

DIRECTORS' REPORT
ON PGNiG GROUP'S OPERATIONS
IN H1 2008



Warsaw, September 1st 2008

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Chapter I: Information on the PGNiG Group

The PGNiG Group is the only vertically integrated gas company in Poland, holding the leading position in most segments of the domestic gas sector. Polskie Górnictwo Naftowe i Gazownictwo S.A. is the parent undertaking of the PGNiG Group.

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

On May 24th 2005, PGNiG S.A. shares were admitted to public trading by virtue of a decision issued by the Polish Securities and Exchange Commission. The Company's debut on the Warsaw Stock Exchange took place on September 23rd 2005. PGNiG S.A. shares have been listed on the WSE since October 20th 2005. Currently, the Company's share capital amounts to PLN 5.9b and is divided into 5,900,000,000 shares.

The scope of the PGNiG Group's business comprises exploration of reserves, extraction and storage of gaseous fuels as well as trade in and distribution of natural gas. The natural gas and crude oil production are among the key factors securing the Company's competitive advantage on the liberalised gas market. The core business of the PGNiG Group includes trade in and distribution of natural gas. The trading activities are handled by PGNiG S.A. and the distribution is carried out by six Distribution System Operators – members of the Group.

1. Structure of the PGNiG Group

As at June 30th 2008, the PGNiG Group comprised PGNiG S.A. (the parent undertaking) and 34 production and service companies, including:

- 27 subsidiaries of PGNiG S.A.;
- 7 indirect subsidiaries of PGNiG S.A.

The table below presents a list of the Group members as at June 30th 2008.

Companies of the PGNiG Group:

	Company	Share capital (PLN)	Shareholding of PGNiG S.A. (PLN)	% of share capital held by PGNiG S.A.	% of the total vote held by PGNiG S.A.
	Subsidiaries of PGNiG S.A.				
1	Poszukiwania Nafty i Gazu Jasło Sp. z o.o.	100,000,000.00	100,000,000.00	100.00%	100.00%
2	Poszukiwania Nafty i Gazu Kraków Sp. z o.o.	105,231,000.00	105,231,000.00	100.00%	100.00%
3	Poszukiwania Nafty i Gazu NAFTA Sp. z o.o.	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⁾	497,327,000.00	497,327,000.00	100.00%	100.00%
9	Polish Oil and Gas Company - Libya B.V. (EUR) ¹⁾	20,000.00	20,000.00	100.00%	100.00%
10	Polskie LNG Sp. z o.o.	50,000,000.00	50,000,000.00	100.00%	100.00%
11	INVESTGAS S.A.	502,250.00	502,250.00	100.00%	100.00%
12	Dolnośląski Operator Systemu Dystrybucyjnego Sp. z o.o.	651,145,000.00	651,145,000.00	100.00%	100.00%
13	Górnośląski Operator Systemu Dystrybucyjnego Sp. z o.o.	1,288,680,000.00	1,288,680,000.00	100.00%	100.00%
14	Karpacki Operator Systemu Dystrybucyjnego Sp. z o.o.	1,476,112,000.00	1,476,112,000.00	100.00%	100.00%
15	Mazowiecki Operator Systemu Dystrybucyjnego Sp. z o.o.	1,217,350,000.00	1,217,350,000.00	100.00%	100.00%
16	Pomorski Operator Systemu Dystrybucyjnego Sp. z o.o.	596,141,000.00	596,141,000.00	100.00%	100.00%
17	Wielkopolski Operator Systemu Dystrybucyjnego Sp. z o.o.	978,287,000.00	978,287,000.00	100.00%	100.00%
18	B.SiP.G Gazoprojekt S.A.	4,000,000.00	3,000,000.00	75.00%	75.00%
19	BUG Gazobudowa Sp. z o.o.	39,220,000.00	39,220,000.00	100.00%	100.00%
20	Zakład Urządzeń Naftowych Naftomet Sp. z o.o.	23,500,000.00	23,500,000.00	100.00%	100.00%
21	Geovita Sp. z o.o.	86,139,000.00	86,139,000.00	100.00%	100.00%
22	Budownictwo Naftowe Naftomontaż Sp. z o.o.	44,751,000.00	39,751,000.00	88.83%	88.83%
23	Górnictwo Naftowe Sp. z o.o.	50,000.00	50,000.00	100.00%	100.00%
24	NYSAGAZ Sp. z o.o.	3,700,000.00	1,887,000.00	51.00%	51.00%
25	ZRUG Sp. z o.o. (Pogórska Wola)	4,300,000.00	4,300,000.00	100.00%	100.00%
26	BUD-GAZ PPUH Sp. z o.o.	51,760.00	51,760.00	100.00%	100.00%
27	PPUiH TURGAZ Sp. z o.o.	176,000.00	90,000.00	51.14%	51.14%

	Company	Share capital (PLN)	Shareholding of PGNiG S.A.'s subsidiaries (PLN)	% of share capital held by PGNiG S.A.'s subsidiaries	% of the total vote held by PGNiG S.A.'s subsidiaries
	Subsidiaries of PGNiG S.A.'s subsidiaries				
28	GEOFIZYKA Kraków Libya JSC (LYD) ^{1), 2)}	1,000,000.00	600,000.00	60.00%	60.00%
29	GEOFIZYKA Torun Kish Ltd (Rial) ^{1), 3)}	10,000,000.00	10,000,000.00	100.00%	100.00%
30	Oil Tech International F.Z.E. (USD) ¹⁾	20,000.00	20,000.00	100.00%	100.00%
31	Zakład Gospodarki Mieszkaniowej Sp. z o.o. (Piła)	1,806,500.00	1,806,500.00	100.00%	100.00%
32	GAZ Sp. z o.o. (Błonie)	300,000.00	153,000.00	51.00%	51.00%
33	GAZ MEDIA Sp. z o.o. (Wołomin)	300,000.00	153,000.00	51.00%	51.00%
34	NAFT-STAL Sp. z o.o.	667,500.00	450,000.00	67.40%	67.40%

1) Figures shown in foreign currencies

2) Paid up: LYD 300,000.00, including LYD 180,000.00 paid by GEOFIZYKA Kraków Sp. z o.o.

3) Not paid up.

The following changes in the Group's structure occurred in H1 2008:

- Share capital increase at Polskie LNG Sp. z o.o. by PLN 11,000,000, to PLN 50,000,000; the increase was registered with the National Court Register on January 7th 2008;
- Share capital increase at Mazowiecki Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 286,531,000, to PLN 1,217,350,000; the increase was registered with the National Court Register on January 24th 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network;
- Share capital increase at Karpacki Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 165,363,000, to PLN 1,476,112,000; the increase was registered with the National Court Register on February 12th 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network;
- Share capital increase at Pomorski Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 93,391,000, to PLN 596,141,000; the increase was registered with the National Court Register on February 29th 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network;
- Share capital increase at GEOFIZYKA Kraków Sp. z o.o. by PLN 30,000 thousand, to PLN 64,400 thousand; the increase was registered with the National Court Register on April 2nd 2008;
- Share capital increase at Dolnośląski Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 104,697 thousand, to PLN 651,145 thousand; the increase was registered with the National Court Register on April 9th 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network;
- Share capital increase at Wielkopolski Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 131,128 thousand, to PLN 978,287 thousand; the increase was registered with the National Court Register on May 27th 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network;

- Share capital increase at Górnośląski Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 91,366 thousand, to PLN 1,288,680 thousand; the increase was registered with the National Court Register on June 25th 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network;
- Registration of amendments to the articles of association of PGNiG Finance B.V. (the Netherlands, February 4th 2008); under the amended articles of association, the company's name was changed to Polish Oil and Gas Company - Libya B.V. and its business profile was redefined;
- Deletion of ZRUG Warszawa S.A. (in liquidation) from the Register of Entrepreneurs on March 31st 2008 (PGNiG S.A.'s share in the share capital was 49%).

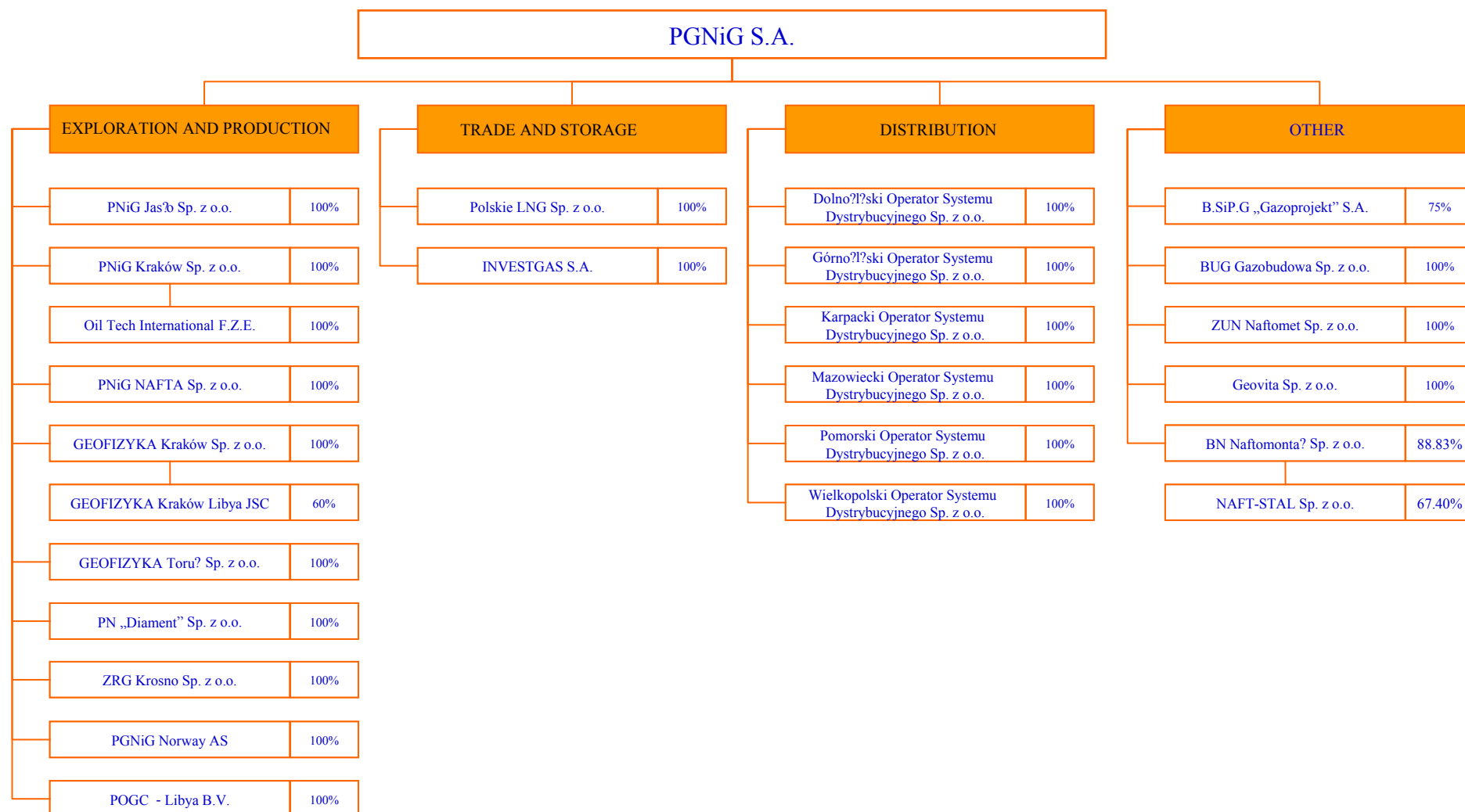
Furthermore, on January 29th 2008, Geofizyka Kraków Sp. z o.o. established a joint-stock company incorporated under Libyan law, under the name of Geofizyka Kraków Libya JSC. The shares in the company are held by two shareholders: Geofizyka Kraków Sp. z o.o. (60% of the share capital) and BARARI Co. For Oil Services (40% of the share capital). The company's share capital amounts to LYD 1,000 thousand and is divided into 10,000 shares with a par value of LYD 100 per share. Upon incorporation of Geofizyka Kraków Libya JSC, the shareholders paid LYD 300 thousand. The balance will be paid within five years from the date of the company's registration. The company's core business is exploration for hydrocarbon deposits in Libya.

