



ENEA Group

Independent Auditor's Report

Financial Year ended

31 December 2017

KPMG Audyt Spółka z ograniczoną odpowiedzialnością sp.k.
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INDEPENDENT AUDITOR'S REPORT

To the General Meeting of ENEA S.A.

Report on the Audit of the Annual Consolidated Financial Statements

We have audited the accompanying annual consolidated financial statements of the ENEA Group, whose parent entity is ENEA S.A., with its registered office in Poznań, Górecka 1 Street (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, the consolidated statement of profit or loss and other comprehensive income, the statement of changes in consolidated equity and the consolidated statement of cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information (the "consolidated financial statements").

Management's and Supervisory Board's Responsibility for the consolidated financial statements

Management of the Parent Entity is responsible for the preparation, of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards, as adopted by the European Union ("IFRS UE") and other applicable laws. Management of the Parent Entity is also responsible for such internal control as Management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

According to the accounting act dated 29 September 1994 (Official Journal from 2017, item 2342 with amendments) ("the Accounting Act"), Management of the Parent Entity and members of the Supervisory Board are required to ensure that the consolidated financial statements are in compliance with the requirements set forth in the Accounting Act.

Auditor's Responsibility for the audit of the consolidated financial statements

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with:

- the act on certified auditors, audit firms and public oversight dated 11 May 2017 (Official Journal from 2017, item 1089) (the „Act on certified auditors”);

- International Standards on Auditing as adopted by the resolution dated 10 February 2015 of the National Council of Certified Auditors as National Standards on Assurance; and
- Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-listed entities and repealing Commission Decision 2005/909/EC (Official Journal of the European Union L 158 from 27.05.2014, page 77 and Official Journal of the European Union L 170 from 11.06.2014, page 66) (the “EU Regulation”).

Those regulations require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the regulations mentioned above will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting a material misstatement resulting from error because fraud may involve collusion, forgery, deliberate omission, intentional misrepresentations or override of internal controls.

The scope of audit does not include assurance on the future viability of the Group or on the efficiency or effectiveness with which the Management has conducted or will conduct the affairs of the Group.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Group’s preparation of the consolidated financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Management of the Parent Entity, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

The most significant assessed risks of material misstatements

During our audit we identified the most significant assessed risks of material misstatements (the “key audit matters”), including those due to fraud, described below and we performed appropriate audit procedures to address these matters. Key audit matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

1. Impairment of property, plant and equipment in the energy production segment

The carrying amount of property, plant and equipment in the energy production segment as at 31 December 2017 amounts to PLN 9,370,558.0 thousand. Impairment loss on property, plant and equipment in the energy production segment as at 31 December 2017 amounts to PLN 1,608,021.0 thousand.

References to consolidated financial statements

Note 3 Material estimates and assumptions, Note 6 Impairment test of property, plant and equipment, Note 7 Property, plant and equipment, Note 50.11 Description of key accounting principles – Impairment of assets.

Key audit matter

As described in the note 6 of consolidated financial statements, due to the significant impairment losses recognized in previous years and the uncertainty of the energy market in Poland, especially the capacity market and the renewable energy support scheme, as at 31 December 2017 the Group has conducted impairment tests of property, plant and equipment in the energy production segment, i.e. assets belonging to ENEA Wytwarzanie Sp. z o.o. and ENEA Elektrownia Połaniec S.A., which comprise the energy production segment.

The Group has performed an estimation of the recoverable amount of property, plant and equipment based on the value in use of corresponding cash generating units using the discounted cash flows model.

Impairment of property, plant and equipment has been considered as a key audit matter due to the fact that the estimation of their recoverable amount is based on a range of assumptions, especially in relation to the future cash flows and the adopted discount rate.

The projected cash flows of the energy production segment are primarily driven by assumptions on the design and the way of functioning of the capacity market in Poland starting from 2021 and the functioning of

Our procedures

Our procedures included, among others:

- Assessment of compliance of the accounting policies adopted by the Group, regarding identification and recognition of impairment of property, plant and equipment, with relevant financial reporting standards;
- Assessment of the internal controls on identification of impairment indicators and testing for impairment of property, plant and equipment;
- Assessment of the Group's judgements in regard to grouping assets into cash generating units;
- Critical assessment of rationality of judgements and assumptions made by the Group, and the estimations of recoverable amount of property, plant and equipment in the energy production segment, and consequently, the amount of impairment loss, with the ongoing support of our internal valuation specialists, including:
 - assessment of the discounted cash flows model prepared by the Group with regard to its compliance with relevant financial reporting standards, compliance with commonly used impairment testing models, and the integrity of the methodology used,
 - assessment of the rationality of the key macroeconomic and discount rate assumptions made by the Group and comparing them to external sources,

renewable energy support scheme, as well as coal prices, energy prices, prices of energy certificates of origin and cost of CO₂ emission rights. The validity of the assumptions made in this regard is considered to be burdened with a significant risk taking into consideration the potential variability of regulations and uncertainty of their effect on energy production economics.

