AB KAUNO ENERGIJA

SET OF CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR, ENDED 31 DECEMBER 2016, PREPARED ACCORDING TO INTERNATIONAL FINANCIAL REPORTING STANDARDS, AS ADOPTED BY THE EUROPEAN UNION, PRESENTED TOGETHER WITH CONSOLIDATED ANNUAL REPORT AND INDEPENDENT AUDITOR'S REPORT

Translation note

This set of Consolidated and Parent Company's Financial Statements presented together with Consolidated Annual Report and Independent Auditor's Report has been prepared in Lithuanian language and in English language. In all matters of interpretations of information, views or opinions, the Lithuanian language version of these documents takes precedence over the English version.

Page

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Kauno Energija AB

Report on the Audit of the Separate and Consolidated Financial Statements

Opinion

We have audited the separate financial statements of Kauno Energija AB (the Company) and consolidated financial statements of Kauno Energija AB and its subsidiaries (the Group), which comprise of the statements of financial position of the Company and the Group as at 31 December 2016, and statements of comprehensive income, changes in equity and statements of cash flows for the year then ended, and notes to the separate and consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying separate and consolidated financial statements present fairly, in all material respects, the financial position of the Company and the Group as at 31 December 2016, and 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.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Separate and Consolidated Financial Statements* section of our report. We are independent of the Company and the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the requirements of the Law on Audit of the Republic of Lithuania that are relevant to audit in the Republic of Lithuania, and we have fulfilled our other ethical responsibilities in accordance with the Law on Audit of the Republic of Lithuania and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the separate and consolidated financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	**How the matter was addressed in the audit**
Fair value determination of net assets in acquisition of subsidiary Petrasiunu katiline UAB	
The Company acquired subsidiary (Petrasiunu Katiline UAB) in October 2016. The fair value of the long term assets (bio fuel boiler) acquired amounts to EUR 6.5 million as at 31 December 2016. The Company performed internal valuation to determine the fair value of the long term assets acquired by comparing production costs of similar boilers. Significant judgment was required by management in determining the fair value of such assets acquired: selecting valuation method, identifying bio fuel boilers with similar characteristics, determining production costs. The judgements made and assumptions used by management in performing the valuation are disclosed in Note 26. Accordingly the valuation of the long term assets acquired is considered to be a key audit matter due to the significance of the balance to the financial statements as a whole, combined with the	We assessed the competence, capabilities and objectivity of management that performed the determination of fair value. We evaluated management's judgments, in particular: • The model used by management; and • The significant assumptions used in determination of fair value of the long term assets, in particular the market price of similar bio fuel boilers. We compared inputs used by management to market data and entity-specific historical information of similar bio fuel boilers to confirm the appropriateness of these judgments. We obtained also independent market information ourselves to compare with the estimates used by the company. Additionally, we performed a sensitivity analysis on the significant assumptions to evaluate the extent of impact on the fair values and assessed the appropriateness of the entity's disclosures relating to valuation judgments.

Key audit matter	How the matter was addressed in the audit
Fair value determination of net assets in acquisition of subsidiary Petrasiunu katiline UAB	
judgment associated with determining the fair value.	
Accounting of settlement agreement with Kauno Termofikacine Elektrine UAB	
The Company recognized EUR 1.8 million of Other operating income from settlement of legal dispute with Kauno Termofikacine Elektrine UAB (further – KTE), described in Note 18. The EUR 1.8 million was received in cash. EUR 0.5 million will be received in equal annual instalments till 28 February 2018. The Company also received certain assets that were immediately leased back to KTE. Significant judgment was required by management in determining the proper accounting of settlement received and to be received as well as fair value of the assets obtained for free and simultaneously leased back to KTE. The Company performed internal valuation to determine the fair value of the assets obtained as a result of the settlement. Proper accounting of the settlement agreement is considered to be a key audit matter due to the significance of the balance to the financial statements as a whole, combined with the judgment associated with determining the fair value of the assets obtained and the timing of income recognition.	We assessed the competence, capabilities and objectivity of management that performed the determination of fair value as well as proper accounting treatment of the settlement agreement. We evaluated management's judgments, in particular: • The asset valuation model used; • Significant valuation assumptions used. We agreed the inputs used in valuation model to settlement and lease agreements and market data to confirm the appropriateness of these judgments. • We reviewed the IFRS accounting treatment of settlement received in cash. Agreed the amount received to bank statement and the decision of arbitration for this legal dispute. We also assessed the appropriateness of deferring revenue recognition for remaining part of cash settlement till cash is actually received. • We assessed the allocation of money received between cash received as penalty as part of settlement and asset lease.

Other information

The other information comprises the information included in the Company's and Group's annual reports, but does not include the separate and consolidated financial statements and our auditor's report thereon. Management is responsible for the other information.

Our opinion on the separate and consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the separate and consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the separate and consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the separate and consolidated financial statements

Management is responsible for the preparation and fair presentation of the separate and consolidated financial statements in accordance with the Law of the Republic of Lithuania on accounting and financial reporting, and 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 the separate and consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the separate and consolidated financial statements, management is responsible for assessing the Company's and Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's separate and Group's consolidated financial reporting processes.

Auditor's responsibilities for the audit of the separate and consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the separate and consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these separate and consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the separate and consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's and Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's and Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the separate and consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company or the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the separate and consolidated financial statements, including the disclosures, and whether the separate and consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company and the Group to express an opinion on the separate and consolidated financial statements. We are responsible for the direction, supervision and performance of the company and group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the separate and consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Simonas Rimašauskas.

Deloitte Lietuva, UAB
Audit Company License No 001275

Simonas Rimašauskas
Lithuanian Certified Auditor
License No. 000466

Vilnius, Republic of Lithuania
31 March 2017

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Statements of Financial Position

		Group		Company	
	Notes	**As of 31 December 2016**	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
ASSETS					
Non-current assets					
Intangible assets	**3**	**107**	**116**	**107**	**116**
Property, plant and equipment	**4**				
Land and buildings		9,290	7,871	7,590	7,832
Structures		84,919	84,833	84,207	84,833
Machinery and equipment		27,420	24,469	23,507	24,472
Vehicles		497	383	448	410
Devices and tools		3,186	2,790	3,175	2,790
Construction in progress and prepayments		974	304	974	304
Investment property		299	304	-	-
Total property, plant and equipment		**126,585**	**120,954**	**119,901**	**120,641**
Non-current financial assets					
Investments into subsidiarys	**1**	-	-	2,968	1,074
Non-current accounts receivable	**5**	-	1	-	1
Other financial assets	**6**	1	1	1	1
Total non-current financial assets		**1**	**2**	**2,969**	**1,076**
Total non-current assets		**126,693**	**121,072**	**122,977**	**121,833**
Current assets					
Inventories and prepayments					
Inventories	**7**	486	289	416	285
Prepayments		491	716	384	716
Total inventories and prepayments		**977**	**1,005**	**800**	**1,001**
Current accounts receivable	**8**				
Trade receivables	**23;25**	10,117	8,975	10,117	8,975
Other receivables		1,001	859	984	846
Total accounts receivable		**11,118**	**9,834**	**11,101**	**9,821**
Cash and cash equivalents	**9;23**	6,285	2,531	6,193	2,518
Total current assets		**18,380**	**13,370**	**18,094**	**13,340**
Total assets		**145,073**	**134,442**	**141,071**	**135,173**

(cont'd on the next page)

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Statements of Financial Position (cont'd)

	Notes	Group		Company	
		As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
EQUITY AND LIABILITIES					
Equity					
Share capital	1	74,476	74,476	74,476	74,476
Legal reserve	10	2,922	2,695	2,922	2,695
Other reserve	10	2,977	713	2,977	713
Retained earnings (deficit)					
Profit for the current year	1	6,957	4,509	6,901	4,528
Profit (loss) for the prior year	1	(313)	(533)	239	-
Total retained earnings (deficit)		**6,644**	**3,976**	**7,140**	**4,528**
Total equity		**87,019**	**81,860**	**87,515**	**82,412**
Liabilities					
Non-current liabilities					
Non-current borrowings	11;23	19,559	19,481	19,559	19,481
Financial lease obligations	12;23	39	35	39	35
Deferred tax liability	21	4,269	3,503	4,461	3,695
Grants (deferred income)	13	17,469	16,761	16,176	16,761
Employee benefit liability	14;25	1,069	585	1,066	585
Non-current trade liabilities	23	18	26	18	26
Total non-current liabilities		**42,423**	**40,391**	**41,319**	**40,583**
Current liabilities					
Current portion of non-current borrowings and financial lease	11;12;23	6,252	2,436	2,849	2,436
Current borrowings	11;23	-	-	-	-
Trade payables	23	7,194	7,778	7,306	7,777
Payroll-related liabilities		668	604	657	601
Advances received		549	499	549	499
Taxes payable		391	282	343	280
Derivative financial instruments	15	34	-	-	-
Current portion of employee benefit liability	14	262	306	262	306
Other current liabilities		281	286	271	279
Total current liabilities		**15,631**	**12,191**	**12,237**	**12,178**
Total liabilities		**58,054**	**52,582**	**53,556**	**52,761**
Total equity and liabilities		**145,073**	**134,442**	**141,071**	**135,173**

(the end)

The accompanying notes are an integral part of these financial statements.

General Manager	Rimantas Bakas		31 March 2017
Head of Finance Department	Gintautas Muznikas		31 March 2017
Chief Accountant	Violeta Staškūnienė		31 March 2017

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Statements of Profit (loss) and other comprehensive income

Group

	Notes	2016	2015
Income			
Sales income	16	61,178	60,725
Other operating income	18	2,288	597
Total income		**63,466**	**61,322**
Expenses			
Fuel and heat acquired		(34,334)	(34,885)
Salaries and social security		(6,992)	(6,498)
Depreciation and amortisation	3;4	(6,172)	(5,890)
Repairs and maintenance		(716)	(788)
Write-offs and change in allowance for accounts receivable	5;8	797	145
Taxes other than income tax		(1,496)	(1,416)
Electricity		(1,212)	(1,218)
Raw materials and consumables		(622)	(619)
Water		(831)	(786)
Change in write-down to net realisable value of inventories and non-current assets	7	(22)	(570)
Other expenses	17	(2,920)	(2,503)
Other activities expenses	18	(306)	(449)
Total expenses		**(54,826)**	**(55,477)**
Operating profit (losses)		**8,640**	**5,845**
Other interest and similar income	19	210	264
Financial assets and short-term investments impairment	20	-	(27)
Interest and other similar expenses	20	(574)	(776)
Finance cost, net		**(364)**	**(539)**
Profit before income tax		**8,276**	**5,306**
Income tax	21	(2)	(9)
Deferred tax income (losses)		(766)	(647)
Profit for the year		**7,508**	**4,650**
Employee benefit liability (accumulation)		(551)	(141)
Comprehensive income		**6,957**	**4,509**
Profit for the year attributable to owners of the Company		**7,508**	**4,650**
Total comprehensive income attributable to owners of the Company		**6,957**	**4,509**
Basic and diluted earnings per share (EUR)	22	**0.16**	**0.11**

The accompanying notes are an integral part of these financial statements.

General Manager	Rimantas Bakas		31 March 2017
Head of Finance Department	Gintautas Muznikas		31 March 2017
Chief Accountant	Violeta Staškūnienė		31 March 2017

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Statements of Profit (loss) and other comprehensive income

Company

	Notes	2016	2015
Income			
Sales income	16	61,188	60,733
Other operating income	18	2,181	519
Total income		**63,369**	**61,252**
Expenses			
Fuel and heat acquired		(34,641)	(34,885)
Salaries and social security		(6,953)	(6,498)
Depreciation and amortisation	3,4	(6,074)	(5,890)
Repairs and maintenance		(711)	(788)
Write-offs and change in allowance for accounts receivable	5,8	810	157
Taxes other than income tax		(1,490)	(1,416)
Electricity		(1,159)	(1,218)
Raw materials and consumables		(619)	(619)
Water		(830)	(786)
Change in write-down to net realisable value of inventories and non-current assets	7	(22)	(570)
Other expenses	17	(2,907)	(2,503)
Other activities expenses	18	(231)	(372)
Total expenses		**(54,827)**	**(55,388)**
Operating profit (losses)		**8,542**	**5,864**
Other interest and similar income	19	213	264
Financial assets and short-term investments impairment		-	(27)
Interest and other similar expenses	20	(541)	(776)
Finance cost, net		**(328)**	**(539)**
Profit before income tax		**8,214**	**5,325**
Income tax	21	1	(9)
Deferred tax income (losses)		(766)	(647)
Profit for the year		**7,449**	**4,669**
Employee benefit liability (accumulation)		(548)	(141)
Comprehensive income		**6,901**	**4,528**
Profit for the year attributable to owners of the Company		**7,449**	**4,669**
Total comprehensive income attributable to owners of the Company		**6,901**	**4,528**
Basic and diluted earnings per share (EUR)	22	**0.16**	**0.11**

The accompanying notes are an integral part of these financial statements.

General Manager	Rimantas Bakas		31 March 2017
Head of Finance Department	Gintautas Muznikas		31 March 2017
Chief Accountant	Violeta Staškūnienė		31 March 2017

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Statements of Changes in Equity

Group	Notes	Share capital	Legal reserve	Other reserve	Retained earnings (accumulated deficit)	Total
Balance as of 31 December 2014		**74,378**	**2,082**	**521**	**401**	**77,382**
Increase in share capital	1	-	-	-	-	-
Transferred to reserves	10	-	613	713	(1,326)	-
Transferred from reserves	10	-	-	(521)	521	-
Dividends	1	-	-	-	(129)	(129)
Total comprehensive income		98	-	-	4,509	4,607
Balance as of 31 December 2015		**74,476**	**2,695**	**713**	**3,976**	**81,860**
Transferred to reserves	10	-	227	2,977	(3,204)	-
Transferred from reserves	10	-	-	(713)	713	-
Dividends	1	-	-	-	(1,798)	(1,798)
Total comprehensive income		-	-	-	6,957	6,957
Balance as of 31 December 2016		**74,476**	**2,922**	**2,977**	**6,644**	**87,019**

Company	Notes	Share capital	Legal reserve	Other reserve	Retained earnings (accumulated deficit)	Total
Balance as of 31 December 2014		**74,378**	**2,082**	**521**	**934**	**77,915**
Increase in share capital	1	-	-	-	-	-
Transferred to reserves	10	-	613	713	(1,326)	-
Transferred from reserves	10	-	-	(521)	521	-
Dividends	1	-	-	-	(129)	(129)
Total comprehensive income		98	-	-	4,528	4,626
Balance as of 31 December 2015		**74,476**	**2,695**	**713**	**4,528**	**82,412**
Transferred to reserves	10	-	227	2,977	(3,204)	-
Transferred from reserves	10	-	-	(713)	713	-
Dividends	1	-	-	-	(1,798)	(1,798)
Total comprehensive income		-	-	-	6,901	6,901
Balance as of 31 December 2016		**74,476**	**2,922**	**2,977**	**7,140**	**87,515**

The accompanying notes are an integral part of these financial statements.

General Manager	Rimantas Bakas		31 March 2017
Head of Finance Department	Gintautas Muznikas		31 March 2017
Chief Accountant	Violeta Staškūnienė		31 March 2017

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Statements of Cash Flows

	Group		Company	
	2016	**2015**	**2016**	**2015**
Cash flows from (to) operating activities				
Comprehensive income	**6,957**	**4,509**	**6,901**	**4,528**
Adjustments for non-cash items:				
Depreciation and amortisation	7,587	7,134	7,466	7,117
Write-offs and change in allowance for accounts receivable	(792)	(136)	(805)	(148)
Interest expenses	557	650	541	650
Change in fair value of derivatives	17	-	-	-
Loss (profit) from sale and write-off of property, plant and equipment and value of the shares	(2)	43	(2)	43
(Amortisation) of grants (deferred income)	(1,090)	(866)	(1,050)	(866)
Change in write-down to net realisable value of inventories and non-current assets	22	570	22	570
Change employee benefit liability	551	141	548	141
Calculation of the value of shares	-	98	-	98
Income tax expenses	768	647	765	647
Change in accruals	87	58	85	55
Impairment of investment in subsidiary	-	-	-	-
Elimination of other financial and investing activity results	(210)	(236)	(210)	(236)
Total adjustments for non-cash items:	**7,495**	**8,103**	**7,360**	**8,071**
Changes in working capital:				
(Increase) decrease in inventories	(170)	(261)	(112)	(262)
(Increase) decrease in prepayments	237	(115)	332	(105)
(Increase) decrease in trade receivables	(317)	6,378	(307)	6,381
(Increase) decrease in other receivables	289	5,991	290	5,992
(Decrease) increase in other non-current liabilities	(8)	(72)	(8)	(72)
(Decrease) increase in current trade payables and advances received	(553)	(11,617)	(421)	(11,616)
(Decrease) increase in payroll-related liabilities	(114)	(132)	(102)	(132)
Increase (decrease) in other liabilities to budget	106	267	63	264
Increase (decrease) in other current liabilities	(60)	(229)	(40)	(235)
Total changes in working capital:	**(590)**	**210**	**(305)**	**215**
Net cash flows from operating activities	**13,862**	**12,822**	**13,956**	**12,814**

(cont'd on the next page)

The accompanying notes are an integral part of these financial statements.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

	Group		Company	
	2016	**2015**	**2016**	**2015**
Cash flows from (to) the investing activities				
(Acquisition) of tangible and intangible assets	(6,678)	(4,722)	(6,680)	(4,722)
Proceeds from sale of tangible assets	3	121	4	121
Interest received for overdue accounts receivable	210	264	210	264
Acquisition of subsidiaries	(1,706)	-	(1,894)	-
Decrease of non-current accounts receivable	-	3	-	3
Net cash (used in) investing activities	**(8,171)**	**(4,334)**	**(8,360)**	**(4,334)**
Cash flows from (to) financing activities				
Proceeds from loans	2,974	9,642	2,974	9,642
(Repayment) of loans	(2,489)	(16,914)	(2,489)	(16,914)
Interest (paid)	(574)	(645)	(558)	(645)
Financial lease (payments)	(60)	(64)	(60)	(64)
Penalties and fines (paid)	-	(28)	-	(28)
Dividends, tantiemes (paid)	(1,797)	(128)	(1,797)	(128)
Received grants	9	1,791	9	1,791
Net cash flows from (used in) financing activities	**(1,937)**	**(6,346)**	**(1,921)**	**(6,346)**
Net (decrease) increase in cash and cash equivalents	**3,754**	**2,142**	**3,675**	**2,134**
	-	-	-	-
Cash and cash equivalents at the beginning of the period	**2,531**	**389**	**2,518**	**384**
Cash and cash equivalents at the end of the period	**6,285**	**2,531**	**6,193**	**2,518**

(the end)

The accompanying notes are an integral part of these financial statements.

General Manager	Rimantas Bakas		31 March 2017
Head of Finance Department	Gintautas Muznikas		31 March 2017
Chief Accountant	Violeta Staškūnienė		31 March 2017

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Notes to the Financial Statements

1. General information

AB Kauno Energija (hereinafter – the Company) is a public limited liability company registered in the Republic of Lithuania. The address of its registered office is as follows: Raudondvario Rd. 84, Kaunas, Lithuania. Data on the Company are collected and stored in the Register of Legal Entities.

AB Kauno Energija consists of the Company's head office and the branch of Jurbarko Šilumos Tinklai.

The Company is involved in heat and hot water supplies, electricity generation and distribution and also in maintenance of manifolds. The Company are also involved in maintenance of heating systems. The Company was registered on 1 July 1997 after the reorganisation of AB Lietuvos Energija. The Company's shares are traded on the Baltic Secondry List of the AB Nasdaq Vilnius.

As of 31 December 2016 and of 31 December 2015 the shareholders of the Company were as follows:

	As of 31 December 2016		As of 31 December 2015	
	Number of shares owned (unit)	Percentage of ownership (percent)	Number of shares owned (unit)	Percentage of ownership (percent)
Kaunas city municipality	39,736,058	92.84	39,736,058	92.84
Kaunas district municipality	1,606,168	3.75	1,606,168	3.75
Jurbarkas district municipality	746,405	1.74	746,405	1.74
Other minor shareholders	713,512	1.67	713,512	1.67
	42,802,143	100.00	42,802,143	100.00

All the shares are ordinary shares. The Company owns no shares as at the end of the reporting periods. All shares were fully paid as of 31 December 2016 and as of 31 December 2015.

On 28 April 2016 the Annual General Meeting of Shareholders has made a decision to pay EUR 1,798 thousand, i.e. at 4.2 cents a share in dividends and EUR 32 thousand tantiemes for the members of the Company's board from the profit of the year 2015. Annual payments are accounted in salaries and social security line of Statements of Profit (loss) and other comprehensive income.

On 28 April 2015 the Annual General Meeting of Shareholders has made a decision to pay EUR 129 thousand, i.e. at 0.3 cents a share in dividends.

Responding to changes in competition in Kaunas heat production sector, the Company signed an agreement with UAB E-Energija on 23 June 2016 regarding purchase of 100 % of shares of UAB Petrašiūnų Katilinė. The agreement became valid on 30 June 2016. On 29 July 2016 the agreement was approved on the extraordinary meeting of shareholders. On 27 October 2016 the Company accomplished transaction of acquisition of UAB Petrašiūnų Katilinė, acquiring block of shares for EUR 1,894 thousand. This acquisition is a result of consistent planning of development of production capacities. Group's heat production capacity using biofuel increased at 19.2 MW after this acquisition, thus a reliability of heat supply to consumers increased additionally.

As of 31 December 2016 the Company and the subsidiarys UAB Kauno Energija NT and UAB Petrašiūnų Katilinė represent the Group (hereinafter – the Group):

Company	Principal place of business	Share held by the Group	Cost of investment	Profit (loss) for the year	Total equity	Main activities
UAB Kauno energija NT	Savanorių Ave. 347, Kaunas	100 percent	1,074	(52)	1,225	Rent
UAB Petrašiūnų katilinė	R. Kalantos g. 49, Kaunas	100 percent	1,894	43	353	Heat production

Legal Regulations

Operations of the Company are regulated by the Heating Law No. IX-1565 of 20 May 2003 of the Republic of Lithuania. According to the Heating Law of the Republic of Lithuania, the Company's activities are licensed and regulated by the State Price Regulation Commission of Energy Resources (hereinafter the Commission).

In 2016 the average number of employees at the Group was 536 (543 employees in 2015). In 2016 the average number of employees at the Company was 523 (540 employees in 2015).

Operational Activity

Group's generation capacities consist of Company's generation capacities and 1 subsidiary boiler-house in Kaunas. Company's generation capacities include Petrašiūnai power plant, 4 boiler-houses in Kaunas integrated network, 7 district boiler-houses in Kaunas district, 1 regional boiler-house in Jurbarkas city, 13 boiler-houses in isolated networks and 27 local gas burned boiler-house in Kaunas city and 8 water heating boiler-houses in Sargėnai catchment.

Total installed heat generation capacities of the Group consist of approx 587 MW (including 39 MW of condensational economizers) and total power generation capacities of the whole Group consist of approx 596 MW (including 39 MW of condensational economizers). Total installed heat generation capacities of Company amount to 568 MW (including 39 MW of condensing economizers). Electricity generation capacities amount up to 8.75 MW. 294.8 MW of heat generation capacities (including 16 MW condensing economizer) and 8 MW of electricity generation capacities are located in Petrašiūnai power plant. 34.8 MW of heat generation capacities (including 2.8 MW condensing economizer) are located in Jurbarkas city. Total Company's power generation capacities consist of approx. 577 MW (including 39 MW of condensing economizers).

The Company accomplished the last (of three) investment litigation with Kauno Termofikacijos Elektrinė (hereinafter – KTE), after Vilnius Court of Commercial Arbitration approved on 29 January 2016 a peaceful agreement concluded on 28 December 2015. Following the terms of agreement the sides agreed to terminate Investment agreement of 31 March 2003, KTE taking obligations to pay compensation for the Company in amount of EUR 2.3 million. The Company has got EUR 1.8 million during 2016, which is disclosed in Note 18, the rest EUR 0.5 million is subject to pay by KTE in equal parts yearly until 28 February 2018. As an additional non-financial compensation according the terms of peaceful agreement KTE disposed to the Company a part of Kaunas centralized heat supplies infrastructure (manifolds building and coherent pipelines, as well as part of technological circuit equipment, necessary to the Company) and the rights of lease of land plot, coherent to the assets disposed. The Company leased out to KTE a technological circuit equipment taken from it for the 25 years period, manifolds building – for 15 years period and subleases land for the 15 year period holding the right for bargain regarding additional term. This juridical litigation with KTE continued from April 2013 and the litigations regarding a non-compliance of investments – from the year 2009. The Company is awarded and has got from KTE in total more than EUR 3.6 million of forfeit in 2011 and 2013 regarding a non-compliance of investment obligations.

In 2012 estimating conditionally high price of the heat bought from KTE, which owns a main Kaunas heat production source, and seeking to contribute to the international liabilities of Lithuania to increase usage of renewable energy sources in heat production, and to reduce Lithuania's dependence from imported fossil fuel and to provide the heat energy at a competitive price, the Company initiated a reconstruction projects of existing boiler-houses, fitting them to work on wooden fuel (wooden chips, waste of deforestation, sawdust).

The Company makes investments estimating economic situation, competition and financing possibilities. Investment plans are approved by shareholders, and regulated and controlled by National Commission for Energy Control and Prices. The Company invested EUR 6,761 thousand in own assets in 2016, and EUR 4,979 thousand in 2015.

2. Accounting principles

2.1. Adoption of new and/or amended IFRS

The following amendments to the existing standards and new interpretation issued by the International Accounting Standards Board (IASB) and adopted by the EU are effective for the current reporting period:

- **Amendments to IFRS 10 "Consolidated Financial Statements", IFRS 12 "Disclosure of Interests in Other Entities" and IAS 28 "Investments in Associates and Joint Ventures"** – Investment Entities: Applying the Consolidation Exception – adopted by the EU on 22 September 2016 (effective for annual periods beginning on or after 1 January 2016),

- **Amendments to IFRS 11 "Joint Arrangements"** – Accounting for Acquisitions of Interests in Joint Operations – adopted by the EU on 24 November 2015 (effective for annual periods beginning on or after 1 January 2016),

- **Amendments to IAS 1 "Presentation of Financial Statements"** – Disclosure Initiative – adopted by the EU on 18 December 2015 (effective for annual periods beginning on or after 1 January 2016),

- **Amendments to IAS 16 "Property, Plant and Equipment" and IAS 38 "Intangible Assets"** – Clarification of Acceptable Methods of Depreciation and Amortisation – adopted by the EU on 2 December 2015 (effective for annual periods beginning on or after 1 January 2016),

- **Amendments to IAS 16 "Property, Plant and Equipment" and IAS 41 "Agriculture"** – Bearer Plants – adopted by the EU on 23 November 2015 (effective for annual periods beginning on or after 1 January 2016),

- **Amendments to IAS 19 "Employee Benefits"** – Defined Benefit Plans: Employee Contributions – adopted by the EU on 17 December 2014 (effective for annual periods beginning on or after 1 February 2015),

- **Amendments to IAS 27 "Separate Financial Statements"** – Equity Method in Separate Financial Statements – adopted by the EU on 18 December 2015 (effective for annual periods beginning on or after 1 January 2016),

- **Amendments to various standards "Improvements to IFRSs (cycle 2010 – 2012)"** resulting from the annual improvement project of IFRS (IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38) primarily with a view to removing inconsistencies and clarifying wording – adopted by the EU on 17 December 2014 (amendments are to be applied for annual periods beginning on or after 1 February 2015),

- **Amendments to various standards "Improvements to IFRSs (cycle 2012 – 2014)"** resulting from the annual improvement project of IFRS (IFRS 5, IFRS 7, IAS 19 and IAS 34) primarily with a view to removing inconsistencies and clarifying wording - adopted by the EU on 15 December 2015 (amendments are to be applied for annual periods beginning on or after 1 January 2016).

The adoption of these amendments to the existing standards has not led to any material changes in the Company's accounting policy.

Standards and amendments to the existing standards issued by IASB and adopted by the EU but not yet effective

At the date of authorisation of these financial statements, the following new standards and amendments to standards issued by IASB and adopted by the EU are not yet effective:

- **IFRS 9 "Financial Instruments"** – adopted by the EU on 22 November 2016 (effective for annual periods beginning on or after 1 January 2018),

- **IFRS 15 "Revenue from Contracts with Customers"** and amendments to IFRS 15 "Effective date of IFRS 15" – adopted by the EU on 22 September 2016 (effective for annual periods beginning on or after 1 January 2018).

New standards and amendments to the existing standards issued by IASB, but not yet adopted by the EU

At present, IFRS as adopted by the EU do not significantly differ from regulations adopted by the International Accounting Standards Board (IASB) except for the following new standards, amendments to the existing standards and new interpretation, which were not endorsed for use in EU (the effective dates stated below is for IFRS in full):

- **IFRS 14 "Regulatory Deferral Accounts"** (effective for annual periods beginning on or after 1 January 2016) – the European Commission has decided not to launch the endorsement process of this interim standard and to wait for the final standard,

- **IFRS 16 "Leases"** (effective for annual periods beginning on or after 1 January 2019),

- **Amendments to IFRS 2 "Share-based Payment"** – Classification and Measurement of Share-based Payment Transactions (effective for annual periods beginning on or after 1 January 2018),

- **Amendments to IFRS 4 "Insurance Contracts"** – Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (effective for annual periods beginning on or after 1 January 2018 or when IFRS 9 "Financial Instruments" is applied first time),

- **Amendments to IFRS 10 "Consolidated Financial Statements" and IAS 28 "Investments in Associates and Joint Ventures"** – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture and further amendments (effective date deferred indefinitely until the research project on the equity method has been concluded),

- **Amendments to IFRS 15 "Revenue from Contracts with Customers"** – Clarifications to IFRS 15 Revenue from Contracts with Customers (effective for annual periods beginning on or after 1 January 2018),

- **Amendments to IAS 7 "Statement of Cash Flows"** – Disclosure Initiative (effective for annual periods beginning on or after 1 January 2017),

- **Amendments to IAS 12 "Income Taxes"** – Recognition of Deferred Tax Assets for Unrealised Losses (effective for annual periods beginning on or after 1 January 2017),

- **Amendments to IAS 40 "Investment Property"** – Transfers of Investment Property (effective for annual periods beginning on or after 1 January 2018),

- **Amendments to various standards "Improvements to IFRSs (cycle 2014 – 2016)"** resulting from the annual improvement project of IFRS (IFRS 1, IFRS 12 and IAS 28) primarily with a view to removing inconsistencies and clarifying wording (amendments to IFRS 12 are to be applied for annual periods beginning on or after 1 January 2017 and amendments to IFRS 1 and IAS 28 are to be applied for annual periods beginning on or after 1 January 2018),

- **IFRIC 22 "Foreign Currency Transactions and Advance Consideration"** (effective for annual periods beginning on or after 1 January 2018).

The adoption of these amendments to the standards will not have significant impact to changes in the Group's and Company's financial statements during the initial adjustment period.

2.2. Statement of Compliance

The financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and interpretations of them. The standards are issued by the International Accounting Standards Board (IASB) and the interpretations by the International Financial Reporting Interpretations Committee (IFRIC).

2.3. Basis of the preparation of financial statements

The financial statements have been prepared on a cost basis, except for certain financial instruments, which are stated at fair value, as explained in the accounting policies below. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

The financial year of the Company and other Group companies coincides with the calendar year.

Items included in the financial statements of the Group and the Company are measured using the currency of the primary economic environment in which they operate (the 'functional currency'). The amounts shown in these financial statements are measured and presented in the local currency of the Republic of Lithuania, Euro (EUR) which is a functional and presentation currency of the Company and its subsidiaries and all values are rounded to the nearest thousands, except when otherwise indicated.

Starting from 1 January 2015 the local currency of the Republic of Lithuania is Euro, the rate of which in regard of other currencies is set daily by European Central Bank. Starting from 2002 till 31 December 2014 local currency was litas which was pegged to Euro at the rate of 3.4528 LTL for 1 Euro and the exchange rates in regard to other currencies was set daily by the Bank of Lithuania.

2.4. Principles of consolidation

Principles of consolidation
The consolidated financial statements of the Group include AB Kauno Energija and its subsidiaries. The financial statements of the subsidiaries are prepared for the same reporting period as the Company. Consolidated financial statements are prepared on the basis of the same accounting principles applied to similar transactions and other events under similar circumstances.

Income and expenses of subsidiaries acquired or disposed of during the year are included in the consolidated statement of Profit (loss) and other comprehensive income from the effective date of acquisition and up to the effective date of disposal, as appropriate. Total comprehensive income of subsidiaries is attributed to the owners of the Company and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Subsidiary is the company which is directly or indirectly controlled by the parent company. The control is normally evidenced when the Group owns, either directly or indirectly, more than 50 percent of the voting rights of a company's share capital or otherwise has power to govern the financial and operating policies of an enterprise so as to benefit from its activities.

Changes in the Group's ownership interests in existing subsidiaries
Changes in the Group's ownership interests in subsidiaries that do not result in the Group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognized directly in equity and attributed to owners of the Company.

When the Group loses control of a subsidiary, the profit or loss on disposal is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets (including goodwill), and liabilities of the subsidiary and any non-controlling interests. When assets of the subsidiary are carried at revalued amounts or fair values and the related cumulative gain or loss has been recognized in other comprehensive income and accumulated in equity, the amounts previously recognized in other comprehensive income and accumulated in equity are accounted for as if the Company had directly disposed of the relevant assets (i.e. reclassified to profit or loss or transferred directly to retained earnings as specified by applicable IFRS). The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under IAS 39 Financial Instruments: Recognition and Measurement or, when applicable, the cost on initial recognition of an investment in an associate or a jointly controlled entity.

2.5. Investments in subsidiaries

Investments in subsidiaries in the Company's Statements of Financial Position are recognized at cost. The dividend income from the investment is recognized in the profit (loss).

The indicators of impairment in IAS 39 are applied to determine whether it is necessary to recognise any impairment loss with respect to the Group's investment in a subsidiary. When necessary, the entire carrying amount of the investment (including goodwill) is tested for impairment in accordance with IAS 36 Impairment of Assets as a single asset by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount. Any impairment loss recognised forms part of the carrying amount of the investment. Any reversal of that impairment loss is recognised in accordance with IAS 36 to the extent that the recoverable amount of the investment subsequently increases.

2.6. Intangible assets

Intangible assets acquired separately
Intangible assets acquired separately are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

Derecognition of intangible assets
An intangible asset is derecognized on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognized in profit or loss when the asset is derecognized.

Licenses
Amounts paid for licenses are capitalised and then amortised over useful life (3 – 4 years).

Software
The costs of acquisition of new software are capitalised and treated as an intangible asset if these costs are not an integral part of the related hardware. Software is amortised over a period not exceeding 3 years.

Costs incurred in order to restore or maintain the future economic benefits of performance of the existing software systems are recognised as an expense for the period when the restoration or maintenance work is carried out.

2.7. Accounting for emission rights

The Group and the Company apply a 'net liability' approach in accounting for the emission rights received. It records the emission allowances granted to it at nominal amount, as permitted by IAS 20 Accounting for Government Grants and Disclosure of Government Assistance.

Liabilities for emissions are recognised only as emissions are made (i.e. provisions are never made on the basis of expected future emissions) and only when the reporting entity has made emissions in excess of the rights held.

When applying the net liability approach, the Group and the Company have chosen a system that measures deficits on the basis of an annual allocation of emission rights.

The outright sale of an emission right is recorded as a sale at the value of consideration received. Any difference between the fair value of the consideration received and its carrying amount is recorded as a gain or loss, irrespective of whether this creates an actual or an expected deficit of the allowances held. When a sale creates an actual deficit an additional liability is recognised with a charge to the profit or loss.

2.8. Property, plant and equipment

Property, plant and equipment are stated at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment losses, if any. Such cost includes the cost of replacing part of such property, plant and equipment when that cost is incurred if the asset recognition criteria are met.

Properties in the course of construction for production, supply or administrative purposes, or for purposes not yet determined, are carried at cost, less any recognized impairment loss. Cost includes professional fees and, for qualifying assets, borrowing costs capitalized in accordance with the Group's and the Company's accounting policy. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Depreciation is recognized so as to write off the cost of assets (other than freehold land and properties under construction) less their residual values over their useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

The useful lives are reviewed annually to ensure that the period of depreciation is consistent with the expected pattern of economic benefits from the items in property, plant and equipment.

Depreciation is computed on a straight-line basis over the following estimated useful lives:

	Years
Buildings	15 – 50
Structures	15 – 70
Machinery and equipment	5 – 20
Vehicles	4 – 10
Equipment and tools	3 – 16

Freehold land is not depreciated.

The Group and the Company capitalizes property, plant and equipment purchases with useful life over one year and an acquisition cost above EUR 144.81.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statement of Profit (loss) and other comprehensive income in the year the asset is derecognized.

Subsequent repair costs are included in the asset's carrying amount, only when it is probable that future economic benefits associated with the item will flow to the Group and the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are recognized in profit or loss in the period in which they are incurred.

Construction-in-progress is stated at cost. This includes the cost of construction, plant and equipment and other directly attributable costs. Construction-in-progress is not depreciated until the relevant assets are completed and put into operation.

2.9. Impairment of property, plant and equipment and intangible assets excluding goodwill

At each statement of financial position date, the Group and the Company reviews the carrying amounts of its property, plant and equipment and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group and the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, Group's and Company's assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss. The Group and the Company has one cash-generating unit for heating business.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit or loss.

2.10. Financial assets

Financial assets are classified as either financial assets at fair value through profit or loss, loans and receivables or available-for-sale financial assets, as appropriate. All purchases and sales of financial assets are recognised on the trade date. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

<u>Effective interest rate method</u>
The effective interest method is a method of calculating the amortized cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.
Income is recognized on an effective interest basis for debt instruments other than those financial assets classified as at FVTPL.

<u>Financial assets at FVTPL</u>
Financial assets are classified as at FVTPL when the financial asset is either held for trading or it is designated as at FVTPL.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling it in the near term; or
- on initial recognition it is part of a portfolio of identified financial instruments that the Group and the Company manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's and the Company's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial assets at FVTPL are stated at fair value, with any gains or losses arising on remeasurement recognized in profit or loss. The net gain or loss recognized in profit or loss incorporates any dividend or interest earned on the financial asset and is included in the 'other gains and losses' line item in the Statement of Profit (loss) and other comprehensive income.

Available-for-sale financial assets (AFS financial assets)

Available-for-sale financial assets are non-derivatives that are either designated as AFS or are not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss.

Listed redeemable notes held by the Group and the Company that are traded in an active market are classified as available-for-sale and are stated at fair value. The Group and the Company also has investments in unlisted shares that are not traded in an active market but that are also classified as available-for-sale financial assets and stated at fair value (because the directors consider that fair value can be reliably measured). Gains and losses arising from changes in fair value are recognized in other comprehensive income and accumulated in the investments revaluation reserve, with the exception of impairment losses, interest calculated using the effective interest method, and foreign exchange gains and losses on monetary assets, which are recognized in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously accumulated in the investments revaluation reserve is reclassified to profit or loss.

Dividends on available-for-sale equity instruments are recognized in profit or loss when the Group's and the Company's right to receive the dividends is established.

The fair value of available-for-sale monetary assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the end of the reporting period. The foreign exchange gains and losses that are recognized in profit or loss are determined based on the amortized cost of the monetary asset. Other foreign exchange gains and losses are recognized 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. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment. Gains or losses are recognized in profit or loss when the asset value decreases or it is amortized.

Interest income is recognized by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

For listed and unlisted equity investments classified as AFS, a significant or prolonged decline in the fair value of the security below its cost is considered to be objective evidence of impairment.

