Management Board's report on activities of the Capital Group of PGE Polska Grupa Energetyczna S.A.

for the period ended June 30, 2011

Warsaw, August 2011

Selected consolidated financial data of PGE Polska Grupa Energetyczna S.A. Capital Group

	Period ended June 30, 2011 *(reviewed)*	**Period ended June 30, 2010** *(reviewed) data restated*	**Period ended June 30, 2011** *(reviewed)*	**Period ended June 30, 2010** *(reviewed) data restated*
	in PLN thousand		**in EUR thousand**	
Sales revenues	13,915,332	10,132,713	3,507,507	2,530,521
Net profit/loss from operating activities	2,663,497	2,280,837	671,363	569,611
Gross profit/loss (before taxation)	2,774,011	2,277,581	699,219	568,798
Net profit/loss for the reporting period	2,261,792	1,842,410	570,109	460,119
Net profit attributable to equity holders of the parent company	2,220,232	1,499,471	559,633	374,475
Total income	2,262,953	1,844,063	570,401	460,532
Net cash from operating activities	2,950,126	3,419,809	743,610	854,055
Net cash from investing activities	(2,166,328)	(1,806,882)	(546,046)	(451,247)
Net cash from financial activities	(677,899)	(2,055,240)	(170,872)	(513,271)
Net change in cash and cash equivalents	105,899	(442,313)	26,693	(110,462)
Net earnings per share (in PLN/EUR per share)	1.19	0.87	0.30	0.22
Diluted earnings per share (in PLN/EUR per share)	1.19	0.87	0.30	0.22
Weighted average number of shares	1,869,760,829	1,730,090,000	1,869,760,829	1,730,090,000
	As at June 30, 2011 *(reviewed)*	**As at December 31, 2010** *(audited) data restated*	**As at June 30, 2011** *(reviewed)*	**As at December 31, 2010** *(audited) data restated*
Non-current assets	43,152,236	44,137,422	10,824,320	11,144,969
Current assets	9,246,540	7,285,844	2,319,405	1,839,720
Total assets	52,398,776	51,423,266	13,143,725	12,984,690
Equity	38,651,211	37,632,100	9,695,282	9,502,336
Equity attributable to equity holders of the parent	38,038,758	37,033,281	9,541,654	9,351,130
Share capital	18,697,837	18,697,837	4,690,171	4,721,318
Long-term liabilities	7,201,327	7,199,809	1,806,383	1,817,996
Short-term liabilities	6,546,238	6,591,357	1,642,060	1,664,358
Number of shares at the end of reporting period	1,869,760,829	1,869,760,829	1,869,760,829	1,869,760,829
Book value per share (in PLN/EUR per share)	20.34	19.81	5.10	5.00
Diluted book value per share (in PLN/EUR per share)	20.34	19.81	5.10	5.00

Selected financial data for PGE Polska Grupa Energetyczna S.A.

	Period ended June 30, 2011 *(reviewed)*	Period ended June 30, 2010 *(not audited)*	Period ended June 30, 2011 *(reviewed)*	Period ended June 30, 2010 *(not audited)*
	in PLN thousand		in EUR thousand	
Sales revenues	5,025,694	5,961,005	1,266,779	1,488,688
Profit/loss on operating activities	107,408	89,163	27,073	22,267
Gross profit/loss (before taxation)	2,444,706	320,720	616,214	80,096
Net profit/loss for the reporting period	2,414,548	281,241	608,612	70,237
Total income	2,415,841	281,131	608,938	70,209
Net cash from operating activities	(330,621)	213,475	(83,337)	53,313
Net cash from investing activities	1,699,672	(1,536,340)	428,420	(383,682)
Net cash from financial activities	(1,106,631)	(441,631)	(278,938)	(110,292)
Net change in cash and cash equivalents	262,420	(1,764,496)	66,146	(440,661)
Net earnings per share (in PLN/EUR per share)	1.29	0.15	0.33	0.04
Diluted earnings per share (in PLN/EUR per share)	1.29	0.15	0.33	0.04
	As at June 30, 2011 *(reviewed)*	**As at December 31, 2010** *(not audited)*	**As at June 30, 2011** *(reviewed)*	**As at December 31, 2010** *(not audited)*
Non-current assets	23,339,287	23,330,403	5,854,434	5,891,070
Current assets	9,266,046	8,530,960	2,324,298	2,154,120
Total assets	32,605,333	31,861,363	8,178,732	8,045,189
Equity	29,605,739	28,405,678	7,426,313	7,172,608
Share capital	18,697,837	18,697,837	4,690,171	4,721,318

Above financial data for first half of 2011 and 2010 were converted into EUR according to the following rules:

- particular items of the assets and liabilities – according to average exchange rate published by the National Bank of Poland as of June 30, 2011 - EUR/PLN 3.9866 and as of December 31, 2010 – EUR/PLN 3.9603,
- particular items of statement of comprehensive income and statement of cash flows – according to the exchange rate constituting an arithmetic average of average exchange rates set out by the National Bank of Poland at the end of every month of the reporting period from January 1, 2011 till June 30, 2011 - EUR/PLN 3.9673 and for the period from January 1, 2010 till June 30, 2010 - EUR/PLN 4.0042.

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1. Organisation of the Capital Group.

The description of the organisation of the PGE Capital Group and list of consolidated companies were presented in Note 1 and 2 to the consolidated financial statements.

1.1. Description of the activity of PGE Capital Group

The Group currently organizes its activities in five business lines:

(i) Mining and Conventional Generation (previously Mining and Generation), including extraction of lignite and generation of electricity and heat from conventional sources and distribution of heat, (ii) Renewable Energy, including electricity generation from renewable sources and in pumped storage power plants, (iii) Wholesale Trading of electricity, related products and fuels; (iv) Distribution of electricity and (v) Retail Sales of electricity. Apart from 5 main business lines, PGE Group holds activities in other areas, including telecommunication. The Group also comprises of other companies, whose main activity are implementation of strategic activities connected with the preparation and execution of construction of nuclear power plants and providing ancillary control services to companies from the energy and mining sectors. These services comprise, inter alia: (i) building, renovation and modernization works and investments in electricity equipment, (ii) comprehensive diagnostic tests and measurements of electricity machines and equipment; (iii) managing by-products of coal combustion, developing, implementing and using technologies and rehabilitation of degraded areas, and (iv) medical and social services.

1.2. Changes in organisation of the Capital Group

The changes which occurred in the Group's structure during 6-month period ended June 30, 2011 are presented in Note 2 to consolidated financial statements and described below.

Shares in subsidiaries and associates

In the first half of 2011 PGE S.A. changed its equity interest in the following entities:

- on February 4, 2011 the meeting of shareholders of Electra Deutschland GmbH, adopted a resolution on increasing the share capital of the company by EUR 2,000,000 to EUR 3,350,000. PGE S.A. took up the share in the increased share capital. The increase of the share capital was registered on March 1, 2011,
- on February 24, 2011 PGE Polska Grupa Energetyczna S.A. purchased 17 inscribed shares of PGE Obrót S.A. from its minority shareholders (constituting 0.0003% of the share capital of the company),
- on May 30, 2011 PGE Polska Grupa Energetyczna S.A. purchased 17 inscribed shares of PGE Obrót S.A. from its minority shareholder (constituting 0.0003% of the share capital of the company),
- on June 6, 2011 Polska Grupa Energetyczna S.A. purchased 17 inscribed shares of PGE Obrót S.A. from its minority shareholder (constituting 0.0003% of the share capital of the company).

In the first half of 2011 PGE Group companies increased their capital exposure in the following entities:

- on January 19, 2011 a share capital increase was registered for Energetyczne Towarzystwo Finansowo-Leasingowe Energo-Utech S.A. (a company in which PGE Energia Odnawialna S.A. holds 50% in the share capital) by PLN 10,000,000 (PLN 5,000,000 by each shareholder) by issue of 1,000 inscribed series C shares with a nominal value of PLN 10,000 (current value of the share capital amounts to PLN 22,400,000).
- on January 26, 2011 NOM Sp. z o.o. bought the minority stake in Energo-Tel S.A. (buyout of the minority shareholder who held 0.1% in the share capital). As a result of the transaction the share of NOM Sp. z o.o. in the share capital of Energo-Tel S.A. increased to 48.9%.
- on February 11, 2011 a share capital increase was registered for Eolica Wojciechowo Sp. z o.o. The company's share capital was increased from PLN 3,550,000 to PLN 9,550,000 i.e. by PLN 6,000,000 through creation of 12,000 new shares with a nominal value of PLN 500 each. New shares from the increased capital were acquired in half by partners: PGE Energia Odnawialna S.A. and Greentech Energy Systems A/S.

- on February 18, 2011 a share capital increase was registered for Biogazownia Wożuczyn Sp. z o.o. from PLN 250,000 to PLN 3,700,000, i.e. by PLN 3,450,000. Newly created shares were acquired by PGE Energia Odnawialna S.A.
- on February 18, 2011 a share capital increase was registered for Biogazownia Łapy Sp. z o.o. from PLN 250,000 to PLN 3,700,000, i.e. by PLN 3,450,000. Newly created shares were acquired by PGE Energia Odnawialna S.A.
- on March 31, 2011 the merger of Przedsiębiorstwo Transportowo Sprzętowe BETRANS Sp. z o.o. with its registered office in Rogowiec (acquiring company) with Przedsiębiorstwo Transportowe ELTUR-TRANS Sp. z o.o. with its registered office in Bogatynia (acquired company) was registered. The merger took place by way of transferring all assets of the acquired company to the acquiring company in exchange for the shares in the increased share capital of the acquiring company. The shares were assigned to the partner of the acquired company. As a result of the merger the share capital of „Betrans" Sp. z o.o. amounting to PLN 8,773,000 was increased by PLN 6,096,500 i.e. to PLN 14,869,500 through creation of 12,193 new shares with a nominal value of PLN 500 each (merger shares). As at June 30, 2011 PGE Górnictwo i Energetyka Konwencjonalna S.A. is the only partner of the „Betrans" Sp. z o.o.
- on April 26, 2011 Energetyczne Towarzystwo Finansowo-Leasingowe Energo-Utech S.A. signed share purchase agreement to buy 50 shares of ENERGOUTECH 2 Sp. z o.o. with nominal value of PLN 100 each for total consideration of PLN 5,000 for all stakes. On April 26, 2011 the company acquired 450 new shares with nominal value of PLN 100 each, i.e. with total value of PLN 45,000, in share capital of ENERGOUTECH 2 sp. z o.o. that was increased to PLN 50,000. Currently the company owns 100% stake in share capital of ENERGOUTECH 2 Sp. z o.o.
- on April 29, 2011 the merger of ELBEST Sp. z o.o. with registered office in Rogowiec (acquiring company) with: BESTUR Sp. z o.o. with registered office in Bełchatów, PHU Global-Tur Sp. z o.o. with registered office in Bogatynia, Energetyk SPA Sp. z o.o. with registered office in Iwonicz-Zdrój, Centrum Szkolenia i Rekreacji Energetyk Sp. z o.o. with registered office in Krasnobród, Media-Serwis Dychów Sp. z o.o. with registered office in Dychów (acquired companies), realised pursuant to art. 492 sec. 1 p. 1 of the CCC, was registered. As a result of the merger, which is a consequence of reorganization of hotel- security- services area within PGE capital group, share capital of ELBEST sp. z o.o. was increased to PLN 123,895,000. Shareholding structure of ELBEST sp. z o.o. is as follows: PGE Górnictwo i Energetyka Konwencjonalna S.A. – 91.19%, PGE Dystrybucja S.A. – 7.60%, PGE Obrót – 1.12% and PGE Energia Odnawialna S.A. – 0.09%.
- On June 13, 2011 companies EO Baltica Sp. z o.o. and Elektrownia Wiatrowa Resko Sp. z o.o. established 3 SPVs: Elektrownia Wiatrowa Baltica 1 Sp. z o.o., Elektrownia Wiatrowa Baltica 2 Sp. z o.o. and Elektrownia Wiatrowa Baltica 3 Sp. z o.o. Elektrownia Wiatrowa Resko Sp. z o.o. acquired 5% of shares in each of 3 companies (i.e. 80 shares with nominal value of PLN 500 each, with total value of PLN 40,000 in each of abovementioned companies). On July 22, 2011 Elektrownia Wiatrowa Baltica 1 Sp. z o.o. was registered in National Court Register.

In the first half of 2011 PGE Group companies reduced their capital exposure in the following entities:

- on March 22, 2011 PGE Elektrownia Opole S.A. concluded an agreement, according to which it agreed for redemption and sold to Eltrans Sp. z o.o. with its registered office in Brzezie all shares possessed in that company, i.e. 384 shares, constituting 40% of the share capital and the company purchased these shares for redemption. After the transaction PGE Elektrownia Opole S.A. is no longer a partner in the company.
- on March 22, 2011 PGE Elektrownia Opole S.A. concluded an agreement, according to which it agreed for redemption and sold to Energotest-Diagnostyka Sp. z o.o. with its registered office in Brzezie all shares possessed in that company, i.e. 26 shares, constituting 26% of the share capital and the company purchased these shares for redemption. After the transaction PGE Elektrownia Opole S.A. is no longer a partner in the company.
- On April 15, 2011 PGE Obrót S.A. concluded an agreement to sell all the shares owned by the company in Zamojskie Przedsiębiorstwo Usługowo-Produkcyjne "Energozam" Sp. z o.o. with registered office in Zamość, constituting 42.59% in share capital of this company.