The following changes have occurred since June 30th 2008:

- Share capital increase at Pomorski Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 18,555,000, to PLN 614,696,000; the increase was registered with the National Court Register on August 4th 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network;
- Share capital increase at Karpacki Operator Systemu Dystrybucyjnego Sp. z o.o. by PLN 8,841,000, to PLN 1,484,953,000; the increase was registered with the National Court Register on August 22nd 2008; the newly issued shares were acquired by PGNiG in exchange for a contribution of non-current assets comprising the components of a transmission or distribution network.

In H1 2008, PGNiG S.A. consolidated 22 subsidiaries and three indirect subsidiaries. The chart below presents the consolidated companies within the PGNiG Group as at June 30th 2008 (by operating segments).

CONSOLIDATED COMPANIES IN THE PGNiG GROUP



2. Employment

The table below presents the employment at the PGNiG Group's consolidated companies as at June 30th 2008, by segments. PGNiG S.A.'s Head Office provides services to all segments. Accordingly, it is disclosed separately.

Employment by segments (no. of staff)

	Jun 30 2008
Head Office	649
Exploration and Production	10,860
Trade and Storage	3,878
Distribution	13,631
Other activities	2,057
Total	31,075

Since 2000, the PGNiG Group has been implementing the "Programme of employment restructuring and employee protection measures for PGNiG S.A. branches and subsidiaries". The Programme provides for a broad-range restructuring, including:

- Employees' age retirement and early retirement,
- Exercise of the right to pre-retirement benefits,
- Employment of personnel at companies in which PGNiG S.A. holds equity interests and at employee-run companies,
- Employment of personnel at entities cooperating with PGNiG S.A.,
- Reduction of work time for selected work posts and liquidation of work posts.

The Programme has been extended until the end of 2008. In H1 2008, 609 persons were covered by the Group Restructuring Programme.

3. Sales and Supplies

The PGNiG Group recorded sales revenue of PLN 9.3bn, with 88.6% of that figure derived from sales of natural gas.

Sales revenue (PLNm)

	Value
Natural gas, including:	8,200.2
- high-methane gas	7,491.5
- nitrogen-rich gas	708.7
Crude oil	447.4
Condensate	2.0
Helium	13.4
Propane-butane	22.4
Reserve exploration services	385.4
Other sales	188.8
Total	9,259.6

In H1 2008, the PGNiG Group sold 7.4bn m³ of natural gas, with 96% of that figure accounted for by revenues from the transmission and distribution systems and the balance – by direct sales of natural gas from deposits.

Natural gas sales volume (million m³)

	Volume
Sales under tariff	7,027.4
Direct sales from deposits	330.9
Total	7,358.3

In H1 2008, the volume of natural gas acquired by the PGNiG Group reached 7.5bn m³, with 72% of that amount sourced from imports, mostly from Russia and the Middle East. Natural gas production from domestic deposits represented 28% of the total volume acquired. The table below sets forth the structure of natural gas supplies measured as high-methane gas equivalent.

Natural gas supplies (million m³)

	Volume
Imports	5,407.5
Domestic production	2,114.5
Domestic suppliers	7.8
Total	7,529.8

Chapter II: Governing Bodies of PGNiG S.A.

1. Management Board

As at January 1st 2008, the Management Board of PGNiG S.A. had the following composition:

- Krzysztof Głogowski – President
- Jan Anysz – Vice-President and Financial, HR and Restructuring Director
- Zenon Kuchciak – Vice-President and Trading Director
- Stanisław Niedbalec – Vice-President and Director of Investments and Technology
- Tadeusz Zwierzyński – Vice-President and Director of Strategic Projects.

On March 12th 2008, PGNiG S.A.'s Supervisory Board removed the following members from the Management Board of the Company:

- Krzysztof Głogowski
- Zenon Kuchciak
- Stanisław Niedbalec
- Tadeusz Zwierzyński.

On March 12th 2008, PGNiG S.A.'s Supervisory Board appointed the following members to the Management Board of the Company:

- Michał Szubski – as President
- Mirosław Dobrut – as Vice-President and Director of Investments and Technology
- Sławomir Hinc – as Vice-President and Financial and Economic Director
- Radosław Dudziński – as Vice-President and Director of Strategic Projects.

On March 20th 2008, the Supervisory Board of PGNiG S.A. removed Jan Anysz from the Management Board and appointed Mirosław Szkałuba as Vice-President of the Management Board.

As at June 30th 2008, the Management Board of PGNiG S.A. had the following composition:

- Michał Szubski – President
- Mirosław Dobrut – Vice-President and Director of Investments and Technology
- Sławomir Hinc – Vice-President and Financial and Economic Director
- Radosław Dudziński – Vice-President and Director of Strategic Projects
- Mirosław Szkałuba – Vice-President and HR and Restructuring Director.

2. Proxies

As at January 1st 2008, there were two Company proxies:

- Ewa Bernacik
- Bogusław Marzec.

On January 3rd 2008, the Management Board of PGNiG S.A. appointed Jan Czerepok, Waldemar Wójcik and Marek Dobryniewski as proxies. On March 17th 2008, the Management Board of PGNiG S.A. revoked the power of proxy granted to Jan Czerepok and on April 25th 2008 revoked the power

of proxy granted to Bogusław Marzec. On April 29th 2008, the Management Board of PGNiG S.A. appointed Stanisław Radecki as proxy.

As at June 30th 2008, there were four Company proxies:

- Ewa Bernacik
- Waldemar Wójcik
- Marek Dobryniewski
- Stanisław Radecki.

3. Supervisory Board

As at January 1st 2008, the Supervisory Board of PGNiG S.A. had the following composition:

- Andrzej Rościszewski – Chairman
- Piotr Szwarec – Deputy Chairman
- Kazimierz Chrobak – Secretary
- Wojciech Arkuszewski – Member
- Mieczysław Kawecki – Member
- Marcin Moryń – Member
- Mieczysław Puławski – Member
- Mirosław Szałuba – Member
- Jarosław Wojtowicz – Member.

On February 7th 2008, Mirosław Szałuba resigned from the Supervisory Board of PGNiG S.A.

On February 15th 2008, the Extraordinary General Shareholders Meeting of PGNiG S.A. removed Piotr Szwarec, Jarosław Wojtowicz, Andrzej Rościszewski and Wojciech Arkuszewski from the Supervisory Board.

On February 15th 2008, the Extraordinary General Shareholders Meeting of PGNiG S.A. appointed Stanisław Rychlicki and Grzegorz Banaszek to the Supervisory Board.

On April 28th 2008, the Extraordinary General Shareholders Meeting of PGNiG S.A. removed Kazimierz Chrobak from the Supervisory Board, with effect as of April 29th 2008.

On April 28th 2008, the Extraordinary General Shareholders Meeting of PGNiG S.A. appointed Agnieszka Chmielarz, Hubert Konarski, Jolanta Siergiej and Joanna Stuglik to the Supervisory Board, with effect as of April 30th 2008.

As at June 30th 2008, the Supervisory Board of PGNiG S.A. had the following composition:

- Stanisław Rychlicki – Chairman
- Marcin Moryń – Deputy Chairman
- Mieczysław Kawecki – Secretary
- Grzegorz Banaszek – Member
- Agnieszka Chmielarz – Member
- Hubert Konarski – Member
- Mieczysław Puławski – Member
- Jolanta Siergiej – Member
- Joanna Stuglik – Member.

Chapter III: Tariff Policy

1. Licences

As a result of the legal separation of distribution and trade functions in mid 2007, the Company acquired by succession from the Gas Trading Companies six licences for trade in gaseous fuels, two licences for international trade in natural gas and one licence for trade in liquid fuels. With a view to maintaining the transparency of its operations, the Company requested the President of URE to harmonise the licences with PGNiG's new business conditions.

On February 18th and 19th 2008, the President of URE issued decisions in which he declared expiry of the licences for trade in gaseous fuels, granted to the six Gas Trading Companies and two licences for international trade in natural gas granted to Karpacka Spółka Obrotu Gazem Sp. z o.o. and Pomorska Spółka Obrotu Gazem Sp. z o.o., as a result of deletion of the Gas Trading Companies from relevant registers.

As at June 30th 2008, the Company held the following licences granted by the President of URE under the Energy Law:

- one licence for transmission and distribution of gaseous fuels,
- one licence for trade in gaseous fuels,
- one licence for international trade in natural gas,
- one licence for storage of gaseous fuels,
- two licences for trade in liquid fuels.

In H1 2008, the Ministry of Environment granted to PGNiG S.A. six licences for exploration and prospecting of crude oil and natural gas reserves and three licences for production of crude oil and natural gas from reserves. Nine licences for exploration and prospecting of crude oil and natural gas reserves were extended. One licence for production of crude oil and natural gas from reserves and one licence for underground gas storage expired. No changes in the number and terms of the licences for waste matter storage occurred in the period under review.

As at June 30th 2008, the Company held the following licences granted under the Geological and Mining Law:

- 73 licences for exploration and prospecting of crude oil and natural gas reserves,
- 215 licences for production of crude oil and natural gas from reserves,
- 7 licences for underground gas storage,
- 4 licences for waste matter storage.

2. Changes in PGNiG S.A.'s Tariffs

On March 28th 2008, the President of URE issued a decision whereby PGNiG S.A. was released from the obligation to submit for approval tariffs for compressed natural gas, used as fuel in motor vehicles.

Until April 24th 2008, settlements with customers were made according to Tariff No. 4 for Gaseous Fuels approved by the President of URE on March 17th 2006.

On November 15th 2007, PGNiG S.A. applied to the President of URE for approval of the Gaseous Fuel Tariff No. 1/2008 of Polskie Górnictwo Naftowe i Gazownictwo S.A. for the period from January 1st 2008 to March 31st 2008. On February 20th 2008, the Regulation of the Minister of Economy and

Labour on detailed rules for preparing and calculating tariffs for gaseous fuels and on settlements in gaseous fuels trade (Dz.U. of February 20th 2008, No. 28, item 165) became effective, which necessitated changes in the application. On February 20th 2008, the Company amended the application in order to bring it to compliance with the new Tariff regulation.

Under his decision of April 10th 2008, the President of URE approved the Gaseous Fuel Tariff No. 1/2008, in effect from April 25th 2008. The tariff provides for:

- the prices, subscription fees and network rates applicable to settlements with customers receiving gaseous fuels from the transmission grid,
- the prices, subscription fees and network rates applicable to settlements with customers receiving gaseous fuels from distribution networks.

The table below sets forth the prices and rates applied in settlements with customers receiving gaseous fuels from the transmission grid.

Tariff Group	Price of gaseous fuel	Subscription fee
	[PLN/m ³]	[PLN/month]
E1A-E4B	0.8983	600.00
Ls1-Ls4	0.5693	600.00
Lw1-Lw4	0.6645	600.00

The tables below set forth the prices and rates applied in settlements with customers receiving gaseous fuels from the distribution network, by tariff groups.

- High-methane natural gas (E groups)

Tariff Group	Price of gaseous fuel	Subscription fee
	[PLN/m ³]	[PLN/month]
W-1	0.9500	4.30
W-2	0.9350	6.40
W-3	0.9215	7.10
W-4	0.9160	18.00
W-5	0.9100	110.00
W-6	0.9011	130.00
W-6A	0.9011	130.00
W-6B	0.9011	130.00
W-7	0.8993	270.00
W-7A	0.8993	270.00
W-7B	0.8993	270.00
W-8	0.8988	600.00
W-9	0.8988	600.00
W-10	0.8988	600.00

- Nitrogen-rich natural gas (Ls subgroups)

Tariff Group	Price of gaseous fuel	Subscription fee
	[PLN/m ³]	[PLN/month]
Z-1	0.6025	4.30
Z-2	0.5930	6.40
Z-3	0.5840	7.10
Z-4	0.5810	18.00
Z-5	0.5770	110.00
Z-6	0.5710	130.00
Z-7	0.5699	270.00
Z-7A	0.5699	270.00
Z-7B	0.5699	270.00
Z-8	0.5695	600.00
Z-9	0.5695	600.00

- Nitrogen-rich natural gas (Lw subgroups)

Tariff Group	Price of gaseous fuel	Subscription fee
	[PLN/m ³]	[PLN/month]
S-1	0.7030	4.30
S-2	0.6920	6.40
S-3	0.6820	7.10
S-4	0.6780	18.00
S-5	0.6740	110.00
S-6	0.6670	130.00
S-7	0.6657	270.00
S-7A	0.6657	270.00
S-7B	0.6657	270.00
S-8	0.6653	600.00
S-9	0.6653	600.00

The introduction of network rates is a material modification in the tariff. These rates are calculated based on fixed and variable costs incurred in connection with the Company's contracting services for gas transmission, distribution, storage and liquefying, and liquefied natural gas regasification, as well as costs of storage in the Company's own facilities and cost of system balancing and system limitation management.

