DIRECTORS' REPORT ON OPERATIONS OF THE PGNIG GROUP IN H1 2012

Polskie Górnictwo Naftowe
i Gazownictwo SA

Warsaw, August 13th 2012

Table of contents

Chapter I: Information on the PGNiG Group

The PGNiG Group operates in the gas sector in Poland and abroad. Polskie Górnictwo Naftowe I Gazownictwo SA is the parent of the PGNiG Group.

Polskie Górnictwo Naftowe i Gazownictwo Spółka Akcyjna (PGNiG SA), registered office in Warsaw, ul. Marcina Kasprzaka 25, was established as a result of transformation of the state-owned enterprise Polskie Górnictwo Naftowe i Gazownictwo into a state-owned stock company. On October 30th 1996, the Company was entered in the commercial register as Polskie Górnictwo Naftowe I Gazownictwo SA of Warsaw, under entry No. RHB 48382. On November 14th 2001, PGNiG SA was entered into the Register of Entrepreneurs of the National Court Register under No. KRS 0000059492.

On May 24th 2005, the Polish Securities and Exchange Commission admitted PGNiG shares to public trading. The Company floated its shares on the Warsaw Stock Exchange on September 23rd 2005. PGNiG shares have been listed on the Warsaw Stock Exchange since October 20th 2005. Currently, the share capital of PGNiG SA amounts to PLN 5.9bn and is divided into 5,900,000,000 shares with a par value of PLN 1 per share.

The PGNiG Group holds the leading position in most segments of the Polish gas sector, such as oil and gas exploration and production, gas fuel storage, natural gas trading and natural gas distribution. The Group's oil and gas upstream operations provide it with a competitive advantage on the liberalised gas market.

1. Structure of the PGNiG Group

As at June 30th 2012, the Group comprised PGNiG SA (the Parent), and 40 production and service companies, including:

- 29 subsidiaries of PGNiG SA, and
- 11 indirect subsidiaries of PGNiG SA.

The list of the PGNiG Group companies as at June 30th 2012 is presented in the table below.

Companies of the PGNiG Group

	Name	Share capital (PLN)	Value of shares held by PGNiG SA (PLN)	Ownership interest held by PGNiG SA	% of total vote held by PGNiG SA
	Direct subsidiaries of PGNiG SA				
1	Poszukiwania Nafty i Gazu Jasło S.A.	100,000,000.00	100,000,000.00	100.00%	100.00%
2	Poszukiwania Nafty i Gazu Kraków S.A.	105,231,000.00	105,231,000.00	100.00%	100.00%
3	Poszukiwania Nafty i Gazu NAFTA S.A.	60,000,000.00	60,000,000.00	100.00%	100.00%
4	GEOFIZYKA Kraków Sp. z o.o.	64,400,000.00	64,400,000.00	100.00%	100.00%
5	GEOFIZYKA Toruń Sp. z o.o.	66,000,000.00	66,000,000.00	100.00%	100.00%
6	Poszukiwania Naftowe Diament Sp. z o.o.	62,000,000.00	62,000,000.00	100.00%	100.00%
7	Zakład Robót Górniczych Krosno Sp. z o.o.	26,903,000.00	26,903,000.00	100.00%	100.00%
8	PGNiG Norway AS (NOK)[1)]	1,092,000,000.00	1,092,000,000.00	100.00%	100.00%
9	Polish Oil and Gas Company - Libya B.V. (USD)[1)2)]	26,724.00	26,724.00	100.00%	100.00%
10	PGNiG Sales & Trading GmbH (EUR)[1)]	10,000,000.00	10,000,000.00	100.00%	100.00%
11	Operator Systemu Magazynowania Sp. z o.o.	5,000,000.00	5,000,000.00	100.00%	100.00%
12	INVESTGAS S.A.	502,250.00	502,250.00	100.00%	100.00%
13	Dolnośląska Spółka Gazownictwa Sp. z o.o.	658,384,000.00	658,384,000.00	100.00%	100.00%
14	Górnośląska Spółka Gazownictwa Sp. z o.o.	1,300,338,000.00	1,300,338,000.00	100.00%	100.00%
15	Karpacka Spółka Gazownictwa Sp. z o.o.	1,484,953,000.00	1,484,953,000.00	100.00%	100.00%
16	Mazowiecka Spółka Gazownictwa Sp. z o.o.	1,255,800,000.00	1,255,800,000.00	100.00%	100.00%
17	Pomorska Spółka Gazownictwa Sp. z o.o.	655,199,000.00	655,199,000.00	100.00%	100.00%
18	Wielkopolska Spółka Gazownictwa Sp. z o.o.	1,033,186,000.00	1,033,186,000.00	100.00%	100.00%
19	Geovita Sp. z o.o.	86,139,000.00	86,139,000.00	100.00%	100.00%
20	PGNiG Energia S.A.	41,000,000.00	41,000,000.00	100.00%	100.00%
21	PGNiG Technologie S.A.	166,914,000.00	166,914,000.00	100.00%	100.00%
22	BUD-GAZ PPUH Sp. z o.o.	51,760.00	51,760.00	100.00%	100.00%
23	Polskie Elektrownie Gazowe Sp. z o.o.	1,212,000.00	1,212,000.00	100.00%	100.00%
24	PGNiG SPV1 Sp. z o.o.	770,020,000.00	770,020,000.00	100.00%	100.00%
25	PGNiG Finance AB (SEK)[1)]	500,000.00	500,000.00	100.00%	100.00%
26	PGNiG Serwis Sp. z o.o.	9,995,000.00	9,995,000.00	100.00%	100.00%
27	MLV 27 Sp. z o.o.	5,000.00	5,000.00	100.00%	100.00%
28	B.S. i P.G. Gazoprojekt S.A.	4,000,000.00	3,000,000.00	75.00%	75.00%
29	NYSAGAZ Sp. z o.o.	9,881,000.00	6,549,000.00	66.28%	66.28%

Companies of the PGNiG Group – contd.

	Indirect subsidiaries of PGNiG SA	Share capital (PLN)	Value of shares held by PGNiG SA's subsidiaries (PLN)	Ownership interest held by PGNiG SA's subsidiaries	% of total vote held by PGNiG SA's subsidiaries
1	Oil Tech International F.Z.E. (USD)[1)]	20,000.00	20,000.00	100.00%	100.00%
2	Powiśle Park Sp. z o.o.	81,131,000.00	81,131,000.00	100.00%	100.00%
3	Zakład Gospodarki Mieszkaniowej Sp. z o.o. (Piła)	1,806,500.00	1,806,500.00	100.00%	100.00%
4	Biogazownia Ostrowiec Sp. z o.o.	105,000.00	105,000.00	100.00%	100.00%
5	XOOL GmbH (EUR)[1]	500,000.00	500,000.00	100.00%	100.00%
6	PGNiG TERMIKA S.A.	246,300,000.00	246,045,490.00	99.89%	99.89%
7	Poltava Services LLC (EUR)[1)]	20,000.00	19,800.00	99.00%	99.00%
8	Ośrodek Badawczo-Rozwojowy Górnictwa Surowców Chemicznych CHEMKOP Sp. z o.o.	3,000,000.00	2,550,000.00	85.00%	85.00%
9	GAZ Sp. z o.o. (Błonie)	300,000.00	240,000.00	80.00%	80.00%
10	PT Geofizyka Torun Indonesia LLC (IDR)[1)3)]	8,773,000,000.00	4,825,150,000.00	55.00%	55.00%
11	GAZ MEDIA Sp. z o.o. (Wołomin)	300,000.00	153,000.00	51.00%	51.00%

[1)] figures expressed in foreign currencies
[2)] financial reporting currency changed from EUR to USD
[3)] paid-up capital: USD 40,687.13

Changes in the PGNiG Group's structure in H1 2012:

- On January 11th 2012, PGNiG SPV 1 Sp. z o.o. executed a final share purchase agreement with Vattenfall AB, whereby PGNiG SPV 1 Sp. z o.o. acquired 24,591,544 shares in Vattenfall Heat Poland S.A., which represented 99.8% of the company's share capital and conferred the right to 99.8% of the total vote at the General Meeting of Vattenfall Heat Poland S.A. In H1 2012, PGNiG SPV 1 Sp. z o.o. acquired 13,005 PGNiG TERMIKA S.A. shares from the company's minority shareholders, thus its interest in the company's share capital increased to 99.9%;
- On January 23rd 2012, Vattenfall Heat Poland S.A. changed its name to PGNiG TERMIKA S.A.;
- On February 24th 2012, Mazowiecka Spółka Gazownictwa Sp. z o.o. executed two share purchase agreements, whereby it acquired an aggregate of 58 shares in GAZ Sp. z o.o. of Błonie. Thus MSG's equity exposure to GAZ rose to PLN 240,000, with the ownership interest increasing to 80%;
- On June 6th 2012, PGNiG Sales & Trading GmbH acquired 500,000 shares in XOOL GmbH, with a par value of EUR 1 per share, representing the entire share capital of the company. XOOL GmbH was acquired to expand the Group's trading activities on the German market;
- On June 6th 2012, PGNiG SA acquired 100 shares in MLV 26 Sp. z o.o., with an aggregate par value of PLN 5,000, representing the entire share capital of the company. The total purchase price was PLN 7,500 in 2013, MLV 26 Sp. z o.o. is to start providing HR and payroll, finance, accounting, as well as IT services to PGNIG TERMIKA S.A. On June 16th 2012, a change of the company's name to PGNiG Serwis Sp. z o.o. was registered with the National Court Register;
- On June 8th 2012, PGNiG SA acquired 100 shares in MLV 27 Sp. z o.o., with an aggregate par value of PLN 5,000, representing the entire share capital of the company. The total purchase price was PLN 7,500. The company's name was changed to PGNiG SPV 4 Sp. z o.o. By the date of this Report, the change in the company's name has not been registered with the National Court Register.

Changes in the Group companies' share capital in H1 2012:

- Share capital increase at PGNiG SPV 1 Sp. z o.o. by PLN 770,000,000, to PLN 770,020,000, by way of an issue of 15,400,000 new shares with a par value of PLN 50 per share. The new issue shares were acquired by PGNiG SA. The share capital increase was registered on January 25th 2012;
- Share capital increase at Pomorska Spółka Gazownictwa Sp. z o.o. by PLN 1,553,000, to PLN 655,199,000. The new issue shares were acquired by PGNiG SA and paid for with an in-kind contribution in the form of a perpetual usufruct right to a plot of land situated in Toruń, along with the ownership title to buildings and structures erected thereon. The share capital increase was registered on March 7th 2012;
- Share capital increase at PGNiG Energia S.A. by PLN 11,000,000, to PLN 41,000,000 by way of an issue of 110,000 new shares with a par value of PLN 100 per share. All new issue shares were acquired by PGNiG SA. The share capital increase was registered on March 22nd 2012;
- Share capital increase at PGNiG Serwis Sp. z o.o. to PLN 9,995,000. The new issue shares were acquired by PGNiG SA. The share capital increase was registered on June 29th 2012.

Also in H1 2012, registry courts registered transformation of the following entities into joint-stock companies:

- January 2nd 2012 – PNiG Jasło Sp. z o.o.
- June 1st 2012 – PNiG Kraków Sp. z o.o.
- June 1st 2012 – PGNiG Technologie Sp. z o.o.
- June 14th 2012 – PNiG NAFTA Sp. z o.o.

<u>Changes subsequent to the end of H1 2012</u>

On July 2nd 2012, registry courts registered transformation of GEOFIZYKA Kraków Sp. z o.o., GEOFIZYKA Toruń Sp. z o.o. and GEOVITA Sp. z o.o. into joint-stock companies.

On July 3rd 2012, a new company PGNiG Poszukiwania S.A. w organizacji (in the process of formation) was incorporated. The company was established to consolidate the exploration and service subsidiaries of PGNiG SA. Its share capital amounts to PLN 10,000,000 and is divided into 10,000,000 shares with a par value of PLN 1 per share. All shares in the company were acquired by PGNiG SA. On July 27th 2012, the company was registered with the National Court Register.

<u>Changes in the segmental structure of PGNiG SA and the PGNiG Group</u>

In H1 2012, the segmental structure of the Company and the PGNiG Group was changed. One new segment was formed, and selected subsidiaries and the underground gas storage facilities were reclassified based on their business profiles.

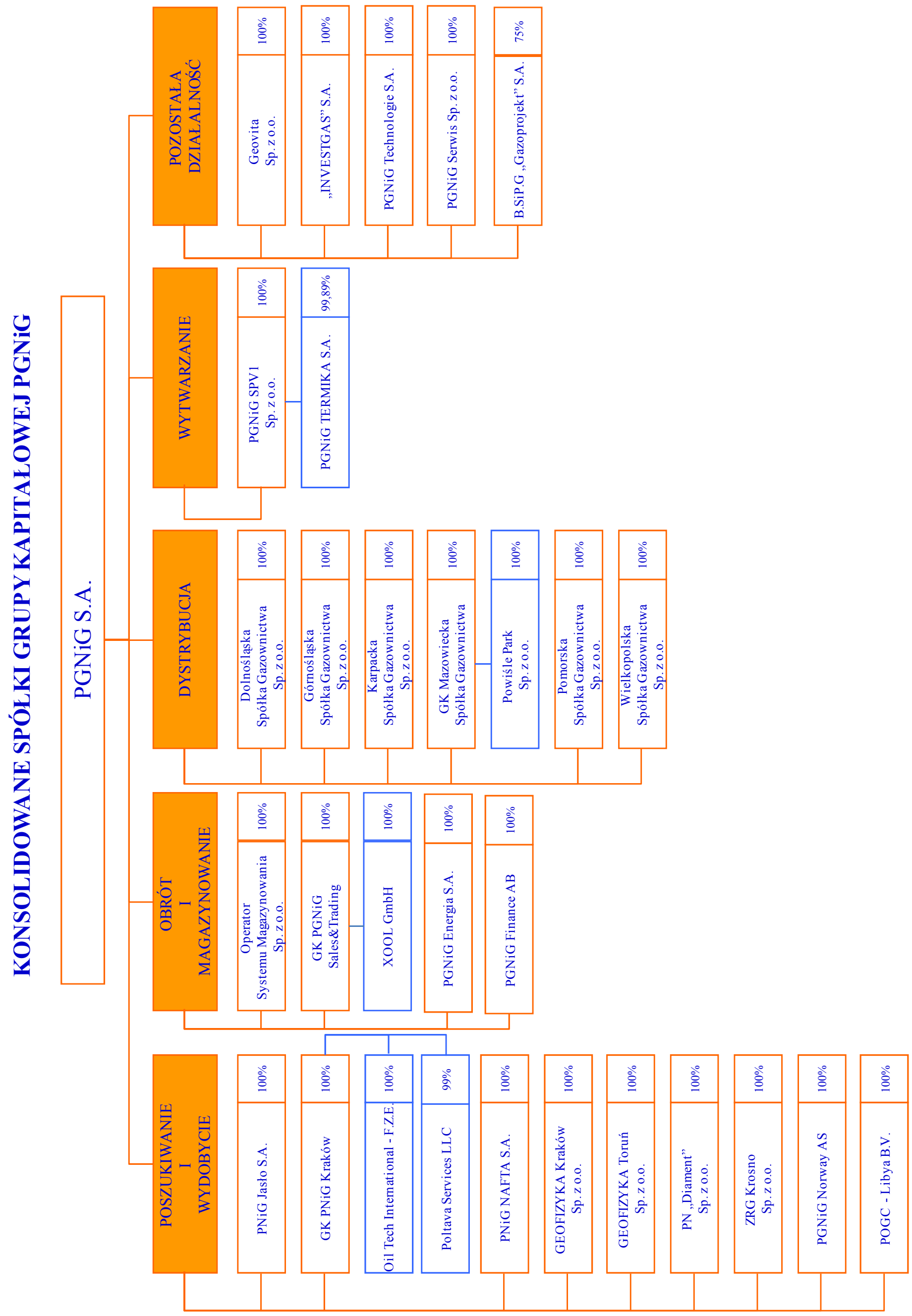
The Brzeźnica, Strachocina and Swarzów underground gas storage facilities were transferred from the Exploration and Production segment to the Trade and Storage segment after PGNiG SA provided access to the facilities' working capacities to third parties (on a TPA basis).

As a result of the acquisition of PGNiG TERMIKA S.A. (former Vattenfall Heat Poland S.A.) in H1 2012, the PGNiG Group expanded the scope of its operations to include electricity and heat generation. A new segment, Generation, was thus established and includes PGNiG TERMIKA S.A. and PGNiG SPV 1 Sp. z o.o..

