



SUSTAINABILITY  
AND ANNUAL  
REPORT 2015



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# Dear readers!

G4-1

2015 was a year full of challenges, new trends and developments. The most important events of the period include the opening of the electricity market for households, further integration of the Baltics into the Nordic electricity market, the overhaul of the Daugava hydropower plants, and the successful issue of Latvenergo AS *green* bonds.

In the complex electricity market situation, Latvenergo Group has proven to be a skilled and experienced operator, capable of responding to various situations and making use of them to strengthen its leading position in the Baltics. We have experience in electricity supply under free market conditions since 2007. Due to this, we have been able to dedicate both time and resources for investment in the transformation of customer service standards according to the market conditions and competition, through developing new offers, improving the existing ones and creating new customer service and electronic billing platforms. All of the above has been brought together under the relatively new name *Elektrum* – electricity supply brand introduced by Latvenergo Group, now comprising electricity supply offers also for households in Latvia.

In 2015, lower wholesale electricity prices were observed throughout the Baltics compared to the previous year. Alongside the global developments, this process has been encouraged by further integration of the Baltics into the Nordic electricity market in recent years. The construction of *NordBalt* interconnection between Lithuania and Sweden, as well as the Lithuania–Poland *LitPolLink* interconnection were completed at the end of the year, promoting an even deeper integration of the Baltics. Both interconnections start operating at full capacity in 2016, this is one of the most significant events after the reporting period ended.



By identifying the market and consumer interests, and drawing on the experience to date, Latvenergo Group has ensured a high level of customer loyalty, enabling it to maintain the leadership in electricity supply not only in Latvia, but also across the Baltics. Latvenergo Group holds approximately a third of the Baltic market. In 2015, Latvenergo Group supplied to its customers 7,869 GWh of electricity, including a third of those – 2,539 GWh in Lithuania and Estonia. In 2015, Latvenergo Group generated 3,882 GWh of electricity and 2,408 GWh of thermal energy.

We are proud that Latvia is among those European Union countries, where a considerable share of energy is generated from renewable sources. The role of our Daugava HPPs can hardly be overestimated. In 2015, electricity generated by Daugava HPPs accounted for 47% of the total volume generated by the Group, and we aspire to increase this proportion. Therefore,



Latvenergo Group is gradually and systematically implementing Daugava HPP reconstruction project, scheduled for completion in 2022. The reconstructed turbines can be operated for at least another 40 years and their efficiency is higher.

Year 2015 has marked the history of Latvia as one of the driest years in terms of the Daugava River measures: even the most experienced hydropower plant employees cannot recall such a low water inflow. The Daugava River lacked the accustomed abundance of water, hence Latvenergo Group attributes its success in the diversified generation portfolio via the role of Riga CHPPs. In 2015, Riga CHPPs generated by 23% more electricity than in 2014. The modernised Riga CHPPs operated effectively and flexibly, adjusting their generation modes to the electricity market situation. It should be noted that the efficient operation of Riga CHPPs limited the risk of electricity price increase in the Latvian and Lithuanian bidding areas. Our reconstructed CHPPs are a benefit not only to users, but also to Latvian energy independence as a whole.

Continuing the successful operations in the debt securities market, Latvenergo AS issued *green* bonds in the amount of EUR 75 million in 2015. The funds raised from the bond issue are invested only in projects compatible with *green* thinking, promoting the use of renewable energy sources, energy efficiency and environmental protection. We are proud to be the first state-owned company in Eastern Europe to enter the capital market with *green* debt securities, and the *Green* Bond Framework of Latvenergo AS has been assigned a Dark Green shading, which is the highest possible assessment. Welcoming Latvenergo AS with the first *green* bond listing on the Baltic Bond List, the Nasdaq Stock Exchange placed Latvenergo logo and a greeting on its billboard in Times Square, New York.

It should be mentioned that the previous bond issues have also been very successful: the Group's loan portfolio has been diversified, and the high investor interest evidences the reliability and stability of Latvenergo Group. This was also attested in early 2015 by the upgrade of the Group's credit rating to Baa2 with a stable outlook by the international credit rating agency Moody's Investors Service.

In 2015, Latvenergo Group continued the previously successful cooperation with stakeholders. This is a model of good practice for quality stakeholder engagement, both at a strategic and operational level.

Since 2009 Latvenergo Group's Sustainability Report is prepared in accordance with the Global Reporting Initiative (GRI) guidelines. This year, we have taken a step forward: the Sustainability Report 2015 is prepared in accordance with the core requirements of the latest GRI G4 guidelines. With the enhanced stakeholder engagement in defining the report content, the amount of information to be included has been enriched and enhanced.

With regard to the corporate social responsibility, last year we proactively boosted interest in hard sciences, and continued to support education. The *Experiment* erudition contest for schoolchildren marked its 20<sup>th</sup> anniversary, while the *fizmix* portal, having no doubt of the fascinating nature of physics, continues the demonstration of experiments for schoolchildren – future students. Engineering High School of Riga Technical University, the first high school with a focus on hard sciences in Latvia under the auspices of a higher educational institution, opened in 2015. Moreover, a Latvenergo AS creative laboratory was opened at the Riga Technical University where every student can carry out their engineering ideas and gain applicable knowledge. It ought to be noted that last year, this project supported by Latvenergo AS received the Student Union of Latvia annual award in the nomination category "Contribution of the year to academic life". We have created traditions in this area, which we plan on continuing.

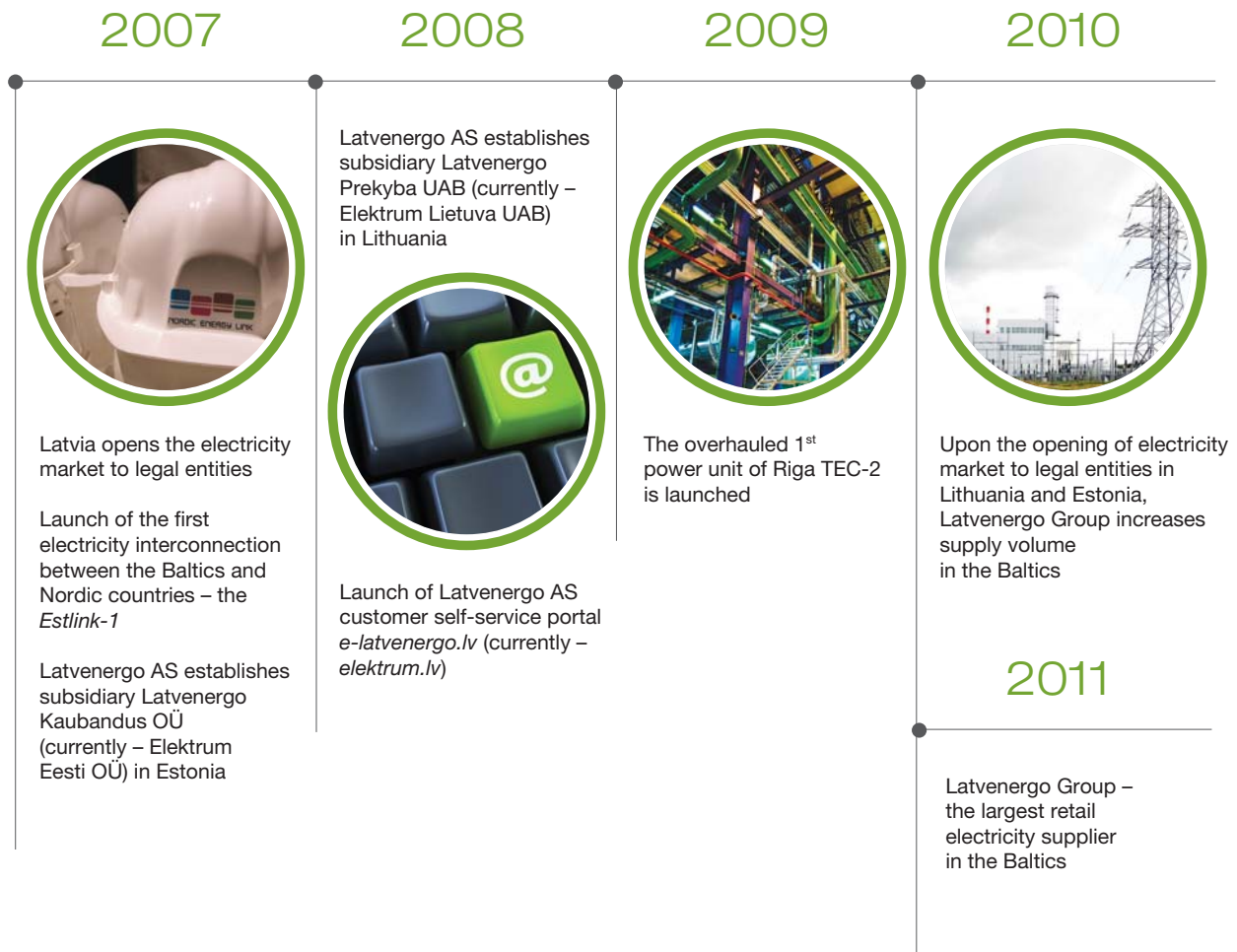
Year 2015 can be evaluated as a solid foundation for the challenges in 2016. Although we have reasons to be content and proud about the progress made in these challenging times, it must not be forgotten that the market and competitive environment do not forgive those players who feel that their past achievements entitle them to any concessions. Which is why we continue our work in offering new, competitive and attractive market products and through this, maintain a high level of competitiveness in the Baltic electricity market for the benefit of our customers.



Dr. sc. ing. Āris Žīgurs  
Chairman of the Management Board of Latvenergo AS

# Latvenergo Group Development

Latvenergo Group's development is concurrent with the opening of the electricity market in the Baltics and the integration in the Nordic market.



2012



Latvenergo Group introduces electricity trading brand – *Elektrum*

Latvenergo AS issues bonds, thus diversifying its sources of funding

2013

As of 1 January, complete liberalisation of the electricity market in Estonia, including households



The second power unit of Riga TEC-2 is commissioned, becoming a state-of-art and the most efficient combined heat and power plant in the Baltics

2014

Latvenergo Group trades all generated electricity on Nord Pool power exchange



*Grobīņa – Ventspīls* transmission line of the *Kurzeme Ring* 330 kV project was commissioned



Second interconnection between the Baltics and Nordic countries – the *Estlink-2* is completed, reducing electricity price difference between the regions

2015



As of 1 January, complete liberalisation of the electricity market in Latvia, including households

Latvenergo AS is the first state-owned company in Eastern Europe to issue *green bonds*

Construction of electricity interconnections connecting Lithuanian to Sweden and Poland are completed, thus further integrating the Baltic countries into the Nordic market





# Latvenergo Group Profile



Prepared in accordance with GRI G4 Guidelines, Core



# 1.1 Report Overview

|       |   |   |
|-------|---|---|
| G4-22 | <b>Reporting period</b>                   | <b>2015 (1 January – 31 December)</b>   |
| G4-23 | Reporting frequency                       | Annually, since 2009, in accordance with the Global Reporting Initiative (GRI) guidelines.  |
|       | Date of publishing                        | 20 April 2016   |
| G4-28 | Global Reporting Initiative               | Sustainability report 2015 is prepared in accordance with GRI Guidelines G4, Core (2012 – 2014 it was prepared in accordance with GRI Guidelines G3.1, level B+).   |
| G4-29 | Report Framework                          | The report discloses information about Latvenergo Group (see section 1.2 Group Profile).  |
| G4-30 | Principles for defining report content    | In 2015, in the process of defining the report content an in-depth stakeholder engagement was carried out. The company organized a stakeholder seminar, where stakeholders' opinion about the most material sustainability aspects of Latvenergo Group were identified. In addition, the employees of the Group were asked to state their opinion about the most material sustainability aspects via annual employees' survey. After combining the results of stakeholders' and Group's management surveys on the most material aspects of operations and sustainable development of Latvenergo Group, a materiality matrix was made (see page 45). It was further approved by the management of the Group.   |
| G4-31 |   | Accordingly the General Standard Disclosures about the operations of Latvenergo Group are fully covered in the report, as well as, on the basis of assessed materiality, 22 material sustainability aspects and 33 Specific Standard Disclosures indicators are disclosed (see GRI Index table on page 93) in accordance with the GRI G4 Core guidelines (see table GRI G4 application requirements). Specific Standard Disclosures indicators include 9 indicators specific to the energy industry (labelled EU), which have been disclosed in accordance with the Electric Utilities Sector Disclosures. Detailed description of the report preparation process is provided in Section 1.9 "Materiality Assessment".  |
|       | Data measurement methods                  | The information included in the report has been obtained from internal information systems, where data processing and quality are fully controlled by the Group. The reliability of this information is ensured by dedicated internal control systems. To achieve a comparative evaluation of the development of the Group across all of its operating segments, the data have been reflected across several consecutive years. The means of collecting data included in the report have been specified. Three data collection methods have been used: <ul style="list-style-type: none"> <li>• measurement – the data were measured precisely;</li> <li>• estimate – the data were estimated approximately on the basis of assumptions;</li> <li>• calculation – the data were obtained using calculations.</li> </ul> The methods for measuring data included in this report have not been significantly altered compared to earlier reports. |
|       | Independent Auditors' Confirmation Report | The auditor's report on the Sustainability Report 2015 has been provided by Ernst & Young Baltic SIA.   |
|       | Report format                             | PDF version available from:<br>Latvenergo Group website: <a href="http://www.latvenergo.lv">http://www.latvenergo.lv</a> (in Latvian and English);<br>GRI Sustainability Disclosure Database: <a href="http://database.globalreporting.org/">http://database.globalreporting.org/</a> (in English).   |
|       | Contact us                                | E-mail address for suggestions and questions regarding the Sustainability Report: <a href="mailto:sustainability@latvenergo.lv">sustainability@latvenergo.lv</a> .  |

GRI G4 application requirements

|   | Core   | Comprehensive  |
|---|--|--|
| <b>General Standard Disclosures</b>               | At least 34 defined indicators                                       | All 58 indicators  |
| <b>Specific Standard Disclosures</b>              |  |  |
| <b>Generic Disclosures on Management Approach</b> | For material Aspects only  | For material Aspects only  |
| <b>Indicators</b>                                 | At least one indicator related to each identified material Aspect    | All indicators related to each identified material Aspect            |
| <b>Specific Standard Disclosures for Sectors</b>  | Required, if available for the organization's sector and if material | Required, if available for the organization's sector and if material |





## 1.2 Group Profile

### Latvenergo Group is the leading power supply utility in the Baltics

Latvenergo Group is the largest power supply utility in the Baltics, which operates in electricity and thermal energy generation and supply, provision of electricity distribution service and lease of transmission system assets. Latvenergo Group comprises the parent company Latvenergo AS and seven subsidiaries. All

shares of Latvenergo AS are owned by the Republic of Latvia and held by the Ministry of Economics of the Republic of Latvia. Latvenergo AS is a shareholder in an associated company Pirmais Slēgtais Pensiju Fonds AS – 46.3% (Latvenergo Group – 48.15%), along with a financial investment in Rīgas siltums AS (0.005%).

More information on operating segments and customers of Latvenergo Group is disclosed in the Section 1.10 "Description of Operating Segments".

### Latvenergo AS shareholding in subsidiaries and associated companies

|                                   | Country of operation | Type of operation   | Participation share |
|-----------------------------------|----------------------|---|---------------------|
| Latvenergo AS                     | Latvia               | Generation and supply of electricity and thermal energy         |                     |
| Sadales tīkls AS                  | Latvia               | Electricity distribution  | 100%                |
| Latvijas elektriskie tīkli AS     | Latvia               | Lease of transmission system assets                             | 100%                |
| Enerģijas publiskais tirgotājs AS | Latvia               | Administration of electricity mandatory procurement process     | 100%                |
| Elektrum Eesti OÜ*                | Estonia              | Electricity supply  | 100%                |
| Elektrum Lietuva UAB              | Lithuania            | Electricity supply  | 100%                |
| Liepājas enerģija SIA             | Latvia               | Thermal energy and electricity generation and supply in Liepāja | 51%                 |
| Pirmais Slēgtais Pensiju Fonds AS | Latvia               | Pension plan management   | 46.3%**             |

\* Elektrum Eesti OÜ owns a subsidiary Elektrum Latvija SIA which is not engaged in any business activities.

\*\* Latvenergo Group shareholding – 48.15%.

### Latvenergo Group company contacts

|                                   | Registered office                                   | Website   |
|-----------------------------------|---|---|
| Latvenergo AS                     | Pulkveža Brieža iela 12, Rīga, Latvia, LV-1230      | <a href="http://www.latvenergo.lv/">http://www.latvenergo.lv/</a>             |
| Sadales tīkls AS                  | Šmerļa iela 1, Rīga, Latvia, LV-1160                | <a href="http://www.sadalestikls.lv/">http://www.sadalestikls.lv/</a>         |
| Latvijas elektriskie tīkli AS     | Dārziema iela 86, Rīga, Latvia, LV-1073             | <a href="http://www.let.lv/">http://www.let.lv/</a>                           |
| Enerģijas publiskais tirgotājs AS | Pulkveža Brieža iela 12, Rīga, Latvia, LV-1010      | <a href="http://www.eptirgotajs.lv/">http://www.eptirgotajs.lv/</a>           |
| Elektrum Eesti OÜ                 | Liivalaia 45, 10145 Tallinn, Estonia                | <a href="http://www.elektrum.ee/">http://www.elektrum.ee/</a>                 |
| Elektrum Lietuva UAB              | Gedimino Prospektas 18, Vilnius LT-01103, Lithuania | <a href="http://www.elektrum.lt/">http://www.elektrum.lt/</a>                 |
| Liepājas enerģija SIA             | Ludviķa iela 15, Liepāja, Latvia, LV-3401           | <a href="http://www.liepajasenergija.lv/">http://www.liepajasenergija.lv/</a> |



## 2015

| General Facts                              |           |               |
|--|-----------|---------------|
| 100% shares are state-owned                |           |               |
| Vertically integrated power supply utility |           |               |
| 4,177 employees                            |           |               |
| Financial Performance                      |           |               |
| Revenue                                    | MEUR      | 929.1         |
| Profit                                     | MEUR      | 85.0          |
| Assets                                     | MEUR      | 3,517.4       |
| Investments                                | MEUR      | 190.5         |
| Credit rating                              | Moody's   | Baa2 (stable) |
| Sales figures                              |           |               |
| Retail electricity supply                  | GWh       | 7,869         |
| Market share in the Baltics                | %         | 32            |
| Retail customers                           | thousands | 865           |
| Thermal energy supply                      | GWh       | 2,318         |

| Technical Parameters                                       |                  |        |
|--|------------------|--------|
| Generation   |                  |        |
| Installed electrical capacity                              | MW <sub>el</sub> | 2,569  |
| Installed thermal capacity                                 | MW <sub>th</sub> | 1,844  |
| Distribution   |                  |        |
| Line length  | km               | 94,120 |
| Transformer capacity                                       | MVA              | 5,881  |
| Transmission   |                  |        |
| Line length  | km               | 5,251  |
| Transformer capacity                                       | MVA              | 8,927  |
| Sustainability report in accordance with GRI G4 guidelines |                  |        |
| Externally assured GRI G4 report                           |                  |        |
| Financial reports in accordance with IFRS                  |                  |        |



## 1.3 Group Strategy

### Significant achievements towards the fulfilment of strategic goals

Latvenergo Group strategy for the period till 2016 was developed and approved in late 2012, taking into account the challenges anticipated at that time:

- complete opening of the electricity market in the Baltics;
- reduced electricity generation capacities in the region;
- need for significant improvements in the distribution infrastructure and quality of service;
- construction of electricity transmission interconnections and continued integration of the Baltics into the Nordic market.

In line with the most significant challenges in the external environment, the understanding of the development of the industry and national economy in subsequent years, and the strong position already achieved by Latvenergo Group, three strategic goals were defined:

- strengthening of the market position in the Baltics;
- diversification of electricity generation sources;
- balanced development of networks.

In 2015, a significant progress was achieved towards each of the goals.

#### **Strengthening of the market position in the Baltics**

Strengthening of the position of the Group in the Baltic market is aimed at making it a full-fledged and equally positioned electricity retail market player in all three Baltic States, retaining an economically justified market share and increasing the number of customers, and focusing on small and medium sized enterprises and households.

Reaching this goal is a particularly challenging task, because an increased price competition is observed among the market players, including those with a long-term experience, having both a large customer base and significant assets, as well as market players who have entered the Baltic market relatively recently.

Since 2014, electricity wholesale transactions are predominantly made on the Nord Pool power exchange. At the current integration stage of the Baltic States in the Nordic electricity market, with two interconnections between Finland and Estonia already in place, electricity prices in the Baltic region are approaching the Nordic

level. A challenge to electricity generation and wholesale operations in the Baltics expected in 2016 is the launch of interconnections between Sweden – Lithuania and Poland – Lithuania in late 2015.

For retail electricity supply 2015 was marked by a complete opening of the market in Latvia, ensuring also the market opening for households. Latvenergo Group handled the task successfully. The market opening took place without any notable incidents. Likewise, the majority of households have chosen to keep Latvenergo as their electricity supplier. What is more, the Group actively participated in the development of support mechanisms for vulnerable customers. Taking care of the customers' convenience, the customer self-service portal and billing system were modernised in the middle of the year, making customer communication with the service provider more user-friendly.

The process of complete market opening took place simultaneously with the *Elektrum* brand introduction into the Latvian market. *Elektrum* electricity products have a stable market position in the Baltics, demonstrating the quality of service and popularity.

Latvenergo Group has managed to strengthen its position as the largest electricity supplier in the Baltics: in 2015, the Group supplied 7.9 TWh of electricity in retail, supplying 865 thousand customers covering about a third of the retail market.

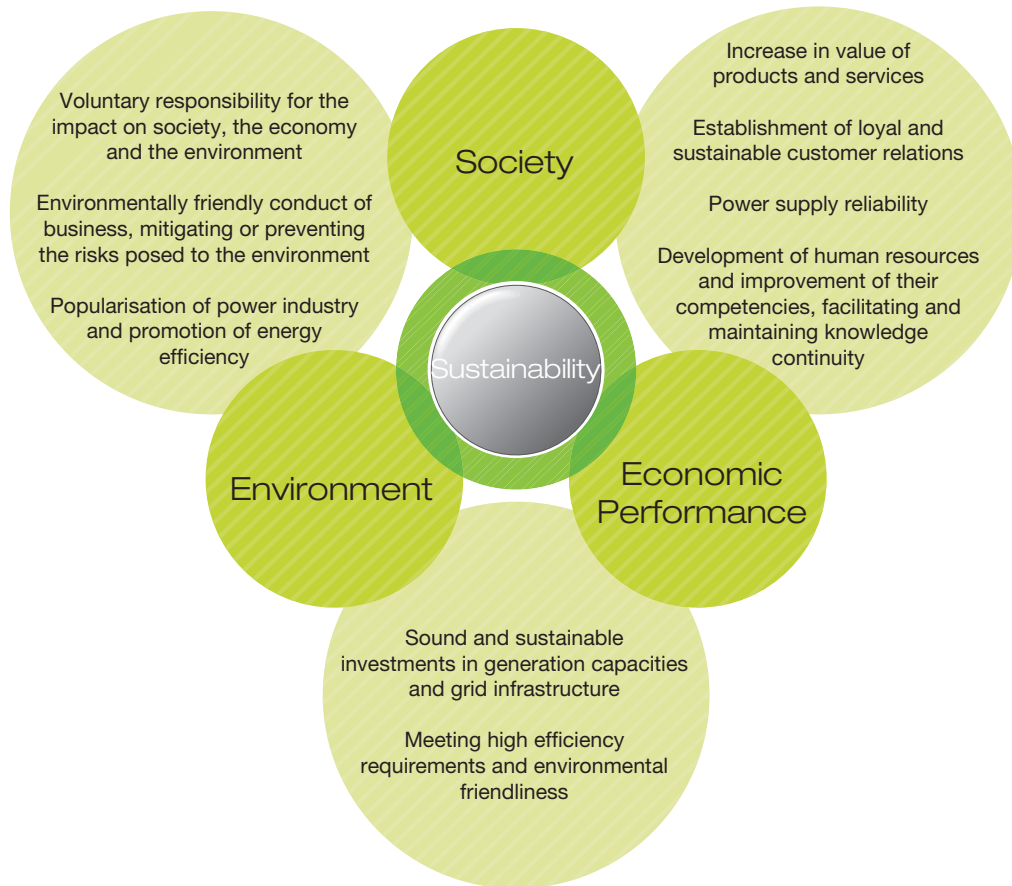
#### **Diversification of electricity generation sources**

Diversification of electricity generation sources is achieved by restoring the existing capacities and investing into new facilities, with a focus on economically justified investments in low-emission sources. At the same time, the efficiency of generation facilities is improved.

The Daugava hydropower plant (HPP) unit reconstruction programme, scheduled for completion in 2022, was successfully continued in 2015. The programme is aimed at improving Daugava HPPs efficiency, safety and competitiveness.

Currently Latvenergo Group has at its disposal a diversified portfolio of capacities – 976 MW at combined cycle gas cogeneration plants and 1,536 MW at hydropower plants. Latvenergo Group facilities allow operating successfully in both base and peak regimes, flexibly adjusting to electricity market processes.

## Three Pillars of Sustainability



### Balanced development of networks

Starting the implementation period of the strategy, the greatest challenge to electricity distribution was the accelerated aging of the electricity distribution infrastructure with poor electricity availability and quality indicators.

Considering the scale of the distribution infrastructure and its complicated structure, improvement of quality indicators while maintaining distribution service tariffs at levels that are affordable to consumers is a long-term endeavour. *Sadales tīkls AS Development plan 2014-2023* defines the investment priorities for the coming years, including replacement of overhead lines with cables, network automation, and development of smart technologies. The implementation of the Development Plan has already ensured significant improvements in the electricity supply reliability indicators: compared to 2012, the system average interruption duration index (SAIDI) has been reduced by 45%, and the system average interruption frequency index (SAIFI) – by 33%.

As for the development of transmission system assets, the most important project for the strategy implementation period is the *Kurzeme Ring*, which will

provide for a better opportunity to use the *NordBalt* submarine cable between Lithuania and Sweden, ensuring further integration of the Baltics into the Nordic electricity market. As of 1 January 2015, the project is implemented by Augstsprieguma tīkls AS, with the required funding provided by Latvijas elektriskie tīkli AS (for more information see Section 1.10 “Description of Operating Segments”).

To ensure an uninterrupted strategic planning process, at the end of 2015, the work on medium-term strategy for the following period (2017-2020) started. The new strategy will take into account the challenges expected in that particular period, and will be improved following the requirements of the Law on the Management of Public Persons’ Capital Shares and Capital companies, entered into force on 1 January 2015, and the guidelines developed by the Cross-Sectoral Coordination Centre. Completion of the new strategy is scheduled for 2016.

By implementing the strategy, Latvenergo Group makes a contribution to meeting the needs of the society and increases the Group’s value, at the same time adhering to the principles of sustainability.



# 1.4 Corporate Social Responsibility

## Responsible business leader

Through corporate social responsibility (CSR) activities, Latvenergo Group promotes a responsible business environment in the Baltic region. Responsible business conduct has been integrated in the strategic goals and development targets, policies and everyday work of Latvenergo Group. Latvenergo Group complies with the statutory requirements and also undertakes voluntary responsibility for its impact on the society, the environment and the national economy, thus contributing to the sustainable development of the Group. In our everyday work, we also follow the basic principles of social responsibility in compliance with the ISO 26000:2010 standard.

Latvenergo Group Corporate Social Responsibility policy specifies the basic principles, directions and criteria for CSR. The Group implements CSR activities in line with its operations and strategic goals, raising public awareness of responsible business conduct and the energy industry, making a substantial long-term impact and ensuring the involvement of large groups of the society. The Group also emphasises the link of CSR activities with the Baltic region, and the electrical or human energy.

## Directions of Corporate Social Responsibility activities



On 10 June 2015 Latvenergo Group promoted CSR best practice at the Responsible Idea Market conference held during the Responsible Business Week. At the "Being Open in Business – Opportunity or Risk" conference held on 24 November 2015, the Group shared its experience on transitioning to GRI G4 non-financial reporting guidelines. At the meeting of Latvian Association of Power Engineers and Energy Constructors (LAPEEC) held on 10 December 2015, the Group informed the audience about the results of the stakeholder workshop "Material aspects for sustainable development of Latvenergo Group".

In a study conducted by TNS Latvia SIA on corporate reputation in 2015 it was demonstrated that the majority of business environment and population representatives, industry experts and media representatives evaluate Latvenergo Group as an example of responsible business. Likewise, according to the study the share of Latvian population who have heard about the cultural and sport events supported by Latvenergo Group has increased. More than half of the population are also informed about the CSR activities related to social support and electrical safety of children and young people. The Latvian population perceive electrical safety of children and young people, preservation of the environment and social support projects as the three main directions of Group's CSR.

## Support for science and education

Latvenergo Group implements projects oriented towards the development of education and science in the energy sector, promotes engineering professions and qualified graduates.

In cooperation with the Latvian Academy of Sciences, for more than 15 years Latvenergo Group has been awarding its Annual Award for outstanding and significant contribution to the energy industry and the achievements of young researchers in the energy industry. Each year, the Group announces competitions for students of higher educational institutions awarding the best graduation papers on topical issues of the energy sector, whilst also organising scholarship competitions for students. The Group also provides internship opportunities to students from various educational institutions. Latvenergo Group employees participate in the Bachelor's and Master's thesis defence committees of Riga Technical University (RTU) and Latvia University of Agriculture (LUA), and the Group annually participates in publishing of books related to





Finalists, mentors, jury and organizers of the contest *Experiment*.

energy industry. In 2015, Latvenergo Group supported the establishment of the Engineering secondary school under the RTU, and the improvement of the laboratory for students of the RTU, Faculty of Power and Electrical Engineering.

To encourage young people to study physics, since 2013 Latvenergo Group has been maintaining the physics portal *fizmix* (<http://www.fizmix.lv>). The *fizmix* team not only publishes physics experiments on the *fizmix* portal, but also demonstrates them during lectures at schools in Latvia, at Researchers' Night events at the Museum of Energy and the Energy Efficiency Centre, and during the Technical Innovation Festival. The *fizmix* interactive stand is also included in the room for youth information and creativity called Room – 15+, opened at the National Library of Latvia in 2015.

For 20 years in a row, Latvenergo Group has been organising the *Experiment* erudition contest for 8th and 9th graders. The contest provides an insight into safe use of theoretical knowledge in practice, encourages interest in physics, in natural phenomena and the environment.

In line with past practice, in 2015 Latvenergo Group donated computers to Latvian educational institutions.

### Raising public awareness on electrical safety

Education of children and young people on electrical safety is one of the corporate social responsibility priorities of the Group's subsidiary Sadales tīkls AS. Education of the young generation on safe and efficient

use of electricity in everyday life is one of the CSR tasks set for the Group's subsidiary.

Encouraging children and youth to act with precaution near electrical installations, in 2015, Latvenergo Group continues to organise an informatively-educational campaign called "Don't approach! In the game with electricity the loser will be YOU!". To raise awareness on electrical safety in the virtual environment, an Electrical Safety page was created on the *draugiem.lv* social network. Sadales tīkls AS specialists took part in the "Summer of Adventures 2015" family safety festival, organised by the State Police and the Riga City Council, in the State Police "Hand in Hand" vocational education and safety project, and in children's summer camps and regional safety days. For almost 10 years, Latvenergo Group has been participating in the making of "Long Live the Children!" movie.

In 2015, Sadales tīkls AS educated those engaged in economic activities, logging and agricultural works, reminding and encouraging them to take care of their own safety and of those surrounding them, and to comply with electrical safety rules while working near electricity lines: to coordinate works in electrical line protection zones, and to not operate without coordination in the vicinity of overhead lines machinery, the height of which exceeds 4.5 meters. In 2015, Sadales tīkls AS specialists participated with educational activities in the Agricultural Forum in Jelgava, at the "Spring 2015" exhibition in the Ramava Exhibition Centre, and in the "Tractor Day 2015" organised by the Ministry of Agriculture of the Republic of Latvia in Bauska District, Davini parish, etc.

## Preservation of the industrial heritage

The Museum of Energy of Latvenergo Group plays a vital role in the exploration and preservation of the documentary and industrial heritage of the energy sector in Latvia and Latvenergo Group. Museum of Energy has created a travelling exhibition of E. Kraucs's collection of glass plate photonegatives entitled "Construction of the Kegums Hydropower Plant (1936-1940)", included in the register of UNESCO Memory of the World Programme.

The Museum of Energy offers exploratory tours to different audiences and thematic educational activities where everyone can get acquainted with the history and industrial heritage of the Latvian energy industry and Latvenergo Group, and watch the film "How the Kegums power plant was built. Memoirs of Karlis Dumbrajs".

In 2015, the museum traditionally participated in local and international campaigns and events: the Museum Night, Researchers' Night, UNESCO Week, and Balttour 2015. In cooperation with Pasažieru vilciens AS, a new project, "By train to the Museum of Energy in Kegums!", was launched at the end of the year. For additional information, go to Latvenergo Group website at <http://www.latvenergo.lv>.

## Openness to culture and sport

By participating in national level cultural and sports events, Latvenergo Group promotes the development of Latvian cultural traditions and strengthening of the Latvian national identity, as well as an active lifestyle.

For a number of years, the Group has supported the *Nāc līdzās Ziemassvētkos!* (Come Along at Christmas!) charity concert, promoting the artistic talents of orphaned and handicapped children and youth. In 2015, the Group also supported the organisation of the XI Latvian School Youth Song and Dance Festival. Latvenergo Group employees also participated in the *Lattelecom Riga Marathon* (formerly *Nordea Riga Marathon*), which is one of the largest in Northern Europe, and in another large-scale national sporting event – the Latvian Cycling Union Race in Sigulda.

For a number of years the Group has been involved in various initiatives of public importance under the leitmotif of light and energy. For the second year in a row, Latvenergo Group took part in the "Riga Carnival" event of the Riga Light Festival. During the festival, the Group headquarters at Pulkveža Brieža Street 12 were illuminated in various colour schemes. During the *Positivus* music festival in 2015, Latvenergo Group organised the *Friendly Energy* lighting object contest for the third time.

At the end of 2015 Latvenergo Group employees participated in the "Christmas Caravan" charity event of the Latvian Olympic Committee by donating sports equipment to schools in Latvia.



## Voluntary responsibility for the environment

In 2015, Latvenergo AS initiated *green bond* offering programme. The main requirement for *green bonds* is the use of the funds raised in the issuance process only for projects relevant to *green* thinking and related to renewable energy sources, improved energy efficiency and sustainable environment. Additional information about *green bonds* is available under Annex "Report on *Green Bonds*".

In 2015, Latvenergo Group also continued cooperation with the Latvian Ornithological Society (LOS) to protect bird species, and with the *Mēs – zivīm* (We to fish) society to protect and replenish the fish stocks in the Daugava River basin.

Additional information about the environmental protection activities implemented by the Group is available under Section 2.4 "Environmental protection".

## Energy efficiency

The opening of the electricity market has highlighted energy efficiency issues among the population and motivated customers to evaluate and improve their energy usage habits.

In 2015, Latvenergo Group specialists participated in the Ministry of Economics of the Republic of Latvia working groups on the implementation of the Directive 2012/27/EU of the European Parliament and of the Council on energy efficiency in Latvia, and in the development of the "Energy Savings Catalogue".

For as long as 18 years the Energy Efficiency Centre of Latvenergo Group has been hosting free of charge lectures and educational workshops, field trips and consultations about efficient ways to use energy by households and businesses, about the latest electric appliances and their selection criteria, and energy efficient usage habits. To advise customers about the energy management best practices, a certified energy management system was introduced at the Energy Efficiency Centre in 2015 in compliance with the ISO 50001:2011 standard. The parking lot of the Energy Efficiency Centre provides a possibility for everyone to charge electric vehicles free of charge, thus promoting environmentally friendly modes of transport. Latvenergo Group website ([http://www.latvenergo.lv/eng/for\\_customers/energy\\_efficiency\\_centre/about\\_eec/](http://www.latvenergo.lv/eng/for_customers/energy_efficiency_centre/about_eec/)) provides simple tips for using electricity more efficiently.

### Social support

In 2015, Latvenergo AS supplied electricity to vulnerable customers (poor or low-income persons, large families), compensating electricity price increase resulting from the market opening. For additional information, go to: <https://www.elektrum.lv/en>.

At the end of 2015, Group employees donated a variety of useful everyday items to those in need and participated in the “Firewood purchase and delivery to low-income families in Latvia” charity campaign, organised by Eurika Charity.

### Social protection of employees

Information about social protection of employees is available under Section 2.5 “Employees and Work Environment”.



# 1.5 Group Governance

G4-34

**Good corporate governance promotes increase in Group's value**

G4-56

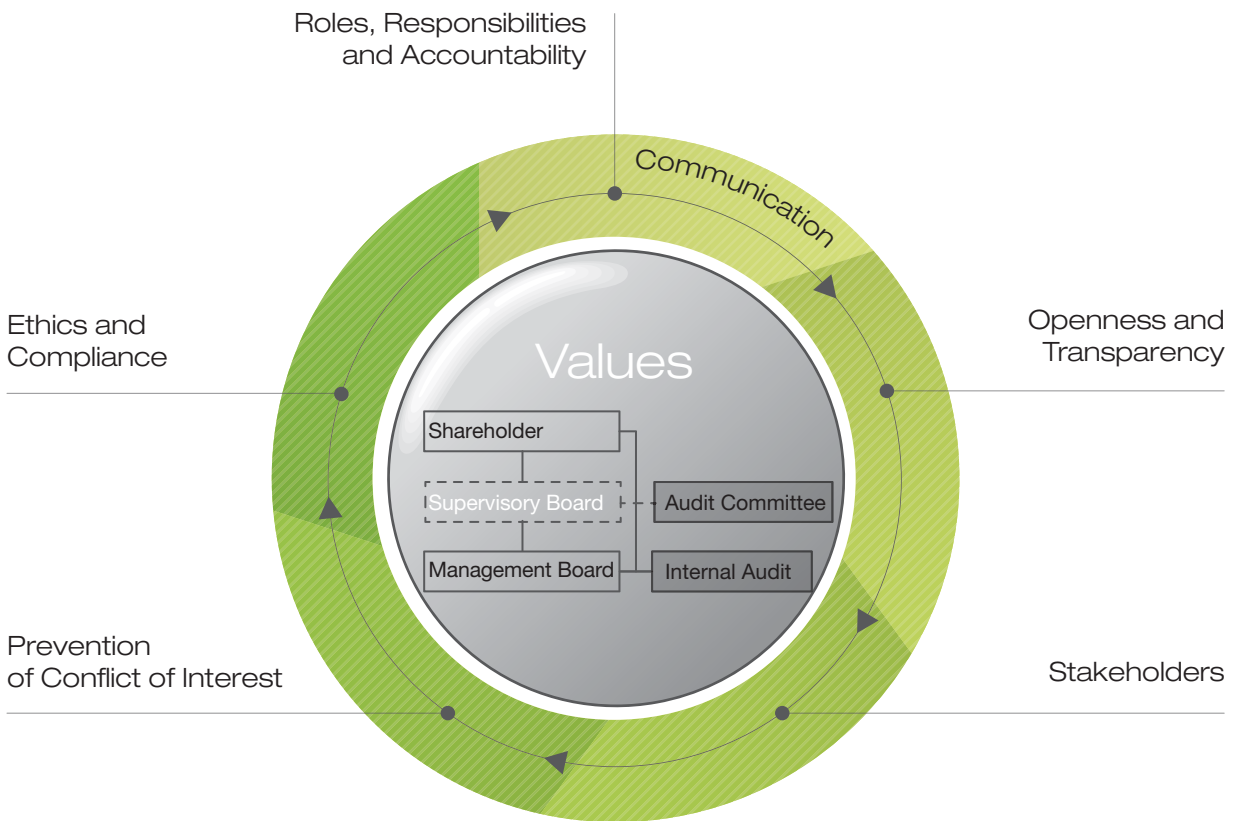
Latvenergo Group corporate governance principles define the elements of its operation concerning the executive and supervisory institutions of the Group companies. These elements are reflected in the Latvenergo Group Corporate Governance Model and are an essential precondition for successful achievement of the goals specified in the strategy and for increasing the value of the Company. Significant role in the maintenance of Latvenergo Group corporate governance system elements is assigned to the values of the Group and active communication, both internally

and in cooperation with stakeholders. The Latvenergo Group governance model is based on good governance practices, legislative regulation, and corporate governance guidelines.

● **Ethics and Compliance**

Latvenergo Group in its operations follows high standards of professional ethics and ensures compliance of its activity with the requirements of the applicable legislation, creating an ethical business environment. Informative activities are carried out on regular basis to ensure employee awareness and understanding of ethics and compliance standards. The Group makes improvements to internal normative documents and takes other measures to prevent the possibility of corruptive or fraudulent activities.

**Group Corporate Governance Model**



Latvenergo Group supports fair business practices, applies fair competition rules and does not engage in transactions that restrict competition, are corruptive or discriminatory. Contractual partners of Latvenergo Group are urged to adhere to similar ethical principles, and upon signing of agreements are asked to provide declarations that the cooperation will be based on fair business cooperation principles.

The fundamental ethical principles of Latvenergo Group for cooperation with contractors are published on the <http://www.latvenergo.lv> website, under the Tenders and offers/Procurement procedures Section.

#### ● Roles, Responsibilities and Accountability

The roles, responsibilities and accountability of governance and supervisory bodies are defined mainly in external laws and regulations and in the internal documents of the Group, among which company's Articles of Association are the most important

#### ● Openness and Transparency

Transparency of Latvenergo Group financial and operational performance is ensured by publishing annual reports of the Group, which since 2002 have been prepared according to the International Financial Reporting Standards (IFRS) approved by the EU.

Since the initiation of the bond emission programme and inclusion of issued bonds in Nasdaq Riga exchange in early 2013, Latvenergo Group has been publishing quarterly interim financial reports in accordance with the requirements of the Financial Instrument Market Law on disclosure of information for issuers of bonds. Likewise, the Latvenergo AS corporate governance report has been published for four years in accordance with Nasdaq Riga AS corporate governance principles, while providing additional information in the Sustainability Report – the only audited sustainability report in Latvia, prepared in compliance with the GRI guidelines since 2009.

As of 2015, interim financial reports of Latvenergo AS and its subsidiaries are published in compliance with the Law on Management of Public Persons' Capital Shares and Capital Companies.

#### ● Prevention of Conflict of Interest

In accordance with the Law on Prevention of Conflict of Interest in Activities of Public Officials, management board members of state capital companies have the status of state officials. The law restricts the activities of management board members outside their official duties in order to prevent the influence of a personal or financial interest. Board members are obliged to submit an annual state official's declaration, specifying income received, positions held, transactions performed, participation in commercial activities and other information.

The Group governance and supervisory bodies ensure that principles for prevention of conflict of interest are adhered to during the fulfilment of duties. The goal of the management is to raise awareness of conflict of interest



situations through explanatory activities, training and control. The management of the Group companies' works towards establishing preventive and detective controls for the elimination of conflicts of interest.

The Latvenergo Group Code of Ethics defines the potential conflict of interest situations and measures to avoid such situations. Employees should evaluate not only their commercial activities outside the Group but also those of their relatives and family members, if such activities are closely related to the Group operations, reports on such situations to the employer. In order to raise employee awareness on potential conflict of interest situations in everyday work, Latvenergo Group organises training and informative activities. The Group has also introduced annual Conflict of Interest Declarations, which are evaluated and monitored. Upon entering into employment relations and signing the declaration, new employees must confirm in writing their understanding of conflict of interest situations and the commitment to prevent their occurrence.

#### ● Stakeholders

Cooperation and communication with stakeholders is an important element of the Latvenergo Group corporate governance system. Latvenergo Group is aware of its impact on stakeholders and vice versa, and handles issues of material importance to its stakeholders with a great sense of responsibility. More information about Latvenergo Group cooperation with stakeholders is provided in Section 1.8 "Stakeholder Engagement".



Management Board of Latvenergo AS

Guntis Stafeckis  
Member of the  
Management Board

Uldis Bariss  
Member of the  
Management Board

Āris Žīgurs  
Chairman of the  
Management Board

Māris Kuņickis  
Member of the  
Management Board

Guntars Baļčūns  
Member of the  
Management Board



## Āris Žīgurs (50)

Chairman of the  
Management Board

Date appointed: 16.11.2015  
Expiration of the term: 15.11.2020

### Experience

- 2015 – present: Employers' Confederation of Latvia, Member of the Council
- 2013 – present: Latvenergo AS, Chief Executive Officer
- 2011 – present: LUA, Member of the Counsellor Convent
- 2011 – present: RTU, Chairman of the Counsellor Convent
- 2011 – present: Latvian National Committee of the World Energy Council, Vice-president
- 2010 – present: Latvenergo AS, Chairman of the Management Board
- 2010 – present: EURELECTRIC, Member of the Board of Directors
- 1996 – 2010: Rigas Siltums AS, President and Chairman of the Management Board

### Education

- Baltic Institute of Corporate Governance, Executive education, Chairman Certificate (2013)
  - Baltic Institute of Corporate Governance, Executive education, Board Member Certificate (2010)
  - RTU, Doctor of Sciences in Engineering, energy sector (2009)
  - RTU Riga Business School, Master in Business Administration (2004)
  - LUA, Faculty of Engineering, engineer-mechanic (1988)
- 

## Uldis Bariss (50)

Member of the  
Management Board

Date appointed: 16.11.2015  
Expiration of the term: 15.11.2020

### Experience

- 2013 – present: Latvenergo AS, Chief Commercial Officer
- 2010 – present: Elektrum Eesti OÜ, Chairman of the Supervisory Board
- 2010 – present: Elektrum Lietuva UAB, Chairman of the Supervisory Board
- 2005 – present: Latvenergo AS, Member of the Management Board
- 2005: Latvenergo AS, Project Director of Distribution Network Restructuring
- 2002 – 2004: Latvenergo AS, Economics Department Director
- 1996 – 2002: Lattelekom SIA, Head of Financial Planning and Control Division, Head of Management Accounting Sector

### Education

- Baltic Institute of Corporate Governance, Executive education, Board Member Certificate (2010)
  - Stockholm School of Economics in Riga, Executive Master in Business Administration (2008)
  - University of Latvia, Master in Economics (2004)
  - International Chartered Accountant qualification (Association of Chartered Certified Accountants (ACCA)) (2000)
- 

## Māris Kuņickis (36)

Member of the  
Management Board

Date appointed: 16.11.2015  
Expiration of the term: 15.11.2020

### Experience

- 2013 – present: Latvenergo AS, Chief Operating Officer
- 2012 – present: EURELECTRIC, Deputy Member of the Board of Directors
- 2011 – present: LAPEEC, Member of the Board
- 2010 – present: Latvenergo AS, Member of the Management Board
- 2006 – 2010: Rigas gaisma LGA, Director, Executive Officer

### Education

- Baltic Institute of Corporate Governance, Executive education, Board Member Certificate (2013)
  - Studies at RTU Doctor's degree programme at the Faculty of Power and Electrical Engineering
  - University of Latvia, Master's degree, Faculty of Physics and Mathematics (2005)
  - RTU, Engineer's degree, Faculty of Power Stations, Networks and Systems (2002)
-



## Guntars Baļčūns (35)

Member of the  
Management Board

Date appointed: 16.11.2015  
Expiration of the term: 15.11.2020

### Experience

- 2015 – present: Latvenergo AS, Chief Financial Officer
- 2015 – present: Latvenergo AS, Member of the Management Board
- 2014 – 2015: Enerģijas publiskais tirgotājs AS, Member of the Management Board
- 2005 – 2015: Latvenergo AS, Business Planning and Control Director, Corporate Strategy Project Manager
- 2003 – 2005: Aizkraukles Banka AS, Credit Specialist
- 1999 – 2000 Heidelberga Audits SIA, Accountant

### Education

- Studies at RTU Riga Business School, Executive Master's degree programme in Business Administration
  - Komercizglitības centrs SIA, Business class (2008)
  - University of Latvia, Master in Economics (2005)
  - Stockholm School of Economics in Riga, Bachelor's degree in Economics and Business Administration (2003)
- 

## Guntis Stafekis (52)

Member of the  
Management Board

Date appointed: 16.11.2015  
Expiration of the term: 15.11.2020

### Experience

- 2015 – present: Latvenergo AS, Chief Development Officer
- 2015 – present: Latvenergo AS, Member of the Management Board
- 2011 – 2015: Latvijas elektriskie tīkli AS, Chairman of the Management Board, Chief Executive Officer
- 2010 – 2011: Siltumelektroprojekts SIA, Chief Executive Officer
- 1995 – 2009: Siemens SIA, Chief Executive Officer, Manager of the Energy and Transport Systems Department
- 1995: Latvenergo AS, Deputy Head of the Technical and Production Department of Daugava HPPs

### Education

- Siemens, S4 – strategic and leadership training (2006)
  - Training course by Larry W. Stout, development of management skills (2005)
  - EBRD, Procurement and project management seminar (1995)
  - Vattenfall, Energy management of the Baltic States (1993)
  - RTU, Master's degree in Electrical Engineering (1986)
- 

## Zane Kotāne (38)

Member of the Management Board

Date appointed: 16.11.2012  
Expiration of the term: 15.11.2015  
(suspended activities on 19.06.2015)

### Experience

- 2013 – 2015: Latvenergo AS, Chief Financial Officer
- 2012 – 2015: Elektrum Eesti OÜ, Member of the Supervisory Board
- 2012 – 2015: Elektrum Lietuva UAB, Member of the Supervisory Board
- 2011 – 2015: Latvenergo AS, Member of the Management Board
- 2010 – 2011: Air Baltic Corporation AS, Head of the Unit for Business Analysis and Reporting at the Commercial Department
- 2005 – 2010: International investment group, Chief Financial Officer, Investment Finance Consultant
- 2003 – 2005: Ernst & Young Hungary, Project Manager, Risk Management Division

### Education

- RTU Riga Business School, Master in Business Administration (2014)
- Baltic Institute of Corporate Governance, Executive education, Board Member Certificate (2011)
- Stockholm School of Economics in Riga, Bachelor in Economics and Business (1997)

## Arnīs Kurģs (48)

Member of the Management Board

Date appointed: 16.11.2012  
Expiration of the term: 15.11.2015

### Experience

- 2013 – present: Latvenergo AS, Chief Administrative Officer
- 2010 – present: Elektrum Eesti OÜ, Member of the Supervisory Board
- 2010 – present: Elektrum Lietuva UAB, Member of the Supervisory Board
- 2006 – 2015: Latvenergo AS, Member of the Management Board
- 1995 – 2006: Latvenergo AS, Head of Legal Services Unit, Deputy Head of Legal Unit, Legal Counsel
- 1993 – 1995: Saeima (the Parliament of the Republic of Latvia), Deputy Assistant, Consultant

### Education

- Baltic Institute of Corporate Governance, Executive education, Board Member Certificate (2010)
  - School of Business Administration Turība, Professional Master in Law
  - University of Latvia, Master in Law (1993)
  - Malta Technical School, qualification of construction technician (1986)
-

## Shareholder

All shares of Latvenergo AS are owned by the state and held by the Ministry of Economics of the Republic of Latvia. The interests of the shareholder are represented at the Shareholders' Meeting by the State Secretary of the Ministry of Economics or his/her authorised representative. Shareholders' Meetings are convened with consideration of the requirements and time lines stipulated by the Law on Management of Public Persons' Capital Shares and Capital Companies.

According to the Energy Law, Latvenergo AS is defined as a national economy object of state importance, and its shares may not be privatised or alienated.

The main duties of Latvenergo AS Shareholders' Meeting are:

- continuous supervision of the Management Board activities;
- appointment and revocation of members of the Management Board and the Audit Committee, and approval of their remuneration;
- monitoring of the compliance of the company's operations with the legislation, its Articles of Association and the decisions of the Shareholders' Meeting;
- approval of the Annual Report of the company and appointment of the auditor;
- decision-making on distribution of the company's profits for the preceding year.

In 2015, 13 Shareholders' Meetings took place. The most important decisions passed in 2015 concerned the approval of the Annual Report 2014, dividend payout in the amount of 90% of the profit, appointment of the auditor, amendments to the Articles of Association of Latvenergo AS, election of Management Board Members for a new term of office, and election of members of the Audit Committee. All members of the Management Board, the Audit Committee and the Auditor participated in the approval of the Annual Report 2014 at the General Meeting of Shareholders.

## Supervisory Board

In 2009, in accordance with the Law on State and Municipality Capital Shares and Capital Companies of the Republic of Latvia, the Supervisory Boards of all state capital companies in Latvia, including Latvenergo AS, were abolished. As of 1 January 2016, the Law on Management of Public Persons' Capital Shares and Capital Companies provides for a possibility to organise supervisory boards at large and medium state-owned capital companies, and Latvenergo AS, Sadales tīkls AS and Latvijas elektriskie tīkli AS match those criteria. Until the establishment of the Supervisory Board, the capital company supervision functions are performed by the Shareholders' Meeting.

Supervisory Boards have been retained as supervisory bodies at fully-owned Latvenergo AS subsidiaries Elektrum Lietuva UAB and Elektrum Eesti OÜ, which operate outside the territory of Latvia and thus are not subject to the legislation of the Republic

of Latvia. The Supervisory Boards of the above-mentioned subsidiaries consist of three members, of which Latvenergo AS employees are appointed for the supervision of the relevant areas of operation. Supervisory functions in Liepājas enerģija SIA, where the equity share of Latvenergo is 51%, are carried out by a Supervisory Board of six individuals, three of whom are representatives of Latvenergo AS. The activities of the Management Boards of Sadales tīkls AS, Latvijas elektriskie tīkli AS and Enerģijas publiskais tirgotājs AS are supervised by the Shareholders' Meeting, whose interests are represented by the Management Board of Latvenergo AS.

## Management Board

The Management Board of Latvenergo AS is in charge of the Group's operations. After evaluating the required competencies, the experience and the intended area of responsibilities, the Shareholders' Meeting appoints five members of the Management Board. On 19 June 2015, the former Management Board member Zane Kotāne decided to discontinue her functions as a member of the Management Board due to personal reasons. During the reporting period, the term of office of the Management Board members expired, and as a result, the Extraordinary Meeting of Shareholders held on 6 November 2015 approved a new Management Board. Guntars Baļčūns and Guntis Stafekis were elected to the Management Board for a five-year term of office, starting 16 November 2015. Āris Žīgurs (Chairman), Uldis Bariss and Māris Kuņickis will continue to serve on the Management Board.

The Management Board operates in compliance with the Articles of Association and the Rules of the Management Board. The principal duties of the Management Board of Latvenergo AS are:

- management and representation of the company;
- accountability for the business activities of the company and for the legal compliance of the accounting;
- management of the company's property;
- defining the strategic direction of the Group, its development plans, goals and policies.

Management Board meetings are organised in order to manage the Group activities and pass decisions in a timely manner. In 2015, 66 Management Board meetings were convened. The Management Board is entitled to pass decisions if at least three of its members are present, including the Chairman of the Management Board or his/her substitute.

Attendance of the Management Board meetings: Āris Žīgurs, Chairman of the Management Board – 61; Uldis Bariss, Member of the Management Board – 63; Māris Kuņickis, Member of the Management Board – 56; Guntars Baļčūns, Member of the Management Board (from 16.11.2015) – 10; Guntis Stafekis, Member of the Management Board (from 16.11.2015) – 10; Zane Kotāne, Member of the Management Board (till 19.06.2015) – 22; Arnis Kurgs, Member of the Management Board (till 15.11.2015) – 50.

The Management Board reports to the Shareholder, and Management Board Members are jointly liable for compliance with all the binding laws and regulations, execution of the decisions made by the Shareholders' Meetings, and for the financial performance of the Group. All members of the Management Board are independent in their activities and have no shareholdings in the capital of the contractual partners or associated companies. Additionally, the Management Board of Latvenergo AS performs the functions of the Shareholder in the fully-owned subsidiaries of Latvenergo AS.

## Management Board Remuneration Policy

Remuneration of the Management Board is regulated by the legislation of the Republic of Latvia – the Law on Management of Public Persons' Capital Shares and Capital Companies, and the Regulations issued by the Cabinet of Ministers based on that law. Legal acts provide for a uniform regulation regarding remuneration of members of management boards at state-owned companies, and management board members are entitled to compensation for the performance of additional duties at the company.

The monthly salary of the Chairman of the Management Board is linked to the average monthly salary of employees in Latvia during the preceding year, as published in the Official Statistical Bulletin of the Central Statistical Bureau of the Republic of Latvia, multiplied by a ratio specified according to the capital company's reference criteria (turnover, assets, number of employees). The maximum ratio applicable to monthly salaries is 10, and in 2015 it was applied to the uniform monthly salary of the Chairman of the Management Board - Chief Executive Officer (CEO). The remuneration of a Member of the Management Board Member - Chief Officer may not exceed 90% of the total remuneration of the Chairman of the Management Board – CEO.

Once a year, following the approval of the Annual Report, the Shareholders' Meeting may decide on payment of bonuses to the Members of the Management Board. The bonuses are based on the results of the company, execution of the strategy and achievements of the set targets. The amount of a bonus may not exceed two monthly salaries of the Member of the Management Board. With the start of the new term of office, i.e., 16 November 2015, authorisation agreements have been signed with the Members of the Management Board on the performance of their duties. The terms and conditions of the authorisation agreements provide for a possibility to receive a severance payment in the amount of three monthly salaries if they are recalled from their duties before the expiration of the term of office, including in the event of reorganisation or liquidation of the company.

Till 15 November 2015, the fringe benefits under the Latvenergo AS Collective Bargaining Agreement, including monthly contributions to the Pension Fund of 5% of the monthly salary, are applicable to the remuneration of the Members of the Management



Board. The remuneration policy does not provide for the option to pay remuneration in the form of shares or share options. Total remuneration in 2015 for the period, when the duties of Chairman of the Management Board or Member of the Management Board were fulfilled, for Latvenergo AS Chairman of the Management Board, CEO Ā. Žīgurs is EUR 141,412; Member of the Management Board, Chief Commercial Officer (CCO) U. Bariss – EUR 122,787; Member of the Management Board, Chief Operating Officer (COO) M. Kuņickis – EUR 120,598; Member of the Management Board, Chief Financial Officer (CFO) G. Baļčūns – EUR 9,055; Member of the Management Board, Chief Development Officer (CDO) G. Staņeckis – EUR 8,334; Member of the Management Board, CFO Z. Kotāne – EUR 99,845 and Member of the Management Board, Chief Administrative Officer (CAO) A. Kurģs – EUR 122,663.

## Audit Committee

An independent Audit Committee operates at Latvenergo AS and is accountable for its operations and performance to the Shareholders' Meeting of Latvenergo AS. Having evaluated the necessary competencies and professional experience, the Shareholders' Meeting elects three members to the Audit Committee. During the reporting period, the term of office of the Audit Committee members expired, and as a result, the Extraordinary Shareholder's Meeting of 3 December 2015 approved a new Audit Committee. Marita Salgrāve was elected as a new member of the Audit Committee for a three-year term of office starting from 5 December 2015; Torben Pedersen and Svens Dinsdorfs will continue to serve on the Committee. All members of the Audit Committee are independent specialists who are not engaged in the operational activities of the Group.

In 2015, 8 Audit Committee meetings took place, of which two were remote. In addition to the regular duties of the Audit Committee, i.e., supervision of the financial reporting process, internal control and risk management system efficiency, as well as monitoring of the work of the internal audit and the external auditor, in 2015, the Audit Committee of Latvenergo AS took part in other duties related to the Latvenergo Group. The Audit Committee of Latvenergo AS made recommendations regarding the establishment and selection of the Head of Compliance and Internal Audit position, discussed and provided input to the Group's risk management processes, the risk approach to be applied in the internal audit plan, as well as an operational effectiveness audit at the subsidiary Sadales tīkls AS.

## Audit Committee



**Torben Pedersen (66)**  
Chairman of the  
Audit Committee

Date appointed: 05.12.2015  
Expiration of the term: 04.12.2018

### Experience

- 2015 – present: Electronic House UAB, Member of the Supervisory Board
- 2013 – present: Vilnius International School, Member of the Supervisory Board
- 2012 – present: Baltic Engineers UAB, Chairman of the Supervisory Board
- 2011 – present: Danish Chamber of Commerce in Lithuania, Member of the Supervisory Board
- 2001 – 2011: Deloitte, Partner
- 1994 – 2001: Arthur Andersen, Partner

### Education

- Aarhus School of Business, Master in Economics and Audit (1974)
- Chartered Accountant qualification (Denmark)



**Marita Salgrāve (50)**  
Member of the  
Audit Committee

Date appointed: 05.12.2015  
Expiration of the term: 04.12.2018

### Experience

- 2015 – present: Advisor on strategic matters to the Auditor General of the Republic of Latvia
- 2007 – 2015: State Audit Office of the Republic of Latvia, Member of the Council, Director of the Fourth Audit Department
- 1998 – 2007: Central Finance and Contracting Agency, Executive Director, Deputy Director, Director of Programme Management Department, Senior Procurement Specialist
- 1993 – 1998: Ramboll Group A/S, Denmark, Project Manager

### Education

- Sint-Aloysius School of Economics (EHSAL) in Brussels, Belgium, MBA (1998)
- University of Latvia, Faculty of Economics and Management, post-graduate qualification of an economist/ (accountant) (1997)
- Oxford College of Petroleum and Energy Studies, post-graduate qualification in energy and environment (1995)
- University of Latvia, Faculty of Chemistry, Master of Science (1988)



**Svens Dinsdorfs (39)**  
Member of the  
Audit Committee

Date appointed: 05.12.2015  
Expiration of the term: 04.12.2018

### Experience

- 2015 – present: Elko Grupa AS, Director, Member of the Management Board
- 2006 – 2014: Elko Grupa AS, Finance Director, Member of the Management Board
- 2004 – 2006: Sirowa Riga AS, Finance Director
- 1998 – 2004: Air Baltic Corporation AS, Vice President in Strategic Development, Business Control Director

### Education

- Stockholm School of Economics, Master in Finance and Economics (2003)
- Stockholm School of Economics in Riga, Bachelor in Economics and Business Administration (1998)

**Inita Hāne (37)**  
Member of the Audit Committee  
Date appointed: 05.12.2012  
Expiration of the term: 04.12.2015

### Experience

- 2014 – 2015: 4finance AS, Chief Audit Executive
- 2012 – 2014: Prime Holding SIA, Chief Financial Officer
- 2001 – 2012: PriceWaterhouseCoopers SIA, Senior Manager

### Education

- BA School of Business and Finance, Master in Finance (2013)
- Certified Internal Auditor (CIA) certificate (2009)
- International Chartered Accountant qualification (ACCA) (2007)
- Vidzeme University, Bachelor in Public Relations (2001)

## Internal Audit

The Internal Audit is an independent unit of Latvenergo AS, and the purpose of its operations is to evaluate and assist the governance bodies and organisational units to improve the efficiency of risk management, internal control systems and corporate management processes, thus achieving the targets set for the Group. The Internal Audit unit complies in its work with the International Standards for the Professional Practice of Internal Auditing, issued by the Institute of Internal Auditors (the Standards), and its activities are monitored by the Audit Committee.