Moreover, the tariff defines the manner for determination of the charge for exceeding the contractual capacity and of the discount for failure to maintain quality parameters for gaseous fuels and quality standards in customer service.

PGNiG S.A.'s tariff is applied in gaseous fuel supplies under such comprehensive agreements or gaseous fuel sale agreements concluded prior to the tariff effective date, whose performance requires PGNiG S.A. to mandate a third party to transport gaseous fuel over the transmission grid or a distribution network, or to use storage facilities. Under a comprehensive agreement, PGNiG S.A. undertakes not only to sell gaseous fuel to customers but also to ensure its delivery to the delivery point specified by the customer.

On August 12th 2008, PGNiG S.A. applied to the President of URE for approval of an amendment to Gaseous Fuel Tariff No. 1/2008 necessitated by PGNiG's changed business conditions, namely the increase in gas acquisition cost above the level assumed for the calculation of prices in the approved tariff; and for adjustment of the wording of the tariff. The adjustment is to ensure harmonisation of the provisions of Gaseous Fuel Tariff No. 1/2008 with provisions of the tariffs of the Transmission System Operator and Distribution System Operators. Until at the date of this Report, the President of URE has not issued any decision in this respect.

3. Changes in the Tariffs of Distribution System Operators

Until April 24th 2008, settlements with customers receiving gaseous fuels from the Distribution System Operators were made according to Gaseous Fuel Tariff No. 2/2006, approved by the President of URE on March 17th 2006.

In his decision of April 10th 2008, the President of URE approved the Tariff for Gaseous Fuel Distribution Services effective from April 25th 2008 and specifying:

- charge rates for gaseous fuel distribution services and subscription fees,
- manner for determination of fees for connecting to the high-pressure network, as well as of fees for connecting to medium- and low-pressure networks.

Moreover, the tariff defines the manner for determination of the charges for exceeding the contractual capacity, illegal draw of gaseous fuels and failure to comply with the imposed limitations, as well as of the discount for failure to maintain quality standards in customer service.

4. Tariff-Related Risks

Regulatory Risk

The key tariff risk relates to the inadequacy of secondary legislation with regard to the current legal acts concerning the Polish gas market. Such a situation occurred at the turn of 2007, when the lack of a Tariff regulation amended in accord with the amended Polish Energy Law delayed the proceedings related to the approval of the Gaseous Fuel Tariff. The Minister of Economy signed the tariff regulation as late as in February 2008. However, another regulation, crucial for the operation of the gas market and outlining detailed terms of the gas system operation (system regulation), is being drafted.

In 2008, further amendments may be made to the legal acts regulating operation of the gas sector. These amendments will be made, first and foremost, to the Polish Energy Law. Once the amended Law becomes effective, the tariff regulation will need to be amended.

Changes in the legal environment gradually implemented in connection with Poland's accession to the European Union may not allow for the nature of PGNiG S.A.'s business. Further legal changes affecting the operation of gas companies may be introduced in following years. Legal changes, including delays in amendments to legal acts, create risks relating to business adaptation to such changes, which might adversely affect the PGNiG Group's business, financial results and growth prospects.

Calculation Risk

PGNiG S.A.'s ability to cover costs of its core operating activities depends on the prices approved by the President of URE. While approving tariffs for a given period, the President of URE considers other external factors which are beyond PGNiG S.A.'s control. In an attempt to protect weaker customers, while verifying costs of operating activities, the President of URE may consider certain cost unjustified or may reject the assumptions adopted by PGNiG S.A. with respect to main drivers of cost changes and profit targets allowing for business risk. The URE may also refuse to accept tariff prices and charge rates applied for by PGNiG S.A. Lower tariff prices and charges might adversely affect PGNiG S.A.'s profitability.

Forecasting Risk

The current methodology for calculation of prices and charge rates is based on forecast values; accordingly, revenue is encumbered with forecasting risk. Inaccurate estimates of demand affecting the accuracy of forecast purchase and supply volumes, as well as the value of costs on which the determinations of prices and charge rates are based may adversely affect financial results. An increase in demand above the forecast level would necessitate additional purchases under all existing contracts (in numerous cases, at prices higher than those forecast).

Market Risk

Prices of imported gas are determined 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 acquisition cost of imported gas. The market of crude oil and petroleum products has recently been to a large extent unpredictable, given the continual price changes. These material changes in fuel prices on the international markets affect the prices of imported gas. Each, even accurate forecast of changes of natural gas prices is encumbered with a high error risk. There can be no assurance that, despite legal possibility of adjusting prices approved for a tariff term, an increase in the price of imported gas may not be fully passed on customers or the changes in selling prices may lag behind the changes in import prices.

Risk of Competition

In recent years, the increase in prices of fuels on global markets has led to increased interest in exploration activities. There is a risk of competition from other companies active on the Polish market seeking licenses for exploration and prospecting of deposits or the implementation of a strategy providing for acquiring access to own hydrocarbon reserves. At present, competition in the domestic market is limited. However, after having been granted relevant licenses, PGNiG S.A.'s competitors will enter the Polish market. A strong competitive edge may be gained especially by large companies which enjoy established positions on the international markets and have access to much greater financial resources compared with PGNiG S.A., helping them to accept the high risk of exploration activities in Poland.

Chapter IV: Exploration and Production

1. Exploration

In H1 2008, the PGNiG Group conducted work related to exploration and prospecting for hydrocarbon reserves, as part of which it performed 151,882.1 m of drillings, 3,992.5 km of 2D seismic surveys and 3,334.3 km² of 3D seismic surveys. The projects were performed both within the PGNiG Group licences and for external companies domestically and abroad.

1.1. Exploratory Work in Poland

For PGNiG S.A., a total of 30,281 m of drillings were made in Poland, in Carpathian Foreland and Polish Lowlands. Drilling work covered 20 boreholes, including 14 exploratory boreholes and six prospecting boreholes. From among the 15 boreholes with known deposit-related results, six (five gas boreholes and one crude oil borehole) were classified as positive, while nine other boreholes were classified as negative. Furthermore, a total of 410 km of 2D seismic surveys and 273.8 km² of 3D seismic surveys were performed.

Producible reserves of natural gas increased by 945m m³ of high-methane equivalent. The size of the reserves was favourably assessed by the Mineral Reserves Commission and accepted by the Minister of Environment.

In H1 2008, PGNiG S.A. continued joint projects with FX Energy Poland Sp. z o.o. in the following areas: Płotki, Płotki-PTZ, Poznań and Blok 255; it also continued to cooperate with Eurogas Polska Sp. z o.o. and Energia Bieszczady Sp. z o.o. in the Bieszczady area.

1.2. Exploratory Work Abroad

Pakistan

PGNiG S.A. conducts exploratory work in Pakistan under an agreement between PGNiG S.A. and the Pakistani government dated May 18th 2005, concerning exploration and production of hydrocarbons in the area covered by the Kirthar licence. Exploratory work in the Kirthar block area is conducted in cooperation with Pakistan Petroleum Ltd. (interests/project cost participation: PGNiG S.A. – 70%; PPL – 30 %). Based on the results of geological and geophysical studies, it was decided to drill the first exploration borehole. The drilling work is due to start at the end of 2008.

Denmark

On December 6th 2007, PGNiG S.A. executed an agreement concerning assignment of an interest in the 1/05 exploration and production licence in Denmark and took over the operator functions. Interests held in the license: PGNiG S.A. – 40%, Odin Energi A/S – 40%, Nordsofonden – 20%. On April 5th 2008, by virtue of the decision of the Danish Energy Agency, the licence was extended until October 5th 2009, contingent on performing a 3D seismic shot covering an area of not less than 50 km². In 2008, 48 km of 2D seismics has been reprocessed; additionally, there are also plans to reprocess approx. 1,000 km of 2D seismics with a view to locating the 3D shot.

Egypt

In 2007, PGNiG S.A. won a tender for the Bahariya exploration and production license (Block 3) in Egypt. The licence covers an area of 4,414.4 km². In July 2007, the Production Sharing Agreement was initialled. Following the ratification of the PSA, PGNiG S.A. plans to perform reprocessing activities and carry out 1,450 km 2D of seismic surveys.

Norway

For the purposes of the Norwegian Continental Shelf project, PGNiG S.A. established PGNiG Norway AS. On October 30th 2007, PGNiG Norway AS acquired from Mobil Development Norway A/S and ExxonMobil Production Norway Inc a 15% interest in the three PL 212, PL 212B and PL 262 licences covering the Skarv and Snadd fields. The remaining interests are held by British Petroleum, as the operator – (30%), StatoilHydro (30%) and E.ON Ruhrgas Norge (25%). PGNiG Norway AS's core business comprises exploration and production of crude oil and natural gas reserves in the Norwegian Continental Shelf and participation in infrastructural projects related to crude oil and natural gas transmission activities at sea.

Reserves are developed by BP and PGNiG Norway AS, StatoilHydro and E.ON Ruhrgas. As a result of combining the Skarv and Snadd fields with the Idun field in the Norwegian Continental Shelf, the companies' approximate shares in the exploration and production area are as follows:

- British Petroleum (the operator) 24%
- StatoilHydro 36%
- E.ON Ruhrgas Norge 28%
- PGNiG Norway AS 12%.

At present, the Skarv project is in the reserve development stage. Production is expected to commence in 2011. Under the development project, 16 boreholes will be drilled, including seven oil extraction boreholes, five natural gas extraction boreholes and four injectors. At a later stage of the reserve life, the injectors will be transformed into gas producers in order to fully exploit the reserve potential. Drilling equipment will be mobilised in June 2009.

Libya

In 2007, PGNiG S.A. won a tender for provision of operating services and obtained the right to carry out exploration on the exploration and production under the exploration and production licence no. 113 located in the Murzuq petroleum basin (western Libya). On February 4th 2008, PGNiG Finance B.V. was transformed into Polish Oil and Gas Company Libya B.V. for the purposes of the project execution in Libya. On February 25th 2008, POGC-Libya B.V. signed the Exploration and Production Sharing Agreement (EPSA) with state-owned Libyan company National Oil Corporation. PGNiG S.A. issued a warranty securing performance by POGC-Libya B.V. of the licence obligations under the agreement. EPSA was ratified by the Libyan government on June 1st 2008. Currently, POGC-Libya B.V. and National Oil Corporation conduct preparatory work regarding 2D and 3D seismic surveys, which are scheduled to begin at the end of 2008.

1.3. Exploration Services

In H1 2008, exploration and production companies conducted drilling work, maintenance and geophysical work for the PGNiG Group and third parties. Drilling work was performed mostly in the south-east and north-west of Poland. Preparations regarding drilling work and maintenance on the

Bonikowo and Kosakowo underground gas storage facilities were commenced. In Poland, as part of services rendered to external investors, boreholes were drilled for RWE Dea Polska Sp. z o.o.; additionally, boreholes were drilled in areas covered with copper deposit licences. A major part of the companies' revenues was derived from services ordered by foreign investors. Drilling projects were performed in Kazakhstan, Pakistan, Egypt, Libya, Mozambique, Uganda and Hungary. Additionally, drilling of a geothermal well was commenced in Germany.

Specialist maintenance related to borehole mining was performed by the exploration and production companies chiefly in Poland. The performed services included production intensification, flushing, cementing, and other specialist drilling, measuring and laboratory services. The companies also performed reconstruction and drill liquidation services; they also liquidated the effects of borehole mining. The main customers for the services performed in Poland were the PGNiG Group companies. Maintenance work was also performed for investors outside of the PGNiG Group, including KGHM Polska Miedź S.A., FX Energy Poland Sp. z o.o., PRWiG Warszawa and Petrobaltic S.A. The exploration and production companies also provided services to customers in such countries as Kazakhstan, Ukraine, Lithuania and Latvia.

The exploration and production companies provide geophysical services related to field seismic surveys, processing and interpreting seismic data, and taking geophysical measurements. Geophysical services were performed both in Poland and abroad, mainly for customers outside of the PGNiG Group. Foreign markets included India, Pakistan, Libya, Syria and Germany. Furthermore, the companies provided geophysical drilling services in certain EU states, including the Netherlands, Latvia, Hungary and Slovakia.

