

SOKOLOVSKÁ UHELNÁ

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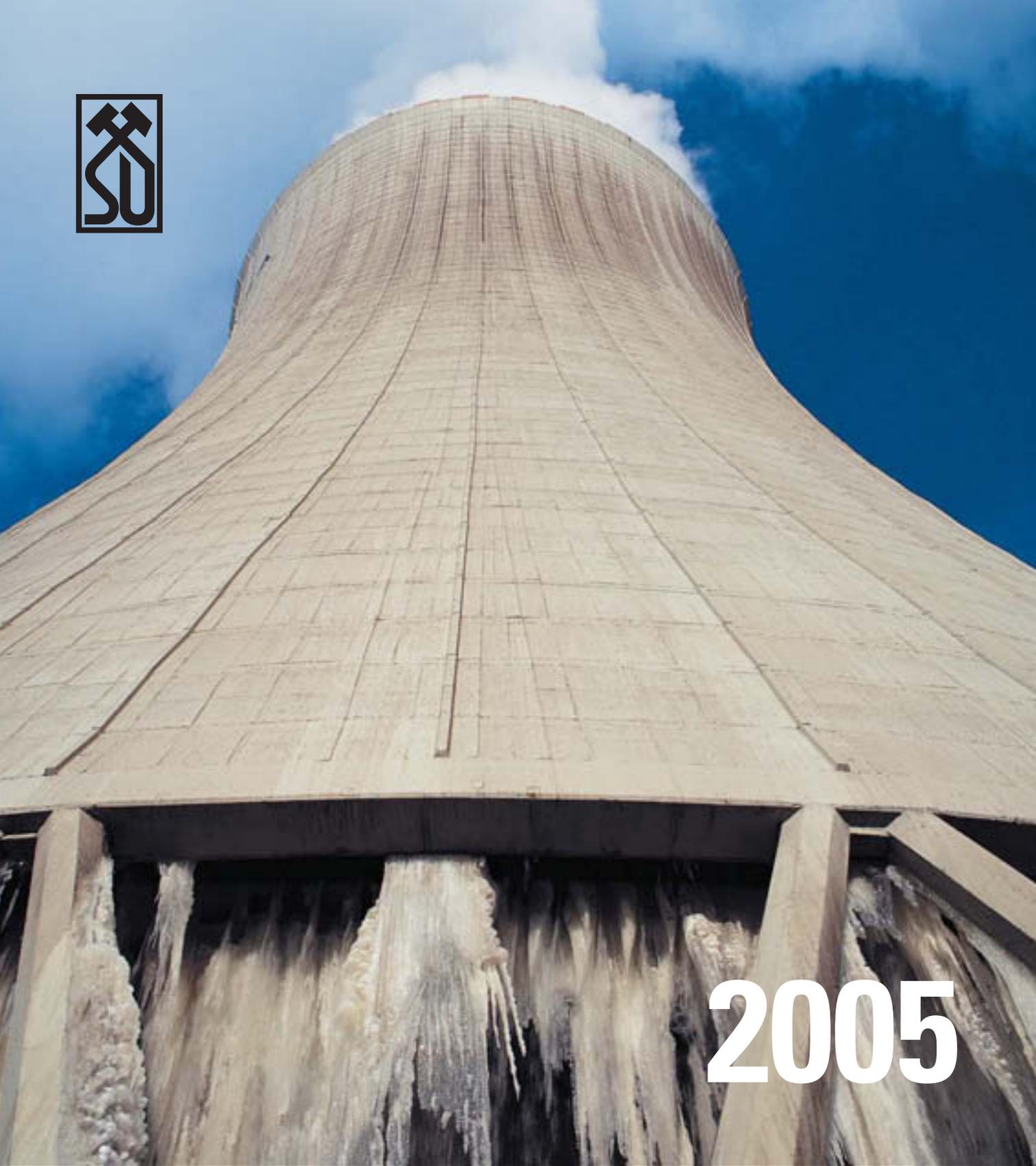
Performance Report 2005



**Sokolovská uhelná
invests millions
in environmental
programs**

**New hi-tech
oxygen plant
in operation**

**Unique golf course
in place of former
surface mine**



2005

"...the long-term focus of the Company's business is on mining coal and converting it into value-added forms of energy – electricity and heat in particular..."

energy for you

Contents



Performance Report
 SOKOLOVSKÁ
 UHELNÁ
 2005
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Reasons for optimism?

...supply of solid fuels continued to outstrip demand in 2005 and the opening of the electricity market to competition took another step **5**

KEY FIGURES

Facts, data, figures 2
Important Moments
 of 2005–2006 3

Letter from the Chairman . . . 4

PEOPLE

People in the Management
 of Sokolovská uhelná 6

COMPANY PROFILE

Company Reorganization
 timeline 2002–2005 10

The Company Today 12

REPORT OF THE BOARD OF DIRECTORS

Business Environment 22

Production and Sales 30

Earnings Analysis 36

Structure of Assets and

Sources of Financing 40

Capital Investment

in 2005 44

Potential is in people 45

Environmental Responsibility . . 50

Sokolovská uhelná –
 a stabilizing element in
 the Sokolov region 54

THE FUTURE

Company Vision 56

APPENDICES

Financial Statement 58

Organization Chart of

Sokolovská uhelná as

of 1 January 2006 60



This Performance Report gives the reader a comprehensive look at Sokolovská uhelná, právní nástupce, a.s. (the “Company” or “Sokolovská uhelná”), including an overview of its performance and business activities over the past several years. For this reason, this Performance Report includes information on past accounting periods which also contain information on the company Sokolovská uhelná, a.s., all of whose capital was taken over in 2005 by Sokolovská těžební, a.s., which was subsequently renamed to Sokolovská uhelná, právní nástupce, a.s.

Facts, Data, Figures

	Units	2005	2004	2003
Production				
Coal extracted	kt	10,307.1	10,081.1	10,082.9
Overburden extracted	kt	32,684.0	32,191.0	26,478.2
Electricity – heat/power plant	GWh	1,698.2	1,633.2	1,610.4
Electricity – combined cycle power plant	GWh	1,899.7	1,791.0	1,819.5
Coal gas	m ³ millions	1,187.9	1,141.3	1,171.5

Sales

Coal	kt	6,153.2	6,068.6	6,045.4
– of which, e.g.: sorted	kt	240.1	258.4	330.3
Briquettes	kt	286.8	285.7	300.8
Electricity – heat/power plant	GWh	1,007.8	839.5	806.1
Electricity – combined cycle power plant	GWh	1,891.9	1,797.6	1,940.4
Heat	TJ	2,251.5	2,298.8	2,329.0
Coal gas	m ³ millions	0.0	3.2	8.4

Financial indicators

Revenues	CZK millions	7,437.0	7,172.2	6,569.8
Net income	CZK millions	533.3	551.4	481.9
Capital expenditure	CZK millions	555.8	808.0	1,376.4
Average number of employees	persons	4,888	5,194	5,373
Average monthly wage	CZK	21,125	20,000	18,008



Important Moments of 2005 – 2006

2005

January

commencement of steps toward take-over of capital of Sokolovská uhelná, a.s., pursuant to Section 69b, 220p and other related provisions of the Commercial Code



March

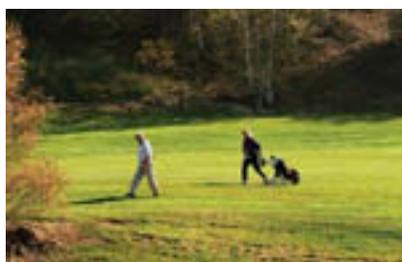
auditors issue an unqualified opinion on the Company's 2004 financial statements



June



Plzeň Regional Court decides to strike Sokolovská uhelná, a.s. from the Commercial Register without liquidation and on the take-over of all assets, receivables, and liabilities, including employment-related rights and obligations, by the principal shareholder Sokolovská uhelná, právní nástupce, a.s. (formerly Sokolovská těžební, a.s.)



November

approval of the 2006 business plan

December

approval of the Mine Opening and Exploitation Preparation Plans for 2006 – 2010 for the Jiří mine



signing of the 2006 Collective Agreement

2006

January

Division Energetika and Division Tlaková plynárna merged to form Division Zpracování (Processing Division)

March

auditors issue an unqualified opinion on the Company's 2005 financial statements



Letter

FROM THE CHAIRMAN



DEAR SHAREHOLDERS AND FRIENDS,

Allow me to inform you of events that took place at Sokolovská uhelná in a time of change in the Company's ownership.

Traditionally, we evaluate the development of selected indicators under Czech Accounting Standards within the wider context of information presented in past annual reports. We also discuss the accomplishments and challenges that are not evident from a mere quantification of selected indicators, yet nonetheless influence the Company's plans for the near and more remote future. In particular, these are facts that influence the Company's health and form the basis of its prosperity.

2005 was not an easy year for our Company. Supply of solid fuels continued to outstrip demand and the opening of the electricity market took another step, and now over 160 electricity traders serve over three quarters of eligible customers. Our business was impacted by movements in the prices of certain commodities such as natural gas, the consumption of which is a major determining factor in the ability to quickly regulate the power generation output of our production processes. Environmental requirements applicable to the Company's production processes

became stricter, and there were also certain impacts related to the new application of rules following our country's accession to the European Union.

My intention in naming these factors is to give the reader an idea of the difficult economic and social environment in which we did business and dealt with conflicts of interest that arose with our competitors and some of our business partners. At the same time, we addressed the changes taking place in our Company on many levels. This is the context in which I judge and appreciate the value of our accomplishments, which I consider to be of key importance for the future of our Company. Because the accomplishments were made in a manner compatible with

“...the accomplishments
were made in
a manner compatible
with the Company's



vision and long-term objectives...”

the Company's vision and long-term objectives, the latter were not compromised and there is no need to adapt them to the changes in the business environment that could not be foreseen so far in advance.

Although we cannot avoid problems that arise outside the company and hence are beyond our control, the performance results achieved last year give us reason to be cautiously optimistic that they will be transformed into further prosperity for the Company, allowing us to retain our position in the national economy and the region.

In conclusion, allow me to thank our employees, business partners, and other stakeholders for the part they played in the accomplishments of last year.

A stylized, handwritten signature in black ink, consisting of a large loop and a trailing flourish.

František Štěpánek
Chairman of the Board of Directors

People in the Management OF SOKOLOVSKÁ UHELNÁ

BOARD OF DIRECTORS



František Štěpánek

Chairman of the Board of Directors and Chief Executive Officer

Member of the Boards of Directors of Kinotechnika Praha, a.s., ZMA a.s., Sokolovská obchodní, a.s., Golf Sokolov a.s.
Member of the Supervisory Board of Coal Energy, a.s.

Graduate of Ostrava Mining University,

Born in 1953,

26 years' mining industry experience;

Production Director in 1994 – 1999, and Member of the Board and

CEO of Sokolovská uhelná, a.s. since 1999, Chairman of the Board

of Sokolovská těžební, a.s. in 2002 – 2005, Chairman of the Board

of Directors of Sokolovská uhelná, a.s. in 2004 – 2005, Chairman

of the Board of Directors of Sokolovská uhelná, právní nástupce, a.s. since 2005.



Jaroslav Rokos

Vice Chairman of the Board of Directors and Finance Director

Statutory representative of Malé Versailles, s.r.o.

Member of the Supervisory Boards of Golf Sokolov a.s. and SATER-CHODOV spol. s r.o.

Graduate of Prague Economics University and Prague International Business School,

Born in 1963,

21 years' mining industry experience;

Finance Director of Sokolovská uhelná, a.s. since 1995, Chairman

of the Supervisory Board of Sokolovská těžební, a.s. in 2002 – 2005,

Vice Chairman of the Board of Directors of Sokolovská uhelná, a.s.

in 2004 – 2005, Vice Chairman of the Board of Directors

of Sokolovská uhelná, právní nástupce, a.s. since 2005.



Jiří Pöpperl

Member of the Board of Directors and Technology Director

Member of the Boards of Directors of Golf Sokolov a.s. and CHEBIO a.s.
Statutory representative of HC Baník Sokolov spol. s r.o.
and Member of the Sokolov City Council

Graduate of Ostrava Mining University,
Born in 1956,
26 years' mining industry experience;
Technology Director of Sokolovská uhelná, a.s. since October 2004,
Member of the Board of Directors of Sokolovská uhelná, právní
nástupce, a.s. since 2005.



Jiří Peterka

Member of the Board of Directors and Production Director

Graduate of Ostrava Mining University,
Born in 1949,
31 years' mining industry experience;
Production Director of Sokolovská uhelná, a.s. since 1999. Member
of the Supervisory Board of Sokolovská uhelná, a.s. elected
by the employees in 1994 – 2001. Member of the Board of Directors
of Sokolovská uhelná, a.s. in 2004 – 2005, Member of the Board
of Directors of Sokolovská uhelná, právní nástupce, a.s. since 2005.



Jiří Radosta

Member of the Board of Directors and Personnel Director

Member of the Board of Directors of the Ohře River Valley Regional Economic Chamber

Graduate of Žilina Mining University
Born in 1948,
33 years' mining industry experience;
Personnel Director of Sokolovská uhelná, a.s. since 1994, Member
of the Board of Directors of Sokolovská uhelná, a.s. in 2004 – 2005,
Member of the Board of Directors of Sokolovská uhelná, právní
nástupce, a.s. since 2005.