On December 15, 2010 the General Meeting of Shareholders of Electra Slovakia s.r.o. adopted a resolution on liquidation of the company. On January 25, 2011 the liquidation was entered into commercial register and from that date company has been using a firm Electra Slovakia s.r.o. in liquidation.

On February 23, 2011 the Extraordinary Assembly of Partners of Pensjonat Dychów Sp. z o.o. (100% owned by PGE Energia Odnawialna S.A.) decided to liquidate the company. The application for liquidation was submitted at the Regional Court in Zielona Góra on March 11, 2011. On May 10, 2011 the court dismissed the application.

On March 14, 2011 the Extraordinary Assembly of Partners of ESP-Usługi Sp. z o.o. (100% owned by PGE Energia Odnawialna S.A.) decided to dissolve and liquidate the company.

On March 30, 2011 the register court registered the liquidation of PGE Inwest Spółka z ograniczoną odpowiedzialnością II spółka komandytowo-akcyjna (in connection with the resolution of the Assembly of Partners dated March 18, 2011).

On March 31, 2011 the conversion of Bio-Energia ESP Sp. z o.o. into the joint stock company was registered – current name is Bio-Energia ESP S.A.

On March 31, 2011 the change of names of the branches of PGE Energia Odnawialna S.A. was registered:

- PGE Energia Odnawialna S.A. Branch in Solina changed to PGE Energia Odnawialna S.A. Branch ZEW Solina – Myczkowce in Solina,
- PGE Energia Odnawialna S.A. Branch in Międzybrodzie Bialskie changed to PGE Energia Odnawialna S.A. Branch ZEW Porąbka – Żar in Międzybrodzie Bialskie,
- PGE Energia Odnawialna S.A. Branch in Czymanowo changed to PGE Energia Odnawialna S.A. Branch EW Żarnowiec in Czymanowo,
- PGE Energia Odnawialna S.A. Branch in Dychów changed to PGE Energia Odnawialna S.A. Branch ZEW Dychów in Dychów.

On May 9, 2011 the bankruptcy proceedings of Wind 1 Koszalin sp. z o.o. were completed (the bankruptcy court's decision was validated on June 4, 2011). On June 14, 2011, the company was deleted from National Court Register.

A division plan, involving the transfer of Zakład Transportu, an organised part of enterprise ELBEST sp. z o.o. to PTS 'Betrans' sp. z o.o., was signed on June 22, 2011. On June 27, 2011 abovementioned division plan was submitted to the Regional Court for Łódź-Śródmieście in Łódź.

During 6-month period ended June 30, 2011 PGE Capital Group did not discontinue any significant operations. Operations, which in the reporting period met the criteria of operations intended for discontinuation, were presented in Note 20 to the consolidated financial statements.

2. Factors and events influencing financial results.

2.1. Macroeconomic situation

The PGE Group runs its activities mainly in Poland. Therefore it has been and will be dependent on macroeconomic trends existing in Poland. As a rule, there is a positive correlation between the growth of electricity demand and economic growth. Thus, the macroeconomic situation of Poland has a direct impact on financial results achieved by the PGE Group. Particularly, the observed restoration of the activities in the economy triggered an increase in demand for electricity in the National Power System in the reporting period by approximately 2.5% in comparison to first half of 2010.

Table: Key economic ratios connected with the Polish economy.

Key data	1H 2011	1H 2010
Real GDP growth (% of growth)[1]	4.2*	3.2
Annual inflation rate (% of consumer prices) [2]	4.2	2.3
Domestic electricity consumption (TWh) [3]	78.8	76.9

* estimates by the Ministry of Economy

Source: [1] Polish Central Statistical Office, real growth of GDP in constant previous year's price, with corresponding period of preceding year = 100; [2] Polish Central Statistical Office, inflation rate, with corresponding period of preceding year = 100; [3] PSE Operator S.A.

2.2. Electricity prices

Prices of electricity on the wholesale market

The situation on domestic and international electricity markets has significant impact on the financial results of PGE S.A. and PGE Capital Group. Electricity prices quoted on domestic market and situation on international markets - due to the interconnectors between Poland and its neighbours - have also significant impact.

Domestic market

The operation of the domestic wholesale electricity market in the first half of 2011 was subject to further transformation reflecting, among others, the requirements of art. 49a section 1 and 2 of the Energy Law (so called "power exchange obligation"). Particularly, the increased role of Towarowa Giełda Energii (TGE) in electricity trading has been observed. The sales realized on TGE have significantly risen in the current year and as a result GFI and TFS platforms have decreased their share in total electricity trading. In first half of 2011 the total volume of transactions concluded for futures and forwards on all three mentioned markets amounted to 68.5 TWh.

National energy consumption in the second quarter of 2011 amounted to 37.1 TWh and was higher by 3.5% than in an analogical period of the previous year. Total energy consumption in the first half of 2011 amounted to 78.8 TWh and was higher by 2.5% than in the first half of 2010.

SPOT market: Second quarter of 2011 was characterised by high SPOT prices. Average SPOT market price on TGE, indexed by IRDN24 (arithmetic average of hourly prices) amounted to 207.08 PLN/MWh in the second quarter of 2011. Thus it was higher by 7.02% than in previous quarter and higher by almost 11.09% than in second quarter of 2010. The average energy price for the peak contracts amounted to 224.75 PLN/MWh in the second quarter of 2011.

Chart. Daily and quarterly base prices in SPOT transactions in 2010–2011 (TGE)*.

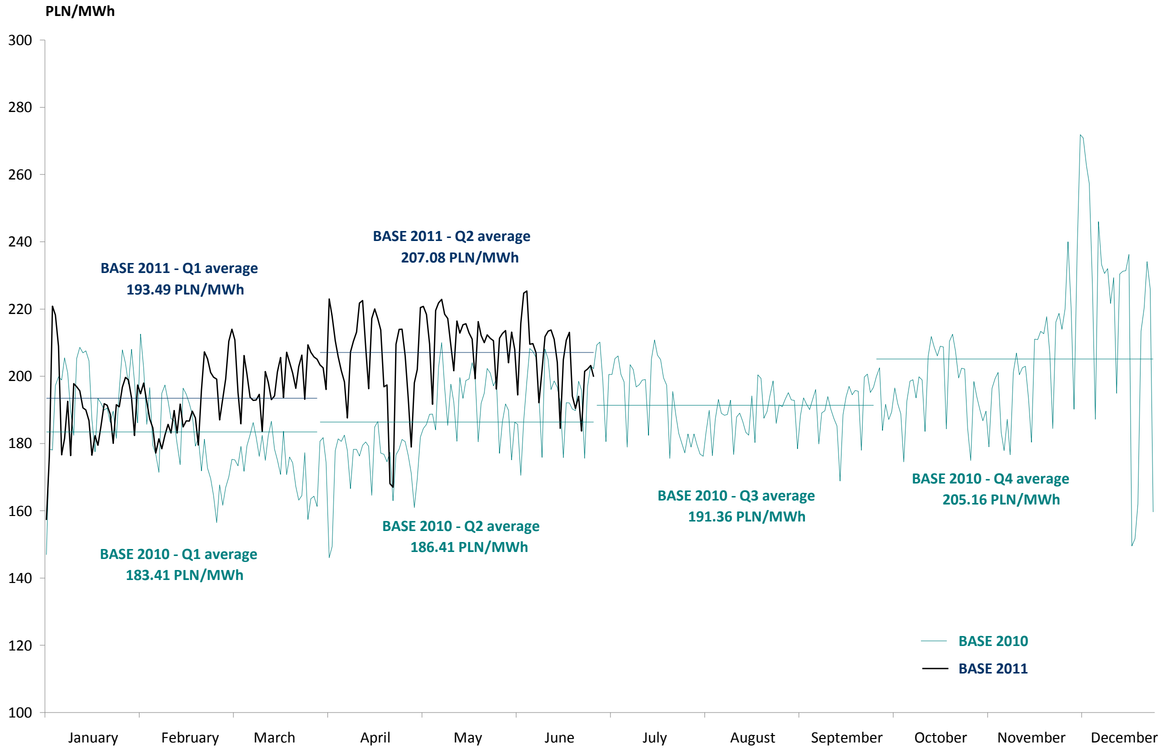
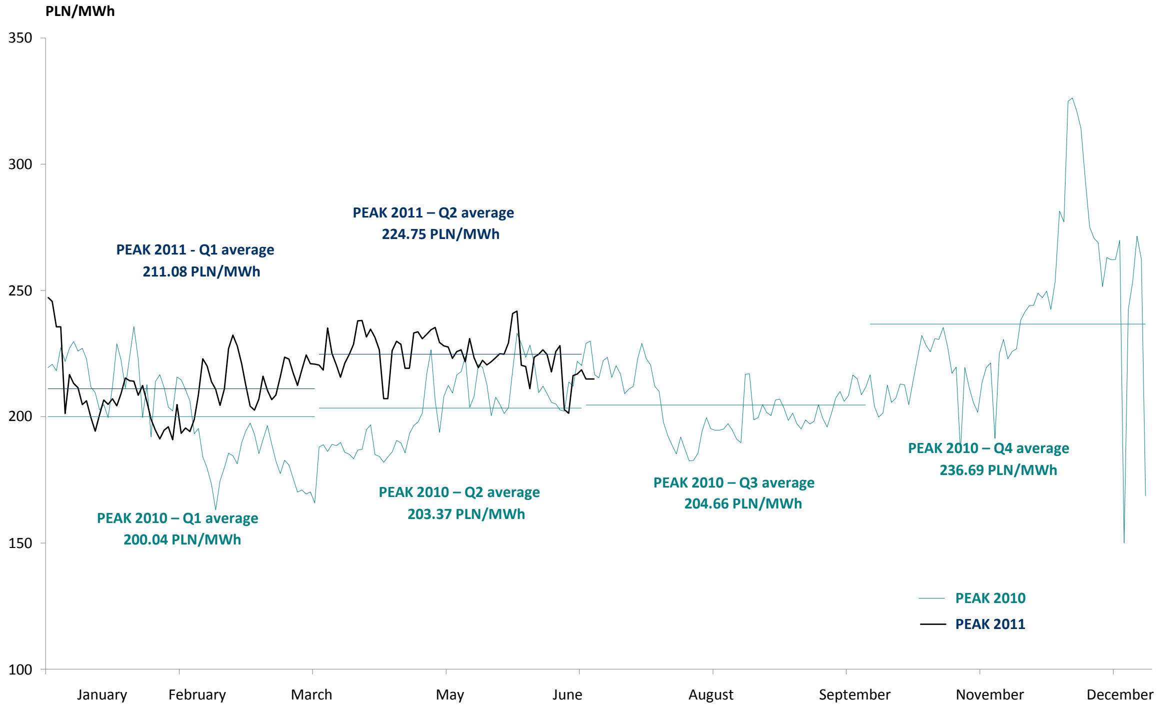


Chart. Daily and quarterly peak prices in SPOT transactions in 2010–2011 (TGE)*.



** arithmetic average of the averages weighted by the volume of the prices of the transactions concluded during fixing and continuous trading on the particular hours of the day from N-1 and N-2 markets for the same delivery date*

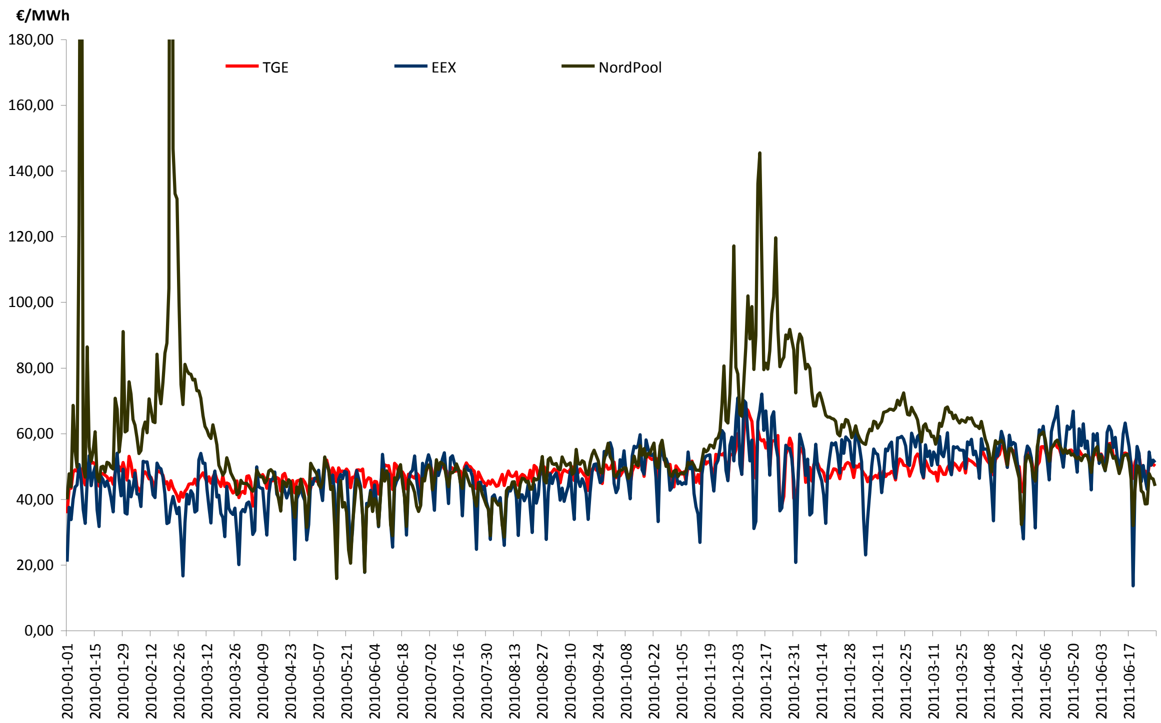
Total trading volumes of electricity on SPOT market, both on TGE and POEE, amounted in the second quarter of 2011 to over 5.7 TWh as compared to 5.2 TWh in the previous quarter. Majority of the transactions volumes was performed on TGE due to the fact, that sale of electricity on this platform was approved by the ERO President as fulfilment of the power exchange obligation imposed on the generators. Total trading volume on SPOT market (TGE and POEE) amounted to 10.9 TWh in the first half of 2011 and was higher by almost 4.7 TWh than in the analogical period of the previous year.

