



PGE Polska Grupa Energetyczna S.A. Capital Group

Consolidated financial statements prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2010.

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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Period ended 31 December 2010	Period ended 31 December 2009
CONSOLIDATED COMPREHENSIVE INCOME			
Continuing operations			
Total sales revenues	15	20.476.465	21.623.350
Costs of goods sold	15	(14.071.540)	(13.727.469)
Gross profit on sales		6.404.925	7.895.881
Other operating revenues	15	666.403	422.568
Distribution and selling expenses	15	(1.527.718)	(1.368.079)
General and administrative expenses	15	(950.702)	(914.109)
Other operating expenses	15	(407.575)	(691.532)
Financial revenues	15	422.115	372.265
Financial expenses	15	(558.217)	(580.617)
Share of profit of associate	25	227.019	242.157
Profit before tax		4.276.250	5.378.534
Corporate income tax expense	17	(673.400)	(1.041.311)
Net profit from continuing operations		3.602.850	4.337.223
Discontinued operations			
Profit for the period on discontinued operations	19	24.237	-
Net profit for the operating period		3.627.087	4.337.223
OTHER COMPREHENSIVE INCOME:			
Valuation of available-for-sale financial assets		80	(41.287)
Revaluation of assets of associates			41
Foreign exchange differences from translation of foreign entities		1.757	531
Other comprehensive income for the period, net		1.837	(40.715)
TOTAL COMPREHENSIVE INCOME		3.628.924	4.296.508
Net profit attributable to:			
- equity holders of the parent company		3.014.120	3.370.712
- non-controlling interest		612.967	966.511
Total comprehensive income attributable to:			
- equity holders of the parent company		3.015.957	3.340.169
- non controlling interest		612.967	956.339
Profit per share (in PLN)			
- basic earnings for the operating period	32	1,70	2,23
- basic earnings from the continuing operations	32	1,70	2,23

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Nota	As at 31 December 2010	As at 31 December 2009
ASSETS			
Non-current assets			
Property, plant and equipment	21	41.442.181	38.945.664
Investment property	22	24.959	25.431
Intangible assets	23	202.629	153.335
Loans and receivables	42	407.831	389.566
Available-for-sale financial assets	42	95.242	198.211
Shares in associates accounted for under the equity method	25	1.408.465	1.354.799
Other long-term assets	29	264.432	485.087
Deferred tax assets	17	286.621	412.353
Non-current assets related to discontinued operations	19	5.062	-
Total non-current assets		44.137.422	41.964.446
Current assets			
Inventories	27	1.090.549	1.271.165
Income tax receivables		29.976	49.827
Held-to-maturity short-term investments	42	-	-
Trade receivables	42	2.094.506	2.059.119
Other loans and financial assets	42	796.663	987.575
Available-for-sale short-term financial assets	42	130.924	5.984
Other current assets	29	445.809	391.147
Cash and cash equivalents	30	2.730.423	7.712.823
Current assets related to discontinued operations	19	10.095	-
Total current assets		7.328.945	12.477.640
Assets classified as held for sale	18	7.572	5.712
TOTAL ASSETS		51.473.939	54.447.798

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

LIABILITIES AND EQUITY	Note	As at 31 December 2010	As at 31 December 2009 <i>restated*</i>
Equity (attributable to equity holders of the parent)			
Share capital	31	18.697.837	17.300.900
Revaluation reserve		(1.081)	(1.161)
Treasury shares	31	(229)	-
Foreign exchange differences from translation of foreign entities		945	(812)
Reserve capital	31	6.727.589	5.449.549
Other capital reserves		49.779	-
Retained earnings	31	11.609.114	8.419.848
Non-controlling interest	31	598.819	7.681.428
Total equity		37.682.773	38.849.752
Long-term liabilities			
Interest-bearing loans and borrowings	42	1.804.429	4.056.270
Other long-term liabilities	42	14.403	15.941
Provisions	35	3.072.295	3.238.759
Deferred tax liabilities	17	1.194.763	1.358.546
Deferred income and government grants	37	1.112.553	1.092.806
Long-term liabilities related to discontinued operations	19	1.366	-
Total long-term liabilities		7.199.809	9.762.322
Short-term liabilities			
Trade liabilities	42	986.301	1.082.582
Financial liabilities at fair value through profit or loss	42	41.165	37.701
Interest-bearing loans and borrowings	42	914.956	969.929
Other short-term financial liabilities	42	1.259.478	566.571
Other short-term non-financial liabilities	36	1.396.213	1.197.829
Income tax liabilities		218.158	372.888
Deferred income	37	100.157	40.903
Short-term provisions	35	1.668.640	1.567.321
Short-term liabilities related to discontinued operations	19	6.289	-
Total short-term liabilities		6.591.357	5.835.724
Total liabilities		13.791.166	15.598.046
TOTAL LIABILITIES AND EQUITY		51.473.939	54.447.798

* For details on 2009 data restatement please refer to Note 13.34 of explanatory notes to the foregoing consolidated financial statements.

STATEMENT OF CHANGES IN CONSOLIDATED EQUITY

For the period ended 31 December 2010

	Share capital	Revaluation reserve	Treasury shares	Foreign exchange differences from translation	Reserve capital	Other capital reserves	Retained earnings	Total	Non-controlling interest	Total equity
As at 1 January 2010	17.300.900	(1.161)	-	(812)	5.449.549	-	8.419.848	31.168.324	7.681.428	38.849.752
Total comprehensive income for the period	-	80	-	1.757	-	-	3.014.120	3.015.957	612.967	3.628.924
Retained earnings distribution	-	-	-	-	136.441	49.779	(186.220)	-	-	-
Dividend	-	-	-	-	-	-	(1.335.330)	(1.335.330)	(673.996)	(2.009.326)
Purchase of new companies	-	-	-	-	-	-	-	-	7.648	7.648
Sale of subsidiaries	-	-	-	-	-	-	-	-	(13.786)	(13.786)
Changes in accounting policy	-	-	-	-	-	-	19.435	19.435	7.465	26.900
Purchase of treasury shares	-	-	(229)	-	(350)	-	-	(579)	-	(579)
Settlement of purchase of additional stock in subsidiaries:	-	-	-	-	-	-	531.526	531.526	(3.646.201)	(3.114.675)
Value of the purchased non-controlling interest	-	-	-	-	-	-	3.646.201	3.646.201	(3.646.201)	-
The acquisition cost of shares and stocks in subsidiaries	-	-	-	-	-	-	(3.114.675)	(3.114.675)	-	(3.114.675)
Settlement of the merger of parent company with subsidiaries:	1.396.937	-	-	-	1.141.949	-	1.145.735	3.684.621	(3.376.706)	307.915
Issue of shares as a result of the merger	1.396.937	-	-	-	1.141.949	-	(2.538.886)	-	-	-
Transfer of non-controlling interest as a result of the merger	-	-	-	-	-	-	3.376.706	3.376.706	(3.376.706)	-
Dividends taken over dividends (attributable to non-controlling interest before the merger)	-	-	-	-	-	-	307.915	307.915	-	307.915
As at 31 December 2010	18.697.837	(1.081)	(229)	945	6.727.589	49.779	11.609.114	37.083.954	598.819	37.682.773

For the period ended 31 December 2009

	Share capital	Revaluation reserve	Foreign exchange differences from translation	Reserve capital	Other capital reserves	Retained earnings	Total	Non-controlling interest	Total equity
As at 1 January 2009	14.705.765	30.154	(1.343)	2.100.156	414.017	5.560.908	22.809.657	7.365.921	30.175.578
Total comprehensive income for the period	-	(31.115)	531	-	-	3.370.753	3.340.169	956.339	4.296.508
Issue of shares	2.595.135	-	-	3.373.676	-	-	5.968.811	-	5.968.811
Issue of shares' expenses	-	-	-	(68.560)	-	-	(68.560)	-	(68.560)
Retained earnings distribution	-	-	-	44.277	-	(44.277)	-	-	-
Purchase of non-controlling shares	-	-	-	-	-	521.473	521.473	(521.473)	-
Settlement of purchased stocks and shares in subsidiaries	-	-	-	-	-	(264.838)	(264.838)	-	(264.838)
Dividend (including distribution from profit for the State Treasury)	-	-	-	-	(414.017)	(725.971)	(1.139.988)	(119.359)	(1.259.347)
Other	-	(200)	-	-	-	1.800	1.600	-	1.600
As at 31 December 2009	17.300.900	(1.161)	(812)	5.449.549	-	8.419.848	31.168.324	7.681.428	38.849.752

CONSOLIDATED STATEMENT OF CASH FLOWS

	Period ended 31 December 2010	Period ended 31 December 2009 <i>restated*</i>
Cash flows – operating activities		
Gross profit related to discontinued operations	29.671	-
Gross profit related to continuing operations	4.276.250	5.378.534
Adjustments for:		
Share of profit from associates accounted for under the equity method	(227.019)	(242.157)
Depreciation and amortization	2.655.210	2.638.676
Interest and dividend, net	253.505	248.924
Difference between fair value and carrying amount of dividends in kind paid	-	-
Profit / (loss) on investment activities	(84.256)	(71.623)
Change in receivables	170.978	(495.567)
Change in inventories	180.616	(141.809)
Change in liabilities (excluding loans and bank credits)	141.759	179.478
Change in prepayments and accruals	28.552	(581.744)
Change in provisions	(57.425)	923.502
Income tax paid	(852.003)	(491.352)
Other	95.122	(45.974)
Net cash from operating activities	6.610.960	7.298.888
Cash flows – investment activities		
Disposal of property, plant and equipment and intangible assets	56.729	32.114
Purchase of property, plant and equipment and intangible assets	(4.522.439)	(4.022.231)
Purchase/disposal of investment property	-	173
Disposal of financial assets	180.032	545.528
Purchase of financial assets	(3.307.940)	(295.399)
Purchase of stocks and shares in subsidiaries	(10.397)	(264.837)
Dividends	134.566	385.187
Interest received	991	12.964
Loans repaid	4.900	14.024
Loans granted	(715)	(61.176)
Other	(4.001)	25.063
Net cash from investment activities	(7.468.274)	(3.628.590)

	Period ended 31 December 2010	Period ended 31 December 2009
Cash flows – financial activities		
Proceeds from the issue of shares	(579)	5.917.532
Proceeds from bank credits and issue of bonds	458.135	8.907.041
Repayment of loans, bonds and finance lease	(2.829.388)	(11.361.744)
Dividends paid (including deductions from profit for the State Treasury)	(1.580.104)	(1.227.352)
Interest paid	(161.644)	(350.878)
Other	1.819	13.720
Net cash from financial activities	(4.111.761)	1.898.319
Net change of cash and cash equivalents	<u>(4.969.075)</u>	<u>5.568.617</u>
Effect of foreign exchange rate changes	4.073	-
Cash and cash equivalents, beginning of the period	7.705.934	2.137.317
Cash and cash equivalents, end of the period, including	2.736.859	7.705.934
including restricted cash and cash equivalents	105.910	115.435

* For details on 2009 data restatement please refer to Note 13.34 of explanatory notes to the foregoing consolidated financial statements.

APPLIED ACCOUNTING PRINCIPLES (POLICIES) AND EXPLANATORY NOTES

1. General information

PGE Polska Grupa Energetyczna S.A. Capital Group ("Group", "Capital Group", "PGE Group") comprises the parent company PGE Polska Grupa Energetyczna S.A. and subsidiaries (please refer to Note 2).

Polska Grupa Energetyczna S.A. ("parent company", "the Company", "PGE S.A.") was founded on the basis of the Notary Deed of 2 August 1990 and registered in the District Court in Warsaw, XVI Commercial Department on 28 September 1990. The Company was registered in the National Court Register of the District Court for the capital city of Warsaw, XII Commercial Department, under no. KRS 0000059307.

As of the date of preparation of the consolidated financial statements, the parent company is seated in Warsaw, 2 Mysia Street.

As of the day of preparation of the foregoing consolidated financial statements, the Company is registered in the National Court Register of the District Court for the capital city of Warsaw, XII Commercial Department of the National Court Register, under no. KRS 0000059307.

Core operations of the Group companies are as follows:

- production of electricity,
- distribution of electricity,
- wholesale and retail sale of electricity,
- production and distribution of heat,
- rendering of other services related to the above mentioned activities.

Business activities are conducted under appropriate concessions granted to particular Group entities.

The State Treasury is the major shareholder of the parent company.

The consolidated financial statements of the Group comprise financial data for the period from 1 January 2010 to 31 December 2010.

2. Entities included in the Group

During the reporting period PGE Polska Grupa Energetyczna S.A. Capital Group consisted of the enumerated below companies, consolidated directly and indirectly:

Entity	Share of Capital Group entities as at 31 December 2010	Parent company as at 31 December 2010	Share of Capital Group entities as at 31 December 2009	Parent company as at 31 December 2009
Segment: wholesale				
1. PGE Polska Grupa Energetyczna S.A. Warszawa		The Parent Company of the Group		
PGE Electra S.A. Warszawa	-	a)	100,00%	PGE Polska Grupa Energetyczna S.A.
2. ELBIS Sp. z o.o. Rogowiec	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE Elektrownia Bełchatów S.A.
3. ELECTRA Deutschland GmbH Germany	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Electra S.A.
Segment: mining and conventional energy				
PGE Górnictwo i Energetyka S.A. Łódź	-	a)	85,00%	PGE Polska Grupa Energetyczna S.A.
4. PGE Górnictwo i Energetyka Konwencjonalna S.A. (formerly: PGE Elektrownia Bełchatów S.A.) Bełchatów	91,03%	PGE Polska Grupa Energetyczna S.A.	69,00%	PGE Górnictwo i Energetyka S.A.
	7,88%	PGE Obrót S.A.		
	0,02%	PGE Energia Odnawialna S.A.	19,10%	PGE Polska Grupa Energetyczna S.A.
5. PGE Elektrownia Opole S.A. Brzezie	85,00%	PGE Polska Grupa Energetyczna S.A.	69,00%	PGE Górnictwo i Energetyka S.A.
			16,00%	PGE Polska Grupa Energetyczna S.A.
PGE Elektrownia Turów S.A. Bogatynia	-	b)	69,00%	PGE Górnictwo i Energetyka S.A.
			16,00%	PGE Polska Grupa Energetyczna S.A.
PGE Kopalnia Węgla Brunatnego Bełchatów S.A. Rogowiec	-	b)	69,00%	PGE Górnictwo i Energetyka S.A.
			16,00%	PGE Polska Grupa Energetyczna S.A.
PGE Kopalnia Węgla Brunatnego Turów S.A. Bogatynia	-	b)	69,00%	PGE Górnictwo i Energetyka S.A.
			16,00%	PGE Polska Grupa Energetyczna S.A.
PGE Zespół Elektrowni Dolna Odra S.A. Nowe Czarnowo	-	b)	85,00%	PGE Energia S.A.
PGE Zespół Elektrociepłowni Bydgoszcz S.A. Bydgoszcz	-	b)	98,50%	PGE Polska Grupa Energetyczna S.A.
			0,53%	PGE Energia Odnawialna S.A.
PGE Elektrociepłownia Kielce S.A. Kielce	-	b)	100,00%	PGE Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.
PGE Elektrociepłownia Lublin - Wrotków Sp. z o.o. Lublin	-	b)	100,00%	PGE Lubelskie Zakłady Energetyczne S.A.

Entity	Share of Capital Group entities as at 31 December 2010	Parent company as at 31 December 2010	Share of Capital Group entities as at 31 December 2009	Parent company as at 31 December 2009
PGE Elektrociepłownia Rzeszów S.A. <i>Rzeszów</i>	-	b)	100,00%	PGE Obrót S.A.
PGE Elektrociepłownia Gorzów S.A. <i>Gorzów Wielkopolski</i>	-	b)	90,09%	PGE Polska Grupa Energetyczna S.A.
Energetyka Boruta Sp. z o.o. <i>Zgierz</i>	-	b)	96,91%	ELBIS Sp. z o.o.
Przedsiębiorstwo Energetyki Ciepłej Gorzów Sp. z o.o. <i>Gorzów Wielkopolski</i>	-	b)	100,00%	PGE Elektrociepłownia Gorzów S.A.
Przedsiębiorstwo Energetyki Ciepłej Sp. z o.o. <i>Gryfino</i>	-	b)	80,00%	PGE Zespół Elektrowni Dolna Odra S.A.
Segment: renewable energy				
6. PGE Energia Odnawialna S.A. <i>Warszawa</i>	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
PGE Zespół Elektrowni Wodnych Dychów S.A. <i>Dychów</i>	-	b)	100,00%	PGE Energia Odnawialna S.A.
Zespół Elektrowni Wodnych Porąbka-Żar S.A. <i>Międzybrodzie Bialskie</i>	-	b)	100,00%	PGE Energia Odnawialna S.A.
EGO-Odra S.A. <i>Warszawa</i>	-	b)	50,14%	PGE Energia Odnawialna S.A.
			49,86%	ZEW Porąbka-Żar S.A.
Zespół Elektrowni Wodnych Solina-Myczkowce S.A. <i>Solina</i>	-	b)	100,00%	PGE Energia Odnawialna S.A.
Elektrownia Wodna Żarnowiec S.A. <i>Czymanowo</i>	-	b)	100,00 %	PGE Energia Odnawialna S.A.
7. Elektrownia Wiatrowa Kamieńsk Sp. z o.o. <i>Kamieńsk</i>	100,00%	PGE Energia Odnawialna S.A.	50,00%	PGE Energia Odnawialna S.A.
			50,00%	ELBIS Sp. z o.o.
Segment: distribution				
8. PGE Dystrybucja S.A. <i>Lublin</i>	89,91%	PGE Obrót S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
	10,05%	PGE Polska Grupa Energetyczna S.A.		
PGE Dystrybucja Zamość Sp. z o.o. <i>Zamość</i>	-	b)	100,00%	PGE Zamojska Korporacja Energetyczna S.A.
PGE Dystrybucja Rzeszów Sp. z o.o. <i>Rzeszów</i>	-	b)	100,00%	PGE Obrót S.A. (previously under business name <i>PGE Rzeszowski Zakład Energetyczny S.A.</i>)
PGE Dystrybucja LUBZEL Sp. z o.o. <i>Lublin</i>	-	b)	100,00%	PGE Lubelskie Zakłady Energetyczne S.A.
PGE Zakłady Energetyczne Okręgu Radomsko-Kieleckiego Dystrybucja Sp. z o.o. <i>Skarżysko-Kamienna</i>	-	b)	100,00%	PGE Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.
PGE Dystrybucja Łódź Sp. z o.o. <i>Łódź</i>	-	b)	100,00%	PGE Łódzki Zakład Energetyczny S.A.

Entity	Share of Capital Group entities as at 31 December 2010	Parent company as at 31 December 2010	Share of Capital Group entities as at 31 December 2009	Parent company as at 31 December 2009
PGE Dystrybucja Białystok Sp. z o.o. <i>Białystok</i>	-	b)	100,00%	PGE Zakład Energetyczny Białystok S.A.
PGE Dystrybucja Łódź-Teren S.A. <i>Łódź</i>	-	b)	85,00%	PGE Energia S.A.
PGE Dystrybucja Warszawa-Teren Sp. z o.o.	-	b)	100,00%	PGE Zakład Energetyczny Warszawa-Teren S.A.
PGE Energia S.A. <i>Lublin</i>	-	a)	85,00%	PGE Polska Grupa Energetyczna S.A.
Segment: retail sale				
9. PGE Obrót S.A. (previously under business name PGE Rzeszowski Zakład Energetyczny S.A.) <i>Rzeszów</i>	99,31%	PGE Polska Grupa Energetyczna S.A.	85,00%	PGE Energia S.A.
PGE Zamojska Korporacja Energetyczna S.A. <i>Zamość</i>	-	b)	85,00%	PGE Energia S.A.
PGE Lubelskie Zakłady Energetyczne S.A. <i>Lublin</i>	-	b)	85,00%	PGE Energia S.A.
PGE Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A. <i>Skarżysko-Kamienna</i>	-	b)	85,00%	PGE Energia S.A.
PGE Łódzki Zakład Energetyczny S.A. <i>Łódź</i>	-	b)	85,00%	PGE Energia S.A.
PGE Zakład Energetyczny Białystok S.A.	-	b)	85,00%	PGE Energia S.A.
PGE ZEŁT Obrót Sp. z o.o. <i>Łódź</i>	-	b)	100,00%	PGE Polska Grupa Energetyczna S.A.
PGE Zakład Energetyczny Warszawa-Teren S.A. <i>Warszawa</i>	-	b)	85,00%	PGE Energia S.A.
Segment: other				
10. EXATEL S.A. <i>Warszawa</i>	94,938% 0,537% 0,137% 0,001%	PGE Polska Grupa Energetyczna S.A. PGE Inwest Sp. z o.o. PGE Obrót S.A. PGE Dystrybucja S.A.	94,94%	PGE Polska Grupa Energetyczna S.A.
11. MEGAZEC Sp. z o.o. <i>Bydgoszcz</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE Zespół Elektrociepłowni Bydgoszcz S.A.
12. ELBEST Sp. z o.o. <i>Rogowiec</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE Elektrownia Bełchatów S.A.
13. Energoserwis - Kleszczów Sp. z o.o. <i>Kleszczów</i>	51,00%	ELBIS Sp. z o.o.	51,00%	ELBIS Sp. z o.o.
14. Niepubliczny Zakład Opieki Zdrowotnej MegaMed Sp. z o.o. <i>Bełchatów</i>	97,4% 2,6%	PGE Górnictwo i Energetyka Konwencjonalna S.A. PGE Elektrownia Opole S.A.	100,00%	PGE Elektrownia Bełchatów S.A.
15. ELMEN Sp. z o.o. <i>Rogowiec</i>	100,00%	ELBIS Sp. z o.o.	100,00%	ELBIS Sp. z o.o.

	Entity	Share of Capital Group entities as at 31 December 2010	Parent company as at 31 December 2010	Share of Capital Group entities as at 31 December 2009	Parent company as at 31 December 2009
16.	EnBud Sp. z o.o. <i>Czymanowo</i>	100,00%	PGE Energia Odnawialna S.A.	100,00%	Elektrownia Wodna Żarnowiec S.A.
17.	Bio-Energia ESP Sp. z o.o. <i>Gdynia</i>	99,65%	PGE Energia Odnawialna S.A.	65,72% 12,16% 21,77%	PGE Energia Odnawialna S.A. Zespół Elektrowni Wodnych Porąbka-Żar S.A. Elektrownia Wodna Żarnowiec S.A.
18.	Dychowskie Przedsiębiorstwo Eksploatacji Elektrowni ELDEKS Sp. z o.o. <i>Dychów</i>	100,00%	PGE Energia Odnawialna S.A.	100,00%	PGE Zespół Elektrowni Wodnych Dychów S.A.
19.	ESP Usługi Sp. z o.o. <i>Warszawa</i>	100,00%	PGE Energia Odnawialna S.A.	100,00%	PGE Energia Odnawialna S.A.
20.	Budownictwo Hydroenergetyka - Dychów Sp. z o.o. <i>Dychów</i>	100,00%	PGE Energia Odnawialna S.A.	100,00%	PGE Zespół Elektrowni Wodnych Dychów S.A.
21.	Przedsiębiorstwo Usługowo- Produkcyjne ELTUR-SERWIS Sp. z o.o. <i>Bogatynia</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE Elektrownia Turów S.A.
22.	Przedsiębiorstwo Produkcji Sorbentów i Rekultywacji ELTUR- WAPORE Sp. z o.o. <i>Bogatynia</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE Elektrownia Turów S.A.
23.	Przedsiębiorstwo Transportowe ELTUR-TRANS Sp. z o.o. <i>Bogatynia</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE Elektrownia Turów S.A.
24.	Przedsiębiorstwo Handlowo- Usługowe GLOBAL - TUR Sp. z o.o. <i>Bogatynia</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	84,46% 15,54%	PGE Elektrownia Turów S.A. PGE KWB Turów S.A.
	Centrum Medyczne Turów Sp. z o.o. <i>Bogatynia</i>	-	c)	36,06% 63,94%	PGE Elektrownia Turów S.A. PGE KWB Turów S.A.
	Energo-Invest-Broker S.A. <i>Toruń</i>	-	-	30,62% 25,00%	PGE Elektrownia Bełchatów S.A. PGE Elektrownia Turów S.A.
25.	Przedsiębiorstwo Usługowo- Produkcyjne TOP SERWIS Sp. z o.o. <i>Bogatynia</i>	100,00%	Przedsiębiorstwo Usługowo-Produkcyjne ELTUR-SERWIS Sp. z o.o.	89,00%	Przedsiębiorstwo Usługowo-Produkcyjne ELTUR-SERWIS Sp. z o.o.
26.	ENESTA Sp. z o.o. <i>Stalowa Wola</i>	84,85% 2,48%	PGE Dystrybucja S.A. PGE Górnictwo i Energetyka Konwencjonalna S.A.	84,85% 2,48%	PGE Dystrybucja Rzeszów Sp. z o.o. PGE Elektrociepłownia Rzeszów S.A.
27.	NOM Sp. z o.o. <i>Warszawa</i>	100,00%	EXATEL S.A.	100,00%	EXATEL S.A.
28.	Energo-Tel S.A. <i>Warszawa</i>	51,10% 48,80%	EXATEL S.A. NOM Sp. z o.o.	51,10% -	EXATEL S.A. -
29.	E-Telbank S.A. <i>Warszawa</i>	100,00%	EXATEL S.A.	100,00%	EXATEL S.A.

Entity	Share of Capital Group entities as at 31 December 2010	Parent company as at 31 December 2010	Share of Capital Group entities as at 31 December 2009	Parent company as at 31 December 2009
Towarzystwo Gospodarcze BEWA Sp. z o.o. <i>Kleszczów</i>	-	-	100,00%	PGE KWB Bełchatów S.A.
30. RAMB Sp. z o.o. <i>Bełchatów</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE KWB Bełchatów S.A.
31. BESTUR Sp. z o.o. <i>Bełchatów</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE KWB Bełchatów S.A.
32. Przedsiębiorstwo Transportowo Sprzętowe BETRANS Sp. z o.o. <i>Rogowiec</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE KWB Bełchatów S.A.
33. Przedsiębiorstwo Wulkanizacji Taśm i Produkcji Wyróbów Gumowych BESTGUM POLSKA Sp. z o.o. <i>Rogowiec</i>	100,00%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	100,00%	PGE KWB Bełchatów S.A.
34. Górniczy Klub Sportowy Bełchatów S.S.A. <i>Bełchatów</i>	-	-	100,00%	PGE KWB Bełchatów S.A.
35. ELECTRA Bohemia s.r.o. <i>The Czech Republic</i>	100,00%	PGE Electra S.A.	100,00%	PGE Electra S.A.
36. Zakład Energetyczny Białystok Przedsiębiorstwo Transportowo-Usługowe ETRA Sp. z o.o. <i>Białystok</i>	100,00%	PGE Dystrybucja S.A.	100,00%	PGE Dystrybucja Białystok Sp. z o.o.
37. Zakład Energetyczny Białystok Przedsiębiorstwo Produkcyjno-Handlowe EKTO Sp. z o.o. <i>Białystok</i>	100,00%	PGE Dystrybucja S.A.	100,00%	PGE Dystrybucja Białystok Sp. z o.o.
38. Energetyczne Systemy Pomiarowe Sp. z o.o. <i>Białystok</i>	100,00%	PGE Dystrybucja S.A.	100,00%	PGE Dystrybucja Białystok Sp. z o.o.
39. Zakład Energetyczny Białystok Pracownia Projektowa ENSPRO Sp. z o.o. <i>Białystok</i>	100,00%	PGE Dystrybucja S.A.	100,00%	PGE Dystrybucja Białystok Sp. z o.o.
40. Zakład Usług Medycznych Dolna Odra Sp. z o.o. <i>Nowe Czarnowo</i>	-	c)	100,00%	PGE Zespół Elektrowni Dolna Odra S.A.
EPO Sp. z o.o. <i>Opole</i>	50,00%	PGE Elektrownia Opole S.A.	50,00%	PGE Elektrownia Opole S.A.
Przedsiębiorstwo Wielobranżowe Agtel Sp. z o.o. <i>Zamość</i>	-	-	70,62%	PGE Zamojska Korporacja Energetyczna S.A.
41. Centrum Szkolenia i Rekreacji „Energetyk” Sp. z o.o. <i>Krasnobród</i>	99,50%	PGE Obrót S.A.	99,50%	PGE Zamojska Korporacja Energetyczna S.A.
42. Zakład Obsługi Energetyki Sp. z o.o. <i>Zgierz</i>	100,00%	PGE Dystrybucja S.A.	100,00%	PGE Dystrybucja Łódź-Teren S.A.
43. PGE Serwis Sp. z o.o. <i>Warszawa</i>	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
44. PGE Systemy S.A. <i>Warszawa</i>	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
45. PGE Inwest S.A. <i>Warszawa</i>	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
46. PGE Inwest spółka z ograniczoną odpowiedzialnością II S.K.A. <i>Warszawa</i>	100,00%	PGE Polska Grupa Energetyczna S.A.	-	-

Entity	Share of Capital Group entities as at 31 December 2010	Parent company as at 31 December 2010	Share of Capital Group entities as at 31 December 2009	Parent company as at 31 December 2009
47. PGE Energia Jądrowa S.A. Warszawa	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
48. PGE EJ 1 sp. z o.o. Warszawa	51,00%	PGE Energia Jądrowa S.A.	-	-
	49,00%	PGE Polska Grupa Energetyczna S.A.	-	-
49. PWE Gubin Sp. z o.o. Sękowice	100,00%	PGE Polska Grupa Energetyczna S.A.	-	-
50. Elektrownia Wiatrowa Resko Sp. z o.o. Czymanowo	100,00%	PGE Energia Odnawialna S.A.	-	-
51. Biogazownia Łapy Sp. z o.o. Warszawa	100,00%	PGE Energia Odnawialna S.A.	-	-
52. Biogazownia Woźuczyn Sp. z o.o. Warszawa	100,00%	PGE Energia Odnawialna S.A.	-	-
53. Przedsiębiorstwo Energetyki Ciepłej Sp. z o.o. Zgierz	50,98%	PGE Górnictwo i Energetyka Konwencjonalna S.A.	-	-
54. Elektrownia Wiatrowa Turów Sp. z o.o. Warszawa	100,00%	PGE Energia Odnawialna S.A.	-	-
55. EO Baltica Sp. z o.o. Warszawa	100,00%	PGE Energia Odnawialna S.A.	-	-

- The merger of parent company with subsidiaries - PGE Górnictwo i Energetyka and PGE Energia S.A. was described in note 9 of explanatory notes to the foregoing consolidated financial statements.
- Mergers of entities within the PGE Group under the „Consolidation Programme” were disclosed in note 45.2 of the explanatory notes to the consolidated financial statements.
- The merger of Niepubliczny Zakład Opieki Zdrowotnej [Non-Public Healthcare Establishment] MegaMed Sp. z o.o. of Bełchatów with: Centrum Medyczne [Medical Center] Turów Sp. z o.o. of Bogatynia; Zakład Usług Medycznych [Medical Service Company] Dolna Odra Sp. z o.o. of Nowy Czarnów; and Zakład Usług Profilaktyczno – Leczniczych [Prophylactic and Medical Treatment Company] "Megavita" Sp. z o.o. of Brzeziny was registered on 31 December 2010.

Apart from the above-mentioned transformations during the year ended 31 December 2010 the following significant changes in the structure of the Group companies that are subject to full consolidation took place:

- On 7 January 2010 the change in ownership structure of Elektrownia Wiatrowa Resko Sp. z o.o. was registered in National Court Register in relation to the purchase of 50% of stocks of this company by PGE Energia Odnawialna S.A. – the company was included in the consolidated financial statements beginning from the year 2010.
- On 28 January 2010 PGE EJ 1 Sp. z o.o. was registered in the National Court Register. The entity's purpose is to build and possibly exploit the first nuclear power station.
- PGE Inwest Sp. z o.o. II S.K.A. was registered in National Court Register on 28 January 2010. PGE Inwest Sp. z o.o. is a general partner of the entity.
- On 5 February 2010 Biogazownia Łapy Sp. z o.o. was registered in the National Court Register – the company was included in the consolidated financial statements beginning from the year 2010.

("Translation of the document originally issued in Polish")

- On 17 February 2010 Przedsiębiorstwo Usługowo-Produkcyjne „ELTUR-SERWIS” sp. z o.o. acquired 11% of shares of Przedsiębiorstwo Usługowo-Produkcyjne „TOP-SERWIS” sp. z o.o. share in the equity of this company increased up to 100%.
- On 23 February 2010 the “Datio in Solutum” agreement was signed, in settlement (related to the dividend paid by ZEW Porąbka-Żar S.A.) of assignment of EGO-ODRA S.A. held by Porąbka-Żar S.A. shares for PGE Energia Odnawialna S.A. The shares were transferred on 8 March 2010.
- On 29 March 2010 PGE KWB Bełchatów S.A. disposed of GKS Bełchatów S.S.A.
- On 31 May 2010 NOM Sp. z o.o. acquired 48,8% of the share capital of ENERGO-TEL S.A. As a result of this transaction NOM Sp. z o.o. holds 48,8% and Exatel holds 51,1% of the company's share capital.
- On 11 June 2010 the shareholders of Electra Deutschland GmbH adopted a resolution to increase the share capital. Shares in the increased share capital, accounting for 25,93% of total share capital, were held by PGE Polska Grupa Energetyczna S.A. The increase was registered on 30 July 2010.
- On 18 June 2010 PGE Polska Grupa Energetyczna S.A. acquired from Kopalnia Węgla Brunatnego Konin S.A. 100% of shares of PWE Gubin sp. z o.o. seated in Sękowice.
- On 9 July 2010 PGE Zamojska Korporacja Energetyczna S.A. sold shares constituting 70,62% of the share capital of Przedsiębiorstwo Wielobranżowe Agtel Sp. z o.o.
- On 15 July 2010 Elbis Sp. z o.o. concluded the agreement on sale of 50% of shares of Elektrownia Wiatrowa Kamieński Sp. z o.o. – the transaction took place on 28 July 2010.
- On 22 July 2010 PGE Zespół Elektrowni Dolna Odra S.A. acquired from Gryfino Commune 19,74% of the share capital of Przedsiębiorstwo Energetyki Ciepłej Sp. z o.o. seated in Gryfino. On 23 July 2010 the company acquired additional 0,26% of the share capital and as a result of this its share in equity of Przedsiębiorstwo Energetyki Ciepłej Sp. z o.o. increased up to 100%..
- On 6 September 2010 PGE Górnictwo i Energetyka Konwencjonalna S.A. sold its shares constituting 100 % of the share capital of Towarzystwo Gospodarcze BEWA Sp. z o.o.
- On 14 December 2010 Elektrownia Wiatrowa Turów Sp. z o.o. (Turów Wind Power Plant Limited Liability Company) was registered in the National Court Register. The company was established by PGE Energia Odnawialna S.A. on 25 November 2010.
- On 16 December 2010 EO Baltica sp. z o.o. was registered in the National Court Register. The company was established by PGE Energia Odnawialna S.A. on 25 November 2010.
- On 28 December 2010 the Company entered into an agreement with the State Treasury whereunder PGE S.A. acquired shares of the following companies: PGE Górnictwo i Energetyka Konwencjonalna S.A., constituting 10.69% of share capital; PGE Obrót S.A., constituting 13.87% of share capital; and PGE Dystrybucja S.A., constituting 1.47% of share capital. The combined value of these transactions was PLN 3.098.387 thousand. The transaction involved non-controlling stakes in key companies of PGE Group, which were acquired by the State Treasury through the shares conversion programme, in accordance with the Act of September 7, 2007 on the Rules of Shares Acquisition from the State Treasury in the Consolidation Process of Energy Sector Companies (Journal of Laws of 2007, No. 191, item 1367).
- On 29 December 2010 a contract of sale of all shares of Energo-Inwest-Broker S.A. Toruń, held by PGE Górnictwo i Energetyka Konwencjonalna S.A. seated in Toruń was signed. The shares were acquired by Energo-Inwest-Broker S.A. for the purpose of redemption.
- On 30 December 2010 an increase of the share capital of Przedsiębiorstwo Energetyki Ciepłej Sp. z o.o. of Zgierz was registered in the National Court Register. Newly formed shares were taken up by PGE Górnictwo i Energetyka Konwencjonalna S.A. After registration of that increase ownership interest of PGE Górnictwo i Energetyka Konwencjonalna S.A. in the latter company's share capital equals to 50.98%.