INVESTGAS S.A. was transferred from the Trade and Storage segment to the Other Activities segment. INVESTGAS S.A. specialises in the provision of comprehensive design services, construction and assembly services, construction supervision services for projects involving construction of gas storage facilities and pipelines, as well as gas storage facility operation services.

PGNiG Energia S.A. and PGNiG Finance AB, previously reported under the Other Activities segment, were transferred to the Trade and Storage segment. PGNiG Energia S.A.'s core business consists in wholesale trade in electricity as well as trade in carbon and other greenhouse gas allowances. PGNiG Finance AB's business involves servicing PGNiG's Euronotes issues.

The chart below presents the consolidated companies of the PGNiG Group as at June 30th 2012 (by segments).



KONSOLIDOWANE SPÓŁKI GRUPY KAPITAŁOWEJ PGNiG	CONSOLIDATED COMPANIES OF THE PGNIG GROUP
POSZUKIWANIA I WYDOBYCIE	EXPLORATION AND PRODUCTION
OBRÓT I MAGAZYNOWANIE	TRADE AND STORAGE
DYSTRYBUCJA	DISTRIBUTION
POZOSTAŁA DZIAŁALNOŚĆ	OTHER ACTIVITIES

2. Employment

The table below presents employment at the PGNiG Group as at June 30th 2012, by segments. As the PGNiG Head Office provides services to all segments in the Group, it is disclosed separately.

Employment by segments (no. of staff)

	June 30th 2012
PGNiG Head Office	754
Exploration and Production	10,641
Trade and Storage	3,863
Distribution	13,642
Generation	1,068
Other Activities	2,299
Total	32,267

3. Sale and acquisition of natural gas

The PGNiG Group recorded revenue of PLN 14.8bn, 83% of which was derived from sales of natural gas.

Sales revenue (PLNm)

	H1 2012
Natural gas, including:	12,273.4
- high-methane gas	11,557.9
- nitrogen-rich gas	715.5
Crude oil	589.7
Condensate	3.8
Helium	66.5
Propane-butane	30.6
Electricity	444.9
Heat	527.5
Certificates of origin for electricity	132.1
Gas storage services	18.8
Geophysical and geological services	161.7
Drilling and well maintenance services	260.3
Construction and erection	50.6
Other sales	204.5
Total	14,764.4

In H1 2012, the PGNiG Group sold 7.9bn m^3 of natural gas, with 95% of that figure represented by sales from the national transmission and distribution systems and the balance – by direct gas sales from the fields.

Natural gas sales (m m^3)

	H1 2012
Trade and Storage	7,533.6
Exploration and Production	365.4
Total	7,899.0

In H1 2012, the volume of natural gas acquired by the PGNiG Group was 8.0bn m^3, with 72% of that amount sourced from imports, mostly from countries east of Poland. Natural gas production from fields in Poland represented 27% of the total volume of gas acquired. The table below presents the structure of natural gas supplies to the Group, measured as high-methane gas equivalent.

Supply sources of natural gas (m m^3)

	H1 2012
Imports	5,761.5
Domestic production	2,163.5
Domestic suppliers	69.2
Total	7,994.2

Chapter II: Company's Governing Bodies

1. Management Board

As at January 1st 2012, the composition of the PGNiG Management Board was as follows:

- Radosław Dudziński – Vice-President, Strategy
- Sławomir Hinc – Vice-President, Finance
- Marek Karabuła – Vice-President, Petroleum Mining
- Mirosław Szkałuba – Vice-President.

At its meeting on March 7th 2012, the Supervisory Board appointed Ms Grażyna Piotrowska-Oliwa to the position of President of the PGNiG Management Board, with effect as of March 19th 2012, for the joint term of office expiring on March 13th 2014.

On May 11th 2012, Mr Marek Karabuła resigned from his position as member of the PGNiG Management Board. The reason for the resignation was his appointment to the position of President of the Management Board of POGC Libya B.V.

As at June 30th 2012, the composition of the PGNiG Management Board was as follows:

- Grażyna Piotrowska-Oliwa – CEO and President of the Management Board
- Radosław Dudziński – Vice-President, Trade
- Sławomir Hinc – Vice-President, Finance
- Mirosław Szkałuba – Vice-President, Procurement and IT

2. Supervisory Board

As at January 1st 2012, the composition of the PGNiG Supervisory Board was as follows:

- Stanisław Rychlicki – Chairman of the Supervisory Board
- Marcin Moryń – Deputy Chairman of the Supervisory Board
- Mieczysław Kawecki – Secretary of the Supervisory Board
- Grzegorz Banaszek – Member of the Supervisory Board
- Agnieszka Chmielarz – Member of the Supervisory Board
- Mieczysław Puławski – Member of the Supervisory Board
- Jolanta Siergiej – Member of the Supervisory Board

On January 5th 2012, Mr Stanisław Rychlicki, Chairman of the Supervisory Board, tendered his resignation from the position with effect as of January 10th 2012.

On January 12th 2012, the Extraordinary General Meeting of PGNiG SA removed Mr Grzegorz Banaszek from the Supervisory Board and appointed Mr Wojciech Chmielewski to serve on the PGNiG Supervisory Board. Also on January 12th 2012, the Minister of State Treasury, acting in consultation with the Minister of Economy, appointed Mr Janusz Pilitowski to serve on the PGNiG Supervisory Board.

On January 13th 2012, the PGNiG Supervisory Board appointed Mr Wojciech Chmielewski as its Chairman.

On March 19th 2012, the Extraordinary General Meeting of PGNiG SA appointed Ms Ewa Sibrecht-Ośka to the Supervisory Board.

As at June 30th 2012, the composition of the PGNiG Supervisory Board was as follows:

- Wojciech Chmielewski – Chairman of the Supervisory Board
- Marcin Moryń – Deputy Chairman of the Supervisory Board
- Mieczysław Kawecki – Secretary of the Supervisory Board
- Agnieszka Chmielarz – Member of the Supervisory Board
- Józef Głowacki – Member of the Supervisory Board
- Janusz Pilitowski – Member of the Supervisory Board
- Mieczysław Puławski – Member of the Supervisory Board
- Ewa Sibrecht-Ośka – Member of the Supervisory Board
- Jolanta Siergiej – Member of the Supervisory Board

Chapter III: Shareholder Structure

As at June 30th 2012, the share capital of PGNiG SA amounted to PLN 5,900,000,000 and was divided into 5,900,000,000 shares with a par value of PLN 1 per share. The State Treasury was the only shareholder directly holding a large block of PGNiG shares. The shares of all series, that is Series A, A1 and B, were ordinary bearer shares and each share conferred the right to one vote at the General Meeting. The shareholder structure as at June 30th 2012 is presented in the table below:

Shareholder structure

Shareholder	Number of shares as at Jun 30 2012	% of share capital held as at Jun 30 2012	Number of votes conferred by shares held	% of total vote at GM as at Jun 30 2012
State Treasury	4,271,911,724	72.40%	4,271,911,724	72.40%
Other shareholders	1,628,088,276	27.60%	1,628,088,276	27.60%
Total	5,900,000,000	100.00%	5,900,000,000	100.00%

As at June 30th 2012, 728,088,275 shares in PGNiG SA were delivered to eligible employees or their heirs. The shares represented 97.1% of the pool of shares available to be acquired free of charge by eligible persons.

PGNiG shares and shares in PGNiG SA's related entities held by management and supervisory personnel

The table below presents PGNiG shares held by the management and supervisory personnel as at June 30th 2012.

PGNiG shares held by the management and supervisory personnel

Name	Position	Number of shares	Par value of shares (PLN)
Mirosław Szkałuba	Vice-President of the Management Board	9,425	9,425
Mieczysław Kawecki	Secretary of the Supervisory Board	19,500	19,500
Jolanta Siergiej	Member of the Supervisory Board	9,425	9,425

Chapter IV: Regulatory Environment

1. Licences

As at June 30th 2012, PGNiG SA held the following licences granted by the President of the Polish Energy Regulatory Office under the Energy Law:

- one licence to trade in gas fuels
- one licence to trade in natural gas with foreign partners
- one licence to trade in liquid fuels
- one licence to produce electricity
- one licence to trade in electricity.

By virtue of a decision issued by the President of the Energy Regulatory Office at the request of PGNiG SA on March 16th 2012, the Company's licence to store store gas fuel was changed to include "gas fuel storage in storage facilities". The President of the Energy Regulatory Office also approved the changes in the working storage capacities of the Strachocina Underground Gas Storage Facility, the Wierzchowice Underground Gas Storage Facility and the Mogilno Cavern Underground Gas Storage Facility following their expansion; and of the Husów Underground Gas Storage Facility for technological reasons.

On May 16th 2012 the President of the Energy Regulatory Office granted a licence authorising Operator Systemu Magazynowania Sp. z o.o. to store gas fuel in storage facilities, valid from June 1st 2012 to May 31st 2022. In light of the above, by way of a decision of May 29th 2012 the President of the Energy Regulatory Office revoked as of May 31st 2012 PGNiG's licence to store gas fuels in storage facilities.

As at June 30th 2012, PGNiG SA held the following licences, granted under the Polish Geological and Mining Law:

- 96 licences to explore for and appraise crude oil and natural gas deposits
- 1 licence to appraise a salt deposit
- 225 licences to produce crude oil and natural gas from deposits
- 9 licences to store gas in underground facilities (underground gas storage facilities)
- 3 licences to store waste.

2. Changes in PGNiG SA's Tariffs

Until March 30th 2012, the Gas Fuel Tariff (Part A – Gas Fuel Supply Tariff No. 4/2011) approved by the President of the Energy Regulatory Office on June 30th 2011 was used in settlements with customers.

By virtue of a decision of January 11th 2012, the President of the Energy Regulatory Office refused to change the Gas Fuel Tariff (Part A – Gas Fuel Supply Tariff No. 4/2011) with respect to gas fuel prices, which was to be applied in settlements with customers from November 15th to December 31st 2011.

By virtue of a decision of March 16th 2012, issued following a request of PGNiG SA dated October 25th 2011, the President of the Energy Regulatory Office approved the Gas Fuel Tariff (Part A – Gas Fuel Supply Tariff No. 5/2012) which, in line with the request by PGNiG SA, was to be applied in settlements with customers from January 1st to March 31st 2012. The tariff became effective as of March 31st 2012 and, pursuant to the decision of the President of the Energy Regulatory Office, it continues in force until December 31st 2012. On average, the prices and charge rates for the supply of high-methane gas type E, and nitrogen-rich gas types Lw and Ls were increased by 12.5%, 12.6% and 11.3%, respectively.

On June 15th 2012, PGNiG SA applied to the President of the Energy Regulatory Office requesting a change to the Gas Fuel Tariff (Part A – Gas Fuel Supply Tariff No. 5/2012). As at the date of this Report, the tariff proceedings were pending.

The following tables present the average tariffs (PLN/m^3) used in settlements with customers purchasing gas fuels, by fuel type and place of receipt.

Area covered by Dolnośląska Spółka Gazownictwa Sp. z o.o.

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
W-1	2.5779	2.7648	7.3%
W-2	2.0167	2.2036	9.3%
W-3	1.8340	2.0209	10.2%
W-4	1.7036	1.8905	11.0%
W-5 - W-7C	1.5629	1.7507	12.0%
W-8A - W-10C	1.3185	1.5063	14.2%

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
S-1	1.8537	2.0010	7.9%
S-2	1.4415	1.5888	10.2%
S-3	1.3152	1.4625	11.2%
S-4	1.1911	1.3384	12.4%
S-5 - S-7B	1.1225	1.2677	12.9%
S-8 - S-10	1.0113	1.1566	14.4%

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
Z-1	1.4575	1.5830	8.6%
Z-2	1.3255	1.4510	9.5%
Z-3	1.1749	1.3004	10.7%
Z-4	1.0954	1.2209	11.5%
Z-5 - Z-7B	1.0825	1.2088	11.7%

Area covered by Górnośląska Spółka Gazownictwa Sp. z o.o.

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
W-1	2.5468	2.7337	7.3%
W-2	2.0803	2.2672	9.0%
W-3	1.8014	1.9883	10.4%
W-4	1.7314	1.9183	10.8%
W-5 - W-7C	1.5854	1.7732	11.8%
W-8A - W-11C	1.3243	1.5121	14.2%

Area covered by Karpacka Spółka Gazownictwa Sp. z o.o.

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
W-1	2.4284	2.6153	7.7%
W-2	1.9928	2.1797	9.4%
W-3	1.7450	1.9319	10.7%
W-4	1.6960	1.8829	11.0%
W-5 - W-7C	1.5918	1.7796	11.8%
W-8A - W-10C	1.2933	1.4811	14.5%

Area covered by Mazowiecka Spółka Gazownictwa Sp. z o.o.

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
W-1	2.8082	2.9951	6.7%
W-2	1.9019	2.0888	9.8%
W-3	1.7044	1.8913	11.0%
W-4	1.6918	1.8787	11.0%
W-5 - W-7C	1.5658	1.7536	12.0%
W-8A - W-10C	1.2341	1.4219	15.2%

Area covered by Pomorska Spółka Gazownictwa Sp. z o.o.

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
W-1	2.6499	2.8368	7.1%
W-2	2.0396	2.2265	9.2%
W-3	1.8144	2.0013	10.3%
W-4	1.7530	1.9399	10.7%
W-5 - W-7C	1.6114	1.7992	11.7%
W-8A - W-10C	1.3075	1.4953	14.4%

Area covered by Wielkopolska Spółka Gazownictwa Sp. z o.o.

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
W-1	2.6742	2.8611	7.0%
W-2	1.9479	2.1348	9.6%
W-3	1.8085	1.9954	10.3%
W-4	1.7181	1.9050	10.9%
W-5 - W-7C	1.5291	1.7169	12.3%
W-8A - W-10C	1.2698	1.4576	14.8%

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
S-1	1.8642	2.0115	7.9%
S-2	1.4032	1.5505	10.5%
S-3	1.2723	1.4196	11.6%
S-4	1.1974	1.3447	12.3%
S-5 - S-7B	1.1246	1.2699	12.9%
S-8 - S-10	-	-	

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
Z-1	1.6976	1.8231	7.4%
Z-2	1.2649	1.3904	9.9%
Z-3	1.1314	1.2569	11.1%
Z-4	1.0645	1.1900	11.8%
Z-5 - Z-7B	1.0184	1.1446	12.4%

Customers connected to the transmission grid of OGP GAZ-SYSTEM S.A.

Tariff group	Tariff No. 4/2011	Tariff No. 5/2012	Change (%)
	1	2	2/1
E-1A - E-2C	1.1818	1.3700	15.9%
Lw-1 - Lw-2	0.9130	1.0583	15.9%
Ls-1 - Ls-2	0.7564	0.8827	16.7%

On January 13th 2012, PGNiG SA applied to the President of the Energy Regulatory Office requesting approval of a new Gas Fuel Storage Services Tariff (Part B – Gas Fuel Storage Services Tariff No. 1/2012), which would be effective in settlements with customers from April 1st 2012 to Match 31st 2013. The tariff submitted for approval takes into account the change in storage charge rates relating to the expected commissioning of new storage capacities (180m m^3 in the Strachocina Underground Gas Storage Facility and 34m m^3 in the Mogilno Cavern Underground Gas Storage Facility). On April 13th 2012 the President of the Energy Regulatory Office approved the proposed Tariff, to be effective until March 31st 2013.

On June 15th 2012 the President of the Energy Regulatory Office approved the Gas Fuel Storage Services Tariff No. 1/2012 for Operator Systemu Magazynowania Sp. z o.o. The Tariff became effective as of July 1st 2012 and will continue in force until May 31st 2013. The OSM Tariff replaced the PGNiG Gas Fuel Storage Services Tariff (Part B – Gas Fuel Storage Services Tariff No. 1/2012) in settlements with customers for gas fuel storage services.

3. Changes in tariffs of Gas Distribution Companies

By virtue of decisions of June 30th 2011, the President of the Energy Regulatory Office approved Tariffs for Gas Fuel Distribution Services for the Gas Distribution Companies; the tariffs have been applied in settlements with customers since July 15th 2011.

By virtue of a decision of January 9th 2012, the President of the Energy Regulatory Office approved a change in the Tariff for Gas Fuel Distribution Services for Pomorska Spółka Gazownictwa Sp. z o.o. The change consisted replacing the previous W-9 service group with two new groups: W-9A and W-9B.