2. Production

Two of PGNiG S.A.'s branches, the Zielona Góra Branch and the Sanok Branch, carry out production of natural gas and crude oil in Poland. As a result of a merger, the Zielona Góra Branch produces crude oil and nitrogen-rich natural gas at 21 mines (including 12 gas mines, and 9 oil and gas mines), while the Sanok Branch produces high-methane natural gas and crude oil at 47 mines (including 25 gas mines, and 22 oil mines and oil and gas mines).

In H1 2008, PGNiG S.A. produced a total of 2,114.5m³ of natural gas (high-methane equivalent) – 1,221.7m³ was produced by the Zielona Góra Branch, and 892.8m³ by the Sanok Branch. Total production of crude oil was 249.5 thousand tones in H1 2008. The table below sets forth PGNiG S.A.'s production in H1 2008:

Production structure

	Product	Unit	Quantity
1.	Natural gas	million m ³ *	2,114.5
2.	Crude oil	thousand tonnes	249.5
3.	Condensate	thousand tonnes	5.1
4.	Sulphur	thousand tonnes	10.8
5.	Propane-butane	thousand tonnes	8.6
6.	Helium	million m ³	1.2
7.	LNG	million m ³ *	10.3

* High-methane equivalent

In H1 2008, a total of four boreholes were put in operation in the Sanok Branch area (Tarnów-81 k, Rzeszów-9, Mirocin-62g,d, Wierzchosławice-5); in the case of the Zielona Góra Branch, two new boreholes were commissioned (BU-101 H and Sławoborze-1). The new boreholes increased the natural gas production capacity by ca. 260 m³/min.

In H1 2008, PGNiG S.A. conducted a number of projects aiming to increase natural gas and crude oil production and maintain the current level of production. In order to achieve hydrocarbon production from the existing fields, 5,647 m of operational drill holes were performed in the following fields: Radlin, Sędziszów, Dzieduszyce and Cierpisz. With a view to limiting the natural decline in production, 24 non-producing boreholes were overhauled (14 overhauls were completed).

In connection with a pressure decrease at interconnector terminal points on the reserves in Palikówka and Kuryłówka, it was necessary to install compressors. Increasing gas pressure to an adequate level will be instrumental in maintaining the level of production and transfer of natural gas to the transmission system. There are plans to install two more compressors on the Jodłówka reserve.

In H1 2008, the exploration and production segment was engaged in off-tariff sale of natural gas, as well as sale of crude oil and other products. The table below presents sales of the key products.

The table below sets forth sales of the key products to third parties:

Unit	Quantity	
Natural gas	million m ³	330.9
Crude oil	thousand tonnes	257.7
Condensate	thousand tonnes	0.6
Helium	million m ³	1.1
LPG	thousand tonnes	8.7
Nitrogen	thousand kilos	624.9
Sulphur	thousand tonnes	10.9

The segment uses underground gas reserves. The chief objective of underground gas storage is to balance the differences between the demand for natural gas in the winter and summer seasons. Besides, the underground storage facilities enable optimum production from domestic deposits during the year and provide tools for rational management of natural gas reserves.

3. Planned Exploratory Work

Exploratory Work in Poland

In 2008, exploratory work is planned mainly in the following regions of southern and western Poland:

- Lubaczów-Tarnogród
- Przemyśl-Jarosław
- Rzeszów-Łańcut-Kolbuszowa
- Pilzno-Tarnów
- Ostrów Wielkopolski-Pogorzela
- Środa Wielkopolska-Jarocin (cooperation with FX Energy Poland Sp. z o.o.)
- Świebódzin-Wolsztyn-Nowy Tomyśl
- Pniew-Stęszew
- Gubin-Krosno Odrzańskie
- Sulęcín-Międzyrzecz
- Kostrzyn-Myślibórz
- Międzychód-Gorzów Wielkopolski
- Wronki-Sieraków.

Exploratory Work Abroad

In H1 2008, the PGNiG Group took a number of steps to acquire new sites for exploration and new licence areas in such countries as Algeria, Iraq, Morocco and Tunisia. All these efforts will be continued in 2008. Furthermore, the PGNiG Group plans to press ahead with the exploratory work in the licence areas in Pakistan, Denmark and Norway, and to start geophysical surveys under the licence in Libya.

Field Exploration Services

In H2 2008, the exploration and production companies plan to strengthen their position in drilling and maintenance services on the Polish market, which is treated as strategic, and to win new orders on foreign markets. With the contracts executed so far, the companies will continue their operations in Kazakhstan, Pakistan, Libya, Mozambique and Uganda, as well as in Ukraine, Hungary and Latvia. They plan to start drilling the next geothermal hole in Germany and to perform reconstruction work in Russia. As regards geophysical works, the companies seek to further strengthen their position in Poland and in selected foreign markets by expanding the range of services rendered and more optimally utilising their resources. They are also expected enter new foreign markets, such as Thailand, Egypt, Turkey, Yemen or Saudi Arabia.

Natural Gas Production

PGNiG S.A. is following an investment programme aimed at increasing, in a longer perspective, the natural gas production capacity. As part of the programme, the Company plans to develop new reserves and boreholes, modernise and expand the existing natural gas mines, and build new underground gas storage facilities and expand the existing ones. Moreover, PGNiG will take steps to maintain the volume of hydrocarbons production from fields already in use at the current levels.

In 2008, the Company envisages to commence production in ten boreholes (Kowale-2; Luchów-1, 3; Cierpisz-2, 3, 4; Wola Różaniecka- 2, 12, 14, 16), whose aggregate production capacity amounts to approximately 196 m³/min. By 2010, PGNiG S.A. plans to develop 20 reserves through the Sanok Branch and 10 through the Zielona Góra Branch.

2010 is to see completion of the construction of the Grodzisk Nitrogen-Removal Plant, with the annual throughput capacity of feedstock gas amounting to 500m m³. The project provides for development of the reserves located in the Nowy Tomyśl-Grodzisk region and of the gas extracted from the Lubiatów-Międzychód-Grotów (LMG) reserves, as well as the construction of a second controller, besides the Odolanów Branch, connecting the system for extraction of nitrogen-rich gas to the high-methane gas transmission network.

The current forecast assumes that the natural gas production volume will reach approx. 4.2bn m³ in 2008 and approx. 4.6bn m³ in 2009. The decrease in natural gas production, relative to **previous** forecast, is primarily due to drilling in increasingly difficult geological and mining conditions. Moreover, in H1 2008 we reported failure of two gas compressor stations in the gas transmission system operated by OGP GAZ-SYSTEM S.A., a process stoppage in gas collection by one of the customers of the Sanok Branch, and delayed supply of field compressors.

Crude Oil Production

Development of the Lubiatów-Międzychód-Grotów (LMG) reserve and intensified production from the Barnówko-Mostno-Buszewo (BMB) reserve are two projects aimed at increasing PGNiG's crude oil production output. The Company will seek to intensify production from the BMB reserve, which will include development of five production boreholes. In 2008, crude oil production is forecast to reach 509 thousand tonnes. A significant increase in crude oil production is expected in 2013, when the LMG reserve is developed and placed in operation, and is to amount to approx. 0.9m tonnes annually.

4. Risks Related to Exploration and Production

Resource Discoveries and Estimates

The main risk inherent in exploration activity is the risk of reserve discovery, i.e. the exploratory risk. This means that not all the identified potential reserve sites have sufficient deposits of hydrocarbons. Whether or not such deposits exist depends on a number of geological factors. Furthermore, the actual quantity and quality of the accumulated hydrocarbons may differ from expected. When the results of successful exploration activity, in the form of documented new reserves, do not offset the production from the existing deposits, the PGNiG Group's documented producible reserves will decrease pro rata to the current production volumes.

A number of the factors and assumptions adopted when determining the extent of resources and production projections may turn out erroneous due to flaws in the methods and measurement equipment used in the geophysical surveys, drilling and production testing. Data on economically viable producible reserves of crude oil and natural gas is actually estimated and the 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 the full business cycle from the commencement of exploration to the launch of production from a developed field lasts six to eight years, while the hydrocarbon production cycle lasts from 10 to 40 years. Deposit parameters established in the course of preparing the relevant documentation are reviewed upon deposit development. Each downgrade of the extent of the resources, the extraction schedule or financial figures may lead to a lower revenue and adversely impact the PGNiG Group's financial performance.

Competition

Both on the Polish market and abroad there is a risk of competition from other companies with respect to acquisition of licences for exploration and prospecting of deposits or implementation of a strategy

providing for acquiring access to own hydrocarbon reserves. In the light of the growing global interest in new exploration and economic expansion areas this risk appears to be high. Certain competitors of the PGNiG Group, especially those active globally, enjoy strong market positions and have financial resources larger than those of the PGNiG Group. Thus it is probable that such companies would submit their bids in tender offers and be able to acquire promising licences. Competitors are also able to define, value, offer and purchase numbers of fields (including the operation thereof and underlying licences) larger than it would be possible in the case of the PGNiG Group, given the Group's financial and human resources. This competitive edge of other market players is particularly important on the international market.

Delayed Work

Under the currently binding Polish legal regulations, obtaining a licence for exploration and prospecting of crude oil and natural gas deposits lasts from one to one and a half year. As regards business activity on foreign markets, it 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 obliged to arrange for numerous formalities, 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 for a work contractor. Under the currently binding legal regulations, another several months pass before an agreement with the work contractor is signed. In addition, companies must frequently wait for a very long time before their imported equipment receives customs clearance. These factors create the risk of delayed exploratory work.

Formal and legal issues beyond the PGNiG Group's control include:

- local governments' failure to adopt local land development plans (MPZPs)
- obstacles in incorporating investment projects into the MPZPs
- need to obtain and comply with administrative or other formal and legal decisions, including environmental decisions
- amendments to the current planning and development concept
- 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, the PGNiG Group's obligation to comply with the Public Procurement Law frequently prolongs 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 Exploratory Work

Exploratory work is capital consuming, given the prices of energy carriers and materials. Cost of exploratory work is especially sensitive to steel prices, which are passed on 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. Profitability of foreign exploratory projects will to a significant extent depend on the movements in prices of oil derivative products and in exchange rates.

Legal Regulations Concerning Safety, Environmental Protection and Health

Ensuring compliance with environmental law in Poland and abroad might significantly increase the PGNiG Group's costs of operations. Currently, the PGNiG Group incurs significant capital expenditure and costs on harmonising its operations with ever more complex and stringent legal regulations concerning safety and health at work, as well as environmental protection. 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 Nature 2000 sites more stringent and enhanced the environmental protection-related requirements in the scope of entering the areas of the occurrence of protected plant species and habitats of protected animals. The tendency to tighten up the environmental protection regulations is clear also in other countries where the PGNiG Group conducts exploratory activity.

Qualified Personnel

The presence of foreign companies on the Polish market intensified the companies' takeover of highly qualified employees with vast professional experience. This risk is especially high with respect to professionals specialised in the exploration of natural gas and crude oil deposits. In countries where the PGNiG Group operates highly qualified staff is difficult to recruit.

Unpredictable Events

Hydrocarbon reserves developed by the PGNiG Group are usually located at great depth, which is accompanied by extremely high pressures, and many of them include hydrogen sulphide in its chemical composition. Consequently, there exists a high degree of risk of an explosion, eruption or hydrocarbon leakage, which in turn may pose a threat to people (workers and local inhabitants), natural environment and also production equipment.

Changes in Legal Regulations

The legal regulations in some countries change frequently and unexpectedly, causing problems to entities conducting exploratory activity. This may be a particular threat in countries where law changes depend on the decisions of authoritarian governments.

Political and Economic Situation

Some countries where the PGNiG Group carries out exploratory activity face the risk of armed conflicts or terrorist attacks, which may result in limitation, suspension or discontinuation of the exploration and production business there.

In some areas of the PGNiG Group's operations there is a risk of social and political destabilisation. Changes of governments may bring to a halt the processes of state administration issuing permits to conduct business activity related to oil. Additionally, these countries are at risk of internal conflicts and social unrest caused by poor social and demographic conditions in which the inhabitants of these countries live. The risks specified above may lead to limitation, suspension or discontinuation of the Company's operations.

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

Chapter V: Trade and Storage

1. Structure of Sales and Purchases

The key products sold by this segment are methane-rich natural gas and nitrogen-rich gas. The sales structure of the PGNiG Group in H1 2008 is presented in the table below.