In accordance with the Standards and based on the results of the audits performed, on an annual basis the Internal Audit prepares general statements on the operational efficiency of the internal control environment at Latvenergo Group, and makes recommendations for its improvement. The latest statement confirms that the controls introduced by Latvenergo Group are sufficient for the management of risks and the achievement of the set goals. In accordance with the Standards, the Internal Audit also prepares and submits an activity report, including information about compliance, self-assessment, and measures to ensure and improve the service quality.

## Dividend Policy

The distribution of Latvenergo AS dividends is regulated by the Republic of Latvia Law on the State Budget for 2016 and the Law on the Medium-Term Budgetary Framework for 2016, 2017 and 2018. In accordance with the aforementioned laws, the anticipated amount payable by Latvenergo AS in dividends in 2016 (for the reporting year 2015) is EUR 77.4 million, EUR 102.8 million in 2017 and EUR 111.5 million in 2018. The actual amount payable by Latvenergo AS in dividends is determined by the Shareholders' Meeting after the approval of the annual report, upon the evaluation of the results for the previous year.

## New Regulation to Improve the Corporate Governance

On 1 January 2015, the Law on Management of Public Persons' Capital Shares and Capital Companies came into force, replacing the former Law on State and Municipality Capital Shares and Capital Companies. The new regulation specifies the procedure for establishment, operation, liquidation and management of capital shares in public and derived public companies, as well as specifies the requirements for definition of goals, assessment of the performance, disclosure of information and the obligation of public companies to develop medium-term strategies. Latvenergo Group already fulfils the information disclosure requirements

specified by the law through publication of quarterly interim financial reports and ensuring the publication of information on its website, as specified by the Nasdaq Riga AS corporate governance principles. Latvenergo Group is also implementing its current medium-term strategy for the period ending in 2016.

In addition to other requirements, the new law provides for reinstatement from 2016 of Supervisory Boards as supervisory bodies at large and medium sized state-owned companies. The number of Supervisory Board members may not exceed five in large capital companies (Latvenergo AS, Sadales tīkls AS) and three in medium sized companies (Latvijas elektriskie tīkli AS). With the effect of the new regulation, no restrictions will apply that might prevent Latvenergo Group from fulfilling all the principles of corporate governance specified by Nasdaq Riga AS.

## Changes in Governance of Subsidiaries

In accordance with the regulatory framework, as of 1 January 2015, Augstsprieguma tīkls AS took over most of the functions previously performed by Latvijas elektriskie tīkli AS, while Latvijas elektriskie tīkli AS continues to carry out transmission system asset management functions – financing and lease of transmission assets to Augstsprieguma tīkls AS. With the reorganisation of the functions, amendments to the Articles of Association and changes in the composition of the Management Board of Latvijas elektriskie tīkli AS were introduced. As of 1 February 2015, the number of the Management Board Members was decreased from five to one.

On 28 February 2015, Uldis Mucinieks, Electricity Sales Director of Latvenergo AS, commenced the duties of Management Board member at Elektrum Lietuva UAB. From 28 February 2015 Uldis Mucinieks is also the Chairman of the Management Board of Elektrum Eesti OÜ. On 10 July 2015, Vilius Juraitis left his position as the Chairman of the Management Board and CEO at Elektrum Lietuva UAB, and his duties were overtaken by Uldis Mucinieks. Along with these changes at Elektrum Lietuva UAB and Elektrum Eesti OÜ, Gatis Junghāns left his position as a Management Board Member and will continue his work on the Supervisory Boards of Elektrum Lietuva UAB and Elektrum Eesti OÜ.

On 29 April 2015, the term of office of the Sadales tīkls AS Management Board member Ilvars Pētersons expired. As of 1 May 2015, the Management Board of Sadales tīkls AS consists of four members.



# 1.6 Group Management

G4-14

G4-56

The Group's management is continuously enhanced for more efficient operations

The management model of Latvenergo Group is based on best practices of corporate governance, separating strategic and operational management. The strategic management of Latvenergo Group is ensured by the Management Board, whose accountability according to the Commercial law is joint. While the

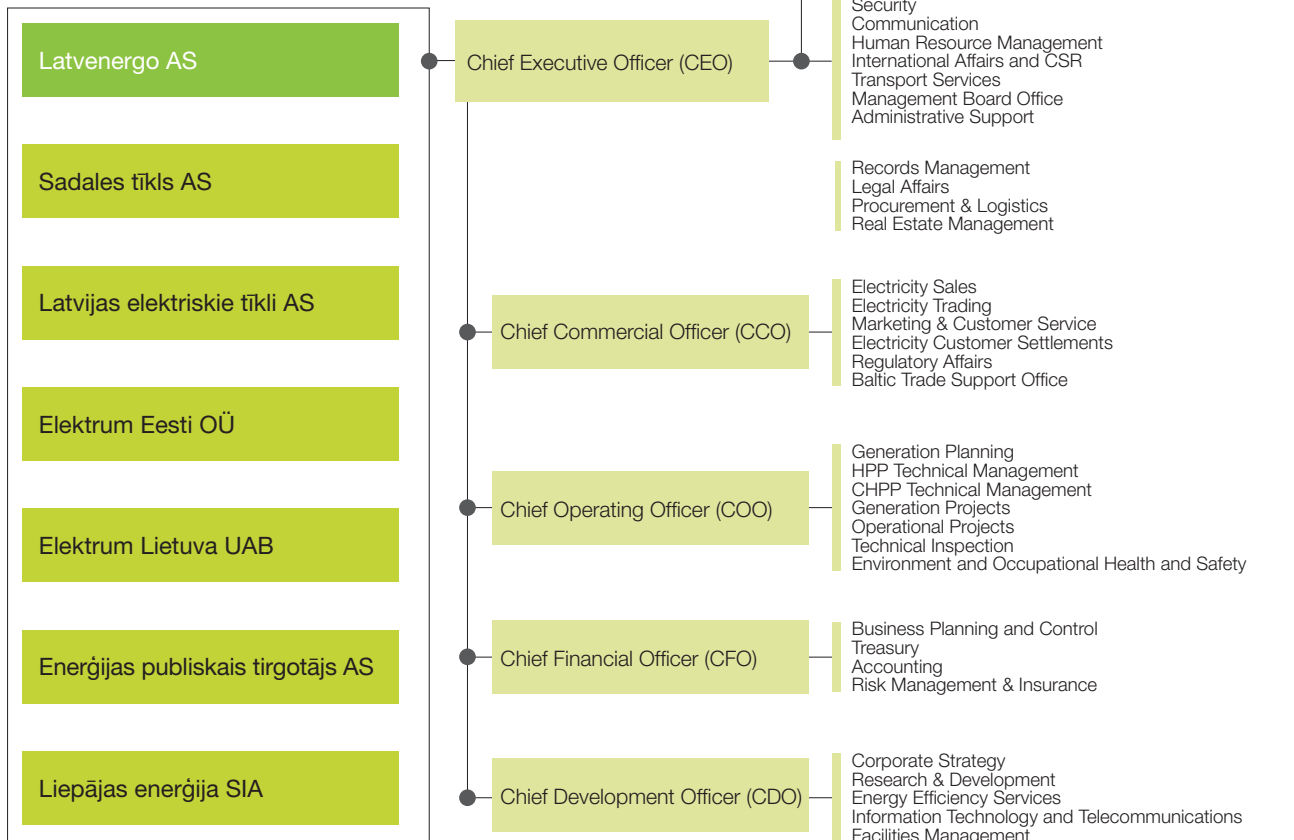
operational management is ensured by Chief Officers, whose accountability is individual. Main duties of the Management Board are to define the strategic direction of the Group, its development plans, goals and policies. The Management Board is accountable to a representative of the Shareholders' Meeting. The Chief Officers ensure the operational management of Latvenergo AS, including the achievement of specified goals, implementation of the strategy and developed policies, and other everyday duties delegated by the Management Board.

## Latvenergo Group Organisational Structure\*

### Audit Committee

### Strategic Management – Management Board of Latvenergo AS

### Latvenergo Group



\* at the end of the reporting period

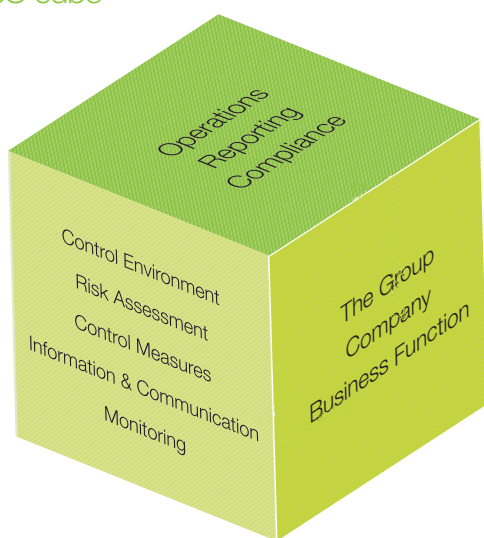
The areas of accountability of the Chief Officers are clearly defined and subordinated functions and supervision of administrative decisions within the framework of these functions are separated. Accordingly, Chief Officers are individually accountable to the CEO for the operational activity of the subordinated functions, ensuring cooperation of their division with the functions of other divisions, and adoption of resolutions according to the strategy of the Group. The CEO is accountable to the Management Board for the operational activity of subordinated functions. The areas and accountability of the Chief Officers are set in accordance to the strategic goals of the Group.

In December 2015, in order to improve the organisational structure for business activities and the process for decision making in Latvenergo AS by restructuring the units of accountability of Chief Officers a new area of responsibility was defined – *Development*. Moreover, a new unit was defined – *Energy Efficiency Services*, which is under the accountability of CDO. Considering the previous experience and knowledge about the Group operations, Chief Officer duties are performed by the Members of the Management Board of Latvenergo AS.

At the end of the reporting period the duties of Chief Officers are as follows:

- Āris Žigurs – Chief Executive Officer (CEO)
- Uldis Bariss – Chief Commercial Officer (CCO)
- Māris Kuņickis – Chief Operating Officer (COO)
- Guntars Baļčūns – Chief Financial Officer (CFO)
- Guntis Stafekis – Chief Development Officer (CDO)

### COSO cube



### Internal control system

To ensure achievement of Latvenergo Group's strategic goals, the Group management has introduced integrated internal control system that is based on COSO (Committee of Sponsoring Organizations of the Treadway Commission) principles. The COSO model ensures that control environment, risk assessment, control activities, information and communications as well as monitoring activities altogether are at the core of an effective internal control system. By implementing

these key activities the aims of internal control system are achieved – efficiency of the Group operations, credibility of information disclosed in reports and compliance with applicable legislation and other regulations.

### Control Environment

Control environment of Latvenergo Group is based upon the values of the Group. The management of the Group promotes business activities on principles of good faith and compliance with ethical norms as well as takes necessary actions in order to prevent risks of corruption and fraudulent activities. The Group promotes employee awareness of internal controls and continuously improves them. Specific responsibilities for creating, developing and implementing the controls are clearly set in all of the organizational levels. In order to ensure achievement of targets in most efficient and effective way, the Group continuously develops the competencies of its employees.

### Risk Assessment

In order to adapt to the ever-changing business environment and new trends in market development Latvenergo Group constantly improves the risk management process. More information on the Group's risk management process and the most significant risks of the Group is provided in this Section's subsection "Risk Management".

### Control Measures

The general level of control (policies, instructions, explanations of the processes, etc.) is set and continuously improved at the Latvenergo Group, which is aimed to promote the achievement of strategy and goals of the Group. Similarly, to ensure the fulfilment of the goals set in the strategy of Latvenergo Group, the goals of the Group are developed and their fulfilment is monitored, while the annual Goals of the Group are cascaded down to individual targets for employees. At the same time for limitation of the most significant business risks Latvenergo Group regularly implements actions to improve controls.

### Information and Communication

Internal information and control systems of Latvenergo Group provide verified, accurate and reliable information for communication both internally and to the external stakeholders.

Latvenergo Group management pays a particular attention to ensuring employee awareness, regularly communicating long-term and short-term plans. Core channels of information exchange and communication are intranet, employee newsletter Latvenergo Vēstis (Latvenergo News), internal record-keeping systems, electronic communication, internal databases, employee forums, workshops, etc. To ensure feedback, the Group relies on internal opinion surveys, employee development interviews, and evaluation of competencies. Workgroups are established, delegating representatives with different skills, know-hows and

## Supervisory bodies

| Institution     | Objective   | Monitoring scope and tasks  | Reporting  |
|-----------------|---|---|--|
| Auditor         | To express an opinion on the compliance of the Group financial reports with the IFRS  | <ul style="list-style-type: none"> <li>audit of financial and sustainability reports</li> <li>evaluation of the validity of assessment of accounting principles and major management accounting estimates</li> </ul>  | Once a year, after the finalization of the consolidated financial statements, the Auditor reports to the Shareholders' Meeting   |
| Audit Committee | To oversee the preparation process of the Group financial reports and the operation of internal control systems, thus stimulating transparency in the company               | <ul style="list-style-type: none"> <li>supervision of the preparation of financial reports</li> <li>supervision of operations of the internal controls and risk management systems</li> <li>monitoring of activities of the Internal Audit and external auditor and implementation of the Fraud Risk Management Plan</li> </ul> | At least once a year, the Audit Committee reports on its activities and performance of tasks to the Shareholders' Meeting  |
| Internal Audit  | To evaluate and assist governance bodies and organisational units in improvement of the efficiency of risk management, internal controls and corporate governance processes | <ul style="list-style-type: none"> <li>evaluation of the efficiency of internal controls, risk management and corporate governance processes, preparation of recommendations for improvement and supervision of its implementation</li> </ul>   | Every quarter the Chief Internal Audit and Compliance Director reports to the Audit Committee about the audits performed and the status of implementation of audit recommendations |

competencies to ensure exchange of employee opinions and knowledge, raise employee motivation, and encourage their involvement in decision-making. Additionally, for the improvement in understanding the relevance of control activities and its practical application in the operations of the Group, as well as employees' responsibilities in the implementation of the controls, the Group trains its employees.

## Monitoring

Through constant improvement of the Group governance system the monitoring of management performance is carried out by the Audit Committee of Latvenergo AS and Internal Audit. The external auditor provides an opinion on the compliance of financial reports. All of the prior mentioned institutions are independent in their operations.

## Risk Management

Latvenergo Group risk management is aimed at timely identification and monitoring of the key factors adversely affecting Group operations, to ensure the achievement of its strategic goals and minimise the potential losses or harm to the reputation of the Group.

The Group has approved a Risk Management Policy which defines the fundamental principles for risk management within the Group.

The risk management process at Latvenergo Group provides for continuous risk identification, evaluation and management. Group risks may have an adverse effect on the achievement of its strategic goals, the financial situation, human health and life, or cause harm to the reputation. The most significant risks of the Group are consolidated in the Material Risk Register, analysed in detail and communicated to the Risk Management Committee, the Management Board of Latvenergo AS, the Audit Committee and the Shareholder. The Risk Management Committee is a designated risk management and monitoring body

established in the Group at the Management Board level of Latvenergo AS.

The Group assesses the risks while carrying out everyday operations as well as when engaging in new projects. The material risks identified by the Group are divided into four categories:

- *Strategic risks* are associated with matters of strategic importance for the Group, such as the development of the industry, new market entrants, and implementation of projects of strategic importance. The main risk management instruments for this category of risks are the monitoring of change and development trends in the energy sector and the political environment, participation in topicalities affecting the Group's operational aspects, as well as evaluation and implementation of the required changes;

- *Operational risks* include risks arising from the Group's operational specifics: energy generation, maintenance of power plants and ensuring of their functionality, energy supply and distribution. Operational risks are associated with loss of assets, threats to human health and safety, information technologies and other issues. Operational risks arise from imperfect or insufficiently effective processes and systems, employee errors or lack of competence, as well as damages to the equipment, or external events. Operational risk management is aimed at mitigating the negative impact of adverse effects. For this purpose, the Group continuously improves the internal control systems, maintenance and development plans, makes use of insurance services and takes other steps to minimise the operational risks;

- *Financial risks* are risks associated with the need for a capital-intensive industry to regularly attract additional funding (financial market, liquidity and financing risks). For minimisation of the financial risks, the Group uses financial instruments, diversify the borrowing sources as much as possible, and ensures a liquidity reserve for a period of at least 12 calendar months. Similarly,



tax, financial statement and reporting risks are also evaluated and monitored;

- **Legal and compliance risks** are risks arising from various rules and regulations issued by the EU and Latvian institutions. The main risk management instruments for this category risks are: monitoring of the changes and development trends in the legal environment affecting the Group's operational aspects, participation in the development process of new regulatory documents, and implementation of the required changes. The Group has developed and maintains internal operations compliance and control system to prevent any kind of abuse, improper or illegal

activities for personal gain. An important instrument for the management of this type of risks is employee training and control.

The Group controls the identified risks and keeps them as low as possible. The material risks of the Group are linked to the Internal Audit system, which allows for the use of risk assessments in the planning of Internal Audit activities.

Additional information about material risks of Latvenergo Group is available in the Base Prospectus of Latvenergo AS Programme for the Issuance of Notes, published on Latvenergo Group and Nasdaq Riga websites.

## Awards

Awards and recognitions received in 2015 affirm the responsible business practice, efficient and safe energy generation and distribution, care for the environment, quality of services, safe work environment, as well as best practice of stakeholder engagement.



### **The most valuable company in Latvia for the seventh year in a row**

For the seventh year in a row, Latvenergo AS has been acknowledged as the most valuable enterprise of Latvia on the Top 101 Most Valuable Companies of Latvia (*Latvijas vērtīgāko uzņēmumu TOP 101*) list compiled by Prudentia IBS and the Nasdaq Riga exchange in cooperation with Lursoft IT SIA and the Kapitāls magazine. According to the study, the value of Latvenergo AS in 2015 was EUR 1.1 billion. The study commended the corporate governance of Latvenergo AS, its transparency and quality of information disclosed to the public (90 points out of 100).

Latvenergo AS ranks six on the list of Top 10 Most Valuable Companies in the Baltics.



### **The highest category in the Sustainability Index of Latvia for the third year in a row**

2015 was the third year in a row when Latvenergo AS received the Platinum (highest) category from the Sustainability Index of Latvia, which assesses the sustainability of companies in all aspects of corporate social responsibility, based on international requirements. Latvenergo AS has participated in the Index for six years and was awarded the Silver category in 2010 and 2011, Gold category in 2012, and Platinum in 2013 and 2014.

At the CSR Idea Market conference held within the Sustainability Week on 10 June 2015, for the fourth year in a row Latvenergo AS received a Family-Friendly Company Certificate from the Ministry of Welfare of the Republic of Latvia. It reflects care about the families of the company's employees and customers, promoting loyalty to the company and improving its reputation.

For long-term cooperation with the trade union and the contribution to the social dialogue, Latvenergo AS also received the Free Trade Union Confederation of Latvia Cooperation Partner Award the "Big Acorn" (*Lielā ozolzīle*).



### **Corporate reputation leader in the electricity, gas and water supply sector**

The Latvian Corporate Reputation TOP organised by Nords Porter Novelli SIA, the Dienas Bizness newspaper, the Investment and Development Agency of Latvia (LIAA) and SKDS Marketing and Public Opinion Research Centre, listed Latvenergo AS as the leader in the electricity, gas and water supply sector for the fourth year in a row.



### Latvenergo AS: TOP 500 most stable company

At the ceremony honouring the largest, most profitable, most stable and most viable Latvian companies, organised in November 2015 by the Dienas Bizness newspaper, Lursoft IT SIA and LIAA, Latvenergo AS received the TOP 500 Most Stable Company award as the largest company in the energy industry of Latvia, and one of the most valuable and transparent companies in 2014. TOP 500 is an annual publication with a 20-year history of evaluating companies in Latvia in various industries for their financial performance, broken down by industry and key financial performance indicators (profit, EBITDA, long-term investments, etc.).

### Latvenergo AS Riga CHPPs: Environmental Excellence

At the end of 2015, both Riga CHPPs of Latvenergo AS received the Green Excellence Award, introduced by the State Environmental Service. The award is a confirmation that the facilities of Latvenergo AS comply with regulatory requirements in the highest possible level, and measures to mitigate the environmental impact of the generation processes are planned and in place.



### Contribution to the Latvian Presidency of the EU Council

In September 2015, Latvenergo AS received recognition from Ministry of Economics for the contribution to the Latvian Presidency of the Council of the EU. It was an acknowledgement of the assistance in the preparatory work for the conference of the EU Energy Ministers on the European Energy Union, and the Eastern Partnership Business Forum.

### Annually the Most Attractive Employer

In 2015, in the survey organised by the CV Market career portal, Latvenergo AS was recognized as the most attractive employer in Latvia for the fourth consecutive year. As the decisive factors for willingness to work at Latvenergo AS, most respondents emphasized the company's good image and reputation: a sustainable development-oriented, competitive and fair market leader with a recognised and prestigious brand.

In the Top Employer 2015 survey conducted by the online recruitment company CV-Online Latvia at the end of the year, Latvenergo Group was ranked as the most attractive employer in Latvia and the TOP employer in the industry sector for the fourth year in a row. The main reasons reported by those willing to work at Latvenergo Group include good image and reputation, motivating and competitive salaries, career development prospects, pleasant corporate culture, values, traditions and inspiring and professional management, colleagues, and good work environment.



The Latvian energy supply company Latvenergo AS was recognized as the most attractive employer in Latvia for the fourth year in a row also in a survey published by the recruitment and executive search company WorkingDay Latvia in March 2016.

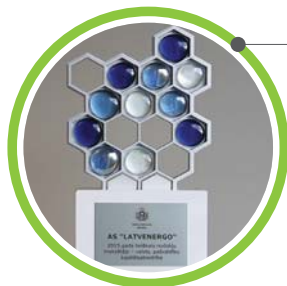
### **Acknowledgements for the erudition contest *Experiment***

At the finals of communication and public relation competition “Baltic PR Awards 2016” erudition contest *Experiment* of Latvenergo AS is awarded the first place at category Corporate Sustainability and Accountability. The contest encourages interest in exact science and annually about 200 teams around Latvia take part in it.



### **Namejs Prize 2015**

The Latvian Chamber of Commerce in Lithuania and the Embassy to the Republic of Latvia in Lithuania awarded to Elektrum Lietuva UAB the Namejs Prize 2015 in the nomination the Largest Tax Contributor to the Lithuanian Budget, for more than EUR 16 million contribution in taxes in 2014.



### **Largest tax payer among state and municipal companies**

Latvenergo AS is awarded in nomination “The Largest Taxpayer in the Country for 2015 Among State and Municipal Companies” at the Largest Tax Payers award ceremony organized by the State Revenue Service.

### **Excellent Employer’s DNA 2015**

In the competition “Excellent Employer’s DNA 2015”, the society “Good deeds” (*Labie Darbi*) awarded Sadales tīkls AS with the people’s choice award for education of the young generation on electricity safety and the “Don’t approach! In the game with electricity the loser will be YOU!” social responsibility project.





## 1.7 Corporate Governance Report

### Compliance with corporate governance principles of Nasdaq Riga

The Management Board of Latvenergo AS has evaluated the compliance of the company with *the Principles of Corporate Governance and Recommendations on their Implementation* approved by Nasdaq Riga AS on 1 June 2010. These principles prescribe the requirements with respect to the Shareholders' Meeting, the Management Board and the Supervisory Board as well as disclosure of information, internal control and risk management and remuneration policy of governing bodies.

Upon evaluating both the governance system of the company and its compliance with the principles in 2015, the Management Board of Latvenergo AS confirms that the company in all key material aspects has complied with all the principles of corporate governance, apart from those relating to the restrictions under the law

that, along with other requirements, provides that no supervisory board is established for state capital companies.

As of 2015, Law on Management of Public Persons' Capital Shares and Capital companies is applied to operations of the company, providing an opportunity to reinstate the Supervisory Board as a supervisory body from 1 January 2016, thus no restrictions will apply that might prohibit fulfilling all the principles of corporate governance specified by Nasdaq Riga AS.

Latvenergo AS Corporate Governance Report 2015 is publicly available on the Latvenergo website <http://www.latvenergo.lv> and the website of Nasdaq Baltic <http://www.nasdaqbaltic.com>. Detailed information on compliance with the corporate governance principles is presented in the Sections 1.5 "Group Governance" and 1.6 "Group Management". From overall 83 Nasdaq Riga corporate governance principles, 61 are complied fully, 22 are not applicable to company operations.

# Report of the Audit Committee

The Audit Committee of Latvenergo AS operates under the Commercial Law and Financial Instruments Market Law of the Republic of Latvia and the Rules of the Audit Committee approved by the Shareholder.

No restrictions have been imposed on our actions, and representatives of Latvenergo AS have ensured us with availability of the necessary information. We have informed the members of the Management Board of our opinions and related suggestions based on the work of the Audit Committee.

In 2015, the activities of the Audit Committee were focused on the following issues that have an impact on operations of the Group:

- recruitment of Chief Internal Audit and Compliance Director;

- supervision of the Fraud risk management plan execution;
- monitoring of internal audit and external auditor operations.

Having assessed the information and processes reviewed during the financial year 2015, nothing has come to our attention that make us to believe that internal controls of Latvenergo AS do not provide a reliable basis for the preparation of the 2015 Annual Report.

We submit the summary of our assessment to the Shareholders' Meeting of Latvenergo AS on the date of approval of Consolidated Annual Report 2015.

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**Torben Pedersen,**  
Chairman of the Audit Committee

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**Marita Salgrāve,**  
Member of the Audit Committee  
(Date appointed: 05.12.2015)

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**Svens Dinsdorfs,**  
Member of the Audit Committee



# 1.8 Stakeholder Engagement

G4-15 | **The Group responsibly addresses the stakeholders' needs**

AA 1000 Stakeholder Engagement Standard (SES), which sets the pattern of the best practice for quality stakeholder engagement, both at a strategic and operational level.

G4-21 | Latvenergo Group is the largest power supply service provider in the Baltic States. Its range of socially and economically essential services and the scale of its activities determine Latvenergo Group interaction with a wide range of stakeholders and the associated responsibilities. Latvenergo Group identifies its stakeholders throughout the entire power supply process and, being aware of the social, environmental and economic impact of its operations, responsibly addresses the stakeholders' needs.

Latvenergo Group engages with stakeholders on several levels:

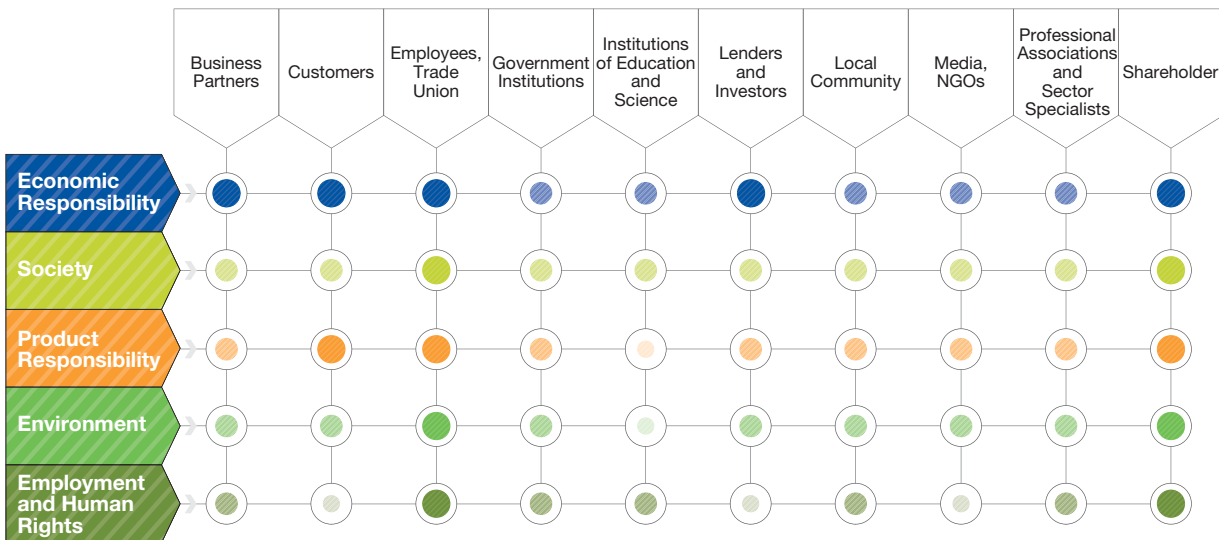
- consult – identification of current issues;
- negotiate – collective discussions;
- involve – exchange of opinion while acting independently;
- collaborate – joint decision-making and operation.

G4-27 | The stakeholders identified through internal and external discussions, consultations and workshops are grouped in the Stakeholder map. Stakeholders are evaluated based on their impact on Latvenergo Group operations and vice versa. The evaluation is carried out in all categories of the GRI: Economic Performance, Environmental Protection, Employment and Work Environment, Society, and Product Responsibility. Identification and grouping is carried out taking into account the GRI G4 Guidelines and the voluntary

In 2015, Latvenergo Group continued to improve stakeholder engagement in compliance with the AA 1000 SES standard and the GRI G4 Guidelines. In addition to the regular cooperation formats described in the table below, in 2015 the Group organised a stakeholder workshop to find out their opinion about the cooperation and aspects material to the sustainability of Latvenergo Group. The workshop led to over 50 recommendations for the improvement of operations, the most important being:

- control over the origin of energy resources and the share of renewables in the energy generation process;

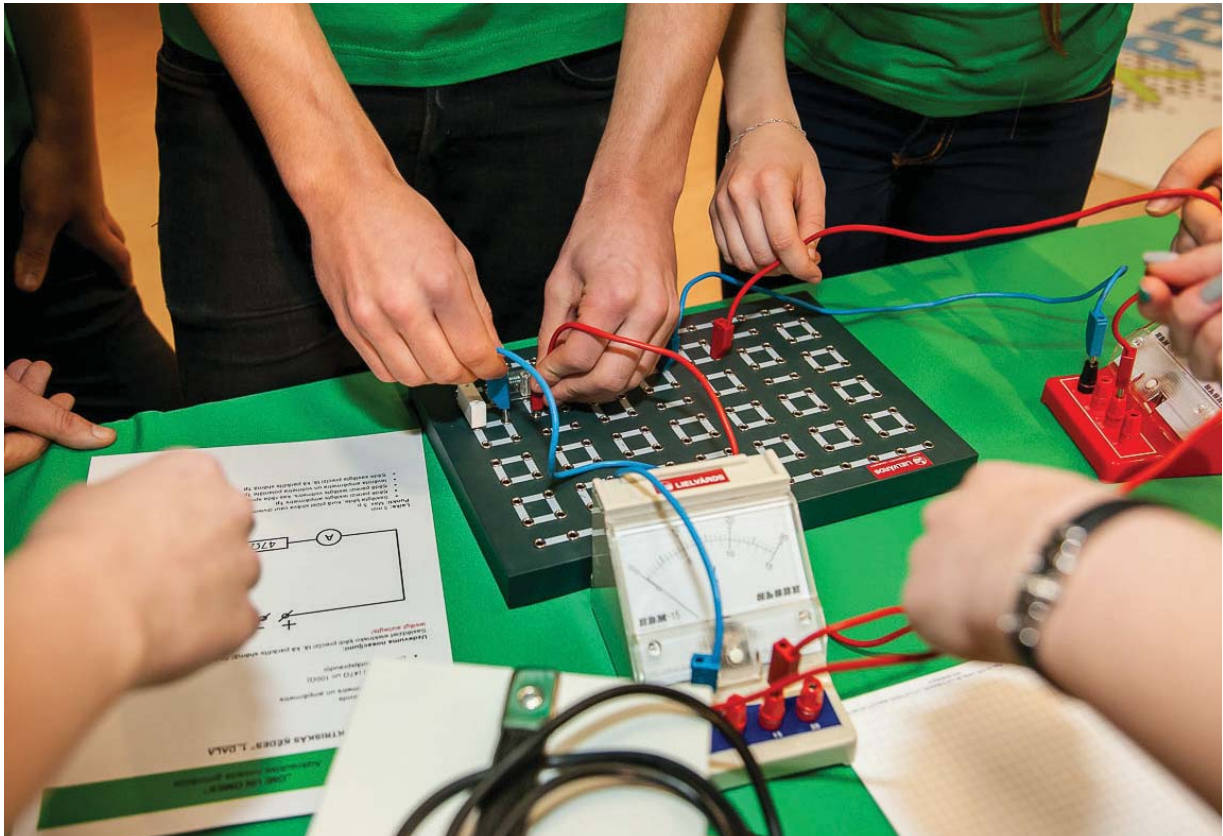
## Stakeholders of Latvenergo Group



- continuing education of employees and improvement of the work environment;
- promotion of best sustainability practice;
- continued cooperation with scientific and educational institutions;
- public awareness raising of electrical safety;
- personalised and operational customer services, availability of information and cooperation.

Overall, the Group is already implementing many of the recommendations received in its everyday work

processes, while those complying with its operational goals and not yet in place, such as further development of the resolution of customer problems during the first contact with the customer service and the development of a long-term plan for the improvement of the work environment, are scheduled for future implementation. For more information on the workshop and aspects relevant to the sustainability of the Group, see Section 1.9 “Materiality Assessment”.



| Stakeholder                                  | Representatives   | Material issues/ Sustainability aspects   | Engagement methods  |
|--|---|---|---|
| <b>Business Partners</b>                     | Construction companies and equipment suppliers, service providers, energy resource suppliers, energy generators and suppliers, transmission system operators (TSO), etc.  | <ul style="list-style-type: none"> <li>● Clear and transparent procurement tenders;</li> <li>● Electricity transmission and distribution;</li> <li>● Mandatory procurement (MP) of electricity and Subsidised Electricity Tax (SET);</li> <li>● Development of electricity interconnections;</li> <li>● Efficiency of energy generation facilities.</li> </ul>  | <p>The Group regularly informs its business partners about the ethical principles regarding contractors, maintains and regularly updates its Register of Qualified Tenderers, and invites partners to submit applications for the inclusion into its qualification system. The Group regularly surveys its current and potential business partners, defining areas for improvement. Business representatives were one of the respondent groups of the Corporate Reputation Study 2015 in the Baltics. The Group's subsidiary Sadales tīkls AS provides on its website up-to-date information about the market and services necessary for the electricity suppliers. In 2015, Latvenergo AS, as an electricity market player, discussed with the electricity TSOs of the Baltics "Terms, Conditions and Methodologies on Cross-Zonal Capacity Calculation, Provision and Allocation within the Baltic States and 3<sup>rd</sup> Countries".</p>  |
| <b>Customers</b>                             | Current and potential customers (households and legal entities)   | <ul style="list-style-type: none"> <li>● Electricity products, tariffs, pricing of related services;</li> <li>● Quality of the services provided;</li> <li>● Customer satisfaction with the Company, its services, service level, availability of information and its content;</li> <li>● Payment options and services;</li> <li>● Availability and efficiency of distribution services;</li> <li>● Reducing the frequency and duration of unscheduled power outages;</li> <li>● Transparent, fair and ethical marketing and communication practice;</li> <li>● Compliance with the requirements of regulatory acts and fair competition;</li> <li>● Emergency management plans.</li> </ul> | <p>Involve</p> <p>Electricity product offers of the Latvenergo Group are adjusted to customer needs. Information required by customers is regularly provided on the <a href="http://www.elektrum.lv">http://www.elektrum.lv</a> customer portal, in social networks, at Customer Service Centres and in other information channels. Latvenergo Group conducts annual customer satisfaction surveys and undertakes activities to increase customer satisfaction. The Group prepares Electricity Market Overviews and regularly sends them to business customers.</p>   |
| <b>Employees, Trade Union</b>                | Existing and potential employees, trade union <i>Energija</i>   | <ul style="list-style-type: none"> <li>● Collective Bargaining Agreement, occupational health and safety, rights and responsibilities of the employer and employees;</li> <li>● Productivity and motivation, competencies, remuneration and welfare of employees;</li> <li>● Data safety;</li> <li>● Availability and efficiency of distribution services;</li> <li>● Group contribution to the national economy.</li> </ul>  | <p>Negotiate and involve</p> <p>Latvenergo Group conducts annual employee opinion polls and employee quarterly performance assessments. The 2015 opinion poll comprised questions about aspects relevant to the sustainability of the Group, engaging the employees in defining the content of the Sustainability Report. During the annual career development interviews, employees and their managers discuss the achievement of the annual targets and further activities for improving employee competencies. In 2015, representatives of the Group had 21 meetings with the trade union on issues of mutual importance.</p>  |
| <b>Government Institutions</b>               | Ministry of Economics of the Republic of Latvia, the Public Utilities Commission (PUC), the Competition Council, Ministry of Environmental Protection and Regional Development, the Procurement Monitoring Bureau (PMB), et al. | <ul style="list-style-type: none"> <li>● Development of Latvian and the EU energy policies and regulatory provisions;</li> <li>● Improvement of the regulatory environment;</li> <li>● Energy tariffs and their components;</li> <li>● Electricity and thermal energy generation from renewable energy resources;</li> <li>● Emergency management plans;</li> <li>● Compliance with the requirements of regulatory acts, and fair competition;</li> <li>● Efficiency of the energy generation facilities.</li> </ul>  | <p>Consult and involve</p> <p>Latvenergo Group experts assist in the development of energy sector policy documents and legislative acts, and regularly give opinions for preparing national position statements regarding energy and environmental matters on the current agenda of the EU Council. Information about position statements prepared in 2015 is available under Section 2.2 "Society". In compliance with the procedures stipulated by legal acts, Latvenergo Group cooperates with the Competition Council, which focusses on the promotion of fair competition and ensuring of transparency in service provision. Latvenergo Group regularly provides information to the PUC about its operations and financial results. In 2015, the Group subsidiary Enerģijas publiskais tirgotājs AS submitted for PUC approval a calculation of the MP public service obligation (PSO) fee. In 2015, the Group cooperated with the PMB to introduce and promote the best procurement practice, and the PMB specialists organised a workshop for Group employees on the best practice of organising procurement procedures.</p> |
| <b>Institutions of Education and Science</b> | Academic institutions, institutions of higher, secondary and vocational education   | <ul style="list-style-type: none"> <li>● Educational programmes meeting the requirements of the labour market;</li> <li>● Content of educational materials for children and youth;</li> <li>● Contribution to the public welfare and CSR activities;</li> <li>● Involvement in the development of the energy sector policy;</li> <li>● Transparent, fair and ethical marketing and communication practice;</li> <li>● Availability of information.</li> </ul>   | <p>Collaborate</p> <p>In 2015, theoretical and practical training of specialists was continued in cooperation with the LUA and the RTU, with experts from the Group participating in study programmes as guest lecturers and in bachelor's and master's dissertation committees and guiding student visits at energy generation facilities and other sites. The Group annually organises graduation paper and scholarship competitions, and provides internship opportunities for students. In cooperation with the Latvian Academy of Sciences, it awards scientists for their achievements in the energy industry. In 2015, the Group supported the establishment of the Engineering School under the RTU, and the improvement of the laboratory for the RTU Faculty of Power and Electrical Engineering. Within social responsibility projects, the Group raises the awareness of secondary and vocational students of electricity safety and industrial heritage matters of the energy sector, encourages them to study physics, and provides the idea base and auxiliary materials for teachers.</p>                           |



|   |   |  |
|---|---|--|
| <p><b>Lenders and Investors</b></p> <p>Banks, international financial institutions, European Commission, bondholders</p>  | <p>Latvenergo Group's financial results, significant events, compliance with the terms of agreements;</p> <ul style="list-style-type: none"> <li>● Involvement in the development of the energy sector policy;</li> <li>● Compliance with the requirements of regulatory acts and fair competition;</li> <li>● Transparent, fair and ethical marketing and communication practice;</li> <li>● Customer satisfaction with the company, its services, service level, availability of information and its content;</li> <li>● Group contribution to the national economy.</li> </ul>   | <p>Consult and collaborate</p> <p>On the Latvenergo Group website, investors are provided with up-to-date information about the financial results and performance indicators, including quarterly publication of interim financial reports. Webinars about Latvenergo Group's financial results are organised since 2015. In 2015, Latvenergo AS initiated green bond offering programme. More information about green bonds is available under Annex "Report of Green Bonds".</p>   |
| <p><b>Local Community</b></p> <p>Residents of Latvia, local governments, residents living near the Group facilities</p>   | <ul style="list-style-type: none"> <li>● Latvenergo Group CSR activities;</li> <li>● Environmental protection, modernisation of generation facilities and electricity network infrastructure projects;</li> <li>● Provision of Latvenergo Group services and problem solving;</li> <li>● MP PSO fee.</li> </ul>   | <p>Consult, involve and negotiate</p> <p>The Group communicates with residents in the vicinity of the Group facilities and engages them in the resolution of current issues. In 2015, the Group organised public consultations regarding the environmental impact assessment of the Estonia-Latvia third power transmission network interconnection project.</p> <p>The opinion of Latvian society is regularly surveyed through various opinion polls, including the Group's Corporate Reputation Study 2015. The Group also organises a wide range of social responsibility activities, which are described in the Section 1.4 "Corporate Social Responsibility".</p> <p>In 2015, Latvenergo Group continued cooperation with local governments regarding issues such as power supply, environmental impact assessment for modernisation projects of the Group facilities, and the development of the regulatory environment for the energy sector by local government and state institutions.</p> |
| <p><b>Media, Non-Governmental Organisations (NGOs)</b></p> <p>Journalists, NGOs</p>                                       | <ul style="list-style-type: none"> <li>● Latvenergo Group operations and corporate governance;</li> <li>● Current issues of energy sector policies in Latvia and the EU;</li> <li>● MP process and MP PSO fee;</li> <li>● Latvenergo Group CSR activities;</li> <li>● Efficiency of the energy generation facilities;</li> <li>● Emergency management plans;</li> <li>● Electricity and thermal energy generation from renewable energy resources;</li> <li>● Occupational health and safety;</li> <li>● Availability and efficiency of distribution services.</li> </ul>   | <p>Consult and involve</p> <p>Latvenergo Group cooperates with national and regional media. Over 250 press releases were issued in 2015, and a number of media events and press conferences were organised, about the issue of green bonds, the introduction of smart meters and their possibilities, as well as the replenishment of the fish stocks in the Daugava River basin and investments in generation facilities and others. The Group regularly provides up-to-date information about its activities and answers questions from journalists on its own website and in the social media. Journalists were also one of the respondent groups of the Corporate Reputation Study 2015.</p> <p>Latvenergo Group also provides information related to its core business to NGOs, whose activities are focused on development of society and protection of individuals' rights.</p>   |
| <p><b>Professional Associations and Sector Specialists</b></p> <p>See below: "Associations, organisations and unions"</p> | <ul style="list-style-type: none"> <li>● Energy sector and related policies and the regulatory environment in Latvia and the EU;</li> <li>● Development trends and innovations in the energy sector;</li> <li>● Optimisation of electricity consumption for own use;</li> <li>● Electricity and thermal energy generation from renewable energy resources;</li> <li>● The amount of air pollution from generation of electricity and thermal energy;</li> <li>● Expenditure on environmental protection;</li> <li>● Compliance with environmental requirements;</li> <li>● Compliance with the requirements of regulatory acts, and fair competition;</li> <li>● Emergency management plans;</li> <li>● Transparent, fair and ethical marketing and communication practice;</li> <li>● Contribution to the national economy.</li> </ul> | <p>Consult and involve</p> <p>In 2015, the Group discussed with sector specialists the development issues of the energy industry and related sectors, and of the regulatory environment, at the "Towards sustainable energy supply in Latvia" energy forum, organised by the Dienas Bizness newspaper, and the "Efficiency. Development. Sustainability" energy forum organised by the LEITA news agency, as well as in other conferences, workshops and working groups. For more information, see Section "Associations, Organisations and Unions".</p>   |
| <p><b>Shareholder</b></p> <p>Ministry of Economics of the Republic of Latvia</p>  | <ul style="list-style-type: none"> <li>● Latvenergo Group strategy, governance, investments and performance;</li> <li>● Compliance with the requirements of regulatory acts and fair competition;</li> <li>● Involvement in the development of the energy sector policy;</li> <li>● Group contribution to the national economy;</li> <li>● Efficiency of the energy generation facilities;</li> <li>● Electricity and thermal energy generation from renewable energy resources and increasing of its share;</li> <li>● Contribution to the promotion of public welfare and CSR activities;</li> <li>● Emergency management plans.</li> </ul>   | <p>Collaborate</p> <p>Information about the number of Shareholders' Meetings and major decisions passed in 2015 is available in the Section 1.5 "Group Governance".</p>  |

## Associations, Organisations and Unions

Latvenergo Group cooperates with national and international associations and professional organisations to ensure representation of its interests in the development of national and international policy

documents and legal acts and standards, and to receive up-to-date information on the latest developments in energy and related industries.

### National associations and professional organisations

#### Latvian Association of Power Engineers and Energy Constructors (LAPEEC)



Participation in the LAPEEC provides for a possibility for the Group to get involved in the evaluation and development of legal acts, policy documents and standards for electrical power engineering and energy construction, organisation of staff certification and training programmes, conduction of scientific research and organisation of scientific and technical events related to the electrical power engineering, and cooperation with educational institutions specialising in electricity power engineering, including in the accreditation of study programmes.

In 2015, Latvenergo Group representatives regularly participated in LAPEEC meetings to ensure exchange of opinion on topical issues of the energy sector and LAPEEC position, including on Energy Sector Development Guidelines 2015–2020.

#### Latvian Association of Large Dams



The Association membership ensures exchange of information about technical, economic, environmental and social aspects of dams, innovations, and safety issues. The Association is represented at the International Commission on Large Dams (ICOLD). In 2015, representatives of the Association participated at the 25th ICOLD congress in Stavanger, Norway, and continued work on the ICOLD Dam Safety Committee.

#### Latvian Association of Heat Supply Companies (LAHC)



The LAHC provides Latvenergo Group with current information about district heating and cogeneration, generation of thermal energy from renewable sources, and other topical issues of sector developments, and represents the interests of the Group at state and local government institutions.

In 2015, the Group's specialists continued participation in the preparation of LAHC position statements on draft policy documents and legal acts on topical issues of the sector, including on the draft Law on Energy Efficiency aimed at increasing the end-use energy efficiency by imposing on traders an energy efficiency service obligation.

#### Latvian Chamber of Commerce and Industry (LCCI)



The LCCI is a member of the Association of European Chambers of Commerce and Industry and of the International Chamber of Commerce. The LCCI represents the interests of its members, including those of Latvenergo Group, in drafting policy documents and legislation specific to business activity in general and the energy sector by state and local government institutions.

#### Employers' Confederation of Latvia (ECL)



Latvijas Darba devēju konfederācija

Participation in the ECL ensures representation of Group interests while drafting policy documents and legislation on labour law and labour protection, and fosters the development of economic, educational and social policies favourable to business development.

In 2015, Latvenergo Group representatives continued their involvement in opinion drafting and the ECL Platform for Energy and Environment, and participated in ECL working groups, competitions, conferences and workshops.

#### Institute for Corporate Sustainability and Responsibility



In 2015, Latvenergo Group representatives continued participation in the Sustainability Index of Latvia, conducted by the Institute for Corporate Sustainability and Responsibility. The Index is an internationally recognised methodology for evaluating corporate sustainability and responsibility.

In 2015, the Group participated in the Sustainability Week, organised by the Institute, including the CSR Idea Market conference, and provided information on how to improve the energy usage habits of customers to achieve higher efficiency in the Responsible Ideas Catalogue.

#### World Energy Council, Latvian National Committee (WEC LNC)



Pasaules Enerģijas padomes Latvijas Nacionālā komiteja

Latvenergo Group representatives actively participate in the work of WEC LNC, particularly on issues related to national electricity policy and strategy. Participation in the WEC LNC provides the opportunity to receive up-to-date information about the research, extraction, transport, transformation and efficient use of energy resources both on a national and international scale.

On 15 October 2015, the participants of the enlarged Board Meeting of WEC LNC, LAPEEC and the National Confederation of Energy discussed the topical issues of Energy Sector Policy in Latvia. Latvenergo Group informed about the progress with coordination of the draft "Energy Sector Development Guidelines 2015–2020", specified by the Ministry of Economics.

## International organisations and unions

### The Baltic Institute of Corporate Governance (BICG)



Latvenergo Group is an active BICG member since the very onset of its operations, engaging in the activities and training and assisting with the development of the corporate governance guidelines for Baltic companies. With the launch of the BICG Latvia Office in August 2015, the Group has become a Development corporate member of BICG, thereby promoting the development of best corporate governance practice in Latvia.

At the BICG, Latvenergo Group management gains deeper insights into the best governance practices and communicates the readiness of the Group to implement these practices. Management Board Members of Sadales tīkls AS participated in BICG corporate governance training in 2015. BICG workshops on good corporate governance were held in 2015, where Latvenergo Group also shared its knowledge.

### Union of the Electricity Industry (EURELECTRIC)



EURELECTRIC represents the interests of the electricity industry on an international scale. Participation of Latvenergo Group representatives in the Union is ensured by the LAPEEC, a member of EURELECTRIC, on the basis of a representation agreement. Participation in EURELECTRIC gives Latvenergo Group access to information on the latest developments in the energy industry and ensures participation in the drafting of the EU policy documents, legislation, EURELECTRIC research papers and positions.

More information about the participation of Latvenergo Group specialists in drafting of various EURELECTRIC positions in 2015 is available in Section 2.2 "Society".

### Organization for Economic Cooperation and Development, (OECD), Business and Industry Advisory Committee (BIAC)



The BIAC is involved in the shaping of OECD policies and provides members with up-to-date information about the business development initiatives of the OECD. Representation on the BIAC enables Latvenergo Group to receive information and participate in discussions and decision-making in business development matters of international importance.

In 2015, Latvenergo Group participated in the OECD Global Forum on Responsible Business Conduct, discussing the long-term vision of responsible business conduct for multinational enterprises and the role of national contact points. During the year under review, Latvia's OECD accession negotiations were continued.

### Technical Association for Power and Heat Generation VGB PowerTech e.V



Representation in the Association ensures information availability to the Latvenergo Group about the best practices of power plants in the areas of exploitation, development and environmental protection, including the availability and safety of similar power plant equipment, and operational flexibility and efficiency increase solutions.

In 2015, the Group submitted and analysed the technical indicator database data of power plants represented at VGB, and also obtained several VGB standards. During the reporting year, experience was exchanged on hydropower plant management, exploitation, renovation and environmental protection issues.

### European Distribution System Operators' Association for Smart Grids



Representation in the Association ensures an up-to-date information to the Group subsidiary Sadales tīkls AS about the plans and activities of European distribution system operators in the area of smart grids, as well as competencies in the selection and implementation of smart grid technologies.

## Commitments to External Initiatives

In addition to the provisions of the applicable legislation, Latvenergo Group complies in its operations with the requirements of international standards.

Certified management systems have been introduced and integrated in Latvenergo AS Generation Segment and Sadales tīkls AS, covering Environmental Management, Quality Management (in the Generation Segment, Project Management has been additionally introduced and certified within the Quality Management System) and Labour Protection areas. An accredited certification company audits and certifies the compliance of the above-mentioned systems with the requirements of ISO 14001:2004, ISO 9001:2008, OHSAS 18001:2007 international standards. Latvijas elektriskie tīkli AS, in turn, has certified and maintains the Quality Management System in compliance with

ISO 9001:2008 requirements. In 2015, in compliance with the requirements of the EU Energy Efficiency Directive (2012/27/EU), the Environmental Management System of Latvenergo AS Generation Segment was complemented with an energy assessment process.

The energy management principles are also followed in the operations of Latvenergo AS Energy Efficiency Centre. In 2015, the Energy Efficiency Centre introduced a certified energy management system in compliance with the international ISO 50001:2011 standard.

In cooperation with stakeholders, Latvenergo Group voluntarily integrates in its operations activities to improve public welfare and the environmental situation, following the principles of social responsibility under the voluntary ISO 26000 standard and principles under the AA 1000 SES.



# 1.9 Materiality Assessment

G4-18 **Greater stakeholder engagement**  
 G4-19 **in the process of defining the content**  
 G4-20 **of the report**

G4-21 The content of Latvenergo Group Sustainability Report is based on the material aspects of the areas of economic performance, environmental protection, employment and work environment, human rights, society, and product responsibility, in compliance with GRI G4 Guidelines and the materiality assessment methodology developed by the Group. Defining the content of the report in 2015 was subject to enhanced engagement of the Group management and stakeholders. The process can be divided into three steps.

|   |
|---|
| <b>Step 1</b>   |
| Identification of the relevant sustainability aspects.<br>Identification of priority stakeholders.                |
| <b>Step 2</b>   |
| Determination of the most material sustainability aspects.  |
| <b>Step 3</b>   |
| Incorporation into a matrix and evaluation of the most material aspects. Selection of the disclosable indicators. |

## Step 1

The content determination process of the Sustainability Report was started with the compilation of the list of the sustainability aspects potentially relevant to Latvenergo Group operations and important for both the Group and its stakeholders. The list was based on the following sources of information:

- GRI G4 Guidelines;
- GRI Electric Utilities Sector Disclosures;
- Information disclosed by similar companies operating in the energy sector;
- Latvenergo Group strategy and policies;
- Information disclosed in previous Sustainability Reports;
- Scrutiny of Group communication;
- Stakeholder opinion, etc.

A list of aspects potentially material to the sustainability of Latvenergo Group was drawn in the areas of environmental protection, employment and work environment, human rights, society, and product responsibility. An assessment was made regarding the

aspects that are consistent with the Group's operations and those meeting stakeholder's expectations, and aspects that could be combined in order to facilitate the evaluation of their significance. A total of 27 aspects were identified as relevant to Latvenergo Group operations (see the Materiality Matrix on page 45).

Latvenergo Group priority stakeholders in each sustainability area were identified through Group management surveys and assessed by responsible managers of the relevant areas.

## Step 2

Group manager surveys were carried out and working groups organised to identify the most material sustainability aspects for the Latvenergo Group.

A workshop was organised for priority stakeholders to find out their views not only about material aspects to the Group's sustainability but also about the previous cooperation and needed improvements for the Group. About 70 stakeholder representatives were invited to the workshop, representing all the priority stakeholder groups of Latvenergo Group. During the workshop, the stakeholders were invited to evaluate the materiality of each pre-selected aspect on the scale of not material to very material. In the following stage of the workshop, participants were asked to work in groups and express ideas and suggestions regarding ways to improve the Group's sustainability in the most material aspects. The discussion results of the working groups were revealed and discussed in a panel discussion.

Furthermore, the opinions of all Group employees were determined via the annual survey, which comprised questions about material aspects to the Groups sustainability.

## Step 3

Compiling the results of the stakeholder workshop and employee opinion survey with those of the Group management survey and the working groups, a materiality matrix of sustainability aspects was drawn up, which has been assessed and approved by the top management of Latvenergo Group.

One axis of the materiality matrix reflects subjects that are most important to the stakeholders, while the other – the importance to Latvenergo Group management. The matrix comprises 27 sustainability aspects identified and relevant to the Latvenergo Group. The materiality matrix is divided into three parts: the most, medium and least material. Nine aspects were evaluated as being

the most material, rated as such by both stakeholders and the Latvenergo Group. The majority of those are “Society” aspects, “Efficiency of energy generation facilities” from the “Economic Performance” category is the most material. Twelve aspects were recognised as being of medium materiality and six as being least material.

This report does not include aspects rated as the least material. During the assessment of the most material aspects, *Biodiversity*, one of the fundamental principles of Latvenergo Group Environmental Policy, was included as an additional disclosable aspect. Latvenergo Group has obtained assurance that certain stakeholders would appreciate information about the Group’s contribution to the protection of biological diversity, especially regarding such issues as the protection of white storks and the replenishment of fish

stocks in the Daugava River basin. Leading to a total of 22 sustainability aspects being disclosed in the Report.

After an assessment of the disclosable aspects according to GRI G4 Guidelines, in cooperation with the responsible managers of the respective areas, the disclosable indicators corresponding to those aspects were identified. Overall, the Report discloses information about 22 sustainability aspects and 33 Specific Standard Disclosures indicators significant for Latvenergo Group operations (see the Table of GRI Indicators on page 93). While preparing information to be disclosed in the Report, the materiality of each aspect to Latvenergo Group companies and stakeholders was evaluated and taken into account (see Section 1.8 “Stakeholder Engagement” and Annex “Materiality of Sustainability Aspects and Conformity to GRI Aspects”).

### Materiality Matrix

#### Economic Performance

- 1 Efficiency of generation plants
- 3 Contribution to the economy
- 20 Support received from state

#### Society

- 2 Emergency planning
- 4 Public policy making
- 7 Compliance and fair business
- 16 Impact on local communities
- 21 Community contribution

#### Product Responsibility

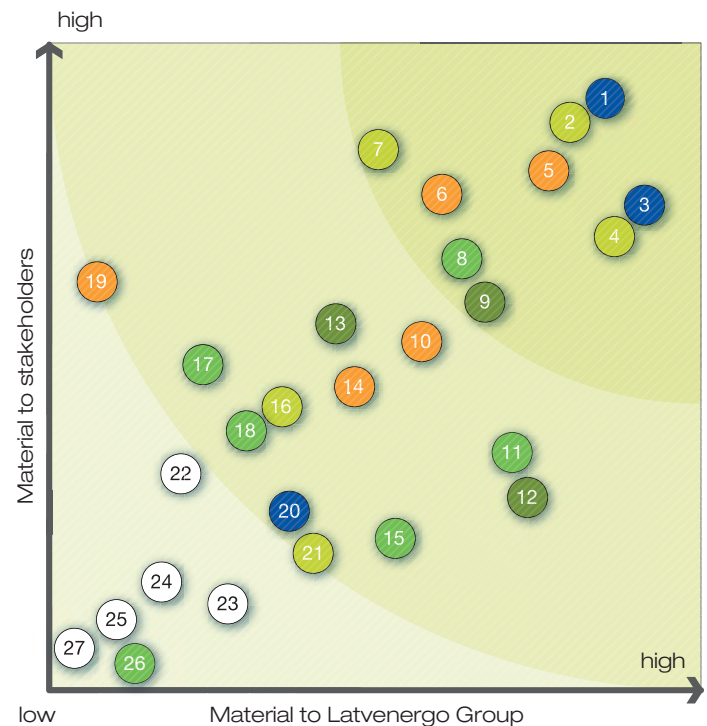
- 5 Availability and efficiency of distribution system
- 6 Customer satisfaction
- 10 Data security
- 14 Information availability
- 19 Fair marketing communication

#### Environmental Protection

- 8 Resource consumption in production
- 11 Environmental compliance
- 15 Air pollution
- 17 Energy consumption
- 18 Renewable energy
- 22 Waste and waste water
- 24 Environmental protection expenditure
- 26 Biodiversity

#### Employment and Work Environment

- 9 Health and safety
- 12 Workplace compliance
- 13 Employee development
- 23 Human rights and workplace diversity
- 25 Work-life balance
- 27 Employee involvement and freedom of association





# 1.10 Description of Operating Segments

G4-13

## Sustainable development in all operating segments

EU1

Latvenergo AS and subsidiaries Elektrum Eesti OÜ and Elektrum Lietuva UAB. The functions of public trader are performed by the subsidiary Enerģijas publiskais tirgotājs AS.

EU2

The activity of Latvenergo Group is organised along three operating segments: generation and supply, distribution, and lease of transmission system assets.

The distribution segment provides electricity distribution services in Latvia through Sadales tīkls AS – the largest distribution system operator in Latvia.

EU3

The generation and supply segment comprises generation of electricity and thermal energy, ensured by Latvenergo AS and Liepājas enerģija SIA, as well as electricity supply (retail and wholesale) operations in the Baltic States carried out by

The lease of transmission system assets segment is ensured by Latvijas elektriskie tīkli AS, the owner of the transmission system assets, which leases them to the transmission system operator Augstsprieguma tīkls AS.

EU4

## 1.10.1 Generation and Supply

### Successful operations in a challenging market environment

Generation and supply is the largest operating segment of the Group both by revenue and by assets. Activities within this segment include supply of generated and procured electricity to retail customers in the Baltics, wholesale activities (mostly done on the Nord Pool exchange), and generation and supply of thermal energy for district heating purposes in Riga and Liepaja. The majority of the generation and supply segment revenues are unregulated, while the tariff-regulated operational revenues comprise revenues from:

- generation of electricity (remuneration for the installed capacity) and thermal energy at Riga combined heat and power plants (CHPPs);
- generation of electricity and thermal energy at Liepaja generation facilities and small plants (Ainazi wind power plant (WPP) until 1 October 2015, and Aiviekste hydropower plant (HPP)).

Latvenergo Group is the largest electricity supplier in the Baltics with approximately 1/3 of the Baltic market in 2015. In 2015, the total amount of electricity supplied in retail and wholesale (including auxiliary consumption) constituted 9,963 GWh, 79% of which were supplied to retail customers. In 2015, 61% or 4,782 GWh of the energy supplied by Latvenergo Group in retail was *green energy* – electricity generated from non-fossil renewable resources, such as hydropower, wind power,

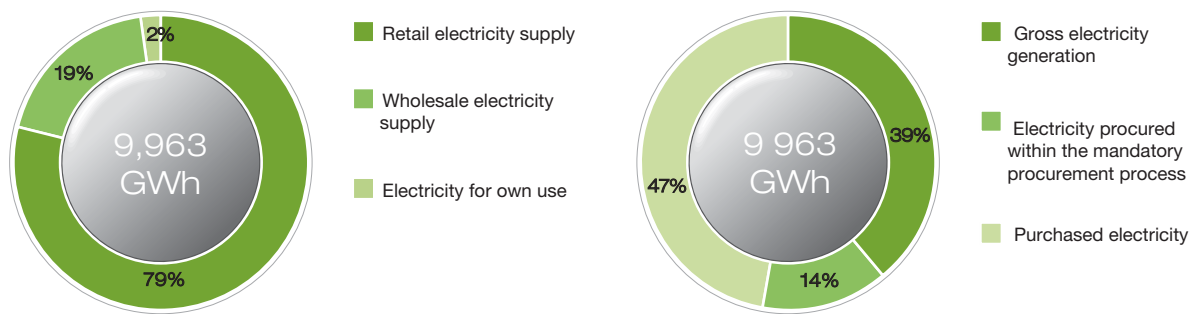


biomass, biogas etc. It includes both energy generated at Latvenergo Group power plants and that procured from other generators on the Nord Pool electricity exchange or in bilateral transactions.