For all other financial assets, including redeemable notes classified as AFS and finance lease receivables, objective evidence of impairment could include:
- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becomes probable that the borrower will enter bankruptcy or financial re-organization; or
- the disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial asset, such as trade receivables, assets that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's and the Company's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 30 days, as well as observable changes in national or local economic conditions that correlate with default on receivables.

<u>Derecognition of financial assets</u>
A financial asset (or, where applicable a part of a financial asset) is derecognised when:
- the rights to receive cash flows from the asset have expired;
- the Group and the Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass through" arrangement; or
- the Group and the Company has transferred their rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group and the Company has transferred its rights to receive cash flows from an asset and has not transferred substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Company's continuing involvement in the asset.

Financial liabilities
A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

2.11. Derivative financial instruments

The Group and the Company uses derivative financial instruments such as interest rate swaps to hedge its interest rate risks. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

Any gains or losses arising from changes in fair value on derivatives during the year are taken directly to the profit (loss) for the period.

The fair value of interest rate swap contracts is determined by the reference to market values for similar instruments.

2.12. Inventories

Inventories are stated at the lower of cost or net realizable value. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale. Costs of inventories are determined on a first-in, first-out (FIFO) basis.

The cost of inventories is net of volume discounts and rebates received from suppliers during the reporting period but applicable to the inventories still held in stock.

2.13. Provisions

Provisions are recognized when the Group and the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group and the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognized as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

2.14. Cash and cash equivalents

Cash includes cash on hand, cash at banks and cash in transit. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, cash with banks, cash in transit, deposits held at call with banks, and other short-term highly liquid investments.

2.15. Employee benefits

Contributions to defined contribution retirement benefit plans are recognized as an expense when employees have rendered service entitling them to the contributions.

The retirement benefit obligation recognized in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognized actuarial gains and losses and unrecognized past service cost, and as reduced by the fair value of plan assets. Any asset resulting from this calculation is limited to unrecognized actuarial losses and past service cost, plus the present value of available refunds and reductions in future contributions to the plan. Actuarial gains and losses are included in Other comprehensive income.

2.16. Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production 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 or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

2.17. Financial liabilities and equity instruments

Classification as debt or equity
Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement and the definitions of a financial liability and an equity instrument.

Equity instruments
An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Group and the Company are recognized at the proceeds received, net of direct issue costs.

Financial liabilities
Financial liabilities are classified as either financial liabilities 'at FVTPL' or 'other financial liabilities'.

Financial liabilities at FVTPL
Financial liabilities are classified as at FVTPL when the financial liability is either held for trading or it is designated as at FVTPL.

Other financial liabilities
Other financial liabilities (including borrowings) are subsequently measured at amortised cost using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Derecognition of financial liabilities
The Group and the Company derecognises financial liabilities when, and only when, the Group's and the Company's obligations are discharged, cancelled or they expire.

2.18. Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term.

The Group and the Company as lessee
Assets held under finance leases are initially recognised as assets of the Group and the Company at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation.

Lease payments are apportioned between finance expenses and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance expenses are recognised immediately in profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's and the Company's general policy on borrowing costs. Contingent rentals are recognised as expenses in the periods in which they are incurred.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

2.19. Grants (deferred income)

Government grants are not recognised until there is reasonable assurance that the Group and the Company will comply with the conditions attaching to them and that the grants will be received.

Government grants are recognised in profit or loss on a systematic basis over the periods in which the Group and the Company recognises as expenses the related costs for which the grants are intended to compensate. Specifically, government grants whose primary condition is that the Group and the Company should purchase, construct or otherwise acquire non-current assets are recognised as deferred revenue in the statement of financial position and transferred to profit or loss on a systematic and rational basis over the useful lives of the related assets.

Grants received in the form of non-current assets or intended for the purchase, construction or other acquisition of non-current assets are considered as asset-related grants. Assets received free of charge are also allocated to this group of grants. The amount of the grants related to assets is recognized as deferred income and is credited to profit or loss in equal annual amounts over the expected useful life of related asset. In the statement of Profit (loss) and other comprehensive income, a relevant expense account is reduced by the amount of grant amortisation.

Assets received free of charge are initially recognised at fair value.

Grants received as a compensation for the expenses or unearned income of the current or previous reporting period, also, all the grants, which are not grants related to assets, are considered as grants related to income. The income-related grants are recognised as used in parts to the extent of the expenses incurred during the reporting period or unearned income to be compensated by that grant.

The balance of unutilised grants is shown in the caption Grants (deferred income) in the balance sheet.

2.20. Income tax

Income tax expense represents the sum of the tax currently payable and deferred tax.

Current tax
The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. Income tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period. In 2016 the income tax applied to the Group and the Company was 15 percent (2015 - 15 percent).

Deferred tax
Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized. Such deferred assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries, except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred income tax assets is reviewed at each statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group and the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax for the period
Current and deferred tax are recognised as an expense or income in profit or loss, except when they relate to items that are recognised outside profit or loss (whether in other comprehensive income or directly in equity), in which case the tax is also recognised outside profit or loss, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is included in the accounting for the business combination.

2.21. Basic and diluted earnings per share

Basic earnings per share are calculated by dividing the net profit attributable to the shareholders by the weighted average of ordinary registered shares issued. There are no instructions reducing earnings per share, there is no difference between the basic and diluted earnings per share.

2.22. Revenue recognition

Revenue is recognised when it is probable that the economic benefits associated with the transaction will flow to the enterprise and the amount of the revenue can be measured reliably. Sales are recognised net of VAT and discounts.

Revenue from sales of heat energy is recognised based on the bills issued to residential and other customers for heating and heating-up of cold water. The customers are billed monthly according to the readings of heat meters.

Revenue from the sale of goods is recognised when all the following conditions are satisfied:
- the Group and the Company has transferred to the buyer the significant risks and rewards of ownership of the goods;
- the Group and the Company retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the Group and the Company; and
- the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Late payment interest income from overdue receivables is recognised upon receipt.

Dividend revenue from investments is recognised when the shareholder's right to receive payment has been established (provided that it is probable that the economic benefits will flow to the Group and the Company and the amount of revenue can be measured reliably).

Interest revenue is recognised when it is probable that the economic benefits will flow to the Group and the Company and the amount of revenue can be measured reliably. Interest revenue is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

The Group's and the Company's policy for recognition of revenue from operating leases is described in Note 2.18 above.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

2.23. Expense recognition

Expenses are recognised on the basis of accrual and revenue and expense matching principles in the reporting period when the income related to these expenses was earned, irrespective of the time the money was spent. In those cases when the costs incurred cannot be directly attributed to the specific income and they will not bring income during the future periods, they are expensed as incurred.

The amount of expenses is usually accounted for as the amount paid or due, excluding VAT. In those cases when a long period of payment is established and the interest is not distinguished, the amount of expenses is estimated by discounting the amount of payment using the market interest rate.

2.24. Foreign currencies

In preparing the financial statements of the individual entities of the Group, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

The presentation currency is euro (EUR). All transactions made in foreign currency are converted into Euros at the official exchange rate determined daily by the European Central Bank. Financial assets and liabilities are converted into Euros at currency rate of creation day of statements of financial state. Gains and losses arising on exchange are included in profit or loss for the period at the moment of its appearance. Income or expenditures arising on exchange when converting financial assets or liabilities into euros are included in profit or loss.

The applicable rates used for principal currencies were as follows:

As of 31 December 2016				**As of 31 December 2015**			
1 EUR	=	1.0453	USD	1 EUR	=	1.09260	USD
1 EUR	=	0.8530	GBP	1 EUR	=	0.73799	GBP

Exchange differences are recognised in profit or loss in the period in which they arise except for:

- exchange differences on foreign currency borrowings relating to assets under construction for future productive use, which are included in the cost of those assets when they are regarded as an adjustment to interest costs on those foreign currency borrowings;
- exchange differences on transactions entered into in order to hedge certain foreign currency risks; and
- exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur (therefore forming part of the net investment in the foreign operation), which are recognised initially in other comprehensive income and reclassified from equity to profit or loss on disposal or partial disposal of the net investment.

2.25. Use of estimates in the preparation of financial statements

The preparation of financial statements requires the management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingencies, at the reporting date. However, uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amount of the asset or liability affected in the future.

<u>Estimates and assumptions</u>
The key assumptions concerning the future and other key sources of estimation uncertainty at the statements of Financial Position date, 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:

Property, plant and equipment – useful life
The key assumptions concerning determination the useful life of property, plant and equipment are as follows: expected usage of the asset, expected physical wear and tear, technical or commercial obsolescence arising from

changes or improvements in the services, legal or similar limits on the use of the asset, such as the expiry dates of related leases.

Property, plant and equipment - fair value measurements and valuation processes
Some of the Group's assets are measured at fair value for financial reporting purposes. In estimating the fair value of an asset, the Group uses market-observable data to the extent it is available. Where Level 1 inputs are not available, the Group engages third party qualified valuers to perform the valuation, if necessary.

Realisable value of inventory
Starting from 2011, the management of the Company forms a 100 percent adjustment to the net realizable value for inventory bought more than one year ago.

Allowances for accounts receivable
The Group and the Company makes allowances for doubtful accounts receivable. Significant judgment is used to estimate doubtful accounts. In estimating doubtful accounts historical and anticipated customer performance are considered. Changes in the economy, industry, or specific customer conditions may require adjustments to the allowance for doubtful accounts recorded in the financial statements.

Deferred Tax Asset
Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

Litigations
The Group and the Company reviews all legal cases for the end of the reporting period and disclose all relevant information in the Note 24.

2.26. Contingencies

Contingent liabilities are not recognised in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is not recognised in the financial statements but disclosed when an inflow of economic benefits is probable.

2.27. Subsequent events

Post-balance sheet events that provide additional information about the Group's and the Company's position at the balance sheet date (adjusting events) are reflected in the financial statements. Post-balance sheet events that are not adjusting events are disclosed in the notes when material.

2.28. Offsetting and comparative figures

When preparing the financial statements, assets and liabilities, as well as revenue and expenses are not set off, except the cases when certain IFRS specifically require such set-off.

2.29. Segments

Operating segments are reported in a manner consistent with the internal reporting provided to the chief-operating decision-maker. The chief operating decision maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Board of Directors that makes strategic decisions.

The activities of the Group and the Company are organised in one operating segment therefore further information on segments has not been disclosed in these financial statements.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

3. Intangible assets

Movements of intangible assets for the current and prior reporting periods are as follows:

	Group	Company
	Patents, licenses	
Cost:		
Balance as of 31 December 2014	**1,584**	**1,585**
Additions	60	59
Disposals and write-offs	(252)	(252)
Transfers from property, plant and equipment	13	13
Balance as of 31 December 2015	**1,405**	**1,405**
Additions	45	45
Disposals and write-offs	(4)	(4)
Transfers from property, plant and equipment	-	-
Balance as of 31 December 2016	**1,446**	**1,446**
Amortisation:	-	-
Balance as of 31 December 2014	**1,509**	**1,510**
Charge for the year	32	31
Disposals and write-offs	(252)	(252)
Balance as of 31 December 2015	**1,289**	**1,289**
Charge for the year	54	54
Disposals and write-offs	(4)	(4)
Balance as of 31 December 2016	**1,339**	**1,339**
Net book value as of 31 December 2014	**75**	**75**
Net book value as of 31 December 2015	**116**	**116**
Net book value as of 31 December 2016	**107**	**107**

Amortisation expenses of intangible assets are included in the operating expenses in the statement of Profit (loss) and other comprehensive income.

As of 31 December 2016 part of the non-current intangible assets of the Group and the Company with the acquisition cost of EUR 1,258 thousand (as of 31 December 2015 – EUR 1,245 thousand) were fully amortised but were still in active use.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

4. Property, plant and equipment

Group	Land and buildings	Structures	Machinery and equipment	Vehicles	Instruments and tools	Construction in progress and prepayments	Investment property	Total
Cost:								
Balance as of 31 December 2014	**15,650**	**146,960**	**38,855**	**1,569**	**10,258**	**12,825**	**382**	**226,499**
Additions	-	-	32	75	357	6,049	-	6,513
Disposals and write-offs	(140)	(34)	(591)	(11)	(98)	-	-	(874)
Reclassifications	1,659	4,582	12,012	136	168	(18,557)	-	-
Transfers to intangible assets	-	-	-	-	-	(13)	-	(13)
Impairment loss(-)	(384)	(31)	(8)	-	-	-	-	(423)
Balance as of 31 December 2015	**16,785**	**151,477**	**50,300**	**1,769**	**10,685**	**304**	**382**	**231,702**
Additions	416	178	1,560	150	713	5,282	-	8,299
Acquisition of subsidiary	1,531	654	4,054	106	10	-	-	6,355
Disposals and write-offs	-	(22)	(383)	(40)	(57)	-	-	(502)
Reclassifications	86	2,547	1,590	9	380	(4,612)	-	-
Transfers to intangible assets	-	-	-	-	-	-	-	-
Impairment loss(-)	-	(97)	-	-	56	-	-	(41)
Balance as of 31 December 2016	**18,818**	**154,737**	**57,121**	**1,994**	**11,787**	**974**	**382**	**245,813**
Accumulated depreciation:								
Balance as of 31 December 2014	**8,657**	**63,566**	**23,622**	**1,309**	**7,166**	**-**	**63**	**104,383**
Charge for the year	343	3,234	2,638	88	784	-	15	7,102
Disposals and write-offs	(86)	(31)	(512)	(11)	(97)	-	-	(737)
Reclassifications	-	(125)	83	-	42	-	-	-
Balance as of 31 December 2015	**8,914**	**66,644**	**25,831**	**1,386**	**7,895**	**-**	**78**	**110,748**
Charge for the year	360	3,087	3,228	87	766	-	5	7,533
Acquisition of subsidiary	254	109	1,016	64	3	-	-	1,446
Disposals and write-offs	-	(22)	(381)	(40)	(56)	-	-	(499)
Reclassifications	-	-	7	-	(7)	-	-	-
Balance as of 31 December 2016	**9,528**	**69,818**	**29,701**	**1,497**	**8,601**	**-**	**83**	**119,228**
Net book value as of 31 December 2014	**6,993**	**83,394**	**15,233**	**260**	**3,092**	**12,825**	**319**	**122,116**
Net book value as of 31 December 2015	**7,871**	**84,833**	**24,469**	**383**	**2,790**	**304**	**304**	**120,954**
Net book value as of 31 December 2016	**9,290**	**84,919**	**27,420**	**497**	**3,186**	**974**	**299**	**126,585**

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Company	Buildings	Structures	Machinery and equipment	Vehicles	Instruments and tools	Construction in progress and prepayments	Total
Cost:							
Balance as of 31 December 2014	**15,296**	**146,964**	**38,702**	**1,353**	**10,203**	**12,825**	**225,343**
Additions	1	-	32	75	357	6,049	6,514
Disposals and write-offs	(140)	(34)	(591)	(11)	(98)	-	(874)
Reclassifications	1,658	4,578	12,016	136	169	(18,557)	-
Transfers to intangible assets	-	-	-	-	-	(13)	(13)
Impairment loss(-)	(384)	(31)	(8)	-	-	-	(423)
Balance as of 31 December 2015	**16,431**	**151,477**	**50,151**	**1,553**	**10,631**	**304**	**230,547**
Additions	-	-	584	134	708	5,290	6,716
Additions from subsidiary	8	-	-	-	-	(8)	-
Disposals and write-offs	-	(22)	(383)	(40)	(57)	-	(502)
Reclassifications	86	2,547	1,586	9	384	(4,612)	-
Transfers to intangible assets	-	-	-	-	-	-	-
Impairment loss(-)	-	(97)	-	-	56	-	(41)
Balance as of 31 December 2016	**16,525**	**153,905**	**51,938**	**1,656**	**11,722**	**974**	**236,720**
Accumulated depreciation:							
Balance as of 31 December 2014	**8,344**	**63,567**	**23,469**	**1,066**	**7,111**	**-**	**103,557**
Charge for the year	342	3,235	2,638	88	783	-	7,086
Disposals and write-offs	(87)	(31)	(512)	(11)	(96)	-	(737)
Reclassifications	-	(127)	84	-	43	-	-
Balance as of 31 December 2015	**8,599**	**66,644**	**25,679**	**1,143**	**7,841**	**-**	**109,906**
Charge for the year	330	3,076	3,126	105	769	-	7,406
Charge for the year from subsidiary	6	-	-	-	-	-	6
Disposals and write-offs	-	(22)	(381)	(40)	(56)	-	(499)
Reclassifications	-	-	7	-	(7)	-	-
Balance as of 31 December 2016	**8,935**	**69,698**	**28,431**	**1,208**	**8,547**	**-**	**116,819**
Net book value as of 31 December 2014	**6,952**	**83,397**	**15,233**	**287**	**3,092**	**12,825**	**121,786**
Net book value as of 31 December 2015	**7,832**	**84,833**	**24,472**	**410**	**2,790**	**304**	**120,641**
Net book value as of 31 December 2016	**7,590**	**84,207**	**23,507**	**448**	**3,175**	**974**	**119,901**

The depreciation charge of the Group's and Company's property, plant and equipment in 2016 amounts to EUR 6,451 thousand and EUR 6,370 thousand, respectively (as of 31 December 2015 – EUR 6,238 thousand and EUR 6,221 thousand respectively). The amounts of EUR 6,433 thousand and EUR 6,330 thousand (as of 31 December 2015 – EUR 6,201 thousand and EUR 6,201 thousand respectively) the depreciation expenses were included into the expenses in statements of Profit (loss) and other comprehensive income, the remaining amounts 18 thousand and EUR 40 thousand (as of 31 December 2015 – EUR 37 thousand and EUR 20 thousand) were included into other activity expenses in statements of Profit (loss) and other comprehensive income.

As of 31 December 2016 part of the property, plant and equipment of the Group with acquisition cost of EUR 51,372 thousand (EUR 42,036 thousand as of 31 December 2015) and the Company – EUR 51,210 thousand were fully depreciated (EUR 41,918 thousand as of 31 December 2015), but were still in active use.

As of 31 December 2016 and as of 31 December 2015 the major part of the Group's and Company's construction in progress consisted of reconstruction and overhaul works of boiler-houses equipment and heat supply networks.

As of 31 December 2016 the sum of the Group and the Company contractual commitments for the acquisition of property, plant and equipment amounted to EUR 15,288 thousand (as of 31 December 2015 – EUR 2,945 thousand).

As of 31 December 2016 property, plant and equipment of the Group with the net book value of EUR 55,788 thousand (EUR 57,556 thousand as of 31 December 2015) and the Company of EUR 51,021 thousand (EUR 57,556 thousand as of 31 December 2015) was pledged to banks as a collateral for loans (Note 11).

The sum of Group's and Company's capitalized interest was equal to EUR 10 thousand in 2016 (in 2015 – EUR 9 thousand). The capitalization rate varied from 0.95 percent to 1.29 percent in 2016 (in 2015 – from 0.15 percent to 4.51 percent).

As of 31 December 2016 the Group and the Company accounted for assets, not yet ready for use, amounting to EUR 416 thousand in the category Equipment and tools (EUR 152 thousand as of 31 December 2015).

The Group and The Company use assets in their operations, acquired by leasing. The acquisition cost of this asset was EUR 136 thousand at December 31, 2016 (EUR 142 thousand in 2015 respectively), and the net book value respectively EUR 112 thousand and 109 thousand. Unpaid part of it is disclosed in Note 12.

5. Non-current accounts receivable

Long-term loans granted to the employees of the Company for the period from the year 1997 until December 31, 2017 are non-interest bearing. These loans are accounted for at discounted value as of 31 December 2015 using 3.7 percent interest rate. In 2015 effect of reversed discounting amounted to EUR 1 thousand .The reversal of discounting is accounted in the change of depreciation of realisable value of receivables line in the Group's and Company's statements of Profit (loss) and other comprehensive income.

As of 31 December 2016 and as of 31 December 2015 the repayment term of non-current accounts receivable is not yet due and valuation allowance is not determined.

6. Other financial assets

Financial assets held for sale consists of ordinary shares are unquoted. On 31 December 2015 the decrease of the value of other financial assets by EUR 27 thousand was determined. This decrease is included in Group's and Company's statements of Profit (loss) and other comprehensive income Financial assets and short-term investments Impairment article.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

7. Inventories

	Group		Company	
	As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
Technological fuel	1,187	1,078	1,120	1,078
Spare parts	446	385	444	385
Materials	435	483	434	479
	2,068	1,946	1,998	1,942
Less: write-down to net realisable value of inventory at the end of the period	(1,582)	(1,657)	(1,582)	(1,657)
Carrying amount of inventories	**486**	**289**	**416**	**285**

As of 31 December 2016 Group's and Company's amounted to EUR 1,582 thousand (as of 31 December 2015 – EUR 1,657 thousand) write-down to net realisable value of inventories. Changes in the Write-down to net realisable value of inventories for the 2016 and for the year 2015 were included into change in write-down to net realisable value of inventories caption in the Group's and the Company's statements of Profit (loss) and other comprehensive income. Reduction of value of the stocks, value of which as at 31 December 2016 amounted to EUR 56 thousand and for which the reduction of value has been formed, has been restored and they were reclassified in the group of instruments and tools of the article of property, plant and equipment.

8. Current accounts receivable

	Group		Company	
	As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
Trade receivables, gross	21,372	21,385	21,410	21,433
Less: impairment of doubtful receivables	(11,255)	(12,410)	(11,293)	(12,458)
	10,117	**8,975**	**10,117**	**8,975**

Change in impairment of doubtful receivables in 2016 and 2015 is included into the caption of write-offs and change in allowance for accounts receivables in the Group's and the Company's statements of Profit (loss) and other comprehensive income.

Impairment of doubtful receivables assessed on the basis of historical experience, using the following percentages:

	Amount not past due	Amounts past due					
		Less than 60 days	60 - 150 days	151 - 240 days	241 - 360 days	More than 360 days	More than 720 days
2016	5%	20%	50%	60%	80%	90%	100%
2015	5%	20%	50%	60%	80%	90%	100%

Movements in the allowance for impairment of the Group's and the Company's receivables were as follows:

	Group	Company
Balance as of 31 December 2014	**12,774**	**12,825**
Additional allowance formed	(233)	(236)
Write-off	(131)	(131)
Balance as of 31 December 2015	**12,410**	**12,458**
Additional allowance formed	(825)	(835)
Write-off	(330)	(330)
Balance as of 31 December 2016	**11,255**	**11,293**

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

In 2016 the Group and the Company wrote off EUR 330 thousand and EUR 330 thousand of bad debts respectively (in 2015 – EUR 131 thousand and EUR 131 thousand). In 2016 the Group recovered EUR 5 thousand and the Company – EUR 5 thousand (in 2015 the Group and the Company – EUR 9 thousand) of doubtful receivables, which were written off in the previous periods.

The ageing analysis of the Group's net value of trade receivables as of 31 December 2016 and 31 December 2015 is as follows:

	Trade receivables not past due	Trade receivables past due					
		Less than 60 days	60 - 150 days	151 - 240 days	241 - 360 days	More than 360 days	Total
2016	8,312	996	194	153	171	291	10,117
2015	7,225	849	177	175	180	369	8,975

The ageing analysis of the Company's net value of trade receivables as of 31 December 2016 and 31 December 2015 is as follows:

	Trade receivables not past due	Trade receivables past due					
		Less than 60 days	60 - 150 days	151 - 240 days	241 - 360 days	More than 360 days	Total
2016	8,312	996	194	153	171	291	10,117
2015	7,225	849	177	175	180	369	8,975

Trade receivables are non-interest bearing and the payment terms are usually 30 days or agreed individually.

Other Group's and the Company's receivables consisted of:

	Group		Company	
	As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
Taxes	228	165	221	161
Other receivables	1,073	961	1,129	1,021
Less: value impairment of doubtful receivables	(300)	(267)	(366)	(336)
	1,001	**859**	**984**	**846**

Movements in the allowance for impairment of the Group's and the Company's other receivables were as follows:

	Group	Company
Balance as of 31 December 2014	**173**	**251**
Additional allowance formed	97	88
Write-off	(3)	(3)
Balance as of 31 December 2015	**267**	**336**
Additional allowance formed	33	30
Write-off	-	-
Balance as of 31 December 2016	**300**	**366**

As of 31 December 2016 and 31 December 2015 the Group's and the Company's other receivables amounted receivable from state taxes, compensations from municipalities for low income families, receivables from sold inventories (metals, heating equipment) and services supplied (maintenance of manifolds and similar services).

The ageing analysis of the Group's net value of other receivables (excluding taxes) as of 31 December 2016 and 31 December 2015 is as follows:

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

	Other receivables not past due	Other receivables past due					
		Less than 60 days	60 - 150 days	151 - 240 days	241 - 360 days	More than 360 days	Total
2016	535	191	23	13	4	7	773
2015	335	170	17	6	3	163	694

The ageing analysis of the Company's net value of other receivables (excluding taxes) as of 31 December 2016 and 31 December 2015 is as follows:

	Other receivables not past due	Other receivables past due					
		Less than 60 days	60 - 150 days	151 - 240 days	241 - 360 days	More than 360 days	Total
2016	525	191	23	13	4	7	763
2015	326	170	17	6	3	163	685

The Group's and the Company's other receivables are non-interest bearing and the payment terms are usually 30 – 45 days.

According to the management opinion, there are no indications as of the reporting date that the debtors will not meet their payment obligations regarding trade receivables and other receivables that are neither impaired nor past due.

9. Cash and cash equivalents

	Group		Company	
	As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
Cash in transit	396	196	396	196
Cash at bank	5,875	2,328	5,783	2,315
Cash on hand	14	7	14	7
	6,285	**2,531**	**6,193**	**2,518**

The Group's accounts in banks amounting to EUR 4,977 thousand as of 31 December 2016 (31 December 2015 – EUR 1,853 thousand) and the Company's to EUR 4,890 thousand as of 31 December 2016 (31 December 2015 – EUR 1,853 thousand) are pledged as collateral for the loans (Note 11).

10. Reserves

<u>Legal and other reserves</u>
A legal reserve is a compulsory reserve under Lithuanian legislation. Annual transfers of not less than 5 percent of net profit calculated in accordance with IFRS are compulsory until the reserve reaches 10 percent of the share capital. The legal reserve cannot be distributed as dividends but can be used to cover any future losses.

On 28 April 2015 the Company annulled by the decision of shareholders other reserves (EUR 521 thousand), transferred EUR 613 thousand from retained earnings to legal reserve and EUR 713 thousand to other reserves. Reserves were formed for investments – EUR 413 thousand, for support – EUR 200 thousand and for maintenance of heat units – EUR 100 thousand.

On 28 April, 2016 the Company annulled other reserves (EUR 713 thousand) by the decision of shareholders, EUR 227 thousand transferred from retained earnings to legal reserve and EUR 2,977 thousand to other reserves. Reserve was formed for long-term loan repayment EUR 2,435 thousand for investments EUR 472 thousand, for support – EUR 50 thousand and for maintenance of heat units – EUR 20 thousand.

11. Borrowings

Terms of repayment of non-current borrowings are as follows:

	Group		Company	
	As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
Non-current borrowings:	**19,559**	**19,481**	**19,559**	**19,481**
Payable in 2 to 5 years	9,605	8,654	9,605	8,654
Payable in more than 5 years	9,954	10,827	9,954	10,827
Current portion of non-current borrowings (except leasing which) is disclosed in Note 12)	6,212	2,402	2,809	2,402
	25,771	**21,883**	**22,368**	**21,883**

Average of interest rates (in percent) of borrowings weighted outstanding at the year-end were as follows:

	Group		Company	
	As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
Current borrowings	0.00	0.00	0.00	0.00
Non-current borrowings	2.27	2.58	2.44	2.58

The Group detailed information on loans as of 31 December 2016:

	Credit institution	Date of contract	Currency	Currency sum, thousand	Sum EUR thousand	Term of maturity	Balance as of 31.12.2016 EUR thousand	A part of 2016, EUR thousand
1	Nordea*	22/08/2012	EUR	3,403	3,403	29/04/2022	3,403	3,403
2	AB DNB Bank	14/11/2007	EUR	576	576	31/12/2016	-	-
3	MF Lithuania***	09/04/2010	EUR	2,410	2,410	15/03/2034	1,685	94
4	MF Lithuania***	26/10/2010	EUR	807	807	15/03/2034	693	38
5	MF Lithuania***	02/09/2011	EUR	1,672	1,672	01/09/2034	1,564	87
6	AB SEB Bank	03/06/2013	LTL	2,760	799	30/06/2020	466	133
7	AB SEB Bank	03/06/2013	LTL	4,240	1,228	30/06/2020	712	204
8	AB SEB Bank	10/09/2013	LTL	5,200	1,506	30/09/2020	941	251
9	Nordea*	27/09/2013	LTL	1,300	377	30/09/2020	27	8
10	MF Lithuania***	15/01/2014	EUR	793	793	01/12/2034	749	41
11	AB SEB Bank	31/03/2014	LTL	5,400	1,564	15/01/2021	1,050	261
12	MF Lithuania***	31/03/2014	EUR	7,881	7,881	01/12/2034	7,444	413
13	AB SEB Bank	09/03/2015	EUR	579	579	28/02/2022	37	37
14	AB SEB Bank	09/03/2015	EUR	579	579	28/02/2022	33	33
15	OP Corporate**	02/12/2015	EUR	4,842	4,842	02/12/2022	4,150	692
16	AB SEB Bank	09/05/2016	EUR	1,000	1,000	30/04/2021	867	200
17	AB SEB Bank	09/05/2016	EUR	579	579	30/04/2023	56	56
18	Nordea*	25/10/2016	EUR	1,894	1,894	29/09/2023	1,894	261
19	AB SEB Bank	22/12/2016	EUR	4,127	4,127	30/11/2024	-	-
							25,771	**6,212**

* Nordea Bank AB. Lithuanian branch, ** OP Corporate Bank Plc Lithuanian branch, *** Ministry of Finance of the Republic of Lithuania;

The Company detailed information on loans as of 31 December 2016:

	Credit institution	Date of contract	Currency	Currency sum, thousand	Sum EUR thousand	Term of maturity	Balance as of 31.12.2016 EUR thousand	A part of 2016, EUR thousand
1	AB DNB Bank	14/11/2007	EUR	576	576	31/12/2016	-	-
2	MF Lithuania***	09/04/2010	EUR	2,410	2,410	15/03/2034	1,685	94
3	MF Lithuania***	26/10/2010	EUR	807	807	15/03/2034	693	38
4	MF Lithuania***	02/09/2011	EUR	1,672	1,672	01/09/2034	1,564	87
5	AB SEB Bank	03/06/2013	LTL	2,760	799	30/06/2020	466	133
6	AB SEB Bank	03/06/2013	LTL	4,240	1,228	30/06/2020	712	204
7	AB SEB Bank	10/09/2013	LTL	5,200	1,506	30/09/2020	941	251
8	Nordea*	27/09/2013	LTL	1,300	377	30/09/2020	27	8
9	MF Lithuania***	15/01/2014	EUR	793	793	01/12/2034	749	41
10	AB SEB Bank	31/03/2014	LTL	5,400	1,564	15/01/2021	1,050	261
11	MF Lithuania***	31/03/2014	EUR	7,881	7,881	01/12/2034	7,444	413
12	AB SEB Bank	09/03/2015	EUR	579	579	28/02/2022	37	37
13	AB SEB Bank	09/03/2015	EUR	579	579	28/02/2022	33	33
14	OP Corporate**	02/12/2015	EUR	4,842	4,842	02/12/2022	4,150	692
15	AB SEB Bank	09/05/2016	EUR	1,000	1,000	30/04/2021	867	200
16	AB SEB Bank	09/05/2016	EUR	579	579	30/04/2023	56	56
17	Nordea*	25/10/2016	EUR	1,894	1,894	29/09/2023	1,894	261
18	AB SEB Bank	22/12/2016	EUR	4,127	4,127	30/11/2024	-	-
							22,368	**2,809**

* Nordea Bank AB. Lithuanian branch, ** OP Corporate Bank Plc Lithuanian branch, *** Ministry of Finance of the Republic of Lithuania;

The immovable property (Note 4), bank accounts (Note 9) and land lease right of the Group and the Company were pledged as collateral for the borrowings.

12. Finance lease obligations

The assets leased by the Group and the Company under finance lease contracts mainly consist of vehicles. The terms of financial lease are 3 years. The finance lease agreement is in EUR.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Future minimal lease payments were:

	Group		Company	
	As of 31 December 2016	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
Within one year	-	-	-	-
From one to five years	80	70	80	70
Total financial lease obligations	80	70	80	70
Interest	(2)	(2)	(2)	(2)
Present value of financial lease obligations	**78**	**68**	**78**	**68**
Financial lease obligations are accounted for as:				
- current	40	34	40	34
- non-current	38	34	38	34

13. Grants (deferred income)

	Group		Company	
	As of 31 December 2016	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
Balance at the beginning of the reporting period	**16,761**	**13,764**	**16,761**	**13,764**
Received during the year	1,798	3,863	465	3,863
Amortisation	(1,090)	(866)	(1,050)	(866)
Balance at the end of the reporting period	**17,469**	**16,761**	**16,176**	**16,761**

On 22 October 2012 the Group signed the agreement on the financing and administration of the project "Construction of boiler-house in Kaunas, installing two biofuel burned boilers at capacity of 8 MW each together with condensational economizer", according to which the Group will be receiving financing from the European Regional Development Fund in the amount of EUR 1,738 thousand after terms and conditions of the agreement are fulfilled. As of 31 December 2016 financing in amount of EUR 1,333 thousand has been received. The project is accomplished.

On 4 October 2015 the Group and the Company signed an agreement with the Lithuanian Environmental Investments Fund (LEIF) regarding financing for the project "Reconstruction of Šilkas boiler-house, replacing depreciated boiler with the new one" rendering subsidy from the Climate Change Special Programme, under which a financing in amount of EUR 150 thousand is allocated for the Company. As at 31 December 2016 financial support in amount of EUR 150 thousand has been received. The project is accomplished.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The modernisation of main pipeline 3Ž of Kaunas integrated network", according to which a financing in amount of EUR 450 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled. EUR 450 thousand are accounted in Group's and Company's other receivables line.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The modernisation of main pipeline 6T of Kaunas integrated network", according to which a financing in amount of EUR 184 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The reconstruction of Kaunas integrated network in Eiguliai catchment" according to which a financing in amount of EUR 894 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The modernisation of main pipeline 1T of Kaunas integrated network", according to which a financing in amount of EUR 967 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The reconstruction of Kaunas integrated network in Kalniečiai catchment" according to which a financing in amount of EUR 905 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The modernisation of main pipeline 4T of Kaunas integrated network", according to which a financing in amount of EUR 447 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The reconstruction of heat supply network built from "Pergalė" boiler-house" according to which a financing in amount of EUR 449 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The reconstruction of Kaunas integrated network in P. Lukšio str.", according to which a financing in amount of EUR 983 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

On 29 December 2016 the Group and the Company signed the agreement on the financing and administration of the project "The reconstruction of main pipeline 2Ž of Kaunas integrated network", according to which a financing in amount of EUR 548 thousand is allocated to the Company from the European Regional Development Fund after terms and conditions of the agreement are fulfilled.

14. Employee benefit liability

According to Lithuanian legislation and the conditions of the collective employment agreement, each employee of the Group and the Company is entitled to 1 - 6 months' salary payment when leaving the job at or after the start of the pension period and at the age of 40, 50 or 60 years, and having not less than15 years of work experience in the Company – jubilee gift of the value fixed in the collective employment agreement. The Group's and the Company's total employee benefit liability is stated below:

	Group		Company	
	2016	**2015**	**2016**	**2015**
Employee benefit liability at the beginning of the year	**891**	**885**	**891**	**885**
Paid	(111)	(135)	(111)	(135)
Formed	551	141	548	141
Employee benefit liability at the end of the year	**1,331**	**891**	**1,328**	**891**
Non-current employee benefit liability	1,069	585	1,066	585
Current employee benefit liability	262	306	262	306

During the 2016 total amount of the benefit paid to the employees by the Group amounted to EUR 111 thousand (in 2015 – EUR 135 thousand), and by the Company – EUR 111 thousand (in 2015 – EUR 135 thousand) and are included in the caption of salaries and social security expenses in the Group's and the Company's statements of Profit (loss) and other comprehensive income.

The principal assumptions used in determining pension benefit obligation for the Group's and the Company's plan is shown below:

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

	As of 31 December 2016	As of 31 December 2015
Discount rate	0.31 percent	4.0 percent
Employee turnover rate	3.37 percent	18.9 percent
Expected average annual salary increases	3.0 percent	3.0 percent

15. Derivative financial instruments

On 16 December 2016, the Group concluded an interest rate swap agreement. For the period from 12 December 2016 to 29 April 2022 the Group set a fixed interest rate at 0.21 % for a floating interest rate at 6-month EURIBOR. The nominal amount of the transaction was EUR 3,403 thousand as at 31 December 2016. Market value of swap agreement as of 31 December 2016 amounted to EUR 34 thousand. 31 December 2015 the Group and Company did not have valid transactions concerning derivative financial instruments.

16. Sales income

The Group's and the Company's activities are heat supplies, maintenance of manifolds, electricity production and other activities. Starting from the year 2010 a part of inhabitants chose the Company as the hot water supplier. Those activities are inter-related, so consequently for management purposes the Group's and the Company's activities are organised as one main segment – heat energy supply. The Group's and the Company's sales income according to the activities are stated below.

	Group		Company	
	2016	2015	2016	2015
Heat supplies	58,004	57,396	58,013	57,404
Hot water supplies	2,611	2,569	2,611	2,569
Maintenance of manifolds	228	226	228	226
Maintenance of heat and hot water systems	9	21	10	10
Electric energy	38	253	38	253
Maintenance of hot water meters	288	260	288	260
Sale of an emission right	-	-	-	11
	61,178	**60,725**	**61,188**	**60,733**

17. Other expenses

	Group		Company	
	2016	2015	2016	2015
Cash collection expenses	171	207	171	207
Equipment verification and inspection	542	545	542	545
Maintenance of manifolds	394	394	394	394
Debts collection expenses	54	54	54	54
Sponsorship	94	93	94	93
Consulting expenses	109	87	109	87
Customer bills issue and delivery expenses	139	126	139	126
Communication expenses	48	47	48	47
Employees related expenses	89	89	89	89
Insurance	67	75	65	75
Long term assets maintenance and related services	77	70	77	70
Membership fee	78	83	78	83
Transport expenses	137	129	137	129
Advertising expenses	48	43	48	43
Audit expenses	14	20	14	20
Rent of equipment and machinery	14	16	14	16
Other expenses	845	425	834	425
	2,920	**2,503**	**2,907**	**2,503**

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

18. Other activities income and expenses

	Group 2016	Group 2015	Company 2016	Company 2015
Income from other operating activities				
Miscellaneous services	387	453	280	375
Materials sold	4	37	4	37
Gain from sale of non-current assets	1	68	1	68
Damage compensation	1,835	-	1,835	-
Other	61	39	61	39
	2,288	**597**	**2,181**	**519**
Expenses from other operating activities				
Cost of miscellaneous services	(236)	(268)	(161)	(191)
Cost of materials sold	(1)	(68)	(1)	(68)
Write off of non-current assets	-	(84)	-	(84)
Other	(69)	(29)	(69)	(29)
	(306)	**(449)**	**(231)**	**(372)**

19. Other interest and similar income

	Group 2016	Group 2015	Company 2016	Company 2015
Interest from late payment of accounts receivable	210	264	210	264
Other	-	-	3	-
	210	**264**	**213**	**264**

20. Financial assets and short-term investments impairment, interest and other similar expenses

	Group 2016	Group 2015	Company 2016	Company 2015
Interest on bank loans and overdrafts	(557)	(650)	(541)	(650)
Calculation of the value of shares	-	(98)	-	(98)
Penalties	-	(28)	-	(28)
Long-term financial assets impairment	-	(27)	-	(27)
Change in fair value of derivative financial instruments	(17)	-	-	-
	(574)	**(803)**	**(541)**	**(803)**

21. Income tax

The recorded income tax for the year can be reconciled with the theoretical calculated income tax, which is computed by applying the standard income tax rate to profit before taxes as follows:

	Group 2016	Group 2015	Company 2016	Company 2015
Profit before tax after the accumulation of employee benefit liability	7,725	5,165	7,666	5,184
Income tax (expenses) calculated at statutory rate	(1,159)	(775)	(1,150)	(778)
Permanent differences and impact of valuation allowance of deferred income tax asset	391	119	385	122
Income tax (expenses) reported in the statement of comprehensive income	(768)	(656)	(765)	(656)
Effective rate of income tax (percent)	**9.94**	**12.70**	**9.98**	**12.65**

	Group		Company	
	2016	**2015**	**2016**	**2015**
Components of the income tax expense				
Current income tax for the reporting year	(2)	(9)	1	(9)
Deferred income tax (expenses)	(766)	(647)	(766)	(647)
Income tax (expenses) recorded in the statement of comprehensive income	**(768)**	**(656)**	**(765)**	**(656)**

As of 31 December 2016 and 31 December 2015 deferred income tax asset and liability were accounted for by applying 15 percent rate. All changes in deferred tax are reported in the Group's and the Company's the statement of Profit (loss) and other comprehensive income.

