of financial projections for the period of December 2016 - December 2023 and residual value (the projection period was extended to take into account the negative effect of the expiration of support offered by green certificates). The projections were prepared on the basis of the Group's strategy and the updated Long-Term Plan of Strategic Investments, while taking into account the changes in Elektrownia Ostrołęka B's business model. To calculate value in use of CGU Ostrołęka B, a discount rate was applied, which was calculated on the basis of the weighted average cost of capital (WACC) at 7.59% (6.93% after tax). The growth rate used to extrapolate cash flow projections beyond the period covered by detailed planning was adopted at the level of 2.0% which does not exceed the average long-term inflation growth rates in Poland.

Based on the results of the tests, it was determined that impairment losses on CGU Ostrołęka B must be recognized in the amount of PLN 132 m (mainly Plant and equipment). The recoverable amount was estimated at the level of PLN 586 m.

Combined Heat and Power Plant Elbląg with BB20 installation ("CGU CHP Elbląg")

The impairment test for CGU CHP Elbląg (including the BB20 installation) was conducted as at 30 November 2016. The value in use was calculated on the basis of financial projections for the period of December 2016 - December 2030 and residual value. The standard projection period of 5 years was extended until 2030 because of the fact that green certificates are applied in this period to the BB20 unit. The year 2030 is the first representative period, which may be used to calculate the residual value. The discount rate set on the basis of the pre-tax weighted-average cost of capital (WACC), used for the calculation, was 7.38% (6.54% after tax). 0% growth rate was used to extrapolate the cash flow forecasts beyond 2030.
Based on the results of the tests, no need was found to recognize impairment losses on CGU CHP Elbląg.

Elektrociepłownia Kalisz („CGU CHP Kalisz")

The impairment test for CGU CHP Kalisz was conducted as at 30 November 2016. The value in use was calculated on the basis of financial projections for the period of December 2016 - December 2020 and residual value. The discount rate set on the basis of the pre-tax weighted-average cost of capital (WACC), used for the calculation, was 7.72% (6.54% after tax). The growth rate used to extrapolate cash flow projections beyond the period covered by detailed planning was adopted at the level of 2.0% which does not exceed the average long-term inflation growth rates in Poland.
Based on the results of the tests, no need was found to recognize impairment losses on CGU CHP Elbląg.

Reversal of impairment loss on Elektrownia Ostrołęka SA

In 2016, the impairment loss on property, plant and equipment under construction of the Elektrownia Ostrołęka SA subsidiary responsible for the execution of the Ostrołęka C project, was reversed. The impairment loss of PLN 123 m was recognized in 2012 in connection with the decision to halt the execution of the Ostrołęka C power plant construction project. The reversal was effected based on the decision of the Management Board of ENERGA SA to recommence the execution of the project, which resulted from the progress of work aimed at executing the investment project, including execution of general terms and conditions of cooperation with Polska Grupa Górnicza Sp. z o.o. setting out the rules of coal supply to the Ostrołęka power plant. This decision was confirmed in the Group's strategy for 2016-2025, where construction of a contemporary Ostrołęka C power plant with the capacity of approx. 1,000 MWe was stated as one of the key strategic projects. In addition to the coal supply contract, the project's profitability should be ensured by the expected implementation of Capacity Market solutions.

Sensitivity analysis

The estimated impact of the change of selected parameters on the overall valuation of the above-mentioned assets is presented below. The sensitivity analyses show that the factors with the highest impact on the estimated value in use of the above CGUs are: electricity prices, discount rates and coal prices. In case of their negative change, impairment losses may have to be recognized for the total amount specified below.

The sensitivity analysis takes into account the change of the factors over the entire forecast period.

Parameter	Amount and direction of change	Impact on overall appraisal value of tested CGUs [PLN m]		Change in impairment loss amount [PLN m]
		Increase in value	Decrease in value	
Electricity prices	[+ 1%]	103	-	(96)
	[- 1%]	-	(103)	90
Discount rates	[+ 0.5 p.p.]	-	(114)	62
	[- 0.5 p.p.]	134	-	(92)
Coal prices	[+ 1%]	-	(45)	42
	[- 1%]	45	-	(42)

If market conditions change, there is a risk that test results will be different in the future.

31 December 2016 (PLN millions)

14. Intangible assets

	Software, licenses and patents	Right of perpetual usufruct of land	Other intangible assets	Intangible assets not in use	Total
Gross value					
As at 1 January 2016	**594**	**87**	**52**	**103**	**836**
Direct purchase	2	1	-	82	**85**
Settlement of intangible assets not in use	115	-	10	(125)	**-**
Sale, disposal	(4)	(1)	-	-	**(5)**
Liquidation	(9)	-	-	-	**(9)**
Reclassification between groups	7	-	(7)	-	**-**
Other changes	-	-	1	2	3
As at 31 December 2016	**705**	**87**	**56**	**62**	**910**
Accumulated amortization and impairment losses					
As at 1 January 2016	**(402)**	**(21)**	**(18)**	**-**	**(441)**
Amortization for the period	(85)	(2)	(8)	-	**(95)**
Liquidation	9	-	-	-	**9**
Reclassification between groups	(5)	-	5	-	**-**
As at 31 December 2016	**(483)**	**(23)**	**(21)**	**-**	**(527)**
Net value as at 1 January 2016	**192**	**66**	**34**	**103**	**395**
Net value as at 31 December 2016	**222**	**64**	**35**	**62**	**383**

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14. Intangible assets (cont.)

	Software, licenses and patents	Right of perpetual usufruct of land	Other intangible assets	Intangible assets not in use	Total
Gross value					
As at 1 January 2015	**463**	**87**	**122**	**76**	**748**
Direct purchase	4	-	1	91	**96**
Settlement of intangible assets not in use	52	1	8	(61)	**-**
Sale, disposal	-	(1)	-	-	**(1)**
Liquidation	(4)	-	-	(3)	**(7)**
Reclassification between groups	79	-	(79)	-	**-**
As at 31 December 2015	**594**	**87**	**52**	**103**	**836**
Accumulated amortization and impairment losses					
As at 1 January 2015	**(276)**	**(18)**	**(61)**	**-**	**(355)**
Amortization for the period	(77)	(3)	(10)	-	**(90)**
Liquidation	4	-	-	-	**4**
Reclassification between groups	(53)	-	53	-	**-**
As at 31 December 2015	**(402)**	**(21)**	**(18)**	**-**	**(441)**
Net value as at 1 January 2015	**187**	**69**	**61**	**76**	**393**
Net value as at 31 December 2015	**192**	**66**	**34**	**103**	**395**

31 December 2016 (PLN millions)

15. Goodwill

In the current reporting period, in connection with the impairment test conducted with respect to the wind farms acquired in 2013, the entire goodwill amount of PLN 117 m recognized upon acquisition of the wind farm portfolio was written off. The test is described in note 13.

As at 30 November 2016, the Group conducted impairment tests of the remaining goodwill in the amount of PLN 26 m recognized as a result of the acquisition of heating assets and wind farms. The total tested goodwill amounted to PLN 26 m. The tests were conducted using the discounted cash flow method based on the projection of assets to which goodwill is attributed. The discount rates at the pre-tax weighted-average cost of capital (WACC) were used and fell within the range from 7.56% to 7.91%. Based on the results, no need was found to recognize impairment losses on other goodwill at the end of the reporting period.

Key assumptions used for testing are consistent with the assumptions of the impairment tests of property, plant and equipment and are described in Note 13.

The performed sensitivity analyses show that the key factor affecting the estimate of the value in use are the discount rate and projected price paths for electricity and prices of heat. In case of significant changes in market conditions there is a risk that test results will be different in the future.

No changes in the goodwill amount occurred in the previous year.

16. Investments in joint ventures measured by the equity method

The key information about investments in joint ventures are presented in note 2.2.1.

Below we present condensed financial information of PGG, which is measured by the equity method, and reconciliation of the financial information to the carrying amount of PGG shares recognized in the Group's consolidated financial statements.

Condensed statement of comprehensive income	8-month period ended 31 December 2016
	Polska Grupa Górnicza Sp. z o.o.
Revenue	3,828
Amortization and depreciation	910
Interest income	9
Interest expenses	48
(Loss)/profit before tax from continuing operations	**(387)**
Income tax	(55)
Net (loss)/profit on continuing operations	**(332)**
Net profit on discontinued operations	**-**
Other comprehensive income	**(11)**
Total comprehensive income	**(343)**
Dividends paid	**-**

Condensed balance sheet	As at 31 December 2016
	Polska Grupa Górnicza Sp. z o.o.
Cash and cash equivalents	310
Other current assets (excl. cash)	697
Total current assets	**1,007**
Non-current assets	**6,277**
Financial liabilities (excl. trade liabilities)	92
Others current liabilities (incl. trade liabilities)	2,424
Total current liabilities	**2,516**
Financial liabilities	1,148
Other liabilities	1,294
Total non-current liabilities	**2,442**
Net assets	**2,326**

16. Investments in joint ventures measured by the equity method (cont.)

Condensed financial information	2016
	Polska Grupa Górnicza Sp. z o.o.
Net assets of the joint venture at the beginning of the period	**2,302**
Net profit/(loss) for the period	(332)
Other comprehensive income	(11)
Recapitalization of the joint venture by investors	367
Net assets of the joint venture at the end of the period	**2,326**
Stake held by the Group in the company's shares	16.63%
Interest in the joint venture	387
Goodwill	3
Carrying amount of shares	**390**

There are no contingent liabilities or any other contractual liabilities related to the Group's shares in the joint venture.