In 2015, Latvenergo Group power plants generated 3,882 GWh or 39% of total electricity supply and approximately half of it was generated from renewable sources. The rest of electricity was mainly procured on the Nord Pool electricity exchange and within the framework of mandatory procurement.

The generation capacity of Latvenergo Group also ensures electricity supply support services, such as provision of emergency back-up capacity and supply of regulating electricity to TSOs, as well as supply of balancing electricity.

### Latvenergo Group electricity balance sheet 2015



### Latvenergo Group electricity balance sheet (2011 – 2015)

|   | Unit       | Method | 2011          | 2012          | 2013         | 2014          | 2015         |
|---|------------|--------|---------------|---------------|--------------|---------------|--------------|
| Retail electricity supply                   | GWh        | m/c    | 8,980         | 8,287         | 7,954        | 8,688         | 7,869        |
| Wholesale electricity supply*               | GWh        | m/c    | 2,283         | 1,886         | 1,588        | 1,562         | 1,907        |
| Electricity for own use                     | GWh        | m/c    | 173           | 177           | 215          | 201           | 188          |
| <b>TOTAL</b>                                | <b>GWh</b> |        | <b>11,436</b> | <b>10,350</b> | <b>9,757</b> | <b>10,451</b> | <b>9,963</b> |
| Gross electricity generation                | GWh        | m/c    | 5,285         | 5,077         | 4,854        | 3,625         | 3,882        |
| Electricity procured within the MP process* | GWh        | m/c    | 754           | 1,019         | 1,247        | 1,235         | 1,380        |
| Purchased electricity**                     | GWh        | m/c    | 5,397         | 4,254         | 3,656        | 5,590         | 4,701        |
| <b>TOTAL</b>                                | <b>GWh</b> |        | <b>11,436</b> | <b>10,350</b> | <b>9,757</b> | <b>10,451</b> | <b>9,963</b> |

\* excluding electricity generated by Latvenergo Group

\*\* including ancillary electricity services and electricity wholesale operations to reduce the price risk  
m – measured, e – estimated, c – calculated

## Generation

Generating facilities affirm their importance in a changing market environment

Latvenergo Group has a balanced energy generation portfolio, consisting of hydropower plants and highly efficient combined heat and power plants. Most of the electricity and thermal energy is generated at the three Daugava HPPs and two Riga CHPPs. Energy is also generated by generation facilities in Liepaja, Aiviekste HPP, Ainazi WPP and Kegums boiler house.

At the end of 2015, the total installed electrical capacity at Latvenergo Group generating facilities was 2,569 MW<sub>el</sub>. The installed thermal energy capacity of Latvenergo Group generation facilities was 1,844 MW<sub>th</sub>.

In 2015, the facilities of Latvenergo Group generated 3,882 GWh of electricity and 2,408 GWh of thermal energy.

## Installed electrical capacity of generation facilities (2011 – 2015)

|                | Unit                   | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|----------------|------------------------|--------|--------------|--------------|--------------|--------------|--------------|
| Daugava HPPs   | MW <sub>el</sub>       | e      | 1,536        | 1,536        | 1,536        | 1,536        | 1,536        |
| Riga CHPPs*    | MW <sub>el</sub>       | e      | 806          | 806          | 1,025        | 1,025        | 1,025        |
| Liepaja plants | MW <sub>el</sub>       | e      | 4            | 6            | 6            | 6            | 6            |
| Small plants   | MW <sub>el</sub>       | e      | 1            | 1            | 2            | 2            | 2            |
| <b>TOTAL</b>   | <b>MW<sub>el</sub></b> |        | <b>2,347</b> | <b>2,349</b> | <b>2,569</b> | <b>2,569</b> | <b>2,569</b> |

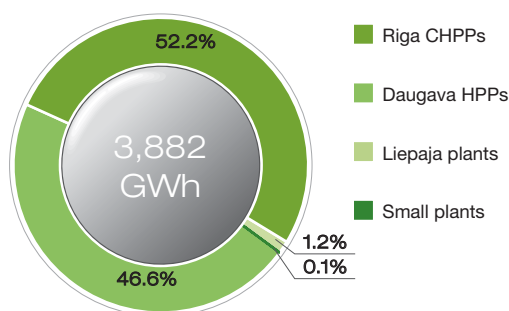
\* installed capacity, when Riga CHPPs is in condensation mode  
m – measured, e – estimated, c – calculated

## Installed thermal energy capacity of generation facilities (2011 – 2015)

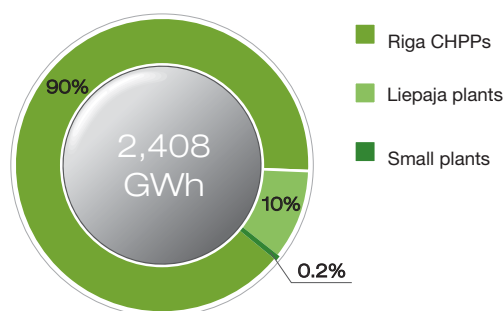
|                | Unit                   | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|----------------|------------------------|--------|--------------|--------------|--------------|--------------|--------------|
| Riga CHPPs     | MW <sub>th</sub>       | e      | 1,840        | 1,840        | 1,617        | 1,617        | 1,617        |
| Liepaja plants | MW <sub>th</sub>       | e      | 198          | 208          | 236          | 223          | 223          |
| Small plants   | MW <sub>th</sub>       | e      | 4            | 4            | 4            | 4            | 4            |
| <b>TOTAL</b>   | <b>MW<sub>th</sub></b> |        | <b>2,042</b> | <b>2,052</b> | <b>1,857</b> | <b>1,844</b> | <b>1,844</b> |

m – measured, e – estimated, c – calculated

## Electricity generation in 2015



## Thermal energy generation in 2015



## Electricity generation (2011 – 2015)

|                | Unit       | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|----------------|------------|--------|--------------|--------------|--------------|--------------|--------------|
| Daugava HPPs   | GWh        | m      | 2,823        | 3,627        | 2,852        | 1,925        | 1,805        |
| Riga CHPPs     | GWh        | m      | 2,425        | 1,409        | 1,957        | 1,648        | 2,025        |
| Liepaja plants | GWh        | m      | 33           | 37           | 43           | 48           | 48           |
| Small plants   | GWh        | m      | 4            | 4            | 3            | 4            | 3            |
| <b>TOTAL</b>   | <b>GWh</b> |        | <b>5,285</b> | <b>5,077</b> | <b>4,854</b> | <b>3,625</b> | <b>3,882</b> |

m – measured, e – estimated, c – calculated

## Thermal energy generation (2011 – 2015)

|                | Unit       | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|----------------|------------|--------|--------------|--------------|--------------|--------------|--------------|
| Riga CHPPs     | GWh        | m      | 2,315        | 2,446        | 2,305        | 2,308        | 2,175        |
| Liepaja plants | GWh        | m      | 248          | 261          | 257          | 248          | 229          |
| Small plants   | GWh        | m      | 5            | 5            | 5            | 5            | 4            |
| <b>TOTAL</b>   | <b>GWh</b> |        | <b>2,568</b> | <b>2,712</b> | <b>2,566</b> | <b>2,560</b> | <b>2,408</b> |

m – measured, e – estimated, c – calculated



## Daugava hydropower plants

Latvenergo Group generates a large part of electricity at three largest Daugava HPPs in Latvia, ensuring an environmentally friendly way of electricity generation, since they operate on water – a renewable energy resource.

Although the installed capacity of generation facilities at hydropower plants is high, their ability to generate electricity depends on the water inflow in the Daugava River. Daugava HPPs allow for accumulating water and generating electricity when demand is high and prices increase. While during the flooding season, which lasts for about one or two months, Daugava HPPs operate at full capacity. Water inflow in the Daugava River during

the spring flooding may more than 10 times exceed the water inflow during low water periods (mainly in summer). During the flooding season Latvenergo Group can cover the entire customer demand for electricity as well as export the excess.

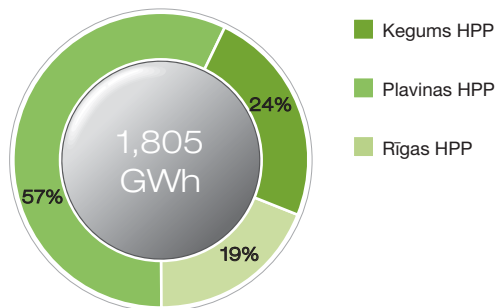
In 2015, Daugava HPPs in total generated 1,805 GWh of electricity, which constitutes 47% of the total electricity output at the Group. The amount of electricity generated was 6% lower compared to the previous year. In 2015, the electricity generated at the Daugava HPPs was considerably below the long-term average electricity generation volume which is explained by the lowest inflows in the Daugava River since 1976.

## Electricity generation at Daugava HPPs (2011 – 2015)

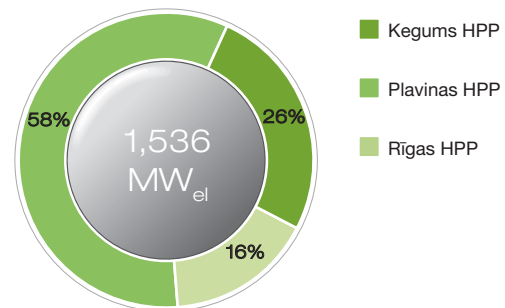
|              | Unit       | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|--------------|------------|--------|--------------|--------------|--------------|--------------|--------------|
| Kegums HPP   | GWh        | m      | 532          | 702          | 532          | 376          | 350          |
| Plavinas HPP | GWh        | m      | 1,621        | 2,067        | 1,640        | 1,089        | 1,022        |
| Riga HPP     | GWh        | m      | 670          | 858          | 679          | 460          | 433          |
| <b>TOTAL</b> | <b>GWh</b> |        | <b>2,823</b> | <b>3,627</b> | <b>2,852</b> | <b>1,925</b> | <b>1,805</b> |

m – measured, e – estimated, c – calculated

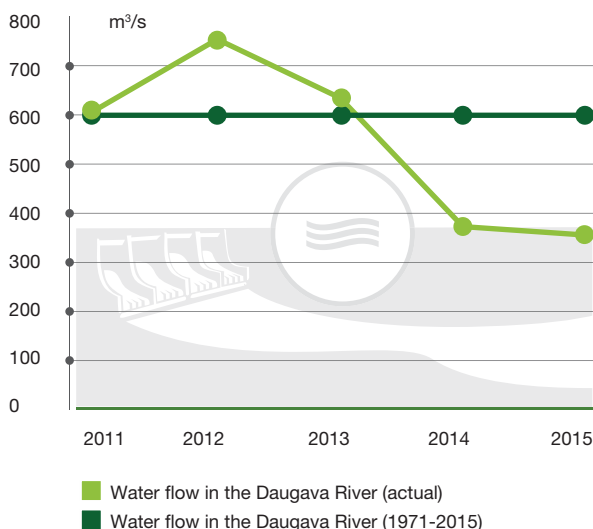
## Electricity generation at Daugava HPPs in 2015



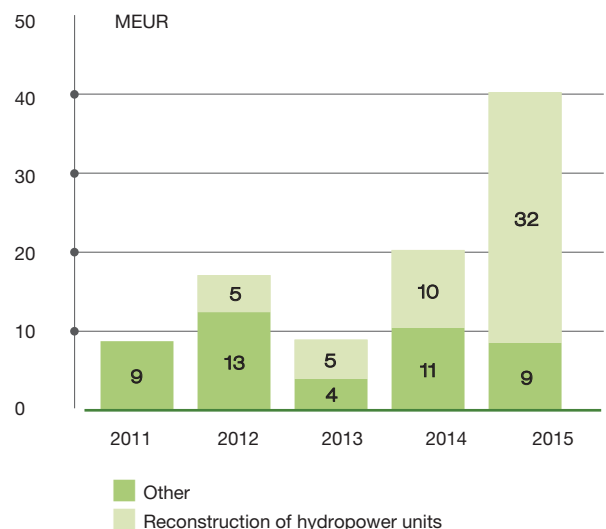
## Electricity generation at Daugava HPPs in 2015



## Water flow in the Daugava River (2011 – 2015)



## Investments in Daugava HPPs (2011 – 2015)



### Daugava HPPs construction chronology

Kegums HPP, built in 1936-1939 and renovated in 1945 – 1947, is the oldest Daugava HPP with initial installed capacity of 72 MW. Currently the total installed capacity of Kegums HPP is 240 MW, with 168 MW installed in 1979 by adding three new hydropower units.

Plavinas HPP is the largest hydropower plant in the Baltics and one of the largest in the EU in terms of installed capacity. The power plant started operating in 1968 with ten hydropower units, with the capacity totalling 825 MW at the time. From 1991 to 2001, six hydropower units were reconstructed, and as a result the installed capacity reached 869 MW.

The reconstruction process of the hydropower units continued from 2007 to 2010, and three hydropower units were upgraded, increasing the installed capacity of the plant to 894 MW. With the reconstruction of the hydropower units, the efficiency ratios of the plant have improved.

Riga HPP, with 6 hydropower units and a total capacity of 402 MW, was commissioned in 1974. Plavinas HPP and Riga HPP can also operate in synchronous compensator mode (adjusting the voltage in high-voltage electric networks), allowing the transmission system operator to ensure a certain voltage quality.



### Investments

Latvenergo Group continues to gradually reconstruct the hydropower units at Daugava HPPs. The main purpose of the reconstruction projects is to replace the outdated hydro turbines and increase the installed capacity, efficiency rate and annual electricity output to ensure reliable, efficient, sustainable and competitive operation of the Daugava HPPs within the entire power supply system and liberalised electricity market.

Out of the twenty-three Daugava HPP hydropower units, twelve are already modernised. The process of the hydropower unit reconstruction might be completed in 2022, and it is expected that the total reconstruction costs of the 11 hydropower units that have not been reconstructed yet will exceed EUR 200 million. In 2013, an agreement was signed on the reconstruction of two hydropower units of Plavinas HPP; the works were started in spring 2015, and will be completed in spring 2017. In 2014, in turn, an agreement was signed

on the reconstruction of three hydropower units of Kegums HPP; the works were started in spring 2015, and will be completed in spring 2018. The agreement on reconstruction of Riga HPP hydropower units was signed in spring 2015.

Increase in installed capacity and efficiency ratios of the hydropower units will ensure more efficient use of water – a renewable energy resource. Each additional megawatt hour (MWh) of electricity generated by Daugava HPPs contributes to the mitigation of climate change impacts – CO<sub>2</sub> emissions are reduced by 0.361 t, assuming that otherwise that energy would be generated at combined heat and power plants in a condensation mode.

In 2015, the total investments in Daugava HPPs assets amounted to EUR 40.5 million, including EUR 31.9 million for Daugava HPP hydropower unit reconstruction programme.

## Riga combined heat and power plants

The upgraded Riga CHPPs owned by Latvenergo Group are operated mostly in the highly efficient cogeneration mode to cover the demanded thermal volume. Consequently, generation of electricity at the combined heat and power plant depends largely on thermal energy consumption, which in turn depends on the climate conditions and duration of the heating season, as well as on the electricity market situation.

Riga CHPPs guarantee significant electricity base-load capacity that can almost fully cover the entire Latvian electricity consumption in circumstances where due to some factors electricity import from foreign countries is limited. In such cases, the plants can operate as stable base-load capacity facilities that will promptly substitute shortage of cross-border supply.

The Riga CHPPs use natural gas as the primary fuel, which is environmentally the friendliest type of fossil fuel available for power generation. In order to ensure

the reliability of thermal energy supply in emergency situations (emergency cut-offs), Riga CHPPs store back-up fuel reserves of diesel.

The amount of electricity generated by Riga CHPPs in 2015 was 2,025 GWh, which is a 23% increase compared to the previous year. Riga CHPPs operate efficiently and flexibly, adjusting the operational modes to market conditions. The amount of electricity generated by Riga CHPPs in 2015 was 52% of the total electricity output by Latvenergo Group.

In 2015, the amount of thermal energy generated by Riga CHPPs was 2,175 GWh or by 6% less compared to the previous year. Generation of thermal energy at Riga CHPPs depends on thermal energy demand, determined by the ambient temperature and duration of the heating season. Thermal energy generated by Riga CHPPs is supplied to Riga district heating company at regulated tariffs.

### Electricity generation at Riga CHPPs (2011 – 2015)

|              | Unit       | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|--------------|------------|--------|--------------|--------------|--------------|--------------|--------------|
| Riga TEC-1   | GWh        | m      | 655          | 328          | 406          | 487          | 464          |
| Riga TEC-2   | GWh        | m      | 1,770        | 1,081        | 1,550        | 1,161        | 1,561        |
| <b>TOTAL</b> | <b>GWh</b> |        | <b>2,425</b> | <b>1,409</b> | <b>1,957</b> | <b>1,648</b> | <b>2,025</b> |

m – measured, e – estimated, c – calculated

### Thermal energy generation at Riga CHPPs (2011 – 2015)

|              | Unit       | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|--------------|------------|--------|--------------|--------------|--------------|--------------|--------------|
| Riga TEC-1   | GWh        | m      | 788          | 976          | 772          | 966          | 978          |
| Riga TEC-2   | GWh        | m      | 1,527        | 1,470        | 1,533        | 1,342        | 1,197        |
| <b>TOTAL</b> | <b>GWh</b> |        | <b>2,315</b> | <b>2,446</b> | <b>2,305</b> | <b>2,308</b> | <b>2,175</b> |

m – measured, e – estimated, c – calculated

### Riga CHPP construction chronology

The first combined heat and power plant in Riga (Riga TEC-1) was built from 1954 to 1958 and fully reconstructed in 2005. At the power plant, two gas turbines, one steam turbine and three water boilers for district heating are operated. The installed electrical capacity of Riga TEC-1 is 144 MW<sub>el</sub>, while its thermal capacity is 493 MW<sub>th</sub>.

The second combined heat and power plant in Riga (Riga TEC-2) is the largest combined heat and power plant in Latvia. It was launched in 1973. The reconstruction of Riga TEC-2 was started in 2006, the construction of the first power unit was completed in late 2008, and the second power unit was commissioned in late 2013, thus finalising the reconstruction of combined heat and power plants of the Group. With the commissioning of the Riga TEC-2 second power unit, the exploitation of inefficient and environmentally unfriendly power units was suspended.

Currently Riga TEC-2 is the most efficient and up-to-date combined cycle power plant in the Baltics. Two combined-cycle gas turbine (CCGT) units and five water boilers are currently operating at the Riga TEC-2. With the commissioning of the second power unit, the electrical capacity of Riga TEC-2 in cogeneration mode reached 832 MW<sub>el</sub>, while the total thermal energy capacity of the two power units is 544 MW<sub>th</sub> in cogeneration mode. The full thermal energy capacity of Riga TEC-2, including water boilers, is 1,124 MW<sub>th</sub>.

The total installed electrical capacity of the Riga CHPPs in cogeneration mode is 976 MW<sub>el</sub> (1,025 MW<sub>el</sub> in condensation mode).

In 2015, the total investment in the Riga CHPP assets was EUR 15.0 million.

### Investments in Riga CHPPs (2011 – 2015)

|             | Unit | Method | 2011  | 2012  | 2013 | 2014 | 2015 |
|-------------|------|--------|-------|-------|------|------|------|
| Investments | MEUR | c      | 168.0 | 104.7 | 32.3 | 11.1 | 15.0 |

m – measured, e – estimated, c – calculated

## Liepaja plants

Latvenergo AS holds 51% share in Liepājas enerģija SIA. The company ensures generation, transmission, distribution and supply of thermal energy in the city of Liepaja, as well as generation of electricity in cogeneration mode.

The total installed thermal energy capacity of the Liepaja plants is 223 MW<sub>th</sub>, including 40 MW<sub>th</sub> from a renewable resource – wood chips. Installed electrical capacity totals 6 MW<sub>el</sub>. In 2015, Liepaja plants generated 229 GWh of thermal energy and 48 GWh of electricity. Over the past few years, co-financed by the EU

Cohesion Fund, new generation capacities were created, increasing the share of biomass consumption within the fuel balance at Liepaja plants: before 2010 it was 0%, but in 2015 the share of biomass was increased to 61%.

Due to the reconstruction of thermal energy transmission and distribution networks in Liepaja, thermal energy losses have also been reduced considerably over the past few years. The loss ratio decreased from 17.3% in 2011 to 14.3% in 2015.

## Liepaja plants (2011 – 2015)

|  | Unit             | Method | 2011 | 2012 | 2013 | 2014 | 2015 |
|--|------------------|--------|------|------|------|------|------|
| Installed electrical capacity of generation facilities     | MW <sub>el</sub> | e      | 4    | 6    | 6    | 6    | 6    |
| Installed thermal energy capacity of generation facilities | MW <sub>th</sub> | e      | 198  | 208  | 236  | 223  | 223  |
| Electricity generation                                     | GWh              | m      | 33   | 37   | 43   | 48   | 48   |
| Thermal energy generation                                  | GWh              | m      | 248  | 261  | 257  | 248  | 229  |
| Thermal energy losses                                      | GWh              | m/c    | 43   | 40   | 38   | 36   | 32   |
| Proportion of losses                                       | %                | c      | 17.3 | 15.5 | 15.4 | 15.2 | 14.3 |

m – measured, e – estimated, c – calculated

## Small plants

Generation facilities within the energy system of Latvenergo Group also include two small power plants – the Ainazi WPP with a capacity of 1.0 MW, and the Aiviekste HPP with a capacity of 0.8 MW.

The Kegums boiler house generates only thermal energy, with an installed thermal capacity of 4 MW. The Kegums boiler house is fuelled by woodchips.

In 2015, the total output at small plants was 3 GWh of electricity, which is approximately 0.1% of the total electricity output of the Latvenergo Group. While the total thermal energy output of Kegums boiler house in 2015 was 4 GWh.

# Electricity supply

Customer-oriented operations contribute to successful operation in the liberalized market

In 2015, Latvenergo Group has successfully retained its leadership in electricity supply in the Baltics. Latvenergo Group has a 32% share in the Baltic electricity market, which consumes a total of nearly 25 TWh.

A gradual liberalisation of the electricity market has been ongoing in the Baltics since 2007. As of 1 January 2015, the electricity market is open for households in Latvia, completing the electricity market liberalisation in the country. At the end of 2015, the majority of households chose Latvenergo as their electricity supplier. Currently, Lithuania is the only country in the Baltics with a regulated market for households. It is expected that this will not change till at least 2017.

Latvenergo Group retail electricity supply in the Baltics in 2015 was 7,869 GWh, or by 9% less compared to the previous year. The decrease in the amount of electricity supplied outside Latvia is primarily related to certain large customers switching to other electricity suppliers due to increased price competition. The decrease in Latvia, in turn, is related to changes in electricity procurement by the TSO: in 2015 Augstsprieguma tīkls AS procured electricity directly on the Nord Pool exchange.

The amount of electricity supplied outside Latvia represents almost 1/3 of the total retail electricity supply, reaching 2,539 GWh, which is by more than 40% more than the amount provided by competing electricity suppliers in Latvia.

In compliance with the Latvian legislation, in 2015 Latvenergo AS ensured electricity supply services to vulnerable consumers (poor or low-income persons, large families), compensating for the electricity

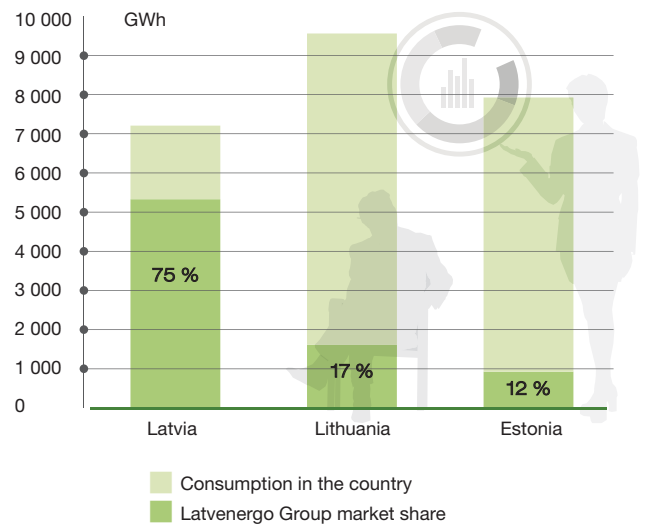
price increase. At the end of 2015, this support was used by more than 68 thousand customers. In 2015, the majority, or 98%, of all retail electricity supply by Latvenergo Group have been made at market price, and approximately 2% at the regulated tariff for vulnerable customers.

As a result of focused electricity trade activities, the number of Latvenergo Group customers in Estonia and Lithuania in 2015 increased by approximately 4%. At the same time, the number of corporate customers in the neighbouring countries increased by approximately 33%. The main focus outside Latvia was on the development of micro, small and medium sized company segments.

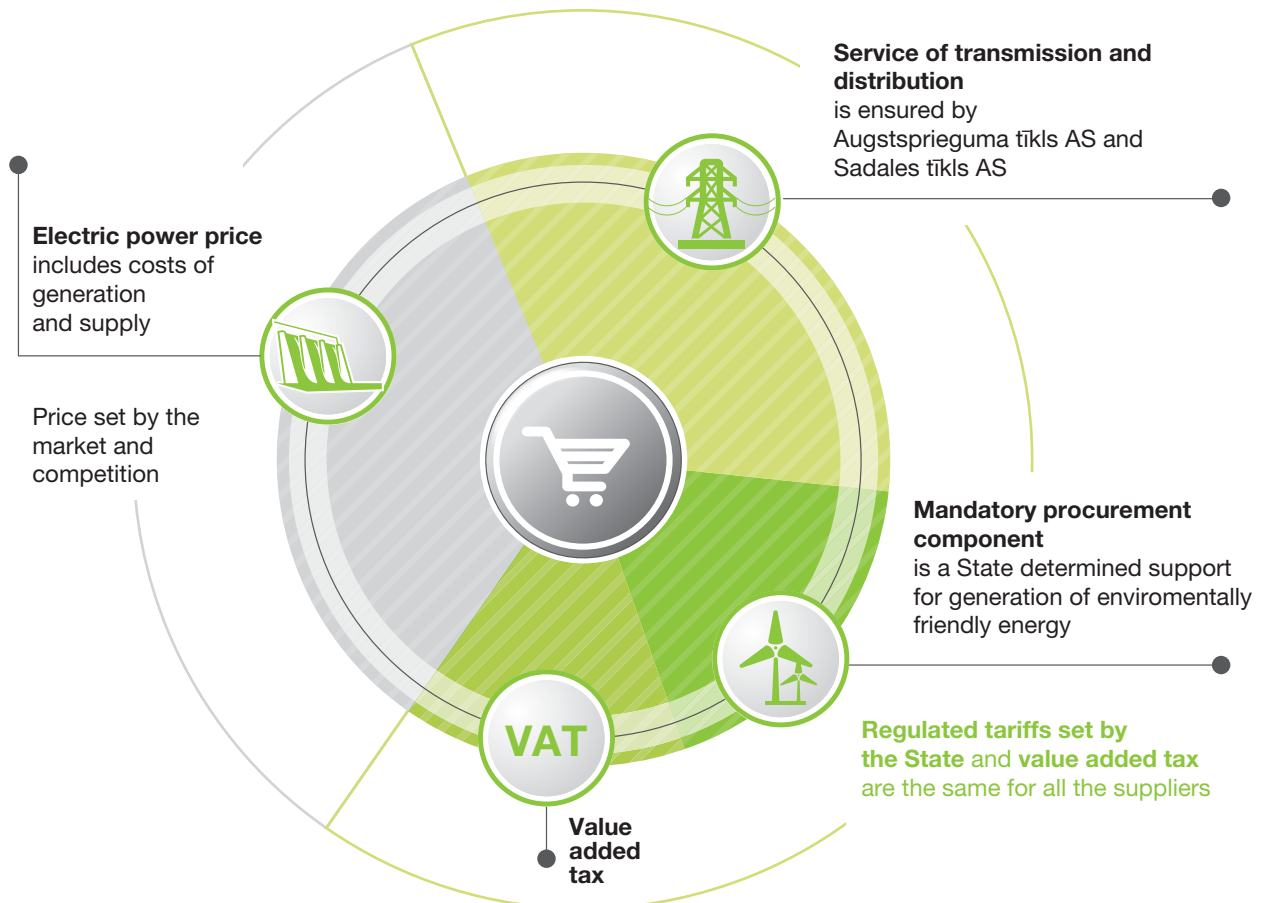
Overall, at the end of 2015, Latvenergo Group supplied electricity to approximately 828.0 thousand customers in the household segment and 36.6 thousand corporate customers, of which 801.8 thousand households and 27.3 thousand corporate customers in Latvia, 7.3 thousand corporate customers in Lithuania, and 26.2 thousand households and 1.8 thousand corporate customers in Estonia.

In the customer breakdown by segments, households constitute 96% of the total number of customers, the industrial segment 1%, and other customers (trade, state and local government institutions, etc.) – 3%.

### Market share in the Baltics in 2015



### The price of electricity is comprised of several components (example of Latvia)



# Mandatory procurement

## Mandatory procurement PSO fee remains unchanged

Mandatory procurement (MP) is a state-regulated support mechanism for electricity generators in Latvia in the form of electricity procurement or guaranteed payments for the installed capacity. Mandatory procurement costs are financed through payments by electricity end-users and a state budget grant.

In accordance with the Electricity Market Law, the right to sell the electricity generated within the MP or receive guaranteed payment for the installed capacity at power plants is granted to generators who generate electricity in efficient cogeneration or from renewable energy resources. The institution granting these rights to generators is the Ministry of Economics of the Republic of Latvia. The provisions for electricity generation, electricity MP pricing and the amount of guaranteed capacity payments are defined by regulations of the Cabinet of Ministers of the Republic of Latvia. The amount of MP support depends on the type of energy resource used (wind, water, biomass, biogas, natural gas), the installed capacity and for some stations the cost of natural gas.

As of 1 April 2014, the functions of public trader have been transferred to Latvenergo AS subsidiary Enerģijas publiskais tirgotājs AS. Expenditures associated with the MP and guaranteed capacity payments are compensated to the public trader by the end-users in Latvia through the MP public service obligation (PSO) fee, in proportion to their electricity consumption. The amount of the MP PSO fee is determined based on the actual expenditures in the preceding year and provision of expected administrative costs as approved by the PUC. Changes in the MP PSO fee enter into force on 1 April of the following year.

One of the instruments designed to control the increase of the MP PSO fee for electricity end-users in Latvia is the introduction of SET on 1 January 2014 for a four-year period and applied to state aid for generators within MP, i.e., the income from electricity supplied within the MP, as well as to guaranteed capacity payments for the installed capacity at combined heat and power plants. The tax differs according to the type of energy source used. Income from the SET is earmarked for the state budget grant for limiting the MP PSO fee increase, and the state budget target programme for 2015 (see Section 2.1 "Economic Performance") is defined by the Law on the State Budget for the relevant year and the Law on Medium-Term Budgetary Framework. For the coming years, the laws above provide for an additional source for limiting the MP PSO fee increase in the form of Latvenergo AS dividends.

### Mandatory procurement key indicators

In 2015, 1,427 GWh of electricity were procured within the MP process, including 629 GWh, or 44% generated in cogeneration and 798 GWh, or 56% generated using renewable energy resources. Compared to 2014, the amount of electricity procured has increased by 143 GWh or 11%. The increase of the amount of electricity procured under the MP was mainly determined by the commissioning of new power plants in 2014 and 2015, which in previous years received permits to supply the energy generated within the MP.

In 2015, the MP PSO fee did not change, and from 1 April 2016 the PUC has set it again at 26.79 EUR/MWh. The main instrument for retaining the MP PSO fee at the previous level is the planned special purpose grant from the state budget for compensating the MP expenses. A state budget grant of EUR 20.3 million was allocated in 2015, while in 2016, a EUR 59.7 million grant is included in the state budget.

### Mandatory procurement key indicators (2011 – 2015)

|   | Unit   | Method | 2011  | 2012  | 2013  | 2014  | 2015  |
|---|--------|--------|-------|-------|-------|-------|-------|
| Power plants                                | number | m      | 272   | 335   | 368   | 386   | 400   |
| MP paid-up capacity                         | MW     | m      | 957   | 1,033 | 1,310 | 1,354 | 1,364 |
| Electricity purchased within the MP         | GWh    | m/c    | 2,844 | 2,263 | 2 610 | 1,284 | 1,427 |
| MP costs above the market price (after SET) | MEUR   | c      | 114.1 | 189.0 | 209.9 | 215.4 | 224.3 |

m – measured, e – estimated, c – calculated

### Mandatory procurement PSO fee (2012 – 2016)

|                               | Unit      | Method | 04/01/12 | 04/01/13 | 04/01/14 | 04/01/15 | 04/01/16 |
|-------------------------------|-----------|--------|----------|----------|----------|----------|----------|
| Mandatory procurement PSO fee | cents/kWh | c      | 1.750    | 2.689    | 2.679    | 2.679    | 2.679    |
| Cogeneration                  | cents/kWh | c      | 1.337    | 1.892    | 1.737    | 1.671    | 1.625    |
| Renewable energy sources      | cents/kWh | c      | 0.413    | 0.797    | 0.942    | 1.008    | 1.054    |

m – measured, e – estimated, c – calculated

## 1.10.2 Distribution

### Investments increase the quality of electricity distribution service

The distribution segment is the second largest within Latvenergo Group in terms of both turnover and asset value, and its operations involve the provision of distribution system services to approximately 834 thousand customers in Latvia at regulated tariffs. The distribution system service is provided by Sadales tīkls AS, the largest distribution system operator in Latvia. The distribution system operator ensures equal access to electricity distribution networks, which is one of the prerequisites for ensuring competition in the electricity market in Latvia.

The electricity distribution network ensures the flow of electricity from the transmission network and electricity generators connected to the distribution networks, to electricity consumers. At the end of 2015, the total length of electricity lines was 94,120 km. Along with a significant investment in the implementation of the Cable Programme, the share of cable lines in the total length of electricity lines has been increasing steadily, reaching 32% of total line length at the end of 2015. The number of distribution network transformers was 29,883, while the number of transformer substations was 26,858, with total installed capacity of 5,881 MVA.

In 2015, the amount of electricity distributed decreased by 2% to 6,263\* GWh. Electricity distribution losses, a significant performance indicator of the distribution segment, have been constantly reduced over the past five years (see also the EU12 indicator), in 2015 constituting 4.6% of the total electricity received by the network, which is historically the lowest rate and the best in the Baltics. Total losses during the 2011-2015 period have decreased by a third or by 119 GWh.

The amount of electricity received by distribution networks from small electricity generators continues to increase, reaching 1,448 GWh in 2015, which is 2.3 times more compared to 2011. The increased electricity input from small generators is mainly explained by the commissioning of new electricity generation capacities.



### Distributed electricity and losses (2011 – 2015)

|   | Unit       | Method | 2011         | 2012         | 2013         | 2014         | 2015                 |
|---|------------|--------|--------------|--------------|--------------|--------------|----------------------|
| Distributed electricity   | GWh        | m/c    | 6,199        | 6,468        | 6,447        | 6,421        | 6,263*               |
| Electricity distribution losses, technological and internal consumption | GWh        | m/c    | 447          | 432          | 361          | 346          | 328**                |
| <b>TOTAL</b>  | <b>GWh</b> |        | <b>6,646</b> | <b>6,900</b> | <b>6,808</b> | <b>6,767</b> | <b>6,591* and **</b> |
| Electricity losses  | %          | m/c    | 6.4          | 5.9          | 5.0          | 4.8          | 4.6                  |

\* The volume of electricity distributed excludes 123 GWh; that amount corresponds to the regulated electricity tariff revenues received at the beginning of 2015 that were recognized in 2014.

\*\* The amount of losses is increased by 30 GWh, which is related to the recalculation of actual consumption of customers and the actual amount paid for electric energy

m – measured, e – estimated, c – calculated

## Electricity received in distribution network (2011 – 2015)

|                           | Unit       | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|---------------------------|------------|--------|--------------|--------------|--------------|--------------|--------------|
| From transmission network | GWh        | m/c    | 6,019        | 5,993        | 5,670        | 5,470        | 5,236        |
| From small generators     | GWh        | m/c    | 627          | 907          | 1,139        | 1,297        | 1,448        |
| <b>TOTAL</b>              | <b>GWh</b> |        | <b>6,646</b> | <b>6,900</b> | <b>6,808</b> | <b>6,767</b> | <b>6,684</b> |

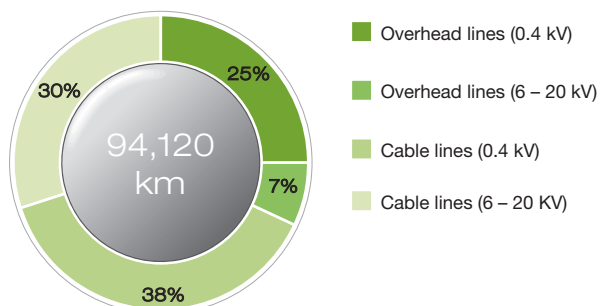
m – measured, e – estimated, c – calculated

## Reconstruction and construction (2011 – 2015)

|   | Unit      | Method   | 2011       | 2012       | 2013         | 2014         | 2015       |
|---|-----------|----------|------------|------------|--------------|--------------|------------|
| Overhead lines constructed (0.4 kV)                   | km        | m        | 60         | 64         | 17           | 19           | 37         |
| Cable lines constructed (0.4 kV)                      | km        | m        | 643        | 852        | 995          | 1,089        | 934        |
| <b>TOTAL low-voltage power lines</b>                  | <b>km</b> | <b>m</b> | <b>703</b> | <b>916</b> | <b>1,012</b> | <b>1,107</b> | <b>972</b> |
| Overhead lines constructed (6 – 20 kV)                | km        | m        | 262        | 149        | 305          | 300          | 556        |
| Cable lines constructed (6 – 20 kV)                   | km        | m        | 61         | 212        | 126          | 104          | 189        |
| Cable lines constructed (6 – 20 kV) – Cable programme | km        | m        | 16         | 144        | 162          | 207          | 210        |
| <b>TOTAL medium-voltage power lines</b>               | <b>km</b> | <b>m</b> | <b>339</b> | <b>505</b> | <b>593</b>   | <b>611</b>   | <b>955</b> |
| Transformer substations reconstructed                 | number    | m        | 617        | 388        | 577          | 649          | 877        |
| Connections constructed                               | number    | m        | 6,968      | 6,944      | 7,335        | 8,510        | 7,588      |

m – measured, e – estimated, c – calculated

## Length of electricity distribution lines in 2015



### Investments and maintenance

Each year maintenance and development of distribution networks include large-scale repairs and investments to establish reliable, high-quality energy supply, to reduce the frequency and duration of scheduled and unscheduled power supply outages due to damages, and to ensure adequate voltage quality. Increased cleaning of electricity transmission rights of way, as well as implementation of long-term investment programme, reduced the number of damages in the 6-20 kV power networks by 16%, and by 18% decreased unplanned power outage duration per user compared to 2014.

For the past five years, the amount invested in distribution assets has significantly increased. In

2015, the amount of investments was more than EUR 100 million. Investments in reconstruction and modernisation of distribution networks are made according to the *Sadales tīkls AS Development Plan 2014 – 2023*.

The medium-voltage electricity network Automation Programme and Cable Programme were continued in 2015. To ensure a more operational recovery from electricity supply disruptions, the Automation Programme involves connection of remote circuit breakers and fault location detectors, facilitating faster receipt of information about electricity supply failures within electricity networks. The Cable Programme includes replacement of medium-voltage overhead lines with cable lines (mostly in forested areas), reducing the number of electricity supply failures due to unfavourable weather conditions. In 2015, 210 km of medium-voltage cable lines were constructed. Restoration of medium and low-voltage lines and reconstruction of transformer substations were also continued. In 2015, 7,588 new connections were built, and voltage quality was improved at 4,215 customer objects. The investment project launched in 2014 in order to introduce smart electricity metering devices in Latvia in accordance with Directive 2009/72/EC of the European Parliament and of the Council was continued. With the introduction of smart meters, customer information about electricity consumption will be improved, promoting energy efficiency and cost reduction for the distribution system operator and customers, as well as electricity suppliers. A total of 116.3 thousand smart meters have been installed over a two year period (2014 and 2015).



## 1.10.3 Lease of Transmission System Assets

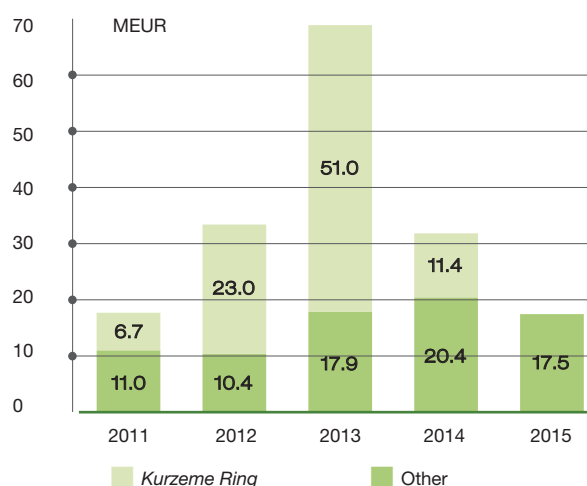
### Realization of transmission network development projects is continued

In 2015 the operations of the segment were characterized by the lease of transmission assets in Latvia owned by Latvijas elektriskie tīkli AS (330 kV and 110 kV electricity transmission lines, substations and distribution points) to the system operator Augstsprieguma tīkls AS.

As of 1 January 2015, the TSO Augstsprieguma tīkls AS has taken over the construction and maintenance functions of the transmission system assets from Latvijas elektriskie tīkli AS. Latvijas elektriskie tīkli AS continues to conduct the transmission asset management, i.e., financing and lease to Augstsprieguma tīkls AS. As a result, the number of employees at Latvijas elektriskie tīkli AS at the end of 2015 was reduced to 11. In 2015, the company's management was also reorganised – the Management Board of Latvijas elektriskie tīkli AS is represented by one Board member (five members in 2014).

At the end of 2015, the total length of electricity transmission lines was 5,251 km, comprised of 74% of 110 kV lines and 26% of 330 kV lines. Sixteen 330 kV substations with a total automatic transformer capacity of 3,825 MVA, and one hundred twenty-one 110 kV substations with a total installed transformer capacity

Investments in transmission system assets (2011 – 2015)



of 5,102 MVA are used for ensuring the operation of the transmission network.

### Investments

The total investments in transmission system assets in 2015 amounted to EUR 17.5 million. The most important future transmission network investment projects include the *Kurzeme Ring* project and the third Latvian-Estonian transmission network interconnection project.

### Length of power transmission lines (2011 – 2015)

|              | Unit      | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|--------------|-----------|--------|--------------|--------------|--------------|--------------|--------------|
| 330 kV       | km        | m/c    | 1,250        | 1,250        | 1,265        | 1,381        | 1,360        |
| 110 kV       | km        | m/c    | 4,006        | 4,010        | 4,010        | 3,891        | 3,891        |
| <b>TOTAL</b> | <b>km</b> |        | <b>5,256</b> | <b>5,260</b> | <b>5,275</b> | <b>5,273</b> | <b>5,251</b> |

m – measured, e – estimated, c – calculated

### Number of transformer substations, transformers, installed capacities (2011 – 2015)

|  | Mērv.  | Metode | 2011  | 2012  | 2013  | 2014  | 2015  |
|--|--------|--------|-------|-------|-------|-------|-------|
| Substations (330 kV)   | number | m      | 15    | 15    | 15    | 16    | 16    |
| Autotransformers (330 kV)  | number | m      | 21    | 22    | 23    | 25    | 25    |
| Installed capacity of autotransformers (330 kV)                            | MVA    | m/c    | 3,200 | 3,325 | 3,575 | 3,825 | 3,825 |
| Transformer substations (110 kV)   | number | m      | 119   | 121   | 122   | 121   | 121   |
| Transformers (110 kV)  | number | m      | 243   | 244   | 246   | 246   | 246   |
| Installed capacity of transformers (110 kV and 10 kV booster transformers) | MVA    | m/c    | 4,829 | 4,902 | 4,968 | 5,075 | 5,102 |

m – measured, e – estimated, c – calculated



### **The third Latvian-Estonian power transmission network interconnection**

Likewise, an important future electricity transmission infrastructure project for the entire Baltic region is a new third electricity transmission network interconnection between Estonia and Latvia. Implementation of this project is a part of the 10-year electricity transmission network development project developed by Augstsprieguma tīkls AS. The 330 kV interconnection will increase the available throughput between the Latvian and Estonian energy systems, decreasing the price differences between Estonian and Latvian/Lithuanian bidding areas.

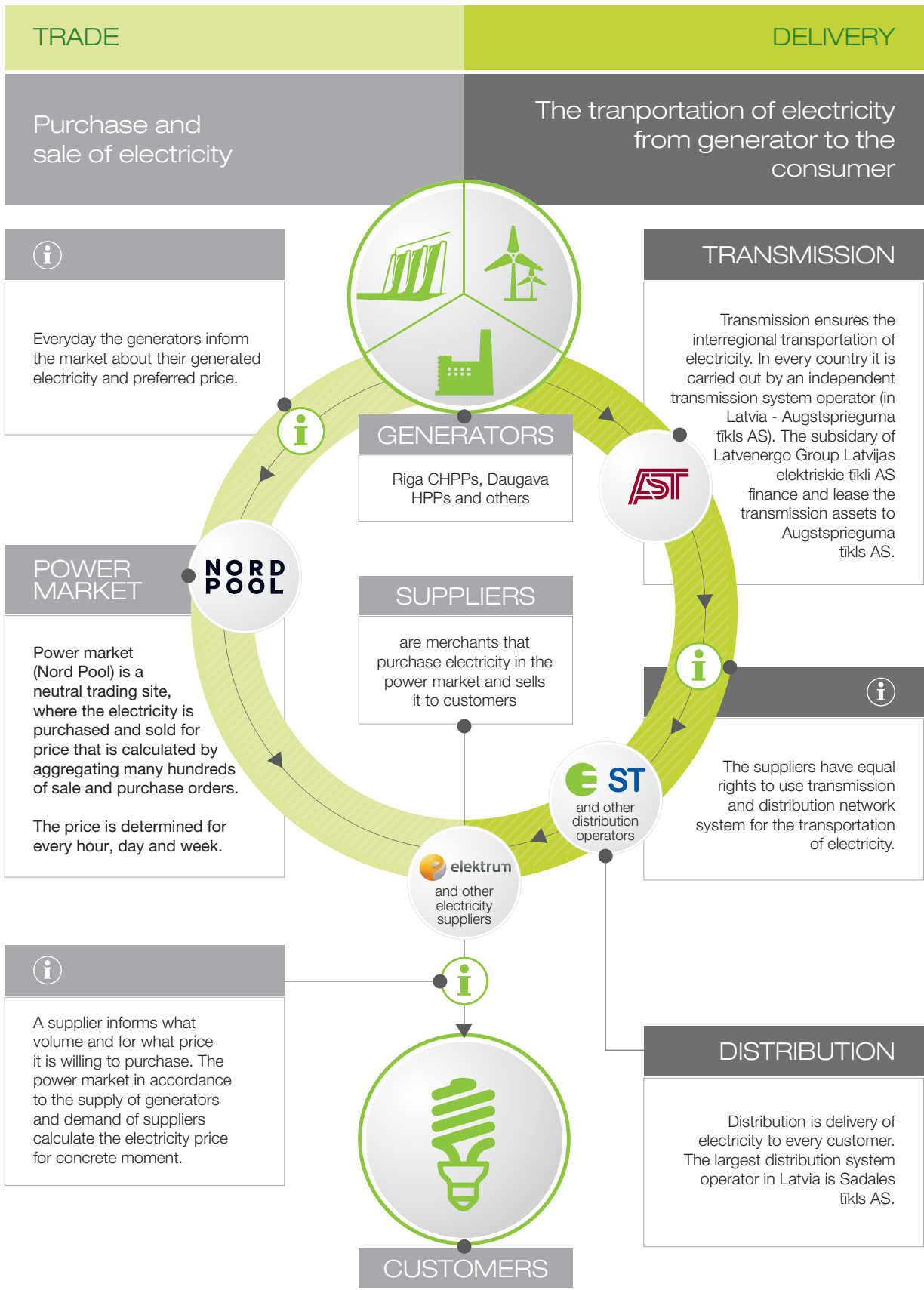
The planned length of the new 330 kV interconnection line will be about 190 km in Latvia, and it is scheduled for completion by the end of 2020. The overall construction costs of the project in Latvia are estimated at approximately EUR 100 million. In 2015, an agreement with the European Commission Innovation and Networks Executive Agency was concluded providing 65% co-funding of the total eligible project costs.

In order to increase the stability of electricity supply for customers and provide the demanded capacity at the transmission network points, other major projects completed in 2015 also include reconstruction of switchgear at the 330 kV *Viskaļi* substation, expansion of the 110 kV *Skulte* substation, reconstruction of the 110 kV *Dagda* substation and replacement of 110 kV transformers at *Sloka*, *Džūkste*, *Kūma*, *Aizpute*, *Ieriķi* and *Bolderāja II* substations. Also, reconstruction of 110 kV facilities at *Imanta* and *Salamandra* substations is continued, and the 330 kV and 110 kV electricity transmission lines are overhauled.

### **The Kurzeme Ring project**

The NORDBALT-02-330 kV *Kurzeme Ring* project, the most ambitious transmission system investment project recently, was launched in 2009 and is being implemented in three stages. The first stage was completed in 2012, by building the *Riga Ring*. Commissioning of the new *Grobiņa-Ventspils* 330 kV electricity transmission line in August 2014 completed the second stage of *Kurzeme Ring*. The environmental impact assessment has been completed for the final stage of the *Ventspils-Tume-Riga* project, and an agreement on 45% co-financing has been concluded with the European Commission Innovation and Networks Executive Agency. The total projected length of the transmission ring is 330 km.

The *Kurzeme Ring* project is scheduled for completion in 2019, and the total project construction costs are expected to constitute approximately EUR 220 million, including EUR 95 million for implementation of the first and second stage of the project.



**TRADE**

**DELIVERY**

Purchase and sale of electricity

The transportation of electricity from generator to the consumer



Everyday the generators inform the market about their generated electricity and preferred price.

**TRANSMISSION**

Transmission ensures the interregional transportation of electricity. In every country it is carried out by an independent transmission system operator (in Latvia - Augstsprieguma tīkls AS). The subsidiary of Latvenergo Group Latvijas elektriskie tīkli AS finance and lease the transmission assets to Augstsprieguma tīkls AS.

**GENERATORS**

Riga CHPPs, Daugava HPPs and others

**POWER MARKET**

**NORD POOL**

Power market (Nord Pool) is a neutral trading site, where the electricity is purchased and sold for price that is calculated by aggregating many hundreds of sale and purchase orders.

The price is determined for every hour, day and week.

**SUPPLIERS**

are merchants that purchase electricity in the power market and sell it to customers

**E ST**  
and other distribution operators

The suppliers have equal rights to use transmission and distribution network system for the transportation of electricity.

**elektrum**  
and other electricity suppliers



A supplier informs what volume and for what price it is willing to purchase. The power market in accordance to the supply of generators and demand of suppliers calculate the electricity price for concrete moment.

**DISTRIBUTION**

Distribution is delivery of electricity to every customer. The largest distribution system operator in Latvia is Sadales tīkls AS.

**CUSTOMERS**



# 1.11 Group Procurement

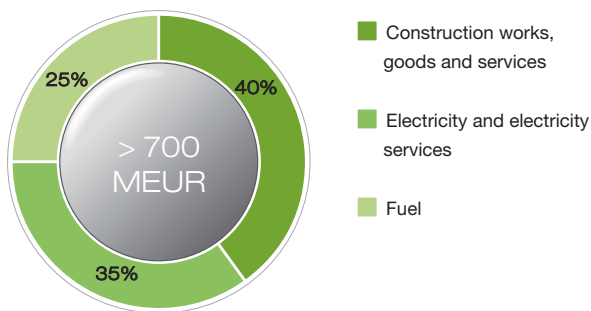
G4-12

Procurements of the Group are based on the principles of fair business cooperation

To ensure its operations, Latvenergo Group procures electricity and fuel, as well as various types of construction works, goods and services. In 2015, the total costs of Latvenergo Group procurement exceeded EUR 700 million, the majority of which or approximately 40% were constituted by construction works, goods and services, approximately 35% by electricity and electricity services and approximately 25% by the fuel.

Most of the Group's procurement was made from suppliers and service providers in the Baltics and in the Nordic countries. The total number of suppliers exceeds 3.5 thousand.

## Types of procurement



The Group procurement complies with the EU legislation and the legal acts of the Republic of Latvia, and of those countries in whose territory the Group carries out its commercial activity. The key principles of the Group procurement are based on the requirements of the Directives 2014/24/EU and 2014/25/EU of the European Parliament and the Council, and those of the Law on Procurement of Public Service Providers of the Republic of Latvia. When making a procurement, Latvenergo Group is committed to provide the most efficient use of funds and follows the principles of transparency, equality and non-discrimination. Supplier selection is based on competition, equal and fair treatment and respect of the transparency principle of the procurement.

Latvenergo Group requests that its contractors comply with the Group's ethical principles and bases mutual relations on the principles of fair business cooperation. Upon signing cooperation agreements, Latvenergo Group proposes partners to provide declarations of adherence to high ethical principles during the cooperation period. The ethical principles of the Latvenergo Group for cooperation with contractual partners are published on the <http://www.latvenergo.lv> website, under the *Tenders and offers/Procurement procedures*.

To ensure a more efficient procurement, Latvenergo Group has established a qualification system for suppliers of construction works and services, aimed at selecting and maintaining a list of qualified suppliers. The qualification system contains 28 types of construction works and services (engineering) with 86 qualified contractors and service providers (constructors).

## Electricity Procurement

In 2015, electricity and electricity services costs of Latvenergo Group totalled to approximately EUR 270 million, constituting about 35% of the overall costs of the overall procurement. The costs of electricity and electricity service include also the ancillary electricity services and electricity wholesale operations in order to reduce price risks. The total amount of electricity purchased in wholesale was 4,701 GWh. The Group sells its generated electricity and at the same time procures electricity for its customers on the Nord Pool – the leading international power exchange in Europe, ensuring a full transparency of the procurement.

The electricity procurement process of Latvenergo Group is targeted at cost optimisation and provides economic benefits to both Latvenergo Group and its customers. Latvenergo Group uses Riga CHPPs and Daugava HPPs to diversify electricity supply and optimise the procurement costs. The possibility to promptly switch the electricity supply source between the exchange and generation at its own power plants provides for an opportunities for cost reduction in electricity procurement and decreases Latvenergo Group exposure to market price fluctuation risk. Moreover, Riga CHPPs provide for a possibility to stabilise electricity prices in the region, which is a significant advantage in the Latvian and Lithuanian markets where the electricity financial instruments market was limited in 2015.

## Purchased electricity (2011 – 2015)

|                       | Unit | Method | 2011  | 2012  | 2013  | 2014  | 2015  |
|-----------------------|------|--------|-------|-------|-------|-------|-------|
| Purchased electricity | GWh  | m/c    | 5,397 | 4,254 | 3,656 | 5,590 | 4,701 |

m – measured, e – estimated, c – calculated

## Fuel Procurement

Latvenergo Group fuel procurement is constituted by natural gas, diesel fuel and wood chips. In 2015, fuel costs of Latvenergo Group totalled approximately EUR 160 million, constituting approximately 25% of the overall costs of procurement. Riga CHPPs accounted for more than 90% of the Latvenergo Group fuel expenditure, the rest being comprised of Liepaja plants and Kegums boiler house.

Natural gas expenditure accounts for approximately 98% of Latvenergo Group overall fuel costs. Riga CHPPs use natural gas as the primary fuel, which is environmentally the friendliest type of fossil fuel available for power generation. Natural gas is partly used also at Liepaja plants. The annual natural gas consumption ranges from 500 to 650 million nm<sup>3</sup>.

Natural gas procurement differs from other purchases, because unlike other energy market segments, natural gas supply is a fully regulated service. According to the legal framework, Latvijas Gāze AS has been granted the right to provide natural gas supply services as the sole merchant in the territory of Latvia until 3 April 2017. Natural gas prices are determined in accordance with the differentiated end-user tariffs approved by the PUC that are pegged to oil product prices. As a result of the global fall in oil prices, in 2015 natural gas prices (including excise duty) in Latvia were on average 15% lower than a year ago, leading to reduced fuel costs for the Latvenergo Group.

Latvijas Gāze AS supplies natural gas to Latvenergo Group facilities based on bilateral agreements. Deliveries are made according to the necessary natural gas volumes, subject to a prior agreement. The total amount of natural gas procured in 2015 was

569 million nm<sup>3</sup>. Natural gas consumption at Latvenergo Group facilities depends on thermal energy demand and the market situation. Riga CHPPs operate in a market conjunction effectively planning the operating modes and fuel consumption, i.e., under unfavourable market conditions, the generation at power plants is reduced, using the opportunity to purchase cheaper electricity on the exchange.

The latest changes in Latvian legislation under a consideration by the Saeima and the government, that are based on the requirements of the EU Directive for the internal market of natural gas, provide for opening of the natural gas market in April 2017. In September 2015, the PUC adopted rules providing third-party access to natural gas infrastructure. Those changes in the legal framework and the fact that in October 2014 a liquefied natural gas terminal was brought into operation in Klaipeda, provide for a possibility for Latvenergo Group to diversify natural gas supply possibilities over the coming years and procure natural gas from the Klaipeda terminal.

Ensuring the reliability of thermal energy supply for emergency situations when the supply of natural gas is interrupted, Riga CHPPs store back-up fuel reserves of diesel. Previously Riga CHPPs used heavy fuel oil as the back-up fuel. Latvenergo Group uses renewable energy sources, i.e., wood chips, at Liepaja plants and Kegums boiler house. In 2015, wood chips accounted for approximately 2% of the total fuel procurement costs of Latvenergo Group. No diesel fuel was procured in 2015. Like all other goods and services, wood chips and diesel fuel are procured under the conditions of free competition.

## Amounts of fuel procurement (2011 – 2015)

|             | Unit                 | Method | 2011    | 2012    | 2013    | 2014    | 2015    |
|-------------|----------------------|--------|---------|---------|---------|---------|---------|
| Natural gas | thsd.nm <sup>3</sup> | m/c    | 641,580 | 514,673 | 597,846 | 517,119 | 569,003 |
| Wood chips  | loose m <sup>3</sup> | m/c    | 7,983   | 45,501  | 162,491 | 226,826 | 211,283 |
| Diesel fuel | t                    | m/c    |         |         |         | 6,843   |         |

m – measured, e – estimated, c – calculated



# Latvenergo Group Performance Indicators



Prepared in accordance with GRI G4 Guidelines, Core



# 2.1 Economic Performance

## Management Approach

Along with sustainable and well-considered investments in energy generation and network development, Latvenergo Group provides a direct economic contribution to society at large – through taxes paid to the state budget, dividends, and jobs created. A great role throughout the energy generation and supply process is attributed to efficiency, improving the competitiveness and quality of services.

Group operations contribute to the development of the economy

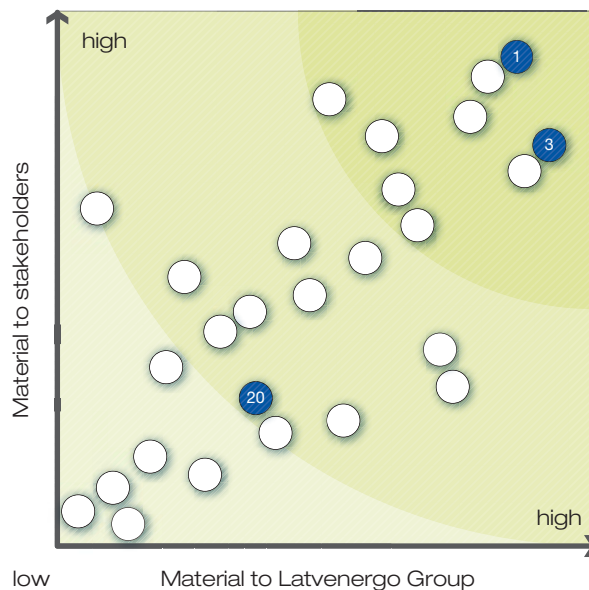
### Contribution to the national economy

Latvenergo Group is the largest power supply utility and one of the most valuable companies in the Baltics. Latvenergo Group operations make a significant contribution to the society and growth of the economy. With its large amount of investment and direct and indirect job creation, the energy industry is an important driving force of the economy. In 2015, Latvenergo Group made investments of EUR 190 million, with the total investments over the past five years exceeding EUR 1 billion. Significant amounts have been invested in environmentally friendly and environment-enhancing energy generation and network development investment projects: Daugava HPPs hydropower unit reconstruction programme, the *Kurzeme Ring* project and others (see Annex “Report on *Green Bonds*”).

At the same time, Latvenergo Group provides a direct economic benefit to society at large. Latvenergo Group is one of the biggest taxpayers in Latvia. Over the past five years, Latvenergo Group has paid in taxes more than EUR 760 million, including about EUR 200 million in dividends for using state capital paid and remitted to the state budget. The Group is also one of the biggest employers in Latvia, with a total of 4,177 employees as of the end of 2015.

Latvenergo Group financial results indicate its stable financial position and development. Detailed information about the performance of the Group is available in the Latvenergo Consolidated Annual Report 2015.

## Economic Performance aspects in the Materiality Matrix\*



\* see Section 1.9 “Materiality Assessment”

### Efficiency of power generation facilities

Daugava HPPs and Riga CHPPs, the biggest energy generation facilities of the Group, operate in free competition conditions, trading all the generated electricity on the Nord Pool power exchange. The efficiency of energy generation facilities is very important for maintaining the competitiveness of the power plants in a changing market situation.

With the commissioning of the Riga TEC-2 power unit in late 2013, which completed the reconstruction of Riga TEC-2 power generation plant, Riga TEC-2 has become the most advanced and efficient combined cycle heat and power plant in the Baltics. Riga TEC-1, in turn, was overhauled in 2005. Riga CHPPs guarantee substantial electricity base-load capacity for Latvia, stabilising electricity prices in the region and limiting the electricity price increase risk.

Out of the 23 Daugava HPP hydropower units, 12 are already modernised, and the reconstruction of the remaining 11 hydropower units is ongoing; as a result, the hydropower unit efficiency ratios and the installed capacity will be improved, increasing the annual electricity output.



Riga CHPPs are efficiently planning their operating modes and fuel consumption according to the market situation. Under unfavourable market conditions, the generation at power plants is reduced, purchasing cheaper electricity from the Nordic countries. The output of Daugava HPPs is planned considering water inflow in the Daugava River and the possibility to accumulate water and generate electricity during periods of high demand and price.