3. The composition of the Management Board of the Parent Company

As at 31 December 2010 the composition of the Management Board was as follows:

- Mr. Tomasz Zadroga – the President of the Management Board,
- Mr. Marek Szostek – the Vice-President of the Management Board,
- Mr. Piotr Szymanek – the Vice-President of the Management Board,
- Mr. Wojciech Topolnicki – the Vice-President of the Management Board,
- Mr. Marek Trawiński – the Vice-President of the Management Board.

On 5 January 2011 Supervisory Board adopted a resolution of Vice-President for Financial matters – Wojciech Topolnicki dismissal and delegation responsibilities of Vice-President for Financial matters to Tomasz Zadroga.

Therefore, as of the day of preparation of the foregoing consolidated financial statements, the composition of the Management Board of the parent company was:

- Mr. Tomasz Zadroga – the President of the Management Board,
- Mr. Marek Szostek – the Vice-President of the Management Board,
- Mr. Piotr Szymanek – the Vice-President of the Management Board,
- Mr. Marek Trawiński – the Vice-President of the Management Board.

4. Approval of the consolidated financial statements

The foregoing consolidated financial statements were prepared and signed by the Management Board of the parent company on 15 March 2011.

5. Going concern

The consolidated financial statements were prepared under the assumption that the Group companies will continue to operate as a going concern for the foreseeable future. As at the day of the approval of the consolidated financial statements, there is no evidence indicating that the Group companies will not be able to continue its business activities as a going concern.

6. Presentation currency

The presentation currency of the consolidated financial statements is the Polish zloty („PLN”). All the amounts are stated in PLN thousand, unless stated otherwise.

7. Statement of compliance with International Financial Reporting Standards

The foregoing consolidated financial statements were prepared in accordance with the International Financial Reporting Standards (“IFRS”) and IFRS approved by the European Union (“EU”). As at the day of the approval of the foregoing consolidated financial statements for publication, with regards to the ongoing implementation of IFRS in EU and the business activities of the Group, there are no differences between Applied Accounting Principles (Policy) of the Group and IFRS which are effective and those adopted by EU.

IFRS comprise standards and interpretations approved by International Accounting Standards Board (IASB) and International Financial Reporting Interpretation Committee (IFRIC).

8. The basis for the preparation of the consolidated financial statements

With regards to financial reporting obligations resulting from the planned public offering of the parent company PGE Polska Grupa Energetyczna S.A., the Management Board decided to implement the International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). The first consolidated financial statement of the PGE Capital Group comprising a statement of unconditional compliance with IFRS were the consolidated financial statements prepared for the year ended 31 December 2007.

The bookkeeping in the PGE Capital Group entities is maintained in accordance with the accounting policies (rules) specified in the Accounting Act dated 29 September 1994 (“the Accounting Act”) and related bylaws, and other applicable regulations (“Polish Accounting Standards”), except from:

- PGE Energia Odnawialna S.A. – which run their books in compliance with IFRS.
- ELECTRA Deutschland GmbH and ELECTRA Bohemia s.r.o., seated in Germany and Czech Republic, which run their books in compliance with German and Czech reporting regulations.

Therefore the consolidated financial statements comprise adjustments which were not included in the books of Group entities. The purpose of these adjustments was to make the financial statements of these entities compliant with IFRS approved by the EU.

9. Business combinations

Creation of PGE Group

As a consequence of the Programme for Electric Power Engineering dated 28 March 2006 the Polska Grupa Energetyczna Capital Group was based on:

- Polskie Sieci Elektroenergetyczne S.A. (currently under the business name PGE Polska Grupa Energetyczna S.A.),
- former BOT Capital Group: BOT Górnictwo i Energetyka S.A. („BOT GiE S.A.”), BOT Elektrownia Bełchatów S.A., BOT Kopalnia Węgla Brunatnego Bełchatów S.A., BOT Elektrownia Opole S.A., BOT Elektrownia Turów S.A. and BOT Kopalnia Węgla Brunatnego Turów S.A.,
- Zespół Elektrowni Dolna Odra S.A. („ZEDO”)
- eight energy companies: Zamojska Korporacja Energetyczna S.A., Rzeszowski Zakład Energetyczny S.A., Lubelskie Zakłady Energetyczne S.A., Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A., Łódzki Zakład Energetyczny S.A., Zakład Energetyczny Łódź-Teren S.A., Zakład Energetyczny Warszawa-Teren S.A. and Zakład Energetyczny Białystok S.A.

In accordance with the Programme for Electric Power Engineering a consolidation model was elaborated under which shares of all of the above mentioned entities were contributed to PSE.

The consolidation took place in two stages. At first, in December 2006, the State Treasury contributed 85% of shares of ZEDO S.A. and eight energy companies to share capital of PGE Energia S.A. In the second stage, on 9 May 2007, an increase of share capital of parent company was made as a result of a contribution of 85% of shares of PGE Energia S.A. and BOT GiE S.A.

Settlement of PGE Group foundation in the consolidated financial statement

Regulations on mergers and acquisitions are specified in IFRS 3 *Business combinations*. However, this standard excludes transactions between entities under common control. Entities contributed to the Company in May 2007 were under control of the State Treasury together with the hitherto existing PSE Group, which means that both the Company and the contributed entities were under common control of the State Treasury. Regarding the above, the transaction fulfilled the definition of a business combination under common control as assessed by the Company, and therefore is excluded from application of IFRS 3.

The absence of a Standard or an Interpretation that specifically applies to a transaction, other event or condition, is covered by IAS 8 point 10-12. Based on these provisions, the entity preparing its financial statement in accordance with IFRS is obliged to develop and apply an accounting policy that results in information that is relevant to the economic decision-making needs of users and is reliable, in that the financial statements represent truly and fairly the financial position, financial performance and cash flows of the entity; reflect the economic substance of transactions other events and conditions, and not merely the legal form; are neutral, prudent and complete in all material respects.

According to analysis made by the Company, the entities of complex financial information and under common control are preferred to be accounted for using the pooling of interest method. The method is based on the assumption that entities were controlled by the same party or parties both before and after the business combination, that control is not transitory, and the consolidated financial statements reflect the continuity of common control and does not reflect a change in net assets to fair value (or recognition of new assets) or goodwill, as none of the entities under business combination is actually acquired. With regards to the above, the consolidated financial statements are prepared as if the entities have always been under business combination.

Financial statements of all PGE Group entities of the State Treasury under business combination were aggregated since transition to IFRS, and the whole business combination transaction was settled within equity with no influence on goodwill.

Further significant transformations of the PGE Capital Group in 2010

As specified in detail in Note 45.2 to the foregoing consolidated financial statements mergers among selected Group companies occurred during 2010. These mergers did not affect the value of assets, liabilities, revenues or expenses presented in these financial statements. However, as a consequence of the above specified mergers (particularly the merger of PGE S.A. with PGE Górnictwo i Energetyka S.A. and PGE Energia S.A.), the parent's share in equity and net profits of consolidated companies increased. The merger influenced the values presented in these consolidated financial statements:

- Part of equity allocated to non-controlling interest was transferred to equity of the parent, in the amount of PLN 3.377 million.
- Retained earnings allocated to shareholders of the parent were increased by the values of dividends which were allocated to non-controlling interest before merger (PLN 308 million).
- As of September 2010 the parent company's share in earnings of subsidiaries has been calculated on the basis of updated percentage in these companies' share capital.

On 31 December 2010 the parent company merged with PGE Electra S.A. The latter was a wholly-owned subsidiary of PGE S.A. and therefore the merger had no impact on the values presented in the foregoing consolidated financial statements.

Furthermore, as described in Note 2 to the foregoing consolidated financial statements, on 28 December 2010 the parent company purchased from the State Treasury shares in key subsidiaries namely in: PGE Górnictwo i Energetyka Konwencjonalna S.A.; PGE Obrót S.A.; and PGE Dystrybucja S.A., for a total price of PLN 3.098.387 thousand. The Group companies also bought smaller stakes in other consolidated entities during the period. As the mergers of companies meeting the criteria of restructuring under common control are consolidated under the pooling of interest method, the value of non-controlling equity interest acquired in subsidiaries was presented as the increase of retained earnings of the Group, while the price of purchase of additional shares was recognized as a decrease of retained earnings of the Group, and additional costs involved in purchase of shares were presented in the income statement. In aggregate, the transactions identified above generated an increase of the Group's retained earnings of PLN 531.526 thousand and a decrease of gross profit of PLN 30.984 thousand.

10. Significant values based on estimates and professional judgment

In the process of applying accounting rules with regards to the below issues, the most significant, apart from estimates, was the professional judgment of the management, which influenced the values presented in the consolidated financial statements and in the supplementary information and explanations. The estimates were based on the best knowledge of the Management Boards relating to current and future operations and events in particular accounting areas. Detailed information on the applied estimates was presented below or in relevant explanatory notes to the consolidated financial statements.

Depreciation period of non-current assets

Depreciation rates and impairment loss are calculated on the basis of the estimated economic useful life of an item of property, plant and equipment and intangible assets as well as estimates of its residual value. Capitalized costs of major inspections and overhauls are depreciated throughout the period until the beginning of the next planned overhaul/ inspection. Estimated economic useful life of assets is subject to verification at least once a year.

Recoverable amount of property, plant and equipment

The electric energy market, which is the basic field of business activities of PGE Group entities, is in the process of significant transformations. These changes can have a significant influence on the recoverable amount of production property, plant and equipment of particular PGE Group entities. If exist indications specified in IAS 36 *Impairment of Assets*, the Group estimates the recoverable amount of an item of property, plant and equipment owned.

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

Valuation of provisions for social benefits

Provisions for social benefits (provision for retirement and pension awards, energy tariff, additional allowances on the Social Fund ("ZFŚS") for the former employees of the Group entities, medical benefits and coal allowances) were estimated on the basis of actuarial methods.

Post-mining land recultivation provisions

On the basis of Geological and Mining Law, lignite mines, which are the part of the Group, are obliged to perform land recultivation after the land exploitation is finished. The proper provision is created as a proportion of lignite excavated to the planned total lignite excavation from the layer in the expected excavation period. Estimates of expected recultivation costs are updated every 5 years at least. The value of the provision is verified each year according to the actual assumptions regarding inflation rate, discount rate and excavation volume.

Provision for a shortage of carbon dioxide emission rights

Provisions related to liabilities resulting from shortage of CO₂ emission rights is created in the period in which the Group entities notice, that emission rights granted within the National Plan of Emission Rights are not sufficient to cover statutory obligations related to their redemption. The entities settle emission rights throughout the whole settlement period and create the provision at the end of the given reporting period.

Other provisions and contingent liabilities

Regarding regulations of IAS 37 on recognition and measurement of provisions and contingent liabilities, the Group estimates the probability of occurrence of potential liabilities. If the occurrence of unfavorable future event is probable, the Group recognizes a provision in the appropriate amount. If the occurrence of unfavorable future event is estimated by the Group as not probable but possible, the contingent liability is recognized.

Deferred tax assets

The deferred tax assets are valued on the basis of tax rates that are expected to be applied at the moment of realization of the asset, based on tax regulations in force as at the balance sheet date. The deferred tax asset is recognized to the extent that it is probable that taxable profit will be available against which the asset can be realized. Deterioration of taxable results in the future would make the above assumption unjustified.

Recognition of financial instruments

Regarding regulations of IAS 39 on classification of non-derivative financial instruments with settled payment dates or expected maturity they are classified as held-to-maturity assets. Under such judgment, the intention and possibility of holding these assets to maturity are evaluated.

Revenues from sale of electric energy estimates

Reading numbers from meters regarding the volume of electric energy sold in retail as well as its invoicing is performed mainly in periods different than reporting periods. Taking into account the above, regional energy companies within the Group perform certain revenues estimates at each balance sheet date for the period not covered with a reading.

Compensations resulting from termination of long-term agreements for the sales of electric power and energy (LTC)

Producers of electric energy, who joined the program of early termination of long-term agreements for the sales of electric power and energy, are entitled to receive compensations to cover stranded costs. The compensations are paid in the form of annual advances as four quarterly installments which are adjusted on yearly basis. At the end of the adjustment period, the final amount of stranded costs will be determined. Due to the above, the producers of electric energy of PGE Group estimate and recognize the revenue from LTC compensations in the amount in which it will be finally approved for the given period, i.e. after final and annual adjustments expected as at the date of the preparation of the consolidated financial statements. For more details on estimation of the above mentioned revenues please refer to note 45.1 of the foregoing consolidated financial statements.

The Group's estimations of compensation related to early termination of long-term agreements for the sales of electric power and energy and recognition of related revenues and receivables prepared by the Group were based on the Group's interpretation of regulations dated 29 June 2007, the Act on rules of covering producer's costs related to early termination of long-term agreements for the sales of electric power and energy (Official Journal, No. 130, item 905, year 2007) ("the LTC Act") and on a number of significant assumptions, some of which are outside the control of the Group.

An unfavorable outcome for the PGE Capital Group of the dispute, described in the Note 45.1, with the President of the Energy Regulation Office with respect to the interpretation of the LTC Act and changes in assumptions used, including those resulting from planned legal mergers within the PGE Group, may impact the estimates and as a consequence may lead to significant changes to the financial position and results of the PGE Capital Group. The final outcome of the dispute with the President of the Energy Regulation Office cannot be determined as at the date of preparation of the foregoing financial statements.

Revaluation write offs on receivables

As at the balance sheet date the PGE Group entities assess whether there is an objective proof for impairment of receivables or a group of receivables. If the recoverable amount of assets is lower than its carrying amount, the entity creates a write off to the amount of the present value of planned cash flows.

11. Change of estimates

In the period covered by the consolidated financial statements, the following significant changes to estimates influencing the numbers presented in the consolidated financial statements took place:

- Change of adopted actuarial assumptions. The influence of change in estimates on the value of provisions and statement of comprehensive income is presented in detail in note 34 and note 35 of the foregoing consolidated financial statements.
- Provisions are liabilities of uncertain timing or amount. During the reporting period the Group changed estimations regarding the basis and amounts of some provisions. Changes of estimations are presented in note 35 of the foregoing consolidated statements.
- During the reporting period the Group updated estimations on the recoverable amount of some items of property, plant and equipment. The influence of the change of estimations is presented in note 21 of the foregoing consolidated financial statements.
- As at the date of preparation of PGE Group consolidated financial statements for the year ended 31 December 2009 the financial statements of Polkomtel S.A., which is an associated company, was not yet audited nor approved by that company's management. On the basis of available data PGE Group recognized in 2009 a share in net profit of Polkomtel S.A., an associated company, in the amount of PLN 241.931 thousand. After publication of the consolidated financial statements for 2009 financial data of the associated company were adjusted respectively. This adjustment was carried to the financial statements of PGE Group in 2010, causing a decrease of consolidated gross profit in amount of PLN 27.419 thousand.
- In the preceding financial periods brown coal mines incorporated in PGE Group did not recognize deferred tax asset related to establishment of provision for recultivation of excavations, as these costs were expected to incur after the end of mine exploitation i.e. after the period of generating revenues by these companies. As a result of merger of mines with energy producers within PGE Górnictwo i Energetyka Konwencjonalna S.A. future costs of recultivation have been recognized as probable tax gains. Therefore during the present reporting period the Group reversed a write off of deferred tax asset in the amount of PLN 130 million.

12. New standards and interpretations published, not yet effective

The following standards, changes in already effective standards and interpretations are approved by the European Union but are not effective as at 1 January 2010:

- amendments to IAS 32 *Financial instruments: Presentation* – effective for the periods starting 1 February 2010;
- amendments to IFRS 1 *Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters* – effective for the periods starting 1 July 2010;
- amendments to IFRS 8 *Operating Segments* – effective for the periods starting 1 January 2011;
- revised IAS 24 *Related Party Disclosures* – effective for the periods starting 1 January 2011;
- amendments to IFRIC 14 *The Limit on Defined Benefit Asset, Minimum Funding Requirements and their Interaction* – effective for the periods starting 1 January 2011;
- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments* – for the periods starting 1 July 2010;
- Amendments do IFRS covering six standards and one interpretation – for periods starting 1 January 2011 (except from the amendments to IFRS 3 *Business combinations*)

The following standards, changes in already effective standards and interpretations are not approved by the European Union and are not effective as at 1 January 2010:

- IFRS 9 *Financial instruments* effective for the periods starting 1 January 2013;
- amendments to IFRS 1 *First-time Adoption of IFRS* – effective for the periods starting 1 July 2011;
- amendments to IFRS 7 *Financial instruments: Disclosures* – effective for the periods starting 1 July 2011;
- amendments to IAS 12 *Income tax* – effective for the periods starting 1 January 2012.

The influence of new regulations on future consolidated financial statements of the Capital Group

The new IFRS 9 introduces fundamental changes to classifying, presenting and measuring of financial instruments. These changes will possibly have material influence on future consolidated financial statements of the Group. At the date of preparation of the foregoing consolidated financial statements IFRS 9 is not yet approved and as a result its impact on the future consolidated financial statements of the PGE Group is not yet determined.

According to the assessment of the Management Board the implementation of new standards and interpretations, except from matters mentioned above, would not have a significant influence on the accounting principles (policies) applied by the Group.

13. Accounting principles applied

The most significant accounting principles applied are presented below.

13.1. Principles of consolidation

The consolidated financial statements comprise the financial statements of PGE Polska Grupa Energetyczna S.A. and financial data of its subsidiaries. Financial statements of subsidiaries are prepared for the same reporting period as the parent company's, with the use of consistent accounting principles, based on unified accounting principles related to classes of transactions and events of similar characteristics

All significant Intra-Group balances and transactions, including unrealized gains from Intra-Group transactions, were fully eliminated. Unrealized losses are eliminated, unless they prove the impairment of assets.

The consolidation of subsidiaries begins on the day of taking over the control and is finished when the control ceases. Control is normally evidenced when the Group holds directly or indirectly more than 50% of the voting rights in a company or it is possible to prove that a certain number of voting rights constitutes control. Control is also evidenced when the Group is able to govern the financial and operating policies of a company so as to benefit from the results of its activity.

All entities, which entered the PGE Capital Group as a result of reorganization in 2007, as described in detail in note 9, were under common control of the State Treasury both before and after the reorganization. IFRS 3 Business Combinations does not apply to entities or businesses under common control both before and after business combinations. A business combination involving entities or businesses under common control is a business combination in which all of the combining entities or businesses are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory. In such cases, the Group should apply IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, paragraph 10-12, and choose a relevant accounting policy. In making the above judgment, the management may also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework as IASB

With regards to the fact that both standards and IASB conceptual framework do not contain either requirements or insights on business combinations under common control, PGE Polska Grupa Energetyczna S.A. chooses an accounting principle according to which such transactions are settled under the pooling of interest method. The pooling of interest method is a method of accounting in which financial information of associates, including the aggregated amounts of assets, liabilities, revenues and expenses are summarized after initial implementation of a unified method of measurement and relevant eliminations. Share capitals of entities are eliminated if their shares were contributed to PGE Polska Grupa Energetyczna S.A. Specified positions in equity are adjusted with a difference between the aggregated amounts of assets and liabilities. All Intra-Group balances and transactions, including unrealized gains from Intra-Group transactions, are fully eliminated. Unrealized losses are eliminated, unless they prove to be impaired. The consolidated financial statements of the Group, which include entities under common control, prepared for the reporting year in which the business combination took place, comprise comparative financial data for the previous reporting year measured as if the business combination took place at the beginning of the previous financial year.

13.2. Investments in associates

Investments in associates are recognized using the equity method. An associate is an entity over which the Parent Company directly, or through dependent entities, has a significant influence and that associate is neither a subsidiary nor an interest in a joint venture. Financial statements of associates are the basis for measurement of parent-owned shares using the equity method. The associates and the parent company have the same financial year.

Upon initial recognition, investments in associates are designated at cost, and the carrying amount is increased or decreased to recognize the investor's share of the profit or loss of the investee after the date of acquisition less impairment losses if applicable. The investor's share of the profit or loss of the investee is recognized in the investor's profit or loss. Adjustments recognized directly in the equity of associates, are recognized in the share owned by the parent company and disclosed in statement of changes in equity if such disclosure is justified.

13.3. Investment in jointly controlled entities

Investments in jointly controlled entities where the Group exercises joint control are accounted for using the equity method. Before measuring the share in net assets, adjustments are made by such entities in order to comply with accounting policy applied in the Group.

Assessment of the value of investments in jointly controlled entities is performed when there are indications that the asset has been impaired or the impairment losses recognized in prior years are no longer required.

13.4. Methods applied to translation of data denominated in foreign currencies

Transactions denominated in currencies other than Polish zloty were translated into Polish zlotys at the rate on the transaction date. As at the balance sheet date:

- Monetary items were translated at the closing rate on the balance sheet date (the closing rate is the average exchange rate established by the National Bank of Poland for this day),
- Non-monetary items were valued at historical cost in foreign currency at an exchange rate on the day of the first transaction (exchange rate of the bank of the company), and
- Non-monetary items measured at fair value in foreign currency are translated at an exchange rate on the day of fair value measurement.

Foreign exchange differences resulting from translation are recognized in the profit or loss or, in cases specified in the accounting principles (policies) applied, recorded in the value of assets.

Foreign exchange differences resulting from translation of non-financial positions, such as equity instruments measured at fair value through the profit or loss, are recognized as a change in fair value.

Foreign exchange differences resulting from translation of non-monetary positions, such as equity instruments classified as financial assets available for sale, are recognized in revaluation reserve.

Foreign exchange differences resulting from translation of assets and liabilities of foreign entities are recognized in equity.

The following exchange rates were used for the valuation of monetary items denominated in foreign currencies at the respective period end:

	31 December 2010	31 December 2009
USD	2,9641	2,8503
EURO	3,9603	4,1082

13.5. Property, plant and equipment

Property, plant and equipment are assets:

- held for use in the production or supply of goods or services, for rental to others, or for administrative purposes;
- expected to be used for more than one year;
- for which it is probable that future economic benefits associated with them will flow to the entity;
- the cost of which can be measured reliably.

Significant items of property, plant and equipment used before the date of transition to IFRS, i.e. 1 January 2006, were measured at fair value as at this day (deemed cost). Differences between fair value and carrying amount were recognized in retained earnings. Property, plant and equipment as well as fixed assets under construction after the date of transition to IFRS are measured at cost of acquisition or cost of manufacturing.

After recognition as an asset, an item of property, plant and equipment shall be measured at its net value, i.e. initial value (or at deemed cost for items of property, plant and equipment used before the transition to IFRS) less any accumulated depreciation and any impairment losses. Initial value comprises of purchase price including all costs directly attributable to the purchase and making capable of operating. The cost of an item of property, plant and equipment comprises an estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period. Capitalization of costs ends when the item is brought to the location and conditions necessary for it to be capable of operating in the manner intended by the management.

As at the day of acquiring of the item of property, plant and equipment or as at the day of transition to IFRS, in case of existing items of property, plant and equipment, all significant elements being part of an item of property, plant and equipment with various economic useful lives (components) are identified and separated. Components of property, plants and equipment also include costs of major inspection and overhaul if they are significant and costs of recurring replacement of major components.

Major special spare parts and stand-by equipment of significant value qualify as property, plant and equipment when an entity expects to use them during more than one year. Other spare parts and servicing equipment are usually carried as inventories and recognized in the profit or loss as consumed, except for costs of replacement of parts during an overhaul of an item of property, plant and equipment. The assessment of significant value is subject to verification at least once a year.

The depreciable amount is the cost of an asset less its residual value. Depreciation commences when the asset is capable of operating. Depreciation is performed on the basis of a depreciation plan reflecting the future useful life of the asset. The depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

Major inspection and overhauls recognized as a component of property, plant and equipment are depreciated starting the next day after finishing the inspection/overhaul until the beginning of the next overhaul/inspection.

Major spare parts and stand-by equipment of significant value qualified as property, plant and equipment are depreciated during the remaining economic useful life of the related item (i.e. from the purchase date of the component till the end of the usage of the property, plant and equipment).

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

Group	Average depreciation period in years	Applied depreciation periods in years
Buildings and construction	17	20 – 40
Machinery and equipment	11	5 – 15
Vehicles	6	5 – 7
Other	5	3 – 10

Depreciation method, depreciation rate and residual value of property, plant and equipment are verified at least each financial year. Changes identified during verification shall be accounted for as a change in an accounting estimate and possible adjustments to depreciation amounts shall be recognized in the year in which the verification took place and in the following periods.

If there have been events or changes which indicate that the carrying amount of property, plant and equipment may not be recoverable, the assets are analyzed for potential impairment. If there are indications of impairment, and the carrying amount exceeds the estimated recoverable amount, the value of those assets or cash-generating units is decreased to the recoverable amount by an appropriate impairment loss.

The carrying amount of an item of property, plant and equipment can be derecognized on disposal or when no future economic benefits are expected from its use or disposal. The gain or loss arising from the derecognizing of an item of property, plant and equipment (determined as the difference between the net disposal revenues, if any, and the carrying amount of the item) shall be included in the profit or loss when the item is derecognized.

Investments relating to fixed assets under construction or assembly are recognized at cost of acquisition or cost of manufacturing less impairment losses. Property, plant and equipment under construction are not depreciated until the construction is finished and the items are available for use.

13.5.1 The cost of making lignite layers available for exploitation

As at the date of transition to IFRS, the technical services of PGE KWB Bełchatów S.A. (current name: Górnictwo I Energetyka Konwencjonalna S.A. Oddział Kopalnia Węgla Brunatnego Bełchatów) performed a revaluation of initial excavation dig into the lignite layer in Bełchatów, previously performed by actuary reviewers as at 1 January 1995, by adjusting it with a construction and assembly production prices index. In case of PGE KWB Turów S.A. (current name: Górnictwo I Energetyka Konwencjonalna S.A. Oddział Kopalnia Węgla Brunatnego Turów), due to a different geological situation and very shallow layers of lignite, the costs of making the layers available for excavation were insignificant and therefore were not subject to valuation.

The cost of making lignite layers available for exploitation is depreciated with the use of the depletion method calculated as the ratio of lignite excavated in the year to the total volume of lignite to be excavated from the layer in the time of mine exploitation. The costs of making the layers available for excavation are recognized as the costs of the current period.

13.6. Investment property

The Capital Group recognizes property as investment property when it is held to earn rentals, for capital appreciation, or both, instead of being for:

- use in the production or supply of goods or services or for administrative purposes; or
- sale in the ordinary course of business.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions can be sold separately (or leased out separately under a finance lease), an entity accounted for the portions separately. If the portions could not be sold separately, the property is investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes.

An investment property is measured initially at its cost (cost of acquisition or cost of manufacturing). The cost of a purchased investment property comprises its purchase price and any directly attributable expenditure. The directly attributable expenditure includes, for example, professional fees for legal services, property transfer taxes and other transaction costs. The cost of a self-constructed investment property is its cost at the date when the construction or development is complete, until then it is recognized as construction in progress.

An investment property is recognized at acquisition price or cost of manufacturing including transaction costs. After recognition as an asset, an item of investment property shall be carried at its cost less any accumulated depreciation and any accumulated impairment losses.

An investment property shall be derecognized (eliminated from the statement of financial position) on disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposal. Gains or losses arising from the retirement or disposal of investment property shall be determined as the difference between the net disposal revenues and the carrying amount of the asset and shall be recognized in the profit or loss in the period of the retirement or disposal.

Transfers to investment property shall be made when, and only when, there is a change in use, evidenced by end-of-owner-occupation, commencement of an operating lease or end of construction or development of an investment property.

Transfers between investment property, owner-occupied property and inventories do not change the carrying amount of the property transferred and they do not change the cost of that property for measurement or disclosure purposes.

13.7. Intangible assets

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

- assets acquired by the entity and recognized in non-current assets, with an economic useful life exceeding one year intended to be used by the company, in particular:
 - copyrights, concessions, licenses (including computer software),
 - patents, trademarks, utility and decorative designs, computer software,
 - know-how, i.e. equivalent value of information related to knowledge on industry, trade, science or organization,
- development costs,
- goodwill excluding internally generated goodwill.

An intangible asset is measured initially at cost (cost of acquisition or cost of manufacturing). The cost of a separately acquired intangible asset comprises:

- purchase price and attributable costs, such as import duties and non-refundable purchase taxes, after deducting trade discounts and rebates, and

- any directly attributable cost of preparing the asset for its intended use: costs of employee benefits, professional fees and costs of testing whether the asset is functioning properly.

After initial recognition, an intangible asset shall be carried at its cost less any accumulated amortization and any accumulated impairment losses.

The cost of an internally generated intangible asset, except for development costs, are not capitalized and are recorded in the profit or loss for the period when the related cost was incurred.

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

The amortizable amount of an intangible asset with a definite useful life is determined after deducting its residual value. The Group adopted a rule according to which the residual value of an intangible asset with a definite useful life shall be assumed to be zero unless:

- there is a commitment by a third party to purchase the asset at the end of its useful life – the residual value is based on the amount recoverable from disposal; or
- there is an active market for the asset and residual value can be determined by reference to that market and it is probable that such a market will exist at the end of the asset's useful life.

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

Intangible assets with a definite useful life shall be amortized over their useful life and analyzed for potential impairment, if there are indications of impairment. The amortization period and method are reviewed at least each financial year. If the expected useful life of the asset is different from previous estimates, the amortization period shall be changed accordingly. If there has been a change in the expected pattern of consumption of the future economic benefits embodied in the asset, the amortization method shall be changed to reflect the changed pattern.

Intangible assets with an indefinite useful life and those not being used are subject to impairment testing each year.

The following useful lives are adopted for intangible assets:

Group	Average depreciation period in years	Applied depreciation periods in years
Acquired patents and licenses	2	3 -5
Costs of finished developed works	1	3 -5
Other	9	3 - 25

13.8. Research and development costs

All intangible assets internally generated by the Group are not recognized as assets, but rather as expenses, and in the period when the related costs are incurred, except for development costs. An intangible asset arising from development shall be recognized if, and only if, an entity can demonstrate all of the following:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale,
- its intention to complete the intangible asset and use or sell it,
- its ability to use or sell the intangible asset,
- how the intangible asset will generate probable future economic benefits,
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset, and
- its ability to reliably measure the expenditure attributable to the intangible asset during its development.

Development works include:

- the design, construction and testing of pre-production or pre-use prototypes and models,
- the design of tools, jigs, moulds and dies involving new technology,
- the design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production, and
- the design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.

The cost of development works is the sum of expenditures incurred from the date when the intangible asset first meets the above mentioned recognition criteria. The cost of an internally generated intangible asset comprises all directly attributable costs necessary to create, produce, and prepare the asset to be capable of operating in the manner intended by management. Examples of directly attributable costs are:

- costs of materials and services used or consumed in generating the intangible asset,
- costs of employee benefits arising from the generation of the intangible asset,
- fees to register a legal right, and
- amortization of patents and licenses that are used to generate the intangible asset.

The following are not components of the cost of a self-constructed intangible asset:

- selling, administrative and other general overhead expenditure unless this expenditure can be directly attributed to preparing the asset for use;
- clearly identified inefficiencies and initial operating losses incurred before an asset achieves planned performance;
- expenditure on training staff to operate the asset.

13.9. Borrowings costs

Borrowing costs, including relevant foreign exchange differences, that are directly attributable to the acquisition, construction or production of a qualifying asset shall be eligible for capitalization relevant to items of property, plant and equipment and intangible assets, in accordance with IAS 23. In case of exchange differences arising from foreign currency borrowings, they are capitalized to the extent that they are regarded as an adjustment to interest costs.

13.10. Financial assets

Financial assets are classified in the following categories:

- Held-to-maturity investments (HTM),
- Financial assets at fair value through the profit or loss (FVP),
- Loans and receivables,
- Available-for-sale financial assets (AFS).

13.10.1 Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intention and ability to hold to maturity. Held-to-maturity investments shall be measured at amortized cost using the effective interest method. If the maturity exceeds 12 months, the financial assets held to maturity are classified as long-term assets.

13.10.2 Financial assets at fair value through profit or loss

A financial asset at fair value through profit or loss is a financial asset that meets either of the following conditions:

- It is classified as held for trading. A financial asset is classified as held for trading if it is:
 - acquired or incurred principally for the purpose of selling in the near term;
 - part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking; or
 - derivative, except for a derivative that is a designated and effective hedging instrument.
- Upon initial recognition it is designated by the entity as at fair value through profit or loss (in accordance with IAS 39). Any financial asset within the scope of this standard may be designated when initially recognized as a financial asset at fair value through profit or loss except for investments in equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured.

These assets are measured at fair value considering the market value as at the balance sheet date. The change in fair value of those assets is recognized in financial income or expense in the statement of comprehensive income.

13.10.3 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are classified as current assets, if their maturity does not exceed 12 months from the balance sheet date. Loans and receivables with maturity exceeding 12 months are classified as non-current assets. If the time value of money changes significantly over the period, the assets are measured at a discounted value. Loans and receivables are recognized at amortized cost.

13.10.4 Available-for-sale financial assets

All other assets account for available-for-sale financial assets. Financial assets available for sale are recognized at fair value as at each balance sheet date. Fair value of an instrument which does not have a quoted market price is estimated with regards to another instrument of similar characteristics or

based on future cash flows relevant to an investment asset (measurement at discounted cash flow method).