- critical assessment of the rationality of projections of future cash flows, including the assumed levels of revenues, costs, investment expenditures by comparing the adopted assumptions to the historical financial information, and by analyzing actions taken by the Group and its subsidiaries until the date of this auditor's report,
- assessment of whether the Group's assumptions regarding future regulatory conditions were based on a rational model of capacity market and renewable energy support scheme;
- Assessment of correctness and completeness of disclosures in the consolidated financial statements with regard to impairment tests, including the assessment of the sensitivity of cash flows model prepared by the Group to changes in its key assumptions such as discount and inflation rates, prices of electric energy and revenues of the capacity market.

2. Claims for non-contractual use of land

The carrying amount of provisions for claims for non-contractual use of land as at 31 December 2017 amounts to PLN 200,830 thousand. Changes in the amount of provisions for claims for non-contractual use of land included in the profits and losses for the financial year ended 31 December 2017 amounts to PLN (2,461) thousand.

References to consolidated financial statements

Note 3 Material estimates and assumptions, Note 32 Provisions for liabilities and other charges, Note 50.21 Description of key accounting principles – Provisions.

Key audit matter

As described in the note 32 of consolidated financial statements, due to the fact the Group does not have the formal right for exploitation of some facilities on which there are power grids and other power grids assets, the Group has recognized provisions for compensations for non-contractual use of land.

The Group has estimated the value of the provisions for compensations both for the

Our procedures

Our procedures included, among others:

- Assessment of compliance of the accounting policies adopted by the Entity with regard to recognizing provisions for potential claims for non-contractual use of lands dependent on the corresponding financial reporting standards;
- Assessment of the internal controls system in regard to registering of claims, substantive assessment of claims, and calculating the amount of provision;

lands on which there have been claims, as well as for those on which the claims have not yet been present.

The claims for non-contractual use of land have been considered by us as a key audit matter, due to the fact that the calculation of the provisions for the claims for non-contractual use of land is inherently uncertain and requires a range of significant assumptions and judgements. Values of the claims can be significant and determining the potential amount that should be recognized or disclosed in the consolidated financial statements is from its nature inherently subjective.

- Analysis of received by us correspondence from the Group's lawyers related to the ongoing court proceedings in terms of: (i) correct and complete recognition in the models for calculating provisions for claims used by the Group and (ii) legal assessment of unfavorable court verdicts, and discussing selected topics with Management Boards of those entities of the Group which are involved in claims;
- On the basis of the analysis of a selected sample of claims, particularly those that are currently in ongoing court proceedings, a critical assessment of assumptions and estimations of the Group (including a probability of unfavorable rulings) in relation to the recognized provisions for claims for the non-contractual land use;
- Assessment of correctness and completeness of disclosures in consolidated financial statements with regard to claims for non-contractual use of land and related provisions recognized.

3. Claims resulting from termination of long-term contracts for purchase of property rights from energy certificates of origin from renewable sources

The carrying amount of the provision for claims resulting from termination of contracts for purchase of property rights from energy certificates of origin from renewable sources as at 31 December 2017 amounts to PLN 85,684 thousand. Changes in the amount of the provision for claims resulting from termination of contracts for purchase of property rights from energy certificates of origin from renewable sources included in the profits and losses for the financial year ended as at 31 December 2017 amounts to PLN 85,684 thousand.

References to the consolidated Financial statements

Note 3 Material estimates and assumptions, Note 32 Provisions for liabilities and other charges, Note 47.7 Dispute concerning prices of energy certificates of origin and terminated contracts for purchase of energy certificates of origin, Note 50.21 Description of key accounting principles – Provisions.

Key audit matter

As described in the note 47.7 of consolidated financial statements, in 2016 the Group has terminated contracts for the purchase of property rights resulting from energy certificates of origin from renewable sources (the "green certificates"). The terminations of

Our procedures

- Our procedures included, among others:
- Assessment of compliance of the accounting policies adopted by the Group regarding recognition of provisions for claims resulting from termination of contracts for purchase of

the above mentioned contracts was caused, according to the Group, by changes in regulations which disturbed the contractual balance and equivalence of the parties. The purpose of the actions taken by the Group was to avoid losses which are calculated by subtracting the current market price of green certificates from the contract prices. As a result of contractors disagreement on the legal basis of termination of these contracts and related trials pending at District Court in Poznań, where contractors demand judgement on no legal effects of contracts termination, the Group has recognize a provision for potential costs of claims.