Dividend payments to PGG shareholders is restricted by the bond issue program agreement ("Agreement") signed between PGG and its bondholders. The Agreement and the terms and conditions of issue of participation bonds allow for a dividend payment only when all of the following conditions are satisfied:

- in the settlement period when the dividend is paid out, a cash sweep redemption installment will be paid (a cash sweep may be effected in 2019 or later and will constitute in total 60% of the surplus cash flow for the previous financial year),
- there is no default on the specified financial ratios,
- the payment will not cause a default on the specified forecast financial ratios, and
- the dividend will be paid out to shareholders and holders of participation bonds, pro rata to their involvement in financing PGG.

17. Inventories

	31 December 2016			31 December 2015		
	Historical cost	Impairment losses	Net value	Historical cost	Impairment losses	Net value
Energy certificates of origin	330	-	**330**	351	-	**351**
Materials	66	(1)	**65**	94	(1)	**93**
CO2 emission allowances	38	-	**38**	34	-	**34**
Semi-finished products and production in progress	15	-	**15**	16	-	**16**
Merchandise	25	(1)	**24**	20	(1)	**19**
TOTAL	**474**	**(2)**	**472**	**515**	**(2)**	**513**

Group companies recognize impairment losses on inventories based on the loss of their economic usefulness determined by aging and turnover, down to the amount of the achievable net sale price.

18. CO_2 emission allowances

Greenhouse gas emission volumes and emission allowances awarded free of charge are presented in the table below:

CO_2 emission allowances	Year ended 31 December 2016	Year ended 31 December 2015
	(000s of tons)	
CO_2 emissions from all installations (thousands of tons), including:	**2,640**	**2,349**
Number of emission allowances received free of charge	1,084	1,408
Number of emission allowances paid for	1,556	941
Cost of the obligation to redeem CO_2 emission allowances (PLN m)	**43**	**33**

31 December 2016 (PLN millions)

19. Cash and cash equivalents

Cash in the bank earns interest at variable interest rates negotiated with banks, the level of which depends on the interest rate applicable to overnight bank deposits. Short-term deposits are made for different periods, from one day to three months, depending on the Group's current cash requirements and earn interest at interest rates negotiated individually with banks.

The balance of cash and cash equivalents presented in the statement of cash flows comprises the following items:

	As at 31 December 2016	As at 31 December 2015
Cash at bank and in hand	633	705
Short-term deposits up to 3 months	838	964
Total cash and cash equivalents presented in the statement of financial position	**1,471**	**1,669**
Unrealized foreign exchange differences and interest	(3)	1
Current account overdraft	(4)	(12)
Total cash and cash equivalents presented in the statement of cash flows	**1,464**	**1,658**
including restricted cash	*29*	-

20. Other assets

20.1. Other non-current assets

	As at 31 December 2016	As at 31 December 2015
Long-term prepayments and accrued expenses	60	50
Investment property	33	41
Advances for property, plant and equipment under construction and intangible assets	5	9
Long-term receivables	3	3
TOTAL	**101**	**103**

20.2. Other current assets

	As at 31 December 2016	As at 31 December 2015
VAT receivables	106	115
Advances for deliveries	31	58
Deferred costs	53	46
Other tax receivables	7	7
Other current assets	1	6
TOTAL	**198**	**232**

21. Share capital and other capital

21.1. Share capital

As at 31 December 2016, the share capital of ENERGA SA amounted to PLN 4,522 m and was divided into shares as specified below:

	As at 31 December 2016	As at 31 December 2015
AA series bearer shares with par value of PLN 10.92 each	269,139,114	269,139,114
BB series registered shares with par value of PLN 10.92 each	144,928,000	144,928,000
Total number of shares	**414,067,114**	**414,067,114**

31 December 2016 (PLN millions)

21. Share capital and other capital (cont.)

21.2. Major shareholders

	As at 31 December 2016	As at 31 December 2015
State Treasury		
share in capital	51.52%	51.52%
share in voting rights	64.09%	64.09%
Other shareholders		
share in capital	48.48%	48.48%
share in voting rights	35.91%	35.91%

21.3. Shareholders' rights

At the end of the reporting period, the State Treasury owned 213,326,317 shares of the Company, constituting 51.52% of its share capital and entitling to exercise 358,254,317 votes at the General Meeting, which makes up 64.09% of the total number of votes at the General Meeting (including 144,928,000 registered series BB shares, preferred with respect to the voting right at the General Meeting in such manner that one series BB share gives the right to two votes at the General Meeting).

According to the Parent Company's articles of association in effect on the date of these financial statements, Supervisory Board members are appointed and dismissed by the General Meeting, but the State Treasury is personally entitled to appoint and dismiss Supervisory Board members so that the State Treasury has an absolute majority of the votes in the Supervisory Board. The above entitlement expires on the date on which the State Treasury's share in the share capital falls below 20%.

21.4. Reserve capital

Reserve capital was created as a result of the share capital reduction made in connection with the reverse split of the parent company's shares in 2013 and upon distribution of the parent company's net profit for 2015. Reserve capital may be used only to cover future losses or to raise the parent company's share capital.

21.5. Supplementary capital

Supplementary capital was created from allowances from profit generated by the Parent Company in previous reporting periods.

Pursuant to the requirements of the Commercial Company Code, joint stock companies are required to create supplementary capital to cover losses. At least 8% of the company's profit for a given financial year presented in the company's financial statements is transferred to supplementary capital until the capital reaches at least one third of the company's share capital. The use of the supplementary capital is decided by the General Meeting, however, the portion of the supplementary capital representing one-third of the share capital may only be used to cover a loss posted in the financial statements and cannot be allocated to other purposes.

21.6. Cash flow hedge reserve

The cash flow hedge reserve follows from valuation of the transaction of cross-currency interest rate swaps (CCIRS) executed to hedge the currency exchange risk connected with Eurobonds issued by the subsidiary – ENERGA Finance AB (publ) and IRS interest rate swaps concluded to hedge interest rate risk related to the external financing used (see the description in Note 28.7).

21.7. Retained earnings and restrictions on dividend payment

The Group's retained earnings include amounts that are not subject to distribution, or cannot be paid out as dividend by the parent company. This refers, in particular, to the retained earnings of subsidiaries (taking into account consolidation adjustments), adjustments resulting from the transition of the parent company's financial statements from the Accounting Act to IFRS EU and actuarial gains and losses from the valuation of provisions for post-employment benefits recognized in other comprehensive income.

21.8. Non-controlling interest

As at 31 December 2016, equity attributable to non-controlling interest refer to minority shareholders of companies in the generation segment, in particular ENERGA Elektrownie Ostrołęka SA.

22. Earnings per share

There were no diluting instruments in the Parent Company and therefore diluted earnings per share are equal to basic earnings per share. The data used to calculate earnings per share are presented below.

22. Earnings per share (cont.)

	Year ended 31 December 2016	Year ended 31 December 2015
Net profit or loss on continuing operations attributable to equity holders of the Parent Company	151	832
Net profit or loss attributable to common equity holders of the Parent Company	**151**	**832**
Number of shares at the end of the reporting period (millions)	414	414
Number of shares used to calculate earnings per share (millions)	414	414
Earnings or loss per share on continuing operations (basic and diluted) (in PLN)	**0.36**	**2.01**

23. Dividends

	Year ended 31 December 2016	Year ended 31 December 2015
Dividends declared in the period		
dividend declared by subsidiaries	-	-
dividend declared by the Parent Company	203	596
TOTAL	**203**	**596**
Dividends paid in the period		
dividends paid in the period by subsidiaries to non-controlling interest	-	-
dividends paid in the period by the Parent Company	203	596
of which attributable to preferred shares	*71*	*209*
TOTAL	**203**	**596**

On 24 June 2016, the Annual General Meeting of the Parent Company adopted a resolution to distribute the 2015 profit, out of which PLN 203 m, i.e. PLN 0.49 per share, was allocated for a dividend to the Company's shareholders (the dividend in 2015 was PLN 1.44 per share).
By the date of approval of these financial statements for publication, the proposed distribution of the 2016 profit has not been adopted.