By virtue of a decision of March 16th 2012, the President of the Energy Regulatory Office approved a change in the Tariff for Gas Fuel Distribution Services for Mazowiecka Spółka Gazownictwa Sp. z o.o. The change extends the scope of the Tariff to include LNG regasification services.

4. Regulatory risks

Polish Energy Law

In H1 2012, work was under way on a set of three acts which are to regulate the energy sector, i.e. the Gas Law, the Energy Law and the Law on Renewable Energy Sources. Work also continues on amending the Regulation of the Minister of Economy on detailed rules for determining and calculating tariffs for gas fuels and on settlement of transactions in gas fuels trading (the Tariff Regulation).

Changes of laws and delays in amending legal acts create risks stemming chiefly from uncertainty as to the final scope of the regulatory changes and short time for adaptation to such changes, which might adversely affect the financial performance and growth prospects of PGNiG SA.

Energy Efficiency Act

The Energy Efficiency Act came into force on August 11th 2011. The Act implements Directive 2006/32/EC of the European Parliament and of the Council of April 5th 2006 on energy end-use efficiency and energy services. The Energy Efficiency Act establishes a national target for economical energy use, according to which savings of end-use energy until 2016 should be no less than 9% of the annual national consumption of energy. In line with the provisions of the new act, PGNiG SA, as a trading company, is required to purchase energy efficiency certificates or, alternatively, to pay the non-compliance penalty. This will drive up the cost of regulated activities and, consequently, inflate the price paid for gas by customers.

Tariff calculation

PGNiG SA's ability to cover the costs of its core operations depends on prices and charge rates approved by the President of the Energy Regulatory Office. When approving tariffs for a given period, the President of the Energy Regulatory Office takes into consideration external factors which are beyond PGNiG SA's control. In an attempt to protect customers, the President of the Energy Regulatory Office may consider certain business costs as unjustified. Moreover, the President of the Energy Regulatory Office does not always agree the assumptions made by PGNiG SA with respect to the main cost drivers and profit targets allowing for business risk. Consequently, the Energy Regulatory Office frequently refuses to approve tariff prices and charge rates applied for by PGNiG SA. Lower tariff prices and charges might adversely affect PGNiG SA's profitability.

In 2012, the President of the Energy Regulatory Office again unilaterally extended tariff's effective term (as was the case in previous tariff proceedings). The Company is of the opinion that such actions by the President of the Energy Regulatory Office create a risk of a tariff being calculated below costs, as it does not account for the cost of supply of gas fuel to customers in the period by which the tariff effective term is extended by the President of the Energy Regulatory Office. As a result, it should be expected that in the next round of tariff approval proceedings this factor may be taken into consideration in the tariff calculation. Further, the President of the Energy Regulatory Office protracts tariff proceedings; consequently, a new tariff takes effect later than originally applied for by PGNiG SA. It was only on March 16th 2012 that Gas Fuel Supply Tariff No. 5/2012 was approved, while the Company had submitted the relevant application on October 25th 2011.

Demand for natural gas

The current methodology for calculation of prices and charge rates is based on demand forecasts; accordingly, revenue is exposed to forecasting risk. Inaccurate estimates of demand, affecting the accuracy of forecast purchase and supply volumes as well as costs on which the determinations of prices and charge rates are based, may adversely affect the Group's financial performance.

Purchase price of imported gas

Prices of imported gas are denominated in USD or EUR and are based on indexation formulae reflecting the prices of petroleum products. Changes in foreign exchange rates and prices of petroleum products materially affect the cost of imported gas. Material changes in prices of fuels on the international markets affect the prices of imported gas. Any accurate forecast of changes of natural gas prices is encumbered with a high risk of error. There can be no assurance that despite the legal possibility of adjusting prices approved for a tariff term an increase in the price of imported gas may not be fully passed on to customers or the changes in gas selling prices may lag behind the changes in its import prices.

Chapter V: Exploration and Production

1. Exploration

In H1 2012, the PGNiG Group was involved in hydrocarbon exploration and appraisal projects in Poland and abroad; the projects were being executed by the Group acting on its own or in cooperation
with partners. Within its own licence areas, the PGNiG Group performed 10,237 m of exploration and appraisal drilling, including 9,977 m in Poland and 260 m in Denmark. Also, 1,059 km of 2D seismic surveys in Poland and 1,793 km in Egypt, as well as 34 km^2 of 3D seismic surveys (in Poland) were performed as part of the exploration work. The PGNiG Group also cooperated with third parties in their licence areas in Poland and on the Norwegian Continental Shelf.

In H1 2012, the PGNiG Group provided services related to exploration for hydrocarbons, solid raw materials and geothermal water. For third-party customers, the Group performed 50,268 m of drillings, 3,388 km of 2D seismic surveys, and 2,081 km^2 of 3D seismic surveys in search of hydrocarbons. For these customers, the Group also performed well servicing activities such as major remedial treatments, workovers, well abandonment services, and application of enhanced recovery techniques.

1.1. Exploration in Poland

In Poland, drillings were performed in five wells: two exploratory wells, two research boreholes and one worked-over well. Three wells were tested in H1 2012, including two drilled in 2011. The tests confirmed presence of gas in two wells – one exploratory well and one appraisal well. No hydrocarbon flow at commercial rates was recorded from the third well, and the well was subsequently abandoned.

One of the positive wells was a 3,357 m appraisal well Kramarzówka-1 drilled in the Carpathian Foothills in 2011. The well produced a natural gas flow. The drilling of a deep well Dukla-1 in the Carpathians was completed. In the Lublin Province, drilling of a shale gas well Lubycza Królewska-1 commenced, marking the opening of a new shale gas exploration area.

As at June 30th 2011, the Group's recoverable reserves were as follows:
- 91.6bn m^3 of natural gas measured as high-methane equivalent,
- 21.0 m tonnes of crude oil.

<u>Joint ventures in Poland</u>

In H1 2012, PGNiG SA collaborated with other entities in licence areas awarded to PGNiG SA, FX Energy Poland Sp. z o.o., and Aurelian Oil & Gas PLC.

Under licences awarded to PGNiG SA, work continued in the following areas:
- “Płotki” – in cooperation with FX Energy Poland Sp. z o.o.
- “Płotki” – “PTZ” – in cooperation with FX Energy Poland Sp. z o.o. and Calenergy Resources Poland Sp. z o.o.
- “Poznań” – in cooperation with FX Energy Poland Sp. z o.o.
- “Bieszczady” – in cooperation with Eurogas Polska Sp. z o.o. and Energia Bieszczady Sp. z o.o.
- “Sieraków” – in cooperation with Orlen Upstream Sp. z o.o.

Under licences awarded to FX Energy Poland Sp. z o.o., work was conducted in the following areas:

- "Warszawa-Południe" (blocks 234, 235, 254, 255, 274N) – in cooperation with FX Energy Poland Sp. z o.o.
- "Ostrowiec" (blocks 163 and 164) – in cooperation with FX Energy Poland Sp. z o.o.
- "Kutno" – in cooperation with FX Energy Poland Sp. z o.o.

Under licences awarded to Aurelian Oil & Gas PLC, work was performed in the following areas:
- "Karpaty Zachodnie" – in cooperation with Energia Karpaty Zachodnie Sp. z o.o. Sp. k. (a subsidiary of Aurelian Oil & Gas PLC)
- "Karpaty Wschodnie" – in cooperation with Energia Karpaty Wschodnie Sp. z o.o. Sp. k. (a subsidiary of Aurelian Oil & Gas PLC).

In the first half of 2012, production continued from the Roszków field in the "Płotki" area, and from the Zaniemyśl field in the "Płotki" – "PTZ" area.

In the "Poznań" licence area, in H1 2012 gas production continued from the Środa Wielkopolska, Kromolice and Kromolice S fields. Work continued on development of the Winna Góra gas field, and development of the Lisewo field commenced. In the Pławce-2 tight gas exploration borehole preparations were under way to carry out a well stimulation operation. In the Żerków-Pleszew area, processing of the second stage 3D seismic survey data was completed and work began on interpretation of the data. Also, drilling of a 4,075 m deep Komorze-3K borehole commenced. The drilling operation was completed in July 2012; the well will be tested in H2 2012.

In the "Bieszczady" area, 2D field work in the Jaśliska-Baligród zone was completed. In the Hoczew-Lutowiska area, gravimetric field work and interpretation of the acquired data were completed. Partners in the project were also in discussions on the selection of the optimum procedure for testing the Niebieszczany-1 deep borehole.

In the "Sieraków" area, in H1 2012, after a revision of the scope of exploration work, the Sieraków-3 borehole was sited. The Sieraków-3 borehole will be drilled in H2 2012 instead of the previously planned Sieraków-2 borehole.

In H1 2012, 235 km of 2D seismic was acquired in the "Warszawa-Południe" area. Analytical work continued for the "Ostrowiec" area. In the "Kutno" area, drilling of the Kutno-2 deep exploration borehole continued.

In H1 2012, a prospectivity analysis was carried out in the "Karpaty Zachodnie" area in preparation for the planned future drilling work, and 2D field seismic work in the Bestwina zone commenced. In the "Karpaty Wschodnie" area, the 2D seismic acquired from the Jordanów zone was processed, and its interpretation began.

On July 4th 2012, PGNiG SA entered into a framework agreement concerning shale oil and gas exploration and production in the Wejherowo licence area with four other Polish companies: Tauron Polska Energia S.A., KGHM Polska Miedź S.A., PGE Polska Grupa Energetyczna S.A. and Enea S.A. Under the agreement, joint work will be conducted on a part of the Wejherowo licence area held by PGNiG, and specifically in the Kochanowo, Częstkowo and Tępcz zones, where preliminary surveys and analyses have confirmed the presence of unconventional gas. The joint effort will cover about 160 km^2 in the Wejherowo licence area. Expenditure on the Kochanowo-Częstkowo-Tępcz (KCT) project is estimated at up to PLN 1.7bn. PGNiG SA will be the licence operator throughout the exploration and appraisal phase.

1.2. Exploration abroad

Pakistan

The PGNiG Group conducts exploration work in Pakistan under an agreement on hydrocarbon exploration and production in the Kirthar licence area executed between PGNiG SA and the government of Pakistan on May 18th 2005. Work in the Kirthar block is conducted jointly with Pakistan Petroleum Ltd., with production and expenses shared proportionately to the parties' interests in the licence: PGNiG SA (operator) – 70%, PPL – 30%. In H1 2012, workover of the Hallel-1 borehole was completed, as was the drilling of the horizontal Hallel-X1 borehole, where gas flow was obtained. Additional interpretation of 3D seismic data confirmed the presence of potential deposits in the northern part of the licence area. On July 6th 2012, the Directorate General of Petroleum Concessions (the Pakistani concession authority) classified the Rehman field as unconventional (tight gas). As a result, the interest holders can raise gas prices by 50% relative to the price of gas produced form conventional reserves. For H2 2012, work is scheduled to commence on construction of a piping system necessary to run a joint production test on the Rehman-1 and Hallel-X1 wells.

Denmark

Since the execution of the agreement on assignment of interests in 2007, the PGNiG Group has conducted exploratory work in the 1/05 licence area in Denmark. Currently, the licence interests are: PGNiG SA (operator) – 80%, Nordsøfonden – 20%. Drilling of the Felsted-1 exploration well was completed in the early 2012. As no hydrocarbon flow at commercial rates had been obtained, the well was abandoned. However, the abandonment procedure proved ineffective. To repeat the abandonment procedure, PGNiG SA obtained a consent from the Danish Energy Agency to extending the licence's term. The Company plans to abandon the licence area by the end of 2012.

Egypt

In Egypt, the PGNiG Group conducts exploration work in the Bahariya licence area (Block 3) under an Exploration and Production Sharing Agreement (EPSA) with the government of Egypt of May 17th 2009. The Company holds a 100% interest in the licence. In H1 2012, the seismic 2D field work was completed and the processing of the seismic data commenced. By the end of H1 2012, 2,300 km of 2D seismic data was acquired. Plans for H2 2012 include completion of the processing and interpretation of 2D seismic data and commencement of drilling of an exploratory well.

Norway

PGNiG Norway AS, a PGNiG company, holds interests in twelve exploratory and production licences on the Norwegian Continental Shelf, in the Norwegian Sea. Jointly with its partners, the company develops the Skarv, Snadd and Idun fields. PGNiG Norway AS holds a 12% interest in the deposits; other interest holders are British Petroleum (operator, 24%), Statoil (36%) and E.ON Ruhrgas (28%). The company has been pre-qualified by the Norwegian authorities as an operator.

In H1 2012, finishing work and technical acceptance procedure was carried out on the FPSO platform anchored in the Norwegian Sea. The platform, which was built in South Korea, is the largest FPSO vessel in the world, able to operate in rough weather conditions. Its hull is 292 metres long and 51 metres wide. The load capacity of the FPSO platform is 140 thousand m^3 (880 thousand barrels), while the expected load capacity of the shuttle tankers operating on the Skarv field will amount to approx. 135 thousand m^3 (850 thousand barrels).

In H1 2012, installation of all 13 risers to the FPSO platform was completed. Rough weather conditions delayed the process. Accordingly, the launch of production was postponed until Q4 2012.

In H1 2012, the Company also carried out exploration work in the PL350, PL212E and PL558 licences. The work in the PL212E licence resulted in the discovery of the Snadd Outer field.

In H1 2012, following the conclusion of the licencing round, PGNiG Norway AS acquired:

- a 50% interest in and the direct operatorship of licence PL648S,
- a 20% interest in licence PL646, the direct operatorship of which was awarded to Wintershall Norge AS (40% interest),
- a 30% interest in licence PL350B, the direct operatorship of which was awarded to E.ON Ruhrgas Norge AS (40% interest).

Libya

Polish Oil and Gas Company - Libya B.V., a PGNiG company, conducts exploration work in the area of licence No. 113, located in the Murzuq petroleum basin in Libya. In H1 2012, the company commenced preparations to resuming performance of the Exploration and Production Sharing Agreement (EPSA), suspended in 2011 after the outbreak of the civil war in Libya. The Tripoli office resumed operations and commenced implementation of safety procedures.

The company have taken steps to officially declare the cessation of the force majeure event, which is a precondition for the extension of the exploration phase under the EPSA. Pre-war approvals for drilling of two wells (including one conditional approval) have expired. The company has applied for the renewal of the pre-war approvals and for approvals for drilling of the other two wells. The approvals may officially be granted only after the force majeure event is declared to have ceased. In H2 2012, the performance of the EPSA having been resumed, the company plans to drill one exploratory well and commence drilling another one, ad to start the second phase of 3D seismic survey. If the wells prove positive, POGC-Libya B.V. intends to commence appraisal work.

1.3. Exploration services

In H1 2012, companies of the Exploration and Production segment were engaged in drilling exploration, appraisal, research and production boreholes. Drilling operations were conducted in search for conventional and non-conventional hydrocarbons and for other mineral resources; the services were rendered mainly for external clients. On the domestic market, drillings for non-PGNiG clients were performed for companies engaged in exploration for non-conventional gas, including Talisman Energy Polska Sp. z o.o. and Chevron Polska Energy Resources Sp. z o.o. (shale gas). As part of conventional hydrocarbon exploration campaigns drilling services were provided to FX Energy Poland Sp. z o.o. and Energia Torzym Sp. z o.o. Other drilling work performed by the PGNiG Group companies included boreholes for KGHM Polska Miedź S.A. in the copper ore licence area, for NWR Karbonia Sp. z o.o. in search for coal, and for Dart Energy in search for coalbed methane; a geothermal well for Termo-Glob Sp. z o.o., and water draining boreholes for the KWB Bełchatów lignite mine. Outside of Poland, the PGNiG Group conducted drilling operations mainly in Asia (Kazakhstan, India, Pakistan), Europe (Germany, Austria, Ukraine, Czech Republic, Denmark, Lithuania, Spain) and in Africa (Uganda, Egypt, Libya).

The E&P companies also performed specialists well servicing activities consisting in application of enhanced recovery techniques, mud and cementing services, major remedial treatments, workovers and well abandonment services. In Poland, the PGNiG Group was the main customer for well servicing. The following work was performed for non-PGNiG customers: datawell services for FX Energy Poland Sp. z o.o.; production testing, well testing, installation of packers and liners (blowout prevention) for Energia Torzym Sp. z o.o. Sp. k. and Exxonmobil Usługi Sp. z o.o.; packer servicing for Hydro Nafta Sp. z o.o.; cementing and well stimulation work as well as mud-related services for Energia Torzym Sp. z o.o. Sp. k. and KGHM Polska Miedź S.A.; and services involving the use of coiled tubing and nitrogen unit for Energia Zachód Sp. z o.o. Outside of Poland, the companies were mainly involved in well-stimulation treatments, well abandonment and workover operations in the Czech Republic, provision of cementing services in Spain, datawell services in Ukraine, and workover operations in Pakistan, Ukraine and Uganda.

