



PGE Polska Grupa Energetyczna S.A. Capital Group

Consolidated financial statements prepared in accordance with International Financial Reporting Standards for the years ended 31 December 2006 and 31 December 2007 together with independent auditor's opinion.

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CONSOLIDATED INCOME STATEMENT

for the years ended 31 December 2006 and 31 December 2007

	Note	Year ended 31 December 2007	Year ended 31 December 2006
<i>Continuing operations</i>			
Operating activities			
Sales of finished goods and merchandise with excise tax		23 651 845	24 849 243
Excise tax		(1 056 550)	(1 098 200)
<i>Net revenues from sale of finished goods and merchandise</i>		22 595 295	23 751 043
Revenues from sale of services		543 081	566 565
Revenues from lease		27 813	26 405
Total sales revenues		23 166 189	24 344 013
Cost of goods sold	14.5	(19 722 036)	(20 838 374)
Gross profit on sales		3 444 153	3 505 639
Other operating revenues	14.1	572 441	476 916
Selling expenses	14.5	(452 732)	(524 379)
General and administrative expenses	14.5	(948 512)	(825 469)
Other operating expenses	14.2	(481 036)	(310 005)
Financial income	14.3	630 898	492 012
Financial expenses	14.4	(1 026 851)	(815 492)
Share of profit of associate	27	239 156	197 957
Profit before tax		1 977 517	2 197 179
Corporate income tax expense	17	948 111	(395 163)
Net profit from continuing operations		2 925 628	1 802 016
<i>Discontinued operations</i>			
Profit for the year on discontinued operations	18	1 845 284	284 256
Net profit for the operating year		4 770 912	2 086 272
Attributable to:			
- equity holders of the parent		3 967 881	1 722 636
- minority interest		803 031	363 636
Profit per share (in PLN)			
- basic earnings for the operating year	20	0,32	0,14
- basic earnings from the continuing operations	20	0,20	0,12

CONSOLIDATED BALANCE SHEET

for the years ended 31 December 2006 and 31 December 2007

	Note	As at 31 December 2007	As at 31 December 2006
ASSETS			
Non-current assets			
Property, plant and equipment	22	36 282 606	35 490 732
Investment property	25	15 933	21 411
Intangible assets	26	138 590	150 324
Held-to-maturity long-term investments	42.1	-	-
Loans and receivables	42.1	324 481	322 212
Available-for-sale financial assets	42.1	181 169	163 843
Shares in associates accounted for under the equity method	27	726 082	724 932
Other financial assets	33	395 417	388 133
Deferred tax assets	17	355 639	99 887
Non-current assets related to discontinued operations	18	-	9 808 008
Total non-current assets		38 419 917	47 169 482
Current assets			
Inventories	32	798 917	747 142
Income tax receivables		93 479	42 014
Short-term financial assets at fair value through profit or loss	42.1	318 586	433 547
Held-to-maturity short-term investments	42.1	69 660	-
Trade and other receivables	42.1	2 335 199	2 403 458
Other loans and financial assets	42.1	232 682	82 332
Available-for-sale short-term financial assets	42.1	84 823	81 876
Other current assets	33	226 562	343 189
Cash and cash equivalents	34, 42.1	2 726 378	3 310 154
Current assets related to discontinued operations	18	-	372 347
Total current assets		6 886 286	7 816 059
Non-current assets classified as held for sale	23	3 147	2 361
TOTAL ASSETS		45 309 350	54 987 902

CONSOLIDATED BALANCE SHEET

for the years ended 31 December 2006 and 31 December 2007

LIABILITIES AND EQUITY	Note	As at 31 December 2007	As at 31 December 2006
Equity (attributable to equity holders of the parent)			
Share capital	35.1	14 705 765	397 452
Equity of subsidiaries to increase the share capital of PGE	35.2	-	14 308 313
Capital for shares granted to employees	35.4	-	963 526
Revaluation reserve		6 214	7 519
Foreign exchange differences from translation of foreign entity		(1 392)	(73)
Reserve capital	35.6	1 945 841	480 703
Other capital reserves		202 311	202 311
Retained earnings	35.7	4 393 675	10 942 089
Minority interest	35.8	8 168 035	7 414 617
Total equity		29 420 449	34 716 457
Long-term liabilities			
Interest-bearing loans and borrowings	42.1	5 739 395	6 856 089
Other long-term liabilities	42.1	7 456	21 555
Provisions	36	2 807 271	2 761 280
Deferred tax liabilities	17	1 013 961	2 168 120
Deferred income and government grants	37	901 741	802 425
Long-term liabilities related to discontinued operations	18	-	1 547 933
Total long-term liabilities		10 469 824	14 157 402
Short-term liabilities			
Trade and other liabilities	42.1	1 553 996	1 634 836
Financial liabilities at fair value through profit or loss	42.1	17 817	86 359
Interest-bearing loans and borrowings	42.1	1 312 089	1 608 675
Other short-term financial liabilities	42.1	520 251	360 439
Other short-term non-financial liabilities		1 073 028	997 182
Income tax liabilities		188 066	186 445
Deferred income	37	28 389	54 692
Accruals		352 152	288 019
Short-term provisions	36	373 289	275 137
Short-term liabilities related to discontinued operations	18	-	622 259
Total short-term liabilities		5 419 077	6 114 043
Total liabilities		15 888 901	20 271 445
TOTAL LIABILITIES AND EQUITY		45 309 350	54 987 902

STATEMENT OF CHANGES IN CONSOLIDATED EQUITY

for the year ended 31 December 2007

	Note	Share capital	Share capital of subsidiaries to increase the share capital of PGE	Capital for shares granted to employees	Revaluation reserve	Foreign exchange differences	Reserve capital	Other capital reserves	Retained earnings	Total	Minority interest	Total equity
As at 1 January 2007		397 452	14 308 313	963 526	7 519	(73)	480 703	202 311	10 942 089	27 301 840	7 414 617	34 716 457
Revaluation of financial assets		-	-	-	(1 305)		-	-	-	(1 305)	(140)	(1 145)
Foreign exchange differences		-	-	-		(1 319)	-	-	-	(1 319)	-	(1 319)
<i>Total revenues and expenses for the period reflected in equity</i>		-	-	-	(1 305)	(1 319)	-	-	-	(2 624)	(140)	(2 764)
Profit		-	-	-			-	-	3 967 881	3 967 881	803 031	4 770 912
Total revenues/expenses for the year		-	-	-	(1 305)	(1 319)	-	-	3 967 881	3 965 257	802 891	4 768 148
Retained earnings distribution		-	-	-	-	-	2 174 975	-	(2 174 975)	-	-	-
Share issue (contribution of BOT GiE and PGE Energia)	35.1 35.4	14 308 313	(14 308 313)	-	-	-	-	-	-	-	-	-
Vesting of share-based payments for employees	35.8	-	-	1 354	-	-	-	-	-	1 354	490	1 844
Execution of vesting share-based payments for employees	35.4	-	-	(964 880)	-	-	-	-	964 880	-	-	-
Dividend in kind (demerger of PGE)		-	-	-	-	-	(709 837)	-	(8 918 460)	(9 628 297)	-	(9 628 297)
Purchase of ZEC Bydgoszcz	28	-	-	-	-	-	-	-	(245 576)	(245 576)	-	(245 576)
Dividend (including deductions from profit for the State Treasury)	35.8	-	-	-	-	-	-	-	(142 164)	(142 164)	(49 963)	(192 127)
As at 31 December 2007		14 705 765	-	-	6 214	(1 392)	1 945 841	202 311	4 393 675	21 252 415	8 168 035	29 420 449

PGE Polska Grupa Energetyczna S.A.



Consolidated financial statements for the year ended 31 December 2007
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STATEMENT OF CHANGES IN CONSOLIDATED EQUITY

for the year ended 31 December 2006

	Note	Share capital	Share capital of subsidiaries to increase the share capital of PGE	Capital for shares granted to employees	Revaluation reserve	Foreign exchange differences	Reserve capital	Other capital reserves	Retained earnings	Total	Minority interest	Total equity
As at 1 January 2006		397 452	14 308 313	899 794	5 146	-	478 922	-	10 142 175	26 231 802	7 068 291	33 300 093
Revaluation of financial assets		-	-	-	2 373	-	-	-	-	2 373	1 673	4 046
Foreign exchange difference		-	-	-	-	(73)	-	-	-	(73)	-	(73)
<i>Total revenues and expenses for the period reflected in equity</i>		-	-	-	2 373	(73)	-	-	-	2 300	1 673	3 973
Profit		-	-	-	-	-	-	-	1 722 636	1 722 636	363 636	2 086 272
Total revenues/expenses for the year		-	-	-	2 373	(73)	-	-	1 722 636	1 724 936	365 309	2 090 245
Retained earnings distribution		-	-	-	-	-	1 781	547 464	(549 245)	-	-	-
Vesting of share-based payments for employees	35.4	-	-	79 522	-	-	-	-	-	79 522	29 983	109 505
Execution of vesting of share-based payments for employees	35.4	-	-	(15 790)	-	-	-	-	15 790	-	-	-
Dividend in kind		-	-	-	-	-	-	(345 153)	-	(345 152)	-	(345 153)
Dividend (including deductions from profit for the State Treasury)	35.8	-	-	-	-	-	-	-	(389 267)	(389 267)	(48 966)	(438 233)
As at 31 December 2006		397 452	14 308 313	963 526	7 519	(73)	480 703	202 311	10 942 089	27 301 840	7 414 617	34 716 457

Applied accounting principles (policies) and explanatory notes are an integral part of the consolidated financial statements

CONSOLIDATED STATEMENT OF CASH FLOWS

for the years ended 31 December 2006 and 31 December 2007

	Year ended 31 December 2007	Year ended 31 December 2006
Cash flows – operating activities		
Gross profit / (loss) related to discontinued operations	1 733 975	256 307
Gross profit / (loss) related to continuing operations	1 977 517	2 197 179
Adjustments for:		
Share of profit from associates accounted under the equity method	(239 155)	(197 956)
Depreciation	3 840 786	3 836 665
Interest and dividend, net	574 268	421 064
Difference between fair value and carrying amount of dividends in kind paid	(1 931 875)	(343 762)
Profit / (loss) on investment activities	205 463	98 220
Change in receivables	(84 360)	(138 270)
Change in inventories	(51 774)	(21 636)
Change in liabilities (excluding loans and bank credits)	140 718	(139 681)
Change in prepayments and accruals	53 127	178 418
Change in provisions	144 143	208 824
Income tax paid	(592 001)	(357 597)
Other	(87 440)	(413 286)
Net cash from operating activities	5 683 391	5 584 490
Cash flows – investing activities		
Disposal of property, plant and equipment and intangible assets	87 018	17 596
Purchase of property, plant and equipment and intangible assets	(3 635 276)	(3 406 295)
Disposal of investment property	73	-
Purchase of investment property	-	-
Disposal of financial assets	750 731	1 200 565
Purchase of financial assets	(818 731)	(899 128)
Acquisition of an associate, after deduction of cash taken over	-	-
Dividends	236 707	388 213
Interest received	38 877	34 601
Loans repaid	7 991	8 191
Loans granted	(3 621)	(2 540)
Other	(175 247)	86 820
Net cash from investing activities	(3 511 478)	(2 571 977)

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	Year ended	Year ended
	31 December 2007	31 December 2006
Cash flows – financing activities		
Proceeds from the issue of shares	-	-
Repayment of finance lease obligations	(30 678)	(29 906)
Proceeds resulting from bank credits and loans	2 793 599	2 674 424
Repayment of bank credits and loans	(4 510 428)	(3 334 790)
Dividends paid	(229 763)	(395 683)
Interest paid	(761 767)	(566 144)
Other	(22 181)	(34 315)
Net cash from financing activities	(2 761 218)	(1 686 413)
Net change of cash and cash equivalents	(589 305)	1 326 100
Effect of foreign exchange rate changes	(130)	3 308
Cash and cash equivalents, beginning of the period	3 312 812	1 986 712
Cash and cash equivalents, end of period	2 723 507	3 312 812
including restricted cash and cash equivalents	51 299	39 567

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**APPLIED ACCOUNTING PRINCIPLES (POLICIES) AND
EXPLANATORY NOTES**

1. General information

PGE Polska Grupa Energetyczna S.A. Capital Group

PGE Polska Grupa Energetyczna S.A. Capital Group ("Group", "Capital Group", "PGE Group") consists of the Parent Company PGE Polska Grupa Energetyczna S.A. and subsidiaries (refer to point 2).

Polska Grupa Energetyczna S.A. ("Parent Company", "Company", "PGE") with its seat in Lublin, 21 A Garbarska Street (previous name: Polskie Sieci Elektroenergetyczne S.A. with its seat in Warsaw, 2 Mysia Street) was founded on the basis of 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 maintained by the District Court for the Capital City of Warsaw, XII Commercial Department, under no. KRS 0000059307.

Effective 7 September 2007, under Notary Deed, the Company changed its business name from Polskie Sieci Elektroenergetyczne Spółka Akcyjna to PGE Polska Grupa Energetyczna Spółka Akcyjna and its seat from Warsaw, 2 Mysia Street to Lublin, 21 A Garbarska Street.

As at the date of the consolidated financial statements, the Company was registered in the National Court Register maintained by the District Court in Lublin, XI Commercial Department, 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 energy,
- rendering of other services related to the above mentioned activities.

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

As described below, in note 18 of the consolidated financial statements, on 31 December 2007 a demerger of PGE Polska Grupa Energetyczna S.A. took place. As a result, an organized part of an enterprise, encompassing transmission system assets and relevant liabilities, was transferred to PSE-Operator S.A.

Effective 1 July 2004, activities related to transmission of electricity, reservation of transmission capacity, connecting users to the network and settling transactions on the balancing market were transferred to a newly-established company, PSE-Operator S.A., which is 100% owned by the State Treasury since 2006.

The State Treasury is the 100% shareholder of the Parent Company.

The consolidated financial statements of the Group comprise financial data for the year ended 31 December 2007 and comparative data for the year ended 31 December 2006.

2. Entities included in the Group

In 2006 and 2007 Polska Grupa Energetyczna Spółka Akcyjna Capital Group consisted of the enumerated below companies, consolidated directly and indirectly:

	<i>Entity</i>	<i>Head office</i>	<i>Scope of activity</i>	<i>Share in Parent Company's equity in 2006</i>	<i>Parent Company in 2006</i>	<i>Share in Parent Company's equity in 2007.</i>	<i>Parent Company in 2007</i>
1.	PGE-Energia S.A.	Lublin	holding management	-	a)	85,00%	PGE Polska Grupa Energetyczna S.A.
2.	Zespół Elektrowni Dolna Odra S.A.	Czarnów	manufacture of electric energy and heat	-	a)	85,00%	PGE-Energia S.A.
3.	Zamojska Korporacja Energetyczna S.A.	Zamość	sale of electric energy	-	a)	85,00%	PGE-Energia S.A.
4.	ZKE - Dystrybucja sp. z o.o.	Zamość	distribution of electric energy	-	b)	100,00%	Zamojska Korporacja Energetyczna S.A.
5.	Rzeszowski Zakład Energetyczny S.A.	Rzeszów	sale of electric energy	-	a)	85,00%	PGE-Energia S.A.
6.	RZE- Dystrybucja sp. z o.o.	Rzeszów	distribution of electric energy	-	b)	100,00%	Rzeszowski Zakład Energetyczny S.A.
7.	Elektrociepłownia Rzeszów S.A.	Rzeszów	manufacture of electric energy and heat	100,00%	Rzeszowski Zakład Energetyczny S.A.	100,00%	Rzeszowski Zakład Energetyczny S.A.
8.	Lubelskie Zakłady Energetyczne S.A.	Lublin	sale of electric energy	-	a)	85,00%	PGE-Energia S.A.
9.	LUBZEL-Dystrybucja sp. z o.o.	Lublin	distribution of electric energy	-	b)	100,00%	Lubelskie Zakłady Energetyczne S.A.
10.	Elektrociepłownia Lublin Wrotków sp. z o.o.	Lublin	manufacture and distribution of electric energy and heat	100,00%	Lubelskie Zakłady Energetyczne S.A.	100,00%	Lubelskie Zakłady Energetyczne S.A.
11.	Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.	Skarżysko-Kamienna	sale of electric energy	-	a)	85,00%	PGE-Energia S.A.
12.	ZEORK Dystrybucja sp. z o.o.	Skarżysko-Kamienna	distribution of electric energy	-	b)	100,00%	Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.

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	<i>Entity</i>	<i>Head office</i>	<i>Scope of activity</i>	<i>Share in Parent Company's equity in 2006</i>	<i>Parent Company in 2006</i>	<i>Share in Parent Company's equity in 2007.</i>	<i>Parent Company in 2007</i>
13.	Elektrociepłownia Kielce S.A.	Kielce	production and distribution of heat	100,00%	Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.	100,00%	Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.
14.	Łódzki Zakład Energetyczny S.A.	Łódź	sale of electric energy	-	a)	85,00%	PGE-Energia S.A.
15.	ŁZE - Dystrybucja sp. z o.o.	Łódź	distribution of electric energy	-	b)	100,00%	Łódzki Zakład Energetyczny S.A.
16.	Zakład Energetyczny Białystok S.A.	Białystok	sale of electric energy	-	a)	85,00%	PGE-Energia S.A.
17.	ZEB Dystrybucja sp. z o.o.	Białystok	distribution of electric energy	-	b)	100,00%	Zakład Energetyczny Białystok S.A.
18.	Zakład Energetyczny Łódź-Teren S.A.	Łódź	distribution of electric energy	-	a)	85,00%	PGE-Energia S.A.
19.	Zakład Energetyczny Łódź - Teren Obrót sp. z o.o.	Warszawa	manufacture and sale of electric energy	-	b)	100,00%	Zakład Energetyczny Łódź Teren S.A. c)
20.	Zakład Energetyczny Warszawa-Teren S.A.	Warszawa	manufacture and sale of electric energy	-	a)	85,00%	PGE-Energia S.A.
21.	ZEWT - Dystrybucja sp. z o.o.	Warszawa	distribution of electric energy	-	b)	100,00%	Zakład Energetyczny Warszawa Teren S.A.
22.	BOT Górnictwo i Energetyka S.A.	Łódź	holding management, electric energy turnover	-	a)	85,00%	PGE Polska Grupa Energetyczna S.A.
23.	BOT KWB Bełchatów S.A.	Bełchatów	coal mining, lignite enrichment	69,00%	BOT Górnictwo i Energetyka S.A.	69,00%	BOT Górnictwo i Energetyka S.A.
24.	BOT KWB Turów S.A.	Bogatynia	coal mining, lignite enrichment	69,00%	BOT Górnictwo i Energetyka S.A.	69,00%	BOT Górnictwo i Energetyka S.A.
25.	BOT Elektrownia Bełchatów S.A.	Rogowiec	manufacture and distribution of electric energy	69,00%	BOT Górnictwo i Energetyka S.A.	69,00%	BOT Górnictwo i Energetyka S.A.
26.	BOT Elektrownia Opole S.A.	Brzezinek/Opola	manufacture and distribution of electric energy, production and distribution of heat	69,00%	BOT Górnictwo i Energetyka S.A.	69,00%	BOT Górnictwo i Energetyka S.A.
27.	BOT Elektrownia Turów S.A.	Bogatynia	manufacture and distribution of electric energy and heat	69,00%	BOT Górnictwo i Energetyka S.A.	69,00%	BOT Górnictwo i Energetyka S.A.

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	<i>Entity</i>	<i>Head office</i>	<i>Scope of activity</i>	<i>Share in Parent Company's equity in 2006</i>	<i>Parent Company in 2006</i>	<i>Share in Parent Company's equity in 2007.</i>	<i>Parent Company in 2007</i>
28.	Elektrownia Turów BV	Nederlands	eurobond issue and processing	100,00%	BOT Elektrownia Turów S.A.	100,00%	BOT Elektrownia Turów S.A.
29.	Elektrownie Szczytowo Pompowe S.A.	Warszawa	manufacture of electric energy	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
30.	ZEW Dychów S.A.	Dychów	manufacture and distribution of electric energy	99,58%	Elektrownie Szczytowo Pompowe S.A.	99,60%	Elektrownie Szczytowo Pompowe S.A.
31.	ZEC Bydgoszcz S.A.	Bydgoszcz	manufacture and distribution of electric energy, distribution of heat	-	d)	85,00%	Elektrownie Szczytowo Pompowe S.A.
32.	PSE Electra S.A.	Warszawa	distribution of electric energy, retail and wholesale, advisory and financial mediation	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
33.	Elektrociepłownia Gorzów S.A.	Rzeszów	manufacture and distribution of electric energy and heat	87,24%	PGE Polska Grupa Energetyczna S.A.	87,24%	PGE Polska Grupa Energetyczna S.A.
34.	EXATEL S.A.	Warszawa	telecommunication services, construction, modernization and utilisation of telecommunication subsystems	94,94%	PGE Polska Grupa Energetyczna S.A.	94,94%	PGE Polska Grupa Energetyczna S.A.
35.	ELBIS sp. z o.o.	Rogowiec	electric energy turnover	100,00%	BOT Elektrownia Bełchatów S.A.	100,00%	BOT Elektrownia Bełchatów S.A.
36.	ELBEST sp. z o.o.	Rogowiec	hotel and gastronomical services, cleaning services	100,00%	BOT Elektrownia Bełchatów S.A.	100,00%	BOT Elektrownia Bełchatów S.A.
37.	Energoserwis – Kleszczów sp z o.o.	Kleszczów	distribution of electric energy, construction works, wholesale of construction materials	51,00%	ELBIS sp. z o.o.	51,00%	ELBIS sp. z o.o.
38.	Niepubliczny Zakład Opieki Zdrowotnej MegaMed sp. z o.o.	Bełchatów	medical practice, dentistry services, medical treatment, health protection	100,00%	BOT Elektrownia Bełchatów S.A.	96,91%	BOT Elektrownia Bełchatów S.A.
39.	ELMEN sp. z o.o.	Rogowiec	construction and renovation services	74,00%	BOT Elektrownia Bełchatów S.A.	74,00%	BOT Elektrownia Bełchatów S.A.
40.	Energetyka Boruta sp. z o.o.	Zgierz	manufacture of electric energy	96,90%	ELBIS sp. z o.o.	96,91%	ELBIS sp. z o.o.

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41.	Elektrownia Wodna Żarnowiec S.A.	Czymanowo	manufacture and distribution of electric energy	89,38%	Elektrownie Szczytowo Pompowe S.A.	89,66%	Elektrownie Szczytowo Pompowe S.A.
42.	Elektrownia Wiatrowa Kamieńsk sp. z o.o.	Kamieńsk	manufacture of electric energy	50,00%	Elektrownie Szczytowo Pompowe S.A.	50,00%	Elektrownie Szczytowo Pompowe S.A.
				50,00%	ZEW Porąbka Żar	50,00%	ZEW Porąbka Żar
43.	EnBud sp. z o.o.	Czymanowo	construction and renovation services for power industry	100,00%	Elektrownia Wodna Żarnowiec S.A.	100,00%	Elektrownia Wodna Żarnowiec S.A.
44.	Zespół Elektrowni Wodnych Porąbka-Żar S.A.	Międzybrodzie Bialskie	manufacture of electric energy	94,22%	Elektrownie Szczytowo Pompowe S.A.	94,36%	Elektrownie Szczytowo Pompowe S.A.
45.	EGO-Odra S.A.	Warszawa	construction of hydroelectric power stations, hydroelectric power stations management services	50,12%	Elektrownie Szczytowo Pompowe S.A.	50,00%	Elektrownie Szczytowo Pompowe S.A.
				47,86%	ZEW Porąbka Żar	50,00%	ZEW Porąbka Żar
46.	Bio-Energia ESP sp. z o.o.	Gdynia	management of energy system projects	65,72%	Elektrownie Szczytowo Pompowe S.A.	65,72%	Elektrownie Szczytowo Pompowe S.A.
				12,16%	ZEW Porąbka Żar	12,16%	ZEW Porąbka Żar
				21,27%	EW Żarnowiec	21,77%	EW Żarnowiec
47.	Zespół Elektrowni Wodnych Solina-Myczkowce S.A.	Solina	exploitation services	100,00%	Elektrownie Szczytowo Pompowe S.A.	100,00%	Elektrownie Szczytowo Pompowe S.A.
48.	Dychowskie Przedsiębiorstwo Eksploatacji Elektrowni ELDEKS sp. z o.o.	Dychów	manufacture of electric energy	100,00%	Zespół Elektrowni Wodnych Dychów S.A.	100,00%	Zespół Elektrowni Wodnych Dychów S.A.
49.	ESP Usługi sp. z o.o.	Warszawa	property management	100,00%	Elektrownie Szczytowo Pompowe S.A.	100,00%	Elektrownie Szczytowo Pompowe S.A.
50.	Budownictwo Hydroenergetyka - Dychów sp. z o.o.	Dychów	manufacture of steel constructions excluding services	100,00%	Zespół Elektrowni Wodnych Dychów S.A.	100,00%	Zespół Elektrowni Wodnych Dychów S.A.