Sales structure of key products

	Product	Unit	Quantity
1	Natural gas, including:	million m ³ *	7,027.4
	- methane-rich gas	million m ³ *	6,574.1
	- nitrogen-rich gas*	million m ³ *	453.3
2	Propane-butane	thousand tonnes	1.0

* Million m³ measured as methane-rich gas equivalent

The Group's main customers who purchased natural gas included chemicals sector, the steel industry and the power sector, as well as households. The table below presents the structure of natural gas sales measured as methane-rich gas equivalent broken down by major customers.

Sales of natural gas supplied via the transmission system (million m³)

	Sales	Quantity	%
1.	Industrial customers	4,164.6	59.3%
2.	Trade and services	805.8	11.5%
3.	Households	1,970.7	28.0%
4.	Wholesale customers	66.9	0.9%
5.	Exports	19.4	0.3%
Total:		7,027.4	100.0%

Households make up the largest group of customers purchasing natural gas, accounting for 97% of the entire customer base (approx. 6.3m). Their share in the sales volume is 28%. The most prominent share in the natural gas sales was claimed by industrial customers (59%).

In H1 2008, the PGNiG Group derived natural gas from imports and, to a limited extent, from domestic suppliers. Natural gas was primarily sourced from the East, i.e. from Russia and Central Asia. The table below presents the natural gas supply structure measured as methane-rich gas equivalent.

Structure of natural gas supplies by supply sources (million m³)

Gas supplies		Quantity	%
1.	Imports, including:	5,407.5	99.9%
	- OOO Gazprom eksport	3,896.9	72.1%
	- ROSUKRENERGO AG	1,093.3	20.2%
	- Other foreign suppliers	417.3	7.7%
2.	Domestic suppliers	7.8	0.1%
Total:		5,415.3	100.0%

2. Major Commercial Agreements

Purchase Agreements

In H1 2008, PGNiG S.A. imported natural gas mainly under the agreements and contracts specified below, i.e. the long-term contracts for imports from OOO "Gazprom Eksport" and VNG-Verbundnetz Gas AG, as well as medium-term contracts for supplies from ROSUKRENERGO AG and VNG-Verbundnetz GAS AG/ E.ON Ruhrgas AG:

- Contract for sales of Russian natural gas to the Republic of Poland, executed with OOO "Gazprom Eksport", dated September 25th 1996, which will remain in force until 2022;
- Agreement on sales of the Lasów natural gas executed with VNG-Verbundnetz GAS AG, dated August 17th 2006, which will remain in force until October 1st 2016;
- Agreement on sales of natural gas executed with VNG-Verbundnetz GAS AG/E.ON Ruhrgas AG, dated September 15th 2004, which will remain in force until September 30th 2008;
- Agreement on sales of natural gas executed with ROSUKRENERGO AG, dated November 17th 2006, which will remain in force until January 1st 2010 and may be extended until January 1st 2012.

Sale Agreements

In H1 2008, PGNiG S.A. signed comprehensive agreements for supply of gaseous fuel, from both transmission and distribution systems, to 33.6 thousand new customers, of which the majority are households (32.9 thousand).

The Company also executed agreements for the supply of crude oil to refineries of the Orlen Group, including Rafineria Trzebinia S.A. and Rafineria Nafty Jedlicze S.A. As far as supplies via pipelines are concerned, the agreement concluded with BP International for the sale of crude oil abroad was replaced with an agreement with TOTSA TOTAL OIL TRADING S.A. The terms of export sales of crude oil remain unchanged.

3. Underground Storage Facilities

The segment uses a part of the capacities of underground storage facilities for its own purposes. Short-term fluctuations in the demand for natural gas are balanced out with the supplies from the Underground Gas Storage Cavern Facility Mogilno located in worked-out salt caverns, which is operating at full capacity. The capacities of the Underground Storage Facility Wierzchowice and the Underground Storage Facility Husów are used to minimise the effect of an uneven demand for natural gas in summer and winter seasons, to meet the obligations under the Take or Pay Contracts for

imports, to safeguard the continuity and security of natural gas supplies and to meet the obligations under sales agreements providing for the delivery of natural gas to customers' premises.

In addition, the capacities of the Underground Storage Facility Wierzychowice, Underground Storage Facility Husów and the Underground Gas Storage Cavern Facility Mogilno help the Group comply with the 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 a Threat to National Fuel Security or a Disruption on the Petroleum Market, dated February 16th 2007.

4. Activities Planned in the Trading Segment

LNG Terminal

As part of its strategy to diversify natural gas supplies and meet the increased demand for natural gas, the PGNiG Group is involved in a project consisting in importing liquefied natural gas to Poland.

PLNG Sp. z o.o., of which 100% shares have been acquired by PGNiG S.A., is constructing a LNG regasification terminal in Świnoujście. PLNG Sp. z o.o.'s main objective is to conduct regasification operations, and in particular unloading, reloading and regasification of LNG at the LNG terminal. The adopted projections provide for the initial volume of gas supplies from the LNG terminal to the network approximating 2.5bn m³ *pa*. Depending on the demand for gas, the annual throughput may increase to 5bn m³ *pa*, with the target throughput of 7.5bn m³ *pa*.

In H1 2008, the work on the construction design of the LNG terminal and efforts aimed at obtaining the required building permits were in progress. On January 10th 2008, an agreement was signed with SNC Lavalin Services Ltd. for the preparation of technical and economic documentation of the LNG terminal, together with the necessary permits.

In August 2008, the Council of Ministers requested the Minister of State Treasury to supervise the LNG terminal in Świnoujście. Such supervision will be possible due to a transfer of the majority stake in Polskie LNG Sp. z o.o. to OGP GAZ-SYSTEM S.A. On August 28th 2008, the Minister of State Treasury met the Management Boards of PGNiG S.A. and OGP GAZ-SYSTEM S.A. to discuss the acquisition by OGP GAZ-SYSTEM S.A. of 100% shares in Polskie LNG Sp. z o.o., a company established for the purpose of construction of the LNG terminal in Świnoujście.

In H2 2008, PGNiG S.A. will continue work on the sourcing of LNG by concluding a long-term contract for LNG supplies.

The Baltic Pipe Project

The objective of the project is to create a direct pipeline for the supply of natural gas from Denmark to Poland and also, in the future, from Poland to Denmark.

In H1 2008, pursuant to a cooperation agreement executed by PGNiG S.A., OGP GAZ-SYSTEM S.A. and Energinet.dk on November 15th 2007, the parties jointly conducted technical analyses and worked on the detailed arrangements relating to the execution of the Baltic Pipe project. To date, the technical analyses focused on the agreement on the different scenarios concerning technical capabilities of natural gas transmission in the subsequent years of project execution, taking into account the necessary extension of the Danish and Polish transmission systems.

Currently, the Baltic Pipe project has entered the stage of preparations for its execution. According to the project schedule, the gas pipeline is to be placed in operation in 2013, with a target throughput within the range of 3bn m³ *pa*. Under the various scenarios, the length of the pipeline varies from 260

to 290 km. The gas pipeline is to run through the Danish and Polish territorial waters, however, its largest section is to be located in the waters of the Polish, Danish, Swedish or German exclusive economic zones. According to the current concept, OGP GAZ-SYSTEM S.A. is to take responsibility for the execution of the Baltic Pipe project going forward. The handing over of the project is in progress.

The Skanled Project

In 2007, PGNiG S.A. joined the consortium established for the purpose of construction of the Skanled gas pipeline which is designed to connect a gas terminal on the Norwegian Continental Shelf with Sweden and Denmark. PGNiG S.A. acquired a 15% stake in the project and became one of its 15 shareholders. The investment is executed by Gassco, a Norwegian operator of off-shore gas pipelines. In January 2008, the Skanled Consortium approved the technical changes in the design, consisting primarily in the increase of the pipeline diameter in order to raise its throughput. On April 17th 2008, the members of the Consortium resolved to commence the pre-design stage of the project and concurrently approved the changes to the technical concept of the network proposed by Gassco, which increased the estimated cost of the project. The investment decision is planned to be made in October 2009. According to the project schedule, the Skanled gas pipeline is to be placed in operation in 2013.

Concurrently, PGNiG S.A. is working on the transfer of its stake in the Skanled Project to its Norwegian subsidiary, PGNiG Norway AS.

Natural Gas Purchase

PGNiG S.A. does not plan to introduce any changes in the structure of supply sources in 2008, or to make any changes to the effective natural gas purchase agreements. Steps are being undertaken to ensure gas supplies in connection with the expiry, on September 30th 2008, of the gas sale agreement executed with VNG-Verbundnetz Gas AG/ E.ON Ruhrgas AG dated September 15th 2004.

Natural Gas Sales

The projected rise in the natural gas sales volume is attributable to development investments of PGNiG S.A.'s strategic customers in the petrochemical, construction and steel sectors. In 2007, PGNiG S.A. established cooperation on possible gaseous fuel supplies with several major prospective customers, including companies operating in the power sector and planning to replace hard coal fired generating units with gas fired ones. In addition, the forecast increase in natural gas sales volume to customers from the petrochemical, construction and power sectors is further attributable to the favourable market conditions in these sectors, encouraging such customers to invest in gradual expansion of their capacities, which is reflected in their higher demand for natural gas.

5. Trade- and Storage-Related Risks

High Natural Gas Prices

The major risk factor posing a threat to gas market growth is a high price of natural gas. Pursuant to the medium- and long-term import contracts to which PGNiG S.A. is a party, prices of natural gas are computed in accordance with pricing formulas based primarily on crude oil derivatives whose prices are closely linked to the quoted prices of crude oil. In H1 2008, the price of crude oil in global exchanges rose significantly. In spite of the present decrease in crude oil prices, the prices of natural gas may remain high throughout H2 2008 on account of the effect of the H1 2008 surge in crude oil prices on the average reference period applied to purchase formulas, and the weaker zloty exchange rate against the dollar.

Competition

At present, the PGNiG Group is the largest supplier of natural gas in Poland. The Group's share in the gas market is approx. 98%, the remaining 2% is represented by suppliers from outside the PGNiG Group which usually purchase gas from the PGNiG Group. Suppliers from outside the PGNiG Group which trade in natural gas operate mostly in the areas which have not yet been covered by the gas pipeline networks. Some of the aforementioned companies own a transmission infrastructure. Recently, new entities are becoming increasingly active on the Polish market. These entities are local gas distributors which offer innovative solutions of the natural gas supply involving the use of LNG. An intensified commercial activity of competitors which aims at attracting current and potential customers of the PGNiG Group may pose in the future a tangible threat of customer churn.

Substitution

The rapidly rising gas prices pose a serious threat. The surge in fuel prices may translate into lower consumption owing to cost-saving by customers and their transition to alternative fuels. In view of the rising gas prices, some customers seek alternative gas suppliers or consider changing the energy source. This trend may cause a loss of prospective benefits, which would result from customers being provided with services by of competitors.

Gas Supplies

In the previous years, the deliveries of natural gas from the eastern markets were disrupted. Taking into consideration the difficult relations with the main supplier of natural gas, as well as between the main supplier and the transit countries, similar incidents are likely to occur in the future.

LNG Terminal

The key risk related to the LNG Project concerns LNG supplies on the terms acceptable to PGNiG S.A. The lack of security in the form of a long-term contract for LNG supplies can result in a failure to attain one of the key objectives of the LNG Project – the diversification of LNG supplies.

Meeting the deadline for the terminal construction is important. If the projected date of the first deliveries and the completion of the project are not concurrent, the party ordering natural gas may have to incur additional costs.

Baltic Pipe Project

The key to success of the concept of transmitting natural gas from the Norwegian Continental Shelf to Poland is the coordination of the Baltic Pipe Project and Skanled Project, as well as of the steps taken to obtain the necessary flow capacity in the Danish transmission system. Main threats which might cause delays in the implementation of the Baltic Pipe Project timetable include a protracted process of obtaining administrative and environmental permits, and a limited access to materials, specialist equipment or qualified personnel.

Skanled Project

The construction of the Skanled Pipeline is conditional upon numerous factors, including principally the execution, by all Consortium members, of gas purchase agreements providing for sufficient quantities of natural gas. Another factor upon which the pipeline construction in line with the current concept is conditional is Ineos's construction of an ethane separation unit in Rafnes, the unit being one of the key elements of the Skanled Project. The execution of the Skanled Project in line with the timetable requires timely obtainment of necessary administrative permits. Moreover, PGNiG S.A.'s

participation in the Project depends upon the final decision concerning implementation of the Baltic Pipe Project and PGNiG S.A. obtaining the required flow capacity in the Danish transmission system.