As of 31 December deferred income tax consists of:

	Group		Company	
	2016	**2015**	**2016**	**2015**
Net deferred income tax asset				
Tax loss carried forward	2,841	2,595	2,841	2,595
Accruals	222	151	222	151
The change in value of financial assets	19	4	19	4
Deferred income tax asset	**3,082**	**2,750**	**3,082**	**2,750**
Deferred income tax liability				
Differences of depreciation	(7,323)	(6,222)	(7,323)	(6,222)
Investment relief	(28)	(31)	(28)	(31)
Revaluation of the assets transferred to subsidiary	-	-	(192)	(192)
Deferred income tax liabilities	**(7,351)**	**(6,253)**	**(7,543)**	**(6,445)**
Deferred income tax, net	**(4,269)**	**(3,503)**	**(4,461)**	**(3,695)**

Deferred income tax assets on tax losses carried forward have been recognised in full amount as the Group's and the Company's management believes it will be realised in the foreseeable future, based on taxable profit forecasts.

At 31 December unrecognized deferred tax assets of the Group and the Company consisted of:

	Group		Company	
	2016	**2015**	**2016**	**2015**
Allowance for trade receivables	1,688	1,862	1,694	1,869
Property, plant and equipment depreciation	39	32	39	32
Allowance for other accounts receivable	38	33	50	45
Impairment for the investment into subsidiary	-	-	122	122
Accruals	(3)	86	(3)	86
Unrecognized deferred tax asset, net	**1,762**	**2,013**	**1,902**	**2,154**

22. Basic and diluted earnings (loss) per share

Calculations of the basic and diluted earnings per share of the Group are presented below:

	Group		Company	
	2016	**2015**	**2016**	**2015**
Net profit	6,957	4,509	6,901	4,528
Number of shares (thousand), opening balance	42,802	42,802	42,802	42,802
Number of shares (thousand), closing balance	42,802	42,802	42,802	42,802
Average number of shares (thousand)	42,802	42,802	42,802	42,802
Basic and diluted earnings per share (EUR)	0.16	0.11	0.16	0.11

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

23. Financial assets and liabilities and risk management

Credit risk

The Group and the Company do not have any credit concentration risk because they work with a large number of customers.

Number of customers	**Group**		**Company**	
	As of 31 December 2016	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
Individuals	114,455	114,493	114,455	114,494
Other legal entities	2,300	2,159	2,300	2,159
Legal entities financed from municipalities' and state budget	683	591	683	591
	117,438	**117,243**	**117,438**	**117,244**

Trade receivables of the Group and the Company by the customer groups:

	Group		**Company**	
	As of 31 December 2016	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
Individuals	8,123	7,370	8,123	7,370
Other legal entities	1,202	934	1,202	934
Legal entities financed from municipalities' and state budget	792	671	792	671
	10,117	**8,975**	**10,117**	**8,975**

Considering trade and other accounts receivables, the terms of which is still not expired and their impairment as of date of financial statements is not determined, according to Management opinion there is no indications that debtors will not fulfil their payment liabilities, because a balance of receivables are controlled constantly. The Group and the Company considers that maximum risk is equal to the sum of receivables from buyers and other receivables, less recognized impairment losses as of the date of balance sheet (note 8).

Cash and cash equivalents in banks, which were evaluated in accordance with long-term borrowing ratings*:

	Group		**Company**	
	As of 31 December 2016	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
AA-	2,202	717	2,110	704
A+	3,510	1,587	3,510	1,587
A	98	6	98	6
Bank with no rating attributed	65	18	65	18
	5,875	**2,328**	**5,783**	**2,315**

*- external credit ratings set by *Fitch Ratings* agency.

The Group and the Company do not guarantee obligations of the other parties in 2015.

On November 28, 2016 the Company provided guarantee in amount of EUR 3,913 thousand to Nordea Bank AB regarding liabilities of subsidiary UAB Petrašiūnų Katilinė to this bank according to credit agreement concluded on August 22, 2012 for the amount of EUR 3,403 thousand. On November 28, 2016 the Company provided guarantee in amount of EUR 95 thousand to Nordea Bank AB regarding liabilities of subsidiary UAB Petrašiūnų Katilinė to this bank according to transaction of derivative financial instruments, described in Note 15.

With respect to credit risk arising from the other financial assets of the Group and the Company, which comprise cash and cash equivalents and available-for-sale financial investments, the Group's and the Company's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Interest rate risk

All of the borrowings of the Group and the Company, except those loans signed with Ministry of Finance of the Republic of Lithuania, are at variable interest rates. Therefore the Group and the Company faces an interest rate risk. In the year 2016 and 2015 the Group and the Company had not been entered into valid interest rate swap agreements in order to manage variable rate risk.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates (increase and decrease in basis points was determined based on Lithuanian economic environment and the Group's and the Company's historical experience), with all other variables held constant, of the Group's and the Company's profit before tax (estimating debts with floating interest rate). There is no impact on the Group's and the Company's equity, other than current year profit impact.

	Increase/decrease in basis points	**Effect on income tax**
2016		
EUR	50	(8)
EUR	(50)	8
2015		
EUR	50	(7)
EUR	(50)	7

Liquidity risk

The Group's and the Company's policy is to maintain sufficient cash and cash equivalents or have available funding through an adequate amount of overdrafts and committed credit facilities to meet its commitments at a given date in accordance with its strategic plans. The Group's liquidity (total current assets / total current liabilities) and quick ((total current assets – inventories) / total current liabilities) ratios as of 31 December 2016 were 1.18 and 1.14, respectively (1.10 and 1.07 as of 31 December 2015). The Company's liquidity and quick ratios as of 31 December 2016 were 1.48 and 1.44, respectively (1.10 and 1.07 as of 31 December 2015). As at 31 December 2016 Groups' and Company's net working capital was plius respectively (EUR 2,749 thousand and EUR 5,857 thousand) (as at 31 December 2015 it was also plius – EUR 1,179 thousand and EUR 1,162 thousand).

In order to increase liquidity the Group and the Company implemented the following action plan:

- Considering the current situation the Group and the Company started to reduce its expenses;
- The Company increased heat production in its own effective production sources;
- The new measures of reducing losses in production and supply were implemented;
- The Company seeks to shorten money cycle increasing turnover of purchaser's debts and reducing turnover of debts to suppliers;
- Organized refinance of part of financial liabilities.

Unsecured bank overdraft and bank loan facilities:

	Group		**Company**	
	As of 31 December 2016	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
Amount used	-	-	-	-
Amount unused	2,896	4,344	2,896	4,344
	2,896	**4,344**	**2,896**	**4,344**

The table below summarises the maturity profile of the Group's financial liabilities as of 31 December 2016 and as of 31 December 2015 based on contractual undiscounted payments (scheduled payments including interest):

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

	Less than 3 months	From 4 to 12 months	2 to 5 years	More than 5 years	Total
Interest bearing loans and borrowings	1,106	5,718	11,274	12,069	30,167
Trade payables	7,136	58	18	-	7,212
Balance as of 31 December 2016	**8,242**	**5,776**	**11,292**	**12,069**	**37,379**

	Less than 3 months	From 4 to 12 months	2 to 5 years	More than 5 years	Total
Interest bearing loans and borrowings	724	2,260	10,430	12,041	25,455
Trade payables	7,744	34	26	-	7,804
Balance as of 31 December 2015	**8,468**	**2,294**	**10,456**	**12,041**	**33,259**

The table below summarises the maturity profile of the Company's financial liabilities, as of 31 December 2016 and as of 31 December 2015 based on contractual undiscounted payments (scheduled payments including interest):

	Less than 3 months	From 4 to 12 months	2 to 5 years	More than 5 years	Total
Interest bearing loans and borrowings	810	2,566	11,274	12,069	26,719
Trade payables	7,248	58	18	-	7,324
Balance as of 31 December 2016	**8,058**	**2,624**	**11,292**	**12,069**	**34,043**

	Less than 3 months	From 4 to 12 months	2 to 5 years	More than 5 years	Total
Interest bearing loans and borrowings	724	2,260	10,430	12,041	25,455
Trade payables	7,743	34	26	-	7,803
Balance as of 31 December 2015	**8,467**	**2,294**	**10,456**	**12,041**	**33,258**

Trade payables

Trade payables of the Group and the Company by supplier groups:

	Group		Company	
	As of 31 December 2016	As of 31 December 2015	As of 31 December 2016	As of 31 December 2015
For heat purchased	4,375	4,989	4,375	4,989
Contractors	649	399	649	399
Other suppliers	2,188	2,416	2,300	2,415
	7,212	**7,804**	**7,324**	**7,803**

30 day settlement period is set with independent heat producers for purchased heat energy, 90–180 day settlement period – with contractors, 5–30 day settlement period – with other suppliers.

As of 31 December 2016 the Group and the Company had an EUR 55 thousand (31 December 2015 – EUR 1,691 thousand) of overdue trade creditors, out of which an EUR 1,593 thousand as of 31 December 2015 related to legal proceedings with KTE.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

Foreign currency risk

All sales and purchases transactions as well as the financial debt portfolio of the Group and the Company are denominated in EUR, therefore, material foreign currency risk is not incurred.

Fair value of financial assets and liabilities

The Group and the Company's principal financial assets and liabilities accounted for at amortised cost are trade and other current and non-current receivables, trade and other payables, long-term and short-term borrowings. The net book value of these amounts is similar to their fair value.

Fair value is defined as the price at which the financial assets or liabilities could be exchanged between knowledgeable willing parties in an arm's length transaction at the measurement date. Fair values are obtained from quoted market prices, discounted cash flow models and option pricing models as appropriate.

The following methods and assumptions are used to estimate the fair value of each class of financial assets and liabilities:

- The carrying amount of current trade accounts receivable, current trade accounts payable, other receivables and other payables and current borrowings approximate their fair value.
- The fair value of non-current borrowings and trade accounts receivable is based on the quoted market price for the same or similar issues or on the current rates available for borrowings with the same maturity profile. The fair value of non-current borrowings with variable and fixed interest rates approximates their carrying amounts.

The Group and the Company's categories of financial instruments:

	Group			Company		
Financial assets:	**As of 31 December 2016**	**As of 31 December 2015**	**As of 31 December 2014**	**As of 31 December 2016**	**As of 31 December 2015**	**As of 31 December 2014**
Cash and bank balances	6,285	2,531	389	6,193	2,518	384
Loans and receivables	11,118	9,835	21,746	11,101	9,822	21,735
Financial assets, carried at fair value through profit or loss (level 3 in the fair value hierarchy)	1	1	28	1	1	28
	17,404	**12,367**	**22,163**	**17,295**	**12,341**	**22,147**

	Group			Company		
Financial liabilities:	**As of 31 December 2016**	**As of 31 December 2015**	**As of 31 December 2014**	**As of 31 December 2016**	**As of 31 December 2015**	**As of 31 December 2014**
Carried at amortised cost	33,216	29,883	48,786	29,891	29,882	48,784
	33,216	**29,883**	**48,786**	**29,891**	**29,882**	**48,784**

The carrying amounts of financial assets and financial liabilities approximate their fair values.

Capital management

The primary objectives of the Group's and the Company's capital management are to ensure that the Group and the Company comply with externally imposed capital requirements and that the Group and the Company maintains healthy capital ratios in order to support its business and to maximise shareholders' value.

The Group and the Company manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. To maintain or adjust the capital structure, the Group and the Company may issue new shares, reconsider the dividend payment to shareholders, and return capital to shareholders. No changes were made in the objectives, policies or processes of capital management as of 31 December 2016 and 31 December 2015.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

The Group and the Company is obliged to upkeep its equity of not less than 50 percent of its share capital, as imposed by the Law on Companies of Republic of Lithuania. The Group and the Company complies with equity requirements imposed by the Law on Companies of Republic of Lithuania. There were no other externally imposed capital requirements on the Group and the Company.

The Group and the Company monitor capital using debt to equity ratio. Capital includes ordinary shares, reserves, earnings retained attributable to the equity holders of the parent. There is no specific debt to equity ratio target set out by the Group's and the Company's management, however current ratios presented below are treated as sustainable performance indicators: as satisfactory performance indicators and as creditable performance indicators:

	Group		**Company**	
	As of 31 December 2016	**As of 31 December 2015**	**As of 31 December 2016**	**As of 31 December 2015**
Non-current liabilities (including deferred tax and grants (deferred income))	42,423	40,391	41,319	40,583
Current liabilities	15,631	12,191	12,237	12,178
Liabilities	**58,054**	**52,582**	**53,556**	**52,761**
Equity	**87,019**	**81,860**	**87,515**	**82,412**
Debt* to equity ratio (percent)	**66.71**	**64.23**	**61.20**	**64.02**

* Debt contains all non-current (including deferred income tax liability and grants (deferred revenues)) and current liabilities,

Market risk
External risk factors that make influence to the Group's and the Company's main activity: increase in fuel prices, unfavourable law and legal acts of Government and other institutions, decisions of local municipality, decrease of number of consumers, the cycle of activity, environmental requirements.

24. Commitments and contingencies

Litigations
On January 2014 insurance company AB Lietuvos Draudimas placed a claim in amount of EUR 33 thousand in case of damage compensation to UAB Korelita, in which AB Litgrid, UAB DK PZU Lietuva and the Company are defendants. A claimant suffered damage due to a fault in the electrical system. The Company placed a response to the court in which asked to ignore a claim as unfounded. Kaunas District Court rejected a claim on 22 April 2015. A claimant submitted an appeal, but it was left unmet by the decision of Kaunas Regional Court of 29 October 2015 and the decision of Kaunas District Court came into force. Whereas a cassation appeal was not submitted, the decision remained unchanged.

Leasing and construction work purchase arrangements
On 20 December 2010 the Company entered into the lease arrangements with UAB ENG for the real estate. Under this lease arrangement the Company leases to UAB ENG Garliava boiler-house for building of heat production equipment. The Company undertakes obligations to procure heat produced in this equipment. The term of lease is 20 years.

Future liabilities of Group and the Company under valid purchase arrangements as of 31 December 2016 amounted to EUR 18,866 thousand.

25. Related parties transactions

The parties are considered related when one party has the possibility to control the other or have significant influence over the other party in making financial and operating decisions.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

In 2016 and 2015 the Group and the Company did not have any significant transactions with the other companies controlled by Kaunas city municipality except for the purchases or sales of the utility services. The services provided to the Kaunas city municipality and the entities controlled by the Kaunas city municipality were executed at market prices. The Kaunas City Municipality related party list can be found here: http://senas.kaunas.lt/index.php?299473330.

In 2016 and 2015 the Group's and the Company's transactions with Jurbarkas city municipality, Kaunas city municipality and the entities, financed and controlled by Kaunas city municipality and amounts of receivables from and liabilities to them at the end of the year were as follows:

2016	**Purchases**	**Sales**	**Receivables**	**Payables**
Kaunas city municipality and entities financed and controlled by Kaunas city municipality	972	5,241	777	181
Jurbarkas city municipality	1	314	22	1

2015	**Purchases**	**Sales**	**Receivables**	**Payables**
Kaunas city municipality and entities financed and controlled by Kaunas city municipality	1,010	5,327	873	296
Jurbarkas city municipality	1	325	13	-

The Group's and the Company's as of 31 December 2016 allowance for overdue receivables from entities financed and controlled by municipalities amounted to EUR 241 thousand (as of 31 December 2015 – EUR 341 thousand). The amounts outstanding are unsecured and will be settled in cash. No guarantees on receivables have been received.

As at 31 December 2016 and 31 December 2015 the Company's transactions with the subsidiaries and the balances at the end of the year were as follows:

UAB Petrašiūnų Katilinė	**Purchases**	**Sales**	**Receivables**	**Payables**
2016	717	3	4	384
	-	-	-	-

UAB Kauno Energija NT	**Purchases**	**Sales**	**Receivables**	**Payables**
2016	5	13	111	-
2015	6	8	125	-

As at 31 December 2016 the Company has formed a value decrease in amount of EUR 111 thousand (as at 31 December 2015 in amount of EUR 125 thousand) for the receivables from subsidiaries.

<u>Remuneration of the management and other payments</u>

As at 31 December 2016 the Group's and the Company's management team comprised 7 and 4 persons respectively (as at 31 December 2015 – 6 and 4).

	Group		**Company**	
	2016	**2015**	**2016**	**2015**
Key management remuneration	150	175	119	160
Calculated post-employment benefits	11	7	11	7

In the year 2016 and 2015 the management of the Group and the Company did not receive any loans or guarantees; no other payments or property transfers were made or accrued.

CONSOLIDATED AND PARENT COMPANY'S FINANCIAL STATEMENTS FOR THE YEAR 2016 (all amounts are in EUR thousand unless otherwise stated)

26. Business Combinations

As described in Note 1, in October 2016 the Company has acquired 100 percent UAB Petrašiūnų Katilinė shares for EUR 1,894 thousand. The Company's management has assessed the fair value of acquired assets, liabilities and contingent liabilities and accounted for this acquisition, based on the purchase price allocation.

The Company's management performed internal valuation to determine the fair value of the long term assets acquired by comparing production costs of similar boilers. The Company's management identified bio fuel boilers with similar technical characteristics and evaluation of the model was based on recent market transactions data. The Company's management estimated that purchased the 1 MW boiler price equals the market with similar characteristics 1 MW boilers installation costs.

As UAB Petrašiūnų Katilinė was purchased in 27 October 2016, financial reporting purposes, the acquisition date is 30 September 2016.

The acquired assets and liabilities
Fair and carrying value of the acquired assets and liabilities at the acquisition date (the Group became the controlling unit) were as follows (100 per-cent):

	Fair value	**Carrying value**
Property, plant and equipment	6,494	4,909
Inventories and prepayments	19	19
Current accounts receivable	6	6
Cash	188	188
	6,707	5,122
Borrowings	3,419	3,419
Trade payables	19	19
Other non current liabilities	1,334	1,334
Other current liabilities	41	41
	4,813	4,813
The fair value of the identifiable net assets	**1,894**	**309**
Attributable to shareholders of the Company	1,894	309

The difference between the price paid and the acquired assets, liabilities and contingent liabilities to fair value at the acquisition date were as follows:

The real assets acquired and liabilities and contingent liabilities is	1,894
The purchase price	1,894
Cash	(188)
The purchase price, net of cash acquired	1,706

UAB Petrašiūnų Katilinė supplied all goods and services to the Company in 2016. Expenditures of UAB Petrašiūnų Katilinė decreased the expenditures of the Group by EUR 46 thousand (expenditures of fuel and energy purchased decreased by EUR 307 thousand, and expenditures of depreciation and all other expenditures increased by EUR 261 thousand).

27. Post balance sheet events

On 16 March 2017 the Company signed a credit agreement with UAB Petrašiūnų Katilinė EUR 600 thousand amount to 6-month EURIBOR interest rate plus 1.2 percent. the margin. The loans expiry date – 31 December 2019.

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CONSOLIDATED ANNUAL REPORT
OF AB KAUNO ENERGIJA
OF THE YEAR 2016




Kaunas, 2017

AB KAUNO ENERGIJA
Company code 235014830
Raudondvario Rd. 84, LT-47179 Kaunas, Lithuania

Confirmation of the persons responsible for the shareholders of the Company and the Bank of Lithuania

Following Article 22 of the Law on Securities of the Republic of Lithuania and the Rules for presentation and delivery of periodic and additional formation, approved by the decision No O3-48 of 28 February 2013 of the Board of the Bank of Lithuania, we hereby confirm that, to our best knowledge, the consolidated annual report and audited consolidated and parent company financial statements of the year 2016 reviewed by auditors of private limited liability company Kauno Energija (hereinafter the Company or the Issuer), prepared in accordance with International Financial Reporting Standards as adopted by the European Union, represent a true and fair view of the total consolidated assets, liabilities, financial position and profit or loss and cash flows, that the consolidated annual report of the year 2016 includes a fair business development and performance review of the Company and the situation of consolidated, together with the description of principal risks and uncertainties encountered.

General Manager of AB Kauno Energija	Rimantas Bakas
Chief Finance Officer of AB „Kauno energija“	Gintautas Muznikas
Chief Accountant of AB Kauno Energija	Violeta Staškūnienė

CONTENTS

AB KAUNO ENERGIJA
Company code 235014830
Raudondvario Rd. 84, LT-47179 Kaunas, Lithuania

LIST OF TABLES

LIST OF CHARTS

1. Reporting period of the Consolidated Annual Report

Reporting period, for which the Consolidated Report of AB Kauno Energija was prepared, is the year 2016.

2. Companies composing the group of companies and their contact details

AB Kauno Energija (hereinafter referred to as the Company or the Issuer) prepares both the Company‘s and the consolidated financial statements. The group (hereinafter referred to as the Group) consists of AB Kauno Energija and its subsidiaries – UAB Kauno Energija NT, in which the Issuer directly controls 100 per cent of the shares and UAB Petrašiūnų Katilinė, which also became the part of the Group starting from 27 October 2016 and the Issuer also directly controls 100 per cent of the shares of this company.

Main details of the Company:

Name of the Company:	Open Limited Liability Company Kauno Energija
Legal-organizational form:	Open Limited Liability Company
Headquarters address	Raudondvario pl. 84, 47179 Kaunas
Code of legal entity:	235014830
Telephone	(8 37) 305 650
Fax	(8 37) 305 622
E-mail:	info@kaunoenergija.lt
Webpage	www.kaunoenergija.lt
Registration date and place	22 August 1997, Kaunas, Order No 513
Register manager	Kaunas Branch of State Enterprise Centre of Registers
VAT payer code	LT350148314

Main information about the subsidiaries:

Company name	Private Limited Liability Company Petrašiūnų Katilinė
Legal-organizational form	Private Limited Liability Company
Headquarters address	R. Kalantos str. 49, 52303 Kaunas
Code of legal entity	304217723
Telephone	+370 687 48413
Registration date and place	1 April 2016, Kaunas
Register manager	Kaunas Branch of State Enterprise Centre of Registers

Company name	Private Limited Liability Company Kauno Energija NT
Legal-organizational form	Private Limited Liability Company
Headquarters address	Savanorių pr. 347, 49423 Kaunas
Code of legal entity	303042623
Telephone	(8 37) 305 693
E-mail	kent@kaunoenergija.lt
Registration date and place	16 April 2013, Kaunas
Register manager	Kaunas Branch of State Enterprise Centre of Registers

3. Nature of core activities of the companies composing the group of companies

The nature of core activities of the Group is manufacture and rendering of services. The Company is the parent company of the Group. The Company generates and supplies heat to consumers (for the purposes of heating and hot water making) in the cities of Kaunas and Jurbarkas and in Kaunas district (Akademija town, Ežerėlis town, Domeikava village, Garliava town, Girionys village, Neveronys village, Raudondvaris village), (hereinafter referred to as Kaunas district).

Also, following provisions of the Law on Heat Sector, the Company supplies hot water (is engaged in hot domestic water supplier activities) from 1 May 2010 for consumers in the cities of Kaunas and Jurbarkas and Kaunas district (hereinafter the supplies of heat and hot domestic water without cold water are referred to as heat, with the exception of information provided in Tables 7 and 8 "Comparison of financial indicators of the Group and the Company of the year 2016 with the indicators of the years 2012–2015"), who chose the Company as a hot water supplier. As at 31 December 2016, the Company was a hot water supplier for 475 residential buildings in Kaunas and Kaunas district and 5 in Jurbarkas. Income from hot water supplies amounts to approximately 4.3 per cent of all of Company's sales revenue.

In addition, the Company produced electric energy in small quantities in Kaunas district until April 2016. It also maintains engineering structures (collectors – manifolds) and operates heat and electricity production facilities. The Group and the Company carries out a supervision of indoor heat and hot water supply systems, maintenance of heat unit equipment, repairs of heat units and other heating equipment, provides rental services premises under particular agreements. The Group and the Company are engaged in licensed activity in accordance with the licenses held. On 26 February 2004 the National Commission for Energy Control and Prices (hereinafter – NCC) issued a heat supplier licence to the Company. The licence is valid indefinitely. Maintenance of indoor heat and hot water supply systems is pursued following the provisions of Article 20 of The Law on Heat Sector of the Republic of Lithuania.

Starting from 28 January 2013 the Company performs as a participant of Natural Gas Exchange. Companies assumed more flexibility acquiring deficient or selling surplus amount of gas after start of operation of natural gas exchange at the same time applying the undertakings for gas suppliers under agreements. Participation in natural gas exchange provides the possibility to companies to know the exact price of gas in a moment, to avoid application of "take or pay" terms and to balance amount of purchased and used natural gas.

On 4 December 2014 NCC issued for the Company Licence of Energy operation No. L2-38(GDT), which allowed the Company to be engaged in natural gas supplies business. NCC withdrew validity of the licence by the decision No. O3-140 of 25 May 2016.

The vision of the Group and the Company is to be a modern, effective, competitive, and added value for shareholders creating group of companies engaged in heat and electric energy generation, supply of heat and hot water, maintenance of indoor heating and hot water supply systems and property lease.

Values of the Group and the Company:

- professionalism;
- reliability;
- transparency;
- being proactive;
- responsibility;
- cooperation.

Strategic goals of the Group and the Company:

- To implement strategic development plans formed by shareholders;
- To properly contribute to the implementation of goals of National Energetics Strategy;
- To reduce dependence from imported fuel, i.e. natural gas;
- To increase competition in heat generation sector;
- To expand current position of the Group companies in the market;
- Development by offering new products and services;
- To ensure implementation of Energy Efficiency Directive 2012/27/EU.

Principled guidelines of Company's heat economy strategy are as follows:

- Increase and expansion of heat economy – Kaunas city needs at least one bigger than 100 MW capacity modern, up-to-date production facility – cogeneration power-plant, using renewable energy sources (hereinafter – RES) and / or waste, and / or natural gas. New power-plant should ensure tankage / use of reserved fuel, reservation of heat production facilities, stable hydraulic mode of centralized heat supply, flexible reaction to network peak demand changes, should have an emergency replenishment system and should be economically "balanced";
- Increase of safety and reliability of heat supply – the Company intends to formulate an expert assessment of safety / vulnerability of heat supply system, to implement update and modernization of system of parameters data transfer, collection and evaluation, to implement optimization of the network hydraulic mode and increase of speed of parameters reaction / change, to reconstruct and optimize sections of thermofication pipelines and elements (average age of pipelines of district heating network

(hereinafter – DHN) reaches approximately 30 years), to implement update and development of the system of DHN water reserve – emergency replenishment, to implement technical solutions and / or use a good practice increasing reliability and safety, ensuring stability of thermofication mode;
- to actively participate in formation of policy of Kaunas city supply with heat and in increase of Company's desirability and in expansion of district heating market;
- formation of good practice and its publicizing;

4. Issuer‘s agreements with credit institutions

On 1 April 2003 the Issuer Service Agreement with AB SEB Bankas (company code 112021238, Gedimino pr. 12, Vilnius), represented by the Finance Markets Department was made.

5. Trade in securities of companies composing the group of companies in regulated markets

20,031,977 (twenty million thirty one thousand nine hundred seventy seven) of the Issuer‘s ordinary registered shares (VP ISIN code LT0000123010) with the total nominal value equal to EUR 34,855,639.98 (thirty four million eight hundred fifty five thousand six hundred thirty nine euro and 98 cents) as at 31 December 2016 were listed in the secondary trade list of Nasdaq Vilnius Baltic stock exchange. The beginning of listing of the Company's shares is 28 December 1998.

6. Overview of the condition, performance and development of the group of companies
6.1. Overview of the condition, performance and development of the Company

In the year 2016 the Company performed its activities with a main focus on development of capacities of production sources and increase of reliability of CHS network, considering Strategic guidelines of centralized heat supplies of Kaunas city.

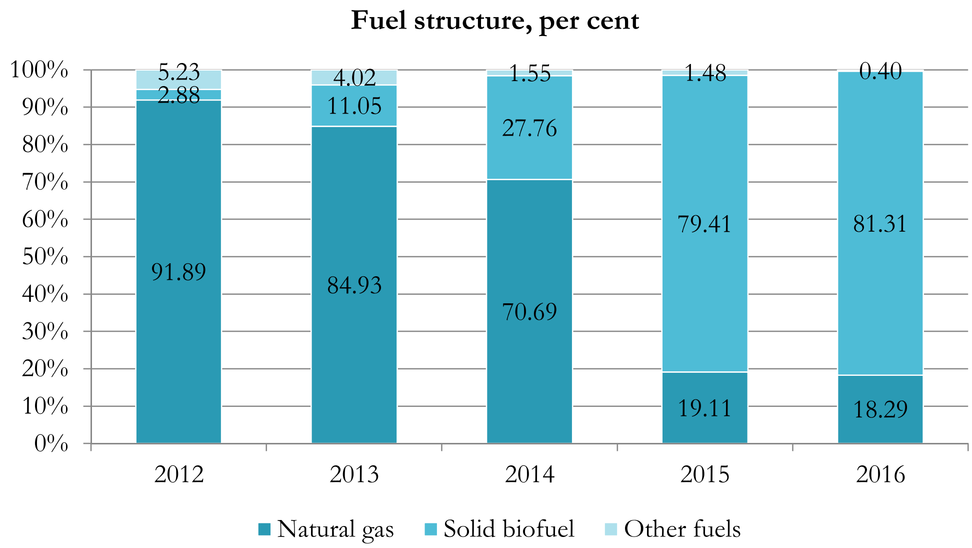
When planning its activities the Company also takes into account the AB Kauno Energija Strategy for the Heating System Development for the years 2007–2020 developed in 2016 by the Lithuanian Energy Institute under initiative of the Company. The main provisions and guidelines for heat supply to the city until 2021, reaching to ensure technical, economical and management effectiveness of the system of centralized heat supply and reliability of heat supply, without prejudice environmental requirements and considering provisions of Lithuanian legislation and obligatory aspirations of European Union (hereinafter – EU) directives are determined in the strategy.

The Company covers a major part of heat production and supply market in the cities of Kaunas and Jurbarkas and Kaunas district. Group's generation capacities consist of Company's boiler-houses capacities and subsidiary's UAB Petrašiūnų Katilinė capacities in Kaunas city. Company's generation capacities consist of Petrašiūnai power plant, 4 boiler-houses in Kaunas integrated network, 7 district boiler-houses in Kaunas district, 1 boiler-house in Jurbarkas city, 13 boiler-houses of isolated networks and 27 local gas burning boiler-houses in Kaunas city, also 8 local water heating boiler-houses in Sargėnai catchment. Total installed heat generation capacity in the year 2016 was approximately 587 MW, and total energy generation capacity of the whole Group is approx. 596 MW (including 39 MW capacities of condensational economizers). Total installed heat production capacity of the Company consists of approx. 568 MW (including 39 MW capacities of condensational economizers), electricity generation capacities – 8.75 MW. 294.8 MW of heat generation capacities (including 16 MW capacities of condensational economizers) and 8 MW of electricity production capacities of them are in Petrašiūnai power plant. 34.8 MW of heat generation capacities (including 2.8 MW capacities of condensational economizer) are in Jurbarkas city. Total Company's power generation capacity is 577 MW (including 39 MW of condensational economizers' capacities).

Almost 41 per cent of heat supplied to consumers in 2016 was produced in Company's heat production facilities. The rest of required quantity of heat was purchased from independent heat producers (hereinafter – IHP) in monthly auctions, according to legal acts.

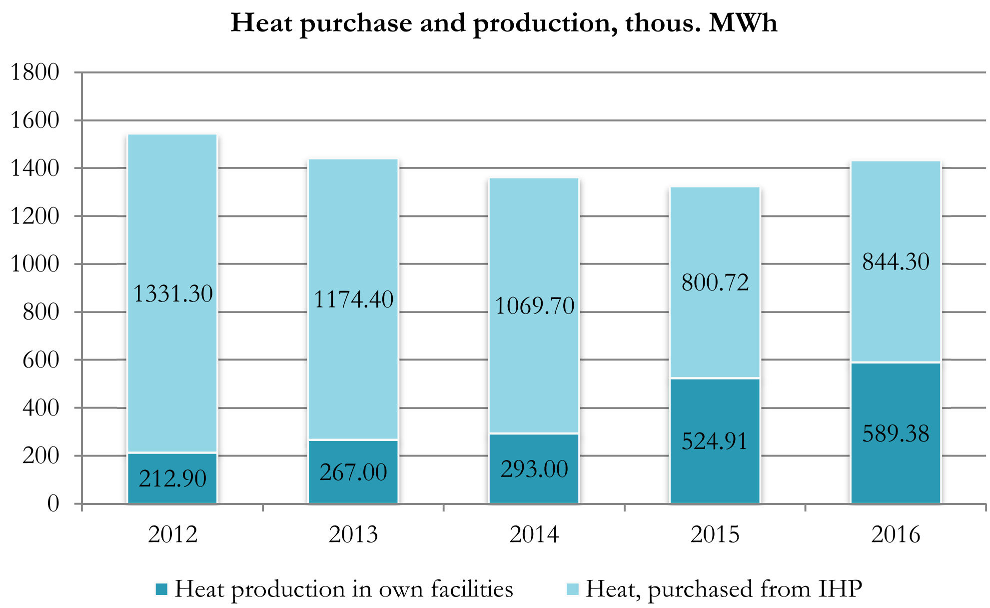
Fuel, used by the Company for heat and electricity production in the year 2016 was as follows:
- Solid biofuel – 81.31 per cent,
- Natural gas – 18.29 per cent,
- other fuels – 0.40 per cent.

Chart 1



In the year 2016, the Company purchased heat from 11 IHP in Kaunas and Kaunas district: from UAB Kauno Termofikacijos Elektrinė, UAB GECO Kaunas, UAB Lorizon Energy, UAB Ekoresursai, UAB Petrašiūnų Katilinė, UAB Aldec General, UAB ENG, UAB Danpower Baltic Biruliškių, UAB Ekopartneris, UAB SSPC-Taika and UAB Foksita. Total purchases consisted of 844.3 thousand MWh of heat, i.e. 59.1 per cent of heat supplied to the network (in the year 2015 – 60.4 per cent). Amounts of heat purchased from IHP and produced with Company's equipment during the period of 2012 – 2016 are presented in chart 2, thousand MWh:

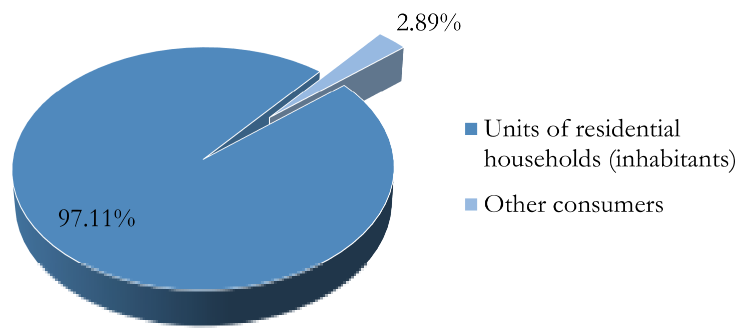
Chart 2



As at 31 December 2016 the Company supplied this produced and purchased heat with integrated heating and local area networks to 3,426 businesses and organizations as well as to 115,078 households, in total – to 118,504 consumers (objects by addresses).

Chart 3

Repartition of Company's heat consumers by groups



Investments

Company's investments in the latest technologies (the reconstruction of heat generation facilities installing economizers, new biofuel burned boilers, automation of boiler-houses of integrated network, systems of electronic services, system of remote reading of heat meters and data transmission, customer service using "one stop" principle, etc.) help the Company to reduce the price of heat sold. Reconstruction of heat supply networks reduces Company's heat supply losses. All these investments help the Company to adapt to market changes and to be an advanced company of heat and hot water supply, also of maintenance of heat production facilities in Kaunas and Jurbarkas cities and Kaunas district.

Investments are made in accordance with Company's revised investment plan for the year 2016, which was approved by decision No T-202 of Kaunas City Municipality Council of 3 May 2016 "Regarding change of decision of Kaunas City Municipality Council No T-749 of 29 December 2015 "Regarding revised investment plan of AB Kauno Energija for the year 2016" and authorisation to sign changes" (hereinafter – Investment plan). EUR 44.54 million were planned to invest in Company's assets according to approved Investment plan during the period of 2016.

The Company implements trunk pipeline replacement projects co-financed by the European Union structural funds, it also optimizes pipeline diameters, connects new objects to the DHN and modernises heat production facilities according to Investment plan.

Amendments to the Law on Heat Sector of the Republic of Lithuania and changes in NCC's regulation allowed favourable conditions to invest to construction and reconstruction of heat production facilities, thus increasing competition in heat production sector and effectively reducing heat price for consumers.

In order to reach these goals, the Company continued modernization of its' own heat generation facilities, installing new heat generation equipment in them. The following projects of heat generation facilities modernization were finished to implement:
1. On September 2016 the Company accomplished a project of installation of 15 MW capacity gas burned boiler No. 2 together with 1.5 MW capacities condensational economizer in "Šilkas" boiler-house. Value of the project is EUR 659 thousand. This new equipment will increase reliability of heat production and supply, and will reduce Company's comparable expenditures of heat production and the final heat price for consumers;
2. The Company for more than EUR 2.1 million EUR start realisating plans to install 5 MW and 3 MW capacities biofuel burned boilers together with condensational economizer in Jurbarkas boiler-house. This project is being planned to accomplish in the years 2017–2018. First stage of the project is accomplished in November 2016, i.e. 5 MW heat capacity biofuel burned boiler together with pertinent is installed. The amount of heat produced using biofuel will amount up to 60 percent of all heat supplied in Jurbarkas city after the

reconstruction. Starting from November 2016 a total of 12 GWh of heat were produced until the end of the year using this new boiler. A natural gas was used for heat production in Jurbarkas boiler-house until that time.
3. In November 2016 the Company signed an outsourcing contract with the winner of procurement on installation of four gas burned boilers at capacity 15 MW each together with 1.5 MW capacity condensational economizers in Pergalė boiler-house. The planned value of continued project is approx. EUR 2.3 million. Accomplishment of the project is expected in 2017–2018. Works of the project are divided in two stages. One boiler together with economizer is planned to install on the first stage, and the rest three boilers – on the second stage. The second stage can still be terminated due to the changes in Company's needs, financing or other circumstances.

The Company builds biofuel equipment coherently pursuing strategy of Company's development, approved by city municipality council and reaching to further reduce heat price for consumers. By increasing and modernizing production capacities the Company increasingly occupies part of heat production market and it seems likely that it will produce in own production facilities and will supply to DHN more than 60 per cent of all heat demand in 2017.