Futures and forward market: TGE has become dominant electricity trading market also on futures and forward market. The TGE's Futures and Forwards Market totalled trading volume of 45.2 TWh in the first half of 2011 – the transactions included deliveries for this year as well as for next years. This trading volume constituted approximately 66% of the total sales volume on the organized market. On the market, the trading of products with 2012 delivery date was realized in first and second quarter of 2011. Total capacity sold in base product for 2012 amounted to 4,864 MW, including 3,594 MW on TGE. The average price of this product amounted to 203.78 PLN/MWh in this period. Apart from yearly contracts, the monthly and quarterly contracts were also popular.

International market

The decommissioning of part of nuclear power plants in Germany resulted in higher demand for export of electricity from Poland. Additionally, significant transmission capacities on interconnectors were being facilitated by PSE-Operator. The above factors and sustaining large disparity of electricity prices between German market (EEX) and Polish market resulted in increased interest in export of electricity. The prices on Scandinavian market (NordPool) started to fall and remained on the slightly lower level than in Poland up till the end of the second quarter. Total international exchange balance amounted to 2.8 TWh in the first half of 2011, with excess of export over import, while in the analogical period of the previous year it was just 0.55 TWh.

Chart: Comparison of electricity prices on TGE and international markets.



Electricity prices on retail market

The average electricity prices in tariffs A-C in PGE Obrót S.A. increased by several to dozen or so per cent as compared to electricity prices in 2010.

The main factors influencing the increase of electricity prices for the end users in 2011 were growth of electricity prices on the wholesale market and increased costs of obtaining and redemption of origin certificates in order to fulfil the requirements imposed by law on the entities dealing with the sales of electricity to the end users.

2.3. Termination of long-term contracts (LTC)

Due to the termination of LTCs in accordance with The Act on coverage of stranded costs resulting at generators in relation to accelerated termination of long-term contracts ("LTC Act"), the producers being earlier the parties to such contracts obtained a right to receive compensations for the coverage of so called stranded costs (capital expenditures resulting from investments in generating assets made by the generator before May 1, 2004 that a generator is not able to recoup from revenues obtained from sales of generated electricity, spare capacity and ancillary services in a competitive environment after early termination of LTC). The LTC Act limits the total amount of funds that may be paid to all generators to cover stranded costs, discounted as at January 1, 2007, to PLN 11.6 billion.

Table: Key data relating to PGE Group generators subject to the LTC Act.

Generator	LTC maturity	Maximum amount of stranded and additional costs
PGE Elektrownia Opole S.A.	2012	PLN 1,966 million
PGE GiEK Branch Elektrownia Turów	2016	PLN 2,571 million
PGE GiEK Branch Zespół Elektrowni Dolna Odra	2010	PLN 633 million
PGE GiEK Branch Elektrociepłownia Gorzów	2009	PLN 108 million
PGE GiEK Branch Elektrociepłownia Lublin-Wrotków	2010	PLN 617 million
PGE GiEK Branch Elektrociepłownia Rzeszów	2012	PLN 422 million
TOTAL		**PLN 6,317 million**

In the period provided for by the LTC Act, i.e. till December 31, 2007, PGE S.A. signed termination agreements with generators being parties to the then applicable LTCs. Therefore generators obtained a right to receive funds to cover their stranded costs.

The impact of LTC compensations on results achieved by the PGE Group is described in Note 21.1 to the consolidated financial statements.

2.4. Balance of energy of PGE Capital Group

As a result of change of the trading model, including implementation of the „power exchange obligation" (see Note 21.3 to the consolidated financial statements), the energy generators sell their energy on the power exchange and PGE S.A. buys the energy on this market. This change resulted in significant increase of volumes and values of the energy sold and purchased by PGE Capital Group as compared to the previous periods, when generators from PGE Group sold most of the energy produced to other entities from PGE Group.

<u>Sales of electricity</u>

Table: Sales of electricity outside the PGE Capital Group (in TWh).

	H1 2011	H1 2010	% change
Sale in TWh, including:	**43.60**	**28.35**	***54%***
Sales to end-users *	15.39	14.86**	*4%*
Sales on the wholesale market, including	27.47	11.31	*143%*
Sales on the domestic wholesale market – power exchange	*24.93*	*3.80*	*556%*
Other sales on the domestic wholesale market	*2.01*	*6.85*	*-71%*
Sales to foreign customers	*0.53*	*0.66*	*-20%*
Sales on the Balancing Market	0.74	2.18	*-66%*

** after elimination of intra-group sales in PGE Group*
*** data restated for comparability*

In the first half of 2011 and in the first half of 2010 the Group sold 43.60 TWh and 28.35 TWh of electricity respectively. Changes in the sales structure for the first half of 2011 versus the first half of 2010 resulted mainly from the increase of sales on the wholesale market, particularly on the power exchange. Significant increase of sales on the power exchange was connected with the change of the trading model in PGE Capital Group and introduction of so called "power exchange obligation". Other sales on the wholesale market, sales to foreign customers and sales on the balancing market were on the lower levels than in first half of 2010. On the other hand, the increase of sales to the end users was recorded.

Purchases of electricity

Table: Purchases of electricity from outside of the PGE Capital Group (in TWh).

	H1 2011	H1 2010	% change
Total purchases in TWh, including:	**18.96**	**5.00**	***279%***
Purchases on the domestic wholesale market, power exchange	16.27	-	-
Purchases on the domestic wholesale market, other	0.27	0.47	*-43%*
Purchases from abroad	0.19	0.67	*-72%*
Purchase from the Balancing Market..	2.23	3.86	*-42%*

In the first half of 2011 and in the first half of 2010 the companies from the Group purchased respectively 18.96 TWh and 5.00 TWh of electricity from outside the PGE Group. Changes in the purchase structure in the first half of 2011 as compared to the first half of 2010 resulted mainly from the increased energy purchase on the power exchange. The decrease of purchase from abroad occurred in connection with the unfavourable situation on foreign markets; additionally the trade agreement with Vattenfall Aktiebolag on exchange of energy on link between Poland and Sweden expired in August 2010. The decrease of the purchase from the balancing market and other purchases on the wholesale market also occurred.

Production of electricity

Table: Generation of electricity by the Group (in TWh).

	H1 2011	H1 2010	% change
Total energy generation (in TWh), including:	**27.26**	**26.21**	**4%**
Lignite-fired power plants	18.07	17.90	1%
Coal-fired power plants..	6.90	6.12	13%
Coal-fired CHP plants..	0.76	0.72	6%
Gas-fired CHP plants...	1.07	0.86	24%
Pumped storage power plants...	0.19	0.25	-24%
Hydroelectric plants...	0.24	0.33	-27%
Wind power plants...	0.03	0.03	0%

In the first half of 2011 and in the first half of 2010 the Group produced respectively 27.26 TWh and 26.22 TWh of electricity. The production increased in coal-fired power plants, lignite-fired power plants, coal-fired CHP plants and gas-fired CHP plants. The pumped storage power plants and hydroelectric plants decreased their production.

The increase in electricity production in coal-fired power plants, lignite-fired power plants was chiefly caused by higher production in Turów power plant and Dolna Odra power plant, in which 2 units were out of order in first half of 2010 due to failures. Additionally, there was higher commercial utilization of electric capacities (MWe) in Opole power plant in first half of 2011 as compared to first half of 2010.

The increase in electricity production in coal-fired CHP plants resulted from lower production in first half of 2010 due to failure of two power units at Elektrociepłownia Pomorzany, that resulted in limited availability of the power units, which needed to operate at lower parameters. As from February 2010, the power units had operated with reduced capacity, thus producing less electricity.

The increase in electricity production in gas-fired CHP plants is mainly related to lower production in first half of 2010 due to steam-gas unit failure at PGE EC Rzeszów S.A. which occurred on January 31, 2010. As a result, the plant suspended its whole electric energy production from February till June 2010.

The decline in production in hydroelectric power plants was connected with the unfavourable hydrologic conditions in first half of 2011.

2.5. Production and sales of heat

In the first half of 2011 the net heat production and sales in PGE Group totalled 13.2 million GJ and 12.4 million GJ respectively and were lower by approximately 8% and 9% respectively, as compared to the first half of 2010, mainly due to weather conditions.

2.6. Tariffs

PGE Group companies earn part of their income based on tariffs approved by the President of the Energy Regulatory Office: (i) tariffs for the sale of electricity to households (G tariff group), (ii) tariffs of distribution system operators ("DSO"), and (iii) heat tariffs.

Sales of electricity

Sales of electricity to recipients from the G tariff group, connected to the distribution network of PGE Dystrybucja S.A. in the first half of 2011 took place on the basis of electricity tariffs approved by the President of the Energy Regulatory Office. The proceedings on the approval of the tariffs for 2011 were started on October 18, 2010 and were finalized on December 16, 2010. The approved tariff came into force on January 1, 2011. In the first half of 2011 sales of energy to the corporate customers (key and business) and to individuals other than from G tariff group connected to the distribution network of PGE Dystrybucja S.A. took place on the basis of Tariff for customers from A, B, C and R tariff groups, approved by the resolution of the Management Board of PGE Obrót S.A. and effective from January 1, 2011, as well as on the basis of individually negotiated offers.

Distribution of electricity

Methodology of and assumptions for tariffs determination were published in the document "Tariffs for the DSO for the year 2011", which were prepared by the President of the Energy Regulatory Office and provided to distribution system operators.

First consolidated tariff of PGE Dystrybucja S.A. for 2011 was approved by the President of the Energy Regulatory Office on December 17, 2010 in the part concerning the transition fee and on December 21, 2010 in other part. Tariffs for 2011, according to resolution of the Management Board of PGE Dystrybucja S.A, dated December 24, 2010, came into force on January 5, 2011 (according to the decision of the President of the Energy Regulatory Office, the transition fee has been in force since January 1, 2011).

Distribution tariffs for 2011 approved by the President of the Energy Regulatory Office, contributed to changes in average payments for customers in particular tariff groups in comparison to year 2010:

- A tariff group – decrease by 1.25 %,
- B tariff group – decrease by 2.35 %,
- C+R tariff group – increase by 2.61 %,
- G tariff group – increase by 3.34 %.

An average price of energy distribution services in comparison to last tariffs binding in 2010 increased by approximately 1.01%.

During the reporting period the approved tariffs for distribution services were not subject to any changes.

Tariff for heat

Pursuant to Art. 47 sections 1 and 2 of the Energy Law energy, companies, which hold licences, set tariffs for heat and propose their duration. Submitted tariff is subject to the approval by the President of the Energy Regulatory Office, provided that it is consistent with rules and regulations referred to in Art. 44-46 of the Energy Law. Conduction of proceedings concerning heat tariffs approval lies within the competence of regional Branches of Energy Regulatory Office.

The binding tariffs for electricity, electricity distribution services and heat, which are subject to the approval by the President of the Energy Regulatory Office, do not cover all costs incurred by the Group companies. At present, costs recognized by the President of the Energy Regulatory Office as justified costs to calculate tariffs for PGE Group companies are lower than costs actually incurred by these companies.

2.7. Prices of fuel

Table: Volume and cost of purchase of fuels from third party suppliers in the 6-month period ended June 30, 2011 and June 30, 2010.

	For the 6-month period ended June 30, 2011		For the 6-month period ended June 30, 2010	
	Volume ('000 tonnes)	**Cost (PLN million)**	**Volume ('000 tonnes)**	**Cost (PLN million)**
Hard coal	3,818	1,005	2,802	736
Gas ('000 m^3)	287,250	233	250,295	177
Biomass..	299	108	211	71
Fuel oil...	25	46	22	32
TOTAL		**1,392**		**1,016**

During the first half of 2011 the costs of purchasing primary fuels from providers outside the Group amounted to PLN 1,392.0 million and were higher by approximately 37% as compared to the first half of 2010. It is connected with the higher utilization of coal-fired power plants and gas-fired CHP plants for production of electricity with the simultaneous increase of gas prices by approximately 15%.