24. Provisions

24.1. Provisions for employee benefits

The Group measures provisions for post-employment benefits and for jubilee bonuses (see description in note 9.15) using actuarial methods.

The amounts of provisions for employee benefits and the reconciliation of changes to the balances are presented in the tables below.

	Pension and similar benefits	Energy tariff	Company Social Benefit Fund	Jubilee bonuses	Restructuring	TOTAL
As at 1 January 2016	**120**	**223**	**59**	**261**	**2**	**665**
Current service cost	5	3	2	11	-	**21**
Past service cost	(1)	-	-	(1)	-	**(2)**
Actuarial gains and losses, of which arising from changes in assumptions:	(6)	(36)	9	(43)	-	**(76)**
financial	(15)	(11)	(6)	(22)	-	**(54)**
demographic	7	(17)	16	(23)	-	**(17)**
other	2	(8)	(1)	2	-	**(5)**
Benefits paid	(3)	(10)	(3)	(22)	-	**(38)**
Interest costs	3	6	2	7	-	**18**
Reversed	-	(20)	-	-	-	**(20)**
Used	-	-	-	-	(1)	**(1)**
As at 31 December 2016, including:	**118**	**166**	**69**	**213**	**1**	**567**
Short-term	**8**	**9**	**3**	**19**	**1**	**40**
Long-term	**110**	**157**	**66**	**194**	**-**	**527**

31 December 2016 (PLN millions)

24. Provisions (cont.)

	Pension and similar benefits	Energy tariff	Company Social Benefit Fund	Jubilee bonuses	Restructuring	TOTAL
As at 1 January 2015	**108**	**209**	**71**	**241**	**18**	**647**
Current service cost	5	2	2	14	-	**23**
Actuarial gains and losses, of which arising from changes in assumptions:	4	16	(13)	11	-	**18**
financial	5	27	(7)	7	-	**32**
demographic	5	2	1	6	-	**14**
other	(6)	(13)	(7)	(2)	-	**(28)**
Benefits paid	(3)	(10)	(3)	(18)	-	**(34)**
Interest costs	3	6	2	7	-	**18**
Reversed	(1)	(2)	(1)	(2)	(10)	**(16)**
Used	-	-	-	-	(6)	**(6)**
Transfer from liabilities related to assets classified as held for sale	4	2	1	8	-	**15**
As at 31 December 2015, including:	**120**	**223**	**59**	**261**	**2**	**665**
Short-term	**4**	**10**	**3**	**20**	**2**	**39**
Long-term	**116**	**213**	**56**	**241**	**-**	**626**

Key assumptions adopted by the actuary to calculate the liability amounts at the end of the reporting period are as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Discount rate	3.29%	2.88%
Average employee turnover rate	3.96%	4.56%
Expected salary growth rate	3.00%	4.00%
Expected growth rate of the Company Social Benefit Fund ("ZFŚS") charge	3.00%	3.60%
Base of the ZFŚS charge	3.00%	3.00%
Expected energy equivalent growth rate	0.80%	0.70%

Based on data received from the actuary, the Group estimates that the change in assumptions would affect the amount of provisions for pension and similar benefits, jubilee bonuses, the company social benefit fund and the energy tariff as follows:

Actuarial provisions	Carrying amount	Analysis of sensitivity to discount rate changes		Analysis of sensitivity to salary growth rate changes		Analysis of sensitivity to energy equivalent changes	
	PLN	deviation in PLN					
		+0.5 p.p.	*-0.5 p.p.*	*+0.5%*	*-0.5%*	*+0.5%*	*-0.5%*
As at 31 December 2016							
Provision for pension and similar benefits	118	(6)	6	7	(6)	-	-
Energy tariff	166	(11)	12	-	-	7	(6)
Company Social Benefit Fund	69	(5)	6	5	(4)	-	-
Jubilee bonuses	213	(8)	9	8	(8)	-	-
TOTAL	**566**	**(30)**	**33**	**20**	**(18)**	**7**	**(6)**
Contribution to profit before tax		*8*	*(9)*	*(8)*	*8*	-	-

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24. Provisions (cont.)

Actuarial provisions	Carrying amount PLN	Analysis of sensitivity to discount rate changes – deviation in PLN: *discount rate +1 p.p.*	*discount rate -1 p.p.*	Analysis of sensitivity to changes in the provisions calculation base – deviation in PLN: *base +1%*	*base -1%*
As at 31 December 2015					
Provision for pension and similar benefits	120	(14)	17	16	(14)
Energy tariff	223	(43)	59	58	(43)
Company Social Benefit Fund	59	(10)	13	13	(10)
Jubilee bonuses	261	(23)	27	26	(23)
TOTAL	**663**	**(90)**	**116**	**113**	**(90)**
Contribution to profit before tax		*23*	*(27)*	*(26)*	*23*

24.2. Other provisions

	Legal claims	Land reclamation and liquidation costs	Liabilities for gas emissions	Obligation to redeem certificates	Other provisions	TOTAL
As at 1 January 2016	**97**	**38**	**33**	**247**	**55**	**470**
Interest costs	-	2	-	-	-	2
Recognized	53	13	44	409	82	601
Reversed	(17)	(3)	-	-	(4)	(24)
Used	(2)	-	(36)	(251)	(38)	(327)
As at 31 December 2016, including:	**131**	**50**	**41**	**405**	**95**	**722**
Short-term	**131**	**-**	**41**	**405**	**94**	**671**
Long-term	**-**	**50**	**-**	**-**	**1**	**51**

* The recognition amount for the provision for reclamation and liquidation costs in 2016 arises from changes in the estimated amounts; provision reversal results from a change in the discount rate to 3.62%.

	Legal claims	Land reclamation and liquidation costs	Liabilities for gas emissions	Obligation to redeem certificates	Other provisions	TOTAL
As at 1 January 2015	**83**	**36**	**40**	**154**	**46**	**359**
Interest costs	-	1	-	-	-	1
Recognized	33	3	33	258	45	372
Reversed	(18)	(2)	-	-	(3)	(23)
Used	(1)	-	(40)	(165)	(33)	(239)
As at 31 December 2015, including:	**97**	**38**	**33**	**247**	**55**	**470**
Short-term	**97**	**-**	**33**	**247**	**55**	**432**
Long-term	**-**	**38**	**-**	**-**	**-**	**38**

* The recognition amount for the provision for reclamation and liquidation costs in 2015 arises from changes in the estimated amounts; provision reversal results from a change in the discount rate to 2.88%.

31 December 2016 (PLN millions)

24. Provisions (cont.)

Provision for land reclamation and liquidation costs

In 2008, ENERGA Elektrownie Ostrołęka SA recognized the provision for ash landfills reclamation, which will be amortized until 2050.

This category also presents provisions for the dismantling costs of the following wind farms:

- FW Bystra – provision recognized in 2012 and amortized until 2037,
- FW Karścino, FW Mołtowo, FW Krukowo – provisions recognized in 2009 and amortized until 2034,
- FW Karcino – provision recognized in 2010 and amortized until 2035,
- FW Myślino – provision recognized in 2015 and amortized until 2040.
- FW Parsówek – provision recognized in 2016 and amortized until 2041.

Provisions for legal claims

As a result of transition to a different political system, in the 1990s, serious problems arose in the present legal and economic system with transmission installations built in the former legal system on private properties. The main purpose of the provisions for legal claims are the court cases relating to power infrastructure located on private land without the necessary legal titles. The balance of these provisions was PLN 82 m at the end of 2016 and PLN 79 m at the end of 2015.

Other provisions

This category contains mainly provisions for excise tax, that is tax liability calculated on the quantities of electricity sold to end users and property tax.

25. Other current liabilities

	As at 31 December 2016	As at 31 December 2015
Liabilities on account of taxes, customs duties, social security, salaries and others	**108**	**115**
VAT	36	47
Liabilities on social security insurance	43	41
Personal income tax	16	15
Environmental and other fees	12	11
Other	1	1
Other non-financial liabilities	**125**	**142**
Amounts paid by business partners relating to future periods and advances received	92	105
Payroll liabilities	31	28
Liabilities to employees on account of restructuring severance pay	-	8
Other	2	1
TOTAL	**233**	**257**

26. Deferred income and grants

	As at 31 December 2016	As at 31 December 2015
Connection fees	267	279
Grants received	203	206
Property, plant and equipment acquired free of charge	65	64
Rental income	15	12
Accruals for annual bonus and other employee bonuses	95	89
Accruals for unused holiday leaves	29	27
Awards for Management Boards	9	8
Other prepayments and accruals	2	7
TOTAL, of which:	**685**	**692**
Long-term	**515**	**531**
Short-term	**170**	**161**

As at 31 December 2016, the Group recognizes as grants: primarily, the valuation effect of the preferential loan from the European Investment Bank in the amount of PLN 88 m, which is recognized over the loan repayment period (see descriptions in Notes 9.19 and 28.6) and co-financing of PLN 34 m received to execute the biomass-fired power unit building project in Elbląg, which is recognized over the depreciation period of the assets until 2054. In the case of the co-financing of the construction of the unit in Elbląg, the Group is obligated to achieve appropriate performance ratios (specified production of electricity and heat) throughout the duration of the project. Additionally, the Generation segment companies received funding from the National Fund for Environmental Protection and Water Management in the amount of PLN 33 m for rebuilding district heating networks.