The result of all of these already implemented investment projects is decreased price of heat for Company's heat consumers. An average price of the heat sold was 5.02 ct/kWh in the year 2016 and in the year 2015 it was 5.40 ct/kWh, and in the year 2014 it was 6.69 ct/kWh.

In June 2016 the Company submitted 9 applications to the Lithuanian Business Support Agency under the measure No. 04.3.2-LVPA-K-102 "Modernisation and development of heat supply networks" 1 invitation of the 4 priority "Promoting energy efficiency and production and use of renewable energy" of Operational Programme for the European Union Funds' Investments in 2014-2020:

- "Modernisation of the main pipeline 3Ž of Kaunas city integrated network" (code 04.3.2-LVPA-K-102-01-0009),
- "Modernisation of the main pipeline 6T of Kaunas city integrated network" (code 04.3.2-LVPA-K-102-01-0010),
- "Reconstruction of Kaunas city integrated network in Eiguliai catchment" (code 04.3.2-LVPA-K-102-01-0011),
- "Modernisation of the main pipeline 1T of Kaunas city integrated network" (code 04.3.2-LVPA-K-102-01-0024),
- "Reconstruction of Kaunas city integrated network in Kalniečiai catchment" (kodas 04.3.2-LVPA-K-102-01-0025),
- "Modernisation of the main pipeline 4T of Kaunas city integrated network" (code 04.3.2-LVPA-K-102-01-0026),
- "Reconstruction of heat supply networks, built from Kaunas city Pergalė boiler-house" (code 04.3.2-LVPA-K-102-01-0036),
- "Reconstruction of Kaunas city integrated network in P. Lukšio street" (code 04.3.2-LVPA-K-102-01-0037),
- "Modernisation of the main pipeline 2Ž of Kaunas city integrated network" (code 04.3.2-LVPA-K-102-01-0038).

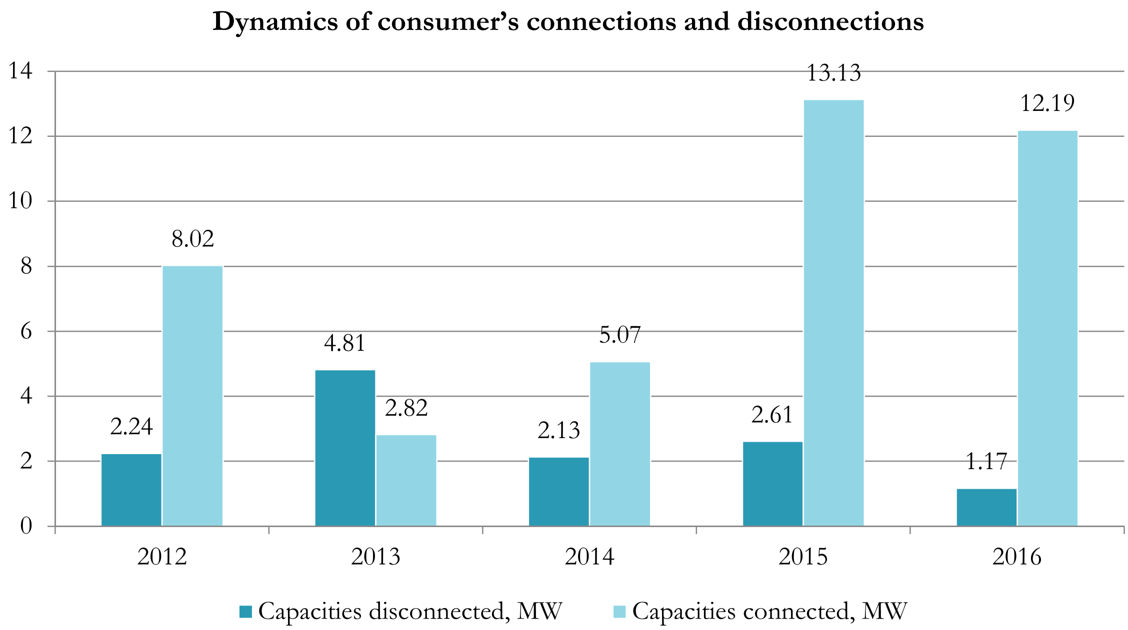
Implementation of these projects started in 2016 and the accomplishment of them is scheduled in 2018. 9 agreements on financial support were signed with LBSA in December 2016. Total value of the projects is EUR 11.7 million. European Union Structural support in amount of EUR 5.8 million is assigned.

19 new objects with total installed capacity of 12.19 MW were connected to Company's heat supplies network during the year 2016.

The biggest consumers connected in the year 2016 are as follows: recreational and shopping centre "Mega", reconstructed Kaunas bus terminal and residential and commercial premises in Savanorių av. 276. The consuming capacity of just those objects will consist of more than 6.33 MW.

The dynamics of consumer's connections to Company's DHN and disconnections from it in 2012-2016 is shown in Chart 4.

Chart 4



On May 2016 the Company took over heat and hot water supply to three municipal education and training institutions by the initiative of Kaunas city municipality: rowing sport base of Kaunas yachting school Bangpūtys, Kaunas Vaišvydava comprehensive school, and Kaunas special school, situated in Apuolės str. 11. The heating of these institutions was performed from local boiler-houses, burned with coal. The decision on connection of Kaunas special school to the district heating network has been made after assessment of situation and possible need in investments. Heat and hot water supply to this school was started on May 2016. Two pellet burned boilers at capacity of 150 kW and 100 kW at Kaunas Vaišvydava comprehensive school were installed in November 2016. 108 MW of heat were produced with these boilers in the year 2016. A connection of boiler-house to the system of data receiving, monitoring and process management is in progress at the moment. Value of the project is EUR 80 thousand. Rowing sport base is intended to be connected to the gas network.

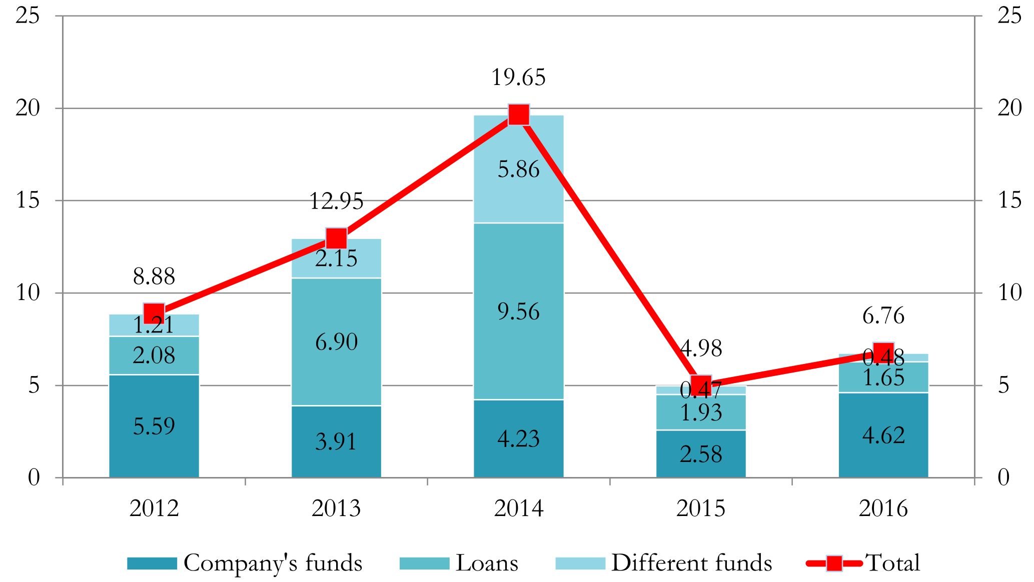
A heat in operational mode was started to supply to Kaunas Clinical Hospital, situated in Josvainių str. 2 in 2016. Heat supply to this hospital in testing mode was started on December 28, 2015. Hospital's consuming capacity is 6.18 MW. Earlier, a heat for this object was supplied from gas boiler-house, operated by UAB "Litesko". A heat for this object is supplied with no interference for more than a year.

A total installed capacity of objects disconnected from DHN in 2016 was approx. 1.167 MW. Disconnection of heat equipment from centralized heat supply networks and the change of heating method is pursued following the order determined by the Civil Code of the Republic of Lithuania, the Law on Heat Sector of the Republic of Lithuania, the Law on Construction of the Republic of Lithuania and sub statutory legal acts implementing these Laws.

In 2016 the Company invested EUR 6.75 million (among them, non-Company's funds, i.e. EUR 1.65 million were loans from commercial banks, EUR 0.48 million was a financial support from European Union Structural Funds and Lithuanian Environmental Investment Fund). A major part of these investments were assigned for modernization of heat supply networks and renewal of heat production boilers (EUR 2.099 million). EUR 0.189 million were assigned for connection of new objects, a total consumption capacity of whose is 12.19 MW, to DHN. Company's investments by funding sources for the years 2012–2016 are shown in Chart 5.

Chart 5

Implementation of investments by funding sources, million euro



In order to expand its' consumer market, the Company started to build a new heat supply pipeline in 2015 to Brasta residential quarter in Kaunas, which is in process of construction. Following the project "Heat supply networks to residential quarter from HC 8K-14-5 near the building at Jurbarko str. 81 to the point "A" at the address Brastos str. 24, Kaunas" a 487 meters length, 200 mm diameter pipeline is built. The heat will be supplied to this residential quarter using this pipeline. According to publicly announced information 10 residential buildings with approximately 500 flats will be built in this residential quarter. Approximately of 4.4 MW capacities consumption equipment are planned to install in them. A new pipeline will allow supplies of an up to 10 MW flow of heat at the coldest period of the year, so it will be possible to connect even more new consumers if it will be necessary. Total value of the project is EUR 244 thousand. Project is implemented using efforts and funds of AB Kauno Energija. Construction works of the project were started in December 2015. Two residential buildings were connected to DHN using this pipeline in the year 2016.

A certified laboratory of measuring of stationary environment pollution sources started its' operation in the Company in June 2016. Analysis of particulates amount and gas flow emitted with smoke from boiler-houses is performed. The laboratory has the right of performing these measures in the territory of whole Lithuania. This service was outsourced earlier.

6.2. Description of exposure to key risks and uncertainties we confront with and their impact on Company's results

External risk factors affecting the Company's core business:

- Increasing competition between heat producers in Kaunas;
- Increase in final (i.e. including all expenditures) price of natural gas and biofuel;
- Ever-changing legal environment;
- Heat production pricing policies.

Competition environment risk factors. In order to operate effectively and reliably in creation the added value for shareholders, the Company is facing threats specific to the sphere of its activity, but also takes advantage of opportunities to work efficiently and effectively by exploiting the available potential. One of the biggest threats that the Company may face is a relatively high price for heat purchased from IHP, who are ranked as private business units committed to profit generation. Purchase of heat is pursued following valid law and the Description of procedure for purchase of heat from independent suppliers of heat approved by NCC. In turn, the Company invests extensively in modernization and construction of its own manufacturing facilities, to reduce the comparative costs of heat production. Thus it takes advantage of the regulatory environment and reduces the energy purchase price.

Together with coming of new IHP the Company faced additional technical, economical, legal and other issues that need to solve: management of heat supply network and balancing of power of these producers in case of emergency stop of them, retaining of optimum working parameters of the network, regulation, change and applying of heat purchase from IHP order.

Commercial risk factors: The Company is a major supplier of the heat produced centrally to the city of Kaunas, part of Kaunas district and the city of Jurbarkas. In order to retain this market, it is necessary to implement modern and efficient heat production technologies in own production facilities and to focus on production at the lowest cost, benefiting from private differences of different types of fuel.

The Company's sales of heat are directly dependent on heat demand, i.e. heat consumption, which is mostly affected by the average outdoor air temperature, the amount of investment of consumers in energy-saving and rational use of heat and the pace of development of the heat sales.

Changes in fuel prices and the price of heat, produced by IHP have an impact on cost of Company's heat and electricity production.

Company's performance is affected by the decline in sales due to reduced and further reducing heat demand (in pursuance of residential buildings renovation and by installing a heat saving equipment), due to consumer's disconnections from DHN (due to the various reasons). Risks can be mitigated by Company current and further investments in heat and electricity production facilities, using renewable energy sources, reducing heat production expenditures and the price heat, purchased from IHP as well as the price of heat supplied for consumers, and continually reasonably informing customers on the benefits of DHN systems (safety, reliability, correlation with one sort of fuel, fuel conversion, local pollution sources in residential areas, total environmental pollution, etc.) in comparison with autonomous heating.

The effects of other competing companies, propagating the only usage of natural gas, irrespective of approved special heating supplies plan, supplies reliability, affection to the only source of fuel, not yet regulated local pollution, in the heat supply sector with the Company are disconnections of consumers from DHN system. Heating equipment disconnection from the DHN and heating mode changes are carried out in accordance with the procedures specified in the "Rules on heat supply and consumption" approved by order No 1-297 of 25 October 2010 of the Minister of Energy of the Republic of Lithuania (and their further amendments) and the Description of procedure for disconnection of the building or heating facilities of premises from heat supply networks at the initiative of consumers approved by order No A 1830 of the director of administration of Kaunas City Municipality of 14 May 2012. Kaunas City Municipality has approved a special heat supply plan, which provides a way to separate the heat supply in different urban areas. Disconnection of buildings in the district heating area from the DH network is only possible with the appropriate permit of Kaunas City Municipality. A special heat supply plan of Kaunas District Municipality was approved by the decision of Kaunas District Municipality No TS-43 of 26 January 2012. A special heat supply plan of Jurbarkas City and District was approved by the decision of Jurbarkas District Municipality No T2-67 of 10 March 2005.

Operational risk: Limited consumers' solvency and the debts. Risks can be mitigated by the factoring of debts and applying more stringent debt collection techniques / methods. Other possible operational risk – changes in interest rates in the banking market.

Detailed information on risk management policy and of risks of credit, currency rates, interest rates and liquidity is provided in Note 23 of Company's explanatory notes to the financial statements of the year 2016.

During the year 2016 in comparison with the year 2015, heat consumer debts decreased by approximately 9 % and consisted of EUR 12.658 million in 2016. During the year 2015 in comparison with the year 2014 heat consumer debts decreased by approximately 10 % and consisted of EUR 13.826 million. Decrease was affected by application of effective methods of debts administration and decrease in heat price.

In order to recover these debts as soon as possible, the Company actively uses a variety of legal debt management measures, such as pre-trial actions, judicial recovery and also cooperation with debt Collection Companies. In addition, when a debt becomes big, a restriction of heat supplies was started to apply as a prevention measure (if there are technical possibilities and according to the law).

In all cases, the Company first notifies the user of his indebtedness. When debtors respond to warnings and contact the Company, the Company discusses the options of debt settlement with them, signs documents guaranteeing the repayment of the debt. If the debtor does not respond to warnings and if pre-trial measures are not effective, the judicial recovery begins. The Company then applies to the court and after a decision accompanied with receiving-order – to bailiff. In such case the debtor must pay not only the debt but also the court and execution expenditures. A number of debt prevention and pre-trial actions were made in 2016. A referral of information on debtors to Collection Company is among them. There were a number of debt management measures applied: more than 16.881 of written notices, 3.170 of telephone notices, 198 bills of exchange 95 peaceful agreements concluded, and 214.591 of notices in bills.

Activities of the Company are cyclical. During the heating season (October – April) the highest operating income is earned. During the non-heating season, the Company's revenues are at their lowest since only heat for hot water is used. In addition, during the non-heating season, the Company incurs more costs because it has to prepare for the upcoming heating season, i.e. to carry out the repairs and reconstruction of heat supply networks and heat production facilities.

Legal conformity risk: Energy activities are governed by the Law on Heat Sector, the Law on Energy, the Law on Electricity, the Law on Natural Gas, the Law on Drinking Water Supply and Wastewater Management, Government resolutions, Heat supply and consumption rules, Methodology of heat prices and payments for heat of NCC and other legislation. Their amendments affect the heating industry.

With new amendments of articles 2, 3, 20, 22, 28, 31, and 32 of the Law on Heat Sector No XI-1608 of the Republic of Lithuania that came in affect from 1 November 2011, in accordance with Article 7, the heat and hot water prices may not include any costs related with the indoor building heating (including heat units), and hot water systems. In implementing the legislation, from 1 November 2011, all of these costs directly reduce the profit of the Company.

The political and legal risks also include political decisions of Kaunas City Municipality, with a controlling stake in the Company, that affect the Company's decision-making on the issues of agenda at the meetings of shareholders (the most significant issues, excluding the shareholder structure formation, are the distribution of profits and support), election of members of the Supervisory Board, who appoint the Company‘s Management Board members (who are often influenced by the politicians who elected them). The risk can be mitigated by informing the main shareholder of the Company's operations, performance, future plans and non-politicized notification of the board.

Legal conformity risk is a risk of increase in losses and (or) loss of prestige, an (or) decrease in confidence, which can be determined by the external environment factors (for example, violation of external legal acts, non-compliance of requirements of supervising institutions, etc.) or internal factors (for example, violation of internal legal acts and ethical standards, cases of employees abuse, etc.).

The Company accomplished the last (of three) investment litigation with Kauno Termofikacijos Elektrinė (hereinafter – KTE), after Vilnius Court of Commercial Arbitration approved on 29 January 2016 a peaceful agreement concluded on 28 December 2015. Following the terms of agreement the sides agreed to terminate Investment agreement of 31 March 2003, KTE taking obligations to pay compensation for the Company in amount of EUR 2.3 million paying in equal parts yearly until 28 February 2018. As an additional non-financial compensation according the terms of peaceful agreement KTE disposed to the Company a part of Kaunas centralized heat supplies infrastructure (manifolds building and coherent pipelines, as well as part of technological circuit equipment, necessary to the Company) and the rights of lease of land plot, coherent to the assets disposed.

This juridical litigation with KTE continued from April 2013 and the litigations regarding a non-compliance of investments – from the year 2009.

Social factors: consumers' disconnections from the system of centralized heat supply can have a negative impact on Company's operations. Consumers with total consumption capacity of 1.167 MW were disconnected in 2016; also limited purchasing power of consumers and slow growth of it, unemployment and exceptionally negative opinion about district heating supplier in the public domain.

However, an increased number of consumers (from 118,404 in the year 2015 to 118,504 in the year 2016) had a positive impact. Total installed capacities of new consumer's amounts to 12.19 MW (mostly business organizations owning big, i.e. heated areas).

Social risk: Company's activities are socially sensitive to many Kaunas region residents and businesses due to the conditionally high costs for heating and hot water. These costs constitute a significant part of expenses for households. But as the price of heat sold is decreasing, a number of complaints regarding big bills also decrease. This decrease was determined by the latest Company's investments in production facilities that allowed reducing the prices of heat and hot water significantly. As measured in terms of Lithuania, the Company's heat price in the year 2016 was lower than an average heat price of all heat supply companies.

This risk is mitigated by reasonably informing consumers about the Company's activities. Articles on Company's activities are coherently published in Company's website and in national or local media. The Company analyses consumer's complaints, provides written responses, advises consumers verbally (in Company's premises), also by phone and e-mails. Heat consumers periodically, i.e. 2 – 4 times per year, are invited to meet Company's specialists, and discuss consumer issues related to the Company's activities. Thus an image of modern and socially responsible company is being created.

Technical and process factors: greatest process risks are so shaded with the condition of heating systems. Company's trunk pipelines are an average about 38 years old. Modernization rate of them is determined by lack of funds – it is necessary to reconstruct more than 13.5 km of pipelines per year in order to condition of age of heat supply system and the minimum investments should consist of approximately 6 million euros. Hydraulic testing identifies their weakest points. Every year, about 200 points where cracks occur are identified during the tests. Upon discovery of defects, pipes are exposed and promptly repaired.

Mains of heating networks in the most worn out places are reconstructed using support from the EU Structural Funds. New industrially (polyurethane foam insulation in polyethylene shell) insulated pipes not requiring concrete channels are mounted in the reconstructed sections of the heat supply network. Heat loss is very low in reconstructed sections (process level), while the pipelines no longer pose a threat of rupture and ensure reliable heat supply to consumers.

The greatest technical risk factor for heat generation facilities is their age. Some of heat generation facilities are already renewed at the moment. Every year boiler repairs and preventive work is carried out during the non-heating season. They are necessary to make secure heat supplies and reliability, i.e. securing of heat production facilities and fuel reserves.

The other risk factor is the lack of own heat generation capacities after selling the main heat generation facility – Kaunas Termofication power-plant in 2003. Existing Company's own capacities of approx. 420 MW cannot secure customers demand (maximum instantaneous demand according to data of three last years is 448 MW) in Kaunas integrated network. In addition, heat supplies companies must have reserve capacities that must be a 30 per cent bigger, than the maximum instantaneous demand of heat according to Lithuanian legal acts. This is why the Company is obliged by NCC to buy a reserve capacity security service. In the year 2016 this service was bought from KTE. Considering that and estimating common trends in development of heat economies in Kaunas and Lithuania, one of the aims of the Company is to continually reasonably invest in own heat production facilities, i.e. to modernize existing and to build new additional heat production capacities. More detailed information on Company's investments and modernization of production facilities is provided in chapters 6.1 and 7.

Process risk can be reduced by reconstructing heat production facilities and supply pipelines, utilizing the latest and advanced technologies and thereby increasing the efficiency of the thermal system, capacity of own heat production facilities necessary for secure of reliability. In addition, significant investments in the modernization of the Company's assets must be made according to the country standards and regulations in line with European Union standards and normative acts regulating qualitative and technical indicators of heat supply systems.

Ecological factors: In terms of the Company they may be divided into those affecting the Company and there was influenced by the Company's operations.

In order not to adversely impact the environment and comply with the pollution limits, vibration and noise values, the Company is guided by the requirements of the Kyoto Protocol, the Helsinki Commission (HELCOM) and environmental constraints of Helsinki Convention, as well as the European Parliament and Council Directive 2001/80/EB of regulating energy emissions and Lithuanian environmental normative document LAND 43-2013 for the use of natural resources, and releases and emissions of air pollutants to the environment in its activities. Main sources of pollution of the Company: burning fossil fuel in the Company's heat sources, production of heat and waste water, are used in the industrial processes.

The Company pays taxes for atmospheric and water pollution. If allowable emission rate limits or annual limits are exceeded, the Company must pay the fines under the applicable laws of the Republic of Lithuania. There have been no pollution-related incidents and the Company was not imposed any penalties in 2016.

Main Company's emission reduction measures: modernization of heat generation sources, heat transfer loss reduction by replacing the existing pipes to the pipes with polyurethane foam insulation, installation of new technology and improvement of existing facilities, use of less polluting fuels, and continuous emission monitoring (in 2016, the fuel balance was dominated by solid biofuel – 81.31%, natural gas – 18.29%, biogas and other fuels – 0.40 %).

7. Analysis of financial and non-financial performance results, information related to environmental issues

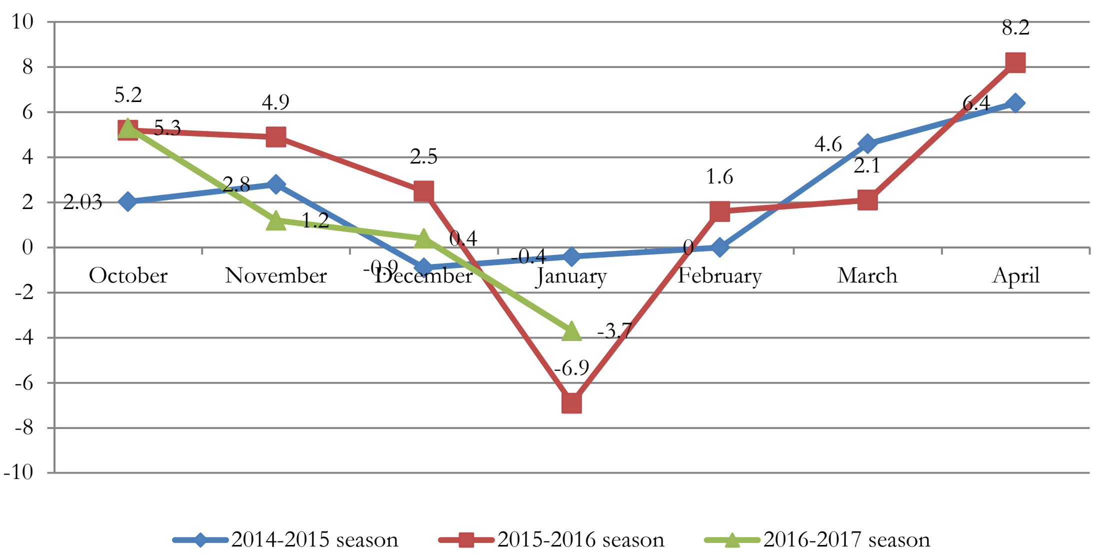
The result of Company's activities of the year 2016 reflects an impact of investments that were implemented by the Company during the years 2014–2015. The Company implemented 3 big investment projects, focused to the development of production sector, reaching to reduce costs of heat production and purchase, ensure reliable heat supplies, reduce losses of heat transmission, and increase effectiveness of heat supply system.

Company's sales revenue of the year 2016 was EUR 61,188 thousand and in comparison with the year 2015 increased by 0.75 per cent (in the year 2015 it consisted of EUR 60,733 thousand). Sales revenue of the Group of the year 2016 was EUR 61,178 thousand (in the year 2015 it consisted of EUR 60,725 thousand).

This change was mainly affected by major amount of heat sold, though the price of heat, the main part of which consist of fuel and purchased heat constituent, decreased. Amount of heat sold in 2016 in comparison with the year 2015 increased at 8.4 per cent. Average price of heat in the year 2016 decreased at 7.04 per cent (in 2016 it was 5.02 ct/kWh, and in 2015 it was 5.40 ct/kWh). Average air temperature of heating season of the year 2016 was 0.6 °C, and of the year 2015 – 3.2 °C.

Chart 6

Average monthly air temperature, °C



The comprehensive income of the Group consisted of EUR 6,957 thousand in 2016, and the Company's – EUR 6,901 thousand.

Turnover from sales of the Group and the Company increased by EUR 0.46 million, Company's comprehensive income of the year 2016 in comparison with the result of the year 2015 increased by EUR 2.37 million due to the compensation in amount of EUR 1.8 million, received from UAB Kauno Termofikacijos Elektrinė under Peaceful Agreement, concluded on 28 December 2015, by which a litigation in Arbitration case regarding noncompliance of Investment Agreement of 31 March 2003 was terminated, and effective Company's activities that allowed to significantly decrease expenditures of fuel and heat purchased, also after start of usage of biofuel as a major part of fuel for heat production instead of natural gas. All of these allowed make heat cheaper both produced by the Company, and purchased from IHP.

The Group and the Company accounts impairment loss in doubtful receivables. Change of impairment loss in doubtful receivables in 2016 in the Group's and the Company's write-offs and change in allowance for accounts receivable is included in the item of the cost of changes in the impairment of receivables and in 2016 amounted to EUR -825 thousand and EUR -835 thousand respectively, i.e. expenditures decreased an because of that profit increased (in 2015 – EUR -233 thousand and EUR -236 thousand). During 2016, the Group and the Company wrote of EUR 330 thousand and EUR 330 thousand of bad debts respectively (in 2015 – EUR 131 thousand and EUR 131 thousand). During 2016 the Group and the Company recovered EUR 5 thousand (in 2015 – EUR 9 thousand) of bad debts which were written off in prior years.

Comparison of financial indicators of the Group of the year 2016 with the indicators of the years 2012–2015 is presented in Table 1.

Table 1

No	Indicator of the Group	2012	2013	2014	2015	2016
1	Revenue from sales, thousand euros	107,079	93,363	75,746	60,725	61,178
1.1	Including: Heat energy	105,036	90,239	72,484	57,396	58,004
1.2	Electric energy	133	222	220	253	38
1.3	Maintenance of indoor heating and hot water supply systems, heating substation facilities	209	81	27	21	10
1.4	Income from the maintenance of collectors	224	226	227	226	227
1.5	Hot water supply including cold water price	1,395	2,494	2,633	2,569	2,611
1.6	Income from maintenance of hot water meters	82	101	155	260	288
2	Profit, thousand euros	346	874	862	4,509	6,957
3	EBITDA, thousand euros	6,151	6,384	7,344	12,083	14,787
4	Profitability of core business, per cent	0.2	-2.1	0.9	9.1	10.0
5	Net profitability, per cent	0.3	0.9	1.1	7.4	11.4
6	Assets, thousand euros	129,524	129,688	145,130	134,442	145,073
7	Equity, thousand euros	75,647	76,522	77,382	81,860	87,019
8	Return on equity (ROE), per cent	0.5	1.1	1.1	5.7	8.5
9	Return on assets (ROA), per cent	0.3	0.7	0.6	3.2	5.0
10	Asset turnover ratio	0.83	0.72	0.52	0.45	0.42
11	Return on tangible assets, per cent	0.4	0.8	0.7	3.7	5.6
12	Debt ratio	0.42	0.41	0.47	0.39	0.40
13	Debt-to-equity ratio	0.7	0.7	0.9	0.6	0.7
14	General liquidity ratio	0.85	0.70	0.69	1.10	1.18

No	Indicator of the Group	2012	2013	2014	2015	2016
15	Quick ratio	0.81	0.66	0.68	1.07	1.14
16	Cash ratio	0.05	0.02	0.01	0.21	0.49
17	Net earnings per share	0.01	0.02	0.02	0.11	0.16
18	Equity per share, euros	1.8	1.8	1.8	1.9	2.0
19	Last share market price of the year /net profit /number of shares at year-end (P / E ratio)	20.66	8.34	6.99	4.36	3.45
20	Share capital, thousand euros	74,256	74,256	74,378	74,476	74,476
21	Share capital-to-assets ratio	0.57	0.57	0.51	0.55	0.51
22	Return on equity (capital), per cent	0.5	1.1	1.1	5.8	8.7
23	Dividend payment ratio	0.00	0.23	0.03	0.38	0.00

Comparison of financial indicators of the Company of the year 2016 with the indicators of the years 2012–2015 is presented in Table 2.

Table 2

No	Indicator of the Company	2012	2013	2014	2015	2016
1	Revenue from sales, thousand euros	107,004	93,356	75,755	60,733	61,188
1.1	Including: Heat energy	105,054	90,255	72,494	57,404	58,013
1.2	Electric energy	133	222	220	253	38
1.3	Maintenance of indoor heating and hot water supply systems, heating substation facilities	116	58	26	21	10
1.4	Income from the maintenance of collectors	224	226	227	226	227
1.5	Hot water supply including cold water price	1,395	2,494	2,633	2,569	2,611
1.6	Income from maintenance of hot water meters	82	101	155	260	288
2	Profit, thousand euros	242	538	867	4,528	6,901
3	EBITDA, thousand euros	6,028	6,007	7,339	12,085	14,631
4	Profitability of core business, per cent	0.2	-2.2	1.0	9.2	9.88
5	Net profitability, per cent	0.2	0.6	1.1	7.5	11.3
6	Assets, thousand euros	130,447	130,380	145,853	135,173	141,071
7	Equity, thousand euros	76,512	77,050	77,915	82,412	87,515
8	Return on equity (ROE), per cent	0.3	0.7	1.1	2.6	8.1
9	Return on assets (ROA), per cent	0.2	0.4	0.6	1.5	5.0
10	Asset turnover ratio	0.82	0.72	0.52	0.45	0.43
11	Return on tangible assets, per cent	0.2	0.5	0.7	1.8	5.7
12	Debt ratio	0.41	0.41	0.47	0.39	0.38
13	Debt-to-equity ratio	0.7	0.7	0.9	0.6	0.6
14	General liquidity ratio	0.85	0.70	0.69	1.10	1.48
15	Quick ratio	0.82	0.66	0.68	1.07	1.44
16	Cash ratio	0.05	0.02	0.01	0.21	0.51

No	Indicator of the Company	2012	2013	2014	2015	2016
17	Net earnings per share	0.01	0.01	0.02	0.11	0.16
18	Equity per share, euros	1.8	1.8	1.8	1.9	2.0
19	Last share market price of the year / net profit / number of shares at year-end (P / E ratio)	29.51	13.55	6.95	4.34	3.47
20	Share capital, thousand euros	74,256	74,256	74,378	74,476	74,476
21	Share capital-to-assets ratio	0.57	0.57	0.51	0.55	0.53
22	Return on equity (capital), per cent	0.3	0.7	1.1	5.8	8.6
23	Dividend payment ratio	0.00	0.23	0.03	0.38	0.00

A more detailed analysis of financial indicators of the Group and the Company is provided in notes to Consolidated and Company's financial statements for the year 2016.

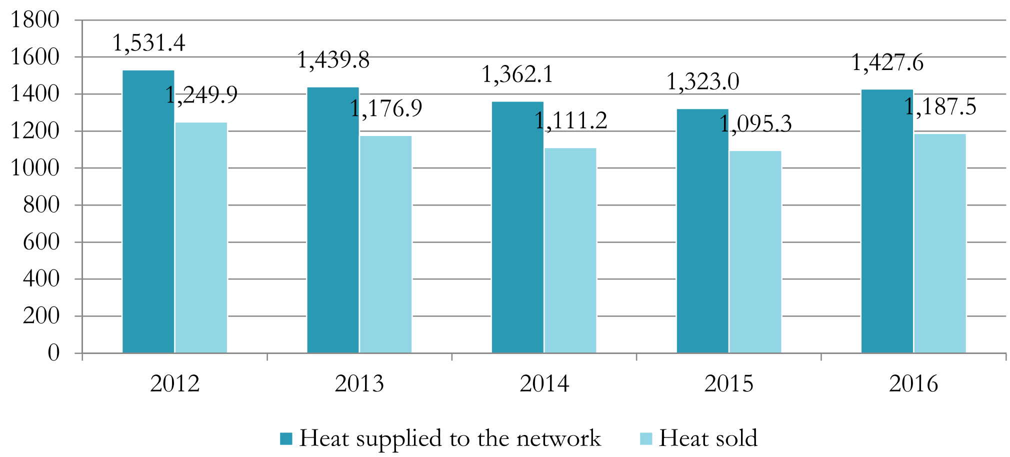
Comparison of non-financial indicators of the Company of the year 2016 with the indicators of the years 2012–2015 is provided in Table 3.

Table 3

No	Denomination of Indicator	2012	2013	2014	2015	2016
1.	Energy produced, purchased and supplied to the network, thous. MWh	1,532.9	1,442.2	1,364.8	1,326.3	1,428.1
1.1.	thermal energy	1,531.4	1,439.8	1,362.1	1,323.0	1,427.6
1.2.	electric energy	1.5	2.4	2.7	3.3	0.5
2.	Energy sold thous. MWh	1,251.4	1,179.3	1,113.9	1,098.6	1,188.0
2.1.	thermal energy	1,249.9	1,176.9	1,111.2	1,095.3	1,187.5
2.2.	electric energy	1.5	2.4	2.7	3.3	0.5
3.	Reconstructed heat supply pipelines, m	7,970	4,789	4,197	1,835	6,201
4.	Newly built heat supply pipelines, m	1,496	893	759	1,062	2,468

Chart 7

Heat supplied to the network, thous. MWh

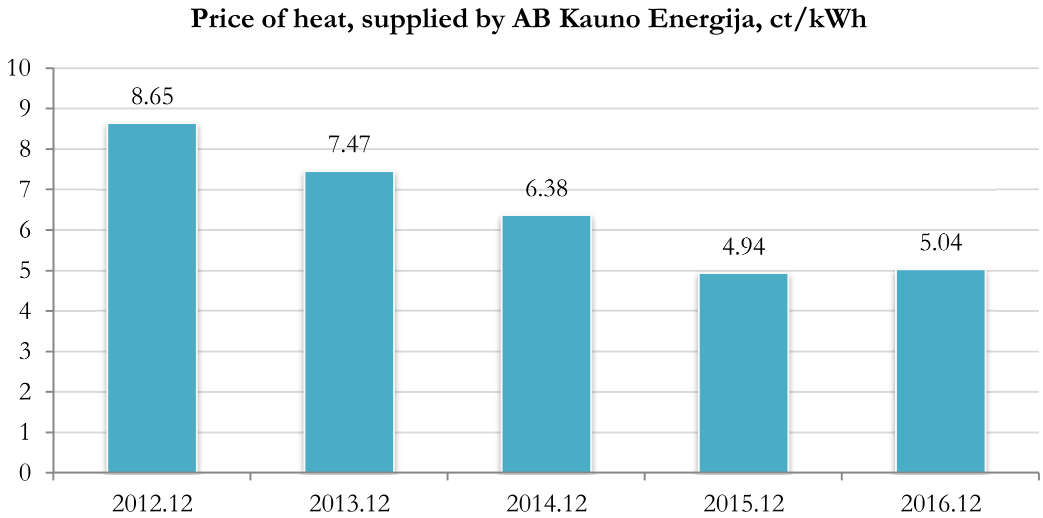


Environmental impact on operations: The Company's performance can be affected by changes in sales turnovers caused by changed heat demand, which can be caused by consumer investments in the renovation of buildings, heat saving and rational consumption, average higher of lower outdoor temperature during the heating season, changes in fuel prices, heat purchase price from IHP.

Company's reconstructed heat production facilities changing fossil fuel to biofuel will make a serious competition with their costs of production to IHP, operating in Kaunas. With modernization of its own production facilities the Company reduced heat price for its consumers by 33 per cent during the last 3 years.

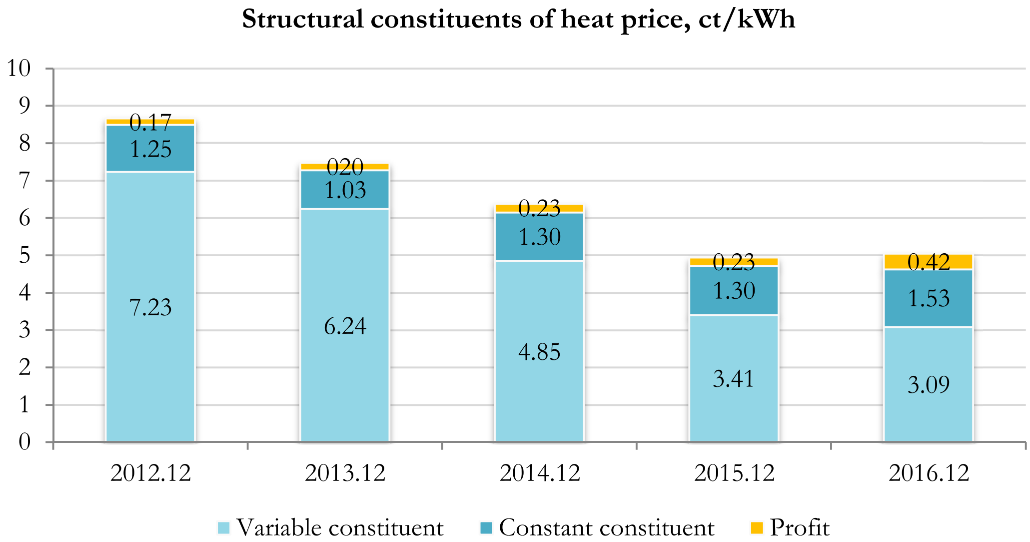
The dynamics of heat price of the Company in 2012–2016 is provided in Chart 8.

Chart 8



Components of Company's heat price structure in 2012–2016 are provided in Chart 9.