In the first half of 2011 approximately 66% of the electricity produced was obtained from internally sourced lignite, whose price is less susceptible to fluctuations than fuel sourced externally. However, certain factors including the aggregate amount of lignite extracted, costs of overburden removal, labour costs and environmental provisioning affect mining costs incurred by the Group and thus PGE Group's generation costs.

2.8. National Allocation Plan for the years 2008-2012 ("NAP II")

The National Allocation Plan on CO_2 emission ("NAP") is subject to the notification to the European Commission, under the EU emission rights trading system. In connection with the fact that the European Commission reduced the quantity of CO_2 emission rights for Poland in both settlement periods in relation to quantities applied by Poland in the NAP, the granted limits constitute a material limitation for the electro energy sector.

As regards the second settlement period, which covers the years 2008-2012, Poland applied for emission caps of 284 million tonnes of CO_2. The European Commission reduced the average free CO_2 emission allowances per year for Poland to 208.5 million tonnes. According to the present NAP II, utility power plants would only be authorized to emit 110.8 million tonnes of CO_2, whereas Polish CO_2 emissions in normal circumstances are estimated at approximately 120 million tonnes per year.

Table: Allocation of emission rights limits (in tonnes).

Sector	Average rights - tonnes of CO_2 per year
Utility power plants	110,791,200
Utility CHP plants	25,391,008

The following table presents data concerning CO_2 emission from major Group installations in the first half of 2011 (as compared to the number of rights granted under free allocations).

Table: Emission of CO_2 from major Group installations in the first half of 2011 in comparison to the average yearly allocation of CO_2 emission rights.

Operator	CO_2 emissions in H12011	Average yearly allocation for 2011 based on the NAP II
PGE GiEK Branch Elektrownia Bełchatów	15,051,154	26,937,155
PGE GiEK Branch Elektrownia Turów	5,804,955	11,158,636
PGE GiEK Branch Zespół Elektrowni Dolna Odra	3,476,413	5,680,137
PGE GiEK Branch Zespół Elektrociepłowni Bydgoszcz	577,964	1,155,252
PGE GiEK Branch Elektrociepłownia Gorzów	233,091	479,305
PGE GiEK Branch Elektrociepłownia Lublin-Wrotków	281,169	570,840
PGE GiEK Branch Elektrociepłownia Rzeszów	178,004	303,155
PGE GiEK Branch Elektrociepłownia Kielce	97,533	194,547
PGE GiEK Branch Elektrociepłownia Zgierz	50,670	104,988
PGE Elektrownia Opole S.A.	3,641,495	6,475,340
TOTAL	**29,392,448**	**53,059,355**

3. Significant achievements and failures of the Company in the reporting period, along with list of most important events.

3.1. Financial results of the Group

Consolidated statement of comprehensive income

In the first half of 2011 total sales revenues of the Group amounted to PLN 13,915.3 million, as compared to PLN 10,132.7 million in the first half of 2010. The biggest increase of revenues was in the revenues from sales of finished goods and merchandise which grew by PLN 3,630.4 million mainly as a result of: (i) increased sales of electricity on the wholesale market in connection with the change of the trading model, including implementation of the power exchange obligation (see Note 21.3 to the consolidated financial statements), (ii) increase in revenues from sales of electricity to end-users, (iii) increase in revenues from distribution services, (iv) increase in revenues from sales of certificates of origin. The decrease in revenues from the electricity sales on the balancing market had the negative impact on the deviation of the revenues from sales of finished goods and merchandise. The revenues from LTC compensations higher by PLN 133.3 million also affected level of the sales revenues.

Cost of goods sold in the first half of 2011 amounted to PLN 10,043.1 million, i.e. it grew by ca. 47% as compared to the first half of 2010. The increase of the cost of goods sold was caused by increase in value of cost of merchandise and materials sold by PLN 3,040.4 million in connection with change of the trading model and the realisation of the power exchange obligation.

Gross profit on sales in the first half of 2011 amounted to PLN 3,872.3 million as compared to PLN 3,286.0 million in the first half of 2010, what means growth by ca. 18%.

In the first half of 2011 total distribution and selling expenses of PGE Group amounted to PLN 785.3 million, what means approximately 5% increase as compared to the first half of 2010. The growth of selling and distribution expenses was mainly associated with higher costs of redemption of property rights incurred by PGE Obrót S.A.

In the first half of 2011 general and administrative expenses amounted to PLN 352.3 million, what means approximately 7% increase as compared to the first half of 2010.

Net income from other operating activities in the first half of 2011 was negative and amounted to PLN 71.2 million as compared to the positive figure of PLN 70.0 million in the first half of 2010.

Other operating revenues of the Group amounted to PLN 118.2 million in the first half of 2011, which means approximately 54% decrease as compared to PLN 257.2 million in the first half of 2010. The decrease in other operating revenues is mainly related to lower level of reversal of balance sheet provisions by PLN 95.3 million and lower – by PLN 23.4 million – level of received compensations, penalties and fines and level of reversed revaluation write-offs lower by PLN 16.9 million.

The other operating expenses in the Group amounted to PLN 189.3 million in the first half of 2011, what meant 1% increase as compared to the first half of 2010.

In the first half of 2011 the net result on financial activities was negative and totalled PLN 57.9 million as compared to the negative result on financial activities in amount of PLN 115.5 million in the first half of 2010.

The Group's financial revenues in the first half of 2011 amounted to PLN 149.2 million, which means decrease by approximately 41% as compared to PLN 254.5 million achieved in the first half of 2010. The decrease in financial revenues is mainly related to lower interest revenues by PLN 74.7 million and lower profit from disposal of investments by PLN 14.0 million.

The decrease of financial expenses by PLN 162.9 million in the first half of 2011 as compared to the first half of 2010 resulted mainly from lower negative foreign exchange differences by PLN 90.3 million, decrease of interest expenses by PLN 47.9 million and lower level of costs related to revaluation of financial by PLN 16.6 million.

The share in profit of associates amounted to PLN 168.4 million and was higher by PLN 56.2 million as compared to the first half of 2010. The share in profit of associates mainly related to PGE's share in profit of Polkomtel S.A.

As a result of the factors discussed above, the gross profit of the Group amounted to PLN 2,774.0 million in the first half of 2011 as compared to PLN 2,277.6 million in the first half of 2010.

Gross profit margin of the Group (gross profit to total sales revenues) in the first half of 2011 decreased to 20% from 22% in the first half of 2010. The decline is connected with the change of the electricity trading model of the Group and realization of the power exchange obligation by the generators. This change caused the increase of the revenues presented in the consolidated statement of the comprehensive income and resulted in lower gross profit margin despite achieving higher gross profit.

After taking the income tax into consideration, the net profit amounted to PLN 2,261.8 million in the first half of 2011 as compared to PLN 1,842.4 million in the first half of 2010.

Net profit attributable to the equity holders of the parent company increased by PLN 720.8 million in the first half of 2011 as compared to the first half of 2010 and amounted to PLN 2,220.2 million. The significant increase of the net profit for the shareholders of the parent company is a result of transformations in the PGE Capital Group, i.e. merger of PGE Polska Grupa Energetyczna S.A. with PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. as a result of implementation of the Consolidation Program, and purchase from the State Treasury of the minority shares packages in key companies of PGE Group.

Total comprehensive income of the Group in the first half of 2011 amounted to PLN 2,263.0 million as compared to PLN 1,844.1 million in the first half of 2010.

Consolidated statement of financial position

As at June 30, 2011 and as at December 31, 2010, non-current assets of the Group amounted respectively to PLN 43,152.2 million and PLN 44,137.4 million and accounted for 82% and 86% of total assets, respectively.

The decrease in the value of non-current assets by PLN 985.2 million in the period ended June 30, 2011 as compared to the year ended December 31, 2010 was mainly due to decrease in shares in associates accounted for under the equity method by PLN 1,349.3 million, what was caused mainly by reclassification of shares in Polkomtel S.A. from non-current assets to current assets (presented in item assets classified as intended for sale). The decline of the above mentioned positions was partly offset by growth in property, plant and equipment by PLN 290.3 million and other long-term assets by PLN 82.8 million (mainly related to increase of prepayments for purchase of shares and property, plant and equipment).

Current assets of the Group as at June 30, 2011 and as at December 31, 2010 amounted respectively to PLN 9,246.5 million and PLN 7,285.8 million.

The increase in the value of the Group's current assets by PLN 1,960.7 million in the period ended June 30, 2011 as compared to the year ended December 31, 2010 was mainly attributable to the described above reclassification of shares in Polkomtel S.A. to item: group's assets classified as intended for sale, increase in other short-term assets by PLN 375.8 million and increase in inventory by PLN 183.5 million.

The increase in other short-term assets in the period ended June 30, 2011 as compared to the year ended December 31, 2010 was chiefly due to receivables from dividends from associates and increase in VAT receivables.

The increase in inventory in the period ended June 30, 2011 as compared to the year ended December 31, 2010 was mainly connected with the increased level of provisions for CO_2 emission rights intended for sale, higher level of stock of materials, increase in intermediate goods and work in progress, as well as increase of level of provisions for certificates of origin of energy. This decrease was partly offset by decline in level of finished goods.

The increase in cash and cash equivalents in the period ended June 30, 2011 as compared to the year ended December 31, 2010 was described in the part relating to cash flow statement.

As at June 30, 2011 and as at December 31, 2010 total equity of the Group amounted respectively to PLN 38,651.2 million and PLN 37,632.1 million, i.e. it represented respectively 74% and 73% of total equity and liabilities. Non-controlling interest as at June 30, 2011 and as at December 31, 2010 amounted to PLN 612.5 million and PLN 598.8 million, respectively.

The increase in total equity by PLN 1,019.1 million results mainly from the profit for the period ended June 30, 2011 in amount of PLN 2,261.8 million. The distribution of profit for 2010 and allocation of part of the net profit, i.e. PLN 1,215.3 million, for the dividend payment and adjustment of payment from the profit for past periods in amount of PLN 0.4 million had the negative impact on the total equity.

The long-term liabilities as at June 30, 2011 amounted to PLN 7,201.3 million and were higher by PLN 1.5 million than as at December 31, 2010. The change in long-term liabilities mainly reflected the higher provision for deferred tax by PLN 201.5 million, higher by PLN 132.8 million deferred income and government grants and lower debt due to bank loans, borrowings, bonds and lease by PLN 298.6 million.

The decrease in long-term debt as at June 30, 2011 as compared to the level as at December 31, 2010 primarily resulted from decrease in long-term credits and loans from PLN 1,804.4 as at December 31, 2010 to PLN 1,505.8 million as at June 30, 2011, i.e. by PLN 298.6 million.

Short-term liabilities decreased from PLN 6,591.4 million as at December 31, 2010 to PLN 6,546.2 million as at June 30, 2011 mainly due to decrease in other financial liabilities by PLN 505.2 million (mainly as a result of decline in liabilities for purchase of the property, plant and equipment), short-term debt from the interest bearing loans, borrowings, bonds and lease lower by PLN 222.7 million, decrease in short-term provisions by PLN 187.7 million (mainly as a result of decrease of the provisions for purchase of CO_2 emission rights and provisions for value of property rights for redemption partly offset by increased provisions for annual reward, unused leaves and creation of provision for Voluntary Redundancy Program). Decrease in trade liabilities by PLN 161.7 million and decrease in income tax liabilities by PLN 150.4 million also affected the level of short-term liabilities. The decrease of described items was partially compensated by increase of value of other non-financial liabilities, mainly in connection with liabilities related to dividend payment.

Consolidated cash flow statement

Cash and cash equivalents amounted to PLN 2,842.8 million as at June 30, 2011 and were lower by PLN 4,420.9 million than at the end of the corresponding period of 2010.

The total net cash flow from operating activities for 6-month period ended June 30, 2011 amounted to PLN 2,950.1 million as compared to PLN 3,419.8 million in 6-month period ended June 30, 2010. Decrease in cash flows from operating activities in the 6-month period ended June 30, 2011 as compared to the 6-month period ended June 30, 2010 is mainly caused by the change in receivables (cash flow lower by PLN 337.2 million), change in inventory (cash flow lower by PLN 220.1 million), change in provisions (cash flow lower by PLN 134.1 million), change in liabilities other than bank loans (cash flow lower by PLN 115.4 million), change in prepayments and accruals (cash flow lower by PLN 40.0 million). The decrease of cash flow resulting from above factors was partly compensated by increase of gross profit from continuing operations by PLN 496.4 million.

Negative net cash flow from investing activities for the 6-month period ended June 30, 2011 amounted to PLN 2,166.3 million and was higher by PLN 359.4 million as compared to 6-month period ended June 30, 2010. The balance of net cash flows from investing activities for the 6-month period ended June 30, 2011 mainly consisted of expenses related to acquisition of property, plant and equipment and intangible assets in amount of PLN 2,130.4 million and to financial assets in amount of PLN 85.8 million.