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

- impairment losses,
- foreign exchange differences gains and losses relevant to financial assets,
- interest calculated based on the effective interest rate method.

Dividends from equity instrument in AFS portfolio shall be recognized in profit or loss on the date that the Group's right to receive payment is established.

When a decline in the fair value of an available-for-sale financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized in other comprehensive income shall be transferred to profit or loss even though the financial asset has not been derecognized. The amount of the cumulative loss that is removed from revaluation reserve and recognized in profit or loss shall be the difference between the acquisition cost (net of any principal repayment and amortization) and current fair value, less any impairment loss on that financial asset previously recognized in profit or loss. Impairment losses recognized in profit or loss for an investment in an equity instrument classified as available for sale shall not be reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss shall be reversed, with the amount of the reversal recognized in profit or loss.

13.11. Impairment of non-financial non-current assets

The Group assesses at each balance sheet date whether there is any indication that an asset may be impaired. If any such indication exists, or if there is a need to perform an annual impairment testing, the Group estimates the recoverable amount of the asset or cash-generating unit.

Recoverable amount is defined as the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use. Recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. If the carrying value is higher than the recoverable value, an impairment loss is made. When estimating the value in use of an asset, future cash flows are discounted to the current value using a discount rate before tax, which represents current market estimation of time and risk relevant to an asset. Impairment loss relevant to assets used in continuing operations are reflected in costs relating to functions of an impaired asset.

The Group assesses at the end of each reporting period whether there is any indication that an impairment loss recognized in prior periods for an asset may no longer exist or may have decreased. If any such indication exists, the Group estimates the recoverable amount of that asset. An impairment loss recognized in prior periods for an asset other than goodwill shall be reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If this is the case, the carrying amount of the asset shall be increased to its recoverable amount. That increase is a reversal of an impairment loss. The increased carrying amount of an asset other than goodwill attributable to a reversal of an impairment loss shall not exceed the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss for an asset other than goodwill shall be recognized immediately in the profit or loss. After a reversal of an impairment loss is recognized, the depreciation (amortization) charge for the asset shall be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

13.12. Embedded derivatives

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract - with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative.

The Group verifies concluded and binding agreements in order to identify embedded derivatives.

An embedded derivative shall be separated from the host contract and accounted for as a derivative if, and only if:

- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract;
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and
- the hybrid (combined) instrument is not measured at fair value with changes in fair value recognized in profit or loss.

Embedded derivatives are recognized in a similar way as stand-alone derivatives which are not classified as hedging instruments.

According to IAS 39, the rule that economic characteristics and risk of an embedded derivative denominated in foreign currency are closely related to economic characteristics and risk of a host contract also includes the situation when the currency of the host contract is a custom currency for the trading contracts of non-financial positions on this derivative market.

A "stand-alone" embedded derivative is reflected in the statement of financial position at fair value, and changes in fair value are recognized in profit or loss.

The Group assesses at initial recognition whether the embedded derivative is to be a stand-alone instrument.

13.13. Derivatives and hedging instruments

The Group uses derivatives in order to hedge against the risk relevant to changes in interest rates and foreign exchange differences. The most frequently used derivatives are forward contracts and interest rate swaps. Such derivatives are designated at fair value. Depending on whether the value of a derivative or a hedge instrument is positive or negative, it can be recognized as a financial asset or financial liability respectively.

The gain or loss from change of values of the hedging instrument at fair value (for a derivative hedging instrument not qualifying for hedge accounting) shall be recognized directly in profit or loss.

The fair value of currency forward contracts is estimated with reference to current forward rates for contracts of similar maturity. Fair value of interest rate swaps is estimated with reference to the market value of similar financial instruments.

Hedge accounting recognizes three types of hedging relationships:

- fair value hedge: a hedge of the exposure to changes in fair value of a recognized asset or liability,
- cash flow hedge: a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with a recognized asset, liability or forecast transaction, or
- hedge of a net investment in a foreign operation.

A hedge of a foreign currency risk of a firm commitment is accounted for as a cash flow hedge.

At the inception of the hedge the Group is formally designating and documenting the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge. That documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the Group will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the

hedged risk. The hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship. The hedge is assessed on an ongoing basis throughout the financial reporting periods for which the hedge was designated to determine if it is effective.

13.14. Inventories

Inventories are assets:

- held for sale in the ordinary course of business;
- in the process of production for such sale; or
- in the form of materials or supplies to be consumed in the production process or in the rendering of services.

Inventories are measured at the lower of cost and net realizable value.

The cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

At initial recognition, inventories are measured as follows:

- Materials and merchandise – at purchase price,
- Finished goods, semi-finished products and production in progress – at the cost of manufacturing, comprising costs of direct materials and labor and a justified portion of indirect production costs.

Cost of usage of inventories is determined as follows:

- Materials and merchandise – at weighed average cost formula, however in case of representation and advertising materials and office supplies the expense can be recognized in profit or loss in the period when incurred.

As at the balance sheet date, the cost of inventories cannot be higher than net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

The inventories of the Group include purchased, intended for a further resale, greenhouse gases emission rights and equivalents of these. These assets are measured at purchase cost less possible impairment as at the balance sheet date. The cost of greenhouse gases emission rights shall be assigned by using specific identification.

13.15. Trade receivables

The recoverable amount of receivables is measured at least at each balance sheet date, i.e. in the nominal value increased by applicable penalty interest, in accordance with the principle of prudence, i.e. less applicable impairment losses.

The Group assesses at each balance sheet date whether there is any objective evidence that a receivable or a group of receivables is impaired. If a recoverable amount of the receivable is lower than the carrying amount, the amount of the impairment loss is measured as the difference between the carrying amount of the receivable and the present value of estimated future cash flows.

A write offs on a receivable is recognized in other operating expenses or financial expenses, depending on the relevant receivable.

Long-term receivables are measured at present (discounted) value.

13.16. Cash and cash equivalents

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

13.17. Other assets and short-term prepayments

The Group recognizes an asset as a short-term prepayment under the following conditions:

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

Prepayments are recognized in reliably measured amounts, which refer to future periods and will generate future economic benefits for the Group.

A prepayment is settled over time or in proportion to the value of goods and services provided. The period and method of the settlement is based on the characteristics of the relevant expenses, in accordance with the principle of prudence.

The entities review at each reporting year-end whether it is probable enough that future economic benefits relevant to a prepayment will flow to the Group, so that the prepayment can be recognized as an asset.

Purchased perpetual usufruct of land is recognized as an operating lease in accordance with IAS 17. The value of perpetual usufruct of land is recognized as other assets and is amortized over the lease term.

Perpetual usufruct of land acquired free of charge due to administrative decision is not recognized in the statement of financial position.

Other assets also comprise receivables from the state.

13.18. Equity

Equity is stated at nominal value, divided by kind, in accordance with law regulations and the Company's Articles of Association.

Share capital in the statement of financial position is stated at the value specified in the parent company's Articles of Association and as registered in the Court Register. Declared, but not yet brought in, share capital contributions are recognized as outstanding share capital contributions with a negative value.

13.19. Provisions

The Group creates a provision when the Group entities have a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and if a reliable estimate can be made of the amount of the obligation.

Provisions are reflected in profit or loss as operating expenses, other operating expenses or financial expenses, depending on relevant future obligations.

When the effect of the time value of money is material, the amount of a provision shall be the present value of the expenditures expected to be required to settle the obligation.

The discount rate (or rates) shall be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money and the risks specific to the liability. The discount rate(s) shall not reflect risks for which future cash flow estimates have been adjusted.

The following provisions are expected to be created in particular:

13.19.1 Provision for coal equivalent, medical benefits, Social Fund allowance and other retirement and pension benefits

The value of liabilities towards former employees is estimated on the basis of conditions of Corporate Collective Labor Agreements (Zakładowe Układy Zbiorowe Pracy) or other legal regulations. These liabilities result from employees' rights acquired during the employment period. The provision created is recognized in operating expenses in the amount corresponding with future employees' benefits.

13.19.2 Provision for cash equivalent related to energy tariff for employees of power industry

Based on the Inter-Corporate Collective Labor Agreement (Ponadzakładowy Układ Zbiorowy Pracy) changed in 2005, the Group entities are obliged to pay benefits, so called "energy tariff", to the former employees of the electric power engineering industry. Due to the above, since December 2005 the PGE Group entities create appropriate provisions.

The cost of the provision for entitled retirees, as at the day when the additional protocol to Inter-corporate Collective Labor Agreement became effective, was fully recognized in the statement of comprehensive income for the year ended 31 December 2005. The cost of past employment, relating to present employees but future retirees, is recognized on a straight-line basis over the average period until the benefits become vested. The value of the provision is estimated by an actuary. The cost of creating the provision is recognized in operating expenses.

13.19.3 Retirement and pension benefits and jubilee benefits

According to the institutional defined remuneration plan the employees of Group entities are entitled to receive jubilee, retirement and pension benefits. Jubilee benefits are paid after an employee has worked for a specified period of time. Retirement and pension benefits are paid once when the employee retires or becomes a pensioner. The amount of benefits paid depends on the period of working and the average remuneration of the employee. The Group recognizes a provision for future obligations relevant to retirement and pension benefits and jubilee benefits for the purpose of assigning costs to the periods in which they are incurred. According to IAS 19 jubilee benefits are classified as other long-term employee benefits, whereas the retirement and pension benefits are classified as post-employment benefits. The present value of these obligations is measured by an independent actuary at each balance sheet date. The ultimate cost of a defined benefit plan comprises discounted future payments, taking into account employee turnover, as at the balance sheet date. Demographic assumptions and employee turnover information are based on historical data. Actuarial gains and losses are recognized in profit or loss.

13.19.4 Provision for reclamation of post-exploitation grounds, including reclamation and development of final excavations and reclamation of ash storages

The mining companies which belong to the Group create provisions for reclamation costs of post-exploitation grounds. The value of the provision is based on the estimated cost of reclamation and development works related to final excavations. In case of mining excavations, the provision is created based on the proportion of the coal excavated to the total planned volume of excavation over the period of exploitation. The estimates of planned reclamation costs are updated at least once every 5 years; however at each year-end the amount of the reclamation provision is verified with regards to inflation rate, discount rate and the volume of excavation. The portion of the provision used in the given period is recognized in operating expenses, the difference resulting from discount of provision from previous years is reflected as financial income or expenses.

The cost of creating a provision for reclamation of ash storages (electricity post-production waste) is recognized in operating costs proportionally as the storage is filled, and the discount is recognized in financial expenses.

13.19.5 Provision for liabilities relating to greenhouse gas emissions.

The Company establishes a provision for liabilities relating to CO₂ emission deficits in the period in which it determines the existing allowances insufficient for covering the statutory obligations related to their redemption. The Company clears its emission allowances throughout the accounting period and establishes a provision as at the end of the given reporting period. That provision is presented in the short- and/or long-term part, depending on the anticipated time of utilization.

The provision is established in the amount corresponding to the most appropriate estimation of expenses necessary to fulfill the existing obligations as at the balance sheet date, particularly with regard to the allowances bought by the company to fulfill the obligation and possibly to cover any shortage with CER (Certified Emission Reductions).

Purchase of allowances to be used by the company for its own purposes does not reduce its liability relating to emission shortage until the date of physical release. The cost of established provision is presented among operating expenses in the statement of comprehensive income (cost of goods sold in the income statement by function of expense, other costs in the income statement by nature of expense).

The company updates the value of provision as at every consecutive balance date, taking into consideration the current prices of emission allowances and foreign exchange rate fluctuations if the price of emission allowances is presented in any other currency than PLN. Average rates of exchange of the National Bank of Poland as at the balance date apply to revaluation of the provision.

To meet the statutory requirements and redeem allowances obtained free of charges, or purchased if necessary, companies offset accruals existing as at the date of balance sheet redemption and provision for missing allowances.

13.20. Share-based payments

Share-based payments are a transfer of equity instruments of the Group or equivalents made by the Group or its shareholders to third parties (including employees), which provided the Group with goods or services, unless the transfer is made for a purpose different than the payment for goods and services supplied.

The Group recognizes the goods or services received or acquired in a share-based payment transaction as well as the corresponding increase in equity when it obtains the goods or as the services are received. When the goods or services received or acquired in a share-based payment transaction do not qualify for recognition as assets, they shall be recognized as expenses.

The Group measures the goods or services received, together with the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity shall measure their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

The cost of the equity instruments granted to the employees shall be recognized in the period from the grant date to the vesting date. The cost is measured at the fair value of equity instruments granted at the grant date. For transactions with employees and others providing similar services, the entity is required to measure the fair value of the equity instruments granted, because it is typically not possible to estimate reliably the fair value of employee services received. If applicable, the Group entities will take into account the terms and conditions upon which those equity instruments were granted when measuring the fair value. For goods or services measured by reference to the fair value of the equity instruments granted, vesting conditions, other than market conditions, shall not be taken into account when estimating the fair value of the shares or share options at the measurement date. Instead, vesting conditions are taken into account by adjusting the number of equity instruments included in the measurement of the transaction amount so that, ultimately, the amount recognized for goods or services received as consideration for the equity instruments granted is based on the number of equity instruments that eventually vest. The entity shall revise that estimate, if necessary, if subsequent information indicates that the number of equity instruments expected to vest differs from previous estimates.

For cash-settled share-based payment transactions, the entity shall measure the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, the entity shall remeasure the fair value of the liability at each balance sheet date and at the date of settlement, with any changes in fair value recognized in profit or loss for the period.

13.21. Profit-based payments for employees benefits and special funds

According to Polish industry practice, shareholders may distribute the entity's profit for employee benefits, such as: an increase of the Social Fund (ZFSS) or employee awards from profit. Such payments are reflected in statutory financial statements, similarly to dividend payments, as changes in equity. According to IFRS, profit distribution to the Social Fund or employee awards from profit are classified as operating expenses in the period for which the profit distribution took place.

13.22. Liabilities

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

Trade and other liabilities are stated at the amount due. When the effect of the time value of money is material, long-term liabilities are presented at the current (discounted) value.

A liability shall be classified as current when it satisfies any of the following criteria:

- it is expected to be settled in the Group's normal operating cycle;
- it is held primarily for the purpose of being traded;
- it is due to be settled within twelve months after the balance sheet date; or
- the entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the balance sheet date.

All other liabilities shall be classified as non-current.

If the Group expects, and has the discretion, to refinance or roll over an obligation for at least twelve months after the balance sheet date under an existing loan facility, it classifies the obligation as non-current, even if it would otherwise be due within a shorter period. However, when refinancing or rolling over the obligation is not at the discretion of the entity (for example, there is no agreement to refinance), the potential to refinance is not considered and the obligation is classified as current.

Some current liabilities, such as trade payables, are part of the working capital used in the entity's normal operating cycle. Such operating items are classified as current liabilities even if they are due to be settled more than twelve months after the balance sheet date.

13.23. The Social Fund

The Group is compensating liabilities and assets of the Social Fund and the Efficiency Improvement Fund. Such an arrangement reflects the relationship between the entity and the Funds, in which the entity is a trustee. This means, that the entity is legitimately entitled to the Funds' assets, however the Fund and its members are the beneficiaries.

13.24. Deferred income

Deferred income is recognized under the principle of prudence and the principle of simultaneous recognition of revenues and expenses. Deferred income comprises:

- equivalents of economical benefits received or due from business partners to be realized in subsequent reporting periods;
- cash obtained to finance acquisition or production of fixed assets, fixed assets under construction and development works, settled through other operating revenue in the amount of depreciation charges of non-current assets financed from this source. This also applies to partially redeemed loans and credits and donations the purpose of which is to acquire an item of property, plant and equipment and to finance the development works;
- property, plant and equipment and intangible assets acquired free of charge. Deferred income allowances are recognized in other operating revenues settled in line with depreciation charges of these assets;
- income relevant to sale and leaseback of property, plant and equipment and intangible assets. Deferred income allowances are reflected in other operating revenues throughout the period of the lease. If there is a high probability of the buy-out of the leased asset after the lease period and the lease period is significantly different from the economic useful life of the asset, then allowances on deferred income are recognized simultaneously with depreciation of the asset.

13.25. Emission rights

A provision for liabilities for gas emissions under the system of emission rights is created only when the actual emission and production plans indicate shortage of emission rights in the reporting period. The provision is created in the value of the most probable estimation of expenses essential to fulfill the obligation as at balance sheet date, in particular related to the emission rights acquired by the entity to cover the obligation and the possibility to cover part of the shortage with CER (Certified Emission Reductions).

The Group settles the shortage of emission rights on the basis of allocation of rights in the whole reporting period, in accordance with planned production and emissions.

When created, the provision is recognized in operating expenses.

13.26. Leases

A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred. At the commencement of the lease term, the lessees shall recognize finance leases as assets and liabilities in their statement of financial positions at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. Any initial direct costs of the lessee are added to the amount recognized as an asset. Classification of the lease is made at the initial recognition, based on the economic contents of the lease agreement. Minimum lease payments shall be apportioned between the finance charge and reduction of the outstanding liability. The finance charge shall be allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Financial costs shall be recognized in financial expenses in profit or loss throughout the lease term in the periods in which they are incurred.

An operating lease is a lease under which the lessor holds significant part of risks and rewards incidental to ownership of the asset. Lease payments under an operating lease shall be recognized as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

13.27. Taxes

Corporate income tax in the statement of comprehensive income comprises actual fiscal charges for the reporting period calculated by the Group entities in accordance with regulations of the Corporate Income Tax Act and a change in deferred tax assets and deferred tax liabilities not charged or credited directly to equity.

Deferred tax asset or deferred tax liability is calculated on the basis of temporary differences between the carrying amount of a given asset or liability and its tax base and tax loss possible for recovering in the future.

A deferred tax liability shall be recognized for all taxable temporary differences, except to the extent that the deferred tax liability arises from:

- the initial recognition of goodwill or the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss)
- taxable temporary differences associated with investments in subsidiaries, branches and associates, and interests in joint ventures in case of which the parent, investor or venturer is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

A deferred tax asset shall be recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized, unless the deferred tax asset arises from:

- the initial recognition of an asset or liability in a transaction that is not a business combination and at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss),

- deductible temporary differences associated with investments in subsidiaries, branches and associates, and interests in joint ventures in case of which a deferred tax asset shall be recognized to the extent that, and only to the extent that, it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized.

The carrying amount of a deferred tax asset shall be reviewed at each balance sheet date. An entity shall reduce the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit of part or all of deferred tax asset to be utilized. Any such reduction shall be reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Deferred tax assets are recognized only to the extent expected for the related amount attributable to negative temporary differences to be used to reduce taxable profits in the future and tax losses to be settled, recognizing the prudence principle. Deferred tax assets are recognized if, and only if, their utilization is probable.

The Group entities shall record deferred tax liabilities in the amount of income tax to be paid in the future due to positive temporary differences, i.e. differences which will result in increase of tax base in the future.

Deferred tax assets and liabilities shall be measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

13.28. Revenues

Revenue from sales is recognized when it is probable that the economic benefits associated with the sale transaction will flow to the Group and the amount of the revenue can be measured reliably. The revenue is recognized after deducting value added tax (VAT), excise tax and other sales-based taxes as well as discounts. When recognizing the revenue, the criteria specified below are also taken into account.

13.28.1 Revenues from sale of goods and merchandise

Revenues from the sale of goods and merchandise are recognized when the finished goods/merchandise are issued and related risks and rewards have been transferred and when the amount of revenue can be reliably measured and costs incurred can be reliably estimated.

Revenues from sale of goods and merchandise include:

- amounts receivable from wholesale and retail sale of: electricity, heat energy, lignite, certificates of origin of energy from renewable energy sources, certificates of production of energy in high efficiency cogeneration plants, emission rights and rendered services relevant to core business operations based on the net price, less applicable discounts, rebates and excise tax,
- amounts receivable from sales of materials and merchandise based on the net price, less applicable discounts and rebates.

13.28.2 Revenues from services rendered

When the outcome of a transaction involving the rendering of long-term services can be estimated reliably, revenue associated with the transaction shall be recognized by reference to the stage of completion of the transaction at the balance sheet date less the revenues which influenced the previous reporting periods. Depending on the class of transaction, the stage of completion of the transaction can be recognized on the basis of:

- surveys of work performed;
- services performed to date as a percentage of total services to be performed; or
- the proportion of costs incurred to a given date to the estimated total costs of the transaction. Only costs that reflect services performed to date are included in costs incurred to date. Only costs that

reflect services performed or to be performed are included in the estimated total costs of the transaction.

When the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenue shall be recognized only to the extent of the expenses recognized that are recoverable.

13.28.3 Revenues from LTC compensations.

In accordance with the Act on rules of covering producers' costs related to early termination of long-term agreements for the sales of electric power and energy (LTC) dated 29 June 2007, the entities of the PGE Capital Group receive compensations in the form of quarter advances to cover stranded costs. The annual adjustment is made after the end of each year and the final adjustment is made after the termination of LTC.

The Group entities as revenue of the period recognize, received as advances, cash, corrected by annual adjustment and adequately part of planned final adjustment. The allocation of final adjustment to the particular period is conducted based on the planned revenues from sales of electric power and energy and sales of system services in the period of adjustment and taking into consideration the final adjustment. The discount is calculated on the basis of intermediate risk-free rate.

13.28.4 Revenues from sales of electricity through Electricity Trading Platform

During the reporting period, The Capital Group entity, Elbis Sp. z o.o., ran business activity related to electricity trading on Internet Electricity Trading Platform ("POEE"). The Platform is designed to conclude contracts for purchase or sale of electric energy, energy origin units of ownership and CO2 emission rights.

Due to the fact, that trading on POEE was made mostly automatically and the Group was exposed to a limited transactional and credit risk related to these business activities, revenues and expenses related to products purchased and sold through POEE are not reflected in the consolidated statement of comprehensive income. The consolidated revenues and expenses include only the fee related to concluding transactions through POEE.

13.29. Expenses

13.29.1 Cost of goods sold

Cost of goods sold includes:

- production costs incurred in the reporting period with adjustments related to changes in inventories (finished goods, semi-finished products and production in progress) and costs relevant to production of goods for the Group's own use,
- value of electricity sold and materials at purchase prices,
- impairment losses on property, plant and equipment, intangible assets and receivables,
- distribution and selling expenses as well as general and administrative expenses incurred in the reporting period (reflected separately in the statement of comprehensive income).

Production costs that can be directly assigned to revenues recognized by the entities influence the profit or loss for the reporting period in which they were incurred.

Production costs that can only be indirectly assigned to revenues or other economic benefits recognized by the entities, influence the profit or loss in the portion they are relevant to the given reporting period, under the principle of matching of expenses and revenue or other economic benefits and the rules of measurement of property, plant and equipment and inventories.

13.30. Other operating revenues and expenses

Other operating expenses and revenues include in particular:

- profit or loss on disposal of property, plant and equipment and intangible assets,
- reversal or creation of write offs, except from write offs related to financial operations or reflected in cost of goods sold,
- acquiring or disposal of assets and cash free of charge, including donations,
- due and obtained compensations, penalties and other expenses not relating to core operations.

13.31. Financial revenues and expenses

Financial revenues and expenses include in particular gains or losses relating to:

- disposal of financial assets, investment property and investment in entities not consolidated,
- revaluation of financial instruments, except from financial assets available for sale, the result of which is reflected in revaluation reserve,
- share of profits of other entities,
- interest,
- changes in provisions related to the approaching incurrence of the expense (unwinding of the discount effect),
- foreign exchange differences resulting from operations performed during the reporting period and measurement of the carrying amount of assets and liabilities at the balance sheet date, except for the foreign exchange differences recognized in the initial value of a non-current asset, to the extent they are recognized as an adjustment to interest costs and foreign exchange differences relevant to valuation of financial instruments classified to AFS portfolio,
- other operations relevant to financial operations.

Revenues and expenses from interest shall be recognized over the relevant period using the effective interest method relating to the carrying amount of a given financial instrument under the principle of materiality. Dividends are recognized when the shareholders' right to receive payments is established.

13.32. Earnings per share

Net earnings per share for each period are calculated by dividing the net profit for a given period allocated to shareholders of the parent company by the weighted average number of shares during that period.

13.33. Cash flow statement

Cash flows shall be prepared using the indirect method.

13.34. Changes in accounting policy and data presentation

IFRIC 18 *Transfers of Assets from Customers*

The purpose of the implementing IFRIC 18 *Transfers of Assets from Customers* was to unify the applied accounting practice in the situation of receiving from customers non-current assets or cash and cash equivalents for construction of non-current assets. The new interpretation have a significant meaning for distribution companies of the PGE Group in relation to the recognition of so-called connection payments or network terminals. According to accounting principles (policies) applied by the Group, the above matter is recognized analogically to the recognition of government donations in compliance with IAS 20, i.e. the value of the assets received is reflected as deferred income and then recognized in profit and loss statement over time in line with the estimated economic useful life of an item of a property, plant and equipment. According to the new IFRIC 18, starting from 1 July 2009 new connection payments charged by distribution companies are recognized directly in revenues. Connection payments received before 1 July 2009 are recognized in profit and loss account under hitherto existing rules.

IFRIC 18 gives companies the choice how to book the assets received before 1 July 2009. The Group decided that the connection fees received before 1 July 2009 will be recorded in the profit and loss account under the previous rules. Applying the IFRIC 18 from 1 January 2010 the Group has revised the recognition of connection fees received between 1 July 2009 and 31 December 2009, which resulted in an increase of consolidated equity of PLN 26.900 thousand

IAS 24 *Related Party Disclosures*

The parent company is controlled by the State Treasury and according to IAS 24 *Related Party Disclosures* presents the value of transactions with other State Treasury controlled entities in the financial statements. PGE Capital Group decided for the earlier application of revised IAS 24 from 1 January 2010.

Revised IAS 24 allows in particular (under the specified conditions) a significant limitation of recognizing other subsidiaries of the State Treasury as related parties. The amendment of IAS 24 did not have significant impact on the extent and detail of the disclosed Group's information about related parties.

Change of presentation in some captions of liabilities and short-term provisions

During the reporting period the Group changed the presentation of some captions of liabilities and short-term provisions. Due to the above the Group restated the data presented in a comparative consolidated cash flow as presented below:

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Period ended 31 December 2009 (data approved)	Change of liabilities and short-term provisions presentation principles	Period ended 31 December 2009 (restated)
Short-term liabilities			
Trade liabilities	1.082.582	-	1.082.582
Financial liabilities at fair value through profit or loss	37.701	-	37.701
Interest-bearing loans and borrowings	969.929	-	969.929
Other short-term financial liabilities	555.758	10.813	566.571
Other short-term non-financial liabilities	1.167.079	30.750	1.197.829
Income tax liabilities	372.888	-	372.888
Deferred income	40.903	-	40.903
Accruals	627.558	(627.558)	-
Short-term provisions	981.326	585.995	1.567.321
Total short-term liabilities	5.835.724	-	5.835.724

CONSOLIDATED STATEMENT OF CASH FLOWS

	Period ended 31 December 2009 (data approved)	Change of liabilities and short-term provisions presentation principles	Period ended 31 December 2009 (restated)
Cash flows – operating activities			
Gross profit related to continuing operations	5.378.534	-	5.378.534
Adjustments for:			
Share of profit from associates accounted for under the equity method	(242.157)	-	(242.157)
Depreciation and amortization	2.638.676	-	2.638.676
Interest and dividend, net	248.924	-	248.924
Difference between fair value and carrying amount of dividends in kind paid	-	-	-
Profit / (loss) on investment activities	(71.623)	-	(71.623)
Change in receivables	(495.567)	-	(495.567)
Change in inventories	(141.809)	-	(141.809)
Change in liabilities (excluding loans and bank credits)	137.915	41.563	179.478
Change in prepayments and accruals	45.814	(627.558)	(581.744)
Change in provisions	337.507	585.995	923.502
Income tax paid	(491.352)	-	(491.352)
Other	(45.974)	-	(45.974)
Net cash from operating activities	7.298.888	-	7.298.888

For the purpose of comparability, the Group has also restated data presented in Notes 35, 36 and 42 to the foregoing financial statements.

14. Operating segments

The Group presents the business segment in accordance with IFRS 8 *Operating segments* for the current and comparative reporting period. The Group reporting is based on business segments:

- Conventional Energy includes exploration and mining of lignite and production of energy in the Group power plants and heat and power plants;
- Wholesale includes trade in electricity on the wholesale market, trading of emissions certificates and property rights related to energy origin units of ownership and fuel trading;
- Retail sale includes sale of electricity and rendering services to end users;
- Distribution includes management over local distribution networks and delivery of electricity with the use of these networks;
- Renewable Energy includes generation of energy in pumped storage power plants and from renewable sources.

Organization and management over the Group is based on the division into segments, taking into account the nature of the products and services. Each segment represents a strategic business unit, offering different products and serving different markets.

Transactions between segments are settled within the Group as if they were concluded with third parties – under market conditions.

Additionally, the Group presents geographical areas of its activities, however these do not constitute for operating segments.

Information on business segments

Period ended 31 December 2010	Segment: Conventional energy	Segment: Renewable energy	Segment: Wholesale	Segment: Distribution	Segment: Retail sale	Other activities	Inter-segment eliminations	Total continued operations
Revenues								
Revenues from sales to external	2.333.766	475.403	4.739.356	671.265	11.497.748	758.927		20.476.465
Revenues from sales between	9.953.684	155.735	7.066.469	4.393.675	966.846	953.933	(23.490.342)	
Total revenues from segments	12.287.450	631.138	11.805.825	5.064.940	12.464.594	1.712.860	(23.490.342)	20.476.465
Financial result								
EBIT *)	2.981.692	153.981	173.119	566.722	204.472	96.462	8.885	4.185.333
EBITDA **)	4.476.484	280.229	202.394	1.441.230	213.519	206.941	13.229	6.834.026
Net financial revenues (expenses)								(136.102)
Share of profit of associates								227.019
Profit (loss) before tax								4.276.250
Income tax								(673.400)
Net profit (loss) for the reporting year								3.602.850
Assets and liabilities								
Assets of the segment	26.906.296	1.719.471	636.581	13.557.306	1.633.656	1.111.755		45.565.065
Shares in associates	9.740					1.398.725		1.408.465
Unallocated assets								4.500.409
Total assets								51.473.939
Liabilities of the segment	5.062.369	113.954	730.960	2.252.812	1.103.752	280.890	(10.394)	9.534.343
Unallocated liabilities								4.256.823
Total liabilities								13.791.166
Other information on business segments								
Capital expenditure	3.818.752	191.844	20.665	1.054.043	24.554	213.174		5.323.032
Amortization, depreciation and revaluation write-offs	1.475.429	109.464	29.701	874.564	10.708	114.067		2.613.933
Other non-monetary expenses	337.419	1.353	20.245	29.826	171.031	8.051		567.925

*) EBIT = profit (loss) before tax and financial revenues / expenses

**) EBITDA = EBIT + amortization (without write-offs)

Consolidated financial statements for the year ended 31 December 2010 prepared in accordance with IFRS (all amounts in PLN thousand)

("Translation of the document originally issued in Polish")

Period ended 31 December 2009	Segment: Conventional energy	Segment: Renewable energy	Segment: Wholesale	Segment: Distribution	Segment: Retail sale	Other activities	Inter-segment eliminations	Total continued operations
Revenues								
Revenues from sales to external	3.090.844	423.332	5.488.306	365.284	11.421.824	833.760		21.623.350
Revenues from sales between	10.298.008	123.824	7.234.681	4.303.441	920.885	1.005.776	(23.886.615)	
Total revenues from segments	13.388.852	547.156	12.722.987	4.668.725	12.342.709	1.839.536	(23.886.615)	21.623.350
Financial result								
EBIT *)	4.026.302	77.603	439.397	263.244	397.681	135.478	5.024	5.344.729
EBITDA **)	5.550.230	202.992	464.982	1.093.218	404.747	254.992	12.245	7.983.406
Net financial revenues (expenses)								(208.352)
Share of profit of associates								242.157
Profit (loss) before tax								5.378.534
Income tax								(1.041.311)
Net profit (loss) for the reporting year								4 337 223
Assets and liabilities								
Assets of the segment	24.938.010	1.636.100	823.247	13.396.376	1.497.681	1.039.535		43.330.949
Shares in associates	9.564					1.345.235		1.354.799
Unallocated assets								9.762.050
Total assets								54.447.798
Liabilities of the segment	4.597.364	100.371	702.048	2.220.270	953.443	265.107		8.838.603
Unallocated liabilities								6.759.443
Total liabilities								15.598.046
Other information on business segments								
Capital expenditure	2.484.302	91.557	13.123	993.119	6.901	136.603		3.725.605
Amortization, depreciation and revaluation write-offs	1.510.696	125.807	22.749	831.943	28.651	123.175		2.643.021
Other non-monetary expenses	452.733	1.968	55.722	34.216	21.047	(24.521)		541.165

*) EBIT = profit (loss) before tax and financial revenues / expenses

**) EBITDA = EBIT + amortization (without write-offs)

Information on geographical areas

Period ended 31 December 2010.

Revenues	Domestic market	EU countries	Other countries	Total
Revenues from continuing operations	19.887.231	572.098	17.136	20.476.465
Revenues from discontinued operations				
Total revenues	19.887.231	572.098	17.136	20.476.465
Sales between areas	23.490.342			23.490.342
Revenues from the area	43.377.573	572.098	17.136	43.966.807
Other information on the area	Domestic market	EU countries	Other countries	Total
Assets of the area	45.562.361	2.704		45.565.065
Unallocated assets	4.486.683	13.726		4.500.409
Investments in associates	1.408.465			1.408.465
Total assets	51.457.509	16.430	-	51.473.939

Period ended 31 December 2009.

Revenues	Domestic market	EU countries	Other countries	Total
Revenues from continuing operations	21.144.799	459.261	19.290	21.623.350
Revenues from discontinued operations	-	-	-	-
Total revenues	21.144.799	459.261	19.290	21.623.350
Sales between areas	23.886.615	-	-	23.886.615
Revenues from the area	45.031.414	459.261	19.290	45.509.965
Other information on the area	Domestic market	EU countries	Other countries	Total
Assets of the area	43.324.654	6.295	-	43.330.949
Unallocated assets	9.744.144	17.876	-	9.762.050
Investments in associates	1.354.799	-	-	1.354.799
Total assets	54.423.627	24.171	-	54.447.798

15. Revenues and expenses

15.1. Sales revenues

	Period ended 31 December 2010	Period ended 31 December 2009
Revenues from operating activities		
<i>Sales of finished goods and merchandise with excise tax</i>	19.758.510	19.760.013
<i>Excise tax</i>	(451.932)	(568.496)
Revenues from sale of finished goods and merchandise	19.306.578	19.191.517
Revenues from sale of services	805.398	879.533
Revenues from lease	30.276	19.953
Revenues from LTC compensations	334.213	1.532.347
Total sales revenues	20.476.465	21.623.350

During the comparable period the change of the excise tax act took place. Until March 2009 the excise tax was paid by the producers of electric energy and according to the changed act the excise tax is to be paid by the entities delivering the electric energy to final customers.