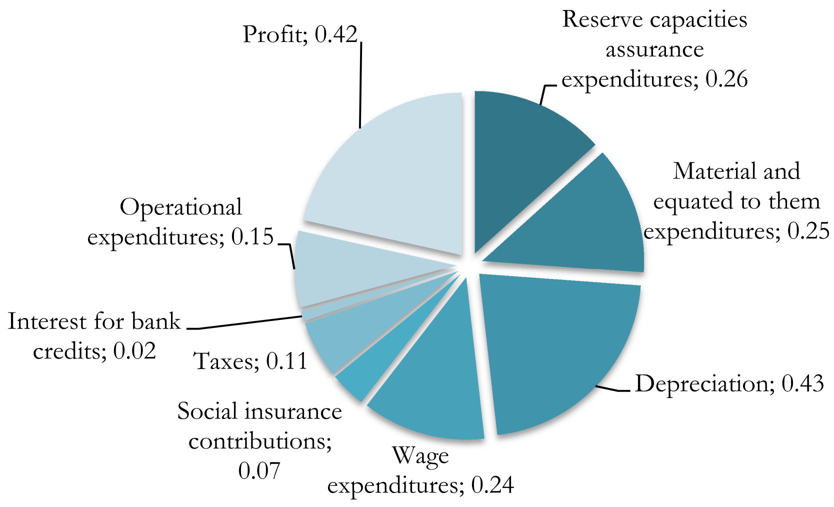
Chart 9



Management Board of AB Kauno Energija determined by its decision of 28 January 2016 No. 2016-2-2 (changed by the decision of AB Kauno Energija Management Board No. 2016-8-3 of 28 April 2016) a heat price constituents for the third year of validity of basic heat price, which were agreed by NCC's decision of 25 May 2016 No. O3-129. Constant constituent of heat price, valid until 31 May 2016 was 1.53 ct/kWh, and a new constant constituent, valid from 1 June 2016 is 1.95 ct/kWh (increase of constant constituent was determined by change in realized heat quantity, inflation, change in investment depreciation and new "expenditures of assurance of reserve capacities" – 0.26 ct/kWh). Details of constant heat price constituent are provided in Chart 10.

Chart 10

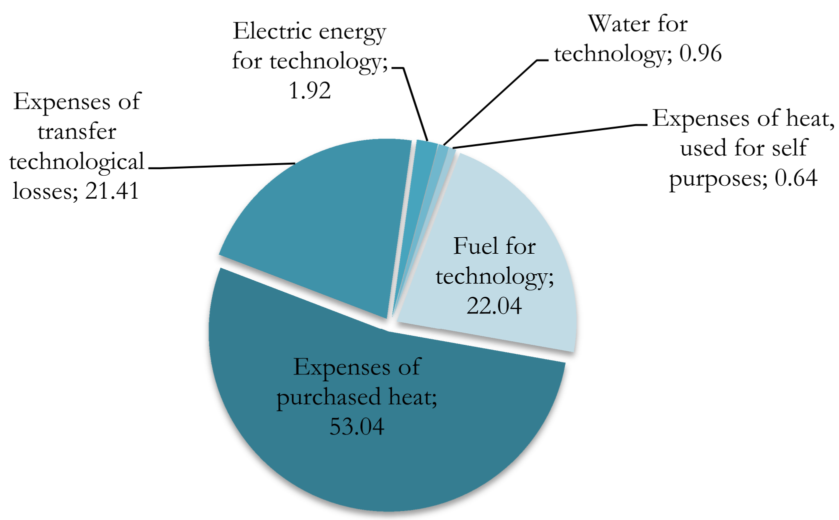
Heat price constant constituent, euro ct/kWh



The Company recalculates values of variable constituents of heat price and final heat prices every month, considering changes in prices of fuel and purchased heat. Details of variable heat price constituent of December 2016 are provided in Chart 11.

Chart 11

Heat price variable constituent in December 2016, per cent



Information related to environmental issues. In carrying out their activities, the Group and the Company seek to prudently use natural resources, install less polluting technologies, and follow the environmental legislation and apply preventive measures to minimize the negative impact on the environment.

Waste management. The Group and the Company have organized the waste collection, sorting and disposal of them to waste managers, i.e. to licensed waste management businesses. In 2016, the Group and the Company disposed for recycling 0.566 tons of waste of electric and electronic equipment, 1,389.76 tons of ash, 387 tons of debris, 1.56 tons of used tires, 0.10 tons of fluorescent lamps, 0.120 tons of building materials containing asbestos.

Wastewater management. In accordance with the schedule agreed with Kaunas Regional Environmental Protection Department, the Group and the Company constantly monitor that the effluent discharges from stationary sources are within the permissible limits set out in the integrated pollution prevention and control permits.

Air pollution. The measurement laboratory of stationary air pollution sources of the Group and the Company, having the permit issued by the Environmental Protection Agency, continuously monitors that the emissions to the atmosphere from stationary sources would not exceed the permissible limits established in integrated pollution prevention and control permits. Company's Šilkas, Ežerėlis, Girionys and Noreikiškės boiler-houses, and starting from 2015 – Inkaras boiler-house and Petrašiūnai power-plant use biofuel, thus reducing atmospheric pollution. Below in Table 4 you will find the comparison of the Company's pollutions to the atmosphere from stationary air pollution sources in 2016 with the amount in 2012-2015.

Table 4

Period	Particulates, t	Nitrogen oxides, t	Carbon monoxide, t	Sulphur dioxide, t	Hydrocarbons, t	Vanadium pentoxide, t	Other pollutants, t
2016	53.7542	265.0797	1155.3349	231.4719	4.2871	0.0000	0.2818
2015	43.5783	203.6775	904.8513	193.3228	20.1586	0.0000	0.2818
2014	23.613	154.570	534.443	47.158	16.294	0.0000	0.440
2013	10.5967	101.3197	299.6656	5.0747	14.9647	0.0000	0.770
2012	7.6130	54.3160	135.1510	6.0280	1.2080	0.0000	0.4397

Cyclones for smoke cleaning from particulates are installed in Šilkas, Ežerėlis, Girionys, Noreikiškės, Inkaras boiler-houses and Petrašiūnai power-plant. Their working efficiency is checked every year. The Company is involved in the greenhouse gas emissions trading system. This system includes emission allowances (EA) allocated to Petrašiūnai power-plant, Šilkas, Pergalė, Garliava, Jurbarkas boiler-houses and Noreikiškės boiler-house with a cogeneration power-plant.

8. References and additional explanations

Main financial data of the Group and the Company are provided in the explanatory notes to the consolidated and Company's financial statements for the year 2015.

Internal control over consolidated statements. When preparing its consolidated financial statements, the Company combines the itemised financial statements of the Company and its subsidiaries, by summing up the items of assets, liabilities, equity, revenue and expenses. Afterwards, it eliminates the book value of the Company‘s investment in the subsidiary and Company‘s share of equity in the subsidiary; amounts on balance sheets, transactions, income and expenses inside the Group (for this purpose, it prepares a reconciled report of all transactions, income and expenses for the period); difference in depreciation of contribution in kind measured at market value as compared to its book value.

For the purpose of the consolidated financial statements of the Group, the financial statements of the Company and subsidiaries are prepared for the same date.

It's controlled if the accounting policy of the company and its subsidiaries for accounting of similar transactions is the same. The subsidiaries' income and expenses are included into the consolidated financial statements as of the date of acquisition.

9. Significant events after the end of the year 2015

The decision of Supervisory Board of AB Kauno Energija No. 2017-1 has been made on 6 March 2017, following which the member of Management Board Vytautas Mikaila was recalled until the end of tenure.

On 25 March 2017 the audit of the financial statements for the year 2016 was accomplished. It was performed by the accounting and control company UAB Deloitte Lietuva (Auditor Certificate No 001275). Candidacy of the company performing audit of the financial statements for the year 2016 was proposed to General Meeting of Shareholders by Company's Management Board, following results of procurement, accomplished in 2015. The financial statements of the year 2016 with the independent auditor's conclusion on them are presented along with this Annual Report.

10. Plans and forecasts of activities of the group of companies

Inasmuch investments allow continual business development and profitability, the aims of the Group's and the Company's investment program for the year 2016 is further increase in volumes of heat production and effectiveness, expansion of heat selling market, through increase of use of biofuel for heat production, development of heat transmission and distribution increasing safety and reliability, developing services of maintenance of engineering systems and further improvement of consumers services quality.

In compliance with the provisions of the plan for the facilities on the implementation of the National Renewable Energy Development Strategy, in order to implement the Company's key business objectives and the provisions of the National Energy Independence Strategy related to the assurance of technical requirements for reliability of heat facilities and heat supply networks, to guarantee the quality keeps apply to consumers, the Company adjusted its investment plan for the year 2016.

On 7 February 2017 Kaunas city municipality decided to approve Company's investment plans for the new regulation period with the decision No. T-26 "Regarding Investment Plans of AB Kauno Energija for the Year 2017 and for the Years 2017 – 2020 and Its Financing".

The main investment goals of the Company for the regulation period of the years 2017–2020 are as follows: use of renewable energy sources, increase in reliability of heat supply to consumers in Kaunas and Jurbarkas cities an Kaunas district, and anticipated reception of EU Structural support under the 4 priority "Promoting energy efficiency and production and use of renewable energy" of Operational Programme for the European Union Funds' Investments in 2014-2020.

In 2017 the implementation of Company's investment program will involve further modernization of boiler-houses owned by the Company automating the production process and installing condensational economizers; reconstruction of heat networks; replacement of heat meters. Implementation of these measures will allow to reduce losses of heat transmission and to perform optimization of heat supply to the consumers and to ensure heat supplies reliability.

It is planned that in 2017 in comparison with 2016, the Group's sales turnover will be lower than in 2016 due to the decreased price of heat; the amount of heat sold to consumers will remain at the comparable level as in 2016. The greatest impact on the Group's and the Company's income and expenses will be made by fuel and purchased heat price changes, as the price of heat under the requirements of the law is recalculated every month. The Group's profit in comparison with 2016 is planned to be lower due to the recalculated constituents of heat price. The submitted data may be adjusted by change in heat demand, i.e. consumption, which is mainly affected by the average outdoor air temperature, the size of user investment in housing renovation, energy-saving and its rational use, as well as changes in the economic situation in Lithuania.

11. Information on research and development activities of the group of companies

On 23 June 2016 the Company signed an agreement with UAB E energija on acquisition of 100 % shares of UAB Petrašiūnų Katilinė. Agreement became valid on 30 June 2016. On 29 July 2016 the extraordinary meeting of shareholders has been held and the decision to approve the purchase – selling agreement of the shares of UAB Petrašiūnų katilinė, signed between the Company and UAB E energija of 23 June 2016 has been made in it. The transaction was accomplished on 27 October 2016, after clearance of merger by Competition Council of the Republic of Lithuania.

It's indicated in EU Directive of renewable sources and in Lithuanian national legal acts, that a part of renewable sources in total end energy consumption must consist not less, than 23 per cent until the year 2020, and the part falling on heating – up to 40 per cent. Meanwhile in Kaunas this indicator exceeds 80 per cent already.

Company's representatives are constantly invited to work in committees of preparation of Energy Engineering studies programs of Kaunas University of Technology and in groups of external and self-evaluation. Working in these groups and committees Company's representatives analyse aims of programs and goals of studies, composition of training plans, appropriateness of staff, material basis, process and evaluation of studies, as well as program management. Performing external and self-evaluation, committees apply recommendations for improvement of program structures and implementation process, in order to satisfy the needs of employers and to meet the requirements of national and European legal acts in the field of higher education.

On 21 April 2016 the Company hosted participants of International biomass energy conference "Nordic Baltic Bioenergy" that took place in Vilnius. The Company was presented to the guests as the company that made a biggest breakthrough in usage of biomass for heat production in the market. Conference guests from Sweden, Finland, France, Poland, Ukraine, Belarus and Lithuania visited the Company and its Inkaras boiler-house, which is considered one of the best boiler-houses of this type in Lithuania. Up to 10 per cent of heat consumed in Kaunas integrated network is produced in Inkaras boiler-house burning wooden chips.

On 24 November 2016 the Company hosted official delegation of specialists in energetics and businessmen from Belarus, accompanied by Ambassador Extraordinary and Plenipotentiary of the Republic of Belarus to the Republic of Lithuania H.E. Mr. Aleksandr Korol. Guests took part in energy effectiveness increasing seminar arranged in Company's premises and were interested Company's experience in implementation of technologies of usage of biofuel for heat production. Lithuania and Kaunas achievements in development of biofuel energetics were presented to the guests. It was emphasized, that the usage of biofuel for heat production and also competition in heat production sector let the Company reduce price of heat for consumers for more than a half starting from the year 2012.

Company's representatives took part as every year in national conference "Heat energetics and technologies" organized by Kaunas University of Technology at the end of January. This year the Company presented steps, which were made for further modernisation of Kaunas heat economy in order to reduce heat price for consumers.

The Company along with Lithuanian Energy Institute takes part in READY project ("Resource efficient cities implementing advanced smart city solutions") supported by European Commission. 23 companies from Denmark, Sweden, Austria, France and Lithuania take part in it. Project will be pursued until the year 2022 by applying the latest measures of effective energy consumption in Kaunas city.

Furthermore the Company takes part in programmes "Green Light" and "Motor Challenge", supported by European Commission, the aim of whose is effective energy consumption in lighting and pumps operation systems.

The project of implementation of quality management system (ISO 9001), standards of employees safety and health (OHSAS 18001) and environment protection management system (ISO 14001) was started in the Company in 2016 and its' accomplishment is anticipated in 2017.

12. Information on own shares acquired and held by the Issuer

The Company does not hold the shares of its own. The Company's subsidiaries have not purchased any of the Company's shares. Neither the Company nor its subsidiaries purchased or sold own shares during the reporting period.

13. Information on the aims of financial risk management, hedging instruments in use

All relevant information on this issue is provided in Notes 2.11, 15, 23 to the consolidated financial statements for the year 2016 of AB Kauno Energija.

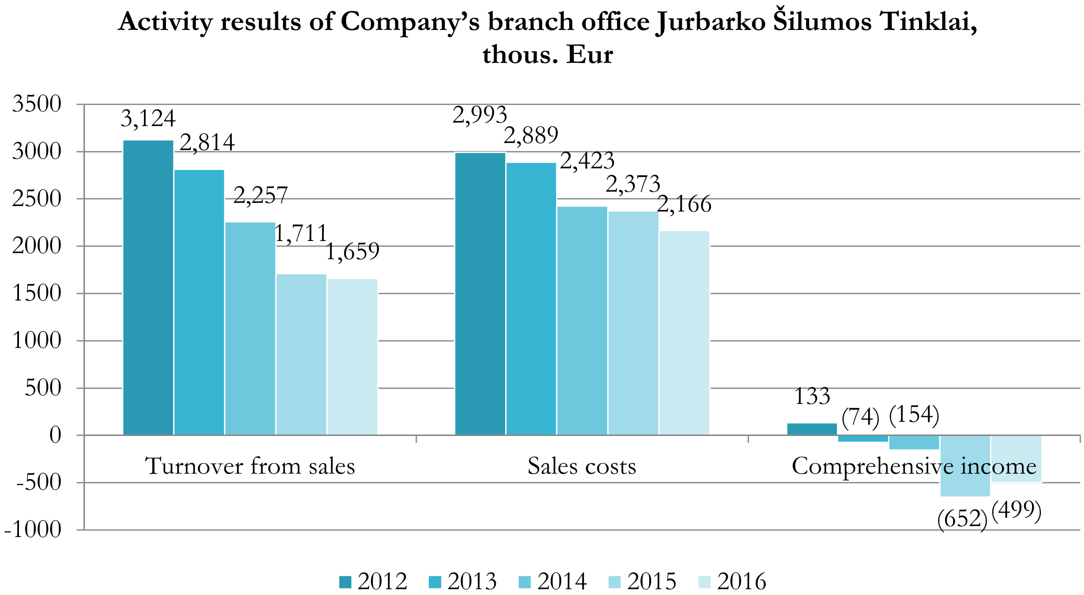
14. Information on the Issuer's branch office and subsidiary undertakings

The Company's affiliate Jurbarko Šilumos Tinklai was established by the decision of the Company's Management Board, and registered on 9 September 1997 at the address V. Kudirkos g. 33, 4430 Jurbarkas. The Company's affiliate produces and sells heat to consumers in the city of Jurbarkas.

The Company's affiliate Jurbarko Šilumos Tinklai had 31 employees as at 31 December 2016.

Comparison of financial indicators of Company's affiliate Jurbarko Šilumos Tinklai of the year 2016 with the indicators of the years 2012-2015 is provided in Chart 12.

Chart 12



Company's Board approved by its decision of 6 April 2012 a reorganization of subsidiary UAB Pastatų Priežiūros Paslaugos by separating assets from activities and by creating on the base of separated assets a new company with the same legal form, named UAB Kauno Energija NT.

After completion of the procedures of reorganisation in the way of separation of AB Kauno Energija subsidiary UAB Pastatų Priežiūros Paslaugos, a statutes of the newly established entity UAB Kauno Energija NT were registered in the Register of Legal Entities on 16 April 2013. Company's headquarter address is Savanorių pr. 347, 49423 Kaunas, company number 303042623.

The authorised capital of UAB Kauno Energija NT registered in the Register of Legal Entities on 31 December 2016 in total of 1,329,872 euros is divided into 45,921 ordinary nominal shares with the par value of 28.96 euros each.

UAB Kauno Energija NT has no holdings directly or indirectly managed in other companies.

Activities of UAB Kauno Energija NT include the real estate development, management, leases, purchase and sale.

Turnover of UAB Kauno Energija NT of the year 2016 was EUR 116 thousand, Comprehensive income was amounted to EUR (52) thousand.

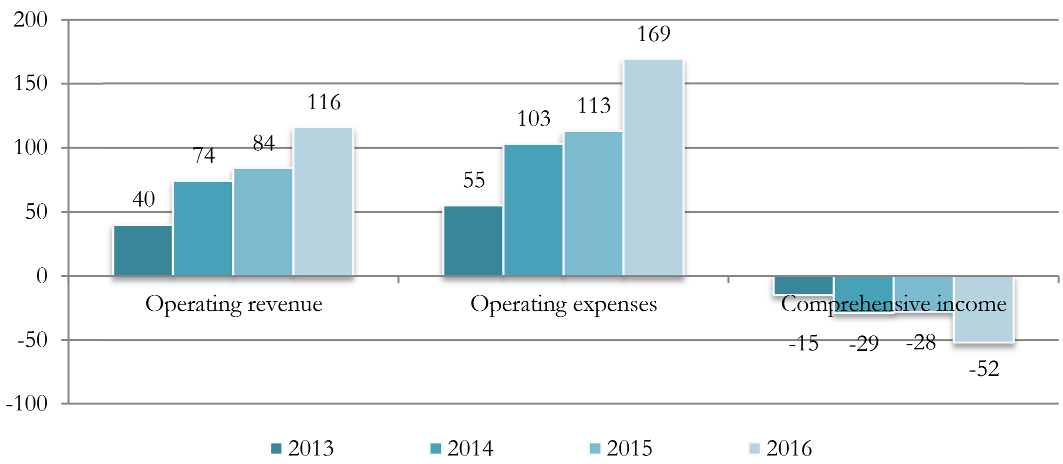
As at 31 December 2016 UAB Kauno Energija NT had 4 employees.

Comparison of financial indicators of UAB Kauno Energija NT of the year 2016 with the indicators of the years 2013-2015 is provided in Chart 13.

AB KAUNO ENERGIJA
Company code 235014830
Raudondvario Rd. 84, LT-47179 Kaunas, Lithuania

Chart 13

Activity results of UAB Kauno Energija NT, thous. euros



Statutes of newly established legal entity with the residence address R. Kalantos str. 49, 52303 Kaunas, code 304217723 were registered at the Register of Legal Entities on 27 October 2016 after accomplishment of procedures of acquisition of 100 per cent of the shares of UAB Petrašiūnų Katilinė.

Authorized capital of UAB Petrašiūnų Katilinė registered at the Register of Legal Entities on 31 December 2016 amounts to EUR 231,696 and is divided into 800 units of ordinary registered shares at par value of EUR 289.62 each.

UAB Petrašiūnų katilinė has no holdings directly or indirectly managed in other companies.

Activities of UAB Petrašiūnų Katilinė include production of heat.

UAB Petrašiūnų Katilinė had 9 employees as at 31 December 2016.

UAB Petrašiūnų Katilinė financial indicators of the year 2016 are as follows: operating revenue is EUR 717 thousand, operating expenses are EUR 635, and Comprehensive income is EUR 43 thousand.

15. Structure of authorized capital

The authorised capital of the Company registered in the Register of Legal Entities of the Republic of Lithuania on 31 December 2016 is EUR 74,475,728.82 (seventy four million four hundred seventy five thousand seven hundred twenty eight euros and 82 cents).

Structure of authorized share capital by types of shares is specified in Table 5.

Table 5

Type of shares	Number of shares, units	Nominal value, euros	Total nominal value, euros	Municipal share in the authorised capital, per cent	Share of private shareholders in the authorised capital, per cent
Ordinary nominal shares	42,802,143	1.74	74,475,728.82	98.33	1.67

16. Data on shares issued by the Issuer

The authorised capital of AB Kauno Energija was registered on 18 May 2015 by the decision of General Meeting of Shareholders held on 28 April 2015 and amounts to EUR 74,475,728.82 (seventy four million four hundred seventy five thousand seven hundred twenty eight euros and 82 cents) and it is divided to 42,802,143 (forty two million eight hundred and two thousand one hundred forty three) ordinary shares of par value of 1.74 euros each.

There are no limitations on the transfer of securities.

16.1. Main characteristics of shares released into free circulation of securities (as at 31 December 2016).

Securities registration No	A01031430
ISON code of securities	LT0000123010
Number of shares	20 031 977 ordinary nominal shares
Nominal value	EUR 1.74
Total nominal value of shares	EUR 34,855,639.98

16.2. Main characteristics of shares issued and registered for non-public trading (as at 31 December 2016).

ISON code of securities	LT0000128407
Number of shares	22,770,166 ordinary nominal shares
Nominal value	EUR 1.74
Total nominal value of shares	EUR 39,620,088.84

History of trade in Company's securities in 2012–2016 is provided in Table 6.

Table 6

Indicator	2012	2013	2014	2015	2016
Opening price, euro	0.565	0.578	0.589	0.486	0.459
Highest price, euro	0.590	0.589	0.600	0.479	0.600
Lowest price, euro	0.415	0.458	0.430	0.400	0.401
Last price, euro	0.578	0.589	0.486	0.459	0.560
Circulation, units	80,421	36,355	70,160	41,193	190,801
Circulation, million euro	0.04	0.02	0.04	0.02	0.10
Capitalisation, million euro	11.58	11.80	9.74	9.19	11.22

Historical data on share prices (in euro) and turnovers in 2012–2016 is provided in Chart 14.

Chart 14

Comparison of Company's share price with the index of own sector (utility services) and OMX Vilnius index is given in Chart 15.

Chart 15

Data of Chart 15:

Index/Shares	01.01.2012	31.12.2016	+/-%
OMX Baltic Benchmark GI	431.94	788.17	82.47
OMX Vilnius	298.78	558.50	86.93
B7000GI Utilities	808.28	2,158.02	166.99
KNR1L	0.350 EUR	0.560 EUR	60.00

17. Information on the Issuer‘s shareholders

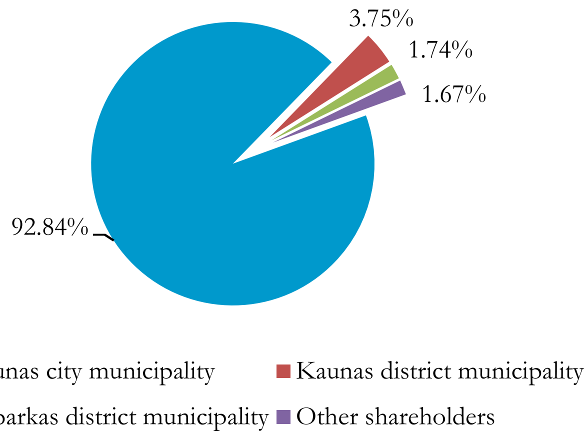
The total number of Company's shareholders as at 31 December 2016 was 295.
Information on Shareholders of the Issuer who owned as at 31 December 2016 more than 5 per cent of the authorised capital of the Company registered on 18 May 2015 (42,802,143 ordinary nominal shares), is provided in Table 7 and Chart 16.

Table 7

Full name of shareholder (company name, type, headquartered dress, code)	Number of ordinary nominal shares owned by the shareholder, units	Owned share in the authorised capital, per cent	Share of votes carried by owned shares. per cent	Share of votes owned by the shareholder together with acting entities, per cent
Kaunas City Municipality Laisvės al. 96, 44251 Kaunas Code 111106319	39,736,058	92.84	92.84	-
Other shareholders	3,066,085	7.16	7.16	-
Total:	42,802,143	100	100	-

Chart 16

Structure of shareholders as at 31 December 2016



Repartition of shareholders in accordance with groups at the end of the reporting period is provided in table 8.

Table 8

The name of the Group	Number of shares owned by the Group, pcs.	Own part of share capital, per cent from all the shares
Local authorities	42,088,631	98.33
Households	366,593	0.85
Securities of other accounts keepers clients	238,411	0.56
Private non-financial enterprises	83,508	0.20
Other financial brokers, except insurance companies and pension funds and other auxiliary enterprises	25,000	0.06
Other shareholders (non-financial enterprises controlled from abroad, financial auxiliary enterprises, companies holing deposits, except central bank	0	0.00
Total	42,802,143	100

17.1. The shareholders, who owned more than 5 per cent of the shares (20,031,977 ORS) issued for public trading (reg. No. A01031430, VP ISIN code – LT0000123010) as at 31 December 2016 are listed in Table 9.

Table 9

Name	Type of shares	Number of shares, units	Total nominal value of shares, euros	Percentage of shares from those released into the public circulation	Share of the authorised capital (%)
Kaunas City Municipality Laisvės al. 96, 44251 Kaunas Code 111106319	Ordinary registered shares	16,965,892	29,520,652	84.69	39.64
Kaunas District Municipality Savanorių pr. 371, 49500 Kaunas, Code 111100622	Ordinary registered shares	1,606,168	2,794,732	8.02	3.75
Other shareholders	Ordinary registered shares	1,459,917	2,540,256	7.29	3.41
Total:		20,031,977	34,855,640	100	46.80

17.2. The shareholders, who owned more than 5 per cent of the shares (22,770,166 ORS) issued for non-public trading (VP ISIN code – LT0000128407) as at 31 December 2016 are listed in Table 10.

Table 10

Name	Type of shares	Number of shares, units	Total nominal value of shares, Euro	Percentage of shares from those released into the public circulation	Share of the authorised capital (%)
Kaunas City Municipality Laisvės al. 96, 44251 Kaunas Code 111106319	Ordinary registered shares	22,770,166	39,620,089	100	53.20

None of the shareholders of the Issuer holds any special rights of control. The rights of all shareholders are the same; they are specified in article 4 of the Law on Companies of the Republic of Lithuania. The number of shares carrying votes at the General Meeting of Shareholders of the Company is 42,802,143 units.

The Company has not been notified on the limitations of voting rights or any other mutual agreements of shareholders which may limit the transfer of securities and / or voting rights.

In 2012, the dividends from the profit of the year 2011 were allocated and paid to the shareholders of the Issuer. Dividend per share was 0.072 euro, in total 3.094 million euros.

In 2013, no dividends from the profit of the year 2012 were allocated and paid to the shareholders of the Issuer. Following the decision no 3 of the General Meeting of Shareholders, the profit was allocated to the statutory reserve, other reserves (repair of heating units), support, and part of the profit was transferred to the next financial year. A total of 0.043 million euros was allocated for sponsorship and charity.

In 2014, the dividends from the profit of the year 2013 were allocated and paid to the shareholders of the Issuer. Dividend per share was 0.0028962 euro, in total – 0.124 million euro. The profit was allocated to the statutory reserve, other reserves, support and annual payments for members of the Board. A total of 0.333 million euros was allocated for sponsorship and charity.

In 2015, the dividends from the profit of the year 2014 were allocated and paid to the shareholders of the Issuer. Dividend per share was 0.003 euro, in total – 0.129 million euro. The profit was allocated to the statutory reserve, other reserves. A total of 0.2 million euros was allocated for sponsorship and charity.

In 2016, the dividends from the profit of the year 2015 were allocated and paid to the shareholders of the Issuer. Dividend per share was 0.042 euro, in total – 1.798 million euro. The profit was allocated to the statutory reserve, other reserves, bonuses for the members of the Management Board and bonuses for employees. A total of 0.05 million euros was allocated for sponsorship.

18. Employees

A total of 521 employees were employed in the Group as at 31 December 2016. Changes in the number of employees of the Group in 2012–2016 are specified in Table 11.

Table 11

Actual number of employees	Group 2012-12-31	Group 2013-12-31	Group 2014-12-31	Group 2015-12-31	Group 2016-12-31
Total:	617	561	545	526	521
including: management	6	7	6	4	6
specialists	327	292	290	279	284
workers	284	262	249	243	231

Changes in the number of employees of the Company in 2012–2016 are specified in Table 12.

Table 12

Actual number of employees	Company 2012-12-31	Company 2013-12-31	Company 2014-12-31	Company 2015-12-31	Company 2016-12-31
Total:	583	548	542	523	508
including: management	4	5	4	3	4
specialists	314	288	290	278	280
workers	265	255	248	242	224

Education of employees of the Group at the end of the reporting period.

Table 13

No	Education	Group 2012-12-31	Group 2013-12-31	Group 2014-12-31	Group 2015-12-31	Group 2016-12-31
1	Secondary incomplete	9	6	6	7	5
2	Secondary	231	217	206	195	187
3	College	89	80	77	72	73
4	Higher	288	258	256	252	256
	Total:	617	561	545	526	521

Education of employees of the Company at the end of the reporting period.

Table 14

No	Education	Company 2012-12-31	Company 2013-12-31	Company 2014-12-31	Company 2015-12-31	Company 2016-12-31
1	Secondary incomplete	8	5	6	7	5
2	Secondary	217	211	205	194	183
3	College	83	78	77	72	71
4	Higher	275	254	254	250	249
	Total:	583	548	542	523	508

Average conditional number of employees and average monthly salary Eur (at the end of 2016 before taxes)

Table 15

No	Employees	Company	Group
1.1.	Average conditional number of managers	3.25	5.4
1.2.	Average monthly salary of managers	3,578.1	2,592.0
2.1.	Average conditional number of specialists	255.9	259.9
2.2.	Average monthly salary of specialists	994.1	992.5
3.1.	Average conditional number of workers	223.8	231.7
3.2.	Average monthly salary of workers	711.4	706.0

Company's management pays a lot of attention to increase in work efficiency, to improve working conditions, to supply of the latest working tools, professional development, planning of internal activities and control implementation, also for improvement of consumer service quality. Executive and professional qualification levels suits their positions, and work experience and practical knowledge of subject of other employees makes them possible to work in their positions. Staff turnover in the Group and the Company is inconsiderable.

In order to increase work efficiency, the company conducts an annual work performance evaluation of managers of structural units, the main goal of which is to evaluate the employee's qualifications and abilities to perform functions assigned in job regulations, to properly evaluate employees' activities, provide feedback on the goals execution in order to increase employee loyalty, satisfaction with conducted work, encouraging them to improve. The result of this process is information allowing for better coordination of the Company's activities and for encouraging employees to improve their working activities.

The company actively cooperates with educational institutions and allow high school students to apply their theoretical knowledge and gain practical skills. 12 students performed their internship in the Company in 2016. With demand for new workers, the most active and best students are provided with access to employment in the Company.

In 2015-2016, the Company participated in the implementation of the National targeted financing studies program and in cooperation with the Kaunas University of Technology signed a tripartite targeted study financing agreements with two first-year students of heat energy and technology program.

The salary of employees of the Issuer consists of the constant part of salary, variable part of salary, benefits and allocations paid according to the Labour Code of the Republic of Lithuania and other laws, Collective agreement of the Company, and bonuses. Bonuses are paid from net profit, if the General Meeting of Shareholders allocates part of the profit for the bonuses of the Company employees. From 1998 till 2014, the General Meeting of Shareholders has never allocated any part of the profit for the bonuses of the Issuer's employees. EUR 207 thousand were allocated as bonuses to employees from the profit of the year 2015 by the meeting of shareholders in 2016.

The Collective agreement provides the special rights and responsibilities of the Issuer's employees or part of them. Under the Collective agreement that became effective in the Company on 28 January 2013:

1. For continuous employment within the Company employees are granted additional paid leave.
2. The length of service of employees of the Lithuanian power system companies transferred to the Company according to the corporate employer agreement, i.e. when the transfer was carried out according to the Labour Code or the Law on Employment Contract, is considered not interrupted, and such employees are granted additional paid leave for a continuous period of employment with the Company.
3. At the agreement of the employer and employee, the employee may be granted unpaid leave for family related issues and other important reasons.
4. Company's employees are entitled to additional paid leave.

The employer obligates:

1. To ensure the conditions of preventive health check and, if necessary, rehabilitation treatment of employees, to provide free health services at the Company's occupational health unit;
2. In case of death of an employee, the Company pays an allowance in the amount of two monthly average salaries of the last year of the Company or a branch (depending on where the employee has worked), gives free transport or covers transport costs. The allowance is granted to the burying person;
3. In case of death of a close relative of the employee (father, mother, child, or spouse), the employee is granted the allowance of the average salary of the previous year of the Company or an affiliate (depending on where the employee works), given free transport or transport costs are covered;
4. In case of birth of one or more children, employees are granted 50 per cent of the of the average salary of the previous year of the Company or an affiliate (depending on where the employee works) for each child;
5. In case of wedding, employees are granted 50 per cent of the of the average salary of the previous year of the Company or an affiliate (depending on where the employee works);
6. Employees who are raising three or more children under the age of 16, widows (widowers) and unmarried persons who raise one child or children alone, if they are studying at secondary schools until the age of 19, and while studying at higher schools or colleges full-time till the age of 21, or if they are caring for other family members with heavy or moderate disability level or lower than 55 per cent working ability level, or family members who have reached the retirement age, which according to the laws are established a major or moderate level of special needs, once a year are granted 50 per cent of the of the average salary of the previous year of the Company or an affiliate (depending on where the employee works) according to the date of request;
7. For the 40th, 50th and 60th anniversary, as proposed by the head of the division, for excellent performance of employees having the 15 and 20 years of continuous employment with the Company are granted a monetary gift of 25 per cent, and having over 20 years of continuous work experience – a monetary gift of 50 per cent of the average salary of the previous year of the Company or an affiliate (depending on where the employee worked);
8. In other cases, where the material support is needed (loss due to natural disasters or other reasons beyond the employee's control), at the mutual agreement of the representatives who have signed the Collective Agreement, employees are granted a benefit of up to 580 euros,
9. In the event of a serious illness or accident of the employee, he is granted an allowance of up to 5 average salaries of the previous year of the Company or an affiliate (depending on where the employee worked) at the mutual agreement of the representatives who have signed the Collective Agreement;

10. For the occasions of the Lithuanian Energy Day and jubilees of the Company deserving employees are granted a monetary gift of up to 145 euros.

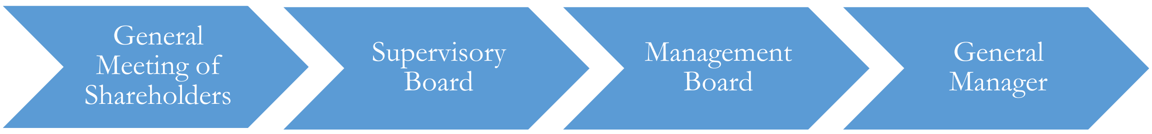
19. Procedure for amending the Issuer‘s Articles of Association

The statutes of the Issuer say that the General Meeting of Shareholders of the Company has the exceptional right to amend the statutes other than the exceptions provided in the Law on Companies of the Republic of Lithuania. The resolution on the amendment of the Company's statutes 2/3 qualified majority of votes of the members participating in the meeting of shareholders is needed.

The statutes of the Company were amended on 28 April 2016 by the decision of the General Meeting of Shareholders. A number of members of Management Board of the Company decreased from 7 (seven) to 5 (five) in these statutes, and the remuneration for the activity of members of the Management Board was anticipated. The new version of the statutes was registered in the Register of Legal Entities of the Republic of Lithuania on 13 May 2016. It can be found in the Internet website of the Company at www.kaunoenergija.lt.

20. Issuer‘s management bodies

According to the statutes of the Company, the management bodies of the Company include the General Meeting of Shareholders, a collegial management body – the Supervisory Board, a collegial management body – the Management Board, and a sole management body – General Manager.



Decisions of the General Meeting of Shareholders made on the issues within the competence of the General Meeting of Shareholders provided for in the statutes of the Company are binding to its shareholders, the Supervisory Board, the Management Board and the General Manager, and also to other employees of the Company.

All persons who are the shareholders of the Company on the date of the General Meeting of Shareholders have the right to attend the Company's General Meeting of Shareholders personally or by proxy, or be represented by persons with whom they had entered into the agreement on the transfer of the voting right. The record date of the meeting of the Company is the fifth working day before the General Meeting of Shareholders or the fifth working day before the repeat General Meeting of Shareholders. A person attending the General Meeting and entitled to vote shall provide a document which is a proof of his personal identity and sign the registration list of the Meeting of Shareholders. A person who is not a shareholder shall additionally provide a document attesting to his right to vote at the General Meeting of Shareholders.

2 (two) General Meetings of Shareholders were convoked in 2016. Company's General Manager and the Chief Finance Officer took part in them. Issuers' shareholders are allowed to ask questions and to get answers or explanations from Company's managers and speakers.

The collegial management body – Supervisory Board is elected by the General Meeting of Shareholders according to the procedure specified in the Law on Companies of the Republic of Lithuania. The Supervisory Board consists of 7 (seven) members. The Supervisory Board is elected for a term of 4 (four) years. The Supervisory Board elects the chairman of the Supervisory Board from among its members. The General Meeting of shareholders may remove from office the entire Supervisory Board or its individual members before the expiry of the term of office of the Supervisory Board. Where individual members of the Supervisory Board are elected, they shall be elected only until the expiry of the term of office of the current Supervisory Board.

The Supervisory Board elects and dismisses the Board members and supervises the activities of the Board and the General manager of the Company; submits its comments and proposals to the General Meeting of Shareholders on the Company's operating strategy, set of annual financial statements, draft of profit / loss allocation and the annual report of the Company as well as the activities of the Board and the General manager of the Company; submits proposals to the Board and the General manager of the Company to revoke their decisions which are in conflict with laws and other legal acts, the statutes of the Company or decisions of the General Meeting of Shareholders; addresses other issues assigned to the scope of powers of the Supervisory Board by decisions of the General Meeting of Shareholders regarding the supervision of the activities of the Company and its management bodies. The Supervisory Board shall not be entitled to assign or delegate the functions assigned to the scope of its powers by the Law on Companies of the Republic of Lithuania and the statutes of the Company to other organs of the Company.

The Supervisory Board, following resolution No 1K-18 of 21 August 2008 of the Securities Commission of the Republic of Lithuania „On the requirement for Audit Committees“, „Guidelines for the application of requirements for Audit Committees“, approved in the decision of 28 November 2008 of the Securities Commission, approves the internal rules of procedure for forming the Audit Committee, and electing the Audit Committee members.

The Supervisory Board of the Company approved a new version of the internal rules of procedure of the Audit Committee of AB Kauno Energija on 26 October 2015.

The Management Board is a collegial management body of the Company. The Management Board is comprised of 5 (five) members. The Management Board is elected for the period of 4 (four) years by the Supervisory Board. The Supervisory Board can remove from office the entire Management Board *incorpore* or its individual members before the expiry of their term. If individual members of the Management Board are elected, they shall serve only until the expiry of the term of office of the current Management Board. The Management Board elects the chairman of the management Board from among its members.

The General Manager is the manager of the Company. The manager of the Company is a sole person management body of the Company organising its activities. Powers and responsibilities of the administration members of the Company are established in the order of the General Manager.