SUPERVISORY BOARD

Miroslav Soural

Chairman of the Supervisory Board

Sales Director of Sokolovská uhelná, právní nástupce, a.s.
Born in 1947

Jan Smolka

Vice Chairman of the Supervisory Board

Member of the Supervisory Board elected by the employees
Chairman of the Association of Labor Organizations of Sokolovská uhelná, právní nástupce, a.s.
Born in 1949

Members of the Supervisory Board:

Otokar Sojka

Private entrepreneur
Born in 1947

Jan Birke

Representative of the Ministry of Finance (under the terms of the privatization of Sokolovská uhelná, a.s.)
Born in 1969

Josef Michalský

Head of the Office of the CEO of Sokolovská uhelná, právní nástupce, a.s.
Born in 1948

Jiří Selvička

Head of the Legal Section of Sokolovská uhelná, právní nástupce, a.s.
Born in 1948

Zbyšek Klapka

Head of the Accounting Section of Sokolovská uhelná, právní nástupce, a.s.
Born in 1964

Jiří Blažek

Member of the Supervisory Board elected by the employees
Chairman of the Družba labor organization of Sokolovská uhelná, právní nástupce, a.s.
Born in 1967

Radovan Třešňák

Member of the Supervisory Board elected by the employees
Chairman of the Zpracování labor organization of Sokolovská uhelná, právní nástupce, a.s.
Born in 1954

THIS RENAISSANCE BUILDING on

Sokolov's historic square was built around 1540 and re-built into today's form after a fire in the 1630s. In the early 19th century its front facade underwent a classicist facelift. In addition to the city tavern, the building used to serve as the town hall. It continued to serve this purpose until the mid-20th century.



SENIOR MANAGEMENT

(as of 1 January 2006)

František Štěpánek
Chief Executive Officer

Jaroslav Rokos
Finance Director

Jiří Pöpperl
Technology Director

Jiří Peterka
Production Director

Miroslav Soural
Sales Director

Jiří Radosta
Personnel Director

Alojz Neveďal
Director, Division Jiří

František Kastl
Director, Division Družba

Pavel Homola
Director, Division Zpracování

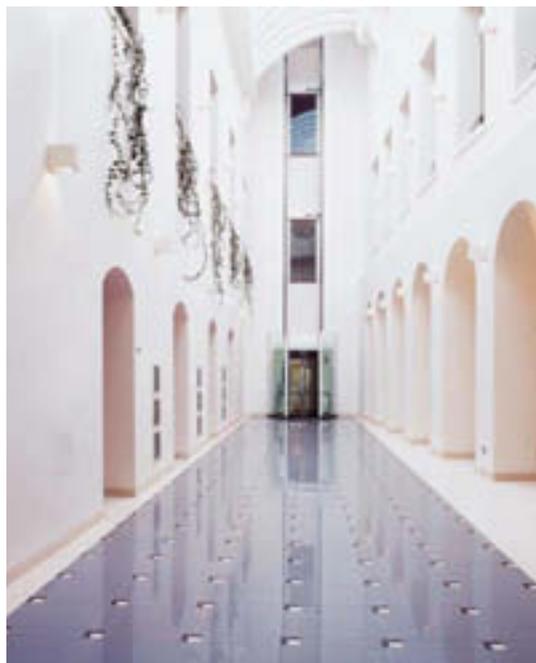
Jan Smolka
Director, Division Služby

Until 31 December 2005

the processing operations of Sokolovská uhelná took place in two divisions: Tlaková plynárna (Director: Petr Záruba) and Energetika (Director: Miroslav Mutinský).

On 1 January 2006, the Energetika and Tlaková plynárna Divisions were merged into Division Zpracování (Processing).

The organization chart appears on page 60.



THE TOWN HALL'S current appearance dates to its last renovation in 1995. Today it serves as the seat of Sokolovská uhelná.

(lower right)

THE SEAT OF THE SUBSIDIARY Malé Versailles and the restaurant of the same name is located in Karlovy Vary.



Company Timeline

2002

February 25: establishment of Sokolovská těžební, a.s.

August 23: Sokolovská těžební, a.s. recorded in the Commercial Register.

2003

October – Sokolovská těžební, a.s. participates in privatization tender for the State's equity stake in Sokolovská uhelná, a.s.

2004

March – Government Resolution No. 263 approves direct sale of the State's equity stake in Sokolovská uhelná, a.s. to Sokolovská těžební, a.s.

Reorganization

2002 – 2005

June – under the Government Resolution, Sokolovská těžební, a. s. purchases shares in Sokolovská uhelná, a.s. owned by the National Property Fund of the Czech Republic and PAL a.s., as well as from other minority shareholders.

August – October – Sokolovská těžební, a.s. carries out mandatory take-over of shares of Sokolovská uhelná, a.s.

2005

July – Commercial Register information amended (retroactively effective January 1) to reflect take-over of capital of Sokolovská uhelná, a.s. pursuant to Section 220p and related provisions of the Commercial Code. Also, the Company's name was changed to Sokolovská uhelná, právní nástupce, a.s. and its registered office was also changed.



The Company Today

THE PRINCIPAL BUSINESS ACTIVITIES OF SOKOLOVSKÁ UHELNÁ ARE the extraction of brown coal and, to a lesser extent, other minerals, and the processing and conversion thereof into value-added forms of energy as well as selling the resulting products, which are gaining in importance from year to year. Furthermore, the Company is involved in reclamation of land affected by coal extraction. Activities in this area include agriculture and forestry. Also significant are the Company's environmental activities, especially in the waste management area. The Company does not have any Research & Development (R&D) activities.



ONE OF THE MOST EXTENSIVE HISTORICAL

ARCHIVES concerning mining in Bohemia, which Sokolovská uhelná has administered since 1994, consists of collections and funds dating from the second half of the 18th century to the present. The most important funds of economic organizations include Dolové a průmyslové závody (formerly Jan David Starck Dolní Rychnov) from 1885-1946, documentation of Karlovy Vary's Duchcovská-podmokelská Line dating from 1805-1946, and Hnědouhelné doly a briketárny Sokolov from the period 1946-1990.



THE SOKOLOV REGION has always been rich in natural resources. There is no other area in the Czech Republic that can boast practically all possible types of minerals in such a small area. Historically, the Sokolov region's location predetermined that it would become a major mining center and a crossroads of business and industry.

BROWN COAL HAS BEEN MINED IN THE SOKOLOV AREA SINCE THE 17TH CENTURY

Brown coal has been mined in the Sokolov area since the 17th century. It reached its first peak in the 19th century when independent miners began to join together to form cooperatives and, later, mining companies. The growth of the industry got a major boost with the construction of the Buštěhrad Line, a railway connecting Prague and Cheb, with further connections to Bavaria and Saxony.

At the beginning, coal was mined exclusively underground and in small-pit operations in locations where the coal seam was directly

accessible from the Earth's surface. Starting in the 1945, the industry began moving gradually toward more efficient large-scale surface mining. After World War II, all privately-owned mines were nationalized by presidential decree. The construction of coal processing centers, first in the western portion of the mining area in Tisová (1955-60) and in the eastern portion at Vřesová (1960-70), created conditions for the growth of surface mining. Through a gradual process of integration and shutting down of inefficient operations, ten national enterprises were formed. In 1965, these ten were

merged to form Hnědouhelné doly a briketárny.

In the early 1990s, state-owned enterprise operations relating to mining and processing of coal extracted in the region were spun off to form Palivový kombinát in Vřesová, Hnědouhelné doly in Březová and Rekultivace in Sokolov. Subsequently, these three enterprises were merged to form Sokolovská uhelná, a.s., which as of 30 June 2005 continues as Sokolovská uhelná, právní nástupce, a.s. Coal mining in the Sokolov area takes place in two mines: Jiří and Družba.



COAL MINING TAKES PLACE IN TWO MINES: JIŘÍ AND DRUŽBA

Division Jiří

Of the Company's two mines, Jiří occupies the largest area and is also the deepest. Its annual production can reach up to 8.5 million tons.

For extraction, the mine is equipped with five bucket-wheel excavators and a 1,400 mm gauge trunk belt conveyor. Extracted coal

is first crushed to the desired grade and then shipped to the Processing Section in Vřesová and, through the Tisová processing and sorting facility in Citice to the Tisová heat/power plant, as well as to customers in the form of sorted coal.

In the Jiří mining field, a 40 meter thick brown coal seam has

been developed and is known as the "Antonín". Since 1950, the mining operation has been moving in a westwardly direction from the village of Vintřův at a rate of approximately 90 meters per year towards the City of Sokolov, where the mine is set to shut down its operation in or around the year 2027, depending



The Company is backed by a long, rich tradition of brown coal mining and processing in the Sokolov region. It is a dynamic fuel-energy complex that mines approximately 10 million tons of brown coal per year.

on the development of actual annual extraction volumes. As of 31 December 2005, the Jiří mine's extractable reserves stood at 170.6 million tons.

Since 2000, the mining operation associated with the first coal cut has been progressing deep into a portion of the seam that had

been worked in the past by the underground mines Marie in Královské Poříčí and Jiří in Lomnice. The implication is that, until the end of the mine's useful life, extraction at the Jiří mine will take place in the portion of the coal seam affected by legacy mining operations and, in the next few years, the ratio of virgin coal to

tainted coal will gradually decrease. Currently, the mining operation has progressed to the point that the second coal cut has begun to produce tainted coal as well. For this reason, more demands are being placed not only for selective extraction of coal matter from sites of legacy "long wall" operations, but also



Over time, brown coal mining in the Sokolov region has changed dramatically. Underground and small-pit techniques have been replaced by large surface mines. Currently, two such mines are in operation.



Since 2000, mining activity has been concentrated in the eastern portion of the mining area. The Jiří mine's gross annual coal output is 8.5 million tons.



From the mine, the coal is conveyed to a loading station, from which it is hauled by rail to the Processing Section in Vřesová and to customers.

for the removal of remnants of the original underground mines and for prevention and extinguishing of spontaneous fires in the seam.

An integral link in the mining process chain is the intermediate product terminal, where a prescribed volume of non-graded brown coal (in 0-400 mm chunks) is kept on hand. This makes it possible to continue supplying customers even during mine outages.

Overburden is excavated using two large machinery complexes, each consisting of a bucket-wheel excavator on a walking truck undercarriage, a 1,800 mm gauge trunk belt conveyor, a re-loading vehicle on tracks and a belt spreader. The machinery complex that excavates the overburden layers nearest to the surface spreads extracted material on the upper levels of the Jiří in-mine spoil-bank. The second machinery complex conveys excavated material in a southerly direction to an in-mine spoil bank. Two smaller

machinery complexes, each consisting of a bucket-wheel excavator on a caterpillar undercarriage, 1,400 mm and 1,600 mm gauge trunk belt conveyors, a track vehicle and a belt spreader, also dump overburden inside the mine.

The coal extraction and overburden excavation operations are secured by a system of drainage conduits which direct rainwater to holding tanks dug into the spoil-bank with the objective of collecting rainwater and pumping it out of the mine before it reaches the bottom of the pit.

Division Jiří operates a coal crushing facility in Vřesová which includes a process dump and produces finely crushed coal for the briquette plant and, on four separate production lines, pulverized coal which is used by the Production Section to generate electricity. Another part of the division is the coal sorting facility in Tisová, where four types of sorted coal are produced. The facility is equipped to load the sorted coal onto both trucks

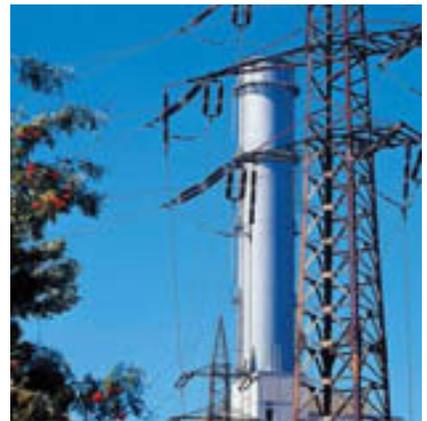
and train cars as well as the belt conveyors that transport some of the coal to the Tisová Power Station.

In addition to the brown coal mine, Division Jiří also operates the Horní Rozmyšl Rock Quarry. In 2005, the Horní Rozmyšl Rock Quarry extracted 749,000 tons of granite, which is used mostly to build roads, railways, and drain fields.

Division Družba

The core activity of Division Družba is the extraction of brown coal from the Družba mine, which has a total annual capacity of over 2 million tons, and the related extraction and dumping of overburden material.

The Družba mine extracts coal from three coal cuts using bucket-wheel excavators. When needed, their reach can be extended using re-loading vehicles on tracks. Overburden is extracted by four



The Družba mine's planned useful life is to expire in 2036. The mine has 39.9 million tons of extractable coal reserves.

After the town gas system was shut down in 1996, Division Tlaková plynárna gasifies coal to meet the fuel needs of the combined-cycle power plant.

bucket-wheel excavators. Overburden is transported mainly via 1,435 mm gauge rail spur. Some of the overburden material is conveyed to a production facility where it is used to make lightweight construction materials. The mine's planned useful life is to expire in 2036. As of 31 December 2005 the mine had 39.9 million tons of extractable coal reserves.

Division Družba operates all the Company's rail tracks, including industrial rail spurs. It is the Company's internal transportation provider, hauling coal from the Jiří and Družba surface mines to the Processing Section as well as shuttling back and forth between Division Jiří and Division Družba (Extraction Section) loading stations and the Tisová Power Station.

