
PGE POLSKA GRUPA ENERGETYCZNA
with its registered office in Warsaw
MANAGEMENT BOARD'S REPORT

JUSTIFYING THE MERGER OF
PGE POLSKA GRUPA ENERGETYCZNA S.A. with its registered office in Warsaw
WITH
PGE GÓRNICtwo I ENERGETYKA S.A. with its registered office in Łódź
PGE ENERGIA S.A. with its registered office in Lublin

(the „Report”)

dated May 11, 2010

In relation to the merger plan of PGE Polska Grupa Energetyczna S.A. (acquiring company) and PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. (acquired companies) (acquiring company and acquired companies hereinafter jointly referred to as the “**Companies**”) signed on January 26, 2010 (the “**Merger Plan**”), defining, as per art. 499 § 1 of the Commercial Companies Code (the “**CCC**”), among others the method of the merger of the Companies and the exchange parity of the shares, accordingly to art. 501 of the CCC, the Management Board of PGE Polska Grupa Energetyczna S.A. prepared this report on justification of the merger of the Companies.

1 Form, name and registered office of the merging Companies

1.1 Acquiring Company

PGE Polska Grupa Energetyczna S.A. with its registered office in Warsaw, at ul. Mysia 2, entered to the Register of Entrepreneurs held by the District Court for the Capital City of Warsaw, the 12th Commercial Division of the National Court Register under KRS no. 0000059307, tax identification (NIP) no. 526-025-05-41, statistical (REGON) no. 006227638. The share capital of the company amounts to PLN 17,300,900,000 and is divided into 1,730,090,000 shares with a nominal value of PLN 10 each (the “**Acquiring Company**”).

1.2 Acquired Companies

PGE Górnictwo i Energetyka S.A. with its registered office in Łódź, at ul. Piłsudskiego 12, entered to the Register of Entrepreneurs by the District Court in Łódź, the 20th Commercial Division of the National Court Register, under KRS no. 0000202169, tax identification (NIP) no. 725-187-45-79, statistical (REGON) no. 473237030. The share capital of the company amounts to PLN 3,827,809,700 and is divided into 382,780,970 shares with a nominal value of PLN 10 each

PGE Energia S.A. with its registered office in Lublin, at ul. Garbarska 21a, entered to the Register of Entrepreneurs by the District Court in Lublin, the 11th Commercial Division of the National Court Register, under KRS no. 0000267235, tax identification (NIP) no. 701-004-62-08, statistical (REGON) no. 140751686. The share capital of the company amounts to PLN 7,519,861,158 and is divided into 7,519,861,158 shares with a nominal value of PLN 1 each,

Jointly referred to as the „**Acquired Companies**”, and individually referred to as the „**Acquired Company**”.

2 Merger method

The Companies shall merge in the manner prescribed in art. 492 § 1 p. 1 of the CCC, i.e. by way of transferring the entire assets of the Acquired Companies onto the Acquiring Company, in exchange for the shares of the Acquiring Company, which shall be issued to the shareholders of the Acquired Companies subject to provisions of art. 514 of the CCC, namely excluding the Acquiring Company as a shareholder of the Acquired Companies, that will not acquire its treasury stock in exchange for the shares of the Acquired Companies (the “**Merger**”).

As a result of the Merger, the Acquired Companies shall be dissolved without going into liquidation.

In relation to the Merger, the share capital of the Acquiring Company shall be increased by the amount arising from the adopted exchange parity of shares in line with the shareholding structure of the Acquired Companies as at the date of adopting the resolution on Merger, while the maximum amount of increase, even if there is no need to round the number of shares to full numbers, shall total PLN 1,396,981,460.00 (in words: one billion three hundred and ninety six million nine hundred and eighty one thousand four hundred and sixty Zloty) and it shall take place by way of issue of maximum 139,698,146 shares (in words: one hundred and thirty nine million six hundred and ninety eight thousand one hundred and forty six) with the nominal value of PLN 10 each (the “**Merger Shares**”), which shall be issued to the shareholders of the Acquired Companies, subject to regulations of art. 514 of the CCC, i.e.

excluding the Acquiring Company as a shareholder of the Acquired Companies, that will not acquire its treasury stock in exchange for the shares of the Acquired Companies.

In accordance with art. 11 section 2 of the Act dated 7 September 2007 on principles of acquisition of shares from the State Treasury in the process of consolidation of companies from the electric power sector (Journal of Laws of 2007 No. 191, item 1367, as subsequently amended) (the “**Conversion Act**”), the share capital of the Acquiring Company is increased while accounting for the rights of successors of those entitled to convert the shares of consolidated companies to the shares of the consolidating company, subject to terms and conditions stipulated in the Conversion Act.

3 Legal basis of the Merger

The legal basis of the Merger are the regulations of the CCC and the clauses of the Companies’ Statutes, according to which the body authorized to take a decision on the merger of the Companies is the general meeting of each of the Companies. The adoption of the resolution on the merger by the general meetings of the Companies is the legal provision for the merger of the joint stock companies.