31 December 2016 (PLN millions)

27. Assets and liabilities of the Company Social Benefit Fund

Pursuant to the Social Benefit Fund Act of 4 March 1994, as amended, the Company Social Benefit Fund is established by employers (companies) employing more than 20 employees on a full time equivalent basis. Group companies establish such funds and make periodic allowances. The funds of ENERGA SA Group companies contain no property, plant and equipment. The purpose of the Funds is to subsidize the social activity of the individual Group companies, grant loans to employees and subsidize other social expenses, such as co-payments to employee holidays.

Group companies have offset the Fund's assets with their liabilities towards the Fund on the individual level, because these assets do not constitute separate assets of the companies.

The table below presents the structure of the Funds' assets, liabilities and expenses.

	As at 31 December 2016	As at 31 December 2015
Loans granted to employees	10	11
Cash	4	5
Fund's liabilities	14	16
Balance after set-off	**-**	**-**
Charges to the fund in the period	30	30

31 December 2016 (PLN millions)

NOTES ON FINANCIAL INSTRUMENTS

28. Financial instruments

28.1. Carrying value of financial instruments by category and class

As at 31 December 2016	Financial assets at fair value through profit or loss	Loans and receivables	Cash and cash equivalents	Financial liabilities measured at amortized cost	Hedging derivatives	Financial instruments excluded from the scope of IAS 39	TOTAL
Assets							
Trade receivables	-	1,947	-	-	-	-	**1,947**
Portfolio of financial assets	2	-	-	-	-	-	**2**
Cash and cash equivalents	-	-	1,471	-	-	-	**1,471**
Other financial assets	-	34	-	-	147	-	**181**
Bonds, treasury bills and other debt instruments	-	17	-	-	-	-	**17**
Derivative financial instruments	-	-	-	-	147	-	**147**
Other	-	17	-	-	-	-	**17**
TOTAL	**2**	**1,981**	**1,471**	**-**	**147**	**-**	**3,601**
Liabilities							
Loans and borrowings	-	-	-	3,420	-	-	**3,420**
Preferential loans and borrowings	-	-	-	1,488	-	-	**1,488**
Loans and borrowings	-	-	-	1,928	-	-	**1,928**
Current account overdraft	-	-	-	4	-	-	**4**
Bonds issued	-	-	-	2,717	-	-	**2,717**
Trade liabilities	-	-	-	811	-	-	**811**
Other financial liabilities	-	-	-	151	-	12	**163**
Liabilities on purchase of property, plant and equipment and intangible assets	-	-	-	132	-	-	**132**
Other	-	-	-	19	-	12	**31**
TOTAL	**-**	**-**	**-**	**7,099**	**-**	**12**	**7,111**

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28. Financial instruments (cont.)

As at 31 December 2015	Financial assets at fair value through profit or loss	Loans and receivables	Cash and cash equivalents	Financial liabilities measured at amortized cost	Hedging derivatives	Financial instruments excluded from the scope of IAS 39	TOTAL
Assets							
Trade receivables	-	1,762	-	-	-	-	**1,762**
Portfolio of financial assets	322	-	-	-	-	-	**322**
Cash and cash equivalents	-	-	1,669	-	-	-	**1,669**
Other financial assets	-	58	-	-	40	-	**98**
Bonds, treasury bills and other debt instruments	-	*19*	-	-	-	-	***19***
Derivative financial instruments	-	-	-	-	*40*	-	***40***
Other	-	*39*	-	-	-	-	***39***
TOTAL	**322**	**1,820**	**1,669**	**-**	**40**	**-**	**3,851**
Liabilities							
Loans and borrowings	-	-	-	2,678	-	-	**2,678**
Preferential loans and borrowings	-	-	-	*1,550*	-	-	***1,550***
Loans and borrowings	-	-	-	*1,116*	-	-	***1,116***
Current account overdraft	-	-	-	*12*	-	-	***12***
Bonds issued	-	-	-	3,192	-	-	**3,192**
Trade liabilities	-	-	-	877	-	-	**877**
Other financial liabilities	-	-	-	186	8	24	**218**
Liabilities on purchase of property, plant and equipment and intangible assets	-	-	-	*155*	-	-	***155***
Derivative financial instruments	-	-	-	-	*8*	-	***8***
Other	-	-	-	*31*	-	*24*	***55***
TOTAL	**-**	**-**	**-**	**6,933**	**8**	**24**	**6,965**

31 December 2016 (PLN millions)

28. Financial instruments (cont.)

28.2. Items of income, expenses, profits and losses recognized in the statement of comprehensive income by category of financial instruments

Year ended 31 December 2016	Assets measured at fair value through profit or loss	Loans and receivables	Cash and cash equivalents	Financial liabilities measured at amortized cost	Derivatives	TOTAL
Interest income/(cost)	3	41	9	(201)	(36)	**(184)**
Foreign exchange differences	-	-	5	(81)	69	**(7)**
Reversal of impairment losses/increase in value	-	35	-	-	-	**35**
Recognition of impairment losses/decrease in value	-	(97)	-	-	-	**(97)**
Net profit/(loss)	**3**	**(21)**	**14**	**(282)**	**33**	**(253)**
Other comprehensive income	-	-	-	-	43	**43**
Comprehensive income	**3**	**(21)**	**14**	**(282)**	**76**	**(210)**

Year ended 31 December 2015	Assets measured at fair value through profit or loss	Loans and receivables	Cash and cash equivalents	Financial liabilities measured at amortized cost	Derivatives	TOTAL
Interest income/(cost)	11	24	23	(213)	(48)	**(203)**
Foreign exchange differences	(3)	-	-	-	-	**(3)**
Reversal of impairment losses/increase in value	-	32	-	-	-	**32**
Recognition of impairment losses/decrease in value	-	(72)	-	-	-	**(72)**
Net profit/(loss)	**8**	**(16)**	**23**	**(213)**	**(48)**	**(246)**
Other comprehensive income	-	-	-	-	28	**28**
Comprehensive income	**8**	**(16)**	**23**	**(213)**	**(20)**	**(218)**

31 December 2016 (PLN millions)

28. Financial instruments (cont.)

28.3. Fair value of financial instruments

28.3.1. Financial instruments measured at fair value on an ongoing basis

Some of the Group's financial assets and liabilities are measured at fair value at the end of each reporting period.

The table below analyses fair value measurements for financial assets and financial liabilities categorised into three level hierarchy:

- level 1 – fair value based on quoted prices (unadjusted) in active markets for identical assets or liabilities that the Group can access at the measurement date;
- level 2 – fair value based on inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly;
- level 3 – fair value based on unobservable inputs for the asset or liability.

	31 December 2016	31 December 2015
	Level 2	Level 2
Assets		
Portfolio of financial assets	2	322
Hedging derivatives (CCIRS I)	135	38
Hedging derivatives (CCIRS II)	8	2
Hedging derivatives (IRS)	4	-
Liabilities		
Hedging derivatives (IRS)	-	8

The Group measures participation units in the ENERGA Trading SFIO fund as the product of their quantity and the value of a single participation unit, as measured by the fund management company pursuant to the Mutual Funds Act of 27 May 2004.

Cross Currency Interest Rate Swaps (CCIRSs) and Interest Rate Swaps (IRSs) are measured at fair value by discounting future cash flows. The interest rates and the basis spread used in discounting are obtained from Bloomberg.

28.3.2. Financial instruments not measured at fair value on an ongoing basis

Except for the information given in the table below, the carrying amounts of financial assets and liabilities do not depart in a material way from their fair values.

Liabilities arising from the issue of Eurobonds	Carrying amount	Fair value Level 1
As at 31 December 2016	2,261	2,408
As at 31 December 2015	2,176	2,266

Fair value measurement of liabilities arising from the issue of Eurobonds was estimated on the basis of quotations from the Bloomberg system from 31 December 2016, which are determined based on transactions on the Luxembourg stock exchange and over-the-counter trading.
The Group also holds bonds with a variable interest rate, which are listed on the regulated market operated by BondSpot S.A. The market is not liquid and transactions on it are concluded incidentally, what makes that the quotations do not reflect the fair value of the bonds.

28.4. ENERGA Trading SFIO fund

The Group has been investing in a portfolio of assets financed through the Fund in which it has 100% participation units.