The division also operates the Erika Sand Quarry. Currently this facility is operated on an as-needed basis only. In 2005, it produced 556 m³ of sand.

Another part of the division is the Reclamation Section. Originally a typical agricultural enterprise that also had extensive forestry operations, in the late 1980s its focus shifted to reclaiming former mines using technical and biological reclamation methods. Now,

agriculture and forestry operations complement its core reclamation operations, and the Section is a major breeder of Charolais cattle.

Large-scale reclamation and construction projects include, for example, the Michal Water Park and the golf course in Dolní Rychnov, as well as the Boden Reservoir and the complete reclamation of the Velký Loket spoilbank with an area of over 400 hectares.



"UNLIKE OTHER brown coal companies, a considerable portion of our coal output is processed in-house to produce value-added fuels and energy in the combined-cycle power plant, which is the only one of its kind in Europe. It makes it possible for us to generate clean, environmentally friendly energy. The plant is unique in that its primary fuel is gas produced from coal."

Jiří Peterka, Production Director

CONVERSION OF COAL INTO VALUE-ADDED FORMS OF ENERGY

Division Zpracování

The Processing Section of Sokolovská uhelná is a complex of industrial processes focused on converting brown coal into value-added forms of energy. The Processing Section of Sokolovská uhelná produces value-added forms of energy through a series of chemical and industrial processes: preparation and processing of basic raw materials, generation of steam, brown coal gasification, purification of the coal gas, processing and purification of by-products and waste materials, and, finally, utilization of the purified coal gas to generate electricity and heat. The Processing Section includes the following three main production processes:

Coal Processing Plant

Coal Processing Plant pulverizes, dries, and sorts coal to prepare it for gasification and for combustion in a conventional heat/power plant. It includes a briquette plant where low-sulfur-content coal is pressed into briquettes without the use of adhesives.

Coal Gasification Plant

After being pulverized, the coal is pre-dried and sorted. The finer grains are combusted in the conventional heat/power plant. The rougher component is used as

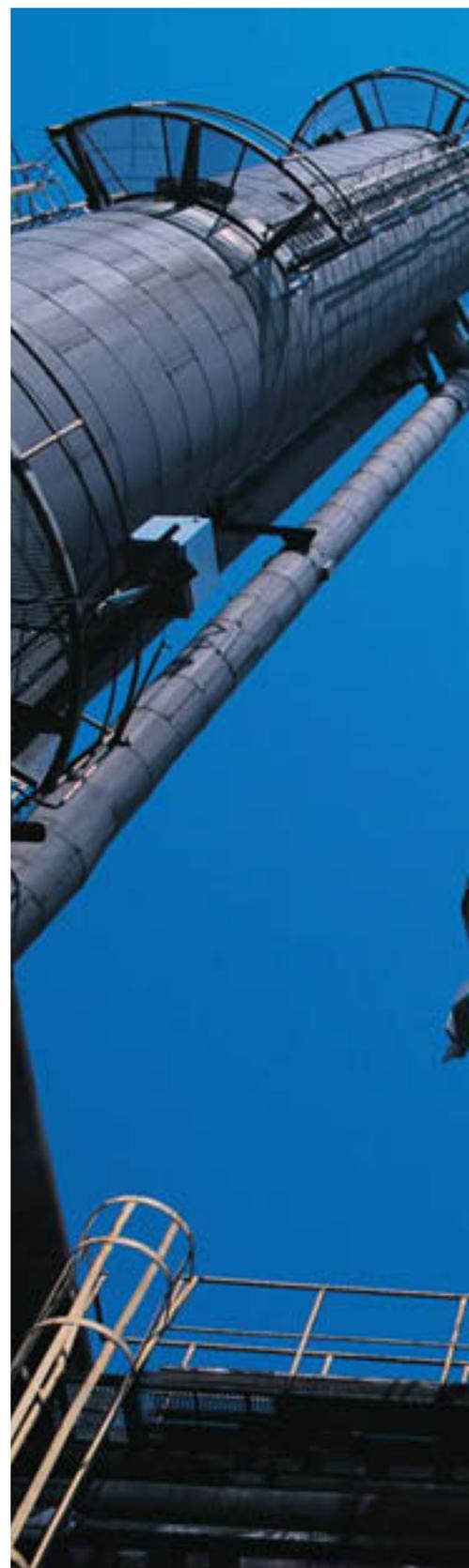
coal charge in the gasworks. Pressurized to 2.7 MPa, the coal is gasified using a mixture of oxygen and steam in sliding-bed generators (Lurgi). The resulting raw gas is purified by a Rectisol process using cooled-methanol scrubbing. The purified coal gas is used as the base fuel in the combined cycle power plant. Nowadays the coal gasification process includes a new unit for gasifying carbochemical by-products in a “burner generator”.

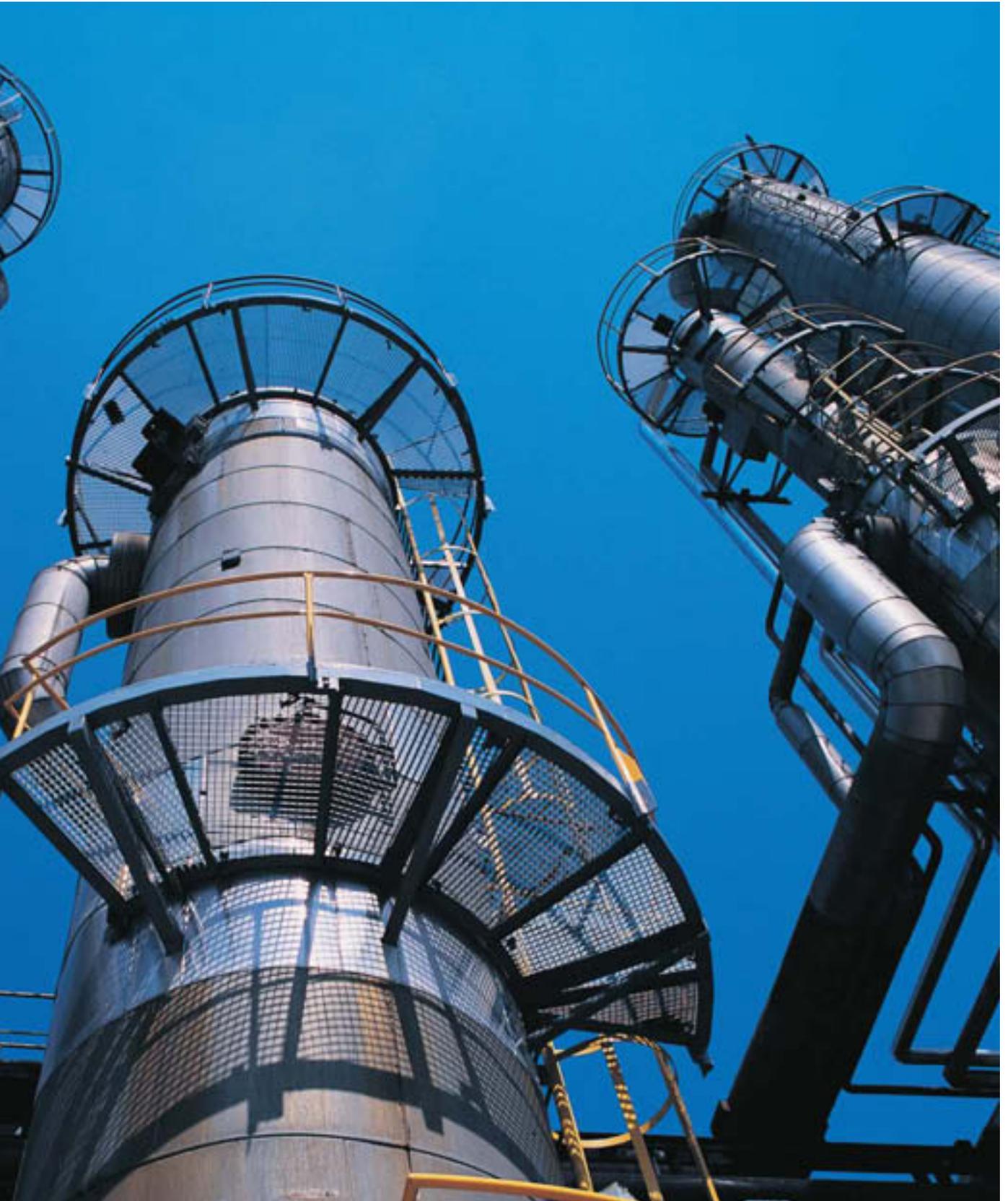
Power Plants

Electricity and process steam used by other Processing Section facilities are generated in a conventional heat/power plant (fired by the finely pulverized coal that falls through the sorting mesh used to prepare coal charge for the gasworks) and in a combined-cycle power plant (the “CCPP”). A portion of the electricity generated is used in-house and the rest is provided to the public power grid. Thermal energy is utilized in the Processing Section as well as in the district heating systems of the surrounding towns.

Gas Purification Process

Selective Rectisol scrubbing is used to purify the gas by removing all benzenes, all hydrogen sulfide, and certain organic compounds as





well as residual ash matter. As the gas generated is used as fuel for gas turbines, most carbon dioxide is left in the gas for two reasons: it performs mechanical work in the gas turbine and, as an inert material, it has a favorable effect on the generation of nitrogen oxides during combustion in the gas turbine.

Desulfurization of expansion gases from the selective scrubbing process gives rise to sulfuric acid (95% hm). The desulfurization process used is based on catalytic oxidation of hydrogen sulfide to produce sulfur trioxide and subsequent condensation into sulfuric acid.

The desulfurization unit is the last stage in the coal gas production process. In essence, it serves to liquidate waste gas from the Rectisol process, which in addition to hydrocarbons also contains hydrogen sulfide and organic sulfur compounds. After desulfurization, the gases released into the atmosphere contain very small amounts of sulfur dioxide, traces of sulfur trioxide and nitrogen oxides, none of

which pose a significant threat to the environment.

After passing through the purification equipment, the gas is at a high pressure (2.1 – 2.5 MPa), allowing it to be used in the gas turbine without further compression. The purified gas is practically sulfur-free and does not contain any nitrogenous substances. This makes it appropriate for use as an environmentally-friendly fuel in the power plant.

Production of Coal Gas

Coal gas, produced by gasification of coal under high pressure, serves as the primary fuel for the combined cycle power plant. Natural gas, which makes it possible to change generating output quickly, is used as a backup fuel. Natural gas is brought to the Vřesová power plant via a spur from the transit gas pipeline that supplies the Czech Republic with natural gas from Russia. Both fuels are combusted in the combustion chamber of the gas turbine.

Air, which is used for combustion and to cool the flow-through portion of the turbine, is delivered by a turbocompressor located on the same driveshaft as the turbine. The combustion gas, which has a temperature of approximately 1,100 °C at this point, then enters the gas turbine proper, which drives a generator. Upon leaving the turbine the gas, now at a temperature of approximately 540 °C, goes to the waste heat boiler. To reduce the formation of nitrogen oxides in gas combustion, steam is injected into the gas turbine's combustion chamber.

The boiler is a dual-pressure unit without supplemental heating. Steam passes into a dual-body, dual-pressure condensation steam turbine with two regulated outputs, which runs its own generator. Prior to reaching the stack, the heat in the flue gases is utilized to pre-heat water for the Karlovy Vary district heating system. The flue gases produced by the boiler comply with all environmental standards.

The electricity generated by both generators runs through a transformer and further over a 220 kV power line to the Vítkov substation. The unit's control system takes full advantage of the gas turbine's features and, since operation is highly automated, allows the facility to be used as a peaking plant. The steam portion of the plant's infrastructure is closely interconnected with the heat/power plant in Vřesová. The interconnection of both plants has created a flexible complex with a high level of operating reliability.

The gas turbine's connection to the steam infrastructure and its cutting-edge control system



Coal gasification and power generation at Vřesová form an intriguing example of how conventional coal technology can be combined with modern power generation techniques.

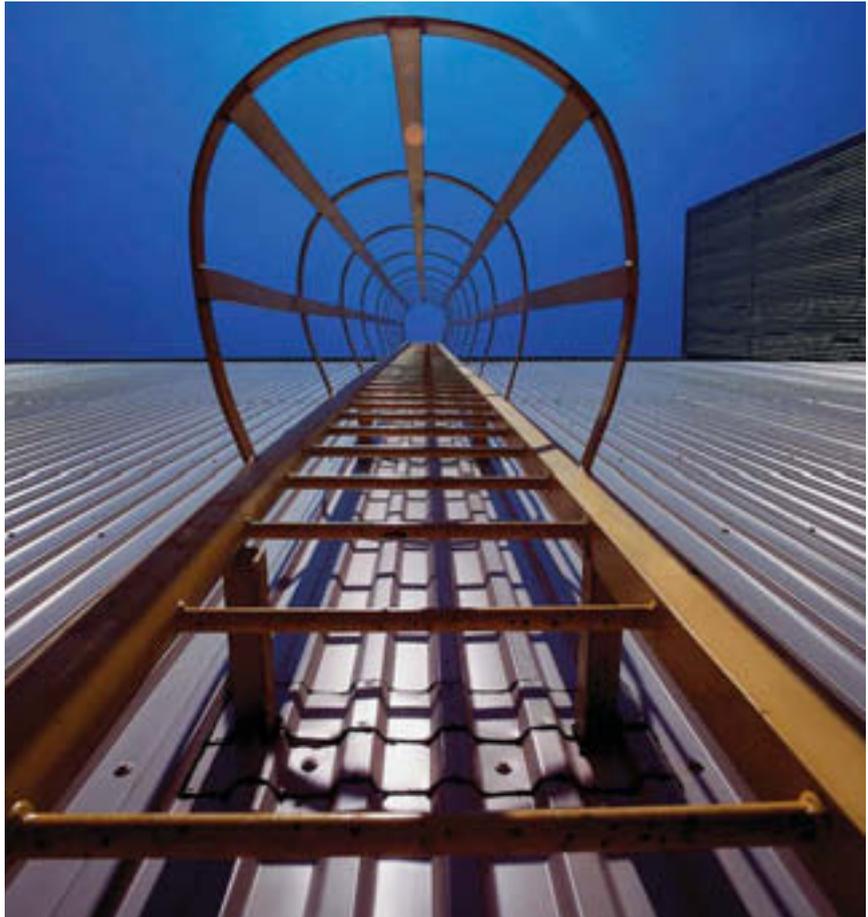
make it possible to take full advantage of the combustion turbine's dynamic features to obtain a peaking power plant with acceptable up-front and operating costs.