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51.	Przedsiębiorstwo Usługowo-Produkcyjne ELTUR-SERWIS sp. z o.o.	Bogatynia	repair of boilers equipment and auxiliaries	100,00%	BOT Elektrownia Turów S.A.	100,00%	BOT Elektrownia Turów S.A.
52.	Przedsiębiorstwo Produkcji Sorbentów i Rekultywacji ELTUR-WAPORE sp. z o.o.	Bogatynia	excavation of limestone rock, plaster and chalk	100,00%	BOT Elektrownia Turów S.A.	100,00%	BOT Elektrownia Turów S.A.
53.	Przedsiębiorstwo Transportowe ELTUR-TRANS sp. z o.o.	Bogatynia	transportation services	100,00%	BOT Elektrownia Turów S.A.	100,00%	BOT Elektrownia Turów S.A.
54.	Przedsiębiorstwo Handlowo-Usługowe ELTUR-GLOBAL sp. z o.o.	Bogatynia	hotel management	100,00%	BOT Elektrownia Turów S.A.	100,00%	BOT Elektrownia Turów S.A.
55.	Centrum Medyczne Turów sp. z o.o.	Bogatynia	medical practice, dentistry services, medical treatment, health protection	-	e)	36,06%	BOT Elektrownia Turów S.A.
						63,94%	BOT KWB Turów S.A.
56.	Energo Invest Broker S.A.	Toruń	insurance brokerage	30,62%	BOT Elektrownia Bełchatów S.A.	30,62%	BOT Elektrownia Bełchatów S.A.
				25,00%	BOT Elektrownia Turów S.A.	25,00%	BOT Elektrownia Turów S.A.
57.	Przedsiębiorstwo Usługowo-Produkcyjne TOP SERWIS sp. z o.o.	Bogatynia	manufacture of equipment used for production of mechanical energy	89,00%	Przedsiębiorstwo Usługowo-Produkcyjne ELTUR-SERWIS sp. z o.o.	89,00%	Przedsiębiorstwo Usługowo-Produkcyjne ELTUR-SERWIS sp. z o.o.
58.	ENESTA sp. z o.o.	Stalowa Wola	manufacture and distribution of electric energy, manufacture of gas, distribution of fuel gas	84,85%	Rzeszowski Zakład Energetyczny S.A.	84,85%	Rzeszowski Zakład Energetyczny S.A.
59.	NOM sp. z o.o.	Warszawa	telecommunication services	65,00%	EXATEL S.A.	100,00%	EXATEL S.A.
60.	Energo-Tel SA	Warszawa	design and construction of technical infrastructure of buildings and communication centers	51,10%	EXATEL S.A.	51,10%	EXATEL S.A.

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61.	E-Telbank S.A.	Warszawa	data transmission and data communication	100,00%	EXATEL S.A.	100,00%	EXATEL S.A.
62.	PEC Gorzów sp. z o.o.	Gorzów Wielkopolski	manufacture, distribution and turnover of heat	100,00%	EC Gorzów S.A.	100,00%	EC Gorzów S.A.
63.	Towarzystwo Gospodarcze BEWA sp. z o.o.	Kleszczów	manufacture and sale of mineral water and carbonated soft drinks	100,00%	BOT KWB Bełchatów S.A.	100,00%	BOT KWB Bełchatów S.A.
64.	RAMB sp. z o.o.	Bełchatów	technical construction works not classified elsewhere	100,00%	BOT KWB Bełchatów S.A.	100,00%	BOT KWB Bełchatów S.A.
65.	BESTUR sp. z o.o.	Bełchatów	hotels, camping sites and restaurants management	100,00%	BOT KWB Bełchatów S.A.	100,00%	BOT KWB Bełchatów S.A.
66.	Przedsiębiorstwo Transportowo Sprzętowe BETRANS sp. z o.o.	Rogowiec	road transport, shipping	100,00%	BOT KWB Bełchatów S.A.	100,00%	BOT KWB Bełchatów S.A.
67.	Górnicy Klub Sportowy Bełchatów S.A.	Bełchatów	operating of stadium and sport facility	100,00%	BOT KWB Bełchatów S.A.	100,00%	BOT KWB Bełchatów S.A.
68.	ELECTRA Deutschland GmbH – pakiety sprawozdawcze wypełniane przez PSE-Electra S.A.	Germany	electric energy turnover	100,00%	PSE ELECTRA S.A.	100,00%	PSE ELECTRA S.A.
69.	ELECTRA Bohemia s.r.o. – pakiety sprawozdawcze wypełniane przez PSE-Electra S.A.	Czech Republic	hydroelectric power stations	100,00%	PSE ELECTRA S.A.	100,00%	PSE ELECTRA S.A.
70.	MEGAZEC sp. z o.o.	Białystok	renovation, installation, engine, boiler and turbine repair services, transportation services	100,00%	ZEC Bydgoszcz S.A.	100,00%	ZEC Bydgoszcz S.A.
71.	Zakład Energetyczny Białystok Przedsiębiorstwo Transportowo-Usługowe ETRA sp. z o.o.	Białystok	transportation services	100,00%	ZEB Dystrybucja sp. z o.o.	100,00%	ZEB Dystrybucja sp. z o.o.
72.	Zakład Energetyczny Białystok Przedsiębiorstwo Produkcyjno-Handlowe EKTO sp. z o.o.	Białystok	manufacture of machines and electric equipment	100,00%	ZEB Dystrybucja sp. z o.o.	100,00%	ZEB Dystrybucja sp. z o.o.

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73.	Energetyczne Systemy Pomiarowe sp. z o.o.	Białystok	publishing services	100,00%	ZEB Dystrybucja sp. z o.o.	100,00%	ZEB Dystrybucja sp. z o.o.
74.	Zakład Energetyczny Białystok Centrum Szkolenia Energetyki ESO sp. z o.o.	Białystok	education and training services	100,00%	ZEB Dystrybucja sp. z o.o.	100,00%	ZEB Dystrybucja sp. z o.o.
75.	Zakład Energetyczny Białystok Pracownia Projektowa ENSPRO sp. z o.o.	Białystok	preparing of technical documentation of network installation and energy equipment	100,00%	ZEB Dystrybucja sp. z o.o.	100,00%	ZEB Dystrybucja sp. z o.o.
76.	Przedsiębiorstwo Energetyki Ciepłej sp. z o.o. z siedzibą w Gryfinie	Gryfino	distribution and turnover of heat	80,00%	Zespół Elektrowni Dolna Odra S.A.	80,00%	Zespół Elektrowni Dolna Odra S.A.
77.	Zakład Usług Medycznych „ZUMED” sp. z o.o.	Nowe Czarnowo	medical practice, dentistry services, medical treatment, health protection	100,00%	Zespół Elektrowni Dolna Odra S.A.	100,00%	Zespół Elektrowni Dolna Odra S.A.
78.	EPO sp. z o.o.	Opole	wholesale of waste and metal scrap	50,00%	BOT Elektrownia Opole S.A.	50,00%	BOT Elektrownia Opole S.A.
79.	Przedsiębiorstwo Wielobranżowe Agtel sp. z o.o.	Zamość	services and manufacture of equipment for power industry	81,01%	Zamojska Korporacja Energetyczna S.A.	81,01%	Zamojska Korporacja Energetyczna S.A.
80.	Centrum Szkolenia i Rekreacji „Energetyk” sp. z o.o.	Krasnobród	organization of conferences, trainings, recreation	99,49%	Zamojska Korporacja Energetyczna S.A.	99,50%	Zamojska Korporacja Energetyczna S.A.
81.	Zakład Obsługi Energetyki sp. z o.o.	Zgierz	exploitation and repair services on security and automation, data transmission	100,00%	Zakład Energetyczny Łódź Teren S.A.	100,00%	Zakład Energetyczny Łódź Teren S.A.
82.	PSE - Południe sp. z o.o.	Katowice	distribution of electric energy	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
83.	PSE - Zachód sp. z o.o.	Poznań	trade and services on exploitation and renovation of electromagnetic networks	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.

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84.	PSE - Serwis sp. z o.o.	Warszawa	management and sale of properties on own account, construction services	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
85.	PSE - Północ sp. z o.o.	Bydgoszcz	distribution of electric energy	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
86.	PSE - Wschód sp. z o.o.	Radom	distribution of electric energy	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
87.	PSE - Info sp. z o.o.	Warszawa	software services and data processing	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
88.	EPC S.A.	Warszawa	research and development in technology	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.
89.	EPCON sp. z o.o.	Wrocław	services on Installation, repair, renovation of steam generators	100,00%	EPC S.A.	100,00%	EPC S.A.
90.	PSE - Centrum sp. z o.o.	Warszawa	management of electrical power engineering and distribution networks	100,00%	PGE Polska Grupa Energetyczna S.A.	100,00%	PGE Polska Grupa Energetyczna S.A.

a) As presented in note 28 of the consolidated financial statements in realization of the creation of PGE Capital Group the State Treasury increased the share capital of PGE-Energia S.A. in December 2006 and contributed 85% of the shares of regional energy companies and Zespół Elektrowni Dolna Odra S.A. The share capital increase was registered in January 2007. As the PGE Capital Group creation was settled by the pooling of interest method, regional energy companies, Zespół Elektrowni Dolna Odra S.A. and their subsidiaries are consolidated within the financial statements from the first presented period i.e. from 1 January 2006.

- b) Distribution companies were set up in 2006 by PGE-Energia S.A. In 2007 they were sold to respective regional energy companies. Operations are performed since 1st July 2007, after the demerger of regional energy companies and transfer of transmission assets.
- c) On 1st July 2007 Zakład Energetyczny Łódź-Teren S.A. transferred its rights from shares to PGE Polska Grupa Energetyczna S.A.
- d) As described in note 28 of the financial statements 85% of shares of ZEC Bydgoszcz S.A. were purchased in February 2007. As at 31 December 2006 the sole shareholder was the State Treasury. As the PGE Capital Group creation was settled by the pooling of interest method the company is being consolidated in the financial statements for the year ended 31 December 2006.
- e) The company Centrum Medyczne sp. z o.o. was created in 2007 as a result of merger of Przychodnia Lekarska TUR-MED sp. z o.o. (100% subsidiary of BOT KWB Turów S.A.) and ELTUR-ZDROWIE sp. z o.o. (100% subsidiary of BOT Elektrownia Turów S.A.).

As presented below in note 28, in the period of 2006-2007 there were changes in direct equity relations within the Group. Due to the settlement of reorganization of the Group as a transaction under common control under the pooling of interest method, the changes mentioned above did not have an influence on Group assets, liabilities, revenues, expenses and cash flows in this period.

As at 31 December 2006 and 31 December 2007 the Group's share in the total number of voting rights corresponded directly with the number of shares owned in equities of the entities.

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

The composition of the Management Board of the Parent Company as at the day of preparing the consolidated financial statements was as follows:

- Tomasz Zadroga – the President of the Management Board,
- Paweł Tomasz Urbański – the Vice President of the Management Board,
- Henryk Majchrzak – the Vice President of the Management Board,
- Adam Cichocki – the Vice President of the Management Board,
- Wojciech Topolnicki – the Vice President of the Management Board,
- Marek Trawiński – the Vice President of the Management Board,
- Piotr Szymanek – the Vice President of the Management Board.

As at 31 December 2006, the composition of the Management Board was as follows:

- Jacek Socha – acting as the President of the Management Board,
- Kazimierz Ferenc – the Vice President of the Management Board,
- Paweł Urbański – the Vice President of the Management Board,
- Henryk Baranowski – the Vice President of the Management Board,
- Andrzej Dudek – the Vice President of the Management Board.

From 1 January 2007 till the day of preparation of the presented consolidated financial statements the following changes in the Management Board took place:

- On 22 February 2007 the Supervisory Board of the Company acknowledged the request of Mr. Andrzej Dudek, the Vice President of the Management Board, concerning resignation from the position of Vice President of the Management Board,
- On 27 February 2007 the Extraordinary General Shareholders' Meeting appointed Mr. Jacek Socha to the position of the President of the Management Board,
- On 27 February 2007 the Extraordinary General Shareholders' Meeting appointed Mr. Emil Wojtowicz to the position of Vice President of the Management Board,
- On 4 July 2007 Mr. Jacek Socha resigned from the position of the President of the Management Board,
- On 4 July 2007 the Supervisory Board appointed Mr. Paweł Urbański, the Vice President of the Management Board, to perform duties of the President of the Management Board,
- On 4 July 2007 the Supervisory Board dismissed Mr. Kazimierz Ferenc from the position of Vice President of the Management Board,
- On 5 October 2007 the Supervisory Board appointed Mr. Paweł Urbański to the position of the President of the Management Board,

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- On 8 November 2007 the Extraordinary General Shareholders' Meeting appointed Mr. Konrad Milterski and Mr. Lech Suchcicki to the Management Board,
- On 12 November 2007 Mr. Konrad Milterski resigned from the function of Member of the Management Board,
- On 21 November 2007 the Supervisory Board suspended Mr. Lech Suchcicki, Member of the Management Board, in his activities until the case is settled but for a period no longer than 3 months from the date of this decision.

After the balance sheet date but before the date of preparing the financial statements the following changes in the Management Board took place:

- On 28 January 2008 the Supervisory Board dismissed Mr. Lech Suchcicki from the position of Member of the Management Board,
- On 30 June 2008 the term of office of the existing Management Board expired,
- On 1 July 2008 Mr. Paweł Urbański was appointed to the position of Vice President of the Management Board responsible for Investments and Development and to perform duties of the President of the Board,
- On 1 July 2008 Mr. Henryk Majchrzak was appointed to the position of Vice President of the Management Board responsible for Production,
- On 1 July 2008 Mr. Wojciech Topolnicki was appointed to the position of Vice President of the Management Board responsible for Finances,
- On 1 July 2008 Mr. Adam Cichocki was appointed to the position of Vice President of the Management Board responsible for Human Resources,
- On 21 July 2008 Mr Piotr Szymanek was appointed to the position of vice President of the Management Board responsible for Corporate and Legal Matters,
- On 23 July 2008 Mr Marek Trawiński was appointed to the position of vice President of the Management Board responsible for Trade and Distribution,
- On 1 August 2008 Mr Tomasz Zadroga was appointed to the position of the President of the Management Board.

4. Approval of the financial statements

The consolidated financial statements were approved for publication and signed by the Management Board of the Parent Company on 20th August 2008.

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.

Issues related to discontinued operations were presented in note 18 of the consolidated financial statements.

6. The basis for the consolidated financial statements

Statement of compliance

The consolidated financial statements are the first full annual consolidated financial statements prepared in accordance with IFRS approved by the European Union ("the EU IFRS"). For the purpose of the consolidated financial statements, the date of transition to IFRS is 1 January 2006.

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 prepare the consolidated financial statements in accordance with International Financial Reporting Standards approved by the European Union.

The consolidated financial statements were prepared in accordance with International Financial Reporting Standards (IFRS) and IFRS approved by the European Union. As at the day of approval of the consolidation financial statements for publication, regarding the EU process of implementing IFRS and the business activities of the Capital Group, there is no difference between the IFRS in force and IFRS approved by the European Union which would influence the Applied Accounting Principles of the Group.

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

The bookkeeping in the Capital Group is maintained in accordance with the accounting policies (rules) specified in the Accounting Act dated 29 September 1994 ("the Accounting Act", "PAS") and related bylaws, and other applicable regulations. The consolidated financial statements contain adjustments not included in the general ledger of Group companies. These were implemented so that the financial statements of these companies comply with IFRS approved by the EU.

7. 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.

8. Significant values based on estimates and professional judgment

8.1 Estimates and professional judgment

In the process of applying accounting rules with regards to the issues below, the most significant, apart from estimates, was the professional judgment of the management, which influenced the values presented in the 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 in the supplementary information and explanations notes to the financial statements.

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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. 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.

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 reclamation reserves

On the basis of Geological and Mining Law, lignite mines being part of the Group are obliged to perform land reclamation after the land exploitation is finished. The proper reserve 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 reclamation costs are updated at least every 5 years. The value of the reserve is verified each year according to the actual assumptions regarding inflation rate, discount rate and excavation volume. The discount rate applied to calculate the current value of reclamation costs is at the same level as for social benefits reserves.

Deferred tax assets

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. A 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.

Share-based payments

The Group shall recognize the cost of a transaction paid with equity instruments at fair value as at the day of the share-based payment. Share-based social benefits programs are specified in the Commercialization and Privatization Act of 30 June 1996, under the assumption that employees or others eligible for the program worked or began working before the grant date. The Group estimated the fair value as at the grant date and as at previous dates for the purpose of measurement of services rendered between the commencement of work and the grant date.

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 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.

Allowance for receivables

As at balance sheet date the entity assesses whether there is objective proof of impairment of receivables or a group of receivables. If the recoverable amount of assets is lower than its carrying amount, the entity performs an allowance to the amount of the present value of planned cash flows.

9. Change of estimates

In the periods covered by the consolidated financial statements there was a change of assumptions for estimation of actuarial and environmental provisions. The influence of the change of estimates on the value of reserves and profit or loss is presented in notes 31 and 36 of the consolidated financial statements.

10. First-time adoption of International Financial Reporting Standards

First-time adoption of IFRS / change of applied accounting principles

The International Accounting Standards Board issued International Financial Reporting Standard 1 (IFRS 1) *First-time Adoption of International Financial Reporting Standards*, effective for financial statements prepared for the periods starting 1 January 2004 or later. IFRS 1 applies when an entity adopts IFRS for the first time or when, in the entity's previous financial statements, discrepancies with particular standards were stated. According to IFRS 1 an entity's first IFRS financial statements are the first annual financial statements in which the entity adopts IFRS, by an explicit and unreserved statement in those financial statements of compliance with IFRS.

According to the above, the consolidated financial statements are the first complete annual financial statements prepared in accordance with IFRS approved by the EU. The date of transition to IFRS is 1 January 2006. As at the date of approval of the consolidated financial statements for publication, the last consolidated financial statements of the Group prepared in accordance with Polish Accounting Standards, specified in the Accounting Act, were the financial statements for the year ended 31 December 2006.

According to IFRS 1, the consolidated financial statements were prepared as if the Capital Group has always applied IFRS; however there were some exemptions from obligatory transitions specified in IFRS 1:

- *Business combinations (IFRS 1.15, Appendix B)*

The Group decided to use an exemption concerning business combinations. As specified in point 1 of Appendix B to IFRS 1, a first-time adopter may elect not to apply IFRS 3 Business Combinations retrospectively to past business combinations (business combinations that occurred before the date of transition to IFRS). As a result, the Group did not restate any business combination that took place before 1 January 2006.

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- *Fair value or revaluation as deemed cost (IFRS 1.16-19).*

According to International Accounting Standard 29 "Financial Reporting in Hyperinflationary Economies" (IAS 29) the value of assets and liabilities reported during the hyperinflationary period should be measured in current prices as at the end of the hyperinflationary period so that they constituted comparative data for the following reporting periods. The above IAS relates to non-monetary balance sheet positions. Property, plant and equipment, intangible assets and equity are significant non-monetary positions for the Group. The Polish economy fulfilled criteria of a hyperinflationary economy until the end of 1996; starting from 1997 the criteria were no longer fulfilled. The Capital Group did not apply IAS 29 regulations for the previous reporting periods. However, with regards to Polish law regulations, a revaluation of non-current assets was made as at 1 January 1995 in order to reflect the hyperinflation effect on their carrying amount with the use of revaluation indexes specified for particular groups of assets by the Ministry of Finance. This revaluation did not comply with IAS 29 as the Group did not use the general price index and did not execute the revaluation as at 31 December 1996.

The Group decided to use an exemption allowed by IFRS 1. Specified items of property, plant and equipment acquired before or during the hyperinflationary period were measured at fair value at the transition to IFRS date, i.e. 1 January 2006 and the Group used the fair value as the deemed cost at that date.

- *Share-based payment transactions (IFRS 1.25B)*

A first-time adopter is encouraged, but not required, to apply IFRS 2 *Share-based Payment* to equity instruments that were granted on or before 7 November 2002; and also those that were granted after 7 November 2002 that vested before the date of transition to IFRS, i.e. 1 January 2006. Due to the above, the Group decided to use the exemption allowed by IFRS 1 and did not apply IFRS 2 to equity instruments that were granted or acquired before 1 January 2006.

- *Cumulative translation differences (IFRS 1.22)*

The Group decided to use an exemption allowed by IFRS 1, so that cumulative translation differences for all foreign operations are deemed to be zero at the date of transition to IFRS.

The reconciliation of equity, assets and net profit for the year ended 31 December 2006 and the equity as at 1 January 2006 prepared in accordance with Polish Accounting Standards and IFRS are presented below.

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Adjustments implemented by the Group allowing full adoption of IFRS and their influence on the financial result and equity are presented below:

	Equity as at 1 January 2006	Equity as at 31 December 2006	Net profit for the year ended 31 December 2006	Assets as at 31 December 2006
Financial data presented in the consolidated financial statements in accordance with Polish Accounting Standards	5 365 694	6 567 777	1 549 003	9 438 518
1. Including minority interest in equity	56 164	60 637	4 161	-
2. Revaluation of property, plant and equipment	6 747 159	6 075 810	(671 137)	7 501 000
3. Payments from the net profit	-	-	288 881	-
4. Revaluation of financial instruments	2 576	4 493	1 917	8 764
5. Revaluation of provisions for employee benefits	(7 178)	(7 737)	(559)	-
6. Profit distribution for employee benefits	(219)	(479)	(479)	-
7. Presentation of net deferred tax	-	-	-	(60 343)
8. Presentation of net social funds	-	-	-	(5 434)
9. Including negative goodwill into equity	5 850	4 915	(935)	-
10. Difference on approach to consolidation of Group entities	21 130 047	22 011 041	915 420	38 105 397
Total of changed accounting principles	27 934 399	28 148 680	537 269	45 549 384
Financial data presented in the consolidated financial statements prepared in accordance with IFRS	33 300 093	34 716 457	2 086 272	54 987 902

Main adjustments between Polish Accounting Standards and IFRS:

Settlement of the creation of the PGE Capital Group

In the consolidated financial statements prepared in accordance with PAS, the settlement of the creation of the Group was accounted for under the purchase method. In the financial statements the above transaction was accounted for under the pooling of interest method. Details of the transaction were presented in detail in note 28.

Property, plant and equipment valuation

The Group valued chosen items of property, plant and equipment purchased prior to or during the hyperinflation period at fair value for the date of transition to IFRS, i. e. 1 January 2006 and used the value as deemed purchase cost at the date.

Reversal of deductions from profit

According to PAS, payments from net profit to the State Treasury are reflected as tax expense in the income statement. Due to its characteristics, such payments are recognized as payments of a dividend and reflected as a change in equity in accordance with IFRS.

Share-based payments

Based on the Commercialization and Privatization Act of 30 June 1996 current and former employees of PGE Capital Group entities are entitled to receive shares of entities that employed them at the date of the entity's removal from the register of state-owned enterprises under commercialization.

According to IFRIC 8, IFRS 2 Share based Payments is applicable to transactions where the entity issues its own financial instruments related to goods and services of which fair value cannot be estimated reliably. As a consequence, the granting of shares to employees was presented in the financial statements in accordance with IFRS 2.

Minority interests

According to Polish legal regulations, minority interest shares are reflected in a separate position in the consolidated equity, and minority interest in net result decreases the net profit. According to IFRS, entities present minority interests in the consolidated balance sheet within equity, separately from the parent shareholders' equity. Minority interests in the profit or loss of the group shall also be separately disclosed. Due to the above, adjustments to the presentation of minority interests were made.

Profit distribution for employee benefits

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

Assets of the Social Fund

According to Polish legal regulations, PGE Group entities manage assets of the Social Fund (ZFŚS) on behalf of their employees. Contributions paid to ZFŚS are deposited in separate bank accounts of entities.

In the consolidated financial statements, assets financing the Social Fund were recognised as cash or receivables.

In the consolidated financial statements, assets of the Social Fund were not recognized as there is no probability of the future economic benefits, which might generate inflow of cash or cash equivalents in the Group's bank account.

Presentation of non-current assets classified as held-for-sale

According to IFRS 5, as at 31 December 2004, the PGE Group classified part of property, plant and equipment and investment property as "Non-current assets classified as held for sale and assets classified in groups held for sale".