In H1 2012, companies of the Exploration and Production segment provided geophysical services in the area of field seismic work, seismic survey planning, seismic data acquisition, as well as seismic data processing and interpretation. They were also conducted geophysical surveys and performed drilling work for geological purposes. In the Polish market the companies were mainly involved in the provisions of 2D and 3D seismic services for PGNiG SA. Other services rendered to the PGNiG Group included well logging. For third-party clients in Poland, the E&P companies provided mainly 2D field seismic services (FX Energy Poland Sp. z o.o. andbnK Polska Sp. z o.o.). In the foreign markets, field seismic services were also tendered to third-party clients; these services included 2D data acquisition in Egypt, 3D data acquisition in Austria and Germany, and 2D and 3D data acquisition in India.

2. Production

In the first half of 2012, PGNiG SA produced 2.2bn m^3 of natural gas (measured as high-methane gas equivalent) and 217.1 thousand tonnes of crude oil. The table below presents PGNiG SA's production volumes in H1 2012.

Production volumes

		Unit	H1 2012
1	Natural gas, including:	million m^3*	2,163.5
a	high-methane gas, including:	million m^3	807.9
	- Zielona Góra Branch	million m^3	0
	- Sanok Branch	million m^3	807.9
b	nitrogen-rich gas, including:	million m^3*	1,355.6
	- Zielona Góra Branch	million m^3*	1,317.2
	- Sanok Branch	million m^3*	38.4
2	Crude oil	thousand tonnes	217.1
	- Zielona Góra Branch	thousand tonnes	193.5
	- Sanok Branch	thousand tonnes	23.6

* Measured as high-methane gas equivalent.

In the area covered by the Sanok Branch, the Rylowa i Rajsko fields came on stream and a new well was hooked up in the Zagorzyce field, where production is already under way. The total addition to gas production capacity from the newly hooked-up wells is approximately 7.5 thousand m^3 of gas per hour (measured as high-methane gas equivalent). No new wells were hooked up in the area covered by the Zielona Góra Branch.

In H1 2012, eight major repairs were performed to restore technological efficiency of producing wells. Thirty-eight well treatment operations (including well stimulations) were carried out to maintain or improve production capacities of producing wells or to restore technological efficiency of in-well extraction equipment.

The PGNiG Group processes crude oil and natural gas to obtain commercial products. The table below presents volumes of natural gas (including LNG) sold directly from the fields, and volumes of crude oil and other products sold to third-party customers. The largest amounts of natural gas were sold to industrial customers, which accounted for 85% of the total sales volume.

Sales of key products

		Unit	H1 2012
1	Natural gas, including:	million m^3	365.4
	- high-methane gas	million m^3	35.6
	- nitrogen-rich gas*	million m^3	329.8
2	Crude oil	thousand tonnes	221.5
3	Condensate	thousand tonnes	1.4
4	Helium	million m^3	1.7
5	Propane-butane	thousand tonnes	10.2
6	Nitrogen	thousand kilograms	227.4
7	Sulphur	thousand tonnes	11.8

*Measured as high-methane gas equivalent.

In H1 2012, PGNiG SA continued to sell crude oil to Rafineria Trzebinia S.A. and TOTSA TOTAL OIL TRADING S.A. under the agreements executed in 2009, and to Rafineria Nafty Jedlicze S.A. under a ten-year contract executed in 2007.

PGNiG Group's foreign customers accounted for 43% of the total volume of crude sales, and for 71% of helium sales. Crude oil was sold to a German refinery (through the Druzhba pipeline), while most of helium was sold in liquid form to foreign wholesale customers, who resell the product in the EU countries.

Underground gas storage facilities (Exploration and Production)

In H1 2012, the Exploration and Production segment used the working capacities of the Daszewo and Bonikowo nitrogen-rich gas storage facilities. Storage capacities used to meet the needs of the Production segment are not storage facilities within the meaning of the Polish Energy Law. The principal role of the underground gas storage facilities is to manage volumes of gas produced in periods of lower demand for the product. The table below presents working capacities of the underground storage facilities used by the Exploration and Production segment as at June 30th 2012.

Working capacities of the underground storage facilities used by the Exploration and Production segment (m m^3)

	Jun 30 2012
Daszewo UGSF (gas type Ls)	30.0
Bonikowo UGSF (gas type Lw)	200.0
Total	230.0

3. Planned activities

Exploration in Poland

In H2 2012, the PGNiG Group plans to conduct geophysical work and drilling operations as part of exploration work in Poland on a few dozen of prospects in the Carpathian Mountains, Carpathian Foothills and the Polish Lowlands. These operations will be carried out by PGNiG SA on its own and in cooperation with foreign partners. As part of these activities, PGNiG SA also intends to pursue projects focused on exploring new potential in the area of unconventional reserves (shale oil/gas and tight gas), where little appraisal has so far been made. In Pomerania, the Company plans to drill the Lubocino-2h well as part of the drilling campaign covering the Lubocino structure. In the Lublin Province, there are plans to continue drilling the Lubycza Królewska-1 well. In Carpathian Mountains, formation testing is to be performed in the Dukla-1 well. In Pomerania, a fracturing operation is planned to be carried out in the Piaski-3 well, and two new wells - Opalino-2 and Kochanowo-1 - are to be drilled.

Exploration abroad

In the second half of 2012 the PGNiG Group plans to continue its operations in Pakistan and Egypt. The Group intends to withdraw from Denmark by the end of 2012. In Libya, performance of the EPSA is to be resumed. In Norway, the PGNiG Group plans to commence production from the Skarv field, and to conduct exploration work in other licence areas.

Exploration services

In H2 2012 the PGNiG Group will provide drilling services in Lithuania, Ukraine, Georgia, Kazakhstan, Pakistan and Ethiopia. In Poland, drilling work is planned to be performed for the PGNiG Group, as well as for third-party customers, including Chevron Polska Energy Resources Sp. z o.o. (shale gas), Talisman Energy Polska Sp. z o.o. (shale gas), Dart Energy, KWB Bełchatów, FX Energy, and Energia Torzym Sp. z o.o. Sp. k.

Workovers, well stimulation operations, measurement of formation parameters, cementing and well abandonment work is planned for PGNiG SA in Poland and in Denmark, and for foreign customers in Uganda, Czech Republic, Spain and Romania. Geophysical services will be performed for customers in Austria, Germany and Hungary, as well as in Pakistan, India and Egypt. In Poland, the services will be rendered to the PGNiG Group and to third parties, including Wuisent Oil & Gas Sp. z o.o., FX Energy Poland Sp. z o.o. and Sierra Bravo Sp. z o.o.,

Natural gas production

In the entire 2012, the PGNiG Group plans to produce 4.4bn m^3 of natural gas in Poland (measured as equivalent of high-methane gas with calorific value of 39.5 MJ/m^3. In Poland in H2 2012, once the extension of the Kościan node is completed and the newly built Kościan-Szczyglice gas pipeline is placed in service, it will be possible to sell additional quantities of type Lw gas to customers buying gas directly from the fields and to the distribution system. There are also plans to hook up new fields and wells with an aggregate production capacity of approximately 19 thousand m^3 per hour (measured as high methane gas equivalent). In the area covered by the Sanok Branch, the Góra Ropczycka, Wola Rokietnicka and Lubliniec fields will come on stream, and new wells will be hooked up in producing fields, including Rudka, Pruchnik, Mirocin and Cierpisz. In the area of the Zielona Górza Branch, two wells in producing fields (Bogdaj-Uciechów and Jarocin) are planned to be hooked up. A new well in the Winna Góra field is planned to be connected to the system (in cooperation with FX Energy Poland Sp. z o.o.).

In H2 2012, the PGNiG Group will commence production from the Skarv field on the Norwegian Continental Shelf. As launch of production from the Skarv field has been postponed to Q4 2012 following delays in the installation of risers caused by adverse weather conditions, the forecast of oil and gas production from the Norwegian fields, and consequently the production forecast for the entire PGNiG Group, will be given after PGNiG SA has obtained relevant data from the operator of the Skarv field.

Crude oil production

In 2012, after three new wells in the BMB (Barnówko-Mostno-Buszewo) field come on stream in the second half of the year, the PGNiG Group expects to produce ca. 480 thousand tonnes of crude from domestic fields. Oil production forecast for the Skarv field will be determined after PGNiG SA has obtained relevant data from the field operator.

4. Risks related to exploration and production

Resource discoveries and estimates

The main risk inherent in exploration activities is the risk of failure to discover reserves, i.e. the exploration risk. This means that not all the identified potential deposit sites have deposits of hydrocarbons which can qualify as an accumulation. Whether or not a sufficient accumulation exists depends on a number of geological factors. Furthermore, the actual quantity and quality of the accumulated hydrocarbons may differ from estimates. When the results of successful exploration activity, in the form of new reserves, do not offset the production from the existing reserves, PGNiG SA's recoverable reserves will decrease pro rata to the current production volumes.

The reserves estimates and production projections may be erroneous due to imperfections inherent in the equipment and technology, which affect the quality of the acquired information concerning the geological factors and the characteristics of the deposit site. Irrespective of the methods applied, data on the volume and quality of commercial reserves of crude oil and natural gas is always an estimate. Actual production, income and expenses relating to a given deposit may significantly differ from the estimates. The weight of this risk is further increased by the fact that in the full business cycle the period from the commencement of exploration to the launch of production from a developed field takes six to eight years, while the production lasts from 10 to 40 years. Formation characteristics determined at the stage of preparing the relevant documentation are reviewed after production starts. Each downgrade of the size of the reserves or production quantities may lead to a lower revenue and adversely affect PGNiG SA's financial performance.

Exploration for unconventional gas

The risk associated with exploration for unconventional gas in Poland relates to the lack of confirmed presence of shale gas and tight gas. Furthermore, even if existence of in-place petroleum is confirmed, its production may prove uneconomic due to insufficient gas recovery and high investment expenditure necessary on drillings and construction of production infrastructure. Another material factor is connected with difficult access to unconventional gas plays given the environmental regulations and the necessity to obtain the landowners' consent **for access to the area.**

Competition

Both on the Polish market and abroad there is a risk of competition from other companies in the area of acquisition of licences for exploration for and appraisal of hydrocarbon deposits. Certain competitors of PGNiG SA, especially those active globally, enjoy strong market positions and have financial resources larger than those of PGNiG SA. Thus, it is probable that such companies would submit their bids in tender procedures and be able to acquire promising licences, offering better terms than PGNiG SA could offer given its financial and human resources. This competitive advantage is particularly important on the international market.

Delayed work

Under the applicable Polish legal regulations, obtaining a licence for exploration for and appraisal of crude oil and natural gas deposits lasts from one to one and a half years. On foreign markets, such procedures may take even two years from the time that the winning bid is awarded in a tender for licence until the relevant contract is ratified. Moreover, prior to the commencement of field work, the Company is required to make a number of arrangements, including obtaining formal and legal permits and approvals for entering the area, meeting environmental protection-related requirements and, in some cases, requirements related to protection of archaeological sites, and abiding by the regulations governing tenders held to select a contractor, which delays execution of an agreement with a contractor by another few months. In addition, frequently the waiting time for customs clearance of imported equipment is very long. These factors create the risk of delays in the start of exploration work.

Formal and legal hurdles beyond PGNiG SA's control include:
- local governments' failure to approve local zoning plans or amendments to those already approved;
- obstacles in incorporating investment projects into the local zoning plans;
- need to obtain and comply with administrative or other formal and legal decisions, including environmental decisions or building permits;
- amendments to the current investment project;
- obstacles in obtaining permission from land owners to enter the site.

These factors significantly delay implementation of investment projects and commencement of on-site construction work. Concurrently, PGNiG SA's obligation to comply with the Public Procurement Law frequently protracts the tender procedure. Notices of appeal and complaints submitted by bidders lead to lengthy court proceedings and, consequently, to delays in implementing an entire investment project. A protracted investment process exacerbates the risk related to estimation of capital expenditure.

Cost of exploration

Exploratory work is capital intensive, given the prices of energy carriers and materials. Cost of exploratory work is especially sensitive to steel prices, which are passed onto prices of casing pipes and lifting casing used in drilling. An increase in prices of energy and materials translates into an increase in the cost of exploratory work. Moreover, profitability of foreign exploration projects to a significant extent depends on the prices of oil derivative products and on exchange rates. In order to reduce costs of drilling work, PGNiG SA applies the Daily Rate system in selecting drilling contractors.

Safety, environmental protection and health regulations

Ensuring compliance with environmental laws in Poland and abroad may significantly increase PGNiG SA's operating expenses. Currently, PGNiG SA incurs significant capital expenditure and costs on ensuring compliance of its operations with ever more complex and stringent regulations concerning safety and health at work, as well as environmental protection. The Act of May 18th 2005 amending the Natural Environment Protection Law and Certain Other Acts (Dz.U. No. 113, item 954 of June 27th 2005) rendered the regulations governing the execution of projects which might affect the Natura 2000 sites more stringent and enhanced the environmental protection-related requirements with regard to entering the areas of the occurrence of protected plant species and habitats of protected animals. Trends to implement increasingly more stringent environmental protection regulations are seen also in other countries where PGNiG SA conducts exploration operations.

Qualified personnel

The presence of foreign companies on the Polish market has intensified competition for highly qualified employees with extensive professional experience. This risk of losing experienced personnel is especially high with respect to oil and gas exploration professionals. In countries where PGNiG SA operates, highly qualified staff is difficult to recruit.

Unpredictable events

Hydrocarbon deposits developed by PGNiG SA are usually located at great depth, which involves extremely high pressures and, in many cases, presence of hydrogen sulphide. Consequently, there the risk of hydrocarbon blowout or leakage is very high, which in turn may pose a threat to people (workers and local population), natural environment and production equipment.

Changes in laws and regulations

The laws and regulations in some countries change frequently and unexpectedly, causing problems to entities involved in exploration activity. This problem may be particularly acute in countries where changes in law depend on decisions made by authoritarian governments.

Political and economic situation

In some countries where PGNiG SA conducts exploration activities there is a risk of armed conflicts or terrorist attacks, which may lead to a limitation, suspension or discontinuation of the exploration and production activities.

Some regions of the world where PGNiG SA operates are exposed to a risk of social and political unrest. Changes of governments may bring to a halt licensing proceedings before state administration authorities. Additionally, these countries are at risk of internal conflicts and social unrest caused by poor social and demographic conditions. The risks specified above may lead to a limitation, suspension or discontinuation of PGNiG SA's activities.

In certain countries, operations of exploration companies may be hindered by the lack of adequate infrastructure, which may be an obstacle in transporting equipment, personnel and materials to the sites. Problems may also arise in providing supplies and ensuring appropriate health care. These risks may lead to a limitation or suspension of the Company's exploration activities.

Chapter VI: Trade and Storage

1. Purchases

In H1 2011, PGNiG SA imported gas and, to a limited extent, purchased the fuel from domestic suppliers. PGNiG SA imported natural gas mainly under the agreements and contracts specified below, i.e. the long-term contract with OOO Gazprom Export and short- and medium-term gas supply agreements with European suppliers:

- Contract with OOO Gazprom Export for sales of natural gas to the Republic of Poland, dated September 25th 1996, which remains in force until December 31st 2022
- individual transactions for natural gas supplies (using reverse flow) with PGNiG Sales & Trading GmbH
- Individual Agreement with Vitol S.A. for sales of natural gas, dated May 13th 2011, which remains in force until October 1st 2014
- Agreement with VNG-Verbundnetz Gas AG for sales of the Lasów natural gas, dated August 17th 2006, which remains in force until October 1st 2016.

The table below presents the structure of the Group's purchases of natural gas fed to the domestic gas system (measured as high-methane gas equivalent).

Structure of natural gas purchases by supply sources (m m^3)

	H1 2012	%
Imports, including:	5,761.5	98.8%
- Gazprom Export	4,570.1	79.3%
- Other foreign suppliers	1,191.4	20.7%
Domestic suppliers	69.2	1.2%
Total	5,830.7	100.0%

<u>New agreements</u>

In order to reduce natural gas acquisition costs, PGNiG SA executed an agreement with OGP GAZ-SYSTEM S.A. for the provision of virtual reverse services on the Yamal gas pipeline in the period from January 1st 2012 to December 31st 2015.