The gas turbine's thermodynamic efficiency is 34.8%; the efficiency of the generating unit as a whole when the steam turbine is run in condensation mode is 50.5%, and the use of flue gas to pre-heat water for use in district heating increases the plant's overall efficiency to 54.5%.

The Company's future development and the operation of the Processing Section must be systematically combined with environmental upgrades and the use of clean coal technologies. This will enable the technologies to be operated for the long term, up until the Sokolov Basin's coal reserves are exhausted.

Currently, the Company's plant and equipment is being expanded with the construction of a unit for gasification of carbochemical products (phenols and tars) generated as waste products by the Lurgi gasification process.

Coal gasification and power generation at Vřesová form an intriguing example of how conventional coal technology can be combined with modern power generation techniques. The result is a highly efficient unit with advantageous regulation features that generates clean, environmentally-friendly electricity from brown coal. Modern purification techniques find wide-ranging application here, reducing the environmental impact of gas production and power plant operation.



The heat/power plant generates nearly half of the Company's overall electricity output. Some of the electricity generated is used to cover the Company's own power needs.

Support Section

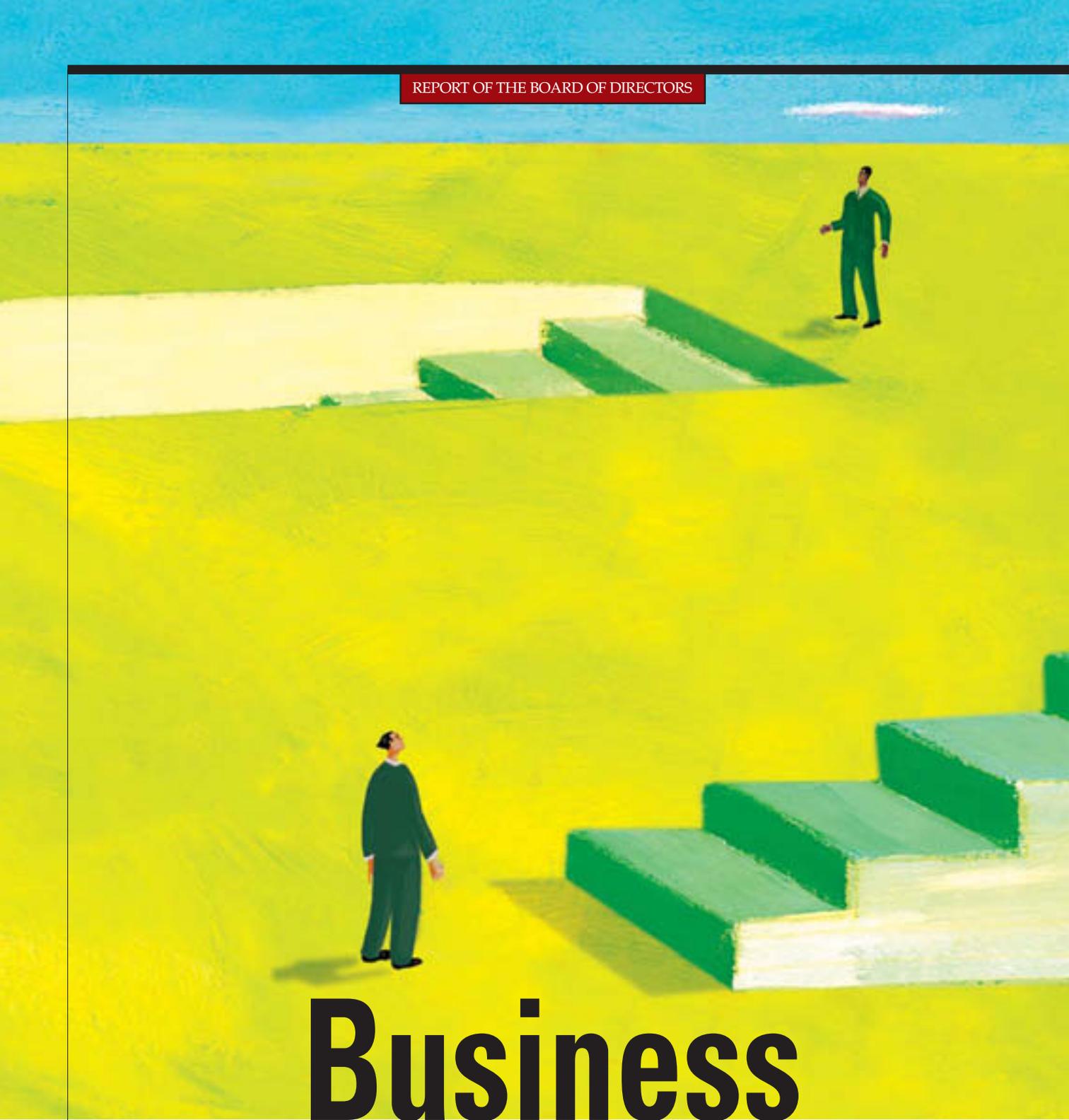
In addition to the core products outlined above, the Company provides a number of ancillary services and products through its Support Section.

Divisions Služby and Správa

Division Služby's primary roles in the overall Company structure are repairing and maintaining production equipment and technologies, providing technical solutions for

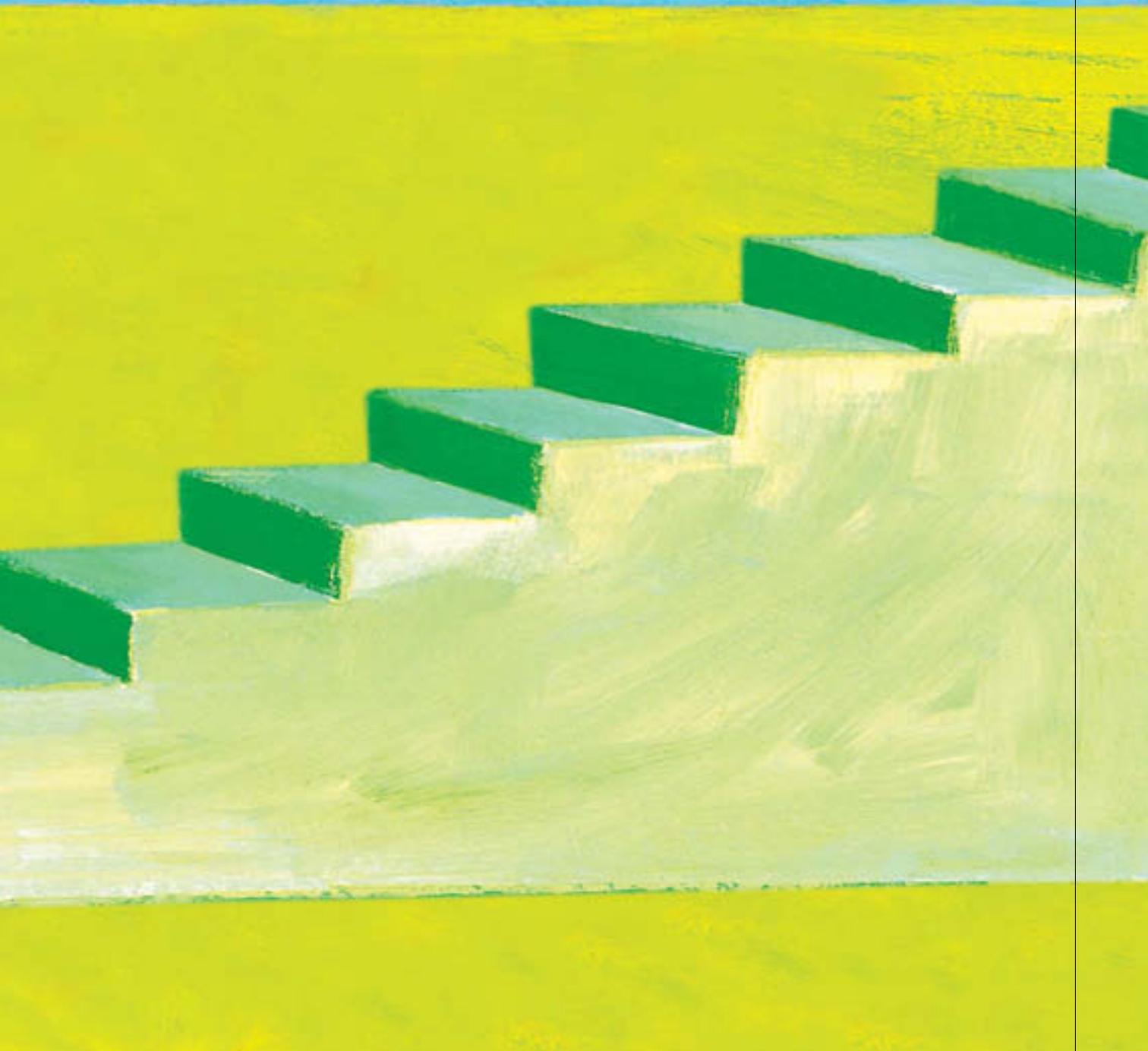
shifting large equipment complexes and other mechanical jobs, sourcing materials for repairs, refurbishing spare parts, obtaining and setting up telecommunications, measurement, and regulation equipment. The division also includes a fire and rescue brigade. This is a professional unit that is part of the regional integrated rescue system.

All white-collar activities of the Company take place in the various sections of Corporate Administration (Správa), which report to the Company's specialized directors.



Business

ENVIRONMENT



IN THE PAST FEW YEARS, coal mining has stabilized in the Czech Republic. The amount of coal extracted in 2005, approximately 62 million tons, was the same as in 2004. Black coal extraction was down slightly (by 0.5%), while brown coal volume increased by 0.6%. In 2005, approximately 49 million tons of brown coal was extracted, which is about 0.3 million tons more than in 2004.



BUSINESS ENVIRONMENT IN THE COAL INDUSTRY

Privatization of the Coal Mining Industry

All of the Czech Republic's coal mining companies have been privatized. Mostecká uhelná a.s. has been in private hands since 1998, Sokolovská uhelná, a.s. and OKD, a.s. since 2004. The privatization of the entire indus-

try was completed by the sale of Severočeské doly a.s. to ČEZ, a.s. ("ČEZ") in late 2005.

Territorial Extraction Limits

The coal mining companies in the North Bohemian brown coal belt await clarification of the situation relating to

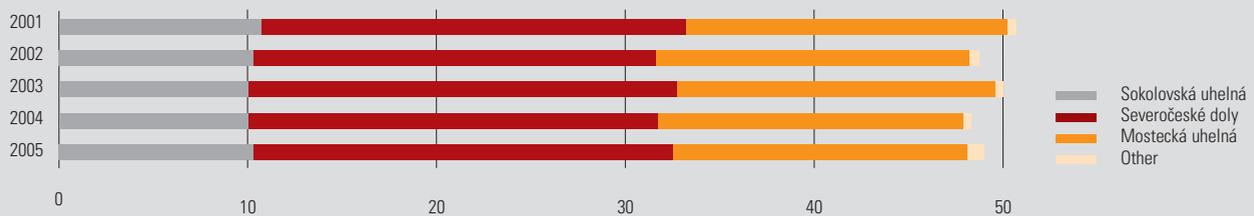
the territorial extraction limits. The limits were set by the Government in 1991. In 2004, the Government approved the State Energy Policy with an outlook to 2030, in which brown coal was declared a strategic resource for ensuring a long-term, safe supply of energy. The State Energy Policy calls for a rational review of the current limits. At present, the Ústí Region



THE NEW COMBINED-CYCLE POWER PLANT, which

expanded the Company's generating capacity to 620 MWe, made us the largest independent electricity producer in the Czech Republic. As it is operated today, the facility is a waste-free technology that processes 3.5 million tons of brown coal a year without any significant negative environmental impact.

Brown Coal Mining in the Czech Republic



Master Zoning Plan is undergoing public review in two versions, on calling for extraction within the

territorial limits and the other permitting extraction beyond today's territorial limits. Sokolovská uhel-

ná has already resolved this issue up to the end of the planned useful lifespans of both of its mines.

Situation and Developments in the Power Industry

The electricity market liberalization process that began in 2002 was finished in 2005 and as of 1 January 2006 the market is fully open to competition. Even households have the option of choosing their electricity supplier. However, no large shifts in the customer base are expected.

The gas market was further liberalized in 2005 and as of 1 January 2006 it is fully open to all non-household customers. It will be fully liberalized for all customers starting in 2007.