11. New standards and interpretations published, not yet effective

The following standards and interpretations were published by the International Accounting Standards Board or International Financial Reporting Interpretation Committee, but are not yet effective, nor have they been approved by the European Union when specified:

- IAS 1 *Presentation of Financial Statements* (revised in September 2007) – effective for annual periods starting on 1 January 2009 or later – until the day of approval of the consolidated financial statement IAS 1 has not been approved by the EU yet,
- IAS 23 *Borrowing costs* (revised in March 2007) – effective for annual periods starting on 1 January 2009 or later – until the day of approval of the consolidated financial statements IAS 23 has not been approved by the EU yet,
- IFRIC 11 *Group and Treasury Share Transactions* – effective for annual periods starting on 1 March 2007 or later,
- IFRIC 12 *Service Concession Arrangements* – effective for annual periods starting 1 January 2008 or later – until the date of approval of the consolidated financial statements IFRIC 12 has not been approved by the EU yet,
- IFRIC 13 *Customer Loyalty Programmes* – effective for annual periods starting on 1 July 2008 or later – until the day of approval of the consolidated financial statements IFRIC 13 has not been approved by the EU yet,
- IFRIC 14 IAS 19 Restrictions in valuation of particular benefit programmes assets, requirements of minimum financing and their interactions – effective for annual periods starting 1 January 2008 – until the date of approval of the consolidated financial statements IFRIC 14 has not been approved by the EU yet.
- IFRS 3 *Business Combinations* (revised in January 2008) – effective for annual periods starting 1 July 2009 or later – until the date of approval of the consolidated financial statements, IFRS 3 has not been approved by the EU yet,
- IAS 27 *Consolidated and Separate Financial Statements* (revised in January 2008) – effective for annual periods starting 1 July 2009 - until the date of approval of the consolidated financial statements, IAS 27 has not been approved by the EU yet,
- IFRS 2 *Share-based payments: vesting conditions and cancellations* (revised in January 2008) - effective for annual periods starting 1 January 2009 - until the date of approval of the consolidated financial statements, IFRS 2 has not been approved by the EU yet,
- Changes to IAS 32 and IAS 1: "Financial instruments with option of selling at fair value" (changed in February 2008) – effective for annual periods starting 1 January 2009 - until the date of approval of the consolidated financial statements, the changes to IAS 32 and IAS 1 have not been approved by the EU yet,

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- Improvements to IFRS – effective for annual periods starting 1 January 2009 - until the date of approval of the consolidated financial statements, the improvements to IFRS have not been approved by the EU yet,
- Amendments to IFRS 1 and IAS 27 “Cost of an investment in a subsidiary, jointly controlled entity or associate” - effective for annual periods starting 1 January 2009 - until the date of approval of the consolidated financial statements, the amendments to IFRS 1 and IAS 27 have not been approved by the EU yet,
- IFRIC 15 *Agreements for the Construction of Real Estate* - until the date of approval of the consolidated financial statements IFRIC 15 has not been approved by the EU yet,
- IFRIC 16 *Hedges of a Net Investment in a Foreign Operation* - until the date of approval of the consolidated financial statements IFRIC 16 has not been approved by the EU yet.

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

The Group decided on earlier adoption of IFRS 8 Operating segments in the consolidated financial statements.

12. Accounting principles applied

The most significant accounting principles applied are presented below.

12.1. Principles of consolidation

The consolidated financial statements comprise the financial statements of PGE Polska Grupa Energetyczna S.A. and financial data of its subsidiaries for the years ended 31 December 2006 and 31 December 2007. 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 to be impaired.

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 note 28, 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 judgement, 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 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 capital 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.

12.2. 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 to the carrying amount may also be necessary for changes in the investor's proportionate interest in the investee arising from changes in the investee's equity that have not been recognized in the investee's profit or loss. The investor's share of those changes is recognized directly in equity of the investor.

12.3. Investments 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 IFRS 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.

12.4. 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, capitalized 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.

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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 year end:

	31 December 2007	31 December 2006
USD	2,4350	2,9105
EUR	3,5820	3,8312

12.5. Property, plant and equipment

Property, plant and equipment are tangible items:

- 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 period;
- 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 carried at its cost 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 its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates, any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management and the initial 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.

An entity allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant parts and depreciates separately each such part. 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 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

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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	16	20 – 40
Machinery and equipment	11	5 – 15
Vehicles	5	5 – 7
Other	7	3 – 10

Depreciation method, depreciation rate and residual value of property, plant and equipment are verified at least each financial year-end. 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 derecognition 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. Construction in progress is not depreciated until the construction is finished and the items are available for use.

The cost of making lignite layers available for exploitation

As at the date of transition to IFRS, the technical services of BOT KWB Bełchatów S.A. performed an actualization of valuation 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 BOT KWB Turów S.A., 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 is recognized as a the cost of the current period.

12.6. 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 accounts 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. 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.

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 balance sheet) 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.

12.7. 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 finite or indefinite and, if finite, the length of, or number of production or similar units constituting, that 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 finite 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 finite 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 finite useful life shall be allocated on a systematic basis over its useful life. Amortization shall begin when the asset is available for

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use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management.

Intangible assets with a finite 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-end. 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	3	3 -5
Costs of finished development works	2	3 -5
Other	4	3 -5

12.8. 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 activities 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 an internally generated intangible asset:

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

12.9. Borrowing 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 an acceptable alternative approach specified in 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.

12.10. 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).

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.

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
 - a 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.

An entity shall not reclassify a financial instrument into or out of the fair value.

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 income statement.

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 discount rate. Loans and receivables are recognized at amortized cost.

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss. 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 (valuation at discounted cash flow method).

Positive and negative differences between fair value and acquisition cost, net of deferred tax, of financial assets available for sale are reflected in revaluation reserve (if their price is determinable on a regulated active market or if the fair value may be estimated by some other reliable method), 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 the 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 directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized directly in equity shall be removed from equity and recognized in profit or loss even though the financial asset has not been derecognized. The amount of the cumulative loss that is removed from equity 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.

12.11. Impairment of non-financial non-current assets

The Group assesses at each reporting 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 recognised 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.

12.12. 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 balance sheet 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.

12.13. 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 remeasuring 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 or an unrecognized firm commitment, or an identified portion of such an asset,

liability or firm commitment, that is attributable to a particular risk and could affect profit or loss,

- 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 or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction which could affect profit or loss, 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.

12.14. Fair value hedges

A fair value hedge is a hedge of the exposure to changes in fair value of a recognized asset, liability or an unrecognized firm commitment; or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss. The gain or loss on the hedged item attributable to the hedged risk shall adjust the carrying amount of the hedged item and be recognized in profit or loss, and the gain or loss from remeasuring the hedging instrument at fair value (for a derivative hedging instrument) or the foreign currency component of its carrying amount (for a non-derivative hedging instrument) shall be recognized in profit or loss.

The adjustment of carrying value of fair value hedges measured at amortized cost is amortized in profit or loss through the remaining period before the maturity.

When an unrecognized firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognized as an asset or liability with a corresponding gain or loss recognized in profit or loss. The changes in the fair value of hedging instruments are also recognized in profit or loss.

The Group shall discontinue prospectively the hedge accounting if the hedging instrument expires, is sold, terminated, exercised, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used shall be amortized to profit or loss. Amortization may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

12.15. Cash flow hedges

Cash flow hedge is a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with a recognized asset or liability or a highly probable forecast transaction and could affect profit or loss. The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge shall be recognized directly in equity through the statement of changes in equity and the ineffective portion of the gain or loss on the hedging instrument shall be recognized in profit or loss.

If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or a financial liability, the associated gains or losses that were recognized directly in equity shall be reclassified into profit or loss in the same period or periods during which the asset acquired or liability assumed affects profit or loss.

If a hedge of a forecast transaction subsequently results in the recognition of a non-financial asset or a non-financial liability, or a forecast transaction for a non-financial asset or non-financial liability becomes a firm commitment for which fair value hedge accounting is applied, the associated gains and losses that were recognized directly in equity shall be reclassified into profit or loss in the same period or periods during which the asset acquired or liability assumed affects profit or loss.

For cash flow hedges no longer qualifying for hedge accounting, amounts that had been recognized directly in equity shall be recognized in profit or loss in the same period or periods during which the hedged forecast transaction affects profit or loss.

The Group shall discontinue hedge accounting if the hedging instrument expires, is sold, terminated, exercised or the hedge no longer meets the criteria for hedge accounting. In this case, the cumulative gain or loss on the hedging instrument that remains recognized directly in equity from the period when the hedge was effective shall remain separately recognized in equity until the forecast transaction occurs. If the transaction is no longer expected to occur, the cumulative gain or loss that had been recognized directly in equity shall be recognized in profit or loss.

12.16. Hedges of shares in net assets of foreign entities

Hedges of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment, is accounted for similarly to cash flow hedges. The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge shall be recognized directly in equity through the statement of changes in equity and the ineffective portion shall be recognized in profit or loss. The gain or loss on the hedging instrument relating to the effective portion of the hedge that has been recognized directly in equity is recognized in profit or loss on disposal of the foreign operation.

12.17. 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.

12.18. 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.

An allowance 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.

12.19. 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.

12.20. 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.

PGE Polska Grupa Energetyczna S.A.

*Consolidated financial statements for the year ended 31 December 2006 and 31 December 2007
prepared in accordance with IFRS (all amounts in PLN thousands)
("Translation of a document originally issued in Polish")*

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 Group reviews 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 balance sheet.

Other assets also comprise receivables from the state.

12.21. 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 balance sheet 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.

12.22. Provisions

The Group recognizes a provision when it has 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:

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.

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 creates an appropriate provision. The amount of the provision is estimated by an actuary.

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 income statement 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.

Provision for recultivation of post-exploitation grounds, incl. recultivation and development of final excavations and recultivation of ash storages

The mining companies which belong to the Group create provisions for recultivation costs of post-exploitation grounds. The value of the provision is based on the estimated cost of recultivation 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 recultivation costs are updated at least once every five years; however at each year-end the amount of the recultivation 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 provision for recultivation of ash storages (electricity post-production waste) is recognized at the discounted value as a reserve when the storage starts operating, and is subsequently depreciated proportionally as the storage is filled. The discount is recognized in financial expenses.

12.23. 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.

12.24. Share-based payments

Share-based payments is 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 reporting date and at the date of settlement, with any changes in fair value recognized in profit or loss for the period.

12.25. 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 (ZFŚS) 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.

12.26. 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 entity'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 and some accruals for employee and other operating expenses, 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.

12.27. 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.

12.28. Accruals and deferred income

The Group recognizes accruals as costs:

- incurring of which is certain or highly probable,
- resulting from past events and causing the outflow of present or future assets of the entity,
- that can be reliably estimated.

Accruals are liabilities to pay for goods or services that have been received or supplied but have not been paid, invoiced or formally agreed with the supplier, including amounts due to employees. Although it is sometimes necessary to estimate the amount or timing of accruals, the uncertainty is generally much lower than it is for provisions.

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.

12.29. Emission rights

Emission rights for gases under the system of emission rights received from the National Emissions Trading Scheme (*Krajowy Plan Rozdziału Uprawnień*) are presented in nil value. 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 at fair value of insufficient rights as at the balance sheet date.

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. Due to the fact that the volume of actual emission of CO₂ by the Group did not exceed the volume granted over last three years (2005-2007), there were no indications to create an additional provision as at the balance sheet date.

When created, the provision is recognized in operating expenses.

12.30. 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 balance sheets 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.

12.31. Taxes

Corporate income tax in the income statement 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 that 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

12.32. 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.

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 sales 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.

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 that costs incurred to date bear 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.

12.33. Expenses

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 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 income statement).

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.

12.34. Other operating expenses and revenues

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 allowances, except from allowances 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.

12.35. Financial income and expenses

Financial income 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 reporting

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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.

12.36. Earnings per share

Earnings per share for each period are calculated by dividing the net profit for a given period by the weighted average number of shares during that period.

Due to the fact that the settlement of PGE Capital Group creation was accounted for under the pooling of interest method (as described in detail in note 28 of the consolidated financial statements), net profit per share both for the year ended 31 December 2006 and 31 December 2007 was calculated using the number of shares as at 31 December 2007.

12.37. Cash flows

Cash flows shall be prepared using the indirect method.

13. Operating segments

The Group adopted business segments as the primary reporting format and geographical segments as the supplementary reporting format. Management and organization of the Group entities is divided into segments based on the nature of goods sold and services rendered. Each segment constitutes a strategic economic unit, offering different goods and services and dealing in different markets.

Transactions between segments are settled within the Group as if they were concluded with third parties – using current market prices.

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Continuing operations							Discontinued operations		
31 December 2007	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Revenues									
Revenues from external customers	3 054 246	392 720	8 162 867	8 959 232	2 597 125	23 166 190	1 051 140		24 217 330
Revenues from sales between segments	5 696 981	34 520	634 706	4 741 327	5 190	11 112 724	-	(11 112 724)	-
Total revenues from segments	8 751 227	427 240	8 797 573	13 700 559	2 602 315	34 278 914	1 051 140	(11 112 724)	24 217 330
Profit / (loss) of a segment	1 423 407	87 557	254 855	264 270	104 225	2 134 314	(189 091)		1 945 223
Unallocated costs						-	-		-
Profit/ (loss) on continuing operations before tax and financial income/ expenses						2 134 314	(189 091)		1 945 223
Net financial income / expenses						(395 953)	1 923 066		1 527 113
Share of profit of associates	(262)				239 418	239 156	-		239 156

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Continuing operations							Discontinued operations		
31 December 2007	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Profit / (loss) before tax						1 977 517	1 733 975		3 711 492
Income tax						948 111	111 309		1 509 420
Net profit / (loss)						2 925 628	1 845 284		4 770 912
Assets and liabilities									
Assets of the segment	23 321 057	1 374 867	14 922 106	1 384 951	1 919 769	42 922 750			42 922 750
Shares in an associates	9 997				716 085	726 082			726 082
Unallocated assets						1 660 518			1 660 518
Total assets for reportable segments						45 309 350			45 309 350
Liabilities of the segment	3 709 922	38 115	2 312 124	521 014	386 433	6 967 608			6 967 608
Unallocated liabilities						8 921 293			8 921 293
Total liabilities for reportable segments						15 888 901			15 888 901

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Continuing operations							Discontinued operations		
31 December 2007	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Other information concerning:									
Capital expenditures:									
- on property, plant and equipment	2 274 922	91 814	874 989	5 119	492 452	3 739 296	322 363		4 061 659
- on intangible assets	11 235	-	10 920	2 316	8 696	33 167	24 260		57 427
- on investment property	1 126	-	426	-	-	1 552	-		1 552
Depreciation of property, plant and equipment	1 530 045	75 494	803 817	48 263	119 420	2 577 039	1 183 276		3 760 315
Amortization of intangible assets	11 332	715	15 995	3 732	11 673	43 447	35 310		78 757
Impairment losses on property, plant and equipment	49 279	930	-	-	-	50 209	-		50 209
Revaluation allowances on inventories	100 461	197	79	-	-	100 737	-		100 737

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Continuing operations							Discontinued operations		
31 December 2007	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Other impairment losses	10 489	31 423	(19 827)	3 732	2 590	28 407	-		28 407
Other non-monetary costs									
- retirement and pension benefits provision	131 573	180	40 274	231	3 871	176 129	-	-	176 129
- recultivation provision	76 841	-	-	-	-	76 841			76 841
- other	19 141	-	7 344	88 108	296	114 889	(126 708)		(11 819)

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Continuing operations							Discontinued operations		
31 December 2006	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Revenues									
Revenues from external customers	3 120 319	369 477	8 123 000	10 385 233	2 345 984	24 344 013	1 289 734		25 633 747
Revenues from sales between segments	5 211 678	113 279	625 843	3 745 037	10 055	9 705 892	-	(9 705 892)	-
Total revenues from segments	8 331 997	482 756	8 748 843	14 130 270	2 356 039	34 049 905	1 289 734	(9 705 892)	25 633 747
Profit / (loss) of a segment	1 307 563	71 580	228 254	643 635	96 672	2 347 704	(135 087)		2 212 617
Unallocated costs						(25 002)	-		(25 002)
Profit/ (loss) on continuing operations before tax and financial income/ expenses						2 322 702	(135 087)		2 187 615
Net financial income / expenses						(323 480)	391 394		67 914
Share of profit of associates	64	-	-	-	197 893	197 957	-		197 957

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Continuing operations							Discontinued operations		
31 December 2006	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Profit / (loss) before tax						2 197 179	256 307		2 453 486
Income tax						(395 163)	27 949		(367 214)
Net profit / (loss)						1 802 016	284 256		2 086 272
Assets and liabilities									
Assets of the segment	22 842 027	1 361 690	14 715 994	2 185 156	1 752 038	42 856 905	10 180 355		53 037 260
Shares in an associates	10 259				714 673	724 932	-		724 932
Unallocated assets						1 225 710	-		1 225 710
Total assets for reportable segments						44 807 547	10 180 355		54 987 902
Liabilities of the segment	3 684 809	41 844	2 129 369	572 402	353 231	6 781 655	330 502		7 112 157
Unallocated liabilities						11 319 598	1 839 690		13 159 288
Total liabilities for reportable segments						18 101 253	2 170 192		20 271 445
Other information concerning:									

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Continuing operations							Discontinued operations		
31 December 2006	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Capital expenditures:									
- on property, plant and equipment	1 306 438	145 950	790 138	10 879	282 400	2 535 805	361 796		2 897 601
- on intangible assets	14 832	152	17 459	5 655	4 594	42 692	33 067		75 759
- on investment property	391	-	-	-	-	391	-		391
Depreciation of property, plant and equipment	1 549 418	70 333	791 915	46 824	121 018	2 579 508	1 191 223		3 770 731
Amortization of intangible assets	9 518	653	13 599	3 536	10 537	37 843	27 142		64 985
Impairment losses on property, plant and equipment	(589)	43	-	-	-	(546)	-		(546)
Revaluation allowances on inventories	99 514	164	(30)	-	-	99 648	-		99 648
Other impairment losses	28 706	-	(30 410)	55	8 441	6 792	-		6 792

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Continuing operations							Discontinued operations		
31 December 2006	Segment: Mining of fuels and production of energy from traditional sources	Segment: Production of energy from renewable sources	Segment: Turnover and distribution of energy and other products of energy market	Segment: Wholesale of energy and other products of energy market	Segment: Other operations	Total	Segment: Lease of transmission system assets	Exclusions	Total
Other non-monetary costs									
- retirement and pension benefits provision	112 610	3 393	41 036	1 447	6 382	164 868			164 868
- recultivation provision	(150 533)	-	-	-	-	(150 533)	-		(150 533)
- other	35 362	-	233	16 809	481	52 885	8 636		61 521

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Geographical segments

Year ended 31 December 2007

Revenues	Domestic market	EU countries	Other countries	Total
Revenues from continuing operations	22 537 972	320 695	307 523	23 166 190
Revenues from discontinued operations	1 051 140	-	-	1 051 140
Total revenues	23 589 112	320 695	307 523	24 217 330
Sales between segments	11 112 724	-	-	11 112 724
Revenues from the segment	34 701 836	320 695	307 523	35 330 054

Other information on the segment	Domestic market	EU countries	Other countries	Total
Assets of the segment	42 904 964	17 786	-	42 922 750
Unallocated assets	1 660 291	227	-	1 660 518
Investment in associates	726 082	-	-	726 082
Total assets	45 291 337	18 013	-	45 309 350

Capital expenditures	Domestic market	EU countries	Other countries	Total
Property, plant and equipment	3 733 770	5 526	-	3 739 296
Intangible assets	33 167	-	-	33 167
Investment property	1 552	-	-	1 552

Year ended 31 December 2006

Revenues	Domestic market	EU countries	Other countries	Total
Revenues from continuing operations	23 130 667	859 316	354 030	24 344 013
Revenues from discontinued operations	1 289 734	-	-	1 289 734
Total revenues	24 420 401	859 316	354 030	25 633 747
Sales between segments	9 705 892	-	-	9 705 892
Revenues from the segment	34 126 293	859 316	354 030	35 339 639

Other information on the segment	Domestic market	EU countries	Other countries	Total
Assets of the segment	42 856 568	337	-	42 856 905
Unallocated assets	1 225 483	227	-	1 225 710
Investment in associates	724 932	-	-	724 932
Total assets	44 806 983	564	-	44 807 547

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Capital expenditures	Domestic market	EU countries	Other countries	Total
Property, plant and equipment	2 530 498	5 307	-	2 535 805
Intangible assets	42 692	-	-	42 692
Investment property	391	-	-	391

14. Revenues and expenses

	Note	Year ended 31 December 2007	Year ended 31 December 2006
14.1. Other operating revenues			
Profit on disposal of non-financial non-current assets		6 880	4 760
Reversal of impairment allowances of receivables	42.2	91 284	83 256
Reversal of impairment allowances of other assets		2 284	3 790
Provisions reversed		91 513	32 718
Compensations, penalties and fines received		44 689	24 085
Donations received		8 050	6 946
Taxes refunded		21 659	26 466
Court fees refund		1 310	2 157
Redemption of liabilities		190	3 852
Assets acquired free of charge		8 495	8 790
Reinvoiced revenues		4 171	1 878
Sale of CO ₂ emission rights		3 777	-
Change of valuation of recultivation provision		232 395	207 482
Illegal consumption of power		3 027	298
Contractual penalties		664	20 179
Other		52 053	50 259
Total other operating revenues		572 441	476 916
14.2. Other operating expenses			
Creation of allowances for impairment of receivables	42.2	26 829	33 786
Creation of allowances for impairment on other assets		77 541	57 451
Loss on disposal of property, plant and equipment and intangible assets		79 536	85 234
Creation of provisions		164 641	35 177
Donations made		5 915	9 569
Compensations		31 694	12 566
Court fees paid		6 194	2 147
Liquidation of damages/removal of failures		18 666	6 415
Liquidation of non-financial non-current assets		7 502	10 753
Write-off of receivables		2 892	1 039
Costs of social activities		7 020	6 458
Other		52 606	49 410
Total other operating expenses		481 036	310 005

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14.3. Financial income	Year ended 31 December 2007	Year ended 31 December 2006
Other financial income from financial instruments	592 238	429 589
Dividends	5 405	3 403
Interest income	226 850	186 120
<i>incl. interest on impaired financial assets</i>	<i>3 217</i>	<i>10 061</i>
Revaluation / reversal of impairment losses	15 947	21 307
Profit on disposal of investments	45 885	26 562
Foreign exchange gains	298 151	192 197
Other financial income	38 660	62 423
Discount rate adjustments	1 420	-
Commissions for guarantees granted	979	428
Interest on state receivables	940	38 944
Reversal of provisions	24 649	14 457
Other	10 672	8 594
Total financial income	630 898	492 012
14.4. Financial expenses		
Financial expenses from financial instruments	866 762	667 388
Interest costs	466 655	530 115
Revaluation	203 278	16 532
Impairment losses	39 699	10 968
Loss on disposal of investments	18 769	15 677
Foreign exchange losses	138 361	94 096
Other financial expenses	160 089	148 104
Interest costs	134 087	124 357
Interest paid relating to state liabilities	293	3 107
Creation of provisions	23 771	12 601
Other	1 938	8 039
Total financial expenses	1 026 851	815 492

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14.5. Cost by kind	Year ended 31 December 2007	Year ended 31 December 2006
Depreciation	2 608 735	2 590 505
Materials and energy	3 252 958	3 197 298
External services	6 569 850	7 286 674
Taxes and charges	849 893	805 974
Personnel expenses	3 502 417	3 451 777
Other	210 521	175 817
Total cost by kind	16 994 374	17 508 045
Change in inventories	(60 852)	30 480
Cost of products and services for own use	(891 369)	(755 000)
Cost of finished goods sold	16 042 153	16 783 525
Selling expenses	(452 732)	(524 379)
General and administrative expenses	(948 512)	(825 469)
Cost of merchandise and materials sold	5 081 127	5 404 697
Cost of goods sold	19 722 036	20 838 374

15. Depreciation costs and impairment losses in the income statement

	Year ended 31 December 2007	Year ended 31 December 2006
Included in cost of goods sold:	2 542 281	2 523 810
Property, plant and equipment depreciation	2 500 075	2 484 564
Intangible assets amortization	34 966	28 222
Impairment losses on property, plant and equipment	(2 067)	(1 532)
Operating lease fees	-	-
Other	9 307	12 556
Included in distribution and selling expenses:	7 922	9 104
Property, plant and equipment depreciation	6 945	7 720
Intangible assets amortization	977	1 384
Included in general and administrative expenses:	55 681	54 850
Property, plant and equipment depreciation	48 177	45 760
Intangible assets amortization	7 504	8 237
Impairment losses on property, plant and equipment	-	853
Other	-	-
Included in change in inventories, prepayments and accruals	1 062	540
Included in costs of products and services for own use	1 789	2 201