15.2. Costs by kind and functions

Costs by kind	Period ended 31 December 2010	Period ended 31 December 2009
Depreciation/ amortization	2.648.692	2.638.676
Materials and energy	3.755.518	3.689.128
External services	2.555.627	2.692.425
Taxes and charges	2.031.139	1.688.109
Personnel expenses	4.071.337	3.865.505
Other cost by kind	475.452	385.419
Total costs by kind	15.537.765	14.959.262
Change in inventories	(130.251)	(85.664)
Cost of products and services for the entity's own needs	(952.567)	(938.935)
Distribution and selling expenses	(1.527.718)	(1.368.079)
General and administrative expenses	(950.702)	(914.109)
Cost of merchandise and materials sold	2.095.013	2.074.994
Cost of goods sold	14.071.540	13.727.469

15.3. Other operating revenues and expenses

	Period ended 31 December 2010	Period ended 31 December 2009
Other operating revenues		
Profit on disposal of property, plant and equipment and intangible assets	12.311	20.140
Reversal of revaluation write offs on receivables	23.021	32.281
Reversal of revaluation write offs on other assets	17.537	52.364
Provisions reversed	356.931	71.311
Compensations, penalties and fines received	158.257	47.583
Donations received	10.116	9.506
Taxes refunded	11.024	5.700
Court fees refunded	2.272	2.442
Redemption of liabilities	407	1.279
Assets acquired free of charge	1.828	2.122
Re-invoiced revenues	15	236
Change of valuation of recultivation provision	-	131.392
Surpluses / disclosures of assets	15.687	-
Profit on subsidiaries disposal	27.858	-
Other	29.139	46.212
Total other operating revenues	666.403	422.568
Other operating expenses		
Creation of revaluation write offs on receivables	58.840	84.971
Creation of revaluation write offs on other assets	4.461	7.044
Loss on disposal of property, plant and equipment and intangible assets	8.508	9.415
Provisions created	121.432	438.872
Donations granted	6.367	5.272
Compensations	7.995	5.213
Court fees paid	5.877	6.531
Liquidation of damages/ removal of failures	108.331	33.098
Liquidation of non-current assets	54.931	53.330
Redemption of receivables	3.009	9.419
Costs of social activities	6.528	7.114
Compensations resulting from shares not received	8.336	-
Other	12.960	31.253
Total other operating expenses	407.575	691.532

15.4. Financial revenues and expenses

	Period ended 31 grudnia 2010	Period ended 31 December 2009
Financial revenues		
Financial revenues from financial instruments	400.908	344.384
Dividends	8.437	12.497
Interest revenue	305.726	163.046
Revaluation/ reversal of revaluation write offs	31.195	33.088
Profit on disposal of investments	3.649	65.299
Foreign exchange gains	51.901	70.454
Other financial revenues	21.207	27.881
Discount rate adjustment	74	4.742
Interest on state receivables	4.363	12.699
Provisions reversed	12.777	884
Other	3.993	9.556
Total financial revenues	422.115	372.265
Financial expenses		
Financial expenses from financial instruments	329.409	391.749
Interest expenses	189.620	285.136
Revaluation	3.772	32.090
Impairment losses	52.511	15.301
Loss on disposal of investments	186	350
Foreign exchange losses	83.320	58.872
Other financial expenses	228.808	188.868
Interest expenses (effect of discount unwinding)	169.308	155.106
Interest paid relating to state liabilities	2.457	5.759
Provisions created	13.910	-
Other	43.133	28.003
Total financial expenses	558.217	580.617

15.5. Depreciation costs and impairment losses in the profit and loss account

	Period ended 31 December 2010	Period ended 31 December 2009
Included in cost of goods sold:	2.573.588	2.554.949
Property, plant and equipment depreciation	2.525.246	2.503.424
Revaluation write offs on property, plant and equipment	4.730	7.244
Intangible assets amortization	43.483	43.257
Other	129	1.024
Included in distribution and selling expenses:	15.203	17.589
Property, plant and equipment depreciation	12.655	14.631
Intangible assets amortization	2.548	2.958
Included in general and administrative expenses:	55.598	60.163
Property, plant and equipment depreciation	45.814	52.039
Intangible assets amortization	9.238	7.826
Revaluation write off on property, plant and equipment	303	32
Other	243	266
Included in change in inventories, goods, prepayments and accruals	1.930	3.345
Included in costs of products and services for the entity's own use	2.373	2.630

16. Employee benefits expenses

	Period ended 31 December 2010	Period ended 31 December 2009
Payroll	3.036.584	2.848.806
Social security expenses	535.364	500.117
Retirement and pensions costs	9.553	14.634
Jubilee benefits and allowances	75.214	60.620
Other post-employment benefits	47.078	39.408
Other payroll-related expenses	367.544	401.920
Total employee benefits expenses:	4.071.337	3.865.505
Included in costs of goods sold	3.116.160	3.008.658
Included in distribution and selling expenses	233.584	236.158
Included in general and administrative expenses	565.127	567.505
Included in costs of products and services for the entity's own use	143.753	120.331
Change in inventories	12.713	(67.147)

17. Income tax

17.1. Tax disclosed in the statement of comprehensive income

Main elements of income tax expense for the period ended 31 December 2010 and for the period ended 31 December 2009 are as follows:

	Period ended 31 December 2010	Period ended 31 December 2009
Consolidated profit and loss account		
Current income tax	718.742	726.934
Current income tax expense	712.520	716.916
Previous periods' current income tax adjustments	6.222	10.018
Deferred income tax related to temporary differences created and reversed	(45.342)	314.377
Income tax expense as in the consolidated profit and loss account	673.400	1.041.311
Income tax expenses presented in discontinued operations	5.434	-
Other comprehensive income		
Deferred income tax on unrealized profit / (loss) from financial assets available for sale	19	(9.685)

A reconciliation of the calculation of income tax on profit before tax at the statutory tax rate and income tax calculated according to the effective tax rate for the Capital Group for the years ended 31 December 2010 and 31 December 2009 is as follows:

	Period ended 31 December 2010	Period ended 31 December 2009
Gross profit before tax from continued operations	4.276.250	5.378.534
Gross profit before tax from discontinued operations	29.671	-
Gross profit/(loss) before tax	4.305.921	5.378.534
Income tax according to Polish statutory tax rate of 19%	818.125	1.021.921
Previous periods current income tax adjustments	6.222	10.018
Costs not classified as tax-deductible costs	77.415	94.526
Non-taxable revenues	(103.908)	(87.788)
Reversal of the deferred tax assets write-offs	(130.648)	-
Other	11.628	2.634
Tax at effective tax rate amounting to 15,9% [2009: 19,4%]	678.834	1.041.311
Income tax (expense) as presented in consolidated statement of comprehensive income	673.400	1.041.311
Income tax attributable to discontinued operations	5.434	-

The effective tax rate of 15,9% in 2010 resulted mainly from the reversal of write-offs revaluating the value of deferred income tax of provision for recultivation of excavations in brown coal mines (the issue is presented in note 17.2 to the foregoing financial statement).

17.2. Deferred tax disclosed in consolidated statement of financial position

Components of deferred tax liability

	Consolidated statement	
	As at 31 December 2010	As at 31 December 2009
1996-2000 investment relief	921	922
Difference between tax value and carrying amount of property, plant and equipment	1.520.852	1.556.111
Accrued interest on deposits, loans granted, bonds and receivables	31.385	27.371
Difference between tax value and carrying amount of other financial assets	601	9.334
Difference between tax value and carrying amount of financial liabilities	24.967	36.055
Current period revenues unrealized for tax purposes	11.458	46.762
Difference between tax value and carrying amount of energy origin units of ownership	36.576	21.660
Revenues from accrued LTC compensations	423.392	351.219
Other	207.349	62.884
Gross deferred tax liability	2.257.501	2.112.318

Components of deferred tax asset

	Consolidated statement	
	As at	As at
	31 December 2010	31 December 2009
Difference between tax value and carrying amount of property, plant and equipment	118.116	117.928
Current period costs not realized for tax purposes	5.099	15.347
Provisions for employee benefits	390.825	370.903
Provisions for recultivation of excavations and recultivation of ash storages	163.187	159.966
Accruals for employee bonuses	21.046	19.369
Difference between tax value and carrying amount of financial assets	41.841	40.728
Difference between tax value and carrying amount of financial liabilities	20.455	14.630
Difference between tax value and carrying amount of inventories	25.094	23.261
Payroll and other employee benefits	18.259	29.861
Tax losses	-	15.349
Energy infrastructure acquired free of charge and connection payments received	183.151	180.099
Provision for purchase of CO ₂ emission rights	61.320	82.835
Other provisions	58.107	96.728
Other	242.859	129.769
Gross deferred tax asset	1.349.359	1.296.773
Revaluation write off on tax asset	-	130.648
Net deferred tax asset	1.349.359	1.166.125
After compensation of balances at the Group companies' level the deferred tax of the Group is presented as:		
Deferred tax asset	286.621	412.353
Deferred tax liability	(1.194.763)	(1.358.546)

As described in note 11 to the foregoing financial statements, during the preceding reporting periods brown coal mines incorporated in PGE Group recognized deferred tax asset related to raise of provision for recultivation of excavations, as these costs were expected to incur after the end of mine exploitation i.e. after the period of generating revenues by these companies. As a result of merger of mines companies with energy producers within PGE Górnictwo i Energetyka Konwencjonalna S.A. future costs of recultivation have been recognized as probable tax gains. Therefore during the present reporting period the Group reversed a write off of deferred tax asset in the amount of PLN 130 million.

18. Non-current assets classified as held for sale

PGE Górnictwo i Energetyka Konwencjonalna S.A. presents in the balance sheet, the non-current assets classified as held for sale. Non-current assets classified as held for sale include mainly the Holiday Resort in Niedzica (Ośrodek Wczasowo-Wypoczynkowy) and packages of stock and shares in companies not included in consolidated financial statement of PGE Capital Group.

	As at 31 December 2010	As at 31 December 2009
Assets		
Intangible assets	-	-
Property, plant and equipment	3.028	5.712
Stock and shares classified as held for sale	4.544	
Non-current assets classified as held for sale	7.572	5.712
Liabilities directly associated with non-current assets classified as held for sale	-	-
Net assets/liabilities classified as held for sale	7.572	5.712

19. Discontinued operations

During the year ended 31 December 2010 the parent company and key subsidiaries did not discontinue any significant operations. However, a "Non-core" Programme is being implemented at PGE Group (as described in Note 45.4 to these financial statements), whereunder assets which are not closely related to core business are sold.

As discontinued operations the Group has disclosed in the consolidated statement of comprehensive income for the year ended 31 December 2010 the financial results of:

- net profit/loss of subsidiaries which were sold during the reporting period, namely: PW Agtel Sp. z o.o., GKS Bełchatów S.S.A., TG BEWA Sp. z o.o., and Energo-Inwest Broker S.A.;
- subsidiaries, which as at 31 December 2010 meet the group criteria of entities for sale, according to the definition contained in IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*: Budownictwo Hydroenergetyka - Dychów Sp. z o.o., and Pracownia Projektowa ENSPRO Sp. z o.o.;
- business related to trading of electricity on the Warsaw Stock Exchange Energy Market ("WSEEM"), which was sold on 10 December 2010.

In the consolidated financial statements the result on sales of subsidiaries amounted to PLN 27.858 thousand and the result on sale of WSEEM amounted to PLN 14.539 thousand.

The amounts related to the discontinued operations are presented in the table below:

	Revenues	Expenses	Gross profit	Income tax	Net profit
PW Agtel Sp. z o.o.	8.472	8.668	(196)	-	(196)
GKS Bełchatów S.S.A.	8.990	7.142	1.848	-	1.848
TG BEWA Sp. z o.o.	43.725	41.688	2.037	391	1.646
Energo-Inwest Broker S.A.	28.018	21.036	6.982	1.397	5.585
BH Dychów Sp. z o.o.	80.146	78.287	1.859	389	1.470
PP ENSPRO Sp. z o.o.	2.076	1.795	281	54	227
WSEEM	89.609	72.749	16.860	3.203	13.657
TOTAL	261.036	231.365	29.671	5.434	24.237

The participation of shareholders of the parent company in the net result attributable to discontinued operations amounted to PLN 17.165 thousand, in 2010.

In 2009, the financial results of the particular companies were as follow:

	Revenues	Expenses	Gross profit	Income tax	Net profit
PW Agtel Sp. z o.o.	23.718	24.207	(489)	36	(525)
GKS Bełchatów S.S.A.	32.568	35.616	(3.048)	564	(3.612)
TG BEWA Sp. z o.o.	72.352	69.730	2.622	735	1.887
Energo-Inwest Broker S.A.	25.293	18.459	6.834	1.427	5.407
BH Dychów Sp. z o.o.	26.956	26.376	580	124	456
PP ENSPRO Sp. z o.o.	2.165	1.911	254	47	207
WSEEM	83.396	71.755	11.641	-	11.641
TOTAL	266.448	248.054	18.394	2.933	15.461

The participation of shareholders of the parent company in the net result attributable to discontinued operations amounted to PLN 10.397 thousand, in 2009.

Assets and liabilities related to discontinued operations and presented in the statement of financial position as at 31 December 2010 are assets and liabilities of Hydroenergetyka - Dychów Sp. z o.o. and Pracownia Projektowa ENSPRO Sp. z o.o.

	BH Dychów	PP ENSPRO	Total
Assets	34.084	1.633	35.717
Intangible assets	17	-	17
Property, plant and equipment	4.431	39	4.470
Deferred tax assets	505	70	575
Tangible assets related to the discontinued operations	4.953	109	5.062
Inventories	1.317	-	1.317
Trade receivables	21.170	125	21.295
Other loans and financial assets	127	-	127
Other current assets	2.845	46	2.891
Cash and cash equivalents	3.672	1.353	5.025
Current assets related to the discontinued operations	29.131	1.524	30.655
Liabilities	27.790	425	28.215
Long-term provisions	580	264	844
Deferred tax liabilities	107	-	107
Other liabilities	415	-	415
Long-term liabilities related to discontinued operations	1.102	264	1.366
Trade liabilities	19.091	12	19.103
Other financial liabilities	659	1	660
Other non-financial liabilities	5.272	43	5.315
Deferred income	550	-	550
Short-term provisions	1.116	105	1.221
Short-term liabilities related to discontinued operations	26.688	161	26.849

As at 31 December 2009 total assets of companies mentioned above amounted to PLN 13.528 thousand and the sum of its liabilities amounted to PLN 7.437 thousand.

20. Assets and liabilities of the Social Fund

The Social Fund Act of 4 March 1994 states that a social fund is created by employers employing over 20 full time employees. The Group entities create such a fund and perform periodical write offs. The fund does not possess any property, plant and equipment. The goal of the fund is to subsidize the social activity for employees of the Group, loans granted to its employees and other social expenses.

The Group entities compensated the Fund's assets with liabilities as the Fund's assets do not constitute the assets of the Capital Group.

As at 31 December 2010, assets assigned to the social fund in the Capital Group amounted to PLN 180.772 thousand and as at 31 December 2009, PLN 191.105 thousand.

21. Property, plant and equipment

31 December 2010	Land	Buildings and construction	Machinery and equipment	Means of transport	Other property, plant and equipment	Construction in progress	Total
Gross book value							
Opening balance	191.919	21.232.633	23.997.864	324.109	495.619	5.200.405	51.442.549
Direct purchase	546	13.953	19.999	1.002	88.796	5.097.990	5.222.286
Transfer from construction in progress	11.480	936.621	1.954.163	45.814	32.877	(2.980.955)	-
Sales/ disposals	(1.552)	(42.688)	(27.682)	(6.522)	(29.824)	(248)	(108.516)
Transfers between groups	(16.429)	(148)	17.656	(940)	(139)	-	-
Donations and transfers free of charge	19	6.666	(88)	-	(465)	-	6.132
Liquidations	(2.005)	(56.386)	(495.884)	(1.728)	(5.840)	(245)	(562.088)
Transfer to discontinued operations	-	(970)	(3.963)	-	(3.654)	-	(8.587)
Other	848	(1.214)	(44.211)	3.520	(23.681)	41.267	(23.471)
Closing balance	184.826	22.088.467	25.417.854	365.255	553.689	7.358.214	55.968.305
Depreciation and revaluation write-offs							
Opening balance	15.998	4.474.661	7.546.991	136.577	308.313	14.345	12.496.885
Depreciation for the period	3.390	981.658	1.524.019	33.534	45.646	-	2.588.247
Increase of impairment losses	-	7.006	847	436	20	706	9.015
Decrease of impairment losses	-	(15.346)	(5.024)	-	-	(659)	(21.029)
Sales/ disposals	(307)	(13.941)	(15.539)	(6.105)	(7.666)	-	(43.558)
Transfers between groups	(2.949)	17	3.457	(436)	(89)	-	-
Donations and transfers free of charge	-	(2)	(99)	-	(455)	-	(556)
Liquidation	(114)	(23.821)	(455.053)	(1.601)	(5.154)	-	(485.743)
Transfer to discontinued operations	-	(348)	(2.135)	-	(2.272)	-	(4.755)
Other	63	13.102	(14.680)	1.710	(12.577)	-	(12.382)
Closing balance	16.081	5.422.986	8.582.784	164.115	325.766	14.392	14.526.124
Opening balance net book value	175.921	16.757.972	16.450.873	187.532	187.306	5.186.060	38.945.664
Closing balance net book value	168.745	16.665.481	16.835.070	201.140	227.923	7.343.822	41.442.181

31 December 2009	Land	Buildings and construction	Machinery and equipment	Means of transport	Other property, plant and equipment	Construction in progress	Total
Gross book value							
Opening balance	180.927	20.391.399	22.654.337	292.774	429.653	4.030.688	47.979.778
Direct purchase	194	22.301	33.673	499	51.178	3.553.821	3.661.666
Transfer from construction in progress	11.743	894.942	1.472.250	37.211	26.491	(2.442.637)	-
Sales/ disposals	(1.119)	(11.473)	(30.658)	(5.110)	(35.252)	(261)	(83.873)
Transfers between groups	(3.583)	909	1.443	4	1.227	-	-
Donations and transfers free of charge	(113)	12.010	394	-	(11)	-	12.280
Liquidations	(146)	(73.794)	(149.409)	(886)	(3.510)	(3.733)	(231.478)
Other changes of values	4.016	(3.661)	15.834	(383)	25.843	62.527	104.176
Closing balance	191.919	21.232.633	23.997.864	324.109	495.619	5.200.405	51.442.549
Depreciation and revaluation write offs							
Opening balance	10.768	3.592.017	6.190.632	109.217	247.154	18.421	10.168.209
Depreciation for the period	3.214	960.951	1.535.242	31.233	45.466	-	2.576.106
Increase of impairment losses	-	1.762	6.209	32	-	3.094	11.097
Decrease of impairment losses	-	(32.997)	(18.003)	-	-	(940)	(51.940)
Sales/ disposals	(122)	(7.099)	(20.323)	(3.155)	(7.127)	-	(37.826)
Transfers between groups	(879)	233	193	294	159	-	-
Donations and transfers free of charge	(3)	-	(102)	-	(9)	-	(114)
Liquidation	-	(44.884)	(123.750)	(687)	(2.591)	-	(171.912)
Other changes of values	3.020	4.678	(23.107)	(357)	25.261	(6.230)	3.265
Closing balance	15.998	4.474.661	7.546.991	136.577	308.313	14.345	12.496.885
Opening balance net book value	170.159	16.799.382	16.463.705	183.557	182.499	4.012.267	37.811.569
Closing balance net book value	175.921	16.757.972	16.450.873	187.532	187.306	5.186.060	38.945.664

During the period ended 31 December 2010, the Capital Group entities included expenses related to external financing in the amount of PLN 44.402 thousand (PLN 72.401 thousand during the year ended 31 December 2009).

The recoverable amount of property, plant and equipment of production companies

As at 31 December 2010 the carrying value of property, plant and equipment owned by production entities amounted to over PLN 25 billion and accounted for ca. 49% of consolidated assets of PGE Capital Group.

During the period ended 31 December 2010 there were no significant changes in the economic environment of production companies operating in Poland. Although, PGE Capital Group performed impairment tests related to cash generating units ("CGU"), including production property, plant and equipment the purpose of which was to determine their recoverable value as at 31 December 2010. Due to the fact, that there were no similar transactions on the Polish market, the recoverable value was determined with the use of the discounted cash flow method on the basis of financial projections for the years 2010 - 2020.

The key assumptions influencing revaluation of the recoverable value of tested CGUs are as follows:

- Kopalnia Węgla Brunatnego Bełchatów (i), Elektrownia Bełchatów (ii), Kopalnia Węgla Brunatnego Turów and Elektrownia Turów were treated respectively as one CGU due to technological and economic connections between these entities;
- The adopted assumptions on fluctuations of electricity prices in the years 2011-2020 determined by the balance between demand and supply of electricity in the country and taking into account the costs of energy production in national generation unit analyzed in terms of the so-called New Entry Cost meaning the cost of production of new power plants.
- Emission limits for the years 2008-2012 for particular CGUs in accordance with the National Allocation Plan II. For the years 2013-2020, the Group assumed gradual reduction of emission limits in relation to average annual allowance of 2012, from 70% in 2013 to 0% in 2020 and the following years.
- Maintenance of production capacities resulting from reconstruction investments.
- In the projection period, the after tax weighed average cost of capital amounts to 9,0%-10,4%.
- Compensations received by entitled producers resulting from earlier termination of long-term contracts.

The sensitivity analysis performed indicates that the most significant factors influencing the estimation of the income value of cash generating units are: the forecast on wholesale prices of electricity and assumed discount rates.

As a result of tests performed as at 31 December 2010 it occurred that the income-based value of property, plant and equipment tested is higher than the carrying value, therefore there is no need for impairment losses.

Measurement estimate of property, plant and equipment in distribution company

As at the balance sheet date carrying value of fixed assets related to the distribution activity amounted to ca. PLN 13 billion and represents almost 26% of the total consolidated assets. Their recoverable amount depends on the tariff granted by the Energy Regulation Office ("ERO"). The regulatory (tariff) revenue of the companies, calculated yearly in the financial plan, assures covering of justified costs: operating costs, depreciation charges, tax charges, purchase costs of electricity to cover balancing differences, costs transferred and return on capital invested in distribution activity on the justified level. Return on equity and depreciation charges are dependent on the so called Regulatory Value of Assets.

Currently the electrical energy market in Poland was facing structural changes. Distribution companies, including those within the PGE Group, lead thorough discussions with the Energy Regulatory Office over the question of accepting the revaluated assets as a basis to calculate the return on equity in tariff. In 2009 the works of the team formed by the Polish Society of Transmission and Distribution of Electricity ("PSTDE") with the participation of the President of ERO were finished. The purpose of the works was to elaborate a proposal of unified principles of measurement of assets' value related to transmission system on the basis of which transmission tariffs will be calculated as well as the so-called access path to a full return on the capital invested on the basis of elaborated assumptions.

As a result of works described above the Regulatory Value of Assets for distribution entities of PGE Group was defined. In some cases this value is lower than the carrying amount of property, plant and equipment of appropriate companies. Nevertheless, the impairment tests performed indicated that as at the date of preparation of the foregoing consolidated financial statements, there is no need to revalue the carrying value of appropriate property, plant and equipment.

Property, plant and equipment of other companies in PGE Capital Group

During the reporting period the Group made reversal of an impairment write off on property, plant and equipment assets belonging to PGE Zespół Elektrowni Wodnych Dychów S.A. (currently one of the branches of PGE Energia Odnawialna S.A.) in the amount of PLN 17.048 thousand.

22. Investment property

	31 December 2010	31 December 2009
Opening balance as at 1 January	25.431	26.612
Increase of value	538	152
Depreciation	(835)	(1.307)
Decrease of value	(175)	(26)
Closing balance as at 31 December 2010	24.959	25.431

Investment property in the Capital Group companies covers mostly buildings located in an entity location, leased to third parties in part or in full.

The Group measures investment property at cost of acquisition less depreciation amount. Fair value of investment property is not significantly higher than their carrying amount regarding the materiality related to the consolidated financial statements as a whole.

23. Intangible assets

31 December 2010	Development costs	Goodwill	Licenses and patents		Other intangible assets	Non-commissioned intangible assets	Total
			Total	Including computer software			
Gross book value							
Opening balance	11.746	-	274.612	203.624	121.013	16.641	424.012
Direct purchase	2.285	9.952	8.891	8.891	30.079	49.539	100.746
Settlement of non-commissioned intangible assets	-	-	32.757	18.549	7.926	(40.683)	-
Sales/ disposals	-	-	(1.469)	(1.469)	(101)	-	(1.570)
Transfers between groups	-	-	33.505	33.505	(33.505)	-	-
Donations and transfers free of charge	-	-	-	-	6.689	-	6.689
Liquidation	-	-	(5.952)	(4.687)	(58)	-	(6.010)
Other changes of values	-	-	(1.817)	(1.996)	(5.837)	166	(7.488)
Closing balance	14.031	9.952	340.527	256.417	126.206	25.663	516.379
Amortization and revaluation write offs							
Opening balance	10.281	-	172.843	135.453	87.322	231	270.677
Amortization for the period	1.532	-	47.413	31.418	6.323	-	55.268
Sales/ disposals	-	-	(952)	(952)	(9)	-	(961)
Transfers between groups	-	-	18.892	18.892	(18.892)	-	-
Liquidation	-	-	(5.734)	(4.677)	(84)	-	(5.818)
Other changes of values	-	-	(724)	1.021	(4.692)	-	(5.416)
Closing balance	11.813	-	231.738	181.155	69.968	231	313.750
Net book value							
Opening balance	1.465	-	101.769	68.171	33.691	16.410	153.335
Closing balance	2.218	9.952	108.789	75.262	56.238	25.432	202.629

The Goodwill presented in the table above relates mainly to the purchase of following companies: Przedsiębiorstwo Energetyki Ciepłej Sp. z o.o. seated in Zgierz and Elektrownia Wiatrowa Resko sp. z o.o.

31 December 2009	Development costs	Licenses and patents		Other intangible assets	Non-commissioned intangible assets	Total
		Total	Including computer software			
Gross book value						
Opening balance	11.377	233.535	175.662	113.748	16.290	374.950
Direct purchase	1.267	6.716	4.312	3.410	52.530	63.923
Settlement of non-commissioned intangible assets	-	47.216	34.840	6.960	(54.176)	-
Sales/ disposals	(898)	(1.516)	(1.516)	(4.006)	-	(6.420)
Donations and transfers free of charge	-	-	-	98	-	98
Liquidation	-	(10.363)	(9.881)	(325)	-	(10.688)
Other changes of values	-	(976)	207	1.128	1.997	2.149
Closing balance	11.746	274.612	203.624	121.013	16.641	424.012
Amortization and revaluation write offs						
Opening balance	9.440	146.774	121.268	76.480	231	232.925
Amortization for the period	1.604	38.066	26.289	14.372	-	54.042
Sales/ disposals	(763)	(1.322)	(1.322)	(3.952)	-	(6.037)
Liquidation	-	(10.187)	(9.805)	(281)	-	(10.468)
Other changes of values	-	(488)	(977)	703	-	215
Closing balance	10.281	172.843	135.453	87.322	231	270.677
Net book value						
Opening balance	1.937	86.761	54.394	37.268	16.059	142.025
Closing balance	1.465	101.769	68.171	33.691	16.410	153.335

24. Leasing

24.1. Operating lease liabilities- the Group as the lessee

As at 31 December 2010 and as at 31 December 2009 the future minimum lease payments related to irrevocable lease agreements are as follows:

	Future liabilities at	
	31 December 2010	31 December 2009
Less than 1 year	100	569
Between 1 and 5 years	104	225
More than 5 years	-	-
Total lease payments	204	794

Additionally the Capital Group entities incur costs related to a perpetual usufruct of land. The value of these costs for the year ended 31 December 2010 amounted to ca. PLN 11.735 thousand.

24.2. Operating lease receivables – the Group as a lessor

As at 31 December 2010 and as at 31 December 2009, the future minimum receivables from lease payments related to irrevocable operating lease agreements are as follows:

	Future receivables as at		Income recognized in	
	31 December 2010	31 December 2009	2010	2009
Less than 1 year	374	364	60	45
Between 1 and 5 years	1.602	1.544	257	195
More than 5 years	-	-	-	-
Total lease payments	1.976	1.908	317	240

The PGE Capital Group companies have signed agreements with PSE-Operator S.A. on rendering intervention services related to administration of and using of production units by the system operator in order to balance active and passive power on an intervention basis in the National Electroenergetic System (NES). This aims at ensuring proper and safe operation of the system. The above mentioned agreements, although not having a legal form of leasing, give the right to use the assets for a series of payments.

24.3. Liabilities from finance lease and lease agreement with option to purchase

As at 31 December 2010 and as at 31 December 2009, the future minimum lease payments related to these agreements and current value of minimum net lease payments are as follows:

	31 December 2010		31 December 2009	
	Minimal payments	Current value of payments	Minimal payments	Current value of payments
Less than 1 year	4.462	3.870	1.126	1.014
Between 1 and 5 years	7.099	6.495	740	656
More than 5 years	-	-	-	-
Total minimum lease payments	11.561	10.365	1.866	1.670
Less financial expenses	(1.196)	-	(196)	-
Current value of minimum lease payments, including:	10.365	10.365	1.670	1.670
Short-term	3.870	3.870	1.014	1.014
Long-term	6.495	6.495	656	656

24.4. Receivables from finance lease and lease agreement with purchase option

	31 December 2010		31 December 2009	
	Minimal payments	Current value of payments	Minimal payments	Current value of payments
Less than 1 year	741	613	358	340
Between 1 and 5 years	945	843	699	602
More than 5 years	-	-	-	-
Total minimum lease payments	1.686	1.456	1.057	942
Less financial expenses	(230)	-	(115)	-
Current value of minimum lease payments, including:	1.456	1.456	942	942
Short-term	613	613	340	340
Long-term	843	843	602	602

25. Investment in associates accounted for using the equity method

	Polkomtel*	PEC Bogatynia*	Atex*	Swe-Pol Link*	TOTAL
Share in voting rights	21,85%	34,93%	43,83%	49,00%	
	Telecommunication services	Transmission, distribution and turnover of heat	Control and monitoring systems	Transmission of electricity	
As at 31 December 2010					
Share of statement of financial position in associate:					
Current assets (short-term)	299.128	2.026	10.322	17.835	329.311
Non-current assets (long-term)	1.441.426	8.560	5.044	275.061	1.730.091
Short-term liabilities	(507.279)	(779)	(1.271)	(34.057)	(543.386)
Long-term liabilities	(413.538)	(66)	(308)	(237.463)	(651.375)
Share of net assets	819.737	9.741	13.787	21.376	864.641
Goodwill	529.803	-	-	14.021	543.824
Shares in associate in the statement of financial position	1.349.540	9.741	13.787	35.397	1.408.465
Period ended 31 December 2010					
Share of revenue of the associate	1.733.053	5.492	8.120	50.792	1.797.457
Share of profit (loss) of the associate:	223.889	176	1.048	1.906	227.019
As at 31 December 2009					
Share of statement of financial position in associate:					
Current assets (short-term)	293.885	1.410	9.444	11.501	316.240
Non-current assets (long-term)	1.543.872	8.865	5.344	275.121	1.833.202
Short-term liabilities	(898.618)	(673)	(1.114)	(29.266)	(929.671)
Long-term liabilities	(211.915)	(38)	(270)	(239.796)	(452.019)
Share of net assets	727.224	9.564	13.404	17.560	767.752
Goodwill	529.803	-	-	57.244	587.047
Shares in associate in the statement of financial position	1 257.027	9.564	13.404	74.804	1.354.799
Period ended 31 December 2009					
Share of revenue of the associate	1.770.804	4.894	7.367	42.967	1.826.032
Share of profit (loss) of the associate:	241.931	(181)	920	(513)	242.157

* preliminary non-audited data

Goodwill of SwePol Link AB

In periods before the balance sheet date the parent company made prepayments for transmission services to Vattenfall Aktiebolag („VAB”). These prepayments were related to an execution of Restructuring Agreement signed by PGE S.A. and VAB on 28 May 2003 and were associated with a purchase of SwePol Link AB shares as well as a construction and exploitation of a permanent electricity link between Polish and Swedish electric system. Taking into consideration the character of transactions mentioned above, in the consolidated financial statements prepared in accordance with IFRS a part of the prepayments made is presented as the cost of purchase of shares in an associate and the other part is presented as a loan. Increased cost of shares acquisition in SwePol Link AB, due to clearing of prepayments, was recognized as goodwill and amounted to PLN 57.244 thousand as at 1 January 2010.

Prepayments were cleared in course of executing the above mentioned contract, which expired in August 2010. During the reporting period works with the objective of settling the issues of prepayments outstanding after expiry of the VAB contract were carried out at the Company. As at the date of preparation of these consolidated financial statements there is no certainty as to successful completion of the Company's efforts with respect to extension of cooperation; therefore there is an uncertainty as to recovery of amounts involved. The Company assumes that the issue of continuing cooperation will be resolved successfully, and that the nominal values of prepayment will be cleared or returned. However, as the value of assets related to VAB in the IFRS financial statements exceeds the nominal value of the same assets, in the foregoing financial statements the Group has created the allowance on goodwill of SwePol Link AB in the amount of PLN 43.223 thousand.

The planned sales of Polkomtel S.A.

Furthermore, as described in note 45.7 to the foregoing consolidated financial statements, the Management Board adopted a decision to commence arrangements for the sale of shares of Polkomtel S.A. As at the day of preparation of these consolidated financial statements the regulations of IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* were not fulfilled, therefore the shares in this entity are presented in accordance with IAS 28 *Investments in Associates*.

26. Investments in jointly controlled entities

During financial periods ended 31 December 2010 and 31 December 2009 the Group did not participate in any jointly controlled entity.

27. Inventories

	31 December 2010		31 December 2009			
	Historical cost	Revaluation write off	Historical cost	Revaluation write off	Historical cost	Revaluation write off
Materials	790.493	(130.439)	660.054	1.022.653	(119.156)	903.497
Finished goods	37.508	(19)	37.489	5.465	(25)	5.440
Semi-products and work in progress	42.863	-	42.863	58.416	-	58.416
Energy origin units of ownership	342.521	-	342.521	295.511	-	295.511
Merchandise	6.918	(718)	6.200	8.235	(767)	7.468
CO ₂ emission rights	1.634	(212)	1.422	949	(116)	833
Total	1.221.937	(131.388)	1.090.549	1.391.229	(120.064)	1.271.165

Revaluation write off on inventories as at 1 January 2010	(120.064)
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Revaluation write offs created	(26.848)
Revaluation write offs reversed	3.768
Revaluation write offs used	11.738
Other	18

Revaluation write off on inventories as at 31 December 2010	(131.388)
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Creation of the above revaluation write offs related mainly to spare parts and materials as a result of their amortization or obsolescence. Reversal of revaluation write offs, mainly on spare parts and materials, resulted from their disposal or usage to the value exceeding the previously measured carrying amount.