Operation of Latvenergo Group generation facilities is organised and planned according to the fundamental principles of sustainable development. A certified integrated management system for electricity and thermal energy generation has been implemented and is maintained at generation facilities, affirming operational efficiency. Latvenergo Group continuously enhances and improves the thermal energy and

electricity generation processes, ensuring quality and stable generation, in line with the requirements of the legal acts and customer demand.

#### Distribution efficiency

Along with the improvement of electricity supply quality, Latvenergo Group pays great attention to programmes and activities to reduce electricity losses in distribution networks: electricity consumption is regularly monitored and measures are taken for its improvement, electric networks are being optimised and automated, and smart grid technologies are gradually introduced. Various measures to reduce distribution network losses will be continued also in the coming years.

For more information, see Sub-Section 1.10.2 "Distribution".

## Direct economic value generated and distributed

In 2015, the economic value generated by Latvenergo Group was EUR 936.9 million, while distributed economic value was EUR 679.4 million. Compared to the previous year, a decline in generated and distributed economic value was mainly due to change in accounting principles along with entrance into operation of Enerģijas publiskais tirgotājs AS as of 1 April 2014 – mandatory procurement PSO fee settlements are no longer included in profit and loss statement of the Group. Likewise, lower distributed economic value was influenced by lower procurement amount of electricity, decline in costs of electricity and fuel due to lower electricity and natural gas prices.

Distributed economic value reached 73% of the economic value generated. The major part or 75% of distributed value represents operating costs, including electricity procurement, electricity services, fuel and other operational costs.

In 2015, dividends paid for 2014 comprised EUR 31.5 million. Latvenergo Group is a significant payer of dividends for the use of state capital. Over the last five years approximately EUR 200 million were remitted into the state budget.

G4-EC1

In 2015, the undistributed economic value of Latvenergo Group represents 27% of the economic value generated reaching EUR 256.7 million, from which EUR 190.5 million has been earmarked for investment. According to the law "On the State budget 2016" Latvenergo AS dividend payout for the use of state capital in 2015 is anticipated in the amount of EUR 77.4 million, which is by EUR 45.9 million more than last year. Latvenergo AS dividends, in addition to the SET revenue, will be used as a source of funding for the State budget program "Electricity user support", thereby maintaining the MP PSO fee in the coming years at the current level.

## Economic value generated and distributed (2014 – 2015)

|   | Unit        | Method   | 2014           | 2015         |
|---|-------------|----------|----------------|--------------|
| <b>Economic value generated</b>                           | <b>MEUR</b> | <b>c</b> | <b>1,018.7</b> | <b>936.9</b> |
| Revenue and other income                                  | MEUR        | c        | 1,016.0        | 934.0        |
| Income from financial activities                          | MEUR        | c        | 2.6            | 2.9          |
| <b>Economic value distributed</b>                         | <b>MEUR</b> | <b>c</b> | <b>825.5</b>   | <b>679.4</b> |
| Raw materials, consumables and other operational expenses | MEUR        | c        | 658.1          | 509.6        |
| Remuneration of employees                                 | MEUR        | c        | 98.0           | 92.4         |
| Payments for the use of state capital                     | MEUR        | c        | 23.6           | 31.5         |
| Payments to providers of debt capital                     | MEUR        | c        | 20.4           | 18.6         |
| State imposed payments                                    | MEUR        | c        | 23.7           | 26.7         |
| Charity and sponsorships                                  | MEUR        | c        | 1.8            | 0.7          |
| <b>Retained economic value</b>                            | <b>MEUR</b> | <b>c</b> | <b>193.2</b>   | <b>256.7</b> |
| Depreciation and amortisation                             | MEUR        | c        | 173.6          | 182.5        |
| Savings and reserves                                      | MEUR        | c        | 19.5           | 74.3         |

m – measured, e – estimated, c – calculated

## Financial assistance received from government

G4-EC4 For the implementation of major investment projects, Latvenergo Group has attracted co-financing (foreign financial assistance) from the EU. One of the key projects for which co-financing was attracted is the *Kurzeme Ring*, implemented within the framework of the NordBalt-02-330kV project, with 50% co-financing provided within the European Energy Programme for Recovery for the construction of the two initial project stages: the *Riga Ring* and *Grobina-Ventspils*. An agreement on 45% co-financing for the final stage of the *Ventspils-Tume-Riga* project has been signed with the European Commission Innovation and Networks Executive Agency.

EU funds have also been attracted with 65% co-financing for the Estonia – Latvia third power transmission 330 kV network interconnection. From 1 January 2015, transmission projects are implemented by Augstsprieguma tīkls AS (for more information about the projects see Section 1.10 “Description of Operating Segments”).

Over previous years, the EU Cohesion Fund co-financing had been attracted for biomass boiler house construction project and heating network reconstruction project in Liepaja. The “Promotion of energy efficiency in households using smart technologies” project received funding within the framework of the Republic of Latvia “Climate Change Financial Instrument” State budget programme.

In 2015, Enerģijas publiskais tirgotājs AS received a EUR 20.3 million targeted grant from the State Budget. The purpose of the grant is to prevent an increase in the MP PSO fee, keeping it at the previous year’s level of 2.69 cents/kWh. The source of funding of the state targeted grant is the SET introduced in Latvia in 2014. The tax applies to companies receiving aid for electricity generation within the framework of the MP, or guaranteed payments for the installed electrical capacity at power plants.

## Funding received from the state and the EU (2011 – 2015)

|                               | Unit        | Method | 2011       | 2012       | 2013        | 2014        | 2015        |
|-------------------------------|-------------|--------|------------|------------|-------------|-------------|-------------|
| Project <i>Kurzeme Ring</i>   | MEUR        | c      |            | 0.2        | 7.6         |             | 18.0        |
| Liepaja plants                | MEUR        | c      | 2.1        | 3.4        | 2.4         | 2.2         |             |
| Smart technology              | MEUR        | c      |            |            | 0.2         |             |             |
| Grant for limiting MP PSO fee | MEUR        | c      |            |            |             | 29.3        | 20.3        |
| <b>TOTAL</b>                  | <b>MEUR</b> |        | <b>2.1</b> | <b>3.6</b> | <b>10.1</b> | <b>31.4</b> | <b>38.3</b> |

m – measured, e – estimated, c – calculated

## Average generation efficiency of thermal plants by energy source and by regulatory regime

EU11 Generation efficiency indicators are calculated as the ratio of electricity and thermal energy generated and the energy used for its generation. Generation efficiency indicators are affected by the generation facility operation modes selected, which are adjusted to the electricity market conditions.

Similarly to 2014, even with the condition of smaller water inflow, the generation efficiency at Daugava HPPs is better than the previous years – consuming less water resources per kWh generated. For the purpose

of improving the generation efficiency, Daugava HPPs make use of the possibility to accumulate water and generate electricity at times when the demand is high (during daily peak hours). Riga CHPPs are mostly operated in a highly efficient cogeneration mode, flexibly adjusting it to electricity demand in the market.

Compared to other power generation companies in the Baltics, the efficiency indicators of Latvenergo Group generation facilities are considered high.

## Generation facility efficiency indicators (2011 – 2015)

|                     | Unit                | Method | 2011 | 2012 | 2013 | 2014 | 2015 |
|---------------------|---------------------|--------|------|------|------|------|------|
| Daugava HPPs        | m <sup>3</sup> /kWh | m/c    | 19.4 | 19.4 | 19.5 | 18.7 | 18.8 |
| Riga CHPPs          | %                   | m/c    | 83   | 85   | 79   | 80   | 79   |
| Liepaja plants      | %                   | m/c    | 92   | 93   | 91   | 91   | 90   |
| Kegums boiler house | %                   | m/c    | 80   | 83   | 86   | 86   | 86   |

m – measured, e – estimated, c – calculated

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## Distribution losses as a percentage of total energy

### Distribution losses (2011 – 2015)

EU12

|                     | Unit | Method | 2011 | 2012 | 2013 | 2014 | 2015 |
|---------------------|------|--------|------|------|------|------|------|
| Distribution losses | %    | m/c    | 6.4  | 5.9  | 5.0  | 4.8  | 4.6  |

m – measured, e – estimated, c – calculated

One of the most important indicators describing the efficiency of the distribution segment is distribution losses as a percentage of total electricity received in

the network. In 2015, this indicator dropped to 4.6% – the historically lowest rate and the best in the Baltics.

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## Average plant availability factor by energy source and by regulatory regime

The power plant availability factor for the generation facilities of Daugava HPPs and Riga CHPPs is calculated as the time period during which a power plant can operate at nominal capacity. The remaining time is intended for scheduled and unscheduled power outages, such as repair works.

In 2015, the plant availability factors of Daugava HPPs and Riga CHPPs were lower than in the previous year. The decrease at the Daugava HPPs was mainly due to the reconstruction of hydropower units, while Riga CHPPs were affected by the reconstruction of the circulation system and other works aimed at the improvement of performance

EU30

### Average plant availability (2011 - 2015)

|              | Unit | Method | 2011 | 2012 | 2013 | 2014 | 2015 |
|--------------|------|--------|------|------|------|------|------|
| Daugava HPPs | %    | m/c    | 86   | 90   | 91   | 93   | 87   |
| Riga CHPPs   | %    | m/c    | 82   | 86   | 93   | 86   | 82   |

m – measured, e – estimated, c – calculated



## 2.2 Society

### Management Approach

Responsibility is one of the Latvenergo Group values and a fundamental principle of corporate governance. The Group and its employees take responsibility for the tasks performed in compliance with the requirements of the applicable regulatory acts. The Group operates in accordance with high ethical and operational compliance standards, engaging stakeholders in the implementation of its activities.

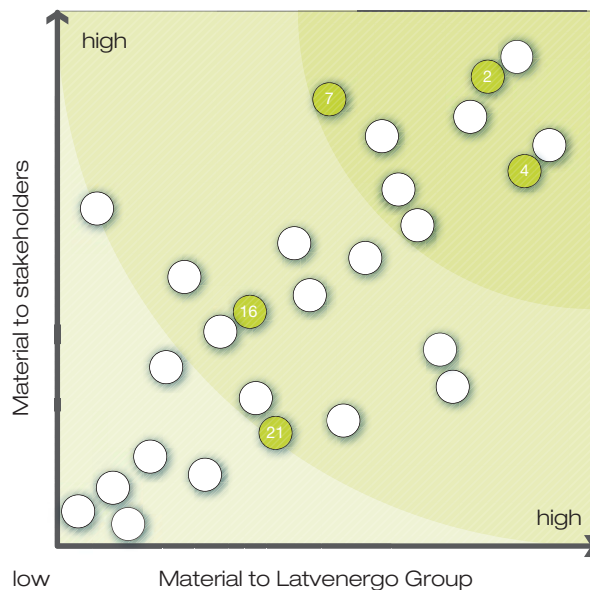
#### Fair and equal treatment in communication with the society

Compared to other areas, Society aspects are quite important in view of both stakeholders and Latvenergo Group (see the Materiality Matrix in Section 1.9 “Materiality Assessment”). Their materiality is determined by the statutory and voluntary responsibility of the Group for the impact on society, the economy and the environment.

The management approach of Latvenergo Group related to its impacts on society is based on socially responsible activity and openness:

- according to the principles defined by its Code of Ethics, Latvenergo Group guarantees fair treatment and equal attitude towards employees, customers, suppliers and other stakeholders, prevents fraud and corruption in its activities;
- the Group responsibly evaluates the impact of its activities on the environment in both day-to-day operations and in the implementation of new projects. Emergency and crisis management and prevention plans have been developed for the Group’s critical infrastructure. The local communities are regularly involved in the discussion of the modernisation projects of the Group facilities. According to the 2015 study conducted by the Institute for Corporate Sustainability and Responsibility, Latvenergo Group is one of the most transparent companies in Latvia;
- while developing international and national regulatory documents for the energy sector and related industries, Latvenergo Group is actively involved in the shaping of public opinion on issues of mutual importance to the Group and its stakeholders.

### Society aspects in the Materiality Matrix\*



\* see Section 1.9 “Materiality Assessment”

#### Compliance with the requirements of regulatory acts and fair competition

One of the cornerstones of Latvenergo Group corporate governance is ethics and compliance.

Latvenergo Group has introduced the Code of Ethics, which defines the Group’s corporate values and high ethical and professional conduct standards in order to ensure that Group employees carry out their responsibilities with utmost integrity, are unbiased in the performance of their duties and decision-making, comply with high ethical standards, and prevent fraud, corruption and unlawful or fraudulent conduct in their activities. The Group’s contractors are urged to adhere to equivalent ethical principles.

Latvenergo Group has also developed and introduced a Fraud and Corruption Risk Management Policy, which defines the basic principles of fraud and corruption risk management, and the main tasks and responsibilities of the parties involved at various organisational levels of the Group. Along with the Policy, a range of measures have been introduced to mitigate the risk of fraud and corruption:

- annual fraud and compliance risk assessment and corrective action planning, and quarterly control over the implementation of risk mitigation measures;
- to prevent potential conflicts of interest, Group employees fill out annual declarations of conflict of interest. New employees entering into employment relations must sign a statement confirming their understanding of conflict of interest situations and the commitment to prevent their occurrence at work;
- Group employees are regularly trained on best control practices for the prevention and mitigation of fraud and corruption risks. The Group also encourages the improvement of internal regulations and other measures to ensure fair commercial practices and to prevent corruption and fraud risks.

Latvenergo Group takes responsibility for conducting its operations in compliance with the applicable law. Financial and human resources are allocated to ensure the legal compliance of the Group's operations, preventing the occurrence of compliance risks. The Group regularly follows any changes to regulatory acts, participates in public hearings and keeps in touch with the responsible institutions. The Group also develops and maintains its internal procedures.

Considering that Latvenergo Group is the dominant player of the electricity market in Latvia, an increased attention is being paid to the principles of equal market competition. To prevent potential occurrence of competition risks, the Group has developed a Competition law compliance manual and organises regular educational workshops for those employees whose activities may impact the occurrence of that risk.

#### **Emergency management plans**

Latvenergo Group is not fully protected against natural disasters and human-caused damage. To mitigate these risks, Latvenergo Group has created a common emergency and crisis management system. The purpose of the system is to define a common approach for resolving issues that arise during emergency or crisis situations and to ensure continuous and reliable operation of the Group, or its prompt and efficient recovery in the event of an emergency or crisis.

The principles developed for action in crisis situations provide for cooperation with the Crisis Management Council, the Energy Crisis Centre, local governments, the Department of Management and Operations of the State Fire and Rescue Service (SFRS), the National Armed Forces, and Augstsprieguma tīkls AS. The emergency and crisis management plan of Latvenergo Group has been coordinated with the Ministry of Economics of the Republic of Latvia, which is responsible for the development of the national energy policy and for the planning and management of energy crisis recovery measures.

Employees are regularly instructed in order to raise the awareness of their duties for managing emergency and crises' situations. Moreover, in cooperation with Augstsprieguma tīkls AS, emergency and crisis



management training for employees of various Latvenergo Group organisational units is carried out annually, reproducing the possible emergency scenarios and involving specialists from the Department of Management and Operations of SFRS and the National Armed Forces. In order to improve recovery response and reduce material losses, subsequently the training process is analysed and the preventive measures to be taken are defined.

#### **Involvement in shaping of the energy sector policy**

The involvement of Latvenergo Group as the Baltic leader of power supply in the shaping of the energy sector policy is important for a sustainable development of the Group, the sector, and national economy. Latvenergo Group experts participate in public discussions and prepare positions, opinions and statements on public policy documents and draft legislation of Latvia and the EU, stating their position in line with the goals and tasks defined by the strategy of the Group.

Lobbying of the Group position in the EU is ensured through participation in the EURELECTRIC professional association. In 2015, the Group participated in drafting of EURELECTRIC positions on the reform of the EU Emissions Trading Scheme, on the European Energy Union and the EU 2030 Climate and Energy Framework.

The formation of a European Energy Union was one of the top priorities of the Latvian Presidency of the EU Council in the field of energy. On 6 February 2015 in Riga, during the conference organised by the Latvian Presidency in collaboration with the European Commission, Energy Ministers from the EU Member States and representatives from EU institutions and international organisations, scientists and other policy makers discussed the creation of a European

Energy Union and its key dimensions, thus launching the *Riga Process*. Latvenergo Group participated in the preparation of the conference, encouraging discussions on new solutions to reduce the European energy dependency and create a fully integrated energy market, ensuring safe, competitive and sustainable energy for Europe.

By participating in various forums, Latvenergo Group furthers exchange of opinions about topical issues of the Latvian and EU energy policies, including the opening of the electricity market for households, electricity market outlook, preconditions for the liberalisation of the Baltic natural gas market, implementation of the Energy Efficiency Directive, and other sector-related subjects.

In 2015, the Group experts also gave recommendations for the development and improvement of various regulatory documents. The most important of those include the draft Energy Efficiency Law, amendments to the Electricity Market Law, the Latvijas Gāze AS Inčukalns Underground Gas Storage Facility Usage Regulations, the Usage Regulations of Latvijas Gāze AS natural gas transmission system, etc.

#### **Impact on society**

Latvenergo Group is aware of its impact on the stakeholders. The Group follows all the regulatory requirements regarding the assessment of the impact of its operations and takes the necessary mitigation measures. To mitigate the potential harm or the risk thereof to the environment and society and to ensure public involvement in the decision-making, stakeholder opinions are identified through public discussions; customers and any third parties may also submit their complaints or applications in the way most convenient for them (see the Section 2.3 "Product Responsibility"). The Group also conducts studies in the area of environmental protection and carries out environmental impact assessments. Latvenergo Group cooperates with the responsible services, institutions and local governments to ensure the safety of local communities affected by the Daugava hydropower plant reservoirs during the spring flood period. More information about the activities in 2015 is available under the G4-SO1 indicator.

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### Percentage of operations with implemented local community engagement, impact assessments, and development programmes

G4-SO1 While implementing electricity network infrastructure projects, Latvenergo Group communicates with society and finds out its opinion. The Estonia–Latvia third power network interconnection is a significant future electricity transmission project in the Baltic region, for which 7 initial public discussions regarding the environmental impact assessment were organised in February and March 2015 and in November and December – a total of 19 public discussions of the environmental impact report in the affected districts were held. Subsequently to the public discussions, obtained suggestions are evaluated and the necessary corrections are made in the environmental impact assessment and the preliminary route project before their submission to the State Environmental Bureau for approval.

Latvenergo Group involves the society in all projects, where the public interests are at stake. Public discussions for the project Estonia–Latvia third power network interconnection took place in accordance with the requirements of the law On Environmental Impact Assessment.

Like every year, in spring 2015, Latvenergo Group representatives took part in informative activities coordinated by SFRS aimed at prompt and harmonised cooperation with the responsible services, institutions and local governments to ensure safety along the banks of the Daugava River and in flood-prone areas.

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### Communication and training on anti-corruption policies and procedures

G4-SO4 In 2015, a training on fraud and corruption risk management and the recommended risk mitigation controls was organised for managers and employees of Latvenergo Group companies. Training has been provided for all Management Board members and Chief Officers and Managers of Latvenergo AS, Sadales tīkls AS and Latvijas elektriskie tīkli AS. To raise employee awareness of anti-corruption issues, discussions were organised in organisational units during which the potential risks were evaluated and the controls needed for mitigation of fraud and corruption risks identified. Overall, over 70% of Latvenergo AS employees and all employees of Sadales tīkls AS and Latvijas elektriskie tīkli AS have undergone fraud and corruption risk management training.

In 2016, Latvenergo Group is planning to introduce electronic training programmes on fraud and corruption risk mitigation and prevention. All employees of Latvenergo Group companies will be ensured a possibility to master the programme.

All contracts signed with business partners during the reporting period include anti-fraud and anti-corruption requirements. Contract forms are available to potential cooperation partners already at the procurement procedure stage, and explanations are given if necessary. Ethical requirements for cooperation with contractors are available on Latvenergo Group websites.

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## Confirmed incidents of corruption and actions taken

No cases of corruption were identified within Latvenergo Group in 2015.

In 2015, fraud and corruption risks were assessed at all operational units of Latvenergo AS and Sadales tīkls AS and business divisions of Latvijas elektriskie tīkli AS. The purpose of the risk assessment was to identify fraud and corruption risks, evaluate the efficiency of controls and prepare the necessary risk mitigation measures in order to minimise the potential losses and harm to the Group's reputation, and the possibility of imposing statutory obligations or sanctions on the Group. According to the risk assessment results, the risk of fraud and corruption at Latvenergo Group is

properly managed. Mitigation of fraud and corruption risks is ensured by the internal documents regulating employees' activities and limiting the scope of authorities (policies, procedures and regulations, the Code of Ethics and other documents). Furthermore, to increase the efficiency of fraud and corruption risk management, Latvenergo Group carries out risk mitigation activities and improves its preventive and detective (for example, report preparation and data comparisons, consistency checks) controls. Management of fraud and corruption risks is assessed by the Internal Audit operational unit ensuring independent evaluation of effectivity of control activities.

G4-SO5

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## Total value of political contributions by country and recipient/ beneficiary

In compliance with the requirements of the legal acts of the Republic of Latvia and the Corporate Social Responsibility Policy, Latvenergo Group does not make

any monetary and/or non-monetary contributions to political organisations.

G4-SO6

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## Total number of legal actions for anti-competitive behaviour, anti-trust, and monopoly practices and their outcomes

In 2015, no cases of anti-competitive behaviour or misuse of the dominant position by Latvenergo Group

have been identified, and no court proceedings against Latvenergo Group have been initiated or are ongoing.

G4-SO7

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## Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with laws and regulations

Latvenergo Group ensures compliance of its operations with the applicable legislation, and no significant fines

or non-monetary sanctions were imposed in 2015 for any failure by the Group to comply with the legislation.

G4-SO8



## 2.3 Product Responsibility

### Management Approach

Latvenergo Group continues the strategic course towards strengthening its position on the Baltic market and becoming a recognizable and competitive electricity market player in all three Baltic States. Operations of the Group are targeted at developing and offering of electricity products and services that meet the needs of customers, and increasing the value of the *Elektrum* product brand. At the same time, Latvenergo Group is striving to achieve a high customer satisfaction level and building of long-term and mutually rewarding relationships with various customer segments. Taking into account the increasing competition in the open electricity market, the Group strategy focuses on cost-effectiveness and operational excellence.

Care for customer satisfaction and loyal relationship building

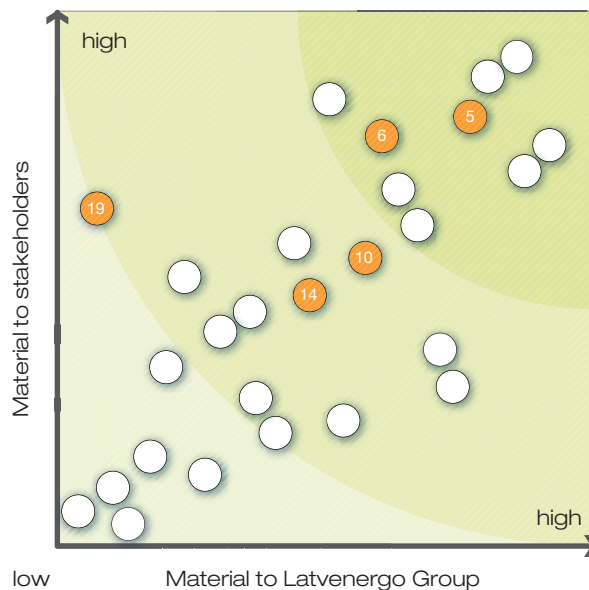
In 2015, the most important event in the electricity supply was the market opening for households in Latvia from 1 January. Thus, in 2015 Latvenergo Group supplied the whole amount of electricity on the open electricity market. Likewise, by the end of 2015 the majority of households in Latvia had selected Latvenergo as their electricity supplier. To secure and strengthen the leading electricity supplier position, in 2015, Group activities were focussed on three areas:

#### Development of new sales and customer relationship management processes and systems in compliance with the requirements of the liberalised market

In 2015, Latvenergo Group introduced a new billing system, completely separating the databases of the electricity supplier and the distribution system operator, and ensuring full compliance of the customer service and billing processes with the open electricity market conditions. With the opening of the electricity market, Latvenergo Group organised extensive information campaigns for Latvian households about changes in the billing procedure and services.

To secure the leading position of electricity supplier, the Group continued the development of the *Elektrum* product brand, promoting its recognition and the image

### Product Responsibility Materiality Matrix \*



\* see Section 1.9 "Materiality Assessment"

of a friendly supplier. Along with the promotion of *Elektrum* electricity products, the *Elektrum* brand name was also given to the *elektrum.lv* customer self-service portal and to the "Elektrum Friendly Benefits" customer loyalty programme. For the purpose of advertisement of the brand image also a range of partnership projects were implemented in cooperation with the "Lottemaa" family theme park, the *Positivus* music festival and the lighting object contest organised within the festival, and with the New Riga Theatre.

In December 2015, promoting the recognition of the *Elektrum* brand, an advertising agreement was signed with the Latvian Olympic Committee, providing for a possibility for *Elektrum* to use its graphical identity and place advertisement at the Olympic Centres in Latvia. The agreement also includes an arrangement on allocation of the *Elektrum* name to the Olympic Sports Centre in Riga. The agreement was signed for a period of two years for the amount of EUR 370 thousand.

#### Contribution to customer satisfaction

In 2015, improvements and activities were made to develop convenient customer service options:

- New billing services, such as automated billing and SMS billing, were developed and introduced for



customer convenience;

- With the transition to the new billing system, the *elektrum.lv* customer self-service portal was updated, ensuring convenient customer access to information from various electronic devices;
- At the end of the year, a new *Elektrum* mobile application was introduced with enhanced capabilities of electricity consumption and market price analysis, and with a new functionality added, facilitating the selection of energy-efficient light bulbs.

To promote the customer loyalty, Latvenergo Group implements the “*Elektrum* Friendly Benefits” programme available on the *elektrum.lv* portal, which was visited by more than 230 thousand customers during the year. In 2015, improvements were made to the programme and range of offers was increased.

Through customer surveys conducted during the development of major and national level communication campaigns, their comprehensibility and compliance with customer needs are tested, enabling their adjustment to customer interests and ensuring maximum efficiency.

To ensure high-quality customer service, in cooperation with sociological research agencies, Latvenergo Group conducts regular customer satisfaction and loyalty surveys, identifying the service aspects to be developed and improved. The level of customer satisfaction is measured across several aspects: overall satisfaction with the company, its services, customer service, payment options, information availability and content. Customer satisfaction and loyalty are evaluated separately in the household and business customer segments (see the G4-PR5 indicator).

#### **Promotion of cost-effectiveness and development of operational excellence approaches**

The Group conducts regular customer surveys to ensure effective communication with customers and to further develop its products and services. In 2015, along with the annual customer satisfaction and loyalty surveys, a more comprehensive study of customer choices and behavioural models in the open electricity market was conducted, specifying customer perception and needs regarding the form and content of billing information, as well a perception study of the *Elektrum* brand and its positioning was conducted.

Latvenergo Group encourages and promotes cost-effective service provision and service formats, such as reporting of electronic meter readings via the customer self-service portal. This type of reporting is used by approximately 75% of the Group’s customers.

#### **Customer service channels**

To maintain a high level of customer satisfaction and service quality and availability, access to a number of service channels is offered for customer convenience. In Latvia, customer service is ensured through the following channels: *elektrum.lv* self-service portal, customer service by phone and on site at Customer

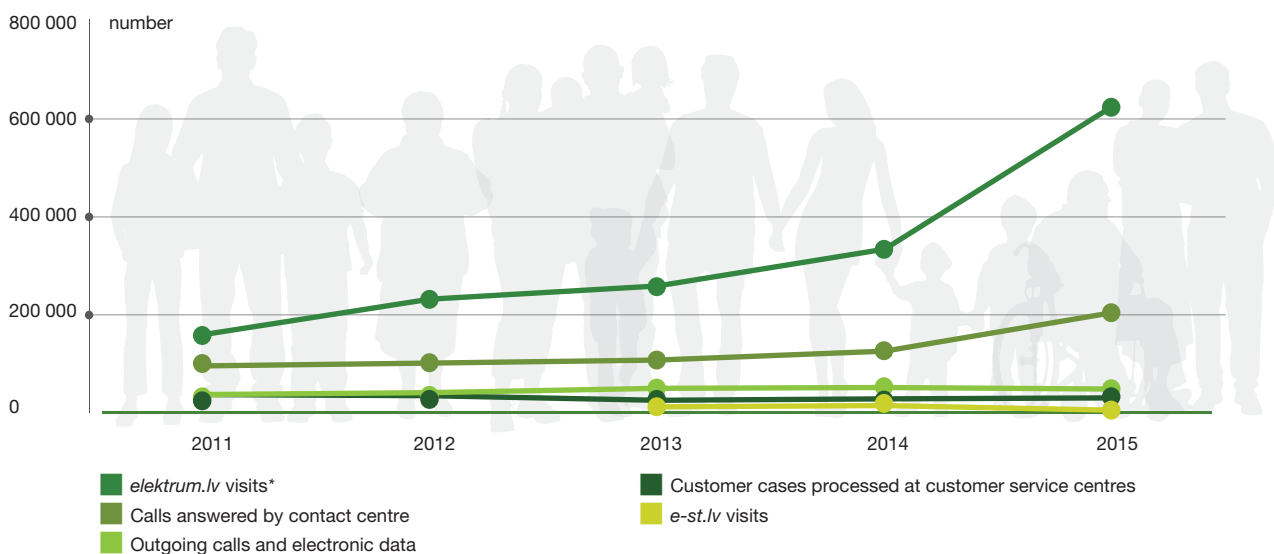


Service Centres; customers are offered an option to submit questions electronically via e-mail, and customer issues are also addressed in social networks. In Lithuania and Estonia, customer service is ensured via the *elektrum.ee* and *elektrum.lt* portals, as well as by phone. Residents who are not Latvenergo Group customers, are also provided a possibility to submit complaints or applications through the aforementioned customer service channels (except customer self-service portals).

The most popular customer service channel is the *elektrum.lv* self-service portal, and the number of visits in 2015 has increased by 87% compared to the previous year. The increase of the number of online visits was largely due to the electricity market opening and the associated possibilities to select electricity product offers, sign contracts or change the payment method on the portal, as well as to the mass notification campaign conducted at the end of the year about the annual recalculation of the balanced payments. In 2015, the monthly average number of unique portal users was over 625 thousand. As a result of the electricity market opening activities, in 2015, the number of customers serviced by phone also increased: the free call centre handled an average of 204 thousand incoming calls per month, or by 62% more compared to the previous year. The 10 Latvenergo Group Customer Service Centres serviced an average of 25 thousand customers per month. Each month, 43 thousand customers were serviced electronically – by e-mail or by processing the voice mail messages.

Overall, in 2015, the monthly average number of customer contacts through various service channels in Latvia was 924 thousand per month, which is a 69% increase over the previous year. Out of those, only 319 customers had complaints, representing less than a tenth of a percent of the Group customers. 10% of the complaints were substantiated and 9% were partially substantiated. Responses were given operationally: 69% of the complaints were handled within 15 days.

## Average number of customer cases serviced per month (2011 – 2015)



\* previously e-latvenergo.lv

## Customer service quality

In contact with customers Latvenergo Group ensures compliance of information with the legislation of Latvia and the EU and with the standards of fair competition, as well as the Group values, the Code of Ethics and policies.

Latvenergo Group has extensive customer databases, and their processing and maintenance complies with all the statutory requirements in terms of data security and confidentiality. Customer service processes are adapted in order to ensure the confidentiality of the data. Data safety and protection is ensured during customer authorisation on the customer portal, providing access to sensitive customer service information, and in direct communication activities with customers.

Latvenergo Group has determined several key performance indicators in order to assess the customer service efficiency: customer call response service level (percentage of calls answered, calls answered within 30 seconds), complaints and applications responded to within 15 days. Although compared to previous years customer activity had significantly increased, the high customer service indicators were maintained also in 2015.

## Ensuring service availability

To ensure the clarity of Latvenergo Group services and availability of convenient services for the widest possible range of customers, the Group provides customer services over the phone, electronically and in person also in Russian and English languages. Information on Latvenergo Group <http://www.latvenergo.lv>, <http://www.sadalestikls.lv> websites and *elektrum.lv*, *elektrum.ee*, *elektrum.lt* and *e-st.lv* customer self-service portals is available not only in the respective national languages, but also in Russian and English, and the <http://www.let.lv> website is available in English as well. The informative and advertising materials about the Company's services disseminated at Latvenergo Group Customer Service Centres are also available in Russian.

Latvenergo Group Customer Service Centres ensure access for customers with reduced mobility and wheelchair users. To reduce the waiting times for customers with children and for pregnant women, a separate queue has been arranged for them.

## Customer service key performance indicators in Latvia (2011 – 2015)

|                                  | Unit | Method | 2011 | 2012 | 2013 | 2014 | 2015 |
|----------------------------------|------|--------|------|------|------|------|------|
| Calls answered                   | %    | m/c    | 89   | 90   | 92   | 90   | 90   |
| Calls answered within 30 seconds | %    | m/c    | 77   | 82   | 86   | 78   | 78   |
| Claims answered in 15 days       | %    | m/c    | 52   | 58   | 63   | 75   | 69   |

m – measured, e – estimated, c – calculated



## Quality and safety of electricity distribution services

Sadales tīkls AS is the largest distribution system operator in Latvia (approximately 834 thousand customers), covering approximately 99% of the territory of Latvia. The operations of Sadales tīkls AS are based on the provision of safe electricity supply services to the residents of Latvia.

Sadales tīkls AS seeks to ensure the highest possible quality of the services provided. The customer service processes are being continuously improved. If provision of electricity distribution services is found to be inconsistent with the quality requirements, the customers are compensated the losses incurred.

The key performance indicator characterising the quality of electricity supply and under an increased focus of Sadales tīkls AS is the average electricity supply interruption, calculated on a per-customer-per-year basis and expressed as the frequency (SAIFI) and duration in minutes (SAIDI).

Electricity supply interruption indicators are subdivided into scheduled and unscheduled interruptions. The scheduled supply interruptions are associated with planned network maintenance repair and network construction works. The frequency of unscheduled supply interruptions is determined by the historical technical solutions of the electricity grid, damages due to adverse weather conditions (storms, snow-breaks, floods, etc.), and damages caused by third parties or theft.

To reduce the duration of unscheduled power outages, the following activities were continued in 2015:

- replacement of overhead lines in forested areas with cables for a total length of 210 km;
- electricity line maintenance and electricity rights-of-

way clearance works for a length of 5,452 km;

- 164 remote-controlled circuit breakers installed for isolation of electricity lines in densely populated areas and forested rural areas, technically and morally obsolete circuit breakers replaced with the ones offered by latest technologies.

Plans for the coming years include a greater attention and preventive measures to reduce the frequency and duration of power outages for customers by continuing construction of new cable lines, carrying out clearance works of electricity transmission line corridors, implementing new technical solutions, improving the existing processes, and by reviewing regulatory documents and cooperation arrangements with contractors.

The priority of Sadales tīkls AS is the provision of safe energy services. Accidents at Sadales tīkls AS electrical installations are most frequently caused by third party negligence – touching 20 kV electricity line wires with machinery, disregarding the requirements of the Protection Zone Law in their business operations.

Sadales tīkls AS carries out a variety of educational activities to reduce the number of electrical injuries and accidents, including lectures at schools and other educational institutions, and educational work at events devoted to electricity safety organised by institutions supervising operations with tractor machinery and agricultural activities. Within the scope of those activities, Sadales tīkls AS employees explain in their lectures the nature of electrical hazards and the behaviour in the event of each specific accident. To raise the electrical safety issues in the virtual environment, an Electrical safety site (*Elektrodrošība*) has been created in the *draugiem.lv* social network, as well a Section “Electrical safety” is maintained at the homepage of Sadales tīkls AS.

## Results of surveys measuring customer satisfaction

### G4-PR5 Supply of electricity

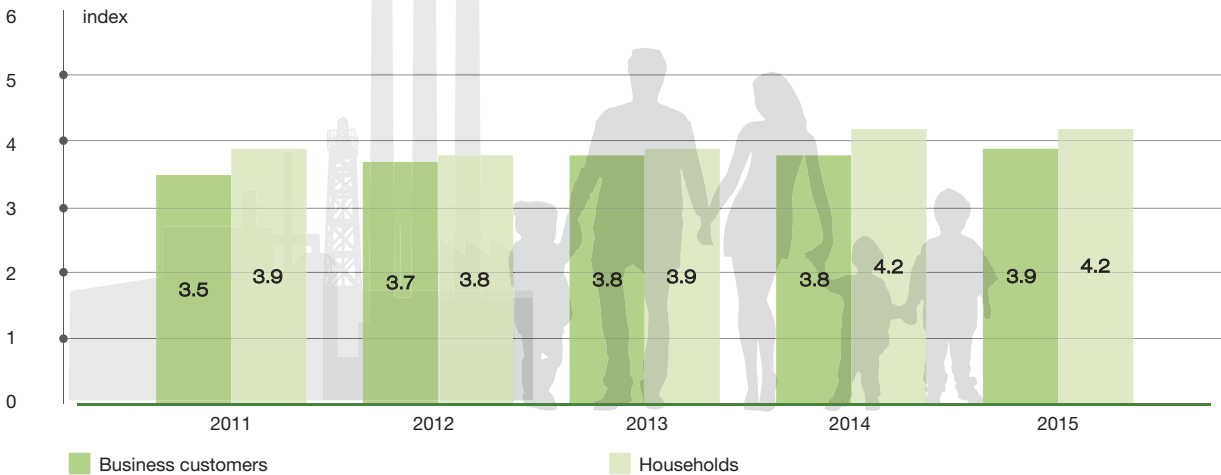
In 2015, the customer satisfaction level remained steadily high among households and slightly increased in the business segment. Generally, customers associate Latvenergo with stability, reliability and quality services.

Customer satisfaction level is measured by customer satisfaction index on a 6-point scale. The aspects receiving the highest rating from households are the delivery convenience of meter readings, payment options in general, and customer service options. Corporate customers, in turn, have given the highest rating to payment options and service employees. A positive fact is that Latvenergo AS has managed

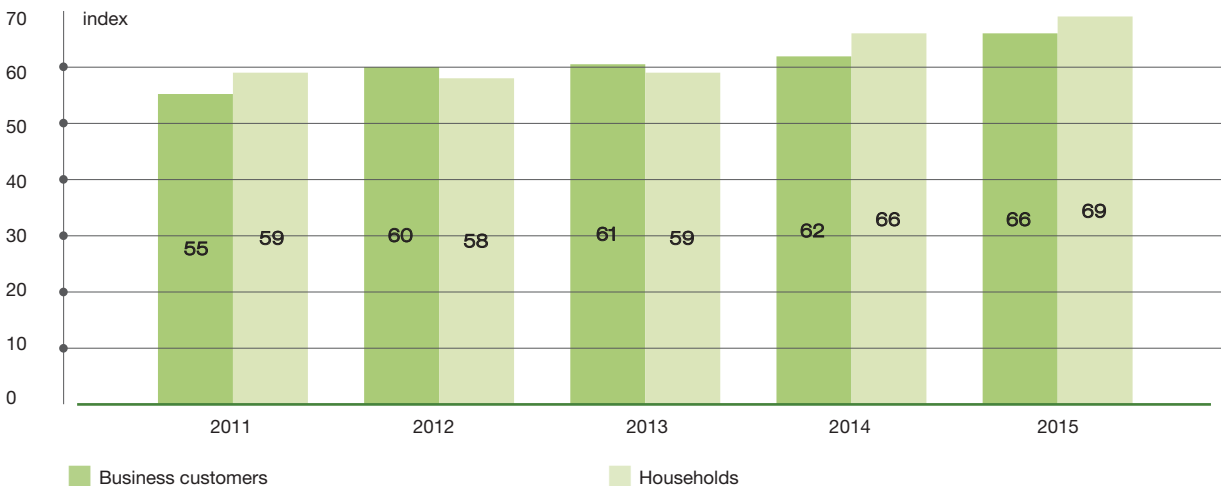
to significantly increase the net promoter score (NPS): from - 6 in the previous year to + 16 in 2015 for households and from - 13 to - 1 for businesses, which indicates to a higher customer readiness to recommend Latvenergo services to others.

Customer satisfaction with Latvenergo AS also correlates with the increase of loyalty. In 2015, the customer loyalty index has significantly increased among both households and businesses. The customer loyalty index is measured by evaluating the aspects of customers' behaviour, future intentions, and rational and emotional ties with the service provider on a scale of 100.

### Customer satisfaction index among business customers and households in Latvia (2011 – 2015)



### Customer loyalty index among business customers and households (2011 – 2015)

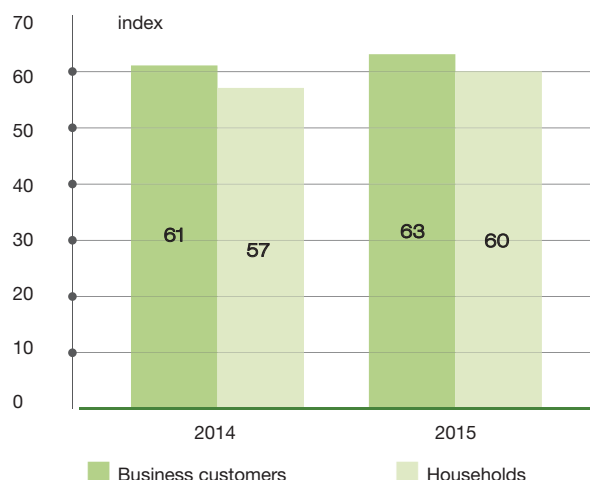


### Distribution services

In 2014, Sadales tīkls AS introduced a customer satisfaction index which enables comparison of the company's service and communication channel evaluations with international customer retention benchmarks, and successive evaluation of the customer satisfaction index and its aspects, by comparing the results with those of the previous year.

In 2015, the overall customer satisfaction index was together 61 index points (households – 60, business customers – 63), which is not a significant change compared to the previous year (59 index points together) and is considered medium high. Stable indicators suggest that communication, customer relationship management and other activities have been effective, i.e., the set of activities related to the opening of the electricity market has been implemented successfully.

### Sadales tīkls AS customer satisfaction index among households and business customers (2014– 2015)



### Total number of incidents of non-compliance with regulations and voluntary codes concerning marketing communications, including advertising, promotion, and sponsorship, by type of outcomes

No cases of noncompliance of Latvenergo Group marketing activities with legal or voluntary provisions

have been identified in 2015.

G4-PR7

### Total number of substantiated complaints regarding breaches of customer privacy and losses of customer data

In 2015, five justified (2014: one) and six unjustified (2014: one) complaints were registered concerning alleged customer data privacy violations. The errors in customer data processing were eliminated immediately after the receipt of the complaints.

The higher number of complaints is related to the increased customer sensitivity and the focus on personal data protection, to large extent furthered by the overall level of customer awareness and the rising relevance of the topic in the public opinion.

G4-PR8

### Monetary value of significant fines for non-compliance with laws and regulations concerning the provision and use of products and services

In 2015, compensations for damages to electrical equipment due to distribution network disruptions were paid in 66 cases for a total amount of EUR 23.0 thousand (2014: 71 cases totalling EUR 31.3 thousand).

A reduced electricity distribution tariff for inadequate voltage quality was applied to 163 customer sites (2014: 156).

G4-PR9

### Reparation for electrical lesions associated with disruptions in distribution system power grids (2011-2015)

|                  | Unit      | Method | 2011 | 2012 | 2013 | 2014 | 2015 |
|------------------|-----------|--------|------|------|------|------|------|
| Reparation cases | number    | m      | 56   | 83   | 97   | 71   | 66   |
| Amount paid      | thsd. EUR | m      | 16.2 | 20.0 | 43.3 | 31.3 | 23.0 |

m – measured, e – estimated, c – calculated

## Number of injuries and fatalities to the public involving company assets, including legal judgments, settlements and pending legal cases of diseases

EU25

Sadales tīkls AS carries out a variety of educational activities to reduce the number of electrical injuries and accidents. In 2015, an increased attention was paid to educating on electrical safety issues persons engaged in agricultural, logging and construction works: participation in sector events and development and dissemination of informative materials. In 2015,

50 persons suffered from electrical injuries, including 16 children (2014: 68 electrical injuries, including 17 to children). Seven accidents occurred in 2015 (2014: three) involving third parties exposure to voltage. Two fatalities occurred in 2015 (2014: zero). There have been no court proceeding during the period.

### The number of accidents to third parties (2011 – 2015)

|              | Unit   | Method | 2011     | 2012     | 2013     | 2014     | 2015     |
|--------------|--------|--------|----------|----------|----------|----------|----------|
| Fatal        | number | m      | 3        | 4        | 2        | 0        | 2        |
| Serious      | number | m      | 0        | 1        | 1        | 1        | 0        |
| Not serious  | number | m      | 2        | 3        | 6        | 2        | 5        |
| <b>TOTAL</b> |        |        | <b>5</b> | <b>8</b> | <b>9</b> | <b>3</b> | <b>7</b> |

m – measured, e – estimated, c – calculated

## Percentage of population unserved in licensed distribution or service areas

EU26

The service area specified in the electricity distribution licence covers 99% of the territory of the Republic of Latvia. Electricity distribution is ensured to approximately 834 thousand electricity distribution

service customers. Electricity distribution services are provided to all households that have concluded agreements on electricity supply within the service area specified in the licence.

## Power outage frequency (SAIFI) and average power outage duration (SAIDI)

EU28

EU29

In 2015, the reduced duration of scheduled power outages was principally due to the action plan to lower the SAIDI indicator implemented by Sadales tīkls AS, and the introduced control and reporting system. One of the measures provides that the duration of a scheduled outage (unless objectively justified) may not exceed 7 hours, and 6 hours during the period between 1 November 2015 and 1 April 2016. The reduced duration of unscheduled outages was ensured by the network automation investment programme.

The lower SAIFI indicator in 2015 was due to the clearance of 20 kV overhead line corridors, replacement of 20 kV overhead lines with 20 kV cables, as well as simultaneous work of several teams from various functions during the scheduled outages, and the commencement of active voltage works in the low-voltage network.

### System Average Interruption Frequency Index (SAIFI) (2011 – 2015)

|  | Unit          | Method | 2011       | 2012       | 2013       | 2014       | 2015       |
|--|---------------|--------|------------|------------|------------|------------|------------|
| Unscheduled: natural phenomena (massive damage)        | number        | m/c    | 1.5        | 0.5        | 0.6        | 0.4        | 0.2        |
| Unscheduled: damage (incl. if caused by third parties) | number        | m/c    | 3.2        | 3.4        | 2.9        | 2.4        | 2.1        |
| Scheduled: network maintenance and overhaul            | number        | m/c    | 0.9        | 0.9        | 1.0        | 1.0        | 0.8        |
| <b>TOTAL SAIFI</b>                                     | <b>number</b> |        | <b>5.6</b> | <b>4.8</b> | <b>4.5</b> | <b>3.8</b> | <b>3.2</b> |

m – measured, e – estimated, c – calculated

## System Average Interruption Duration Index (SAIDI) (2011 – 2015)

|  | Unit           | Method | 2011       | 2012       | 2013       | 2014       | 2015       |
|--|----------------|--------|------------|------------|------------|------------|------------|
| Unscheduled: natural phenomena (massive damage)        | minutes        | m/c    | 416        | 116        | 149        | 57         | 18         |
| Unscheduled: damage (incl. if caused by third parties) | minutes        | m/c    | 293        | 255        | 192        | 153        | 126        |
| Scheduled: network maintenance and overhaul            | minutes        | m/c    | 236        | 265        | 280        | 256        | 206        |
| <b>TOTAL SAIDI</b>                                     | <b>minutes</b> |        | <b>945</b> | <b>636</b> | <b>621</b> | <b>466</b> | <b>350</b> |

m – measured, e – estimated, c – calculated





## 2.4 Environmental Protection

### Management Approach

Latvenergo Group is aware of the role of environmental protection in sustainable development and implements its key principles in all of its operations. To meet the current needs without compromising the needs of future generations and keep the environment and natural resources, Latvenergo Group organises its operations and plans its development, taking into account environmental, economic and social aspects.

With the improvement in technology, the impact on the environment is diminishing

#### Environmental Policy

The key principles of Latvenergo Group in relation to environmental issues are consolidated in its Environmental Policy. One of the priority Environmental Policy issues is to reduce the impact on climate change in accordance with the initiatives and decisions of the European Parliament, the Council, and the Commission. The following key principles of the Environmental Policy characterise the environmental philosophy of the Group and its attitude towards the environment:

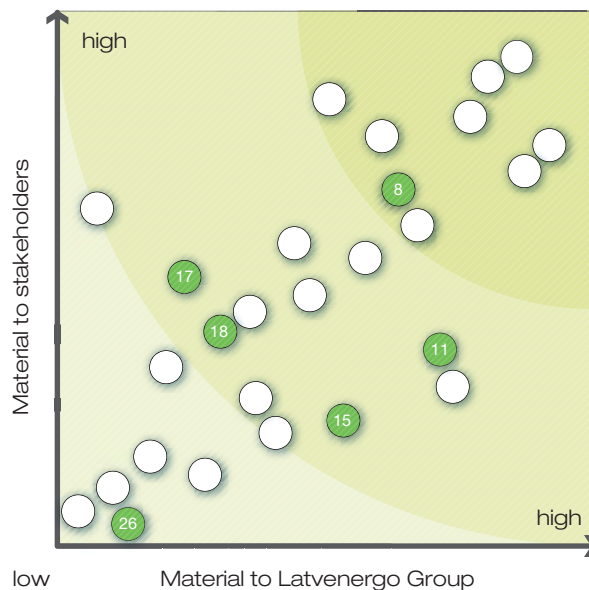
- effective management of the environmental risks in all business areas of Latvenergo Group;
- reduction in pollutant emissions and the Group's impact on climate change;
- efficient use of natural resources;
- fostering the preservation of biodiversity;
- assessment of the environmental impact of investment projects in development planning and minimisation of the harm caused to the environment;
- regular and open information to the society and stakeholders about environmental activities;
- acting in an environmentally friendly way and urging the society and partners to act in the same manner;
- stimulating the inclusion of the key principles of *green* procurement into procurement procedures.

#### Resource and energy consumption

An increasing attention is being paid to an efficient use of resources at both national and European level, which is especially promoted by the implementation of the requirements of the EU Energy Efficiency Directive and the EU level commitment to reduce the consumption of primary energy resources by 20% by 2020, which is a

serious challenge to the energy sector.

Environmental Protection aspects in the Materiality Matrix\*



\* see Section 1.9 "Materiality Assessment"

The Group is proud of its achievements in generating electricity from renewable sources, its goal-oriented behaviour and environmentally friendly technologies. In 2015, about half of the total electricity output of Latvenergo Group comes from renewable energy sources, while the remaining part was generated at combined heat and power plants fuelled by the most environmentally-friendly fossil fuel – natural gas.

To strengthen its position as one of the environmentally friendliest power supply utilities in Europe, Latvenergo Group is proactively dealing with environmental issues and improving its environmental performance. Latvenergo Group continues the implementation of investment projects leading not only to technological improvements, but also to reduction of environmental impact from the generation processes and facilities. In 2015, Latvenergo issued *green* bonds, earmarking the gains for projects limiting climate change and reducing its effects, including the promotion of energy efficiency and use of renewable resources, and improving flood and the associated risk management. More information about *green* bonds and related projects is available in Annex "Report on *Green* Bonds".



The use of efficient and modern technologies is one of the main methods to save resources and reduce emissions. One of the CHPPs' performance indicators is the fuel utilization efficiency. For the reconstructed facilities of Latvenergo Group CHPPs, this indicator is between 86% and 90% in cogeneration mode, and may decrease to 48% in condensation mode. Compared to condensation mode in cogeneration mode, savings of primary energy resources are achieved. In 2015, the use of the cogeneration potential resulted in 26.5% (TEC-1) and 15% (TEC-2) savings of primary energy resources.

#### **Compliance with environmental requirements**

To ensure compliance with the environmental protection legislation, Latvenergo Group actively cooperates with national environmental institutions, providing information related to environmental protection, ensuring compliance with the provisions of permits for polluting activities, and consulting on issues related to environmental protection.

#### **Air pollution**

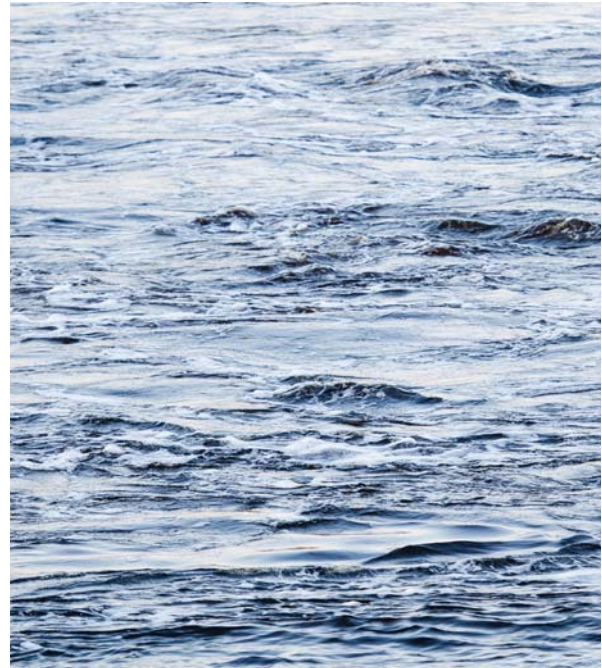
One of the most topical global environmental issues is greenhouse gas-induced climate change. Modernization of Latvenergo Group facilities, replacing older and less efficient facilities with ones complying with the Best Available Techniques reference documents, is a significant contribution to the reduction of climate change and the achievement of the set goals.

Latvenergo Group climate change activities comply with the climate change policy targets defined by the Latvian policy planning documents, including the Environmental policy guidelines for the period 2014-2020 and the Energy Development Guidelines for 2016-2020, as well as the EU climate goals.

On the way towards the CO<sub>2</sub> emission reduction target, changes are expected in the operation of the EU Emission Trading Scheme (EU ETS). Latvenergo Group expects that the drafting and implementation of the new legislation will create fair and equal conditions for the EU ETS participants and the prices of emission allowances will reflect the advantages of efficient and environmentally friendly technologies on the electricity market.

#### **Biodiversity**

Preservation of biodiversity and mitigation of the environmental impact of Latvenergo Group operations are among the key principles of the Group's Environmental Policy. In its operations, the Group plans



and implements measures that are aimed at preserving biodiversity. The main initiatives in this field are bird protection and the replenishment of fish stocks.

#### **Environmental management and energy efficiency**

The ability of Latvenergo Group to develop and to enhance its environmental performance is confirmed by its Environmental Management System, implemented and certified in compliance with the ISO 14001 standard. As a follow-up to the issue of the EU Energy Efficiency Policy implementation, actively discussed at both sectoral and company level in Latvia and in other Member States, in 2015, the Environmental Management System of the Groups facilities was complemented with an energy assessment process. One of the energy efficiency elements is the obligation for large companies to conduct energy audits and plan energy efficiency measures. Latvenergo Group so far has focused on efficient use of energy resources, as evidenced by the inclusion of energy management principles into the certified Environmental Management System. Latvenergo Group will continue the progress also in 2016, with the aim of introducing and certifying the energy management system in compliance with the ISO 50001 standard.

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## Materials used by weight or volume and energy consumption within the organization

Latvenergo Group uses renewable energy sources (water, wind, wood) as well as fossil fuel (primarily natural gas and other types of fuel in smaller amounts) for generation of electricity and thermal energy. In 2015, renewables accounted for 25% of the total consumption of energy resources. Other energy resources mostly consisted of fossil fuel.

Generation of electricity and thermal energy require a different proportion between renewable and fossil energy resources. In 2015, 38% of the consumption of primary energy resources for electricity generation were constituted by renewables and 62% – by the environmentally friendly fossil fuel – natural gas. The high proportion of renewable energy sources was

G4-EN1  
G4-EN3

## Consumption of primary energy resources (2011 – 2015)

|                                      | Unit | Method | 2011   | 2012   | 2013   | 2014   | 2015   |
|--------------------------------------|------|--------|--------|--------|--------|--------|--------|
| Water, wind*                         | TJ   | m/c    | 10,177 | 13,072 | 10,278 | 6,946  | 6,511  |
| Natural gas                          | TJ   | m/c    | 21,618 | 17,364 | 20,168 | 17,459 | 19,194 |
| Wood                                 | TJ   | m/c    | 49     | 147    | 522    | 718    | 693    |
| Others (diesel fuel, fuel oil, coal) | TJ   | m/c    | 6      | 1      | 1      | 6      | 2      |

\* the amount of resources evaluated as the amount of energy generated using these resources (3.6 GJ = 1 MWh)  
m – measured, e – evaluated, c – calculated

## Direct energy consumption by primary energy source for electricity generation (2011 – 2015)

|              | Unit | Method | 2011   | 2012   | 2013   | 2014  | 2015   |
|--------------|------|--------|--------|--------|--------|-------|--------|
| Water, wind* | TJ   | m/c    | 10,177 | 13,072 | 10,278 | 6,946 | 6,511  |
| Natural gas  | TJ   | m/c    | 11,388 | 6,746  | 10,253 | 8,391 | 10,910 |
| Wood         | TJ   | m/c    |        | 14     | 59     | 173   | 181    |

\* the amount of resources evaluated as the amount of energy generated using these resources (3.6 GJ = 1 MWh)  
m – measured, e – evaluated, c – calculated

## Direct energy consumption by primary energy source for thermal energy generation (2011 – 2015)

|                                      | Unit | Method | 2011   | 2012   | 2013  | 2014  | 2015  |
|--------------------------------------|------|--------|--------|--------|-------|-------|-------|
| Natural gas                          | TJ   | m/c    | 10,231 | 10,618 | 9,915 | 9,068 | 8,284 |
| Wood                                 | TJ   | m/c    | 49     | 133    | 463   | 545   | 512   |
| Others (diesel fuel, fuel oil, coal) | TJ   | m/c    | 6      | 1      | 1     | 6     | 2     |

m – measured, e – evaluated, c – calculated

primarily ensured by generation of electricity at the Daugava HPPs. For thermal energy generation, in turn, renewable energy sources represented 6% of the total consumption of primary energy resources. Woodchips are used for thermal energy generation at the Kegums boiler house and Liepaja generation facilities: a biomass-fired cogeneration power plant and a biomass-fired boiler house.

The share of renewables in the overall energy resource consumption over the years depends on the amount of energy generated, which in turn is determined by hydrological conditions and market factors (see Section 1.10.1 “Generation and Supply”).

In 2015, the amount of electricity generated from renewable resources (water, wind, wood) was 1,824 GWh, while 2,058 GWh were generated using natural gas as the fuel. The amount of thermal energy generated from wood (woodchips) was 163 GWh or 7% of the total amount of thermal energy generated by Latvenergo Group, and 2,256 GWh or 93% of the total amount were generated by using natural gas and in a small amount – diesel fuel.

In 2015, energy consumption for generation processes (own use) was 174 GWh.

In 2015, fuel used for vehicles includes 1,511 thousand litres of petrol, 2,221 thousand litres of diesel fuel, and 2.3 thousand litres of autogas.

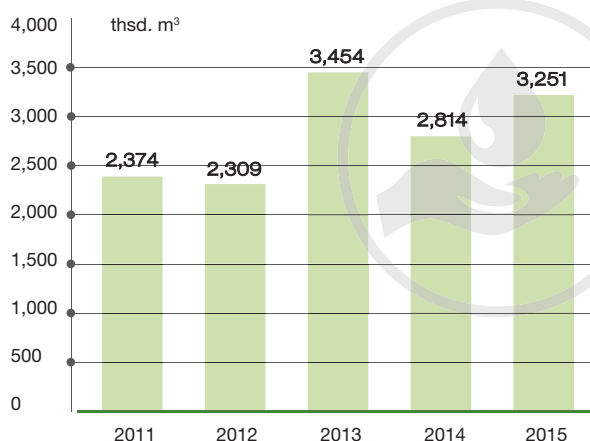
## Total water withdrawal by source

G4-EN8 Latvenergo Group uses water resources mainly for the support of generation processes. A relatively small amount of water is used for various technological needs and also for water supply to external consumers.

The water consumption balance of Latvenergo Group includes surface, underground and supply system water. In 2015, water used for operational needs amounted to 3,251 thousand m<sup>3</sup>, including 3,054 thousand m<sup>3</sup> of surface water, 125 thousand m<sup>3</sup> of underground water and 72 thousand m<sup>3</sup> of supply system water.

The largest consumer of surface water resources is Riga TEC-2, which in 2015 consumed 3,047 thousand m<sup>3</sup> of water for generation needs (2014: 2,582 thousand m<sup>3</sup>), 2,684 thousand m<sup>3</sup> from that amount is used for cooling.

## Total water withdrawal (2011 – 2015)



The consumption of water resources at Riga TEC-2 is affected by the operational modes of generation facilities and the amount of energy generated. The

largest consumer of underground water is Riga TEC-1, which consumed 53 thousand m<sup>3</sup> of underground water to feed the heating networks.

## Description of significant impacts of activities, products, and services on biodiversity in protected areas and areas of high biodiversity value outside protected areas

### Bird protection

Latvenergo Group cooperates with the LOS to address the bird protection and research issues. A particular attention is paid to the issue of protecting the white storks. For the fifth year, Latvenergo Group jointly with the LOS have been implementing the White Stork Monitoring project to gather information on white stork population in Latvia. At least 12,000 white stork couples nest in Latvia. Power line poles are the most frequent sites selected by these birds for building nests. 9,194 white stork nests were placed on electricity line poles in 2015. To ensure compliance with the safety requirements of electricity supply and reduce the number of white stork deaths on electric lines, following the approval from environmental authorities, 942 potentially dangerous nests were removed from electricity line poles in 2015. During the stork nesting period, the birds are disturbed only in exceptional cases when the safety of electricity supply or people is endangered.

In 2015, Latvenergo Group participated in the “Birds and us” programme (*Putni un mēs*) for schools, organised by the LOS, within which the LOS conducted training sessions at several schools, prepared information materials and awarded the most active schools, furthering teachers’ and children’s understanding of and interest in birds.

### Fish resource replenishment and reinforcement of the Daugava riverbanks

In compliance with the applicable laws, Latvenergo Group makes annual contributions to replenish fish stocks (EUR 1,035.5 thousand in 2015) and invests in reinforcement of the Daugava River banks and maintenance of engineering protective structures/embankments (EUR 1,209.4 thousand in 2015).

