

4.2 Equity and capital management policy

Accounting policy applied

The share capital is presented in the consolidated financial statements at the value specified in the Parent Company's Articles of Association, regardless of the entry in the National Court Register (the 'substance over form' rule).

Share capital

| | 31/12/2018 | 31/12/2017 |
|--|------------|------------|
| The share capital consists of: | | |
| Ordinary shares - fully paid up and registered | 2,239.3 | 2,239.3 |

As at 31 December 2018 and 31 December 2017, the share capital consisted of common shares with a par value of PLN 50 each. Fully paid up ordinary shares with a par value of PLN 50 are equivalent to one vote at the shareholder meeting and carry the right to a dividend.

PKP S.A. is the parent company of PKP CARGO S.A. Pursuant to the articles of association of the Parent Company, PKP S.A. holds special personal rights to appoint and dismiss Supervisory Board Members in a number equal to half the composition of the Supervisory Board plus one. PKP S.A. has a personal right to appoint the Supervisory Board Chairman and to determine the number of Supervisory Board Members. Additionally, in the event that PKP S.A.'s share in the Company's share capital is 50% or less, PKP S.A. will have an exclusive personal right to propose candidates for the President of the Parent Company's Management Board. The personal rights of PKP S.A. shall be vested always when PKP S.A. holds at least 25% of the Parent Company's share capital.

In the financial years ended 31 December 2018 and 31 December 2017, there were no movements in the share capital of the Parent Company.

Supplementary capital

| | 31/12/2018 | 31/12/2017 |
|--|--------------|--------------|
| Share premium (agio) | 201.3 | 201.3 |
| Distribution of profit (established pursuant to statutory regulations) | 56.2 | 48.7 |
| Distribution of profit (established in excess statutory value) | 230.7 | 229.3 |
| Capital formed from retirement of shares | 140.0 | 140.0 |
| Total | 628.2 | 619.3 |

Pursuant to the requirements of the Commercial Company Code, entities with the status of joint-stock companies are obligated to establish supplementary capital to cover losses. Transfers to supplementary capital should be at least 8% of the earnings for a given financial year as stated in the Company's standalone financial statements, until the amount of capital reaches at least one third of the entity's share capital. The use of supplementary capital is decided upon by the Shareholder Meeting, however the portion of the supplementary capital representing one third of the share capital may only be used to cover a loss shown in the standalone financial statements and must not be set aside for other purposes. The amount to be divided among the shareholders may be increased by undistributed earnings from previous years and amounts transferred from the supplementary capital established from earnings.

Agio is the share premium of the Parent Company transferred to supplementary capital without possibility of paying the dividend.

The capital established from retirement of shares was created as a result of reduction of the Parent Company's share capital in 2013 earmarked for coverage of losses.

In the financial year ended 31 December 2018, changes in the Group's supplementary capital resulted from a resolution of 13 June 2018 adopted by the Ordinary Shareholder Meeting of PKP CARGO S.A. in the matter of a partial allocation to supplementary capital of the net profit generated in 2017 of PLN 7.5 million, and a resolution of 29 June 2018 adopted by the Ordinary Shareholder Meeting of PKP CARGO SERVICE Sp. z o.o. in the matter of a partial allocation to supplementary capital of the net profit generated in 2017 of PLN 0.8 million and resolution of 29 May 2018 adopted by the Ordinary Shareholder Meeting of CARGOSPED Terminal Braniewo Sp. z o.o. in the matter of a partial allocation of the 2017 net profit of PLN 0.6 million to supplementary capital.

Retained earnings

The Group's retained earnings include:

- a) profit or loss of the current year;
- b) undistributed earnings and uncovered losses from previous years;
- c) differences attributable to transition to EU IFRS.

On 13 June 2018, the Ordinary Shareholder Meeting of PKP CARGO S.A. adopted a resolution on the distribution of the net profit earned in 2017 of PLN 94.0 million as follows:

- a) allocate PLN 7.5 million to increase the supplementary capital;
- b) allocate PLN 86.5 million to cover losses carried forward.

As at 1 January 2018, the line item "retained earnings" has been restated in connection with the implementation of IFRS 9 and correction of previous period errors, as described in [Notes 1.3](#), [1.4](#) and [1.5](#) to these Consolidated Financial Statements.

As at the moment of approval of these Consolidated Financial Statements, the Parent Company's Management Board has not adopted any resolution on the distribution of net profit generated in 2018.

Equity management

In accordance with the adopted policy and assumptions following from the bank loans concluded by the Group companies, the Group accepts the maximum level of debt up to 60% of total assets (hence equity may not be lower than 40% of total assets). The debt level is monitored by the Group as at the end of each quarter. The main objective of equity management in the Group is to ensure the ability to continue operations, create value for shareholders and benefits for other stakeholders. The assumed capital structure can be ensured through: issue of new shares, sale of assets, return of capital to the shareholders or adjustment of the dividend amount.

The total debt ratio as at the end of the year was as follows:

| | 31/12/2018 | 31/12/2017 |
|---------------------|------------|------------|
| Total liabilities | 3,322.8 | 3,328.5 |
| Total balance sheet | 6,806.3 | 6,645.7 |
| Total debt ratio | 49% | 50% |