28. Carbon dioxide emission rights

On 14 November 2008, the Council of Ministers adopted a National Allocation Plan on carbon dioxide emission for the years 2008-2012 ("KPRU II") in the European Community emission rights trading system dividing the carbon dioxide (CO₂) emission limits between the installations participating in the emission rights trading system. The accepted regulation is based on a draft of the regulation dated 12 February 2008, after the changes dated 16 May 2008. According to the decision of the European Commission Polish companies will be able to emit ca. 1,043 million tons of CO₂ during the 2008-2012 period. This gives a volume of 209 million tons per year.

The below table contains CO₂ emission limits granted to particular Group entities for the 5-year period, forecasts of CO₂ emission for the period and exposure of particular entities after having taken into consideration the actual emission in 2008-2010 period, based on the adopted method of allocating emission limits.

Company	Emission limits for years 2008-2012 (5 years in total) in thousand tones CO ₂	Emission plan for years 2008-2012, regarding the actual usage of limits	Planned (shortage) / surplus in years 2008 – 2012	Shortage as at 31 December 2010 after redemption until the balance sheet date
PGE Górnictwo i Energetyka Konwencjonalna S.A.	232.742	251.745	(19.003)	(5.481)
PGE Elektrownia Opole S.A.	31.417	35.245	(3.828)	(1.059)
TOTAL	264.159	286.990	(22.831)	(6.540)

The principles of allocation of emission limits for particular years of the settlement period are described in details in note 13.25 to the foregoing consolidated financial statements. The provision is calculated on the basis of shortage of CO₂ emission rights in the period, based on actual and planned CO₂ emission in the reporting period. The value of the provision as at the balance sheet date is accrued from the beginning of the reporting period to the balance sheet date, taking into consideration the actual CO₂ emission in the period.

The provision as at the balance sheet date is calculated based on prices included in contracts on covering the emission rights shortage and the remaining emission rights shortage is calculated on the basis of weighted average price of SPOT contracts as at the balance sheet date.

The provision calculated as at 31 December 2010, after taking into consideration the redemption of emission which took place until 31 December 2010, for the PGE Capital Group amounted to PLN 322.734 thousand and is described in detail in note no 35 to the foregoing consolidated financial statements.

29. Other short-term and loan-term assets

Other long-term assets

	31 December 2010	31 December 2009
Prepayments for property, plant and equipment under construction	217.790	427.529
Other prepayments	46.642	57.558
Total other long-term financial assets	264.432	485.087

Other prepayments comprise mainly of acquired right of perpetual usufruct that is presented in a similar way as an operating lease in accordance with the accounting policies of the PGE Capital Group.

Other short-term assets

	31 December 2010	31 December 2009
Deferred expenses		
Tax on civil law transactions	76.784	1
Property and tort insurance	20.339	19.488
IT services	3.634	3.176
Purchased right of perpetual usufruct		
Real estate tax settled in time	488	233
Other costs settled in time	37.989	10.154
Other short-term assets		
VAT receivable	75.096	192.934
Excise tax receivable	16.727	17.802
Other tax receivables	131	1.712
CO ₂ emission rights for own use	168.810	116.661
Advances for deliveries of non-current assets	20.743	15.385
Prepayments for deliveries	271	3.998
Other short-term assets	24.797	9.603
Total other short-term financial assets	445.809	391.147

Tax on civil law transactions presented in the table above relates to the acquisition process of PGE Capital Group (see also Note 45.6 to the foregoing financial statements).

30. Cash and Cash equivalents

Cash at the bank is subject to variable interest rates which are based on bank deposits' interest rates. Short-term deposits are made for different periods, from one day up to one month, depending on the Group's needs for cash, and are deposited at individually settled interest rates. Fair value of cash and cash equivalents as at 31 December 2010 amounted to PLN 2.730.423 thousand (as at 31 December 2009, amounted to PLN 7.712.823 thousand).

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

	As at 31 December 2010	As at 31 December 2009
Cash on hand and cash at bank	652.458	267.336
Overnight deposits	749.139	493.813
Short-term deposits	1.328.826	6.951.674
Total	2.730.423	7.712.823
Cash and cash equivalents presented in cash flow statement	2.736.859	7.705.934
Credit limits at disposal	1.195.974	2.357.685

The difference between the value of cash and cash equivalents presented in the statement of financial position and the one presented in cash flow statements results mainly from interests accrued for but not received as at balance sheet date, foreign exchange differences from cash and cash equivalents as well as cash attributed to discontinued operations in amount of PLN 5.025 thousand (please refer to the note 19 to the foregoing consolidated financial statements).

Restricted cash is related mainly to the Mine Liquidation Trust and Mine Recultivation Trust and amounted to PLN 100.746 thousand as at 31 December 2010 and PLN 60.673 thousand as at 31 December 2009.

Furthermore, apart from cash and cash equivalents presented in the table above, there was also included cash treated as collateral of settlements with PGE S.A. and Warsaw Commodity Clearing House (described in detail in note 42.6 to the foregoing consolidated financial statements).

31. Share capital and other capitals

The basic assumption of the Group policy regarding capital management is to maintain an optimal capital structure over the long term in order to assure a good financial standing and secure capital structure ratios that would support the operating activity of the Group. It is also crucial to maintain a sound capital base that would be the basis to win confidence of potential investors, creditors and the market and assure further development of the Company.

31.1. Share capital

As at 31 December 2009.

Series/ issue	Type of shares	Type of preference	Number of shares	Value of series/ issue at nominal value	Capital coverage method
"A"	ordinary shares	n/a	1.470.576.500	14.705.765.000,00	contribution/cash
"B"	ordinary shares	n/a	259.513.500	2.595.135.000,00	cash
Razem			1.730.090.000	17.300.900.000,00	

As at 31 December 2010.

Series/ issue	Type of shares	Type of preference	Number of shares	Value of series/ issue at nominal value	Capital coverage method
"A"	ordinary shares	n/a	1.470.576.500	14.705.765.000,00	contribution/cash
"B"	ordinary shares	n/a	259.513.500	2.595.135.000,00	cash
"C"	ordinary shares	n/a	73.241.482	732.414.820,00	merger with PGE GiE S.A
"D"	ordinary shares	n/a	66.452.245	664.522.450,00	merger with PGE Energia S.A..
Razem			1.869.783.727	18.697.837.270,00	

All shares of the Company have been paid.

Changes in the value and the structure of share capital of the Company in 2009.

On 3 September 2009, the Extraordinary Meeting of Shareholders adopted a resolution related to an increase of the share capital of the Company in the manner of an issue of new shares excluding the subscription right of the hitherto existing shareholder. Based on the resolution, the share capital was increased by the amount no greater than PLN 2.595.135.000 (PLN two billion five hundred and ninety five million one hundred and thirty five thousand) through an issue of B series shares of the nominal value of PLN 10 each. New shares were offered to Polish individual investors as well as to Polish and foreign corporate investors in the manner of a public offering within the Republic of Poland in accordance with the Act on Public Offering, Conditions Governing the Introduction of Financial Statements to Organized Trading, and Public Companies dated 29 July 2005 ("Act on Public Offering") as well as individual offerings outside of the Republic of Poland. The B series shares were issued on the basis of the above mentioned resolution participate in the 2009 dividend, i.e. starting from 1 January 2009, under the same conditions as all other shares of the Company.

The increase of share capital was registered on 30 November 2009. The share capital was increased by PLN 2.595.135 thousand.

Changes in the value and the structure of share capital of the Company in 2010.

The merger of PGE S.A. and the subsidiaries: PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. was registered by the District Court in Warsaw on 31 August 2010. The issue of the merger was described in details in note 9 of the supplementary information and explanations to the foregoing financial statements. The merger took place in compliance with art. 492 par. 1 p. 1 the Commercial Code i.e., namely by transfer of all assets of the companies being acquired to PGE S.A. in exchange for merger shares, issued by the Company and released to shareholders of the acquired entities, for the purpose of the merger. As a result of merger the shareholders of the acquired entities received shares in the increased share capital of PGE S.A. in exchange for their shares in PGE Energia S.A. and PGE Górnictwo i Energetyka S.A.

As a result of the merger, share capital of PGE S.A. increased from PLN 17.300.900 thousand to PLN 18.697.837 thousand i.e. by the amount of PLN 1.396.937 thousand through the issuance of 139.693.727 shares, including 73.241.482 bearer shares of series C and 66.452.245 bearer shares Series D with a nominal value of PLN 10 each.

As the merger with the subsidiaries took place, in the foregoing consolidated financial statements an increase of share capital was recognized on the debit side in correspondence with retained earnings and equity attributable to non-controlling shareholders.

The merger with PGE Electra S.A. on 31 December 2010 did not have impact on the amount of the Company' share capital.

31.2. Treasury shares

As a consequence of PGE S.A. merger with PGE GiE S.A. and PGE Energia S.A., PGE S.A. acquired 22.898 treasury shares for the amount of PLN 579 thousand. These shares were acquired because with the applied exchange parity scheme, shareholders of merged companies should have received fractions of shares. As this is not allowed, the numbers of shares assignable to shareholders of merged companies were rounded down in the process of allocation of the Company's shares. Fractional values of shares receivable by each specific shareholder were paid in cash (PLN 25,29 per share). With this transaction structure, outstanding shares not taken up by shareholders of the merged companies remained. These shares were acquired by PGE S.A. for a fee equivalent to the amount of capital contributions. The purpose of the acquisition was the redemption of shares. Treasury shares shall be redeemed pursuant to a resolution of the general meeting of shareholders, through decrease of the share capital.

31.3. Rights of the shareholders

Rights of the State Treasury.

The Company's shares are ordinary bearer shares listed on Warsaw Stock Exchange. The shares of the Company are not privileged.

Even though, the shares of the Company are not privileged, the Company's Status takes into account special rights of the State Treasury as long as it is the shareholder of the Company. According to its provisions, the State Treasury holds right to approach the Management Board with a written demand of gathering the General Meeting of Shareholders, including particular issues to the meeting agenda, submitting projects of resolutions related to issues included in the agenda or issues that might be included in the agenda, obtaining copies of announcements placed in Court and Economical Monitor.

Moreover, based on the Company's Status, the State Treasury holds right to appoint one member of the Supervisory Board in the form of a written statement submitted to the Company during the General Meeting of Shareholders or outside the General Meeting of Shareholders with the use of the Management Board. Furthermore, this right can be executed by the State Treasury regardless the voting right during appointing other members of the Supervisory Board.

Based on the Art.9 of the act of 18 March 2010 on special powers the Minister of the Treasury and their performance in certain capital companies or holding companies operating in the sectors of electricity, oil and gaseous fuels (OJ No 65, dated 21 April 2010, item. 404) the Minister of the Treasury, as long as the State Treasury is directly or indirectly shareholder in the Company, has the right to object any resolution or legal action of the Management Board that relates to the ability to dispose a part of company's property that is fundamental for its activities. The objection only relates to the Company of a significant importance for public order or safety if there is a reasonable assumption that such legal action might violate public order or public safety.

The objection also comprised the resolution of the General Meeting of Shareholders relating to:

- liquidation of the Company,
- movement of the Company's office abroad,
- change of a core competence of the Company,
- sale or lease of a company or its organized part or establishment of limited law property

if there is a reasonable assumption that such a resolution might violate public order or public safety.

. According to the Act, the State Treasury has the special right to object to any resolution adopted or another legal action taken by the company's Management Board that relates to the ability to dispose a part of company's property that is fundamental for its activities.

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

- liquidation of a company,
- changes of the aim or discontinuance of exploitation of the company's asset, which is critical infrastructure,
- change of a core competence of a company,
- sale or lease of a company or its organized part or establishment of limited law property,
- approval of material and financial plan, investment plan, or long-term strategic plan,
- movement of a company's office abroad

if an accomplishing of such a resolution resulted in an actual threat to operation, going concern or integrity of the critical infrastructure.

The new act introduces a function of attorney to critical infrastructure. The attorney is chosen by the company in consultation with the Minister of Treasury and the director of the Government Security Center. As at the date of preparation of the consolidated financial statements the attorney to critical infrastructure has not been chosen yet in the Company.

31.4. Equity holders of a significant share.

Changes in the structure of share capital of PGE S.A. during the period ended 31 December 2010, presents as follows:

Ownership structure and the percentage of held shares:

(in PLN)	State Treasury		Other Shareholders*		Total	
	Share's value	Portion (%) of share capital and votes' number	Share's value	Portion (%) of share capital and votes' number	Share's value	Portion (%) of share capital and votes' number
Shares as at 1 January 2010	14.705.765.000	85,00	2.595.135.000	15,00	17.300.900.000	100,00
Issue of shares as a result of merger of PGE S.A., PGE GiE S.A. and PGE Energia S.A.	120.394.520	-	1.276.542.750	-	1.396.937.270	-
Sale on 8 October 2010 186.978.000 shares of PGE S.A. attributable to State Treasury	(1.869.780.000)	-	1.869.780.000	-	0,00	-
Shares as at 31 December 2010	12.956.379.520	69,29	5.741.457.750	30,71	18.697.837.270	100,00

* Nominal value of shares held by other shareholders includes treasury shares of parent company.

The share in share capital of particular shareholders reflects the share in votes during General Meetings of Shareholders.

As described in note 31.1 to the foregoing consolidated financial statements on 31 August 2010 the merger of PGE Polska Grupa Energetyczna S.A. with PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. took place and resulted in issuance of new shares. Furthermore, on 8 October 2010, the State Treasury sold 186.978.000 shares of PGE S.A. representing 9,99% of the share capital of the Company.

Merger with PGE Electra S.A. on 31 December 2010 had no impact on the amount of share capital of the Company.

31.5. Reserve capital

In accordance with adopted accounting policy reserve capital of the Capital Group is reserve capital presented in the stand alone financial statement of the parent company.

Reserve capital results from a surplus of issue value over nominal value less costs of share issue recognized as a decrease of reserve capital. Furthermore, a reserve capital results from statutory write-offs on profits generated in previous reporting periods, as well as from a surplus of profit distribution over the value of a statutory write-off.

In 2010 the reserve capital of PGE Capital Group increased mainly due to the settlement of the merger of parent company with consolidated subsidiaries. Therefore changes in reserve capital were recognized in correspondence with retained earnings and equity attributable to non-controlling interest.

31.6. Retained earnings and limitations to payment of a dividend.

Retained earnings comprise of the amounts that are not subject to distribution i.e. that cannot be paid as a dividend by the parent company:

	31 December 2010	31 December 2009
Amounts included in retained earnings that cannot be distributed by the parent:		
- retained earnings of subsidiaries, attributable to equity holders of the parent	8.626.658	7.021.543
- differences in the value of retained earnings as presented in stand-alone statutory financial statement and IFRS financial statement of the parent company	(58.442)	(43.993)
- 8% of the value of the parent company's statutory profit to be distributed to reserve capital as specified in the Commercial Code	-	115.240
Retained earnings of the parent, subject to distribution	3.040.898	1.327.058
Total retained earnings presented in the consolidated financial statements attributable to equity holders of the parent	11.609.114	8.419.848

As described in note 8 to the foregoing consolidated financial statements, statutory financial statements of majority of PGE Capital Group entities are prepared in accordance with Polish accounting standards. The dividend can be paid on the basis of the financial result recognized in separate annual financial statements prepared for statutory purposes.

According to regulations of the Commercial Code of the Companies, the parent company and subsidiaries which are joint stock companies are obliged to create reserve capital to cover potential losses. At least 8% of the profit for the reporting year recognized in the statutory financial statements is transferred to reserve capital, until this capital amounts to at least one third of the share capital. As at the 31 December 2010, resulting from merger of the parent company and subsidiaries, the reserve capital reached the amount specified in the Commercial Code.

The General Shareholders' Meetings decides on the use of the reserve capital; however the part of reserve capital which amounts to one third of share capital can only be used to cover losses recognized in statutory financial statements and cannot be distributed for other purposes.

As at 31 December 2010 the share capital of the parent company amounted to PLN 18.697.837 thousand and reserve capital amounted to PLN 6.727.592 thousand. As at 31 December 2009 share capital of parent company presented in the statutory financial statements in accordance with the Accounting Act amounted to PLN 17.300.900 thousand and reserve capital PLN amounted to 6.591.666 thousand.

As at 31 December 2010 there were no other limitations to payment of a dividend.

31.7. Equity attributable to non-controlling interests

	Year ended 31 December 2010	Year ended 31 December 2009
Opening balance	7.681.428	7.365.921
Share of profit of subsidiaries	612.967	966.511
Dividends divided by subsidiaries	(673.996)	(119.359)
Change in accounting policy	7.465	-
Share in change in value of financial instruments	-	(10.172)
Purchase of new companies	7.648	-
Sale of subsidiaries	(13.786)	-
Transfer of non-controlling interests to equity attributable to shareholders of parent company	(3.376.706)	-
Purchase of non-controlling interest by the Capital Group	(3.646.201)	(521.473)
Closing balance	598.819	7.681.428

The purchase of non-controlling shares during the year ended 31 December 2009 refers to the share purchase transactions in PGE Elektrownia Opole S.A., PGE Kopalnia Węgla Brunatnego Turów S.A., and PGE Zespół Elektrociepłowni Bydgoszcz S.A.

Purchase of non-controlling shares during the year ended 31 December 2010 relates mainly to purchases of shares of PGE Górnictwo i Energetyka Konwencjonalna S.A., PGE Obrót S.A., and PGE Dystrybucja S.A. by the Company. Transfer of non-controlling interest to capital allocated to equity holders of the parent is a consequence of merger of the parent company with PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. as well as other mergers under the Consolidation Program. The method of recognizing of the above transactions is presented in note 9 to the foregoing financial statements.

32. Earnings per share

Basic earnings per share shall be calculated by dividing profit or loss attributable to ordinary equity holders of the parent entity by the weighted average number of ordinary shares outstanding during the period.

An entity shall calculate diluted earnings per share by dividing profit or loss attributable to ordinary equity holders of the parent entity (after deduction of interest on redeemable convertible preference shares) by the weighted average number of shares outstanding during the period (adjusted with the number of dilutive options or dilutive redeemable convertible preference shares).

Presented below are data on profit and shares used to calculate basic earnings per share.

	Year ended 31 December 2010	Year ended 31 December 2009
Net profit on continuing operations	3.602.850	4.337.223
Net profit on discontinued operations	24.237	-
Net profit, attributed to	3.627.087	4.337.223
- shareholders of the parent company	3.014.120	3.370.712
- non-controlling interest	612.967	966.511
Net profit attributable to ordinary equity holders of the Company used to calculate diluted earnings per share	3.014.120	3.370.712
Number of ordinary shares at the beginning of reporting period	1.730.090.000	1.470.576.500
Number of ordinary shares at the end of reporting period*	1.869.760.829	1.730.090.000
Average weighted number of ordinary shares issued used to calculate basic earnings per share	1.776.646.943	1.513.947.249

* Ordinary shares as at the end of reporting period do not include treasury shares acquired by the parent company for redemption.

As described in Note 31.1 on 3 September 2009 the Extraordinary General Meeting of Shareholders of the Company passed a resolution on increasing the share capital of the Company through issuance of new shares, to the exclusion of current shareholder's pre-emptive rights. According to IAS 33.21 ordinary shares issued in exchange for cash are included in calculation of earnings per share as from the time when the cash value becomes due and payable. Therefore, in order to calculate the weighted average number of issued shares, the Company recognized the new shares as from November 2009.

Furthermore, as described in Note 31.1, a merger of PGE Polska Grupa Energetyczna S.A. with PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. was registered on 31 August 2010. As a result of the merger the parent company issued shares for the previous shareholders of merged companies. According to IAS 33.21 shares issued as a result of merger were recognized as at the effective date of transfer of the subsidiaries' assets and liabilities to PGE Polska Grupa Energetyczna S.A.

The merger with PGE Electra S.A. on 31 December 2010 had no impact on the amount of the Company' share capital.

33. Dividends paid and dividends declared

	Period ended 31 December 2010	Period ended 31 December 2009
<i>Cash dividends from ordinary shares</i>		
Dividend paid from retained earnings	1.335.330	527.829
Dividend paid from other capital reserves	-	414.017
Obligatory distribution from profit paid to the State Treasury by the parent company	-	198.142
Total cash dividends from ordinary shares	1.335.330	1.139.988
Cash dividends per share (in PLN)*	0,71**	0,78*

* As described in Note 31.1 in September 2009 the Extraordinary Meeting of Shareholders of PGE Polska Grupa Energetyczna S.A. adopted a resolution on increasing the value of the share capital. The increase of the share capital was registered in the National Court Register on 30 November 2009. Due to the above, the cash dividend per share was calculated based on the number of shares in the period in which the resolution was adopted, i.e. before the increase of the share capital.

** As described in note 9 and note 31.1. to the foregoing financial statements on 31 August 2010, there was the merger of PGE Polska Grupa Energetyczna S.A. with PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. In the foregoing financial statements as dividend paid from parent company's capital were presented the relevant amounts related to merged companies (as described below). Therefore to calculate the DPS ratio the number of shares after increase of share capital related to the merger was used. Dividend per share paid by the parent company without considering the impact of the merger amounted to PLN 0,76.

Until the debut on Warsaw Stock Exchange PGE Polska Grupa Energetyczna S.A. was subject to provisions related to an obligatory distribution of profit paid by sole-shareholders companies of the State Treasury, which amounts to 15% of the Company's gross financial result reflected in the statutory financial statements less current corporate income tax. According to IFRS such payments are recognized as payments of a dividend to a shareholder and reflected as a change in equity. Since December 2009 the Company is no longer obliged to pay distribution from profit.

Dividend in 2009

On 30 June 2009 the Ordinary Meeting of Shareholders decided to allocate PLN 509,185 thousand of 2008 profit to pay the dividend. Furthermore the retained earnings in the amount of PLN 18,644 thousand and reserve capital in the amount of PLN 414,017 thousand were also allocated to pay the dividend. The dividend defined by the Ordinary Meeting of Shareholders resolutions of 30 June 2009 was paid on 31 August 2009.

Dividend in 2010

As a result of the merger of the parent company with PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. dividends attributable to shareholders of the parent company that are presented in the statements of changes in consolidated equity include also appropriate amounts referring to these companies.

In 2010 the General Meetings of Shareholders of PGE S.A., PGE Górnictwo i Energetyka S.A., PGE Energia S.A. and PGE Electra S.A. divided net profits gained in 2009 in the following manner:

- net profit of PGE S.A. amounted to PLN 1.440.498 thousand allocated to reserve capital in amount of PLN 125.629 thousand and to pay a dividend for Shareholders in amount of PLN 1.314.868 thousand
- Net profit PGE GiE S.A. amounted to PLN 221.367 thousand, allocated in Total amount to pay a dividend for Shareholders. The amount of PLN 111.006 thousand was paid in 2009 as an interim dividend.

- Net profit of PGE Energia S.A. amounted to PLN 57.205 thousand allocated to reserve capital in amount of PLN 4.576 thousand and to pay a dividend in amount of PLN 52.628 thousand. The amount of PLN 26.574 thousand was paid in 2009 as an interim dividend.

The table below presents specification of dividends transferred to the shareholders after elimination of dividends transferred to PGE S.A. by PGE Górnictwo i Energetyka S.A. and PGE Energia S.A.

	Dividends paid for:		TOTAL
	State Treasury	Other shareholders	
Dividends paid by:			
PGE Polska Grupa Energetyczna S.A.	1.117.638	197.230	1.314.868
PGE Górnictwo i Energetyka S.A.	1.759	14.795	16.554
PGE Energia S.A.	250	3.658	3.908
TOTAL	1.119.647	215.683	1.335.330

The merger with PGE Electra S.A. on 31 December 2010 had no impact on the amount of dividends presented in the foregoing financial statements.

Limitation of dividend payment was described in note 31.6 to the foregoing consolidated financial statements.

34. Employment benefits

Retirement and pension allowances, coal allowance, medical care, allowance for Social Fund and other benefits for

The Group entities pay retirement or pension allowances in the amount specified in the Corporate Collective Labor Agreement when an employee retires or becomes a pensioner. Moreover, the former employees of the companies of PGE Capital Group receive benefits in the form of medical care, coal allowance, Social Fund allowance, etc. Due to the above, entities create a relevant provision for mentioned allowances based on the valuation made by an actuary.

Energy Tariff

Based on the Inter-Corporate Collective Labor Agreement, changed in 2005, the obligation of payment of benefits, the so called "energy tariff", to former employees of the electric power engineering industry and other entitled persons is imposed on entities in which the entitled persons were employed. As a result, from 2006 the Group creates an appropriate provision. The amount of the provision is measured by an independent actuary. The cost of creating the provision is recognized in operating expenses.

Social Fund and medical benefits

The Group entities create a write off for Social Fund for retirees and pensioners. The Group entities also provide medical care for retirees and pensioners. Provisions are created to cover such costs and these are measured using actuarial methods.

Amounts of these provisions and a reconciliation of changes in provisions during the reporting period are presented below:

Year ended 31 December 2010

	Retirement, pension and other benefits provisions	Coal allowance	Energy tariff	Social Fund	Medical benefits	Total
As at 1 January 2010	338.702	117.323	443.761	196.790	35.126	1.131.702
Present employment costs	13.652	1.044	9.642	3.157	668	28.163
Actuarial gains and losses excluding discount rate adjustment	(40.805)	325	(1.369)	(2.569)	(1.404)	(45.822)
Benefits paid	(14.676)	(6.983)	(16.675)	(5.439)	(1.200)	(44.973)
Past employment costs	-	-	9.897	-	-	9.897
Discount rate adjustments	13.630	5.606	40.346	12.444	2.093	74.119
Interest costs	19.631	6.861	31.910	11.488	2.071	71.961
Transfer to discontinued operations	(88)	-	(143)	(19)	-	(250)
Other changes	2.262	-	8.829	1.073	(300)	11.864
As at 31 December 2010	332.308	124.176	526.198	216.925	37.054	1.236.661
Short-term	55.407	8.168	22.559	9.970	1.715	97.819
Long-term	276.901	116.008	503.639	206.955	35.339	1.138.842

Year ended 31 December 2009

	Retirement, pension and other benefits provisions	Coal allowance	Energy tariff	Social Fund	Medical benefits	Other	Total
As at 1 January 2009	341.216	123.220	412.648	170.949	37.220	325	1.085.578
Present employment costs	12.986	1.139	6.238	2.702	649	-	23.714
Actuarial gains and losses excluding discount rate adjustment	5.618	(1.161)	39.188	32.544	(17)	-	76.172
Benefits paid	(17.844)	(6.813)	(14.717)	(6.059)	(1.244)	-	(46.677)
Past employment costs	-	-	9.867	-	-	-	9.867
Discount rate adjustments	(17.046)	(5.683)	(38.988)	(12.236)	(2.108)	-	(76.061)
Interest costs	18.080	6.621	27.929	9.057	1.957	-	63.644
Other changes	(4.308)	-	1.596	(167)	(1.331)	(325)	(4.535)
As at 31 December 2009	338.702	117.323	443.761	196.790	35.126	-	1.131.702
Short-term	48.539	7.976	21.421	9.199	1.771	-	88.906
Long-term	290.163	109.347	422.340	187.591	33.355	-	1.042.796

Major actuarial assumptions related to the calculation of provisions as at the balance sheet date are as follows:

	31 December 2010	31 December 2009
Discount rate (%)	5,5	6,0
Expected inflation rate (%)	2,5	2,5
Employee turnover (%)	0,27-8,78	0,24 - 9,27
Expected salary growth rate (%)	0-7,0	1,0 – 9,5
Expected medical costs growth rate (%)	2,3-5,0	2,5 – 25,0
Expected Social Fund (ZFŚS) allowance rate (%)	3,5-5,0	3,5 – 5,0

Based on data obtained from an actuary, the Group assesses that the influence of changes in assumptions on the value of provisions for retirement and pension benefits, coal allowance, social fund, medical care and jubilee awards (note 35) would be as follows:

- should the discount rate be higher by 1 percentage point (p.p.), relevant provisions would decrease by ca. 8% and should the discount rate be lower by 1 p.p. relevant provisions would increase by ca. 9%,
- should the planned increase in the basis for estimations be higher by 1 p.p., relevant provisions would increase by ca. 10% and should the planned increase in the basis for estimations be lower by 1 p.p., relevant provisions would decrease by ca. 8%.

35. Provisions

Year ended 31 December 2010

	Post-employment benefits	Provisions for jubilee benefits	Provisions for third parties claims	Provisions for legal disputes	Provisions for purchase of CO ₂ emission rights	Provisions for employee claims	Provisions for recultivation	Provisions for liquidation of property, plant and equipment	Provisions for certificates of origin held for redemption	Other provisions	TOTAL
As at 1 January 2010 (restated)	1.131.702	801.866	351.023	85.378	383.025	29.349	903.661	102.055	415.155	602.866	4.806.080
Costs of present employment	28.163	43.803	-	-	-	-	-	-	-	-	71.966
Actuarial gains and losses excluding discount rate adjustment	(45.822)	(53.829)	-	-	-	-	-	-	-	-	(99.651)
Benefits paid	(44.973)	(81.597)	-	-	-	-	-	-	-	-	(126.570)
Costs of past employment	9.897	-	-	-	-	-	-	-	-	-	9.897
Revaluation of provision/ discount rate adjustments	74.119	25.880	-	-	-	-	1.030	-	-	-	101.029
Interest costs	71.961	44.405	-	-	-	-	47.321	5.614	-	-	169.301
Created during the year	-	-	109.883	47.366	233.182	24.530	36.443	1.997	152.032	406.943	1.012.376
Reversed	-	-	(110.613)	(34.937)	(14.899)	(22.667)	(52.136)	(8.549)	(360)	(301.627)	(545.788)
Used	-	-	-	(653)	(310.638)	(9.444)	(6.628)	(5.676)	(3.491)	(355.296)	(691.826)
Transfer to discontinued operations	(250)	(713)	-	-	-	-	-	-	-	(1.101)	(2.064)
Other changes	11.864	1.726	-	(5.625)	32.064	(2.836)	475	-	-	(1.483)	36.185
As at 31 December 2010	1.236.661	781.541	350.293	91.529	322.734	18.932	930.166	95.441	563.336	350.302	4.740.935
Short-term	97.819	92.297	350.293	61.238	269.781	3.614	4.057	17.744	563.336	208.461	1.668.640
Long-term	1.138.842	689.244	-	30.291	52.953	15.318	926.109	77.697	-	141.841	3.072.295

According to the current recultivation of excavation plans, lignite mines of the Capital Group estimate that relevant costs will be incurred in the years 2032-2081 (for Lignite Mine Bełchatów) and in the years 2041-2090 (for Lignite Mine Turów).

Year ended 31 December 2009

	Post-employment benefits	Provisions for jubilee benefits	Provisions for third parties claims	Provisions for legal disputes	Provisions for purchase of CO ₂ emission rights	Provisions for employee claims	Provisions for recultivation of final excavations and ash storages	Provisions for liquidation of property, plant and equipment	Provisions for certificates of origin held for redemption	Other provisions	TOTAL
<i>(restated)</i>											
As at 1 January 2009	1.085.578	825.453	285.285	99.613	391.271	27.619	983.768	73.183	367.744	229.409	4.368.923
Costs of present employment	23.714	38.438	-	-	-	-	-	-	-	-	62.152
Actuarial gains and losses excluding discount rate adjustment	76.172	17.328	-	-	-	-	-	-	-	-	93.500
Benefits paid	(46.677)	(77.044)	(100)	-	-	-	-	-	-	-	(123.821)
Costs of past employment	9.867	-	-	-	-	-	-	-	-	-	9.867
Revaluation of provision/ discount rate adjustments	(76.061)	(29.898)	-	-	-	-	(147.811)	-	-	-	(253.770)
Interest costs	63.644	42.064	-	-	-	-	48.734	3.865	-	1.650	159.957
Created during the year	-	-	61.874	29.192	170.509	965	55.023	25.775	735.727	577.433	1.656.498
Reversed	-	-	-	(34.016)	(10.405)	(286)	(30.730)	-	(1.145)	(128.749)	(205.331)
Used	-	-	-	(9.446)	(168.350)	(329)	(5.323)	(768)	(687.171)	(95.170)	(966.557)
Other changes	(4.535)	(14.475)	3.964	35	-	1.380	-	-	-	18.293	4.662
As at 31 December 2009	1.131.702	801.866	351.023	85.378	383.025	29.349	903.661	102.055	415.155	602.866	4.806.080
Short-term	88.906	82.597	351.023	52.756	311.004	5.357	6.236	3.902	415.155	250.385	1.567.321
Long-term	1.042.796	719.269	-	32.622	72.021	23.992	897.425	98.153	-	352.481	3.238.759

35.1. Provisions for post employments benefits

The amount of provisions disclosed in the financial statements results from the valuation prepared by the independent actuary and was described in note 34 to the foregoing financial statements.

35.2. Provisions for jubilee benefits

According to the corporate system of remuneration the employees of the Group entities are entitled to jubilee awards. These awards are paid after an employee has worked a specified period of time. The amount of awards paid depends on the period of employment and the average remuneration of the employee. The entity recognizes a provision for future obligations relevant to jubilee awards in order to assign costs to the periods they refer to. The current value of these obligations is measured by an independent actuary at each balance sheet date.

35.3. Provisions for third-party claims

Provisions presented in this position relate mainly to dispute of the parent company with Alpiq Holding AG. The issue was described in note 38 to the foregoing consolidated financial statements.

35.4. Provision for legal disputes

Provisions for the use of land

Entities of the PGE Group create provisions related to a non-agreed usage of property. This issue mainly relates to distribution companies, which own distribution grids. As of the reporting date the provision amounted to ca. PLN 64 million. The provision is created to cover claims under court proceedings.

Claim of Tajfun Real Sp. z o.o.

In 2005, EXATEL S.A. filed a statement on termination of the Lease Agreement of Tajfun building in Warsaw, effective 1 August. Tajfun Real Sp. z o.o. filed to the Court of Arbitration at National Chamber of Commerce, a claim to establish that the Lease Agreement is binding for both parties until 31 July 2010 and related to the payment of the rent for August 2005. On 24 January 2006, Tajfun Real Sp. z o.o. terminated to lease agreement without the period of notice. By the verdict of 11 May 2007, the Supreme Court dismissed the further appeal of EXATEL S.A. related to the verdict of the Appeal Court in Warsaw of 8 November 2006 which confirmed that the Agreement on lease of the Tajfun building was binding until 31 July 2010. On 11 September 2007, Tajfun Real Sp. z o.o. filed to the Court of Arbitration at National Chamber of Commerce a claim for payment the rent for the period from September to January 2006. As at the balance sheet date the related provision amounted to PLN 12.047 thousand. The Management Board of EXATEL S.A. commenced actions aimed at conciliatory finishing of the dispute, in the form of an amicable settlement on the subject issue between EXATEL S.A. and Tajfun Real Sp. z o.o.