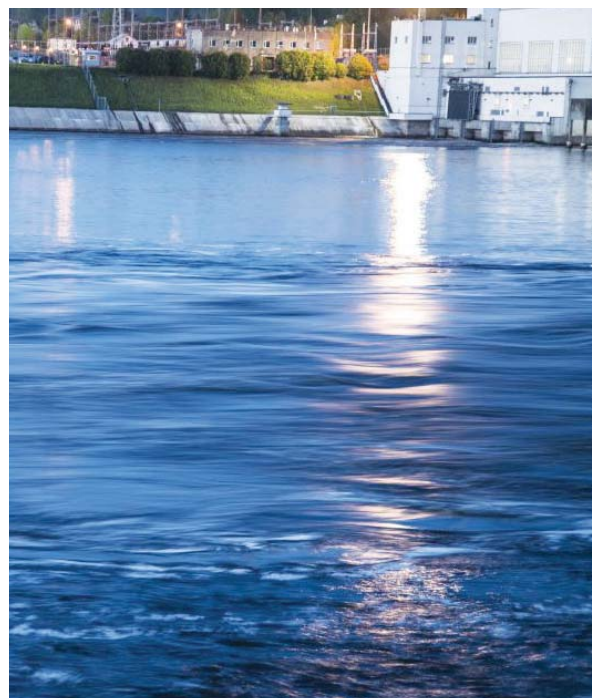
These funds are earmarked for both artificial replenishment of fish stocks and for works to maintain the protective structures and reinforce the riverbanks, thereby mitigating the impact of the Daugava HPPs on fish resources and deformation of the banks of the Daugava. 610.6 thousand salmon and sea trout smolts and fries and 731.2 thousand pike perch, whitefish and vimba fries, along with 9.8 million pike and lamprey larvae were released into the Daugava River basin in 2015.

In 2015, Latvenergo Group continued cooperation with the “We for Fish” (*Mēs zivīm*) society: in May 2015, artificial spawning nests were placed in the Kegums HPP reservoir to stimulate the replenishment of common fish species within the Daugava River basin.

In addition to the above-mentioned fish stock replenishment activities, Latvenergo Group organised events significantly reducing fish mortality during the lowering of the water level for the performance of the necessary repair works at HPPs during the summer period. Lowering of the water levels at Riga HPP and Aiviekste HPP reservoirs was performed in optimal HPP operation modes, and transfer of fish from the uncovered areas was organised in cooperation with the “We for Fish” society.

In cooperation with local and foreign experts, the study of fish migration and natural replenishment possibilities in the Daugava basin initiated in 2013 were continued. A study of Atlantic salmon behaviour was started in 2014 using the radio telemetry method. The experiment involved tagging salmon with radio signal transmitters, enabling researchers to identify the location of each individual fish. The study started in 2014 and planned continuation in 2015 was affected by weather conditions uncharacteristic for the autumn period (floods in the Ogre river in 2014, a very low water level and inflow in 2015), as a result of which the behaviour study of the Atlantic salmon was postponed to 2016. The results of the study will be used in the planning of other scientifically justified fish stock protection activities in the Daugava River, supplementing the current ones.

G4-EN12



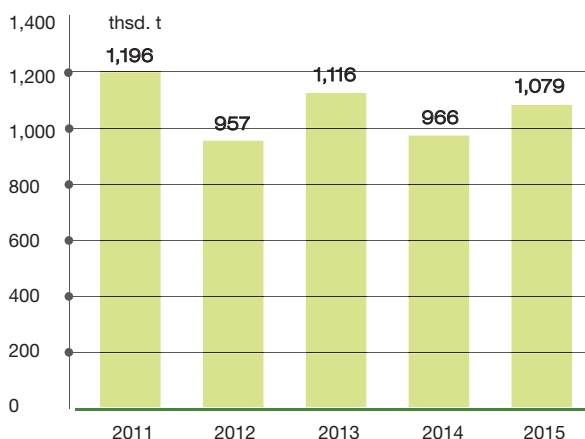
## Direct greenhouse gas (GHG) emissions (Scope 1)

G4-EN15 The volume of direct greenhouse gas emissions of Latvenergo Group is determined by the fuel consumption, which, in turn, depends on the amount of energy generated and the operational modes selected by the facilities. In 2015, the combustion plants of Latvenergo Group emitted 1,079 thousand tonnes of CO<sub>2</sub>, which is an increase of 113 thousand tonnes compared to the previous year (for CO<sub>2</sub> emission amount per one MWh see indicator G4-18). The CO<sub>2</sub> emission increase in comparison to the previous year was mainly due to the fact that in 2015 Riga CHPPs increased the electricity generation by 23%, and consequently the fuel consumption.

The volume of the Group's CO<sub>2</sub> emissions includes emissions from both the facilities that participate in the EU ETS (combustion plants with total rated thermal input exceeding 20 MW) and non-participating facilities (8.9 tonnes of CO<sub>2</sub>).

In addition to the above volumes, CO<sub>2</sub> emissions also result from the use of fuel by Latvenergo Group vehicles. In 2015, the volume of CO<sub>2</sub> emissions from vehicles was 9.5 thousand tonnes or less than 1% of total emissions.

### CO<sub>2</sub> emissions (2011– 2015)

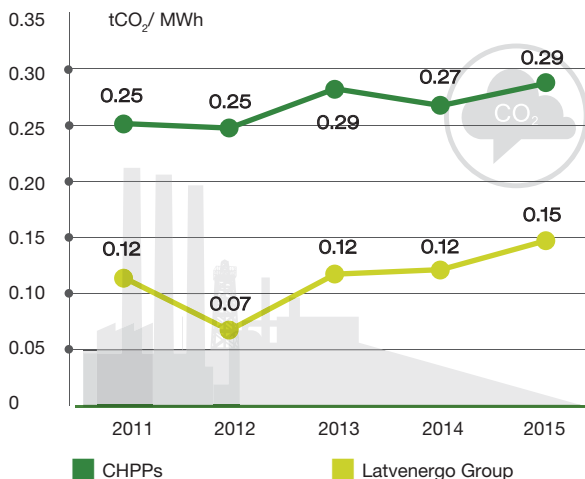


## Greenhouse gas (GHG) emissions intensity

G4-EN18 The specific CO<sub>2</sub> emission indicators per unit of electricity generated by the entire Group characterise the allocation and efficiency of renewable energy sources and fossil fuel – the lower these indicators, the larger the share of electricity that may be generated from renewable energy sources, and the higher the performance efficiency of the CHPP facilities. In 2015, CO<sub>2</sub> emissions per unit of energy generated were 0.15 t CO<sub>2</sub>/MWh<sub>el</sub>, with 0.29 t CO<sub>2</sub>/MWh<sub>el</sub> at Riga CHPPs alone.

In 2015, in addition to larger volumes of electricity generated by Riga CHPPs, the increase in the overall CO<sub>2</sub> emission intensity was also determined by the 6% decrease in electricity generated by the Daugava HPPs due to the unusually low water inflow.

### CO<sub>2</sub> emissions per unit of electricity generated (2011– 2015)



## NO<sub>x</sub>, SO<sub>x</sub> and other significant air emissions

G4-EN21 The emission of harmful substances into the atmosphere depends directly on the amount of energy generated, the type of fuel used, the efficiency of its consumption, and the technology. Latvenergo Group uses renewable energy sources, such as water, wind, and wood, and also fossil fuel (primarily natural gas, and diesel as a back-up fuel for Riga TEC-1 and Riga TEC-2 heat only boilers).

- Natural gas is one of the most environmentally friendliest type of fossil fuel, and Latvenergo Group uses it not only at its CHPPs, but also at small boiler houses if possible. However, apart from carbon

dioxide, combustion of natural gas emits into the atmosphere other harmful substances. These are nitrogen oxides (NO<sub>x</sub>) and carbon monoxide (CO);

- When burning diesel fuel, insignificant amounts of sulphur dioxide (SO<sub>2</sub>) and particulate matter emissions are produced. Diesel fuel emits hydrocarbons during storage;
- Thermal energy generation at Group boiler houses and at the Liepaja bio-cogeneration plant is based on woodchips. Wood combustion produces NO<sub>x</sub>, CO and particulate matter emissions.

Emission volumes from combustion plants complying with the provisions of the Industrial Emissions Directive are determined based on continuous emission measurement results. Emissions from small and medium-sized combustion plants (up to 50 MW installed capacity) are determined with the help of emission factors under the regulatory acts.

With the completion of the Riga CHPPs reconstruction project, older, less efficient facilities were replaced with new ones, complying with the Best Available Techniques reference documents developed by the European Commission, and resulting in a significant reduction of specific emissions and concentration levels of harmful substances, especially nitrogen oxides (NO<sub>x</sub>), in flue gases. For electricity generation at the reconstructed Riga TEC-2 power units, NO<sub>x</sub> emissions per unit of energy generated were only 0.17 kg/MWh (Group level – 0.09 kg/MWh), which is a 73% decrease compared to the emissions before the reconstruction

(0.6 kg/MWh). As a result of the implementation of the Riga TEC-2 reconstruction project, the statutory requirements specifying the emission limit values of NO<sub>x</sub> and CO emissions in flue gases have been met: NO<sub>x</sub> – 50 mg/m<sup>3</sup>, and CO – 100 mg/m<sup>3</sup> at a standardised O<sub>2</sub> content of 15% for gas turbines.

In 2015, the NO<sub>x</sub> emission increase in comparison with the previous year was due to larger amounts of energy generated by Riga CHPPs.

To limit pollutant emissions from combustion plants and to comply with the threshold values specified by the regulatory acts, Latvenergo Group performs pollutant monitoring and accounting, and planning and implementation of energy efficiency and environmental protection activities. Modernisation of facilities is important in terms of both efficiency and environmental protection.

### NO<sub>x</sub>, CO, SO<sub>2</sub> and other emission (2011 - 2015)

|                 | Unit | Method | 2011 | 2012 | 2013 | 2014 | 2015 |
|-----------------|------|--------|------|------|------|------|------|
| NO <sub>x</sub> | t    | m/c    | 912  | 674  | 792  | 623  | 737  |
| CO              | t    | m/c    | 356  | 336  | 397  | 415  | 319  |
| SO <sub>2</sub> | t    | c      | 5    | 0    | 3    | 1    | 4    |
| Other*          | t    | c      | 10   | 10   | 14   | 17   | 4    |

\* including emissions of solid particles, vanadium, hydrocarbons  
m – measured, e – evaluated, c – calculated

### Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with environmental laws and regulations

No breaches of environmental protection requirements have been identified at Latvenergo Group facilities in 2015.

In 2015, fifteen planned thematic inspections were performed by the State Environmental Service of the Ministry of Environmental Protection and Regional

Development of the Republic of Latvia, and one planned inspection by the Health Inspectorate of the Ministry of Health of the Republic of Latvia. No material remarks or sanctions have been issued by the controlling bodies as a result of the inspections of Group operations in 2015, and no fines were paid. G4-EN29

### Allocation of CO<sub>2</sub> emissions allowances or equivalent, broken down by carbon trading framework

The third phase of the EU ETS was launched in 2013. In contrast to the previous arrangements, the new regulations grant free emission allowance units only for thermal energy generation, and until 2020 the number of allowance units granted is gradually reduced to 30% of the necessary amount.

In 2015, Riga CHPPs were granted 392,255 allowance units (2014: 442,778) and Liepaja generation facilities - 29,855 allowance units (2014: 29,025). One allowance unit is equivalent to one tonne of CO<sub>2</sub> emitted. EU5



## 2.5 Employees and Work Environment

### Management Approach

Latvenergo Group management acknowledges that its greatest value is employees and their various competencies and diversity, which fosters high performance results. The Group's employees are unique, they differ not only by gender, age, experience and knowledge, but also by their needs. Therefore, the Group is improving the systems already in place to ensure employee development, engagement, and greater flexibility of the motivation programmes introduced. We believe that employee diversity is not an obstacle, but rather an opportunity to look at things from a different perspective and thus achieve better results.

The Group continuously attracts good managers and leaders capable of driving Group's development and ensuring compliance of employee knowledge with the company's future needs, and assist in achieving the company's goals. The Group management has set the creation of an innovative environment as one of its priorities for 2015, boosting employee development and a sense of belonging to the company as the basis for their personal improvement and successful future growth of the company.

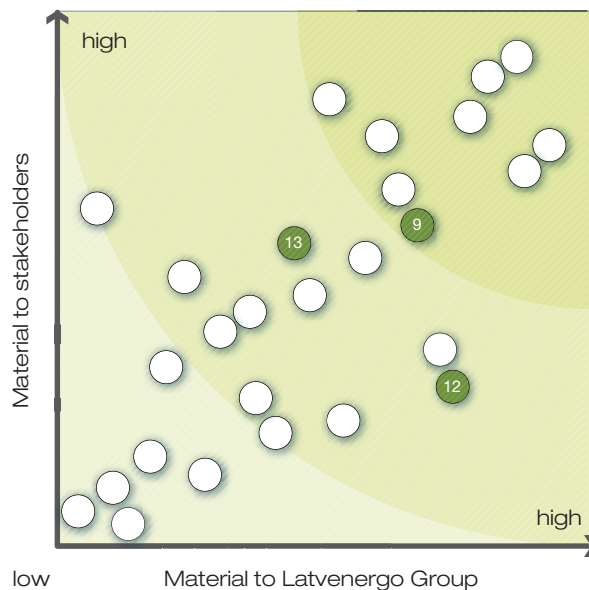
Work environment promotes employees' development and sense of belonging

The principal tasks of Latvenergo Group human resources management are subject to its strategy and aimed at ensuring that the conduct of each and every employee is in line with the values of the Group: responsibility, efficiency and openness. Latvenergo Group facilitates a safe and motivating work environment, by providing for a possibility for employees to engage in the Group processes, advancing exchange of information, taking care of labour safety, developing staff competencies, ensuring knowledge continuity and promoting work-life balance.

#### Employee engagement and awareness

Work performance and productivity depend on the employees' sense of engagement and belonging. Therefore, annual anonymous surveys are conducted to find out their opinion. The surveys are processed by

Employment and Work Environment aspects in the Materiality Matrix\*



\* see Section 1.9 "Materiality Assessment"

service provider, and the Group only receives a report of the results of the survey. The 2015 survey data show that the number of respondents has increased. The results also indicates positive trend in employee satisfaction and loyalty indicators, with the highest rating achieved in recent years.

In 2015, the Group continued the improvement of employee self-service system, which is available to all employees both at the workplace and outside of it. This system ensures fast and efficient exchange of information, a possibility to set tasks and targets, and to give feedback of task execution control and performance evaluation.

#### Safe work environment

Latvenergo Group pays a special attention to creating a safe work environment. Occupational safety measures are covered by the Collective Bargaining Agreement. As an employer, Latvenergo Group provides its employees with adequate workplaces for the fulfilment of their duties, appropriate individual means of protection and technical resources, as well as organises employee training on occupational safety and safe working methods. The core business divisions of Latvenergo

Group have implemented and maintain an occupational safety management system compliant with the requirements of the OHSAS 18001 standard.

Occupational safety measures apply not only to Latvenergo Group employees, but also to employees of the Group's service providers. The Group instructs and trains employees of all contractors on safe performance of work.

In 2015, Latvenergo Group paid a special attention to employee opinion about the safety of work environment, particularly to the impact of psychological and emotional factors on their health and performance results.

#### Developing employee competencies

Latvenergo Group takes care of the development of employees' competencies, increasing efficiency and linking the Group's common goals with the employee's individual tasks and objectives. To fairly and appropriately evaluate the contribution of each employee, a work performance evaluation system has been established by the Group according to which base salaries are defined based on employee competencies and labour market trends, while the variable part of salaries is linked to the performance quality and achievement of targets. Latvenergo Group encourages employee involvement, training, awareness and exchange of experience. Employees' professional knowledge and skills are improved through both internal and external training (see indicator G4-LA9).

#### Knowledge continuity

The operational specifics of Latvenergo Group require that in order to ensure a sustainable development, it is essential to accumulate and transfer knowledge, including well-considered and balanced replacement of retirement age employees. To ensure continuity and carry out socially responsible work for future development of the labour force as a whole, the

Group encourages accumulation of knowledge and its transfer to colleagues and potential employees, such as students. Latvenergo Group cooperates with educational institutions in Latvia, encouraging studies in the field of energy and providing students with paid internship opportunities at Group companies. The Group ensures a balanced generational replacement (see indicator EU15).

#### Work-life balance

Latvenergo Group recognizes that employees' opinions about the right work-life balance and the perception of the issue may differ. Moreover, this perception may change depending on the career development stage and family situation.

Work-life balance is of great importance to us. Therefore, starting from April 2015, the Group has introduced an benefit option system, enabling employees to receive a part of the fringe benefits guaranteed in addition to those envisaged by regulatory acts, in the desired proportions. According to employees' personal priorities at the benefit option system they may vary between additional free days, contribution to the pension fund and support for health improvement.

#### Number of employees and the Collective Bargaining Agreement

Latvenergo Group constantly improves its processes to ensure that its employee structure is efficient and optimal in size. At the end of 2015, Latvenergo Group employed 4,177 people. A transfer of 430 employees to Augstsprieguma tīkls AS was made along with the transfer of transmission system asset construction and maintenance functions. As a result, at the end of 2015 the number of employees at Latvijas elektriskie tīkli AS (lease of transmission system assets segment) dropped to 11 people. No significant changes in the number of employees of other segments have taken place during the last five years.

G4-10

G4-11

### Distribution of employees by operating segments (2011 – 2015)

|                                     | Unit          | Method | 2011         | 2012         | 2013         | 2014         | 2015         |
|-------------------------------------|---------------|--------|--------------|--------------|--------------|--------------|--------------|
| Generation and supply               | number        | m      | 920          | 940          | 971          | 989          | 992          |
| Distribution                        | number        | m      | 2,543        | 2,502        | 2,505        | 2,545        | 2,568        |
| Lease of transmission system assets | number        | m      | 493          | 438          | 444          | 443          | 11           |
| Corporate functions                 | number        | m      | 534          | 577          | 592          | 586          | 606          |
| <b>TOTAL</b>                        | <b>number</b> |        | <b>4,490</b> | <b>4,457</b> | <b>4,512</b> | <b>4,563</b> | <b>4,177</b> |

m – measured, e – evaluated, c – calculated

The structure of Latvenergo Group employees has a relatively high proportion of male individuals: 73% male and 27% female. This is related to the industry specifics, requiring a large number of technical positions.

The majority of employment contracts at Latvenergo Group are concluded on a full-time basis and for an indefinite period. Only 8 employees or 0.2% of the total workforce had part-time agreements (0.1% of male and

0.3% of female employees of the Group), which is close to the previous year's figures. Only 3% (2014: 2%) of the employment contracts were concluded for a fixed-term (1% of male and 6% of female employees). The slight increase in the number of fixed-term contracts is related to the electricity market opening for households and additional positions in the customer service area. Harmonisation of the social and economic interests of Latvenergo Group employees is ensured through

the Collective Bargaining Agreement concluded between Latvenergo AS, Sadales tīkls AS, Latvijas elektriskie tīkli AS, Enerģijas publiskais tirgotājs AS and the *Enerģija* trade union. The Agreement provides employees with guarantees or benefits in addition to those envisaged by national regulatory acts. In 2015, the Collective Bargaining Agreement was applicable to 97% of the Group employees, and over the last years this percentage has remained unchanged.

Collective agreements concluded by Latvenergo Group companies apply not only to trade union members,

currently constituting approximately 60% of the total number of the Group employees, but also to all people employed by those companies. Thus, social guarantees ensure equal treatment of all employees and reduce the likelihood of conflict between employees and the employer.

Contractors manage their technical and human resources and the Group supervises their activities performed at the facilities of the Group. The Group does not keep statistics regarding contracted personnel, except for health and safety training.

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### Minimum notice periods regarding operational changes, including whether these are specified in collective agreements

G4-LA4 Latvenergo Group regularly notifies employees and the trade union about its business activities, current events and development. The Latvenergo Collective Bargaining Agreement specifies that the employer must give a no less than one-month prior notice to the

trade union of application for the consent to terminate an employment contract with an employee. Employees must be informed about organisational changes leading to redundancies no later than five days following the decision.

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### Percentage of total workforce represented in formal joint management-worker health and safety committees that help monitor and advise on occupational health and safety programs

G4-LA5 For addressing the labour protection issues, Latvenergo Group cooperates with employee representatives – trustees elected from amongst employees and participating in both the resolution of work environment improvement issues and evaluation of work environment risks. The Group trains the trustees

on work environment matters and allocates time for the performance of those duties. 45 trustees (1% of the total number of employees) were active at the Group in 2015.

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### Health and safety topics covered in formal agreements with trade unions

G4-LA8 Labour protection issues are stipulated by the Collective Bargaining Agreement concluded by Latvenergo AS, Sadales tīkls AS, Latvijas elektriskie tīkli AS and Enerģijas publiskais tirgotājs AS. The Agreement specifies the rights and obligations of the employer, the trade union, employees and trustees in the area of labour protection (see the G4-LA5 indicator).

- to guarantee a safe and healthy work environment;
- perform internal monitoring of the work environment, including its risk evaluation;
- inform employees and trustees about labour safety measures and engage them in the improvement of labour protection.

The main obligations of the employer:

- ensure the operation of the labour protection system

The Collective Bargaining Agreement also specifies the obligations of the employer in the event of accidents at work.

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### Average hours of training per employee by gender, and by employee category

G4-LA9 The Group makes dedicated investments in employee development through both external and internal training. In 2015, an average of 74 hours per employee were devoted to external training, including an average of 92 hours for management positions, 67 hours for

specialists, 79 hours for qualified workers and 100 hours for other positions. Internal training, experience sharing events and discussions involving all employees are organised on a regular basis and not less than once per year.



## Percentage of employees eligible to retire in the next 5 and 10 years broken down by job category and by region

The share of employees who might retire within the next 10 years complies with the Group specifics and its

ability to ensure a balanced generational replacement.

EU15

### Retirement time (2011 – 2015)

| Profession groups                | Unit     | Method | 5 years    |             | 10 years   |             |
|----------------------------------|----------|--------|------------|-------------|------------|-------------|
|                                  |          |        | Women      | Men         | Women      | Men         |
| Managers                         | %        | m/c    | 0.1        | 1.4         | 0.4        | 2.1         |
| Professionals                    | %        | m/c    | 3.1        | 5.6         | 5.5        | 10.3        |
| Craft and related trades workers | %        | m/c    | 0.3        | 4.7         | 0.5        | 9.7         |
| Other professions                | %        | m/c    | 0.9        | 0.4         | 1.9        | 0.5         |
| <b>TOTAL</b>                     | <b>%</b> |        | <b>4.4</b> | <b>12.1</b> | <b>8.4</b> | <b>22.7</b> |

m – measured, e – evaluated, c – calculated

## Percentage of contractor and subcontractor employees that have undergone relevant health and safety training

The Group instructs and trains employees of all contractors on safe performance of works, as required by Latvian energy standards and the mutual agreements signed. The Group's labour protection specialists instruct persons employed by contractors. The instruction and applicable documents on safe

performance of works are also available electronically, with which the personnel of the contractors should familiarize themselves. Therefore, by using various methods all of the employees employed by contractors working at the Group's facilities are instructed.

EU18



## Report on *Green Bonds*

### The first state – owned company in Eastern Europe to issue *green bonds*

On 10 June 2015, Latvenergo AS issued 7-year green bonds in the value of EUR 75 million, with a 1.9% annual interest rate (coupon) and a 1.922% yield, becoming the first state-owned company in Eastern Europe to issue *green bonds*.

The issue was a continuation of Latvenergo AS bond issue launched in 2012. With this, the total value of bonds issued is EUR 180 million, constituting over 20% of Latvenergo Group total borrowings. By issuing bonds, we have diversified our borrowing sources and, with the *green* bond issue we have provided a possibility for investors to invest in environmentally friendly projects. The *green* bond issue is organised by SEB banka AS. On the primary market our *green* bonds have attracted not only investors from the Baltics, but also from Austria, Finland and Germany. By the volume of bonds purchased, 71% were banks, 28% asset managers, and 1% insurance companies.

As of 1 July 2015, the *green* bonds are listed on Nasdaq Riga AS. In honour of the *green* bond listing on the Baltic Bond List, on the first day of trading the Nasdaq Stock Exchange placed a greeting on its billboard in New York, Times Square, welcoming Latvenergo AS *green* bonds to the market. The international credit rating agency Moody's Investors Service has assigned a Baa2 credit rating with a stable outlook to the *green* bonds issued by Latvenergo AS, in line with the company's credit rating.

### Moody's assigns to the *green* bonds a Baa2 (stable) credit rating

The main requirement for *green* bonds is the use of the funds raised only for projects relevant to *green* thinking and related to renewable energy sources, energy efficiency and environment preservation. To ensure the issue of *green* bonds, Latvenergo AS has developed and approved the Green Bond Framework<sup>1</sup>, specifying the selection criteria of eligible projects, their selection



procedure, creation of a special account and regular reporting.

### Green Dark shading assigned by CICERO

The *Green Bond Framework* has also been assessed by an external party – CICERO<sup>2</sup>. The shading given by CICERO – Dark Green, is the highest possible assessment indicating compliance of the planned eligible projects with the long-term environmental protection and mitigation of climate change ambitions, as well as good corporate governance and transparency.

The funds raised within the framework of *green* bonds are allocated to generation (55%), transmission (33%), and distribution projects (12%). At project level, in turn, major eligible projects are the *Kurzeme Ring* and the *Daugava HPP* hydropower unit reconstruction programme. For more information about eligible projects and their costs, project objectives and benefits, see the next table.

<sup>1</sup> A full version of the Green Bond Framework is available on Latvenergo website <http://www.latvenergo.lv/eng/investors/>.

<sup>2</sup> CICERO – the Center for International Climate and Environmental Research, Oslo.

| Latvenergo Group Operating segment (share in total eligible costs) |   |                                |                                     |   |
|--|---|--------------------------------|-------------------------------------|---|
| Projects   | Costs MEUR  | Project group (share of total) | Project objectives and benefits*    |   |
| GENERATION<br>(54.7%)  | Daugava HPPs hydropower unit reconstruction programme and renovation of technological equipment | 22.9                           | RENEWABLE ENERGY<br>(30.5%)         | Extension of useful live of the Daugava HPPs hydropower units maintaining a high share of renewables in the energy mix of Latvia<br>Increasing capacity and efficiency ratios of the hydropower units<br>Increased safety of operation of the Daugava HPPs  |
|  | Renovation of Daugava HPPs and Aiviekste HPP hydro engineering structures                       | 18.1                           | ENVIRONMENT PRESERVATION<br>(24.1%) | Reduction of oil leakage risk into the Daugava River<br>Improvement of the resilience and safety, and extension of useful lives of hydro engineering structures and dams<br>Accident risk probability reduction of dams<br>Efficient flood risk management, reducing the potential impact on the population, property and environment (water quality, species and habitats)   |
|  | Study of migratory fish migrations restoration in the Daugava River                             | 0.07                           | SUSTAINABLE ENVIRONMENT<br>(0.1%)   | Identification of possible measures to be taken in order to compensate more efficiently for the impact of the Daugava HPPs on fish stocks<br>Reduction of an impact on biological diversity   |
| Annual monitoring of white storks                                  | 0.004   |                                |                                     |   |
| DISTRIBUTION<br>(12.2%)  | Smart electricity meters  |                                |                                     | Increasing the security of electricity supply   |
|  | Building and reconstruction of electricity lines and transformer points                         | 9.1                            |                                     | Reduction of electricity losses<br>Improving energy efficiency and operational efficiency   |
| LEASE OF TRANSMISSION SYSTEM ASSETS<br>(33.1%)                     | Kurzeme Ring, Grobiņa-Ventspils connection  | 24.9                           | ENERGY EFFICIENCY<br>(45.3%)        | Network life-time extension<br>Increasing competition in the electricity market<br>Integration of electricity generators in the supply networks using renewable sources, and diversification of electricity supply sources<br>Contribution to the global climate change prevention commitments of Latvia and to the achievement of greenhouse gas emission reduction targets 2020 set for Latvia by the European Parliament and the Council |
|  |   |                                |                                     |   |
| <b>TOTAL</b>   |   | <b>75.0</b>                    |                                     |   |

On 14 April 2016 Latvenergo AS has issued EUR 25 million *green* bonds thus completing the bond programme. Information on allocation of proceeds will

be provided within the next Report on *Green* Bonds. For additional information see [http://www.latvenergo.lv/eng/investors/financial\\_information/bonds/](http://www.latvenergo.lv/eng/investors/financial_information/bonds/)

**Renewable energy** – developing new capacities and reconstruction of the existing capacities of renewable energy - hydro, bio energy (non-food) and wind and related infrastructure

**Energy efficiency** – construction and reconstruction of transmission and distribution networks to decrease network losses and provide possibilities to connect renewable energy; smart grid projects

**Environmental protection** – flood protection, waste and water management

**Sustainable environment** (up to 10 % of the issued amount) – environmental research and development and programs within nature conservation and biodiversity

\* Additional information about the projects is available under the Section 1.10 of the Report "Description of Operating Segments".



# Materiality of Sustainability Aspects and Conformity to GRI Aspects

G4-20

| Sustainability aspect                       | Corresponding GRI aspect  | Importance of aspect   |                  |                                     |
|---|---|--|------------------|-------------------------------------|
|   |   | Generation and supply  | Distribution     | Lease of transmission system assets |
|   |   | Latvenergo AS, Enerģijas publiskais tirgotājs AS, Elektrum Eesti OÜ, Elektrum Lietuva UAB, Liepājas enerģija SIA | Sadales tīkls AS | Latvijas elektriskie tīkli AS       |
| Efficiency of generation plants             | System efficiency<br>Access   |  |                  |                                     |
| Emergency planning                          | Disaster/Emergency planning and response                              |  |                  |                                     |
| Contribution to the economy                 | Economic performance  |  |                  |                                     |
| Public policy making                        | Public policy   |  |                  |                                     |
| Availability and efficiency of distribution | System efficiency<br>Access   |  |                  |                                     |
| Customer satisfaction                       | Product and service labeling  |  |                  |                                     |
| Compliance and fair business                | Anti-corruption<br>Anti-competitive behaviour<br>Compliance (society) |  |                  |                                     |
| Resource consumption in production          | Materials<br>Water  |  |                  |                                     |
| Health and safety                           | Occupational health and safety<br>Employment                          |  |                  |                                     |
| Data security                               | Customer privacy  |  |                  |                                     |
| Environmental compliance                    | Compliance (environmental)  |  |                  |                                     |
| Workplace compliance                        | Labor/ management relations   |  |                  |                                     |
| Employee development                        | Training and education<br>Employment                                  |  |                  |                                     |
| Availability of information                 | Compliance (Product responsibility)<br>Provision of information       |  |                  |                                     |
| Air pollution                               | Emissions   |  |                  |                                     |
| Impact on local communities                 | Local communities<br>Customer health and safety                       |  |                  |                                     |
| Energy consumption                          | Energy  |  |                  |                                     |
| Renewable energy                            | Materials<br>Energy   |  |                  |                                     |
| Fair marketing communications               | Marketing communications  |  |                  |                                     |
| Support received from state                 | Economic performance  |  |                  |                                     |
| Community contribution                      | Economic performance  |  |                  |                                     |
| Biodiversity                                | Biodiversity  |  |                  |                                     |



## GRI Index

### G4-32 General Standard Disclosures

|   |  | Page           | External Assurance |
|---|--|----------------|--------------------|
| <b>Strategy and analysis</b>                      |  |                |                    |
| G4-1  | Statement from the most senior decision-maker of the organization  | 4 – 5          | √                  |
| <b>Organizational Profile</b>                     |  |                |                    |
| G4-3  | Name of the organization   | 12             | √                  |
| G4-4  | Primary brands, products, and services   | 12             | √                  |
| G4-5  | Location of organization's headquarters  | 12             | √                  |
| G4-6  | Countries where there are relevant operations  | 12             | √                  |
| G4-7  | Nature of ownership and legal form   | 12             | √                  |
| G4-8  | Markets served   | 12             | √                  |
| G4-9  | Scale of the reporting organization  | 12 – 13        | √                  |
| G4-10   | Total workforce by employment type, employment contract, and region, broken down by gender   | 87 – 88        | √                  |
| G4-11   | Percentage of employees covered by collective bargaining agreements  | 88             | √                  |
| G4-12   | Supply chain   | 60 – 61        | √                  |
| G4-13   | Significant changes during the reporting period regarding size, structure, ownership or its supply chain   | 12,<br>46 – 58 | √                  |
| G4-14   | Precautionary approach or principle addressed by the organization  | 31 – 32        | √                  |
| G4-15   | Externally developed economic, environmental, and social charters, principles, or other initiatives to which the organization subscribes or endorses | 43             | √                  |
| G4-16   | Memberships in associations and/or national or international advocacy organizations  | 42 – 43        | √                  |
| EU1   | Installed capacity, broken down by primary energy source and by regulatory regime  | 48             | √                  |
| EU2   | Net energy output broken down by primary energy source and by regulatory regime  | 48             | √                  |
| EU3   | Number of residential, industrial, institutional and commercial customer accounts  | 53             | √                  |
| EU4   | Length of above and underground transmission and distribution lines by regulatory regime   | 56 – 57        | √                  |
| EU5   | Allocation of CO <sub>2</sub> emissions allowances or equivalent, broken down by carbon trading framework  | 85             | √                  |
| <b>Identified Material Aspects and Boundaries</b> |  |                |                    |
| G4-17   | Entities included in the organization's consolidated financial statements  | 12             | √                  |
| G4-18   | Reporting principles for defining report content   | 44 – 45        | √                  |
| G4-19   | Material aspects identified in defining report content   | 45, 92         | √                  |
| G4-20   | Material aspects within the organization   | 40 – 41        | √                  |
| G4-21   | Material aspects outside the organization  | 10             | √                  |

|                               |  |                      |   |
|-------------------------------|--|----------------------|---|
| G4-22                         | Effect of any restatements of information provided in previous reports, and the reasons for such restatements. | 10                   | √ |
| G4-23                         | Significant changes from previous reporting periods in the Scope and Aspect Boundaries                         | 10                   | √ |
| <b>Stakeholder Engagement</b> |  |                      |   |
| G4-24                         | List of stakeholder groups engaged by the organization   | 40 – 41              | √ |
| G4-25                         | Basis for identification and selection of stakeholders with whom to engage                                     | 38                   | √ |
| G4-26                         | Approach to stakeholder engagement   | 38                   | √ |
| G4-27                         | Key topics collected through stakeholder engagement  | 38 – 39              | √ |
| <b>Report Profile</b>         |  |                      |   |
| G4-28                         | Reporting period (e.g., fiscal/calendar year) for information provided   | 10                   | √ |
| G4-29                         | Date of most recent previous report (if any)   | 10                   | √ |
| G4-30                         | Reporting cycle (annual, biennial, etc.)   | 10                   | √ |
| G4-31                         | Contact point for questions regarding the report or its contents   | 10                   | √ |
| G4-32                         | GRI Index with respect to the 'in accordance' option chosen  | 93 – 96              | √ |
| G4-33                         | External assurance for the report  | 98 – 99              | √ |
| <b>Governance</b>             |  |                      |   |
| G4-34                         | Governance structure   | 20                   | √ |
| <b>Ethics and Integrity</b>   |  |                      |   |
| G4-56                         | Organization's values, principles, standards and norms of behavior   | 13, 20 – 21, 30 – 31 | √ |

### Specific Standard Disclosures

| Material Aspects                          | DMA and Indicators | Page   | Omissions | External Assurance |   |
|---|--------------------|--|-----------|--------------------|---|
| <b>Economic Performance</b>               |                    |  |           |                    |   |
| Aspect: Economic performance              | G4-DMA             | 64   | –         | √                  |   |
|   | G4-EC1             | Direct economic value generated and distributed  | 65        | –                  | √ |
|   | G4-EC4             | Financial assistance received from government  | 66        | –                  | √ |
| Sector specific aspect: System efficiency | G4-DMA             | 64 – 65  | –         | √                  |   |
|   | EU11               | Average generation efficiency of thermal plants by energy source and by regulatory regime  | 66        | –                  | √ |
|   | EU12               | Distribution losses as a percentage of total energy  | 67        | –                  | √ |
| <b>Environmental Protection</b>           |                    |  |           |                    |   |
| Aspect: Materials                         | G4-DMA             | 80   | –         | √                  |   |
|   | G4-EN1             | Materials used by weight or volume   | 81 – 82   | –                  | √ |
| Aspect: Energy                            | G4-DMA             | 80   | –         | √                  |   |
|   | G4-EN3             | Energy consumption within the organization   | 81 – 82   | –                  | √ |
| Aspect: Water                             | G4-DMA             | 80   | –         | √                  |   |
|   | G4-EN8             | Total water withdrawal by source   | 82        | –                  | √ |
| Aspect: Biodiversity                      | G4-DMA             | 81   | –         | √                  |   |
|   | G4-EN12            | Description of significant impacts of activities, products, and services on biodiversity in protected areas and areas of high biodiversity value outside protected areas | 83        | –                  | √ |

|  |         |  |         |   |   |
|--|---------|--|---------|---|---|
| Aspect:<br>Emissions                         | G4-DMA  |  | 81      | – | √ |
|  | G4-EN15 | Direct greenhouse gas (GHG) emissions (Scope 1)  | 84      | – | √ |
|  | G4-EN18 | Greenhouse gas (GHG) emissions intensity   | 84      | – | √ |
|  | G4-EN21 | NOx, SOx, and other significant air emissions  | 84 – 85 | – | √ |
| Aspect:<br>Compliance                        | G4-DMA  |  | 81      | – | √ |
|  | G4-EN29 | Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with environmental laws and regulations  | 85      | – | √ |
| <b>Employment and Work Environment</b>       |         |  |         |   |   |
| Aspect: Labor/<br>Management<br>relations    | G4-DMA  |  | 87      | – | √ |
|  | G4-LA4  | Minimum notice periods regarding operational changes, including whether these are specified in collective agreements   | 88      | – | √ |
| Aspect:<br>Occupational<br>health and safety | G4-DMA  |  | 86      | – | √ |
|  | G4-LA5  | Percentage of total workforce represented in formal joint management-worker health and safety committees that help monitor and advise on occupational health and safety programs | 88      | – | √ |
|  | G4-LA8  | Health and safety topics covered in formal agreements with trade unions  | 88      | – | √ |
| Aspect: Training<br>and education            | G4-DMA  |  | 87      | – | √ |
|  | G4-LA9  | Average hours of training per year per employee by gender, and by employee category  | 88      | – | √ |
| Aspect:<br>Employment                        | G4-DMA  |  | 86      | – | √ |
|  | EU15    | Percentage of employees eligible to retire in the next 5 and 10 years broken down by job category  | 89      | – | √ |
|  | EU18    | Percentage of contractor and subcontractor employees that have undergone relevant health and safety training   | 89      | – | √ |
| <b>Society</b>                               |         |  |         |   |   |
| Aspect: Local<br>communities                 | G4-DMA  |  | 70      | – | √ |
|  | G4-SO1  | Percentage of operations with implemented local community engagement, impact assessments, and development programs   | 70      | – | √ |
| Aspect: Anti-<br>corruption                  | G4-DMA  |  | 68      | – | √ |
|  | G4-SO4  | Communication and training on anti-corruption policies and procedures  | 70      | – | √ |
|  | G4-SO5  | Confirmed incidents of corruption and actions taken  | 71      | – | √ |
| Aspect: Public<br>policy                     | G4-DMA  |  | 69      | – | √ |
|  | G4-SO6  | Total value of political contributions by country and recipient/beneficiary  | 71      | – | √ |
| Aspect: Anti-<br>competitive<br>behaviour    | G4-DMA  |  | 68      | – | √ |
|  | G4-SO7  | Total number of legal actions for anti-competitive behaviour, anti-trust, and monopoly practices and their outcomes  | 71      | – | √ |

|   |        |  |         |   |   |
|---|--------|--|---------|---|---|
| Aspect:<br>Compliance   | G4-DMA |  | 68      | – | √ |
|   | G4-SO8 | Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with laws and regulations  | 71      | – | √ |
| Aspect:<br>Customer health and safety                             | G4-DMA |  | 75      | – | √ |
|   | EU25   | Number of injuries and fatalities to the public involving company assets, including legal judgments, settlements and pending legal cases of diseases   | 78      | – | √ |
| Sector specific aspect: Disaster/ Emergency planning and response | G4-DMA |  | 69      | – | √ |
| <b>Product Responsibility</b>                                     |        |  |         |   |   |
| Aspect: Product and service labeling                              | G4-DMA |  | 73      | – | √ |
|   | G4-PR5 | Results of surveys measuring customer satisfaction   | 76 – 77 | – | √ |
| Aspect:<br>Marketing communications                               | G4-DMA |  | 74      | – | √ |
|   | G4-PR7 | Total number of incidents of non-compliance with regulations and voluntary codes concerning marketing communications, including advertising, promotion, and sponsorship, by type of outcomes | 77      | – | √ |
| Aspect:<br>Customer privacy                                       | G4-DMA |  | 74      | – | √ |
|   | G4-PR8 | Total number of substantiated complaints regarding breaches of customer privacy and losses of customer data  | 77      | – | √ |
| Aspect:<br>Compliance   | G4-DMA |  | 74      | – | √ |
|   | G4-PR9 | Monetary value of significant fines for non-compliance with laws and regulations concerning the provision and use of products and services   | 77      | – | √ |
| Sector specific aspect: Provision of information                  | G4-DMA |  | 74      | – | √ |
| Sector specific aspect: Access                                    | G4-DMA |  | 75      | – | √ |
|   | EU26   | Percentage of population unserved in licensed distribution or service areas  | 78      | – | √ |
|   | EU28   | Power outage frequency (SAIFI)   | 78      | – | √ |
|   | EU29   | Average power outage duration (SAIDI)  | 78      | – | √ |
|   | EU30   | Average plant availability factor by energy source and by regulatory regime  | 67      | – | √ |





## Glossary

|                 |  |            |   |
|-----------------|--|------------|---|
| ACCA            | Association of Chartered Certified Accountants                   | LCCI       | Latvian Chamber of Commerce and Industry                                      |
| AS              | <i>akciju sabiedrība</i><br>(Eng. Joint Stock Company)           | LGA        | local government agency   |
| BIAC            | Business and Industry Advisory Committee                         | LIAA       | Investment and Development Agency of Latvia                                   |
| BICG            | The Baltic Institute of Corporate Governance                     | LOS        | Latvian Ornithological Society  |
| CAO             | Chief Administrative Officer                                     | LUA        | Latvian University of Agriculture   |
| CCGT            | combined-cycle gas turbine                                       | MP         | Mandatory procurement   |
| CCO             | Chief Commercial Officer   | MWh        | megawatt hour   |
| CDO             | Chief Development Officer  | NGO        | non-governmental organization   |
| CEO             | Chief Executive Officer  | NPS        | net promoter score  |
| CFO             | Chief Financial Officer  | OECD       | Organization for Economic Cooperation and Development                         |
| CIA             | Certified Internal Auditor                                       | OHSAS      | Occupational Health and Safety Assessment Series of Standards                 |
| CO <sub>2</sub> | carbon dioxide   | OÜ         | <i>Osaühing</i><br>(Eng. Private Limited Company)                             |
| COO             | Chief Operating Officer  | PMB        | the Procurement Monitoring Bureau   |
| COSO            | Committee of Sponsoring Organizations of the Treadway Commission | PSO fee    | public service obligation fee   |
| CSR             | Corporate Social Responsibility                                  | PUC        | Public Utilities Commission   |
| Daugava HPPs    | Daugava hydropower plants  | Riga CHPPs | Riga combined heat and power plants   |
| DMA             | Disclosure on Management Approach                                | Riga TEC-1 | The first combined heat and power plant in Riga                               |
| EBRD            | European Bank for Reconstruction and Development                 | Riga TEC-2 | The second combined heat and power plant in Riga                              |
| ECL             | Employers' Confederation of Latvia                               | RTU        | Riga Technical University   |
| EU              | European Union   | SAIDI      | system average interruption duration index                                    |
| EU ETS          | European Union Emission Trading Scheme                           | SAIFI      | system average interruption frequency index                                   |
| EURELECTRIC     | Union of the Electricity Industry                                | SES        | Stakeholder Engagement Standard   |
| GHG             | greenhouse gas   | SET        | Subsidised Electricity Tax  |
| GRI             | Global Reporting Initiative                                      | SFRS       | State Fire and Rescue Service   |
| HPP             | hydropower plant   | SIA        | <i>sabiedrība ar ierobežotu atbildību</i><br>(Eng. Limited Liability Company) |
| ICOLD           | International Commission on Large Dams                           | TSO        | transmission system operator  |
| IFRS            | International Financial Reporting Standards                      | UAB        | <i>Uždarīti Akcinē Bendrovē</i><br>(Eng. private limited-liability company)   |
| ISO             | International Organization for Standardization                   | WEC LNC    | World Energy Council, Latvian National Committee                              |
| JSC             | joint-stock company  | WPP        | wind power plant  |
| LAHC            | Latvian Association of Heat Supply Companies                     |            |   |
| LAPEEC          | Latvian Association of Power Engineers and Energy Constructors   |            |   |

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## INDEPENDENT AUDITOR'S REVIEW REPORT ON THE SUSTAINABILITY REPORT

To the shareholder of AS Latvenergo

### **Report on the sustainability report**

We have been engaged by the management of AS Latvenergo to perform limited assurance engagement in respect to the Sustainability Report including GRI Content Index as referred to and summarised on page 93-96 of AS Latvenergo and its subsidiaries ('the Group') for the year ended 31 December 2015.

### Management's responsibility for the sustainability report

The Management of the Group is responsible for the preparation and presentation of the Sustainability Report 2015, 'In accordance' - Core criteria of The Global Reporting Initiative Guidelines ('GRI Guidelines'), issued by The Global Reporting Initiative (GRI), a non-profit organisation with secretariat based in Amsterdam, the Netherlands. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the Sustainability Report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. The Management is responsible for ongoing activities regarding the environment, health & safety, quality, social responsibility and sustainable development, and for the preparation and presentation of the Sustainability Report in accordance with the applicable criteria.

### Auditors' responsibility

Our responsibility is to express a conclusion on the Sustainability Report based on our review. We conducted our engagement in accordance with the International Standard on Assurance Engagements (ISAE) 3000 (Revised), 'Assurance engagements other than audits or reviews of historical financial information', issued by the International Auditing and Assurance Standards Board (IAASB).

A review consists of making inquiries, primarily of persons responsible for preparing the Sustainability Report, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with IAASB's Standards on Auditing and Quality Control. The procedures performed consequently do not enable us to obtain an assurance that would make us aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Our assurance does not comprise the assumptions used by the Group or whether or not it is possible for the Group to reach certain future targets described in the report (e.g. goals, expectations and ambitions).

The criteria on which our review is based on are the parts of the "Sustainability Reporting Guidelines, G4" published by GRI as well as the accounting and calculation principles that the Group has developed. We consider these criteria suitable for the preparation of the Sustainability Report.

### Quality

The firm applies International Standard on Quality Control 1 and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

### Independence

We have complied with the independence and other ethical requirements of the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

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**INDEPENDENT AUDITOR'S REVIEW REPORT ON THE SUSTAINABILITY REPORT  
(CONTINUED)**

Our review

Our review has, based on an assessment of materiality and risk, included the following procedures:

- interviews with the responsible management, at group level, subsidiary level, and at selected business units in order to assess if the qualitative and quantitative information stated in the Sustainability Report is complete, accurate and sufficient;
- review of internal and external documents in order to assess if the information stated in the Sustainability Report is complete, accurate and sufficient;
- an evaluation of the design of the systems and processes used to obtain, manage and validate sustainability information;
- verifying the information included in the Sustainability report 2015 through enquires to the relevant management of the Group;
- a reconciliation of financial information with the Group's Consolidated Annual Report for the financial year 2015;
- an assessment of the overall impression of the Sustainability Report, and its format, taking into consideration the consistency of the stated information with applicable criteria,
- testing performance data, on a selective basis, substantively at both an operational and corporate level;
- inspecting documentation to corroborate statements of management and senior executives in our interviews;
- a reconciliation of the reviewed information with the sustainability information in the Group's Consolidated Annual Report for the financial year 2015;

Opinion

Based on our review, nothing has come to our attention that causes us to believe that the Sustainability Report 2015 including GRI Content Index as referred to and summarised on page 93-96 of Latvenergo AS and its subsidiaries has not, in all material respects, been prepared in accordance with the above stated criteria.

SIA Ernst & Young Baltic  
Licence No. 17



Diāna Krišjāne  
Chairperson of the Board  
Latvian Certified Auditor  
Certificate No. 124

Riga,  
19 April 2016





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CONSOLIDATED  
ANNUAL  
REPORT 2015

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FINANCIAL STATEMENTS PREPARED IN ACCORDANCE  
WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS  
AS ADOPTED BY THE EU AND INDEPENDENT AUDITORS'S REPORT



## KEY FIGURES

### Financial figures

|   | 2015             | 2014             | 2013             | 2012             | 2011             |
|---|------------------|------------------|------------------|------------------|------------------|
|   | EUR'000          | EUR'000          | EUR'000          | EUR'000          | EUR'000          |
| Revenue   | 929,128          | 1,010,757        | 1,099,893        | 1,063,691        | 962,453          |
| EBITDA <sup>1)</sup>                            | 307,015          | 236,838          | 248,694          | 244,103          | 254,670          |
| Operating profit <sup>2)</sup>                  | 108,188          | 49,243           | 61,091           | 70,234           | 74,053           |
| Profit before tax <sup>3)</sup>                 | 92,535           | 31,510           | 48,841           | 59,859           | 60,711           |
| Profit  | 85,039           | 29,790           | 46,149           | 50,856           | 62,290           |
| Dividends                                       | 77,413           | 31,479           | 23,605           | 40,618           | 56,773           |
| <b>Total assets</b>                             | <b>3,517,372</b> | <b>3,486,576</b> | <b>3,575,358</b> | <b>3,517,752</b> | <b>3,255,536</b> |
| Non-current assets                              | 3,113,719        | 3,109,253        | 3,128,064        | 3,102,019        | 2,883,583        |
| Total equity                                    | 2,096,702        | 2,020,801        | 2,021,714        | 2,006,975        | 1,923,119        |
| Borrowings                                      | 797,483          | 827,222          | 944,675          | 846,961          | 730,408          |
| Net debt <sup>4)</sup>                          | 692,940          | 706,211          | 689,252          | 604,468          | 575,492          |
| <b>Net cash flows from operating activities</b> | <b>246,278</b>   | <b>135,329</b>   | <b>146,540</b>   | <b>214,526</b>   | <b>256,685</b>   |
| Capital expenditure                             | 190,461          | 177,607          | 224,868          | 264,260          | 282,757          |

### Financial ratios

|  | 2015   | 2014   | 2013   | 2012   | 2011   |
|--|--------|--------|--------|--------|--------|
| Net debt / EBITDA ratio                | 2.3    | 3.0    | 2.8    | 2.5    | 2.3    |
| EBITDA margin <sup>5)</sup>            | 33.0 % | 23.4 % | 22.6 % | 22.9 % | 26.5 % |
| Operating profit margin <sup>6)</sup>  | 11.6 % | 4.9 %  | 5.6 %  | 6.6 %  | 7.7 %  |
| Profit before tax margin <sup>7)</sup> | 10.0 % | 3.1 %  | 4.4 %  | 5.6 %  | 6.3 %  |
| Profit margin <sup>8)</sup>            | 9.2 %  | 2.9 %  | 4.2 %  | 4.8 %  | 6.5 %  |
| Equity-to-asset ratio <sup>9)</sup>    | 60 %   | 58 %   | 57 %   | 57 %   | 59 %   |
| Return on assets (ROA) <sup>10)</sup>  | 2.4 %  | 0.8 %  | 1.3 %  | 1.5 %  | 1.9 %  |
| Return on equity (ROE) <sup>11)</sup>  | 4.1 %  | 1.5 %  | 2.3 %  | 2.6 %  | 3.2 %  |
| Current ratio <sup>12)</sup>           | 1.9    | 1.3    | 1.6    | 1.3    | 1.2    |
| Dividend pay-out ratio <sup>13)</sup>  | 82 %   | 90 %   | 90 %   | 90 %   | 49.6 % |

### Operational figures

|                           |     | 2015          | 2014          | 2013          | 2012          | 2011          |
|---------------------------|-----|---------------|---------------|---------------|---------------|---------------|
| Retail electricity supply | GWh | 7,869         | 8,688         | 7,954         | 8,287         | 8,980         |
| Electricity generated     | GWh | 3,882         | 3,625         | 4,854         | 5,077         | 5,285         |
| Thermal energy supply     | GWh | 2,318         | 2,442         | 2,517         | 2,669         | 2,524         |
| Number of employees       |     | 4,177         | 4,563         | 4,512         | 4,457         | 4,490         |
| Moody's credit rating     |     | Baa2 (stable) | Baa3 (stable) | Baa3 (stable) | Baa3 (stable) | Baa3 (stable) |

1) EBITDA – earnings before interest, income tax, share of result of associates, depreciation and amortisation, and impairment of intangible assets and property, plant and equipment

2) Operating profit – earnings before income tax, finance income and costs

3) Profit before tax – earnings before income tax

4) Net debt – borrowings at the end of the year minus cash and cash equivalents at the end of the year

5) EBITDA margin – EBITDA / revenue

6) Operating profit margin – operating profit / revenue

7) Profit before tax margin – profit before tax / revenue

8) Profit margin – profit / revenue

9) Capital ratio – total equity / total assets

10) Return on assets (ROA) – profit / average value of assets (assets at the beginning of the year + assets at the end of the year / 2)

11) Return on equity (ROE) – profit / average value of equity (equity at the beginning of the year + equity at the end of the year / 2)

12) Current ratio = current assets / current liabilities

13) Dividend pay-out ratio = dividends / profit of the Parent Company

## MANAGEMENT REPORT

Latvenergo Group is the largest power supply company in the Baltic States, operating in generation and supply of electricity and thermal energy, provision of electricity distribution services and lease of transmission system assets.

### Latvenergo Group – the largest power supply company in the Baltic States

Latvenergo Group has successfully maintained the leading electricity supplier position in the Baltics with around 1/3 market share. In 2015 the total amount of supplied electricity to the Baltic retail customers reached 7,869 GWh (2014: 8,688 GWh), of which the amount supplied outside Latvia was about one third.

### As of 1<sup>st</sup> of January 2015 the electricity market is open for households in Latvia

As a result of focused trade activities, in 2015 compared to last year the number of business clients in Estonia and Lithuania was increased by about 33 % compared to the previous year.

Electricity market for households in Latvia is open since 1<sup>st</sup> of January 2015. Until 31<sup>st</sup> of December 2015, the majority of households have chosen Latvenergo AS to keep as their electricity supplier. According to the Electricity Market Law, in 2015, Latvenergo AS has supplied electricity to vulnerable customers (poor or low-income persons, large families) at lower electricity price.

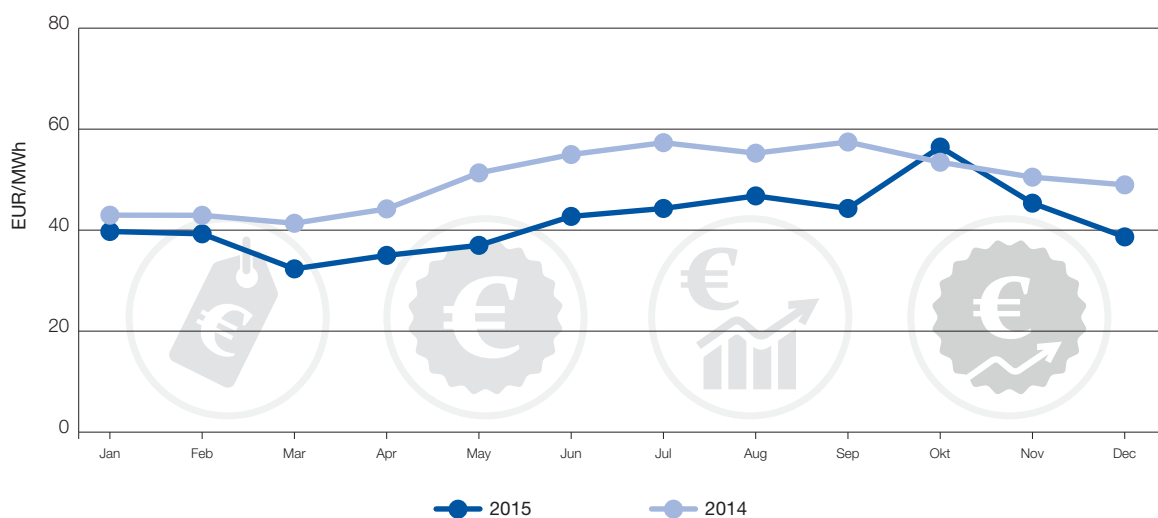
Amount generated by the power plants of Latvenergo Group in 2015 was 3,882 GWh (2014: 3,625 GWh). In Riga CHPPs the electricity generation has increased by 23 %, reaching 2,025 GWh. The increased generation was fostered by 15 % decrease in the average natural gas price compared to 2014. The amount of power generated by Daugava HPPs has decreased by 6% compared to 2014, reaching 1,805 GWh. This was due to unusually low water inflow in the Daugava River. The last time such a low water inflow was observed was back in 1976.

In 2015 the total amount of generated thermal energy was 2,408 GWh (2014: 2,560 GWh). The decrease was due to warmer weather.

In 2015, Latvenergo Group's revenue was EUR 929.1 million (2014: EUR 1,010.8 million). Revenue decline was due to change in accounting principles along with entrance into operation of Enerģijas publiskais tirgotājs AS since 1<sup>st</sup> of April 2014. Mandatory procurement public service obligation (hereinafter – PSO) fee revenues are no longer recognised in the revenue of the Group. Likewise, there was a negative impact on the revenue from: 6 % lower thermal energy output, which was due to a warmer weather; by 2 % lower volume of distributed electricity, which contributed to a EUR 13.0 million decrease in distribution segment revenue; as well as revenue decrease in the transmission system asset lease segment by EUR 14.1 million, due to transmission system asset construction and maintenance function transfer to transmission system operator Augstsprieguma tīkls AS on 1<sup>st</sup> of January 2015.

EBITDA of Latvenergo Group has increased by 30 % reaching EUR 307 million (2014: EUR 236.8 million). EBITDA margin in 2015 has improved and increased to 33 % (in 2014: 23 %).

### Electricity Nord Pool price in Latvia





Latvenergo Group's profit in 2015 is EUR 85.0 million (2014: EUR 29.8 million). The results of the Group were mainly positively impacted by the opening of electricity market for households in Latvia as of 1<sup>st</sup> of January 2015. Until that Latvenergo AS supplied electricity to households at the regulated tariff, which was lower than the market price. In 2014, lost revenues due to electricity supply at the regulated tariff were EUR 48.2 million. Likewise, the results were positively impacted by lower electricity prices in the market.

## EBITDA of the Group has increased

The average electricity spot price in Latvia and Lithuania bidding areas were 16 %, in Estonia – 17 % lower and the natural gas price was 15 % lower than in 2014. The results were negatively affected by 6 % lower output from Daugava HPPs. Additionally the results were negatively affected by lower distributed electricity and thus, lower distribution revenue.

## Investments in environmentally friendly and environmental development projects

In 2015, the total amount of investments was EUR 190.5 million, which is 7 % higher than in 2014. Increase in investments was mainly determined by implementation of Daugava HPPs hydropower unit reconstruction programme thereby contributing to environmentally friendly and environmental development projects. In 2015, the amount invested in Daugava HPPs hydropower unit reconstruction was EUR 31.9 million. To improve the quality of network services, technical parameters and safety of the operations, a significant amount is invested in modernisation of power network. In 2015, the amount invested in the networks represented 62 % of the total investments.

## Diversified borrowing sources

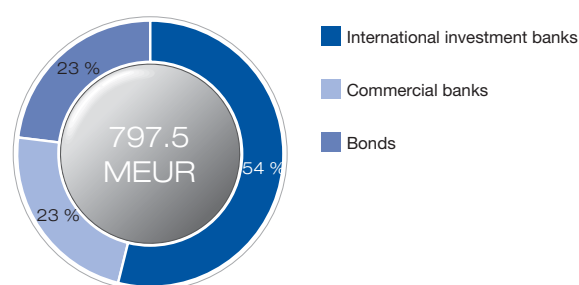
### Financial risk management

Activities of the Latvenergo Group are exposed to a variety of financial risks: market risk, credit risk and liquidity risk. The risk management programme of the Group focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects

Latvenergo Group finances its investment projects from its own resources and external long-term borrowed funds, which are regularly and timely sourced in financial and capital markets. Latvenergo AS issued *green* bonds in the amount of EUR 75 million, the issue was carried out under the second bond offering programme. Total amount of bonds represent more than 1/5 of the total amount of borrowings.

As of 31<sup>st</sup> of December 2015, the net borrowings of Latvenergo Group are EUR 692.9 million (2014: EUR 706.2 million), while the net debt/EBITDA ratio was 2.3 (3.0). Latvenergo Group's capital structure remains strong and at the end of 2015 the capital ratio is 60 % (2014: 58 %).

### Latvenergo group borrowings by categories of lenders



At the beginning of 2015 international rating agency Moody's Investors Service upgraded Latvenergo AS credit rating to Baa2 with a stable outlook. Likewise, in August 2015 the green bonds issued by Latvenergo AS received a Baa2 rating. After the end of the reporting period, on 12<sup>th</sup> of February 2016 *Moody's Investors Service* reconfirmed the rating of Latvenergo AS at the same level.

Latvenergo Group results of 2015 indicate a progress in achieving the goals set in Group strategy 2013-2016. The Group has managed to strengthen its position as the leading electricity supplier in the Baltic States after the full market opening in Latvia. Generation source reconstruction program is continued as set by the plan and it is expected that at the end of the strategy period, the objectives for financial indicators will be met. At the end of 2015, work on strategy for the following period (2017-2020) was started. The new strategy will take into account the challenges expected in that particular period. The new strategy of Latvenergo Group is expected to be finalised in 2016.

on the financial performance of the Group. In order to maintain financial stability the Group used various financial risk control and limiting activities, as well the Group uses derivative financial instruments to hedge certain risk exposures (see Note 3).

## Events after the reporting period

Fulfilling the requirements of the “State Administration Structure Law” and the Directive No. 235 of the Cabinet of Ministers of the Republic of Latvia, dated 29th of March 2016 – “On the establishment of the Supervisory Boards for State-Owned Companies”, the Ministry of Economics of the Republic of Latvia as the owner of Latvenergo AS shares must ensure the establishment

of the Supervisory Board of Latvenergo AS until 30<sup>th</sup> of September 2016.

Events that would materially affect the financial position of the Group after the reporting period are disclosed in Note 27 of the Consolidated Financial Statements.

## Statement of management responsibility

Based on the information available to the Management Board of Latvenergo AS, in all material aspects Latvenergo Consolidated Annual Report 2015 has been prepared in accordance with applicable laws and

regulations and gives a true and fair view of assets, liabilities, financial position, profit or loss, equity and cash flows of the Latvenergo Group. All information included in the Management report is true.