Resolution of the general meeting of the Acquiring Company on the merger with the Acquired Companies, and respectively resolutions of the general meetings of the Acquired Companies will be adopted on the ground of art. 506 § 1 of the CCC and § 37 sec. 1 p. 6 of the Statutes of the Acquiring Company, § 28 sec. 3 p. 6 of the Statutes of PGE Górnictwo i Energetyka S.A., § 28 sec. 3 p. 6 of the Statutes of PGE Energia S.A. respectively, and will constitute that the merger of the Companies will be made through the acquisition of the Acquired Companies by the Acquiring Company by way of transferring the entire assets of the Acquired Companies onto the Acquiring Company, in exchange for the Merger Shares, which will be granted by the Acquiring Company to the shareholders of the Acquired Companies.

As far as the obtaining of the administrative permits and consents proves necessary, the obtaining by the merging Companies and its shareholders of all the administrative permits and consents required by law will be a provision for the Merger.

4 Economic justification of the Merger

The Merger of PGE Polska Grupa Energetyczna S.A., PGE Energia S.A. and PGE Górnictwo i Energetyka S.A. is being implemented under the Consolidation Program of PGE Capital Group approved by the Management Board of PGE Polska Grupa Energetyczna S.A. in resolution no. 215/33/2009 dated May 29, 2009 and updated by resolution no. 289/43/2009 dated August 4, 2009 and by the resolution no. 322/45/2009 dated August 18, 2009.

The main goal of the Consolidation Program is to achieve a strong market and financial position of the PGE Group, what will assure among others the further development of the Group. Assumptions of the Consolidation Program include reorganization of the complex capital structure, implementation of the optimal management structure along with the centralization of functions conducted in particular business segments and achieving synergy effects in the PGE Capital Group.

The Merger of PGE Polska Grupa Energetyczna S.A., PGE Energia S.A. and PGE Górnictwo i Energetyka S.A. is meant to create one corporate center, which will be responsible for the management of the whole Capital Group. This will improve the decision making process and will make it more transparent and coherent.

The Merger of PGE Polska Grupa Energetyczna S.A., PGE Energia S.A. and PGE Górnictwo i Energetyka S.A. is also carried out as an implementation of art. 11 of the Conversion Act. This regulation constitutes that “shareholders of PGE Energia S.A. and PGE Górnictwo i Energetyka S.A., who purchased the shares of these companies on rules described in this act, become the shareholders of PGE Polska Grupa Energetyczna S.A. as a result of merger of PGE Energia S.A. and PGE Górnictwo i Energetyka S.A. with PGE Polska Grupa Energetyczna S.A., in the manner prescribed in art. 492 § 1 p. 1 of the CCC.” The merger will

allow the issuance of shares of PGE Polska Grupa Energetyczna S.A. to the shareholders, who purchased shares of PGE Energia S.A. and PGE Górnictwo i Energetyka S.A. as a result of process of conversion of shares.

5 Exchange parity of the shares

5.1 Determination of the projected Exchange parity of the shares

Merger Shares shall be issued to:

- (i) the shareholders of the Acquired Companies, subject to provisions of art. 514 of the CCC, i.e. excluding the Acquiring Company as a shareholder of the Acquired Companies, that will not acquire its treasury stock in exchange for the shares of the Acquired Companies;
- (ii) the successors of those authorised to convert the shares of consolidated companies to the shares of the consolidating company, as specified in art. 11 section 2 of the Conversion Act.

The Merger Shares shall be issued to entities referred to in items (i) and (ii) above, while applying the following exchange parity of the shares (the “**Exchange Parity**”):

PGE Górnictwo i Energetyka S.A. 1* : 1.27560301

PGE Energia S.A. 1* : 0.05891657

The basis for the setting of the Exchange Parity were the appraisals prepared by PricewaterhouseCoopers Sp. z o.o. (al. Armii Ludowej 14, 00-638 Warszawa) (the „**Appraisals**”). The Appraisals of the merging Companies were accomplished with the following methods:

- (i) For the Acquiring Company – income method, including the value of financial assets determined using one of the following: income method, market multiplier method, transaction multiplier method, adjusted net asset method, stock exchange capitalization method, book value method.
- (ii) For the Acquired Companies – adjusted net asset method, including value of financial assets calculated using one of the following: income method, market multiplier method, transaction multiplier method, adjusted net asset method, stock exchange capitalization method, book value method.

After acquainting with the results of the Appraisals, the Management Boards of the merging Companies decided to accept the Exchange Parities as indicated above.