Negative net cash flow from financial activities for the 6-month period ended June 30, 2011 amounted to PLN 677.9 million as compared to negative net cash flow from financial activities in amount of PLN 2,055.2 million for the 6-month period ended June 30, 2010. The balance of net cash flows from financial activities for the 6-month period ended June 30, 2011 mainly consisted of: (i) balance of inflows/ payments from loans, borrowings, bonds issues and financial lease amounting to PLN (-) 535.0 million, (ii) dividends paid to shareholders in amount of PLN (-) 91.5 million and (iii) interest paid in amount of PLN (-) 53.6 million. Among others, the investment loans were repaid by PGE Elektrownia Opole S.A. (PLN 212.6 million) and by PGE Górnictwo i Energetyka Konwencjonalna S.A. (PLN 91.7 million) in the first half of 2011.

3.2. Business segments

Table: Key operational figures.

Key figures	**Unit**	**H1 2011**	**H1 2010**
Lignite extraction	millions of tonnes	22.81	21.52
Net electricity production*, including:	TWh	27.26	26.21
Power plants - lignite	TWh	18.07	17.90
Power plants – hard coal	TWh	6.90	6.12
CHPs – hard coal	TWh	0.76	0.72
CHPs – gas	TWh	1.07	0.86
Pumped storage power plants	TWh	0.19	0.25
Hydro power plants	TWh	0.24	0.33
Wind power plants	TWh	0.03	0.03
Heat sales	GJ millions	12.37	13.62
Sales to Final Customers**	TWh	15.85	15.36
Sales to Final Customers outside PGE Group***, including:	TWh	15.34	14.81
Tariff G	TWh	4.61	4.61
Distribution of electricity ****	TWh	15.37	15.13

* including productions from biomass in period January-June 2011 – 0.42 TWh, in period January-June 2010 – 0.28 TWh
** sales by PGE Obrót S.A. with additional estimation and with taking into account the sales within PGE Group
*** total sales by PGE Obrót S.A. with additional estimation
**** with additional estimation

Table: Breakdown of the Group's gross income (including flows between segments), by business segments, for the first half of 2011 and 2010.

in PLN million	**Total gross income**				
	H1 2011	*(%) share*	**H1 2010**	*(%)share*	**% change**
Conventional Generation	6,718.0	*31%*	6,183.4	*28%*	*9%*
Renewable Energy	271.4	*1%*	323.5	*1%*	*-16%*
Wholesale Trading	5,010.4	*23%*	6,007.6	*27%*	*-17%*
Distribution	2,628.7	*12%*	2,494.7	*11%*	*5%*
Retail Sale	6,227.3	*29%*	6,198.7	*28%*	*0%*
Other activity	850.4	*4%*	826.0	*4%*	*3%*
Total	**21,706.2**	*100%*	**22,033.9**	*100%*	***-1%***
Intersegmental eliminations	**-7,790.9**		**-11,901.2**		***-35%***
Net income	**13,915.3**		**10,132.7**		***37%***

Table: Key financial indicators for each business segment for the first half of 2011 (after eliminations).

in PLN million, unless specified otherwise	**Conventional Generation**	**Renewable Energy**	**Wholesale Trading**	**Distribution**	**Retail Sales**	**Other**
			H1 2011			
EBITDA	2,775.1	104.5	110.1	854.1	80.2	71.1
EBIT	2,030.8	40.4	98.0	404.6	75.9	20.0
Capex	1,098.1	68.1	3.7	392.8	1.9	46.2
Segment Assets	27,462.0	1,793.2	769.6	13,520.5	1,766.7	1,097.5

Table: Key financial indicators for each business segment for the first half of 2010 (after eliminations).

in PLN million, unless specified otherwise	**Conventional Generation**	**Renewable Energy**	**Wholesale Trading**	**Distribution**	**Retail Sales**	**Other**
			H1 2010			
EBITDA	2,336.5	165.0	102.2	745.6	140.2	100.6
EBIT	1,589.2	102.1	89.7	312.5	136.0	44.8
Capex	1,359.6	52.0	13.4	342.5	3.1	87.2
Segment Assets	25,232.4	1,697.8	580.0	13,361.2	1,614.0	1,079.9

3.2.1 Conventional Generation

In the first half of 2011 total sales revenues for Conventional Generation amounted to PLN 6,718.0 million, which means ca. 9% growth as compared to the first half of 2010. EBIT of the segment in the first half of 2011 was PLN 2,030.8 million, and EBITDA was PLN 2,775.1 million. In the analogical period of previous year EBIT was PLN 1,589.2 million, while EBITDA was PLN 2,336.5 million. Growth of EBIT in the first half of 2011 as compared to the first half of 2010 was mainly due to higher revenues from sales of electricity and to higher income - by PLN 133.3 million - achieved from LTC compensations. Higher revenues were mainly due to higher volume of energy sold and growth of electricity prices.

In the first half of 2011 capital expenditures in Conventional Generation segment amounted to PLN 1,098.1 million as compared to PLN 1,359.6 million in the first half of 2010.

Table: Capital expenditures incurred in Conventional Generation segment in the first half of 2011 and 2010, by particular investment tasks.

in PLN million	**Capital expenditures**		
	H1 2011	**H1 2010**	**% change**
Investments in generating capacities, including:	1,032.4	1,262.0	*-18%*
Development	*837.9*	*1.053.8*	*-20%*
Modernization and replacement	*194.5*	*208.2*	*-7%*
Purchases of finished capital goods	10.9	15.4	*-29%*
IT	5.7	9.4	*-39%*
Vehicles	2.5	0.9	*178%*
Other	46.6	71.9	*-35%*
TOTAL	**1,098.1**	**1,359.6**	*-19%*

During the first half of 2011 highest capital expenditures were incurred for the following projects: (i) modernization of units 5-6 in Bełchatów power plant (PLN 281.2 million), (ii) modernization of units 7-12 in Bełchatów power plant (PLN 48.6 million) (iii) construction of a 858 MW power unit in

Bełchatów power plant (PLN 203.3 million), (iv) construction of desulphurization installation on units 1-2 in Bełchatów power plant (PLN 93.7 million), (v) construction of desulphurization installation on units 5-6 in Dolna Odra power plant (PLN 77.2 million) and construction of steam boiler producing electricity from biomass in Szczecin power plant (PLN 63.8 million).

3.2.2 Renewable energy

In the first half of 2011 total sales revenues in the Renewable Energy segment amounted to PLN 271.4 million as compared to PLN 323.5 million in the first half of 2010. The segment's EBIT in the first half of 2011 was PLN 40.4 million, and EBITDA was PLN 104.5 million. In the corresponding period of the previous year, EBIT was PLN 102.1 million, and EBITDA was PLN 165.0 million. The decline if EBIT in the first half of 2011 was mainly caused by lower electricity production volume due to unfavourable hydrological conditions.

In the first half of 2011 capital expenditures in the Renewable Energy segment amounted to PLN 68.1 million as compared to PLN 52.0 million in the first half of 2010.

Table: Capital expenditures incurred in Renewable Energy segment in the first half of 2011 and 2010.

in PLN million	**Capital expenditures**		
	H1 2011	**H1 2010**	**% change**
Investments in generating capacities, including:	65.5	50.0	*31%*
Development	*2.4*	*3.9*	*-38%*
Modernization and replacement	*63.1*	*46.1*	*37%*
Purchases of finished capital goods	0.1	0.3	*-67%*
IT	0.6	0.6	*0%*
Vehicles	0.1	0.3	*-67%*
Other	1.8	0.8	*125%*
TOTAL	**68.1**	**52.0**	*31%*

3.2.3 Wholesale trading

In the first half of 2011 total sales revenues in the Wholesale Trading amounted to PLN 5,010.4 million, which means an approximately 17% decrease comparing to the first half of 2010. The decline in sales revenues is mainly connected with the change of trading model in PGE Capital Group. The segment's EBIT in the first half of 2011 was PLN 98.0 million, and EBITDA was PLN 110.1 million. In the corresponding period of the previous year, EBIT was PLN 89.7 million, while EBITDA was PLN 102.2 million. The higher EBIT in the first half of 2011 as compared to the first half of 2010 resulted mainly from realization of higher margin on trading of related products, that offset lower margin on electricity trading and lower result on other operating activities (in the corresponding period of 2010 provision for costs related to the claim of Alpiq Holding AG was decreased).

In the first half of 2011 capital expenditures in Wholesale Trading segment amounted to PLN 3.7 million and related mainly to IT.

3.2.4 Distribution

In the first half of 2011 total sales revenues in the Distribution segment amounted to PLN 2,628.7 million, as compared to PLN 2,494.7 million in the first half of 2010. The segment's EBIT in the first half of 2011 was PLN 404.6 million, and EBITDA was PLN 854.1 million. In the corresponding period of the previous year, EBIT was PLN 312.5 million, while EBITDA was PLN 745.6 million. The growth of EBIT by 29% was mainly due to higher revenues from sales of the distribution service as a result of higher volume of distributed energy, the change in average distribution tariffs in particular groups and increase in revenues from grid connection fees.

In the first half of 2011 capital expenditures in Distribution segment amounted to PLN 392.8 million and constituted approximately 24% of total capital expenditures of PGE Group. In the first half of 2010 capital expenditures in this segment amounted to PLN 342.5 million, what constituted more than 18% of total capital expenditures of PGE Group. Capital expenditures were mostly related to connection of new customers to the network and constituted 49% and 50% of total expenditures incurred in the segment in the first half of 2011 and 2010 respectively, and to investments resulting from construction of new HV, MV and LV electro energy grids which constituted approximately 32% and 27% of total expenditures incurred in the segment in the first half of 2011 and 2010 respectively.

Table: Capital expenditures incurred in Distribution segment in the first half of 2011 and 2010, by particular investment tasks.

in PLN million	Capital expenditures		
	H1 2011	**H1 2010**	**% change**
HV, MV and LV power networks	127.0	90.8	*40%*
Communication, remote switching and metering equipment	39.8	24.5	*62%*
IT	5.2	10.8	*-52%*
Land buyout	5.0	1.2	*317%*
Connection of off-takers	193.6	170.1	*14%*
Purchases of finished capital goods	8.0	24.3	*-67%*
Other	14.2	20.8	*-32%*
TOTAL	**392.8**	**342.5**	*15%*

3.2.5 Retail Sales

In the first half of 2011 total sales revenues in the Retail Sales segment amounted to PLN 6,227.3 million compared to PLN 6,198.7 million in the first half of 2010. EBIT of the segment in the first half of 2011 was PLN 75.9 million, and EBITDA was PLN 80.2 million. In the analogical period of the previous year EBIT was PLN 136.0 million, and EBITDA was PLN 140.2 million. Decline of EBIT in Retail Sales segment by approximately 44% in the first half of 2011 as compared to the first half of 2010 resulted mainly from higher expenses related to obligation of redemption of property rights (certificates of origin of electricity), what was partly compensated by the growth of prices.

Capital expenditures in Retail Sales segment amounted to PLN 1.9 million in the first half of 2011, constituted approximately 0.1% of total capital expenditures of PGE Group, and were mainly related to expenditures for IT (customer support systems), modernisations of small hydroelectric power plants and purchase of finished capital goods.

3.2.6 Other operations

In the first half of 2011 total sales revenues for Other operations amounted to PLN 850.4 million, as compared to PLN 826.0 million in the first half of 2010. EBIT of the segment in the first half of 2011 was PLN 20.0 million, and EBITDA was PLN 71.1 million. In the analogical period of the previous year EBIT was PLN 44.8 million, and EBITDA was PLN 100.6 million. Decline of EBIT in the first half of 2011 as compared to the first half of 2010 mainly resulted from higher costs incurred by the companies from this segment as compared to the first half of 2010.

Capital expenditures for tangible fixed assets in Other operations segment in the first half of 2011 amounted to PLN 46.2 million. Within the above mentioned amount, PLN 9.5 million was spent by Exatel S.A. for IT development in the first half of 2011. The rest of the capital expenditures were mostly related to expenses for development and modernization of fixed assets required to render services under ancillary activities.

In the reporting period PGE S.A. did not record any significant failures in its activities which would have effect on achieved results.

3.3. Publication of financial forecasts

PGE Polska Grupa Energetyczna S.A. did not publish forecasts of the Company's financial results.

4. Risks and threats of the PGE Capital Group

The activity of major PGE Capital Group companies, as well as other entities operating in the electrical and power sector, is exposed to a number of both external risk and threats connected with market, regulatory and legal environment, as well as internal risks and threats accompanying their operations.

Key risks and threats, to which the PGE Capital Group's activity is exposed, are described below.

4.1. Risk factors connected with market environment and general macroeconomic situation in Poland and in the world

4.1.1 Risk connected with macroeconomic situation in Poland and in the world

The operations of PGE Group are affected mainly by macroeconomic factors related to Polish economy, such as interest rates, PLN exchange rate, inflation rate, unemployment rate, Polish GDP, changes in directions of the economic and tax policy of the state, and also volatility of prices of electricity, fuel, CO_2 emission rights, and availability of materials used for production of electric power and heat. Other than factors associated with Polish economy, our operations are also affected by macroeconomic conditions in other countries, particularly other Member States of the European Union. Any deterioration of the general economic conditions in Poland or in the world may considerably and negatively impact the operations, performance or financial standing of the Group.