The Fund has been established to manage financial surpluses of ENERGA Group companies and is an alternative to bank deposits, even overnight deposits. The fund is high liquidity and low risk. Mechanisms embedded in the fund settlement system offer the redemption of Fund units to cash on the same or the next business day. Additionally, ENERGA Group companies may offset their mutual receivables and liabilities using the units in the Fund.

The Group classifies the following assets within the Fund portfolio structure:

- treasury bills and bonds,
- corporate debt instruments – financial sector,
- corporate debt instruments – non-financial sector,
- bonds issued by Bank Gospodarstwa Krajowego,
- mortgage bonds,
- municipal bonds,
- other.

31 December 2016 (PLN millions)

28. Financial instruments (cont.)

The following table presents the structure of the Fund's assets at the end of the reporting period and comparative periods.

	As at 31 December 2016	As at 31 December 2015
Treasury bills and bonds	2	115
Corporate debt instruments – financial sector	-	51
Corporate debt instruments – non-financial sector	-	29
Bonds issued by Bank Gospodarstwa Krajowego	-	47
Mortgage bonds	-	63
Municipal bonds	-	17
TOTAL	**2**	**322**

28.5. Description of material items in individual categories of financial instruments

28.5.1. Financial assets

Loans and receivables

The main item of the loans and receivables category are trade receivables.

Trade receivables	Not overdue	Overdue (days)					Total
		<30	30–90	90-180	180-360	>360	
As at 31 December 2016							
Before impairment losses	1,658	152	93	41	46	262	**2,252**
Impairment losses	(1)	(3)	(4)	(5)	(31)	(261)	**(305)**
After impairment losses	**1,657**	**149**	**89**	**36**	**15**	**1**	**1,947**
As at 31 December 2015							
Before impairment losses	1,502	165	67	29	40	245	**2,048**
Impairment losses	(1)	(2)	(4)	(5)	(29)	(245)	**(286)**
After impairment losses	**1,501**	**163**	**63**	**24**	**11**	**-**	**1,762**

Hedging derivatives

Hedging derivatives, CCIRS and IRS, are described in detail in Note 28.7.

Financial assets at fair value through profit or loss

The Group classifies its investments in the portfolio of financial assets, which consists of participation units in the ENERGA Trading SFIO Fund, as financial assets at fair value through profit or loss.

Impairment losses on financial assets

	Impairment losses on trade receivables	Impairment losses for bonds, treasury bills and other debt instruments
Impairment losses as at 1 January 2016	**286**	**25**
Recognition of impairment losses	97	-
Used	(43)	-
Unused amounts written off (reversal of the allowance)	(35)	-
Impairment losses as at 31 December 2016	**305**	**25**
Impairment losses as at 1 January 2015	**284**	**25**
Recognition of impairment losses	72	-
Used	(38)	-
Unused amounts written off (reversal of the allowance)	(32)	-
Impairment losses as at 31 December 2015	**286**	**25**

31 December 2016 (PLN millions)

28. Financial instruments (cont.)

28.5.2. Financial liabilities

All of the Group's financial liabilities are classified as financial liabilities measured at amortized cost, except for hedging derivatives. This category of the Group's financial instruments includes primarily contracted loans and borrowings and issued bonds.

Loans and borrowings

	As at 31 December 2016	As at 31 December 2015
Currency	PLN	
Reference rate	WIBOR, Rediscount rate	
Value of the loan/borrowing	**3,420**	**2,678**
Of which maturing in:		
up to 1 year (short-term)	334	203
1 to 2 years	357	223
2 to 3 years	372	259
3 to 5 years	776	561
over 5 years	1,581	1,432

As at 31 December 2016 and 31 December 2015, the amount of credit limits available to the Group was PLN 4,326 m (79.6% used) and PLN 4,763 m (57.4% used), respectively.

Detailed information on contracted loans and borrowings is presented in Note 28.6.

Liabilities under bonds issued

	As at 31 December 2016	As at 31 December 2015
Currency	PLN	
Reference rate	WIBOR	
Value of the issue	**456**	**1,016**
of which maturing in:		
up to 1 year (short-term)	14	16
2 to 3 years	442	-
3 to 5 years	-	1,000

	As at 31 December 2016	As at 31 December 2015
Currency	EUR	
Reference rate	fixed	
Value of the issue		
in currency	511	511
in PLN	2,261	2,176
of which maturing in:		
up to 1 year (short-term)	64	60
3 to 5 years	2,197	2,116

Detailed information on bonds issued is provided in Note 28.6.

28.6. Available external financing

In the current reporting period, the following external financing from International Financial Institutions were disbursed:

- on 9 December 2016, the last tranche in the amount of PLN 200 m of the loan from the European Investment Bank granted under the agreement of 10 July 2013,
- on 19 December 2016, the last tranche in the amount of PLN 276 m of the loan from the European Bank of Reconstruction and Development granted under the agreement of 29 April 2010,
- on 19 December 2016, the last tranche in the amount of PLN 460 m of the loan from the European Bank of Reconstruction and Development granted under the agreement of 26 June 2013.

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28. Financial instruments (cont.)

In the current reporting period and as at the last day of the reporting period and as at the date of approving these financial statements for publication, there were no events of default on contractual obligations under the terms and conditions of any external funding acquired.

Financing institution	Type of liability	Purpose of financing	Date of the agreement	Financing limit	Available financing amount	Nominal debt as at 31.12.2016	Repayment date
European Investment Bank	Loan	ENERGA-OPERATOR SA Investment Program	16-12-2009	1,050	-	720	15-12-2025
European Investment Bank	Loan	ENERGA-OPERATOR SA Investment Program	10-07-2013	1,000	-	1,000	15-09-2031
European Bank for Reconstruction and Development	Loan	ENERGA-OPERATOR SA Investment Program	29-04-2010	1,076	-	741	18-12-2024
European Bank for Reconstruction and Development	Loan	ENERGA-OPERATOR SA Investment Program	26-06-2013	800	-	762	18-12-2024
Nordic Investment Bank	Loan	ENERGA-OPERATOR SA Investment Program	30-04-2010	200	-	119	15-06-2022
Bondholders	Eurobonds	General corporate purposes	19-03-2013	2,212*	-	2,212*	19-03-2020
Bondholders	Domestic bonds	General corporate purposes	19-10-2012	1,000	-	442	19-10-2019
PKO Bank Polski SA	Credit limit	General corporate purposes	30-08-2011	3	-	3	31-12-2019
PKO Bank Polski SA	Credit limit	General corporate purposes	12-10-2011	300	300	-	07-06-2021
PKO Bank Polski SA	Bonds	ENERGA Elektrownie Ostrołęka SA Investment Program	30-05-2012	100	67	-	31-12-2022
PKO Bank Polski SA	Credit limit	General corporate purposes	20-09-2012	200	121	79**	19-09-2017
Bank PEKAO SA	Renewable loan	General corporate purposes	13-10-2011	500	500	-	29-05-2020
Bank PEKAO SA	Loan	ENERGA Elektrownie Ostrołęka SA Investment Program	30-05-2012	85	-	21	29-05-2022
Nordic Investment Bank	Loan	FW Myślino construction	23-10-2014	68	-	61	15-09-2026
TOTAL				**8,741**	**988**	**6,160**	

* liability in amount of EUR 500 m converted using the middle exchange rate for 31 December 2016
** the limit amount has been used in the form of a bank guarantees

28.7. Cash flow hedge accounting

FX risk hedging

The special purpose vehicle ENERGA Finance AB (publ) (the issuer of Eurobonds – see description in Note 28.6) and ENERGA SA signed two loan agreements denominated in EUR for the total amount of EUR 499 m. In order to hedge currency risk under these loans, in 2013 and in July 2014, the Group concluded cross-currency interest rate swap transactions with nominal values of EUR 400 m (CCIRS I) and EUR 25 m (CCIRS II), respectively.

As a hedged position under the above hedging relationships the Group designated the foreign currency risk arising from intra-group loans denominated in EUR. The foreign currency risk is hedged at the level of 85% of the total nominal amount of loans.

As the hedge the Group designated CCIRS transactions under which the Group receives fixed-rate cash flows in EUR and pays fixed-rate cash flows in PLN. Cash flows received by the Group correspond with the cash flows under the intra-group loans. The Group expects that the hedged cash flows will continue until March 2020.

Consolidated financial statements for the year ended 31 December 2016 (PLN millions)

28. Financial instruments (cont.)

Interest rate risk hedging

In January 2016, the Group concluded interest rate swap transactions to hedge the interest rate risk arising from the financing used under (see description in note 28.6):

- loan agreement concluded with EIB in 2013 – PLN 200 m;
- loan agreement concluded with EBRD in 2010 – PLN 200 m.

In August 2016, the Group additionally concluded IRS transactions with similar characteristics for the following:

- loan agreement concluded with EBRD in 2010 – PLN 150 m;
- loan agreement concluded with EBRD in 2013 – PLN 150 m;
- loan agreement concluded with EIB in 2013 – PLN 150 m.