In H1 2012, PGNiG Sales & Trading GmbH executed short-term contracts for natural gas supply on Germany's energy exchange (EEX) and virtual trading platforms Gaspool and NetConnect Germany. In the period under review, the company supplied approximately 510 m m^3 of natural gas to PGNiG SA using the virtual reverse service.

On March 19th 2012, in exercise of its contractual rights, PGNiG SA requested VNG-Verbundnetz Gas AG to lower the price of gas under the Lasów gas sales agreement of August 17th 2006. On March 29th 2012, VNG-Verbundnetz Gas AG requested PGNiG SA to review the pricing terms of the agreement and increase the price of gas. As at the date of this Report, renegotiations of the gas price were pending.

2. Sales

In H1 2012, PGNiG SA executed comprehensive gas fuel supply contracts, both from the transmission system and from the distribution system, with 33.4 thousand new customers.

The key products sold by the Trade and Storage segment are high-methane gas and nitrogen-rich gas. In H1 2012, sales of natural gas rose ca. 4% year on year. The strongest growth was seen in sales to industrial customers, primarily in the oil refining and petrochemical sector. PGNiG SA sold gas on the Polish market. The structure of sales of the PGNiG Trade and Storage segment in H1 2012 is presented in the table below.

Structure of sales of key products

	Unit	H1 2012
Natural gas, including:	m m^3	7,533.6
- high-methane gas	m m^3	7,259.2
- nitrogen-rich gas*	m m^3	274.4
Propane-butane	thousand tonnes	0.6

* Measured as high-methane gas equivalent.

Gas was purchased primarily by industrial customers (mainly from the chemical, oil refining, petrochemical and metallurgical sectors) as well as households. Households made up the largest group of customers purchasing natural gas, accounting for 97% of the entire customer base (approximately 6.5m). Their share in the total volume of gas sales increased by 4.5% year on year. Industrial customers had the largest share in the sales volume, with sales to this group having grown by 4.6% on H1 2011. The table below presents the structure of sales of natural gas (measured as high-methane gas equivalent) by customer groups.

Sales of natural gas through the national grid (m m^3)

	H1 2012	%
Industrial customers	4,275.2	56.7%
Trade and services	925.1	12.3%
Households	2,213.4	29.4%
Wholesale customers	119.9	1.6%
Total	7,533.6	100.0%

In the first half of 2012, PGNiG SA continued a gas distribution project consisting in LNG distribution of gas fuel to Ełk and Olecko. This project is a part of an initiative to switch Pisz, Ełk, Suwałki and Olecko to high-methane gas (the PESO project). The project involves construction of an LNG regasification station and two-step pressure reduction and odorising stations in Ełk and Olecko, and switching customers in Ełk and Olecko to high-methane gas. The construction work is set for completion by the end of 2013. On June 29th 2012 an agreement was signed for co-financing of the project with EU funds under the Infrastructure and Environment Operational Programme.

In H1 2012 the PGNiG Group also traded in energy and carbon allowances on the European Energy Exchange in Leipzig (EEX). Further, the Group commenced:

- trading in energy and carbon allowances at the Polish Power Exchange

- trading in natural gas on the European Energy Exchange in Leipzig (EEX) and virtual trading platforms Gaspool and NetConnet Germany
- selling natural gas to end users in Germany.

3. Storage

The Trade and Storage segment uses for its own needs the working capacities of the Wierzchowice, Husów, Strachocina, Swarzów and Brzeźnica Underground Gas Storage Facilities, as well as the Mogilno Underground Gas Storage Cavern Facility. A part of the working capacity of the Mogilno facility, which is not a storage facility within the meaning of the Polish Energy Law, was made available to OGP GAZ-SYSTEM S.A.

Short-term peak fluctuations in demand for natural gas are balanced out with the supplies from the Mogilno Underground Gas Storage Cavern Facility, where gas is stored in worked-out caverns. The capacities of the Wierzchowice, Husów, Strachocina, Swarzów and Brzeźnica Underground Gas Storage Facilities are used to minimise the effect of changes in demand for natural gas in the summer and winter seasons, to meet the obligations under the take-or-pay import contracts, to ensure the continuity and security of natural gas supplies and to meet the obligations under agreements providing for the delivery of natural gas to customers' premises.

In addition, the capacities of the Wierzchowice, Husów and Mogilno facilities are used by the Group to meet its obligation to maintain mandatory stocks, imposed by the Act on Stocks of Crude Oil, Petroleum Products and Natural Gas, as well as on the Rules to be Followed in the Event of Threat to National Fuel Security or Disruptions on the Petroleum Market, dated February 16th 2007.

On May 11th 2012, PGNiG SA and Operator Systemu Magazynowania Sp. z o.o. executed an agreement for exclusive operation of storage facilities and designation of the storage system operator. Execution of such agreement was required under the Polish Energy Law and was a precondition for appointing OSM Sp. z o.o. the storage system operator.

Until May 31st 2012, the function of the storage system operator had been performed by PGNiG SA. By virtue of a decision by the President of the Polish Energy Regulatory Office's of May 22nd 2012, Operator Systemu Magazynownia Sp. z o.o. was appointed the system operator for the period from June 1st 2012 to May 31st 2022. On May 16th 2012 the President of the Polish Energy Regulatory Office granted to OSM Sp. z o.o. a licence to store gas fuel in storage facilities, valid from June 1st 2012 to May 31st 2022.

In order to ensure equal treatment of customers, the storage services are provided based on the Rules of Provision of Storage Services and the Gas Fuel Storage Tariff. The current versions of the Rules and the Gas Fuel Storage Tariff are available at the Storage System Operator's website.

In H1 2012, PGNiG SA completed extension of the Strachocina Underground Gas Storage Facility. The facility's working capacity was increased from 150m m^3 to 330m m^3. PGNiG SA also placed in service one of the caverns of the Mogilno Underground Gas Storage Cavern Facility, which increased the facility's working capacity to 411.9m m^3. Following these extensions, as of May 1st 2012 PGNiG SA made available for third party access additional 214m m^3 of working storage capacity.

As at June 30th 2012, the PGNiG Group made available a total of 1,642.5m m^3 of working storage capacity for third party access and for OGP GAZ-SYSTEM S.A.; of this volume, 1,621m m^3 was made available under long-term agreements and 21.5m m^3 – under short-term agreements. The table below presents storage facilities' working capacities and the working capacities made available to third parties as at June 30th 2012.

	Working capacities (m m^3)	Working capacities made available to third parties (m m^3)
Brzeźnica Underground Gas Storage Facility	65.0	65.0
Husów Underground Gas Storage Facility	350.0	350.0
Mogilno Cavern Underground Gas Storage Facility	411.9	407.5
Strachocina Underground Gas Storage Facility	330.0	330.0
Swarzów Underground Gas Storage Facility	90.0	90.0
Wierzchowice Underground Gas Storage Facility	575.0	400.0
Total	1,821.9	1,642.5

As of July 1st 2012, as part of long-term storage services, the PGNiG Group made available to third parties 173.5m m^3 of working capacity at the Wierzchowice Underground Gas Storage Facility. A further capacity of 1.5m m^3 was made available as of August 1st 2012.

4. Planned activities

Purchases of natural gas

In H2 2012, PGNiG SA will continue to purchase of imported gas under the long-term contract with OOO Gazprom Export and short- and medium-term gas supply agreements with European suppliers. With a view to optimise the costs of gas fuel acquisition, the Company will purchase natural gas through PGNiG Sales & Trading GmbH on the German market, under short-term agreements. The gas will be delivered using the virtual reverse flow service on the Yamal gas pipeline.

Sales of electricity

The PGNiG Group plans to launch activities involving sale of electricity to end customers in Germany. The launch of sales is planned for Q4 2012, as part of the dual fuel offering (sale of gas and power).

Storage

In H2 2012, PGNiG SA will continue work on extending the Mogilno Underground Gas Storage Cavern Facility and the Wierzchowice Underground Gas Storage Facility. The Wierzchowice Underground Gas Storage Facility is to be placed in service in Q4 2012, while first volumes of gas are to be injected and drawn from the facility in the 2013/2014 season. On May 21st 2012, a decision was made to extend the Mogilno Underground Gas Storage Cavern Facility by constructing five new caverns. The Company will also continue construction of the Kosakowo Underground Gas Storage Cavern Facility, designed to store high-methane gas. Completion of the leaching process in the first storage chamber is scheduled for 2013.

5. Risks related to Trade and Storage

Requirement to diversify supplies of imported gas

In 2010, the President of the Energy Regulatory Office imposed a PLN 2m fine on PGNiG SA for breaching the terms of its licence for international trade in natural gas, by failing to comply with the requirement to diversify supplies of imported gas in 2007 and 2008. The maximum share of gas imported from one country in total gas imports in a given year is determined in the Council of Ministers' Regulation of October 24th 2000 on the minimum level of diversification of foreign sources of gas supplies. On January 4th 2011, PGNiG SA filed (through the agency of the President of the Energy Regulatory Office) an appeal against the decision imposing the fine with the Competition and Consumer Protection Court at the Regional Court of Warsaw. The Company challenged in full the decision of the President of the Energy Regulatory Office, citing, among others, breach of the Constitution as well as erroneous interpretation and improper application of the Energy Law. The appeal proceedings are pending. In 2011, the President of the Energy Regulatory Office instigated administrative proceedings to impose a fine on PGNiG SA for its failure to comply with the requirement to diversify supplies of imported gas in 2009. Similar administrative proceedings concerning PGNiG SA's failure to comply with the requirement to diversify supplies of imported gas in 2010 were instituted on May 11th 2012. The 2009 and 2010 proceedings were suspended ex officio until conclusion of the 2007 and 2008 proceedings, held before the Competition and Consumer Protection Court.

In order to avoid similar situations in the future, PGNiG SA submitted an inquiry to the Constitutional Court concerning the compliance of the Council of Ministers' Regulation of October 24th 2000 on the minimum level of diversification of foreign sources of gas supplies with the Polish Constitution.

If the Regulation is not amended, the President of the Energy Regulatory Office may continue imposing fines on the Company for failing to comply with the diversification requirement until gas starts to be supplied from other sources (e.g. through the LNG terminal).

Deregulation of gas prices for customers

PGNiG SA is the largest supplier of natural gas in Poland. Its share in the gas market is estimated at approximately 96%, while the remaining share of 4% is held by suppliers from outside the PGNiG Group which usually purchase gas from PGNiG SA. However, in 2012-2013, major changes are expected to take place on the natural gas market and in its legal environment. In H1 2012, PGNiG SA commenced development of the Gas Release Programme which provides for release of gas prices paid by institutional customers as of January 1st 2013, followed by release of gas prices for households (in 2–3 years time). Additionally, a set of three energy acts, including the Gas Law, is to be enacted in 2012. As a result of the expected changes, the Company's share in the natural gas sales volume may significantly fall to the benefit of the existing as well as new gas trading entities. On the other hand, following the deregulation process, gas prices will be chiefly market-driven.

Storage

Pursuant to the Act on Mandatory Stocks, as of October 1st 2012, the volume of mandatory stocks must be increased from 20 to 30 days of the average annual imports. As a result, there is a risk that the Company will not be able to meet its obligations under the existing gas sales agreements, given that significant storage capacities which will have to be used for storage of the increased mandatory stocks.

The draft Transmission Grid Code (TGC) for the Gas Transmission System Operator is an important factor affecting operations of the Storage System Operator. The Code is based on the assumption that the Storage System Operator will be the only entity qualified to order throughput capacities at the entry points from the underground storage facilities to the transmission system and at the exit points from the transmission system to the underground storage facilities. These changes may result in a significant rise of charges for storage service customers in the Storage System Operator's Tariff, and as a consequence adversely affect the attractiveness of storage services provided by OSM Sp. z o.o. relative to services offered by operators in the neighbouring countries.

Chapter VII: Distribution

1. Operations of the Gas Distribution Companies

In H1 2012, the Gas Distribution Companies focused on transmitting high-methane and nitrogen-rich gas, as well as small amounts of propane-butane and coke-oven gas, over the distribution network. Based on a decision of the President of the Energy Regulatory Office, since mid-2007 the Gas Distribution Companies have had the status of Distribution System Operators.

The Gas Distribution Companies also continued work aimed at extending and modernising the gas network and connecting new customers to the existing network and to new sections of the network. Furthermore, the Gas Distribution Companies continued the replacement of the most failure-prone sections of cast iron piping and the modernisation of gas piping with long operating lives whose continued operation posed a safety hazard and resulted in substantial gas losses.

The key projects carried out as part of gas network extension and modernisation efforts by the Gas Distribution Companies in H1 2012 included:

- continuation of design work related to the upgrade of a 61 km high-pressure gas pipeline from Sandomierz to Ostrowiec Świętokrzyski; the project is scheduled for completion in 2015;
- continuation of design work related to the upgrade of a 37 km high-pressure gas pipeline from Parszów to Kielce; the project is scheduled for completion in 2015;
- continuation of reconstruction of a 20.2 km high-pressure gas pipeline from Warzyce to Gorlice (stages IV and V) in the Skołyszyn and Jasło communes; in H1 2012, construction and assembly work was carried out on Section I in the Skołyszyn commune and Section II in the Jasło commune (a 12 km section of the high-pressure gas pipeline was completed), and design work was performed on Section III covering the city of Jasło;
- continuation of reconstruction of a 12.2 km high-pressure gas pipeline from Tuszyma to Mielec; in H1 2012, approximately 3 km of the gas network and the cathodic protection station with grounding were upgraded;
- continuation of construction (stage 2) of a high-pressure pipeline as part of project "Duplex Supply for the City of Toruń"; the project is designed to ensure gas supplies to the city of Toruń, to industrial customers, to the municipality of Łysomice and commune of Wielka Nieszawka, and to the Pomeranian Special Economic Zone; in H1 2012, the construction of the high-pressure gas pipeline from Ostaszewo to Różankowo continued;
- continuation of construction work for phase 1 of gas network connection to Długołęka, Domaszczyn, Kamień and Szczodre in the Długołęka commune; the project involves construction of a medium-pressure gas pipeline and a pressure reduction station; in H1 2012, work continued on construction of the pipeline from the station in Mirków to the Długołęka ring road, and from Długołęka to Byków;
- connection of Pęgów, Zajączków, Golędzinów, Paniowice in the Oborniki Śląskie commune and Szewce in the Wisznia Mała commune to the gas supply system; the project involves construction of medium-pressure gas pipelines and connections; in H1 2012, project design documents were drafted for the construction of gas pipelines in Pęgów and Zajączków;
- upgrade of a 15 km high-pressure gas pipeline from Piotrków Trybunalski to the Warta river (stage I: Piotrków); construction work commenced in H1 2012;
- continuation of construction of the Błonie commune section of the medium-pressure gas pipeline from Kopytów to Pass; the project is designed to secure gas supplies to customers in the Błonie commune and to increase the volume of gas fuel collected by the largest industrial customer in the area, i.e. the Błonie-Pass Strefa Przemysłowa co-generation plant; the project is scheduled for completion in 2012; the work remaining to complete the project includes: completing the design

documentation for the reconstruction of gas connections and switching the connections to the newly built pipeline;
- construction of a medium-pressure gas-pipeline in Warsaw at ul. Zdziarska, along the eastern bank of Kanał Markowski, and at ul. Wyszkowska and ul. Chudoby along the northern bank of Kanał Markowski; in H1 2012, work continued on the design documentation 3,6;
- continuation of work on the gas network extension to Mieroszów, with the use of the LNG technology; in H1 2012, the construction of a 1.4 km medium-pressure gas pipeline from the LNG station to ul. Hoża in Mieroszów was completed.