## Profit distribution

Fulfilling the requirements of the law “On the State budget 2016” and law “On the Management of State-Owned Capital Shares and Capital Companies”, the Management Board of Latvenergo AS proposes to allocate profit for the year of Latvenergo AS in the amount of EUR 77.4 million to be paid out in

dividends and the rest of the profit to be transferred to Latvenergo AS reserves.

The distribution of profit for 2015 is subject to a resolution of Latvenergo AS Shareholders’ Meeting

The Management Board of Latvenergo AS:



**Āris Žigurs**  
Chairman of the Management Board



**Guntars Baļčūns**  
Member of the Management Board



**Uldis Bariss**  
Member of the Management Board



**Māris Kuņickis**  
Member of the Management Board



**Guntis Stafeckis**  
Member of the Management Board

Riga 19<sup>th</sup> of April 2016

## CONSOLIDATED FINANCIAL STATEMENTS

### Consolidated Statement of Profit or Loss

|  | Notes      | 2015           | 2014          |
|--|------------|----------------|---------------|
|  |            | EUR'000        | EUR'000       |
| Revenue  | 6          | 929,128        | 1,010,757     |
| Other income   | 7          | 4,880          | 5,273         |
| Raw materials and consumables used   | 8          | (470,444)      | (621,285)     |
| Personnel expenses   | 9          | (94,609)       | (97,954)      |
| Depreciation, amortisation and impairment of intangible assets and property, plant and equipment | 13 a, 14 a | (198,827)      | (187,595)     |
| Other operating expenses   | 10         | (61,940)       | (59,953)      |
| <b>Operating profit</b>  |            | <b>108,188</b> | <b>49,243</b> |
| Finance income   | 11 a       | 2,926          | 3,004         |
| Finance costs  | 11 b       | (18,579)       | (20,380)      |
| Share of profit / (loss) of associates   | 15         | –              | (357)         |
| <b>Profit before tax</b>   |            | <b>92,535</b>  | <b>31,510</b> |
| Income tax   | 12         | (7,496)        | (1,720)       |
| <b>Profit for the year</b>   |            | <b>85,039</b>  | <b>29,790</b> |
| <b>Profit attributable to:</b>   |            |                |               |
| – Equity holders of the Parent Company   |            | 83,509         | 28,515        |
| – Non-controlling interests  |            | 1,530          | 1,275         |
| Basic earnings per share (in euros)  | 20 c       | 0.065          | 0.023         |
| Diluted earnings per share (in euros)  | 20 c       | 0.065          | 0.023         |

The notes on pages 112 to 163 are an integral part of these Consolidated Financial Statements.

## Consolidated Statement of Other Comprehensive Income

|   | Notes      | 2015           | 2014           |
|---|------------|----------------|----------------|
|   |            | EUR'000        | EUR'000        |
| <b>Profit for the year</b>  |            | <b>85,039</b>  | <b>29,790</b>  |
| <i>Other comprehensive income / (loss) to be reclassified to profit or loss in subsequent periods (net of tax):</i>     |            |                |                |
| Gains / (losses) from change in hedge reserve   | 20 a, 21 c | 4,077          | (6,495)        |
| Losses on currency translation differences  | 20 a       | –              | (14)           |
| <b>Net other comprehensive income / (loss) to be reclassified to profit or loss in subsequent periods</b>               |            | <b>4,077</b>   | <b>(6,509)</b> |
| <i>Other comprehensive income / (loss) not to be reclassified to profit or loss in subsequent periods (net of tax):</i> |            |                |                |
| Gains on revaluation of property, plant and equipment   | 20 a       | 20,485         | 14             |
| (Losses) / gains as a result of re-measurement on defined post-employment benefit plan                                  | 22 a       | (1,158)        | 159            |
| <b>Net other comprehensive income / (loss) not to be reclassified to profit or loss in subsequent periods</b>           |            | <b>19,327</b>  | <b>173</b>     |
| <b>Other comprehensive income / (loss) for the year, net of tax</b>   |            | <b>23,404</b>  | <b>(6,336)</b> |
| <b>Total other comprehensive income for the year</b>  |            | <b>108,443</b> | <b>23,454</b>  |
| <b>Attributable to:</b>   |            |                |                |
| – Equity holders of the Parent Company  |            | 106,913        | 22,179         |
| – Non-controlling interests   |            | 1,530          | 1,275          |

The notes on pages 112 to 163 are an integral part of these Consolidated Financial Statements.

The Management Board of Latvenergo AS:



**Āris Žigurs**  
Chairman of the Management Board



**Guntars Baļčūns**  
Member of the Management Board



**Uldis Bariss**  
Member of the Management Board



**Māris Kuņickis**  
Member of the Management Board



**Guntis Stafeckis**  
Member of the Management Board

Riga 19<sup>th</sup> of April 2016

## Consolidated Statement of Financial Position

|  | Notes   | 31/12/2015       | 31/12/2014       |
|--|---------|------------------|------------------|
|  |         | EUR'000          | EUR'000          |
| <b>ASSETS</b>  |         |                  |                  |
| <b>Non-current assets</b>  |         |                  |                  |
| Intangible assets  | 13 a    | 14,405           | 13,011           |
| Property, plant and equipment                                      | 14 a    | 3,076,256        | 3,066,316        |
| Investment property  | 14 b    | 696              | 1,343            |
| Non-current financial investments                                  | 15      | 41               | 41               |
| Other non-current receivables                                      |         | 1,712            | 14               |
| Investments in held-to-maturity financial assets                   | 21 a    | 20,609           | 28,528           |
| <b>Total non-current assets</b>                                    |         | <b>3,113,719</b> | <b>3,109,253</b> |
| <b>Current assets</b>  |         |                  |                  |
| Inventories  | 16      | 24,791           | 22,560           |
| Trade receivables and other receivables                            | 17 a, b | 263,452          | 233,045          |
| Deferred expenses  |         | 3,008            | 707              |
| Investments in held-to-maturity financial assets                   | 21 a    | 7,859            | –                |
| Cash and cash equivalents  | 18      | 104,543          | 121,011          |
| <b>Total current assets</b>  |         | <b>403,653</b>   | <b>377,323</b>   |
| <b>TOTAL ASSETS</b>  |         | <b>3,517,372</b> | <b>3,486,576</b> |
| <b>EQUITY</b>  |         |                  |                  |
| Share capital  | 19      | 1,288,531        | 1,288,446        |
| Reserves   | 20 a    | 669,596          | 645,829          |
| Retained earnings  |         | 131,662          | 79,995           |
| <b>Equity attributable to equity holders of the Parent Company</b> |         | <b>2,089,789</b> | <b>2,014,270</b> |
| Non-controlling interests  |         | 6,913            | 6,531            |
| <b>Total equity</b>  |         | <b>2,096,702</b> | <b>2,020,801</b> |
| <b>LIABILITIES</b>   |         |                  |                  |
| <b>Non-current liabilities</b>                                     |         |                  |                  |
| Borrowings   | 21 b    | 714,291          | 688,297          |
| Deferred income tax liabilities                                    | 12      | 273,987          | 268,026          |
| Provisions   | 22      | 15,984           | 15,588           |
| Derivative financial instruments                                   | 21 c    | 8,291            | 11,698           |
| Other liabilities and deferred income                              | 23      | 196,386          | 194,474          |
| <b>Total non-current liabilities</b>                               |         | <b>1,208,939</b> | <b>1,178,083</b> |
| <b>Current liabilities</b>   |         |                  |                  |
| Trade and other payables   | 24      | 117,249          | 139,909          |
| Income tax payable   |         | 4,007            | 3                |
| Borrowings   | 21 b    | 83,192           | 138,925          |
| Derivative financial instruments                                   | 21 c    | 7,283            | 8,855            |
| <b>Total current liabilities</b>                                   |         | <b>211,731</b>   | <b>287,692</b>   |
| <b>TOTAL EQUITY AND LIABILITIES</b>                                |         | <b>3,517,372</b> | <b>3,486,576</b> |

The notes on pages 112 to 163 are an integral part of these Consolidated Financial Statements.

The Management Board of Latvenergo AS:



**Āris Žigurs**  
Chairman of the Management Board



**Guntars Bajčūns**  
Member of the Management Board



**Uldis Bariss**  
Member of the Management Board



**Māris Kuņickis**  
Member of the Management Board



**Guntis Stafeckis**  
Member of the Management Board

Riga 19<sup>th</sup> of April 2016

## Consolidated Statement of Changes in Equity

|   | Notes | Attributable to equity holders of the Parent Company |                |                   |                  | Non-controlling interests | TOTAL            |
|---|-------|--|----------------|-------------------|------------------|---------------------------|------------------|
|   |       | Share capital  | Reserves       | Retained earnings | Total            |                           |                  |
|   |       | EUR'000  | EUR'000        | EUR'000           | EUR'000          | EUR'000                   | EUR'000          |
| <b>As of 31<sup>st</sup> of December 2013</b>                                     |       | <b>1,288,011</b>                                     | <b>652,418</b> | <b>74,832</b>     | <b>2,015,261</b> | <b>6,453</b>              | <b>2,021,714</b> |
| Increase in share capital   | 19    | 435  | –              | –                 | 435              | –                         | 435              |
| Dividends for 2013  | 20 b  | –  | –              | (23,605)          | (23,605)         | (1,197)                   | (24,802)         |
| <b>Total contributions and profit distributions recognised directly in equity</b> |       | <b>435</b>   | <b>–</b>       | <b>(23,605)</b>   | <b>(23,170)</b>  | <b>(1,197)</b>            | <b>(24,367)</b>  |
| Profit for the year   |       | –  | –              | 28,515            | 28,515           | 1,275                     | 29,790           |
| Other comprehensive (loss) / income   | 20 a  | –  | (6,589)        | 253               | (6,336)          | –                         | (6,336)          |
| <b>Total comprehensive (loss) / income</b>  |       | <b>–</b>   | <b>(6,589)</b> | <b>28,768</b>     | <b>22,179</b>    | <b>1,275</b>              | <b>23,454</b>    |
| <b>As of 31<sup>st</sup> of December 2014</b>                                     |       | <b>1,288,446</b>                                     | <b>645,829</b> | <b>79,995</b>     | <b>2,014,270</b> | <b>6,531</b>              | <b>2,020,801</b> |
| Increase in share capital   | 19    | 85   | –              | –                 | 85               | –                         | 85               |
| Dividends for 2014  | 20 b  | –  | –              | (31,479)          | (31,479)         | (1,148)                   | (32,627)         |
| <b>Total contributions and profit distributions recognised directly in equity</b> |       | <b>85</b>  | <b>–</b>       | <b>(31,479)</b>   | <b>(31,394)</b>  | <b>(1,148)</b>            | <b>(32,542)</b>  |
| Profit for the year   |       | –  | –              | 83,509            | 83,509           | 1,530                     | 85,039           |
| Other comprehensive income / (loss)   | 20 a  | –  | 23,767         | (363)             | 23,404           | –                         | 23,404           |
| <b>Total comprehensive income</b>   |       | <b>–</b>   | <b>23,767</b>  | <b>83,146</b>     | <b>106,913</b>   | <b>1,530</b>              | <b>108,443</b>   |
| <b>As of 31<sup>st</sup> of December 2015</b>                                     |       | <b>1,288,531</b>                                     | <b>669,596</b> | <b>131,662</b>    | <b>2,089,789</b> | <b>6,913</b>              | <b>2,096,702</b> |

The notes on pages 112 to 163 are an integral part of these Consolidated Financial Statements.

## Consolidated Statement of Cash Flows

|  | Notes      | 2015             | 2014             |
|--|------------|------------------|------------------|
|  |            | EUR'000          | EUR'000          |
| <b>Cash flows from operating activities</b>  |            |                  |                  |
| Profit before tax  |            | 92,535           | 31,510           |
| <b>Adjustments:</b>  |            |                  |                  |
| – Amortisation, depreciation and impairment of intangible assets and property, plant and equipment | 13 a, 14 a | 198,828          | 187,595          |
| – Loss from disposal of non-current assets   |            | 4,075            | 2,470            |
| – Losses on investments accounting at equity method  | 15         | –                | 357              |
| – Interest costs   | 11 b       | 18,693           | 20,351           |
| – Interest income  | 11 a       | (1,578)          | (2,045)          |
| – Fair value gains on derivative financial instruments   | 8, 11      | (902)            | (8,759)          |
| – (Decrease) / increase in provisions  | 22         | (762)            | 150              |
| – Unrealised losses on currency translation differences  | 11 b       | 27               | 65               |
| <b>Operating profit before working capital adjustments</b>   |            | <b>310,916</b>   | <b>231,694</b>   |
| (Increase) / decrease in inventories   |            | (2,231)          | 2,468            |
| (Increase) in trade and other receivables  |            | (27,626)         | (93,285)         |
| (Decrease) / increase in trade and other payables  |            | (20,825)         | 19,062           |
| <b>Cash generated from operating activities</b>  |            | <b>260,234</b>   | <b>159,939</b>   |
| Interest paid  |            | (19,189)         | (20,915)         |
| Interest received  |            | 1,606            | 2,082            |
| Repaid / (paid) corporate income tax and real estate tax   |            | 3,627            | (5,777)          |
| <b>Net cash flows from operating activities</b>  |            | <b>246,278</b>   | <b>135,329</b>   |
| <b>Cash flows from investing activities</b>  |            |                  |                  |
| Purchase of intangible assets and PPE  |            | (188,915)        | (177,988)        |
| Proceeds from sales of investments   | 15         | –                | 5,779            |
| Proceeds on financing from EU funds and other financing  |            | 17,972           | 2,161            |
| Proceeds from redemption of held-to-maturity assets  |            | 70               | 60               |
| <b>Net cash flows used in investing activities</b>   |            | <b>(170,873)</b> | <b>(169,988)</b> |
| <b>Cash flows from financing activities</b>  |            |                  |                  |
| Proceeds from issued debt securities (bonds)   | 21 b       | 74,893           | –                |
| Proceeds on borrowings from financial institutions   | 21 b       | 30,000           | 22,600           |
| Repayment of borrowings  | 21 b       | (134,875)        | (139,695)        |
| Dividends paid to non-controlling interests  |            | (1,148)          | (1,197)          |
| Dividends received from associates   |            | –                | 1,924            |
| Dividends paid to equity holders of the Parent Company   |            | (31,479)         | (12,649)*        |
| <b>Net cash flows (used in) / generated from financing activities</b>                              |            | <b>(62,609)</b>  | <b>(129,017)</b> |
| <b>Net increase / (decrease) in cash and cash equivalents</b>                                      |            | <b>12,796</b>    | <b>(163,676)</b> |
| Cash and cash equivalents at the beginning of the year   | 18         | 91,747           | 255,423          |
| <b>Cash and cash equivalents at the end of the year</b>  | <b>18</b>  | <b>104,543</b>   | <b>91,747**</b>  |

\* dividends declared for 2013 in the amount of EUR 23,605 thousand are settled partly by corporate income tax overpayment in the amount of EUR 10,956 thousand

\*\* at the end of 2014 received government grant for mandatory procurement public service obligation costs compensation in the amount of EUR 29,264 was not included in cash and cash equivalents because it was defined as restricted cash and cash equivalents (Note 18)

The notes on pages 112 to 163 are an integral part of these Consolidated Financial Statements.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### 1. CORPORATE INFORMATION

All shares of public limited company Latvenergo or Latvenergo AS (hereinafter – the Parent Company) are owned by the Republic of Latvia and are held by the Ministry of Economics of the Republic of Latvia. The registered address of the Company is 12 Pulkveža Brieža Street, Riga, Latvia, LV-1230. According to the Energy Law of the Republic of Latvia, Latvenergo AS is designated as a national economy object of State importance and, therefore, is not subject to privatisation.

Public limited company Latvenergo is power supply utility engaged in electricity and thermal energy generation, as well as supply of electricity. Latvenergo AS is one of the largest corporate entities in the Baltics.

Latvenergo AS heads the Latvenergo Group (hereinafter – the Group) that includes following subsidiaries:

- Sadales tīkls AS (since 18<sup>th</sup> of September 2006) with 100 % interest held;
- Elektrum Eesti OÜ (since 27<sup>th</sup> of June 2007) and its subsidiary Elektrum Latvija SIA (since 18<sup>th</sup> of September 2012) with 100 % interest held;
- Elektrum Lietuva UAB (since 7<sup>th</sup> of January 2008) with 100 % interest held;
- Latvijas elektriskie tīkli AS (since 10<sup>th</sup> of February 2011) with 100 % interest held;
- Liepājas enerģija SIA (since 6<sup>th</sup> of July 2005) with 51 % interest held;
- Enerģijas publiskais tirgotājs AS (since 25<sup>th</sup> of February 2014) with 100 % interest held.

Latvenergo AS and its subsidiaries Sadales tīkls AS, Latvijas elektriskie tīkli AS and Enerģijas publiskais tirgotājs AS are also shareholders with 48.15 % interest held in company Pirmais Slēgtais Pensiju Fonds AS that manages a defined-contribution corporate pension plan in Latvia.

On 12<sup>th</sup> of February 2014 the Cabinet of Ministers of the Republic of Latvia adopted decision No. 67 „On Latvenergo AS termination of partnership in Nordic

Energy Link AS” and on 19<sup>th</sup> of March 2014 at the Nordic Energy Link AS Shareholders’ meeting was approved decision to liquidate Nordic Energy Link AS. In December 2014 Latvenergo AS terminated its shareholding in Nordic Energy Link AS with 25 % interest held.

The Parent Company’s shareholding in subsidiaries, associates and other non-current financial investments is disclosed in Note 15.

Since 15<sup>th</sup> of August 2011 until 19<sup>th</sup> of June 2015 the Management Board of Latvenergo AS includes the following members: Āris Žīgurs (Chairman), Uldis Bariss, Māris Kuņickis, Arnis Kurgs and Zane Kotāne. Reposing on Shareholder’s resolution, Zane Kotāne as of 20<sup>th</sup> of June 2015, and Arnis Kurgs as of 16<sup>th</sup> of November 2015, were excluded from the composition of the Management Board of Latvenergo AS. Since 16<sup>th</sup> of November 2015 Guntars Baļčūns and Guntis Stafekis have been acting as a members of the Management Board of Latvenergo AS and until the date of approving of the 2015 Annual Report, the Management Board of Latvenergo AS includes the following members: Āris Žīgurs (Chairman), Uldis Bariss, Māris Kuņickis, Guntars Baļčūns and Guntis Stafekis.

The Consolidated Financial Statements for year 2015 include the financial information in respect of the Parent Company and its subsidiaries for the year ending 31<sup>st</sup> of December 2015 and comparative information for year 2014. Financial Statements for year 2015 are prepared by comparability of financial results, and where it is necessary, comparatives for year 2014 are reclassified using the same principles applied for preparation of the 2015 Annual Report.

The Management Board of Latvenergo AS has approved the Consolidated Financial Statements for year 2015 on 19<sup>th</sup> of April 2016. The decision on approval of the Consolidated Financial Statements is made by Shareholder’s Meeting.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these Consolidated Financial Statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated. Where it is necessary comparatives are reclassified.

#### 2.1. Basis of Preparation

The Consolidated Financial Statements are prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted for use in the European Union. Due to the European Union’s endorsement procedure, the standards and interpretations not

approved for use in the European Union are presented in this note as they may have impact on the Consolidated Financial Statements in the following periods if endorsed.

The Consolidated Financial Statements are prepared under the historical cost convention, except for some financial assets and liabilities (including derivative financial instruments) measured at fair value through profit or loss and for the revaluation of property, plant and equipment carried at revalued amounts to other comprehensive income as disclosed in accounting policies presented below.



All amounts shown in these Consolidated Financial Statements are presented in thousands of euros (EUR).

The preparation of the Consolidated Financial Statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on the Parent Company Management's best knowledge of current events and actions, actual results ultimately may differ from those. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the Consolidated Financial Statements are disclosed in Note 4.

#### **Adoption of new and/or changed IFRS and International Financial Reporting Interpretations Committee (IFRIC) interpretations**

The following new and/or amended International Financial Reporting Standards or interpretations published or revised during the reporting year, which became effective for the reporting period started from 1<sup>st</sup> of January 2015, have been adopted by the Group:

*Annual Improvements to IFRSs 2011 – 2013 Cycle is a collection of amendments to the following IFRSs*

- *IFRS 3 Business Combinations:* This improvement clarifies that IFRS 3 excludes from its scope the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself.
- *IFRS 13 Fair value Measurement:* This improvement clarifies that the scope of the portfolio exception defined in paragraph 52 of *IFRS 13* includes all contracts accounted for within the scope of *IAS 39 Financial Instruments: Recognition and Measurement* or *IFRS 9 Financial Instruments*, regardless of whether they meet the definition of financial assets or financial liabilities as defined in *IAS 32 Financial Instruments: Presentation*.
- *IAS 40 Investment property:* This improvement clarifies that determining whether a specific transaction meets the definition of both a business combination as defined in *IFRS 3 Business Combinations* and investment property as defined in *IAS 40 Investment Property* requires the separate application of both standards independently of each other.

The implementation of these annual improvements had no effect on the financial statements of the Group.

#### *IFRIC Interpretation 21 Levies*

This interpretation addresses the accounting for levies imposed by governments. Liability to pay a levy is recognized in the financial statements when the activity that triggers the payment of the levy occurs. The

implementation of this interpretation had no effect on the financial statements of the Group.

#### **Standards issued but not yet effective**

The Group has not applied the following amendments to *IAS, IFRS* and its amendments that have been issued as of the date of authorisation of these financial statements for issue, but which will become effective for the reporting periods started from 1<sup>st</sup> of January 2016 or later. At present the Management of the Group evaluates the impact or expected effect from adoption of these standards, but does not consider that these amendments will have significant effect to the Consolidated Financial Statements, except IFRS 9 "Financial Instruments", IFRS 15 "Revenue from Contracts with Customers" and IFRS 16 "Leases".

- *Amendments to IAS 1 Presentation of financial statements: Disclosure Initiative* (effective for financial years beginning on or after 1<sup>st</sup> of January 2016). The amendments to *IAS 1* further encourage companies to apply professional judgment in determining what information to disclose and how to structure it in their financial statements. The Group has not yet evaluated the impact of the implementation of these amendments, but considers that these amendments will have an effect to the Consolidated Financial Statements.
- *Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative* (effective for financial years beginning on or after 1<sup>st</sup> of January 2017, once endorsed by the EU). The amendments improve information provided to users of financial statements about an entity's financing activities. Entities are required to disclose changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes, for example, by providing reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities. The implementation of these amendments will not have any impact on the financial position or performance of the Group but may result in changes in disclosures.
- *Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealized Losses* (effective for financial years beginning on or after 1<sup>st</sup> of January 2017, once endorsed by the EU). The amendments clarify how to account for deferred tax assets for unrealized losses on debt instruments measured at fair value. The Group has not yet evaluated the impact of the implementation of these amendments, but considers that they will not have an effect to the Consolidated Financial Statements.
- *Amendments to IAS 16 Property, Plant & Equipment and IAS 38 Intangible assets: Clarification of Acceptable Methods of Depreciation and Amortization* (effective for financial years

beginning on or after 1<sup>st</sup> of January 2016). The amendment provides additional guidance on how the depreciation or amortisation of property, plant and equipment and intangible assets should be calculated. It is clarified that a revenue-based method is not considered to be an appropriate manifestation of consumption. The implementation of these amendments will not have an effect to the Consolidated Financial Statements as the Group does not use revenue based depreciation and amortisation methods.

- *IFRS 9 “Financial Instruments”* (effective for financial years beginning on or after 1<sup>st</sup> of January 2018, once endorsed by the EU). *IFRS 9* replaces *IAS 39* and introduces new requirements for classification and measurement, impairment and hedge accounting. The Group has not yet evaluated the impact of the implementation of this standard, but considers that this standard will have an effect to the Consolidated Financial Statements.
- *Amendments to IFRS 10 and IAS 28 – “Sale or Contribution of Assets between an Investor and its Associate or Joint Venture”* (endorsement deferred indefinitely). The amendments address an acknowledged inconsistency between the requirements in *IFRS 10* and those in *IAS 28*, in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognised when a transaction involves a business and partial gain or loss is recognised when a transaction involves assets that do not constitute a business. The Group has not yet evaluated the impact of the implementation of these amendments, but does not consider that any of them will have significant effect to the Consolidated Financial Statements.
- *IFRS 15 “Revenue from Contracts with Customers”* (effective for financial years beginning on or after 1<sup>st</sup> of January 2018, once endorsed by the EU). *IFRS 15* establishes a five-step model that will apply to revenue earned from a contract with a customer, regardless of the type of revenue transaction or the industry. Extensive disclosures will be required, including disaggregation of total revenue; information about performance obligations; changes in contract asset and liability account balances between periods and key judgments and estimates. The management of the Group has assessed that adoption of this *IFRS* will have an impact on the presentation of revenue disclosures in the Consolidated Financial Statements and financial position or performance of the Group.
- *IFRS 16 “Leases”* (effective for financial years beginning on or after 1<sup>st</sup> of January 2019, once endorsed by the EU). *IFRS 16* replaces *IAS 17* and specifies how to recognise, measure, present

and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessor accounting is substantially unchanged. The management of the Group has assessed that adoption of this *IFRS* will have an impact on the recognition, measurement and disclosures of the Group’s leases.

The Management of the Group plans to adopt the above mentioned standards and amendments that were applicable for the Group on their effectiveness date.

#### **Standards issued but not yet effective and not applicable for the Group**

- *Amendments to IAS 19 “Employee Benefits”* (effective for financial years beginning on or after 1<sup>st</sup> of February 2015). The amendments address accounting for the employee contributions to a defined benefit plan. Since the Group’s employees do not make such contributions, the implementation of these amendments will not have any impact on the financial statements of the Group.
- *Amendments to IAS 27 “Equity method in separate financial statements”* (effective for financial years beginning on or after 1<sup>st</sup> of January 2016). The amendments reinstate the equity method as an accounting option for investments in subsidiaries, joint ventures and associates in an entity’s separate financial statements. The implementation of these amendments will have no impact on the financial statements of the Group since these are only applicable for the separate financial statements of the Parent Company.
- *Amendments to IFRS 10, IFRS 12 and IAS 28 – “Investment Entities: Applying the consolidation exception”* (effective for financial years beginning on or after 1<sup>st</sup> of January 2016, once endorsed by the EU). The amendments address issues that have arisen in the context of applying the consolidation exception for investment entities. The implementation of these amendments will have no impact on the financial statements of the Group, as the parent of the Group is not an investment entity.
- *Amendment to IFRS 11 “Joint arrangements: Accounting for Acquisitions of Interests in Joint Operations”* (effective for financial years beginning on or after 1<sup>st</sup> of January 2016). *IFRS 11* addresses the accounting for interests in joint ventures and joint operations. The amendment adds new guidance on how to account for the acquisition of an interest in a joint operation that constitutes a business in accordance with *IFRS* and specifies the appropriate accounting

treatment for such acquisitions. Management has assessed that this amendment will have no impact on the financial statements of the Group, as the Group has not any interests in joint ventures and joint operations.

- *IFRS 14 “Regulatory Deferral Accounts”* (effective for financial years beginning on or after 1<sup>st</sup> of January 2016, once endorsed by the EU). *IFRS 14* provides first-time adopters of *IFRS* with relief from derecognising rate-regulated assets and liabilities. However, to enhance comparability with entities that already apply *IFRS* and do not recognise such amounts, the standard requires that the effect of rate regulation must be presented separately from other items. An entity that already presents *IFRS* financial statements is not eligible to apply the standard. The implementation of this standard will not have any impact on the Group since the Group is not first-time adopter of *IFRS*.

The Management of the Group will not adopt these amendments because they will not be applicable for the Group.

#### **Improvements to IFRSs**

- In December 2013 IASB (International Accounting Standards Board) issued the *Annual Improvements to IFRSs 2010 – 2012 Cycle* (effective for financial years beginning on or after 1<sup>st</sup> of February 2015): *IFRS 2 Share-based Payment; IFRS 3 Business Combinations; IFRS 8 Operating Segments; IFRS 13 Fair value Measurement; IAS 16 Property, Plant and Equipment; IAS 24 Related Party Disclosures; IAS 38 Intangible Assets*.
- In September 2014 IASB issued the *Annual Improvements to IFRSs 2012 – 2014 Cycle* (effective for financial years beginning on or after 1<sup>st</sup> of January 2016): *IFRS 5 Non-current Assets Held for Sale and Discontinued Operation, IFRS 7 Financial Instruments: Disclosures, IAS 19 Employee Benefits and IAS 34 Interim Financial Reporting*.

The adoption of these amendments may result in changes to accounting policies or disclosures but will not have any impact on the financial position or performance of the Group.

## **2.2. Consolidation**

### **a) Subsidiaries**

Subsidiaries, which are those entities where the Group has control over the financial and operating policies of the entity, financial reports are consolidated. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee).

Subsidiaries' financial reports are consolidated from the date on which control is transferred to the Parent Company and are no longer consolidated from the date when control ceases. General information about entities included in consolidation and its primary business activities are disclosed in Note 15.

The acquisition method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured, as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Costs directly attributable to the acquisition are expensed to the Consolidated Statement of Profit or Loss as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in business combination are measured initially at their fair values at the acquisition date. Goodwill is initially measured as the excess of the aggregate of the consideration transferred and the value of non-controlling interest over the net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognised in the Consolidated Statement of Profit or Loss.

Intercompany transactions, balances and unrealised gains on transactions between the Group's entities are eliminated. Unrealised losses are also eliminated but considered an impairment indicator of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

### **b) Transactions with non-controlling interests**

The Group treats transactions with non-controlling interests as transactions with equity owners of the Group's Parent Company. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in the Group's equity.

### **c) Associates**

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20 % and 50 % of the voting rights. Investments in associates are accounted for using the equity method of accounting in the consolidated financial statements and are initially recognised at cost. Under this method the Group's share of its associate's post-acquisition profits and losses is recognised in the Consolidated Statement of Profit or Loss, and its share of post-acquisition movements in other comprehensive income is recognised in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in associate equals or exceeds its interest in associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

### 2.3. Disclosures of reportable segments

For segment reporting purposes the Group allocates division into reportable segments based on the Group's internal management structure, which is the basis for the reporting system, performance assessment and the allocation of resources by the chief operating decision maker.

The Group allocates its operations into three main reportable segments – generation and supply, distribution and lease of transmission system assets. In addition Corporate Functions, that covers administration and other support services, are presented separately.

### 2.4. Foreign currency translation

#### a) Functional and presentation currency

Items included in the Consolidated Financial Statements are measured using the currency of the primary economic environment in which the Group's entity operates ("the functional currency"). The Consolidated Financial Statements have been prepared in euros (EUR), which is the Parent Company's functional currency.

#### b) Transactions and balances

All transactions denominated in foreign currencies are translated into functional currency at the exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into functional currency using the exchange rate at the last day of the reporting year. The resulting gain or loss is charged to the Consolidated Statement of Profit or Loss.

#### c) Consolidation of the Group's foreign companies

The results and financial position of all the Group's entities (none of which has the currency of a hyper-inflationary economy) that have functional currency different from the presentation currency are translated into the presentation currency as follows:

- 1) Assets and liabilities for each financial position presented are translated at the closing rate at the date of that financial position;
- 2) Income and expenses for each statement of profit or loss are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of transactions).

### 2.5. Intangible assets

#### a) Licenses and software

Licenses and software are shown at historical cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of licenses and software over their estimated useful lives (5 years). Computer software development costs recognised as assets are amortised over their estimated useful lives, not exceeding a period of five years.

#### b) Greenhouse gas emission allowances

Emission rights for greenhouse gases (or allowances) are recognised at purchase cost. Allowances received from the Government free of charge are recognised at zero cost as off-balance sheet assets. Emission rights are recognised at cost when the Group is able to exercise the control. In those cases when the quantity of emitted greenhouse gases exceeds the quantity of allowances allocated by the state free of charge, the Group purchases additional allowances and carrying value of those allowances is determined on the basis of the market price of greenhouse gas emission allowances at the reporting period. Allowances are accounted for within 'Intangible assets' (see Note 13 b).

### 2.6. Property, plant and equipment

Property, plant and equipment (PPE) are stated at historical cost or revalued amount (see point 2.8) less accumulated depreciation and accumulated impairment loss.

The cost comprises the purchase price, transportation costs, installation, and other direct expenses related to the acquisition or implementation. The cost of the self-constructed item of PPE includes the cost of materials, services and workforce. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of an item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repair and maintenance expenses are charged directly to the Consolidated Statement of Profit or Loss when the expenditure is incurred. Borrowing costs are capitalised proportionally to the part of the cost of fixed assets under construction over the period of construction. Effective part of the changes in the fair value of forward foreign currencies exchange contracts, the purpose of which is to hedge currency exchange risk on PPE items, are also capitalised and included in the Consolidated Statement of Profit or Loss along with the expenses of depreciation over the useful life of the asset or at the disposal of the asset.

If an item of PPE consists of components with different useful lives, these components are depreciated as separate items. Homogenous items with similar useful lives are accounted for in groups.

Land is not depreciated. Depreciation on the other assets is calculated using the straight-line method to allocate their cost over their estimated useful lives, as follows:

| Type of property, plant and equipment (PPE)                | Estimated useful life, years |
|--|------------------------------|
| <b>Buildings and facilities, including</b>                 |                              |
| Hydropower plants, combined heat and power plants          | 15 – 100                     |
| Electricity transmission lines                             | 30 – 50                      |
| Electricity distribution lines                             | 30 – 40                      |
| <b>Technology equipment and machinery, including (TEM)</b> |                              |
| Hydropower plants  | 10 – 40                      |
| Combined heat and power plants                             | 3 – 25                       |
| Transmission and distribution machinery and equipment      | 10 – 40                      |
| <b>Other property, plant and equipment</b>                 | 2 – 25                       |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (see point 2.9).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. Those are included in the Consolidated Statement of Profit or Loss. If revalued property, plant and equipment have been sold, appropriate amounts are reclassified from revaluation reserve to retained earnings.

All fixed assets under construction are stated at historical cost and comprised costs of construction of assets. The initial cost includes construction and installation costs and other direct costs related to construction of fixed assets. Assets under construction are not depreciated as long as the relevant assets are completed and ready for intended use.

### 2.7. Investment property

Investment properties are land or a building or part of a building held by the Group as the owner to earn rentals or for capital appreciation, rather than for use in the production of goods or supply of services or for administrative purposes, or sale in the ordinary course of business. The investment properties are initially recognised at cost and subsequently measured at acquisition cost net of accumulated depreciation and impairment losses. The applied depreciation rates are based on estimated useful life set for respective fixed asset categories – from 15 to 80 years.

### 2.8. Revaluation of property, plant and equipment

Revaluations have been made with sufficient regularity to ensure that the carrying amount of property, plant and equipment items subject to valuation does not differ materially from that which would be determined using fair value at the end of reporting period.

The following property, plant and equipment groups are revalued regularly but not less frequently than every five years:

- a) Buildings and facilities, including
  - Daugava hydropower plants' buildings and facilities,
  - Buildings and facilities of transmission system,
  - Buildings and facilities of distribution system;
- b) Technology equipment and machinery, including
  - Daugava hydropower plants' technology equipment and machinery,
  - Technology equipment and machinery of transmission system,
  - Technology equipment and machinery of distribution system;
- c) Other property, plant and equipment, including
  - Other PPE of Daugava hydropower plants',
  - Other PPE of transmission system,
  - Other PPE of distribution system.

Increase in the carrying amount arising on revaluation net of deferred tax is credited to the 'Other comprehensive income' as "Property, plant and equipment revaluation reserve" in shareholders' equity. Decreases that offset previous increases of the same asset are charged in 'Other comprehensive income' and debited against the revaluation reserve directly in equity; all other decreases are charged to the current year's Consolidated Statement of Profit or Loss.

Any gross carrying amounts and accumulated depreciation at the date of revaluation is restated proportionately with the change in the gross carrying amount of the asset so that the carrying amount of the asset after the revaluation equals its revalued amount.

Property, plant and equipment revaluation reserve is decreased at the moment, when revalued asset has been eliminated or disposed.

Revaluation reserve cannot be distributed in dividends, used for indemnity, reinvested in other reserves, or used for other purposes.

### 2.9. Impairment of assets

Assets that are subject to depreciation or amortisation and land are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. In assessing the value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market expectations regarding the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognised in the Other Comprehensive Income within PPE revaluation reserve for the assets accounted at revalued amount and in the Consolidated Statement of Profit or Loss within amortisation, depreciation and impairment charge

expenses for the assets that are accounted at amortised historical cost and for the assets accounted at revalued amount in case if impairment charge exceeds revaluation surplus previously recognised on individual asset.

The key assumptions used in determining recoverable amount of the asset are based on the Group entities' or the Parent Company's management best estimation of the range of economic conditions that will exist over the remaining useful life of the asset, on the basis of the most recent financial budgets and forecasts approved by the management for a maximum period of 10 years. Assets are reviewed for possible reversal of the impairment whenever events or changes in circumstances indicate that impairment must be reviewed. The reversal of impairment for the assets that are accounted at amortised historical cost is recognised in the Consolidated Statement of Profit or Loss. Reversal of impairment loss for revalued assets is recognised in the Consolidated Statement of Profit or Loss to the extent that an impairment loss on the same revalued asset was previously recognised in the Consolidated Statement of Profit or Loss; the remaining reversals of impairment losses of revalued assets are recognised in Other Comprehensive Income.

## 2.10. Leases

### a) The Group is the lessee

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the Consolidated Statement of Profit or Loss on a straight-line basis over the period of the lease (Note 14 e).

### b) The Group is the lessor

Assets leased out under operating leases are recorded within property, plant and equipment at historic cost less depreciation and accumulated impairment loss. Depreciation is calculated on a straight-line basis to write down each asset to its estimated residual value over estimated useful life. Rental income from operating lease and advance payments received from clients (less any incentives given to lessee) are recognised in the Consolidated Statement of Profit or Loss on a straight-line basis over the period of the lease (Note 14e).

## 2.11. Inventories

Inventories are stated at the lower of cost or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses. Cost is determined using the weighted average method.

Purchase cost of inventories consists of the purchase price, import charges and other fees and charges, freight-in and related costs as well as other costs directly incurred in bringing the materials and goods to their present location and condition. The value of inventories is assigned by charging trade discounts, reductions and similar allowances.

Amount of inventories as of the end of reporting period is verified during stock-taking.

At the end of each reporting year the inventories are reviewed for any indications of obsolescence. In cases when obsolete or damaged inventories are identified allowances are recognised. During the reporting year at least each month revaluation of the inventories is performed with the purpose to identify obsolete and damaged inventories. Allowances for an impairment loss are recognised for those inventories.

The following basic principles are used in determining impairment losses for idle and obsolete inventories:

- a) Inventories (smaller spare parts or stocks) for machinery and equipment of hydropower plants and thermal power plants that haven't turned over during last 12 months are impaired in amount of 90 %,
- b) Other inventories that haven't turned over during last 12 months are fully impaired,
- c) Inventories (smaller spare parts or stocks) for machinery and equipment of hydropower plants and thermal power plants that haven't turned over during last 6 months are impaired in amount of 45 %,
- d) Other inventories that haven't turned over during last 6 months are impaired in amount of 50 %,
- e) Allowances are not calculated for the inventory of heating materials necessary to ensure uninterrupted operations of heat power plants.

## 2.12. Trade and other receivables

Trade receivables are recognised initially at fair value and subsequently carried at amortised cost or cost less impairment. An allowance for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of repayment. Significant financial difficulties of the debtor, probabilities that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 30 days overdue) are considered as indicators that the trade receivable is impaired.

Trade receivables are classified in groups:

- a) Electricity supply and electricity services receivables,
- b) Heating receivables,
- c) Other services trade receivables (IT & telecommunication services, connection service fees, distribution system services and services of transmission system assets construction, management and lease).

An allowance for impairment of doubtful debts is calculated on the basis of trade receivables aging analysis according to estimates defined by the Group entities management and the Parent Company's management, which are revised at least once a year. Allowances for electricity supply and electricity services receivables are calculated for debts overdue 45 days, and, if the debt is overdue for more than 181 day, allowances

are established at 100 %. For other trade receivables allowances are calculated for debts overdue 31 day, and, if the date of payment is overdue for more than 91 day, allowances are established at 100 % (see Note 17 a).

Individual impairment assessments are performed for the debtors:

- a) In Latvia – if their debt balance exceeds EUR 700 thousand and debt repayment schedule has been individually agreed,
- b) In Lithuania and Estonia – if their debt balance exceeds EUR 200 thousand and debt repayment schedule has been individually agreed,
- c) If debtor has been announced as insolvent, allowances are established at 100 %.

The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the Consolidated Statement of Profit or Loss within 'Other operating expenses' as selling expenses and customer service costs. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against selling and customer services costs in the Consolidated Statement of Profit or Loss.

### 2.13. Cash and cash equivalents

Cash and cash equivalents include cash balances on bank accounts, demand deposits at bank and other short-term deposits with original maturities of three months or less. Cash and cash equivalents also are consisting of restricted cash, that are excluded from cash and cash equivalents in the Consolidated Statement of Cash Flows (see Note 18).

### 2.14. Dividend distribution

Dividend distribution to the Parent Company's shareholders is recognised as a liability in the Consolidated Financial Statements in the period in which the dividends are approved by the Parent Company's shareholders.

### 2.15. Pensions and employment benefits

#### a) Pension obligations

The Group makes monthly contributions to a closed defined contribution pension plan on behalf of its employees. The plan is managed by the non-profit public limited company *Pirmais Slēgtais Pensiju Fonds*, with the participation of the Group companies amounting for 48.15 % of its share capital. A defined contribution plan is a pension plan under which the Group pays contributions into the plan. The Group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees benefits relating to employee service in the current and prior periods. The contributions amount to 5 % of each pension plan member's salary. The Group recognizes the contributions to the defined contribution plan as an expense when an employee has rendered services in exchange for those contributions.

#### b) Provisions for post-employment obligations arising from collective agreement

In addition to the aforementioned plan, the Group provides certain post-employment benefits to employees whose employment meets certain criteria. Obligations for benefits are calculated taking into account the current level of salary and number of employees eligible to receive the payment, historical termination rates as well as number of actuarial assumptions.

The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method.

The liability recognised in the Consolidated Statement of Financial Position in respect of post-employment benefit plan is the present value of the defined benefit obligation at the end of the reporting period. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of government bonds. The Group uses projected unit credit method to establish its present value of fixed benefit obligation and related present and previous employment expenses. According to this method it has been stated that each period of work makes benefit obligation extra unit and the sum of those units comprises total Group's obligations of post-employment benefits. The Group uses objective and mutually compatible actuarial assumptions on variable demographic factors and financial factors (including expected remuneration increase and determined changes in benefit amounts).

Actuarial gains or losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to the Consolidated Statement of Other Comprehensive Income in the period in which they arise. Past service costs are recognised immediately in the Consolidated Statement of Profit or Loss.

### 2.16. Income tax

#### a) Corporate income tax

##### *Latvia and Lithuania*

Income tax expense for the period comprises current income tax and deferred income tax. Current income tax charges are calculated on current profit before tax using the tax rate 15 % in accordance with applicable tax regulations as adjusted for certain non-deductible expenses/non-taxable income and are based on the taxable income reported for the taxation period.

##### *Estonia*

Under the Income Tax Act, the annual profit earned by entities is not taxed in Estonia. Corporate income tax is paid on dividends, fringe benefits, gifts, donations, costs of entertaining guests, non-business related disbursements and adjustments of the transfer price. The tax rate on the net dividends paid out of retained earnings is 20/80 (21/79 until 1<sup>st</sup> of January 2015). In certain circumstances, it is possible to distribute dividends without any additional income tax expense. The corporate income tax arising from the payment of dividends is accounted for as a

liability and expense in the period in which dividends are declared, regardless of the actual payment date or the period for which the dividends are paid.

#### **b) Deferred income tax**

##### *Latvia and Lithuania*

Deferred income tax is provided in full, using the liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax relating to items recognised outside profit or loss is recognised outside profit or loss. Deferred tax items are recognised in correlation to the underlying transaction either in other comprehensive income or directly in equity. However, the deferred income tax is not accounted if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss. Deferred income tax is determined using tax rates (and laws) that have been enacted by the end of reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit of the respective Group entity will be available against which the temporary differences can be utilised.

Tax incentives for new technological equipment are not considered when calculating deferred income tax.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the Group controls the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

##### *Estonia*

Due to the nature of the taxation system, the entities registered in Estonia do not have any differences between the tax bases of assets and their carrying amounts and hence, no deferred income tax assets and liabilities arise.

#### **2.17. Subsidised Energy Tax**

In order to limit the increase of the mandatory procurement PSO fee for electricity consumers in Latvia, a Subsidised Energy Tax (SET) has been introduced for a four-year period as of 1st of January 2014, which applies to state support for generators of subsidised electricity. The SET applies both to income from electricity supplied under the mandatory procurement process as well as to mandatory procurement capacity payments for installed capacity at cogeneration plants. The tax is differentiated according to the type of energy sources used. For cogeneration plants that use fossil energy sources a 15 % tax rate applies to the received support (taxable income) amount, 10 % tax rate – plants that use renewable energy sources, 5 % – cogeneration plants that use gas, biogas and biomass energy sources and installed electrical capacity in

cogeneration plants is below 4 MW. Payers of SET are all producers of subsidised electricity. Revenues from SET are used as a funding for the grant included in the State Budget programme “Electricity user support” to limit the increase of mandatory procurement PSO fee. SET applied for the subsidised electricity produced by the Group are recognised in the Consolidated Statement of Profit or Loss as ‘Other operating expenses’ (Note 10) at gross amount, but SET for subsidised electricity produced by other producers – as ‘Other financial current payables’ in the Consolidated Statement of Financial Position (Note 24).

#### **2.18. Borrowing costs**

General and specific borrowing costs directly attributable to the acquisition or construction of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use. All other borrowing costs are expensed in the period in which they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

#### **2.19. Provisions**

Provisions are recognised when the Group has a present obligation as a result of past event; it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and when a reliable estimate can be made of the amount of the obligation. Provisions are not recognised for future operating losses.

Provisions are presented in the Consolidated Statement of Financial Position at the best estimate of the expenditure required to settle the present obligation at the end of reporting period. Provisions are used only for expenditures for which the provisions were originally recognised and are reversed if an outflow of resources is no longer probable.

Provisions are measured at the present value of the expenditures expected to be required for settling the obligation by using pre-tax rate that reflects current market assessments of the time value of the money and the risks specific to the obligation as a discount rate. The increase in provisions due to passage of time is recognised as interest expense.

Environmental protection provisions are recognised to cover environmental damages that have occurred before the end of the reporting period when this is required by law or when the Group’s past environmental policies have demonstrated that the Group has a constructive present obligation to liquidate this environmental damage. Experts’ opinions and prior experience in performing environmental work are used to set up the provisions (see Note 22 b).

#### **2.20. Grants**

Government grants are recognised as income over the period necessary to match them with the related costs, for



which they are intended to compensate, on a systematic basis. A government grant is not recognised until there is reasonable assurance that the entity will comply with the conditions attaching to it, and that the grant will be received. Receipt of a grant does not of itself provide conclusive evidence that the conditions attaching to the grant have been or will be fulfilled. Government grants are received with the purpose to reduce the increase of mandatory procurement public service obligation fee partly compensating the increase of mandatory procurement costs. Acceptance from European Union is a prerequisite for use of the government grant received in 2014.

Property, plant and equipment received at nil consideration are accounted for as grants. Those grants are recognised at fair value as deferred income and are credited to the Consolidated Statement of Profit or Loss on a straight-line basis over the expected lives of the related assets.

#### **Financing provided by European Union funds**

The Group ensures the management, application of internal controls and accounting for the Group's projects financed by the European Union funds, according to the guidelines of the European Union and legislation of the Republic of Latvia.

Accounting of the transactions related to the projects financed by the European Union is ensured using separately identifiable accounts. The Group ensures separate accounting of financed projects with detailed income and expense, non-current investments and value added tax in the relevant positions of the Group's Consolidated Statement of Profit or Loss and Consolidated Statement of Financial Position.

### **2.21. Financial instruments – initial recognition, subsequent measurement and de-recognition**

#### **a) Financial assets**

##### *I) Initial recognition and measurement*

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial assets at initial recognition.

All financial assets are recognised initially at fair value plus transaction costs, except in the case of financial assets recorded at fair value through profit or loss.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognised on the trade date, i.e., the date that the Group commits to purchase or sell the asset.

##### *II) Subsequent measurement*

###### *Financial assets at fair value through profit or loss*

Financial assets at fair value through profit or loss include financial assets held for trading and financial

assets designated upon initial recognition at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are classified as current assets if expected to be settled within 12 months; otherwise, they are classified as non-current. Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value presented as finance costs (negative net changes in fair value) or finance income (positive net changes in fair value) in the Consolidated Statement of Profit or Loss. Financial assets designated upon initial recognition at fair value through profit or loss are designated at their initial recognition date and only if the criteria under IAS 39 are satisfied. The Group has not designated any financial assets at fair value through profit or loss.

Derivatives embedded in host contracts are accounted for as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contracts and the host contracts are not held for trading or designated at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in profit or loss.

##### *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such financial assets are subsequently measured at amortised cost using the EIR method, less impairment. The losses arising from impairment are recognised in the Consolidated Statement of Profit or Loss in finance costs for loans and in other operating expenses for receivables.

##### *Held-to-maturity investments*

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held to maturity when the Group has the positive intention and ability to hold them to maturity. After initial measurement, held to maturity investments are measured at amortised cost using the EIR, less impairment. If the Group were to sell other than an insignificant amount of held-to-maturity financial assets, the whole category would be tainted and reclassified as available for sale. Held-to-maturity financial assets with maturities more than 12 months from the end of the reporting period are included in non-current assets; however those with maturities less than 12 months from the end of the reporting period are classified as current assets.

The Group follows the IAS 39 guidance on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgement. In making this judgement, the Group evaluates its intention and ability to hold such investments to maturity (see Note 4 g).

If the Group fails to keep these investments to maturity other than for specific circumstances explained in IAS 39, it will be required to reclassify the whole class as available-for-sale. Therefore the investments would be measured at fair value not at amortised cost.

Purchases and sales of financial assets held-to-maturity are recognised on trade date – the date on which the Group commits purchase of the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired. Held-to-maturity financial assets are carried at amortised cost using the effective interest rate method, net of accumulated impairment losses. Gains and losses arising from changes in the amortised value of the financial instruments are included in the Consolidated Statement of Profit or Loss in the period in which they arise.

#### *Available-for-sale financial assets*

Available-for-sale financial assets include equity instruments and debt securities. After initial measurement available-for-sale financial assets are subsequently measured at fair value with unrealised gains or losses recognised in other comprehensive income and credited in the available-for-sale financial assets reserve until the investment is derecognised.

#### *III) De-recognition*

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- 1) the rights to receive cash flows from the asset have expired,
- 2) the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

### **b) Financial liabilities**

#### *I) Initial recognition and measurement*

Financial liabilities within the scope of IAS 39 are classified as financial liabilities at fair value through profit or loss, loans and borrowings, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial liabilities at initial recognition.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs.

The Group's financial liabilities include trade and other payables, bank overdrafts, loans and borrowings, financial guarantee contracts, and derivative financial instruments.

#### *II) Subsequent measurement*

*Financial liabilities at fair value through profit or loss*  
Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss. This category includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IAS 39. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on liabilities held for trading are recognised in the Consolidated Statement of Profit or Loss.

#### *Loans and borrowings*

Loans and borrowings are recognised initially at fair value. After initial recognition, interest bearing loans and borrowings are subsequently measured at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in the statement of profit or loss, except for the capitalised part. Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability at least for 12 months after the end of reporting period.

#### *Trade and other payables*

The Group's trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

#### *III) De-recognition*

A financial liability is derecognised when the obligation under the liability is discharged or cancelled, or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the de-recognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the statement of profit or loss.

### **2.22. Derivative financial instruments and hedging activities**

The Group uses derivatives such as interest rate swaps and electricity forward and future contracts to hedge risks associated with the interest rate and purchase price fluctuations.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. Fair values are obtained from quoted market prices and discounted cash flow models as appropriate (see point 2.23.).

The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, on the nature / content of the relevant asset or liability being hedged.

The Group designates certain derivatives as hedges of a particular risk associated with specific variable rate borrowings (cash flow hedge). Other derivatives are accounted for at fair value through profit or loss.

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Group also documents its assessment, both at hedge inception and on an on-going basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

The fair value of the derivative instruments is presented as current or non-current based on settlement date. Derivative instruments that have maturity of more than twelve months and have been expected to be held for more than twelve months after the end of the reporting year are classified as non-current assets or liabilities. Derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

#### **a) Cash flow hedge**

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and accumulated in equity within 'Hedging reserve'. The gain or loss relating to the ineffective portion, if such arise, would be recognised immediately in the Consolidated Statement of Profit or Loss.

Amounts accumulated in equity are recycled in the Consolidated Statement of Profit or Loss in the periods when the hedged item affects profit or loss.

The gain or loss relating to the ineffective portion of interest rate swaps hedging variable rate borrowings is recognised in the Consolidated Statement of Profit or Loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the Consolidated Statement of Profit or Loss.

#### **b) Fair value changes of derivatives through profit and loss**

Changes in the fair value of derivatives at fair value through profit or loss, ineffective part of changes in the fair value of hedging derivatives and amounts accumulated in equity that are recycled to the Consolidated Statement of Profit or Loss, are classified

according to the purpose of the derivatives – gains/ losses from electricity forward and future contracts are recognised within 'Raw materials and consumables used', while gains / losses from interest rate swap agreements and forward foreign currencies exchange contracts are recognised within 'Finance costs' or 'Finance income'.

#### **2.23. Fair value measurement**

The Group measures financial instruments, such as, derivatives, at fair value at each balance sheet date. Such non-financial assets as investment properties are measured at amortised cost, but some items of property, plant and equipment at revalued amounts. Also fair values of financial instruments measured at amortised cost are disclosed in Note 21 d.

The fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair values are estimated based on market prices and discounted cash flow models as appropriate (see Note 4 c).

The fair value of financial instruments traded in active markets is based on quoted market prices at the end of reporting period. The quoted market prices used for financial assets held by the Group is the current bid prices.

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Group use a variety of methods and make assumptions that are based on market conditions existing at each end of reporting period. Estimated discounted cash flows are used to determine fair value for the remaining financial instruments.

The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows, by discounting their future contractual cash flows at current market interest rates for similar financial instruments.

The fair value of electricity forward and future contracts is calculated as discounted difference between actual market and settlement prices multiplied by the volume of the agreement.

If counterparty is a bank, then fair values of financial instruments are obtained from corresponding bank's revaluation reports and in financial statements fair values of financial instruments as specified by banks are disclosed. In case of electricity forward and future contracts concluded with counterparties others than a bank; fair values as calculated by the Group are disclosed in Consolidated Financial Statements.

#### **2.24. Revenue recognition**

Revenue comprises the value of goods sold and services rendered in the ordinary course of the Group's activities. The Latvian regulatory authority (Public

Utilities Commission) determines tariffs for electricity and heat. Revenue is measured at the fair value of the consideration received or receivable, net of value-added tax, estimated returns, rebates and discounts. Revenue is recognised as follows:

**a) Electricity sales**

The Group records electricity sales to residential customers on the basis of reported meter readings. Where relevant, this includes an estimate of the electricity supplied between the date of the last meter reading and the year-end. Electricity sales to corporate customers are recognised on the basis of issued invoices according to meter readings of customers. Revenues from electricity sales to associated users are based on regulated tariffs approved by Public Utilities Commission, while revenues from market participants – on contractual prices included in electricity trade agreements. Revenues from trade of electricity in Nord Pool power exchange are based on the calculated market prices.

**b) Heat sales**

The Group recognises revenue from sales of thermal energy at the end of each month on the basis of the meter readings.

**c) Connection fees**

When connecting to the electricity network, the clients must pay a connection fee that partly reimburses for the cost of infrastructure to be built to connect the client to the network. Connection fees are carried in the Consolidated Statement of Financial Position as deferred income and amortised to Consolidated Statement of Profit or Loss on a straight-line basis over the estimated customer relationship period.

**d) Sales of distribution services**

Revenues from electricity distribution services are based on regulated tariffs that are subject to approval by the Public Utilities Commission. The Group recognizes revenue from sales of distribution services at the end of each month on the basis of the automatically made meter readings or customers' reported meter readings.

**e) Lease and management of transmission system assets**

Revenues from lease and management of transmission system assets are recognised on the basis of invoices which are prepared for transmission system operator accordingly to lease agreement.

**f) Sales of IT & telecommunication services**

Revenues derived from information technology services (internet connection services, data communication services), open electronic communication network and telecommunication services to customers are recognised on the basis of invoices which are prepared for clients upon either usage of services listed in telecommunications billing system.

**g) Interest income**

Interest income is recognised using the effective interest method. Interest income is recorded in the Consolidated Statement of Profit or Loss as "Finance income".

**h) Dividend income**

Revenue is recognised when the Group's right to receive the payment is established, which is generally when shareholders approve the dividend.

**i) Accrued income on mandatory procurement public service obligation fee**

Before the applying of agent principle (until 1<sup>st</sup> of April 2014) revenue on mandatory procurement PSO fee was recognised as accrued income as the amount of income on mandatory procurement can be reliably measured and it was virtually certain that the economic benefits from mandatory procurement will flow to the Group with collected mandatory procurement PSO fees from electricity end users. Income from mandatory procurement component was calculated as difference between mandatory procurement expenses above the electricity market price and collected mandatory procurement component payments from all end users of electricity.

**j) Mandatory procurement public service obligation fees**

Since 1<sup>st</sup> of April 2014 revenue from mandatory procurement public service obligation fees is not recognised in the Consolidated Statement of Profit or Loss, but as assets or liabilities in the Consolidated Statement of Financial Position by applying agent accounting principle as subsidiary Energijas publiskais tirgotājs AS (hereinafter – the entity) is acting in management of the mandatory procurement process as an agent. Features that indicate that an entity is acting as an agent include:

- The entity has not the primary responsibility for including the mandatory procurement public service obligation fee as a part of the services or products ordered or purchased by customers;
- The entity has not latitude in establishing prices, either directly or indirectly,
- The entity does not bear the customer's credit risk for the amount receivable from the customer.

By applying agent principle revenue from sale of electricity (generated by subsidised electricity producers) in Nord Pool power exchange by market price, received mandatory procurement PSO fee, received government grant for compensating the increase of mandatory procurement costs, costs of purchased electricity under the mandatory procurement from electricity producers who generate electricity in efficient cogeneration process or using renewable energy sources, as well as guaranteed fees for installed electrical capacity in cogeneration plants (over 4 MW), are recognised in net amount in assets as unsettled revenue on mandatory procurement PSO fee or in net amount in liabilities. Fee

from mandatory procurement administration or agent fee is recognised in the Consolidated Statement of Profit or Loss in 'Other revenue' (Note 6).

#### **2.25. Related parties**

The parties are considered related when one party has a possibility to control the other one or has significant influence over the other party in making financial and operating decisions. Related parties of the Group are associates, Shareholder of the Parent Company who could control or who has significant influence over the Group's entities in accepting operating business decisions, key management personnel of the Group's entities including members of Supervisory body – Audit Committee and close family members of any above-mentioned persons, as well as entities over which those persons have control or significant influence.

#### **2.26. Non-current assets held for sale**

The Group classifies non-current assets as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use, and sale is considered highly probable. Non-current assets held for sale are measured at the lower of their carrying amount and fair value less costs of selling.

#### **2.27. Share capital**

The Group's share capital consists of the Parent Company's ordinary shares. All shares have been fully paid.

#### **2.28. Events after the reporting period**

Events after the reporting period that provide additional information about the Group's position at the balance sheet date (adjusting events) are reflected in the financial statements. Events after the reporting period that are not adjusting events are disclosed in the notes when material.

### 3. FINANCIAL RISK MANAGEMENT

#### 3.1. Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value and cash flow interest rate risk), credit risk, pricing risk and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.

Risk management (except for pricing risk) is carried out by the Parent Company's Treasury department (the Group Treasury) according to the Financial Risk Management

Policy approved by the Parent Company's Management Board. The Group Treasury identifies, evaluates and hedges financial risks in close co-operation with the Group's operating units / subsidiaries. The Parent Company's Management Board by approving the Financial Risk Management Policy provides written principles for overall risk management, as well as written policies covering specific areas, such as interest rate risk, foreign exchange risk, liquidity risk, and credit risk, use of financial instruments and investment of excess liquidity. Pricing risk management is carried out by the Parent Company's Electricity Trading department according to Electricity Wholesale Regulation approved by the Parent Company's Management Board.

#### Financial assets by categories:

|  | Notes | Loans and receivables | Derivatives used for hedging | Held-to-maturity assets |
|--|-------|-----------------------|------------------------------|-------------------------|
|  |       | EUR'000               | EUR'000                      | EUR'000                 |
| <b>Financial assets as of 31<sup>st</sup> of December 2015</b> |       |                       |                              |                         |
| Trade receivables, net   | 17 a  | 112,163               | -                            | -                       |
| Other non-current receivables                                  |       | 1,712                 | -                            | -                       |
| Accrued income and other financial current receivables         | 17 b  | 144,182               | -                            | -                       |
| Held-to-maturity financial assets                              | 21 a  | -                     | -                            | 28,468                  |
| Cash and cash equivalents                                      | 18    | 104,543               | -                            | -                       |
|  |       | <b>362,600</b>        | <b>-</b>                     | <b>28,468</b>           |
| <b>Financial assets as of 31<sup>st</sup> of December 2014</b> |       |                       |                              |                         |
| Trade receivables, net   | 17 a  | 122,293               | -                            | -                       |
| Other non-current receivables                                  |       | 14                    | -                            | -                       |
| Accrued income and other financial current receivables         | 17 b  | 99,210                | -                            | -                       |
| Held-to-maturity financial assets                              | 21 a  | -                     | -                            | 28,528                  |
| Cash and cash equivalents                                      | 18    | 121,011               | -                            | -                       |
|  |       | <b>342,528</b>        | <b>-</b>                     | <b>28,528</b>           |

#### Financial liabilities by categories:

|   | Notes   | Derivatives used for hedging | Other financial liabilities at amortised cost | Liabilities at fair value through the profit or loss |
|---|---------|------------------------------|---|--|
|   |         | EUR'000                      | EUR'000                                       | EUR'000  |
| <b>Financial liabilities as of 31<sup>st</sup> of December 2015</b> |         |                              |   |  |
| Borrowings  | 21 b    | -                            | 797,483                                       | -  |
| Derivative financial instruments                                    | 21 c, l | 12,256                       | -   | 3,318  |
| Trade and other payables  | 24      | -                            | 80,948  | -  |
|   |         | <b>12,256</b>                | <b>878,431</b>                                | <b>3,318</b>   |
| <b>Financial liabilities as of 31<sup>st</sup> of December 2014</b> |         |                              |   |  |
| Borrowings  | 21 b    | -                            | 827,222                                       | -  |
| Derivative financial instruments                                    | 21 c, l | 16,333                       | -   | 4,220  |
| Trade and other payables  | 24      | -                            | 101,940                                       | -  |
|   |         | <b>16,333</b>                | <b>929,162</b>                                | <b>4,220</b>   |

## **a) Market risk**

### *I) Foreign currencies exchange risk*

The introduction of euro in Latvia as of 1<sup>st</sup> of January 2014 prevented the euro currency risk, which primarily was arising from settlements in foreign currencies for borrowings, capital expenditures and imported electricity. As of 31<sup>st</sup> of December 2015 the Group had borrowings denominated only in euros (Note 21 b).