Chapter VI: Distribution

1. Business of the Distribution System Operators

Before April 25th 2008 the Distribution System Operators used in their settlements with customers the tariff which was effective before the separation of the distribution function from trade and was not adjusted to the business profile of the Distribution System Operators. The tariff did not include the costs incurred in connection with the operation of the Operators' assets, reduced their revenues and restricted their growth and investment opportunities.

On April 10th 2008, the President of URE issued a decision on the approval of Tariff No. 1 for the provision of gaseous fuel distribution services, effective as of April 25th 2008. The increase in the price of the distribution service was calculated based on the cost of operation of the distribution assets acquired by the Distribution System Operators.

In H1 2008, PGNiG S.A. made an in-kind contribution to the Distribution System Operators in the form of network assets which previously represented an element of a transmission network and were managed by OGP GAZ-SYSTEM S.A.

The core business activity of the Distribution System Operators is the transmission of high-methane and nitrogen-rich gas as well as small quantities of propane-butane and coke-oven gas. In H1 2008, in order to increase the volume of transmitted gas and maintain their current market positions, the Distribution System Operators extended and modernised their gas networks and connected new customers to their distribution grids.

The Distribution System Operators modernised gas piping with long operating lives and largely worn out, which did not guarantee the safe operation of the gas system. The Distribution System Operators also replaced the most failure-prone sections of cast iron piping whose continued operation posed a safety hazard and resulted in substantial gas loss. The implementation of the programme of replacement of cast iron piping and the regular technical inspections of the network resulted in a drop in the share of gas loss in sales. The modernisation work also included changing a pipeline route, which resulted from changes in zoning plans or claims raised by the owners of land through which the pipeline was routed.

The Distribution System Operators also connected new customers to both the existing and extended networks. The Operators took steps to obtain co-financing for the projects of delivering gas to new areas under the EU Operational Programme – Infrastructure and Environment.

The major investment projects related to the extension of gas infrastructure carried out by the Distribution System Operators in H1 2008 included:

- continuation of the construction of the Bytów-Słupsk pipeline commenced in 2007; the primary objective of the Bytów-Słupsk extension is to improve security of gas supplies to Słupsk and its vicinity, as well as to enable connection of municipalities and communes located along the pipeline to the gas network; this project will connect the two gas systems supplying the Pomerania region, i.e. the system covering the area serviced by POSD Sp. z o.o. and the system operated by WOSD Sp. z o.o.;
- extension of the gas grid in Toruń in order to improve security of gas supplies to Toruń, industrial customers, as well as Łysomice and Wielka Nieszawka communes and the Pomeranian Special Economic Zone;
- construction of the Moroczyn-Werbkowice high-pressure transmission pipeline, completed in H1 2008, which was designed to connect the Ukrainian high-pressure network with the

- domestic gas grid; the investment project will also activate potential customers and ensure higher volumes of distributed gas;
- Stage 1 of the project aimed at delivering gas to the communes located to the west of Częstochowa, involving the construction of gas networks in the area of Herby and Blachownia communes; the project includes the construction of approx. 32 km of network.

The table below presents the volume of gas transmitted through the distribution grid, the length of the distribution network, the number of metering devices and the employment as at June 30th 2008.

Key information on the Distribution System Operators

Distribution System Operators	Unit	DOSD	GOSD	KOSD	MOSD	POSD	WOSD
Volume of gas transmitted through the distribution system	'000,000 m ³	502.5	740.0	1,108.2	1,031.4	474.5	938.8
Length of network (excluding connections)	km	7,558.9	20,386.1	43,685.4	17,894.9	8,825.8	14,353.0
Number of metering devices	'000	743.4	1,294.7	1,394.5	1,475.1	734.2	889.0
Employment	person	1,371	2,554	3,289	2,892	1 738	1,787

In Q2 2008, the process of switching the left-bank part of Poznań and the East Poznań Province from less caloric nitrogen-rich gas to high-caloric high-methane gas was launched. This process will improve the security and capacity of the distribution network. The switching process will be completed in 2009.

On June 3rd 2008, an experimental CNG fuelling station was opened in Toruń under an agreement concluded between POSD Sp. z o.o., Toruń Municipality, Toruń Municipal Transportation Company, Biogaz Inwestor Sp. z o.o. and the Bydgoszcz Gas Company. The experimental nature of the investment project follows from the fact that the station is to ultimately use biogas as fuel for vehicles.

2. Planned Directions for Development in the Distribution Segment

Poland's economic growth and its membership in the European Union positively affect the condition of energy businesses, contributing to the increase of demand for natural gas. The economic growth and consequent increase in people's income entail rapid growth of construction market, which in turn offers prospects of higher natural gas sales. The growth of natural gas sales volumes is reflected in the quantities of natural gas transmitted and indirectly affects the economic condition of the Distribution System Operators.

In the next few years, the Distribution System Operators will focus on maintaining their existing market position and further increasing the volumes of transported gas through:

- extension of pipeline infrastructure for new customers,
- replacement of cast iron piping and modernisation of high-, medium- and low-pressure networks,
- overview of infrastructure, with a particular focus on an overview of reduction and metering stations in terms of their profitability,
- use of new natural gas distribution systems by employing CNG and LNG technologies,
- delivery of natural gas to the areas that are not serviced by gas distribution companies,
- implementation of IT tools to analyse network operation in order to determine free capacities and "bottlenecks",

- cooperation with local and territorial authorities.

3. Risks Related to Distribution

Direct Competition

The liberalisation of the gas market resulting from the legal requirement to separate gas trading from distribution is likely to boost activity of competitors. The activity of natural gas suppliers has proved regular and steady for the last several years. They gradually developed their gas networks and acquire new customers, both among individuals and businesses. Additionally, since an increased marketing activity aimed at soliciting customers of Distribution System Operators could be observed on the part of competitors, the actual threat of losing these customers for the benefit of competition may occur in the future.

Legislation

The negative phenomena observed in the Polish legal system include inconsistency or duality of the applicable laws (the Construction Law and the Supervision Law regulating the construction of gas pipeline networks being a case in point) as well as permanent delays in drafting secondary legislation for the purposes of statutes under which it is issued. This leads to differing interpretations of the laws. Another adverse factor is the lack of understanding for the needs of the gas industry as opposed to strong support in the case of other fuels, especially coal.

Payments to Third Parties

Maintaining business profitability by Distribution System Operators is threatened to a large extent by the Operators' obligation to make payments to third parties. The obligation rests on the Distribution System Operators under relevant laws (charges for blocking a road lane and charges paid for gas networks located under public roads), as well as a draft regulation (charges for gas networks which are to be ultimately put under supervision of the Office of Technical Inspection (*Urząd Dozoru Technicznego*)). Distribution System Operators are bound to post lower sales revenues as a result of separation of trading activities from distribution, which in turn will affect profits and development prospects.

Chapter VII: Other Activities

In H1 2008, the segment performed work for the Group's own purposes as well as for external customers in Poland and abroad.

In H1 2008, the segment companies mainly executed work related to construction of medium and high pressure gas pipelines, production of drilling equipment, construction and assembly work concerning: development of natural gas deposits, construction of technical installations of underground gas storage facilities, crude oil transport, repair of coal mining equipment, design of installations for gas transport as well as hotel and catering services and SPA centre services.

In H1 2008, the companies constructed 40.7 km of pipelines, including 39.6 km of gas transmission pipelines, both for external customers and for the Group's own needs. For the customers from within the PGNiG Group, the segment produced drilling equipment, including pressure equipment used in surface development of boreholes, and provided construction and assembly services, including modernisation of the Borzęcin Natural Gas Mine (KGZ Borzęcin) and its adjustment to store waste. Additionally, work on development of natural gas deposits was performed and technical installations connected with oil transport were made. For external customers, the companies produced equipment and spare parts for oil platforms and drill ships and provided such services as development of natural gas deposits, repairs of coal mining equipment, connecting to gas network and construction of water and sewage installations.

Planned Activity

A significant growth of demand for products offered by the fuel and power industry can be seen both in Poland and in foreign markets. The segment companies plan to capitalise on such favourable market and strengthen their positions in the industry of drilling equipment, gas system designing and construction and assembly services at oil and gas facilities. They seek to enter other segments of the Polish market and foreign markets, among other things, by offering such services as construction of water supply and sewage systems, together with the auxiliary infrastructure, and steel structures.

Risks

The segment companies are exposed to a range of unfavourable factors. The business and financial standing of the companies is to a significant extent affected by legal regulations and administrative procedures to be followed in the preparation of investments and obtaining building permits, including in particular with respect to environmental protections requirements. Other adverse factors are the provisions of the Public Procurement Act, as they protract the investment process.

The construction and assembly services market, in which "turn-key" projects (design, delivery, execution) are gaining significance, is exposed to financial risk. To execute such project, the companies form consortiums with contractors and extend their range of services with the services of general project manager. Such increased range of services leads to increased operating expenses, driven mainly by the cost of financing the projects with external funds and by the cost of staff training. The incurred expenses not always translate into higher income and the earned profit may not be satisfactory in relation to the capital expenditure.

Other significant factors which affect the companies' operations are the movements in prices of metallurgical products, unfavourable exchange rate of the euro (shrinking profitability of exports), difficulties in attracting new engineering and technical personnel to execute the projects and unforeseen geological conditions.

Chapter VIII: Environmental Protection

Carbon Credit Trade System

Under the existing carbon credit trading system (CCTS), in H1 2008 PGNiG S.A. reviewed the annual reports on carbon dioxide emissions for 2007 and brought the volumes of carbon dioxide emission in line with the amounts stipulated by the permit held. Following the cancellation of the carbon credits used in 2007, 8,405 Mg CO₂ credit units were retained.

Preliminary analysis of the volumes of carbon dioxide emission in H1 2008 did not exceed half of the volumes allowed for each of the facilities. In that settlements period, the system included the facilities of the Odolanów Branch, Zielona Góra Branch and the Gas Storage Facility in Mogilno.

Furthermore, in H1 2008, in the National Plan for the Distribution of Carbon Credits for 2008–2012 (KPRU II) the facilities of PGNiG S.A. were allowed the total of 99,982 Mg CO₂ per annum.

Environmental Management System

On January 2nd 2008, PGNiG S.A. started to implement the environmental management system meeting the requirements of PN-EN ISO 14001:2005 at its Warsaw head office. In H1 2008, within the framework of the undertaken actions, the Company carried out an initial inspection, developed a schedule concerning the implementation of the environmental management system, conducted trainings of employees and developed system procedures.

REACH (Registration, Evaluation, Authorisation of Chemicals)

In order to ensure compliance with the new regulations concerning mandatory registration of chemical substances, evaluation of substances and authorisations for use of substances in production and trading, which came into effect in H1 2008, PGNiG S.A. undertook actions to fulfil its obligations such as updating of chemical data sheets. The first stage – the initial registration commenced on June 1st and shall continue until the end of November 2008.

Natura 2000

As part of extensive social consultations concerning the already indicated and planned to be marked out areas of Natura 2000, PGNiG S.A. identifies the areas of current and planned projects pertaining to the construction of UGS, the Baltic Pipe project, the LNG terminal, construction of gas network, crude oil and natural gas mines, crude oil shipment and exploration projects. The key projects of PGNiG S.A., located within or in the vicinity of the already indicated and planned to be marked out areas of Natura 2000, will be included in the National Spatial Strategy 2008-2033.

Methane Emissions

In each of its Branches, PGNiG S.A. conducted inspections which enabled to identify the sources of methane emission. PGNiG S.A. commissioned preparation of an analysis, which will set out uniform methods and rates of methane emission for specific processes. This study will be concluded in H2 2008, and its results will be presented to the Ministry of the Environment and the National Emission Centre.

Chapter IX: Other Events

Distribution of 2007 Profit

On June 26th 2008, the Annual General Shareholders Meeting of PGNiG S.A. adopted a resolution on the 2007 net profit distribution in the amount of PLN 2,154.9m. Distributions from profit were allocated in the following manner:

- PLN 991.6m was allocated to the Company's statutory reserve funds
- PLN 1,121m was allocated to dividend payments (PLN 0.19 per share), including:
 - PLN 950m as non-cash dividend to the State Treasury – 29 transmission subsystems, along with their constituent and accessory parts, and PLN 5,885.30 in cash.
 - PLN 171m as cash dividend to the other shareholders
- PLN 8.4m was allocated to increase the Company's social benefits fund
- PLN 33.9m was allocated to awards for the Company employees.