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16. Employee benefits expenses

	Year ended 31 December 2007	Year ended 31 December 2006
Payroll	2 556 793	2 414 053
Social security expenses	495 223	472 096
Retirement and pensions costs	54 231	40 848
Jubilee benefits and allowances	67 234	68 187
Other post-employment benefits	48 855	71 451
Other payroll-related expenses	280 081	385 142
General employee benefits expenses:	3 502 417	3 451 777
Included in costs of goods sold	2 806 930	2 942 015
Included in distribution and selling expenses	165 357	83 847
Included in general and administrative expenses	537 609	440 943
Included in costs of products and services for own use	22 207	18 429
Change in inventories	(29 686)	(33 457)

17. Income tax

Main elements of income tax expense for the year ended 31 December 2007 and for the year ended 31 December 2006 are as follows:

	Year ended 31 December 2007	Year ended 31 December 2006
Consolidated income statement		
<i>Current income tax</i>	461 396	308 547
Current income tax expense	467 344	352 552
Previous periods' current income tax adjustments	(5 948)	(44 005)
 <i>Deferred income tax</i>	 (1 409 507)	 86 616
Related to creation and reversal of temporary differences	(1 409 507)	86 616
 <i>Income tax expense as in the consolidated income statement</i>	 (948 111)	 395 163
Statement of changes in consolidated equity		
<i>Current income tax</i>		
Tax effect of increase in share capital expenses	-	-
 <i>Deferred income tax</i>		
Tax on net profit / (loss) from cash flows hedges revaluation	-	-
Tax on unrealized profit / (loss) from financial assets available for sale	403	(655)
Tax on cash flow hedges settled during the financial year	-	-
 <i>Tax income/(expense) recognized in equity</i>	 403	 (655)

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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 year ended 31 December 2007 and 31 December 2006 is as follows:

	Year ended 31 December 2007	Year ended 31 December 2006
Gross profit/(loss) before tax from continuing operations	1 977 517	2 197 178
Gross profit/(loss) before tax from discontinued operations	1 733 975	256 307
Gross profit/(loss) before tax	3 711 492	2 453 485
Income tax according to Polish statutory tax rate of 19% (2006: 19%)	705 183	466 162
Previous periods current income tax adjustments	(5 948)	(44 005)
Non -tax deductible costs	99 234	149 119
Non -taxable revenues	(436 314)	(249 444)
Taxable revaluation of assets	(1 369 451)	
Other	(52 124)	45 381
Tax at effective tax rate of 28,5 % (2006: 15 %)	(1 059 420)	367 213
Income tax as presented in consolidated income statement	(948 111)	395 163
Income tax related to discontinued operations	(111 309)	(27 950)

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Deferred tax liability	Consolidated balance sheet	
	As at 31 December 2007	As at 31 December 2006
1996-2000 investment relief	924	612
Difference between tax value and carrying amount of property, plant and equipment	1 133 477	2 456 819
Accrued interest on deposits, loans granted, bonds and receivables	3 921	5 820
Interest and discount on bonds	16 094	10 114
Difference between tax value and carrying amount of other financial assets	19 142	17 360
Difference between tax value and carrying amount of financial liabilities	5 173	-
Current period revenues unrealized for tax purposes	138 757	223 208
Difference between tax value and carrying amount of energy origin units of ownership	14 489	10 492
Elektrownia Turów BV tax to be paid in Poland	-	4 349
Difference between tax value and carrying amount of financial assets	2 524	2 927
Other	177 952	146 078
Gross deferred tax liability	1 512 453	2 877 779

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Deferred tax asset	Consolidated balance sheet	
	As at	As at
	31 December 2007	31 December 2006
<i>Deferred tax asset</i>		
Difference between tax value and carrying amount of property, plant and equipment	100 608	67 079
Current period costs not realized for tax purposes	39 094	42 495
Provisions for employee benefits	231 977	225 281
Provisions for recultivation of final excavations	258 998	274 908
Provisions for costs of liquidation of property, plant and equipment and recultivation of ash storages	28 405	21 394
Accruals for employee bonuses	21 920	28 267
Difference between tax value and carrying amount of financial assets	10 861	14 733
Difference between tax value and carrying amount of financial liabilities	4 252	21 976
Difference between tax value and carrying amount of inventories	18 950	18 175
Payroll and other employee benefits	60 696	65 731
Tax losses	14 129	44 808
Energy infrastructure acquired free of charge and connection payments received	123 229	-
Other provisions	9 080	5 510
Other	186 615	248 370
Gross deferred tax asset	1 108 814	1 078 727
Impairment losses on tax asset	254 682	269 179
Net deferred tax asset	854 132	809 548
Presentation of deferred tax asset and liability at the Group level	(658 322)	(2 068 233)
Deferred tax asset	355 639	99 887
Net deferred tax liability	(1 013 961)	(2 168 120)

The above presented impairment allowances on deferred tax asset mainly relate to provisions for recultivation in lignite mines.

18. Discontinued operations

In March 2006 the Ministry of Economy prepared "The Programme for Electroenergetic Power Engineering" ("Programme"). The Programme's purpose is to decrease costs of energy production, distribution and transmission as well as to solve the long-term contracts problem in the energy sector, to increase the safety of the sector and to realize economic, harmonic growth through limitation of the power industry influence on the environment.

The Programme included among other things the demerger of PGE Polska Grupa Energetyczna S.A. and separation of Transmission System Operator (TSO), together with the assets related to the transmission system, followed by transferring the TSO to the State Treasury. The demerger took place in two stages:

- In 2006 100% of PSE-Operator S.A. shares were transferred to the State Treasury as a dividend in kind;
- In 2007 the demerger of PGE S.A. took place and the organized part of an enterprise was contributed in kind to PSE-Operator S.A.

For the purpose of realization of the above mentioned Programme, the Management Board of PGE Polska Grupa Energetyczna S.A. ("Demerged Entity") together with the Management Board of PSE-Operator S.A. ("Taking over Entity") prepared the Demerger Plan of PGE S.A.

The demerger activities were as follows:

- split of the Demerged Entity's property, plant and equipment and intangible assets required to run the TSO activity, constituting a separate entity (the TSO enterprise) in the meaning of article 551 of the Civil Code,
- split of liabilities related to the TSO Enterprise,
- transfer of assets and liabilities to PSE-Operator S.A. (Taking over Entity)

The above mentioned transfer was executed on 31 December 2007, i.e. at the date of registration of the increase in share capital of the Taking over Entity (the "Demerger date"). Within the demerger the Taking over Entity took over the assets and liabilities of the Demerged Entity specified (enumeratively or exemplified) in the Tables to the Demerger Plan, subject to changes in the TSO Enterprise assets and relevant liabilities resulting from continuance of operations.

The Demerged Entity as the owner of the TSO Enterprise and the Taking over Entity as the lessee of the majority of property, plant and equipment and intangible assets required to run the TSO activity, that constituted the organized part of an enterprise, ran their business activity until the Demerger date so that no significant changes to the assets were made apart from their general administration. The following actions were taken within the business activity:

- purchasing and disposals of assets and relevant changes in receivables and liabilities,
- continuing of investments started,
- applying for administrative decisions, including permits.

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Such new assets and liabilities acquired or recognized in the period of TSO enterprise functioning were booked and presented in the accounting records of the TSO enterprise, under the condition that they were related to the TSO operations and were transferred to the Taking over Entity in accordance with article 531 of the Commercial Code.

Other purchased assets and relevant liabilities recognized in the period between the creation of the Demerger Plan and the Demerger Date, including consequences of administrative decisions, were assigned to the Demerged Entity.

Subsequent to the demerger, the Demerged Entity separated a group of property, plant and equipment and intangible assets relevant to running the electricity turnover activity and functioning as a holding (including rendering centralized strategic and support services to Capital Group entities).

In the consolidated financial statements the operations transferred within the Demerger Plan to PSE-Operator S.A. were presented in the following manner:

- in the balance sheet – as separate positions of non-current and current assets related to the discontinued operations;
- in the income statement – as a separate position of profit from discontinued operations

Financial results of the transmission activity were as follows:

	Year ended 31 December 2007	Year ended 31 December 2006
Revenues	1 222 118	1 292 827
Expenses	(1 411 209)	(1 427 914)
Loss on sales	(289 091)	(135 087)
Net financial result	(8 809)	47 632
Difference of dividend in kind at fair value and its carrying amount	1 931 875	343 762
Profit before tax	1 733 975	256 307
Income tax	111 309	27 949
Net profit from discontinued operations	1 845 284	219 256

The main item influencing the profit from discontinued operations in the above presented periods is the difference between the fair value of assets transferred as dividend in kind and their carrying amount:

- In 2006 – on 31 December 2006 the transfer of all of PSE-Operator S.A. shares to the State Treasury as a dividend in kind took place for the purpose of realization of the above described "Programme for Electric Power Engineering" and fulfilling the requirements of the Energy Law. As a result, a previously created reserve capital in the amount of PLN 345,152 thousand was reversed. The difference between the carrying amount of the transferred shares and their fair value in the amount of PLN 343,762 thousand was recognized in the income statement related to the discontinued operations.
- In 2007 – the transfer of assets and liabilities relevant to the discontinued operations to PSE-Operator S.A. took place as realization of the last stage of the Demerger Plan. As a result, reserve capital and retained earnings of the parent entity were decreased by the amount of the fair value of net assets specified at the Demerger date. The difference between their carrying amount and the fair value of PLN 1,931,875 thousand was

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recognized in the income statement in the section associated to the discontinued operations.

The main groups of assets and liabilities related to discontinued operations as per carrying amount as at 31 December 2006 were as follows:

	As at 31 December 2006
Assets	
Intangible assets	154 608
Property, plant and equipment	9 653 400
Trade receivables	354 295
Other assets	18 052
Assets related to discontinued operations	<u>10 180 355</u>
Liabilities	
Trade liabilities	2 899
Loans and credits	466 577
Deferred tax liability	1 373 113
Short-term provisions	126 764
Other liabilities (mainly due to purchases of non-current assets)	200 839
Liabilities relevant to assets classified as discontinued operations	<u>2 170 192</u>
Net assets related to discontinued operations	<u><u>8 010 163</u></u>

Net cash flows from discontinued operations were as follows:

	Year ended 31 December 2007	Year ended 31 December 2006
Cash flows from operating activities	1 218 803	842 332
Cash flows from investment activities	(389 570)	(464 902)
Cash flows from financial activities	(477 731)	(49 855)
Net cash inflow/(outflow)	351 502	327 575
Profit per share:		
Basic from discontinued operations	0,13	0,02
Diluted from discontinued operations	0,13	0,02

Presented below are changes in the value of property, plant and equipment and intangible assets related to discontinued operations in the periods covered by the consolidated financial statements.

Changes in property, plant and equipment from 1 January 2007 to 31 December 2007:

Position	Land (including right of perpetual usufruct of land)	Buildings and construction	Machinery and equipment	Vehicles and other	Other	Construction in progress	Total
Gross book value							
Opening balance	42 574	8 145 729	1 942 601	88	4 255	696 359	10 831 606
Direct purchase	-	-	-	-	-	322 363	322 363
Transfer from construction in progress	-	203 679	95 599	-	2 100	(301 378)	-
Disposal	(11 699)	(159)	(17)	-	-	(82 614)	(94 489)
Liquidation	-	(590)	(10 422)	-	(30)	-	(11 042)
Other	-	-	(142)	-	(1)	-	(143)
Transfer to PSE-Operator	(30 875)	(8 348 659)	(2 027 619)	(88)	(6 324)	(634 730)	(11 048 295)
Closing balance	-	-	-	-	-	-	-
Accumulated depreciation (amortization)							
Opening balance	800	966 571	209 545	19	772	499	1 178 206
Depreciation	800	968 332	213 212	19	913	-	1 183 276
Decrease of impairment losses	-	-	-	-	-	(499)	(499)
Disposal	-	(6)	(6)	-	-	-	(12)
Liquidation	-	(125)	(6 437)	-	(20)	-	(6 582)
Other	-	-	(128)	-	-	-	(128)
Transfer to PSE-Operator	(1 600)	(1 934 772)	(416 186)	(38)	(1 665)	-	(2 354 261)
Closing balance	-	-	-	-	-	-	-
Opening balance, net book value	41 774	7 179 158	1 733 056	69	3 483	695 860	9 653 400
Closing balance, net book value	-	-	-	-	-	-	-

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Changes in property, plant and equipment from 1 January 2006 to 31 December 2006:

Position	Land (including right of perpetual usufruct of land)	Buildings and construction	Machinery and equipment	Vehicles and other	Other	Construction in progress	Total
Gross book value							
Opening balance	44 159	7 954 220	1 799 958	88	3 477	694 774	10 496 676
Direct purchase	-	-	-	-	-	361 796	361 796
Transfer from construction in progress	268	193 018	166 236	-	802	(360 324)	-
Disposal	(1 844)	(858)	(8)	-	-	(11)	(2 721)
Transfer between groups of assets	-	-	(2)	-	2	-	-
Liquidation	-	(492)	(23 577)	-	(23)	-	(24 092)
Other	(9)	(159)	(6)	-	(3)	124	(53)
Closing balance	42 574	8 145 729	1 942 601	88	4 255	696 359	10 831 606
Accumulated depreciation (amortization)							
Opening balance	-	-	-	-	-	46 155	46 155
Depreciation	800	966 590	223 053	19	761	-	1 191 223
Decrease of impairment losses	-	-	-	-	-	(45 656)	(45 656)
Disposal	-	(21)	(1)	-	-	-	(22)
Liquidation	-	(42)	(13 829)	-	(13)	-	(13 884)
Other	-	44	322	-	24	-	390
Closing balance	800	966 571	209 545	19	772	499	1 178 206
Opening balance, net book value	44 159	7 954 220	1 799 958	88	3 477	648 619	10 450 521
Closing balance, net book value	41 774	7 179 158	1 733 056	69	3 483	695 860	9 653 400

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As at 31 December 2006 the specified below loans related to investments in the transmission assets were related to the discontinued operations:

- Borrowing facility signed with the World Bank on 25 January 1996 in the amount of USD 160 million; the aim of which was to finance the development and modernization of transmission assets, fully guaranteed by the State Treasury. As at 31 December 2006 the liability amounted to PLN 198.1 million.
- Borrowing facility signed with a consortium of banks (with ING Bank N.V. London Branch acting as the agent) on 20 August 2002 in the amount of EUR 47.5 million and PLN 498.6 million; the aim of which was to refinance long term liabilities. The liability as at 31 December 2006 amounted to PLN 268.5 million.

The above mentioned liabilities were fully repaid during the financial year ended 31 December 2007 before the demerger was executed.

19. 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 Capital 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 Capital Group, loans granted to its employees and other social expenses.

The Capital Group entities compensated the Fund's assets with liabilities as the Fund's assets do not constitute the assets of the Capital Group. Due to the above, the balance of receivables and liabilities with the fund as at 31 December 2007 amounted to PLN 3,162.12 thousand. Liabilities due to the Fund as at 31 December 2006 amounted to PLN 4,016.58 thousand.

The table below presents the analysis of assets, liabilities and costs of the Fund

	As at 31 December 2007	As at 31 December 2006
Property, plant and equipment contributed to the fund	-	-
Loans granted to employees	100 676	101 260
Cash	48 946	33 432
Other Fund assets	1 033	20 116
Fund liabilities	(147 493)	(150 791)
Balance after compensation	3 162	4 017
Fund allowances in the reporting period	102 880	83 068

20. Earnings per share

Basic earnings per share shall be calculated by dividing profit or loss attributable to ordinary equity holders of the parent entity (the numerator) by the weighted average number of ordinary shares outstanding (the denominator) 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 weighed average number of shares outstanding during

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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 2007	Year ended 31 December 2006
Net profit on continuing operations	2 925 628	1 867 016
Net profit on discontinued operations	1 845 284	219 256
Net profit	4 770 912	2 086 272
Interest on redeemable convertible preference shares	-	-
Net profit attributable to ordinary equity holders used to calculate diluted earnings per share	4 770 912	2 086 272
Number of ordinary shares at the end of reporting period	14 705 765	397 452
Number of ordinary shares issued used to calculate basic earnings per share	14 705 765	14 705 765
Adjusted number of ordinary shares outstanding used to calculate diluted earnings per share	14 705 765	14 705 765

Earning per share for 2006 and 2007 was calculated on the basis of the number of shares as at 31 December 2007 as a result of the following:

- In the period covered by the consolidated financial statements, the PGE Group entities were under control of the State Treasury and as a result the creation of PGE Group is accounted for under the pooling of interest method.
- 2006 and 2007 financial results encompass the entire of financial results of PGE Group entities; therefore it is relevant to relate them to share capital of the parent company after the creation of the Group.

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21. Dividends paid and dividends declared

	Year ended 31 December 2007	Year ended 31 December 2006
Dividends from ordinary shares		
final dividends paid from the profit by subsidiaries	267	53 172
distribution of profit paid by parent company	141 264	288 881
dividend paid by subsidiaries*	632	47 215
Total dividends from ordinary shares	142 163	389 268
Dividends in kind		
dividend paid from retained earnings	8 918 460	-
dividend paid from reserve capital	709 837	-
dividend paid from other reserve capitals	-	345 152
Total dividends in kind	9 628 297	345 152
Total dividends	9 770 460	734 420

* As described in note 28 the creation of PGE Group was settled using the pooling of interest method, as a consequence in the financial statements included are financial data of subsidiaries for the period where they were indirectly dependant to the State Treasury and were therefore distributing the profit.

Restrictions to payment of dividends are described in note 35.7 of Supplementary information and explanations to the consolidated financial statements.

	Year ended 31 December 2007	Year ended 31 December 2006
Dividend per share paid by Capital Group entities (In PLN)	9,7	26,5

In order to calculate the value of dividend per share paid by Capital Group entities apart from period end dividend, all dividends from current profit to the State Treasury were included. However no dividends in kind were taken into account. Similarly as in calculation of profit per share described in note 20 of the financial statements, for both 2006 and 2007 the number of shares of parent entity as at 31 December 2007 was applied.

22. Property, plant and equipment

31 December 2007	Land	Buildings and construction	Machinery and equipment	Vehicles and other	Other	Construction in progress	Total
<i>Gross book value</i>							
Opening balance	183 972	18 468 705	19 960 500	225 778	438 402	1 777 188	41 054 545
Direct purchase	417	206 619	205 711	2 626	121 687	3 202 236	3 739 296
Transfer from construction in progress	6 197	1 062 126	1 057 202	36 822	17 761	(2 180 108)	-
Disposals	(6 079)	(5 759)	(11 302)	(4 521)	(187 147)	(2 533)	(217 341)
Transfer between groups	(1 031)	6 555	(5 364)	(54)	(94)	(12)	-
Donations and transfers free of charge	(394)	(12 148)	(3 411)	(253)	(943)	(542)	(17 691)
Liquidations	(78)	(58 734)	(138 611)	(942)	(1 572)	(469)	(200 406)
Other	(7 399)	15 985	17 830	(1 076)	47 947	(70 346)	2 941
Closing balance	175 605	19 683 349	21 082 555	258 380	436 041	2 725 414	44 361 344
<i>Accumulated depreciation (amortization)</i>							
Opening balance	8 616	1 632 729	3 699 634	51 512	166 995	4 327	5 563 813
Depreciation	2 840	1 026 244	1 473 987	32 229	41 739	-	2 577 039
Increase of impairment losses	384	35 621	20 284	-	109	2 275	58 673
Decrease of impairment losses	-	(1 817)	(2 087)	-	(9)	(250)	(4 163)
Disposals	(188)	(2 620)	(9 959)	(1 857)	(3 625)	-	(18 249)
Transfer between groups	-	2 016	(2 022)	-	6	-	-
Donations and transfers free of charge	(48)	(5 898)	(2 620)	(148)	(726)	-	(9 440)
Liquidations	-	(12 036)	(90 098)	(418)	(983)	-	(103 535)
Other	(14)	(328)	(14 167)	(426)	29 535	-	14 600
Closing balance	11 590	2 673 911	5 072 952	80 892	233 041	6 352	8 078 738
Opening balance net book value	175 356	16 835 976	16 260 866	174 266	271 407	1 772 861	35 490 732
Closing balance net book value	164 015	17 009 438	16 009 603	177 488	203 000	2 719 062	36 282 606

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31 December 2006	Land	Buildings and construction	Machinery and equipment	Vehicles and other	Other	Construction in progress	Total
<i>Gross book value</i>							
Opening balance	179 280	17 582 968	18 986 831	192 522	301 343	1 453 992	38 696 936
Direct purchase	1 250	111 054	71 172	847	169 352	2 182 130	2 535 805
Transfer from construction in progress	6 687	872 068	962 835	34 082	15 692	(1 891 364)	-
Disposals	(1 565)	(13 239)	(7 068)	(3 809)	(47 914)	(4 503)	(78 098)
Transfer between groups	-	(30)	(435)	109	356	-	-
Donations and transfers free of charge	(243)	4 363	133	2 956	842	-	8 051
Liquidations	(11)	(82 466)	(102 277)	(929)	(1 272)	(1 884)	(188 839)
Other	(1 426)	(6 013)	49 309	-	3	38 817	80 690
Closing balance	183 972	18 468 705	19 960 500	225 778	438 402	1 777 188	41 054 545
<i>Accumulated depreciation (amortization)</i>							
Opening balance	6 279	701 889	2 215 291	22 626	133 197	3 380	3 082 662
Depreciation	2 446	955 338	1 552 313	29 876	39 535	-	2 579 508
Increase of impairment losses	204	24 371	9 211	200	22	1 078	35 086
Decrease of impairment losses	-	(3 773)	(12)	-	-	(231)	(4 016)
Disposal	(59)	(5 273)	(7 032)	(827)	(4 694)	-	(17 885)
Transfer between groups	-	52	(344)	107	185	-	-
Donations and transfers free of charge	(15)	-	(1)	(14)	(4)	-	(34)
Liquidations	-	(42 551)	(63 920)	(457)	(1 203)	-	(108 131)
Other	(239)	2 676	(5 872)	1	(43)	100	(3 377)
Closing balance	8 616	1 632 729	3 699 634	51 512	166 995	4 327	5 563 813
Opening balance net book value	173 001	16 881 079	16 771 540	169 896	168 146	1 450 612	35 614 274
Closing balance net book value	175 356	16 835 976	16 260 866	174 266	271 407	1 772 861	35 490 732

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During the year ended 31 December 2007 the Capital Group companies included in the value of fixed assets and fixed assets under construction costs of external financing in the amount of PLN 34,339 thousand.

During the year ended 31 December 2006, the Group recognized an impairment loss on property, plant and equipment included in a cash generating unit of Zespół Elektrowni Wodnych Dychów S.A. in the amount of PLN 31 million.

During the year ended 31 December 2007, the Group recognized an impairment loss on property, plant and equipment included in a cash generating unit of Elektrownia Kielce S.A. in the value of PLN 51 million.

Test for impairment of property, plant and equipment of distributing companies

During the year ended 31 December 2007, significant changes took place in the economical environment of production companies operating in Poland. Main changes include:

- final settlement of issue related to long-term contracts (please refer to note 45 of supplementary information and explanatory notes for detailed information),
- acceptance of a binding proposition of National Emissions Trading Scheme (*Krajowy Plan Rozdziału Uprawnień*) on emission rights of carbon dioxide for the years 2008-2012 (KPRU II), in which the limitations granted to PGE Group entities are lower than those for the years 2005-2007,
- forecast on electricity prices that changed with regards to the above mentioned factors.

The above had a significant impact on the residual value of property, plant and equipment of production companies. As a result of the above, taking under consideration regulations of IAS 36 *Impairment of Assets*, the PGE 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 2007. 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 2008-2025. Impairment tests covered property, plant and equipment of total value of PLN 19 947 million as at 31 December 2007.