Taking into consideration provisions of these contract, there is a material uncertainty on the final outcome of the disputes pending at the court and related to the legal grounds for contracts termination and submitted claims, which requires a detailed analysis and making assumptions and judgements. The amounts of claims can be significant and determination of the potential amount that should be recognized or disclosed in the financial statements is from its nature inherently subjective. For these reasons, submitted and potential claims resulting from termination of contracts for purchase of green certificates have been considered by us as a key audit matter.

green certificates with relevant financial reporting standards;

- Analysis of the content of the terminated contract for purchase of green certificates, especially the legal basis for their termination, and collecting the most up-to-date court trial documentation in order to assess the risks caused by court decisions for contract termination which would be unfavorable for the Group;
- Analysis of legal opinions obtained by the Group and received by us correspondence from the Group's lawyers on claims and ongoing court proceedings, and discussing selected topics with the Management Board of the Parent Entity;
- Based on the above-mentioned analysis and the assessment of the Group's provision calculation model:
 - critical assessment of the Group's assumptions and estimates (including the probability of unfavorable court decisions),
 - critical assessment of the rationality of the cost projections of unfavorable court decisions by comparison, on a sample basis, of volumes of unrealized purchases of green certificates and contractual prices with transaction notifications, and with respect to market prices, by comparing them to publicly available exchange market quotations of green certificates;
- Assessment of correctness and completeness of disclosures in the consolidated financial statements regarding the status of claims resulting from termination of contracts for purchase of green certificates and recognized provisions the reserves made for this purpose.

4. Acquisition of shares of ENGIE Energia Polska S.A.

Fair value of net assets of ENGIE Energia Polska S.A. Group (currently, ENEA Elektrownia Połaniec S.A.) as at the date the Group obtained control of it, i.e. 14 March 2017, amounted to PLN 1,276,112 thousand. The recognized amount of the gain from the bargain purchase of ENGIE Energia Polska S.A. Group amounts to PLN 11,953 thousand.

References to consolidated financial statements

Note 3 Material estimates and assumptions, Note 12.1 Acquisition of shares of ENGIE Energia Polska S.A., Note 50.3 Description of key accounting principles – Business combinations/acquisitions.

Key audit matter

As described in the note 12.1 of consolidated financial statements, on 14 March 2017, the Group acquired 100% of shares of ENGIE Energia Polska S.A. (currently, ENEA Elektrownia Połaniec S.A.) which owns the Power station Połaniec and a subsidiary ENGIE Bioenergia Sp. z o.o. (currently, ENEA Bioenergia Sp. z o.o.) for the price of PLN 1.264 million.

The Group, supported by external appraiser, has conducted a purchase price allocation by determining the fair values of identifiable assets and acquired liabilities as at the date of obtaining control.

The fair value of key assets of the acquired group, i.e., fixed assets of Power station Połaniec, has been determined based on the discounted cash flows model, which requires the adoption of a range of assumptions and estimations, especially in relation to the future cash flows and the adopted discount rate. The projected cash flows of the acquired group are primarily driven by prices of coal, electric energy, energy certificates of origin, and participation of Power station Połaniec in the capacity market and renewable energy support scheme.

The validity of the assumptions made in this regard is considered to be burdened with a significant risk taking into consideration the potential variability of regulations and uncertainty of their effect on energy production economics.

Our procedures

Our procedures included, among others:

- Assessing the experience, competences, and objectivity of the appraiser contracted by the Group for the purpose of estimating the fair value of identified assets and liabilities, and the allocation of ENGIE Energia Polska S.A. group purchase price;
- Critical assessment, with support of our internal valuation specialists, of the report prepared by the appraiser engaged by the Group, in particular in terms of:
 - completeness of the identified assets and liabilities based on our understanding of the activities of ENGIE Energia Polska S.A. Group and the analysis of documentation of the acquired entities,
 - correctness of the adopted methodology of valuation of individual assets and liabilities by comparing it to commonly used methodologies of valuation and the appropriate financial reporting standards,
 - validity of macroeconomic assumptions and the discount rate adopted for the purpose of valuation of property, plant and equipment by comparing them to external sources,
 - rationality of adopted projections of future cash flows, including the assumed levels of revenues, costs, and investment expenditures by comparing them to historical financial information, and by assessing the probability of implementing plans made by the acquired group
 - assessing rationality of the key assumptions made by the appraiser for the purpose of valuing other assets and liabilities, in particular, inventories, deferred tax assets, trade receivables and payables, and provisions for CO₂ emission costs;
- Assessment of correctness and completeness of disclosures in consolidated financial statements related to allocation of acquired entities purchase price.