Management has set up a Financial Risk Management Policy inter alia to manage the Group's foreign currencies exchange risk against functional currency. To manage the Group's foreign currencies exchange risk arising from future transactions and recognised assets and liabilities, the Financial Risk Management Policy is to use forward contracts. Foreign currencies exchange risk arises when future transactions or recognised assets or liabilities are denominated in a currency that is not the Group's functional currency.

The Group Treasury's Financial Risk Management Policy is to hedge all anticipated cash flows (capital expenditure and purchase of inventory) in each major foreign currency that might create significant currency risk. During 2015 the Group had not any capital expenditure project which expected transactions would create significant currency risk (Note 21 c, IV).

In 2015 the Parent Company had not any certain investments, which were exposed to foreign currency risks. The introduction of euro in Lithuania as of 1<sup>st</sup> of January 2015 prevented the euro currency risk arising from Parent Company's investments in subsidiary in Lithuania.

### *II) Cash flow and fair value interest rate risk*

As the Group has significant floating interest-bearing assets and liabilities exposed to interest rate risk, the Group's financial income and operating cash flows are substantially dependent on changes in market interest rates.

During 2015, if euro interest rates had been 50 basis points higher or lower with all other variables held constant, the Group's income from the cash reserves held at bank for the year would have been EUR 638 thousand higher or lower (2014: EUR 314 thousand).

The Group's cash flow interest rate risk mainly arises from long-term borrowings at variable rates. They expose the Group to a risk that finance costs might increase significantly when interest rates rise up. The Group's policy is to maintain at least 35% of its borrowings as fixed interest rates borrowings (taking into account the effect of interest rate swaps) with duration between 2–4 years.

The Group analyses its interest rate risk exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions and hedging. Based on these scenarios, the Group calculates the impact on profit and loss as well as on cash

flows of a defined interest rate shift.

Generally, the Group raises long-term borrowings at floating rates and based on the various scenarios, the Group manages their cash flow interest rate risk by using floating-to-fixed interest rate swaps. Such interest rate swaps have the economic effect of converting borrowings from floating rates to fixed rates. Thereby fixed rates are obtained that are lower than those available if the Group borrowed at fixed rates directly. Under the interest rate swaps, the Group agrees with other parties to exchange, at specified intervals (primarily semi-annually), the difference between fixed contract rates and floating-rate interest amounts calculated by reference to the agreed notional amounts.

To hedge cash flow interest rate risk the Group has entered into rate swap agreements with total notional amount of EUR 221.5 million (2014: EUR 320.0 million) (Note 21 c, II). As of 31<sup>st</sup> of December 2015 55 % of the total Group's borrowings (31/12/2014: 42 %) had fixed interest rate (taking into account the effect of the interest rate swaps) and average fixed rate duration was 2.4 years (2014: 2.2 years).

During 2015, if interest rates on euro denominated borrowings at floating base interest rate (after considering hedging effect) had been 50 basis points higher with all other variables held constant, the Group's profit for the year net of taxes would have been EUR 1,929 thousand lower (2014: EUR 2,164 thousand), while if the rates had been 50 basis points lower – profit for the year net of taxes would have been EUR 1,894 higher.

The Group's borrowings with floating rates do not impose fair value interest rate risk. Derivatives such as interest rate swaps are the only source of fair value interest rate risk.

At 31<sup>st</sup> of December 2015, if short and long term euro interest rates had been 50 basis points higher with all other variables held constant fair value of interest rate swaps would have been EUR 4,126 thousand higher (31/12/2014: EUR 5,321 thousand), of which EUR 52 thousand (2014: EUR 209 thousand) would have been attributable to Consolidated Statement of Profit or Loss and EUR 4,074 thousand (2014: EUR 5,112 thousand) to the Consolidated Statement of Other Comprehensive Income as hedge accounting item, while if the rates had been 50 basis points lower, fair value of interest rate swaps would have been EUR 4,269 lower, of which EUR 53 thousand (2014: EUR 209 thousand) would have been attributable to Consolidated Statement of Profit or Loss and EUR 4,216 thousand (2014: EUR 5,112 thousand) to the Consolidated Statement of Other Comprehensive Income as hedge accounting item.

### *III) Price risk*

Price risk is the risk that the fair value and cash flows of financial instruments will fluctuate in the future due to reasons other than changes in the market prices resulting from interest rate risk or foreign exchange

risk. The purchase and sale of goods produced and the services provided by the Group under the free market conditions, as well as the purchases of resources used in production is impacted by the price risk.

The most significant price risk is related to purchase of electricity. To hedge the risk related to changes in the price of electricity the Parent Company during 2015 has purchased electricity forward and future contracts (Note 21 c, III).

#### b) Credit risk

Credit risk is managed at the Group level. Credit risk arises from cash and cash equivalents, derivative financial instruments and deposits with banks,

outstanding receivables. Credit risk exposure in connection with trade receivables is limited due to broad range of the Group's customers. The Group has no significant concentration of credit risk with any single counterparty or group of counterparties having similar characteristics. Impairment loss has been deducted from gross accounts receivable (Note 17).

The maximum credit risk exposure related to financial assets comprises of carrying amounts of cash and cash equivalents (see table below and Note 18), trade and other receivables (Note 17), derivative financial instruments (Note 21 c) and held-to-maturity financial assets (Note 21 a).

#### Assessment of maximum possible exposure to credit risk

|   | Notes | 31/12/2015     | 31/12/2014     |
|---|-------|----------------|----------------|
|   |       | EUR'000        | EUR'000        |
| Trade receivables                       | 17 a  | 112,163        | 122,293        |
| Accrued income                          | 17 b  | 1,148          | 17,063         |
| Other non-current financial receivables |       | 1,712          | 14             |
| Other current financial receivables     | 17 b  | 1,974          | 19,001         |
| Cash and cash equivalents               | 18    | 104,543        | 121,011        |
| Held-to-maturity financial assets       | 21 a  | 28,468         | 28,528         |
|   |       | <b>250,008</b> | <b>307,910</b> |

For banks and financial institutions, independently rated parties with own or parent bank's minimum rating of investment grade are accepted. Otherwise, if there is no independent rating, management performs risk control to assess the credit quality of the financial counterparty, taking into account its financial position, past co-operation experience and other factors. After performed assessment individual credit limits are set based on internal ratings in accordance with principles set by the Financial Risk Management Policy. The basis for estimating the credit quality of financial assets not past due and not impaired is credit ratings assigned by the rating agencies or, in their absence, the earlier credit behaviour of clients and other parties to the contract.

For estimation of the credit quality of fully performing trade receivables two rating categories are used:

- Customers with no overdue receivables,
- Customers with overdue receivables.

Credit limits are regularly monitored.

Credit risk related to cash and short-term deposits with banks is managed by balancing the placement of financial assets in order to maintain the possibility to choose the best offers and to reduce probability to incur losses.

The table below shows the balance of cash and cash equivalents by financial counterparties at the end of the reporting period:

|  | 31/12/2015     | 31/12/2014     |
|--|----------------|----------------|
|  | EUR'000        | EUR'000        |
| Investment level credit rating*          | 99,069         | 95,325         |
| No or non-investment level credit rating | 5,474          | 25,686         |
|  | <b>104,543</b> | <b>121,011</b> |

\* investment level credit rating assigned for the parent companies of Baltic banks



No credit limits were exceeded during the reporting period, and the Group management does not expect any losses due to occurrence of credit risk.

### c) Liquidity risk

The Group's policy of liquidity risk management is to maintain sufficient amount of cash and cash equivalents, the availability of long and short term funding through an adequate amount of committed credit facilities to meet commitments according to the Group's strategic plans as well as to compensate the fluctuations in the cash flows due to occurrence of variety of financial risks.

The Group entities' management is monitoring rolling forecasts of the Group's liquidity reserve, which comprises of undrawn borrowing facilities (Note 21 b), and cash and cash equivalents (Note 18).

The table below analyses the Group's financial liabilities into relevant maturity groupings based on the settlement terms. The amounts disclosed in the table are the contractual undiscounted cash flows. Contractual undiscounted cash flows originated by the borrowings are calculated taking into account the actual interest rates at the end of the reporting period.

### Liquidity analysis (contractual undiscounted cash flows)

|  | Less than<br>1 year | From<br>1 to 2 years | From<br>3 to 5 years | Over<br>5 years | TOTAL            |
|--|---------------------|----------------------|----------------------|-----------------|------------------|
|  | EUR'000             | EUR'000              | EUR'000              | EUR'000         | EUR'000          |
| <b>At 31<sup>st</sup> of December 2015</b> |                     |                      |                      |                 |                  |
| Borrowings from banks                      | 88,727              | 81,556               | 307,390              | 175,820         | 653,493          |
| Issued debt securities (bonds)             | 4,365               | 74,519               | 41,864               | 77,751          | 198,499          |
| Derivative financial instruments           | 17,320              | 4,950                | 5,727                | 1,683           | 29,680           |
| Trade and other payables*                  | 80,948              | –                    | –                    | –               | 80,948           |
|  | <b>191,360</b>      | <b>161,025</b>       | <b>354,981</b>       | <b>255,254</b>  | <b>962,620</b>   |
| <b>At 31<sup>st</sup> of December 2014</b> |                     |                      |                      |                 |                  |
| Borrowings from banks                      | 148,268             | 96,802               | 312,507              | 211,340         | 768,917          |
| Issued debt securities (bonds)             | 2,940               | 2,940                | 74,900               | 35,980          | 116,760          |
| Derivative financial instruments           | 10,704              | 5,351                | 7,029                | 3,146           | 26,230           |
| Trade and other payables*                  | 101,940             | –                    | –                    | –               | 101,940          |
|  | <b>263,852</b>      | <b>105,093</b>       | <b>394,436</b>       | <b>250,466</b>  | <b>1,013,847</b> |

\* excluding advances received, deferred income, tax related liabilities and other non-current or current non-financial payables

### 3.2. Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern as well as to ensure necessary financing for investment program and to avoid breaches of covenants, which are linked to capital structure and are stipulated in the majority of loan agreements.

In order to maintain or adjust the capital structure, the Group may evaluate the amount and timing of raising new debt due to investment programs or initiate new investments in the share capital

by shareholder. Also asset revaluation directly influences the capital structure. To comply with loan covenants, the Group monitors capital on the basis of the capital ratio.

This ratio is calculated by dividing the equity by the sum of total assets and nominal value of issued and outstanding financial guarantees. According to the Group's strategy and defined loan covenants as per loan agreements the capital ratio shall be maintained at least at 30 % level.

The capital ratio figures were as follows:

|                      | 31/12/2015  | 31/12/2014  |
|----------------------|-------------|-------------|
|                      | EUR'000     | EUR'000     |
| Total equity         | 2,096,702   | 2,020,801   |
| Total assets         | 3,517,372   | 3,486,576   |
| <b>Capital Ratio</b> | <b>60 %</b> | <b>58 %</b> |

## 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgments are regularly evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

### **a) Estimates concerning property, plant and equipment**

#### *1) Useful lives of property, plant and equipment*

The Group makes estimates concerning the expected useful lives and residual values of property, plant and equipment. These are reviewed at the end of each reporting period and are based on the past experience as well as industry practice. Previous experience has shown that the actual useful lives have sometimes been longer than the estimates. As of 31<sup>st</sup> of December 2015, the net book amount of property, plant and equipment of the Group totalled EUR 3,076 million (31/12/2014: EUR 3,066 million), and the depreciation charge for the reporting period was EUR 179.1 million (2014: EUR 174.1 million) (Note 14 a). If depreciation rates were changed by 10 %, the annual depreciation charge would change by EUR 17.9 million (2014: EUR 17.4 million).

#### *II) Recoverable amount of property, plant and equipment*

When the events and circumstances indicate a potential impairment, the Group performs impairment tests for items of property, plant and equipment. According to these tests assets are written down to their recoverable amounts, if necessary. When carrying out impairment tests management uses various estimates for the cash flows arising from the use of the assets, sales, maintenance, and repairs of the assets, as well as in respect of the inflation and growth rates. The estimates are based on the forecasts of the general economic environment, consumption and the sales price of electricity. If the situation changes in the future, either additional impairment could be recognised, or the previously recognised impairment could be partially or fully reversed. Such factors as high maintenance and reconstruction costs, low load of several auxiliaries, comparatively substantial maintenance expense, limited facilities to sell property, plant and equipment in the market and other essential factors have an impact of decreasing of the recoverable amounts. If discount rate used for the purposes of impairment charge calculation would be lower or higher by one per cent point the current year's impairment charge on technological equipment would be by EUR 29.0 million higher or lower (2014: EUR 32.5 million). Impairment charges recognised during the current reporting year are disclosed in Note 14 d.

#### *III) Revaluation*

External, certified valuers have performed revaluation for part of the Group's property, plant and equipment by applying the depreciated replacement cost model. Valuation has been performed according to international standards on property valuation and IAS 16, *Property, plant and equipment*, based on current use of property, plant and equipment that is estimated as the highest and best use of these assets. As a result of valuation, depreciated replacement cost was determined for each asset. Depreciated replacement cost is calculated as property, plant and equipment instant market value at its current use, increased by the replacement cost of existing buildings, machinery and equipment as well as refinements on the said property, plant and equipment decreased by the depreciation expenses and other impairment losses. In 2015 the Group started revaluation process for property, plant and equipment of distribution system. Amounts of revalued property, plant and equipment categories had been determined as of 1<sup>st</sup> of January 2015, but considering the large amount of revalued assets, the revaluation process had been finished in December 2015. Respectively, after the recognition of revaluation results (see Note 14 c), the impairment charge in the amount of EUR 14,564 thousand for revalued distribution system technology equipment and machinery recognised in 2014 had been reversed. For property, plant and equipment of Daugava hydropower plants revaluation was performed as of 1<sup>st</sup> of January 2012 and for property, plant and equipment of transmission system as of 1<sup>st</sup> of January 2011.

### **b) Recoverable amount of trade receivables**

The estimated collectability of accounts receivable is assessed on the basis of trade receivables aging analysis according to estimates defined by the Group entities management and the Parent Company's management. In case individual assessment is not possible due to the large number of individual balances, receivables are classified into groups of similar credit risk characteristics and are collectively assessed for impairment, using historical loss experience. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. The circumstances indicating an impairment loss may include initiated insolvency of the debtor and inability to meet payment terms (point 2.12.). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss incurred (Note 17).

### **c) Fair value estimation for financial instruments**

The following table presents the Group's financial assets and liabilities that are measured at fair value, by valuation method. The different levels have been defined as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1),
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (Level 2),
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (Level 3).

#### d) Recognition of connection service fees

Connection and other service fees are recognised as income over the estimated customer relationship period, which is 20 years (see Note 23). The estimated customer relationship period is based on the Management's estimate. In the reporting period the Group's received connection fees totalled EUR 16.2 million (2014: EUR 18.2 million), and to the Consolidated Statement of Profit or Loss credited EUR 11.6 million (2014: EUR 10.9 million), see Note 23.

| As of 31 <sup>st</sup> of December 2015                     | Notes     | Level 1 | Level 2       | Level 3 | Total balance |
|---|-----------|---------|---------------|---------|---------------|
|   |           | EUR'000 | EUR'000       | EUR'000 | EUR'000       |
| <b>Liabilities</b>  |           |         |               |         |               |
| Financial liabilities at fair value through profit or loss: |           |         |               |         |               |
| – Electricity trading derivatives                           | 21 c, III | –       | 2,558         | –       | 2,558         |
| – Interest rate derivatives                                 | 21 c, II  | –       | 760           | –       | 760           |
| Interest rate derivatives used for hedging                  | 21 c, II  | –       | 12,256        | –       | 12,256        |
| <b>Total liabilities</b>                                    |           | –       | <b>15,574</b> | –       | <b>15,574</b> |

| As of 31 <sup>st</sup> of December 2014                     | Notes     | Level 1 | Level 2       | Level 3 | Total balance |
|---|-----------|---------|---------------|---------|---------------|
|   |           | EUR'000 | EUR'000       | EUR'000 | EUR'000       |
| <b>Liabilities</b>  |           |         |               |         |               |
| Financial liabilities at fair value through profit or loss: |           |         |               |         |               |
| – Electricity trading derivatives                           | 21 c, III | –       | 2,112         | –       | 2,112         |
| – Interest rate derivatives                                 | 21 c, II  | –       | 2,108         | –       | 2,108         |
| Interest rate derivatives used for hedging                  | 21 c, II  | –       | 16,333        | –       | 16,333        |
| <b>Total liabilities</b>                                    |           | –       | <b>20,553</b> | –       | <b>20,553</b> |

If the estimated customer relationship period is reduced/increased by 25 %, the annual income from connection service fees would increase/decrease by EUR 2.9 million (2014: EUR 2.7 million).

#### e) Recognition and revaluation of provisions

As of 31<sup>st</sup> of December 2015, the Group had set up provisions for environmental protection and post-employment benefits totalling EUR 16.0 million (31/12/2014: EUR 15.6 million) (Note 22). The amount and timing of the settlement of these obligations is uncertain. A number of assumptions and estimates have been used to determine the present value of provisions, including the amount of future expenditure, inflation rates, and the timing of settlement of the expenditure. The actual expenditure may also differ from the provisions recognised as a result of possible changes in legislative norms, technology available in the future to restore environmental damages, and expenditure covered by third parties. For revaluation of provisions for post-employment obligations probabilities of retirement in different employees' aging groups as well as variable demographic factors and financial factors (including expected remuneration increase and determined changes in benefit amounts) have been estimated. The probabilities and other factors are determined on the basis of previous experience.

#### f) Evaluation of effectiveness of hedging instruments

The Group has concluded significant number of forward and future contracts and swap agreements to hedge the risk of the changes in prices of electricity and interest rate fluctuations to which cash flow hedge risk accounting is applied and the gains and losses from changes in the fair value of the effective hedging instruments and items secured against risk are included in respective equity reserve. The evaluation of the effectiveness of the hedging is based on Management's estimates with regard to future purchase transactions of electricity and signed variable interest loan agreements. When hedging instruments turn out to be ineffective, gains/losses from the changes in the fair value are recognised in the Consolidated Statement of Profit or Loss (Note 21 c).

#### g) Held-to-maturity financial assets

The management of the Group applies judgement in assessing whether financial assets can be categorised as held-to-maturity at initial recognition, in particular (a) its intention and ability to hold the assets to maturity and (b) whether the assets are quoted in an active market. If the Group fails to keep these investments to maturity other than in certain specific circumstances – for example, selling an insignificant amount or settle

a position close to maturity – it will be required to reclassify the entire category as available-for-sale. The investments would therefore be measured at fair value rather than amortised cost. For the estimated fair value of investment securities held-to-maturity as of 31<sup>st</sup> of December 2015 refer to Note 21 a.

Evidence of an active market exists if quoted prices are readily and regularly available from an exchange, dealer, broker, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis.

#### **h) Financial investments**

The Group has applied judgement in determining that it has a financial investment with 48.15 % interest held in the company Pirmais Slēgtais Pensiju Fonds AS that manages closed pension plan in Latvia as investment that has been valued at cost without applying equity method. The Group is only a nominal shareholder as all risks and benefits arising from management of pension plan will accrue to the Group's employees who are members of the pension plan and the Group does not have existing rights that give it the current ability to direct the relevant activities of the investee. Therefore this investment has been determined as financial investment in Pirmais Slēgtais Pensiju Fonds AS and not as investment in associate.

#### **i) Use of agent principle**

The Group has applied significant judgement for use of agent principle for recognition of net revenue on mandatory procurement PSO fee (difference between revenue from sale of electricity in Nord Pool power exchange by market price, received mandatory procurement PSO fee, received government grant for compensating the increase of mandatory procurement costs and costs of purchased electricity under the mandatory procurement from electricity generators who generate electricity in efficient cogeneration process or using renewable energy sources, as well as guaranteed fees for installed electrical capacity in cogeneration plants). Since 1st of April 2014 net revenue from mandatory procurement PSO fees is not recognised in the Consolidated Statement of Profit or Loss, but as assets or liabilities in the Consolidated Statement of Financial Position by applying agent accounting principle as subsidiary Enerģijas publiskais tirgotājs AS is acting in management of the mandatory procurement process as an agent because it does not have exposure to the significant risks and rewards associated with mandatory procurement PSO fees according to IAS 18. PSO fee by its nature is considered as part of service that is compensated to administrator of the mandatory procurement process by electricity suppliers and distribution system operators.

## 5. OPERATING SEGMENT INFORMATION

### **Operating segments**

For segment reporting purposes, the division into operating segments is based on the Group's internal management structure, which is the basis for the reporting system, performance assessment and the allocation of resources by the operating segment decision maker.

The Group divides its operations into three main operating segments – generation and supply, distribution and lease of transmission system assets. In addition, Corporate Functions, that cover administration and other support services, are presented separately.

**Generation and supply** comprises the Group's electricity and thermal energy generation operations, which are organised into the legal entities: Latvenergo AS and Liepājas enerģija SIA; electricity supply (including electricity wholesale), in the Baltics carried out by Latvenergo AS, Elektrum Eesti OÜ and Elektrum Lietuva UAB, as well as administration of the mandatory procurement process provided by Enerģijas publiskais tirgotājs AS.

**The operations of the distribution operating segment** relates to the provision of electricity distribution services in Latvia and is managed by the subsidiary Sadales tīkls AS (the largest distribution system operator in Latvia) and by Latvenergo AS – the owner of real estate assets related to distribution system assets.

**The operations of the lease of transmission system assets operating segment** is managed both by Latvijas elektriskie tīkli AS – the owner of transmission system assets (330 kV and 110 kV transmission lines, substations and distribution points), which provides financing of investments in these assets, and Latvenergo AS – the owner of real estate assets related to the transmission

system assets, providing the lease of these assets to the transmission system operator Augstsprieguma tīkls AS.

The following table presents revenue, profit information and segment assets and liabilities of the Group's operating segments. Inter-segment revenue is eliminated on consolidation.

|  | Genera-<br>tion and<br>supply | Distri-<br>bution<br>system<br>services | Lease of<br>trans-<br>mission<br>system<br>assets* | Corporate<br>Functions | TOTAL<br>segments | Adjust-<br>ments and<br>elimina-<br>tions | Consoli-<br>dated |
|--|-------------------------------|---|--|------------------------|-------------------|---|-------------------|
|  | EUR'000                       | EUR'000                                 | EUR'000  | EUR'000                | EUR'000           | EUR'000                                   | EUR'000           |
| <b>Year ended 31<sup>st</sup> of December 2015</b>                           |                               |   |  |                        |                   |   |                   |
| <b>Revenue</b>   |                               |   |  |                        |                   |   |                   |
| External customers   | 593,937                       | 282,752                                 | 44,151   | 8,288                  | <b>929,128</b>    | –   | <b>929,128</b>    |
| Inter-segment  | 16,173                        | 1,599                                   | 2,459  | 46,198                 | <b>66,429</b>     | (66,429)                                  | –                 |
| <b>TOTAL revenue</b>   | <b>610,110</b>                | <b>284,351</b>                          | <b>46,610</b>                                      | <b>54,486</b>          | <b>995,557</b>    | <b>(66,429)</b>                           | <b>929,128</b>    |
| <b>Results</b>   |                               |   |  |                        |                   |   |                   |
| Amortisation, depreciation and property, plant and equipment impairment loss | (76,709)                      | (85,865)                                | (24,206)   | (12,047)               | <b>(198,827)</b>  | –   | <b>(198,827)</b>  |
| <b>Segment profit</b>  | <b>87 221</b>                 | <b>(4 177)</b>                          | <b>20 750</b>                                      | <b>4 394</b>           | <b>108 188</b>    | <b>(15 653)</b>                           | <b>92 535</b>     |
| <b>Segment assets at the end of the year</b>                                 | <b>1,548,341</b>              | <b>1,312,819</b>                        | <b>432,028</b>                                     | <b>89,350</b>          | <b>3,382,538</b>  | <b>134,834</b>                            | <b>3,517,372</b>  |
| <b>Segment liabilities at the end of the year</b>                            | <b>63,880</b>                 | <b>179,257</b>                          | <b>45,818</b>                                      | <b>6,685</b>           | <b>295,640</b>    | <b>1,125,030</b>                          | <b>1,420,670</b>  |
| Capital expenditure  | 57,305                        | 101,283                                 | 17,453   | 14,420                 | <b>190,461</b>    | –   | <b>190,461</b>    |
| <b>Year ended 31<sup>st</sup> of December 2014</b>                           |                               |   |  |                        |                   |   |                   |
| <b>Revenue</b>   |                               |   |  |                        |                   |   |                   |
| External customers   | 652,778                       | 295,314                                 | 57,795   | 4,870                  | <b>1,010,757</b>  | –   | <b>1,010,757</b>  |
| Inter-segment  | 24,603                        | 2,040                                   | 2,933  | 46,432                 | <b>76,008</b>     | (76,008)                                  | –                 |
| <b>TOTAL revenue</b>   | <b>677,381</b>                | <b>297,354</b>                          | <b>60,728</b>                                      | <b>51,302</b>          | <b>1,086,765</b>  | <b>(76,008)</b>                           | <b>1,010,757</b>  |
| <b>Results</b>   |                               |   |  |                        |                   |   |                   |
| Amortisation, depreciation and property, plant and equipment impairment loss | (74,492)                      | (77,498)                                | (24,293)   | (11,312)               | <b>(187,595)</b>  | –   | <b>(187,595)</b>  |
| <b>Segment profit</b>  | <b>11,935</b>                 | <b>15,010</b>                           | <b>16,416</b>                                      | <b>5,882</b>           | <b>49,243</b>     | <b>(17,733)</b>                           | <b>31,510</b>     |
| <b>Segment assets at the end of the year</b>                                 | <b>1,514,218</b>              | <b>1,272,355</b>                        | <b>456,723</b>                                     | <b>87,283</b>          | <b>3,330,579</b>  | <b>155,997</b>                            | <b>3,486,576</b>  |
| <b>Segment liabilities at the end of the year</b>                            | <b>73,185</b>                 | <b>185,019</b>                          | <b>48,934</b>                                      | <b>6,300</b>           | <b>313,438</b>    | <b>1,152,337</b>                          | <b>1,465,775</b>  |
| Capital expenditure  | 33,542                        | 99,830                                  | 31,836   | 12,399                 | <b>177,607</b>    | –   | <b>177,607</b>    |

\* in accordance with European Union Directive 2009/72/EC and concerning common rules for the internal market of electricity and the Electricity Market Law of the Republic of Latvia, Latvijas elektriskie tīkli AS on 1<sup>st</sup> of January 2015 transferred to Augstsprieguma tīkls AS functions of the reconstruction or renewal, operation and routine maintenance of the existing transmission system network as well as development of the transmission system and construction of new networks. Due to transfer of these functions has been changed the name of operating segment from "Management of transmission system assets" to "Lease of transmission system assets"

### Adjustments and eliminations

Finance income and expenses, fair value gains and losses on financial assets are not allocated to individual segments as the underlying instruments are managed on a group basis. Taxes and certain financial assets and liabilities are not allocated to those segments as they are also managed on a group basis.

Capital expenditure consists of additions of property, plant and equipment, intangible assets and investment properties including assets from the acquisition of subsidiaries.

### Reconciliation of profit

|  | Notes | 2015           | 2014          |
|--|-------|----------------|---------------|
|  |       | EUR'000        | EUR'000       |
| <b>Segment profit</b>                  |       | <b>108,188</b> | <b>49,243</b> |
| Finance income                         | 11 a  | 2,926          | 3,004         |
| Finance costs                          | 11 b  | (18,579)       | (20,380)      |
| Share of profit / (loss) of associates | 15    | –              | (357)         |
| <b>Profit before tax</b>               |       | <b>92,535</b>  | <b>31,510</b> |

### Reconciliation of assets

|                                       | Notes | 31/12/2015       | 31/12/2014       |
|---------------------------------------|-------|------------------|------------------|
|                                       |       | EUR'000          | EUR'000          |
| <b>Segment operating assets</b>       |       | <b>3,382,538</b> | <b>3,330,579</b> |
| Non-current financial investments     | 15    | 41               | 41               |
| Held-to-maturity financial assets     | 21 a  | 28,468           | 28,528           |
| Other assets and assets held for sale |       | 1,782            | 6,417            |
| Cash and cash equivalents             | 18    | 104,543          | 121,011          |
| <b>Group operating assets</b>         |       | <b>3,517,372</b> | <b>3,486,576</b> |

### Reconciliation of liabilities

|  | Notes | 31/12/2015       | 31/12/2014       |
|--|-------|------------------|------------------|
|  |       | EUR'000          | EUR'000          |
| <b>Segment operating liabilities</b>     |       | <b>295,640</b>   | <b>313,438</b>   |
| Deferred income tax liabilities          | 12    | 273,987          | 268,026          |
| Current corporate income tax liabilities |       | 4,007            | 3                |
| Borrowings                               | 21 b  | 797,483          | 827,222          |
| Derivative financial instruments         | 21 c  | 15,574           | 20,553           |
| Trade and other payables                 |       | 33,979           | 36,533           |
| <b>Group operating liabilities</b>       |       | <b>1,420,670</b> | <b>1,465,775</b> |

### Geographical information on segments

|  | 2015           | 2014             |
|--|----------------|------------------|
|  | EUR'000        | EUR'000          |
| <b>Revenue from external customers</b> |                |                  |
| Baltics                                | 914,927        | 997,445          |
| Scandinavian countries                 | 14,201         | 13,312           |
| <b>TOTAL revenue</b>                   | <b>929,128</b> | <b>1,010,757</b> |

Non-current assets are located in the Group's country of domicile – Latvia and consist of intangible assets, property, plant and equipment and investment properties.

Revenue from major customer in 2015 amounted to EUR 83,137 thousand (2014: EUR 98,410 thousand) arising from sales by the generation and supply segment.

## 6. REVENUE

|  | 2015           | 2014             |
|--|----------------|------------------|
|  | EUR'000        | EUR'000          |
| Electricity supply and electricity services        | 495,010        | 540,157*         |
| Distribution system services                       | 267,189        | 280,366          |
| Heat sales   | 92,525         | 108,963          |
| Lease and management of transmission system assets | 43,630         | 57,161           |
| Other revenue                                      | 30,774         | 24,110           |
| <b>TOTAL revenue</b>                               | <b>929,128</b> | <b>1,010,757</b> |

\* revenue from mandatory procurement PSO fee since the 1<sup>st</sup> of April 2014 was recognised as assets in the Consolidated Statement of Financial Position by applying agent accounting principle (Note 2.24. j)

## 7. OTHER INCOME

|   | 2015         | 2014         |
|---|--------------|--------------|
|   | EUR'000      | EUR'000      |
| Net gain from sale of assets held for sale and PPE    | 291          | 754          |
| Net gain from sale of current assets and other income | 4,589        | 4,519        |
| <b>TOTAL other income</b>                             | <b>4,880</b> | <b>5,273</b> |

## 8. RAW MATERIALS AND CONSUMABLES USED

|   | 2015           | 2014           |
|---|----------------|----------------|
|   | EUR'000        | EUR'000        |
| <b>Electricity:</b>   |                |                |
| Purchased electricity   | 196,602        | 338,551*       |
| Fair value loss / (income) on electricity forwards and futures (Note 21 c, III) | 446            | (7,800)        |
| Electricity transmission services costs   | 73,849         | 73,824         |
|   | <b>270,897</b> | <b>404,575</b> |
| Fuel expense  | 164,397        | 178,033        |
| Raw materials, spare parts and maintenance costs                                | 35,150         | 38,677         |
| <b>TOTAL raw materials and consumables used</b>                                 | <b>470,444</b> | <b>621,285</b> |

\* costs of purchased electricity under the mandatory procurement from electricity generators who generate electricity in efficient cogeneration process or using renewable energy sources, as well as guaranteed fee for installed electrical capacity in cogeneration plants (over 4 MW) since the 1<sup>st</sup> of April 2014 are recognised as assets or respective liabilities in the Consolidated Statement of Financial Position by applying agent accounting principle (Note 2.24. j)

Decrease of purchased electricity costs was impacted by lower average electricity spot prices in Baltics and lower purchased electricity amount (see Management report).

## 9. PERSONNEL EXPENSES

|   | 2015          | 2014          |
|---|---------------|---------------|
|   | EUR'000       | EUR'000       |
| Wages and salaries  | 70,437        | 74,770        |
| Expenditure of employment termination   | 2,031         | 1,824         |
| Pension costs – defined contribution plan   | 2,599         | 3,243         |
| State social insurance contributions and other benefits defined in the Collective Agreement | 17,374        | 18,376        |
| Life insurance costs  | 2,286         | 40            |
| Capitalised personnel expenses  | (118)         | (299)         |
| <b>TOTAL personnel expenses, including remuneration to the management</b>                   | <b>94,609</b> | <b>97,954</b> |

### Including remuneration to the management:

|   |              |              |
|---|--------------|--------------|
| Wages and salaries  | 1,509        | 1,459        |
| Expenditure of employment termination   | 171          | –            |
| Pension costs – defined contribution plan   | 45           | 58           |
| Life insurance costs  | 34           | 6            |
| State social insurance contributions and other benefits defined in the Collective Agreement | 235          | 251          |
| <b>TOTAL remuneration to the management*</b>  | <b>1,994</b> | <b>1,774</b> |

|   | 2015  | 2014  |
|---|-------|-------|
| Number of employees at the end of the year  | 4,177 | 4,563 |
| Average number of employees during the year | 4,162 | 4,559 |

\* remuneration to the management includes remuneration to the members of the Management Boards and Supervisory body of the Group entities

## 10. OTHER OPERATING EXPENSES

|  | 2015          | 2014          |
|--|---------------|---------------|
|  | EUR'000       | EUR'000       |
| Selling expenses and customer services         | 7,873         | 8,172         |
| Information technology maintenance             | 4,428         | 3,694         |
| Transportation expenses                        | 6,120         | 7,546         |
| Environment protection and work safety         | 4,431         | 4,224         |
| Real estate maintenance and utilities expenses | 5,760         | 5,351         |
| Telecommunications services                    | 2,009         | 1,737         |
| Electric power transit and capacity services   | 272           | 270           |
| Real estate tax                                | 1,064         | 1,063         |
| Public utilities regulation fee                | 1,172         | 987           |
| Subsidised energy tax (SET)*                   | 15,284        | 15,338        |
| Audit fee                                      | 88            | 80            |
| Other expenses                                 | 13,439        | 11,491        |
| <b>TOTAL other operating expenses</b>          | <b>61,940</b> | <b>59,953</b> |

\* subsidised energy tax according to the “Subsidised energy tax Law” has been introduced for a four-year period as of 1<sup>st</sup> of January 2014 and applies to state support for generators of subsidised electricity (Note 2.17.)



## 11. FINANCE INCOME AND COSTS

### a) Finance income

|  | 2015         | 2014         |
|--|--------------|--------------|
|  | EUR'000      | EUR'000      |
| Interest income on bank accounts and deposits                                    | 33           | 501          |
| Interest income from held-to-maturity financial assets                           | 1,545        | 1,544        |
| Fair value gain on interest rate swaps (Note 21 c, II)                           | 1,348        | 943          |
| Fair value gain on forward foreign currencies exchange contracts (Note 21 c, IV) | –            | 16           |
| <b>TOTAL finance income</b>  | <b>2,926</b> | <b>3,004</b> |

### b) Finance costs

|   | 2015          | 2014          |
|---|---------------|---------------|
|   | EUR'000       | EUR'000       |
| Interest expense on borrowings                                | 8,013         | 9,856         |
| Interest expense on issued debt securities (bonds)            | 3,748         | 2,940         |
| Interest expense on interest rate swaps                       | 6,932         | 7,555         |
| Net losses on redemption of held-to-maturity financial assets | 60            | 60            |
| Net losses on issued debt securities (bonds)                  | 9             | 1             |
| Capitalised borrowing and finance costs (Note 14 a)           | (268)         | (167)         |
| Net losses on currency exchange rate fluctuations             | 27            | 65            |
| Other finance costs   | 58            | 70            |
| <b>TOTAL finance costs</b>                                    | <b>18,579</b> | <b>20,380</b> |

## 12. INCOME TAX

|                         | 2015         | 2014         |
|-------------------------|--------------|--------------|
|                         | EUR'000      | EUR'000      |
| Current tax             | 5,011        | 2,796        |
| Deferred tax            | 2,485        | (1,076)      |
| <b>TOTAL income tax</b> | <b>7,496</b> | <b>1,720</b> |

The tax on the Group's profit before tax differs from the theoretical amount that would arise if using the tax rate applicable to profits of the Group as follows:

|   | 2015          | 2014          |
|---|---------------|---------------|
|   | EUR'000       | EUR'000       |
| <b>Profit before tax</b>  | <b>92,535</b> | <b>31,510</b> |
| Corporate income tax at the statutory rate 15 %   | 13,880        | 4,727         |
| Expense non-deductible for tax purpose  | 253           | 639           |
| Impairment of receivables   | 640           | 186           |
| Previous years losses that reduce the tax base covered by profit of the year            | 1,276         | –             |
| (Losses) / income as a result of re-measurement on defined post-employment benefit plan | (174)         | 24            |
| Real estate tax   | (160)         | (159)         |
| Tax discounts on donations  | (141)         | –             |
| Other expenses  | (76)          | 222           |
| Tax incentives for new technological equipment*   | (8,002)       | (3,919)       |
| <b>TOTAL income tax:</b>  | <b>7,496</b>  | <b>1,720</b>  |

\* increase in the amount of depreciation of PPE applying coefficients for additions of PPE and calculation of depreciation for tax purposes as defined in article No. 13 of the Law of Corporate Income Tax of the Republic of Latvia

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same taxation authority.

#### The movement on the deferred income tax accounts

|   | 2015           | 2014           |
|---|----------------|----------------|
|   | EUR'000        | EUR'000        |
| <b>At the beginning of the year</b>   | <b>268,026</b> | <b>269,116</b> |
| (Income) credited / expense charged to the Consolidated Statement of Profit or Loss | 2,485          | (1,076)        |
| Attributable to non-current assets revaluation reserve in equity (Note 20 a)        | 3,476          | (14)           |
| <b>Deferred tax liabilities at the end of the year</b>                              | <b>273,987</b> | <b>268,026</b> |

Deferred income tax has been calculated from the following temporary differences between assets and liabilities values for financial reporting and tax purposes:

|   | 2015            | 2014            |
|---|-----------------|-----------------|
|   | EUR'000         | EUR'000         |
| <b>Deferred tax liabilities</b>   |                 |                 |
| <b>Accelerated tax depreciation</b>   |                 |                 |
| <b>At the beginning of the year</b>   | <b>278 453</b>  | <b>275,167</b>  |
| (Income) credited / expense charged to the Consolidated Statement of Profit or Loss | (2,803)         | 3,300           |
| Attributable to non-current assets revaluation reserve in equity (Note 20 a)        | 3,476           | (14)            |
| <b>At the end of the year</b>   | <b>279,126</b>  | <b>278,453</b>  |
| <b>Deferred tax assets</b>  |                 |                 |
| <b>Accruals/provisions</b>  |                 |                 |
| <b>At the beginning of the year</b>   | <b>(10,427)</b> | <b>(6,051)</b>  |
| Expense charged / (income) credited to the Consolidated Statement of Profit or Loss | 5,288           | (4,376)         |
| <b>At the end of the year</b>   | <b>(5,139)</b>  | <b>(10,427)</b> |

## 13. INTANGIBLE ASSETS

### a) Intangible assets

|  | Licenses     | Software      | Assets under construction | TOTAL         |
|--|--------------|---------------|---------------------------|---------------|
|  | EUR'000      | EUR'000       | EUR'000                   | EUR'000       |
| <b>At 31<sup>st</sup> of December 2013</b>         |              |               |                           |               |
| Cost   | 2,490        | 30,654        | 3,805                     | 36,949        |
| Accumulated amortisation                           | (1,438)      | (24,381)      | –                         | (25,819)      |
| <b>Net book amount</b>                             | <b>1,052</b> | <b>6,273</b>  | <b>3,805</b>              | <b>11,130</b> |
| <b>Year ended 31<sup>st</sup> of December 2014</b> |              |               |                           |               |
| Additions  | –            | 268           | 4,740                     | 5,008         |
| Transfers  | –            | 8,217         | (8,217)                   | –             |
| Disposals  | (210)        | (27)          | –                         | (237)         |
| Amortisation charge                                | –            | (2,890)       | –                         | (2,890)       |
| <b>Closing net book amount</b>                     | <b>842</b>   | <b>11,841</b> | <b>328</b>                | <b>13,011</b> |
| <b>At 31<sup>st</sup> of December 2014</b>         |              |               |                           |               |
| Cost   | 2,490        | 38,992        | 328                       | 41,810        |
| Accumulated amortisation                           | (1,648)      | (27,151)      | –                         | (28,799)      |
| <b>Net book amount</b>                             | <b>842</b>   | <b>11,841</b> | <b>328</b>                | <b>13,011</b> |
| <b>Year ended 31<sup>st</sup> of December 2015</b> |              |               |                           |               |
| Additions  | 17           | 720           | 4,350                     | 5,087         |
| Transfers  | –            | 4,335         | (4,335)                   | –             |
| Disposals  | (211)        | –             | –                         | (211)         |
| Amortisation charge                                | –            | (3,482)       | –                         | (3,482)       |
| <b>Closing net book amount</b>                     | <b>648</b>   | <b>13,414</b> | <b>343</b>                | <b>14,405</b> |
| <b>At 31<sup>st</sup> of December 2015</b>         |              |               |                           |               |
| Cost   | 2,507        | 44,038        | 343                       | 46,888        |
| Accumulated amortisation                           | (1,859)      | (30,624)      | –                         | (32,483)      |
| <b>Net book amount</b>                             | <b>648</b>   | <b>13,414</b> | <b>343</b>                | <b>14,405</b> |

**b) Greenhouse gas emission allowances:**

|                                     | <b>2015</b>          | <b>2014</b>          |
|-------------------------------------|----------------------|----------------------|
|                                     | Number of allowances | Number of allowances |
| <b>At the beginning of the year</b> | <b>2,021,259</b>     | <b>2,619,839</b>     |
| Allowances allocated free of charge | 427,669              | 494,041              |
| Purchased allowances                | 18,000               | –                    |
| Used allowances                     | (932,725)            | (1,092,621)          |
| Sold allowances                     | (18,000)             | –                    |
| <b>At the end of the year</b>       | <b>1,516,203</b>     | <b>2,021,259</b>     |

Allowances are allocated free of charge in accordance with the law “On Pollution” and Directives of the Ministry of Environmental Protection and Regional Development of the Republic of Latvia and are recognised as off-balance sheet assets.

As of 31<sup>st</sup> of December 2015 the number of allowances in the Group received in 2015 from the Government free of charge was 427,669 (31/12/2014: 494,041). Therefore their carrying amount as of 31<sup>st</sup> of December 2015 was nil (31/12/2014: nil).

The fair value of greenhouse gas emission allowances as of 31<sup>st</sup> of December 2015 was EUR 12,509 thousand

(31/12/2014: EUR 14,755 thousand). For estimation of the fair value of allowances was used fixed daily price in NASDAQ Commodities Exchange for European Union Allowances (EUA) on 30<sup>th</sup> of December 2015 what was the last trade date in 2015 – 8.25 EUR/t (30/12/2014: 7.30 EUR/t).

Received European Union Allowances (EUA) must be used until the end of 2020.

All greenhouse gas emission allowances purchased in 2015 are sold (31/12/2014: nil).

## 14. PROPERTY, PLANT AND EQUIPMENT

### a) Property, plant and equipment

|  | Revalued buildings and facilities |                |                      | Non-re-valued buildings and facilities |                  | Land and buildings, Total |                | Revalued technology equip-ment, machinery (TEM) |                      | Non-re-valued TEM |                     | TEM TOTAL    |                      | Revalued other property, plant and equipment (PPE) |               | Non-re-valued other PPE |                  | Other PPE, Total     |                      | Assets under construction |                     | PPE TOTAL |                      |                      |         |
|--|-----------------------------------|----------------|----------------------|--|------------------|---------------------------|----------------|---|----------------------|-------------------|---------------------|--------------|----------------------|--|---------------|-------------------------|------------------|----------------------|----------------------|---------------------------|---------------------|-----------|----------------------|----------------------|---------|
|  | Hydro-power plants'               |                | Trans-mission system | Distri-bution system                   |                  | Hydro-power plants'       |                | Trans-mission system                            | Distri-bution system |                   | Hydro-power plants' |              | Trans-mission system | Distri-bution system                               |               | Hydro-power plants'     |                  | Trans-mission system | Distri-bution system |                           | Hydro-power plants' |           | Trans-mission system | Distri-bution system |         |
|  | EUR'000                           | EUR'000        | EUR'000              | EUR'000                                | EUR'000          | EUR'000                   | EUR'000        | EUR'000   | EUR'000              | EUR'000           | EUR'000             | EUR'000      | EUR'000              | EUR'000  | EUR'000       | EUR'000                 | EUR'000          | EUR'000              | EUR'000              | EUR'000                   | EUR'000             | EUR'000   | EUR'000              | EUR'000              | EUR'000 |
| <b>At 31<sup>st</sup> of December 2013</b>         |                                   |                |                      |  |                  |                           |                |   |                      |                   |                     |              |                      |  |               |                         |                  |                      |                      |                           |                     |           |                      |                      |         |
| Cost or valuation                                  | 1,499,501                         | 457,126        | 1,945,801            | 429,211                                | 4,331,639        | 329,450                   | 402,886        | 709,077   | 604,840              | 2,046,253         | 13,657              | 9,409        | 8,734                | 121,952  | 153,752       | 115,063                 | 6,646,707        |                      |                      |                           |                     |           |                      |                      |         |
| Accumulated depreciation and impairment            | (862,778)                         | (297,093)      | (1,125,961)          | (97,407)                               | (2,383,239)      | (213,422)                 | (223,970)      | (381,523)                                       | (238,687)            | (1,057,602)       | (8,209)             | (6,150)      | (5,625)              | (92,459)   | (112,443)     | (6,948)                 | (3,559,932)      |                      |                      |                           |                     |           |                      |                      |         |
| <b>Net book amount</b>                             | <b>636,723</b>                    | <b>160,033</b> | <b>819,840</b>       | <b>331,804</b>                         | <b>1,948,400</b> | <b>116,028</b>            | <b>178,916</b> | <b>327,554</b>                                  | <b>366,153</b>       | <b>988,651</b>    | <b>5,448</b>        | <b>3,259</b> | <b>3,109</b>         | <b>29,493</b>                                      | <b>41,309</b> | <b>108,415</b>          | <b>3,086,775</b> |                      |                      |                           |                     |           |                      |                      |         |
| <b>Year ended 31<sup>st</sup> of December 2014</b> |                                   |                |                      |  |                  |                           |                |   |                      |                   |                     |              |                      |  |               |                         |                  |                      |                      |                           |                     |           |                      |                      |         |
| Additions  | -                                 | -              | -                    | 49                                     | 49               | -                         | -              | 1,067   | -                    | 1,073             | -                   | 602          | 2,986                | 6,264  | 9,852         | 161,190                 | 172,164          |                      |                      |                           |                     |           |                      |                      |         |
| Invested in share capital (Note 19)*               | -                                 | -              | -                    | 435                                    | 435              | -                         | -              | -   | -                    | -                 | -                   | -            | -                    | -  | -             | -                       | 435              |                      |                      |                           |                     |           |                      |                      |         |
| Transfers  | -                                 | 56,772         | 60,266               | 29,432                                 | 146,470          | 714                       | 22,391         | 24,665  | 16,939               | 64,709            | 1                   | 385          | 489                  | 3,479  | 4,354         | (215,533)               | -                |                      |                      |                           |                     |           |                      |                      |         |
| Reclassified to investment property                | -                                 | -              | -                    | (434)                                  | (434)            | -                         | -              | -   | -                    | -                 | -                   | -            | -                    | -  | -             | -                       | (434)            |                      |                      |                           |                     |           |                      |                      |         |
| Disposals  | 13,266                            | (229)          | (1,108)              | (13,354)                               | (1,425)          | -                         | (400)          | (1,130)   | (16)                 | (1,546)           | -                   | (1,530)      | (7)                  | (6)  | (1,543)       | (11)                    | (4,525)          |                      |                      |                           |                     |           |                      |                      |         |
| Impairment charge                                  | -                                 | -              | -                    | 2                                      | 2                | -                         | -              | (14,564)  | -                    | (14,564)          | -                   | -            | -                    | -  | -             | -                       | (13,961)         |                      |                      |                           |                     |           |                      |                      |         |
| Reclassified depreciation of emergency spare parts | -                                 | -              | -                    | -                                      | -                | -                         | -              | -   | (3,394)              | (3,394)           | -                   | -            | -                    | -  | -             | -                       | (3,394)          |                      |                      |                           |                     |           |                      |                      |         |
| Depreciation                                       | (15,904)                          | (10,400)       | (41,241)             | (13,218)                               | (80,763)         | (8,958)                   | (11,960)       | (17,517)  | (39,652)             | (78,087)          | (503)               | (971)        | (910)                | (9,510)  | (11,894)      | -                       | (170,744)        |                      |                      |                           |                     |           |                      |                      |         |
| <b>Closing net book amount</b>                     | <b>634,085</b>                    | <b>206,176</b> | <b>837,757</b>       | <b>334,716</b>                         | <b>2,012,734</b> | <b>107,784</b>            | <b>188,947</b> | <b>320,075</b>                                  | <b>340,036</b>       | <b>956,842</b>    | <b>4,946</b>        | <b>1,745</b> | <b>5,667</b>         | <b>29,720</b>                                      | <b>42,078</b> | <b>54,662</b>           | <b>3,066,316</b> |                      |                      |                           |                     |           |                      |                      |         |

| <b>At 31<sup>st</sup> of December 2014</b>         |                |                |                |                |                  |                |                |                |                |                |              |              |              |               |               |               |                  |  |  |  |  |  |  |  |  |  |
|--|----------------|----------------|----------------|----------------|------------------|----------------|----------------|----------------|----------------|----------------|--------------|--------------|--------------|---------------|---------------|---------------|------------------|--|--|--|--|--|--|--|--|--|
| Cost or valuation                                  | 1,512,382      | 511,341        | 1,989,627      | 444,991        | 4,458,341        | 330,151        | 414,944        | 724,848        | 621,680        | 2,091,623      | 13,657       | 6,214        | 11,708       | 126,683       | 158,262       | 60,709        | 6,768,935        |  |  |  |  |  |  |  |  |  |
| Accumulated depreciation and impairment            | (878,297)      | (305,165)      | (1,151,870)    | (110,275)      | (2,445,607)      | (222,367)      | (225,997)      | (404,773)      | (281,644)      | (1,134,781)    | (8,711)      | (4,469)      | (6,041)      | (96,963)      | (116,184)     | (6,047)       | (3,702,619)      |  |  |  |  |  |  |  |  |  |
| <b>Net book amount</b>                             | <b>634,085</b> | <b>206,176</b> | <b>837,757</b> | <b>334,716</b> | <b>2,012,734</b> | <b>107,784</b> | <b>188,947</b> | <b>320,075</b> | <b>340,036</b> | <b>956,842</b> | <b>4,946</b> | <b>1,745</b> | <b>5,667</b> | <b>29,720</b> | <b>42,078</b> | <b>54,662</b> | <b>3,066,316</b> |  |  |  |  |  |  |  |  |  |
| <b>Year ended 31<sup>st</sup> of December 2015</b> |                |                |                |                |                  |                |                |                |                |                |              |              |              |               |               |               |                  |  |  |  |  |  |  |  |  |  |
| Increase due PPE revaluation (Note 20 a)           | -              | -              | -              | -              | -                | -              | -              | 23,782         | -              | 23,782         | -            | -            | 179          | -             | 179           | -             | 23,961           |  |  |  |  |  |  |  |  |  |
| Decrease due PPE revaluation                       | -              | -              | -              | -              | -                | -              | -              | (30,657)       | -              | (30,657)       | -            | -            | (137)        | -             | (137)         | -             | (30,794)         |  |  |  |  |  |  |  |  |  |
| Additions  | -              | -              | 5              | 48             | 53               | -              | -              | 1,220          | 263            | 1,483          | -            | 24           | -            | 15,628        | 15,652        | 168,076       | 185,264          |  |  |  |  |  |  |  |  |  |
| Invested in share capital (Note 19)*               | -              | -              | -              | 85             | 85               | -              | -              | -              | -              | -              | -            | -            | -            | -             | -             | -             | 85               |  |  |  |  |  |  |  |  |  |
| Transfers  | 6,369          | 234            | 65,170         | 12,359         | 84,132           | 1,400          | 14,208         | 25,096         | 3,193          | 43,897         | 2,449        | 504          | (1,669)      | 5,590         | 6,874         | (134,903)     | -                |  |  |  |  |  |  |  |  |  |
| Reclassified to investment property                | -              | -              | -              | (12)           | (12)             | -              | -              | -              | -              | -              | -            | -            | -            | -             | -             | -             | (12)             |  |  |  |  |  |  |  |  |  |
| Disposals  | -              | (212)          | (1,937)        | (53)           | (2,202)          | (377)          | (110)          | (1,154)        | (4)            | (1,645)        | -            | -            | (4)          | (137)         | (141)         | (25)          | (4,013)          |  |  |  |  |  |  |  |  |  |
| Impairment charge                                  | -              | -              | -              | -              | -                | -              | -              | 14,564         | -              | 14,564         | -            | -            | -            | -             | -             | -             | 14,506           |  |  |  |  |  |  |  |  |  |
| Depreciation                                       | (16,116)       | (10,797)       | (39,857)       | (13,792)       | (80,562)         | (8,062)        | (11,866)       | (24,176)       | (41,520)       | (85,624)       | (627)        | (574)        | (1,315)      | (10,355)      | (12,871)      | -             | (179,057)        |  |  |  |  |  |  |  |  |  |
| <b>Closing net book amount</b>                     | <b>624,338</b> | <b>195,401</b> | <b>861,138</b> | <b>333,351</b> | <b>2,014,228</b> | <b>100,745</b> | <b>191,179</b> | <b>328,750</b> | <b>301,968</b> | <b>922,642</b> | <b>6,768</b> | <b>1,699</b> | <b>2,721</b> | <b>40,446</b> | <b>51,634</b> | <b>87,752</b> | <b>3,076,256</b> |  |  |  |  |  |  |  |  |  |

| <b>At 31<sup>st</sup> of December 2015</b> |                |                |                |                |                  |                |                |                |                |                |              |              |              |               |               |               |                  |  |  |  |  |  |  |  |  |  |  |
|--|----------------|----------------|----------------|----------------|------------------|----------------|----------------|----------------|----------------|----------------|--------------|--------------|--------------|---------------|---------------|---------------|------------------|--|--|--|--|--|--|--|--|--|--|
| Cost or valuation                          | 1,518,751      | 508,457        | 1,984,641      | 457,599        | 4,469,448        | 331,399        | 420,117        | 696,255        | 624,749        | 2,072,520      | 16,106       | 6,358        | 7,357        | 143,297       | 173,118       | 93,858        | 6,808,944        |  |  |  |  |  |  |  |  |  |  |
| Accumulated depreciation and impairment    | (894,413)      | (313,056)      | (1,123,503)    | (124,248)      | (2,455,220)      | (230,854)      | (228,938)      | (367,505)      | (322,781)      | (1,149,878)    | (9,338)      | (4,659)      | (4,636)      | (102,851)     | (121,484)     | (6,106)       | (3,732,688)      |  |  |  |  |  |  |  |  |  |  |
| <b>Net book amount</b>                     | <b>624,338</b> | <b>195,401</b> | <b>861,138</b> | <b>333,351</b> | <b>2,014,228</b> | <b>100,745</b> | <b>191,179</b> | <b>328,750</b> | <b>301,968</b> | <b>922,642</b> | <b>6,768</b> | <b>1,699</b> | <b>2,721</b> | <b>40,446</b> | <b>51,634</b> | <b>87,752</b> | <b>3,076,256</b> |  |  |  |  |  |  |  |  |  |  |

\* in December 2015, in accordance with the Directive No. 583 of the Cabinet of Ministers of the Republic of Latvia, dated 29<sup>th</sup> of September 2015 "On the Investment of the State's property units in the Share Capital of Latvenergo AS", real estate in the amount of EUR 85 thousand was invested in the share capital of Latvenergo AS (in October 2014: real estate in the amount of EUR 435 thousand)

Impairment charge is included in the Consolidated Statement of Profit or Loss under 'Depreciation, amortisation and impairment of intangible assets and property, plant and equipment'.

As of 31<sup>st</sup> of December 2015 cost or valuation of fully depreciated PPE amounted to EUR 801,427 thousand (31/12/2014: EUR 929,068 thousand).

In 2015 the Group has capitalised borrowing and finance costs in the amount of EUR 268 thousand (2014: EUR 167 thousand). Rate of capitalised borrowing costs was of 1.50 % (2014: 1.61 %).

Information about the Group's pledged property, plant and equipment is disclosed in Note 21 b, I.

#### b) Investment property

Land or a building or part of a building held by the Group as the owner to earn rentals or for capital appreciation, rather than for use in the production of goods or supply of services or for administrative purposes, or sale in the ordinary course of business, after decision of the Group's management are initially recognised as investment properties at cost and subsequently measured at acquisition cost net of accumulated depreciation and impairment losses (Note 2.7.).

|   | Land       |            | Buildings  |              | TOTAL Investment property |              |
|---|------------|------------|------------|--------------|---------------------------|--------------|
|   | 2015       | 2014       | 2015       | 2014         | 2015                      | 2014         |
|   | EUR'000    | EUR'000    | EUR'000    | EUR'000      | EUR'000                   | EUR'000      |
| <b>Net book amount at the beginning of the year</b> | <b>430</b> | <b>435</b> | <b>913</b> | <b>1,038</b> | <b>1 343</b>              | <b>1,473</b> |
| Reclassified from property, plant and equipment     | 7          | 80         | 5          | 354          | 12                        | 434          |
| Sold  | (12)       | (85)       | (373)      | (389)        | (385)                     | (474)        |
| Disposal  | -          | -          | (5)        | (7)          | (5)                       | (7)          |
| Impairment charge                                   | -          | -          | (235)      | -            | (235)                     | -            |
| Depreciation  | -          | -          | (34)       | (83)         | (34)                      | (83)         |
| <b>Net book amount at the end of the year</b>       | <b>425</b> | <b>430</b> | <b>271</b> | <b>913</b>   | <b>696</b>                | <b>1,343</b> |

#### c) Property, plant and equipment revaluation

As of 1<sup>st</sup> of January 2011 transmission system assets and as of 1<sup>st</sup> of September 2011 distribution system assets were evaluated for property investment in subsidiaries share capital (Latvijas elektriskie tīkli AS and Sadales tīkls AS respectively). Latvenergo AS revalued assets of Daugava hydropower plants as of 1<sup>st</sup> of January 2012. In 2015 the Group started revaluation process for property, plant and equipment of distribution system. At the reporting year were revalued categories of distribution system technology equipment and machinery, considering the substantial changes of carrying amounts of these categories. Valuation have been done by independent certified valuers by applying the cost model, which provides, that the assets value comprises replacement or renewal costs of similar asset at the date of revaluation less the accumulated depreciation and impairment losses. To determine original cost replacement value of the revaluated asset current acquisition or purchase cost is used. Amounts of revalued property, plant and equipment categories had been determined as of 1<sup>st</sup> of January 2015, but considering the large amount of revalued assets, the revaluation process had been finished in December

2015, while the revaluation process for distribution system buildings and facilities will continue in 2016.

As a result of revaluation in 2015 the carrying amounts of revalued distribution system assets decreased by EUR 6,832 thousand. Increase of property, plant and equipment in the amount of EUR 23,961 thousand, net of deferred income tax, is included in the Group's equity as non-current assets revaluation reserve (see Note 20 a), while decrease of property, plant and equipment in the amount of EUR 30,794 thousand – in the Consolidated Statement of Profit or Loss position 'Depreciation, amortisation and impairment of intangible assets and property, plant and equipment'. Respectively, the impairment charge in the amount of EUR 14,564 thousand for distribution system technology equipment and machinery category 'Transformers for AC voltage lowering' recognised in 2014 had been reversed.

The carrying amounts of revalued property, plant and equipment of Daugava hydropower plants, transmission and distribution system assets at revalued amounts and their cost basis are as follows:

|   | Revalued property, plant and equipment categories |                                    |                                     |                    |
|---|---|------------------------------------|-------------------------------------|--------------------|
|   | Buildings and facilities                          | Technology equipment and machinery | Other property, plant and equipment | Total              |
|   | EUR'000   | EUR'000                            | EUR'000                             | EUR'000            |
| <b>At revalued amounts</b>                        |   |                                    |                                     |                    |
| <b>At 31<sup>st</sup> of December 2014</b>        |   |                                    |                                     |                    |
| Revalued  | 4,013,350   | 1,469,943                          | 31,579                              | <b>5,514,872</b>   |
| Accumulated depreciation                          | (2,335,332)                                       | (853,137)                          | (19,221)                            | <b>(3,207,690)</b> |
| <b>Revalued net book amount</b>                   | <b>1,678,018</b>                                  | <b>616,806</b>                     | <b>12,358</b>                       | <b>2,307,182</b>   |
| <b>At 31<sup>st</sup> of December 2015</b>        |   |                                    |                                     |                    |
| Revalued  | 4,011,849   | 1,447,771                          | 29,821                              | <b>5,489,441</b>   |
| Accumulated depreciation                          | (2,330,972)                                       | (827,097)                          | (18,633)                            | <b>(3,176,702)</b> |
| <b>Revalued net book amount</b>                   | <b>1,680,877</b>                                  | <b>620,674</b>                     | <b>11,188</b>                       | <b>2,312,739</b>   |
| <b>At amounts stated on historical cost basis</b> |   |                                    |                                     |                    |
| <b>At 31<sup>st</sup> of December 2014</b>        |   |                                    |                                     |                    |
| Cost  | 1,019,203   | 688,276                            | 26,825                              | <b>1,734,304</b>   |
| Accumulated depreciation                          | (300,559)   | (336,857)                          | (18,640)                            | <b>(656,056)</b>   |
| <b>Net book amount</b>                            | <b>718,644</b>                                    | <b>351,419</b>                     | <b>8,185</b>                        | <b>1,078,248</b>   |
| <b>At 31<sup>st</sup> of December 2015</b>        |   |                                    |                                     |                    |
| Cost  | 1,088,555   | 725,157                            | 25,286                              | <b>1,838,998</b>   |
| Accumulated depreciation                          | (323,428)   | (350,822)                          | (17,626)                            | <b>(691,876)</b>   |
| <b>Net book amount</b>                            | <b>765,127</b>                                    | <b>374,335</b>                     | <b>7,660</b>                        | <b>1,147,122</b>   |

#### d) Impairment

As of the end of reporting period the Group has been performed impairment evaluation for PPE. There are no additional impairment loss recognised and the accumulated impairment as of 31<sup>st</sup> of December 2015 amounted to EUR 93,770 thousand and consists of impairment charge on technological equipment and machinery of the Riga combined heat and power plant (carried in non-revalued technology equipment and machinery) (31/12/2014: impairment charge in the amount of EUR 93,770 thousand on technological equipment and machinery of the Riga combined heat and power plant and partial impairment charge on PPE category's 'Technology equipment and machinery' subcategory 'Transformers for AC voltage lowering' – EUR 14,564 (carried in revalued distribution system's technology equipment and machinery)). Impairment review performed in accordance with IAS 36 *Impairment of Assets* resulted in an impairment charge on technological equipment and machinery of the Riga combined heat and power plant (carried in non-revalued technology equipment and machinery) based on value in use calculations. The recognised impairment charge is included in the Consolidated Statement of Profit or Loss position 'Depreciation, amortisation and impairment of intangible assets and property, plant and equipment'.