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

- BOT Kopalnia Węgla Brunatnego Bełchatów, BOT Elektrownia Bełchatów S.A., BOT Kopalnia Węgla Brunatnego Turów S.A. and BOT Elektrownia Turów S.A. were treated as one CGU due to technological and economic connections between these entities;
- The adopted assumptions on fluctuations of electricity prices in the years 2008-2025 take into account the influence of settlements in the system of covering stranded costs, as specified in the Act on covering costs related to earlier dissolution of long-term contracts on sales of electric power and energy, as well as costs of carbon dioxide emission rights' purchase (for more details please refer to note 45 Subsequent events). For the purpose of the impairment test, the Group assumed that the wholesale price of 1 MWh of electricity shall rise from PLN 151 in 2008 (including excise tax) to PLN 185 in 2012 (without excise tax) and PLN 244 in 2020;

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- Emission limits for years 2008-2012 for particular CGUs – in accordance with the project of “KPRU II” of 12 February 2008;
- The operations of Bełchatów and Turów Mining-Energetic Complexes shall end in 2036 and 2040, respectively i.e. in the years of estimated termination of lignite mines exploitation;
- Maintenance of production capacities resulting from reconstruction investments;
- Compensations received by entitled producers resulting from earlier termination of long-term contracts;
- In the projection period, the level of weighted average cost of capital (WACC) used for calculation ranges from 9,9% to 10,8% for the nominal after tax value, which relates to the range from 11,7% to 12,7% before tax.

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 impairment tests performed, it occurred that the income value of remaining CGUs, i.e. other than Elektrociepłownia Kielce, is higher than their carrying value.

The Management of the parent company assesses that, for purposes of this test as at the 31 December 2007, cautious assumptions were adopted regarding the main factor shaping the income value, i.e. electricity prices. Contracts concluded on the electricity market in Poland, after the termination of long-term contracts in 2008, indicate that wholesale prices of electricity are on a higher level than previously anticipated. Financial projections of Capital Group PGE are currently being actualized by the parent company. These include negative scenarios according to which the electricity prices will be on a higher level than used in impairment tests on property, plant and equipment. Due to the above and regarding the expected increase in electricity prices, the Group does not present sensitivity analysis of impairment test results for this parameter, assuming this scenario as unlikely.

Due to uncertainty existing on the financial markets and related changes in interest rates, the Group performed sensitivity analysis of results of impairment tests on property, plant and equipment for the assumed discount rate level. Results of this analysis, assuming the lack of changes of other factors, indicates that when the discount rate is decreased by 0.5 percentage point there is no need for additional impairment loss. Moreover an impairment allowance on property, plant and equipment of Elektrociepłownia Kielce S.A. would have to be lowered by PLN 10 million. If the discount rate is increased by 0.5 percentage point, an impairment loss on property, plant and equipment of Elektrociepłownia Kielce S.A. would have to be increased by PLN 10 million, and additional impairment write-off would have to be made on property, plant and equipment of Turów Mining-Energetics Complex in the amount of ca. PLN 250 million. The above analysis was performed under the assumption of stability of wholesale prices of electricity. The Management of the parent company assesses that an estimated increase of wholesale electricity prices in the following years shall balance a potential unfavorable impact of market interest rate increases.

Valuation estimate of property, plant and equipment in distributing companies

The recoverable amount of property, plant and equipment of eight distribution companies within the Capital Group depends on the tariff granted by the Energy Regulation Office. The key revenues driver of these companies is the so called regulatory value of assets calculated in

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order to recalculate the depreciation charge and return on equity in tariff calculation formulas. Tariffs for distribution companies within the PGE Group for the year 2008 were prepared with depreciation of revaluated assets and return on equity of historical book value of these assets.

Currently the electrical energy market in Poland is 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. The Group estimates that the total value of revaluated assets will be accepted in the tariff within 3 years. Taking this assumption into account, for fixed assets of total value as a 31 December 2007 of PLN 12 966 million, no risk of impairment occurs.

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23. Non-current assets classified as held for sale

Non-current assets classified as held for sale include the Holiday Resort in Niedzica (*Ośrodek Wczasowo-Wypoczynkowy*) classified as held for sale by a subsidiary - BOT Kopalnia Węgla Brunatnego Bełchatów S.A.

	Year ended 31 December 2007	Year ended 31 December 2006
Assets		
Intangible assets	-	-
Property, plant and equipment	3 147	2 361
Non-current assets classified as held for sale	3 147	2 361
Liabilities		
Loans and credits	-	-
Other liabilities	-	-
Liabilities directly related to non-current assets classified as held for sale	-	-
Net assets/liabilities classified as held for sale	3 147	2 361

24. Leases

24.1. Operating lease liabilities – the Group as a lessee

As at 31 December 2007 and as at 31 December 2006, the future minimum lease payments related to non-cancellable lease agreements are as follows:

	Liability as at	
	31 December 2007	31 December 2006
Less than 1 year	968	631
Between 1 and 5 years	207	75
More than 5 years	322	-
Total lease payments	1 497	706

Additionally the Capital Group companies bear the expense resulting from perpetual usufruct right to land. The amount of these expenses for the year ended 31 December 2007 amounted to around PLN 10 million (PLN 8,5 million for 2006).

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24.2. Operating lease receivables – the Group as a lessor

As at 31 December 2007 and as at 31 December 2006, the future minimum lease receivables related to non-cancellable operating lease agreements are as follows:

	Receivables as at		Income recognized in	
	31 December 2007	31 December 2006	2007	2006
Less than 1 year	966	926	267	258
Between 1 and 5 years	1 394	1 358	1 142	1 113
More than 5 years	-	-		
Total lease payments	2 360	2 284	1 409	1 371

The PGE Capital Group companies have signed agreements with PSE-Operator S.A. on rendering intervention services meaning disposing 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 2007 and as at 31 December 2006 the future minimum net lease payments related to these agreements and present value of minimum net lease payments are as follows:

	31 December 2007		31 December 2006	
	Minimum payments	Present value of payments	Minimum payments	Present value of payments
Less than 1 year	20 147	19 181	30 914	27 518
Between 1 and 5 years	3 242	2 983	21 990	21 470
More than 5 years	-	-		
Total minimum lease payments	23 389	22 164	52 904	48 988
Less financial expenses	(1 225)	-	(3 916)	-
Present value of minimum lease payments, including:	22 164	22 164	48 988	48 988
Short-term	19 181	19 181	27 518	27 518
Long-term	2 983	2 983	21 470	21 470

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

	31 December 2007		31 December 2006	
	Minimum payments	Present value of payments	Minimum payments	Present value of payments
Less than 1 year	337	217	387	267
Between 1 and 5 years	563	411	982	628
More than 5 years	-	-	-	-
Total minimum lease payments	900	628	1 369	895
Less financial expenses	(272)	-	(474)	-
Present value of minimum lease payments, including:	628	628	895	895
Short-term	217	217	267	267
Long-term	411	411	628	628

25. Investment property

	31 December 2007	31 December 2006
Opening balance as at 1 January	21 411	21 825
Increase of value	1 554	366
Depreciation	734	780
Decrease of value	6 298	-
Closing balance as at 31 December	15 933	21 411

Investment property in Capital Group companies cover 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.

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26. Intangible assets

31 December 2007	Development costs	Goodwill	Licenses and patents			Intangible assets under construction	Total
			Total	incl. computer software	Other		
Gross book value							
Opening balance	9 071	-	179 214	135 730	110 400	14 162	312 847
Direct purchase	-	-	13 438	8 401	8 503	14 066	36 007
Transfer from intangible assets under construction	-	-	10 173	8 816	2 539	(12 712)	-
Disposals	-	-	(147)	(34)	(20)	-	(167)
Transfer between groups	-	-	(314)	-	591	(277)	-
Donations and transfers free of charge	-	-	(170)	-	103	-	(67)
Liquidations	-	-	(5 720)	(5 714)	(795)	-	(6 515)
Acquired/obtained due to demerger of an electricity generating entity	-	-	(350)	119	(38)	388	-
Other	1 744	-	79	4	(4 946)	(454)	(3 577)
Closing balance	10 815	-	196 203	147 322	116 337	15 173	338 528
Amortization							
Opening balance	6 255	-	94 294	87 728	61 974	-	162 523
Amortization	1 467	-	29 725	21 251	12 255	-	43 447
Disposal	-	-	(63)	(9)	12	-	(51)
Transfers between groups	-	-	(8)	-	8	-	-
Donations and transfers free of charge	-	-	(70)	-	-	-	(70)
Liquidation	-	-	(5 090)	(5 084)	(383)	-	(5 473)
Acquired/obtained due to demerger of electricity generating entity	-	-	1 227	533	(1 227)	-	-
Other	-	-	(110)	(110)	(328)	-	(438)
Closing balance	7 722	-	119 905	104 309	72 311	-	199 938
Net book value							
Opening balance	2 816	-	84 920	48 002	48 426	14 162	150 324
Closing balance	3 093	-	76 298	43 013	44 026	15 173	138 590

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31 December 2006	Development costs	Goodwill	Licenses and patents			Intangible assets under construction	Total
			Total	incl. computer software	Other		
<u>Gross book value</u>							
Opening balance	8 112	-	161 027	126 615	188 119	11 226	368 484
Direct purchase	173	-	15 048	9 441	11 988	16 780	43 989
Transfer from intangible assets under construction	786	-	8 767	5 239	4 907	(14 460)	-
Disposals	-	-	(3)	(3)	-	-	(3)
Donations and transfers free of charge	-	-	-	-	23	-	23
Liquidations	-	-	(5 857)	(5 776)	(94 637)	-	(100 494)
Other	-	-	232	214	-	616	848
Closing balance	9 071	-	179 214	135 730	110 400	14 162	312 847
<u>Amortization</u>							
Opening balance	5 268	-	69 897	69 888	146 305	-	221 470
Amortization	987	-	27 366	20 809	9 490	-	37 843
Liquidation	-	-	(3 433)	(3 414)	(94 555)	-	(97 988)
Other	-	-	464	445	734	-	1 198
Closing balance	6 255	-	94 294	87 728	61 974	-	162 523
<u>Net book value</u>							
Opening balance	2 844	-	91 130	56 727	41 814	11 226	147 014
Closing balance	2 816	-	84 920	48 002	48 426	14 162	150 324

27. Investment in associates accounted for using the equity method

The table below presents information on investments in associates accounted for using the equity method.

	Polkomtel	PEC Bogatynia	Atex	Swe-Pol Link	TOTAL
Share in voting rights	17,56%	24,44%	43,83%	33,00%	
Core operations	Telecommunication services	Transmission, distribution and turnover of heat	Control and monitoring systems	Transmission of electricity	
Year ended 31 December 2007					
Share of balance sheet in associate:					
Current assets (short-term)	244 689	1 211	8 237	5 616	259 753
Non-current assets (long-term)	1 239 724	9 600	5 627	209 161	1 464 112
Short-term liabilities	(663 133)	(786)	(721)	(17 951)	(682 591)
Long-term liabilities	(205 461)	(28)	(438)	(185 232)	(391 159)
Share of net assets	615 819	9 997	12 705	11 594	650 115
Goodwill	25 252			50 715	75 967
Shares in associate presented in the balance sheet	641 071	9 997	12 705	62 309	726 082
Share of revenue of the associate	1 369 508	4 399	6 317	33 371	1 413 595
Share of profit/ (loss) of the associate	238 655	(262)	1 073	(310)	239 156
Year ended 31 December 2006					
Share of balance sheet in associate:					
Current assets (short-term)	191 895	1 516	7 524	6 826	207 761
Non-current assets (long-term)	1 155 363	9 607	4 849	225 607	1 395 427
Short-term liabilities	(505 065)	(844)	(561)	(20 471)	(526 941)
Long-term liabilities	(228 343)	(20)	(180)	(198 738)	(427 283)
Share of net assets	613 850	10 259	11 632	13 224	648 965
Goodwill	25 252			50 715	75 967
Shares in associate presented in the balance sheet	639 102	10 259	11 632	63 939	724 932
Share of revenue of the associate	1 292 243	4 667	6 141	32 354	1 335 405
Share of profit/ (loss) of the associate	197 344	64	1 033	(484)	197 957

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PGE Polska Grupa Energetyczna S.A. owns a 17,56% share of equity of Polkomtel S.A. Nevertheless, the parent company participates in supervisory bodies as well as in the process of decision making, therefore it has a significant influence over Polkomtel S.A., which, as a result, is considered as an associate accounted for using the equity method.

28. Business combinations

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.),
- BOT Capital Group (including: BOT Górnictwo i Energetyka 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 electricity generating entities: 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 distribution entities 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.

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, and were under control of the State Treasury together with the 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.

In the absence of a Standard or an Interpretation that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying 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 under common control are preferred to be accounted for using the pooling of interest method.

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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 under business combination were aggregated starting 1 January 2006, i.e. a transition date to IFRS for all consolidated entities. Income statement and cash flows for both years presented in the IFRS consolidated financial statements encompass all Group operations. Contribution of shares of subsidiaries to the share capital of the Parent company on 9 May 2007 was presented in the statement of changes in a consolidated equity as an increase of share capital from the Capital Group retained earnings.

Furthermore, on 27 February 2007, the Group acquired 85% of Zespół Elektrociepłowni Bydgoszcz S.A. from the State Treasury. This transaction also fulfils the definition of a business combination under common control and, as a result, was accounted for using the pooling of interest method. Zespół Elektrociepłowni Bydgoszcz S.A. was included in the consolidated financial statements since the first applicable period, i.e. 1 January 2006. The cost of acquisition of this company was presented in the statement of changes in consolidated equity as a decrease in retained earnings of the Capital Group.

29. Investments in jointly controlled entities

During financial years ended 31 December 2007 and 31 December 2006 the Group did not participate in any jointly controlled entity.

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30. Carbon dioxide emission rights

The below table comprises a summary of changes in volume (in tons) and book value of emission rights owned by the Group in the years 2005-2007:

	2005 Number	2006 Number	2007 Number	Total Number
Emission rights granted by National Emissions Trading Scheme	61 652 700	61 652 700	61 652 700	184 958 100
Emission rights bought on a secondary market	-	-	-	-
Total	61 652 700	61 652 700	61 652 700	184 958 100
Used for own purposes	59 628 657	59 764 396	57 753 819	176 966 872
Sold	321 909	782 870	4 830 262	5 935 041
Rights unused (+)/ missing (-)	(+) 1 702 134	(+) 1 105 434	(-) 751 381	(+) 2 056 187

Due to the fact that there were no shortages of emission rights in the first reporting period, the Group entities did not create any relevant provisions.

Emission right obtained within the National Plan of Emissions System for the years 2008 – 2012 are presented in note 45 of the consolidated financial statements: Subsequent events.

31. Employment benefits

31.1. Employee shares programme

The employee shares programme is described in note 35.4.

31.2. Retirement benefits and other post-employment benefits

Retirement and pension allowances

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. Due to the above, an entity creates a provision for retirement and pension allowance 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.

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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 2007

	Retirement, pension and other benefits provisions	Coal allowance	Energy tariff	Social Fund	Medical benefits	Other post- employment provisions	Total
As at 1 January 2007	216 591	124 445	232 444	100 785	31 268	226	705 759
Purchase of a subsidiary	-	-	-	-	-	-	-
Present employment costs	12 583	1 593	12 075	2 943	726	96	30 016
Actuarial gains and losses	41 718	(3 582)	(32 229)	35 811	5 181	-	46 899
Benefits paid	(21 301)	(6 032)	(18 284)	(9 815)	(1 009)	(18)	(56 459)
Past employment costs	-	-	13 021	-	-	-	13 021
Transferred/ obtained due to demerger	-	-	-	-	-	-	-
Discount rate adjustments	366	-	-	90	-	-	456
Interest costs	10 568	6 111	18 680	6 219	1 507	-	43 085
Other	1 131	-	2 578	(2 990)	612	-	1 331
As at 31 December 2007	261 656	122 535	228 285	133 043	38 285	304	784 108
Short-term	46 694	7 612	15 623	7 039	1 874	100	78 942
Long-term	214 962	114 923	212 662	126 004	36 411	204	705 166

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Year ended 31 December 2006

	Provisions for retirement, pension and other benefits	Coal allowance	Energy tariff	Social Fund	Medical benefits	Other post-employment provisions	Total
As at 1 January 2006	191 610	119 724	188 276	78 099	31 465	140	609 314
Purchase of a subsidiary	-	-	-	-	-	-	-
Present employment costs	10 106	1 600	9 363	2 131	834	97	24 131
Actuarial gains and losses	16 686	2 997	2 578	19 747	(1 754)	-	40 254
Benefits paid	(11 053)	(5 758)	(10 708)	(3 016)	(788)	(11)	(31 334)
Past employment costs	-	-	8 340	-	-	-	8 340
Transferred/ obtained due to demerger							
Discount rate adjustments	473	-	-	83	-	-	556
Interest costs	8 620	5 882	14 669	3 623	1 522	-	34 316
Other	149	-	19 926	118	(11)	-	20 182
As at 31 December 2006	216 591	124 445	232 444	100 785	31 268	226	705 759
Short-term	29 466	6 621	12 978	4 673	1 303	5	55 046
Long-term	187 125	117 824	219 466	96 112	29 965	221	650 713

Major actuarial assumptions as at the balance sheet date are as follows:

	31 December 2007	31 December 2006
Discount rate (%)	6,0	5,0
Expected inflation rate (%)	2,5	2,5
Employee turnover (%)	0,68 - 8,2	1,01 - 8,2
Expected salary growth rate (%)	2,5 - 8,5	0,05 - 8,8
Expected medical costs growth rate (%)	2,8 - 3,4	2,8 - 3,4
Expected Social Fund (ZFŚS) allowance rate (%)	2,8 - 3,4	2,8 - 3,4

32. Inventories

	31 December 2007			31 December 2006		
	Historical cost	Impairment allowance	Net realizable value	Historical cost	Impairment allowance	Net realizable value
Materials	681 578	99 664	581 914	687 339	98 699	588 640
Finished goods	7 719	-	7 719	808	5	803
Semi-products and work in progress	57 884	50	57 834	57 692	87	57 605
Energy origin units of ownership	145 635	152	145 483	95 792	-	95 792
Merchandise	6 838	871	5 967	5 159	857	4 302
Total	899 654	100 737	798 917	846 790	99 648	747 142

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Impairment allowance on inventories as at 31 December 2006	99 648
Creation of impairment allowances	15 172
Transferred/ obtained due to demerger of electricity generating entity	-
Reversal of impairment allowances	(5 464)
Utilization of impairment allowances	(8 622)
Other	3
Impairment allowance on inventories as at 31 December 2007	100 737

Creation of the above impairment allowances related mainly to spare parts and materials as a result of their amortization or obsolescence. Reversal of impairment allowances, mainly on spare parts and materials, resulted from their disposal or usage to the value exceeding the above mentioned carrying amount.

33. Other short-term and long-term assets

Other long-term assets

	Year ended 31 December 2007	Year ended 31 December 2006
Prepayments for transmission services	5 424	1 247
Prepayments for construction in progress	249 796	310 826
Other prepayments	140 197	76 060
Total other long-term financial assets	395 417	388 133

Other short-term assets

	Year ended 31 December 2007	Year ended 31 December 2006
Subscription	650	540
Property and tort insurances	21 774	24 073
Reservation of power	14	8 531
Membership fees, trainings	257	215
IT services	2 273	1 053
Prepayments for deliveries	972	994
Information services	447	10
Other costs settled in time	10 480	7 663
Advance on deliveries	16 329	6 782
VAT receivable	90 373	84 441
Excise tax receivable	26 436	72 484
Deductions from profit receivable	14 797	18 556
Other tax receivables	18 074	101 230
Other short-term assets	23 686	16 617
Total other short-term financial assets	226 562	343 189

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34. Cash and cash equivalents

Cash at the bank is subject to variable interest rates which are based on one-day 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 2007 amounted to PLN 2,726,378 thousand (31 December 2006: PLN 3,310,154 thousand)

Restricted cash is related to the Mine Liquidation Trust in the value of PLN 51,299 thousand as at 31 December 2007 and PLN 39,567 thousand as at 31 December 2006.

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

	Year ended 31 December 2007	Year ended 31 December 2006
Cash on hand and cash at bank	1 020 834	628 341
Short-term deposits	1 705 621	2 681 574
Resulting from foreign exchange differences	(77)	239
Total	2 726 378	3 310 154
Cash and cash equivalents presented in cash flow statement	2 723 507	3 312 507
Unutilized credit limits	1 242 333	1 101 880

The difference between the value of cash and cash equivalents presented in the balance sheet and the one presented in cash flow statements results mainly from interests accrued for but not paid as at balance sheet date as well as foreign exchange differences from cash and cash equivalents.

35. 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. The Group can issue new shares to keep or correct the capital structure which is monitored by means of the debt ratio and return on capital ratio.

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35.1. Share capital

Share capital

	As at 31 December 2007	As at 31 December 2006
Number of registered preference A series shares of nominal value PLN 1000 each	51 500	51 500
Number of registered preference B series shares of nominal value PLN 1000 each	158 500	158 500
Number of registered preference C series shares of nominal value PLN 1000 each	119 968	119 968
Number of registered preference D series shares of nominal value PLN 1000 each	67 484	67 484
Number of ordinary E series shares of nominal value PLN 1000 each	14 308 313	-
Total number of shares	14 705 765	397 452

On 9 May 2007, an increase of share capital took place related to contribution of shares of PGE Energia S.A. and BOT Górnictwo i Energetyka S.A. to the Company:

- 6,391,456,984 (six billion three hundred and ninety one million four hundred fifty six thousand and nine hundred eighty four) shares owned by the State Treasury in PGE Energia S.A. with its seat in Warsaw, of B series from the no. B 000000000001 to no. B 006391456984 of nominal value PLN 1 (one) each and total market value of PLN 6 391 413 thousand,
- 325,363,824 (three hundred twenty five million three hundred sixty three thousand eight hundred twenty four) of shares owned by the State Treasury in BOT Górnictwo I Energetyka S.A. with its seat in Łódź, of B series from the no. B 000000001 to no. B 325363824 of nominal value of PLN 10 (ten) each and of total market value of PLN 7,916,900 thousand.

The total value of non-monetary contributions amounted to PLN 14,308,313 thousand. The value of a non-monetary contributions was measured using the valuation made by independent external experts with the use of the discounted cash flows method as at 31 December 2006 (for PGE Energia S.A.) and as at 30 June 2006 (for BOT Górnictwo I Energetyka S.A.).

The value of the non-monetary contribution allowed issuing of 14,308,313 new E series share with a nominal value PLN 1,000 each.

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	<i>Number</i>	<i>Value (in PLN)</i>
As at 1 January 2006	397 452	397 452 000
Issued in exchange for cash due to realization of share options	-	-
As at 31 December 2006	397 452	397 452 000
As at 1 January 2007	397 452	397 452 000
Shares issued in 2007	14 308 313	14 308 313 000
As at 31 December 2007	14 705 765	14 705 765 000

35.2. Share capital of subsidiaries to increase the share capital of PGE

As at 1 January 2006 BOT Górnictwo i Energetyka S.A., Zespół Elektrowni Dolna Odra S.A. and 8 electricity generating entities were 100% owned by the State Treasury.

As described in note 28 to the consolidated financial statements, on 29 December 2006, 85% of shares of the electricity generating entities and Zespół Elektrowni Dolna Odra S.A. were contributed to PGE Polska Grupa Energetyczna S.A. to increase its share capital. Subsequently, on 9 May 2007, shares of PGE Energia S.A. and BOT Górnictwo i Energetyka S.A. were contributed to PGE Polska Grupa Energetyczna S.A. (then under the business name Polskie Sieci Elektroenergetyczne S.A.). However, as described in note 28 to the consolidated financial statements, as the creation of the PGE Group is assessed to be a restructuring under common control, it was accounted for using the pooling of interest method. Due to the above, assets, liabilities and equity of all of the entities contributed to PGE on 9 May 2007 are presented in the consolidated financial statements since the first presented period, i.e. 1 January 2006.

In the consolidated equity, both as at 1 January 2006 and 31 December 2006, there is a position "Share capital of subsidiaries to increase the share capital of PGE" which amounts to PLN 14,308,313 thousand. This amount corresponds with the value of share capitals which as a result of the restructuring in 2007 became the share capital of the parent company.

35.3. Nominal value of shares

All issued shares have their nominal value amounting to PLN 1,000 and were fully paid.

35.4. Equity holders' rights

State Treasury rights

The Golden Share Act regulates special rights of the State Treasury and their execution in capital companies of significant importance for the public order or public safety. PGE, BOT GiE and Exatel are the companies of significant importance for the public order or public safety and are subject to Golden Share Act regulations. Special rights executed on the basis of Golden Share Act relate to: (i) right to express objection towards specified actions or resolutions passed by companies' bodies, and (ii) right to appoint one or two observers in a company.