Opinion

In our opinion, the accompanying consolidated financial statements of ENEA Group:

- give a true and fair view of the consolidated financial position of the Group as at 31 December 2017 and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with IFRS UE and the adopted accounting principles (policy);
- comply, in all material respects, with regard to form and content, with applicable laws and the provisions of the Parent Entity's articles of association.

Auditor's Report on other legal and regulatory requirements

Report on activities of ENEA S.A. and ENEA Capital Group

Our opinion on the consolidated financial statements does not cover the report on activities of ENEA S.A. and ENEA Capital Group (the "report on activities").

Management of the Parent Entity is responsible for the preparation of the report on activities in accordance with the requirements of the Accounting Act and other applicable laws. Furthermore, Management of the Parent Entity and members of the Supervisory Board, are also required to ensure that the report on activities is in compliance with the requirements set forth in the Accounting Act.

In accordance with Act on certified auditors our responsibility was to report if the report on activities, excluding the content of the chapter "*Statement on non-financial information*" was prepared in accordance with applicable laws and the information is consistent with the consolidated financial statements. Our responsibility was also to state, if based on our knowledge about the Group and its environment obtained in the audit, we have identified material misstatements in the report on the activities and describe the nature of each material misstatement.

We report that the accompanying report on activities, excluding the chapter titled "*Statement on non-financial information*", in all material respects:

- was prepared in accordance with applicable laws, and
- is consistent with the consolidated financial statements.

Furthermore, based on our knowledge about the Group and its environment obtained in the audit, we have not identified material misstatements in the report on activities.

Opinion on corporate governance statement

Management of the Parent Entity and members of the Supervisory Board are responsible for preparation of the corporate governance statement in accordance with the applicable laws.

In connection with the audit of the consolidated financial statements, our responsibility in accordance with the requirements of the Act on certified auditors was to report whether the issuer of securities obliged to file a statement on corporate governance, constituting a separate part of the report on activities, included information required by the applicable laws and regulations, and in relation to specific information indicated in these laws or regulations, to determine whether it complies with the applicable laws and whether it is consistent with the consolidated financial statements.

We report that the statement of corporate governance, which is a separate part of the report on the Group's activities, includes the information required by paragraph 91 subparagraph 5 point 4 letter a, b, j, k and letter l of the Decree of the Ministry of Finance dated 19 February 2009 on current and periodic information provided by issuers of securities and the conditions for recognition as equivalent of information required by the laws of a non-member state (Official Journal from 2014, item 133 with amendments) (the "decree"). Furthermore, in our opinion the information identified in paragraph 91 subparagraph 5 point 4 letter c-f, h and letter i of the decree, included in the statement on corporate governance, in all material respects:

- has been prepared in accordance with the applicable laws; and
- is consistent with the consolidated financial statements.

Information about preparation of statement on non-financial information

In accordance with the requirements of the Act on certified auditors, we report that the Parent Entity has prepared a statement on non-financial information referred to in art. 55 paragraph 2b of the Accounting act as a separate part of the report on activities.

We have not performed any attestation works in relation to the statement on non-financial information of the Group and, accordingly, we do not express any assurance thereon.

Information, confirmations and statements required by the EU Regulation

Our opinion on the audit of consolidated financial statements is consistent with our report to the audit committee.

During our audit key certified auditors and the audit firm remained independent of the Group in accordance with requirements of the Act on certified auditors, the EU Regulation and the Code of Ethics for Professional Accountants of the International Ethics Standards Board for Accountants' (IFAC) as adopted by the resolutions of National Council of Certified Auditors.

We declare that, to the best of our knowledge and belief, we did not provide prohibited non-audit services referred to in art. 5 paragraph 1 second subparagraph of the EU Regulation and art. 136 including transitional provisions in art. 285 of the act on certified auditors.

The audit of consolidated financial statements was conducted based on resolution of the Supervisory Board dated 18 December 2014.

Our total uninterrupted period of engagement is 6 years, covering the periods ending 31 December 2012 to 31 December 2017.

On behalf of audit firm
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Signed on the Polish original

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22 March 2018