The Annual General Shareholders Meeting of PGNiG S.A. set July 25th 2008 as the dividend record date and October 1st 2008 as the dividend payment date.

Approval for the Performance of Duties

On June 26th 2008, the Annual General Shareholders Meeting of PGNiG S.A. adopted resolutions on the approval of the non-consolidated financial statements and the Director's Report, on approval of the consolidated financial statements and the Director's Report on the activities of the PGNiG Group, and on granting approval to members of the Management and Supervisory Boards of PGNiG S.A. for the performance of their duties in the financial year 2007.

Employee Shares

On June 25th, the Ministry of State Treasury disposed of one share in PGNiG S.A. The transaction was concluded on market terms. Pursuant to the Commercialisation and Privatisation Act of August 30th 1996, eligible employees will gain the right to acquire the Company shares free of charge as of October 1st 2008; the right will expire on October 1st 2009. The eligible employees have the right to acquire free of charge, on the Company registration date, up to 15% of the shares acquired by the State Treasury, i.e. up to 750,000,000 shares with a par value of PLN 1 per share. The Company shares acquired free of charge by the eligible employees cannot be traded before July 1st 2010, and the shares acquired free of charge by members of the Company's Management Board cannot be traded before July 1st 2011.

Actions Against PI GAZOTECH Sp. z o.o.

1. On March 7th 2006, the Regional Court of Warsaw dismissed PGNiG S.A.'s action instituted against PI GAZOTECH Sp. z o.o. to rescind or assert invalidity of the resolutions of the General Shareholders Meeting of PI GAZOTECH Sp. z o.o., dated April 23rd 2004, including the resolution whereunder PGNiG S.A. is obliged to pay additional contributions in the amount of PLN 52m. In view of the dismissal, PGNiG S.A. filed an appeal against the court ruling, which was rejected by the Court of Appeals in Warsaw on January 10th 2007 on account of the Company's failure to duly paid the required fees. On March 1st 2007, PGNiG S.A. filed a complaint with the Supreme Court regarding the Court of Appeals's ruling. On July 20th 2007, the Supreme Court examined the complaint in closed session and overruled the Court of Appeals's decision to reject PGNiG's appeal. On February 4th 2008, the Court of Appeals dismissed PGNiG's appeal. The decision is final and binding. From the date of passing the verdict by the Court of Appeals the Company's claim is no longer secured by suspension of the resolution

authorising the additional contributions. On July 8th 2008, a cassation complaint against the decision of the Court of Appeals of February 4th 2008 was filed.

2. On December 7th 2006, the Regional Court of Warsaw dismissed PGNiG's action instituted against PI GAZOTECH Sp. z o.o. to confirm the non-existence of the resolution on redemption of shares, adopted by the General Shareholders Meeting of PI GAZOTECH Sp. z o.o. on April 23rd 2004. PGNiG S.A. filed an appeal against the ruling. The Court of Appeals in Warsaw dismissed the appeal at the hearing of February 5th 2008. The decision is final and binding. On May 27th 2008, a cassation complaint against the decision of the Court of Appeals of February 5th 2008 was filed.
3. The proceedings based on PGNiG S.A.'s action against PI GAZOTECH Sp. z o.o. to rescind or assert invalidity of the resolution of the General Shareholders Meeting of PI GAZOTECH Sp. z o.o., dated January 19th 2005, whereunder PGNiG S.A. is obliged to pay additional contributions in the amount of PLN 25,999,998, held before the Regional Court of Warsaw were taken up for further hearing. The case is pending. The Company's claim is secured by suspension of the resolution authorising the additional contributions.
4. The proceedings based upon PGNiG S.A.'s action against PI GAZOTECH Sp. z o.o. to rescind or assert invalidity of the resolution of the General Shareholders Meeting of PI GAZOTECH Sp. z o.o., dated October 6th 2005, whereunder PGNiG S.A. is obliged to pay additional contributions in the amount of PLN 6,552,000, instigated before the Regional Court of Warsaw were concluded in the first instance. On May 30th 2008, the Regional Court dismissed the Company's claim and reversed the decision on securing this claim. Neither of the decisions is final and binding. PGNiG S.A. filed for presenting grounds for both decisions in order to lodge an appeal against the verdict and a complaint against the reversing of the decision on securing the Company's claim. The claim is still secured by suspension of the resolution authorising the additional contributions. On July 22nd 2008, PGNiG S.A. lodged a complaint against the reversing of the decision on securing its claim, and on July 29th 2008, it filed appeal against the Regional Court's judgement.

Dispute with Bartimpex S.A.

On August 9th 2005, in connection with a motion filed by PHZ Bartimpex S.A., the President of the Anti-Trust and Consumer Protection Authority ruled that the Company pursues anti-competitive practices through abusing its dominant position on the domestic natural gas transmission market, this being manifested in the refusal to provide the services of transmitting natural gas extracted outside Poland. The President of the Anti-Trust and Consumer Protection Authority also stated the abovementioned practices ceased as of June 2nd 2003. By virtue of his decision of August 9th 2005, the President of the Anti-Trust and Consumer Protection Authority imposed a fine on PGNiG S.A. in the amount of PLN 2,000,000 along with an order to repay the costs of proceedings for the benefit of PHZ Bartimpex S.A.

By way of submitting a letter of August 31st 2005, PGNiG appealed against the decision. As a consequence, on January 31st 2007 the Regional Court of Warsaw issued a verdict reducing the fine imposed on PGNiG S.A. to the amount of PLN 500,000.

As a result of appeals filed by both parties to the proceedings, the Court of Appeals changed the Regional Court's decision. Accordingly, a fine of PLN 2,000,000 was imposed and PGNiG's appeal was dismissed. On September 1st 2008, PGNiG S.A. filed a cassation complaint against the decision of the Court of Appeals of March 27th 2008 was filed.

Dispute with EUROPOL GAZ S.A.

The proceedings based upon PGNiG S.A.'s actions against EUROPOL GAZ S.A. to receive payment of interest due under agreement no. DF/33/95, dated September 25th 1995, on a loan and guarantee to finance the construction of a system of transmission pipelines, have been pending since February 27th 2004. On March 31st 2006, the Regional Court of Warsaw passed a decision whereby PGNiG S.A. was to receive PLN 32,699,276.36 with statutory interest accrued from February 27th 2004 to the payment date, and PLN 107,200 as costs of proceedings. EUROPOL GAZ S.A. appealed against the decision. On December 7th 2006, the Court of Appeals in Warsaw overruled the decision and submitted the case for re-examination by the Regional Court of Warsaw, which was also to decide on costs of the appellate instance. By way of submitting a letter of April 23rd 2007, PGNiG S.A. modified its claim to the effect that it demanded PLN 36,618,037.33 and withdrew its claim concerning payment of PLN 2,382,581.66, due to the statute of limitation. On July 2nd 2007, the Regional Court of Warsaw rejected the claim for payment of PLN 36,618,037.33, discontinued the proceedings concerning payment of PLN 2,382,581.66, and decided that PGNiG S.A. is to cover costs of proceedings of PLN 119,815 to EUROPOL GAZ S.A. On July 30th 2007, PGNiG S.A. appealed against this decision. On November 15 2007, the Court of Appeals in Warsaw dismissed the appeal. The decision is final and binding. On March 20th 2008, a cassation complaint was filed against the Court of Appeals's decision.

Dispute with EMFESZ NG Sp. z o.o.

On March 9th 2006, proceedings before the President of URE were instigated upon a motion filed by EMFESZ NG Polska Sp. z o.o. regarding refusal to execute an agreement on provision of gaseous fuel storage services. On June 11th 2007, a team of URE experts completed their work aimed at preparing an expert opinion on the technological feasibility of provision of gas storage services by PGNiG S.A. to third parties. On August 24th 2007, the President of URE announced that the relevant decision would be made by October 24th 2007.

Afterwards, by virtue of subsequent documents, the President of URE was continuously postponing this date up to February 24th 2008. On February 25th, he passed a resolution suspending the proceedings until the decision of the European Commission on the introductory issue regarding examination of the President of URE's stand on PGNiG's request for temporary exemption from the obligation to store gaseous fuels.

Chapter X: Financial Performance

The consolidated financial statements of the PGNiG Group have been prepared in accordance with the International Financial Reporting Standards ("IFRS") and the Minister of Finance's regulation on current and periodic information to be published by issuers of securities, dated October 19th 2005 (Dz. U. No. 209, item 1744).

The accounting policies applied in preparing the non-consolidated financial statements are presented in the consolidated financial statements of the PGNiG Group for the period ended June 30th 2008.

1. Financial Standing

The H1 2008 net profit of the PGNiG Group stood at PLN 1,059.3m, down by PLN 55.2m (or 5%) compared with the figure posted in H1 2007.

Summary information on the PGNiG Group's financial standing in H1 2008 is presented in the following financial statements prepared in accordance with the International Financial Reporting Standards:

- the balance sheet,
- the income statement,
- the cash flow statement,
- the selected financial ratios.

Consolidated Balance Sheet (PLNm)

ASSETS	June 30th 2008	December 31st 2007
Non-current assets	22,445.5	22,131.1
Property, plant and equipment	19,677.4	18,715.5
Investment property	9.8	10.6
Intangible assets	134.1	84.6
Investments in associated undertakings valued with equity method	556.7	557.5
Financial assets available for sale	73.9	20.0
Other financial assets	1,528.4	2,292.2
Deferred tax asset	434.3	419.8
Other non-current assets	30.9	30.9
Current assets	6,642.4	6,270.8
Inventories	1,364.7	1,216.0
Trade and other receivables	2,479.2	3,331.0
Current income tax receivable	12.0	17.5
Prepayments and accrued income	226.6	82.4
Financial assets held for sale	17.6	22.4
Derivative financial instrument assets	85.9	17.4
Cash and cash equivalents	2,456.0	1,583.6
Assets available for sale	0.4	0.5
Total assets	29,087.9	28,401.9

Consolidated Balance Sheet (PLNm)

EQUITY AND LIABILITIES	June 30th 2008	December 31st 2007
Equity	20,926.9	21,021.8
Share capital	5,900.0	5,900.0
Currency-translation differences on foreign-currency undertakings	(64.2)	(44.5)
Share premium account	1,740.1	1,740.1
Other reserve funds	10,341.9	3,478.1
Retained earnings/(deficit)	3,000.8	9,939.4
Equity (attributable to equity holders of the parent)	20,918.6	21,013.1
Equity attributable to minority interests	8.3	8.7
Non-current liabilities	3,848.9	3,879.5
Loans, borrowings and debt securities	36.6	31.4
Provisions	1,231.2	1,153.8
Deferred income	1,125.5	1,142.4
Deferred tax liability	1,431.4	1,530.3
Other non-current liabilities	24.2	21.6
Current liabilities	4,312.1	3,500.6
Trade and other payables	3,094.4	2,408.0
Loans, borrowings and debt securities	116.8	106.7
Liabilities under derivative financial instruments	41.3	36.2
Current tax liability	281.8	281.4
Provisions	233.2	181.2
Deferred income	544.6	487.1
Total liabilities	8,161.0	7,380.1
Total equity and liabilities	29,087.9	28,401.9

Consolidated Income Statement (PLNm)

	H1 2008	H1 2007
Sales revenue	9,259.6	8,440.5
Total operating expenses	(8,049.3)	(7,054.6)
Raw materials and energy used	(4,893.8)	(4,291.2)
Employee benefits	(1,036.4)	(973.8)
Depreciation and amortisation	(721.4)	(702.3)
Contracted services	(1,338.9)	(1,274.6)
Cost of products and services for own needs	307.9	278.9
Other net operating expenses	(366.7)	(91.6)
Operating profit	1,210.3	1,385.9
Financial income	199.2	133.2
Financial expenses	(39.7)	(80.8)
Share in profit/(loss) of undertakings valued with equity method	0.1	(33.0)
Pre-tax profit	1,369.9	1,405.3
Corporate income tax	(310.6)	(290.8)
Net profit	1,059.3	1,114.5
attributable to:		
equity holders of the parent	1,059.6	1,114.1
minority interests	-0.3	0.4
	1,059.3	1,114.5

Consolidated Cash Flow Statement (PLNm)

	H1 2008	H1 2007
Net cash provided by/used in operating activities	1,940.1	1,981.0
Net cash provided by/used in investing activities	(1,099.6)	(666.5)
Net cash provided by/used in financing activities	31.6	(2,384.0)
Change in net cash	872.1	(1,069.5)
Cash and cash equivalents at beginning of period	1,584.9	3,559.2
Cash and cash equivalents at end of period	2,457.0	2,489.7

Financial Ratios

Profitability Ratios

	H1 2008	H1 2007
EBIT (PLNm) operating profit	1,210.3	1,385.9
EBITDA (PLNm) operating profit + depreciation/amortisation	1,931.7	2,088.2
ROE (Return on Equity) net profit * to equity at end of period	5.1%	-
Net margin net profit * to sales revenue	11.4%	13.2%
ROA (Return on Assets) net profit * to assets at end of period	3.6%	-

*net profit for the financial year attributable to equity holders of the parent

Liquidity Ratios

	H1 2008	2007
CURRENT RATIO current assets (net of prepayments and accrued income) to current liabilities	1.5	1.8
QUICK RATIO current assets (net of prepayments and accrued income) decreased by inventories to current liabilities	1.2	1.4

Debt Ratios

	H1 2008	2007
DEBT RATIO total liabilities to total equity and liabilities	28.1%	26.0%
DEBT/EQUITY RATIO total liabilities to equity *	39.0%	35.1%

* equity attributable to equity holders of the parent

In H1 2008, the PGNiG Group's operating profit deteriorated by PLN 175.6m (13%) year on year. The decrease in operating profit (EBIT) is an effect of lower profitability of trading in methane-rich gas, resulting from:

- a change in the structure of purchases of methane-rich gas, and
- an increase in unit purchase costs of imported gas.