35.5. Provisions for costs of recultivation

Provision for recultivation of mine storage

According to regulations of the Act of 3 February 1995 on Agricultural and Forest grounds and regulations of the Act of 4 February 1994 on Geological and Mining Law, the entrepreneur causing loss or reduction of value in the use of the ground is obliged to recultivate the ground at the entrepreneur's expense.

Lignite Mine Bełchatów and Lignite Mine Turów create provisions for recultivation of final excavations. Costs of recultivation of final excavations are reflected and settled throughout the period of the exploitation of mines, with the use of the depletion method based on the rate of coal excavation. The provision as at the end of the period is calculated as a product of the discounted total cost of recultivation divided by the rate of coal excavation, less period-end value of Mine Liquidation Trust created in accordance with Geological and Mining Law.

Provision for recultivation of ash storages

The PGE Group producers create provisions for recultivation of ash storages. The provision is created with the use of the natural method - proportionally as the storage is filled. The provision at the end of each year is calculated as a product of the discounted value of total recultivation costs for the given year and the proportion in which the storage is filled.

35.6. Liquidation of property, plant and equipment

The provision for liquidation of property, plant and equipment relates to assets of Elektrownia [Power Plant] Turów, which are going to be excluded from the production until year 2013. The obligation of liquidation and recultivation of the area results from „The integrated permission for running electric energy and heat energy producing installation” in which the restitution of the area was specified. The amount of created provision was established on the basis of expected liquidation expenses and was recognized on the debit side in initial value of property, plant and equipment. Depreciation of activated liquidation expenses which is calculated on the basis of the estimated economic useful life of an appropriate item of property, plant and equipment as well as change in provision value resulting from reversal of the discount as at the balance sheet date influence on financial result of the Group. As at the balance sheet date, the value of provision amounts to PLN 95 million.

35.7. Provision for energy origin units held for redemption

The companies from the Group create provision for the amount of certificates of origin related to sales in the current or previous reporting periods, in amount of certificates not redeemed till the balance sheet date. The provision as at 31 December 2010 amounted to PLN 563 million.

35.8. Other provisions

Dispute concerning the scope of taxation with real estate tax.

The main caption of other provisions is a provision covering declared and predicted claims relating to real estate tax. The matter of dispute was described in detail in note 40 of the foregoing consolidated financial statements.

Dispute concerning the redemption of energy origin units of ownership

Energy companies included in the Group are parties to proceedings against the Energy Regulatory Office, related to an obligation of redemption of energy units of origin – so called green and red certificates. As at 31 December 2010 the provision created to cover possible penalties amounted to PLN 38 million. The final value of possible penalties will depend on the results of the court proceedings and may be subject to change.

Annual bonus

Employees of PGE Capital Group are entitled to the "annual bonus" paid on the basis of the corporate collective labor agreement or regulations applicable to individual entities. As at 31 December 2010 created provisions amounted to PLN 68 million.

Provision for unused annual leave

The Group creates provision for employee benefits related to unused annual leave. As at 31 December 2010 the provision amounted to PLN 55 million.

36. Other non-financial liabilities

The non-financial liabilities for the years ended 31 December 2010 and 31 December 2009 are as follows:

	As at 31 December 2010	As at 31 December 2009 <i>restated</i>
Liabilities from dividends	116.861	1.810
Excise tax	93.336	81.737
VAT tax	182.335	314.392
Real estate tax	8	4.094
Liabilities from social insurances	226.147	207.868
Personal income tax	70.124	64.249
Distribution from profit	-	869
Environmental fees	116.853	99.397
Payroll	264.518	213.564
Third party payments related to future periods	117.533	173.684
Other	208.498	36.165
Total	1.396.213	1.197.829

The "other" position comprise mostly of the liability related to advances on deliveries received, payments to the Corporate Fund for Employment Benefits, the Employment Pension Program and to the State Fund for Rehabilitation of Persons with Disabilities.

37. Deferred income and government grants

Government grants	As at 31 December 2010	As at 31 December 2009
Redemption of loans from environmental funds	42.261	42.447
Other government grants	133.371	35.966
Total deferred income, including:	175.632	78.413
Long-term	171.218	75.284
Short-term	4.414	3.129

Other deferred income	As at 31 December 2010	As at 31 December 2009
Property, plant and equipment acquired free of charge	131.990	139.807
Subsidies granted and connection fees	839.048	880.571
Lease income	3.269	3.609
Other deferred income	62.771	31.309
Total deferred income, including:	1.037.078	1.055.296
Long-term	941.335	1.017.522

Short-term	95.743	37.774
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Government grants presented in the consolidated financial statements represent, mainly, the value of redeemed loans granted by environmental funds. A portion of loans from environmental funds is redeemed under the condition that they are used for investments aimed at protection of the environment.

Furthermore, in May 2010, PGE Elektrownia Bełchatów S.A. (current name: PGE Górnictwo i Energetyka Konwencjonalna S.A.) entered into an agreement with the European Commission for co-financing of a demonstration project entitled "Construction of a Carbon Capture and Storage System", with a value of EUR 180 million. The funds obtained by Bełchatów Power Plant for co-financing the project will be allocated to one of the key components of the CCS system, i.e. the CO₂ capture component. The amount of grant, which is presented in the above table, is approximately PLN 68 million.

Subsidies granted in caption other deferred income comprise mainly fees received until 1 July 2010 for connection to power network, which are presented as donations to property, plant and equipment in the foregoing consolidated financial statements. The issue of change in accounting policy related to fees for connection to power network was described in note 13.34 to the foregoing consolidated financial statements.

38. Legal claims and contingent liabilities and receivables.

	As at 31 December 2010	As at 31 December 2009
Contingent liabilities		
Credit collateral	-	250
Repayment of bill collateral	-	4.425
Liabilities from bank guarantees	-	50
Collaterals for repayment of bank guarantees granted	-	25
Legal claims	8.598	11.556
Contractual fines and penalties	12.481	6.880
Damages related to non-agreed usage of property	-	7.099
Real estate property buyout	-	536
Other contingent liabilities	180.338	85.097
Total contingent liabilities	201.417	115.918

Presented below are the most significant legal claims and other contingent liabilities in the PGE Capital Group.

38.1. Contractual fines and penalties

Contingent liability concerns contractual fines for delays in realization of investments commenced by the Mayor of Gryfino City and Commune for PGE Zespół Elektrowni Dolna Odra S.A. In December 2010 proceedings were suspended.

38.2. Other contingent liabilities

Other contingent liabilities mainly (PLN 126 million) comprise mainly of possible refund of means that were received by PGE Group entities from environmental funds for chosen investments. If an investment does not bring expected environmental effect, a relevant financing will have to be reimbursed. Furthermore, in this position are presented, among others, values of environmental disputes and contractors claims related to allowing excise tax in the price of electricity.

38.3. Other legal and court issues

Risk related to PGE - ATEL (presently Alpiq Holding AG) dispute.

On 28 October 1997 PSE S.A. (presently PGE Polska Grupa Energetyczna S.A.) entered into an electricity supply agreement with Atel for a term of 16 years, i.e. from January 1, 1998 to September 30, 2014 (the "Agreement"). The Agreement had been executed in accordance with the terms prescribed therein by both parties until 2007. However, as a result of changes in Community laws, a legal dispute occurred between the Parties as regards discontinuation of proper performance by the Polish party.

In 2004, as a consequence of implementation of European Union legislation concerning distinguishing of a separate transmission system operator (so-called unbundling), after splitting of PSE-Operator S.A. from the organizational structure of PGE S.A. (formerly PSE S.A.), the procedure of implementing the Agreement had to change, as PSE-Operator S.A. became the only company allowed to transmit electricity. Therefore, on July 2, 2004 the Company entered into an agreement with PSE-Operator S.A. for provision of transmission capacity for purposes of executing historical contracts, which regulates the terms of providing transmission capacity for the Agreement. Trans-border capacity necessary for executing the Agreement was booked yearly, outside the auction scheme. The Agreement was executed without interruption until the end of 2007. At the end of 2006, EU laws concerning reservation of trans-border transmission capacity were changed. On the basis of these changes, booking of any trans-border capacity for historical contracts, disregarding the auction rules, has become illegal. Referring to these changes, PSE-Operator S.A. notified a force majeure occurrence, and demanded termination of the transmission agreement with PGE. Therefore, PGE sent a similar notice to Atel, stating that certain force majeure circumstances occurred, preventing implementation of historical long-term export contract without guaranteed booking of appropriate trans-border capacity, and calling Atel to renegotiate the Agreement. Atel refused to accept PGE's

reference to Force Majeure and demanded that the implementation of the Agreement would be continued without adapting to new legal, technical and economic realities, stating that otherwise it shall pursue indemnity from PGE for failure to supply.

Finally, Atel notified the Company in 2009 of no intention to continue negotiations.

Arbitration proceedings commenced pursuant to a Request for Arbitration of 1 March 2009. The Request included a preliminary statement of Alpiq's claims and the scope of proceedings.

An organizational session took place on 11 December 2009, at which the timing of the entire proceedings was agreed until April 2011. During that meeting it was agreed that Alpiq should file a Statement of Claim until 1 March 2010, with an exhaustive presentation of its claims and evidence to support these claims, identifying the witnesses and experts. A similar requirement was imposed on PGE in regard of the obligation to file a Statement of Defense until 15 June 2010 at the latest.

In the Statement of Claim dated 1 March 2010, Alpiq demanded payment by PGE of an amount exceeding EUR 67 million for alleged losses incurred during the period from 1 March 2008 to 28 February 2009. On 4 October 2010 Alpiq filed the Claimant's Reply to Respondent's Statement of Defense. In its reply, Alpiq rephrased the claims from the original Statement of Claim entirely and requested that a total amount of nearly EUR 150 million be adjudicated to the benefit of itself, to be paid by PGE for the period from 1 March 2008 until the end date of the term of Agreement. Alpiq further attached testimony of three new witnesses and two expert opinions (by economic and technical experts).

Pursuant to strong objection by PGE attorneys against such a major extension of claims, the Arbitration Tribunal issued a procedural decision extending the deadline for PGE S.A. to file another substantive procedural writ until February 14, 2011. Within the prescribed deadline, PGE S.A. filed a Rejoinder to Alpiq's Reply. Testimony of witnesses as well as two opinions by foreign experts (economic and technical) and one opinion by a Polish expert were attached to the writ of procedure.

The final hearing, which will summarize the outcomes of proceedings in writing and during which witnesses and experts will be heard by the Arbitration Tribunal, is scheduled for early April 2011.

On the basis of available data, to its best knowledge, PGE S.A. made a reasonable estimation of claims which can be reasonably considered justified by the Arbitration Tribunal. The Company established a provision for the claim thus estimated, in the amount exceeding EUR 88 million (including the main amount of EUR 79 million).

At the present stage of arbitration proceedings, it is not possible to foresee the outcome or to determine the final amount of indemnity.

PGE Polska Grupa Energetyczna S.A. - ŻEG Sp. z o.o. claim

On 17 May 2006 the Company informed Żarnowiecka Elektrownia Gazowa Sp. z o.o. (ŻEG Sp. z o.o.) of a breach of agreement for supply of electric power and energy signed on 30 December 1998. The obligations resulting from the agreement included, among others, the construction of a gas power plant by ŻEG Sp. z o.o., in a proper term, and commencing supplies of electric energy to the Company. On 14 May 2003, ŻEG Sp. z o.o. informed PGE S.A. about the breach of its contract. The breach had to be followed by study prepared on the behalf on the Company referring to restructuring of long term contract (LTC), the part of which the Company was. In ŻEG Sp. z o.o. opinion the publication of the study on restructuring of LTC resulted in the refusing the credit by the bank, that was supposed to finance the construction of the gas power plant indicated in the agreement. The company did not consider claims of ŻEG Sp. z o.o. On 17 May 2006, the Company informed ŻEG Sp. z o.o. about the breach of the agreement by ŻEG Sp. z o.o. which was not to put into exploitation the agreed gas power plant. The Company is unable to fairly and reliably assess the value of the potential claim

As the deadlines were not kept, the Company terminated the agreement and demanded a penalty payment amounted to USD 15.520.000 (equivalent of PLN 47.553.280) and the transfer of ownership of the power plant being the subject of the agreement. None of the parties has taken the proceeding yet. There is evidence to state that the claims of both parties expired. However, the court proceeding

is still possible. The eventual dispute would take place in the court of arbitration in Wien or Warsaw in accordance with the UNCITRAL Arbitration Rules.

Contractual liabilities related to the purchase of gas from PGNiG

According to the concluded agreements on the purchase of gas, the PGE Group heat and power stations are obliged to collect the minimum volume of gas fuel and not to exceed the maximum level of collection of gas fuel in particular hours and months. If an entity does not collect a minimum volume of gas fuel, is obliged to pay appropriate fee calculated in accordance with the formula specified in the agreements. The agreements also allow collect the gas fuel that is paid for but not collected, in the period of three years. The terms of the agreements according to which the buyer is obliged to pay for the uncollected gas fuel may be a source of significant financial liabilities of the heat and power stations in case of appearing of not collected gas fuel. In the opinion of the Group, the terms and conditions of gas fuel deliveries from PGNiG do not differ from other gas fuel deliveries conditions on the Polish market.

Non-agreed usage of property

Due to the nature of its activities the companies of the Capital Group use many properties, on which the buildings and structures or devices used to the transmission of the electricity are based. In respect of many properties there are doubts as to the title of usage. In the case of property, for which the Group companies have no legal title or the title is doubtful, there is a risk of claims by their owners, the alleged owner or other person for compensation in respect of non-agreed usage of these properties. As described in note 35.4 to the foregoing consolidated financial statements the relevant provision is created to cover claims under court proceedings. Moreover, there are disputes at an early stage in the Group as well as there is a possibility of increased number of disputes in the future.

Legal issues related to the Consolidation Programme

The legal issue related to the claims of some shareholders of the companies merged within the Consolidation Programme, were described in note 45.2.2. to the foregoing financial statements.

38.4. Contingent receivables

As at balance sheet date, the Group has ca. PLN 52 million of contingent receivables related to a reimbursement of VAT and financing received from the National Fund for Environmental Protection and Water Management to realize a project of purification of mining water in PGE Górnictwo I Energetyka Konwencjonalna S.A. Oddział KWB Turów S.A.

Additionally, the matter of a possible excise tax refund for the years 2006-2008 described in detail in note 45.5 to the consolidated financial statements.

39. Investment liabilities

As at the balance sheet date, the Group was obliged to incur capital expenditures on property, plant and equipment in the amount of PLN 5.433.823 thousand. These amounts relate to modernization of Group's assets and a purchase of machinery and equipment. The major investment currently realized in the Group is the construction of an 858 MW block together with a transmission line realized by PGE Górnictwo I Energetyka S.A. in Bełchatów Power Plant. The estimated capital expenditures related to this investment to be incurred amount to PLN 490 million. Other significant investment liabilities concern:

- The modernization of blocks form no. 7-12 in Elektrownia Bełchatów for the total amount of ca. PLN 3.301 million;
- The modernization of blocks no. 5 and 6 in Elektrownia Bełchatów. for the total amount of ca. PLN 310 million;

- The construction of installation for desulfurization of fumes and construction of biomass cauldron in PGE Power Plants Dolna Odra. for a total amount of ca. PLN 268 million;
- Investment liabilities of PGE Dystrybucja S.A. in total amount of ca. PLN 386 million.

40. Tax settlements

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

From the point of view of economic units, the most important is the taxation of incomes (corporate income tax), taxation of turnover (value added tax, excise tax) followed by taxation of assets (real estate tax and vehicle tax). Other payments classified as quasi – taxes cannot be omitted. Among these there are social security charges and in case of entities solely owned by the State Treasury – distribution from profit.

Basic tax rates in 2009 were as follows: corporate income tax – 19%, basic value added tax rate – 22%, lowered: 7%, 3%, 0%, furthermore some goods and products are subject to tax exemption.

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

The significant proceedings regarding public and state settlement within the Capital Group entities are presented below.

40.1. Excise tax

For details on a possible excise tax refund for the years 2006-2008 for production entities please refer to note 45.5 of the consolidated financial statements.

PGE Górnictwo i Energetyka Konwencjonalna S.A Oddział Elektrownia Turów.

In the period from 2 June 2008 to 24 July 2008, Elektrownia Turów was facing a control of a customs office related to excise tax settlement for the period from 1 January 2006 to 31 December 2006. After the control, the entity submitted remarks and asked the customs office for adequate explanations on the control protocol (in relation to possible surplus payment). In the following actions taken, the entity adjusted "Statements on volume and manner of using the released electricity" (adjustment of these documents does not have any impact on the value of the excise tax). However, as there was no unambiguous explanation on the surplus payment from the customs office, the entity filed a motion to the Minister of Finance demanding an individual interpretation. As a result of a negative response from the Minister of Finance, the Entity filed a complaint to Regional Administrative Court (WSA) in Wrocław on 11 February 2009. On 13 July 2009, due to the incorrect legal foundation of the interpretation, the Regional Administrative Court decided about reversal of complained interpretation. In January 2010, the company received a changed interpretation of the Minister of Finance in which it was reconfirmed that the entity's opinion is incorrect. In February 2010, PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Turów. issued an appeal to remove the legal provision. The authority did not recognize sufficient grounds for changing its opinion, hence Elektrownia Turów lodged another appeal to the Provincial Administrative Court in Wrocław, which again repealed the tax interpretation. The Minister of Finance filed a further appeal in cassation proceedings to the Supreme Administrative Court against the Wrocław Court's ruling – until the day of preparation of the consolidated financial statements, the issue was not settled.

40.2. Real estate tax

There are tax proceedings carried out to determine the scope subject to real estate tax in PGE Capital Group power stations. Based on the proceedings performed the amount of tax liabilities in particular entities was determined. The proceedings encompassed all years for which the tax liability was not expired. The dispute is related to the subject of taxation and concerns mainly a decision whether installations in buildings and technical machinery should be taxed as autonomous constructions. Within the proceedings held, the power stations carry out disputes at the level of tax authorities and the verdict that was pronounced for one of the power stations did not constitute for an essential solution. The verdicts of Provincial Administrative Courts relate to the above matter were different, however the most recent verdicts (including the verdict of the Supreme Administrative Court of 2 February 2010 sign. II FSK 1292/08) indicate that the machinery located in buildings might be a subject of taxation as autonomous constructions.

In order to define the subject of taxation, the act on taxes and local fees refers to building legal regulations, the amendment of which is unfavorable for PGE Group entities. The definition of the building was change with an act of 23 April 2009 on the change to building law act and other acts (including the act on taxes and local fees). According to the new definition, the notion of a building also comprises installations and technical machinery used for exploitation of a particular building. It is possible that the change of this definition will cause that the notion of a building will be expanded and comprise installations and technical machinery located in buildings, including the buildings of electric energy producing entities, which were hitherto considered as part of a building. According to the Ministry of Finance, the change of the definition of a building is only specifying of the regulation and should not influence the scope of taxation of particular building objects with real estate tax. The change in building law regulations could mean that the scope of taxation has always been interpreted so widely or lead to a conclusion that the scope of taxation was expanded since amendment of building regulations came into force. At the moment the mentioned change in building law regulations has not come into force yet due to the submission the request by the President of Poland to the Constitutional Court to examine the compatibility of some regulations with the constitution.

Taking into consideration changes mentioned above and proceedings carried out in the Group entities as at 31 December 2010, the Group discloses appropriate provisions. No further details are disclosed due to the professional secret, which is compliant with IAS 37.92.

41. Information on related entities

Transactions with related entities are concluded using current market prices of provided goods, products and services based on the cost of manufacturing.

41.1. Associates

The information on investments in associates accounted for using the equity method is presented in note 25.

	Sale to related parties	Purchase from related parties	Receivables from related parties	Liabilities towards related parties
2010	45.442	31.143	5.570	7.015
2009	36.941	21.687	5.281	2.879

41.2. Transactions with State Treasury entities

The State Treasury is the dominant shareholder of PGE Polska Grupa Energetyczna S.A. and as a result in accordance with IAS 24 *Related Party Disclosures*, State Treasury companies are recognized as related entities. PGE Group entities identify in detail transactions with almost 40 of the biggest State Treasury related companies. The total value of transactions with such entities is presented in the table below.

	Sale to related parties	Purchase from related parties	Trade receivables from related parties	Including overdue	Trade liabilities towards related parties	Including overdue
2010	4.291.017	4.915.880	307.300	897	478.873	-
2009	4.709.255	5.581.066	423.245	43.179	523.156	444

(restated)

**the restatement of the data for 2009 resulted in taking into account the additional State treasury companies, from which the Group buys the production fuel.*

The most important transactions with State Treasury entities refer to PSE-Operator S.A., professional power stations, regional energy companies and purchase of coal from Polish mines.

41.3. Key management personnel remuneration

The key management comprises of the Management Boards and Supervisory Boards of the Group entities i.e. entities included in main business lines presented in note 2 to the foregoing consolidated financial statements.

	Year ended 31 December 2010	Year ended 31 December 2009 (restated*)
Short-term employee benefits (salaries and salary related costs)	40.738	45.683
Jubilee and retirement benefits	491	1.061
Post-employment benefits	1.236	831
Termination benefits	1.019	1.322
Share-based payments	-	-
Total remuneration paid to key management	43.484	48.897

	Year ended 31 December 2010	Year ended 31 December 2009 (restated*)
The Management Board of the Parent	3.725	3.844
The Supervisory Board of the Parent	648	767
The Management Boards – subsidiaries	32.147	35.219
The Supervisory Boards – subsidiaries	6.964	9.067
Total	43.484	48.897

* the amounts refer to the Management Board and the Supervisory Board of the parent company comprise also of the remuneration of merged Companies (PGE Górnictwo i Energetyka S.A., PGE Energia S.A. and PGE Electra S.A.) for respective periods.

Furthermore, remuneration of the Management Boards and Supervisory Boards of other subsidiaries during the reporting period amounted to PLN 21.476 thousand and PLN 19.044 thousand in comparable period.

For detailed information on the remuneration of the Management Board and the Supervisory Board of the parent company please refer to note 1.6 of the Management Report on activities of PGE Capital Group.

42. Financial instruments

42.1. Carrying amount and fair value of categories and classes of financial instruments

Categories and classes of financial assets:	Carrying amount						Fair value		
	31 December 2010			31 December 2009			31 December 2010	31 December 2009	
	Long-term	Short-term	Total	Long-term	Short-term	Total	Total	Total	
1. Held-to-maturity investments									
(i) Bonds, bills and notes receivable acquired	-	-	-				-		
Total held-to-maturity investments:	-	-	-				-		
2. Loans and receivables, including:									
(i) Trade receivables	a)	-	2.094.506	2.094.506	-	2.059.119	2.059.119	2.089.327	2.054.595
(ii) Deposits and investments		50	114	164	1.226	24.344	25.570	164	25.570
(iii) Other financial loans and receivables		406.938	795.936	1.202.874	387.738	962.891	1.350.629	1.202.874	1.354.651
▪ Bonds, bill and notes receivable acquired	b)	253.538	-	253.538	238.204	46.737	284.941	253.538*	284.941*
▪ Originated loans	b)	141.863	32.540	174.403	144.391	25.885	170.276	174.403	174.298
▪ Other financial receivables	b)	11.537	317.891	329.428	5.143	159.640	164.783	329.428	164.783
▪ LTC compensations	b)	-	445.505	445.505	-	730.629	730.629	445.505	730.629
Total loans and receivables:		406.988	2.890.556	3.297.544	388.964	3.046.354	3.435.318	3.292.365	3.434.816
3. Available-for-sale financial assets, including:									
(i) Shares in entities not quoted on active markets		90.622	119.000	209.622	193.534	688	194.222	n/a	n/a
(ii) Shares quoted on active markets		1.953	-	1.953	1.854	-	1.854	1.953	1.854
(iii) Investment funds' units		2.667	3.917	6.584	-	4.617	4.617	6.584	4.617
(iv) Other financial assets available for sale		-	8.007	8.007	2.823	679	3.502	8.007	3.502
Total available-for-sale financial assets:		95.242	130.924	226.166	198.211	5.984	204.195	16.544	9.973

	Carrying amount						Fair value	
	31 December 2010			31 December 2009			31 December 2010	31 December 2009
Categories and classes of financial assets:	Long-term	Short-term	Total	Long-term	Short-term	Total	Total	Total
4. Cash and cash equivalents	-	2.730.423	2.730.423	-	7.712.823	7.712.823	2.730.423	7.712.823
Financial assets not included in IAS 39								
Lease receivables	b)	843	613	1.456	602	340	942	1.456
							1.456	942

* as described in note 44.5.1 of the foregoing consolidated financial statements, the main item in the caption "bonds, bills and notes receivable acquired" are bonds issued by the company Autostrada Wielkopolska S.A. The bonds are measured at amortized cost with the use of an effective discount rate. Taking into account that these bonds are not quoted on an active market and are subject to variable interest rate as well as the fact, that there is no available information on current market credit margin applicable to similar financial instruments, the Company assumed that the bonds' book value is approximately the fair value for the purpose of a disclosure compliant with IFRS 7. The Company is currently in the process of determining the fair value of this financial instrument.

- a) Long-term trade receivables are presented in the statement of financial position as "Other long-term financial assets". Short-term trade receivables are presented in the statement of financial position as "Trade receivables".
- b) These are presented in the statement of financial position as "Loans and receivables".

	Carrying amount						Fair value	
	31 December 2010			31 December 2009			31 December 2010	31 December 2009
Categories and classes of financial liabilities:	Long-term	Short-term	Total	Long-term	Short-term	Total	Total	Total
1. Financial liabilities at fair value through profit or loss held for trading:								
(i) Derivatives	-	41.165	41.165	-	37.701	37.701	41.165	37.701
Total financial liabilities at fair value through profit or loss:	-	41.165	41.165	-	37.701	37.701	41.165	37.701
2. Financial liabilities at amortized cost:								

Carrying amount							Fair value		
31 December 2010				31 December 2009			31 December 2010	31 December 2009	
Categories and classes of financial liabilities:		Long-term	Short-term	Total	Long-term	Short-term	Total	Total	Total
(i) Interest bearing loans and credits	a)	1.804.429	914.956	2.719.385	4.056.270	855.018	4.911.288	2.728.942	4.947.462
(ii) Bonds issued	a)	-	-	-	-	114.911	114.911	-	114.911
(iii) Trade liabilities		-	986.301	986.301	-	1.082.582	1.082.582	984.544	1.080.641
(v) Other financial liabilities at amortized cost	b)	7.908	1.255.608	1.263.516	15.285	565.557	580.842	1.263.516	580.842
Total financial liabilities at amortized cost:		1.812.337	3.156.865	4.969.202	4.071.555	2.618.068	6.689.623	4.977.002	6.723.856
3. Other financial liabilities not included in IAS 39									
(i) Liabilities from finance lease and lease agreements with option of purchase	b)	6.495	3.870	10.365	656	1.014	1.670	n/a	n/a
Total other financial liabilities:		6.495	3.870	10.365	656	1.014	1.670	-	-

a) These are presented in the statement of financial position as "Interest bearing loans and borrowings"

b) These are presented in the statement of financial position as "Other financial liabilities"

42.2. Statement of comprehensive income

	Assets and liabilities at fair value through profit or loss	Available-for-sale financial assets	Held-to-maturity financial assets	Loans and receivables	Financial liabilities at amortized cost	Total financial instruments by class
Year ended 31 December 2010						
Dividends	-	8.437	-	-	-	8.437
Gains / (losses) from interest	234.618	476	168	70.348	(189.504)	116.106
Gains / (losses) from foreign exchange	23.803	(1)	-	(21.528)	(33.693)	(31.419)
Reversal of revaluation write offs / increase of value	3	2.804	-	51.409	-	54.216
Creation of revaluation write offs / decrease of value	-	(19.838)	-	(91.821)	(3.464)	(115.123)
Gains / (losses) on investment disposal	16	3.376	(38)	109	-	3.463
Total net profit / (loss)	258.440	(4.746)	130	8.517	(226.661)	(35.680)
Year ended 31 December 2009						
Dividends	-	12.497	-	-	-	12.497
Gains / (losses) from interest	84.319	6.387	-	46.253	(259.049)	(122.090)
Gains / (losses) from foreign exchange	47.020	(32)	-	(29.130)	(6.276)	11.582
Reversal of revaluation write offs / increase of value	25.018	1.868	2.202	36.280	1	65.369
Creation of revaluation write offs / decrease of value	-	(5.082)	-	(97.264)	(30.016)	(132.362)
Gains / (losses) on investment disposal	147	54.529	1.928	8.345	-	64.949
Total net profit / (loss)	156.504	70.167	4.130	(35.516)	(295.340)	(100.055)

During the period ended 31 December 2010, the amount of PLN 80 thousand, net of the effect of deferred tax, related to a measurement of available-for-sale financial assets was reflected in other comprehensive income.

42.3. Fair value of financial instruments

The book value of the following assets and liabilities constitutes a reasonable estimate of their value:

- held-to-maturity investments, based on variable interest rates,
- available-for-sale financial assets except for shares in entities not quoted on an active markets,
 - financial assets and liabilities at fair value through profit or loss.

42.3.1 Financial instruments quoted on active markets (shares, bonds)

Fair value of shares and bonds listed on a stock exchange were measured on the basis of the closing rate of these financial instruments, published on the Internet page of the Warsaw Stock Exchange S.A. as at the balance sheet date.

42.3.2 Financial instruments not quoted on active markets, for which the fair value can be measured reliably

Fair value of instruments not quoted on active markets is measured by the Group with the use of an appropriate valuation method as long as a reliable measurement is possible with the use of prices from the most recent transactions conducted under standard market rules; a comparison with prices from other instruments' active markets, which are essentially identical; analysis of discounted cash flows and other methods/techniques of measurement commonly used on the market, suitable for particular specifics and characteristics of a measured financial instrument and the situation of the issuer (drawer).

Fair value of the Group's financial instruments not quoted on active markets is based on market prices or with the use of valuation methods for which input data can only be observed market data, which are obtained from renowned providers of financial information.

Fair value of derivative transactions of an IRS type is based on the market curve of future interest rates. Risk-free interest rates used for discounting future cash flows are calculated on the basis of quotations of IRS transactions on the inter-bank market, obtained from the Reuters agency.

42.3.3 Financial instruments not quoted on active markets, for which the fair value cannot be measured reliably

Basic assets of the Company classified as available-for-sale financial assets are shares in entities not quoted on active markets. For shares in entities that are not listed, there is no active market nor is there a possibility of using measurement techniques for reliable valuation of given shares. Due to the above, the Company is not able to establish a range of reasonable fair value estimates. Such assets are measured at cost of acquisition less impairment losses.

As at the balance sheet date the main position presented in stock and shares in entities not quoted on active markets were shares in AWSA Holland II, representing 55% of this kind of instruments. Due to the process of sales of shares, PGE Capital Group did not disclose fair value of financial instrument mentioned above.

42.4. Description of significant positions within particular classes of financial instruments

42.4.1 Loans and receivables

The most significant position of loans and receivables are trade receivables, described in detail in note 43.7

42.4.2 Available-for-sales financial assets

The most significant positions of available-for-sale financial assets are shares in entities not quoted on active markets and shares quoted on active markets. The Group is not able to reliably estimate the fair value of entities that are not quoted on active markets, therefore the value of these is presented in the purchase price adjusted by applicable revaluation write-offs.

As at 31 December 2010, the shares of AWSA Holland II BV of the value of PLN 115.173 thousand are the most significant position of shares not quoted on active financial markets.

42.4.3 Financial assets and liabilities at fair value through profit or loss

The most significant positions of financial instruments valued at fair value through the profit or loss are bonds, bills and notes. As at 31 December 2010, the Group did not recognize any financial assets at fair value through profit or loss.

The Group presented IRS hedge transactions, related to swap concluded by PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Turów as financial liabilities at fair value through profit or loss. These transactions were concluded on 18 September 2003 with Citibank N.A. London Branch and are meant to hedge variable (USD LIBOR 6m) interest rates on investment credits granted by Nordic Investment Bank in the value of USD 30, 40 and 80 million.

Based on the transaction, the bank – party to a contract pays to the entity interest based on a variable rate, and PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Turów pays to Citibank interest based on a fixed rate. As a result of the imposition of the IRS transactions on the hedged Nordic Investment Bank credit, the interest rate changed from variable to fix.

Hedge instruments owned by the Group are presented in the table below:

Type of hedge	Description of the hedging instrument	Fair value of the hedging instrument as at the balance sheet date	Description of the risk subject to the hedge
Cash flow hedge	IRS transaction - change of a variable interest rate USD LIBOR 6m to a fixed rate (5,20%) for NIB 40 credit; half-year payments, amortized in accordance to credit repayment schedule	(4.990)	Currency credit in the amount of USD 40 million, interest rate LIBOR 6m+ 0,23% margin; half-yearly payments
Cash flow hedge	IRS transaction - change of a variable interest rate USD LIBOR 6m to a fixed rate (5,2050%) for NIB 30 credit; half-year payments, amortized in accordance to credit repayment schedule	(6.060)	Currency credit in the amount of USD 30 million, interest rate LIBOR 6m +0,18% margin; half-yearly payments
Cash flow hedge	IRS transaction - change of a variable interest rate USD LIBOR 6m to a fixed rate (5,61%) for NIB 80 credit; half-year payments, amortized in accordance to credit repayment schedule	(30.115)	Currency credit in the amount of USD 80 million, interest rate LIBOR 6m +0,5% margin; half-yearly payments
Total		(41.165)	

As the Group does not apply hedge accounting, the change in fair value of the above hedging instruments is recognized in profit or loss in the relevant reporting period.

The above mentioned agreements were concluded in September 2003 and expire in years 2015, 2016 and 2019. The estimation of the fair value of IRS instruments is based on the comparison of discounted future cash flows, so-called "swap legs". The value of cash flows resulting from interest rate on "variable leg" of the transaction and the amount of the discount is calculated on the basis of the curve of market interest rates.

During the period ended 31 December 2010 the Group revaluated the fair value of IRS transaction and recognized the negative accrued valuation of the IRS transaction fair value amounting to PLN 3.464 thousand in the statement of comprehensive income. Furthermore, during the period the Group incurred the costs of swap payments accounting for PLN 18.607 thousand. Taking into account the long-term period of the transactions concluded and that the credit limit granted by the party of the transaction has not been exceeded, the entity did not take any actions aimed at closing the above described transaction.

Data adopted for measurement of the fair value of the above hedge financial instruments have the Level 2 in the fair value hierarchy introduced by the amended in 2009 IFRS 7 item 27A and 27B.