The cash-generating unit is defined as the assets of Riga combined heat and power plant. In 2015 has been prepared impairment review for Riga combined heat and power plants (Riga CHHPs) and as a result of this review there is no additional impairment loss has been recognised (2014: no additional impairment has been recognised). Nominal pre-tax discount rate used to determine value in use of cash-generating unit by discounting cash flows is 7.5 % (2014: 7.2 %). Forecasts for cash-generating unit were performed for 5 years period.

For sensitivity analysis see Note 4 a, II.

#### e) Operating leases

|   | 2015          | 2014          |
|---|---------------|---------------|
|   | EUR'000       | EUR'000       |
| <b>Rental income (the Group is the lessor)</b>  | <b>45,208</b> | <b>38,933</b> |
| of which:                                       |               |               |
| Transmission system assets lease                | 43,630        | 37,490        |
| <b>Rental expense (the Group is the lessee)</b> | <b>1,310</b>  | <b>1,228</b>  |

**Future minimum lease receivables under non-cancellable operating lease contracts by due dates:**

|                            | 2015           | 2014           |
|----------------------------|----------------|----------------|
|                            | EUR'000        | EUR'000        |
| - < 1 year                 | 46,471         | 37,490         |
| - 1-5 years                | 185,885        | 178,999        |
| - > 5 years                | 232,356        | 287,867        |
| <b>TOTAL rental income</b> | <b>464,712</b> | <b>504 356</b> |

**Future minimum lease payments under non-cancellable operating lease contracts by due dates:**

|                            | 2015          | 2014          |
|----------------------------|---------------|---------------|
|                            | EUR'000       | EUR'000       |
| - < 1 year                 | 1,417         | 1,349         |
| - 1-5 years                | 5,913         | 5,458         |
| - > 5 years                | 8,129         | 7,375         |
| <b>TOTAL rental income</b> | <b>15,459</b> | <b>14,182</b> |

Transmission system assets had been leased out to Augstsprieguma tīkls AS under non-cancellable operating lease agreement.

## 15. NON-CURRENT FINANCIAL INVESTMENTS

|   | 2015      | 2014      |
|---|-----------|-----------|
|   | EUR'000   | EUR'000   |
| <b>At the beginning of the year</b>                                       | <b>41</b> | <b>41</b> |
| Share of profit / (loss) in Nordic Energy Link AS using the equity method | -         | (357)     |
| Received dividends from Nordic Energy Link AS                             | -         | 1,924     |
| Net loss from disposal of investment in Nordic Energy Link AS*            | -         | (1,567)   |
| <b>At the end of the year</b>   | <b>41</b> | <b>41</b> |

\* on 12<sup>th</sup> of February 2014 the Cabinet of Ministers of the Republic of Latvia adopted decision No. 67 "On Latvenergo AS termination of partnership in Nordic Energy Link AS" and on 19<sup>th</sup> of March 2014 at the Nordic Energy Link AS Shareholders' meeting was approved decision to liquidate Nordic Energy Link AS. In December 2014 Latvenergo AS terminated its partnership as a shareholder of Nordic Energy Link AS with 25 % interest held

The table below discloses the Group's share of profit from investments in significant associates and summarised financial information on the amounts of assets, liabilities and net sales of these entities.

|   | Assets        | Liabilities | Net sales | Share of profit / (loss) |
|---|---------------|-------------|-----------|--------------------------|
|   | EUR'000       | EUR'000     | EUR'000   | EUR'000                  |
| <b>As of 31<sup>st</sup> of December 2015</b>   |               |             |           |                          |
| Nordic Energy Link AS                           | -             | -           | -         | -                        |
|   | -             | -           | -         | -                        |
| <b>As of 30<sup>th</sup> of September 2014*</b> |               |             |           |                          |
| Nordic Energy Link AS                           | 21,163        | 6           | 7         | -                        |
|   | <b>21,163</b> | <b>6</b>    | <b>7</b>  | <b>-</b>                 |

\* final financial data before liquidation



**Participating interest in subsidiaries and other non-current financial investments:**

| Name  | Country of incorporation | Business activity held   | Interest held, % |            |
|---|--------------------------|--|------------------|------------|
|   |                          |  | 31/12/2015       | 31/12/2014 |
| <b>Subsidiaries:</b>                            |                          |  |                  |            |
| Latvijas elektriskie tīkli AS                   | Latvia                   | Management of transmission system assets                                     | 100 %            | 100 %      |
| Sadales tīkls AS                                | Latvia                   | Electricity distribution   | 100 %            | 100 %      |
| Enerģijas publiskais tirgotājs AS*              | Latvia                   | Management of the mandatory procurement process                              | 100 %            | 100 %      |
| Elektrum Eesti OÜ                               | Estonia                  | Electricity supply   | 100 %            | 100 %      |
| Elektrum Latvija SIA                            | Latvia                   | Electricity supply   | 100 %            | 100 %      |
| Elektrum Lietuva UAB                            | Lithuania                | Electricity supply   | 100 %            | 100 %      |
| Liepājas enerģija SIA                           | Latvia                   | Thermal energy generation and supply in Liepāja city, electricity generation | 51 %             | 51 %       |
| <b>Other non-current financial investments:</b> |                          |  |                  |            |
| Pirmais Slēgtais Pensiju Fonds AS               | Latvia                   | Management of pension plans  | 48.15 %          | 48.15 %    |
| Rīgas siltums AS                                | Latvia                   | Thermal energy generation and supply in Riga, electricity generation         | 0.0051 %         | 0.0051 %   |

\* in order to improve the transparency of administration of electricity mandatory procurement process, new subsidiary Enerģijas publiskais tirgotājs AS was established on 25<sup>th</sup> of February 2014. The subsidiary as of 1<sup>st</sup> of April 2014 has taken over the mandatory procurement administration functions from Latvenergo AS

The Group owns 48.15 % of the shares of the closed pension fund Pirmais Slēgtais Pensiju Fonds AS. However, the Group is only a nominal shareholder as all risks and benefits arising from associate's activities

will accrue to the Group's employees who are members of the pension fund. Therefore, investment in Pirmais Slēgtais Pensiju Fonds AS is valued at cost and equity method is not applied.

## 16. INVENTORIES

|   | 31/12/2015    | 31/12/2014    |
|---|---------------|---------------|
|   | EUR'000       | EUR'000       |
| Raw materials and materials                       | 17,983        | 15,510        |
| Other inventories                                 | 8,422         | 8,437         |
| Allowance for raw materials and other inventories | (1,614)       | (1,387)       |
| <b>TOTAL inventories</b>                          | <b>24,791</b> | <b>22,560</b> |

Changes in the allowance for raw materials and materials at warehouses are included in the Consolidated Statement of Profit or Loss position 'Raw materials and consumables used'.

**Movement on the allowance for raw materials, spare parts and technological fuel:**

|   | 2015         | 2014         |
|---|--------------|--------------|
|   | EUR'000      | EUR'000      |
| <b>At the beginning of the year</b>                     | <b>1,387</b> | <b>4,259</b> |
| Inventories written off                                 | (106)        | (32)         |
| Reclassified to property, plant and equipment           | -            | (3 394)      |
| Charged to the Consolidated Statement of Profit or Loss | 333          | 554          |
| <b>At the end of the year</b>                           | <b>1,614</b> | <b>1,387</b> |

## 17. TRADE RECEIVABLES AND OTHER CURRENT RECEIVABLES

### a) Trade receivables, net

|   | 2015            | 2014            |
|---|-----------------|-----------------|
|   | EUR'000         | EUR'000         |
| <b>Receivables</b>                                      |                 |                 |
| – Electricity supply and electricity services customers | 121,112         | 117,942*        |
| – Heating customers                                     | 11,735          | 17,477          |
| – Other trade receivables                               | 25,405          | 30,877          |
|   | <b>158,252</b>  | <b>166,296</b>  |
| <b>Allowances for impairment of receivables</b>         |                 |                 |
| – Electricity supply and electricity services customers | (43,319)        | (41,080)        |
| – Heating customers                                     | (423)           | (393)           |
| – Other trade receivables                               | (2,347)         | (2,530)         |
|   | <b>(46,089)</b> | <b>(44,003)</b> |
| <b>Receivables, net</b>                                 |                 |                 |
| – Electricity supply and electricity services customers | 77,793          | 76,862          |
| – Heating customers                                     | 11,312          | 17,084          |
| – Other trade receivables                               | 23,058          | 28,347          |
|   | <b>112,163</b>  | <b>122,293</b>  |

\* reclassified accrued income on electricity supply and electricity services from other accrued income (Note 17 b) in the amount of EUR 14,186 thousand

There is no significant concentration of credit risk with respect to trade receivables, as the Group has a large number of customers except the major heating customer the net debt of which as of 31<sup>st</sup> of December 2015 amounted to EUR 9,683 thousand (31/12/2014: EUR 14,658 thousand).

**Electricity supply and electricity services receivables grouped by past due days and calculated impairment loss:**

|   | 31/12/2015      | 31/12/2014      |
|---|-----------------|-----------------|
|   | EUR'000         | EUR'000         |
| <b>Electricity supply and electricity services receivables:</b>                         |                 |                 |
| Fully performing receivables  | 67,351          | 67,858          |
| Receivables past due but not impaired:  |                 |                 |
| – Receivables past due by 1–45 days   | 7,833           | 5,351           |
| Impaired receivables:   |                 |                 |
| – Receivables past due by 46–90 days  | 2,012           | 683             |
| – Receivables past due by 91–180 days   | 2,842           | 621             |
| – Receivables past due by more than 181 day   | 12,281          | 11,275          |
| – Individually impaired receivables with scheduled payments*                            | 28,793          | 32,154          |
|   | <b>121,112</b>  | <b>117,942</b>  |
| <b>Allowances for impaired electricity supply and electricity services receivables:</b> |                 |                 |
| – Receivables past due by 46–90 days  | (1,011)         | (341)           |
| – Receivables past due by 91–180 days   | (2,133)         | (466)           |
| – Receivables past due by more than 181 day   | (12,281)        | (11,275)        |
| – Individually impaired receivables with scheduled payments*                            | (27,894)        | (28,998)        |
|   | <b>(43,319)</b> | <b>(41,080)</b> |
| <b>Electricity supply and electricity services receivables, net:</b>                    |                 |                 |
| Fully performing receivables  | 67,351          | 67,858          |
| Receivables past due but not impaired:  |                 |                 |
| – Receivables past due by 1–45 days   | 7,833           | 5,351           |
| Net impaired receivables:   |                 |                 |
| – Receivables past due by 46–90 days  | 1,001           | 342             |
| – Receivables past due by 91–180 days   | 709             | 155             |
| – Individually impaired receivables with scheduled payments*                            | 899             | 3,156           |
|   | <b>77,793</b>   | <b>76,862</b>   |

\* receivables under insolvency process and other individually impaired receivables

#### Heating and other receivables grouped by past due days and calculated impairment loss:

|   | 31/12/2015     | 31/12/2014     |
|---|----------------|----------------|
|   | EUR'000        | EUR'000        |
| <b>Heating and other trade receivables:</b>                         |                |                |
| Fully performing receivables  | 33,557         | 44,605         |
| Receivables past due but not impaired:                              |                |                |
| – Receivables past due by 1–30 days                                 | 570            | 713            |
| Impaired receivables:   |                |                |
| – Receivables past due by 31–90 days                                | 255            | 211            |
| – Receivables past due by more than 91 day                          | 2,473          | 2,645          |
| – Individually impaired receivables with scheduled payments*        | 285            | 180            |
|   | <b>37,140</b>  | <b>48,354</b>  |
| <b>Allowances for impaired heating and other trade receivables:</b> |                |                |
| – Receivables past due by 31–90 days                                | (128)          | (105)          |
| – Receivables past due by more than 91 day                          | (2,473)        | (2,645)        |
| – Individually impaired receivables with scheduled payments*        | (169)          | (173)          |
|   | <b>(2,770)</b> | <b>(2,923)</b> |
| <b>Heating and other trade receivables, net</b>                     |                |                |
| Fully performing receivables  | 33,557         | 44,605         |
| Receivables past due but not impaired:                              |                |                |
| – Receivables past due by 1–30 days                                 | 570            | 713            |
| Net impaired receivables:   |                |                |
| – Receivables past due by 31–90 days                                | 127            | 106            |
| – Individually impaired receivables with scheduled payments*        | 116            | 7              |
|   | <b>34,370</b>  | <b>45,431</b>  |

\* receivables under insolvency process and other individually impaired receivables

The Group's Management has estimated allowances for impairment of receivables on the basis of aging of trade receivables and by evaluating liquidity and history of previous payments of each significant debtor (see point 2.12). The carrying amount of trade receivables, less allowances for impairment, is assumed to approximate their fair values.

The Group's Management assumptions and methodology for estimation of recoverable amount of trade receivables and evaluation of impairment risk are described in Note 4 b.

#### Receivables credit quality:

|  | 31/12/2015    | 31/12/2014    |
|--|---------------|---------------|
|  | EUR'000       | EUR'000       |
| <b>Fully performing electricity supply and electricity services receivables:</b> |               |               |
| – customers with no overdue receivables  | 53,428        | 60,060        |
| – customers with overdue receivables   | 13,923        | 7,798         |
|  | <b>67,351</b> | <b>67,858</b> |
| <b>Fully performing heating and other receivables:</b>                           |               |               |
| – customers with no overdue receivables  | 32,584        | 43,527        |
| – customers with overdue receivables   | 973           | 1,078         |
|  | <b>33,557</b> | <b>44,605</b> |

The basis for estimating the credit quality of fully performing trade receivables not due yet and not

written down are internal ratings by reference to earlier credit behaviour of clients.

**Movements in allowances for impairment of trade receivables are as follows:**

|  | 2015          | 2014          |
|--|---------------|---------------|
|  | EUR'000       | EUR'000       |
| <b>At the beginning of the year</b>                      | <b>44,003</b> | <b>43,494</b> |
| Receivables written off during the year as uncollectible | (2,143)       | (934)         |
| Allowance for impaired receivables                       | 4,229         | 1,443         |
| <b>At the end of the year</b>                            | <b>46,089</b> | <b>44,003</b> |

The charge and release of allowance for impaired trade receivables due to delayed payments have been recorded in the Consolidated Statement of Profit or Loss

position 'Other operating expenses' as selling expenses and customer services costs (Note 10).

**b) Other current receivables**

|   | 31/12/2015     | 31/12/2014     |
|---|----------------|----------------|
|   | EUR'000        | EUR'000        |
| Compensated accrued revenue on mandatory procurement PSO                | –              | 15,887         |
| Unsettled revenue on mandatory procurement PSO fee recognised as assets | 141,060        | 63,146         |
| Other accrued income  | 1,148          | 1,176*         |
| Pre-tax and overpaid taxes  | 4,387          | 9,268          |
| Other current financial receivables                                     | 1,974          | 19,001         |
| Other current non-financial receivables                                 | 2,720          | 2,274          |
| <b>Total other current receivables</b>                                  | <b>151,289</b> | <b>110,752</b> |

\* reclassified accrued income on electricity supply and electricity services to electricity supply and electricity services trade receivables (Note 17 a) in the amount of EUR 14,186 thousand

Accrued revenue on mandatory procurement public service obligation fee is calculated as difference between procurement expenditure above electricity market price and collected payments from electricity end users for mandatory procurement public service obligation fees for period from 1<sup>st</sup> of January 2013 through 31<sup>st</sup> of March 2014. Since 1<sup>st</sup> of April 2014 according to the conditions included in the article No. 37 of transition terms of the Electricity Market Law of the Republic of Latvia, Public Supplier licence holder (established in 2014) was obliged to compensate the uncollected difference of mandatory procurement service obligation for period from 1<sup>st</sup> of January 2013 until transfer of Public Supplier licence.

By applying agent principle unsettled revenue on mandatory procurement PSO fee is recognised as assets in net amount as difference between revenue from sale of electricity in Nord Pool power exchange

by market price, received mandatory procurement PSO fees, received government grant for compensating the increase of mandatory procurement costs and costs of purchased electricity under the mandatory procurement from electricity generators who generate electricity in efficient cogeneration process or using renewable energy sources, as well as guaranteed fees for installed electrical capacity in cogeneration plants (over 4 MW).

The growth of other current financial receivables is affected by accounting of accepted, but unsettled financing from European Union funds for The European Energy Development Program – 330 kV Kurzeme Ring.

None of the receivables are secured with pledges or otherwise. The carrying amounts of other receivables are assumed to approximate their fair values.

## 18. CASH AND CASH EQUIVALENTS

|  | 31/12/2015     | 31/12/2014     |
|--|----------------|----------------|
|  | EUR'000        | EUR'000        |
| Cash at bank                           | 89,391         | 38,141         |
| Short-term bank deposits               | 10,000         | 52,000         |
| Restricted cash and cash equivalents*  | 5,152          | 30,870         |
| <b>TOTAL cash and cash equivalents</b> | <b>104,543</b> | <b>121,011</b> |

\* restricted cash and cash equivalents as of 31<sup>st</sup> of December 2015 consist of the financial security for participating in NASDAQ OMX Commodities Exchange in the amount of EUR 5,152 thousand (31/12/2014 – EUR 1,606 thousand) and as of 31<sup>st</sup> of December 2014 – government grant for compensation of the increase of mandatory procurement public service obligation costs in the amount of EUR 29,264 thousand that was restricted until acceptance from European Union and was not included in the Consolidated Statement of Cash Flows

Cash at bank balances earns daily interest mostly based on floating interbank deposit rates. Short-term deposits are placed for different periods between several days and three months depending on the immediate cash needs of the Group and cash flow forecasts. During 2015 the average annual effective interest rate earned

on short-term cash deposits was 0.16 % (2014: 0.32 %). See also Note 3.1.b.

The carrying amounts of cash and cash equivalents are assumed to be approximate to their fair values.

## 19. SHARE CAPITAL

As of 31<sup>st</sup> of December 2015, the registered share capital of the Latvenergo AS is EUR 1,288,531 thousand (31/12/2014: EUR 1,288,446 thousand) and consists of 1,288,531 thousand ordinary shares (31/12/2014: 1,288,446 thousand) with the nominal value of EUR 1 per share (31/12/2014: EUR 1 per share). On 25<sup>th</sup> of February 2014 due to introduction of euro in Latvia new articles of association for Latvenergo AS had been approved and as a result of denomination of shares registered share capital amounted to EUR 1,288,011 thousand, consisting of 1,288,011 thousand ordinary shares with nominal value of EUR 1. All shares have been fully paid.

In December 2015, in accordance with the Directive No. 583 of the Cabinet of Ministers of the Republic of Latvia, dated 29<sup>th</sup> of September 2015 – “On the Investment of the State’s property units in the Share Capital of Latvenergo AS”, real estate in the amount of EUR 85 thousand was invested in the share capital of Latvenergo AS (2014: real estate in the amount of EUR 435 thousand). The value of real estate was determined by independent certified valuation experts applying amortised cost model, based on construction or acquisition costs of similar assets. Increase in the share capital was approved by the Latvenergo AS Shareholders’ Meeting on 5<sup>th</sup> of October 2015 and registered with the Commercial Register of the Republic of Latvia on 10<sup>th</sup> of December 2015.

## 20. RESERVES, DIVIDENDS AND EARNINGS PER SHARE

### a) Reserves

As of 31<sup>st</sup> of December 2015, the Group’s reserves are in the amount EUR 669,596 thousand (31/12/2014: EUR 645,829 thousand) and consist of the property, plant and equipment revaluation reserve, hedge reserve, currency translation reserve and other reserves. The

Group cannot distribute as dividends the property, plant and equipment revaluation reserve, currency translation and hedge reserves. Other reserves are maintained with the aim to maintain stability in the operations of the Group entities.

|   | Notes   | Non-current assets revaluation reserve | Hedge reserve   | Currency translation | Other reserves | TOTAL          |
|---|---------|--|-----------------|----------------------|----------------|----------------|
|   |         | EUR'000                                | EUR'000         | EUR'000              | EUR'000        | EUR'000        |
| <b>As of 31<sup>st</sup> of December 2013</b>                                 |         | <b>662,132</b>                         | <b>(9,838)</b>  | <b>111</b>           | <b>13</b>      | <b>652,418</b> |
| Disposal of non-current assets revaluation reserve                            |         | (94)                                   | –               | –                    | –              | (94)           |
| Deferred tax related to non-current assets revaluation reserve                | 12      | 14                                     | –               | –                    | –              | 14             |
| Currency translation differences  |         | –                                      | –               | (14)                 | –              | (14)           |
| Losses from fair value changes in derivative financial instruments            | 21 c, l | –                                      | (6,495)         | –                    | –              | (6,495)        |
| <b>As of 31<sup>st</sup> of December 2014</b>                                 |         | <b>662,052</b>                         | <b>(16,333)</b> | <b>97</b>            | <b>13</b>      | <b>645,829</b> |
| Increase of non-current assets revaluation reserve as a result of revaluation | 14 a    | 23,961                                 | –               | –                    | –              | 23,961         |
| Disposal of non-current assets revaluation reserve                            |         | (795)                                  | –               | –                    | –              | (795)          |
| Deferred tax related to non-current assets revaluation reserve                | 12      | (3,476)                                | –               | –                    | –              | (3,476)        |
| Gains from fair value changes in derivative financial instruments             | 21 c, l | –                                      | 4,077           | –                    | –              | 4,077          |
| <b>As of 31<sup>st</sup> of December 2015</b>                                 |         | <b>681,742</b>                         | <b>(12,256)</b> | <b>97</b>            | <b>13</b>      | <b>669,596</b> |

#### b) Dividends

The dividends declared to equity holders of the Parent Company for 2014 were EUR 31,479 thousand or EUR 0.02443 per share (2013: EUR 23,605 thousand or EUR 0.02608 per share) and to non-controlling interests – EUR 1,148 thousand or EUR 0.336 per share (2013: EUR 1,197 thousand or EUR 0.35 per share). Dividends declared for 2013 and paid in 2014 were settled partly by corporate income tax overpayment in the amount of EUR 10,956 thousand (see Consolidated Statement of Cash Flows).

The Management Board of Latvenergo AS proposes to allocate profit of Latvenergo AS for the year ended 31<sup>st</sup> of December 2015 in the amount of EUR 77,413 thousand

to be paid out in dividends. These financial statements do not reflect this amount as a liability as the dividends have not been approved as of 31<sup>st</sup> of December 2015.

The distribution of net profit for the 2015 is subject to a resolution of the Parent Company's Shareholders Meeting.

#### c) Earnings per share

Basic earnings per share are calculated by dividing profit attributable to the equity holders of the Parent Company by the weighted average number of ordinary shares outstanding (Note 19). As there are no potential ordinary shares, diluted earnings per share are equal to basic earnings per share in all comparable periods.

|   | 2015      | 2014      |
|---|-----------|-----------|
| Profit attributable to the equity holders of the Parent Company (in thousand EUR) | 83,509    | 28,515    |
| Weighted average number of shares (thousand)                                      | 1,288,489 | 1,230,405 |
| Basic earnings per share (in euros)   | 0.065     | 0.023     |
| Diluted earnings per share (in euros)   | 0.065     | 0.023     |

## 21. FINANCIAL ASSETS AND LIABILITIES

#### a) Held-to-maturity financial assets

As of 31<sup>st</sup> of December 2015 the entire Group's held-to-maturity financial assets were State Treasury bonds with 5 year and 10 year maturity, which were purchased with the purpose to invest liquidity reserve in the low risk financial instruments with higher yield. During 2015

and 2014 there were no gains or losses recognised in association with the disposal of held-to-maturity financial assets. All held-to-maturity financial assets are denominated in euros. The maximum exposure to credit risk at the reporting date is the carrying amount of held-to-maturity financial assets.

In 2015 the fair value of held-to-maturity financial assets is greater than the carrying amount by EUR 5,959 thousand (2014: EUR 6,403 thousand). The fair value of financial assets is calculated by discounting their future

cash flows and using as discount factor the banks quoted prices of the financial instruments at the end of the reporting period.

#### Held-to-maturity financial assets carrying amount:

|  | 31/12/2015    | 31/12/2014    |
|--|---------------|---------------|
|  | EUR'000       | EUR'000       |
| Held-to-maturity financial assets:             |               |               |
| – current                                      | 7,859         | –             |
| – non-current                                  | 20,609        | 28,528        |
| <b>TOTAL held-to-maturity financial assets</b> | <b>28,468</b> | <b>28,528</b> |

#### b) Borrowings

|   | 31/12/2015     | 31/12/2014     |
|---|----------------|----------------|
|   | EUR'000        | EUR'000        |
| Non-current borrowings from financial institutions                    | 534,586        | 583,494        |
| Issued debt securities (bonds)  | 179,705        | 104,803        |
| <b>TOTAL non-current borrowings</b>                                   | <b>714,291</b> | <b>688,297</b> |
| Current portion of non-current borrowings from financial institutions | 80,842         | 136,809        |
| Accrued interest on non-current borrowings                            | 848            | 1,422          |
| Accrued coupon interest on issued debt securities (bonds)             | 1,502          | 694            |
| <b>TOTAL current borrowings</b>                                       | <b>83,192</b>  | <b>138,925</b> |
| <b>TOTAL borrowings</b>   | <b>797,483</b> | <b>827,222</b> |

#### Movement in borrowings:

|  | 2015           | 2014           |
|--|----------------|----------------|
|  | EUR'000        | EUR'000        |
| <b>At the beginning of the year</b>      | <b>827,222</b> | <b>944 675</b> |
| Borrowings received                      | 30,000         | 22,600         |
| Borrowings repaid                        | (134,875)      | (139,695)      |
| Change in accrued interest on borrowings | 234            | (358)          |
| Issued debt securities (bonds)           | 74,902         | –              |
| <b>At the end of the year</b>            | <b>797,483</b> | <b>827,222</b> |

#### Borrowings by categories of lenders:

|                                | 31/12/2015     | 31/12/2014     |
|--------------------------------|----------------|----------------|
|                                | EUR'000        | EUR'000        |
| Foreign investment banks       | 432,979        | 482,869        |
| Commercial banks               | 183,298        | 238,856        |
| Issued debt securities (bonds) | 181,207        | 105,497        |
| <b>TOTAL borrowings</b>        | <b>797,483</b> | <b>827,222</b> |



**Borrowings by maturity (excluding the effect of derivative financial instruments):**

|  | 31/12/2015     | 31/12/2014     |
|--|----------------|----------------|
|  | EUR'000        | EUR'000        |
| <b>Fixed rate non-current and current borrowings:</b>    |                |                |
| - < 1 year (current portion of non-current borrowings)   | 1,703          | 1,099          |
| - 1-5 years  | 172,985        | 70,433         |
| - > 5 years  | 74,902         | 34,570         |
| <b>TOTAL fixed rate borrowings</b>                       | <b>249,590</b> | <b>106,102</b> |
| <b>Floating rate non-current and current borrowings:</b> |                |                |
| - < 1 year (current portion of non-current borrowings)   | 81,489         | 137,826        |
| - 1-5 years  | 300,669        | 383,220        |
| - > 5 years  | 165,735        | 200,074        |
| <b>TOTAL floating rate borrowings</b>                    | <b>547,893</b> | <b>721,120</b> |
| <b>TOTAL borrowings</b>                                  | <b>797,483</b> | <b>827,222</b> |

**Borrowings by pricing period (considering the effect of derivative financial instruments):**

|                          | 31/12/2015     | 31/12/2014     |
|--------------------------|----------------|----------------|
|                          | EUR'000        | EUR'000        |
| - < 1 year               | 360,578        | 482,528        |
| - 1-5 years              | 282,003        | 230,124        |
| - > 5 years              | 154,902        | 114,570        |
| <b>TOTAL borrowings:</b> | <b>797,483</b> | <b>827,222</b> |

At 31<sup>st</sup> of December 2015 and at 31<sup>st</sup> of December 2014 all of the Group's borrowings were denominated in euros.

The fair value of current and non-current borrowings with floating rates equals their carrying amount, as their actual floating interest rates approximate the market price of similar financial instruments available to the Group, and the effect of fair value revaluation is not significant. The fair value of current and non-current borrowings with fixed rates (excluding the effect of derivative financial instruments) exceeds their carrying amounts by EUR 5.7 thousand (2014: EUR 32.6 thousand). The fair value calculations are based on discounted cash flows using discount factor of respective EUR swap rates increased by the Group's credit risk margin. The average interest rate for discounting cash flows of non-current borrowings was 0.9 % (2014: 1.1 %).

**I) Pledges**

As of 31<sup>st</sup> of December 2015 the Group's assets are not pledged to secure the borrowings, except the pledge on assets of Liepājas Enerģija SIA of maximum secured claims in the amount of EUR 31.0 million (31/12/2014: EUR 33.5 million) to secure its current and non-current borrowings. As of the end of the reporting year there has been pledged the property, plant and equipment in the net book amount of EUR 28.5 million and the claims

on the receivables accounts in the amount of EUR 2.5 million (31/12/2014: EUR 30.2 million and EUR 3.3 million, respectively).

**II) Un-drawn borrowing facilities**

As of 31<sup>st</sup> of December 2015 the un-drawn portion of committed non-current credit facilities amounts to EUR 290 million (31/12/2014: EUR 320 million).

As of 31<sup>st</sup> of December 2015 the Group had entered into three overdraft agreements with total notional amount of EUR 34.2 million (31/12/2014: EUR 34.2 million) and in respect of those all conditions precedent had been met. At the end of the reporting year overdrafts were not used.

**III) Weighted average effective interest rate**

During the reporting year the weighted average effective interest rate (including interest rate swaps) on non-current borrowings was 2.40 % (2014: 2.47 %), weighted average effective interest rate for current borrowings was 0.87 % (2014: 1.06 %). At 31<sup>st</sup> of December 2015 interest rates for non-current borrowings in euros were 3, 6 and 12 month EURIBOR+0.78 % (31/12/2014: +1.09 %). At 31<sup>st</sup> of December 2015 the total notional amount of interest rate swap agreements concluded by the Group amounts to EUR 221.5 million (31/12/2014: EUR 320.0 million) and the interest rate was fixed for the initial periods from 6 to 10 years.

#### IV) Bonds issued

The Parent company (Latvenergo AS) in 2012 and 2013 issued bonds in the amount of EUR 70 million with the maturity date – 15<sup>th</sup> of December 2017 (ISIN code – LV0000801090) in the amount of EUR 35 million with maturity date – 22<sup>nd</sup> of May 2020 (ISIN code – LV0000801165), both of them with the annual coupon rate of 2.8 %. In 2015, Latvenergo AS issued bonds in the amount of EUR 75 million with the maturity date 10<sup>th</sup> of June 2022 (ISIN code – LV0000801777) with the annual coupon rate of 1.9 %. Thus the total nominal amount of issued bonds amounts to EUR 180 million. All issued bonds are quoted in NASDAQ Baltic Stock Exchange. At the end of reporting year the issued debt securities (bonds) are measured at amortised cost.

In 2015 the fair value of issued debt securities (bonds) exceeds their carrying amount by EUR 5,040 thousand (2014: EUR 4,899 thousand). The fair value of debt securities (bonds) issued is calculated by discounting their future cash flows and using the banks' quoted prices of the financial instruments at the end of the reporting year as discount factor.

#### c) Derivative financial instruments

##### I) Outstanding fair values of derivatives and their classification

In the table below outstanding fair values of derivatives are disclosed as follows:

| Notes  | 31/12/2015 |               | 31/12/2014 |               |
|--|------------|---------------|------------|---------------|
|  | EUR'000    |               | EUR'000    |               |
|  | Assets     | Liabilities   | Assets     | Liabilities   |
| Interest rate swaps 21 c, II                         | -          | 13,016        | -          | 18,441        |
| Electricity forwards and futures 21 c, III           | -          | 2,558         | -          | 2,112         |
| <b>TOTAL outstanding fair values of derivatives:</b> | <b>-</b>   | <b>15,574</b> | <b>-</b>   | <b>20,553</b> |

|  | 31/12/2015 |               | 31/12/2014 |               |
|--|------------|---------------|------------|---------------|
|  | EUR'000    |               | EUR'000    |               |
|  | Assets     | Liabilities   | Assets     | Liabilities   |
| Non-current  | -          | 8,291         | -          | 11,698        |
| Current  | -          | 7,283         | -          | 8,855         |
| <b>TOTAL fair values of derivative financial instruments</b> | <b>-</b>   | <b>15,574</b> | <b>-</b>   | <b>20,553</b> |

#### (Gains) / losses on fair value changes as a result of realised hedge agreements:

|   | Notes | 2015           | 2014           |
|---|-------|----------------|----------------|
|   |       | EUR'000        | EUR'000        |
| <b>Included in the Consolidated Statement of Profit or Loss</b> |       |                |                |
| Interest rate swaps   | 11    | (1,348)        | (943)          |
| Electricity forwards and futures                                | 8     | 446            | (7,800)        |
| Forward foreign currencies exchange contracts                   | 11    | -              | (16)           |
|   |       | <b>(902)</b>   | <b>(8,759)</b> |
| <b>Included in the Statement of Other Comprehensive Income</b>  |       |                |                |
| Interest rate swaps   | 20    | (4,077)        | 6,495          |
| Electricity forwards and futures                                | 20    | -              | -              |
| Forward foreign currencies exchange contracts                   | 20    | -              | -              |
|   |       | <b>(4,077)</b> | <b>6,495</b>   |

According to amendments to IAS 1 a financial liability or asset that is not held for trading purposes should be presented as current or non-current on the basis of its settlement date. Derivatives that have a maturity of more than twelve months and are expected to be held for more than twelve months after the end of the reporting period have been classified as non-current assets or liabilities.

#### II) Interest rate swaps

As of 31<sup>st</sup> of December 2015 the Group had interest rate swap agreements with total notional amount of EUR 221.5 million (31/12/2014: EUR 320.0 million). Interest rate swaps are concluded with 6 to 10 year initial maturities and hedged floating rates are 6 month EURIBOR. As of 31<sup>st</sup> of December 2015 fixed interest rates vary from 0.7725 % to 4.4925 % (31/12/2014: from 0.7725 % to 4.4925 %).

At the end of the year 91 % of all outstanding interest rate swap agreements or agreements with notional amount of EUR 201.5 million are designated to comply with hedge accounting and were re-measured prospectively and retrospectively to test whether they are effective within the hedging period (31/12/2014: 88 % with

notional amount of EUR 280.0 million). All contracts are designed as cash flow hedges. It was established that they are fully effective and therefore there is no ineffective portion to be recognised within profit or loss in the Consolidated Statement of Profit or Loss.

#### Fair value changes of interest rate swaps:

|   | 2015    |             | 2014    |             |
|---|---------|-------------|---------|-------------|
|   | EUR'000 |             | EUR'000 |             |
|   | Assets  | Liabilities | Assets  | Liabilities |
| <b>Outstanding fair value at the beginning of the year</b>                | -       | 18,441      | (617)   | 13,506      |
| Included in the Consolidated Statement of Profit or Loss, net (Note 11 a) | -       | (1,348)     | -       | (943)       |
| Included in other comprehensive income (Note 20 a)                        | -       | (4,077)     | 617     | 5,878       |
| <b>Outstanding fair value at the end of the year</b>                      | -       | 13,016      | -       | 18,441      |

The main interest rate hedging criteria stated in the Financial Risk Management policy is to ensure average fixed rate duration from 2 to 4 years and fixed rate portion at more than 35 % of borrowings. As of 31<sup>st</sup> of December 2015 55 % (31/12/2014: 42 %) of the Group's borrowings had fixed interest rates (taking into account the effect from the interest rate swaps), and average remaining time to interest re-pricing was 2.4 years (2014: 2.2 years).

Since the Parent company (Latvenergo AS) has become a member of NASDAQ Commodities Exchange in 2014, it has started to conclude future contracts in NASDAQ Commodities Exchange, as well as has continued concluding forward contracts with other counterparties. Electricity forward and future contracts are agreed for electricity price hedging purposes in order to fix electricity purchase price in the Nord Pool power exchange. All purchased forward and future contracts were contracts with fixed amount of electricity and price in euros.

#### III) Electricity forwards and futures

As of 31<sup>st</sup> of December 2015 the Group has entered into electricity forward and future contracts with total outstanding volume of 2,880,436 MWh (31/12/2014: 1,144,162 MWh) and notional value of EUR 64.1 million (31/12/2014: EUR 38.0 million). Electricity forward and future contracts are concluded for the maturities from one quarter to one year during the period from 1<sup>st</sup> of January 2015 to 31<sup>st</sup> of December 2018.

As of 31<sup>st</sup> of December 2015 none of the electricity forward and future contracts is designated to comply with hedge accounting treatment (31/12/2014: no contracts) and consequently as of 31<sup>st</sup> of December 2015 all outstanding fair value changes of valid electricity forward and future contracts are included in the Consolidated Statement of Profit or Loss (see Note 8).

#### Fair value changes of electricity forward and future contracts:

|   | 2015    |             | 2014    |             |
|---|---------|-------------|---------|-------------|
|   | EUR'000 |             | EUR'000 |             |
|   | Assets  | Liabilities | Assets  | Liabilities |
| <b>Outstanding fair value at the beginning of the year</b>        | -       | 2,112       | -       | 9,912       |
| Included in the Consolidated Statement of Profit or Loss (Note 8) | -       | 446         | -       | (7,800)     |
| <b>Outstanding fair value at the end of the year</b>              | -       | 2,558       | -       | 2,112       |

#### IV) Forward foreign currencies exchange contracts

As of 31<sup>st</sup> of December 2015 the Group has no outstanding forward foreign currencies exchange contracts.

In 2014 fair value changes of EUR/USD forward foreign currencies exchange contract in the amount of EUR 16 thousand are included in the Consolidated Statement of Profit or Loss – see Note 11.

**Fair value changes of forward foreign currencies exchange contracts:**

|   | 2015    |             | 2014    |             |
|---|---------|-------------|---------|-------------|
|   | EUR'000 |             | EUR'000 |             |
|   | Assets  | Liabilities | Assets  | Liabilities |
| <b>Outstanding fair value at the beginning of the year</b>              | -       | -           | -       | <b>16</b>   |
| Included in the Consolidated Statement of Profit or Loss (Note 11 a, b) | -       | -           | -       | (16)        |
| <b>Outstanding fair value at the end of the year</b>                    | -       | -           | -       | -           |

**d) Fair values and fair value measurement**

In this Note are disclosed the fair value measurement hierarchy for the Group's assets and liabilities.

**Quantitative disclosures of fair value measurement hierarchy for assets at the end of the year:**

|  | Date of valuation | Fair value measurement using              |   |   | TOTAL            |
|--|-------------------|---|---|---|------------------|
|  |                   | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) |                  |
|  |                   | EUR'000                                   | EUR'000                                 | EUR'000                                   | EUR'000          |
| <b>Assets for which fair values are disclosed</b>  |                   |   |   |   |                  |
| Revalued property, plant and equipment (Note 14 c) | 31/12/2015        | -   | -                                       | 2,312,739                                 | <b>2,312,739</b> |
|  | 31/12/2014        | -   | -                                       | 2,307,182                                 | <b>2,307,182</b> |
| Investment property                                | 31/12/2015        | -   | -                                       | 1,726                                     | <b>1,726</b>     |
|  | 31/12/2014        | -   | -                                       | 1,904                                     | <b>1,904</b>     |
| Held-to-maturity financial assets                  | 31/12/2015        | -   | 34,427                                  | -   | <b>34,427</b>    |
|  | 31/12/2014        | -   | 34,931                                  | -   | <b>34,931</b>    |

There have been no transfers for assets between Level 1 and Level 2 during the reporting period.

**Quantitative disclosures of fair value measurement hierarchy for liabilities at the end of the year:**

|  | Date of valuation | Fair value measurement using              |   |   | TOTAL          |
|--|-------------------|---|---|---|----------------|
|  |                   | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) |                |
|  |                   | EUR'000                                   | EUR'000                                 | EUR'000                                   | EUR'000        |
| <b>Liabilities measured at fair value</b>              |                   |   |   |   |                |
| Derivative financial instruments, including:           |                   |   |   |   |                |
| Interest rate swaps                                    | 31/12/2015        | –   | 13,016                                  | –   | <b>13,016</b>  |
|  | 31/12/2014        | –   | 18,441                                  | –   | <b>18,441</b>  |
| Electricity forwards and futures                       | 31/12/2015        | –   | 2,558                                   | –   | <b>2,558</b>   |
|  | 31/12/2014        | –   | 2,112                                   | –   | <b>2,112</b>   |
| <b>Liabilities for which fair values are disclosed</b> |                   |   |   |   |                |
| Issued debt securities (bonds)                         | 31/12/2015        | –   | 186,247                                 | –   | <b>186,247</b> |
|  | 31/12/2014        | –   | 110,395                                 | –   | <b>110,395</b> |
| Floating rate borrowings                               | 31/12/2015        | –   | 616,074                                 | –   | <b>616,074</b> |
|  | 31/12/2014        | –   | 721,120                                 | –   | <b>721,120</b> |
| Fixed rate borrowings                                  | 31/12/2015        | –   | 206                                     | –   | <b>206</b>     |
|  | 31/12/2014        | –   | 633                                     | –   | <b>633</b>     |

There have been no transfers for liabilities between Level 1 and Level 2 during the reporting period.

The fair value hierarchy for the Group's financial instruments that are measured at fair value, by using specific valuation methods, is disclosed in Note 4 c.

Set out below, is a comparison by class of the carrying amounts and fair value of the Group's financial instruments, other than those with carrying amounts which approximates their fair values:

|   | Carrying amount |            | Fair value |            |         |
|---|-----------------|------------|------------|------------|---------|
|   | 31/12/2015      | 31/12/2014 | 31/12/2015 | 31/12/2014 |         |
|   |                 | EUR'000    | EUR'000    | EUR'000    | EUR'000 |
| <b>Financial assets</b>   |                 |            |            |            |         |
| Held-to-maturity financial assets                                       | 28,468          | 28,528     | 34,427     | 34,931     |         |
| <b>Financial liabilities</b>  |                 |            |            |            |         |
| Interest-bearing liabilities, including:                                |                 |            |            |            |         |
| issued debt securities (bonds)  | 181,207         | 105,496    | 186,247    | 110,395    |         |
| – floating rate borrowings  | 616,074         | 721,120    | 616,074    | 721,120    |         |
| – fixed rate borrowings   | 202             | 605        | 206        | 633        |         |
| Derivative financial instruments not designated for hedging, including: |                 |            |            |            |         |
| – electricity forwards and futures                                      | 2,558           | 2,112      | 2,558      | 2,112      |         |
| interest rate swaps   | 760             | 2,108      | 760        | 2,108      |         |
| Derivative financial instruments used for hedging, including:           |                 |            |            |            |         |
| interest rate swaps   | 12,256          | 16,333     | 12,256     | 16,333     |         |

The management assessed that cash and short-term deposits, trade receivables, trade payables, bank overdrafts and other current liabilities approximate their carrying amounts largely due to the short-term maturities of these instruments. The fair value of the financial assets and liabilities is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The following methods and assumptions were used to estimate the fair values:

- a) The fair values of borrowings with floating interest rates are equal their carrying amount, as their actual floating interest rates approximate the market price of similar financial instruments available to the Group;
- b) The borrowings with fixed interest rates had the fixed repayment period and the financial instrument is not traded in the active market; the financial instrument, which is not traded in the active market, the fair value is measured, using valuation techniques. The Groups uses various methods and models and make assumptions, which are based on the market conditions regarding the interest rates and other market conditions, existing at the end of reporting period. The fair value calculations are based on discounted cash flows using discount

factor of respective EUR swap rates increased by the Group's credit risk margin;

- c) The Group enters into derivative financial instruments with various counterparties, principally financial institutions with investment grade credit ratings. The derivative financial instruments are determined by using various valuation methods and models with market observable inputs. The models incorporate the credit quality of counterparties, foreign exchange spot and forward rates; the fair value of interest rate swaps is calculated as the present value of the estimated future cash flows, by discounting their future contractual cash flows at current market interest rates for similar financial instruments. The fair value of electricity forward and future contracts is calculated as discounted difference between actual market and settlement prices for the volume set in the agreements. If counterparty is a bank, calculated fair values of financial instruments are compared to bank's revaluation reports and the bank's calculated fair values of the financial instruments are used in the financial reports;
- d) The fair value of the bonds issued and held-to-maturity financial assets are calculated, based on the bank's quoted prices of the financial instruments at the end of the reporting period.

## 22. PROVISIONS

### a) Provisions for post-employment benefits

|   | 2015          | 2014          |
|---|---------------|---------------|
|   | EUR'000       | EUR'000       |
| <b>At the beginning of the year</b>                               | <b>12,650</b> | <b>12,195</b> |
| Provisions transferred to transmission system operator*           | (1,254)       | –             |
| Current service cost  | 1,604         | 507           |
| Past service cost   | –             | 9             |
| Interest cost   | 195           | 459           |
| Post-employment benefits paid                                     | (734)         | (361)         |
| Losses / (income) as a result of changes in actuarial assumptions | 1,158         | (159)         |
| <b>At the end of the year</b>                                     | <b>13,619</b> | <b>12,650</b> |

\* provisions were transferred due transmission system assets construction and maintenance functions transfer as of 1<sup>st</sup> of January 2015 that also comprised transition of 430 employees from the Group to transmission system operator

Total charged/credited provisions are included in the Consolidated Statement of Profit or Loss position 'Personnel expenses' within state social insurance

contributions and other benefits defined in the Collective agreement (Note 9):

|   | 2015          | 2014          |
|---|---------------|---------------|
|   | EUR'000       | EUR'000       |
| <b>At the beginning of the year</b>                                 | <b>12,650</b> | <b>12,195</b> |
| Charged to the Consolidated Statement of Other Comprehensive Income | 1,158         | (159)         |
| Charged to the Consolidated Statement of Profit or Loss             | (189)         | 614           |
| <b>At the end of the year</b>                                       | <b>13,619</b> | <b>12,650</b> |

Weighted average discount rate used for discounting benefit obligations was 1.71 % (2014: 3.63 %), considering the market yields on government bonds at the end of the reporting year. The Group's Collective Agreement provides indexation of employees' wages at least at the level of inflation. Long-term inflation determined at the level of 3.5 % (2014: 2.5 %) when calculating

long-term post-employment benefits. In calculation of these liabilities also the probability, determined on the basis of previous experience, of retirement in different employees' aging groups was also considered.

A quantitative sensitivity analysis for significant assumptions as of the end of the year is as shown below:

| Assumptions                                       |         | Date of valuation | Discount rate |             | Future salary changes |             | Retirement probability changes |             |
|---|---------|-------------------|---------------|-------------|-----------------------|-------------|--------------------------------|-------------|
|   |         |                   | 1% increase   | 1% decrease | 1% increase           | 1% decrease | 1% increase                    | 1% decrease |
| Impact on provisions for post-employment benefits | EUR'000 | 31/12/2015        | 1,464         | (1,199)     | 1,426                 | (1,194)     | 1,581                          | (1,305)     |
|   | EUR'000 | 31/12/2014        | 1,981         | (1,588)     | 1,984                 | (1,617)     | 1,361                          | (1,143)     |

The sensitivity analysis above have been determined based on a method that extrapolates the impact on defined benefit obligation as a result of reasonable

changes in key assumptions occurring at the end of the reporting period.

#### b) Environmental provisions

|   | 2015         | 2014         |
|---|--------------|--------------|
|   | EUR'000      | EUR'000      |
| <b>At the beginning of the year</b>                     | <b>2,938</b> | <b>3,402</b> |
| Charged to the Consolidated Statement of Profit or Loss | (573)        | (464)        |
| <b>At the end of the year</b>                           | <b>2,365</b> | <b>2,938</b> |

The environmental provision in the amount of EUR 2,365 thousand (31/12/2014: EUR 2,938 thousand) represents the estimated cost of cleaning up Riga TEC-1 combined heat and power plant ash-fields in accordance with the requests made by the regional Environmental Authority of Riga and feasibility study on this project in the amount of EUR 1,160 thousand (31/12/2014:

EUR 1,205 thousand) and Liepājas Enerģija SIA provision for the environmental recovery measures in the amount of EUR 1,205 thousand (31/12/2014: EUR 1,733 thousand). The amount of the provisions is calculated taking into account the construction cost index (data from the Central Statistical Bureau of the Republic of Latvia).

## 23. OTHER LIABILITIES AND DEFERRED INCOME

|  | 31/12/2015     | 31/12/2014     |
|--|----------------|----------------|
|  | EUR'000        | EUR'000        |
| Deferred non-current income from connection fees                 | 149,378        | 145,591        |
| Deferred income on financing from European Union funds           | 46,681         | 48,515         |
| Deferred income from plant and equipment received free of charge | 327            | 368            |
| <b>TOTAL other liabilities and deferred income</b>               | <b>196,386</b> | <b>194,474</b> |

#### Movement in deferred connection fees (non-current and current part):

|   | 2015           | 2014           |
|---|----------------|----------------|
|   | EUR'000        | EUR'000        |
| <b>At the beginning of the year</b>   | <b>156,382</b> | <b>149,131</b> |
| Received fees   | 16,172         | 18,178         |
| Credited to the Consolidated Statement of Profit or Loss (Note 6 "Other revenue") | (11,621)       | (10,927)       |
| <b>At the end of the year</b>   | <b>160,933</b> | <b>156,382</b> |

## 24. TRADE AND OTHER PAYABLES

|   | 31/12/2015     | 31/12/2014     |
|---|----------------|----------------|
|   | EUR'000        | EUR'000        |
| <b>Financial liabilities:</b>   |                |                |
| Payables for materials and services   | 44,499         | 60,231         |
| Payables for electricity  | 22,518         | 26,205         |
| Accrued expenses  | 7,514          | 7,564          |
| Other financial current payables  | 6,417          | 7,940          |
| <b>Total financial liabilities</b>  | <b>80,948</b>  | <b>101,940</b> |
| <b>Non-financial liabilities:</b>   |                |                |
| State social security contributions and other taxes                                 | 10,318         | 12,351         |
| Advances received   | 8,612          | 8,852          |
| Deferred income from connection fees  | 11,555         | 10,792         |
| <b>Deferred income on financing from European Union funds:</b>                      |                |                |
| – The European Energy Development Program – 330 kV Kurzeme Ring                     | 1,121          | 1,130          |
| – The EU Cohesion Fund – reconstruction of Liepājas enerģija SIA heat source        | 320            | 320            |
| – The EU Cohesion Fund – construction of Liepājas enerģija SIA biomass boiler house | 196            | 196            |
| – The EU Cohesion Fund – reconstruction of Liepājas enerģija SIA heating network    | 244            | 244            |
| – The EU's Climate change financial instrument – introduction of smart technologies | 23             | 23             |
| – The EU Regional Development Fund – woodchip boiler house construction in Ķegums   | 16             | 16             |
| Other non-financial current payables  | 3,896          | 4,045          |
| <b>TOTAL non-financial liabilities</b>  | <b>36,301</b>  | <b>37,969</b>  |
| <b>TOTAL trade and other current payables</b>                                       | <b>117,249</b> | <b>139,909</b> |

The carrying amounts of trade and other payables are assumed to approximate their fair values.

## 25. RELATED PARTY TRANSACTIONS

The Parent Company and, indirectly, the other Group entities are controlled by the Latvian state. Related parties of the Group are associates, Shareholder of the Parent Company who controls or who has significant influence over the Group's entities in accepting operating business decisions, key management

personnel of the Group's entities including members of Supervisory body – Audit committee and close family members of any above-mentioned persons, as well as entities over which those persons have control or significant influence.

**The following transactions were carried out with related parties:**

|   | 2015     | 2014       |
|---|----------|------------|
|   | EUR'000  | EUR'000    |
| <b>Finance income / (loss):</b>   |          |            |
| – Received dividends from associates  | –        | 1,924      |
| – Net loss from disposal of non-current financial investments in associates | –        | (1,567)    |
| <b>TOTAL finance income</b>   | <b>–</b> | <b>357</b> |



**Balances at the end of the year arising from sales/purchases:**

|   | 31/12/2015 | 31/12/2014 |
|---|------------|------------|
|   | EUR'000    | EUR'000    |
| <b>Trade payables to related parties:</b> |            |            |
| – Other related parties                   | 252        | 354        |
| <b>TOTAL payables</b>                     | <b>252</b> | <b>354</b> |

The Group has not incurred write-offs of trade payables and receivables from transactions with related parties, as all debts are recoverable.

Receivables and payables with related parties are current balances for services and goods. None of the amounts at the end of the reporting year are secured.

Remuneration to the key management personnel that is defined as Members of the Management Boards of the Group entities and Supervisory body is disclosed in Note 9.

Dividend payments to Shareholder of the Parent Company and share capital contributions are disclosed in Note 20 b and Note 19, respectively.

**26. CAPITAL COMMITMENTS AND CONTINGENT LIABILITIES**

As of 31<sup>st</sup> of December 2015 the Group had commitments amounting to EUR 235.8 million (31/12/2014: EUR 152.2 million) for capital expenditure contracted but not delivered at the end of the reporting period.

In 2016 Latvenergo AS has issued support letters to its subsidiaries Enerģijas publiskais tirgotājs AS, Sadales tīkls AS, Latvijas elektriskie tīkli AS and Liepājas enerģija SIA acknowledging that its position as shareholders is to ensure that subsidiaries are managed so that they have sufficient financial resources and are able to carry their operations and settle their obligations.

**27. EVENTS AFTER THE REPORTING YEAR**

On 20<sup>th</sup> of January 2016 Sadales tīkls AS has submitted to Public Utilities Commission (PUC) electricity distribution system services tariff (distribution tariff) structure rebalancing project, which determines to decrease by 20 % the price of electricity distributed to households, and at the same time to set the fixed fee for network connection providing regardless of electricity consumption level.

Public Utilities Commission (PUC) on 11<sup>th</sup> of February 2016 approved mandatory procurement PSO fee submitted by Enerģijas publiskais tirgotājs AS to PUC on 20<sup>th</sup> of January 2016, and as of 1<sup>st</sup> of April 2016 mandatory procurement PSO fee is unchanged – EUR 2.679 cents/kWh.

On 12<sup>th</sup> of February 2016 international credit rating

agency Moody's Investors Service has affirmed the credit rating of Latvenergo AS to Baa2 (stable).

On 14<sup>th</sup> of April 2016 Latvenergo AS issued additional first series notes (*green* bonds) in the total amount of EUR 25 million under the second programme for the issuance of notes of Latvenergo AS. With this issue total of EUR 100 million bonds under the second programme for the issuance of notes has been issued thus covering the entire amount of the programme approved on 25<sup>th</sup> of May 2015.

There have been no other significant events subsequent to the end of the reporting year that might have a material effect on the Group's Consolidated Financial Statements for the year ended 31<sup>st</sup> of December 2015.

**28. FINANCIAL INFORMATION ON THE PARENT COMPANY**

The unconsolidated primary financial statements of the Parent Company have been prepared in accordance with the Annual Accounts Law of the Republic of Latvia and these are not separate financial statements of the Parent Company in the meaning of IAS 27 "Consolidated Financial Statements". According with the Annual Accounts Law of the

Republic of Latvia gains on revaluation of property, plant and equipment and gains or losses as a result of re-measurement on defined post-employment benefit plan are disclosed in the Statement of Profit or Loss, but according to IFRS – as other comprehensive income or loss through Statement of Other Comprehensive Income.

The Parent Company financial information below is presented in accordance with the International Financial Reporting Standards as adopted by the European Union:

### Statement of Profit or Loss

|  | 2015           | 2014          |
|--|----------------|---------------|
|  | EUR'000        | EUR'000       |
| Revenue  | 521,146        | 741,108       |
| Other income   | 1,695          | 3,277         |
| Raw materials and consumables used   | (252,882)      | (419,144)     |
| Personnel expense  | (38,321)       | (35,032)      |
| Depreciation, amortisation and impairment of intangible assets and property, plant and equipment | (90,507)       | (86,894)      |
| Other operating expenses   | (50,656)       | (185,157)     |
| <b>Operating profit</b>  | <b>90,475</b>  | <b>18,158</b> |
| Income from investments in subsidiaries  | 17,739         | 25,562        |
| Finance income   | 14,097         | 12,829        |
| Finance costs  | (19,099)       | (21,504)      |
| <b>Profit before tax</b>   | <b>103,212</b> | <b>35,045</b> |
| Income tax   | (8,465)        | (246)         |
| <b>Profit for the year</b>   | <b>94,747</b>  | <b>34,799</b> |

### Statement of Other Comprehensive Income

|  | 2015          | 2014           |
|--|---------------|----------------|
|  | EUR'000       | EUR'000        |
| <b>Profit for the year</b>   | <b>94,747</b> | <b>34,799</b>  |
| <i>Other comprehensive income / (loss) to be reclassified to profit or loss in subsequent periods (net of tax)</i>     |               |                |
| Gains / (losses) from change in hedge reserve  | 4,077         | (6,495)        |
| Losses on currency translation differences   | -             | (14)           |
| <b>Net other comprehensive income / (loss) to be reclassified to profit or loss in subsequent periods</b>              | <b>4,077</b>  | <b>(6,509)</b> |
| <i>Other comprehensive income / (loss) not to be reclassified to profit or loss in subsequent periods (net of tax)</i> |               |                |
| Gains on revaluation of property, plant and equipment  | 21            | 93             |
| (Losses) / gains as a result of re-measurement on defined post-employment benefit plan                                 | (234)         | 84             |
| <b>Net other comprehensive income / (loss) not to be reclassified to profit or loss in subsequent periods</b>          | <b>3,864</b>  | <b>177</b>     |
| <b>Other comprehensive income / (loss) for the year, net of tax</b>  | <b>98,650</b> | <b>(6,332)</b> |
| <b>Total other comprehensive income for the year</b>   | <b>98,611</b> | <b>28,467</b>  |

## Statement of Financial Position

|  | 31/12/2015       | 31/12/2014       |
|--|------------------|------------------|
|  | EUR'000          | EUR'000          |
| <b>ASSETS</b>                          |                  |                  |
| Intangible assets                      | 19,846           | 18,687           |
| Property, plant and equipment          | 1,415,711        | 1,429,916        |
| Investment property                    | 522              | 1,136            |
| Financial investment                   | 1,201,968        | 1,184,411        |
| <b>Total non-current assets</b>        | <b>2,638,047</b> | <b>2,634,150</b> |
| Inventories                            | 8,388            | 8,742            |
| Trade and other receivables            | 367,941          | 372,734          |
| Derivative financial instruments       | -                | -                |
| Current financial investments          | 7,859            | -                |
| Cash and cash equivalents              | 101,819          | 88,966           |
| <b>Total current assets</b>            | <b>486,007</b>   | <b>470,442</b>   |
| <b>TOTAL ASSETS</b>                    | <b>3,124,054</b> | <b>3,104,592</b> |
| <b>EQUITY</b>                          |                  |                  |
| Share capital                          | 1,288,531        | 1,288,446        |
| Non-current assets revaluation reserve | 662,055          | 662,146          |
| Hedge reserve                          | (12,256)         | (16,333)         |
| Other reserves                         | 82,021           | 78,524           |
| Retained earnings                      | 94,747           | 34,799           |
| <b>Total equity</b>                    | <b>2,115,098</b> | <b>2,047,582</b> |
| <b>LIABILITIES</b>                     |                  |                  |
| Provisions                             | 6,371            | 5,799            |
| Borrowings                             | 701,822          | 673,817          |
| Deferred income tax liabilities        | 127,934          | 123,102          |
| Derivative financial instruments       | 8,291            | 11,698           |
| Other non-current liabilities          | 1,133            | 749              |
| <b>Total non-current liabilities</b>   | <b>845,551</b>   | <b>815,165</b>   |
| Borrowings                             | 81,143           | 136,864          |
| Trade and other payables               | 61,356           | 82,911           |
| Derivative financial instruments       | 7,283            | 8,855            |
| Other current liabilities              | 13,623           | 13,215           |
| <b>Total current liabilities</b>       | <b>163,405</b>   | <b>241,845</b>   |
| <b>TOTAL EQUITY AND LIABILITIES</b>    | <b>3,124,054</b> | <b>3,104,592</b> |



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## INDEPENDENT AUDITORS' REPORT

To the shareholder of AS Latvenergo

### Report on the financial statements

We have audited the accompanying consolidated financial statements of AS Latvenergo and its subsidiaries (the "Group"), set out on pages 107 through 163 of the accompanying 2015 Consolidated Annual Report, which comprise the consolidated statement of financial position as at 31 December 2015, and consolidated statement of profit or loss, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

### Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' responsibility

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

Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or

error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the consolidated financial statements give a true and fair view of the financial position of AS Latvenergo and its subsidiaries as of 31 December 2015, and of its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

### Report on other legal and regulatory requirements

Furthermore, we have read the management report for the year ended 31 December 2015 (set out on pages 104 through 106 of the accompanying 2015 Consolidated Annual Report) and have not noted any material inconsistencies between the financial information included in it and the consolidated financial statements for the year ended 31 December 2015.

We have assured ourselves that the Group has prepared the corporate management report for the year 2015 and verified information presented in the report according to requirements listed in the section 56.1 first paragraph clauses 3, 4, 6, 8 and 9 and the section 56.2 second paragraph clause 5 in the Law on Financial Instruments Market of Republic of Latvia.

SIA Ernst & Young Baltic  
Licence No. 17



Diāna Krišjāne  
Chairperson of the Board  
Latvian Certified Auditor  
Certificate No. 124

Rīga, 19 April 2016