5.2 Opinion of the legal expert

Acting in accordance with the art. 500 § 1 in connection with art. 502 § 2 of the CCC, the Management Boards of the merging Companies jointly filed to the register court, adequate for the registered office of the Acquiring Company, for the appointment of the expert in order to audit the Merger Plan in scope of correctness and reliability. The expert appointed by the register court, accordingly to art. 502 and art. 503 of the CCC and providing for the standards related to the profession of the expert auditor, issued by the National Chamber of Statutory Auditors in Poland, performed the audit of the Merger Plan and prepared opinion in writing in

* “1” means one share of the Acquired Company. Due to the fact that parity is not an integer, it is not possible to specify *in abstracto* the number of shares of the Acquiring Company that is the integer (it is not possible to take up a fraction of the share). It will be possible to determine a specific number of shares of the Acquiring Company in relation to individual shareholders of the Acquired Company, in respect of the specific number of shares held by those shareholders, however, if as the result of multiplying the number of shares by the adopted parity, the number of shares of the Acquiring Company is not an integer, the remaining fraction due to the shareholders shall be settled by way of payments referred to in item 5 of the Merger Plan..

scope of its correctness and reliability and filed the opinion with the register court on March 15, 2010.

The expert auditor stated in his opinion that:

- the Merger plan of the Acquiring Company and the Acquired Companies, complies in both form and content with the effective provisions of the CCC and, in particular, contains all the information required under art. 499 § 1 of the CCC. Furthermore, the merger plan:
 - adequately defines the proportion of the exchange of shares of the Acquired Companies' shares into shares of the Acquiring Company,
 - rightly assumes the methods of appraisal of shares, described in the Merger Plan, for defining the proportion of exchange parity of shares,
- The appraisal of the shares of the merging Companies serving as the basis for defining the exchange parity specified in the merger plan did not raise difficulties whereas the applied method enabled a reliable presentation of the current market value of the Companies,
- Information presented in the statement on the accounting position of the Acquiring Company and of the Acquired Company comply with the information contained in the balance sheet and the profit and loss account of the Companies.

5.3 Principles of issuing the Merger Shares

5.3.1 The Merger Shares shall be issued to entities that are shareholders of the Acquired Companies as at the date of Merger registration (the "**Merger Date**").

5.3.2 The number of the Merger Shares to be received by each authorised shareholder of the Acquired Company shall be determined by multiplying the number of shares of the Acquired Company held by that shareholder as at the Merger Date by the Exchange Parity, and rounding the result (if it is not an integer) down to the nearest integer.

5.3.3 Each authorised shareholder of the Acquired Company, that as a result of rounding referred to in item (ii) above has not been received the fraction of the Merger Shares due to that shareholder in line with the Exchange Parity, that shareholder shall be entitled to a cash payment (the "**Payment**").

5.3.4 The amount of Payment due to a given authorised shareholder of the Acquired Company shall be calculated using the following formula:

$$D = A \times W,$$

where: D – the amount of Payment, A – fraction used to round down the result specified in item 5.3.2 above, W – price of one share of the Acquiring Company as per valuation prepared for the purposes of the Merger.

5.3.5 If the total amount of Payments for all the shareholders of the Acquired Companies exceeds 10% of the balance sheet value of the Merger Shares, determined according to the statement referred to in art. 499 § 2 item 4 of the CCC, the amount of Payments for individual shareholders shall be proportionally decreased.

5.3.6 The Management Board of the Acquiring Company shall define, in agreement with Management Boards of Acquired Companies, a detailed manner of issuing Merger Shares to the shareholders of the Acquired Companies.

6 Particular difficulties connected with the appraisal of shares of the merging Companies

No particular difficulties connected with the appraisal of the shares of the merging Companies were found.

7 Additional information

7.1 *Date from which the Merger Shares entitle their holders to participation in profit of the Acquiring Company*

The Merger Shares shall participate in dividend as from 1 January 2010, i.e. in dividend for the financial year ended 31 December 2010.

7.2 *Rights granted by the Acquiring Company to the shareholders of the Acquired Companies or other persons with privileged position in the Acquired Companies*

There are no special rights planned to be granted to the shareholders of the Acquired Companies or other persons with privileged position in the Acquired Companies.

7.3 *Special benefits for members of statutory bodies of the merging Companies and other participants of the Merger*

There are no special benefits planned to be offered in relation to the Merger to members of authorities of merging companies or other participants of the Merger.

7.4 *Shareholders structure after the Merger*

After the Merger:

- shareholders of PGE Górnictwo i Energetyka S.A. will become the holders of the shares constituting not more than 3.9% of the capital share of the Acquiring Company and entitling up to 3.9% of the votes on the general meeting,
- shareholders of PGE Energia S.A. will become the holders of the shares constituting not more than 3.6% of the capital share of the Acquiring Company and entitling up to 3.6% of the votes on the general meeting,
- current shareholders of the Acquiring Company will hold shares constituting at least 92.5% of the capital share of the Acquiring Company and entitling to at least 92.5% of the votes on the general meeting.

8 Summary and recommendation

The economic and financial rationale for the merging Companies, as well as for their shareholders, indicates the legitimacy of the Merger. The Merger is deliberate in strategic, operating and cost categories.

Taking the above into account, the Management Board of PGE Polska Grupa Energetyczna S.A. hereby recommends to the shareholders of PGE Polska Grupa Energetyczna S.A. the concept of the merger of the Companies, as well as adoption of the resolution on the merger of the Companies and on the changes in the Statutes of the Acquiring Company.

For the Management Board