42.4.4 Financial liabilities measured at amortized cost

42.4.4.1 Interest bearing loans and credits

Loans and credits drawn by the Group as at 31 December 2010

Currency	Reference rate	Value of credit / loan as at reporting date (in thousands)		Due in the period:					
		In currency	In PLN	Until 1 year	From 1 to 2 years	From 2 to 3 years	From 3 to 4 years	From 4 to 5 years	Above 5 years
PLN	Variable	755.419	755.419	401.262	187.649	78.835	20.167	13.962	53.544
	Fixed	832.821	832.821	425.960	406.861	-	-	-	-
Total PLN		1.588.240	1.588.240	827.222	594.510	78.835	20.167	13.962	53.544
EURO	Variable	148.112	586.567	333	10.453	10.423	16.796	35.317	513.245
	Fixed	-	-	-	-	-	-	-	-
Total EURO		148.112	586.567	333	10.453	10.423	16.796	35.317	513.245
USD	Variable	108.153	320.578	44.916	44.462	44.462	44.462	38.533	103.743
	Fixed	-	-	-	-	-	-	-	-
Total USD		108.153	320.578	44.916	44.462	44.462	44.462	38.533	103.743
CHF	Variable	70.799	224.000	42.485	42.120	42.120	42.120	34.683	20.472
	Fixed	-	-	-	-	-	-	-	-
Total CHF		70.799	224.000	42.485	42.120	42.120	42.120	34.683	20.472
Total loans and credits			2.719.385	914.956	691.545	175.840	123.545	122.495	691.004

Loans and credits drawn by the Group as at 31 December 2009

		Value of credit / loan as at reporting date (in thousands)		Due in the period:					
Currency	Reference rate	In currency	In PLN	Until 1 year	From 1 to 2 years	From 2 to 3 years	From 3 to 4 years	From 4 to 5 years	Above 5 years
PLN	Variable	2.448.340	2.448.340	336.040	556.037	307.283	305.697	205.580	737.703
	Fixed	1.259.234	1.259.234	427.073	832.161	-	-	-	-
Total PLN		3 707.574	3.707.574	763.113	1.388.198	307.283	305.697	205.580	737.703
EURO	Variable	148.176	608.734	276	10.277	8.408	13.773	11.268	564.732
	Fixed	-	-	-	-	-	-	-	-
Total EURO		148.176	608.734	276	10.277	8.408	13.773	11.268	564.732
USD	Variable	123.171	351.075	43.241	42.755	42.755	42.755	42.755	136.814
	Fixed	-	-	-	-	-	-	-	-
Total USD		123.171	351.075	43.241	42.755	42.755	42.755	42.755	136.814
CHF	Variable	84.180	232.851	37.334	36.824	36.824	36.824	36.824	48.221
	Fixed	3.996	11.054	11.054	-	-	-	-	-
Total CHF		88.176	243.905	48.388	36.824	36.824	36.824	36.824	48.221
Total loans and credits			4.911.288	855.018	1.478.054	395.270	399.049	296.427	1.487.470

Among the borrowing items presented above, the Group presents the following facilities:

- investment credit facility taken out by PGE Elektrownia Opole S.A. from Bank PEKAO S.A. for financing construction of power units 1 to 4, with a carrying value of PLN 832,161 thousand as at December 31, 2010. The above mentioned investment facility is denominated in PLN, at a fixed interest rate, ultimately due for repayment on December 31, 2010.
- investment credit facility taken out by PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Bełchatów from Nordycki Bank Inwestycyjny to finance construction of 858 MW power plant - with a carrying value of PLN 586,567 thousand as at December 31, 2010.

The issue of financing investments in PGE Górnictwo i Energetyka S.A. Oddział Elektrownia Bełchatów was described in Note 42.13 to the foregoing consolidated financial statements.

As at 31 December 2010, the value of available overdraft facilities in current account amounted to PLN 1.195.974 thousand. No other overdraft facilities are available to the Group under other credits as at 31 December 2010. Overdrafts in current account are due for repayment until July 2013.

42.4.4.2 Liabilities from bonds issued

As at 31 December 2010 the Group had no liabilities from bond issued.

Bonds issued as at 31 December 2009.

Currency	Reference rate	Value of the issue as at reporting date (in PLN thousand)	Due in the period:					
			Until 1 year	From 1 to 2 years	From 2 to 3 years	From 3 to 4 years	From 4 to 5 years	Above 5 years
PLN	Variable	114.911	114.911	-	-	-	-	-
	Fixed	-	-	-	-	-	-	-
Total in PLN		114.911	114.911	-	-	-	-	-

In 2010, an agency agreement, which was signed on 11 May 2009 with ING Bank Śląski S.A., was in force. The agreement concerned setting up of a bonds issuance programme targeted at PGE Group companies. The maximum amount of that programme for the Group is 5 billion PLN. Under that programme, PGE S.A. may issue coupon bonds or zero-coupon bonds to Group companies.

In addition, on 9 November 2010, PGE S.A. signed two following agreements, under which the bond issue programme ("Programme") was established:

- Bond Purchase Commitment Agreement ("Commitment Agreement") whose parties, apart from the Company, are Bank Polska Kasa Opieki S.A., Banca Infrastrutture Innovazione e Sviluppo S.p.A., Nordea Bank Polska S.A., ING Bank Śląski S.A. (acting as Lead Arrangers) and Bank Polska Kasa Opieki S.A., Banca Infrastrutture Innovazione e Sviluppo S.p.A., Nordea Bank AB, Nordea Bank Polska S.A. and ING Bank N.V. (acting as Underwriters of the Programme) and ING Bank Śląski S.A. (acting as Issue Agent),
- Bond Issue Programme Agreement ("Programme Agreement") whose parties, apart from the Company, are ING Bank Śląski S.A. (acting as Agent, Issue Agent, Paying Agent and Depository) and Bank Polska Kasa Opieki S.A. and Nordea Bank Polska S.A. (acting as Agents, Paying Sub-Agents and Sub-Depositories).

The maximum Programme amount (representing a maximum aggregate nominal amount of bonds issued and outstanding under the Programme) is PLN 10 billion. The Programme was signed for a period of 36 months from the agreements signing date and shall expire no later than on 8 November 2013.

The Underwriters of the Programme have an obligation to purchase bonds issued by the Company under the Programme, as it is stated in the Commitment Agreement. After the accession of any additional underwriter (as defined in the Commitment Agreement) the aggregate underwriting amount cannot exceed the maximum Programme amount, i.e. PLN 10 billion. Underwriters of the Programme are obliged to purchase bonds during the period from 15 November 2010 till 31 October 2013.

Bonds are to be issued as specified in article 9 paragraph 3 of the Act on Bonds dated 29 June 1995 (Official Journal 2001, no. 120, item 1300 with amendments) based on the Programme Agreement and the Issue Terms, as bearer discount bonds (bearer zero-coupon bonds with maturity of 1, 3 or 6 months but their maturity cannot exceed 6 months. The maturity of the last issue of bonds may be different (but not shorter than 7 days and not longer than 6 months), however the last issue maturity date cannot fall after the Programme maturity date.

Bonds under the Programme will be denominated in Polish zlotys (PLN) and the nominal value of one bond will amount to PLN 100,000. As a rule, the bonds will pay a guaranteed interest rate, defined as the reference rate increased by a guaranteed margin. The reference rate is the appropriate WIBOR for deposits with maturity corresponding to the bond issue maturity (different rules apply for establishing the profitability of the last bond issue and bonds issued for the purpose of, so called, rollovers of the previous bond issues).

The bondholders are entitled to the benefits of monetary nature only.

42.5. Compliance with covenants of credit agreements

PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Bełchatów

In 2006, PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Bełchatów, concluded long-term financing agreements in the total amount of EUR 879 million with the following Commercial banks and European Multilateral Institutions. In 2008, PGE Górnictwo i Energetyka S.A. Oddział Elektrownia Bełchatów received from the Global Credit Agent a notification on alleged infringement of finance agreement conditions. During 2008 and 2009, the company and the creditors were negotiating key conditions on infringement annulment (negotiations concerned among others changes to documentation of financing including mechanism on principles of establishing electricity sale prices, prolongation of agreement with bank's market adviser company and increase margin of interest and fees for unused part of credit.

On 4 March 2010, the Global Credit Agent informed the company that as a result of publication of the consolidation programme within implemented Consolidation Programme (described in detail in note 45.2 to the consolidated financial statements), the First Date of Mechanism Activation compliant with the Agreement on the General Conditions of Project financing occurred. As a result of the above, the Global Credit Agent demands a fulfillment of the contractual conditions by assuring, that all proceeds received by the company resulting from sales of electric energy and producing capacities will be paid to a pointed Revenues Account, from which payments related to business operations of the company can be realized.

On 12 March 2010, the Management Board of PGE Górnictwo i Energetyka S.A. Oddział Elektrownia Bełchatów adopted a resolution related to an intention of an earlier repayment of the majority of the debt in April 2010. The repayment was made on 12 April 2010 from funds raised as a result of bond issuance acquired by PGE Polska Grupa Energetyczna S.A.

42.6. Collaterals for repayment of liabilities

The Group uses many financial instruments and combinations thereof as collaterals for repayment of loans. The most frequently used are agreements of cessions, bills and execution statements. Additionally, the Group uses power of attorney to bank accounts and cessions of receivables.

As at 31 December 2010 and 31 December 2009, the Group has also recognized a mortgage on the 858 MW Block under construction by PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Bełchatów and a registered deposit on movable assets and marketable property rights related to this Block and the agreement for transfer of ownership of steam-gas block as a security in PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrociepłownia Rzeszów.

As at the balance sheet date, assets of the following value were collateral for repayment of liabilities or contingent liabilities:

	Carrying amount of assets being collateral for repayment of liabilities as	
	31 December 2010	31 December 2009
Property, plant and equipment ¹⁾	5.112.145	3.688.228
Inventories	8.220	23.220
Trade receivables ²⁾	318.752	446.926
Cash	63.565	57.186
Other assets	33.943	-
Total assets being collaterals for repayment of liabilities	5.536.625	4.215.560

1) Including assets from finance lease

2) Including receivables subject to pledge and cession of rights

Furthermore, in 2010 PGE Górnictwo i Energetyka Konwencjonalna S.A. and PGE Elektrownia Opole S.A. entered into an alienation agreement with Warsaw Commodity Clearing House (WCCH), to secure electricity purchase or sale transaction. Under the above agreement, the companies placed an order of transfer of emission allowances of 16.762.780 tons EUA. The object of alienation is deposited in the register kept by the National Allowances Trade System Administrator.

The allowances constituting the subject-matter of the alienation agreement were allocated to the companies gratuitously, under the National Allowances Allocation Programme. Great majority of these allowances will be used by companies to meet the requirement to redeem an appropriate quantity of allowances in relation to CO₂ emissions. According to the applied accounting policy, the emission allowances received gratuitously are presented with null value in the statement of financial position. However, the market value of these allowances as at 31 December 2010 is approximately PLN 934 million.

Furthermore, as described in Note 30 to the foregoing consolidated financial statements, according to the Rules of WCCH, PGE Polska Grupa Energetyczna S.A. is obliged to maintain a specified cash balance on its account held with Bank Ochrony Środowiska S.A. The amount of that deposit depends on the value of transactions cleared by WCCH on the given day, and on the quantity and value of open items on electricity forward market. The cash balance maintained as a security deposit on the above mentioned account as at 31 December 2010 was PLN 164.297 thousand.

42.7. Issues related to financial instruments not applicable for the Group

During the reporting period ended 31 December 2010, there were no events in the Capital Group that needed to be disclosed, such as:

- Until the balance sheet date, the Group did not designate any financial instrument at fair value through profit or loss at initial recognition (IFRS 7, item 9, 10, 11),
- There was no reclassification of financial assets that might have changed the method of their measurement (IFRS 7, item 12),
- There were no collaterals held by the Group on any class of assets, which might have improved credit terms (IFRS 7, item 15), nor has the Group taken over any assets resulting from vindications of collaterals it held as security (IFRS 7, item 38),
- The Group has not issued any instruments that contain both a liability and an equity component (IFRS 7, item 17),
- Except from the issued described in not 42.13 of the consolidated financial statements, the Capital Group did not breach any other provisions of credit agreements (IFRS 7, item 18),
- The Group manages assets accumulated on the bank account of the mine liquidation trust; however it does not receive any income from this kind of trust activities (IFRS 7, item 20.c.ii),
- The Group does not apply hedge accounting,
- There were no financial assets acquired at a price significantly different from their fair value (IFRS 7, item 28).

43. Objectives and principles of financial risk management

PGE Capital Group companies, due to their business activities, are exposed to the following types of financial risks:

- Market risk, including:
 - Interest rate risk;
 - Currency risk;
 - Price risk;
- Credit risk;
- Liquidity risk;

Since the contribution of the entities to PGE, the Group manages financial risk in shape and range as presented in further part of this paragraph. Currently the Group is in the stage of elaborating group procedures and policies on financial risk management. In the previous period, financial risk management was executed on the level of entities constituting the PGE Capital Group.

The main objective of financial risk management in PGE Group entities is to reduce fluctuations of cash flows and financial result related to entities' exposure to market risk. The defined objective is realized on the level of PGE Capital Group or on the level of each entity, as long as it is consistent with objectives at the Group level.

Both on the Capital Group level and entity level, the objectives are achieved with the use of the mechanism of natural hedging and hedging derivative transactions in the range compliant with the Group's internal regulations.

None of the PGE Capital Group entities concludes derivative transactions for purposes other than to secure an identified exposure to market risk. As a result, it is prohibited in the Group to conclude speculative transactions, i.e. such transactions that increase the exposure to interest rate risk, currency risk or merchandise risk, in comparison to the risk level resulting from identified sources of entities' exposure to the mentioned types of market risk, the purpose of which is to obtain additional gains on changes of risk level.

The PGE Capital Group applies an active approach to interest rate risk and currency risk management. This approach assumes that the market risk generated by the PGE Capital Group entities shall be transferred to the parent company, i.e. PGE SA with the use of Intra-Group transactions. The active approach to market risk management assumes the following:

- Adjustment of the level of collateral (the ratio of secured exposure in relation to the whole of exposure for interest rate risk and currency risk) to the Group expectations on the shaping of risk factors in order to obtain benefits resulting from expected changes of risk factors,
- Supporting the realization of budgetary assumptions of the Group, realization of investment programmes and Group development strategy with the use of a collateral mechanism against interest rate risk and currency risk.

The function of interest rate risk and currency risk management in the PGE Capital Group is held by the parent company, i.e. PGE SA with active support of other PGE Group entities.

43.1. Liquidity risk

PGE Capital Group entities run an active policy on investment of cash. It means that the entities are monitoring the state of monetary surplus and are forecasting future cash flows, and on such a basis the investment strategy is realized towards cash aimed at realization of the investment strategy objectives.

In case of monetary shortage, PGE Group entities use available financing sources in the order presented below:

- Bank credit granted in current account;
- Bonds issued that are acquired by PGE S.A.

43.2. Interest rate risk

PGE Capital Group entities are exposed to interest rate risk as a result of financing their operating and investment activities with interest bearing indebtedness at variable interest rates or through investments in financial assets at variable or fixed interest rates. On the other hand, financing business activity with indebtedness at a fixed interest rate is related to the opportunity cost risk in case of interest rates' decline.

The entities are exposed to interest rate risk related to deposits placed, cash, investment in bonds issued by Autostrada Wielkopolska S.A. and liabilities from credits granted and bonds issued.

The below table presents the interest rate gap, constituting the Group's exposure to interest rate risk and risk concentration, with regards to currencies and type of interest rate:

		Type of interest rate	Nominal value as at 31.12.2010	Nominal value as at 31.12.2009
Financial assets exposed to interest rate risk	PLN	Fixed	7.458	90.805
		Variable	2.643.817	7.346.595
	Other currencies	Fixed	422.103	390.924
		Variable	86.606	366.228
Financial liabilities exposed to interest rate risk	PLN	Fixed	832.821	1.259.234
		Variable	755.419	2.563.251
	Other currencies	Fixed	-	11.054
		Variable	1.172.310	1.230.361
Net exposure	PLN	Fixed	(825.363)	(1.168.429)
		Variable	1.888.398	4.783.344
	Other currencies	Fixed	422.103	379.870
		Variable	(1.085.704)	(864.133)

Interest on financial instruments of a variable interest rate is updated in periods shorter than one year. Interest on financial instruments of a fixed interest rate are flat throughout the whole period until maturity of these instruments, except for bonds issued by Autostrada Wielkopolska S.A., which were acquired with a discount and are interest-free until 30 November 2018, and since 30 November 2018 are interest bearing at variable interest rate.

The Group is exposed to the risk of change of fair value of SWAP derivatives, resulting from changes of interest rates.

43.3. Currency risk

In PGE Capital Group entities two types of exposure to currency risk can be identified:

Exposure to transaction risk

The risk results from the fact that a portion of cash flows related to core operations of entities is denominated in or indexed to foreign currencies. The other sources of exposure to the risk are capital investments and financing in foreign currencies. Currency risk relates to changes in future cash flows denominated in or indexed to foreign currencies as a result of changes in foreign exchange rates.

Exposure to translation risk

The risk results from translation of carrying amounts of items of assets and liabilities denominated in foreign currency to the functional currency of financial statements of the entities, i.e. PLN. Similar to transaction risk, the lack of certainty of future foreign exchange rates, at which the carrying amounts of items of assets and liabilities shall be translated as at the balance sheet date, causes uncertainty concerning carrying amounts of these items in PLN as at the balance sheet date and relevant financial income and/or expenses resulting from foreign exchange differences recognized in profit or loss

Presented below are main sources of exposure to currency risk:

- Capital expenditures denominated in or indexed to foreign currencies;
- Loans and borrowings of Group entities denominated in foreign currencies;
- Sales (export) of electricity denominated in foreign currencies;
- Purchases of electricity denominated in foreign currencies or purchases of electricity for which part of the purchase is indexed to foreign currency rates;
- Fees denominated in or indexed to foreign currency relevant to purchase of transmission capacities;
- Sales of CO₂ emission rights denominated in or indexed to foreign currencies;
- Purchase of CO₂ emission rights denominated in or indexed to foreign currencies;
- Expenses related to current exploitation of production goods denominated in or indexed to foreign currencies;
- Financial assets of deposit characteristics denominated in foreign currencies.

The below table presents the Group's exposure to currency risk with regards to particular classes of financial instruments:

	Total carrying amount in PLN	Currency position as at 31 December 2010							
		EUR		USD		CHF		SEK	
		in currency	in PLN	in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets									
Deposits and investment	164								
Bonds, bills and notes receivable acquired	253.538	64.020	253.538						
Trade receivables	2.094.506	4.535	17.958	554	1.643	27	86	74	33
Cash and cash equivalents	2.730.423	21.844	86.510	33	96	-	-		
Originated loans	174.403	-	-	-	-	-	-	381.801	168.565
Other financial receivables	329.428	-	-	-	-	-	-		
Shares in entities not quoted on active markets	209.622	-	-	-	-	-	-		
Shares quoted on active markets	1.953	-	-	-	-	-	-		
Other financial assets	14.591	-	-	-	-	-	-		
Lease receivables	1.456	-	-	-	-	-	-		
Compensations related to LTC	445.505	-	-	-	-	-	-	-	-
Financial liabilities									
Derivatives	(41.165)	-	-	(13.888)	(41.165)	-	-	-	-
Interest bearing loans and credits	(2.719.385)	(148.112)	(586.567)	(108.153)	(320.578)	(70.799)	(224.000)	-	-
Bonds and debt instruments issued	-								
Trade and other financial liabilities at amortized cost	(2.249.817)	(25.945)	(102.748)	(276)	(818)	(48)	(153)	(33.653)	(14.858)
Liabilities from finance lease and lease agreements with option of purchase	(10.365)	-	-	-	-	-	-	-	-
Net currency position		(83.658)	(331.309)	(121.730)	(360.822)	(70.820)	(224.067)	(348.222)	(153.740)

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	Total carrying amount in PLN	EUR		USD		CHF		SEK	
		in currency	in PLN	in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets									
Deposits and investment	25.570	-	-	-	-	-	-	-	-
Bonds, bills and notes receivable acquired	284.941	57.983	238.204	-	-	-	-	-	-
Trade receivables	2.059.119	7.215	29.641	236	673	4	12	-	-
Cash and cash equivalents	7.712.823	89.121	366.125	5	15	20	55	82	33
Originated loans	170.276	-	-	-	-	-	-	381.801	152.720
Other financial receivables	164.783	500	2.054	-	-	-	-	-	-
Shares in entities not quoted on active markets	194.222	-	-	-	-	-	-	-	-
Shares quoted on active markets	1.854	-	-	-	-	-	-	-	-
Other financial assets	8.119	-	-	-	-	-	-	-	-
Lease receivables	942	-	-	-	-	-	-	-	-
Compensations related to LTC	730.629	-	-	-	-	-	-	-	-
Financial liabilities									
Derivatives	(37.701)	-	-	(13.227)	(37.701)	-	-	-	-
Interest bearing loans and credits	(4.911.288)	(148.176)	(608.734)	(123.171)	(351.075)	(88.176)	(243.905)	-	-
Bonds and debt instruments issued	(114.911)	-	-	-	-	-	-	-	-
Trade and other financial liabilities at amortized cost	(1.663.424)	(17.949)	(73.739)	(381)	(1.085)	(6)	(17)	(38.067)	(15.227)
Liabilities from finance lease and lease agreements with option of purchase	(1.670)	-	-	-	-	-	-	-	-
Net currency position		(11.306)	(46.449)	(136.538)	(389.173)	(88.158)	(243.855)	343.816	137.526

43.4. Goods' price risk

Due to their type of business activities, the PGE Group entities are susceptible to change of cash flows and financial results in domestic currency due to price changes of the following risk factors:

- Electric energy;
- Heat energy;
- Coal;
- Gas;
- CO₂ emission rights;
- Energy origin units of ownership of electricity from renewable sources ("green certificates") or from high efficiency cogeneration plants ("red certificates").

Due to the fact that most of the natural resources used by power generation plants and originate from Group-owned mines, the Group's exposure to price fluctuations of these resources is not significant.

The Group's exposure to price risk of merchandise reflects the volume of internal purchase of particular resources presented in the table below:

Type of fuel	Year 2010		Year 2009	
	Tonnage – external purchase (in thousand tons)	Cost of purchase (PLN million)	Tonnage – external purchase (in thousand tons)	Cost of purchase (PLN million)
Coal	6.467	1.661	6.987	1.915
Gas [m3 thousand]	553.478	401	561.601	423
Biomass	490	172	451	140
Fuel oil	48	72	48	58
Total		2.306		2.536

43.5. Credit risk

Significant Group entities that trade electricity in bulk conclude transactions only with companies with a good credit rating or they require collateral from the companies with a lower credit rating. All customers who want to conclude significant transactions and use trade credits are initially verified. Moreover, due to a current monitoring of receivables, the risk of unrecoverable receivables is insignificant.

Credit risk is connected with a potential credit event that can occur, such as insolvency of a customer, partial payment of a receivable, significant delay in receivable payment or other breaches of contract conditions.

The PGE Capital Group entities are exposed to credit risk arising in the following areas:

- Basic activities of entities – the credit risk results from, among others, purchases and sales of electricity and heat energy, purchases and sales of mine fuels, etc.;
- Investment activities of entities – the credit risk results from transactions resulting from investment projects which depend on the financial situation of the Group's suppliers;
- Management of market risk in the Group – the credit risk relates to the possibility of there being a lack of fulfilling of liabilities of the second side of the derivative transaction in relation to the PGE Capital Group entity, if fair value of the derivative transaction is positive from the point of view of the Group. The said source of the credit risk relates mainly to PGE S.A.

- Allocation of free cash of entities – the credit risk results from investing free cash of PGE Group entities in securities bearing credit risk i.e. financial instruments other than those issued by State Treasury.

The classes of financial instruments exposed to credit risk but have different characteristics of credit risk:

- Deposits;
- Bonds, bills, notes receivable acquired;
- Trade receivables;
- Loans granted;
- Other financial receivables;
- Cash and cash equivalents;
- Derivatives;
- Guarantees and sureties granted.

There are significant concentrations of credit risk within the Group related to:

- Trade receivables from key customers, as at 31 December 2010 the three most significant customers accounted for 8% of the trade receivables balance. In addition, receivables from sale of electricity to households account for ca. 23% of the trade receivables balance.
- Compensation to dissolvent of Long-Term Contracts described in note 45 of the foregoing consolidated financial statements.

Maximum credit risk exposure resulting from Company's financial assets is equal to the carrying value of these items. The total maximum credit risk exposure resulting from the Company's assets amounted to PLN 6.255.589 thousand as at 31 December 2010.

43.6 Bonds, bills and notes receivable acquired

As at 31 December 2010, in this position are presented only the bonds issued by Autostrada Wielkopolska S.A.

43.7 Trade receivables

The terms of payments for trade receivables are usually 2-3 weeks, however in 2010 the Group received payments for receivables after 30 days on average. Trade receivables relate mainly to receivables for energy sold and additional services rendered. According to the management, due to current control over trade receivables, there is no additional credit risk that would exceed the level reflected by allowances for receivables.

The Group manages the credit risk of customers mainly by using the following mechanisms and techniques: evaluation of financial standing of the customers and setting up credit limits; requiring certain credit collaterals from customers with lower financial standing; standardization of contents of agreements relating to credit risk and standardization of credit collaterals; system of current monitoring of payments and system of early vindication; systematic measurement of credit risk resulting from trade activity; cooperation with business intelligence agencies and debt collection companies.

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

Geographical region/ country	31 December 2010		31 December 2009	
	Receivables balance	Share %	Receivables balance	Share %
Poland	2.061.962	98,4%	2.011.406	97,7%
United Kingdom	14.329	0,7%	15.559	0,8%
Germany	6.388	0,3%	8.361	0,4%
Czech Republic	2.332	0,1%	6.830	0,3%
Other	9.495	0,5%	16.963	0,8%
Total	2.094.506	100,0%	2.059 119	100,0%

43.8 Deposits, cash and cash equivalents

The Group manages credit risk related to cash by diversification of banks in which surpluses of cash are allocated. All entities, that the Group concludes deposit transactions with, operate in the financial sector. These can only be banks registered in Poland or divisions of foreign banks with high ratings, adequate equity and strong, stable market position in Poland. The most significant cash balances of the Group allocated in three banks accounted for 69% as at 31 December 2010.

43.9 Loans granted, other receivables

Other financial receivables and loans comprise mostly of the receivables from to LTC compensations (for more details please refer to note 45.1 to the foregoing consolidated financial statements) and acquired bonds of Autostrada Wielkopolska S.A. as well as other financial receivables. LTC compensations' receivable constitutes ca. 37% and bonds of Autostrada Wielkopolska S.A. constitute 21% and other receivables constitute ca. 27% of loans and receivables balance as at 31 December 2010 (excluding trade receivables). As at 31 December 2010, other financial receivables increased by 100%. Receivables from grants received by PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Bełchatów and receivables from sale of stocks and shares represent 21% and 15% of other receivables and loans granted, respectively.

43.10 Derivatives

All entities the Group concludes derivative transactions with operate in the financial sector. These are Polish banks with high ratings, of adequate equity and strong, stable market position. As at the balance sheet date, the Group presented derivative transactions concluded, described in detail in note 42.4.3 to the foregoing consolidated financial statements.

43.11 Guarantees granted

Guarantees granted by the Group entities are presented in note 38 to the foregoing consolidated financial statements.

43.12 Ageing of receivables and write offs on receivables

As at 31 December 2010, trade receivables, loans granted and shares in entities not quoted on active markets were subject to revaluation write offs. The change in write offs' accounts for these classes of financial instruments are presented in the table below:

	Trade receivables	Loans granted	Shares in entities not quoted on active markets
Year ended 31 December 2010			
Revaluation write offs as at 1 January	(242.336)	(11.788)	(34.388)
Revaluation write offs used	17.382	-	-
Revaluation write offs reversed	93.486	-	2.921
Revaluation write offs created	(94.319)	-	(5.221)
Change of the presentation	(5.843)	11.788	(33.221)
Revaluation write offs as at 31 December	(231.630)	-	(69.919)
Value before the revaluation write off	2.326.136	174.403	279.541
Net value (carrying amount)	2.094.506	174.403	209.622
Year ended 31 December 2009			
Revaluation write offs as at 1 January	(246.423)	(11.897)	(48.680)
Revaluation write offs used	23.853	-	-
Revaluation write offs reversed	65.414	109	17.719
Revaluation write offs created	(85.180)	-	(3.427)
Revaluation write offs as at 31 December	(242.336)	(11.788)	(34.388)
Value before the revaluation write off	2.301.455	182.064	228.610
Net value (carrying amount)	2.059.119	170.276	194.222

The majority of revaluation write offs created by the Group during the reporting period relate to trade receivables of energy companies from retail customers. Revaluation write offs in companies of retail sale and distribution segment as at 31 December 2010 amounted to PLN 197.671 thousand (PLN 209.705 thousand in 2009). Factors that were taken into consideration by the Company in the calculation of the impairment of the above positions are described in note 13 to the foregoing consolidated financial statements.

As described in note 25 to the foregoing financial statements i periods before the balance sheet date, the parent company made prepayments for transmission services to Vattenfall Aktiebolag („VAB”). As at 31 December 2010, the value of prepayments presented as a loan amounted to PLN 169 million. During the reporting period, the Company was working on the settlement of the status of the remaining prepayments after the expiry of the contract with the VAB. As at the day of preparation of the foregoing consolidated financial statements, there is an uncertainty whether the Company's efforts to extend the cooperation will be successful. As a result, it is uncertain that the amounts engaged will be retrieved. The Company, however, assesses that the cooperation will continue and that the prepayments will be settled, and as a consequence there are no sufficient premises to create a revaluation write off on prepayment presented as a loan as at the balance sheet date.

There are no other significant receivables positions within the Group, except from trade receivables, that would be past due but not covered by a revaluation write off. The ageing structure of trade receivables and other loans and receivables taking into account revaluation write offs, are presented below:

Trade receivables and other loans and receivables	Before due date	< 30 days	30 – 90 days	Past due 90 – 180 days	180 – 360 days	>360 days
31 December 2010						
Before the revaluation write off	2.870.953	264.074	117.807	30.519	35.412	404.128
Revaluation write off	(11.249)	(6.487)	(4.227)	(4.936)	(23.239)	(375.375)
After revaluation write off	2.859.704	257.587	113.580	25.583	12.173	28.753

Trade receivables and other loans and receivables	Before due date	< 30 days	30 – 90 days	Past due 90 – 180 days	180 – 360 days	>360 days
31 December 2009						
Before the revaluation write off	3.048.949	216.215	83.222	102.655	35.168	344.880
Revaluation write off	(37.284)	(7.042)	(4.883)	(17.468)	(25.379)	(329.285)
After revaluation write off	3.011.665	209.173	78.339	85.187	9.789	15.595

43.13 Liquidity risk

The Group is monitoring the risk of lack of funds with the use of a periodical liquidity planning tool. This tool takes into account the maturity of both investments and financial assets (i.e. receivables' and other financial assets' accounts) and estimated future cash flows from operating activities.

PGE Capital Group entities are exposed to liquidity risk in the following areas:

- Core operations of entities – liquidity risks results from maladjustment of structure of dates of operating activities cash flows and execution of assets and liabilities
- Market risk management within the Group – liquidity risk results from possible necessity of settlement of collateral derivative transactions, the value of which is negative from the point of view of the Group or the necessity of granting a guarantee to the second party of the collateral deposit transaction (cash collateral) in the case of negative valuation of derivatives over the duration of a collateral transaction
- Allocation of free cash of entities – the liquidity results from necessity of liquidation of financial assets owned, the market of which is characterized by low volume of turnover and/or relatively high discrepancy between purchase price and sale price.

The table below presents the maturity of the Group's financial liabilities as at the balance sheet dates on the basis of the maturity date based on contractual non-discounted payments.

31 December 2010	Less than 3 months	Between 3 and 12 months	Between 1 and 5 years	More than 5 years	Total
Bonds issued	-	-	-	-	-
Interest bearing loans and credits	402.924	582.322	1.171.759	786.991	2.943.996
Trade and other financial liabilities at amortized cost	2.236.055	5.854	6.520	1.388	2.249.817
Liabilities from finance lease and lease agreements with an option of purchase	968	2.902	6.495	-	10.365
Derivatives	1.295	14.431	40.567	11.166	67.459
Total	2.641.242	605.509	1.225.341	799.545	5.271.637

31 December 2009	Less than 3 months	Between 3 and 12 months	Between 1 and 5 years	More than 5 years	Total
Bonds issued	114.951	-	-	-	114.951
Interest bearing loans and credits	210.787	762.541	2.815.519	1.900.076	5.688.923
Trade and other financial liabilities at amortized cost	1.614.636	33.503	15.277	8	1.663.424
Liabilities from finance lease and lease agreements with an option of purchase	253	761	656	-	1.670
Derivatives	1.461	15.904	47.864	17.341	82.570
Total	1.942.088	812.709	2.879.316	1.917.425	7.551.538

43.14 Market risk – analysis of sensitivity

The Company identifies the following types of market risk as the most significant:

- interest rate risk,
- currency risk.

The PGE Capital Group is exposed mainly to currency risk related to foreign exchange rates between EUR/PLN, USD/PLN, CHF/PLN and SEK/PLN. Furthermore, the Group is exposed to interest rate risk related to referential interest rates of PLN, EUR, USD and CHF. The Group uses a script analysis method for the purpose of analyzing sensitivity to changes of market risk factors. The Group uses experts' scripts reflecting the subjective opinion on the Group in relation to future fluctuations of individual market risk factors.

The scenario analysis presented in this point is intended to analyze the influence of changes in market risk factors on the financial results of the Group. Only positions that can be defined as financial instruments are subject to the analysis.

Potential foreign exchange rates' changes were calculated on $\pm 12,30\%$ for EUR/PLN, $\pm 20,30\%$ for USD/PLN, $\pm 19,21\%$ for CHF/PLN i $\pm 11,37\%$ for SEK/PLN.

In sensitivity analysis related to interest rate risk, the Group applies parallel shift of interest rate curve related to a potential possible change of referential interest rates during the following year. For the purpose of sensitivity analysis on the interest rate risk for currencies, for which the Group is exposed to as at the balance sheet date, potential interest rates' changes was estimated on ± 94 pb for WIBOR, ± 50 pb for EURIBOR, ± 48 pb for LIBOR USD i ± 49 pb for LIBOR CHF.

In case of sensitivity analysis of interest rates' fluctuations, the effect of risk factors' changes were recognized in the value of interest income or expenses related to financial instruments at amortized cost and as the fair value as at the balance sheet date of financial instruments at fair value.

Presented below is the sensitivity analysis related to all types of market risks the Group is exposed to as at the balance sheet date, indicating the potential influence of changes of individual risk factors by class of assets and liabilities on the gross financial result.

43.15 Sensitivity analysis for currency risk

The Group identifies an exposure to fluctuations of foreign exchange rates of the following pairs of currencies: EUR/PLN, USD/PLN, CHF/PLN and SEK/PLN.