Energy Prices

Effective 1 January 2006 the prices of electricity, gas, and heat all went up. The price of electricity for households, which is set once per year, increased by an average of 8.9%.

The price of natural gas for protected customers, which is set by the Energy Regulatory Authority once per calendar quarter, increased by an average of 4.8% as of 1 January 2006. Overall, the price of natural gas grew by an average of 21.2% during the past year, and the highest growth was seen in October 2005, when natural gas prices rose by an average of 17.4%. In view of the price growth, the Energy Regulatory Authority decided to continue to regulate natural gas prices this year.

The price of heat also rose. The cost of heat generated in gas boiler rooms rose by 10–11% on average, while coal-generated heat rose in price by 1.1–2.9%.

As for coal itself, the average price increase in 2006 is not expected to exceed 5%.

ČEZ's Decision to Retrofit Brown-coal Power Plants

ČEZ decided to retrofit its brown-coal power plants Tušimice II, Pruněřov II and three of five generating units at Počerady. Further, it plans to build two new 600 MW units at Ledvice and Počerady. The total installed capacity of the new and retrofitted units is to be 3,700 MW and total capital expenditure is estimated at CZK 100 billion. The projects are to be completed over the period 2007–20.

Should the territorial extraction limits be extended, ČEZ is considering building another two 600 MW units. This would increase the amount of retrofitted/new capacity to 5,000 MW and capital expenditures would rise to approximately CZK 150 billion.

ČEZ Group ("ČEZ") is currently the number-eight power utility in Europe in terms of the number of customers (6.6 million).

Significant Changes in the Power Industry

Two legislation-driven processes had an impact on the market environment in the Czech electric



power industry. The separation (or “unbundling”) of electricity distribution from electricity sales and the ongoing expansion of eligible customer status to all customers except households during the year, with the objective of achieving 100% customer eligibility by 31 December 2005. Both processes are to contribute to the liberalization of the Czech power industry.

The increased numbers of eligible customers did not lead to significant changes in suppliers of electricity, though of course the “unbundled” sales units did take over eligible and captive customers from their parent regional electricity distribution

companies and reorganized themselves in line with the structures of the newly formed distribution companies.

In terms of regulation, the price of electricity supply for all customers except households became a market price and ceased to be subject to regulation by the Energy Regulatory Authority. Electricity distribution prices continue to be regulated by the same Authority.

The past year brought no significant changes in the ownership structure of power plant facilities. ČEZ continues in its dominance as the largest producer, seller, and distributor of electricity.



2005 was also to the first year in which greenhouse-gas reduction measures under the Kyoto Protocol were implemented. Within the EU, National Allocation Plans were drawn up and emission permit registers were formed. Concurrently, there was a massive onset of trading in emission permits, the impact of which on the strategies of individual Czech power market players can already be felt.

The Czech Republic was allotted 292.8 million permits for the 2005–07 period, i.e. 97.6 million per year. 3% and 1.5% of the total projected emissions of all plants, except new participants, is allocated for Early Action and Combined Heat and Power (CHP), respectively. The reserve allocation for new participants is 0.5 million permits per year, and any permits from this amount that go unused will be voided. Pooling of operators is allowed.

On 13 October 2005, a National Register for trading in greenhouse gas emission permits was put into operation. The first international transaction followed on 18 October 2005.

Nearly 160 electricity traders now serve over three quarters of eligible customers in the Czech Republic.



SOKOLOVSKÁ UHELNÁ – THE SMALLEST BROWN COAL COMPANY WITH SIGNIFICANT POSITION IN ITS MARKET

Although Sokolovská uhelná is the smallest brown coal company in the Czech Republic, and therefore a small organization in the European context as well, it maintains a significant position in its market. The

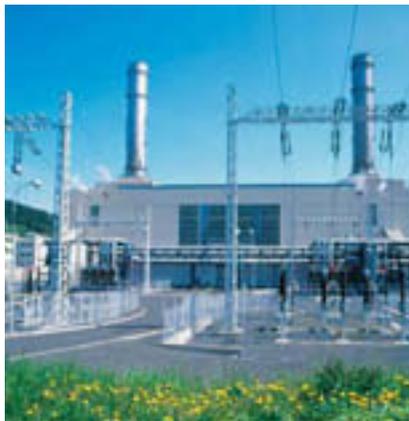
22.51% and in sorted coal our market share was 6.93%. Throughout the year, supply of coal was higher than demand. With key contractual customers, prices are negotiated individually based on the amount of coal they purchase.

sions in the region and, thereby, to an improvement in the overall Czech Republic living environment.

As the prices of fuels and resources for heat generation



The specific qualities of the brown coal we mine make it suitable for producing multipowder and briquettes.



Using the combined-cycle generation techniques, the Company generated 1,900 GWh of power in 2005.



Company is also involved in transporting coal and converting it into fuels and energy with higher utility and market value. This makes us a significant energy company at the national level.

In 2005, the Company also retained its position in the brown coal market. Our share in the total amount of brown coal extracted in the Czech Republic by brown coal companies was 21.39%. Our share of the pulverized coal market was

Brown coal mined from deposits in the western portion of the Podkrušnohorská area along the border with Germany (Saxony) is unique in that it is suitable not only for straight combustion but also for the production of multi-powder and briquettes, of which we are the only producer in the Czech Republic. Firing of Sokolov coal in facilities with varying generation capacities, large and small, contributed to reduced air emis-

grow, brown coal continues to be one of the lowest-priced fuels. Throughout 2005, the price of heat and electricity generated from coal remained far below the equivalent prices for natural gas and oil. Therefore, we can anticipate that some of the customers who switched to other fuels for heating in recent years will return to solid fuels.

Price movements in the electricity market have a fundamental

influence on the price of Czech coal. These movements, no doubt, will impact Sokolovská uhelná's actual sales of solid fuels.

Each year, the Company supplies approximately 2,300 TJ of thermal energy to adjoining industrial and urban areas. With the commissioning of the combined cycle power plant in 1996, bringing the Company's aggregate power generation capacity to 620 MWe, Sokolovská uhelná became the second largest electricity producer in the country.

well in the domestic market, mainly to heat plants for use as a fuel.

The Company's other chemical products are produced in relatively small volumes and in these commodities we are under strong competitive pressure from both domestic and foreign producers. In order to maintain our share in the markets for these products, product quality is very important. In sulfuric acid especially, very good qualitative parameters were achieved.

plants, heat plants and wholesalers. A large portion of solid fuel sales goes to other sectors of industry, such as chemicals and machinery production. Through wholesale partners, our solid fuels are distributed both in the Czech Republic and to export markets. A total of 2.1 million tons of brown coal was supplied to our strategic trading partner – ČEZ – in 2005. New customers have appeared, buying coal on a trial basis as they explore the future potential of low-sulfur coal as a fuel. Sokolovská uhelná also



Amount of coal sold in 2005 exceeded 6 millions.



"IN THE YEARS TO COME, the Company will continue to reinforce its position as the largest independent electricity producer in the Czech Republic. We will continue to focus our attention on effective utilization of the environmentally friendly power generation facilities built in previous years."

Miroslav Soural, Sales Director

Carbochemical by-products of the brown coal gasification process are unique not only in the Czech Republic but in all of Europe, since similar products elsewhere are produced exclusively from black coal and petroleum.

Phenol concentrate is in demand mainly in the EU market as a raw material for making pure phenol-based products. Brown coal generator tar sells

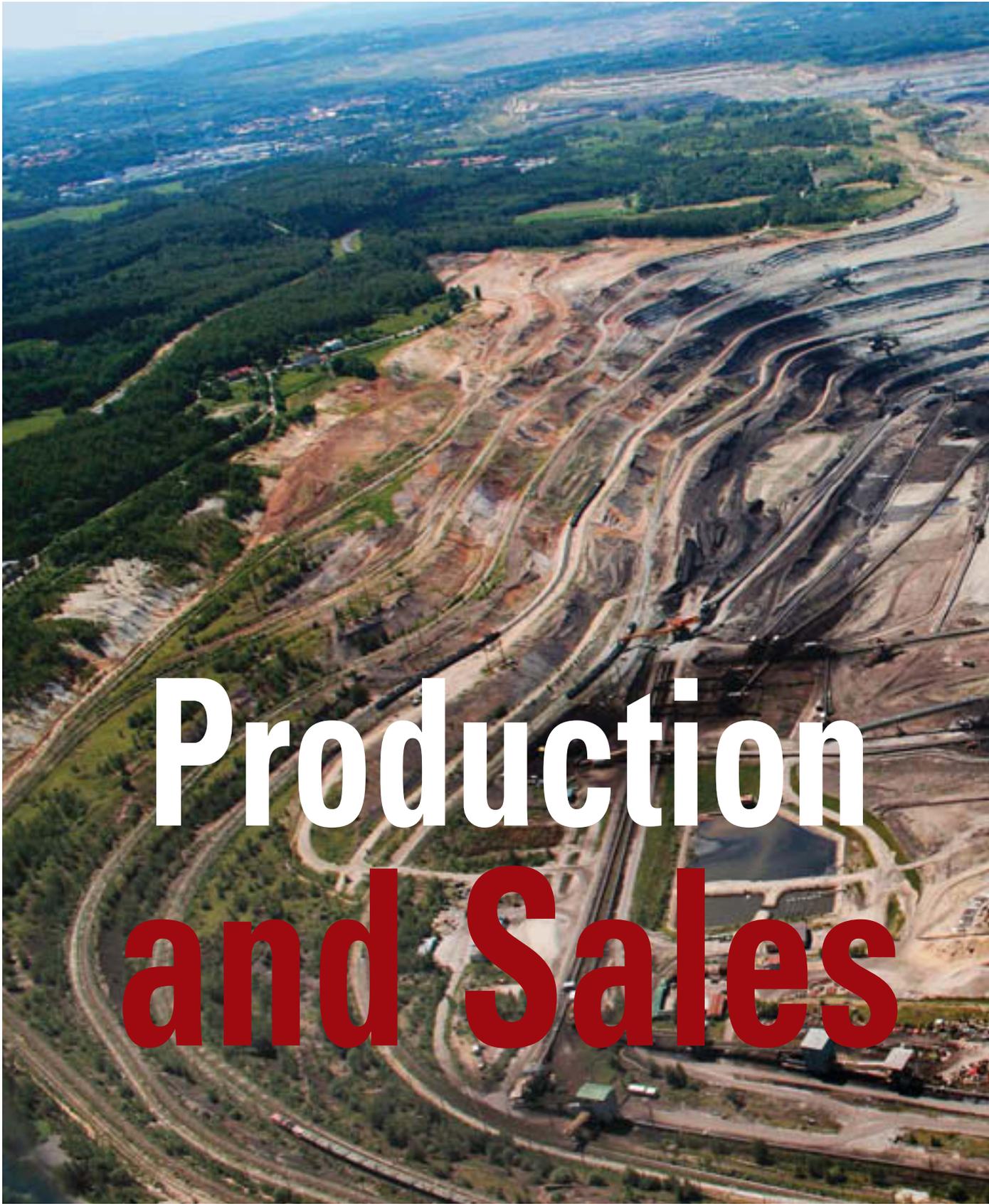
Customers of Sokolovská uhelná

The Company trades in its core products mostly on the basis of long-term framework agreements and one-year purchase contracts. The customer portfolio in electricity did not see any significant changes in 2005. ČEZ continues to be the largest customer.

In solid fuels, the Company's largest customers are power

increased its exports to Hungary and Slovakia.

In carbochemical products, Sokolovská uhelná sells to both foreign customers (Germany, Spain, and Austria) and domestic customers. Commercial relations with these partners were very good, thanks especially to the quality of the Company's services and maintenance of high product quality.



Production and Sales



SOKOLOVSKÁ UHELNÁ EXTRACTED a total of 10.307 million tons of coal in 2005, up 2.2% from the previous year. Division Jiří and Division Družba accounted for 79% and 21% of this amount, respectively.

Coal extraction increases, production and sales of fuels in 2005 higher than previous year

To gain access to the extracted coal, it was necessary to remove a total of 32.684 million m³ of overburden material from both the Company's mines. Of this total amount, Division Jiří accounted for 73% and Division Družba's share was 27%. Compared to 2004, overburden extraction volume was flat.

The briquette plant produced a total of 301,000 tons of briquettes in 2005, which is in line with 2004's production volume. Of the total, 9.7% were packaged briquettes, which are in high demand. In the past few years, annual production of this commodity has stabilized at approximately 30,000 tons.

Weather conditions last year were favorable to higher solid fuel sales for two reasons: first, they led to higher consumption and, second, customers had a greater need to form sufficient storage stocks for this year's winter. All purchase contracts were filled and some were significantly exceeded. New customers accounted for a significant share in excess sales of pulverized coal over plan.

On the downside, České dráhy (Czech Railways) implemented a large number of rail transport outages and this had a negative impact on solid fuel sales. Freight cars were not always available in sufficient numbers at the desired locations, there were some irregularities in supplying empty freight cars, and some track sections were operated only at certain times of the day. Especially in April and from September to the end of the year, this situation disrupted the sales process.

Solid fuel sales were also impacted by fluctuations in the quality of coal charge used to produce rougher-grade fuels. Even so, sales volumes of these grades rose by 10,000 tons compared to 2004. Compared to 2004 the sorted coal loading situation at the coal sorting plant was slightly improved, but there were still some supply outages.