As hedged positions under hedging relationships, the Group designated the risk related to the WIBOR 3M interest rate arising from interest payments on the financial liabilities stated above in the period no longer than 2 years from the date of the hedging transactions. In the case of the PLN 150 m transaction pertaining to the 2013 EIB loan agreement, this is a four-year period.

As the hedge the Group designated the IRS transactions under which the Group receives floating-rate cash flows in PLN and pays fixed-rate cash flows in PLN. Interest cash flows received by the Group correspond with interest cash flows under the hedged financial liabilities. The Group expects that the hedged cash flows will continue until June 2020 and not longer.

Additionally, the IRS transactions concluded in June 2014 expired in June 2016. They previously hedged the interest rate risk arising from the financing used in the amount of PLN 1,940 m.

Fair value of hedges

The fair value of hedges was:

	Value	Recognition in the statement of financial position
As at 31 December 2016		
CCIRS I	135	Non-current assets – Other financial assets
CCIRS II	8	Non-current assets – Other financial assets
IRS	4	Non-current assets – Other financial assets
As at 31 December 2015		
CCIRS I	38	Non-current assets – Other financial assets
CCIRS II	2	Non-current assets – Other financial assets
IRS	8	Equity and liabilities – Other non-current financial liabilities

Under cash flow hedge accounting, the cash flow hedge reserve (the effective portion of changes in the value of the hedge, less deferred tax) increased in the reporting period by PLN 35 m.

The table below presents changes in the cash flow hedge reserve resulting from the hedge accounting in the reporting period:

Change in cash flow hedge reserve during the reporting period	Year ended 31 December 2016	Year ended 31 December 2015
At the beginning of the reporting period	**6**	**(17)**
Amount recognized in the cash flow hedge reserve in the period, equal to the change in the fair value of hedging instruments	112	26
Accrued interest transferred from the reserve to financial income/costs	-	2
Revaluation of hedging instruments transferred from the reserve to financial income/costs	(69)	-
Income tax on other comprehensive income	(8)	(5)
At the end of the reporting period	**41**	**6**

As at 31 December 2016, no inefficiencies were identified resulting from the applied cash flow hedge accounting.

28. Financial instruments (cont.)

28.8. Collateral securing repayment of liabilities

At the end of the reporting period, there were no material assets securing repayment of liabilities or contingent liabilities. As at 31 December 2015, the carrying amount of assets securing repayment of liabilities, primarily the loan granted to ENERGA Elektrownie Ostrołęka SA by the National Fund for Environmental Protection and Water Management and the guarantees extended by banks to contractors of ENERGA-OBRÓT SA, was PLN 124 m.

29. Financial risk management principles and objectives

The major financial instruments used by the Group include bank loans, bonds, cash, short-term investments and hedging instruments. The main purpose of these financial instruments is to secure funds to finance the Group's operations or to mitigate financial risks.

Key risks generated by the Group's financial instruments include:

- market risk,
- liquidity risk,
- credit risk.

The Management Board verifies and agrees the principles of managing these risks. In 2014, the Management Board of ENERGA SA approved and introduced the ENERGA Group Liquidity Management Policy and the ENERGA Group Market Risk Management Policy (applicable to FX risk and interest rate risk). The two documents have been introduced across the ENERGA Group, which allows the holding company to manage these risks effectively. Both documents define financial risk management procedures for individual Group companies and introduce appropriate reporting obligations.

29.1. Market risk

The Group identifies the following major market risks to which it is exposed:

- interest rate risk,
- foreign exchange risk,
- commodity price risk.

For the purposes of sensitivity analysis to changes in market risk factors, the ENERGA Group uses scenario analysis method, which uses expert scenarios reflecting the Group's subjective judgment on how individual market risk factors will develop in the future.

Scenario analyses presented in this item aim to analyze the impact of changes in market risk factors on the Group's financial results. Only those items, which satisfying the definition of financial instruments, are subject to analysis.

Interest rate risk

The ENERGA Group is exposed to interest rate risk in connection with the fact that it holds assets and liabilities for which income and expenses are calculated on the basis of market interest rates, which are subject to change.

The Group identifies exposure to the risk of WIBOR interest rate changes, which involves primarily long-term financial debt. The Group's financial policy envisages that the risk of changing interest rates is mitigated by keeping a portion of debt at fixed rates. Additionally, at the holding company level the ENERGA Group has entered into a number of transaction hedging the interest rate risk (IRS). As at 31 December 2016, 51% of financial debt (2015: 70%) recorded in the statement of financial position (loans and borrowings and bonds issued) bore a fixed interest rate or was hedged against interest rate risk with IRS transactions.

In interest rate risk sensitivity analysis, the Group uses a parallel shift of the interest rate curve by the possible change in reference interest rates in the coming year. The levels of reference interest rates on the final day of a reporting period were used for this purpose. The extent of potential changes to interest rates was assessed on the basis of volatility of implied options per interest rate quoted on the inter-bank market. in the case of WIBOR, due to the low liquidity of the interest rate option market, the shift of the yield curve has been assumed arbitrarily.

In the case of analysis of sensitivity to interest rate changes, the effect of changes to risk factors would be carried to:

- other comprehensive income for hedging derivatives,
- interest income/cost for other financial instruments.

The table below presents sensitivity of financial result before tax and other comprehensive income to reasonably possible interest rate changes, assuming that there are no variations in other risk factors for these financial instrument classes that are exposed to interest rate risk:

31 December 2016 (PLN millions)

29. Financial risk management principles and objectives (cont.)

Financial assets and liabilities	31 December 2016		Interest rate risk sensitivity analysis as at 31 December 2016			
	Carrying amount	Value at risk	WIBOR		EURIBOR	
	PLN	PLN	*WIBOR +50 bp*	*WIBOR -50 bp*	*EURIBOR +20 bp*	*EURIBOR -20 bp*
Assets						
Cash and cash equivalents	1,471	1,471	7	(7)	(1)	1
Liabilities						
Preferential loans and borrowings	1,488	1,488	(7)	7	-	-
Loans and borrowings granted on market terms	1,928	1,928	(10)	10	-	-
Bonds and debt securities issued	2,717	456	(2)	2	-	-
Current account overdraft	4	4	-	-	-	-
Change in profit before tax			**(12)**	**12**	**(1)**	**1**
Hedging derivatives (assets)	147	147	35	(35)	(14)	14
Change in other comprehensive income			**35**	**(35)**	**(14)**	**14**

Financial assets and liabilities	31 December 2015		Interest rate risk sensitivity analysis as at 31 December 2015			
	Carrying amount	Value at risk	WIBOR		EURIBOR	
	PLN	PLN	*WIBOR +50 bp*	*WIBOR -50 bp*	*EURIBOR +20 bp*	*EURIBOR -20 bp*
Assets						
Cash and cash equivalents	1,669	1,669	8	(8)	(1)	1
Liabilities						
Preferential loans and borrowings	1,550	1,550	(8)	8	-	-
Loans and borrowings granted on market terms	1,116	1,116	(6)	6	-	-
Bonds and debt securities issued	3,192	1,016	(5)	5	-	-
Current account overdraft	12	12	-	-	-	-
Change in profit before tax			**(11)**	**11**	**(1)**	**1**
Hedging derivatives (assets)	40	40	38	(39)	(17)	18
Hedging derivatives (liabilities)	8	8	2	(2)	-	-
Change in other comprehensive income			**40**	**(41)**	**(17)**	**18**

Foreign exchange risk

The Group is exposed to foreign currency risk on account of trade and financial transactions that it concludes. The risk arises as a result of the Group companies entering into purchase and sale transactions or incurring financial liabilities in currencies other than the valuation currency or holding financial assets in such currencies. The Group identifies primarily the exposure to the risk of changes in the EUR/PLN exchange rate.

In the foreign exchange risk sensitivity analysis, the possible fluctuations of currency exchange rates were calculated on the basis of annual variability implied for currency options quoted on the inter-bank market for the given currency pair at the date ending the reporting period.