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As long as the State Treasury is directly or indirectly stockholder (shareholder) in a company, State Treasury Minister who represents the State Treasury has the right to object to any resolution or legal action taken by the company's Board of Directors that relates to the ability to dispose a part of company's property that is fundamental for its activities. Moreover State Treasury Minister has the right to object to any resolution of the Shareholders Meeting relating to: (i) liquidation of a company, (ii) movement of a company's office abroad, (iii) change of a core competence of a company, (iv) sale or lease of a company or its organized part or establishment of limited law property. State Treasury Minister can also oppose in case of: (i) the change of activity actually performed by a company, (ii) resolution taken by a company's bodies that results in change of destination or abandonment of use of a basic component of company's property. Objection can also be raised if there is justified suspicion that resolution (activity) of a company's bodies violates public order or public safety.

The objection is raised in the form of administrative decision against which an action can be brought in accordance with administrative proceedings principles. The objection can be reported within 14 days with effect from a day of receiving by observer (please compare with explanations below) the information that actions were performed, yet the company is obligated to inform observer about actions performed within maximum three days. Legal act (resolution) comes into force after the deadline for raising objection passed, or if the objection was reported before that date, after its abatement, acknowledgement of invalidity or change of State Treasury Minister decision as a result of administrative proceeding. Whereas the final State Treasury Minister decision on objection results in invalidity of legal act since it was performed. Moreover, the legal act is invalid if State Treasury Minister was not informed about it on time.

There can be one or two observers appointed by an appropriate minister in a company, for which the Golden Share Act is applicable. Observer has a right to demand from company's bodies any information and explanations relating to issues, to which objections can be reported.

Till the day of this consolidated financial statement there were no observers appointed in PGE, GiE nor Exatel in accordance with the Golden Share Act.

Employee shares programme

Under regulations of the Commercialization and Privatization Act of 30 June 1996, if a current or a former employee was employed in an entity at the date of the entity's cancellation from the register of state-owned enterprises under commercialization, he/she is entitled to receive shares of this enterprise.

According to IFRIC 8, IFRS 2 *Share-based payments* is applicable for transactions in which the entity exchanges its equity instruments for unidentifiable goods and services. Due to the above, granting employee shares was presented in the consolidated financial statement in accordance with IFRS 2.

For the purpose of settlement of employee shares' costs, the start of work by the employees in return for the rights is the date of commercialization of the company and the vesting and grant date is the date of final publication of lists, including the number of shares granted to employees of a given entity. Due to the above, the cost of granted shares recognized in the

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consolidated financial statements is related to current and former employees of the following entities:

- Elektrociepłownia Gorzów S.A.
- Zakład Energetyczny Białystok S.A.
- Zakład Energetyczny Warszawa-Teren S.A.
- Zamojska Korporacja Energetyczna S.A.
- Lubelskie Zakłady Energetyczne S.A.
- Rzeszowskie Zakłady Energetyczne S.A.
- Zakłady Energetyczne Okręgu Radomsko-Kieleckiego S.A.
- Łódzki Zakład Energetyczny S.A.
- Zakład Energetyczny Łódź-Teren S.A.
- Zespół Elektrowni Dolna Odra S.A.
- Zespół Elektrociepłowni Bydgoszcz S.A.

Employees of other PGE Group entities were not entitled to receive shares or the granting of shares took place before 1 January 2006 and therefore was settled before the first period presented in the consolidated financial statements.

Valuation of the programme during the presented reporting periods was as follows:

	Minority interests	Equity holders of the parent	Total
Valuation as at 1 January 2006	335 173	899 794	1 234 967
Costs incurred in 2006	29 983	79 522	109 505
Employees' vest	(2 309)	(15 790)	(18 100)
Valuation as at 31 December 2006	362 847	963 526	1 326 372
Costs incurred in 2007	490	1 354	1 844
Measurement as at end date in 2007	363 337	964 880	1 328 216
Employees' vest	(363 337)	(964 880)	(1 328 216)
As at 31 December 2007	-	-	-

Part of the employee shares programme attributable to equity holders of the parent is reflected in share capital as "Capital for granting shares to the employees". Cost of vesting for the periods before 1 January 2006 was recognized in retained earnings as at this date. Cost of vesting for the years 2006 and 2007 was recognized in costs of employee benefits in relevant periods.

Except for the above mentioned employee shares programme based on the Commercialization and Privatization Act, there are no other employee shares programmes in the Group.

35.5. Equity holders of significant share

	As at 31 December 2007	As at 31 December 2006
State Treasury		
share in equity	100%	100%
Voting shares	100%	100%

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35.6. Reserve capital

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.

35.7. Retained earnings and limitations to payment of a dividend

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

	31 December 2007	31 December 2006
Amounts included in retained earnings that cannot be distributed by the parent:		
- retained earnings of subsidiaries, attributable to equity holders of the parent	3 179 441	694 678
- differences in the value of retained earnings as presented in accordance with PAS and IFRS of the parent company	369 254	8 588 326
- 8% value of distribution to reserve capital as specified in the Commercial Code	66 106	-
Retained earnings of the parent, subject to distribution	778 874	1 659 085
Total retained earnings presented in the consolidated financial statements attributable to equity holders of the parent	4 393 675	10 942 089

Statutory financial statements of all 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, 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 share capital. 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 2007, the value of share capital of the parent company presented in statutory financial statements prepared in accordance with the Polish Accounting Act amounted to PLN 14,705,765 thousand and reserve capital amounted to PLN 1,945,841 thousand. As at 31 December 2006 the value of share capital of the parent company presented in statutory financial statements prepared in accordance with the Polish Accounting Act amounted to PLN 397,452 thousand and reserve capital amounted to PLN 202,312 thousand.

As at 31 December 2007 there were no limitations to payment of a dividend.

A dividend policy assumption is that in the nearest future less than 50% of the net profit would be devoted to dividends for shareholders. It would depend on the financial leverage, the level of planned investment expenditures, dividends from subsidiaries and potential capital acquisitions. In the long term, after the Group restructuring, the Company intends to adjust the level of dividend payments to industry standards.

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35.8. Minority interests

	Year ended 31 December 2007	Year ended 31 December 2006
Opening balance	7 414 617	7 068 291
Dividends paid by subsidiaries, incl. distribution of profit to State		
Treasury	(49 963)	(48 966)
Share in change in value of financial instruments	(139)	1 673
Capital Group Employees' vesting	490	29 983
Share in profit of subsidiaries	803 030	363 637
Closing balance	8 168 035	7 414 617

As described in note 28 to the consolidated financial statements, the creation of PGE Capital Group was accounted for using the pooling of interests method. Due to the above, the minority interests were calculated as if the PGE Capital Group had existed in the present structure since 1 January 2006.

36. Provisions

36.1. Changes in provisions

Year ended 31 December 2007

	Post- employment benefits (note 31.2)	Provisions for jubilee benefits	Provisions from third parties claims	Provisions for legal disputes	Provisions for employee claims	Provisions for recultivation of final excavations	Provisions for liquidation of property, plant and equipment	Other provisions	TOTAL
As at 1 January 2007	705 759	604 170	2 020	99 207	12 972	1 501 203	44 582	66 504	3 036 417
Acquisition of a subsidiary	-	-	-	-	-	-	-	-	-
Costs of present employment	30 016	32 132	-	-	-	-	-	-	62 148
Actuarial gains and losses	46 899	28 777	-	-	-	-	-	-	75 676
Benefits paid	(56 459)	(56 886)	(19)	(1 593)	-	-	-	-	(114 957)
Costs of past employment	13 021	(293)	-	-	-	-	-	-	12 728
Recalculation of provision value	456	1 213	-	-	-	(233 814)	-	-	(232 145)
Interest costs	43 085	28 320	-	-	-	75 148	2 447	-	149 000
Created during the period	-	7 519	34	131 610	11 225	88 229	39 730	45 097	323 443
Reversed	-	(7 102)	(2 344)	(53 338)	(10 868)	-	(30)	(13 273)	(86 955)
Utilized	-	-	(567)	(8 174)	(5 177)	-	(4 851)	(35 621)	(54 390)
Other changes	1 331	(654)	1 974	19 804	(40)	-	-	(12 820)	9 595
As at 31 December 2007	784 108	637 196	1 098	187 515	8 112	1 430 766	81 878	49 887	3 180 560
Short-term as at 31 December 2007	78 942	69 035	809	173 572	4 398	874	4 572	41 087	373 289
Long-term as at 31 December 2007	705 166	568 161	289	13 943	3 714	1 429 892	77 306	8 880	2 807 271

According to the current recultivation of final excavation plans, lignite mines of the Capital Group estimate that costs will be borne in the years 2032-2082 (for BOT Kopalnia Węgla Brunatnego Bełchatów S.A.) and in the years 2041-2090 (for BOT Kopalnia Węgla Brunatnego Turów S.A.).

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Year ended 31 December 2006

	Post-employment benefits (note 31.2)	Provisions for jubilee benefits	Provisions for contraheant claims	Provisions for legal disputes	Provisions for employee claims	Provisions for recultivation of final excavations	Provisions for liquidation of property, plant and equipment	Other provisions	TOTAL
As at 1 January 2006	609 314	572 589	2 020	63 753	13 188	1 588 037	51 019	71 815	2 971 735
Acquisition of a subsidiary	-	-	-	-	-	-	-	-	-
Costs of present employment	24 131	26 806	-	-	-	-	-	-	50 937
Actuarial gains and losses	40 254	30 151	-	-	-	-	-	-	70 405
Benefits paid	(31 334)	(53 570)	-	-	(52)	-	-	-	(84 956)
Costs of past employment	8 340	-	-	-	-	-	-	-	8 340
Discount rate adjustments	556	913	-	-	-	-	-	-	1 469
Interest costs	34 316	24 210	-	-	-	68 277	1 184	-	127 987
Provisions created during the period	-	8 218	-	40 624	4 579	54 388	1 017	33 488	142 316
Reversed	-	(5 141)	-	(4 594)	(4 542)	(209 500)	-	(10 323)	(234 100)
Utilized	-	-	-	(692)	(6)	-	(8 638)	(38 439)	(47 775)
Other changes	20 181	(6)	-	116	(195)	-	-	9 963	30 059
As at 31 December 2006	705 759	604 170	2 020	99 207	12 972	1 501 203	44 582	66 504	3 036 417
Short-term as at 31 December 2006	55 046	58 295	40	88 347	9 534	-	2 077	61 798	275 137
Long-term as at 31 December 2006	650 713	545 875	1 980	10 860	3 438	1 501 203	42 505	4 706	2 761 280

36.2. Description of other provisions

Provisions for recultivation

According to regulations of the Act of 3 February 1995 on Agricultural and Forest grounds and regulations of the Act of 4 February 1995 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.

BOT KWB Bełchatów S.A. and BOT KWB Turów S.A. 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 in the period divided by the rate of coal excavation, less period-end value of Mine Liquidation Trust created in accordance with Geological and Mining Law.

According to the Act of 27 April 2001 on Environment protection law and the permission based on the Act, when the exploitation is finished, an entity is obliged to liquidate the installations and recultivate the ground of the plant. As a result, the Group is obliged to incur the above costs in the future, and therefore creates a provision for recultivation of ash storages.

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.

PKN Orlen S.A. claim

In 2005, the Court of Arbitration concluded a verdict favorable for PGE S.A. related to the complaint of PKN Orlen S.A. for the repayment of liabilities with interest (resulting from a concluded agreement on the sale of NOM S.A. shares by PKN Orlen S.A. for PLN 115 million). Then, PKN Orlen filed a claim at the Court of Arbitration against PGE S.A. to pay a contractual penalty of PLN 33,453 thousand (i.e. 30% of the contractual penalty for not fulfilling the provisions of the agreement). In 2007 the claim was expanded and as a result PKN Orlen demanded a total amount of contractual penalty in the amount of PLN 111,511 thousand. On 7 April 2008, the Company received the verdict of the Court of Arbitration at the Polish Chamber of Commerce, awarding PKN Orlen S.A. with the total amount of PLN 107 660 thousand. The provision for the above amount was recognized in the consolidated financial statements as at 31 December 2007.

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37. Deferred income and government grants

Government grants

Position	As at 31 December 2007	As at 31 December 2006
Redemption of loans from environmental funds	27 699	30 060
Other government grants	26 117	18 792
Total deferred income, including:	53 816	48 852
Long-term	50 160	44 886
Short-term	3 656	3 966

Other deferred income

Position	As at 31 December 2007	As at 31 December 2006
Settlement of investment relief	83	83
Property, plant and equipment acquired free of charge	136 565	116 028
Subsidies granted	682 383	587 748
Property, plant and equipment donated	11 875	29 184
Lease income	2 527	3 533
Other income settlements	42 881	71 689
Total deferred income, including:	876 314	808 265
Long-term	851 581	757 539
Short-term	24 733	50 726

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.

Other subsidies in the line of other deferred incomes comprise mainly of connection fees settled over time, which Group entities present as a donation to property, plant and equipment.

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38. Legal claims and other contingent liabilities

	31 December 2007	31 December 2006
Credit collateral	250	250
Call options for shares	94 257	104 884
Repayment of bill collateral	310 676	113 472
Collaterals for credits granted to third parties	11 564	30 260
Collaterals for repayment of bank guarantees granted	-	15 017
Legal claims	3 760	10 332
Contractual fines and penalties	-	33 453
Employees claims	-	178
Penalties resulting from using the land which does not belong to the Group	-	3 861
Real estate property buyout	-	3 738
Other contingent liabilities	50 769	25 196
Contingent liabilities in total	471 276	340 641

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

PGE Polska Grupa Energetyczna S.A. - Options for shares.

On 28 May 2003 PGE S.A. signed a Restructuring Agreement with Vattenfall Aktiebolag regarding Swe-Pol Link. According to point 8.2 of the Restructuring Agreement, until 30 September 2004 Vattenfall Aktiebolag had an irrevocable and unconditional right to require PGE to buy shares representing 32% of voting rights in Swe-Pol Link for the price settled in Annex 3. The first option was executed on 5 January 2005. The second option will grant an irrevocable right for Vattenfall Aktiebolag to sell shares constituting 16% or 17% of voting rights to PGE S.A.

PGE Polska Grupa Energetyczna S.A. - Tri-lateral claim PGE – Atel – PSE-Operator S.A.

The contingent liability refers to a potential claim of Atel towards PGE S.A. in connection to limitation of exports performed by PSE-Operator S.A. due to a heat-wave in July 2006. On 22 August 2006 Aare Tessin Ltd for Electricity ("Atel") presented its initial claim towards the Company. The claims resulted from losses that were incurred by Atel as a result of reductions performed by the Company to supplies of energy agreed in long-term and short-term contracts for supplies of energy. The reductions performed by the Company were a consequence of reductions in cross-border exchange in electrical power transmission allocated for execution of the above mentioned contracts performed by the Transmission System Operator – PSE-Operator S.A. company. The described situation took place in July 2006 and was connected to the high temperatures noted at that time in Poland.

The company is currently holding talks with Atel in order to assess the reasons for the situation and its legal status as well as to assess whether the subject claims may be settled by conciliation. It is possible that the Company will require a compensation of amounts to be eventually paid to Atel from PSE-Operator S.A. On the other hand Atel did not reply to the Company's request for proof in the form of contracts, invoices or bills proving actual amount of losses. The claims remain therefore a written form of differences between the value of

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contract and the cost of energy bought from alternative sources. The Company is unable to fairly and reliably assess the value of the potential claim.

On 11 September 2007 PSE-Operator S.A. commenced proceedings at the conciliation court against the Company in relation to the agreement allowing access to transmission capacities for execution of historical contracts signed by PSE S.A. on 2 July 2004. PSE-Operator S.A. filed a claim on 18 January 2008. In the claim PSE-Operator S.A. states that there is no liability resulting from the above mentioned agreement signed on 2 July 2004 resulting in PSE-Operator S.A. being responsible for allowing access to transmission capacities in respect of the Atel contract. Moreover PSE-Operator S.A. applied for a decision stating that the agreement dated 2 July 2004 expired. Alternatively, PSE-Operator S.A. filed for dissolution of the agreement. The Company filed a counter-claim presenting lack of legal basis for agreement termination and refusal of rendering of reservation of transmission capacities and transmission services. The parent company is unable to fairly and reliably assess the value of the potential claim.

Furthermore, due to the fact that PSE-Operator S.A. ceased to execute the contract on allowing access to transmission capacities, Atel filed a claim against the Company. For the Company to be able to deliver energy to Atel, it has to have access to transmission capacities on the Poland-Slovakia cross-border energy connection. Lack of execution of the agreement dated 2 July 2004 by PSE-Operator S.A. may result in lack of execution or improper execution of the contract between the Company and Atel and as a consequence may lead to claims from Atel against the Company. Currently, in order to keep the possibility to execute the contract with Atel, from the beginning of 2008 Atel purchases transmission capacities on the Poland-Slovakia cross-border energy connection in auctions. Atel requires a reimbursement of costs incurred. The amount of these costs is not set as the transmission capacities are purchased at monthly auctions and their price changes over time. Currently the contract realization is impossible due to the fact of PSE-Operator S.A. deciding to freeze the transmission capacity allocation for exports from 1 March 2008. As at the date of preparation of the consolidated financial statements, the Company is unable to fairly and reliably assess the value of the potential claim.

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. 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, in a proper term, and commencing supplies of electric energy to the Company. Due to the fact of the breach of agreement conditions, the Company cancelled the agreement and demanded a penalty payment with statutory interest from ŻEG. PGE S.A. also asked for a cession of ownership rights of ŻEG, as specified in the above mentioned agreement. In response ŻEG informed in a letter dated 3 July 2006 of assessing the claims as unjustified. In the letter ŻEG accused the Company of breaching the agreement on supply of electric power and energy and informed of plans to prosecute the claims. As at the date of preparation of the consolidated financial statements the Company was unable to fairly and reliably assess the value of the potential claim.

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Elektrociepłownia Rzeszów S.A. - contingent liabilities related to the purchase of gas

If an entity does not collect a minimum annual volume of gas fuel during a contractual year, that is 85% of an agreed annual volume, then every m³ of gas fuel constituting the difference between the minimum annual volume and the volume actually collected will be subject to a fee that is 80% of the weighed average unitary variable charge of 12 months of the given year.

The fuel that is not collected, but paid for, may be collected by the buyer in the period of three years after the year in which the event took place, under the condition that minimum annual volumes shall be collected during those years.

Furthermore, in the summer period, i.e. from 1 April to 30 September, the buyer is obliged to collect the minimum summer volume of gas fuel that is 42.5% of the agreed annual volume. If an entity does not collect the minimum summer volume of gas fuel during a contractual year, then every m³ of gas fuel constituting the difference between the minimum summer volume and the volume actually collected will be subject to a fee that is 10% of the weighed average unitary variable charge of 6 months of the given summer period. If the buyer carries on an additional overhaul during the contractual year, then the minimum summer volume decreases to 35%. In every year in which the buyer experiences a decrease in energy sales in the period longer than three months of a calendar year, the minimum summer volume is not applicable.

Zakład Energetyczny Łódź-Teren Obrót sp. z o.o. – antitrust proceedings

Currently, the company is subject to antitrust proceedings from the Office for Competition and Consumers' Protection (the Office) started after the motion of VIVA MANUFAKTURING (POLAND) Spółka z o.o. The proceedings relate to fees for exceeding the contractual capacities. The company assesses that the calculation of these charges for this enterprise was prepared in accordance with relevant regulations of electricity tariff. Nevertheless, as at the day of preparation of the consolidated financial statements, there is a risk of a penalty in accordance with art. 106, point 1 of the Act of 16 February 2007 on competition and consumers' protection. There is a possibility of an increase of this risk if the Office shall commence a detailed inspection of the calculation of ZEŁT S.A. for the period subject to control. According to art. 106 of the Act on competition and consumers' protection, the President of the Office can levy a penalty in the amount no higher than 10% of the revenue from the reporting year preceding the year in which the penalty was levied.

Elektrownie Szczytowo-Pompowe S.A. – buy-out of employee shares

In 2007, ESP S.A. acquired from the State Treasury 85% of shares of ZEC Bydgoszcz S.A. As specified in the agreement, ESP S.A. declared it will buy out the employee shares of ZEC Bydgoszcz S.A. during 2010-2012. Due to the year of the buy out, the purchase price is established at different price. The liability of ESP S.A. towards the employees of ZEC Bydgoszcz S.A. will amount from PLN 27,840,000 to PLN 32,016,000.

PGE S.A. – dispute with ENION S.A.

The dispute concerned a 2002 complaint of PGE S.A. against ENION S.A. to pay the PLN 461,937 thousand due to sales to BZE S.A. In 2005 the court dismissed the complaint of PGE S.A. of PLN 341,260 thousand. The remaining amount, i.e. PLN 120,677 thousand comprised the main receivable of PLN 95,134 thousand and interest of PLN 25,543 thousand. In 2007, a settlement was concluded between the parties that fully dismissed the liabilities under court

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proceedings. ENION S.A. declared a payment of PLN 55,000 thousand to PGE S.A. The full amount was to be paid to the bank account of PGE S.A.

PGE S.A. – the claim of AIG Insurance Company S.A.

AIG Insurance Company S.A. demanded from both PSE-Zachód S.A. and PGE S.A. a total of PLN 150,192 thousand with statutory interest calculated from the date of filing the claim till the date of the payment and reimbursement of court fees in accordance with the law. The claim was based on the destruction of machinery and equipment of Elektrownia Turów S.A. in a fire in December 1998 and the opinion of AIG that this event resulted from actions taken by one of the sued entities. On 28 December 2007, the Appeal Court in Wrocław pronounced a verdict in which it dismissed the appeal of AIG. The case was legally closed. Due to the above, the entity reversed the relevant provision of PLN 126,708 thousand. In April 2008 AIG claimed for the final appeal – of which copy was delivered to PGE e on 16th April 2008. The Company replied to the claim on 30th April 2008.

Zespół Elektrowni Dolna Odra S.A. – the obligation to maintain fuels' reserves

In 2007, the proceedings commenced in 2006 against the company in front of the President of the Energy Regulatory Office (ERO), for the purpose of imposing a monetary fine on the entity due to disclosure of irregularities concerning non-compliance with the obligation of maintaining liquid fuels' reserves in the volume specified in relevant law regulations. After the proceedings finished, the President of ERO levied a fine on ZEDO S.A. in the amount of PLN 80 thousand. The penalty was levied despite the supplied documentary evidence that proved ZEDO S.A. as not guilty of the shortage of lignite. According to art. 56 of the Energy Law, the President of ERO is obliged, but not entitled, to levy a fine when a non-compliance with the obligation of maintaining lignite reserves on the specified level is identified, regardless of whether the entity is or is not guilty. The penalty imposed amounted to 0,006% of revenues from concessioned operations, whereas the maximum penalty could be up to 15% of these revenues. Similar proceedings with the President of URE were commenced on 31 December 2007.

Zespół Elektrowni Dolna Odra S.A. – real estate property tax

In 2007, two tax proceedings were carried out to determine the amount of liability from real estate tax for the years 2002 and 2007. As a result of the 2006 audit on real estate tax, the Company filed a 2007 tax declaration, the value of which was lower by PLN 4 million in comparison with the previous years' declarations. In January 2007, the Mayor of Gryfino City and Commune commenced proceedings to determine formal correctness of the 2007 real estate property tax declaration.

In November 2007, the Mayor of Gryfino City and Commune commenced another tax proceeding to determine the value of real estate tax liability for 2002. According to the verdict of 20 December 2007, the tax liability of the Company amounted to PLN 22,767 thousand and was ca. PLN 14 million higher than the amount declared by the Company. In order to secure the real estate tax receivable, a mandatory deposit mortgage was established up to the value of PLN 59,217 thousand. On 2 January 2008, the Company filed an appeal from the above decision to the Self-Government Appeal Council (SAC) in Szczecin.

The Company assesses, with regards to the opinion of tax advisors, based on the activities to date of administrative authorities (SAC, the President of Szczecin), the interpretations of the Ministry of Finance and administrative courts' jurisdiction, that the risk of increasing the tax

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expenses is very low. Currently the proceeding is in progress. Current status of the litigation is introduced in note 40 "Tax settlements" of this consolidated financial statement.

BOT Elektrownia Turów S.A. – the claim of Instytut Automatyki Systemów Energetycznych

The Company creates a provision for costs of disputes related to the claim of Instytut Automatyki Systemów Energetycznych (IASE). As at 31 December 2007, the provision amounted to PLN 2,149 thousand. Currently, two court proceedings on behalf of BOT Elektrownia Turów S.A. are being carried.

The first court proceeding is related to the complaint of Instytut Automatyki Systemów Energetycznych (IASE) in Wrocław for the payment of PLN 14,133 thousand from the distribution of profits from the use of common technological improvements, with statutory interest. On 30 May 2007, the Appeal Court in Wrocław awarded IASE the total amount of PLN 4,701 thousand comprising the receivable and related statutory interest. Both parties filed claims of cassation for this verdict. During the trial on 19 March 2008, the Supreme Court dismissed both claims and cancelled the costs of cassation proceedings between the parties. This means, that the verdict of the Appeal Court in Wrocław was confirmed and that the proceedings are finished.