4.1.2 Risk relating to an increase in competition (right to choose an energy supplier)

Given the on-going development of the retail market, increasing knowledge of energy recipients on market operation and their rights (including a TPA rule), as well as increasing activity of energy sellers, the PGE Group is exposed to the risk of losing its existing customers in the retail market and the risk of decreasing margin on sale to the existing customers. It is, however, necessary to point out that market development is also an opportunity for the retail sales segment of the PGE Group to acquire new customers from outside the historic operating area of the Retail Sales companies of the PGE Group and increase both sales volume and profit.

4.1.3 Risk of a decrease in demand for electricity and heat

The PGE Capital Group's income is substantially dependant on the consumption of power and heat by the end users. In a long run, power consumption is expected to grow. However, there is no guarantee that such a growth will occur and that the rate of growth will achieve an assumed level. Demand for electricity may decline, in particular, as a result of: (i) economic slowdown, (ii) possible reduction of power consumption level by recipients of low economic standing, (iii) development of new energy saving technologies, (iv) weather conditions. Decreasing growth rate of demand for electricity and limited access to interconnectors limiting opportunities for exporting electricity produced by the Group may have a significant adverse impact on the activity and financial results of Group companies.

4.2. Risk factors connected with regulatory and legal environment

4.2.1 Political risk

The activity of the PGE Group in key operating areas, i.e. lignite mining, generation, distribution and sale of electricity and heat, is subject to legislation, government regulation and government policy adopted by Polish authorities and agencies, authorities of the European Communities and the European Union, and other states. Changes in such legislation, regulations and/or policies may be influenced by political factors, which in turn may affect business activity of the Group including, inter alia, the regulation of electricity prices, heat prices and distribution services for off takers, in particular households.

4.2.2 Risk of changes in law and other regulations relating to our activity, as well as changes in interpretation or application thereof

The Group's activity is subject to numerous Polish and European laws and regulations (including treaties, orders, directives, decisions of the European Commission, and decisions of the European Tribunal of Justice) and international law (treaties, other international agreements).

The provisions of the laws, regulations, decisions, positions, opinions and actions of relevant authorities important for the Group's activity are subject to changes. In particular, the Energy Law was amended several dozen times, and some of the amendments introduced significant changes with respect to core business areas. Types, directions and scopes of such amendments may have an unpredictable impact on the Group's activity.

Moreover, environment protection regulations become more strict, and adjustment to these changes may be connected with the additional significant expenditures. Non-compliance with regard to environment protection requirements may lead to PGE Group responsibility, including financial sanctions or periodical or even permanent suspension of exploitation of particular installations.

The Group's activity is also significantly dependant on decisions, positions, opinions and other actions of Polish authorities, authorities of the European Communities and the European Union, and authorities of other states, and although certain decisions, positions, opinions and other actions of such authorities may not take the form of laws, but must be, in practice, applied by the Group companies. In particular, in the energy sector, an authority regulating the Polish fuel and energy market is the President of the Energy Regulatory Office, who is competent, for example, to grant and withdraw concessions based on which we run our activity, and approve (to a defined extent) and control the application of electricity and heat tariffs in terms of their compliance with the provisions of the Energy Law, including the analysis and verification of costs applied by power companies as reasonable to calculate prices and rates under tariffs. Therefore there is a risk that the tariffs subject to approval by the President of the Energy Regulatory Office, are not approved or are approved with delay or are approved in different form than applied for. Additionally, for the violation of obligations set forth in the Energy Law, the President of the Energy Regulatory Office may impose pecuniary fines of up to 15% of income earned by the entity subject to the fine (PGE S.A. or a Group company) in a previous tax year and, and if the fine is related to the licensed activity, the fine may amount up to 15% of income earned on the licensed activity by the fined entity in the previous fiscal year.

4.2.3 Risk relating to the requirement for licenses

The Group's core activity is subject to a number of licenses, including licenses for the electricity and heat generation, the distribution of electricity and heat, the electricity trading, the heat trading, the fuel gas trading, as well as for the lignite mining. In order to continue business activity, the Group needs to maintain and extend existing licenses. Any withdrawal or limitation of licenses or the imposition of additional conditions under the license may cause that Group companies will not be able to run their activities, their activities will be significantly limited or substantially influenced otherwise.

4.2.4 Risk related to the obligation of public sales of electricity

The Energy Law introduced an obligation for electric power producers (as from August 9, 2010) to sell, to a certain extent, their electric power on the power exchange or on a public basis with equal access through the open tender or on the internet platform on the regulated market. The new regulations were imprecise and raise significant doubts in terms of interpretation, what caused uncertainty how electric power producers can fulfil that obligation. In particular, interpretation doubts were raised whether the sale through the internet platform, which runs outside of the regulated market, fulfilled the obligation of public sale imposed by the Energy Law. On July 15, 2011 the lower house of the Polish Parliament passed the law on change of the Energy Law that included more precise provisions on the above issue. The next step is the approval of the law by the Senate, signing by the President of the Republic of Poland and the publication of law.

In case of successful legislative process, there is a risk that the President of the Energy Regulatory Office may question the actual fulfilment of the requirement, imposed on the given producers from the PGE Group, to sell the electricity on a public basis that was being sold through the trading internet platform until the date of passage of the resolution. As a result, the President of the Energy Regulatory Office may levy certain sanctions on the energy producer, including a fine, and even question electric power sale contracts concluded by that entity.

4.2.5 Risk resulting from the potential violation of antitrust regulations

Distribution company of the PGE Group is a natural monopolist in the area of electricity distribution services. In addition the PGE Group is the main electricity producer in Poland (approximately 40% share in the electricity generation market) and is one of the biggest electricity sellers in Poland. Given its monopolist or dominant position in relevant markets, the PGE Group is subject to limitations in the form of a ban on overusing its dominant position based on antitrust regulations of the Polish law and the law of the European Union. In the case of any violation thereof, antitrust authorities (the President of the Office for Consumer and Competition Protection, European Commission) may order to take up defined actions or enforce sanctions in the form of financial penalties.

4.2.6 Risk connected with regulations obligating the Company to ensure the sufficient number of certificates of origin

PGE Group companies active in electricity trading must obtain and present for redemption to the President of the Energy Regulatory Office with certificates of origin for electricity coming from renewable sources (green certificates). Alternatively, such companies may pay a substitute fee. In the case an obligation to obtain and present for redemption to the President of the Energy Regulatory

Office with certificates of origin of energy from renewable sources is not fulfilled or a substitute fee is not paid, a company may be charged with a financial penalty. Similar rules apply to energy produced in the cogeneration (yellow, red and violet certificates). Current support system guarantees the effectiveness of green and violet certificates for few years ahead, while effectiveness of yellow and red certificates is guaranteed till the end of 2012, then the cogeneration support system, based on these certificates, expires.

Additionally, prices of certificates of origin are determined by current regulations, decisions of regulatory or other authorities, including in particular those relating to the definition of relevant substitute fees. Therefore, income earned by PGE Group companies from the sale of certificates of origin of energy produced thereby depends on administrative decision and legal regulations. Currently in Poland, as well as in EU institutions, a discussion lasts on the future level of support for the renewable energy producers. That may result in limiting of that support or its dependency from the market electricity price, and also in its diversification depending on the renewable energy source.

4.2.7 Risk connected with the excise tax

The transfer of an obligation to pay excise from electricity producers to entities selling electricity to end-users as of March 1, 2009 is subject, in practice, to the detailed analysis of all issues connected with the calculation and collection of the tax by competent services at PGE Group companies. Because of the shortage of stabilised practice at tax authorities, some of mechanisms of the Excise Tax Act still raise controversies and doubts.

There is also a risk that in case of recovery of the undue but paid income tax by the generating entities from the PGE Group, the civil law claims may be directed against them by the off-takers of the electricity, who in past actually took the economic burden of the excise tax (e.g. based on the accusation of the baseless enrichment). The electricity off-takers started to file requests to companies from PGE Group for the payment in this regard and the Group expects that the number of such claims will rise. The appraisal of the scale of the prospective claims is currently not possible, but this issue may have material adverse effect on the future activity, results or the situation of the Group.

4.2.8 Risk connected with the programme of CO_2 emissions reduction

The electricity and heat generation at power plants and CHP plants fuelled with fossil fuels is connected with relatively high CO_2 emissions. Therefore, any regulations on the reduction of emission of CO_2 to the environment, including regulations coming within the so called power and climate package of the European Union, will have a significant impact on the Group's activity. In particular limited number of free CO_2 emission allowances under NAP II for 2008-2012 as compared to NAP I for 2005-2007 mean that CO_2 emissions outside the scope of free allowances allocated to Polish installations under NAP requires the purchase of EUA emission allowances or CER or ERU units, the prices of which fluctuate. There is also risk that the newly commissioned generating units from PGE Group will not be granted the assumed free allowances or that the actually granted amount will be lower than projected.

Resolutions, which will be taken in 2011, likely will decide what derogations Poland will obtain with regard to free CO_2 emission allowances for generators for 2013-2020. Moreover on the European forum there's a strong lobby postulating the rise of EU's CO_2 reduction target from 20% to 30% till 2020, however it does not seem that this voting will close the discussion on that matter. Additionally, according to the assumptions of the third settlement period, from 2020 free CO_2 emission allowances will not be granted. The above issues may lead to significant growth of electricity prices, what could result in decline of electricity demand and negatively affect the financial situation of the Group.

4.2.9 Risk of restrictions on emissions of substances other than CO_2 to the environment and the enforcement of more restrictive BAT standards

The activity of Group companies, including in particular the electricity and heat generation, is connected with the emission of not only CO_2, but NO_x, SO_2, dusts and other substances, to the environment. The systems that require an integrated permit, i.e. systems that, due to their type and scale of operation, may materially pollute some component parts or the environment as a whole, must comply with the best available techniques requirements (Best Available Techniques, "BAT"), and that involves making significant investment expenditures.

New Directive of European Parliament and Council of Europe no 2010/75/UE of November 24, 2010 on industrial emissions (integrated prevention of pollution and its control), called IED, introduces more strict requirements with regard to limits of pollution emissions with reference to previously binding (inter alia, LCP directive). IED Directive must be implemented to the domestic laws by January 7, 2013. IED Directive introduces increased role of the BAT reference documents (so called BREFs). More restrictive emission standards may force PGE Group to make substantial expenses to adapt to new requirements. Therefore, there is a risk that certain of our equipment or installations will not be adjusted to applicable requirements by the imposed deadline, which may reduce electricity output.

4.3. Risk factors connected with the operating activity of the PGE Capital Group

4.3.1 Risk of disruption of fuel supplies to our power plants, CHP plants and heat plants

The generation of electricity and heat by Group power plants, CHP plants and heat plants depends on fuel supplies, including lignite (in particular to PGE GiEK S.A. Branch Elektrownia Bełchatów and PGE GiEK S.A. Branch Elektrownia Turów), hard coal (in particular to PGE Elektrownia Opole S.A. and PGE GiEK S.A. Branch Zespół Elektrowni Dolna Odra), and gas. There is a risk of disruptions in fuel supplies to Group's generating units, mainly for technical reasons (breakdown), natural reasons (calamities, difficult weather conditions), social reasons (strikes), economic and political reasons (limited supply of fuel or transport services and imposing unfavourable conditions of supply and transport) and other reasons. Any break or limitation in fuel supplies may cause a break or significant limitation in electricity or heat generation.

4.3.2 Risk of insufficient stocks of fuel

The Energy Law obliges every electricity or heat generating enterprise to maintain a stock of fuel in an amount that can guarantee the continuity of electric power and heat supply. The ERO President imposes fines (of up to 15% of income) for the failure to maintain the required level of fuel stocks. The shortage of required level of fuel stocks may also result in the suspension or reduction of electricity or heat generation.

4.3.3 Risk connected with mining site rehabilitation expenses

Mining companies representing the Conventional Generation segment must rehabilitate sites where they carry out their mining works. The Geological and Mining Act, as well as implementing regulations thereto, obligate mining companies to make contributions to the mine liquidation fund constituting 10% of a maintenance fee. Such funds may be used only to cover costs of mine liquidation, including rehabilitation costs. It may happen that funds and reserves of mining companies allocated to such a purpose will not cover actual rehabilitation expenses that the companies will have to bear in future. This may result in a need to increase amounts payable to the rehabilitation fund, create other reserves, and finance site rehabilitation from external sources.

4.3.4 Risk connected with weather conditions

Weather conditions influence technical and economic conditions of energy and heat generation and distribution and create seasonable demand for energy. Such factors may cause limitations to energy generation, mainly as a result of water in natural and artificial basins that is used for cooling the generating units getting too hot or too low, as well as limitations to transmission capacities of the electrical and power system. In addition, bad weather conditions, including in particular the force of wind in the case of wind farms and water surface in the case of water power plants, have a significant impact on electricity production from renewable sources. While, large rains cause problems with the dehydration of opencast lignite mines. Extreme weather conditions break lines or damage electrical and power devices very often, which results in breaks of or limitations to power supply. It must be added that all the above phenomena are mostly unpredictable and in consequence may cause lowering of PGE Group income and claims by the electricity and heat off-takers for compensations or for discounts. Removal of damages in the electro energy grid is also connected with additional expenses relating to reconstruction of the damaged elements.