The table below presents sensitivity of the financial result before tax and other comprehensive income to reasonably possible changes of exchange rates, assuming that there are no changes of other risk factors for such classes of financial instruments which are exposed to the exchange rate change risk:

31 December 2016 (PLN millions)

29. Financial risk management principles and objectives (cont.)

Financial assets and liabilities	31 December 2016		FX risk sensitivity analysis as at 31 December 2016	
	Carrying amount	Value at risk	EUR/PLN	
	PLN	*PLN*	*EUR/PLN rate +8.0%*	*EUR/PLN rate -8.0%*
Assets				
Trade receivables	1,947	22	2	(2)
Cash and cash equivalents	1,471	255	20	(20)
Hedging derivatives	147	2,120	170	(170)
Liabilities				
Trade liabilities	811	11	(1)	1
Bonds and debt securities issued	2,717	2,261	(181)	181
Change in profit before tax			**(9)**	**9**
Change in other comprehensive income*			**19**	**(19)**

* in respect to hedging derivatives

Financial assets and liabilities	31 December 2015		FX risk sensitivity analysis as at 31 December 2015	
	Carrying amount	Value at risk	EUR/PLN	
	PLN	*PLN*	*EUR/PLN rate +7.0%*	*EUR/PLN rate -7.0%*
Assets				
Trade receivables	1,762	17	1	(1)
Cash and cash equivalents	1,669	279	20	(20)
Hedging derivatives	40	2,084	127	(127)
Liabilities				
Trade liabilities	877	11	(1)	1
Bonds and debt securities issued	3,192	2,176	(152)	152
Change in profit before tax			**(24)**	**24**
Change in other comprehensive income*			**19**	**(19)**

* in respect to hedging derivatives

With regard to trade transactions, the Group is not exposed, to a material extent, to the exchange rate risk because the Group's cash settlements are mainly in PLN.

With regard to financial transactions, the Group is exposed to currency exchange risk because of loans within the Group connected with issued Eurobonds. To hedge that risk, the Group has entered into cross-currency interest rate swap (CCIRS) transactions and has implemented hedge accounting (see the description in Note 28.7).

Commodity risk

The Group is exposed to risks tied to variation in prices of commodities used in the operating activity.

The most significant risk is the risk of changing purchase prices of electricity and certificates of origin on the wholesale market in long-, medium- and short-term contracts executed by ENERGA-OBRÓT SA on the Polish market, and financial instruments on foreign markets, such as futures/forward contracts for electricity, CO_2 emission allowances.

29. Financial risk management principles and objectives (cont.)

Accordingly, it is important to refer the actual risk exposure to the assumed financial result for the year. Market risk exposure arises on all open positions (transactions) and it is mitigated using the Value at Risk (VaR) risk management model. The model mitigates market risk related to, among others, volatility of electricity prices, prices of CO_2 certificates or property rights. The model assumes that risk is incurred within the acceptable boundaries only for an open position of the product portfolio, by imposing risk exposure limits on each portfolio and for ENERGA-OBRÓT SA as a whole. Value at Risk (VaR) is regularly monitored and reported to make sure that it does not exceed the set levels and takes into account, among others, the open position volume (difference between volume sold and bought), volatility of product prices and correlation between individual products in the portfolio.

Additionally, to mitigate the risk associated with the volatility of electricity purchase prices on the wholesale end user contracting market, the following hedging measures are taken:

- the open position on the electricity portfolio is minimized; this involves coordination and optimization of the purchasing and selling process to ensure that the difference between volumes purchased and sold do not exceed the pre-defined levels.
- contracts are concluded in specific proportions and for different products,
- volume limits are set for the open position for participation on selected markets, minimizing risk related to large fluctuations of electricity prices on the market.
- mark to market valuation of the open position.

Additionally, as part of the trading activity on CO_2 emission allowances (EUA) and emission reduction certificates (CER), to reduce the possible loss, Stop Loss and Take Profit (SL/TP) levels are set for each transaction and are monitored on an ongoing basis.

29.2. Credit risk

In the Group, credit risk is defined as the probability that a counterparty defaults on its financial obligations. Credit risk is minimized by actions aiming at value-based risk assessment, monitoring the counterparties' financial standing and securing trade credit by available instruments such as bank guarantees, sureties, etc.

Credit risk is reduced in the case of counterparties having the highest turnover, or the portfolios of wholesalers and strategic clients. The following are of special importance in this respect: credit rating, trade limits, special provisions in agreements with counterparties and obtaining security from clients with a low credit rating.

In the Group, appropriate procedures have been established to minimize the risk of counterparties' insolvency. On the wholesale energy market, the procedures set the limits for possible electricity sales without requiring security. Transactions above the limit require security, such as bank guarantees.

For sales to strategic and business clients, the procedures impose the duty to rate clients' creditworthiness. For clients with a low credit rating, the sales may begin on the condition that security acceptable to the seller is obtained.

Moreover, thanks to the ongoing monitoring of the status of receivables, the Group's exposure to the risk of uncollectable receivables is minor.

With respect to the Group's other financial assets, such as cash and cash equivalents and certain derivatives, the Group's credit risk arises when the other party to a contract is unable to make a payment and the maximum exposure to this risk equals the carrying amount of such instruments.

In the financial area, credit risk is mitigated through ongoing monitoring of the ratings of financial institutions and by limiting the risk of concentrating cash surpluses in a single financial institution.

No significant concentrations of credit risk exist within the Group.

29.3. Liquidity risk

The Group monitors the risk of insufficient funds, which are required to settle the liabilities at maturity dates, using a tool for periodic liquidity planning. This tool is based on projected cash flows from operating, investing and financing activities, which are prepared by all Group companies. Additionally regular reviews are conducted to test reliability of the projections.

On 4 January 2016, a one-way zero-balancing cash pooling service was launched in the ENERGA Group for funds in Polish zloty. This tool allows the holding company to manage the Group's liquidity in an efficient fashion. According to the assumptions about the structure, at the end of each business day, cash owned by the Group's companies is consolidated on ENERGA SA's accounts and on the following day it may be used to finance payment liabilities of the individual participants. This tool makes it possible to finance the operations first of all with the funds generated by the Group and only then with debt financing.

In respect to liquidity risk management, the Group aims at maintaining the balance between continuity and flexibility of financing through use of various sources of financing, such as overdrafts, bank loans, bonds, Eurobonds and financial lease agreements.

Detailed information on contracted external financing obtained by the Group is set out in Note 28.6.

The table below presents the Group's financial liabilities by maturity dates, based on contractual, undiscounted payments (at nominal values, including payments of possible interest).

31 December 2016 (PLN millions)

29. Financial risk management principles and objectives (cont.)

	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
31 December 2016					
Interest-bearing loans and borrowings	104	333	1,816	1,717	**3,970**
Bonds	81	26	3,502	-	**3,609**
Trade liabilities	811	-	-	-	**811**
Other financial liabilities	146	10	7	-	**163**
TOTAL	**1,142**	**369**	**5,325**	**1,717**	**8,553**
31 December 2015					
Interest-bearing loans and borrowings	63	208	1,365	1,595	**3,231**
Bonds	78	23	3,525	-	**3,626**
Trade liabilities	874	3	-	-	**877**
Other financial liabilities	177	24	17	-	**218**
TOTAL	**1,192**	**258**	**4,907**	**1,595**	**7,952**

The Group's financial assets are highly liquid. They are comprised mainly of cash and cash equivalents and trade receivables. The structure of cash and cash equivalents is presented in note 19. Aging analysis of trade receivables is presented in Note 28.5.1.

NOTES TO CONSOLIDATED STATEMENT OF CASH FLOWS

30. Statement of cash flows

Loss on investing activities

	Year ended 31 December 2016	Year ended 31 December 2015
Result on disposal of property, plant and equipment and intangible assets	28	47
Impairment losses for property, plant and equipment and intangible assets	459	18
Goodwill impairment allowance	117	-
Other	7	1
TOTAL	**611**	**66**

Change in receivables

	Year ended 31 December 2016	Year ended 31 December 2015
Change in trade receivables	(185)	(211)
Change in VAT receivables	9	27
Change in advances for deliveries	27	(36)
Other	22	(15)
TOTAL	**(127)**	**(235)**

Consolidated financial statements for the year ended 31 December 2016 (PLN millions)

30. Statement of cash flows (cont.)

Change in liabilities excluding loans and borrowings

	Year ended 31 December 2016	Year ended 31 December 2015
Change in trade liabilities	(66)	8
Change in other non-current financial liabilities	(19)	(7)
Change in other financial liabilities	(36)	(36)
Change in other current liabilities	(24)	(106)
Adjustment by the change in investment commitments	23	56
Adjustment by the change in liabilities recognized as liabilities related to assets classified as held for sale	-	(10)
Other	18	(5)
TOTAL	**(104)**	**(100)**

Change in provisions

	Year ended 31 December 2016	Year ended 31 December 2015
Change in non-current provisions	(86)	32
Change in current provisions	240	97
Adjustment by the change in provisions recognized as liabilities related to assets classified as held for sale	-	(16)
Adjustment by the change in actuarial provisions recognized in other comprehensive income	32	(7)
Other	(10)	-
TOTAL	**176**	**106**

OTHER NOTES

31. Investment commitments

At the end of the reporting period, the Group's commitments to incur expenditures for the purchase of property, plant and equipment and intangible non-current assets, which have not yet been included in the statement of financial position, were about PLN 3,482 m, of which:

- undertakings covered by the development plan of ENERGA-OPERATOR SA to satisfy the current and future demand for electricity in the years 2015-2019 (agreed upon with the President of the Energy Regulatory Office) – approx. PLN 3,214 m;
- undertakings executed in the Ostrołęka Power Plant (modernization of power units, construction of an installation for denitrifying exhaust fumes) – approx. PLN 93 m;
- execution of the Przykona Wind Farm project – approx. PLN 141 m;
- gas-steam power plants in Grudziądz and Gdańsk – approx. PLN 34 m.