Briquette sales performance in 2005 was practically identical to 2004. After a traditionally weaker sales period lasting until the end of the briquette plant's summer break, demand for briquettes skyrocketed and in the next four months (August – November), 140,000 tons of this commodity were sold (i.e. 48.8% of total annual production).

In the domestic market, 128,500 tons of briquettes were sold – this is in line with 2004. Also, 158,200 tons of briquettes were exported. The 2005 performance is actually higher, however, because the briquette plant's summer break was one week longer than in 2004. The situation in sales of packaged briquettes was the same as in 2004 – demand for packaged goods exceeded production capacity.

Sales of dried brown coal multipowder were in line with plan, with a total of 53,000 tons shipped.

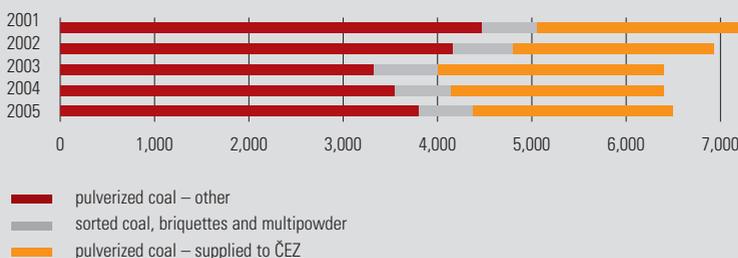


Electricity and Heat

The heat/power plant generated a total of 1,698 GWh of electricity. This is a record, and it was achieved largely thanks to the plant's operating reliability. No serious equipment failure occurred in the entire year 2005.

Generation volume at the CCPP totaled 1,900 GWh in 2005. This plant also exhibited high reliability throughout 2005. The only negative factor in the plant's operation was a modification to the control

Solid Fuel Sales (kt)



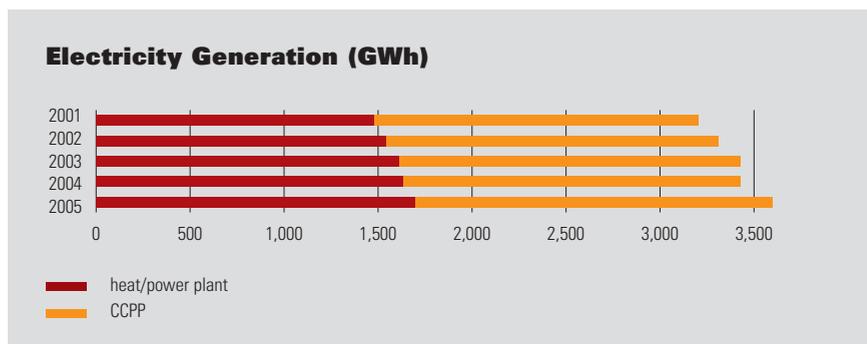
system which took longer than expected to complete.

An important change in electricity supplies took place in 2005. After several years, reserve capacity and regulation energy were not supplied to ČEPS, a.s. These supplies were replaced by provision of regulation capacity and regulation energy to ČEZ Group.

The customer change for regulation services also made it necessary to change how we do business with the Czech Republic market operator (OTE). In 2005, electricity was supplied to a primary electricity customer (ČEZ) and regulation responsibility was shifted to that customer. Sokolovská uhelná ceased being a settlement entity and became an electricity trader. This new arrangement was necessary in order to provide regulation services to the primary customer of electrical work. The changes also temporarily blocked our access to electricity spot markets.

Another important change was the commencement of electricity supplies to an external process gas supplier. This changed both the customer base and the volume of supplies from the heat/power plant due to lower in-house consumption.

The overall business plan figure for electricity revenues was exceeded by a slight margin. The revenues were achieved on significantly increased supplies of electrical work from both the heat/power plant and the CCPP (total supplies exceeded plan by 7.4%), which resulted in higher variable electricity generation costs. A total of 1,892 GWh was supplied to outside customers from the CCPP in the form of electric power and regulation



energy, while the heat/power plant supplied 1,007 GWh in the form of electric power. In the customer portfolio, ČEZ is in the number-one position by electrical work supply volume, with 74%. In terms of revenues, ČEZ's position is even stronger, since it also purchased regulation energy from us in 2005.

The vast majority of electricity supplies take place under long-term bilateral agreements; short-term contracts account for less than 2%.

The Company supplies heat to district heat systems in the Karlovy Vary Region, especially in the cities Karlovy Vary, Chodov, Nejdek, and Nové Sedlo.

Coal Gas and Carbochemical Products

Production of chemical products is dependent on production of **coal gas**, the primary fuel used in the combined cycle power plant. In 2005, 1.188 billion m³ of coal gas was produced.

Sales plans for 2005 were met for all chemical product commodities.

Brown coal generator tar – 85,000 tons of this commodity was shipped, down 6,000 tons from

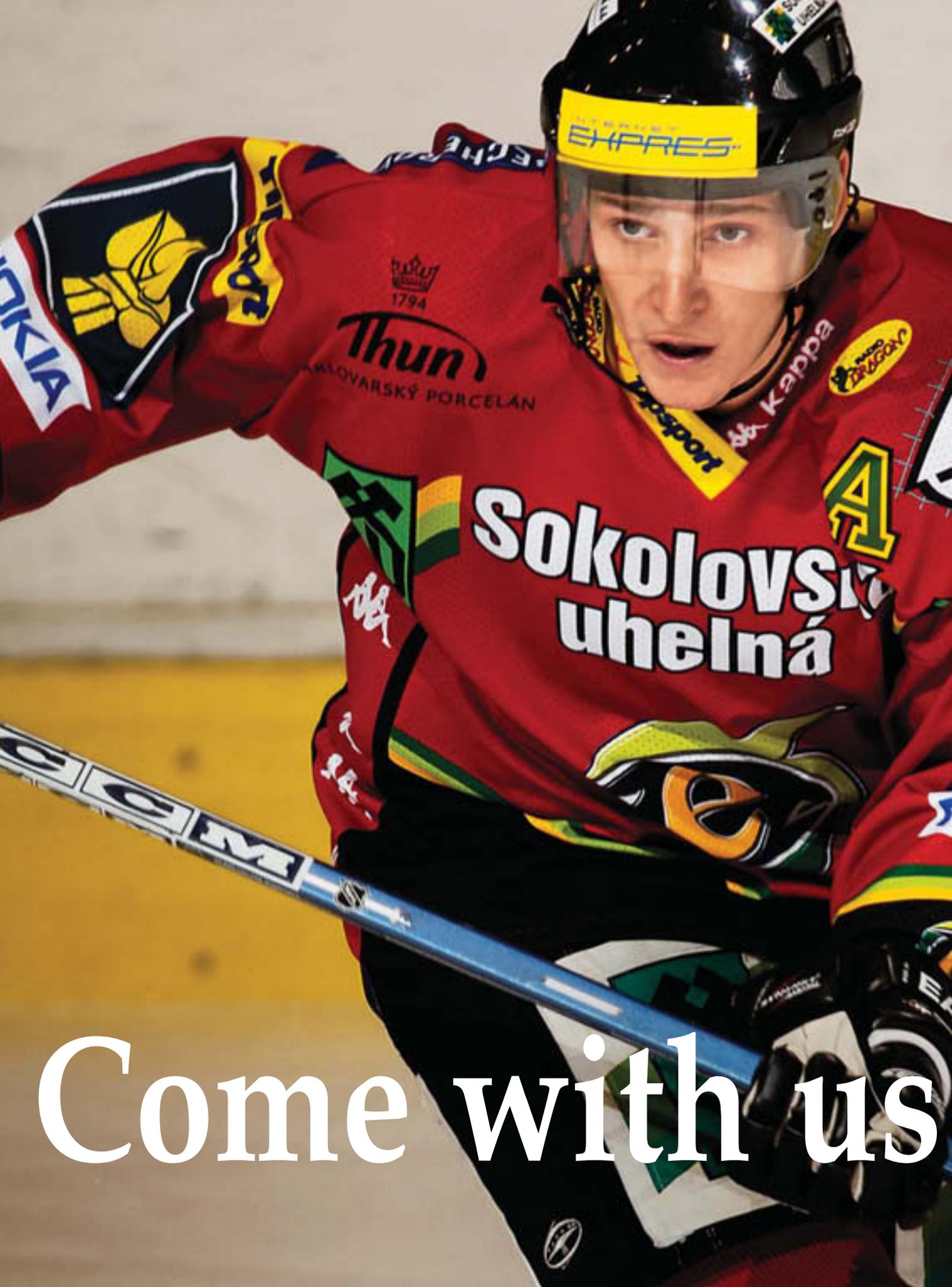
2004. The shortfall was caused primarily by stockpiling of this commodity to serve as fuel for the planned operation of the new burner generator.

Phenol concentrate – total 2005 production was 14,000 tons. All of this amount was shipped to customers, and the largest quantity – 9,080 tons – was exported to Germany. The rest was divided equally between Spain and the domestic market.

Liquid ammonia was sold, mainly to domestic customers, in a total volume of 7,000 tons. Like phenol concentrate, the amount produced relates directly to the higher coal gas generation volume.

Sulfuric acid – 18,000 tons shipped. Production of this commodity is not directly dependent on coal gas generation, but rather on the sulfur content in the coal gasified in the generator station.





Come with us



The first hockey matches in Karlovy Vary were placed on a small pond in front of the "Malé Versailles" restaurant.

In 1948, a skating rink with artificial ice was built in the city center.

Today, Karlovy Vary boasts an Extraleague hockey team.

for **hockey**

Earnings Analysis

Sokolovská uhelná

IN 2005, THE COMPANY POSTED after-tax earnings of CZK 533 million. This earnings result was achieved on revenues of CZK 15.4 billion and expenses of CZK 14.9 billion.

REVENUES

Sales of the Company's own goods and services totaled CZK 7.4 billion and account for 48% of overall revenues. The two most significant sources of these sales revenues were: sales of energy (CZK 3.4 billion) and sales of solid fuels (CZK 2.8 billion); thus, the Company again succeeded in converting a major portion of its coal into value-added energy products at or near the extraction sites.

The largest components in energy sales revenues were sales of electricity and ancillary power system services (CZK 3.1 billion) and heat sales revenues (CZK 0.3 billion). Of the Company's two plants, the combined cycle power plant accounted for the largest share of these revenues (68.4%), while the remaining 31.6% corresponds to the heat/power plant.

Coal sales revenues, at CZK 2.4 billion, comprised the bulk of solid fuel revenues. Briquette

sales contributed CZK 0.4 billion to the overall figure.

Sokolovská uhelná also generated revenues from sales of chemicals and other products (agricultural products, process gases, etc.).

Another revenue component is services, which consist in particular of sales of pre-invoiced solid fuels transport fees, cafeteria services, and rents.

In 2005, the Company continued to sell off superfluous real property, machinery, and equipment. Also, an amount of CZK 2.9 billion was charged to other operating revenues to account for emission permits used.

Financing revenues consisted of proceeds from sales of securities, returns on short-term financial assets, and interest revenues, all of which were generated by the Company's treasury function.

COSTS

Costs of materials, energy and outside services, personnel costs, and depreciation and amortization account for a major portion of overall costs.

Consumption of **fuels, energy, and natural gas** reached nearly CZK 0.6 billion. The increase from last year was due in part to purchasing of process gases from the oxygen plant run by Linde Sokolovská s.r.o. (until June 2005 gases were produced in the Company's own oxygen plant) and, further, to year-on-year increases in prices of fuels and natural gas by 13% and 21.2%, respectively.

Consumption of materials and repair costs totaled CZK 1.1 billion in 2005. Major repairs conducted in the period included a spreader and locomotives in the Extraction Section and steam ducts and a gas turbine in the Processing Section. Also, gale-force winds in late July 2005 necessitated extensive roof repair work.



The amount spent by Sokolovská uhelná for **shipping and other services** in 2005 was CZK 1.5 billion. The most significant components of other services, as in previous years, were costs of operating cafeterias, buildings and grounds security, and outsourced clean-up and reclamation work.

Personnel costs totaled CZK 1.8 billion last year, and wages accounted for CZK 1.3 billion of the total. The average monthly wage grew to CZK 21,125.

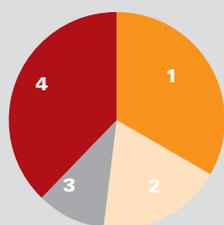
Other operating costs in the year in question totaled CZK 3.1 billion. Here, the most significant item, at CZK 2.9 billion, was consumption of emission permits. The second most significant item was property and casualty insurance premiums.

Depreciation and amortization totaled CZK 1 billion.

Net provisioning in 2005 totaled CZK 0.3 billion (i.e., creation of provisions exceeded their release by that amount). As usual, the most significant items are the creation and release of statutory provisions for repairs, clean-up, and reclamation, as well as creation and reversal of provisions relating to impaired assets.

Financing and tax costs consisted in particular of the value of securities sold, interest on borrowings, foreign currency losses, and income tax (due and deferred).

Structure of 2005 Operating Costs (%)



1	costs of materials, energy and services	33.39
2	personnel costs	18.56
3	depreciation	10.48
4	other	37.57



Sales of the Company's own goods and services totaled CZK 7.4 billion and account for 48% of overall revenues. The two most significant sources of these sales revenues were: sales of energy (CZK 3.4 billion) and sales of solid fuels (CZK 2.8 billion); thus, the Company again succeeded in converting a major portion of its coal into value-added energy products at or near the extraction sites.