In the period under review, the Company purchased more imported gas to meet the domestic demand for gaseous fuels caused by lower air temperatures in the heating season. In addition, the use of gas from underground storage facilities was less intensive year-on-year on account of optimal management of import contracts. Gas production decreased as a result of the Company's facing natural production barriers; while an increase in sales volume of nitrogen-rich gas reduced the deliveries of feedstock to denitrating plants.

An upward trend prevailed in unit purchase prices of imported gas throughout the first six months of 2008, driven primarily by the situation on the global oil and oil derivatives market. The continuing depreciation of the dollar/zloty exchange rate partly mitigated the rise in prices of imported gas.

Despite the approval by the President of URE of a new tariff for gaseous fuels at the end of April 2008, the price level still did not guarantee a satisfactory recovery of unit purchase costs of imported gas for the Group. The gains on gas trading generated by the PGNiG Group are attributable only to sales of methane-rich gas from own production.

The EBIT figure was weaker also due to a PLN 275.1m (300%) surge in other operating expenses, which occurred as a consequence of:

- a rise in foreign exchange losses on non-financial items,
- a decline in income under a lease of transmission assets, which was due to a reduction in the operating lease assets (following from the payment of non-cash dividend to the State Treasury and provision of a contribution-in-kind to the Distribution System Operators)
- a decline in the value of released provisions for liquidation of boreholes, mining pits and drilling pits
- a decline in the value of reversed impairment losses on property, plant and equipment and a lower value of reversed impairment losses on trade receivables.

Business Segments of the PGNiG Group
(PLNm)

H1 2008	Exploration and production	Trading and storage	Distribution	Other operations	Elimination	Total
Sales to external customers	1,103.1	8,073.5	11.9	71.1	-	9,259.6
Sales to other segments	724.5	522.4	1,745.4	75.5	(3,067.8)	-
Segment revenue	1,827.6	8,595.9	1,757.3	146.6	(3,067.8)	9,259.6
Segment costs	(1,284.5)	(8,158.3)	(1,503.6)	(148.9)	3,046.0	(8,049.3)
Operating profit/(loss)	543.1	437.6	253.7	(2.3)	(21.8)	1,210.3
Net financial expenses	-	-	-	-	-	159.5
Share in net profit/(loss) of undertakings valued with equity method	-	0.1	-	-	-	0.1
Pre-tax profit						1,369.9
Income tax	-	-	-	-	-	(310.6)
Net profit						1,059.3

Business Segments of the PGNiG Group
(PLNm)

H1 2007	Exploration and production	Trading and storage	Distribution	Other operations	Elimination	Total
Sales to external customers	1,027.0	2,317.2	5,037.8	58.5	-	8,440.5
Sales to other segments	587.7	3,772.9	4.9	113.5	(4,479.0)	-
Segment revenue	1,614.7	6,090.1	5,042.7	172.0	(4,479.0)	8,440.5
segment costs	(1,068.8)	(5,377.1)	(4,921.4)	(166.4)	4,479.1	(7,054.6)
Operating profit/(loss)	545.9	713.0	121.3	5.6	0.1	1,385.9
Net financial expenses	-	-	-	-	-	52.4
Share in net profit/(loss) of undertakings valued with equity method	-	-	-	-	-	(33.0)
Pre-tax profit						1,405.3
Income tax	-	-	-	-	-	(290.8)
Net profit						1,114.5

Exploration and Production

In H1 2008, the Group's operating profit in the Exploration and Production segment was PLN 543.1m, which means that it remained relatively flat year-on-year. In the segment, the Group recorded a significant increase in profitability of sales of crude oil and natural gas, notably of nitrogen-rich gas. Higher margins on sales of oil were driven primarily by rising prices of crude oil on global markets. The increase in the average selling prices of oil was partially offset by strengthening of the Polish zloty against the US dollar. The improved result on sales of nitrogen-rich gas was driven by higher average selling prices and a 14% increase in sales volume of nitrogen-rich gas. The margin on sales of crude oil and nitrogen-rich gas improved despite higher production costs which may be attributed to more substantial exploration spending and higher expenses – charged to costs – incurred on drilling wells classified as dry.

Trading and Storage

In H1 2008, the Group's operating profit in the Trading and Storage segment reached PLN 437.6m, down by PLN 275.4m (39%) year-on-year. The decline was brought by lower margins on sales of methane-rich gas which dropped due to an increase in the volume of imported gas, a decrease in production volumes and higher prices of gas from imports. The operating result posted by the Trading and Storage segment was weaker despite higher selling prices of gaseous fuels. In addition to the abovementioned factors, the operating profit was affected by changes in the organisational structure of the segments. The increase in sales and costs of the segment is attributable to the fact that the trading segment commenced to directly purchase the services provided by the Distribution System Operators, the costs of which are subsequently passed onto external customers.

Distribution

The Group's operating profit in the Distribution segment was PLN 253.7m, up by PLN 132.4m (109%) compared with the corresponding period of 2007. The improved profitability of the distribution segment was driven to a large extent by higher rates and charges on transmission of gaseous fuel, which rose following the approval of new tariffs applicable to the Distribution System Operators at the end of April 2008 and on the back of larger volumes of transmitted gas. Also, the

changed scope of activities of the Distribution System Operators resulted in reduced costs and revenues of the segment.

Gross profit achieved in 2007 fell slightly, i.e. by PLN 35.4m (3%), compared with the previous year, and was positively affected by the profit on financing activities, which rose by PLN 140.2m owing to:

- higher income on forward and swap transactions,
- higher income on disposal of financial investments resulting, taking into account that more funds were allocated to short-term financial investments and interest rates were higher,
- more substantial share in net profit/(loss) of undertakings valued with equity method.

The balance sheet of the PGNiG Group as at June 30th 2008 shows a balance-sheet total of PLN 29,087.9m, up by PLN 686.0m (2%) relative to the figure as at December 31st 2007.

The largest item in assets is represented by property, plant and equipment whose value disclosed as at June 30th 2008 was PLN 19,677.4m, up by PLN 961.9m (5%) from the end of 2007. The increase is attributable primarily to investment activities undertaken by the PGNiG Group.

A considerable decline in other financial assets – by PLN 763.8m, or 33%, relative to December 31st 2007 – was caused mainly by lower non-current receivables under operating lease, and lease payments being made on a consistent basis by OGP GAZ-SYSTEM S.A.

As at June 30th 2008, current assets totalled PLN 6,642.4m, up by 371.6m (6%) compared with the end of 2007. The key factors contributing to the change in current assets included an increase in cash and a decrease in trade receivables.

Trade and other receivables fell by PLN 851.8m (26%) compared with the end of 2007, mainly due to seasonal fluctuations in sales volumes.

As at the end of June 2008, cash and cash equivalents totalled PLN 2,456.0m, up by PLN 872.4m (55%) compared with the end of December 2007. The increase was caused by seasonal fluctuations in trade receivables and trade payables.

During the period under review, the value of inventories advanced by PLN 148.7m (12%). The inventories disclosed in the balance sheet comprise mainly the gas stored in underground storage facilities. The increase in the volumes of natural gas stored was caused by a seasonal rise in reserves to be used during the coming heating season. Also, the level of inventories was affected by an increase in the purchase prices of imported gas.

Despite a substantial rise in cash, the liquidity ratios of the Company edged down. The current ratio dropped from 1.8 to 1.5, while the quick ratio fell from 1.4 to 1.2. This resulted from a considerable decrease in trade receivables and a rise in current liabilities. Despite the decline in liquidity ratios, the value and structure of current assets held by the PGNiG Group still enables it to settle all its current operating liabilities.

The main financing source of the Group's assets was equity, whose value dropped by PLN 94.9m (1%) relative to December 31st 2007. The change was largely caused by net profit generated during the year to date (PLN 1,059.3m) and distribution of the previous year's profit in the form of non-cash and cash dividend (PLN 1,121.0m).

Compared with December 31st 2007, the total value of current liabilities rose by PLN 811.5m (23%), which was mainly caused by the fact that unpaid dividend for the previous financial year was disclosed under trade and other payables in June 2008. In addition, the current liabilities were driven up by a PLN 52m rise in provisions, in particular other provisions for retirement and similar benefits, and a PLN 57.5m increase in deferred income on estimated future gas sales.

Movements in the structure of the Group's equity and liabilities brought about changes in the ratios reflecting the relation between capital and other items of shareholders' equity and liabilities. The total debt-to-equity ratio advanced from 35.1% to 39%, while the debt ratio (total liabilities to total equity and liabilities) increased from 26% to 28.1%.

Although net profit posted in H1 2008 was PLN 55.2m (5%) lower year-on-year, the financial standing of the PGNiG Group is strong. However, the development of the growth path in the years ahead will be primarily conditional on the position of the Polish Energy Regulatory Authority on gas selling prices in the domestic market.

2. Forecast Financial Performance

The financial performance of the PGNiG Group will be under a strong influence of the prices of crude oil and its derivatives quoted on international markets. An upward trend in crude oil prices continued on global markets in the first six months of this year. At the end of June, the oil price broke the USD 140 per-barrel mark. The situation seen on the fuel market in H1 2008 will significantly drive the prices of imported gas in the next few months.

Under Polish law, the Group does not pursue a fully independent pricing policy. As long as PGNiG S.A. is obliged to apply the tariffs approved by the President of URE, there will always be a risk that any increases in purchase prices of gas will not be fully reflected in gas prices determined in accordance with the tariffs. Consequently, the approval by the President of URE of such new tariffs as would allow the Group to fully recover the increased cost of purchase of imported gas will be of crucial importance for the Group's financial performance.

Profitability of crude oil production is closely linked to prices of oil derivative products. Any increase in commodity prices on global exchanges automatically improves the profitability of crude oil production, partly offsetting the losses incurred by the Company in connection with having to pay more for imported gas.

In addition, the situation on the currency markets has profound implications for the Group's financial performance. In H1 2008, depreciation of the dollar against the złoty significantly mitigated the effect of increases in prices of imported gas. In the periods ahead, the dollar exchange rate will still affect the PGNiG Group's financial standing and performance.

The Group's good financial standing supports the performance of planned investment projects. The balance of available funds provides PGNiG S.A. with flexibility with regard to performance of the investment projects. Owing to the low financial leverage and positive assessment of the PGNiG S.A.'s risk, as confirmed by the rating agencies (BBB+ with stable prospects), along with the creditworthiness, the opportunity arise for the Company to finance the planned investment projects with the bank loans advanced on favourable conditions or the issue of debt securities.

Members of the Management Board

President

Michał Szubski

Vice-President Mirosław Dobrut

Vice-President Radosław Dudziński

Vice-President Sławomir Hinc

Vice-President Mirosław Szkałuba