The Gas Distribution Companies also worked on network roll-out projects in new areas, for which they concluded agreements for EU co-financing under the Infrastructure and Environment Operational Programme. The key projects included:

- continuation of construction of a high-pressure gas network connecting Szczytno, Młynowo and Muławki near Kętrzyn and distribution network roll-out in the communes; in H1 2012, construction work was carried out on the medium-pressure gas pipeline in Barciany, where a 1.4 km section of the distribution network was completed by the end of June, and on the medium-pressure gas pipeline in Sątopy-Samulewo, where a 2.4 km section of the network was completed, project design documents were drafted for the second phase of construction of the high-pressure gas pipeline from Szczytno to Rybno, the high-pressure gas pipeline from Rybno to Młynowo, the high-pressure gas pipeline from Młynowo to Muławki and the pressure reduction and metering stations in Mikołajki and Muławki near Kętrzyn;
- continuation of construction of the south-eastern gas supply for the city of Gdańsk, and the distribution network roll-out in Wiślinka and Wyspa Sobieszewska; in H1 2012, the projects involving construction of a high-pressure gas pipeline from Kolnik to Gdańsk, construction of a high-pressure gas station for the city of Gdańsk and construction of a high-pressure gas station for Grupa LOTOS S.A. were completed, the design work for distribution network roll-out in Wyspa Sobieszewska was completed and the design documents were drafted for distribution network roll-out in Wiślinka and the Żuławy communes;
- continuation of construction of the DN 300 high-pressure gas network connecting Brodnica, Nowe Miasto Lubawskie and Iława, and the distribution network roll-out; the project involves construction of high-pressure gas pipelines from Brodnica to Nowe Miasto Lubawskie with a pressure reduction station, and from Nowe Miasto Lubawskie to Iława; and construction of medium-pressure gas pipelines in Nowe Miasto Lubawskie and Kurzętniki; in H1 2012, work continued on the design and cost estimate documentation for the high-pressure gas pipeline from Brodnica to Nowe Miasto Lubawskie with a pressure reduction and metering station in Kurzętnik and for the medium-pressure gas pipelines in Nowe Miasto Lubawskie and Kurzętniki;
- continuation of the distribution network roll-out for the municipalities and communes of Blachownia, Herby, Wręczyca Wielka, Kłobuck, Opatów and Krzepice; the project involves construction of (i) an approximately 18 km high-pressure gas pipeline from Blachownia to Kłobuck, with a pressure reduction station, (ii) high- and medium-pressure gas pipelines and two pressure reduction stations for the towns of Herby and Blachownia, and (iii) a 52 km medium-pressure gas pipeline serving Wręczyca Wielka and Kłobuck; in H1 2012, design work continued and building permits were obtained for a construction project in the Krzepice municipality and one of the projects in the Blachownia municipality;
- continuation of the distribution network roll-out in the Włodawa area; the project comprises construction of a 54.8 km high-pressure gas pipeline from Kamień to Włodawa, with a 18.6 km medium-pressure gas network and three pressure reduction stations; the project is scheduled for completion in 2015; in H1 2012, design work, which is nearing completion, continued, and a tender for construction work was called;
- continuation of design work for the planned roll-out of the gas distribution system in the Włoszczowa and Małogoszcz communes; the project comprises construction of a 43.3 km high-pressure gas pipeline with pressure reduction stations, and a 51 km medium-pressure gas pipeline with eight gas governor stations; the project is scheduled for completion in 2015;

- continuation of design work for the planned roll-out of the gas distribution network to industrial and municipal customers and households in the Chęciny and Sitówka communes; the project comprises construction of a 4.5 km high-pressure gas pipeline with a pressure reduction station, and a 67.2 km medium-pressure gas pipeline network with connections and gas governor stations; the project is scheduled for completion in 2015; in H1 2012, a tender for the construction work in stage I one of the project was called;
- continuation of the distribution network roll-out in selected localities in the Strzelin and Wiązów communes, Strzelin county; the project involves construction of high-pressure and medium-pressure gas pipelines with connections, two pressure reduction stations, as well as connections and a pressure reduction station for a key customer; in H1 2012, design documentation was drafted for stage I of the project, i.e. construction of a 1.6 km medium-pressure gas pipeline from the pressure reduction station in Chociwel to Strzelin, and design work was commenced on stages II-VII of the project;
- continuation of the distribution network roll-out in the Prażmów, Tarczyn, Góra Kalwaria and Żabia Wola communes (stage I); the project involves construction of approximately 100 km of medium-pressure gas pipeline and approximately 1,400 connections in 2011-2014; in H1 2012, stage I of the project, i.e. construction of 5.5 km of gas pipeline with connections in Ustanów, Prażmów commune, which is planned to be placed in service in H2 2012, was completed, while design work continued on the remaining tasks under the project;
- continuation of construction of an LNG-based gas supply system in Suwałki; the project involves construction of an LNG regasification station, a 23 km medium-pressure gas pipeline with connections and a pressure reduction station; construction work is scheduled for 2012-2014; in H1 2012, a building permit was obtained and a contractor was selected to perform the construction work on the pressure reduction station; also, design work was carried out on further sections of the medium-pressure gas pipeline network;
- provision of equal access to gas network in the Gorzów Wielkopolski region; the project involves construction of an 11.6 km of high-pressure gas pipeline from Mościszki (Witnica commune) to Osiedle Warniki (Kostrzyn n. Odrą commune), and construction of a 13.2 km medium-pressure gas pipeline with connections in the village of Białcz; in H1 20121, construction and assembly work was carried out on the high-pressure pipeline and design work was performed on the medium-pressure pipeline;
- continuation of the distribution network roll-out in the Komprachcice and Dąbrowa communes; the project involves construction of 62 km of medium-pressure gas pipelines which are planned to be placed in service in 2012-2013; approximately 20 km of gas network was completed by June 30th 2012.

The table below presents the volume of gas transmitted via the distribution network, network's length, number of customers, number of new customers connected to the network and the employment as at June 30th 2012.

Key data on Gas Distribution Companies

	Entity	DSG	GSG	KSG	MSG	PSG	WSG
Volume of gas transmitted via the distribution system	m m^3	540.5	1,006.9	1,112.2	1,212.5	538.3	863.8
Length of network, excl. connections*	km	7,859.3	21,058.2	45,180.1	19,276.0	10,052.3	16,105.2
No. of customers	('000)	750.9	1,306.5	1,450.5	1,519.3	744.0	919.4
No. of new customers connected to the network	('000)	2.8	2.9	4.5	10.1	2.6	2.8
Employment	persons	1,385	2,589	3,259	2,879	1,726	1,804

*Own and third-party networks

2. Planned activities

Major projects to be implemented in H2 2012 include:

- continuation of construction of a high-pressure gas network connecting Szczytno, Młynowo and Muławki near Kętrzyn, and the distribution network roll-out in the communes;
- continuation of construction of the south-eastern gas supply for the city of Gdańsk, and the distribution network roll-out in Wiślinka and Wyspa Sobieszewska;
- continuation of construction of the DN 300 high-pressure gas network connecting Brodnica, Nowe Miasto Lubawskie and Iława, and the distribution network roll-out;
- continuation of design work related to the upgrade of the Sandomierz–Ostrowiec Świętokrzyski and the Parszów–Kielce high-pressure gas pipelines;
- roll-out of the gas network in the Włodawa, Włoszczowa and Małogoszcz regions,
- continuation of work on reconstruction of the high-pressure gas pipelines from Warzyce to Gorlice and from Tuszyma to Mielec;
- continuation of design work as part of the project to connect the municipalities of Herby and Blachownia to the gas grid;
- continuation of construction work in Komprachcice and Dąbrowa;
- roll out of gas distribution systems in the Prażmów, Tarczyn, Góra Kalwaria and Żabia Wola communes.

In the next few years, the Gas Distribution Companies will focus on maintaining their respective market positions and further increasing the volumes of transmitted gas by taking the following measures:

- extending the pipeline infrastructure to reach new customers,
- ensuring adequate transmission capacity and securing sources of gas supply for the gas distribution system,
- replacing socket joint piping and modernising high-, medium- and low-pressure networks,
- introducing new LNG-based gas distribution systems,
- improving the quality of customer service,
- using EU funds to refinance the extension of distribution systems.

3. Risks related to distribution

Direct competition

Liberalisation of the gas market contributes to intensification in competition faced by the Gas Distribution Companies. Companies distributing natural gas progressively expand their gas networks and attract new customers. Additionally, companies have emerged which offer LNG distribution services. The market entry barriers are definitely lower here, as LNG distribution involves significantly lower capital expenditure and does not require a connection to the gas system or adequate reserve capacity to be maintained in the transmission and distribution networks. Another issue which affects the Gas Distribution Companies' competitive position is the tariff policy of the Energy Regulatory Office, which prevents the Gas Distribution Companies from operating a flexible pricing policy for their key customers. With the lack of flexible pricing, the competitors' offerings may prove to be an attractive alternative for the Gas Distribution Companies' customers.

Legislation

The long time required to prepare an investment project is an important factor affecting the Gas Distribution Companies' operations. Complex provisions of the Construction Law and regulations governing implementation of investment projects impose the obligation to prepare extensive project and legal documentation. The process is time-consuming, but indispensable for any investment project.

Substitution

Easy and quick access to alternative energy sources (i.e. fuel oil, LPG, hard coal, electricity or heat generated by central CHP plants, or local or community heat plants) may weaken the position of the Gas Distribution Companies on the local energy markets.

Sources of gas supply for MSG Sp. z o.o.'s distribution system

MSG Sp. z o.o.'s distribution network is connected to the transmission system operated by OGP GAZ-SYSTEM S.A., which is its main source of gas supplies. The geographical distribution of gas supply sources and the topology of domestic transmission networks are unfavourable across a large portion of the company's coverage area. A risk exists that no reserve transmission capacity will be available at the points of entry into the company's distribution system, which may inhibit the development of the gas fuel market in most of the company's area of operation.

Claims raised by property owners

More and more frequently, the Gas Distribution Companies face excessive financial claims raised by owners of land plots where gas network was developed in the past. Under applicable laws, the Gas Distribution Companies do not hold a clear legal title to use the real estate – no transmission easements have been established. Transmission easement serves as a basis for determining the scope of the use of third-party property by a transmission company, for which a relevant consideration is due to the owner. The owners' claims give rise to additional, frequently considerable, costs and thus may adversely affect the financial performance of the Gas Distribution Companies.

Lower volumes of transmitted gas fuel

The global economic crisis adversely affects Poland's economic growth. Given the weaker economic situation of the existing and prospective gas customers, there is a risk that the demand for natural gas and distribution services will fall.

Chapter VIII: Generation

In 2012, PGNiG TERMIKA SA (formerly Vattenfall Heat Poland S.A.) was included in the PGNiG Group. PGNiG SA acquired the assets of Vattenfall Heat Poland S.A. in January 2012, via its subsidiary PGNiG SPV 1 Sp. z o.o. Following the purchase of the Vattenfall assets and the related extension of the PGNiG Group's business to include electricity and heat generation, a new business segment (Generation) was established in the Group's structure.

The core business of the segment is generation of heat and electricity. The segment's business also includes execution of major natural gas-fired projects in the power segment. The segment includes PGNiG SPV 1 Sp. z o.o. and PGNiG TERMIKA SA.

1. Segment's operations

PGNiG TERMIKA SA is involved in the generation, distribution and sale of heat and electricity. The company's main revenue sources are sales of heat, electricity, system services, and certificates of energy origin. The installed capacity of the company's generating assets is 4.8 GW of achievable thermal power and 1 GW of achievable electrical power, which satisfies approximately 75% of the heat demand on the Warsaw metropolitan market. PGNiG TERMIKA SA is also a producer and supplier of heat and the owner of heat sources and heat networks in Pruszków, Komorów and Piastów.

Heat and electricity are generated at the company's six production plants:
- Siekierki CHP Plant
- Żerań CHP Plant
- Pruszków CHP Plant
- Kawęczyn Heating Plant
- Wola Heating Plant
- Regaty Heating Plant.

In H1 2012, PGNiG TERMIKA SA produced 2,402.9 GWh of electricity (93.2% of which was cogenerated with heat) and 23,415.2 TJ of heat.

PGNiG TERMIKA SA sold heat mainly to Stołeczne Przedsiębiorstwo Energetyki Cieplnej S.A. (SPEC S.A.), which purchased 97% of the heat generated by the company. In H1 2012, SPEC S.A. contracted 3.6 GW of PGNiG TERMIKA's heat generation capacity. The balance of heat produced was sold to local customers, mainly in Pruszków and the surrounding areas.

PGNiG TERMIKA SA sold electricity mainly to Vattenfall Energy Trading Sp. z o.o. and Tauron Sprzedaż GZE Sp. z o.o., whose aggregate share in the company's sales of electricity was to 93% in H1 2012. The company also sold electricity to smaller customers.

In H1 2012, the company provided Network Constrained Generation services under an agreement with PSE Operator S.A. Under the agreement, the company maintains long-term plant margin, which helps overcome limitations in the operation of power sources in the national power system. PGNiG TERMIKA SA is required to generate electricity whenever so instructed by the Transmission System Operator. In the performance of the agreement, the company sold 66.4 GWh of electricity by June 30th 2012.
PGNiG TERMIKA SA also sold property rights in the form of certificates of electricity origin. Certificates of origin for energy produced by cogeneration (known as red certificates) were mainly sold as forward contracts. In H1 2012, the company concluded contracts for the sale of certificates

of origin for energy produced in 2012 with Polska Grupa Energetyczna S.A., ENEA S.A., TAURON Polska Energia S.A., PKP Energetyka S.A. and ENERGA SA.

2. Planned activities

The sales of electricity, heat and certificates of origin will be the key revenue source for PGNiG TERMIKA SA. The company plans to increase the production of energy by cogenerating electricity and useful heat in cogeneration units. Taking into consideration the risk of rising prices of CO_2 emission allowances, the company will also strive to diversify types of fuel used to fire its Warsaw-based generating assets, gradually replacing coal with gas or renewable fuel (biomass).

In cooperation with SPEC S.A., the company will seek ways to strengthen its position as the leading heat supplier on the Warsaw and Pruszków markets, to expand the area covered by its heat supplies from the municipal heating network, and to connect further users to its network.

In H2 2012, PGNiG TERMIKA SA will, as earlier, sell electricity mainly to Vattenfall Energy Trading Sp. z o.o. and Tauron Sprzedaż GZE Sp. z o.o.

In H2 2012, the management of electricity portfolio and commercial balancing for PGNiG TERMIKA SA has been taken over by PGNiG Energia S.A., which concludes dated power purchase contracts on the Commodity Derivatives Market, for delivery in 2013. PGNiG TERMIKA SA will also continue to sell electricity on the Commodity Derivatives Market through the agency of ALPIQ S.E. Further, in H2 2012, PGNiG Energia S.A. has commenced trading in property rights from certificates of energy origin and CO_2 emission allowances held by PGNiG TERMIKA SA.

3. Generation risk

More stringent gas and dust emission standards

In order to meet more stringent gas and dust emission standards expected to be implemented in 2016, producers will have to thoroughly modernise their power and CHP plants and shut down a number of generating units (with a total capacity 4,000-6,000 MWe by 2020) where installation of expensive SOx and NOx units is not economically viable. In order to meet the more stringent emission standards, PGNiG TERMIKA SA has gradually been modernising its generating assets.

Maintaining the share in the municipal heat market

Following extension of the Warsaw municipal waste incineration plant, the quantity of heat supplied to the city's municipal network will increase. As a result, PGNiG TERMIKA SA's share in total heat supplies to the municipal network will fall from the current 98% to 95% in 2019.

Joint marketing efforts conducted with SPEC S.A. and connecting further western districts of Warsaw to the municipal heating network should significantly reduce potential future decline in the volume of energy produced at PGNiG TERMIKA SA's generating plants. With a view to maintaining its share in the municipal heat market, the company also offers "green" heat generated in biomass-fired units, continues to sell energy at competitive prices, and takes advantage of the TPA rule to gain access to new end users.

Chapter IX: Other Activities

1. Segment's operations

In H1 2012, the segment companies conducted work involving construction and assembly of gas transmission pipelines, construction and extension of underground gas storage facilities, and development of hydrocarbon deposits. They were also involved in production of drilling equipment, repair of coal mining equipment, design of gas transport systems, and provision of hotel, restaurant and spa centre services.

The PGNiG Group was the key customer of the segment. Key projects executed in H1 2012 included construction and assembly of high-pressure gas pipelines, construction and extension of natural gas storage facilities and development of natural gas and crude oil deposits. The projects included:

- construction of a high-pressure gas pipeline from the Szczyglice node to KGHM Polkowice/Żukowice;
- preparation for construction and supervision over the construction of a pipeline from KGZ Kościan to KGHM Polkowice/Żukowice;
- extension of the Mogilno Cavern Underground Gas Storage Facility;
- construction of the Kosakowo Underground Gas Storage Facility;
- development of gas wells in the Rylowa-Rajsko, Pruchnik, Góra Ropczycka, Lubliniec and KGZ Mirocin fields, and development of Barnówko-Mostno oil wells in the BMB field.