Structure of Assets and Sources of Financing

PROFIT BROUGHT FORWARD TOTALED CZK 5.1 billion. Earnings for the accounting period reached CZK 0.5 billion.



Sokolovská uhelná assets as of 31 December 2005 (net, CZK billions):

Fixed assets	10.3
Current assets	4.1
Prepayments and accruals	0.1
Total	14.5

The largest component of fixed assets was **tangible fixed assets**, whose total net book value was CZK 9.8 billion. Here the most significant items

are plant and equipment (CZK 4.7 billion), and real property (CZK 4.4 billion).

Current assets consist of inventories, long- and short-term receivables, and short-term financial assets.

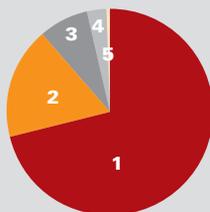
Inventories, which consist in particular of materials and spare parts necessary to keep extraction and production plant and equip-

ment in good working order, totaled CZK 0.4 billion at year end 2005.

At 31 December 2005, **receivables** stood at CZK 1.1 billion.

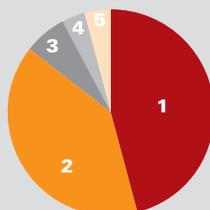
Short-term financial assets totaled CZK 2.5 billion. During 2005 they were used to finance the Company's operating and capital spending needs and meet the Company's financial obligations.

Structure of Assets as of 31 December 2005 (%)



1	fixed assets	71.21
2	financial assets	17.61
3	receivables	7.71
4	inventories	2.96
5	prepayments and accruals	0.51

Structure of Fixed Assets as of 31 December 2005 (%)



1	movables	46.07
2	buildings and structures	39.59
3	other assets	6.67
4	land	3.67
5	long-term financial assets	4.00



Come enjoy yourself at the

Michal Water Park!

*A former mine that just ten years ago
was in operation has been reclaimed
and turned into a modern water park.*



Sokolovská uhelná liabilities and equity as of 31 December 2005 (CZK billions):

Equity	5.7
Liabilities	8.8
Total	14.5

As of 31 December 2005, the **share capital** was CZK 2 million and the **statutory reserve fund** had a balance of CZK 0.4 million.

The **social fund** balance was CZK 5 million. This fund was used by the employees, among other purposes, to pay for cafeteria meals, recreation, purchase of health aids not covered by health insurance, children's recreation, and cultural and social events. **Profit brought forward** totaled CZK 5.1 billion. **Earnings for the accounting period** reached CZK 0.5 billion.

As of 31 December 2005, the Company had **provisions** totaling CZK 3.2 billion. A significant portion of these are statutory provi-



sions for cleaning up and reclaiming land affected by mining activity, and provisions for repairs of assets.

The Company's **payables** are divided into long-term and short-term payables. Long-term payables consist of the CZK 0.8 billion deferred tax liability. Short-term payables were comprised mainly by trade payables (CZK 0.8 billion). None of the trade payables were overdue. Another major item consists of

December wages payable to employees and related social security payables, and employees' deposits in the Company savings bank.

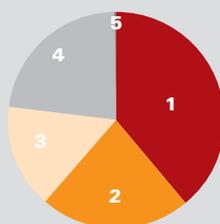
Bank loans at 31 December 2005 had an aggregate balance of CZK 3.3 billion.

Late in the year, as planned, the Company restructured its largest bank loan.

Sokolovská uhelná's obligations to the State, banks, employees, and business partners were met on time and in full during 2005.

The financial performance was not affected by any material, unexpected movements in Czech Crown exchange rates against principal currencies. Movements in Czech Crown interest rates, too, were relatively minor.

Structure of Liabilities and Equity as of 31 December 2005 (%)



1	equity	39.10
2	provisions	22.42
3	payables	15.70
4	bank loans	22.66
5	accruals and deferred income	0.12

Capital Investment in 2005

A NUMBER OF CAPITAL PROJECTS were undertaken in 2005 to develop both the Processing and Extraction Sections. Capital expenditures exceeded CZK 0.5 billion for the year.



Another significant project completed in the Processing Section was the connection to the new oxygen plant which interconnected the new plant's media inputs and outputs and other infrastructure with the Company's existing piping and infrastructure, including the installation of new oxygen piping in the Processing Section. The new oxygen plant is owned by Linde Sokolovská s.r.o.

In addition to capital projects in the Processing and Extraction

Sections, 2005 saw the completion of construction and interior decoration and furnishing of a group of buildings at the Michal Water Park site. This lake-side complex was built in previous years as part of the reclamation of the decommissioned Michal mine. The main purpose of the current project was to enable the facility to be used for sports and recreation. In the near future, a year-round water park will be added to the complex.

The most significant project in the Processing Section is the new burner generator which will be used to break down liquid by-products from the current coal gasification process based on sliding-bed generators. Construction work on the project was completed and extensive functional testing commenced in late 2005. The tests are to be completed in 2006.



"THE INTRODUCTION of effective and environmentally friendly technologies continues to be the Company's principal strategy for the future. We will focus on further reducing the environmental burden on the region and improving the environment by reclaiming spoilbanks and other areas affected by mining activity." Jiří Pöpperl, Technology Director

Potential is in people

IN 2005, SOKOLOVSKÁ UHELNÁ conducted its human resources management activities to maintain a constant ratio of personnel costs to sales revenues, increase the quality of personnel in all positions at the Company, and maintain proper relations between the Company and its employees.



The Company's average monthly wage in 2005 reached CZK 21,125. Compared to 2004 this is an increase of 5.6%.



The growth in the average wage was fully covered by growth in labor productivity from sales of the Company's own goods and services.



The Company continued to implement a gradual reduction in work force levels. The average adjusted number of employees for the year was 4,888 (down by 306). The Company's long-standing and sole method for reducing the work force is natural attrition, i.e. retirement and unplanned employee resignations. Employees for whom the Company no longer has work are offered the option of transferring to a different vacant position for which they are qualified, and these employees are given the opportunity to gain additional training and education to increase their qualifications.

Because the number of unplanned resignations and retirements is higher than the planned work force reduction, the Company had the opportunity to hire

new employees. In 2005, there were 134 new hires. The Company selects new employees from its own database of past applicants, from Labor Office records, and from graduates of schools such as the Integrated Technical and Economic Secondary School in Sokolov.

All changes to the Sokolovská uhelná work force are made to improve the employee qualification structure and limit growth in the average employee age, which at year end 2005 had fallen slightly to 45.72 years.



"OUR WORK TEAM

is our greatest asset, guaranteeing that we will pass the tests the future has in store for us. Sokolovská uhelná is one of the fundamental elements stabilizing the development of the region as a whole."

Jiří Radosta, Personnel Director



The Company provides Supplemental Pension Insurance contributions to 89% percent of its employees.



EMPLOYEE EARNINGS

at Sokolovská uhelná are one of the top drivers of wage growth in the Karlovy Vary region. That said, however, the region is at the bottom of the income ladder among regions of the Czech Republic.

The Company enjoys labor peace that ensues not only from the long-term human resources strategy but also from high-quality collective agreements that are negotiated and signed on a timely basis. As is customary for the Company, the Collective Agreement for the next five-year period was signed in late 2005. The agreement defines the framework of employee benefits. Each year, a collective bargaining process takes place to negotiate their specific amounts.

The Company's average employee monthly wage in 2005 was CZK 21,125, which is 5.62% higher than in 2004. The growth in the average wage was fully covered by growth in labor productivity from sales of the Company's own goods and services. By this, all wage provisions of the Collec-

tive Agreement were fulfilled. In addition, an extraordinary bonus was paid to express Company management's appreciation for the excellent 2005 performance. In terms of employee earnings, Sokolovská uhelná is a leading driver of wage growth in the Karlovy Vary region. That said, however, our region is at the bottom of the income ladder among regions of the Czech Republic.

Another benefit of being a Company employee is the opportunity to draw from the social fund the Company creates from its earnings. Most of this fund is distributed to employees through their personal accounts. Employees choose for themselves how to use these funds by selecting from a variety of offerings such as employee meal plan, recreational sojourns including chil-

dren's recreation, employee insurance, cultural and sports activities, and health expenses not covered by national health insurance. This type of social plan is not the norm and exceeds the standard within the region. CZK 25 million, or over CZK 5,100 per employee, was allocated to the fund in 2005.

In addition to wages and social fund distributions, the Company helps employees to secure their retirement by providing them a supplemental pension insurance contribution. In 2005, the monthly contribution was CZK 300 and all employees that had completed their three-month trial period were eligible to receive it, provided they had a signed agreement with a pension fund. At year end 2005, 4,250 employees, or 89% of the work force, were receiving the contribution.



Come and play

The newly completed golf course on Sokolovská uhelná land is located at the site of the former Silvestr surface mine near Dolní Rychnov. What used to be a monotonous “moonscape” is now a golf course whose parameters, design, and quality make it one of the top master courses in the Czech Republic.

A close-up photograph of a golfer's lower legs and feet on a green. The golfer is wearing white trousers and white loafers with pinkish-red stripes. A silver putter is positioned on the grass to the left, with a white golf ball resting on the green just in front of its head. The background is a blurred green lawn.

golf

Environmental Responsibility



2005 saw the commencement and/or completion of a number of construction projects designed to mitigate or eliminate the environmental impacts of mining and fuel production operations.



Phase Two of Stepping Up Multipowder Production aims to reduce the amount of multipowder that is flushed into the sewer designated for coal-bearing water, thereby reducing the load placed on the specialized facility for treating coal-bearing

water. At the same time, measures are being taken at the ash matter dump facility to separate out fine coal-bearing sludges. After gravity removes water from these sludges, they will be recovered and further utilized as fuel. Thanks to the Redepositing of

Energy Generation By-products project, products that used to be permanently disposed at the ash matter dump will be converted through a certified industrial process into forms capable of further utilization. The third quarter of 2006 will see the completion of the Malodorous Gases Liquidation project, the aim of which is to substantially lower and minimize the negative environmental impact of waste gases arising in the gas production and purification processes.

Intensive mining of brown coal is one of the significant factors negatively influencing the environment of the Sokolov area. For this reason, a Master Plan for Reclamation of Land Affected by Coal Mining in the Sokolov District was drafted on the basis of Resolution of the Government of the Czech Republic No. 490/91 on the Sokolov District Environmental Revitalization Program. The Master Plan focuses on restoration of lakes and water management conditions in the area following coal extraction with the objective of attaining maximum diversity and aesthetic value in the reclaimed landscape.

This also forms the basis of Sokolovská uhelná's reclamation work from the beginning of mining operations until the end of 2005:

completed	2,888.98 hectares (31.20%)
in progress	1,868.26 hectares (20.18%)
planned	4,502.24 hectares (48.62%)

As the summary indicates, the Company has a total of 9,259.48 hectares of land for reclamation. Since the establishment of Sokolovská uhelná in 1994, 934.66 hectares of land have been com-



SINCE RECLAMATION WORK in the Sokolov region began in the 1950s, 2,889 hectares of land have been completely reclaimed. Over one half of this area is forest land. Over one thousand hectares have been returned to the landscape in the form of fully utilizable farmland. The remainder consists of man-made lakes.



pletely reclaimed. This can be broken down into cropland (445.79 hectares), forests (416.72 hectares), and man-made lakes (72.15 hectares).

Since reclamation work began in the Sokolov area in the 1950s, a total of 2,888.98 hectares has been reclaimed: 1,081.21 hectares as cropland, 1,700.76 hectares as forests, 77.75 hectares as man-made lakes, and 29.26 hectares for other purposes.

Ongoing Reclamation Work

At the Lítov – Boden site, located between the towns of Habartov, Chlum Sv. Máří, and Lítov, 2004 saw the completion of trial operation of the 16.97-hectare man-made lake which is designated for recreation. Forestry work continues on the Lítov – North (Phase One) and Boden – West forest reclamation projects.

At the Medard – Libík site, between the towns of Citice, Bukovany, Habartov, Svatava, and the City of Sokolov, forest reclamation work is ongoing.

The former Michal surface mine located southeast of the City of Sokolov was backfilled in 1995, in accordance with the liquidation plan, and subsequently prepared for clean-up and reclamation. Forestry reclamation work began in 1997 in the eastern portion of



THE NEWLY-BUILT golf course at the site of a former surface mine is part of a 200-hectare sports and recreation facility near the recently completed Michal reservoir. In addition to the golf course, the site will also house a zoo and a forest park.

the slopes. Currently, a 32.1 hectare man-made lake is in operation in the summer season, with an adjoining recreation complex that opened its doors in 2004. The latest project at this site is a 33.92 hectare forestry reclamation.

At the Silvestr site, located south of the City of Sokolov, as part of Phase II.B of the Silvestr reclamation project, most of the technical work was completed, topsoil was brought in for cropland, and tree-

planting work was done for the forest portion. Two man-made lakes, feeder canals, and roads around the lakes still remain to be completed.

At the Podkrušnohorská Spoilbank site located north of the City of Sokolov, 2003 saw the last overburden material deposited on the spoilbank via Division Jiří's technology complexes and Division Družba's 1,435 mm gauge rail spur. In 2005, project documenta-

tion was prepared for Phase XI and XII of the site's reclamation.

At the Smolnická Spoilbank, the area between the City of Chodov and the town of Božičany has been reclaimed, including the area around the Bílá Voda lake, which is used for recreation.

At the Velký Locket Spoilbank, which is located in the eastern portion of the Sokolov Basin, reclamation work was completed in 2005.