20.1. Data on the committees in the Company

On 26 October 2015 the Supervisory Board appointed by the decision No. 2015-4 the members of Audit Committee:

Full name	Position	Beginning of term	End of term*
Edita Plūkienė	Independent member of Audit Committee	27 October 2015	29 May 2019
Židrūnas Garšva	Independent member of Audit Committee	27 October 2015	29 May 2019
Audrius Lukoševičius	Independent member of Audit Committee	27 October 2015	29 May 2019
Inga Šliačkuvienė	Member of Audit Committee	27 October 2015	29 May 2019
Aušra Smolskienė	Member of Audit Committee	27 October 2015	29 May 2019
Juozas Gontis	Member of Audit Committee	27 October 2015	29 May 2019

** The term of office of the Audit Committee coincides with the term of office of the Supervisory Board of the Company.*

In carrying out its activities, the Audit Committee follows the internal rules of procedure of the Company's Audit Committee approved by decision No 2015-4 of 26 October 2015 of the meeting of the Supervisory Board of the Company. The Audit Committee performs its functions provided for in article 52 of the Law on Audit of the Republic of Lithuania. The Audit Committee had no sessions in 2015.

Mrs. Edita Plūkienė is a Project Manager of UAB Aksa Holdingas, Director of UAB Amžiaus Pasaka, Director of UAB Savas Kazino, and member of public organization Vieningas Kaunas, member of Kaunas city municipality council. She was elected as a member of Company's independent Audit Committee on 26 October 2015. Education – University degree, master in agricultural economy from Aleksandras Stulginskis University

(1993). Mrs. Edita Plūkienė holds no shares of the Company. No interest in the capital of other Lithuanian companies.

Mr. Židrūnas Garšva is a member of the Kaunas City Municipality Council, member of Committee of City Economy and Services, member of Supervisory Board of AB Kauno Energija, General Manager of UAB Dextera, member of supervisory board of Public Institution K. Grinius Nursing and Sustaining Treatment Hospital, Chairman of the Supervisory Board of Public institution Kaunas Central Clinic, also involved in personal business (activities such as head offices and management consultancy activities). He was elected as a member of Company's independent Audit Committee on 26 October 2015. Education – University degree, bachelor in economy from Kaunas University of Technology (2007). Workplaces and positions held over the last 10 years: 1996 – 2008 and from 2015 – General Manager of UAB Dextera. Mr. Židrūnas Garšva holds no shares of the Company. Mr. Ž. Garšva holds the shares of UAB Dextera Holding.

Mr. Audrius Lukoševičius is Director of budgetary institution "Kauno biudžetinių įstaigų buhalterinė apskaita" Specialist of supervision of credit unions of Lithuanian Central Credit Union, voluntary assistant of member of Kaunas city municipality Rimantas Mikaitis, member of the board of Public institution "Automobilių stovėjimo aikštelės", member of the board of association "Kauno mažoji beisbolo lyga". He was elected as a member of Company's independent Audit Committee on 26 October 2015. Education – University degree, bachelor in business administration and management from Vilnius University (1996), master in business administration and management from Vilnius University (1998). Workplaces and positions held over the last 10 years: 08.2004–12.2013 – Manager of customer service centre at Swedbank, AB, 04.2015–12.2015 – Specialist of supervision of credit unions of Lithuanian Central Credit Union. Mr. Audrius Lukoševičius holds no shares of the Company. No interest in the capital of other Lithuanian companies.

Mrs. Inga Šliačkuvienė is a Deputy Chief Accountant of the Company. She was elected as a member of Company's Audit Committee on 26 October 2015. Education – University degree, bachelor in economy from Faculty of Economy and Management of Kaunas University of Technology (2007). Workplaces and positions held over the last 10 years: 08.2009–05.2014 – senior accountant of the Company. Mrs. Inga Šliačkuvienė holds no shares of the Company. No interest in the capital of other Lithuanian companies.

Mrs Aušra Smolskienė is a senior economist of Economy and Planning Division of the Company. She was elected as a member of Company's Audit Committee on 26 October 2015. Education – University degree, bachelor in management and business from Faculty of Economy and Management of Kaunas University of Technology (2008), master in economy from Faculty of Economy and Management of Kaunas University of Technology (2010). Workplaces and positions held over the last 10 years: 10.2003–02.2007 – Technical secretary of Public Relations Division of the Company. Mrs. Aušra Smolskienė holds no shares of the Company. No interest in the capital of other Lithuanian companies.

Mr. Juozas Gontis is a senior lawyer of the Law Division of the Department of Law and Purchases of the Company. He was elected as a member of Company's Audit Committee on 26 October 2015. Education – University degree, bachelor in English philology from Vilnius University (1998), master in international law from Vytautas Magnus University (2002). Workplaces and positions held over the last 10 years: 08.2002–06.2010 – senior solicitor of Kaunas branch of Bank of Lithuania, 08.2010–03.2012 – lawyer of UAB Vilniaus Valda, 04.2014–11.2014 – lawyer of AB Kauno Dujotiekio Statyba, 09.2010–12.2014 – lawyer of UAB Rotada, 08.2010–12.2014 – lawyer of UAB KDS Group. Mr. Juozas Gontis holds no shares of the Company. No interest in the capital of other Lithuanian companies.

21. Members of collegiate bodies, Company's manager, chief financier

21.1. Information about the members of the Company's Supervisory Board:

Members of the Supervisory Board of the Company as at 31 December 2016:

Full name	Position	Beginning of term	End of term
Visvaldas Matijošaitis	Chairman of the Supervisory Board	29 May 2015	29 May 2019
Povilas Mačiulis	Deputy Chairman of the Supervisory	29 May 2015	29 May 2019

	Board		
Tomas Bagdonavičius	Member of the Supervisory Board	29 May 2015	29 May 2019
Visvaldas Varžinskas	Member of the Supervisory Board	29 May 2015	29 May 2019
Rimantas Mikaitis	Member of the Supervisory Board	29 May 2015	29 May 2019
Židrūnas Garšva	Member of the Supervisory Board	29 May 2015	29 May 2019
Andrius Palionis	Member of the Supervisory Board	29 May 2015	29 May 2019

The Company's Supervisory Board consists of seven dependant members, who are also the members of the Kaunas City Municipality Council, as they partially represent the controlling shareholder, i.e. Kaunas City Municipality, holding 92.84 per cent of the Company's voting shares.

2 sessions of the Supervisory Board were held during the year 2016. More than ½ of members of the Supervisory Board attended all the sessions.

Mr. Visvaldas Matijošaitis is a Mayor of Kaunas city, Member of the Kaunas City Municipality Council. He is also a founder, leader and Chairman of the board of public organization Vieningas Kaunas (United Kaunas), Chairman of the board of association Mentor Lietuva, President of association Žalgirio Fondas (Žalgiris Fund), President of Lithuanian federation of cycling, Vice-president of Council of Lithuanian economic and trade cooperation with Russian Federation of Lithuanian Confederation of Industrialists. Mr. Visvaldas Matijošaitis holds no shares of the Company. Mr. V. Matijošaitis holds the shares of Vičiūnai Group of companies.

Mr. Povilas Mačiulis is a Deputy Mayor of Kaunas city, member of the Kaunas City Municipality Council (Deputy Chairman of Committee of City Economy and Services), Deputy Chairman of Kaunas Regional Development Council, and member of the board of public organization Vieningas Kaunas (United Kaunas), Director of Public Institution Maironio Fondas (Maironis Fund). Mr. Povilas Mačiulis holds no shares of the Company. Mr. P. Mačiulis holds the shares of UAB Munava.

Mr. Rimantas Mikaitis is a member of the Kaunas City Municipality Council, Head of Public Institution Centre for Liberty Studies. Mr. Rimantas Mikaitis holds no shares of the Company. No interest in the capital of other Lithuanian companies.

Dr. Visvaldas Varžinskas is a member of the Kaunas City Municipality Council, Chairman of Committee of Sustainable Development and Investments, Docent of Environmental Engineering Institute of Kaunas University of Technology, Head of Centre of Packaging Innovations and research of Kaunas University of Technology, member of special workgroup Strategic Development of Lithuanian Packaging Industry of Small and medium-sized business council (at the Ministry of Economy of the Republic of Lithuania), member of the board of public organization Vieningas Kaunas, member of expert group of Sustainable Development and Urbanism of Kaunas city Business council, member of council of National Cluster of Renewable Energy of Baltic Littoral. Mr. Visvaldas Varžinskas holds no shares of the Company. No interest in the capital of other Lithuanian companies.

Mr. Tomas Bagdonavičius is a member of the Kaunas City Municipality Council, head of Business planning and analysis of UAB Vičiūnai Group, member of public organization Vieningas Kaunas (United Kaunas). Mr. Tomas Bagdonavičius holds no shares of the Company. Mr. T. Bagdonavičius holds the shares of UAB Baltic Fish Export.

Mr. Židrūnas Garšva is a Member of the Kaunas City Municipality Council, Head of Committee of City Economy of Kaunas City Council, General Manager of UAB Dextera, Member of supervisory board of Public Institution K. Grinius Nursing and Sustaining Treatment Hospital also involved in personal business (activities such as head offices and management consultancy activities). Mr. Židrūnas Garšva holds no shares of the Company. Mr. Ž. Garšva holds the shares of UAB Dextera Holding.

Mr. Andrius Palionis is a member of the Kaunas City Municipality Council, Director of Irena Matijošaitienė fund, Director of public organization Vieningas Kaunas (United Kaunas), member of Kaunas city Youth Affairs Council. Mr. Andrius Palionis holds no shares of the Company. No interest in the capital of other Lithuanian companies.

21.2. Information on the members of the Company‘s Management Board

Members of Company‘s Management Board as at 31 December 2016:

Full name	Position	Beginning of term	End of term
Vytautas Mikaila	Chairman of the Management Board	1 June 2015	6 March 2017
Algimantas Stasys Anužis	Deputy chairman of the Management Board	1 June 2015	1 June 2019
Eugenijus Ušpuras	Member of the Management Board	1 June 2015	1 June 2019
Nerijus Mordas	Member of the Management Board	1 June 2015	1 June 2019
Giedrius Bielskus	Member of the Management Board	1 June 2015	1 June 2019

26 sessions of Company's Management Board were held in the year 2016. More than 2/3 members of the Management Board attended all the sessions.

Mr. Vytautas Mikaila is a doctor in engineering, Director of UAB MVE Group, member of Association of Heating Technics Engineers, member of Rotary Club Kauno Tauras, honorary consul of Slovak Republic in Lithuania, Manager of the Company's Strategy and Investment Projects department from 1 July 2015 to 13 May 2016. He was a chairman of the Company's Management Board from 1 June 2015 to 6 March 2017. Mr. Vytautas Mikaila holds no shares of the Company. He holds 55% of shares of UAB MVE Group. Mr. Vytautas Mikaila charged EUR 5.26 thousand of salary in 2016, also EUR 8.61 thousand of remuneration under agreement of activity of member of the Management Board, bonuses from the profit of the year 2015 in amount of EUR 6.48 housand were estimated, nor any assets were transferred or guarantees issued during the reporting period.

Mr. Algimantas Stasys Anužis is a member of the Management Board of UAB Kauno Švara, member of the Council of Kaunas Chamber of Commerce, Industry and Crafts, president of Lithuanian Veterans Basketball League. He is a member of Company's Management Board from 1 June 2015. Mr. Algimantas Stasys Anužis holds no shares of the Company. No interest in the capital of other Lithuanian companies. Mr. Algimantas Stasys Anužis charged EUR 5.16 thousand of remuneration under agreement of activity of member of the Management Board, bonuses from the profit of the year 2015 in amount of EUR 6.48 thousand were estimated, nor any assets were transferred or guarantees issued during the reporting period.

Mr. Eugenijus Ušpuras is a habilitated doctor, chief of Laboratory of Nuclear Installation Safety, Lithuanian Energetic, full member of the Lithuanian Academy of Sciences, professor, and member of Company's Management Board from 1 June 2015. Mr. Eugenijus Ušpuras holds no shares of the Company. No interest in the capital of other Lithuanian companies. Mr. Eugenijus Ušpuras charged EUR 5.16 thousand of remuneration under agreement of activity of member of the Management Board, bonuses from the profit of the year 2015 in amount of EUR 6.48 thousand were estimated, nor any assets were transferred or guarantees issued during the reporting period.

Mr. Giedrius Bielskus is a director of public institution S. Dariaus ir S. Girėno Sporto Centras (S. Darius and S. Girėnas Sports Centre), member of Company's Management Board from 1 June 2015. Mr. Giedrius Bielskus holds no shares of the Company. No interest in the capital of other Lithuanian companies. Mr. Giedrius Bielskus charged EUR 5.16 thousand of remuneration under agreement of activity of member of the Management Board, bonuses from the profit of the year 2015 in amount of EUR 6.48 thousand were estimated, nor any assets were transferred or guarantees issued during the reporting period.

Mr. Nerijus Mordas is a chief finance officer for Eastern European and Asian markets of UAB Vičiūnų Grupė (UAB Vičiūnai Group), member of Company's Management Board from 1 June 2015. Mr. Nerijus Mordas holds no shares of the Company. No interest in the capital of other Lithuanian companies. Mr. Nerijus Mordas charged EUR 5.16 thousand of remuneration under agreement of activity of member of the Management Board, bonuses from the profit of the year 2015 in amount of EUR 6.48 thousand were estimated, nor any assets were transferred or guarantees issued during the reporting period.

Members of Company's Management Board until 23 March 2016:

Mr. Justas Jankauskas is a partner of lawyers' professional community Jankauskas ir Partneriai (Jankauskas and Partners). He is a practising arbitrator of Vilnius International and National Commercial Arbitration Court, also a mediator of Lithuanian Arbitration Association, member of Company's Management Board from 1 June 2015 until 23 March 2016. Mr. Justas Jankauskas holds no shares of the Company. No interest in the capital of other Lithuanian companies. No remuneration amounts (salary, bonuses) were estimated, nor any assets were transferred or guarantees issued during the reporting period.

Mr. Ramūnas Gatautis is a doctor in technology sciences, research associate of Laboratory of Energy Systems Research of Lithuanian Energy Institute, member of International Association of Energy Economists (IAEE), member of Company's Management Board from 1 June 2015 to 23 March 2016. Mr. Ramūnas Gatautis holds no shares of the Company. He holds 33 per cent of shares of UAB RENEKS. No remuneration amounts (salary, bonuses) were estimated, nor any assets were transferred or guarantees issued during the reporting period.

21.3. Information on the General Manager and Chief accountant of the Company:

Mr. Rimantas Bakas is a Doctor in Technical sciences. Company's General Manager since 24 November 2008. Member of the Lithuanian Thermal Engineers Association, member of council of PI Kaunas Regional Energy Agency, member of Council of The Lithuanian District Heating Association, member of Scientific Council of Lithuanian Energy Institute, chairman of Master Qualification Committee of the Thermal and Nuclear Energy Department of Kaunas University of Technology, certified expert of the PET Lithuanian Committee on Energy approved by the Lithuanian committee of the World Energy Council, member of the Company‘s Management Board from 3 May 2011 to 2 January 2012 and from 28 September 2012 to 1 June 2015. Mr. Rimantas Bakas has a higher university education of Kaunas University of Technology, graduated in 1985, industrial thermal energy engineer. Workplaces and positions over the last 10 years: Manager of Strategy Division – 01.2006–11.2008.

Company's General Manager Rimantas Bakas was awarded with letters of appreciation from the Lithuanian District Heating Association (2007), Lithuanian Electricity Association (2008), Lithuanian Committee of World Energy Council (2010), Minister of Energy of the Republic of Lithuania (2013), Chairman of the Seimas of the Republic of Lithuania (2013), Lithuanian Committee of World Energy Council (2013), and the 600th Anniversary medal of Kaunas City Municipality (2008), Medal of Honour of Lithuanian energetics (2011), silver-plated brassy medal of Jonas Vileišis, burgomaster of Kaunas city for the merits in development of energy economy of the city (2015).

Mr. Rimantas Bakas holds no shares of the Company. No interest in the capital of other Lithuanian companies.

Mrs. Violeta Staškūnienė is a Company's Chief Accountant since 16 January 2003. She has a University education from Vilnius University, graduated in 1984, labour economics, profession – economist. Mrs. Violeta Staškūnienė holds 2,641 of the Company's shares, which represent less than 5 per cent of the authorised capital. No interest in the capital of other Lithuanian companies.

Company's General Manager and the Chief Accountant charged 86.1 euros of remuneration during the year 2015, and the average amount per member is 43.05 thousand euros. No other assets have been transferred, no guarantees granted.

22. Information on significant agreements

There are no significant agreements that would come into force, change or termination in case of change in controls of Issuer (their impact as well, except cases when due to the character of agreements the disclosure of them would make a significant harm).

23. Information on agreements of the Issuer and its managerial body members or employees

There are no agreements of the Issuer or its managerial body members or employees (which provide for compensation in case of their resignation or termination of employment on no grounds or in case their employment is terminated due to changes in controls of the Issuer).

24. Information on major transactions with related parties

There were no larger individual transactions. More detailed information is provided in Note 25 of the explanatory notes to financial statements.

25. Information on harmful transactions concluded on behalf of the Issuer during the reporting period

There are no harmful transactions concluded on behalf of the Issuer during the reporting period (not complying with the Company's objectives, normal market conditions, detrimental to the interests of shareholders and other interest groups etc.) which were or are likely to have an adverse effect on the Issuer's activities and (or) performance in the future, as well as information on transactions entered into in a conflict of interest between the Issuer's management, controlling shareholders or other related parties' obligations to the Issuer and their private interests and (or) other duties.

26. Information on compliance with the Governance Code of Companies and the Company's corporate social initiatives and policies

Information on compliance with the corporate governance code is provided in Annex 1 to this annual report. Annual reports on the Company's corporate social initiatives and policies are provided in Annex 2 to this annual report named AB Kauno Energija Report on Social Responsibility and on the Company's website.

27. Data on publicised information

In performing its obligations under the applicable legislation regulating the securities market, the Issuer has announced the following information starting from 1 January 2016 over the GlobeNewswire news distribution service, in which notices are disseminated within the European Union. This information was also posted on the website of the Issuer. All information is available on **Nasdaq Vilnius** websites (http://www.baltic.omxgroup.com/?id=3304) and the issuer's website (http://www.kaunoenergija.lt).

Title	Announcement category	Language	Time
Information on recall of the member of Management Board of AB Kauno Energija	Notice of stock event	EN, LT	2017-03-07 16:30
Interim information on 12 months of the year 2016 of AB Kauno Energija	Interim information	EN, LT	2017-01-31 16:00
Activity results of 12 months of the year 2016	Notice of stock event	EN, LT	2017-01-30 16:08
Activity results of 9 months of the year 2016	Interim information	EN, LT	2016-10-31 16:00
AB Kauno Energija acquired the shares of UAB Petrašiūnų Katilinė	Notice of stock event	EN, LT	2016-10-27 17:39
Regarding clearance of merger for AB Kauno Energija	Notice of stock event	EN, LT	2016-10-11 16:28
Intermediate information on AB Kauno Energija for the first half of the year 2016	Interim information	EN, LT	2016-09-09 13:46
Resolutions of the Extraordinary General Meeting of Shareholders of AB Kauno Energija	Notice of stock event	EN, LT	2016-07-29 16:00
Activity results of the 1 half of the year 2016	Notice of stock event	EN, LT	2016-07-28 16:00
Convocation of the Extraordinary General Meeting of Shareholders of AB Kauno Energija	Notice of stock event	EN, LT	2016-06-30 16:44
AB Kauno Energija and UAB E energija signed an agreement on acquisition of the shares of UAB Petrašiūnų Katilinė	Notice of stock event	EN, LT	2016-06-23 16:00
Regarding decision on acquisition of the shares of UAB Petrašiūnų Katilinė	Notice of stock event	EN, LT	2016-06-16 17:33
CORRECTION: Resolutions of the General Meeting of Shareholders of AB Kauno Energija	Notice of stock event	EN, LT	2016-04-29 11:28

Title	Announcement category	Language	Time
Activity results of the 1 quarter of the year 2016	Interim information	EN, LT	2016-04-28 17:06
Resolutions of the General Meeting of Shareholders of AB Kauno Energija	Notice of stock event	EN, LT	2016-04-28 16:27
Financial statements with the annual report and Social Responsibility Report	Annual information	EN, LT	2016-04-28 16:44
Supplement of AB „Kauno energija" eilinio visuotinio akcininkų susirinkimo darbotvarkės papildymas	Notice of stock event	EN, LT	2016-04-11 16:04
Convocation of General Meeting of Shareholders of AB Kauno Energija	Notice of stock event	EN, LT	2016-03-30 18:17
Audited activity results of AB Kauno Energija of the year 2015	Notice of stock event	EN, LT	2016-03-30 18:16
Information on recall of the members of Management Board of AB Kauno Energija	Notice of stock event	EN, LT	2016-03-24 13:50
Vilnius Commercial Arbitration Court approved a peaceful agreement between AB Kauno Energija and UAB Kauno Termofikacijos Elektrinė by which a litigation in case No. 268 was terminated	Notice of stock event	EN, LT	2016-02-02 16:26
Activity results of 12 months of the year 2015	Interim information	EN, LT	2016-01-28 16:00

General Manager of AB Kauno Energija Rimantas Bakas

AB KAUNO ENERGIJA
Company code 235014830
Raudondvario Rd. 84, LT-47179 Kaunas, Lithuania

AB Kauno Energija report on the compliance with the Governance Code for the companies listed on the Stock Exchange Nasdaq Vilnius

AB Kauno Energija (hereinafter – the Company), following paragraph item 3of Article 22 of the Law on Securities of the Republic of Lithuania and item 24.5 of The Listing Rules of AB Nasdaq Vilnius, discloses its compliance with the Governance Code, approved by the Stock Exchange Nasdaq Vilnius, for the companies listed on the regulated market, and its specific provisions.

PRINCIPLES/ RECOMMENDATIONS	YES/NO /NOT APPLIC ABLE	COMMENTARY
Principle I: Basic Provisions **The overriding objective of a company should be to operate in common interests of all the shareholders by optimizing over time shareholder value.**		
1.1. A company should adopt and make public the company's development strategy and objectives by clearly declaring how the company intends to meet the interests of its shareholders and optimize shareholder value.	Yes	The Company prepares and revises the strategies of heat production and supply system development every year, specifies investment plans and the sources of their financing. Investment plans are being presented for ratifying to Kaunas city, Kaunas region and Jurbarkas region municipalities as well as to The National Control Commission for Prices and Energy (NCC). The provisions of the Company's strategy which contain no confidential information and the decisions-making process, as well as the Company's development policies and objectives are published in Company's interim and annual reports and company's website. Periodic reports and notifications are disclosing the directions for Company's growth. Those reports, notification on stock event and notifications are presented by the Company's managers and are published in press.
1.2. All management bodies of a company should act in furtherance of the declared strategic objectives in view of the need to optimize shareholder value.	Yes	The Company's board accepts strategic decisions and approves Company's activities strategy. The Company's board has also created a long-term and short-term Company's development strategic objectives. Company's Supervisory Board renders responses and suggestions for shareholders regarding Company's activities strategy. The management of the Company, the heads of the areas concerned are making their every effort in order to implement those objectives – the structure of the Company and of the subdivision of the Group is optimised.
1.3. A company's supervisory and management bodies should act in close co-operation in order to attain maximum benefit for the company and its shareholders.	Yes	The Supervisory Board and the Management Board are formed. All the bodies of the Company (Manager, the Management board and the Supervisory board) aim to implement this recommendation, mutual meetings of the Management board and the Supervisory board are

		held during the year.
1.4. A company's supervisory and management bodies should ensure that the rights and interests of persons other than the company's shareholders (e.g. employees, creditors, suppliers, clients, local community), participating in or connected with the company's operation, are duly respected.	Yes	The Company's supervisory and managing bodies aim to ensure with their activities all interests of the persons concerned. The Company's management and the separate areas managers spend a lot of time communicating with customers, suppliers, contractors, representatives of the municipalities, in order to find optimal solutions, related to the Company's activities. Company's politics in respect of employees, customers and local society is stated in Company's Social Responsibility politics and implementation of this politics is described in Company's Corporate Social Responsibility reports. The specific of Company's activities ensures that consumers (customers) are periodically, i.e. 2-3 times per year invited to attend meetings where the relevant issues related to the activity of the Company are discussed. In addition the "Open doors days" are being arranged in order to better inform customers and to ensure closer relations with them.
Principle II: The corporate governance framework **The corporate governance framework should ensure the strategic guidance of the company, the effective oversight of the company's management bodies, an appropriate balance and distribution of functions between the company's bodies, protection of the shareholders' interests.**		
2.1. Besides obligatory bodies provided for in the Law on Companies of the Republic of Lithuania – a general shareholders' meeting and the chief executive officer, it is recommended that a company should set up both a collegial supervisory body and a collegial management body. The setting up of collegial bodies for supervision and management facilitates clear separation of management and supervisory functions in the company, accountability and control on the part of the chief executive officer, which, in its turn, facilitate a more efficient and transparent management process.	Yes	The General Meeting of Shareholders and the Company's general manager are compulsory management bodies of the Company set by the Law on Joint Stock Companies of the Republic of Lithuania. The collegial supervisory body - the Supervisory Board and the collegial management body – the Management Board are also being formed. Division of Company's management bodies' competences and responsibility is determined in Company's statute, regulations of management bodies' activities, are published Company's web site and in Company's managers' job description.
2.2. A collegial management body is responsible for the strategic management of the company and performs other key functions of corporate governance. A collegial supervisory body is responsible for the effective supervision of the company's management bodies.	Yes	A collegial management body of the Company – the Management Board is responsible for the strategic management of the Company and also performs other key functions of the Company management. A collegial supervisory body – the Supervisory Board is responsible for the effective supervision of activities of the Company's managing bodies.
2.3. Where a company chooses to form only one collegial body, it is recommended that it should be a supervisory body, i.e. the supervisory board. In such a case, the supervisory board is responsible for the effective monitoring of the functions performed by the company's chief executive	Not applicable	The Supervisory Board and the Management Board is being formed.

officer.		
2.4. The collegial supervisory body to be elected by the general shareholders' meeting should be set up and should act in the manner defined in Principles III and IV. Where a company should decide not to set up a collegial supervisory body but rather a collegial management body, i.e. the board, Principles III and IV should apply to the board as long as that does not contradict the essence and purpose of this body.[1]	Yes	The Supervisory Board of the Company is elected and it acts partly in compliance with the principles III and IV set out in the procedures and basic principles for the requirements are not violated.
2.5. Company's management and supervisory bodies should comprise such number of board (executive directors) and supervisory (non-executive directors) board members that no individual or small group of individuals can dominate decision-making on the part of these bodies.[2]	Yes	According to the Statute of the Company the Supervisory Board of 7 (seven) members is elected and the Supervisory Board elects the Management Board. It is elected of 5 (five) members.
2.6. Non-executive directors or members of the supervisory board should be appointed for specified terms subject to individual re-election, at maximum intervals provided for in the Lithuanian legislation with a view to ensuring necessary development of professional experience and sufficiently frequent reconfirmation of their status. A possibility to remove them should also be stipulated however this procedure should not be easier than the removal procedure for an executive director or a member of the management board.	Yes	The Supervisory Board of the Company is elected for 4 (four) years. According to the Statute of the Company and to the practice it is not forbidden to re-elect the single members of the Supervisory Board for the new term (Supervisory Board member's number of terms of office is not limited). Also the General meeting of shareholders is able to recall the Supervisory Board in-corpore or its individual members before the end of term of Supervisory Board and the member of Supervisory Board is able to resign before the end of term giving a 14 days written warning.

[1] Provisions of Principles III and IV are more applicable to those instances when the general shareholders' meeting elects the supervisory board, i.e. a body that is essentially formed to ensure oversight of the company's board and the chief executive officer and to represent the company's shareholders. However, in case the company does not form the supervisory board but rather the board, most of the recommendations set out in Principles III and IV become important and applicable to the board as well. Furthermore, it should be noted that certain recommendations, which are in their essence and nature applicable exclusively to the supervisory board (e.g. formation of the committees), should not be applied to the board, as the competence and functions of these bodies according to the Law on Companies of the Republic of Lithuania (*Official Gazette*, 2003, No 123-5574) are different. For instance, item 3.1 of the Code concerning oversight of the management bodies applies to the extent it concerns the oversight of the chief executive officer of the company, but not of the board itself; item 4.1 of the Code concerning recommendations to the management bodies applies to the extent it relates to the provision of recommendations to the company's chief executive officer; item 4.4 of the Code concerning independence of the collegial body elected by the general meeting from the company's management bodies is applied to the extent it concerns independence from the chief executive officer.

[2] Definitions *'executive director'* and *'non-executive director'* are used in cases when a company has only one collegial body.

2.7. Chairman of the collegial body elected by the general shareholders' meeting may be a person whose current or past office constitutes no obstacle to conduct independent and impartial supervision. Where a company should decide not to set up a supervisory board but rather the board, it is recommended that the chairman of the board and chief executive officer of the company should be a different person. Former company's chief executive officer should not be immediately nominated as the chairman of the collegial body elected by the general shareholders' meeting. When a company chooses to departure from these recommendations, it should furnish information on the measures it has taken to ensure impartiality of the supervision.	Yes	The Chairman of the Company's Supervisory Board hasn't been the General Manager of the Company. His current or past position is not an obstacle for independent and impartial supervision.
Principle III: The order of the formation of a collegial body to be elected by a general shareholders' meeting **The order of the formation a collegial body to be elected by a general shareholders' meeting should ensure representation of minority shareholders, accountability of this body to the shareholders and objective monitoring of the company's operation and its management bodies.**[3]		
3.1. The mechanism of the formation of a collegial body to be elected by a general shareholders' meeting (hereinafter in this Principle referred to as the 'collegial body') should ensure objective and fair monitoring of the company's management bodies as well as representation of minority shareholders.	Yes	The mechanism of forming of the Supervisory Board, which corresponds to the requirements of the Law on Joint Stock Companies of the Republic of Lithuania, ensures the objective supervision of the collegial management body.
3.2. Names and surnames of the candidates to become members of a collegial body, information about their education, qualification, professional background, positions taken and potential conflicts of interest should be disclosed early enough before the general shareholders' meeting so that the shareholders would have sufficient time to make an informed voting decision. All factors affecting the candidate's independence, the sample list of which is set out in Recommendation 3.7, should be also disclosed. The collegial body should also be informed on any subsequent changes in the provided information. The collegial body should, on yearly basis, collect data provided in this item on its members and disclose this in the company's annual report.	Yes	Information regarding candidates for the members of Supervisory Board is being disclosed for shareholders even before and during General meeting of shareholders. Information regarding their education, qualifications, professional experience, occupation and other important professional obligations is being presented in Company's annual and interim reports and publicized in Company's website as well. It is foreseen in the work regulations of the Supervisory Board that every member of the body has to inform the Chairman of the Supervisory Board and the Company about his data changes and this data is being presented in the Company's annual and interim reports and publicized in Company's website as well.

[3] Attention should be drawn to the fact that in the situation where the collegial body elected by the general shareholders' meeting is the board, it is natural that being a management body it should ensure oversight not of all management bodies of the company, but only of the single-person body of management, i.e. the company's chief executive officer. This note shall apply in respect of item 3.1 as well.

3.3. Should a person be nominated for members of a collegial body, such nomination should be followed by the disclosure of information on candidate's particular competences relevant to his/her service on the collegial body. In order shareholders and investors are able to ascertain whether member's competence is further relevant, the collegial body should, in its annual report, disclose the information on its composition and particular competences of individual members which are relevant to their service on the collegial body.	Yes	The shareholders of the Company by offering candidates for the collegial body must ensure that these members have the required competence. The Company publishes only the information which is provided by the members of the collegial body. Information which is presented in the annual and in interim report (data on participation of the issuer's statute capital, data on participation in other undertakings, bodies and organisations (title of the company, institution or organization and personal occupation), is publicized in Company's website.
3.4 In order to maintain a proper balance in terms of the current qualifications possessed by its members, the desired composition of the collegial body shall be determined with regard to the company's structure and activities, and have this periodically evaluated. The collegial body should ensure that it is composed of members who, as a whole, have the required diversity of knowledge, judgment and experience to complete their tasks properly. The members of the audit committee, collectively, should have a recent knowledge and relevant experience in the fields of finance, accounting and/or audit for the stock exchange listed companies. At least one of the members of the remuneration committee should have knowledge of and experience in the field of remuneration policy.	Yes	According to the Company's structure and activities, the main shareholder of the Company introduces candidates for members of the collegial body with relevant qualifications. The Collegial body as a unit has a versatile knowledge, opinions and experience enabling them to perform their tasks properly. Audit Committee as a unit, has up-to-date knowledge and relevant experience in finance, accounting, and (or) auditing.
3.5. All new members of the collegial body should be offered a tailored program focused on introducing a member with his/her duties, corporate organization and activities. The collegial body should conduct an annual review to identify fields where its members need to update their skills and knowledge.	Yes	In the practice of the Company all the new members of Supervisory Board are regularly informed about Company's activities and its alterations, as well as substantial changes of legal acts, regulating Company's activities and of circumstances, making an influence on Company's activities at the sessions of Supervisory Board of individually if there is such need or upon request of members.
3.6. In order to ensure that all material conflicts of interest related with a member of the collegial body are resolved properly, the collegial body should comprise a sufficient[4] number of independent[5] members.	No	The Company does not make any influence on the composition of the collegial body. Candidates to the members of the Company's collegial body are offered by the main shareholder. Detailed information is provided in article 3.7.

[4] The Code does not provide for a concrete number of independent members to comprise a collegial body. Many codes in foreign countries fix a concrete number of independent members (e.g. at least 1/3 or 1/2 of the members of the collegial body) to comprise the collegial body. However, having regard to the novelty of the institution of independent members in Lithuania and potential problems in finding and electing a concrete number of independent members, the Code provides for a more flexible wording and allows the companies themselves to decide what number of independent members is sufficient. Of course, a larger number of independent members in a collegial body is encouraged and will constitute an example of more suitable corporate governance.

[5] It is notable that in some companies all members of the collegial body may, due to a very small number of minority shareholders, be elected by the votes of the majority shareholder or a few major shareholders. But even a member of the collegial body elected by the majority shareholders may be considered independent if he/she meets the independence criteria set out in the Code.

3.7. A member of the collegial body should be considered to be independent only if he is free of any business, family or other relationship with the company, its controlling shareholder or the management of either, that creates a conflict of interest such as to impair his judgment. Since all cases when member of the collegial body is likely to become dependent are impossible to list, moreover, relationships and circumstances associated with the determination of independence may vary amongst companies and the best practices of solving this problem are yet to evolve in the course of time, assessment of independence of a member of the collegial body should be based on the contents of the relationship and circumstances rather than their form. The key criteria for identifying whether a member of the collegial body can be considered to be independent are the following: 1) He/she is not an executive director or member of the board (if a collegial body elected by the general shareholders' meeting is the supervisory board) of the company or any associated company and has not been such during the last five years; 2) He/she is not an employee of the company or some any company and has not been such during the last three years, except for cases when a member of the collegial body does not belong to the senior management and was elected to the collegial body as a representative of the employees; 3) He/she is not receiving or has been not receiving significant additional remuneration from the company or associated company other than remuneration for the office in the collegial body. Such additional remuneration includes participation in share options or some other performance based pay systems; it does not include compensation payments for the previous office in the company (provided that such payment is no way related with later position) as per pension plans (inclusive of deferred compensations); 4) He/she is not a controlling shareholder or representative of such shareholder (control as defined in the Council Directive 83/349/EEC Article 1 Part 1); 5) He/she does not have and did not have any material business relations with the company or associated company within the past year directly or as a partner, shareholder, director or superior employee of the subject having such relationship. A subject is considered to	No	Elected Company's Supervisory Board consists of seven dependent members who are also the members of the Kaunas City Council. All the members of Supervisory Board meet criteria indicated in item 3.7 of recommendations, except criteria 4, because all the members of Supervisory Board partly represent controlling shareholder, i.e. Kaunas city municipality having 92.84 % of votes.

have business relations when it is a major supplier or service provider (inclusive of financial, legal, advisory and consulting services), major client or organization receiving significant payments from the company or its group; 6) He/she is not and has not been, during the last three years, partner or employee of the current or former external audit company of the company or associated company; 7) He/she is not an executive director or member of the board in some other company where executive director of the company or member of the board (if a collegial body elected by the general shareholders' meeting is the supervisory board) is non-executive director or member of the supervisory board, he/she may not also have any other material relationships with executive directors of the company that arise from their participation in activities of other companies or bodies; 8) He/she has not been in the position of a member of the collegial body for over than 12 years; 9) He/she is not a close relative to an executive director or member of the board (if a collegial body elected by the general shareholders' meeting is the supervisory board) or to any person listed in above items 1 to 8. Close relative is considered to be a spouse (common-law spouse), children and parents.		
3.8. The determination of what constitutes independence is fundamentally an issue for the collegial body itself to determine. The collegial body may decide that, despite a particular member meets all the criteria of independence laid down in this Code, he cannot be considered independent due to special personal or company-related circumstances.	Yes	Company's Supervisory Board does not determine the term of independence, notwithstanding that a particular member meets all the requirements for independence indicated in this Code, because the elected Company's Supervisory Board consists of seven dependent members who are also the members of Kaunas City Municipality Council.
3.9. Necessary information on conclusions the collegial body has come to in its determination of whether a particular member of the body should be considered to be independent should be disclosed. When a person is nominated to become a member of the collegial body, the company should disclose whether it considers the person to be independent. When a particular member of the collegial body does not meet one or more criteria of independence set out in this Code, the company should disclose its reasons for nevertheless considering the member to be independent. In addition, the company should	Yes	The Company discloses dependence of the members of Supervisory Board in this report.

annually disclose which members of the collegial body it considers to be independent.		
3.10. When one or more criteria of independence set out in this Code has not been met throughout the year, the company should disclose its reasons for considering a particular member of the collegial body to be independent. To ensure accuracy of the information disclosed in relation with the independence of the members of the collegial body, the company should require independent members to have their independence periodically re-confirmed.	Not applicable	Information provided by members of the Supervisory Board regarding their professional experience, occupation and other important professional obligations and their relations with the Company is being presented in Company's annual and interim reports.
3.11. In order to remunerate members of a collegial body for their work and participation in the meetings of the collegial body, they may be remunerated from the company's funds.[6]. The general shareholders' meeting should approve the amount of such remuneration.	Not applicable	The members of the Supervisory Board are not remunerated from the Company's funds. So, this provision is not relevant for the Company.
Principle IV: The duties and liabilities of a collegial body elected by the general shareholders' meeting **The corporate governance framework should ensure proper and effective functioning of the collegial body elected by the general shareholders' meeting, and the powers granted to the collegial body should ensure effective monitoring[7] of the company's management bodies and protection of interests of all the company's shareholders.**		
4.1. The collegial body elected by the general shareholders' meeting (hereinafter in this Principle referred to as the 'collegial body') should ensure integrity and transparency of the company's financial statements and the control system. The collegial body should issue recommendations to the company's management bodies and monitor and control the company's management performance.[8]	Yes	The Supervisory Board presents to the general shareholders meeting their opinions and proposals about the Company's activities, set of the annual financial statements, profit allocation project, the Company's annual report, the activity of the Company's general manager and the Management Board, and also carries out other functions allotted to the Supervisory Board competence regarding the Company's and it's managing bodies activity supervision. The Chairman of the Supervisory Board regularly meets the Chairman of the Management Board and the General Manager to discuss the events or changes of the Company that have taken place, also the essential questions of the Company's activity.