4.3.5 Risk relating to maintenance, repairs and modernisations

PGE Group companies' business activity consisting in lignite mining and energy generation and distribution requires regular maintenance, repairs and modernization of assets. Such actions should ensure that equipment's life is optimum and guarantee necessary availability of key assets, including cost minimisation. Untimely or inadequate maintenance or repair and operation services shorten the life and worsen parameters of assets. This may contribute to breakdowns and outages or limitations to coal mining, energy generation and power supply, which may consequently result in the reduction of the companies' income. While assets recovery and modernisation investments are subject to substantial expenditure and, at the same time, particular stages of modernisation works may be delayed, for example, by uncertainty relating to the acquisition of sufficient financial resources, protests of environmental organisations, strikes of employees, growth of costs, delays caused by contractors, difficulties in the acquisition of necessary permits, or other unexpected difficulties.

4.3.6 Risk of unsettled legal status of the real estates

In the case of many properties (land and buildings) owned by the PGE Group (in particular those used by distribution companies), there are doubts as to the legal title of such companies to use the properties. Very frequently, investments, mainly ones related to lines, were carried out in third party properties without express consent of owners. Corresponding national legal regulations are not clear and judicature on cases relating to such situations has been changed in recent years. This situation is connected with a risk of claims to be filed against PGE Group companies, like in the case of distribution system operators. We may not exclude further cases of this type and related additional costs or even a need to stop using certain properties.

4.3.7 Risk relating to obtaining debt financing

A part of the Group's activities is financed from external sources (bank loans, bonds, etc.). PGE S.A. and Group companies are parties to many financial agreements of the complex legal structure. It is possible that in future it will be difficult to obtain new finance at an amount and terms desired by the Group. This may be caused by still unstable situation in the financial and capital markets in Poland and abroad, poor general economic situation in Poland and abroad, or other reasons that are unpredictable now. Such circumstances may negatively affect the terms of financing, in particular may lead to the growth of costs of such financing (higher interest rates, commissions, etc.). Higher costs of financing may affect the Group's results.

4.3.8 Risk associated with a downgrade or withdrawal of the rating of PGE

PGE S.A. has received positive evaluations from rating agencies confirming its high reliability connected with investment in its debt securities. Nonetheless, rating agencies may at any time downgrade or inform PGE S.A. of their intention to downgrade the rating. The rating agencies may also completely withdraw their ratings which may have the same consequences as a downgrade in PGE's ratings. Any decrease in PGE's rating may increase the costs of external financing, limit access to capital markets and adversely affect the capacity of PGE Group companies to sell their products or contract economic transaction, especially long-term ones. This may in turn decrease the liquidity of PGE S.A. and adversely affect the operating results and financial condition of PGE Group (see p. 5.5 Rating).

4.3.9 Risk associated with the decisions of the President of the Energy Regulatory Office regarding the implementation of LTC Act

PGE S.A. and certain Group generators ware parties to LTC. The termination of LTC set forth in the LTC Act is a precedential programme of this type in Poland. The provisions of the LTC Act defining, in particular, terms for the calculation, payment and adjustments of funds to cover stranded costs, calculation and payment of such funds to generators coming within capital groups (including PGE Capital Group), tax consequences of LTC termination and fund payment, as well as other issues, are complicated and there is no defined practice for their application in Poland. Producers that terminated LTC and are authorised to receive funds to cover stranded costs, including PGE Group generation companies, are exposed to an obligation to return funds received in the case of the negative (annual or final) correction of stranded costs.

Up till now, the decisions on determining the annual adjustment of stranded costs and the annual adjustment of costs generated in gas-fuelled units were issued the President of the Energy Regulatory Office three times. The first decisions were issued on July 31, 2009 and were related to the settlement of year 2008, which was the first, not full year of execution of LTC Act. The further decisions were issued in dates determined by the LTC Act.

The aggregate value of stranded costs and the annual adjustment of costs generated in gas-fuelled units for years 2008-2010 for the entitled generators from PGE Group, resulting from the decisions of the President of the Energy Regulatory Office, amounts to PLN (-) 941.1 million.

The Management Board of PGE, as well as the Management Boards of the generators from PGE Group, that are subject to LTC compensations scheme, consider the decisions of the President of the Energy Regulatory Office as issued with the breach of the LTC Act and appealed to the District Court in Warsaw, Court of Competition and Consumer Protection (details of the on-going proceedings are presented in Note 21.1 to the consolidated financial statements).

4.3.10 Risk of transfer prices

The Company and its subsidiaries have concluded, and continue to conclude, many transactions with the other PGE Group members. These transactions specifically relate to the sale of fuels, electricity, emission allowances, certificates of origin and certain services. Even though the Company and the Group companies carefully follow the arm's length principle in dealings with related parties, and even though they are now implementing unified standards regarding the compiling of documentation and procedures in this regard, we cannot preclude potential disputes with the tax authorities in this regard.

4.3.11 Risk of insufficient insurance protection

The activity of the PGE Capital Group is exposed to a number of risks connected with natural calamities, breakdowns and damages. The Group's business activity is also connected with third party liability towards third persons for personal injuries, property damages or so called pure financial loss. The Group maintains insurance policies covering only certain types of damages and there is a risk of insufficient insurance coverage. In addition, there are risks that are not subject to any insurance protection or in the case of which compensations, if any, are not likely to fulfil claims or loss. Consequences of such events will be charged to costs of particular Group companies, what may have a negative impact on their results.

4.3.12 Risk relating to court, arbitration and administrative proceedings

PGE S.A. and other PGE Group companies are parties to court, arbitration or administrative proceedings that are important for the Group's activity. The Group takes up actions aiming at the settlement of such cases to our benefit, but there is a risk that they will be resolved unfavourably for Group companies. There is also a risk that in future other proceedings will be initiated against PGE S.A. and other PGE Group companies, which will be resolved unfavourably for us, which may have an adverse impact on the Group's activity and financial results.

Risks connected with court, arbitration and administrative proceedings that are essential for the Group's activity are described in Note 15 to the consolidated financial statement.

Over 100 company and inter-company trade unions are present in the PGE S.A. and PGE Group companies and over 27 thousand employees of the Group are members. Pursuant to the current provisions of law, trade unions influence the legislative process. They are also able to exert pressure on employers in a number of ways, including in the form of collective labour disputes. PGE Group companies are parties to a number of corporate and sectoral collective bargaining agreements. Furthermore, management boards of many Group companies have entered into social agreements with trade unions which confer considerable power upon employees and trade unions. The necessity to consult or co-ordinate certain actions with the trade unions may delay, or even render impossible, such actions and may lead to collective disputes, involving strikes or other labour protests. Furthermore, should any significant redundancy program be required in the PGE Group in the future, the obligation to make high severance payments to employees may delay or limit our ability to carry out such redundancy program or may increase its cost.

5. Other significant events of the reporting period and subsequent events

Other significant events, having impact on the Group's activities and the ones which occurred after the end of the reporting period until the date of approval of the financial statements, were described in detail below and in Note 21 to the consolidated financial statements.

5.1. Agreement for performance of electricity transmission services concluded between PGE Dystrybucja S.A. and PSE Operator S.A.

On January 13, 2011 PGE Dystrybucja S.A. and PSE Operator S.A. concluded an agreement for provision of the electricity transmission services ("Agreement"). Agreement was concluded for indefinite period and will be performed on the whole operation area of PGE Dystrybucja S.A. As at effective date of the Agreement, the agreements existing between PSE Operator S.A. and the companies, which as from consolidation date were incorporated into PGE Dystrybucja S.A., were dissolved. As a result of concluding of above Agreement, centralization of settlements of services provided by Transmission System Operator ("TSO"), that are subject matter of the agreement, took place in PGE Dystrybucja S.A.

The subject matter of the Agreement is the provision of the services of electricity transmission, comprising both domestic and international transmission services provided by TSO for PGE Dystrybucja S.A. The Agreement also comprises the National Power System accessibility services provided by TSO to PGE Dystrybucja S.A. The settlements are conducted on the ground of tariff of PSE Operator. Total value of the Agreement for 5-year period is estimated at PLN 6.1 billion.

5.2. Development plans of PGE Dystrybucja

The President of Energy Regulatory Office ("ERO") informed in the letter dated December 23, 2010, that the drafts of development plan for PGE Dystrybucja S.A. submitted to ERO, are considered agreed in material scope with regard only to 2011. However, in the letter dated June 29, 2011, the President of ERO informed that the submitted drafts of development plan are considered agreed in material scope for years 2012-2015. Simultaneously, the final volume of revenue from distribution activities will be determined during the proceedings on the approval of the tariffs set by PGE Distribution S.A. for the years included the plan. The capital expenditures totalling approximately PLN 5.8 billion were considered as justified expenditures for years 2011-2015 for PGE Dystrybucja S.A.

The mentioned capital expenditures are presented in 2010 constant prices and will be adjusted with the index of consumer goods and services (consumer price index 'CPI') in particular years during the tariff proceedings.

5.3. Conclusion of an agreement for the sale of shares in Polkomtel S.A. to Spartan Capital Holdings Sp. z o.o.

On 30 June, 2011 a preliminary agreement was signed between PGE, PKN ORLEN S.A. ("PKN"), KGHM Polska Miedź S.A. ("KGHM"), Vodafone Americas Inc, Vodafone International Holdings B.V. (together "Vodafone") and Węglokoks S.A. ("Weglokoks") as the sellers ("Sellers"), and Spartan Capital Holdings Sp. z o.o as the purchaser ("Purchaser") for the sale of 100% shares in Polkomtel S.A. (the "Agreement"), including the entire 21.85% PGE shareholding in Polkomtel S.A.

As a result of the Agreement, PGE agreed to sell 4,479,191 ordinary registered shares of Polkomtel S.A., with nominal value of PLN 100 per share, representing approximately 21.85% of registered capital of Polkomtel S.A. at the total price of PLN 3,289.5 million.

The total transaction consideration payable in cash implies an Enterprise Value of PLN 18.1 bn. After deductions attributable to debt of Polkomtel S.A. and dividend payable for the benefit of current Shareholders (i.e. Sellers) the net proceeds amount to PLN 15.1 billion.

The transaction is subject to approval by the Polish Office of Competition and Consumer Protection which, based on the Agreement, must be obtained till the end of year 2011, otherwise the Agreement will be terminated unless parties agree differently. Following the completion of the transaction and the acquisition by the Purchaser of 100% of shares in Polkomtel S.A., PGE, PKN, KGHM, Vodafone and Weglokoks will no longer hold any shares in Polkomtel S.A.

5.4. Decisions of the President of the Energy Regulatory Office regarding the annual adjustments of the stranded costs for 2010

In letters dated July 29, 2011 and July 31, 2011 the President of the Energy Regulatory Office (the "ERO President") handed over his decisions concerning the annual adjustment of the stranded costs and annual adjustment of the costs generated in gas-fired units for the year 2010, which are due to five generators from PGE Capital Group according to the Act of June 29, 2007 on coverage of stranded costs resulting at generators in relation to accelerated termination of long-term contracts.

According to the mentioned decisions, generators from PGE Capital Group are obliged to return approximately PLN 317 million in total to Zarządca Rozliczeń S.A. The return of this amount will not affect the reported results of the PGE Capital Group.

The Management Board of the Company, as well as the Management Boards of PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Elektrownia Opole S.A., disagree with the decisions of the ERO President and the appeals were filed to the District Court in Warsaw, Court of Competition and Consumer Protection ("CCCP") between August 16-18, 2011.

A similar dispute with the ERO President, regarding the annual adjustment for the year 2008 was settled fully in favour of PGE Capital Group. In accordance with six verdicts of the CCCP announced on May 26, 2010, the decision of the ERO President, regarding the settlement of value of annual adjustment of the stranded costs for 2008, due to the termination of long-term contracts for sale of capacity and electricity, was changed in accordance with the appeals filed by the entities from PGE Capital Group. These verdicts are not yet valid and the ERO President appealed against these decisions.

The dispute regarding the annual adjustment for the year 2009 has not been settled yet.

5.5. Rating

On August 4, 2011 Fitch Ratings affirmed the PGE's Issuer Default Rating ("IDR") at BBB+ with stable outlook and changed PGE's senior unsecured rating to BBB+, as a result of implementation of new methodology.

The change of senior unsecured rating to BBB+ from A- is connected with the implementation of new, more restrictive methodology of utilities assessment, introduced by Fitch Ratings, according to which the issuer of instruments may obtain rating by 1 notch higher that its IDR, when around or more than 50% of its cash flows come from regulated activities. As a result of the change in methodology, senior unsecured ratings of 8 European utilities were downgraded.

5.6. Creation of a mortgage on the assets of material value by PGE Górnictwo i Energetyka Konwencjonalna S.A.

On August 9, 2011 PGE Górnictwo i Energetyka Konwencjonalna S.A. (PGE GiEK S.A.) created a mortgage up to the amount of EUR 195,000,000, in favour of the Nordic Investment Bank ("NIB") with its registered office in Helsinki, on perpetual usufruct of the property and on the ownership right concerning the buildings and all of their parts (the "Mortgage"). The Mortgage was created in order to secure the repayment of liabilities resulting from the loan granted by NIB to PGE GiEK S.A. The Mortgage was created on the property, on which the new 858 MW unit is being built. The book value of the assets, on which the Mortgage was created, amounts to approximately PLN 4.4 billion, what constitutes more than 10% of the Company's equity and thereby meets the criteria of the assets of material value.