Sokolovská uhelná

– a stabilizing element in the Sokolov region

THE COMPANY'S FINANCIAL PERFORMANCE and good reputation confirmed the importance of Sokolovská uhelná for the region as a whole and were reflected in its social climate. The recognition of the Company's position is all the more valuable because it was achieved in a context of dynamic change both inside and outside the Company. Strict compliance with all obligations toward State and local government agencies is a matter of course and a factor stabilizing the budgets of the region's cities and towns – especially those in the Sokolov area.



The public's perception of Sokolovská uhelná has undergone a fundamental change as revitalization projects have been completed and others have entered the preparatory stages. These demonstrate how seriously the Company takes the renewal and revitalization of the landscape upon completion of brown coal mining operations. A new golf course on the reclaimed Silvestr spoilbank in Dolní Rychnov, prepared for full operation starting in the summer

of 2006, and the Michal Water Park in the location of a decommissioned mine of the same name, have convinced the general public that even a large-scale project, currently in preparation to deal with the pit left by the decommissioned Medard and Libík mines, will not remain a mere urban development study but that it will be completed in the next few years, contributing to the revitalization and development of this site.

Corporate Social Responsibility

Another integral part of the Company's philosophy is support for cultural and sports activities, especially those focusing on children and youth, within the wider Karlovy Vary region.

In 2005, the Company continued to serve as a patron of physical education groups with large member bases, specializing primarily in ice hockey and football. In addition to these, the Company also financially supported a number of small sports clubs in football, basketball, table tennis, indoor football, volleyball, chess, swimming, hiking, wrestling, boxing, and kick-boxing. The Company's financial contributions also made it possible to successfully organize prestigious events

such as the Motocross World Championship in Loket, the Czech Republic Biketrial Championship in Březová, the International Golden Czech Trophy Run in Mariánské Lázně, and the Sokolov Dance Cup.

Further recipients of the Company's financial support included a number of non-profit organizations, local clubs, and regional organizations and institutions. The donations went toward holding many cultural events, as well as restoration of heritage sites.

Also significant is the Company's unique relationship with the Sokolov Regional Museum, which has resulted in the preservation of 900 mm gauge rail cars and an exhibit of the same at the Mining Museum in Krásna. In addition, the exhibit features a number of other objects from Sokolovská uhelná that were used in mining operations in the Sokolov area over a period of approximately one century.

September 2005 marked the ten-year anniversary of the complete renovation of the Old Town Hall, an important architectural heritage site, that today serves as the Company's seat. The renovation was the largest construction project in the old part of Sokolov and, thanks to it, a unique historical building has been preserved for future generations.



COMPANY

Business Plan

IN THE YEARS TO COME, the Company will continue to reinforce its position as the largest independent electricity producer in the Czech Republic. In so doing, emphasis will be placed on providing ancillary services in the electricity market. Currently, these have already become an integral part of electricity revenues.

As in the past, the attention of Sokolovská uhelná management will be focused on achieving the most effective possible utilization of plant and equipment built and acquired in previous years. 2006 will see the commissioning of the new burner generator, which will enable the utilization of liquid by-products in the Processing Section. This will conclude the process of large-scale process innovations for the near future. The Company's operations will continue to focus on mining coal and converting it into value-added forms of energy – electricity and heat in particular. On the other hand, it must be mentioned that both Sokolovská uhelná mines, and Jiří in particular, are moving into areas where „long-wall“ underground mines operated in the past. It is becoming more and more complicated and cost-intensive to obtain high-quality coal from these areas, and this will continue to be the case.

Sokolovská uhelná will continue to invest in protecting the environment. Closely linked to this is

the area of cleaning up and reclaiming land affected by mining activity. Thus, our attention will be focused both on further reducing the region's environmental burden by continuing to maintain low levels of the pollutants we release into the surface water and the air, as well as on reclaiming spoilbanks and other areas affected by the Company's operations and implementing subsequent revitalization programs.

Company management is aware of the indispensable role that Sokolovská uhelná plays in the region. Therefore, all future steps in the Company's development will be taken with the awareness that the Company is the largest and strongest participant in the Karlovy Vary regional economy. In the near future, then, we will remain one of the basic elements stabilizing the development of the entire region.



“WE ESTIMATE that our coal reserves will last roughly 30 years more. Currently the Jiří mining operation has reached areas where underground mines operated in the past. This has increased the demands placed on our miners in terms of selective extraction.”

Jaroslav Rokos,
Finance Director

Balance Sheet (TCZK)

Short form

	31 December 2005		1 January 2005	
	Gross	Provision	Net	Net
ASSETS				
B. Fixed assets	24,528,084	(14,233,578)	10,294,506	10,603,418
B. I. Intangible fixed assets	264,237	(173,449)	90,788	19,041
B. II. Tangible fixed assets	23,851,890	(14,060,129)	9,791,761	10,247,446
B. III. Long-term financial investments	411,957	0	411,957	336,931
C. Current assets	4,277,695	(189,162)	4,088,533	4,832,446
C. I. Inventories	472,549	(44,739)	427,810	266,960
C. II. Long-term receivables	28,146	0	28,146	59,206
C. III. Short-term receivables	1,230,486	(144,423)	1,086,063	780,488
C. IV. Short-term financial assets	2,546,514	0	2,546,514	3,725,792
D. Accruals and deferrals	74,204	0	74,204	62,348
D. I. Prepayments and accruals	74,204	0	74,204	62,348
TOTAL ASSETS	28,879,983	(14,422,740)	14,457,243	15,498,212

	31 December 2005	1 January 2005
LIABILITIES AND EQUITY		
A. Equity	5,653,304	5,135,698
A. I. Share capital	2,000	2,000
A. II. Capital contributions	54,121	44,994
A. III. Reserve funds	5,794	5,618
A. IV. Retained earning	5,058,086	5,083,086
A. V. Net profit for the current period	533,303	0
B. Liabilities	8,787,178	10,362,405
B. I. Provisions	3,241,788	3,072,933
B. II. Long-term liabilities	782,408	658,054
B. III. Short-term liabilities	1,486,982	1,355,488
B. IV. Bank loans and overdrafts	3,276,000	5,275,930
C. I. Accruals and deferrals	16,761	109
TOTAL LIABILITIES AND EQUITY	14,457,243	15,498,212

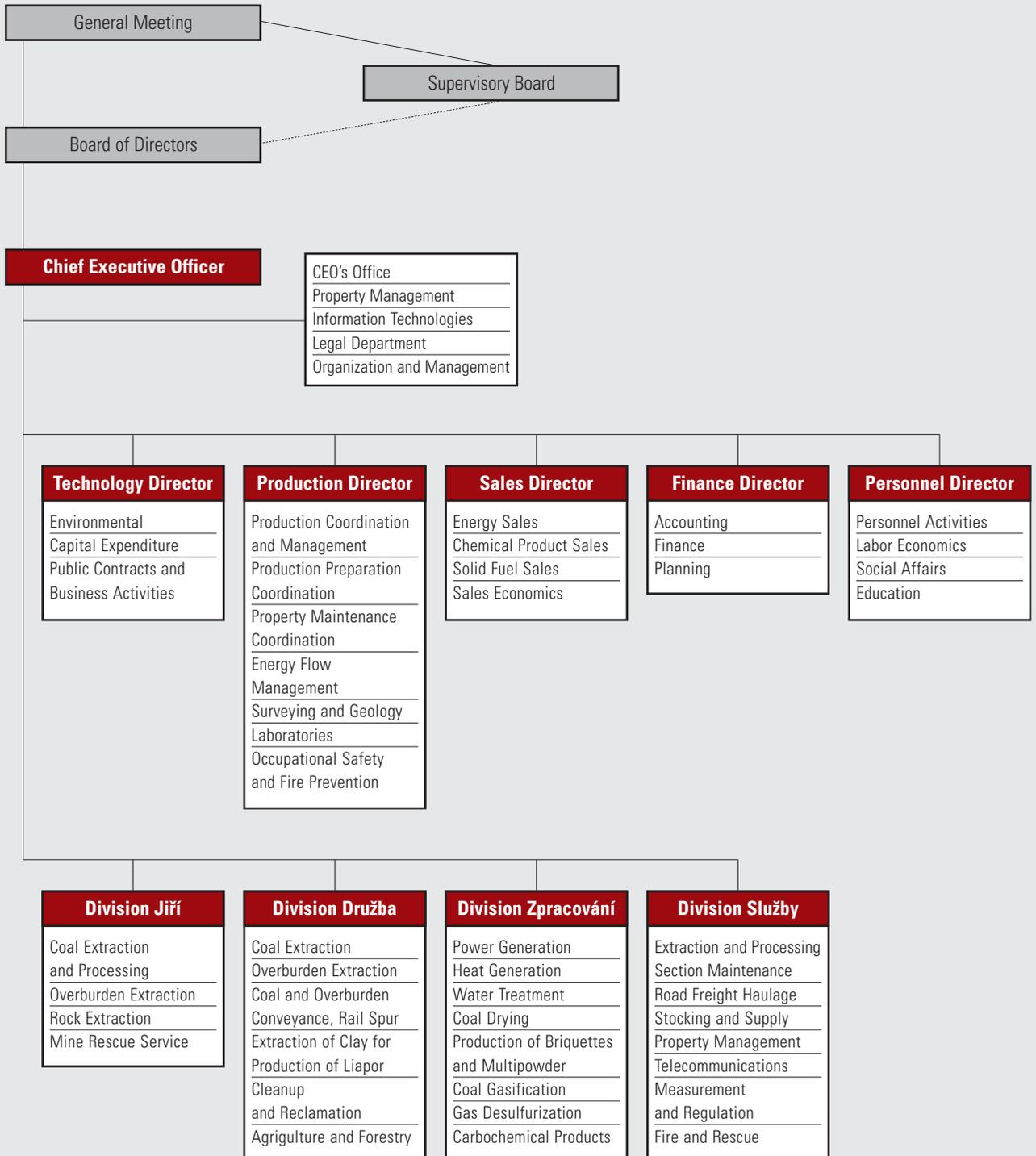
Profit and Loss Account (TCZK)

Short form

Year ended 31 December 2005

I.	Sales of goods	15
A.	Cost of goods sold	3
+	Gross profit/loss on goods for resale	12
II.	Sale of production	7,541,943
B.	Cost of sales	3,187,092
+	Value added	4,354,863
C.	Personnel costs	1,771,322
D.	Taxes and changes	143,677
E.	Depreciation of fixed assets	1,000,309
III.	Revenues from sale of fixed assets and materials	73,333
F.	Net book value of fixed assets and raw materials sold	25,487
G.	Increase (+) in operating provisions and impairment allowances	331,158
IV.	Other operating income	2,907,221
H.	Other operating charges	3,085,006
*	Operating profit	978,458
VI.	Income from sale of securities and interests	4,687,790
J.	Cost of securities and interests sold	4,714,237
VII.	Income from long-term financial investments	25,622
VIII.	Income from short-term financial assets	105,927
L.	Cost on revaluation of investments and derivatives	5,802
X.	Interest income	30,037
N.	Interest expense	29,207
XI.	Other financial income	933
O.	Other financial expenses	91,502
*	Loss from financing activities	(258,439)
Q.	Corporation tax on ordinary activities	186,716
**	Net profit on ordinary activities	533,303
***	Profit for the financial period	533,303
	Profit before tax	720,019

Sokolovská uhelná Organization Chart as of 1 January 2006



Contact Information

Company name:	Sokolovská uhelná, právní nástupce, a.s.
Seat:	Sokolov, Staré náměstí 69, postcode 356 00
ID:	26348349
Tax ID:	CZ26348349
Commercial Register:	Plzeň Regional Court, Part B, Entry 980
Bankers:	ČSOB Praha, account no.: 17331033/0300
E-mail:	info@suas.cz
Internet:	http://www.suas.cz

Telephone and Fax Numbers:	Telephone:	Fax:
Switchboard	+420 352 461 111	
Office of the Chief Executive Officer	352 462 103	352 621 052
Office of the Technology Director	352 462 113	352 621 038
Office of the Production Director	352 462 123	352 621 038
Office of the Finance Director	352 462 133	352 462 132
Office of the Personnel Director	352 462 153	352 462 132
Office of the Sales Director	352 462 143	352 621 032
Office of the Director of Division Jiří	352 463 001	352 675 139
Office of the Director of Division Družba	352 463 501	352 669 457
Office of the Director of Division Zpracování	352 465 001	352 465 002
Office of the Director of Division Služby	352 465 801	352 465 802

Sales Contacts:	Telephone:	Fax:
Brown coal, briquettes, multipowder	352 462 142	352 621 032
	352 462 272	352 624 541
	352 462 273	
	352 622 596	
	352 623 340	
Electricity, heat	352 465 210	352 465 212
Carbochemical products and sulfuric acid	352 464 480	352 464 481
	352 464 482	
	352 464 492	
	352 464 493	
Rock/gravel	352 465 910	352 465 910
Secondary materials (expansion clays, adsorption and zeolitic claystones, etc.)	352 462 232	352 462 231
Laboratory work	352 465 650	352 465 670
Stocking and supply	352 465 340	352 465 350
Capital expenditure	352 465 622	352 465 620
Road freight haulage	352 463 207	352 463 211

This report is not a full annual report in accordance with the Act on Accounting, the Commercial Code, the Securities Act and the Act on Business in the Capital Market. A full annual report is available at the company seat, and in the Collection of Documents of the Commercial Register.