For the PGNiG Group, the segment provided operator and repair services related to the operation of the Mogilno Cavern Underground Gas Storage Facility, prepared design documentation for gas transmission systems and manufactured drilling equipment, including surface pressure equipment, heads, casing heads and spare parts for production equipment.

Services provided to customers outside the PGNiG Group included construction of high-pressure gas pipelines, design of gas transmission systems, production of equipment and spare parts for drilling rigs and ships. The segment's companies also carried out repairs of coal mining equipment and provided hotel, restaurant and spa centre services. Key projects executed for third-party customers included:

- construction of a high-pressure gas pipeline from Wiczlino to Kosakowo for OGP GAZ-SYSTEM S.A.;
- construction of a high-pressure gas pipeline between Rogaska Slatina and Trojane in Slovenia for Geoplin Plinovodi d.d.

2. Planned activities

In H2 2012, the segment's companies will continue the projects commenced in the preceding period, and will launch new projects. The continued projects will include the construction of high-pressure gas pipelines from the Szczyglice node to KGHM Polkowice/Żukowice, from Wiczlino to Kosakowo, from Hermanowice to Strachocina and from Rogaska Slatina to Trojane (Slovenia). The companies will also continue to develop gas wells in the Rylowa-Rajsko, Pruchnik, Góra Ropczycka, Lubliniec and KZG Mirocin fields, and oil wells in the BMB field. Work on new construction and design projects will be launched. The key projects include construction of gas transmission pipelines from Rembelszczyzna to Gustorzyn, from Wierzbno Terminal to the Paproć Gas Production Facility and from Koszalin to Słupsk, as well as upgrade of the Hermanowice distribution and metering node.
The segment's companies intend to maintain their market positions in the area of manufacturing of drilling equipment, including surface equipment for conventional and unconventional deposits,

drilling platforms, and equipment for oil and gas production facilities; and in the area of gas system design, construction and assembly services for oil and gas facilities.

3. Risks related to Other Activities

Legislation

Administrative regulations and procedures related to the preparation of investment projects and obtaining building permits, including in particular regulations governing compliance with the environmental requirements, may significantly delay project execution and expose the company to the risk of cost overruns caused by potential delays in contract performance, and to the risk of lower revenues. The Public Procurement Law and other regulations which stipulate contract price as the only criterion in bid evaluation cause the segment's companies to lose against competitors who offer lower prices for services of inferior quality. Moreover, in H1 2012 the President of the Public Procurement Office published guidelines concerning the obligation to call tenders for design supervision services. The new guidelines are unfavourable for design offices. Prior to the change, such services could be provided exclusively to design authors, and commissioning such work was not governed by the Public Procurement Law.

Competition

The operations of companies offering construction and assembly services and manufacturers of drilling equipment are significantly exposed to growing competition from foreign companies, both those operating in their local markets abroad and those entering the Polish market, and from Polish market players. Given the current level of investment in the segment's area of operations, growing competition results in, among other consequences, continually low prices for the services offered by the segment companies. As far as designing of gas transmission installations is concerned, acquisition of medium-sized design offices by large contractors and setting up of new design offices within gas industry operators are unfavourable phenomena which adversely affect the segment companies' capacity to form consortia with project execution companies and secure new orders. Another major threat in this area is the growing competition from new business groups.

Chapter X: Environmental protection

Well and mining pit abandonment

Pursuant to the Polish Geological and Mining Law, PGNiG SA is required to properly abandon worked-out mining pits, eliminate the danger and repair any damage caused by mining activities, and restore the land to its original condition. Plugging of wells and pits prevents leakage of crude oil and natural gas to the surface and to water courses. Furthermore, if gas wells remain unplugged, there is a risk that escaping gas could accumulate inside, posing a fire hazard. In H1 2012, four mining pits were plugged.

Carbon credit trading system

In the first half of 2012, PGNiG SA reviewed annual reports on carbon dioxide emissions for 2011. After reconciling its CO_2 emissions with emission rights held and after cancelling used allocations for 2011, the remaining amount was 8,884 Mg CO_2 of free emission units. In 2011, the installations participating in the scheme were the Odolanów Branch, the Zielona Góra Branch and the Mogilno Underground Gas Storage Cavern Facility. Emissions from those installations amounted to 91,098 Mg CO_2.

Methane emissions

H1 2012 saw completion of the first stage of detailed recording of methane emissions from the gas distribution system, commenced in 2011. Its purpose is to estimate the volume of methane emissions from particular elements of the system, review the emission indicators applied to date, and develop uniform indicators and calculation methods for methane emissions. Standardised and reliable methane emission indicators will help reduce the cost of environmental fees and charges.

Land reclamation and non-productive asset surveying

Pursuant to the Environmental Protection Law, PGNiG SA conducts diagnosis tests and surveys and land reclamation work in the areas polluted in the course of past activities with a view to restoring them to the condition required under the environmental quality standards. In H1 2012, the Company monitored the environmental impact of the reclaimed landfill site in Zabrze-Biskupice and a property in Zabrze, and carried out supplementary tests and surveys on a property located in Szczecin.

REACH and CLP

In 2011, PGNiG SA took measures to ensure compliance of the labelling of substances produced by the Company with the regulations of the European Parliament and the Council of the European Union on safe use of chemicals (REACH) and on the classification, labelling and packaging of substances and mixtures (CLP). In H1 2012, PGNiG SA adjusted the Material Safety Data Sheets for natural gas, crude oil, hydrocarbon condensate, LPG, LNG, helium and nitrogen, to meet the CLP Regulation.

Integrated Management System and Environmental Management System

In H1 2012, a recertification audit of the Environmental Management System was carried at the PGNiG Head Office, with a positive result. The certificate confirming compliance of the system with PN-EN ISO 14001:2005 was extended until 2015. A recertification audit was also conducted at Mazowiecka Spółka Gazownictwa Sp. z o.o. to verify the company's Environmental Management System, implemented in 2011.

Chapter XI: Other information

Distribution of the 2011 profit

On June 6th 2012, the Annual General Meeting of PGNiG SA adopted a resolution to allocate the 2011 net profit of PLN 1,615.7m and retained earnings of PLN 72.5m to the Company's statutory reserve funds.

Discharge granted to Management Board and Supervisory Board members in respect of their duties

On June 6th 2012, the Annual General Meeting of PGNiG SA approved the financial statements and the Director's Report on operations of PGNiG SA, as well as the consolidated financial statements and the Director's Report on operations of the PGNiG Group, and granted discharge to members of the Management and Supervisory Boards of PGNiG SA in respect of their performance of duties in the financial year 2011.

Issue of Euronotes

On February 10th 2012, PGNiG SA issued (through its subsidiary PGNiG Finance AB) five-year Euronotes for EUR 500m. The notes were assigned the Baa1 (Moody's) and BBB+ (Standard & Poor's) credit ratings. Further, in May 2012 PGNiG SA executed transaction documentation for a five-year PLN 4.5bn notes issuance programme addressed to investors in Poland. The first note issue under the programme, with a nominal value of PLN 2.5bn, took place on June 19th 2012.

Legal actions against PI GAZOTECH Sp. z o.o.

Proceedings concerning PGNiG SA's action against PI GAZOTECH Sp. z o.o. to rescind or declare invalidity of resolutions by the General Meeting of PI GAZOTECH Sp. z o.o., dated April 23rd 2004, including the resolution obliging PGNiG SA to pay additional contributions in the amount of PLN 52m, were held in turn before the Regional Court of Warsaw, the Warsaw Court of Appeals and the Supreme Court. On June 25th 2010, the Regional Court granted PGNiG SA's claims and declared the resolution concerning share redemption and the resolution concerning the additional contributions as invalid. On November 12th 2010, PI GAZOTECH Sp. z o.o. filed an appeal with the Regional Court, along with a petition to be exempt from court fees. On December 14th 2011, the Court of Appeals dismissed PI GAZOTECH Sp. z o.o.'s appeal. The decision was final. On April 24th 2012, PI GAZOTECH Sp. z o.o. lodged a cassation appeal, which had not been accepted for consideration by the Supreme Court by the date of this Report.

Proceedings based on PGNiG SA's action against PI GAZOTECH Sp. z o.o. to rescind or declare invalidity of the resolution of the General Meeting of PI GAZOTECH Sp. z o.o., dated January 19th 2005, whereunder PGNiG SA was obliged to pay additional contributions in the amount of PLN 25,999,998, were held before the Regional Court of Warsaw and the Warsaw Court of Appeals. By virtue of its ruling of October 18th 2010, the Regional Court of Warsaw rescinded the resolution on additional contributions. On November 12th 2010, PI GAZOTECH Sp. z o.o. filed an appeal with the Regional Court, along with a petition to be exempt from court fees. By virtue of its decision of June 22nd 2012, the Court of Appeals of Warsaw dismissed PI GAZOTECH Sp. z o.o.'s appeal. The decision was final. As at the date of these financial statements, PI GAZOTECH Sp. z o.o. has not lodged an appeal in cassation against that decision.

Proceedings based upon PGNiG SA's action against PI GAZOTECH Sp. z o.o. to rescind or declare invalidity of the resolution of the General Meeting of PI GAZOTECH Sp. z o.o., dated October 6th 2005, whereunder PGNiG SA was obliged to pay additional contributions in the amount of PLN 6,552,000, were brought before the Regional Court of Warsaw. On May 30th 2008, the Regional Court dismissed the Company's claim and reversed the decision concerning implementation of measures to safeguard the claim (the temporary injunction order). The proceedings to rescind or declare invalidity of the resolution on additional contributions and to maintain the safeguarding measures have been held before the Court of Appeals and the Regional Court of Warsaw since 2008. By virtue of its decision of May 25th 2010, the Court of Appeals changed the Regional Court's decision concerning maintenance of the safeguarding measures dated May 30th 2008 and dismissed the request for reversing the final decision on implementation of the safeguarding measures. By virtue of its decision of May 21st 2012, the Regional Court of Warsaw declared the resolution of the General Meeting of PI GAZOTECH Sp. z o.o. on additional contributions invalid. As at the date of these financial statements, PI GAZOTECH Sp. z o.o. has not lodged an appeal against that decision.

Proceedings before the President of the Polish Office of Competition and Consumer Protection (UOKiK)

On December 28th 2010, the President of the Polish Office of Competition and Consumer Protection ("UOKiK") instigated, ex officio, anti-trust proceedings concerning abuse of dominant position by PGNiG SA on the domestic natural gas wholesale market, which consisted in inhibiting sale of gas against the interest of other business players or consumers and impeding the development of market conditions necessary for the emergence or development of competition by refusing to sell gas fuel under a comprehensive supply contract to an entrepreneur that intended to further resell the gas, i.e. NowyGaz Sp. z o.o. of Warsaw. In its decision of July 5th 2012, the President of UOKiK found these actions to be anti-competitive practices, concluded that PGNiG SA discontinued those practices as of November 30th 2010, and imposed on the Company a fine of PLN 60,016,474.40. On July 24th 2012, PGNiG SA filed an appeal against the decision of the President of UOKiK with the Competition and Consumer Protection Court at the Regional Court of Warsaw.

On July 4th 2011, the President of UOKiK instigated anti-trust proceedings concerning abuse of dominant position by PGNiG SA on the domestic retail natural gas market. In the President's opinion, the abuse consisted in frustrating the emergence or development of competition on the domestic natural gas wholesale and retail markets by limiting the customers' ability to terminate comprehensive gas fuel supply contracts. In the course of the proceedings, PGNiG SA voluntarily agreed to change certain contractual provisions. By virtue of the decision of April 13th 2012, the President of UOKiK resolved not to impose a fine on the Company and required the Company to change certain contractual provisions. PGNiG S.A has satisfied this requirement.

On February 9th 2012, the President of UOKiK instigated anti-trust proceedings concerning practices employed by PGNiG SA which infringe collective consumer interests. The President of UOKiK accused PGNiG SA of using in comprehensive gas fuel supply contracts a provision classified as illegal contractual clause. In the course of the proceedings, PGNiG SA voluntarily agreed to change certain contractual provisions. By virtue of a decision of August 10th 2012, the President of UOKiK resolved not to impose a fine on the Company and required the Company to start using a new form of comprehensive gas fuel supply contract containing revised general provisions.

Proceedings before the Court of Arbitration

On March 31st 2011, PGNiG SA requested OOO Gazprom Export to renegotiate the price of gas deliveries under the Contract dated September 25th 1996, providing for supplies of natural gas to the Republic of Poland, so as to reduce the price. Since the parties failed to reach an agreement in the period of six months, on November 7th 2011, PGNiG SA filed a request to OAO Gazprom and OOO Gazprom Export to start arbitration proceedings before the Court of Arbitration in Stockholm. In accordance with the Court's procedure, on February 20th 2012, the Company filed a suit against OAO Gazprom and OOO Gazprom Export. On May 24th 2012, OAO Gazprom/OOO Gazprom Export responded to the statement of claim and dismissed all the arguments put forward by PGNiG SA. As at the date of this Report, the proceedings before the Court of Arbitration were pending. PGNiG SA does not rule out a possibility of reaching an agreement in commercial negotiations, provided that OAO Gazprom and OOO Gazprom Eksport agree to reduce the price of natural gas supplied under the Yamal Contract.

Chapter XII: Financial performance

The interim consolidated financial statements of the PGNiG Group for the six months ended June 30th 2012 have been prepared in accordance with the International Financial Reporting Standards (IFRS) as endorsed by the European Union ("EU") as at June 30th 2012.

The accounting policies applied in preparing the interim consolidated financial statements are presented in the interim consolidated financial statements of the PGNiG Group for the six months ended June 30th 2012.

1. Financial performance

In H1 2012, the PGNiG Group reported a net loss of PLN 16.5m, i.e. its net result fell PLN 1,021.4m year on year.

Summary information on the PGNiG SA's financial standing in H1 2012 is presented below, in the financial statements prepared in accordance with the International Financial Reporting Standards, which comprise:

- statement of financial position,
- income statement,
- statement of cash flows,
- selected financial ratios.

Consolidated statement of financial position (PLNm)

ASSETS	Jun 30 2012	Dec 31 2011
Non-current assets	35 060,5	30 435,4
Property, plant and equipment	31 841,1	28 427,0
Investment property	12,8	7,1
Intangible assets	1 081,5	275,5
Investments in equity-accounted associates	685,0	598,4
Financial assets available for sale	56,5	56,4
Other financial assets	81,6	9,4
Deferred tax assets	1 206,5	963,8
Other non-current assets	95,5	97,8
Current assets	7 120,2	7 529,0
Inventories	2 719,3	2 082,4
Trade and other receivables	2 379,2	3 378,1
Current income tax receivable	136,7	164,5
Prepayments and accrued income	307,6	83,9
Financial assets available for sale	2,8	22,3
Derivative financial instrument assets	197,9	284,6
Cash and cash equivalents	1 369,5	1 504,8
Non-current assets held for sale	7,2	8,4
Total assets	42 180,7	37 964,4

Consolidated statement of financial position (PLNm) – contd.

EQUITY AND LIABILITIES	Jun 30 2012	Dec 31 2011
Equity	24 398,1	24 496,7
Share capital	5 900,0	5 900,0
Currency translation differences on foreign operations	(11,2)	(23,0)
Share premium account	1 740,1	1 740,1
Other capital reserves	16 011,8	14 149,3
Retained earnings/(deficit)	750,7	2 723,5
Equity (attributable to owners of the Parent)	24 391,4	24 489,9
Equity attributable to non-controlling interests	6,7	6,8
Non-current liabilities	10 728,6	5 621,5
Loans, borrowings and debt securities	5 819,3	1 382,3
Provisions	1 883,7	1 625,8
Deferred income	1 204,6	1 160,1
Deferred tax liabilities	1 797,8	1 433,4
Other non-current liabilities	23,2	19,9
Current liabilities	7 054,0	7 846,2
Trade and other payables	3 001,6	3 354,9
Loans, borrowings and debt securities	3 137,5	3 616,6
Derivative financial instrument liabilities	399,1	416,8
Current tax liabilities	45,3	57,7
Provisions	371,7	305,2
Deferred income	98,8	95,0
Total liabilities	17 782,6	13 467,7
Total equity and liabilities	42 180,7	37 964,4

Consolidated income statement (PLNm)

	H1 2012	H1 2011
Sales revenue	14 764,4	11 523,4
Total operating expenses	(14 817,0)	(10 450,6)
Raw and other materials used	(10 633,2)	(6 890,1)
Employee benefits	(1 365,4)	(1 380,2)
Depreciation and amortisation	(1 003,9)	(776,9)
Contracted services	(1 487,4)	(1 567,5)
Cost of products and services for own needs	362,4	481,4
Other operating expenses, net	(689,5)	(317,3)
Operating profit/loss	-52,6	1 072,8
Finance income	68,8	192,7
Finance expenses	(196,4)	(25,5)
Share in net profit/loss of equity-accounted entities	86,6	(0,4)
Pre-tax profit/loss	-93,6	1 239,6
Income tax	77,1	(234,7)
Net profit/loss	-16,5	1 004,9
Attributable to:		
Owners of the Parent	-13,3	1 003,5
Non-controlling interests	-3,2	1,4
	-16,5	1 004,9

Consolidated statement of cash flows (PLNm)

	H1 2012	H1 2011
Net cash provided by/(used in) operating activities	1 179,6	2 256,5
Net cash provided by/(used in) investing activities	(4 288,1)	(2 107,9)
Net cash provided by/(used in) financing activities	2 974,1	(487,5)
Net change in cash	(134,4)	(338,9)
Cash and cash equivalents at beginning of the period	1 503,8	1 372,9
Cash and cash equivalents at end of the period	1 369,4	1 034,1

Financial Ratios

Profitability

	H1 2012	2011
EBIT (PLNm) operating profit	-52,6	1 072,8
EBITDA (PLNm) operating profit + depreciation/amortisation	951,3	1 849,7
ROE net profit* to equity at end of the period	-0,1%	4,1%
NET MARGIN net profit* to sales revenue	-0,1%	8,7%
ROA net profit* to assets at end of the period	0,0%	2,6%

*Net profit for the financial year attributable to owners of the parent.