The below table presents the sensitivity of a gross financial result to reasonably possible changes to foreign currencies exchange rates, under the assumption of stability of other risk factors for these classes of financial instruments exposed to currency risk.

Financial instruments by class	31 December 2010		Sensitivity analysis for currency risk as at 31 December 2009							
	Carrying amount	Amount exposed to risk	EUR/PLN		USD/PLN		CHF/PLN		SEK/PLN	
	PLN thousand	PLN thousand	gross financial result		gross financial result		gross financial result		gross financial result	
			Exchange rate EUR/PLN + 12,30%	Exchange rate EUR/PLN - 12,30%	Exchange rate USD/PLN + 20,30%	Exchange rate USD/PLN - 20,30%	Exchange rate CHF/PLN + 19,21%	Exchange rate CHF/PLN - 19,21%	Exchange rate SEK/PLN + 11,37%	Exchange rate SEK/PLN - 11,37%
Trade receivables	2.094.506	19.720	2.209	(2.209)	334	(334)	17	(17)	4	(4)
Loans granted	-	-	-	-	-	-	-	-	19.169	(19.169)
Bonds, bills, notes receivable acquired	253.538	253.538	31.185	(31.185)	-	-	-	-	-	-
Cash and cash equivalents	2.730.423	86.606	10.641	(10.641)	20	(20)	-	-	-	-
Derivatives	(41.165)	(41.165)	-	-	(8.357)	8.357	-	-	-	-
Interest bearing loans and credits	(2.719.385)	(1.131.145)	(72.148)	72.148	(65.077)	65.077	(43.031)	43.031	-	-
Trade liabilities and other financial liabilities at amortized cost	(2.249.817)	(118.577)	(12.638)	12.638	(166)	166	(29)	29	(1.690)	1.690
Gross profit change			(40.751)	40.751	(73.246)	73.246	(43.043)	43.043	17.483	(17.483)

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Financial instruments by class	31 December 2009		Sensitivity analysis for currency risk as at 31 December 2009							
	Carrying amount	Amount exposed to risk	EUR/PLN		USD/PLN		CHF/PLN		SEK/PLN	
	PLN thousand	PLN thousand	gross financial result		gross financial result		gross financial result		gross financial result	
			Exchange rate	Exchange rate	Exchange rate	Exchange rate	Exchange rate	Exchange rate	Exchange rates	Exchange rate
			EUR/PLN + 13,25%	EUR/PLN -13,25%	USD/PLN + 19,69%	USD/PLN -19,69%	CHF/PLN + 16,16%	CHF/PLN -16,16%	SEK/PLN + 12,46%	SEK/PLN -12,46%
Trade receivables	2.059.119	30.326	3.927	(3.927)	132	(132)	2	(2)	-	-
Loans granted	170.276	152.720	-	-	-	-	-	-	19.021	(19.021)
Bonds, bills, notes receivables acquired	284.941	238.204	31.562	(31.562)	-	-	-	-	-	-
Cash and Cash equivalent	7.712.823	366.228	48.512	(48.512)	3	(3)	9	(9)	4	(4)
Derivatives	(37.701)	(37.701)	-	-	(7.423)	7.423	-	-	-	-
Interest bearing loans and credit	(4.911.288)	(1.203.714)	(80.657)	80.657	(69.126)	69.126	(39.413)	39.413	-	-
Trade liabilities and other financial liabilities at amortized cost	(1.663.424)	(90.068)	(9.770)	9.770	(214)	214	(3)	3	(1.897)	1.897
Gross profit change			(6.426)	6.426	(76.628)	76.628	(39.405)	39.405	17.128	(17.128)

43.16 Sensitivity analysis for interest rate risk

The Group identifies exposure to interest rate risk related to WIBOR, EURIBOR and LIBOR rates. The table below presents the sensitivity of the gross financial result based on reasonable, possible future fluctuations of interest rates, under assumption of stability of other risk factors for these classes of financial instruments that are exposed to interest rate risk:

Financial assets and liabilities	31 December 2010		Sensitivity analysis for interest rate risk as at 31 December 2010							
	Carrying amount	Amount exposed to risk	WIBOR		EURIBOR		LIBOR USD		LIBOR CHF	
			gross financial result		gross financial result		gross financial result		gross financial result	
	PLN thousand	PLN thousand	WIBOR + 94 pb	WIBOR – 94 pb	EURIBOR+ 50pb	EURIBOR - 50 pb	LIBOR USD + 48pb	LIBOR USD – 48pb	LIBOR CHF + 49pb	LIBOR CHF – 49 pb
Cash and cash equivalents	2.730.423	2.730.423	46.755	(46.755)	1.123	(1.123)	-	-	-	-
Derivatives	(41.165)	(41.165)	-	-	-	-	(5.675)	5.675	-	-
Interest bearing loans and credits	(2.719.385)	(1.886.564)	(20.887)	20.887	(2.965)	2.965	(1.608)	1.608	(1.146)	1.146
Bonds issued	-	-	-	-	-	-	-	-	-	-
Gross profit change o			25.868	(25.868)	(1.842)	1.842	(7.283)	7.283	(1.146)	1.146

Financial assets and liabilities	31 December 2009		Sensitivity analysis for interest rate risk as at 31 December 2009							
	Carrying amount	Amount exposed to risk	WIBOR		EURIBOR		LIBOR USD		LIBOR CHF	
			gross financial result		gross financial result		gross financial result		gross financial result	
			WIBOR + 105bp	WIBOR - 105bp	EURIBOR+ 51bp	EURIBOR - 51bp	LIBOR USD +41bp	LIBOR USD -41bp	LIBOR CHF +16bp	LIBOR CHF -16bp
	PLN thousand	PLN thousand								
Cash and cash equivalents	7.712.823	7.712.823	49.587	(49.587)	1.129	(1.129)	3	(3)	-	-
Derivatives	(37.701)	(37.701)	-	-	-	-	(5.718)	5.718	-	-
Interest bearing loans and credits	(4.911.288)	(3.641.000)	(38.171)	38.171	(2.580)	2.580	(1.525)	1.525	(424)	424
Bonds issued	(114.911)	(114.911)	(9.205)	9.205	-	-	-	-	-	-
Gross profit change			2.211	(2.211)	(1.451)	1.451	(7.240)	7.240	(424)	424

The change of the interest rates will have a direct influence on the valuation of derivatives referring to the conversion of floating interest rate into the fixed rate. For the other financial assets and liabilities disclosed in the above tables, changes in rates would effect on the future value of these instruments.

Above changes of rates are recognized in the consolidated statement of comprehensive income and as a consequence in the equity as retained earnings of the Capital Group. The changes of interest rates do not effect on the value of other equity positions disclosed in the consolidated statement of financial position.

44 Employment structure

Employment in the Group (in posts) as at 31 December 2010 and 31 December 2009 was as follows:

	As at 31 December 2010	As at 31 December 2009
Total employees, including:	45.715	46.357
Mining and Production	22.496	22.774
Renewable Energetics	531	483
Wholesale turnover	376	454
Distribution	12.590	12.687
Retail sale	1.799	1.778
Other consolidated entities	7.923	8.181

45 Significant events during the reporting period and subsequent events

45.1 Compensation for long term contacts

Pursuant to the Act of June 29, 2007 on the Rules of Coverage of Costs Occurring at Production Plants as a Consequence of Early Termination of Long-Term Power and Electricity Sales Contracts (Journal of Laws No. 130, item 905, of 2007) (the "Long-Term Contracts Act"), some PGE Group companies became entitled to receive funds to cover stranded costs (so-called "compensation").

The maximum value of stranded costs including stranded costs relating to 2007 and additional costs (according to 44 article of the LTC Act), according to an appendix 2 amounted to:

- PGE Elektrownia Opole S.A. – PLN 1.965.700 thousand;
- PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrownia Turów – PLN 2.571.151 thousand;
- PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Zespół Elektrowni Dolna Odra – PLN 633.496 thousand;
- PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrociepłownia Rzeszów – PLN 421.810 thousand;
- PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrociepłownia Lublin Wrotków – PLN 616.743 thousand;
- PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrociepłownia Gorzów – PLN 108.028 thousand.

Under the Long-Term Contracts Act, PGE Group companies will receive compensation to cover stranded cost in the form of quarterly advances. Yearly adjustments are made after the end of each year, followed by a final adjustment upon the lapse of the entire term of Long-Term Contract.

The revenue for the period comprises cash received in the form of advances, adjusted by an annual adjustment and an appropriate portion of the final adjustment planned. Allocation of the final adjustment to the given reporting period is made with the use of fixed prices, based on planned revenues from the sale of electric energy and system services in the adjustment period with final adjustment taken into account. The discount rate is based on a risk-free weighed average term rate.

The LTC Act is ambiguous in many points and raise important questions of interpretation. The calculation of the estimated results of each company and resulting compensations, annual adjustments of stranded costs and final adjustments was performed by the Group with the best of its knowledge in this area and with support of external experts.

Proceedings related to annual adjustment of stranded costs for the year 2008

On 31 July 2009, the President of ERO issued against the PGE Group production entities, entitled to receive means to cover stranded costs on the basis of LTC Act, decisions on annual adjustment of stranded costs for the year 2008 and annual adjustments of costs related to natural gas-fired entities for the year 2008 (the first, but incomplete year of this Act being effective). These decisions were unfavorable for particular PGE Group entities and according to the Group these have been issued with a breach of the LTC Act. In accordance with the decisions, producers from PGE Capital Group have been obliged to return to the Zarządca Rozliczeń S.A. the total amount of ca. PLN 140.8 million.

On 19 and 20 August 2009, the interested PGE Capital Group entities filed an appeal against the above mentioned decisions of the President of ERO to the District Court in Warsaw, to the Competition and Consumer Protection Court, raising among others that:

- the calculation of the annual adjustment for particular entities was at variance with mathematical formulas included in the LTC Act,
- the costs of CO₂ emission rights incurred by particular entities were not included in the annual adjustment of the stranded costs,
- the correction of annual adjustment of stranded costs of particular entities was at variance with regulations included in art. 32 of the LTC Act which related to capital group production entities,
- incorrect assumption (which was a basis for the ERO decisions under appeal proceedings) that particular entities do not operate on the competitive electric energy market, which is contrary to the previous statement of the President of ERO that PGE Group entities operate on the competitive market and therefore, in particular, are not obliged to submit the used tariffs for approval of the President of ERO.

On 17 May 2010, at the District Court in the Competition and Consumer Protection Court, XVII Commercial Department a trial took place of PGE Capital Group companies appealing against the decisions of the President of ERO on annual adjustment of stranded costs for the 2008. On 26 May 2010, the court announced a sentence taking into account companies' appeals i.e. changing the appealed decisions of ERO as a whole by setting for each producer the amount of the annual adjustments for 2008 up to the requested amounts. The amounts should be paid to plaintiffs by Zarządca Rozliczeń S.A. The above sentences are not legally valid and the President of ERO has filed an appeal against them. In September, October and November 2010 entitled producers of the PGE Group addressed a response of appeal to the President of ERO.

Proceedings related to annual adjustment of stranded costs and gas costs for the year 2009

Between 3 and 9 August 2010, the entitled producers from PGE Group received decisions of the President of ERO related to setting the annual adjustment of stranded costs and the final adjustment of costs in gas-heated entities in 2009. According to the decisions, the producers from PGE Group are obliged to refund to Zarządca Rozliczeń S.A. the total amount of ca. PLN 566 million.

The Board of Directors of PGE as well as the Management Boards of PGE Capital Group producers under the compensation system do not agree with the decisions of the President of ERO.

Between 16 and 23 August 2010, the entities filed appeals to the District Court in Warsaw, Competition and Consumer Protection Court. The entities raise mostly:

- correct of annual adjustment of stranded costs of particular entities against the rules related to producers of capital group enclosed in the Art. 32 of the LTC Act;
- calculation of revenues from sales of energy on the basis of hypothetical price, disregarding revenues from production capacity;
- issues of interest charged by the President of the Energy Regulatory Authority;
- as regards the gas-related adjustment of Elektrociepłownia Lublin Wrotków and Elektrociepłownia Rzeszów - calculation of annual adjustment on the basis of the quantity of electricity produced

from gas fuel acquired in course of exercising the "take or pay" obligation instead of the quantity of electricity produced from gas fuel acquired in aggregate during the given year; and calculation of the President of the Energy Regulatory Authority related to production cost of 1 MWh of electricity, disregarding overheads related to electricity production.

Agreement with Zarządca Rozliczeń S.A. concerning deferred payment of amounts arising from the decision by the President of the Energy Regulatory Authority to determine adjustment of stranded costs for 2009 for Elektrownia Opole, Elektrownia Turów, Elektrociepłownia Rzeszów and Elektrociepłownia Lublin Wrotków

In August 2010, PGE Elektrownia Opole S.A., Elektrownia Turów, Elektrociepłownia Rzeszów and Elektrociepłownia Lublin-Wrotków entered into agreements with Zarządca Rozliczeń to defer repayment of the entire amount of stranded costs. Under the agreement, repayment of adjustment values was postponed for two months. In addition, the agreement obliged the companies to pay interest to Zarządca Rozliczeń S.A. on the deferred adjustments, where Zarządca Rozliczeń S.A. is entitled to charge interest for any delay by either company in repayment of the adjustment amounts at the statutory rate of penalty interest. The companies authorized Zarządca Rozliczeń S.A. to offset the entire amount outstanding as at the due date stipulated in the agreements, including any interest charged according to the agreements, with any amounts receivable by these companies as advances for covering stranded costs falling due at the earliest date. The agreement foresees an option of entering into separate annexes. Until the date of these financial statements, the companies exercised this option twice. PGE Elektrownia Opole S.A. had its payments postponed until 16 December 2011 (amounting to PLN 241.7 million), and the following production plants: Elektrownia Turów, Elektrociepłownia Rzeszów, and Elektrociepłownia Lublin-Wrotków had their payments postponed until 17 February 2011 (in an aggregate amount of PLN 323.0 million).

Adjustment of stranded costs concerning Elektrociepłownia Gorzów

On 17 September 2010 PGE Górnictwo i Energetyka Konwencjonalna S.A. Oddział Elektrociepłownia Gorzów filed a notice to the President of the Energy Regulatory Authority concerning inactivity in respect of initiating a procedure to determine final adjustment amount. President of the Energy Regulatory Authority responded to the above notice on 12 October 2010, stating that issuance of a final adjustment decision was unfeasible. On 19 November 2010 Elektrociepłownia Gorzów lodged a complaint with the Provincial Administrative Court concerning inactivity of the President of the Energy Regulatory Authority, whereto the President of the Energy Regulatory Authority responded in its notice of 20 December 2010. On 24 January 2011 Gorzów Heat & Power Generating Plant Branch filed a reply to the Energy Regulatory Authority President's response to the complaint with the Provincial Administrative Court.

Suspended proceedings

In March 2011, PGE Capital Group got known that in February 2011, the Court for Competition and Consumer Protection suspended proceedings related to annual adjustment of Elektrownia Turów for year 2008 and 2009, Elektrownia Opole for 2008 and annual adjustment of Zespół Elektrowni Dolna Odra for 2009. The reason for suspending these proceedings was the vacancy in the position of President of the Energy Regulatory Authority.

Summary

The Management Board of the Group is convinced that the appeal shall be settled in favor of the particular entities subject to compensations, therefore the PGE Group recognizes the revenues from LTC compensations in accordance with the LTC Act interpretation adopted by the Group. Due to the above, the present consolidated financial statements do not comprise the adjustments resulting from unfavorable interpretations included in the ERO decisions both in relation to revenues for the year 2008, revenues for the year 2009 as well as to assess revenues for the period ended 31 December 2010. However, we draw attention to the uncertainty of final interpretation of the President of ERO in this scope.

45.2 PGE Capital Group Consolidation

The consolidation process of PGE Capital Group, realized under the Consolidation Programme of PGE Capital Group, commenced in 2009. The purpose of the Programme is a legal and organizational merger of the entities in the following business areas:

- retail sale of electric energy;
- distribution of electric energy
- mining and conventional energy (mining and generation);
- energy from renewable sources;

and also a merger of PGE Górnictwo i Energetyka S.A. and PGE Energia S.A. with PGE Polska Grupa Energetyczna S.A., as well as carrying out legal and organizational changes in the field of wholesale energy trade. The merger in each business line will take place in compliance with art. 492 par. 1 p. 1 of the Commercial Code i.e. by takeover.

Before 31 August 2010, the PGE Capital Group comprised of 42 entities covered by the consolidation programme. Thanks to the consolidation programme of PGE Capital Group in each line of business operates a company that brings together all the assets and operations of each business of PGE Capital Group.

Consolidation Programme includes also the creation of the organizational structure and identification of improving efficiency and competitiveness programs. Efforts related to the project will be continued.

45.2.1 Consolidation of PGE Capital Group

Conventional Energy

The company bringing together all of the extracting and generating assets within mining and conventional energy area is PGE Górnictwo i Energetyka Konwencjonalna S.A. The merger in this area was registered on 1 September 2010. In the area of Conventional Energy (mining and generation) the following companies has merged:

- PGE Elektrownia Bełchatów S.A. – taking over company
- PGE Kopalnia Węgla Brunatnego Bełchatów S.A.
- PGE Kopalnia Węgla Brunatnego Turów S.A.
- PGE Elektrownia Turów S.A.
- PGE Zespół Elektrowni Dolna Odra S.A.
- PGE Zespół Elektrociepłowni Bydgoszcz S.A.
- PGE Elektrociepłownia Lublin-Wrotków Sp. z o.o.
- PGE Elektrociepłownia Gorzów S.A.
- PGE Elektrociepłownia Rzeszów S.A.
- PGE Elektrociepłownia Kielce S.A.
- Energetyka Boruta Sp. z o.o.
- Przedsiębiorstwo Energetyki Ciepłej Sp. z o.o. in Gryfino
- PEC Gorzów Sp. z o.o.

Moreover the merger with PGE Elektrownia Opole S.A. is currently in progress.

Renewable energy

The company bringing together all of the production assets in the area of renewable energy (excluding plants co-incinerating biomass) is PGE Energetyka Odnawialna S.A. The merger in this area was registered on 31 August 2010.

In the area of renewable energy the following companies have merged:

- PGE Energia Odnawialna S.A. – taking over company
- Elektrownia Wodna Żarnowiec S.A.
- PGE Zespół Elektrowni Wodnych Dychów S.A.
- Zespół Elektrowni Wodnych Porąbka-Żar S.A.
- EGO-Odra S.A.
- Zespół Elektrowni Wodnych Solina-Myczkowce S.A.

Moreover the merger with Elektrownia Wiatrowa Kamieńsk Sp. z o.o. is currently in progress.

Distribution of electricity

The company bringing together all the activities in the area of distribution of electricity is PGE Dystrybucja S.A. The merger in this area was registered on 31 August 2010.

In the area of distribution of electricity the following companies have merged:

- PGE Dystrybucja S.A. – taking over company
- PGE Dystrybucja LUBZEL Sp. z o.o.
- PGE Dystrybucja Łódź Sp. z o.o.
- PGE Dystrybucja Rzeszów Sp. z o.o.
- PGE Dystrybucja Białystok Sp. z o.o.
- PGE Dystrybucja Łódź-Teren S.A.
- PGE Zakłady Energetyczne Okręgu Radomsko-Kieleckiego Dystrybucja Sp. z o.o.
- PGE Dystrybucja Warszawa-Teren Sp. z o.o.
- PGE Dystrybucja Zamość Sp. z o.o.

The sales of electricity to the final customers

The company bringing together all the activities in the area of the sales of electricity to the final customers is PGE Obrót S.A. The merger in this area was registered on 31 August 2010.

In the area of retail sales of electricity the following companies have merged:

- PGE Obrót S.A. (previously under business name PGE Rzeszowski Zakład Energetyczny S.A.) – taking over company
- PGE Lubelskie Zakłady Energetyczne S.A.
- PGE Łódzki Zakład Energetyczny S.A.
- PGE Zakład Energetyczny Białystok S.A.
- PGE ZEŁT Obrót Sp. z o.o.
- PGE Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.
- PGE Zakład Energetyczny Warszawa-Teren S.A.
- PGE Zamojska Korporacja Energetyczna S.A.

Financial implications and the impact of changes mentioned above on the consolidated financial statements of PGE Capital Group were described in note 9 and 31.1 to the foregoing consolidated financial statements.

The merger of PGE Polska Grupa Energetyczna S.A. and subsidiaries

Moreover, as a result of realization of the Consolidation Programme PGE S.A. has been merged with PGE Górnictwo i Energetyka S.A., PGE Energia S.A. and PGE Electra S.A. The description of the merger, financial implications and recognition in the financial statements of PGE Capital Group were presented in note 9 and 31.1 to the foregoing consolidated financial statements.

45.2.2 Legal issues related to the Consolidation Programme

Within the Consolidation Programme, on August 3 and August 16, 2010 extraordinary general meetings of PGE Group entities passed resolutions to consolidate. Few shareholders of these companies lodged appeals against the above mentioned resolutions for determining their invalidity and possibly demanding that the resolutions be repealed. Furthermore, these claimants would demand safeguarding of their claims through withholding enforcement of consolidation resolutions and suspension of registration proceedings.

The above claims were made with reference to the consolidation resolution adopted by PGE Elektrownia Opole S.A. and consolidation resolutions adopted by some companies merged within the Mining and Conventional Energy business line (PGE Górnictwo i Energetyka Konwencjonalna S.A. conducts these cases), as well as a consolidation resolution adopted by shareholders of PGE Górnictwo i Energetyka S.A. (PGE S.A. conduct this case).

In the cases under consideration, PGE S.A. and other defendants prepared relevant statements of defense and they are taking active part in the proceedings, where they question all claims raised by the shareholders. PGE S.A. and the remaining defendant companies believe that the shareholders' claims are unfounded and the actual aim of these shareholders is to question the parity of shares, which is unacceptable on the basis of procedure of appeals against resolutions.

On January 2011 the Regional Court in Łódź, 10th Commercial Department, ruled to repeal the plaintiff's claims. The claim was lodged by one of the shareholder of Secus Investment Sp. z o.o. fund.

Furthermore, there are some proceedings pending resulting from challenging the decision concerning registration of merger within the conventional energy business line.

On 11 February 2011 the Regional Court in Łódź, pursuant to an appeal against the decision of District Court for Łódź-Śródmieście in Łódź, 20th Commercial Department of the National Court Register ("District Court") to register consolidation of 12 merged companies with PGE Elektrownia Bełchatów S.A. (with omission of PGE Elektrownia Opole S.A. - with respect to which registration proceedings were suspended) ruled to repeal the disputed decision and to forward the matter for reconsideration to the District Court. The judgment was passed pursuant to consideration of appeals lodged by three non-controlling shareholders.

After reconsideration the District Court may decide about the registration of the merger, reject the registration and delete existing entry in the registry. As at the date of preparation of the foregoing financial statements, it is difficult to assess the risk of actual occurrence of the particular scenarios, or the potential time of such occurrence. The Company believes that deletion of existing entry from the registry, if required, will be inconsistent with mandatory rules of the law.

However, if such entry is still deleted, legal personalities of the merged companies will be restored. It would cause taking steps to prepare reactivated companies to independent operational activities including appointment of companies' bodies, division of assets PGE Górnictwo i Energetyka Konwencjonalna S.A. to each acquired company, transfer of employees in accordance with the law regulations governing change of employer as well as re-obtaining the legally required licenses, permissions, authorizations and other administrative decisions.

The process of reversing the consequences of consolidation, which is not sufficiently regulated by the existing legislative system, may generate multiple additional risks and costs. These risks and costs, considering, in particular, possible different interpretations of laws and regulations by public administration authorities, cannot be fully identified or measured at the present stage.

PGE Górnictwo i Energetyka Konwencjonalna S.A. took appropriate proceedings to dismiss the objections of non-controlling shareholders. The legal experts possessed by PGE Górnictwo i Energetyka Konwencjonalna S.A. clearly indicate that the process of consolidation is not actually threatened by the proceeding initiated by the non-controlling shareholders.

At the present stage of arbitration proceedings, it is not possible to foresee the courts' decisions.

45.3 Guarantee agreements for employees of PGE Group

With regard to the aforementioned consolidation process, three guarantee agreements were executed at PGE Górnictwo i Energetyka Konwencjonalna S.A. for the brown coal sector, for the heat & power generating plants sector, and for heat power sector separately. In addition, guarantee agreements were signed at PGE Obrót S.A. and PGE Dystrybucja S.A. According to the assumptions of the Consolidation Programme, the above mentioned agreements guarantee maintaining employee and trade union rights at the current level defined in cross-company collective bargaining agreements, company collective bargaining agreements, welfare agreements and other agreements existing in the companies, without extending the scope of rights or benefits currently available to employees. The guarantee agreements were signed by the acquiring companies, the acquired companies, and representatives of trade union organizations. PGE Polska Grupa Energetyczna S.A. is the guarantor responsible for proper execution of the agreements.

45.4 „Non-core” Programme

In 2009, the “Conception of non-energy related assets management in PGE Capital Group” was adopted. The purpose of this conception is to transparently separate core business activities from other activities and disposal and reorganization of mentioned assets.

It has been assumed, that the simplification of capital relations and organizational structures of PGE Group, as well as the unification of management standards will allow achieve the following effects:

- transparency of the business model of PGE Capital Group (focus on core business activities);
- transparency of management of assets and expenses of energy entities;
- resources of energy entities will be discharged from engagement in non-energy related assets;
- reduction of services expenses not related to core business.

Within the realized Conception, there were non-energy related assets identified acting in the form of entities and areas not separated from the structures of core business entities and the process of disposal and reorganization of these assets was commenced within the PGE Group. Information about changes in the composition of consolidated subsidiaries that were sold or meet the criteria of IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* was presented in note 2 and 19 to the foregoing consolidated financial statements.

45.5 Excise tax on electricity in energy production entities

As a result of non-compliance of Polish legal regulations on excise tax on electricity with the European Union law, on 11 February 2009, power plants and heat and power stations of PGE Group filed adjusted excise tax declarations together with motions stating surplus payments of excise tax in the years 2006-2008 and the months January and February 2009. The total value of the surplus declared (without the cost of interest) in the subject motions amounted to ca. PLN 3.4 billion.

On 12 February 2009, the European Union Court of Justice issued a verdict confirming that Poland broke the law by relinquishment of adjusting its system of electricity taxation, before 1 January 2006, to requirements of art. 21 passage 5 of the Council Directive 2003/96/EC of 27 October 2003 on restructuring Community frame regulations related to taxation of power industry products and electricity (changed by the Council Directive 2004/74/EC of 29 April 2004). According to Polish law, the electricity excise tax obligation originates in the moment the electricity is produced, not in the moment it is delivered by the distribution or redistribution entity.

Due to the above, there are significant chances to receive the return of the excise tax paid inconsistently with the Community law. However, the Ministry of Finance claims that such a return might result in an unjust enrichment of the producers, therefore it is groundless. As a result, the process related to return of the excise tax may last until court decisions.

Furthermore, on 15 October 2009, the Supreme Administrative Court addressed the Constitutional Tribunal with a legal inquiry whether the provisions of the Tax Ordinance Act which are basis for the Group production companies to apply for an excise tax excess payment refund are complicate with the Constitution of the Republic of Poland. On November 29, 2010 the Constitutional Tribunal decided to discontinue the proceedings on assessing non-compliance with the Constitution of the legal regulation concerning overpayment. According to the Constitutional Tribunal the Tax Ordinance Act assumes a certain model of proceeding with overpaid tax and reasons substantiating reimbursement of such tax, and the fact of incurring the economic burden of tax is not recognized by the Act as a reason substantiating return of overpaid tax. On the other hand, the Supreme Administrative Court in a decision of February 3, 2011 presented a legal issue for resolving by the entire Economic Chamber of the Supreme Administrative Court on whether an amount of excise tax paid for sale of electricity qualifies as overpaid tax if the payer did not suffer a financial disadvantage for reason of making that payment.

Taking into account a significant incertitude related to final court decision on the above described matter, the Group does not disclose any financial results related to possible return of the excise tax surplus payment in the consolidated financial statements.

Moreover, there is a risk that if the production entities of the PGE Group receive the refund of the excise tax excess payment, civil and legal claims might be filed against these entities by electric energy buyers, which have been actually economically burdened with the excise tax in the past (i.e. based on unjustified enrichment accusation). During the reporting period and after the balance sheet date, the energy buyers started to claim refund payments related to excise tax from the Group entities. The Group anticipates that the number of such claims will increase. Currently, the estimation of the value of possible claims is not possible, however this matter may have a significant and unfavorable impact on the future activities, financial results or financial situation of the Group.

Furthermore, in September 2009 the Company filed a motion related to an excess payment of the excise tax on imports and Intra-Community acquisition of electric energy in the period from January 2006 to February 2009. The Company states that the excess payment results from discrepancies between the Polish and Community law. In May 2010, the Company received a part of decisions refusing to grant a request to determine overpayment, and decisions determining the excise tax obligation for intra-Community purchases of electricity, against which the Company had lodged appeals. In December 2010, the Company received decisions from the Director of Customs Chamber, which fully supported the decisions of the first instance authority concerning excise tax on energy import in 2006. The Company filed complaints against these decisions to the Provincial Administrative Court in Warsaw. The issue has not been finally resolved as at the date of preparation of these financial statements. The total amount of claim is 54 million PLN plus interest charge.

45.6 Agreement to acquire shares of PGE Energa S.A.

On 29 September 2010, the Management Board of PGE Polska Grupa Energetyczna S.A. concluded with the State Treasury, represented by the Minister of the State Treasury, agreement on sales of shares of Energa S.A., seated in Gdańsk ("Agreement"). The subject of the agreement is to acquire 4,183,285,486 shares of the Company, representing 84,19% of its share capital. The purchase price of all shares representing 84,19% of share capital of the Company is PLN 7,529,913 thousand. The buyer declared the guaranteed investment programme to be implemented in the Energa Capital Group within 10 years in amount of PLN 5 billion. Failure to comply will entail the contractual penalties to pay for the Seller. The total liability of the Purchaser could not exceed PLN 1 billion. Moreover, PGE S.A. committed to maintaining control over the Company, to not restrict the core activities of the company and its main subsidiaries covering production, sales and distribution of the electricity and heat as well as to not changing the seat of the company. Moreover, PGE S.A. committed to placing shares to trading on the Warsaw Stock Exchange.

The transaction shall be effective after obtaining by PGE S.A. the consent to a concentration of capital by PGE S.A. from the President of the Office of Competition and Consumer ("the President of the Office") (condition precedent).

On 13 January 2011, the President of the Office for Competition and Consumer Protection issued a Decision preventing PGE S.A. from buying shares of Energa S.A.

Therefore, on 18 January 2011 PGE S.A. entered into an annex to the Agreement of sale of Energa S.A. shares, with the Seller. Under that Annex, the term of Agreement was set as 12 months of the effective date, whereby the State Treasury and PGE S.A. decided to withhold the term of Agreement until a valid and binding closing of court proceedings concerning appeal against the Decision.

On 28 January 2011, the Regional Court in Warsaw, Competition and Consumer Protection Court, received an appeal filed through intermediation of the President of the Office by PGE S.A. against the Decision of the President of the Office for Competition and Consumer Protection, preventing amalgamation of PGE S.A. with Energa S.A. In its appeal, the Company requests that the said decision be replaced in its entirety by another Decision to the effect of permitting amalgamation of PGE S.A. with Energa S.A., or that the former decision be revoked.

According to the information held by PGE S.A., in mid-February 2011, the President of the Office forwarded the Company's appeal to the Competition and Consumer Protection Court in Warsaw, thus waiving its right to self-assess the decision.

Until the preparation date of the foregoing financial statements, the Competition and Consumer Protection Court has not yet issued a decision regarding appeal by PGE S.A. against the Decision of the President of the Office, preventing amalgamation of PGE S.A. with Energa S.A.

45.7 Sales of shares of Polkomtel S.A. and Exatel S.A.

The process of selling the shares of Polkomtel S.A. began in January 2011, after intensive preparations that were taking place in 2010. All the Polish shareholders of the company participate in the process, namely: PGE S.A., KGHM Polska Miedź S.A., PKN Orlen S.A. and Węglukoks S.A., along with foreign shareholders: Vodafone Americas Inc and Vodafone International Holdings B.V. The largest telecommunication groups and most significant global financial investors participate in the transaction on the investor side, resulting that the transaction is executed in the conditions of strong international competition. As at the date of preparation of the foregoing financial statements, another phase of transaction following selection of the most advantageous preliminary quotations is in progress. The Company expects that the contract of sales of Polkomtel S.A. shares will be executed before the end of June 2011.

The process of selling the assets of Exatel S.A. commenced in September 2010. After verification of preliminary quotations by the Project Team appointed by the Management Board of the Company, two potential investors were selected. One of the investors ultimately withdrew from participation during the process. Finally, because no binding tenders were received as at 13 January 2011, the Management Board of the Company decided to cancel the tender procedure. However, PGE S.A. is still planning to sell Exatel S.A. shares until the end of 2011. Next steps in the process are scheduled for the second quarter of 2011.

As at 31 December 2010, investments mentioned above did not fulfill the definition of assets classified as held for sale nor discontinued operations in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, they were presented in the foregoing consolidated financial statement in according with IAS 28 *Investments in Associates* and IAS 27 *Consolidated and Separate Financial Statements*.

45.8 Damages in properties of PGE Elektrownia Turów S.A. and PGE Kopalnia Węgla Brunatnego Turów S.A.

At the beginning of August 2010 heavy rainfalls caused damages in properties of PGE Elektrownia Turów S.A. and PGE Kopalnia Węgla Brunatnego Turów S.A. (currently operating as branches of PGE Górnictwo i Energetyka Kopenwencyonalna S.A.) As a result of the damages, the lignite's mining and electricity production in these plants were temporarily reduced. The reduction of production in PGE Elektrownia Turów S.A. was compensated by the increase of production in other plants of the Capital Group. Until 31 December 2010, plants affected by flooding recognized costs related to repairing damages and infrastructure as well as power generating asset impairment in the profit and loss account in amount of PLN 41.238 thousand. Furthermore, some work associated with reconstruction after flooding has been recognized as an increase of non-current assets in total amount of PLN 23.411 thousand.

Assets affected by flooding were insured and the winding-up proceedings are bringing against insurers in the affected companies.

45.9 Establishment of the underwritten Bond Issue Programme of PLN 10 billion

The description of the Bond Issue Programme of PLN 10 billion was presented in note 42.4.4.2. of explanatory notes to the foregoing consolidated financial statements.

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

Signed on the Polish original

*Tomasz Zadroga
President of the
Management Board*

Signed on the Polish original

*Marek Szostek
Vice-President of the
Management Board*

Signed on the Polish original

*Piotr Szymanek
Vice-President of the
Management Board*

Signed on the Polish original

*Marek Trawiński
Vice-President of the
Management Board*