[6] It is notable that currently it is not yet completely clear, in what form members of the supervisory board or the board may be remunerated for their work in these bodies. The Law on Companies of the Republic of Lithuania (*Official Gazette*, 2003, No 123-5574) provides that members of the supervisory board or the board may be remunerated for their work in the supervisory board or the board by payment of annual bonuses (tantiems) in the manner prescribed by Article 59 of this Law, i.e. from the company's profit. The current wording, contrary to the wording effective before 1 January 2004, eliminates the exclusive requirement that annual bonuses (tantiems) should be the *only* form of the company's compensation to members of the supervisory board or the board. So it seems that the Law contains no prohibition to remunerate members of the supervisory board or the board for their work in other forms, besides bonuses, although this possibility is not expressly stated either.

[7] See Footnote 3.

[8] See Footnote 3. In the event the collegial body elected by the general shareholders' meeting is the board, it should provide recommendations to the company's single-person body of management, i.e. the company's chief executive officer.

4.2. Members of the collegial body should act in good faith, with care and responsibility for the benefit and in the interests of the company and its shareholders with due regard to the interests of employees and public welfare. Independent members of the collegial body should (a) under all circumstances maintain independence of their analysis, decision-making and actions (b) do not seek and accept any unjustified privileges that might compromise their independence, and (c) clearly express their objections should a member consider that decision of the collegial body is against the interests of the company. Should a collegial body have passed decisions independent member has serious doubts about, the member should make adequate conclusions. Should an independent member resign from his office, he should explain the reasons in a letter addressed to the collegial body or audit committee and, if necessary, respective company-not-pertaining body (institution).	Yes	According to the knowledge of the Company all the members of the Supervisory Board are acting in good faith in the interests of the Company following the Company's but not the own interests or interests of the third persons.
4.3. Each member should devote sufficient time and attention to perform his duties as a member of the collegial body. Each member of the collegial body should limit other professional obligations of his (in particular any directorships held in other companies) in such a manner they do not interfere with proper performance of duties of a member of the collegial body. In the event a member of the collegial body should be present in less than a half[9] of the meetings of the collegial body throughout the financial year of the company, shareholders of the company should be notified.	Yes	The members of the Company's Supervisory Board devote enough time and pay enough attention individually and collectively for the functions assigned to the competence of the Supervisory Board to carry properly. All the members of Supervisory Board took part in more than a half sessions of the Supervisory Board during Company's financial year. A quorum determined in all standard acts was present in all sessions (was attended by more than 2/3 of the Supervisory Board members) of Supervisory Board in 2016. Members of Supervisory Board participating in session are registered in session protocol and in list of session participants.
4.4. Where decisions of a collegial body may have a different effect on the company's shareholders, the collegial body should treat all shareholders impartially and fairly. It should ensure that shareholders are properly informed on the company's affairs, strategies, risk management and resolution of conflicts of interest. The company should have a clearly established role of members of the collegial body when communicating with and committing to shareholders.	Yes	The Company's Supervisory Board in its work aim to behave honestly and impartially with all of the Company's shareholders and by the knowledge of the Company, there was no such kind of the contrary case. The Chairman of the Company's Supervisory Board and the Chairman of the Management Board harmonizes and coordinates interaction with Company's General Manager and in the name of Supervisory and Management Boards communicates with shareholders, informs the shareholders about the Company's strategy, activity and other essential questions.

[9] It is notable that companies can make this requirement more stringent and provide that shareholders should be informed about failure to participate at the meetings of the collegial body if, for instance, a member of the collegial body participated at less than 2/3 or 3/4 of the meetings. Such measures, which ensure active participation in the meetings of the collegial body, are encouraged and will constitute an example of more suitable corporate governance.

4.5. It is recommended that transactions (except insignificant ones due to their low value or concluded when carrying out routine operations in the company under usual conditions), concluded between the company and its shareholders, members of the supervisory or managing bodies or other natural or legal persons that exert or may exert influence on the company's management should be subject to approval of the collegial body. The decision concerning approval of such transactions should be deemed adopted only provided the majority of the independent members of the collegial body voted for such a decision.	Yes	Company's management bodies conclude and approve their contracts following requirements of legal acts and Company's Statute. Members of Company's supervision or management bodies or shareholders are not concluded any contracts with Company, including of a big value or concluded in non-standard conditions. More detailed information is provided in Note 25 of explanatory notes to the financial statements.
4.6. The collegial body should be independent in passing decisions that are significant for the company's operations and strategy. Taken separately, the collegial body should be independent of the company's management bodies[10]. Members of the collegial body should act and pass decisions without an outside influence from the persons who have elected it. Companies should ensure that the collegial body and its committees are provided with sufficient administrative and financial resources to discharge their duties, including the right to obtain, in particular from employees of the company, all the necessary information or to seek independent legal, accounting or any other advice on issues pertaining to the competence of the collegial body and its committees. When using the services of a consultant with a view to obtaining information on market standards for remuneration systems, the remuneration committee should ensure that the consultant concerned does not at the same time advice the human resources department, executive directors or collegial management organs of the company concerned.	Yes	As members of the Supervisory Board are partly related with Kaunas city municipality because they are members of Kaunas City Municipality Council, all their decisions are made only following Company's interests. Company's Supervisory Board is independent from Company's management bodies. Based on the Company's opinion, the collegial body and the Audit Committee are provided with sufficient resources, including their right to get all the necessary information, especially from the employees of the Company. Remuneration Committee is not set up in the Company because the salaries of the managers of the Company, their deputies and of the chief accountant are determined according to the schedule approved by Kaunas Municipality used in the municipality enterprises. Salary of Company's General Manager is determined by the Company's Board. The schedule of accounting and allocation of employees' variable part of salary is presented in the annex of the Company's collective agreement. Determination of per cent of variable part of salary, accounting and allocation of variable part of salary is detailed in this schedule.

[10] In the event the collegial body elected by the general shareholders' meeting is the board, the recommendation concerning its independence from the company's management bodies applies to the extent it relates to the independence from the company's chief executive officer.

4.7. Activities of the collegial body should be organized in a manner that independent members of the collegial body could have major influence in relevant areas where chances of occurrence of conflicts of interest are very high. Such areas to be considered as highly relevant are issues of nomination of company's directors, determination of directors' remuneration and control and assessment of company's audit. Therefore when the mentioned issues are attributable to the competence of the collegial body, it is recommended that the collegial body should establish nomination, remuneration, and audit committees[11]. Companies should ensure that the functions attributable to the nomination, remuneration, and audit committees are carried out. However they may decide to merge these functions and set up less than three committees. In such case a company should explain in detail reasons behind the selection of alternative approach and how the selected approach complies with the objectives set forth for the three different committees. Should the collegial body of the company comprise small number of members, the functions assigned to the three committees may be performed by the collegial body itself, provided that it meets composition requirements advocated for the committees and that adequate information is provided in this respect. In such case provisions of this Code relating to the committees of the collegial body (in particular with respect to their role, operation, and transparency) should apply, where relevant, to the collegial body as a whole.	Not applicable	Company's Audit Committee is formed by the Supervisory Board starting from 31 March 2009. The Supervisory Board appointed six member of Audit Committee from 29 May 2015. The Nomination and the Remuneration Committees are not formed in the Company. The Remuneration Committee is not formed according to the circumstances shown in the article No. 4.6. Nomination Committee, which would be obliged to perform all the functions appointed for this committee is not formed in Company and these functions are partly performed by the Supervisory Board and / or Company's Board. The Company will seek to implement this provision In the future.
4.8. The key objective of the committees is to increase efficiency of the activities of the collegial body by ensuring that decisions are based on due consideration, and to help organize its work with a view to ensuring that the decisions it takes are free of material conflicts of interest. Committees should exercise independent judgement and integrity when exercising its functions as well as present the collegial body with recommendations concerning the decisions of the collegial body. Nevertheless the final decision shall be adopted by the collegial body. The recommendation on creation of committees is not intended, in principle, to constrict the competence of the collegial body or to remove the matters	Yes	Audit committee is being formed in the Company. Al least one member of this Committee is independent. Three independent members act in Audit committee starting from 29 May 2015. The Committee acts independently and principally and renders recommendations and prepares reports that are presented to Supervisory Board.. The Supervisory Board is responsible for decisions made within its competence.

[11]The Law on Audit of the Republic of Lithuania (*Official Gazette*, 2008, No 82-53233) determines that an Audit Committee shall be formed in each public interest entity (including, but not limited to public companies whose securities are traded in the regulated market of the Republic of Lithuania and/or any other member state).

considered from the purview of the collegial body itself, which remains fully responsible for the decisions taken in its field of competence.		
4.9. Committees established by the collegial body should normally be composed of at least three members. In companies with small number of members of the collegial body, they could exceptionally be composed of two members. Majority of the members of each committee should be constituted from independent members of the collegial body. In cases when the company chooses not to set up a supervisory board, remuneration and audit committees should be entirely comprised of non-executive directors. Chairmanship and membership of the committees should be decided with due regard to the need to ensure that committee membership is refreshed and that undue reliance is not placed on particular individuals. Chairmanship and membership of the committees should be decided with due regard to the need to ensure that committee membership is refreshed and that undue reliance is not placed on particular individuals.	Yes	Audit Committee acts in the Company and it consists of six members, three of whom are independent members. Term of office of this Committee coincides with the term of office of the Company's Supervisory Board.
4.10. Authority of each of the committees should be determined by the collegial body. Committees should perform their duties in line with authority delegated to them and inform the collegial body on their activities and performance on regular basis. Authority of every committee stipulating the role and rights and duties of the committee should be made public at least once a year (as part of the information disclosed by the company annually on its corporate governance structures and practices). Companies should also make public annually a statement by existing committees on their composition, number of meetings and attendance over the year, and their main activities. Audit committee should confirm that it is satisfied with the independence of the audit process and describe briefly the actions it has taken to reach this conclusion.	No	The Company does not follow this recommendation partly because there are no Committees of Nomination and Remuneration at the Company. The Remuneration Committee is not formed according to the circumstances shown in the article No 4.6. Allocation Committee, which would be obliged to implement all the functions allocated to this committee, is not being formed in Company and all these functions are being performed by the Supervisoty Board and / or Management Board. The information on composition of the Audit Committee, the number of sessions and attendance during the year 2016 is being announced in this Annual Report.
4.11. In order to ensure independence and impartiality of the committees, members of the collegial body that are not members of the committee should commonly have a right to participate in the meetings of the committee only if invited by the committee. A committee may invite or demand participation in the meeting of particular officers or experts. Chairman of each of the committees should have a possibility to maintain direct communication with the shareholders. Events	No	The Company does not follow this recommendation partly because there are no Committees of Nomination and Remuneration at the Company. The Remuneration Committee is not formed according to the circumstances shown in the article No 4.6.

when such are to be performed should be specified in the regulations for committee activities.		
4.12. Nomination Committee. 4.12.1. Key functions of the nomination committee should be the following: • Identify and recommend, for the approval of the collegial body, candidates to fill board vacancies. The nomination committee should evaluate the balance of skills, knowledge and experience on the management body, prepare a description of the roles and capabilities required to assume a particular office, and assess the time commitment expected. Nomination committee can also consider candidates to members of the collegial body delegated by the shareholders of the company; • Assess on regular basis the structure, size, composition and performance of the supervisory and management bodies, and make recommendations to the collegial body regarding the means of achieving necessary changes; • Assess on regular basis the skills, knowledge and experience of individual directors and report on this to the collegial body; • Properly consider issues related to succession planning; • Review the policy of the management bodies for selection and appointment of senior management. 4.12.2. Nomination committee should consider proposals by other parties, including management and shareholders. When dealing with issues related to executive directors or members of the board (if a collegial body elected by the general shareholders' meeting is the supervisory board) and senior management, chief executive officer of the company should be consulted by, and entitled to submit proposals to the nomination committee.	No	The Company does not form the committee which would be obligated to perform all of the tasks that were designated for the Nomination Committee. These functions are partly being performed by Supervisory Board and / or Company's Management Board.
4.13. Remuneration Committee. 4.13.1. Key functions of the remuneration committee should be the following: • Make proposals, for the approval of the collegial body, on the remuneration policy for members of management bodies and executive directors. Such policy should address all forms of compensation, including the fixed remuneration, performance-based remuneration schemes, pension arrangements, and termination payments. Proposals considering performance-based remuneration schemes should be accompanied with recommendations on the related objectives and evaluation criteria, with a view to properly aligning the pay of executive	Not applicable	The Committee of Remuneration is not formed according to the circumstances shown in the article No 4.6.

director and members of the management bodies with the long-term interests of the shareholders and the objectives set by the collegial body; • Make proposals to the collegial body on the individual remuneration for executive directors and member of management bodies in order their remunerations are consistent with company's remuneration policy and the evaluation of the performance of these persons concerned. In doing so, the committee should be properly informed on the total compensation obtained by executive directors and members of the management bodies from the affiliated companies; • Ensure that remuneration of individual executive directors or members of management body is proportionate to the remuneration of other executive directors or members of management body and other staff members of the company; • Periodically review the remuneration policy for executive directors or members of management body, including the policy regarding share-based remuneration, and its implementation; • Make proposals to the collegial body on suitable forms of contracts for executive directors and members of the management bodies; • Assist the collegial body in overseeing how the company complies with applicable provisions regarding the remuneration-related information disclosure (in particular the remuneration policy applied and individual remuneration of directors); • Make general recommendations to the executive directors and members of the management bodies on the level and structure of remuneration for senior management (as defined by the collegial body) with regard to the respective information provided by the executive directors and members of the management bodies. 4.13.2. With respect to stock options and other share-based incentives which may be granted to directors or other employees, the committee should: • Consider general policy regarding the granting of the above mentioned schemes, in particular stock options, and make any related proposals to the collegial body; • Examine the related information that is given in the company's annual report and documents intended for the use during the shareholders		

meeting; • Make proposals to the collegial body regarding the choice between granting options to subscribe shares or granting options to purchase shares, specifying the reasons for its choice as well as the consequences that this choice has. 4.13.3. Upon resolution of the issues attributable to the competence of the remuneration committee, the committee should at least address the chairman of the collegial body and/or chief executive officer of the company for their opinion on the remuneration of other executive directors or members of the management bodies. 4.13.4. The remuneration committee should report on the exercise of its functions to the shareholders and be present at the annual general meeting for this purpose.		
4.14. Audit Committee. 4.14.1. Key functions of the audit committee should be the following: • Observe the integrity of the financial information provided by the company, in particular by reviewing the relevance and consistency of the accounting methods used by the company and its group (including the criteria for the consolidation of the accounts of companies in the group); • At least once a year review the systems of internal control and risk management to ensure that the key risks (inclusive of the risks in relation with compliance with existing laws and regulations) are properly identified, managed and reflected in the information provided; • Ensure the efficiency of the internal audit function, among other things, by making recommendations on the selection, appointment, reappointment and removal of the head of the internal audit department and on the budget of the department, and by monitoring the responsiveness of the management to its findings and recommendations. Should there be no internal audit authority in the company, the need for one should be reviewed at least annually; • Make recommendations to the collegial body related with selection, appointment, reappointment and removal of the external auditor (to be done by the general shareholders' meeting) and with the terms and conditions of his engagement. The committee should investigate situations that lead to a resignation of the audit company or auditor and make recommendations on required actions in such	Yes	However, as of 31 March 2009 the Audit Committee was formed by the Supervisory Board. The term of office of this committee coincides with the term of office of the Company's Supervisory Board. This committee will seek to fully implement functions assigned to it by this recommendation.

situations; • Monitor independence and impartiality of the external auditor, in particular by reviewing the audit company's compliance with applicable guidance relating to the rotation of audit partners, the level of fees paid by the company, and similar issues. In order to prevent occurrence of material conflicts of interest, the committee, based on the auditor's disclosed inter alia data on all remunerations paid by the company to the auditor and network, should at all times monitor nature and extent of the non-audit services. Having regard to the principals and guidelines established in the 16 May 2002 Commission Recommendation 2002/590/EC, the committee should determine and apply a formal policy establishing types of non-audit services that are (a) excluded, (b) permissible only after review by the committee, and (c) permissible without referral to the committee; • Review efficiency of the external audit process and responsiveness of management to recommendations made in the external auditor's management letter. 4.14.2. All members of the committee should be furnished with complete information on particulars of accounting, financial and other operations of the company. Company's management should inform the audit committee of the methods used to account for significant and unusual transactions where the accounting treatment may be open to different approaches. In such case a special consideration should be given to company's operations in offshore centres and/or activities carried out through special purpose vehicles (organizations) and justification of such operations. 4.14.3. The audit committee should decide whether participation of the chairman of the collegial body, chief executive officer of the company, chief financial officer (or superior employees in charge of finances, treasury and accounting), or internal and external auditors in the meetings of the committee is required (if required, when). The committee should be entitled, when needed, to meet with any relevant person without executive directors and members of the management bodies present. 4.14.4. Internal and external auditors should be secured with not only effective working relationship with management, but also with free access to the collegial body. For this purpose the audit committee should act as the principal contact person for the internal and external		

auditors. 4.14.5. The audit committee should be informed of the internal auditor's work program, and should be furnished with internal audit's reports or periodic summaries. The audit committee should also be informed of the work program of the external auditor and should be furnished with report disclosing all relationships between the independent auditor and the company and its group. The committee should be timely furnished information on all issues arising from the audit. 4.14.6. The audit committee should examine whether the company is following applicable provisions regarding the possibility for employees to report alleged significant irregularities in the company, by way of complaints or through anonymous submissions (normally to an independent member of the collegial body), and should ensure that there is a procedure established for proportionate and independent investigation of these issues and for appropriate follow-up action. 4.14.7. The audit committee should report on its activities to the collegial body at least once in every six months, at the time the yearly and half-yearly statements are approved.		
4.15. Every year the collegial body should conduct the assessment of its activities. The assessment should include evaluation of collegial body's structure, work organization and ability to act as a group, evaluation of each of the collegial body member's and committee's competence and work efficiency and assessment whether the collegial body has achieved its objectives. The collegial body should, at least once a year, make public (as part of the information the company annually discloses on its management structures and practices) respective information on its internal organization and working procedures, and specify what material changes were made as a result of the assessment of the collegial body of its own activities.	No	There was no practice of assessment of the activity of Supervisory Board at the Company and of informing shareholders about that up to now because the controlling shareholder who proposes candidates to the Supervisory Board exhaustively knows the experiences and competences of each candidate.
Principle V: The working procedure of the company's collegial bodies **The working procedure of supervisory and management bodies established in the company should ensure efficient operation of these bodies and decision-making and encourage active co-operation between the company's bodies.**		
5.1. The company's supervisory and management bodies (hereinafter in this Principle the concept 'collegial bodies' covers both the collegial bodies of supervision and the collegial bodies of management) should be chaired by	Yes	The Company fully implements this recommendation. The Company's Supervisory Board and Management Board are run by the Chairman de jure and de facto. In accordance with the work regulations of the bodies the chairmen

chairpersons of these bodies. The chairperson of a collegial body is responsible for proper convocation of the collegial body meetings. The chairperson should ensure that information about the meeting being convened and its agenda are communicated to all members of the body. The chairperson of a collegial body should ensure appropriate conducting of the meetings of the collegial body. The chairperson should ensure order and working atmosphere during the meeting.		of Supervisory Board and Managing Board convenes meetings, ensures proper informing about convening meeting and about agenda of the meeting. This recommendation is fully implemented by the Supervisory Board and by the Managing Board.
5.2. It is recommended that meetings of the company's collegial bodies should be carried out according to the schedule approved in advance at certain intervals of time. Each company is free to decide how often to convene meetings of the collegial bodies, but it is recommended that these meetings should be convened at such intervals, which would guarantee an interrupted resolution of the essential corporate governance issues. Meetings of the company's supervisory board should be convened at least once in a quarter, and the company's board should meet at least once a month[12].	Yes	This recommendation is implemented by the Supervisory Board and by the Management Board.
5.3. Members of a collegial body should be notified about the meeting being convened in advance in order to allow sufficient time for proper preparation for the issues on the agenda of the meeting and to ensure fruitful discussion and adoption of appropriate decisions. Alongside with the notice about the meeting being convened, all the documents relevant to the issues on the agenda of the meeting should be submitted to the members of the collegial body. The agenda of the meeting should not be changed or supplemented during the meeting, unless all members of the collegial body are present or certain issues of great importance to the company require immediate resolution.	Yes	The Company follows the order foreseen in the work regulations of the Supervisory Board and the Management Board and the information about the convened meeting is presented in advance together with an agenda and all the necessary information and documents related to the meeting agenda. The Supervisory Board and the Board meeting agenda may be changed or added during the meeting, in the presence of all members of the collegial body, or when there is an urgent need to deal with Company's certain key issues.
5.4. In order to co-ordinate operation of the company's collegial bodies and ensure effective decision-making process, chairpersons of the company's collegial bodies of supervision and management should closely co-operate by co-coordinating dates of the meetings, their agendas and resolving other issues of corporate governance. Members of the company's board should be free to attend meetings of the company's supervisory board, especially where issues concerning removal of the board members, their liability or remuneration are	Yes	The chairmen of Company's supervisory and management bodies coordinate dates of the meetings, their agendas and cooperate in solving other issues of corporate governance.

[12] The frequency of meetings of the collegial body provided for in the recommendation must be applied in those cases when both additional collegial bodies are formed at the company, the board and the supervisory board. In the event only one additional collegial body is formed in the company, the frequency of its meetings may be as established for the supervisory board, i.e. at least once in a quarter.

discussed.		
Principle VI: The equitable treatment of shareholders and shareholder rights **The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. The corporate governance framework should protect the rights of the shareholders.**		
6.1. It is recommended that the company's capital should consist only of the shares that grant the same rights to voting, ownership, dividend and other rights to all their holders.	Yes	The ordinary registered shares which make the authorized capital of the Company give the equal rights for all share owners.
6.2. It is recommended that investors should have access to the information concerning the rights attached to the shares of the new issue or those issued earlier in advance, i.e. before they purchase shares.	Yes	The Company allows investors to take a look at the rights conceded by newly issued or already issued shares. Company's Statute in which the rights conceded to Company's shareholders are determined, are publicized in Company's website.
6.3. Transactions that are important to the company and its shareholders, such as transfer, investment, and pledge of the company's assets or any other type of encumbrance should be subject to approval of the general shareholders' meeting.[13] All shareholders should be furnished with equal opportunity to familiarize with and participate in the decision-making process when significant corporate issues, including approval of transactions referred to above, are discussed.	Yes	In compliance with the Law on the Companies and the Company's statutes the transactions confirmation issues foreseen in this recommendation are ascribed to the competence of the Management Board but in individual cases for the asset disposal transactions the Company applies to the Meeting of Shareholders, as it is prescribed in Company's statutes.
6.4. Procedures of convening and conducting a general shareholders' meeting should ensure equal opportunities for the shareholders to effectively participate at the meetings and should not prejudice the rights and interests of the shareholders. The venue, date, and time of the shareholders' meeting should not hinder wide attendance of the shareholders.	Yes	There is a possibility for shareholders to vote in advance by filling up a general vote bulletin.

[13] The Law on Companies of the Republic of Lithuania (*Official Gazette*, 2003, No 123-5574) no longer assigns resolutions concerning the investment, transfer, lease, mortgage or acquisition of the long-terms assets accounting for more than 1/20 of the company's authorised capital to the competence of the general shareholders' meeting. However, transactions that are important and material for the company's activity should be considered and approved by the general shareholders' meeting. The Law on Companies contains no prohibition to this effect either. Yet, in order not to encumber the company's activity and escape an unreasonably frequent consideration of transactions at the meetings, companies are free to establish their own criteria of material transactions, which are subject to the approval of the meeting. While establishing these criteria of material transactions, companies may follow the criteria set out in items 3, 4, 5 and 6 of paragraph 4 of Article 34 of the Law on Companies or derogate from them in view of the specific nature of their operation and their attempt to ensure uninterrupted, efficient functioning of the company.

6.5. If it is possible, in order to ensure shareholders living abroad the right to access to the information, it is recommended that documents on the course of the general shareholders' meeting should be placed on the publicly accessible website of the company not only in Lithuanian language, but in English and /or other foreign languages in advance. It is recommended that the minutes of the general shareholders' meeting after signing them and/or adopted resolutions should be also placed on the publicly accessible website of the company. Seeking to ensure the right of foreigners to familiarize with the information, whenever feasible, documents referred to in this recommendation should be published in Lithuanian, English and/or other foreign languages. Documents referred to in this recommendation may be published on the publicly accessible website of the company to the extent that publishing of these documents is not detrimental to the company or the company's commercial secrets are not revealed.	Yes	Draft decisions of convoked meeting and decisions taken by meeting are being disclosed publicly by the Company in Company's website and using GlobeNewswire information dissemination system of Nasdaq Vilnius Stock Exchange as it is foreseen in the Law on Companies not only in Lithuanian, but also in English.
6.6. Shareholders should be furnished with the opportunity to vote in the general shareholders' meeting in person and in absentia. Shareholders should not be prevented from voting in writing in advance by completing the general voting ballot.	Yes	The shareholders of the Company can implement the right to participate in the General meeting of shareholders personally or through their representatives if the person has a proper authorization or the voting right delegation agreement is made with him in compliance with the legal acts order. The Company also creates conditions for the shareholders to vote in advance in writing by completing the general voting bulletin as it is foreseen by the Law on the Joint Stock Companies.
6.7. With a view to increasing the shareholders' opportunities to participate effectively at shareholders' meetings, the companies are recommended to expand use of modern technologies by allowing the shareholders to participate and vote in general meetings via electronic means of communication. In such cases security of transmitted information and a possibility to identify the identity of the participating and voting person should be guaranteed. Moreover, companies could furnish its shareholders, especially shareholders living abroad, with the opportunity to watch shareholder meetings by means of modern technologies.	Not applicable	According to the order of the Company's shareholders meetings and the lists of shareholders, there was no need to implement this recommendation in the Company up to now.
Principle VII: The avoidance of conflicts of interest and their disclosure **The corporate governance framework should encourage members of the corporate bodies to avoid conflicts of interest and assure transparent and effective mechanism of disclosure of conflicts of interest regarding members of the corporate bodies.**		

7.1. Any member of the company’s supervisory and management body should avoid a situation, in which his/her personal interests are in conflict or may be in conflict with the company’s interests. In case such a situation did occur, a member of the company’s supervisory and management body should, within reasonable time, inform other members of the same collegial body or the company’s body that has elected him/her, or to the company’s shareholders about a situation of a conflict of interest, indicate the nature of the conflict and value, where possible.	Yes	The members of the Company's Supervisory and of the managing bodies act in according with the interests of the Company and their competences and individual features suggest that they behave so as to avoid conflicts of interests and they were not observed in practice. The members of the Company's Supervisory and of the managing bodies did not conclude deals with the Company, including high value deals or ones made in not standard conditions.
7.2. Any member of the company’s supervisory and management body may not mix the company’s assets, the use of which has not been mutually agreed upon, with his/her personal assets or use them or the information which he/she learns by virtue of his/her position as a member of a corporate body for his/her personal benefit or for the benefit of any third person without a prior agreement of the general shareholders’ meeting or any other corporate body authorized by the meeting.	Yes	
7.3. Any member of the company’s supervisory and management body may conclude a transaction with the company, a member of a corporate body of which he/she is. Such a transaction (except insignificant ones due to their low value or concluded when carrying out routine operations in the company under usual conditions) must be immediately reported in writing or orally, by recording this in the minutes of the meeting, to other members of the same corporate body or to the corporate body that has elected him/her or to the company’s shareholders. Transactions specified in this recommendation are also subject to recommendation 4.5.	Yes	The members of the Company's supervisory and management body are not entered into transactions with the Company, including those consisting of high value or non-standard conditions.
7.4. Any member of the company’s supervisory and management body should abstain from voting when decisions concerning transactions or other issues of personal or business interest are voted on.	Yes	In accordance with regulations of Company’s supervisory and management bodies, the provisions of the Law on Joint Stock companies of the Republic of Lithuania, the members of the Company's Supervisory and of the managing bodies must abstain from voting when decisions on deals or other questions in which they have a personal or professional interest.
Principle VIII: Company’s remuneration policy **Remuneration policy and procedure for approval, revision and disclosure of directors’ remuneration established in the company should prevent potential conflicts of interest and abuse in determining remuneration of directors, in addition it should ensure publicity and transparency both of company’s remuneration policy and remuneration of directors.**		

8.1. A company should make a public statement of the company's remuneration policy (hereinafter the remuneration statement) which should be clear and easily understandable. This remuneration statement should be published as a part of the company's annual statement as well as posted on the company's website.	Not applicable	The Company publicizes average wages of employees of the Company (by category) and the average wage of all employees of the Company. The remuneration policy as provided in this recommendation is not confirmed in the Company because this is not determined by the valid legal acts. The remuneration for the Supervisory Board and the Management Board of the Company is determined by the meeting of shareholders. Remuneration for the members of the Management Board for the results of the year 2015 was allocated. Remuneration for members of the Management Board is paid following the order determined in Company's Statutes. The remuneration of the managing director is determined by the Managing Board considering the schedule of remuneration order of managers of municipal enterprises, companies, municipal controlled joint-stock and close-end companies, their deputies and chief accountants approved by Kaunas municipality. Considering this schedule the remuneration of the General Manager and chief accountant of the Company is determined. Estimating this there was no need to prepare separate remuneration policy. Nevertheless in compliance with the legal acts orders, the Company publicly announces the information on the termination payments and loans for the members of the Supervisory Board, the Management Board and General Manager, Chief accountant in the annual report. The information regarding average remuneration of employees of the Company is also announced in Company's website.
8.2. Remuneration statement should mainly focus on directors' remuneration policy for the following year and, if appropriate, the subsequent years. The statement should contain a summary of the implementation of the remuneration policy in the previous financial year. Special attention should be given to any significant changes in company's remuneration policy as compared to the previous financial year.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1 the remuneration policy according to which the report on remuneration would be prepared is not approved by the Company.

8.3. Remuneration statement should leastwise include the following information: • Explanation of the relative importance of the variable and non-variable components of directors' remuneration; • Sufficient information on performance criteria that entitles directors to share options, shares or variable components of remuneration; • An explanation how the choice of performance criteria contributes to the long-term interests of the company; • An explanation of the methods, applied in order to determine whether performance criteria have been fulfilled; • Sufficient information on deferment periods with regard to variable components of remuneration; • Sufficient information on the linkage between the remuneration and performance; • The main parameters and rationale for any annual bonus scheme and any other non-cash benefits; • Sufficient information on the policy regarding termination payments; • Sufficient information with regard to vesting periods for share-based remuneration, as referred to in point 8.13 of this Code; • Sufficient information on the policy regarding retention of shares after vesting, as referred to in point 8.15 of this Code; • Sufficient information on the composition of peer groups of companies the remuneration policy of which has been examined in relation to the establishment of the remuneration policy of the company concerned; • A description of the main characteristics of supplementary pension or early retirement schemes for directors; • Remuneration statement should not include commercially sensitive information.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1. the remuneration policy according to which the report on remuneration would be prepared is not approved by the Company.
8.4. Remuneration statement should also summarize and explain company's policy regarding the terms of the contracts executed with executive directors and members of the management bodies. It should include, inter alia, information on the duration of contracts with executive directors and members of the management bodies, the applicable notice periods and details of provisions for termination payments linked to early termination under contracts for executive directors and members of the management bodies.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1 the remuneration policy according to which the report on remuneration would be prepared is not approved by the Company, but the information on the termination and other payments is publicly announced in the Company's annual report.. Also Company publicizes average wages of employees of the Company (by category).

8.5. Remuneration statement should also contain detailed information on the entire amount of remuneration, inclusive of other benefits, that was paid to individual directors over the relevant financial year. This document should list at least the information set out in items 8.5.1 to 8.5.4 for each person who has served as a director of the company at any time during the relevant financial year. 8.5.1. The following remuneration and/or emoluments-related information should be disclosed: • The total amount of remuneration paid or due to the director for services performed during the relevant financial year, inclusive of, where relevant, attendance fees fixed by the annual general shareholders meeting; • The remuneration and advantages received from any undertaking belonging to the same group; • The remuneration paid in the form of profit sharing and/or bonus payments and the reasons why such bonus payments and/or profit sharing were granted; • If permissible by the law, any significant additional remuneration paid to directors for special services outside the scope of the usual functions of a director; • Compensation receivable or paid to each former executive director or member of the management body as a result of his resignation from the office during the previous financial year; • Total estimated value of non-cash benefits considered as remuneration, other than the items covered in the above points. 8.5.2. As regards shares and/or rights to acquire share options and/or all other share-incentive schemes, the following information should be disclosed: • The number of share options offered or shares granted by the company during the relevant financial year and their conditions of application; • The number of shares options exercised during the relevant financial year and, for each of them, the number of shares involved and the exercise price or the value of the interest in the share incentive scheme at the end of the financial year; • The number of share options unexercised at the end of the financial year; their exercise price, the exercise date and the main conditions for the exercise of the rights; • All changes in the terms and conditions of existing share options occurring during the	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1 the remuneration policy according to which the report on remuneration would be prepared is not approved by the Company.

financial year. 8.5.3. The following supplementary pension schemes-related information should be disclosed: • When the pension scheme is a defined-benefit scheme, changes in the directors' accrued benefits under that scheme during the relevant financial year; • When the pension scheme is defined-contribution scheme, detailed information on contributions paid or payable by the company in respect of that director during the relevant financial year. 8.5.4. The statement should also state amounts that the company or any subsidiary company or entity included in the consolidated annual financial **report** of the company has paid to each person who has served as a director in the company at any time during the relevant financial year in the form of loans, advance payments or guarantees, including the amount outstanding and the interest rate.		
8.6. Where the remuneration policy includes variable components of remuneration, companies should set limits on the variable component(s). The non-variable component of remuneration should be sufficient to allow the company to withhold variable components of remuneration when performance criteria are not met.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1 the remuneration policy according to which the report on remuneration would be prepared is not approved by the Company.
8.7. Award of variable components of remuneration should be subject to predetermined and measurable performance criteria.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1 the remuneration policy according to which the report on remuneration would be prepared is not approved by the Company.
8.8. Where a variable component of remuneration is awarded, a major part of the variable component should be deferred for a minimum period of time. The part of the variable component subject to deferment should be determined in relation to the relative weight of the variable component compared to the non-variable component of remuneration.	Not applicable	
8.9. Contractual arrangements with executive or managing directors should include provisions that permit the company to reclaim variable components of remuneration that were awarded on the basis of data which subsequently proved to be manifestly misstated.	Not applicable	
8.10. Termination payments should not exceed a fixed amount or fixed number of years of annual remuneration, which should, in general, not be higher than two years of the non-variable component of remuneration or the equivalent thereof.	Not applicable	

8.11. Termination payments should not be paid if the termination is due to inadequate performance	Not applicable	
8.12. The information on preparatory and decision-making processes, during which a policy of remuneration of directors is being established, should also be disclosed. Information should include data, if applicable, on authorities and composition of the remuneration committee, names and surnames of external consultants whose services have been used in determination of the remuneration policy as well as the role of shareholders' annual general meeting.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1 the remuneration policy according to which the report on remuneration would be prepared is not approved by the Company.
8.13. Shares should not vest for at least three years after their award.	Not applicable	
8.14. Share options or any other right to acquire shares or to be remunerated on the basis of share price movements should not be exercisable for at least three years after their award. Vesting of shares and the right to exercise share options or any other right to acquire shares or to be remunerated on the basis of share price movements, should be subject to predetermined and measurable performance criteria.	Not applicable	
8.15. After vesting, directors should retain a number of shares, until the end of their mandate, subject to the need to finance any costs related to acquisition of the shares. The number of shares to be retained should be fixed, for example, twice the value of total annual remuneration (the non-variable plus the variable components).	Not applicable	
8.16. Remuneration of non-executive or supervisory directors should not include share options.	Not applicable	
8.17. Shareholders, in particular institutional shareholders, should be encouraged to attend general meetings where appropriate and make considered use of their votes regarding directors' remuneration.	Not applicable	
8.18. Without prejudice to the role and organization of the relevant bodies responsible for setting directors' remunerations, the remuneration policy or any other significant change in remuneration policy should be included into the agenda of the shareholders' annual general meeting. Remuneration statement should be put for voting in shareholders' annual general meeting. The vote may be either mandatory or advisory.	Not applicable	

8.19. Schemes anticipating remuneration of directors in shares, share options or any other right to purchase shares or be remunerated on the basis of share price movements should be subject to the prior approval of shareholders' annual general meeting by way of a resolution prior to their adoption. The approval of scheme should be related with the scheme itself and not to the grant of such share-based benefits under that scheme to individual directors. All significant changes in scheme provisions should also be subject to shareholders' approval prior to their adoption; the approval decision should be made in shareholders' annual general meeting. In such case shareholders should be notified on all terms of suggested changes and get an explanation on the impact of the suggested changes.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1., remuneration policy according to which the report on remuneration would be prepared is not approved by the Company. Nevertheless, the Company publishes information on the remuneration and other payments of the members of the Supervisory Board, Management Board, General Manager and to the chief accountant in Company's annual reports in accordance with the legislation. Information on average remuneration of Company's employees is also announced in Company's website. The Company does not use schemes under which the directors can be paid with the shares, stock selection transactions or other rights to acquire shares, or to be paid by the stock price changes.
8.20. The following issues should be subject to approval by the shareholders' annual general meeting: 1) Grant of share-based schemes, including share options, to directors; 2) Determination of maximum number of shares and main conditions of share granting; 3) The term within which options can be exercised; 4) The conditions for any subsequent change in the exercise of the options, if permissible by law; 5) All other long-term incentive schemes for which directors are eligible and which are not available to other employees of the company under similar terms. Annual general meeting should also set the deadline within which the body responsible for remuneration of directors may award compensations listed in this article to individual directors.	Not applicable	Because of the reasons foreseen in the recommendation No. 8.1. the Company does not use schemes under which the directors can be remunerated with the shares, stock selection transactions or other rights to acquire shares, or to be paid by the stock price changes.
8.21. Should national law or company's Articles of Association allow, any discounted option arrangement under which any rights are granted to subscribe to shares at a price lower than the market value of the share prevailing on the day of the price determination, or the average of the market values over a number of days preceding the date when the exercise price is determined, should also be subject to the shareholders' approval.	Not applicable	

8.22. Provisions of Articles 8.19 and 8.20 should not be applicable to schemes allowing for participation under similar conditions to company's employees or employees of any subsidiary company whose employees are eligible to participate in the scheme and which has been approved in the shareholders' annual general meeting.	Not applicable	
8.23. Prior to the annual general meeting that is intended to consider decision stipulated in Article 8.19, the shareholders must be provided an opportunity to familiarize with draft resolution and project-related notice (the documents should be posted on the company's website). The notice should contain the full text of the share-based remuneration schemes or a description of their key terms, as well as full names of the participants in the schemes. Notice should also specify the relationship of the schemes and the overall remuneration policy of the directors. Draft resolution must have a clear reference to the scheme itself or to the summary of its key terms. Shareholders must also be presented with information on how the company intends to provide for the shares required to meet its obligations under incentive schemes. It should be clearly stated whether the company intends to buy shares in the market, hold the shares in reserve or issue new ones. There should also be a summary on scheme-related expenses the company will suffer due to the anticipated application of the scheme. All information given in this article must be posted on the company's website.		
Principle IX: The role of stakeholders in corporate governance **The corporate governance framework should recognize the rights of stakeholders as established by law and encourage active co-operation between companies and stakeholders in creating the company value, jobs and financial sustainability. For the purposes of this Principle, the concept "stakeholders" includes investors, employees, creditors, suppliers, clients, local community and other persons having certain interest in the company concerned.**		
9.1. The corporate governance framework should assure that the rights of stakeholders that are protected by law are respected.	Yes	The Company follows all the requirements foreseen by the law for the stakeholders' opportunities to participate in the management of

9.2. The corporate governance framework should create conditions for the stakeholders to participate in corporate governance in the manner prescribed by law. Examples of mechanisms of stakeholder participation in corporate governance include: employee participation in adoption of certain key decisions for the company; consulting the employees on corporate governance and other important issues; employee participation in the company’s share capital; creditor involvement in governance in the context of the company’s insolvency, etc.		the Company, but any group of interest, having the right to participate in management of the Company, determined by the law, is not created yet in accordance with law.
9.3. Where stakeholders participate in the corporate governance process, they should have access to relevant information.		
Principle X: Information disclosure and transparency **The corporate governance framework should ensure that timely and accurate disclosure is made on all material information regarding the company, including the financial situation, performance and governance of the company.**		
10.1. The company should disclose information on: 1) The financial and operating results of the company; 2) Company objectives; 3) Persons holding by the right of ownership or in control of a block of shares in the company; 4) Members of the company’s supervisory and management bodies, chief executive officer of the company and their remuneration; 5) Material foreseeable risk factors; 6) Transactions between the company and connected persons, as well as transactions concluded outside the course of the company’s regular operations; 7) Material issues regarding employees and other stakeholders; 8) Governance structures and strategy. This list should be deemed as a minimum recommendation, while the companies are encouraged not to limit themselves to disclosure of the information specified in this list. 10.2. It is recommended to the company, which is the parent of other companies, that consolidated results of the whole group to which the company belongs should be disclosed when information specified in item 1 of Recommendation 10.1 is under disclosure. 10.3. It is recommended that information on the	Yes	The Company discloses information, provided in this recommendation, in the reports, in the annual and interim reports, the Company's website and Centre of Registers electronic publication, in which the public information of legal persons are announced, except the report of remuneration policy determined in VIII principle. This report is not prepared in the Company because of the reasons foreseen in the article No. 8.1., and it is not approved, as it is not required by the law. According to the Law on Companies and to Company’s Statute the remuneration for the members of the Company's Supervisory Board and of the Management Board can be determined by the meeting of shareholders. In the year 2016 remuneration has been allotted for the members of Company’s Management Board for the results of the year 2015 and it is paid following the order determined in Company’s Statutes. The company also attempts not to disclose the information that can affect the price of Securities issued by the Company in the comments, interviews or other means, as long as such information will be publicly announced at the Nasdaq Vilnius Stock Exchange GlobeNewswire dissemination system on the Company's website.

professional background, qualifications of the members of supervisory and management bodies, chief executive officer of the company should be disclosed as well as potential conflicts of interest that may have an effect on their decisions when information specified in item 4 of Recommendation 10.1 about the members of the company's supervisory and management bodies is under disclosure. It is also recommended that information about the amount of remuneration received from the company and other income should be disclosed with regard to members of the company's supervisory and management bodies and chief executive officer as per Principle VIII. 10.4. It is recommended that information about the links between the company and its stakeholders, including employees, creditors, suppliers, local community, as well as the company's policy with regard to human resources, employee participation schemes in the company's share capital, etc. should be disclosed when information specified in item 7 of Recommendation 10.1 is under disclosure.		
10.5. Information should be disclosed in such a way that neither shareholders nor investors are discriminated with regard to the manner or scope of access to information. Information should be disclosed to all simultaneously. It is recommended that notices about material events should be announced before or after a trading session on the Vilnius Stock Exchange, so that all the company's shareholders and investors should have equal access to the information and make informed investing decisions.	Yes	The Company simultaneously presents the information using the Nasdaq Vilnius Stock Exchange information dissemination system GlobeNewswire in Lithuanian and English languages as it possible. The Stock Exchange places received information on its website and in trading system assuring simultaneous presentation of this information to all. In addition, the Company strives to announce the information before or after a trading session on the Nasdaq Vilnius Stock Exchange and to present it to all the markets in whom the trade in Company's stocks is being in progress at the same time. The Company does not provide the information which can have an influence on the price of its issued stocks on comments, interview and other ways till this information is publicly announced using the Nasdaq Vilnius Stock Exchange dissemination system.
10.6. Channels for disseminating information should provide for fair, timely and cost-efficient or in cases provided by the legal acts free of charge access to relevant information by users. It is recommended that information technologies should be employed for wider dissemination of information, for instance, by placing the information on the company's website. It is recommended that information should be published and placed on the company's website not only in Lithuanian, but also in English, and,	Yes	Company's information is published on its website in Lithuanian. Topical information for investors is published also in English.

whenever possible and necessary, in other languages as well.		
10.7. It is recommended that the company's annual reports and other periodical accounts prepared by the company should be placed on the company's website. It is recommended that the company should announce information about material events and changes in the price of the company's shares on the Stock Exchange on the company's website too.	Yes	All the information provided in this recommendation is announced publicly and placed on the Company's website, on the website of Nasdaq Vilnius Stock Exchange and it can be reached by all the interested persons.
Principle XI: The selection of the company's auditor **The mechanism of the selection of the company's auditor should ensure independence of the firm of auditor's conclusion and opinion.**		
11.1. An annual audit of the company's financial reports and interim reports should be conducted by an independent firm of auditors in order to provide an external and objective opinion on the company's financial statements	Yes	The set of annual financial statements and the annual report of the Company is verified by the independent audit company.
11.2. It is recommended that the company's supervisory board and, where it is not set up, the company's board should propose a candidate firm of auditors to the general shareholders' meeting.	No	The candidature of the Company's audit company which accomplished audit of financial statements of the year 2016, was presented to the General meeting of shareholders by the Management Board in compliance with the results of the public procurement implemented in 2015.
11.3. It is recommended that the company should disclose to its shareholders the level of fees paid to the firm of auditors for non-audit services rendered to the company. This information should be also known to the company's supervisory board and, where it is not formed, the company's board upon their consideration which firm of auditors to propose for the general shareholders' meeting.	Not applicable	The information provided in the recommendation was not presented to the shareholders because the audit company did not provide non-audit services for the Company in the year 2016.