The second court proceeding is directly related to the first one. The proceeding carried on behalf of BOT Elektrownia Turów S.A. relates to the annulment of the feasibility of the verdict of the Appeal Court in Wrocław of 30 May 2007. The amount disputable is PLN 1,948 thousand.

Furthermore, the Group electricity generating entities are parties to court disputes related to compensations for the use of real estate properties and the removal of electrical machinery and equipment from private premises.

PGE S.A. – arbitration proceedings with Vodafone Americas, Inc. as a plaintiff

On 10 March 2006 Vodafone Americas, Inc („Vodafone”) filed a law suit to International Court of Arbitration by Federal Chamber of Commerce in Vienna against TDC Mobile International A/S („TDC”), Polkomtel S.A., PGE S.A., PKN Orlen S.A., KGHM Polska Miedź S.A. and Węglkokoks S.A. („Polish Shareholders”). In the above mention law suit, Vodafone questioned the interpretation of provisions of the Articles of Association of Polkomtel related to execution of pre-emption rights.

The law suit is related to the offer of sale of Polkomtel shares made on 8 February 2006 by TDC (owner of 19,61% of total shares of this company) for other shareholders of Polkomtel, including the parent company (owner of 17,56% of total shares). As a result of the offer, the shareholders of Polkomtel (including Vodafone) obtained, in accordance with the Articles of Association of Polkomtel, rights to purchase the shares owned by TDC, in the proportion relevant to the percentage of shares owned by each shareholder (apart from TDC).

As a result of the above mentioned offer of TDC, on 10 March 2006 an “Agreement on acceptance of the offer and conditional sale of shares of Polkomtel S.A.” (“Agreement on sale of shares”) was concluded between the Company and Polish Shareholders as buyers and TDC as a seller. Furthermore, on the same day, Polish Shareholders concluded an agreement on purchase of shares from TDC and undertaking common activities targeted at sale of all shares

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of Polkomtel. Vodafone refused to conclude the Agreement on sale of shares with TDC and filed a law suit which questioned the one-sided calculation of the price of shares offered by TDC to Polish Shareholders on 8 February 2008. In particular, Vodafone claimed that the price has not been settled by the shareholders and as a result of no such settlement – it has not been calculated by independent auditors. Therefore, it is contradictory with the Articles of Association and the Agreement of Shareholders of Polkomtel.

The value of the above described law suit amounts to EUR 45 146 thousand. The Company together with Polish Shareholders filed a countersuit to dismiss the complaint of Vodafone. Furthermore, due to the above arbitration proceedings, Vodafone filed a complaint to the District Court in Warsaw for issue of a prohibition for sale of Polkomtel shares owned by TDC as specified in the Agreement on sale of shares. In resolution of 24 February 2006, the District Court in Warsaw established such a prohibition.

On 25 March 2008 the Court of Arbitration issued a verdict that confirmed the validity of the Agreement on sale of shares. However, the verdict is only partial and does not settle all matters. The Agreement on sale of shares includes the following suspensive conditions: i) a reversal of the resolution of the District Court in Warsaw dated 24 February 2006 or other similar decisions or means prohibiting TDC to sell shares of Polkomtel, ii) lack of invalidity or ineffectiveness risks related to the transfer of shares as specified in the Agreement on sale of shares. If the suspensive conditions are not executed until 10 March 2009, the Agreement on sale of shares shall be subject to dissolution. On 20 May 2008 TDC filed a motion to the District Court in Warsaw for reversal of the prohibition for sale of shares of Polkomtel.

As at the day of preparation of the consolidated financial statements, the above described legal proceedings were not settled.

39. Investment liabilities

As at 31 December 2007 the Group was obliged to incur capital expenditures on property, plant and equipment in the amount of PLN 3,448,793 thousand. These amounts relate to modernization of Group's assets and a purchase of new machinery and equipment. The major investment being currently realized in the Group is the construction of a 858 MW block together with a transmission line with a cost of PLN 2,714,368 thousand realized by BOT Elektrownia Bełchatów S.A.

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 unreturnable 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, elsewhere not classified.

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 and means of transportation tax). Other payments classified as quasi –

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taxes cannot be omitted. Among these social security charges and payments of dividends for 100% State Treasury owned entities must be enumerated.

Basic tax rates in 2007 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 this tax exemption. Dividend to the State Treasury – 15%.

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.

As at the date of the consolidated financial statements the Capital Group companies were subject to the following proceedings regarding public and state settlements:

- Since June 2008 BOT Elektrownia Turów S.A. is facing a control over excise tax settlement for the period from 1 January 2006 to 31 December 2006. Currently the Company is submitting remarks to control protocol. The control found few misstatements causing surplus payment by Elektrownia.,
- As described in note 38 of the consolidated financial statements Zespół Elektrowni Dolna Odra S.A. is subject to tax proceedings regarding real estate tax. The Company received the decision defining tax liability for previous payments in total amount of PLN 46,913 thousand. On 6 August 2008 the Company has received a decision on land tax for year 2002 from Self-Government Appeal Court (SKO). According to the decision, SKO has appealed from a decision and remanded a case to first degree of jurisdiction.
- Since 2008 BOT Elektrownia Bełchatów S.A. is subject to tax proceedings regarding its application to assess the overpayment of real estate tax for the years 2003-2007.

As a result of the above described controls the tax settlements of the Group may be increased with additional tax liabilities. The Group believes that as at 31 December 2007 proper reserves were created for known and quantifiable tax risks.

41. Information on related entities

100% of shares of PGE Polska Grupa Energetyczna S.A. are owned by the State Treasury.

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

As described in note 45 of the consolidated financial statements, to the end of the year 2007 the parent company has long term contracts with electrical energy producers, including entities dependent on the State Treasury.

According to agreement signed on 1 July 2004 the parent company was a part of lease transaction on an organized part of a company responsible for distribution including fixed assets and distribution rights entitled to the Company till 31 December 2007.

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41.1. Associates

The information on investments in associates accounted for using the equity method is presented in note 27.

	Sale to related entities	Purchase from related entities	Receivables from related entities	Liabilities towards related entities
2007	373 057	63 657	112 094	17 948
2006	121 518	25 982	13 229	2 409

41.2. Transactions with State Treasury entities

The State Treasury is the 100% shareholder of the Group 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 the biggest State Treasury related companies. The total value of transactions with such entities is presented in the table below.

	Sale to related entities	Purchase from related entities	Trade receivables from entities	Incl. past due	Trade liabilities towards related entities	incl. past due
2007	9 495 279	6 322 996	866 813	69 008	667 954	72
2006	11 821 904	7 095 223	1 355 963	8 790	691 176	578

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

Revenues from transaction regarding lease of an organized part of a company responsible for distribution to PSE - Operator S.A. were described in note 18 of this consolidated financial statement.

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41.3. Remuneration of key management

The key management comprises the Management Boards and Supervisory Boards of PGE Group entities and other specified managing positions.

	Year ended 31 December 2007	Year ended 31 December 2006
Short-term employee benefits (salaries and salary related costs)	43 208	32 591
Jubilee and retirement benefits	1 125	617
Post-employment benefits	231	131
Termination benefits	1 023	976
Share-based payments	-	-
Total remuneration paid to key management	45 587	34 315

	Year ended 31 December 2007	Period ended 31 December 2006
The Management Board of the Parent	1 299	1 554
The Supervisory Board of the Parent	278	257
The Management Board – subsidiaries and associates	23 790	19 857
The Supervisory Board – subsidiaries and associates	6 925	5 839
Total	32 292	27 507

Furthermore members of Management Boards and Supervisory Boards of subsidiaries benefit from loans from the Social Funds. The value of these loans as at 31 December 2007 amounted to PLN 88 thousand.

41.4. Shares of the managing personnel in share-based employee benefits and in other transactions

The managing personnel of subsidiaries who fulfilled requirements of the Commercialization and Privatization Act of 30 June 1996 are entitled to receive, free of charge, shares of entities consolidated within the created Polska Grupa Energetyczna Capital Group based on principles specified in the above mentioned act. The amount of relevant costs is not significant to the consolidated financial statements of Polska Grupa Energetyczna. This amount is included in the total amount of costs related to share-based employee benefits, as presented in note 35.4 of the consolidated financial statements.

During 2006 and 2007 there were no significant transactions in which the managing personnel participated.

42. Financial instruments

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

Categories and classes of financial assets:	Position in the balance sheet	Carrying amount						Fair value	
		31 December 2007			31 December 2006			31 December 2007	31 December 2006
		Long-term	Short-term	Total	Long-term	Short-term	Total	Total	Total
1. Held-to-maturity investments									
Bonds, bills and notes receivable acquired		-	69 660	69 660	-	-	-	69 660	-
Total held-to-maturity investments:		-	69 660	69 660	-	-	-	69 660	-
2. Loans and receivables, incl.:									
(i) Trade receivables	a)	1 342	2 335 199	2 336 541	2 113	2 403 458	2 405 571	2 327 080	2 396 815
(ii) Deposits and investments		-	104 993	104 993	34	575	609	104 993	609
(ii) Other financial loans and receivables		322 728	126 784	449 512	319 437	80 802	400 239	627 985	561 243
• Bonds, bill and notes receivable acquired	b)	193 286	1 334	194 620	175 558	-	175 558	377 097	338 456
• Loans granted	b)	126 593	12 693	139 286	141 200	11 290	152 490	135 282	150 596
• Other financial receivables	b)	2 849	112 757	115 606	2 679	69 512	72 191	115 606	72 191
Total loans and receivables:		324 070	2 566 976	2 891 046	321 584	2 484 835	2 806 419	3 060 058	2 958 667
3. Available-for-sale financial assets, incl.:									
(i) Share in entities not quoted on active markets		131 831	6 365	138 196	119 723	12 690	132 413	n/a	n/a
(ii) Shares quoted on active markets		33 379	41 816	75 195	29 141	33 454	62 595	75 195	62 595
(iii) Investment funds' units		7 719	10 137	17 856	5 628	21 469	27 097	17 856	27 097
(iv) Bonds, bills and notes receivable acquired		-	3 046	3 046	-	-	-	3 046	-
(v) Other financial assets available for sale		8 240	23 459	31 699	9 351	14 263	23 614	31 699	23 614
Total assets available for sale:		181 169	84 823	265 992	163 843	81 876	245 719	-	-

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Categories and classes of financial assets:	Position in the balance sheet	Carrying amount						Fair value	
		31 December 2007			31 December 2006			31 December 2007	31 December 2006
		Long-term	Short-term	Total	Long-term	Short-term	Total	Total	Total
4. Financial assets at fair value through profit or loss, held for trading:									
(i) Cash and cash equivalents		-	64 909	64 909	-	180 128	180 128	64 909	180 128
(ii) Bonds, bills and notes receivable acquired		-	22 833	22 833	-	86 084	86 084	22 833	86 084
(iii) Shares quoted on active markets		-	230 844	230 844	-	167 335	167 335	230 844	167 335
Total assets at fair value through profit or loss:		-	318 586	318 586	-	433 547	433 547	318 586	433 547
5. Cash and cash equivalents			2 726 378	2 726 378	-	3 310 154	3 310 154	2 726 378	3 310 154
Financial assets not included in IAS 39									
Lease receivables	b)	411	905	1 316	628	955	1 583	1 316	1 583

a) Long-term trade receivables are presented in the balance sheet as "Other long-term financial assets". Short-term trade receivables are presented in the balance sheet as "Trade receivables".

b) These are presented in the balance sheet as "Loans and receivables".

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Categories and classes of financial liabilities:	Position in the balance sheet	Carrying amount						Fair value	
		31 December 2007			31 December 2006			31 December 2007	31 December 2006
		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		-	17 817	17 817	-	86 359	86 359	17 817	86 359
Total financial liabilities at fair value through profit or loss:		-	17 817	17 817	-	86 359	86 359	17 817	86 359
2. Financial liabilities at amortized cost:									
(i) Interest bearing loans and credits	a)	4 207 266	1 103 125	5 310 391	5 512 428	1 323 134	6 835 562	5 242 690	7 195 800
(ii) Bonds issued	a)	1 532 129	208 964	1 741 093	1 343 661	285 541	1 629 202	1 741 093	1 826 277
(iii) Trade liabilities		-	1 553 996	1 553 996	-	1 634 836	1 634 836	1 548 432	1 648 435
(iv) Other financial liabilities at amortized cost	b)	3 781	501 070	504 851	85	332 921	333 006	504 851	333 006
Total financial liabilities at amortized cost:		5 743 176	3 367 155	9 110 331	6 856 174	3 576 432	10 432 606	9 037 066	11 003 518
3. Other financial liabilities not included in IAS 39									
(i) Liabilities from finance lease and lease agreements with option of purchase	b)	2 983	19 181	22 164	21 470	27 518	48 988	22 164	48 988
Total other financial liabilities:		2 983	19 181	22 164	21 470	27 518	48 988	22 164	48 988

a) These are presented in the balance sheet as "Interest bearing loans and credits"

b) These are presented in the balance sheet as "Other financial liabilities"

42.2. Income statement

	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	Note
For the period from 01.01.2007 to 31.12.2007							
Dividends	-	5 405	-	-	-	5 405	14.3
Gains / (losses) from interest	119 599	14 820	2 021	81 090	(457 335)	(239 805)	14.3,14.4
Gains / (losses) from foreign exchange	51 479	(4 643)	-	(39 793)	152 747	159 790	14.3,14.4
Reversal of impairment allowances / increase of value	1 032	3 236	-	100 690	2 273	107 231	14.1, 14.2, 14.3
Creation of impairment allowances / decrease of value	(187 560)	(43 430)	-	(38 831)	15	(269 806)	14.1, 14.4,14.2
Gains / (losses) on investment disposal	9 258	28 299	1 140	-	(11 581)	27 116	14.3,14.4
Total net profit / (loss)	(6 192)	3 687	3 161	103 156	(313 881)	(210 069)	
For the period from 01.01.2006 to 31.12.2006							
Dividends	-	3 403	-	-	-	3 403	14.3
Gains / (losses) from interest	66 816	39 186	897	65 413	(516 307)	(343 995)	14.3,14.4
Gains / (losses) from foreign exchange	33 139	(1 854)	-	(18 386)	85 202	98 101	14.3,14.4
Reversal of impairment allowances / increase of value	1 478	5 756	5	94 061	3 263	104 563	14.1, 14.2, 14.3
Creation of impairment allowances / decrease of value	(14 875)	(3 391)	(148)	(42 872)	-	(61 286)	14.2
Gains / (losses) on investment disposal	15 437	9 395	1 363	-	(15 310)	10 885	14.3,14.4
Total net profit / (loss)	101 995	52 495	2 117	98 216	(443 152)	(188 329)	

Interest on financial assets that were subject to an impairment allowance in the year ended 31 December 2007 amounted to PLN 3,217 thousand (PLN 10,061 thousand in the year ended 31 December 2006).

The expenses regarding charges for financial liabilities, for which regular payments schedules were not settled (f. ex. overdrafts) amounted to PLN 4,656 thousand in 2007 (and PLN 6,821 thousand in 2006).

During the year ended 31 December 2007 the amount of PLN (1,445) thousand from valuation of assets held for sale was recognized in equity (during the year ended 31 December 2006 respectively PLN 4,046 thousand). In these years non of the amounts from equity were referred to income statement – position of assets held for sale.

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 alternative 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 Group does not plan any significant disposals of the above positions. The Group does not have any information that would allow reliable estimation of the range of fair values of the above positions.

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

42.4.1 Held-to-maturity financial assets

Held-to-maturity financial assets comprise mainly of bills acquired by BOT KWB Bełchatów (PLN 69,660 thousand).

42.4.2 Loans and receivables

The most significant position of loans and receivables are trade receivables presented in note 43.5.2.

42.4.3 Available-for-sale 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 most significant position of shares not quoted on active financial markets is comprised of shares of AWSA Holland II of PLN 64,500 thousand as of 31 December 2007 (PLN 83,000 thousand as of 31 December 2006).

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

The most significant position of financial instruments valued at fair value through the profit or loss is comprised of bonds, bills and notes.

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42.4.5 Financial liabilities at amortized cost

42.4.5.1 Interest bearing loans and credits

Loans and credits drawn by the Group as at 31 December 2007 are presented below.

Currency	Referential rate	Value of credit / loan as at reporting date (in thousands)		Due in the year					
		in currency	in PLN	2008 (short-term)	2009	2010	2011	2012	2013 and later
PLN	Variable	2 335 617	2 335 617	578 706	675 780	200 054	170 569	161 899	548 610
	Fixed	2 165 242	2 165 242	452 039	453 028	853 314	203 430	203 430	0
Total PLN		4 500 859	4 500 859	1 030 745	1 128 808	1 053 368	373 999	365 329	548 610
EUR	Variable	57 026	204 267	10 977	9 996	9 996	8 932	8 932	155 434
	Fixed	-	-	-	-	-	-	-	-
Total EUR		57 026	204 267	10 977	9 996	9 996	8 932	8 932	155 434
USD	Variable	111 543	241 089	30 766	28 774	28 774	28 774	28 774	95 227
	Fixed	11 988	25 911	8 923	8 494	8 494	-	-	-
Total USD		123 531	267 000	39 689	37 268	37 268	28 774	28 774	95 227
CHF	Variable	138 918	338 265	21 714	17 046	26 785	36 525	36 525	199 670
	Fixed	-	-	-	-	-	-	-	-
Total CHF		138 918	338 265	21 714	17 046	26 785	36 525	36 525	199 670
Total loans and credits			5 310 391	1 103 125	1 193 118	1 127 417	448 230	439 560	998 941

Loans and credits drawn by the Group as at 31 December 2006 are presented below:

Currency	Referential rate	Value of credit / loan as at reporting date (in thousands)		Due in the year:					
		in currency	in PLN	2007 (short-term)	2008	2009	2010	2011	2012 and later
PLN	Variable	3 254 836	3 254 836	777 661	1 060 006	484 518	247 567	205 654	479 430
	Fixed	2 537 527	2 537 527	425 299	426 967	426 967	426 133	425 300	406 861
Total PLN		5 792 363	5 792 363	1 202 960	1 486 973	911 485	673 700	630 954	886 291
EUR	Variable	42 366	162 313	20 164	19 893	19 893	19 529	3 671	79 163
	Fixed	-	-	-	-	-	-	-	-
Total EUR		42 366	162 313	20 164	19 893	19 893	19 529	3 671	79 163
CHF	Variable	124 651	297 193	33 450	31 740	31 740	31 740	31 740	136 783
	Fixed	15 984	38 109	9 999	9 370	9 370	9 370	-	-
Total CHF		140 635	335 302	43 449	41 110	41 110	41 110	31 740	136 783
USD	Variable	187 454	545 584	56 561	46 918	41 620	59 083	59 083	282 319
	Fixed	-	-	-	-	-	-	-	-
Total USD		187 454	545 584	56 561	46 918	41 620	59 083	59 083	282 319
Total loans and credits			6 835 562	1 323 134	1 594 894	1 014 108	793 422	725 448	1 384 556

The values presented in the above tables as at 31 December 2007 comprise an investment credit drawn by BOT Elektrownia Opole in PEKAO SA Bank. The purpose of the credit is to finance the "block 1-4" construction with a carrying amount of PLN 2,108,060 thousand as at 31 December 2007 (as at 31 December 2006: PLN 2,533,360 thousand). The above mentioned investment credit is a credit drawn in PLN at a fixed interest rate and a due date of 31 December 2012. Furthermore BOT Elektrownia Bełchatów has drawn 5 investment credits from the European Investment Bank, the European Bank of Restructuring and Development

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and a consortium of banks with Citi Bank Handlowy acting as the agent in order to finance a 858 MW block's construction with a cost of PLN 1,248,304 thousand as at 31 December 2007 (PLN 753,699 thousand as at 31 December 2006). The above mentioned investment credits are credits drawn in PLN at a variable interest rate based on WIBOR 3M and WIBOR 6M. Moreover, BOT Elektrownia Bełchatów has drawn in Nordycki Bank Inwestycyjny a credit with a variable interest rate, denominated in EUR. The due dates of the above credits are 2016-2025.

The value of unused cash in current accounts amounted to PLN 1,242,333 thousand and PLN 1,101,880 thousand as at 31 December 2007 and 31 December 2006 respectively. The due dates of used credit lines are within six months from the balance sheet date.

42.4.5.2 Liabilities from bonds issued

As at 31 December 2007 the main programme of issuing bonds in the Capital Group are agreements signed with a consortium of banks, with ING Bank Śląski S.A. acting as an agent, on 7 December 2007, of a borrowing facility in the value of PLN 6,200,000 thousand, the purpose of which is to refinance liabilities of PGE Group entities, to finance operations of the parent company and to finance the purchase of shares of Polkomtel S.A. The following banks were original guarantors of the issue:

- ING Bank N.V. (PLN 2 billion),
- Rabobank International (PLN 1.5 billion),
- DEPFA Bank plc (PLN 850 million),
- ABN AMRO Bank (Polska) S.A. (PLN 850 million),
- Rabobank Polska S.A. (PLN 500 million),
- PKO BP S.A. (PLN 500 million).

On 14 December 2007, Fortis Bank Nederland N.V. joined the agreement as a guarantor and took over part of the guarantee of ABN AMRO Bank (Polska) in the value of PLN 600 million. The agreement allows issuance of both coupon and zero coupon bonds. As at 31 December 2007, the programme was used in the nominal value of PLN 1,540 million. The date of realization of the agreements is 7 June 2009.

As at 31 December 2006 main position on liabilities on bonds issued was a programme of issuing Eurobonds in BOT Elektrownia Turów S.A. In frames of debt restructuring these bonds were totally repurchased before due date in December 2007.

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Bonds issued as at 31 December 2007

Currency	Referential rate	Value of the issue as at the balance sheet date (in PLN thousand)	Due in the year:					2013 and later
			2008 (short-term)	2009	2010	2011	2012	
PLN	Variable	1 741 093	208 964	1 532 129	-	-	-	-
	Fixed	-	-	-	-	-	-	-
Total bonds		1 741 093	208 964	1 532 129	-	-	-	-

Bonds issued as at 31 December 2006

Currency	Referential rate	Value of the issue as at the balance sheet date (in PLN thousand)		2007 (short-term)	Due in the year:				2012 and later
		in currency	in PLN		2008	2009	2010	2011	
PLN	Variable	513 817	513 817	204 580	249 597	59 640	-	-	-
	Fixed	-	-	-	-	-	-	-	-
Total PLN		513 817	513 817	204 580	249 597	59 640	-	-	-
EURO	Variable	-	-	-	-	-	-	-	-
	Fixed	291 132	1 115 385	80 961	-	-	1 034 424	-	-
Total EURO		291 132	1 115 385	80 961	-	-	1 034 424	-	-
Total bonds			1 629 202	285 541	249 597	59 640	1 034 424	-	-

42.5. Collaterals for repayment of liabilities

The Group uses financial instruments such as securities or combinations thereof as collaterals for repayment of loans. The most frequently used are agreements of cessions, bills and execution statements. As at 31 December 2006 and 31 December 2007 the Group has also recognized a mortgage on the 858 MW Block under construction by BOT Elektrownia Bełchatów and a registered deposit on movable assets and marketable property rights related to this Block. Additionally as at 31 December 2006 has recognized deposit on property, plant and equipment in Elektrociepłownia Lublin- Wrotków sp. z o.o.

Repayment of loans are also secured by deposits on property, plant and equipment, a long-term agreement on coal supply, guarantee contracts and transfer of ownership of coal as a security (for a loan).

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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 at	
	31 December 2007	31 December 2006
Property, plant and equipment ¹⁾	1 107 420	828 792
Inventories	13 000	12 600
Trade liabilities ²⁾	282 620	279 121
Cash	2 408	7 782
Other assets	14 819	46 064
Total assets being collaterals for repayment of liabilities	1 420 267	1 174 359

1) Including assets from finance lease

2) Including subject to pledge and cession of rights to receivables

As at 31 December 2006 the Company has also set deposit mortgage on plots used in perpetual lease rights received in force of administrative decisions of Elektrociepłownia Lublin- Wrotków sp. z o.o, that are not revealed in this consolidated financial statement prepared according to IFRS. Maximum value of burden as at today amounts to PLN 789 milion and liability value amounts to PLN 161 milion.