At the same time, the creation of the Mortgage will result in waiver of the existing collaterals of higher value created on the mentioned property. The changes with regard to the collaterals are intended to simplify the collaterals structure and to adjust them to the current indebtedness level toward NIB.

5.7. Establishment of PGE Polska Grupa Energetyczna S.A. bond issue program

On August 29, 2011 the Company concluded an agreement for indefinite period with Bank Polska Kasa Opieki S.A. (acting as Agent, Paying Agent and Depository) and ING Bank Śląski S.A. (acting as Sub-Agent, Paying Sub-Agent and Sub-Depository). The bond issue program (the "Programme") was established on the ground of the above agreement.

The maximum indebtedness amount from the bonds issued (representing a maximum aggregate nominal value of bonds issued and outstanding) under the Programme cannot exceed PLN 5 billion.

Under the Programme, the company is entitled to issue bearer bonds ("Bonds") in dematerialized form in accordance with the Act on Bonds dated June 29, 1995 (Journal of Laws of 1995 No. 83, item 420 as amended) (the "Act on Bonds") with projected maturity – depending on the type of Bonds – for zero-coupon Bonds not longer than 1 year, and for coupon Bonds not shorter than 1 year and not longer than 10 years, according to the terms of issue of the given Bonds series. The Bonds will be issued pursuant to Article 9, section 3 of the Act on Bonds and the issues will be non-public. The Bonds may be dematerialized at the National Depository for Securities and quoted on the Alternative Trading System ("ASO") organized by the Warsaw Stock Exchange or Bondspot S.A. within the Catalyst.

Bonds under the Programme will be denominated in Polish zlotys (PLN) and the nominal value of one bond will amount to PLN 10,000 or multiple of that amount. The price terms of the Bonds – discount for zero-coupon bonds and interest rate/coupon for the coupon bonds – will be determined during the Bonds offering. The bondholders are only entitled to the benefits of monetary nature.

Bonds issued under the Programme will be treated as unsubordinated and unsecured liability of the Company.

5.8. Activities related to nuclear energy

Project of construction of nuclear power plant

In order to accomplish the project, the pre-feasibility study of construction of Polish first 2 nuclear power plants was carried out. The goal of pre-feasibility study is preliminary assessment of main feasibility and risk factors of the project, particularly in the scope of market aspects, schedule and organizational aspects, environmental and localization aspects and business aspects.

In first quarter of 2011 two public tender proceedings were started in PGE EJ 1 Sp. z o.o.: for Owner's Engineer and for performer of site characterisation. In second quarter of 2011 the short lists were announced in both tender proceedings. With regard to the announced short lists, the appeal proceedings were conducted before the National Appeal Chamber. In both cases the appeals were dismissed.

Tender for provision of legal advisory services to support PGE EJ 1 Sp. z o.o. in negotiations and contracting of Owner's Engineer and performer of site characterisation was settled in April 2011.

The research regarding the determination of optimal site localizations for the nuclear power plants was also carried out in the first half of 2011 – the criteria for its assessment were defined and the analyses of approximately 90 sites were performed on that basis.

The representatives of nuclear companies also participated in legislative works, cooperating with the Ministry of Treasury and Ministry of Economy, and then presenting its PGE's attitude during the works at Parliament. As a result of legislative works, the acts, comprising so called nuclear package, were passed by the Parliament, creating the legal provisions for the construction of nuclear power plants in Poland.

Additionally, the following works are continued: (i) preparations to tender for selection of technology, (ii) cooperation with universities and research institutes, (iii) preparation of procedures and documents connected with the safety of the company, including in particular procedures regarding the safety of the information.

5.9. Non-core asset management concept within the PGE Capital Group

In the first half of 2011, the PGE Capital Group continued its activities under "Non-core asset management concept within the PGE Capital Group". The aim of the programme is to transparently separate core activity from other activities as well as disposal and reorganisation of the assets.

In the first half of 2011, under the programme, shares/stocks of 4 companies were sold, liquidation of 1 company and bankruptcy proceedings in 2 companies were completed and 3 holiday resorts were sold. Sale of shares in one of the listed companies (Bank Ochrony Środowiska S.A.) had been continued.

In 2011 the sales of next shares/stocks of non-core companies, qualified to particular portfolios assigned for sale, will be finalised. The next stages of reorganization in the hotel-security-services, transport and medical areas will be implemented. The liquidation and bankruptcy proceedings of the non-core companies will also be finalized.

5.10. Consolidation Programme

In 2009-2010 Consolidation Programme was carried out in PGE Capital Group. As a result of the execution of the Consolidation Programme in 2010, the following formal and legal mergers took place in the given segments: (i) mining and conventional generation; (ii) renewables; (iii) distribution of the electric energy; (iv) retail sale of electric energy; as well as the merger of PGE Górnictwo i Energetyka S.A., PGE Energia S.A. and PGE Electra S.A. with PGE Polska Grupa Energetyczna S.A.

Merger of PGE Elektrownia Opole S.A. with PGE Górnictwo i Energetyka Konwencjonalna S.A. and Elektrownia Wiatrowa Kamieńsk Sp. z o.o. with PGE Energia Odnawialna S.A. are currently on-going (for detailed description of the legal issues see Note 15.3 to the consolidated financial statements).

5.11. Information regarding the change in Management Board of PGE Polska Grupa Energetyczna S.A. in the first half of 2011

From January 1, 2011 to June 30, 2011 the Management Board of the Company consisted of:

Name and surname of the Member of the Management Board	Position
Tomasz Zadroga	President of the Management Board
Marek Szostek	Vice-President of the Management Board responsible for Trading from June 29, 2011 till July 1, 2011 Vice-President of the Management Board responsible for Development from October 1, 2010 till June 28, 2011
Piotr Szymanek	Vice-President of the Management Board responsible for Corporate Affairs, from April 28, 2009 till July 1, 2011
Marek Trawiński *(member of the Management Board till March 16, 2011)*	Vice-President of the Management Board responsible for Operations since April 28, 2009 until March 16, 2011
Wojciech Topolnicki *(member of the Management Board till January 5, 2011)*	Vice-President of the Management Board responsible for Finance from October 1, 2010 till January 5, 2011
Paweł Skowroński	Vice-President of the Management Board responsible for Operations from March 17, 2011 till July 1, 2011
Wojciech Ostrowski	Vice-President of the Management Board responsible for Finance from March 17, 2011 till July 1, 2011

The Management Board of the (new) eighth term, as from 2 July, 2011, consists of the following Members:

Name and surname of the Member of the Management Board	Position
Tomasz Zadroga	President of the Management Board
Wojciech Ostrowski	Vice-President of the Management Board responsible for Finance
Paweł Skowroński	Vice-President of the Management Board responsible for Operations
Marek Szostek	Vice-President of the Management Board responsible for Trading
Piotr Szymanek	Vice-President of the Management Board responsible for Corporate Affairs

6. Factors, which in Company's opinion, will affect the results within at least the next quarter.

In the opinion of the Company Management Board, the following factors will influence the Company and the Group's performance within at least next quarter of 2011:

- demand for electricity and heat;
- electricity prices on wholesale market;
- prices of property rights;
- availability and prices of fuels used in generation of electricity and heat, in particular prices of hard coal, fuel gas and oil;

- availability and costs of CO_2 emission rights;
- availability of cross-border transmission capacities;
- changes in Group macroeconomic factors, including in particular interest rates and exchange rates, values of which affects evaluation of assets and liabilities shown by the Group;
- amendments to the Energy Law of April 10, 1997 and to other laws in scope affecting results of PGE Capital Group;
- the tariff process for 2012, including in particular costs recognised by the President of the Energy Regulatory Office as reasonable and the amount of reasonable return on equity, as well as tariff approval date;
- decisions of the ERO President related to realisation of LTC Act;
- court's ruling on the dispute between the President of the Energy Regulatory Office and generators from the PGE Group entitled to receive compensations under LTC Act with regard to the annual adjustments of the stranded costs for 2008-2010 and annual adjustments of the stranded costs and annual adjustments of costs generated in gas-fuelled units for 2009-2010;
- decision of National Administrator of the Emission Rights Trading System („KASHUE") on allocation from the reserve of free allocations for CO_2 emission for PGE Górnictwo i Energetyka Konwencjonalna S.A. Branch Elektrownia Bełchatów;
- consent of the Polish Office of Competition and Consumer for completion of the sale of shares in Polkomtel S.A. to Spartan Capital Holdings Sp. z o.o.;
- verdict of the Court of Competition and Consumer Protection in case of PGE's appeal against the decision on the President of the Office of the Competition and Consumer Protection with regard to the purchase of shares of ENERGA S.A.;
- possible different decision in law, tax and other contingent liabilities disputes, from which most relevant were presented in Note 15 to the consolidated financial statements.

7. Shareholders holding directly or indirectly by subsidiaries at least 5% of the total votes at Company's General Meeting.

As at the date of this consolidated half-year report, according to the information held by the Company, the only shareholder holding at least 5% of the total number of votes on the General Meeting of PGE Polska Grupa Energetyczna S.A. was the State Treasury, which held 1,295,637,952 shares of the Company, what constitutes 69.29% of the share capital and entitles to exercise the same amount of the votes at the General Meeting of the Company.

Table: Shareholders holding directly or indirectly by subsidiaries at least 5% of the total votes at the General Meeting of PGE Polska Grupa Energetyczna S.A.

Shareholder	Number of shares	Number of votes	% in total votes on General Meeting
State Treasury	1,295,637,952	1,295,637,952	69.29%
Others	574,145,775	574,145,775	30.71%
Total	**1,869,783,727**	**1,869,783,727**	**100.00%**

As of the publication date of this consolidated half-year report, PGE S.A. has held 22,898 own shares with a nominal value of PLN 10 each representing 22,898 of the total number of votes in the Company.

8. Number of shares or rights to shares of the Company held by Company's managers and supervisors, as of the date of submission of the half-year report.

According to the best knowledge of the Management Board of PGE S.A., as of the date of submission of this half-year report and as of the date of publishing of consolidated report for the first quarter of 2011, Company's managers and supervisors had following number of shares:

Shareholder	Number of shares as of the date of publishing of report for Q1 2011 (May 16, 2011) (pieces)	Change in number of owned shares (pieces)	Number of shares as of submission date of this half-year report (pieces)
The Management Board	**0**	**no change**	**0**
The Supervisory Board	**1,123**	**-500**	**623**
Marcin Zieliński	500	-500	0
Grzegorz Krystek	350	no change	350
Katarzyna Prus	273	no change	273

Management Board members and other Supervisory Board members did not own PGE shares.

9. Information on issue, redemption and repayment of debt securities and other securities.

Information on issue, redemption and repayment of debt securities and other securities were described in Note 16 to the consolidated financial statements and part B p. 1.2. of the foregoing report.

10. Information on granting by the Company or its subsidiary of loan securities or guarantees – jointly to a single entity or its subsidiary, if the total value of the existing securities or guarantees is equivalent to at least 10% of Company's equity.

Within the Group, in the period from January 1, 2011 to June 30, 2011 PGE S.A. and its subsidiaries did not grant any loan securities or guarantees to another entity or its subsidiary, where the value of securities and guarantees constituted at least 10% of the Company's equity.

11. Transactions with related entities.

Information about transactions with related entities is presented in Note 18 to the consolidated financial statements.

12. Information concerning proceedings in front of court, body appropriate for arbitration proceedings or in front of public administration authorities.

As at June 30, 2011 PGE S.A. and its subsidiaries were not a party in proceedings concerning liabilities or claims, in which the total value of a dispute constitutes at least 10% of Company equity except for applying by generators from PGE Group with application of statement of the overpaid excise tax and tax return with provisions for years 2006-2008 and first two months of 2009. The total overpaid tax to be returned to the PGE Group may amount to approximately PLN 3.4 billion, excluding interest (the generators are entitled to interest on the overpaid tax accrued from the date of payment of the overstated tax). This proceeding was described in Note 19.1 to the consolidated financial statements.

Significant proceedings pending in front of the court, competent arbitration authority or public administration authority were described in Note 15 to the consolidated financial statements.

13. Statements of the Management Board

13.1. Statement on the reliable preparation of the financial statements

To the best knowledge of the Management Board of PGE Polska Grupa Energetyczna S.A., half-year consolidated and stand-alone financial statements and comparable data were prepared in accordance with the governing accounting principles, present a fair, true and reliable view of the material and financial situation of PGE and PGE Capital Group and its financial result.

The report of the Management Board on the activities of PGE Capital Group presents a true view of the development, achievements and situation of the Capital Group, and provides a description of the basic risks and threats.

13.2. Statement on the entity authorised to audit the financial statements

The Management Board of PGE Polska Grupa Energetyczna S.A. declares that the entity authorised to audit the financial statements, that reviews the interim consolidated financial statements, has been appointed in accordance with provisions of the law. The entity and the statutory auditors fulfilled all the requirements for issuing an unbiased and independent opinion on the audit, in accordance with the governing provisions and professional standards.

Warsaw, August 2011

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

Tomasz Zadroga
President of the Management Board

Wojciech Ostrowski
Vice-President of the Management Board

Paweł Skowroński
Vice-President of the Management Board

Marek Szostek
Vice-President of the Management Board

Piotr Szymanek
Vice-President of the Management Board