SUSTAINABILITY REPORT IN ACCORDANCE WITH GRI STANDARDS 2016

AB KAUNO ENERGIJA

AB Kauno Energija is the second largest district heating company in Lithuania, producing and supplying heat for consumers in the cities of Kaunas and Jurbarkas and in Kaunas district for more than 50 years already. The company takes care on the living and working conditions of inhabitant of these cities, of their wellbeing and even health, because people cannot live without heat.

As a heat generating enterprise, our Company is directly related with emissions of combustion products into environment, therefore it is especially sensitively observed by both institutions responsible for environment protection and citizens of the city. This is why we – heat producers and suppliers must work insomuch not to only making certain reliable uninterrupted heat supplies at any circumstances, but also that equipment used in our activities would not pollute environment or at least would not exceed permissible limits. Therefore heat supplies may be considered more as social favour, not a profit seeking business.

In 2016, in order to reduce heat price for consumers, to reduce demand in fossil fuel, to increase the efficiency of heat production and the usage of renewable energy sources, the Company continued accomplishing of its strategic program of modernization of its heat production facilities. A new 5 MW capacity biofuel burned boiler was built in the boiler-house of company's affiliate "Jurbarkas heat networks". Implementation of this project let reduce heat production costs in Jurbarkas at more than three times and practically to refuse usage of fossil fuel in this boiler-house.

In order to encourage society's progress, the Company further supported academic community, cooperated with Kaunas University of Technology, with Lithuanian Energy Institute and other scientific institutions.

This report provides the information on Company's progress during the year 2016, considering economic, social and environmental aspects, as well as our Company's environmental policy and indicators.

The Company intends to further follow principles of social responsibility in its activities, allowing remaining reliable and responsible company.

Dr. Rimantas Bakas
General Director of AB Kauno Energija

Content

The GRI Standards will come into full use from 2018, although organisations are being encouraged to adopt them sooner. This report has been prepared in accordance with GRI Standards: Core option.

There are two options for preparation in accordance with GRI Standards Core and Comprehensive. As this is the first time the company has applied the GRI Standards, the report will be 'Core' option – providing the minimum information required in order to understand the nature of the company and how it manages its material topics and related impacts.

The GRI Standards list 33 categories of material topics under three topic specific standards: Economic (GRI 200 x 6); Environmental (GRI 300 x 8); and Social (GRI 400 x 19). The GRI 101: Foundation clause 1.3 is quite clear on how to choose the material topics for Core reporting:

The report shall cover topics that:

- 1.3.1 reflect the reporting organization's significant economic, environmental, and social impacts;
  or
- 1.3.2 substantively influence the assessments and decisions of stakeholders.

Therefore, only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or if the topics have an influence on the decisions of stakeholders, should be reported on.

However, the procurement for services to complete this report states that all 33 GRI standards should be reported on.

Therefore, although all 33 material topic are reported on, only those with significance under clause 1.3 (quoted above) are reported on in full and with reference to the comprehensive conditions of GRI 103.

In all other cases where a required disclosure is reported using a reference to another source where the information is located, all efforts have been made to ensure that a specific location is referenced, as well as ensuring that this location is readily and publicly available. These additional sources may include other materials produced by the company such as its annual report and full financial statements. In this case, a section name or other specific information is provided. If disclosures are not provided, then any reason for omission is within the GRI 101 / Clause 3.2 'Reasons for Omission'.

Under the GRI Standards, the reporting conditions are clear. There are three inclusions to consider:

- **Requirements.** These are mandatory instructions and are read in the context of recommendations and guidance. An organization is required to comply with all applicable requirements in order to claim that its report has been prepared in accordance with the GRI Standards.
- **Recommendations.** These are cases where a particular course of action is encouraged, but not required. Guidance. These sections include background information, explanations and examples to help organizations better understand the requirements. However, **an organization is not required to comply with recommendations or guidance in order to claim that a report has been prepared in accordance with the Standards**. This report has fulfilled all applicable requirements, and where possible, all applicable recommendations.

The material topics chosen for this report are as follows:

- **GRI 204 Procurement Practices**: the company (in 2016) procured some 60% of its heat provision from independent heat producers, this GRI standard is perhaps the most important within this topic.
- **GRI 305 Emissions**: (2016 figures) emissions increased if compared to the previous periods. This topic is perhaps also the most relevant for GRI 300.
- **GRI 307 Environmental Compliance**: because Kauno energija is compliant, this is a highly positive reporting standard for the company.
- **GRI 308 Supplier Environmental Assessment**: included because it needs to improve as there is currently no environmental assessment of suppliers. In order to comply with GRI standards this situation will need to improve.
- **GRI 403 Occupational Health and Safety**: the company is strong on employee relations. This topic is mainly related to illnesses and trade union agreements - for which the information is readily available.
- **GRI 414 Supplier Social Assessment**: Linked to GRI 308, and important also for the same reasons
- **GRI 415 Public Policy**: connected to contributions / connections to political parties and lobbying.
- **GRI 416 Customer Health and Safety**: compliance to regulations and to list any serious accidents or issues.

This report presents the AB Kaunas energy activity in 2016. This GRI Standards Report forms part of the seventh AB Kaunas Energy "Social responsibility report", which is produced annually and published in conjunction with the company's consolidated annual report and financial statement.

To the best of our knowledge, the ten reporting principles as laid down in GRI 101 have been applied, disclosures provide contextual information about the company, and every relevant material topic has been identified and reported on.

Reporting Principles for defining report content	Reporting Principles for defining report quality
Stakeholder Inclusiveness	Accuracy
Sustainability Context	Balance
Materiality	Clarity
Completeness	Comparability
	Reliability
	Timeliness

With this report AB Kaunas Energija seeks to provide non-financial corporate responsibility information to its stakeholders: clients (users), shareholders, investors, employees, suppliers, business and social partners and the public.

GRI 102 General Disclosures

ORGANIZATIONAL PROFILE

102-1	Name of the organization	AB „Kauno energija“ (EN Public Company Kaunas Energy)
102-2	Activities, brands, products, and services	http://www.kaunoenergija.lt/bendroves-veikla/apie-bendrove/
102-3	Location of headquarters	Raudondvario pl. 84, 47179 Kaunas, Lithuania
102-4	Location of operations	Lithuania, Kaunas, Kauno region, Jurbarkas.
102-5	Ownership and legal form	Information presented in the annual report. Section 2
102-6	Markets served	Information presented in the annual report. Section 3
102-7	Scale of the Organisation:	Information presented in the annual report: i) total number of employees Section 18 ii) total number of operations Section 5 iii) net revenues Section 7 iv) Not Applicable v) quantity of products / services provided Section 6.1

102-8	Information on employees and other workers	Information about employees (data Kauno Energija including Jurbakas Branch) from December 2016.

	Total Number of Employees 2016-12-31	Fixed-term employment contracts			Open-ended contracts		
		Total	Women	Men	Total	Women	Men
a)	508	6	1	5	502	157	345

	Total Number of Employees 2016-12-31	Full-time Employees			Part-time Employees		
		Total	Women	Men	Total	Women	Men
b)	508	476	136	340	32	22	10

c) All these employees work within the Kaunas and Jurbarkas region.

d) The major part of the company's activities are carried out by company employees. There are external service contractors employed on projects and these are selected and employed through Public Procurement in accordance with Lithuanian law. The percentage of work that they perform is not monitored.

e) No significant changes in these figures.

f) All employee data is compiled and processed by the company's staff and administration departments.

102-9 Supply chain

The main suppliers in terms of bulk services bought are the independent heat producers of which, in accordance with legislation, the company buys heat from, and supplies heat to consumers. In 2016, the company bought from 11 suppliers in Kaunas and the Kaunas area. These suppliers are:

- UAB Kauno termofikacijos elektrinė
- UAB „GECO Kaunas“
- UAB „Lorizon energy“
- UAB „Ekoresursai“
- UAB „Petrašiūnų katilinė“
- UAB „Aldec General“
- UAB „ENG“
- UAB „Danpower Baltic Biruliškių“
- UAB „Ekopartneris“
- UAB „SSPC-Taika“
- UAB „Foksita“

In total the company purchased 844.3 thousand. MWh of heat vol. i. y. representing 59.1 percent of the heat supplied to the grid (compared to 60.4 percent in 2015).

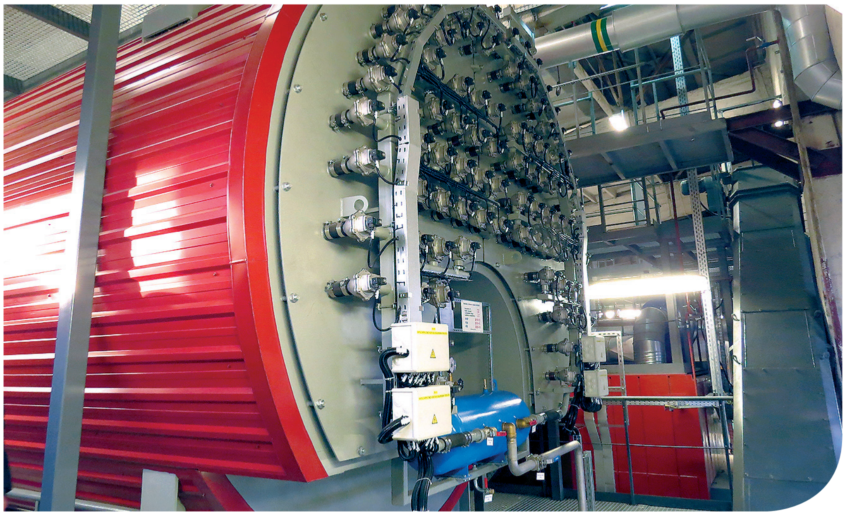
In 2016, the company engaged with a total of 579 Lithuanian suppliers and six external to Lithuania: a total of 585 suppliers providing a range of small local services across the broad scope of the company's activities.

102-10 Significant changes to the organization and its supply chain

There were no significant changes to the organisation and its supply chain or in the structure of outsourcing of services for heat supply.

102-11	Precautionary Principle or approach	The EU policy on the environment states that it *shall aim at a high level of protection taking into account the diversity of situations in the various regions of the Union. It shall be based on the precautionary principle and on the principles that preventive action should be taken, that environmental damage should as a priority be rectified at source and that the polluter should pay.* Within this understanding, the company applies where practical the same precautionary principle in seeking not to generate significant environmental impact, and where there is impact of any nature the company seeks to address this quickly and clearly.
102-12	External initiatives	Kauno Energija is a member of the UN Global Compact. The company also supports and encourages its employees to participate in the national and regional initiative „MesDarom.lt" (http://mesdarom.lt/aktualijos.html). This is scheme for community and companies to clean up the local areas.
102-13	Membership of associations	The company is a member of the following associations: - Lithuanian District Heating Association - Lithuanian Electricity Association - Kaunas Region Industrialists and Employers Association - Kaunas Regional Energy Agency (Kauno Energija is one of the four founders of this Agency)

STRATEGY



102-14	Statement from senior decision-maker	The year 2016 proved to be a significant year in progress made. The company commitment to social responsible reporting has stepped up a gear to now include the GRI Standards methodology, further strengthening our commitment to being a socially and environmentally supportive company. Our committment to being people focused and results driven has helped the company to reduce by half the cost of heating for customers. We constantly seek to improve our range of environmental management initiatives in all our day-to-day activities, from the attention paid to strict control of emissions from our heat sources, to the emission data collected from our use of fluorescent lamps, tyres, wastewater and other waste amounts. Our company strategy remains one that is fully focused on strengthening our role as a leader in transparent and inclusive social, economic and environmental reporting.
102-15	Key impacts, risks, and opportunities	Not required for CORE reporting

ETHNICS AND INTEGRITY

102-16	Values, principles, standards, and norms of behaviour	Information provided on the company website under mission and vision, and values and strategic objectives: http://www.kaunoenergija.lt/bendroves-veikla/apie-bendrove/misija-ir-vertybes/
102-17	Mechanisms for advice and concerns about ethics	Not required for CORE reporting

GOVERNANCE

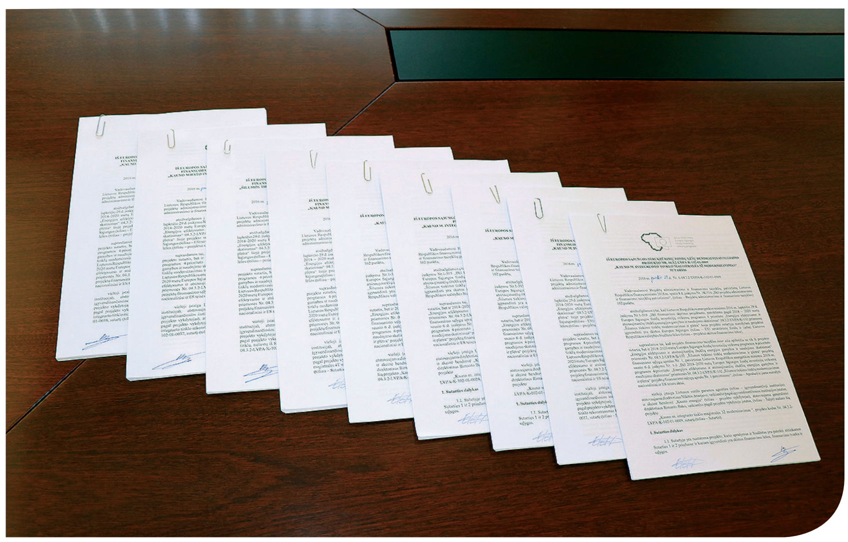
102-18	Governance structure	a) Information about the company's management structure is here http://www.kaunoenergija.lt/bendroves-veikla/apie-bendrove/bendroves-valdymas/ b) Committees responsible for decision-making on economic, environmental, and social topics include: ■ **Audit Committee** made up from a minimum of three members, at least one of which is independent. There are currently six members: three external and independent, and three from among the company's employees (Economic, Accounting, and Judicial/Legal department). The Audit Committee operates under the supervisory board in 2015. 26 October approved by the company's audit committee's internal rules (http://www.kaunoenergija.lt/wp-content/uploads/2016/02/Audito-komiteto-vidaus-taisykl%C4%97s_20151026.pdf) ■ **Technical Board** (under the General Order of the Director), which examines adopted resolutions and makes recommendations to the company's General Manager on a range of economic, social and environmental topics. During 2016, the Technical Council met 13 times. ■ **A number of permanent committees** established too address specific operational issues. ■ **Occupational health & safety committee** – will be established in 2017
102-19 to 102-39	Governance	Not required for CORE reporting

STAKEHOLDER ENGAGEMENT

102-40	List of stakeholder groups	These stakeholders are those individuals or groups to whom the company considers itself accountable and those to whom we expect to be affected by the company's activities or provision of services: - The company's shareholders (among them the city of Kaunas, and Kaunas and Jurbarkas District Municipality). A full list of the 300 or so individual shareholders is held by our financial partner SEB Bank. - The company's managers and employees, and workers union - Non-employee workers (connected to key service providers for the company), and service customers - Business partners - including suppliers of goods, service providers, contractors, independent heat producers,
102-41	Collective bargaining agreements	Yes, the company is set up and operate a Collective Agreement. It is posted on the company intranet site and updated periodically. It applies not only to workers' trade union members, but also to all employees of the company (100%). The Company's intranet site is provided here (but please note that it is only accessible from within the company's local network): http://web/sharepoint/portal/Shared%20Documents/KOLEKTYVINE_SUTARTIS_2013.pdf
102-42	Identifying and selecting stakeholders	All stakeholders and interest groups are identified through their direct connection to the company and the company activities. Any other interested individuals or groups are encouraged to be involved in our engagement activities or events. With regard to the goods suppliers, service providers and works contractors are selected through public procurement in accordance with Lithuanian and/or EU law.
102-43	Approach to stakeholder engagement	The company's shareholders receive periodical activity reports, annual reports, CSR reports, and reports on coordinated investment projects. The company's managers and employees communicate daily through departmental and inter-departmental communication. Customers with queries about their service provision are in touch with the company Customer Service Department via telephone, e-mail, and postal mail. Information is also available to consumers and the media through the company and Kaunas Municipality websites. Once a year the company carries out customer quality service surveys. Also, two to three times a year there are face to face meetings with customers held at the company premises and organised to respond to relevant new development sin the company services. Here members of the management take questions from participants. Announcement of the meetings are published in local newspaper "Kauno diena", also on the company web site and at the entrance to the company's Customer Service Department building door. In 2016 we held two such meetings.

		The purpose of the company's interaction with stakeholders is to ensure that the company remains an open and transparent company, constantly seeking to improve its performance and service delivery standards.
102-44	Key topics and concerns raised	With customers the key issues relate to costs and technical problems with the heating system. The company also has regular issues to respond to, that are raised by the main shareholder Kaunas City Municipality as well as the National Commission for Energy Control and Prices. All such issues are controlled and responded to through the company's customer service department in partnership with the relevant technical and management leaders within the company. An example of where company practice has changed/improved based on customer feedback is as follows: Three years ago, the Company changed the order of hydraulic testing of pipelines. The new method divided the network into smaller zones meaning that the supply of hot water was stopped for a smaller number of consumers and for a shorter time. Instead of the previous two week stoppage during testing, the supply of hot water is now stopped for only two to three days.

REPORTING PRACTICE



102-45	Entities included in the consolidated financial statements	a) A list of all entities included in the organization's consolidated financial statements or equivalent documents: please see AR Section 4 to 17. b) The organization's consolidated financial statements or equivalent documents cover the Kauno Energija (together with its affiliates "Jurbarkas heat networks").
102-46	Defining report content and topic Boundaries	a) Due to the GRI Standards being a totally new methodology, untried so far and in its inaugural phase, Kauno Energija have chosen those material topics that have the biggest bearing on their day to day activities, and that constitute the biggest part of their economic, social and environmental impact. The choice of material topics will more likely increase for the next year report because some pre-planning reporting structures should be in place in the coming year. b) Kauno Energija has used material topics that have been previously reported on through the inclusion of stakeholders. These material topics are within our previous sustainability reporting structures.

102-47	List of material topics	GRI 204 – Procurement Practices GRI 305 – Emissions GRI 307 – Environmental Compliance GRI 308 – Supplier Environmental Assessment GRI 403 - Occupational Health and Safety GRI 414 - Supplier Social Assessment GRI 415 – Public Policy GRI 416 – Customer Health and Safety
102-48	Restatements of information	There are no reasons for restatements of information during the reporting period of 2016.
102-49	Changes in Reporting	None to report
102-50	Reporting Period	January 1st 2016 to December 31st 2016
102-51	Date of most recent report	This is the first report produced under GRI Standards. There are however annual reports and financial statements available for the period 2015
102-52	Reporting Cycle	Annual
102-53	Contact point for questions regarding the report	Mr. Ūdrys Staselka Personnel and Administration Division - Public Relations AB „Kauno energija" Tel. +370 37 30 58 85 / Mob. +370 650 96 883 e-mail: u.staselka@kaunoenergija.lt / www.kaunoenergija.lt
102-54	Claims of reporting in accordance with the GRI Standards	This report has been prepared in accordance with the GRI Standards: Core option
102-55	GRI content index	This report represents this GRI standard in full and in doing so fulfils the reporting requirements.
102-56	External assurance	This report has been prepared by an externally appointed organisation, procured through an open tender call for services. The preparation of the report takes information prepared for the audited accounts and annual report. However, the assurance of the quality of this GRI Standards Report is limited to the preparation following the guidelines of the GRI Standards only. This GRI Standards report has not been externally assured. However, the completed audited accounts and annual report have been passed and assured by the company board as part of its normal quality control of all information that is prepared for shareholders.

GRI 103 Management Approach

GRI 204 PROCUREMENT PRACTICES

103-1 GRI 204	Explanation of the material topic and its Boundary	The company main procurement of services comes through the monthly procurement of provision of heating services from independent heat producers. These services represent 59% of consumers heat demand. This is a substantial amount of procurement, making this topic an obvious choice. The boundary is with all of the business and residential customers who receive heating using these sources, and it is here where any potential impacts will be felt. The company seeks to minimise these and any other boundary impacts through close management and quality control of these relationships on a regular basis. If serious impacts are likely to occur, we can correct through improved procurement procedure month by month.
103-2 GRI 204	The management approach and its components	The company's services procurement procedure is organized by the Heat Procurement Commission (which includes company's employees from various departments). Much of our procurement procedures are governed by national regulations based on 2010 legislation. This governs all heat providers in Lithuania. https://www.e-tar.lt/portal/lt/legalAct/TAR.A37C2263838C/qCQgCxlhFq The rules of procurement represent our Procurement policy: http://www.kaunoenergija.lt/bendroves-veikla/viesieji-pirkimai/viesuju-pirkimu-taisykles/ Company goals and targets for procurement practices are defined in law as we are obliged to provide the lowest price. All heat providers have technical measurements made of their service delivery to make sure it satisfies the conditions of the procurement contract. Responsibilities are within the company's Heat Procurement Commission and associated company departments. Grievances are dealt with here also. All procurement announcements and winning contracts are published on the company website: http://www.kaunoenergija.lt/bendroves-veikla/viesieji-pirkimai/biokuro-isigijimas/?ay=2017&am=2 http://www.kaunoenergija.lt/verslui/nepriklausomiems-silumos-gamintojams/silumos-supirkimas/

103-3 GRI 204	Evaluation of the management approach	Evaluation of the management approach is not formally carried out. However, the management approach is systematically linked to the procurement process and although evaluation is not carried out, adjustments can be made to the management approach through employee or client feedback. It is expected that this disclosure will provide details that are more positive next year.
103	With reference to clause 1.1 of GRI 103 Management Approach, the disclosures are combined for GRI 300 'Environmental' material topics. - GRI 305 – Emissions - GRI 307 – Environmental Compliance - GRI 308 – Supplier Environmental Assessment	
103-1 GRI 300	Explanation of the material topic and its Boundary:	Three material topics have been chosen here as the most relevant for reporting purposes: **Emissions**; **Environmental Compliance** and **Supplier Environmental Assessment**. The company has high emissions into the air from its activities; environmental compliance is crucial if the company wants to maintain its commitment to the environment, to stay compliant, and to continue its high level of transparency in reporting such actions. Supplier environmental assessment needs to improve, which is why it is included here. The company wants to break with old practices and establish itself as positively encouraging suppliers to adopt a more environmental approach to business. Emissions and environmental compliance have an impact wider than local sites. Therefore, the boundary for impacts for these material topics are within all company sites as well as throughout the whole country.
103-2 GRI 300	The management approach and its components	The company does a good job of managing the topic within the company but could improve its management approach outside the company in relationships with clients / service providers. Internally the management systems in place to record and report on environmental impact are very strong. There is a special certified environmental laboratory installed to manage, collect, and process all relevant environmental data on company activities. The management systems in place to manage and control the environmental impact made by suppliers / external relationships are non-existent, and would be difficult to impose if they did exist. For smaller suppliers (eg: stationery, printing, and similar) there is a process of installing into the procurement for these smaller priced suppliers, conditions for environmental goods, materials, or equipment to be used or provided. The printing of the company's Annual Report and Financial Statement, along with the Sustainability Report are printed on recycled or environmentally friendly paper. Such small improvements to the company's environmental commitment can be more easily implemented than any similar such improvements to larger technical service providers whose contracts are regulated based on national guidelines.
103-3 GRI 300	Evaluation of the management approach	Evaluation of the management approach is not formally carried out. However, the management approach is systematically linked to the company's committment to non-financial reporting and although evaluation is not carried out, suggestions can be made to the management approach through employee or client feedback. It is expected that this disclosure will provide marked improvements for next year.

103	With reference to clause 1.1 of GRI 103 Management Approach, the disclosures are combined for GRI 400 ''Social' material topics. - GRI 403 - Occupational Health and Safety - GRI 414 - Supplier Social Assessment - GRI 415 – Public Policy - GRI 416 – Customer Health and Safety	
103-1 GRI 400	Explanation of the material topic and its Boundary:	The company has identified and chosen four material topics within GRI 400. These are: **Occupational Health and Safety**; **Supplier Social Assessment**; **Public Policy** and **Customer Health and Safety**. The company is strong on employee relations and wants to provide regular reports on progress made in the health and safety issues for the company and its employees. The social assessment of suppliers fits into improvements we wish to make in this topic and is linked to environmental assessment of suppliers. Public policy is important because we provide a public service and are part of the city municipality services offered to the public. Any connections to political parties or political lobbying we want to be open and transparent. Customer health and safety is tantamount to our company, and as such, it should be included here. The company follows a strict regime of compliance to regulations. Here the boundary for impacts remains mainly focused on local and regional sites, along with all stakeholders within these areas.
103-2 GRI 400	The management approach and its components	Internally the company has a strong management approach for social and health and safety issues related to employees. This includes a collective agreement for all employees, an employee's safety and health department, health and safety committee being established, and established procedures for employees to voice their concerns, suggestions, or grievances. Employee's safety and health department has five staff: three for safety issues and two for health issues, as well as a company medical team on site in the head office. They follow and implement regulations as laid down by national state institutions. Regular articles and campaign notices related to health and safety issues are posted on the company intranet for employees. New employees are provided with instructions on basic health and safety company policies. Those working in manual roles are provided with a safety supervisor during the initial starting period. The company's health and safety team carry out regular workplace inspections both of company sites where employees are working, as well as company sites where non-employees are working.
103-3 GRI 400	Evaluation of the management approach	Evaluation of the management approach is not formally carried out. However, the management approach is systematically linked to the company's committment to non-financial reporting and although evaluation is not carried out, suggestions can be made to the management approach through employee or client feedback. It is expected that this disclosure will provide marked improvements for next year.

Please note: Reasons for omissions are permitted for all topic-specific disclosures (see clause 3.2)

Topic Specific Standards

GRI 200 ECONOMIC

201	Economic Performance	Only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or those which have an influence on the decisions of stakeholders, have been included and reported on (**GRI 101 Foundation: 3.1 guidance**).
202	Market Presence	
203	Indirect Economic Impacts	
204	Procurement Practices 204-1 Proportion of spending on local suppliers	The percentage of procurement budget that is spent on suppliers local to that operation (such as percentage of products and services purchased locally) is 100%. Local is defined as being within Lithuania. Our definition of 'signifcant locations of operation' is as above: the wider areas in which the company operates
205	Anti-corruption	Only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or those which have an influence on the decisions of stakeholders, have been included and reported on (**GRI 101 Foundation: 3.1 guidance**).
206	Anti-competitive behaviour	

GRI 300 ENVIRONMENTAL

301	Materials	Only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or those which have an influence on the decisions of stakeholders, have been included and reported on (**GRI 101 Foundation: 3.1 guidance**).
302	Energy	
303	Water	
304	Biodiversity	
305	Emissions	
	305-1 Direct (Scope 1) GHG emissions	Omission of Disclosure (allowed under **GRI 101 Foundation – section 3.2**): Full disclosure information is available but not in the format required for this report. A new company data collection system is currently being implemented and this disclosure will be fully on in 2017. GHG emissions from company's heat production facilities
	305-2 Energy indirect (Scope 2) GHG emissions	Omission of Disclosure (allowed under **GRI 101 Foundation – section 3.2**): Full disclosure information is available but not in the format required for this report. A new company data collection system is currently being implemented and this disclosure will be fully on in 2017.
	305-3 Other indirect (Scope 3) GHG emissions	Omission of Disclosure (allowed under **GRI 101 Foundation – section 3.2**): Full disclosure information is available but not in the format required for this report. A new company data collection system is currently being implemented and this disclosure will be fully on in 2017.
	305-4 GHG emissions intensity	Omission of Disclosure (allowed under **GRI 101 Foundation – section 3.2**): Full disclosure information is available but not in the format required for this report. A new company data collection system is currently being implemented and this disclosure will be fully on in 2017.

GHG emissions from company's heat production facilities (305-1):

Year	2013	2014	2015	2016
Emissions of GHG, t CO_2 equivalent	36042	32711	8607	8480

	305-5 Reduction of GHG emissions	Omission of Disclosure (allowed under **GRI 101 Foundation – section 3.2**): Full disclosure information is available but not in the format required for this report. A new company data collection system is currently being implemented and this disclosure will be fully on in 2017. In order not to adversely impact the environment and comply with the pollution limits, vibration and noise values, the Company is guided by the requirements of the Kyoto Protocol, the Helsinki Commission (HELCOM) and environmental constraints of Helsinki Convention, as well as the European Parliament and Council Directive 2001/80/EB of regulating energy emissions and Lithuanian environmental normative document LAND 43-2013 for the use of natural resources, and releases and emissions of air pollutants to the environment in its activities. Main sources of pollution of the Company: burning fossil fuel in the Company's heat sources, production of heat and waste water, are used in the industrial processes. The Company pays taxes for atmospheric and water pollution. If allowable emission rate limits or annual limits are exceeded, the Company must pay the fines under the applicable laws of the Republic of Lithuania. There have been no pollution-related incidents and the Company was not imposed any penalties in 2015. The measurement laboratory of stationary air pollution sources of the Group and the Company, having the permit issued by the Environmental Protection Agency, continuously monitors that the emissions to the atmosphere from stationary sources would not exceed the permissible limits established in integrated pollution prevention and control permits. Boiler-houses of Šilkas, Ežerėlis, Girionys and Noreikiškės, and starting from 2015 – Inkaras boiler-house and Petrašiūnai power-plant use biofuels, thus reducing atmospheric pollution.
	305-6 Emissions of ozone-depleting substances (ODS)	Omission of Disclosure (allowed under **GRI 101 Foundation – section 3.2**): Full disclosure information is available but not in the format required for this report. A new company data collection system is currently being implemented and this disclosure will be fully on in 2017.
	305-7 Nitrogen oxides (NOX), sulphur oxides (SOX), and other significant air emissions	Full reporting of those available and relevant requirements of this disclosure is contained in AR Section 7.

Per Year, t	2012 m.	2013 m.	2014 m.	2015 m.	2016 m.
Particulates	54,3160	10,5967	23,613	43,5783	53,7542
Nitrogen Oxides	54,3160	101,3197	154,570	203,6775	265,0797
Carbon Monoxide	135,1510	299,6656	534,443	904,8513	1155,3349
Sulphur Dioxide	6,0280	5,0747	47,158	193,3228	231,4719
Hydro-carbons	1,2080	14,9647	16,294	20,1586	4,2871
Vanadium Pentoxide	0,0000	0,0000	0,0000	0,0000	0,0000
Others	0,4397	0,770	0,440	0,2818	0,2818

306	Effluents and waste	Only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or those which have an influence on the decisions of stakeholders, have been included and reported on (**GRI 101 Foundation: 3.1 guidance**).

307	Environmental compliance	
	307-1 Non-compliance with environmental laws and regulations	During this reporting period, the company did not receive any fines or sanctions for non-compliance with environmental laws and/or regulations at all, nor were any legal cases brought against the company during this time.
308	Supplier environmental assessment	
	308-1 New suppliers that were screened using environmental criteria	No suppliers were screened using environmental criteria during this reporting period.
	308-2 Negative environmental impacts in the supply chain and actions taken	No suppliers were screened or assessed for environmental impacts using environmental criteria during this reporting period.

GRI 400 SOCIAL

401	Employment	Only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or those which have an influence on the decisions of stakeholders, have been included and reported on (**GRI 101 Foundation: 3.1 guidance**).
402	Labour management relations	
403	Occupational health and safety	
	403-1 Workers representation in formal joint management-worker health and safety committees	The company is establishing now an occupational health and safety committee following the principles, roles and responsibilities as defined by the Occupational Safety and Health Committees of the General Regulations, approved by the Lithuanian Ministry of Social Security and Labour Minister in 2013. 9 September. Order no. A1-502. This committee will operate at a senior management level within the company, reporting directly to the Company Director / Board. This committee will represent 100% of the workforce employees.

	403-2 Types of injury and rates of injury, occupational diseases, lost days, and absenteeism, and number of work-related fatalities	Omission of Disclosure (allowed under **GRI 101 Foundation – section 3.2**): Full disclosure information is available but not in the format required for this report. A new company data collection system is currently being implemented and this disclosure will be fully on in 2017. All accidents are recorded and investigated if necessary under minor or major categories. Much of this reporting is required and covered by legal requirements and linked to information required by the national Social Insurance organisation (SODRA).
	403-3 Workers with high incidence or high risk of diseases related to their occupation	The company does not have any occupational activities that would put its workers at high incidence rate, or high risk of specific diseases.
	403-4 Health and safety topics covered in formal agreements with trade unions	The company is establishing an occupational health and safety committee following the principles, roles and responsibilities as defined by the Occupational Safety and Health Committees of the General Regulations, approved by the Lithuanian Ministry of Social Security and Labour Minister in 2013. 9 September. Order no. A1-502. This committee will work with the trade union and will cover 100% of all health and safety topics within the work place and work broader work environment.
404	Training and Education	Only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or those which have an influence on the decisions of stakeholders, have been included and reported on (**GRI 101 Foundation: 3.1 guidance**).
405	Diversity and Equal Opportunity	
406	Non-discrimination	
407	Freedom of association and collective bargaining	
408	Child labour	
409	Forced or compulsory labour	
410	Security practices	
411	Rights of indigenous peoples	
412	Human rights assessment	
413	Local communities	
414	Supplier social assessment 414-1 New suppliers that were screened using social criteria	No suppliers were screened using social criteria during this reporting period.

	414-2 Negative social impacts in the supply chain and actions taken	No suppliers were screened or assessed for social impacts using social criteria during this reporting period.
415	Public policy 415-1 Political contributions	No financial or in-kind political contributions made directly or indirectly.
416	Customer health and safety 416-1 Assessment of the health and safety impacts of product and service categories	No significant product and service categories for which health and safety impacts are assessed for improvement.
	416-2 Incidents of non-compliance concerning the health and safety impacts of products and services	The company has had no identifed or recorded non-compliance with regulations and/or voluntary codes.
417	Marketing and labelling	Only those material topics which the company believes to bear a significance upon the company's economic, social and environmental impacts, or those which have an influence on the decisions of stakeholders, have been included and reported on (**GRI 101 Foundation: 3.1 guidance**).
418	Customer privacy	
419	Socioeconomic compliance	

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AB Kauno Energija is the second largest district heating company in Lithuania, producing and supplying heat for consumers in the cities of Kaunas and Jurbarkas and in Kaunas district for more than 50 years already. The company takes care on the living and working conditions of inhabitant of these cities, of their wellbeing and even health, because people cannot live without heat.