32. Information on related entities

Related party transactions are made based on market prices of goods, products or services delivered resulting from their manufacturing costs.

32.1. Transactions involving parties related to the State Treasury

The Group's controlling entity is the State Treasury. Accordingly, other parties related to the State Treasury are treated by the Group as related parties.

Transactions with parties related to the State Treasury were concluded in regular business dealings and pertained mainly to the purchase and sale of electricity and property rights, sale of electricity distribution services (including transit), settlements with the transmission system operator in the balancing market, for transmission services, system services and intervention work services and the purchase and transportation of fuel (mainly coal). The Group does not keep records that would allow it to aggregate the value of all transactions concluded with all state institutions and with subsidiaries of the State Treasury.

32.2. Transactions with joint ventures

In the period from the acquisition to the end of the current reporting period, the total value of purchases from the associate Polska Grupa Górnicza Sp. z o.o. was PLN 33 m, while sales in the corresponding period was PLN 17 m. The value of receivables as at 31 December 2016 is PLN 5 m. The value of liabilities as at 31 December 2016 is PLN 2 m.

31 December 2016 (PLN millions)

32. Information on related entities (cont.)

32.3. Transactions with Parent Company's Management Board members

During the reporting period, the Parent Company did not conclude material transactions with Management Board members.

32.4. Compensation paid or due to key management and Supervisory Boards of Group companies

	Year ended 31 December 2016	Year ended 31 December 2015
Management Board of the parent company	6	3
Supervisory Board of the parent company	<1	<1
Management Boards of subsidiaries	31	33
Supervisory Boards of subsidiaries	2	1
Other key management	16	16
TOTAL	**55**	**53**

33. Lease

33.1. Operating lease liabilities

The Group does not have nay material operating lease liabilities.

33.2. Operating lease receivables

Future receivables on account of minimum leasing fees resulting from non-cancellable operating lease agreements are presented in the table below.

	Leasing fees receivable as at	
	31 December 2016	31 December 2015
Up to 1 year	30	23
Within 1 to 5 years	59	88
TOTAL	**89**	**111**

The leasing fees mentioned above refer mainly to machines of the pumped-storage plant in Żydowo, through which peak-load operation is provided in favor of PSE SA (Transmission System Operator, "TSO"). The service involves the TSO having the plant at its disposal and using it to intervene to balance active and reactive power and to control load-flows in the power grid of the Polish Public Power System. The service includes intervention reserve of active power and regulation of voltage and reactive power. The property used to provide the service remains exclusively at the TSO's disposal and the TSO has the right to use the generating units of the power plant. The agreement pursuant to which the service is provided has sufficient features, as defined in KIMSF4, to be recognized as leasing, but does not transfer the entire risk and benefits associated with the leased property to the TSO.

33.3. Liabilities under financial lease agreements

The future minimum leasing fees for the agreements and the present value of the minimum net leasing fees are as follows:

	Leasing fees payable as at			
	31 December 2016		31 December 2015	
	Minimum lease payments	Current value of payments	Minimum lease payments	Current value of payments
Up to 1 year	9	8	15	14
Within 1 to 5 years	4	4	10	10
Total minimum lease payments	**13**	**12**	**25**	**24**
Less financial costs	1	-	1	-
Present value of the lease payments	**12**	**12**	**24**	**24**

34. Capital management

The Group manages its capital in order to maintain investment-grade credit rating and safe financial ratios to support the Group's operating activity and increase its value for shareholders. This goal is achieved through the internal regulations adopted in the Group. The parent company is responsible for managing the Group's debt policy.

31 December 2016 (PLN millions)

34. Capital management (cont.)

The Group monitors its basic debt ratio, that is net debt to EBITDA, estimated on the consolidated basis. As at the balance sheet date, this ratio was 2.3, while the financing agreements called for the level of 3.5.

The level of the ratio is also regularly monitored by institutions financing the Group and by rating agencies; therefore, it has a significant influence on the evaluation of the Group's credit rating and consequently the availability and cost of debt financing.

	As at 31 December 2016	As at 31 December 2015 (restated)
Interest-bearing loans and borrowings	3,420	2,678
Bonds and debt securities issued	2,717	3,192
Cash and cash equivalents	(1,471)	(1,669)
Net debt	**4,666**	**4,201**
EBITDA	**2,027**	**2,216**
Net debt / EBITDA	**2.30**	**1.90**

35. Contingent assets and liabilities

35.1. Contingent liabilities

As at 31 December 2016, the Group recognizes contingent liabilities of PLN 255 m (PLN 217 m as at 31 December 2015), including mainly the contingent liabilities relating to disputes involving ENERGA Group companies, where a victory by the company is probable and no provision has been recognized for these cases.

The largest contingent liability item consists of disputes relating to power infrastructure of ENERGA-OPERATOR SA where it is located on private land. The Group recognizes provisions for reported legal claims. If there is uncertainty whether a claim amount or legal title to land is justified, the Group recognizes contingent liabilities. As at 31 December 2016, the estimated value of those claims recognized as contingent liabilities is PLN 214 m, compared with PLN 164 m on 31 December 2015. The amounts are estimated by the Group's lawyers, who consider the risk of a situation in which liability arises as insignificant.

35.2. Contingent assets

At the end of the reporting period there were no significant contingent assets. As at 31 December 2015, the Group recognized contingent assets in the amount of PLN 36 m.

36. Employment structure

The average headcount in the Group was as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Blue collar employees	2,971	3,004
Non-blue collar employees	5,644	5,468
TOTAL	**8,615**	**8,472**

37. Other information significantly affecting the assessment of assets, financial position and the financial result of the Group

- On 30 November 2016, ENERGA SA together with PGE S.A., Enea S.A. and PGNiG Termika S.A. submitted a new proposal to EDF International SAS ("EDF") to purchase shares in EDF companies in Poland holding conventional generation assets and carrying out service activities. The new proposal was submitted in connection with the approaching date of expiry of the proposal submitted on 16 September 2016. The new proposal will be valid for 90 days of the date of submission and will be conditional on, among others, the outcome of the due diligence process, which will provide the basis for making further decisions regarding the transaction, if any.
- On 8 December 2016, ENERGA SA, ENEA S.A. and Elektrownia Ostrołęka SA signed an investment agreement regarding the execution of the new power unit construction project in Ostrołęka. The condition precedent for the transaction was obtaining an approval from the President of the Office of Competition and Consumer Protection for the concentration involving the purchase of 50% of shares in the special-purpose vehicle Elektrownia Ostrołęka SA by Enea S.A. On 11 January 2017, the President of UOKiK issued an unconditional approval, which means that the condition precedent has been fulfilled.

38. Subsequent events

- On 18 January 2017, the Management Board of ENERGA SA along with ENEA S.A., PGE S.A., PGNiG Technologie S.A. ("Investors") and Polimex-Mostostal S.A. ("Polimex") signed an investment agreement under which the Investors undertook to make a capital investment in Polimex. ENERGA SA subscribed to 37,500,000 newly-issued shares with the par value of PLN 2 each, for the total amount of PLN 75 m and 1,500,000 Polimex shares from SPV Operator sp. z o.o. which are approved for trading on WSE in a block transaction for the total amount of PLN 5.8 m. As a result of this transaction, its stake in the Company reached approximately 16%.
- In Q1 2017, a subsidiary Energa Finance AB (publ) carried out a public subscription for the Eurobonds issued under the updated EMTN Program (the bookbuilding process was closed on 1 March 2017). It was EUR 300 m bond issue with the issue price of 98,892% and 10-year maturity. The 2.125% coupon will be payable annually, after the discount rate is taken into account, the yield for bondholders is 2.25%. The Eurobonds are listed on the Luxembourg stock exchange. The final settlement of the transaction was effected on 7 March 2017. ENERGA SA acts as the guarantor of the issue. The funds raised through the bond issue will be applied to general corporate purposes.

Signatures of ENERGA SA Management Board Members:

Daniel Obajtek …………………………………………
President of the Management Board

Jacek Kościelniak …………………………………………
Vice-President of the Management Board for Financial Matters

Grzegorz Ksepko …………………………………………
Vice-President of the Management Board for Corporate Matters

Alicja Klimiuk …………………………………..…………..
Vice-President of the Management Board for Operations

Person responsible for the preparation of the consolidated financial statements of the ENERGA SA Group:

Marek Pertkiewicz …………………………………………
Deputy Director of the Finance Department

Gdańsk, 29 March 2017