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

During the reporting periods ended 31 December 2007 and 31 December 2006 there were no events in the 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),
- The Capital Group did not breach any loan agreement terms (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 hedging 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 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 two levels:

- on the level of PGE Capital Group;
- 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. During 2007 procedures were implemented imposing an obligation on Group entities to conclude collateral derivative transactions only when the second party of the transaction is PGE SA. PGE SA is the only entity in the Group that holds a mandate to conclude collateral derivative transactions with external entities, especially with banks and other financial institutions. Collateral strategies implemented by PGE are targeted to provide an optimum level of security with simultaneous minimalization of costs of collateral transactions.

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 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,

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- 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 gathered by PGE SA.

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 31/12/2007	Nominal value as at 31/12/2006
Financial assets exposed to interest rate risk	PLN	Fixed	578 487	511 631
		Variable	2 726 378	3 310 154
	Other currencies	Fixed	0	0
		Variable	0	0
Financial liabilities exposed to interest rate risk	PLN	Fixed	2 188 838	2 588 544
		Variable	4 080 544	3 768 650
	Other currencies	Fixed	25 911	1 153 495
		Variable	450 026	585 978
Net exposure	PLN	Fixed	(1 610 351)	(2 076 913)
		Variable	(1 354 166)	(458 496)
	Other currencies	Fixed	(25 911)	(1 153 495)
		Variable	(450 026)	(585 978)

Interest on financial instruments of variable interest rate is updated in periods shorter than one year. Interest on financial instruments of 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. Due to the low nominal value of such transactions, the relevant risk to which the Group might be exposed to is not significant.

43.3. Currency risk

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

- Exposure to transaction risk results from the fact that part 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 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 investments 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 powers;
- 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.

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	Total carrying amount in PLN	Currency position as at 31 December 2007							
		EUR		USD		CHF		SEK	
		in currency	in PLN	in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets									
Deposits	104 993	-	-	-	-	-	-	-	-
Bonds, bills and notes receivable acquired	332 235	-	-	-	-	-	-	-	-
Trade receivables	2 336 541	10 972	39 303	-	-	-	-	-	-
Cash and cash equivalents	2 726 378	20 852	74 692	184	447	15	33	3	1
Loans granted	139 286	-	-	-	-	-	-	168 759	64 213
Other financial receivables	115 606	-	-	-	-	-	-	-	-
Shares in entities not quoted on active markets	138 196	-	-	-	-	-	-	111 837	42 554
Shares quoted on active markets	75 195	-	-	-	-	-	-	-	-
Other financial assets	303 231	-	-	-	-	-	0	-	-
Lease receivables	1 316	-	-	-	-	-	-	-	-
Financial liabilities									
Derivatives	(17 817)	-	-	(7 317)	(17 817)	-	-	-	-
Interest bearing loans and credits	(5 310 391)	(57 027)	(204 267)	(138 918)	(338 265)	(123 531)	(267 000)	-	-
Bonds and debt instruments issued	(1 741 093)	-	-	-	-	-	-	-	-
Trade and other financial liabilities at amortized cost	(2 058 847)	(5 539)	(19 841)	(635)	(1 547)	-	-	(8 205)	(3 122)
Liabilities from finance lease and lease agreements with option of purchase	(22 164)	-	-	-	-	-	-	-	-
Net currency position		(30 742)	(110 113)	(146 686)	(357 182)	(123 516)	(266 967)	272 394	103 646

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	Total carrying amount in PLN	Currency position as at 31 December 2006							
		EUR		USD		CHF		SEK	
		in currency	in PLN	in currency	in PLN	in currency	in PLN	in currency	in PLN
Financial assets									
Deposits	609	-	-	-	-	-	-	-	-
Bonds, bills and notes receivable acquired	355 686	39 815	152 540	-	-	-	-	-	-
Trade receivables	2 405 571	17 168	65 774	-	-	-	-	-	-
Cash and cash equivalents	3 310 154	45 779	175 388	3	8	16	39	7	3
Loans granted	152 490	-	-	-	-	-	-	185 742	78 643
Other financial receivables	72 191	-	-	-	-	-	-	-	-
Shares in entities not quoted on active markets	132 413	-	-	-	-	-	-	111 837	47 352
Shares quoted on active markets	62 595	-	-	-	-	-	-	-	-
Other financial assets	304 130	-	-	-	-	-	-	-	-
Lease receivables	1 583	-	-	-	-	-	-	-	-
Financial liabilities									
Derivatives	(86 359)	(152 036)	(582 481)	(3 052)	(8 884)	-	-	-	-
Interest bearing loans and credits	(6 835 562)	(42 366)	(162 313)	(187 454)	(545 585)	(140 635)	(335 302)	-	-
Bonds and debt instruments issued	(1 629 202)	(291 132)	(1 115 385)	-	-	-	-	-	-
Trade and other financial liabilities at amortized cost	(1 967 842)	(4 149)	(15 896)	(755)	(2 199)	-	-	(7 821)	(3 311)
Liabilities from finance lease and lease agreements with option of purchase	(48 988)	-	-	-	-	-	-	-	-
Net currency position		(386 921)	(1 482 373)	(191 258)	(556 660)	(140 619)	(335 263)	289 765	122 687

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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:

- Electricity;
- 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	2007		2006	
	Tonnage – external purchase	Cost of purchase (PLN thousand)	Tonnage – internal purchase	Cost of purchase (PLN thousand)
Coal [t]	7 111 962	1 140 575	6 796 485	1 072 632
Gas [m3]	450 013 398	424 184	483 256 287	334 651
Biomass [t]	370 108	60 414	283 369	38 841
Fuel oil [t]	24 439	25 064	27 177	27 302
Total		1 650 237		1 473 426

43.5. Credit risk

Significant Group entities that trade electricity in bulk conclude transactions only with renowned 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.;

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- 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 granted.

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

- Long-term loan granted to Swe-Pol Link accounting for 79% of the balance of loans granted,
- Trade receivables from key customers, as at 31 December 2007 the three most significant customers accounted for 30% of the trade receivables balance, while as at 31 December 2006 they accounted for 53%. The difference between risk concentration as at balance sheet dates results from the decrease in dependence from PSE-Opertor S.A.

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 financial assets amounted to PLN 6,272,976 thousand as of 31 December 2007 and PLN 6,797,421 thousand as of 31 December 2006. As described in note 38, the maximum credit risk exposure resulting from guarantees amounted to PLN 322,490 thousand as of 31 December 2007 and PLN 158,999 thousand as of 31 December 2006.

43.5.1 Bonds, bills and notes receivable acquired

Bonds issued by Autostrada Wielkopolska S.A. accounted for 59% and 43% of the purchased bonds balance as at 31 December 2007 and 31 December 2006, respectively.

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43.5.2 Trade receivables

The terms of payments for trade receivables are usually 2-3 weeks, however in 2007 the Group received payments for receivables after 38 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 allowances for trade receivables are created on the basis of an individual analysis of particular receivables.

Within the restructuring process of receivables for electric energy delivered on the bulk market in 2007 the Group received payments resulting from a court agreement concluded in 2003 with Będziński Zakład Elektroenergetyczny S.A., (currently ENION S.A.). On 4 June 2007 an agreement was concluded with ENION S.A. relating to disputable receivables under court proceedings in the value of PLN 95,134 thousand. Subsequent to the court agreement, ENION S.A. paid to the Company the amount of PLN 55,000 thousand. The remaining amount of the receivables was written off in accordance with prior created provisions.

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 2007		31 December 2006	
	Receivables balance	Share %	Receivables balance	Share %
Poland	2 245 277	96%	2 320 479	96%
Germany	47 986	2%	18 428	1%
Switzerland	25 762	1%	30 061	1%
Other	17 516	1%	36 603	2%
Total	2 336 541	100%	2 405 571	100%

43.5.3 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 64% and 62% of total cash balance as at 31 December 2007 and 31 December 2006 respectively.

43.5.4 Loans granted, other receivables

Other financial receivables comprise mostly prepayment for transmission fees for Vattenfall Sweden. In the consolidated financial statements the above mentioned transaction is presented as a loan. The above receivable from Vattenfall amounted to 24% and 31% of the balance of loans granted as at 31 December 2007 and 31 December 2006 respectively (excluding trade

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receivables). The prepayment was made in January 2005 by PSE S.A. as a payment for future transmission fees. The Group evaluates that credit quality of receivables from Vattenfall is high. The receivables due to the above are denominated in Swedish crowns.

43.5.5 Other financial assets

Other financial receivables comprise assets that are not classified to any other class of financial assets. The concentration of credit risk related to other financial assets in relation to each single customer in this class does not exceed 5% of other financial assets balances.

43.5.6 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. The maximum share of one entity in the total of derivative transactions concluded by the Group amounted to 100% and 33% as at 31 December 2007 and 31 December 2006 respectively (calculated on the basis of fair value of the transaction)

43.5.7 Guarantees granted

Guarantees granted by the companies of the Group are presented in note 38 of the consolidated financial statements.

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43.5.8 Ageing of receivables and allowances on receivables

As at 31 December 2007 and 31 December 2006, only trade receivables and shares in entities not quoted on active markets were subject to impairment allowances. The change in allowance for these classes of financial instruments is presented in the table below:

	Trade receivables	Loans granted	Shares in entities not quoted on active markets
31 December 2006			
Allowances on receivables as at 1 January	331 211	-	130 293
Allowance used	(34 848)		(8 807)
Write-off of unused amounts (reversal of allowance)	(77 250)		(5 571)
Transferred/ obtained due to demerger of electricity generating entity	-		-
Creation of allowances	94 070		2 240
Allowances on receivables as at 31 December	313 183	-	118 155
Value before the allowance	2 716 641	152 490	250 568
Net value (carrying amount)	2 403 458	152 490	132 413
31 December 2007			
Allowances on receivables as at 1 January	313 183	-	118 155
Allowance used	(13 968)		(8 147)
Write-off of unused amounts (reversal of allowance)	(80 978)		(1 592)
Transferred/ obtained due to demerger of electricity generating entity	8		0
Creation of allowances	52 955		32 113
Allowances on receivables as at 31 December	271 110	-	140 529
Value before the allowance	2 606 309	139 286	278 725
Net value (carrying amount)	2 335 199	139 286	138 196

The majority of impairment allowances created by the Group during the reporting relate to trade receivables of electricity generating entities from retail customers. Impairment allowances of electricity generating units amounted to PLN 215,404 thousand as at the reporting date 31 December 2007.

The most significant positions included in impaired shares in entities not quoted on active markets are as follows:

- Impairment allowance on shares in AWSA Holland II – PLN 50,673 thousand,
- Impairment allowance on shares in Telewizja Familijna S.A. in liquidation – PLN 26,005 thousand,

Factors that were taken into consideration by the Company in the calculation of the impairment of the above positions are described in note 12.

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There are no other significant receivables positions within the Group, except for trade receivables, that would be past due but not impaired. The ageing structure of trade receivables and other loans and receivables regarding impairment allowances, is presented below:

Trade receivables and other loans and receivables	Due	Past due				
		< 30 days	30 – 60 days	60 – 90 days	90 – 120 days	>120 days
31 December 2007						
Before the allowance on receivables	2 513 685	174 731	44 194	48 120	9 216	416 820
Allowance on receivables	35 994	3 928	3 874	3 564	661	371 376
After allowance on receivables	2 477 691	170 803	40 320	44 556	8 555	45 444
31 December 2006						
Before the allowance on receivables	2 484 751	195 489	89 989	94 710	7 884	601 170
Allowance on receivables	5 739	65 265	31 819	30 453	969	532 356
After allowance on receivables	2 479 012	130 224	58 170	64 257	6 915	68 814

43.6. 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

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The below table presents the maturity of the Group's financial liabilities as at 31 December 2007 and 31 December 2006 with regards to the maturity date based on contractual non-discounted payments.

31 December 2007	Less than 3 months	Between 3 and 12 months	Between 1 and 5 years	More than 5 years	Total
Bonds issued	24 692	274 957	1 575 640	-	1 875 289
Interest bearing loans and credits	483 104	823 599	3 593 374	1 344 095	6 244 172
Trade and other financial liabilities at amortized cost	2 054 392	-	3 781	-	2 058 173
Liabilities from finance lease and lease agreements with an option of purchase	4 964	14 891	2 983	-	22 837
Derivatives	183	2 440	8 828	5 441	16 892
Total	2 567 335	1 115 887	5 184 606	1 349 536	10 217 363

31 December 2006	Less than 3 months	Between 3 and 12 months	Between 1 and 5 years	More than 5 years	Total
Bonds issued	111 734	88 079	1 468 624	-	1 668 437
Interest bearing loans and credits	456 027	1 170 186	4 707 356	1 627 029	7 960 598
Trade and other financial liabilities at amortized cost	1 967 161	-	1 516	-	1 968 677
Liabilities from finance lease and lease agreements with an option of purchase	7 029	21 086	21 470	-	49 585
Derivatives	14 782	614	97 938	2 072	115 406
Total	2 556 734	1 279 965	6 296 903	1 629 101	11 762 703

Trade liabilities are interest-free and usually settled within 14 days.

43.7. 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 $\pm 6,025\%$ for EUR/PLN, $\pm 9,4\%$ for USD/PLN, $\pm 9,39\%$ for CHF/PLN and $\pm 6,46\%$ for SEK/PLN.

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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 ± 49 pb for WIBOR, ± 65 pb for EURIBOR, ± 116 pb for LIBOR USD and ± 53 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.

43.7.1 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 table below presents the sensitivity of the gross financial result based on reasonable, possible future fluctuations of foreign exchange rates, under the assumption of stability of other risk factors for these classes of financial instruments that are exposed to currency risk:

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Financial instruments by class	31 December 2007		Sensitivity analysis for currency risk as at 31 December 2007							
	Carrying amount	Amount exposed to risk	EUR/PLN		USD/PLN		CHF/PLN		SEK/PLN	
			Net financial result		Net financial result		Net financial result		Net financial result	
			exchange rate	exchange rate	exchange rate	exchange rate	exchange rate	exchange rate	exchange rate	exchange rate
PLN thousand	PLN thousand	EUR/PLN + 6,025%	EUR/PLN - 6,025%	USD/PLN + 9,4%	USD/PLN - 9,4%	CHF/PLN + 9,399%	CHF/PLN - 9,399%	SEK/PLN + 6,46%	SEK/PLN - 6,46%	
Trade receivables	2 336 541	39 303	2 368	(2 368)	-	-	-	-	-	-
Loans granted	139 286	64 213	-	-	-	-	-	-	4 148	(4 148)
Shares in entities not quoted on active markets	138 196	42 554	-	-	-	-	-	-	2 749	(2 749)
Cash and cash equivalents	2 726 378	75 174	4 500	(4 500)	42	(42)	3	(3)	-	-
Derivatives	(17 817)	(17 817)	-	-	(1 675)	1 675	-	-	-	-
Interest bearing loans and credits	(5 310 391)	(809 532)	(12 307)	12 307	(31 797)	31 797	(25 071)	25 071	-	-
Trade and other liabilities at amortized cost	(2 058 847)	(21 388)	(1 195)	1 195	(145)	145	-	-	-	-
Gross profit change			(6 634)	6 634	(33 575)	33 575	(25 068)	25 068	6 897	(6 897)

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Financial instruments by class	31 December 2006		Sensitivity analysis for currency risk as at 31 December 2006							
	Carrying amount	Amount exposed to risk	EUR/PLN		USD/PLN		CHF/PLN		SEK/PLN	
			Net financial result		Net financial result		Net financial result		Net financial result	
			exchange rate	exchange rate	exchange rate	exchange rate	exchange rate	exchange rate	exchange rate	exchange rate
PLN thousand	PLN thousand	EUR/PLN + 7,25%	EUR/PLN - 7,25%	USD/PLN + 10%	USD/PLN - 10%	CHF/PLN + 9,08%	CHF/PLN - 9,08%	SEK/PLN + 8,69%	SEK/PLN - 8,69%	
Bonds, bill and notes receivable acquired	355 686	152 540	11 059	(11 059)	-	-	-	-	-	-
Trade receivables	2 405 571	65 774	4 769	(4 769)	-	-	-	-	-	-
Loans granted	152 490	78 643	-	-	-	-	-	-	6 834	(6 834)
Shares in entities not quoted on active markets	132 413	47 352	-	-	-	-	-	-	4 115	(4 115)
Cash and cash equivalents	3 310 154	175 438	12 716	(12 716)	1	(1)	4	(4)	-	-
Derivatives	(86 359)	573 598	42 230	(42 230)	(888)	888	-	-	-	-
Bonds and other debt instruments issued	(1 629 202)	(1 115 385)	(80 865)	80 865	-	-	-	-	-	-
Interest bearing loans and credits	(6 835 562)	(1 043 200)	(11 768)	11 768	(54 558)	54 558	(30 446)	30 446	-	-
Trade and other liabilities at amortized cost	(1 967 842)	(18 095)	(1 152)	1 152	(220)	220	-	-	-	-
Gross profit change			(23 011)	23 011	(55 665)	55 665	(30 442)	30 442	10 949	(10 949)

Exposure to risk as at 31 December 2006 and as at 31 December 2007 is representative for the Group's exposure to the risk in the preceding annual periods.

43.7.2 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 2007		Sensitivity analysis for interest rate risk as at 31 December 2007							
	Carrying amount	Amount exposed to risk	WIBOR		EURIBOR		LIBOR USD		LIBOR CHF	
			Net financial result		Net financial result		Net financial result		Net financial result	
			WIBOR + 49 bp	WIBOR - 49 bp	EURIBOR + 65 bp	EURIBOR -65 bp	LIBOR USD + 116 bp	LIBOR USD -116 bp	LIBOR CHF + 53 bp	LIBOR CHF -53 bp
PLN thousand	PLN thousand									
Cash and cash equivalents	2 726 378	2 726 378	13 308	(13 308)	813	(813)	0	0	0	0
Derivatives	(17 817)	(17 817)	0	0	0	0	18 626	(18 626)		
Interest bearing loans and credits	(5 310 391)	(3 119 238)	(13 697)	13 697	(1 191)	(1 191)	(5 126)	5 126	(1 426)	1 426
Bonds issued	(1 741 093)	(1 741 093)	(4 266)	4 266	0	0	0	0	0	0
Gross profit change			(4 655)	4 655	(378)	(2 004)	13 500	(13 500)	(1 426)	1 426

Interest rates fluctuations do not have a direct influence on equity of the Group.

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Financial assets and liabilities	31 December 2006		Sensitivity analysis for interest rate risk as at 31 December 2006							
	Carrying amount	Amount exposed to risk	WIBOR		EURIBOR		LIBOR USD		LIBOR CHF	
			Net financial result		Net financial result		Net financial result		Net financial result	
	PLN thousand	PLN thousand	WIBOR + 49 bp	WIBOR - 49 bp	EURIBOR + 65bp	EURIBOR -65 bp	LIBOR USD + 116 bp	LIBOR USD -116 bp	LIBOR CHF + 53 bp	LIBOR CHF -53 bp
Cash and cash equivalents	3 310 154	3 310 154	15 987	(15 987)	789	(789)	0	0	0	0
Derivatives	(86 359)	(86 359)	12 739	(12 739)	(10 500)	10 500	7 136	(7 136)	0	0
Interest bearing loans and credits	(6 835 562)	(4 259 927)	(16 600)	16 600	(730)	730	(1 855)	1 855	(565)	565
Bonds issued	(1 629 202)	(513 817)	(2 620)	2 620	0	0	0	0	0	0
Gross profit change			9 506	(9 506)	(10 441)	10 441	5 281	(5 281)	(565)	565

Interest rates fluctuations do not have a direct influence on equity of the Group.

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44. Employment structure

Average employment in the Group as at 31 December 2007 and 31 December 2006 was as follows:

	Year ended 31.12.2007	Year ended 31.12.2006
Total employees, including:	47 734	47 663
Mining and production	23 552	24 317
Production of energy from renewable sources	160	155
Wholesale and retail sale entities	14 508	14 641
Wholesale of electricity and other products of energetics	370	311
Other consolidated entities	9 144	8 239

45. Subsequent events

Long-term contracts

The process of preparation of restructuring of long-term contracts (LTC), started in 2001-2006, was continued in 2007. Legislation procedures ended on 29 June 2007, when the legislator passed the bill on rules of covering producers' costs related to early dissolution of long-term agreements on sales of electric power and energy (Official Journal, No. 130, item 905, year 2007).

During 2007 legislation works were held which related to legal analysis of provisions of the above mentioned act, along with threats and risks relevant to the European Union accession – in case of rejection of the Polish government program by the EU. After publication of the European Commission's decision on 25 September 2007, PGE Polska Grupa Energetyczna S.A. organized works on analysis of the decision's legal consequences for particular producers of PGE Group. The Company took part in the process of coordination of works related to termination of long-term contracts, as an active participant of the Group for LTC termination.

Within the term specified in the Act, i.e. until 31 December 2007, PGE Polska Grupa Energetyczna S.A. signed Termination Agreements with all producers that were parties at LTC. Signing of a termination agreement by the producers was the basis for receiving compensation for expenses not covered by revenues from sales of electricity, power reserve and system services on the competitive market after early dissolution of LTC, which resulted from expenditures made by producers before 1 May 2004 for property, plant and equipment related to production of electricity. In accordance with the Act, the maximum stranded cost limit and amounts used for calculation of annual cost adjustments were established for every producer. After LTC termination, a producer shall receive compensation in the form of an advance, starting from 2008. Then, during the so-called period of adjustment, lasting until expiration of the longest long-term agreement of the given producer, an annual adjustment of not compensated costs shall be made.

PGE Capital Group entities were also parties to long-term contracts and after their termination they were granted rights for compensation. The maximum value of uncompensated costs (total value of compensations for PGE Group entities), according to an appendix to the above mentioned Act, amounted to:

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- BOT Elektrownia Opole S.A. – PLN 1,965,700 thousand;
- BOT Elektrownia Turów S.A. – PLN 2,571,151 thousand;
- Zespół Elektrowni Dolna Odra S.A. – PLN 633,496 thousand;
- Elektrociepłownia Rzeszów S.A. – PLN 297,415 thousand;
- Elektrociepłownia Lublin-Wrotków sp. z o.o. – PLN 425,263 thousand;
- Elektrociepłownia Gorzów S.A. – PLN 72,755 thousand.

Final value of compensations received shall depend mainly on electricity prices, which will become known after the Act becomes effective.

Adoption of the National Plan of Emissions Scheme for the years 2008 – 2012

On 1st July 2008 the Council of Ministers accepted the project of a regulation concerning the adoption of the National Plan of Emissions Scheme regarding carbon dioxide emissions for the years 2008-2012 in the Community emissions trading system dividing the carbon dioxide emissions limits between the installations participating in the emissions 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 issue around 1 043 million tons of carbon dioxide during the following five years. This gives a volume of 209 million tons per year.

Until the date of approval of the consolidated financial statements, the National Plan of Emissions Scheme was not published.

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The below shown table presents annual carbon dioxide emission limits allowed to installations in PGE Group:

LP.	NAME	DESCRIPTION	AVERAGE ANNUAL LIMIT (Mg CO ₂)
1	BOT Elektrownia Bełchatów S.A.	Power plant	26 937 155
2	BOT Elektrownia Opole S.A.	Power plant	6 475 340
3	BOT Elektrownia Turów S.A.	Power plant	11 158 636
4	Zespół Elektrowni Dolna Odra S.A.	Dolna Odra Power plant	4 796 497
5	Zespół Elektrowni Dolna Odra S.A.	Pomorzany Power plant	640 857
6	Zespół Elektrowni Dolna Odra S.A.	Szczecin Power plant	242 783
7	Elektrociepłownia Gorzów S.A.	Heat and power plant	476 690
8	Elektrociepłownia Lublin-Wrotków sp. z o.o.	Heat and power plant	570 840
9	Zespół Elektrociepłowni Bydgoszcz S.A.	Bydgoszcz II Heat and power plant	1 092 499
10	Zespół Elektrociepłowni Bydgoszcz S.A.	Bydgoszcz I Heat and power plant	62 746
11	Zespół Elektrociepłowni Bydgoszcz S.A.	Bydgoszcz III Heat and power plant	7
12	Elektrociepłownia Rzeszów	Heat and power plant	194 588
13	Elektrociepłownia Rzeszów	Coal boiler plant	108 567
14	Elektrociepłownia Kielce S.A.	Heat and power plant	189 357

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

Signed on the Polish Original

*Tomasz Zadroga
President*

Signed on the Polish Original

*Adam Cichocki
Vice-President*

Signed on the Polish Original

*Henryk Majchrzak
Vice-President*

Signed on the Polish Original

*Piotr Szymanek
Vice-President*

Signed on the Polish Original

*Wojciech Topolnicki
Vice-President*

Signed on the Polish Original

*Marek Trawiński
Vice-President*

Signed on the Polish Original

*Paweł Urbański
Vice-President*