Liquidity

	Jun 30 2012	Dec 31 2011
CURRENT RATIO current assets (net of prepayments and accrued income) to current liabilities	1,0	0,9
QUICK RATIO current assets (net of prepayments and accrued income) less inventories to current liabilities	0,6	0,7

Debt

	Jun 30 2012	Dec 31 2011
DEBT RATIO total liabilities to total equity and liabilities	42,2%	35,5%
DEBT/EQUITY RATIO total liabilities to equity*	72,9%	55,0%

*Equity attributable to owners of the parent.

Year on year, the Group's EBIT decreased by PLN 1,125.4m. The decline was caused by the considerably lower profitability of high-methane gas sales.

Exploration and Production

Significant losses incurred on sales of high-methane gas were partially offset by the positive performance of the Exploration and Production segment. The Exploration and Production segment posted operating profit of PLN 769.8m, up PLN 316.6m on H1 2011. Relative to H1 2011, the profitability of crude sales improved considerably, as crude oil selling prices rose by 23%, in line with the general trend on global markets. Further, profitability of helium sales improved driven by rising prices of the gas. The segment's operating profit was also strongly influenced by a decrease in other net operating expenses, attributable to higher reversals of impairment losses related to exploration activities.

Trade and Storage

Financial performance of the Trade and Storage segment suffered most. The segment reported an operating loss of PLN 1,435.1m, i.e. down PLN 1,559.5m year on year. The decline was caused by the considerably lower profitability of high-methane gas sales, which was primarily brought about by:

- higher unit purchase price of imported gas.
- the level of average gas prices and related charges.

Following the rise of crude prices on the global markets, and with the USD exchange rate being much higher than in H1 2011, the unit purchase price of imported gas increased by 47%.

In a decision of March 16th 2012, the President of the Energy Regulatory Office approved the Gas Fuel Tariff, which was to be applied in settlements with customers in the period from January 1st to March 31st 2012. The absence of approval of the new tariff by the President of the Energy Regulatory Office as at the beginning of Q1 2012 prevented the Group from offsetting the higher cost of imported gas with higher gas prices charged to the customers. Consequently, the profitability of high-methane gas sales fell significantly below the break-even point. Although the new gas fuel tariff has been effective since March 31st 2012, the new prices of gas have not yet secured profitable sales of high-methane gas by the Company. Relative to H1 2011, average prices and charge rates for the supply of high-methane gas type E, nitrogen-rich gas type Lw and nitrogen-rich gas type Ls were increased by 13.1%, 12.6% and 10.5%, respectively.

The segment's operating profit was also strongly affected by higher other net operating expenses, attributable primarily to a negative valuation of derivative financial instruments and lower foreign exchange gains. In addition, an increase in provisions (following a fine being imposed on the Group by the Polish Office of Competition and Consumer Protection for monopolistic practices) and an increase in impairment losses on gas stocks were recognised in the Trade and Storage segment. At the same time, the PGNiG Group derived significant proceeds from the sale of pipelines to OGP GAZ-SYSTEM S.A.

Distribution

The Distribution segment's operating profit was PLN 566.4m, up PLN 64.4m on H1 2011. The rise was driven principally by higher sales revenue following the increase of prices and charges for network services as of July 15th 2011 and higher volumes of transmitted gas. However, the improvement of the operating result coincided with an increase in operating expenses, including in particular costs of materials and energy used (mainly gas used to compensate system imbalance). Other items of operating expenses are on a decline following a series of cost-cutting measures implemented across the segment.

Generation

Following the acquisition of Vattenfall Heat Poland SA's assets in January 2012, the PGNiG Group commenced operations consisting in generation of electricity and generation and distribution of heat. In H1 2012, the Generation segment produced a positive result of PLN 53.8m.

Segments' operating results

Financial data of the PGNiG Group's segments for H1 2012 (PLNm)

H1 2012	Exploration and Production	Trade and Storage	Distribution	Generation	Other Activities	Eliminations	Total
Sales to external customers	1 475,9	12 032,5	63,6	1 114,5	77,9	-	14 764,4
Intercompany sales	570,7	266,8	1 864,9	-	151,9	(2 854,3)	-
Segment's total revenue	2 046,6	12 299,3	1 928,5	1 114,5	229,8	(2 854,3)	14 764,4
Segment's expenses	(1 276,8)	(13 735,2)	(1 362,1)	(1 060,7)	(259,7)	2 877,5	(14 817,0)
Operating profit/loss	769,8	(1 435,9)	566,4	53,8	(29,9)	23,2	(52,6)
Net finance expenses	-	-	-	-	-	-	(127,6)
Share in net profit/loss of equity-accounted entities	-	86,6	-	-	-	-	86,6
Pre-tax profit/loss							(93,6)
Income tax	-	-	-	-	-	-	77,1
Net profit/loss							(16,5)
Capital expenditure on property, plant and equipment and intangible assets	(796,6)	(149,0)	(583,4)	(59,6)	(12,4)	(16,0)	(1 617,0)

Financial data of the PGNiG Group's segments for H1 2011 (PLNm)

H1 2011	Exploration and Production	Trade and Storage	Distribution		Other Activities	Eliminations	Total
Sales to external customers	1 275,3	10 099,1	54,6		94,4		11 523,4
Intercompany sales	564,4	93,3	1 777,2		219,2	(2 654,1)	-
Segment's total revenue	1 839,7	10 192,4	1 831,8		313,6	(2 654,1)	11 523,4
Segment's expenses	(1 386,5)	(10 068,8)	(1 329,8)		(304,8)	2 639,3	(10 450,6)
Operating profit/loss	453,2	123,6	502,0	0,0	8,8	(14,8)	1 072,8
Net finance expenses	-	-	-		-	-	167,2
Share in net profit/loss of equity-accounted entities	-	(0,4)	-		-	-	(0,4)
Pre-tax profit/loss							1 239,6
Income tax	-	-	-		-	-	(234,7)
Net profit/loss							1 004,9
Capital expenditure on property, plant and equipment and intangible assets	(1 346,4)	(487,8)	(460,8)		(6,9)	25,8	(2 276,1)

Compared with H1 2011, the result on financing activities fell by PLN 294.8m, chiefly as a consequence of higher interest expense due to the increase in the PGNiG Group's debt and lower net foreign exchange gains/losses. Concurrently, following a revaluation of shares in SGT EUROPOL

GAZ S.A. the PGNiG Group recognised a PLN 87.0m increase in the share of equity-acccounted entities in net profit/loss.

Deterioration of the PGNiG Group's financial position is reflected in the decline of the key financial ratios. Return on equity decreased from 4.1% to -0.1%, return on assets was 0.0% against 2.6% in H1 2011, and net margin dropped from 8.7% to -0.1%.

As at June 30th 2012, total assets were PLN 42,180.7m, up PLN 4,216.3m on the end of 2011.

Property, plant and equipment, of PLN 31,841.1m as at the end of June 2012 (up PLN 3,414.1m on December 31st 2011), was the largest item of the Group's assets. This strong growth of property, plant and equipment is attributable to the recognition in the consolidated financial statements of the assets of PGNiG TERMIKA SA following the acquisition of a 99.8% equity interest in Vattenfall Heat Poland S.A. in January 2012. Property, plant and equipment also rose in connection with the PGNiG Group's investment projects and changes resulting from the revaluation of non-current assets.

As at June 30th 2012, intangible assets were PLN 1,081.5m, up PLN 806.0m on December 31st 2011. The increase was caused mainly by the consolidation of the assets of PGNiG TERMIKA SA and the fact that the acquisition was accounted for with the equity method. The change follows mainly from the valuation of perpetual usufruct right to land and CO_2 emission allowances, previously not recognised in the financial statements of Vattenfall Heat Poland S.A.

The PLN 86.6m rise in investments in equity-accounted associates relative to December 31st 2011 was mainly due to the revaluation of shares in SGT EUROPOL GAZ S.A.

The value of other financial assets was PLN 72.2m up on the figure reported as at December 31st 2011. Other financial assets increased chiefly as a result of granting a loan to Elektrociepłownia Stalowa Wola S.A.

Compared with December 31st 2011, the PGNiG Group recorded a PLN 242.7m rise in the deferred tax asset, particularly as a result of capitalising the tax loss for the current period, to be deducted in future years from income tax, and following recognition of investment incentives at PGNiG Norway AS.

As at June 30th 2012, current assets of the PGNiG Group were PLN 7,120.2m, down PLN 408.8m (or 5%) on December 31st 2011.

Relative to December 31st 2011, the PGNiG Group's inventories rose by PLN 636.9m (31%). The inventories disclosed in the balance sheet comprise mainly gas stored in the underground storage facilities. Inventories increased chiefly on the back of higher unit costs of imported gas and first-time recognition of inventories of PGNiG TERMIKA SA (coal for electricity and heat generation) in the consolidated financial statements. At the end of the reporting period the PGNiG Group recognised an impairment loss on inventories of high-methane gas stored in the underground storage facilities.

Trade and other receivables fell PLN 998.9m (30%) relative to the end of 2011. The fall was due to the seasonal decline in gas fuel sales.

Relative to December 31st 2011, accruals and deferrals rose by PLN 223.7m, following recognition of property tax expense accounted for over time, including mainly tax on gas pipelines and gas infrastructure as well as cost of contribution to the Social Benefits Fund.

Cash and equivalents stood at PLN 1,369.5m, down PLN 135.3m on the end of 2011. The drop occurred despite a considerable increase in the PGNiG Group's borrowings and was principally due to high investment spending and operating losses.

The value and structure of current assets held by the PGNiG Group guarantee its ability to settle liabilities in a timely manner. Current ratio was 1.0, compared with 0.9 as at the end of December 2011, while quick ratio fell from 0.7 to 0.6.

Equity is the primary source of financing of the PGNiG Group's assets. Relative to the end of 2011, the Group's equity fell PLN 98.6m. The change was chiefly an outcome of the net loss reported for the period (PLN 16.5m) and changes in other capital reserves.

As at June 30th 2012, non-current liabilities were PLN 10,728.6m, up PLN 5,107.1m on the end of December 2011. The rise is a consequence of a PLN 4,437.0m increase in long-term debt, following the issue of Euronotes by PGNiG Finance AB (EUR 500m) and the issue of five-year notes on the domestic market (PLN 2.5bn). Non-current liabilities increased also due to a PLN 257.9m increase in provisions, attributable to higher provisions for well decommissioning costs, consolidation of the provisions of PGNiG TERMIKA SA, and higher deferred tax liability (up PLN 364.4m).

Compared with the end of December 2011, current liabilities fell PLN 792.2m (10%) following a PLN 479.1m decrease in loans, borrowings and debt securities (redemption of short-term notes) and lower trade and other payables (down by PLN 353.3m). Trade payables fell mainly on the back of lower public dues and charges and lower liabilities on purchase of non-financial non-current assets.

Due to the significant increase in external financing used by the PGNiG Group, the ratios of equity to liabilities changed. Debt to equity rose from 55.0% to 72.9%, and debt ratio (total liabilities to total equity and liabilities) went up from 35.5% to 42.2%.

Transactions concluded on non-arm's length terms

In H1 2012, PGNiG SA and its subsidiaries did not enter into any material related-party transactions on non-arm's length terms.

Guarantees and sureties

In H1 2012, PGNiG SA and its subsidiaries did not grant any loan sureties or guarantees to any entity where the total value of such sureties or guarantees would represent 10% or more of PGNiG SA's equity.

The Group's ability to meet published financial forecasts

In H1 2012, the PGNiG Group did not publish any financial forecasts.

2. Projected future financial performance

Key factors with a bearing on the PGNiG Group's financial performance will include crude oil prices on the international markets, conditions prevailing on the currency markets, and the stance taken by the President of the Energy Regulatory Office with regard to gas fuel tariffs.

The financial position of the PGNiG Group is to a significant extent affected by the prices of crude oil and petroleum products, as they directly affect purchase prices of imported gas. In Q2 2012, crude prices were lower relative to Q1 2012. Prices of crude oil in subsequent months will depend on the general condition of the global economy and the political developments in countries which produce crude oil.

The PGNiG Group is, to large extent, exposed to changes in foreign exchange rates, which are reflected in prices of imported gas in the złoty terms. In H1 2012, the currency market was highly volatile, and the Polish currency depreciated. Exchange rates may continue to fluctuate given the difficult economic conditions in several member states of the European Union.

Another factor with a bearing on the financial performance of the PGNiG Group relates to the level of rates and charges provided for in gas fuel tariffs. The gas fuel supply tariffs effective in Q1 2012 were particularly detrimental to the financial performance of PGNiG SA. Pursuant to a decision of the President of the Energy Regulatory Office, the new gas fuel tariff became effective as of March 31st 2012 and will continue in force until the end of the year. As PGNiG SA generated losses on sales of high-methane gas even following the approval of the new tariff, in June 2012 the Company again applied for an increase in gas prices.

In 2011, PGNiG SA began to renegotiate the price of gas supplied under the long-term contract with OOO Gazprom Export and then referred the case to the Arbitration Court in Stockholm. In 2012, the Company approached VNG-Verbundnetz Gas AG of Germany with a similar request for lowering the price of gas and gas transmission charges. A favourable outcome of the arbitration proceedings and of the negotiations with VNG-Verbundnetz Gas AG would result in a significant reduction of the cost of acquisition of the gas fuel by the Company.

In June 2012, the Parent's General Meeting resolved to allocate the entire 2011 net profit and retained earnings, of PLN 1,615.7m and PLN 72.5m, respectively, to the Group's statutory reserve funds. The increase in Group's equity will facilitate the financing of projects scheduled for 2012.

Given the high level of current and planned capital expenditure, PGNiG SA uses external financing raised by issuing debt securities on the domestic and foreign markets. The Company issued domestic notes first in 2010. The amount of financing available under the underwritten notes issue programme is PLN 7bn. In February 2012, the Company issued (through its subsidiary PGNiG Finance AB) five-year Euronotes for EUR 500m. Then, in May 2012 PGNiG SA executed transaction documentation for a five-year PLN 4.5bn note issuance programme addressed to investors in Poland. The first note issue under the programme, with a nominal value of PLN 2.5bn, took place on June 19th 2012. PGNiG SA does not intend to issue any Euronotes or notes on the Polish market in H2 2012.

The launch of production from the Skarv field on the Norwegian Continental Shelf has been postponed from Q2 2012 to Q4 2012 due to delays in the installation of production risers caused by adverse weather conditions.

In the coming quarters, the PGNiG Group intends to maintain a high level of capital expenditure. The spending will focus on projects involving extension of underground gas storage facilities, maintenance of hydrocarbon production capacities, and diversification of gas supply sources, as well as on projects related to the exploration for and appraisal of crude oil and natural gas deposits and development of the Group's power generation segment.

Members of the Management Board

President of the Management Board	Grażyna Piotrowska-Oliwa	....
Vice-President of the Management Board	Radosław Dudziński	....
Vice-President of the Management Board	Sławomir Hinc	....
Vice-President of the Management Board	Mirosław Szkałuba	....