

## ***INDEPENDENT AUDITORS' REPORT***

***To the Shareholders of AS Daugavpils Lokomotīvu Remonta Rūpnīca***

### ***Our Opinion on the Consolidated Financial Statements***

We have audited the accompanying consolidated financial statements of AS Daugavpils Lokomotīvu Remonta Rūpnīca (the Company) and its subsidiaries (“the Group”) set out on pages 7 to 38 of the accompanying consolidated annual report, which comprise:

- the statement of financial position as at 31 December 2016,
- the statement of comprehensive income for the year then ended,
- the consolidated statement of changes in equity for the year then ended,
- the consolidated statement of cash flows for the year then ended, and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies and other explanatory notes.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Company and its subsidiaries as at 31 December 2016, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS).

### ***Basis for Opinion***

In accordance with the Law on Audit Services of the Republic of Latvia (the Law on Audit Services) we conducted our audit in accordance with International Standards on Auditing adopted in the Republic of Latvia (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report.

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and independence requirements included in the Law on Audit Services that are relevant to our audit of the consolidated financial statements in the Republic of Latvia. We have also fulfilled our other professional ethics responsibilities and objectivity requirements in accordance with the IESBA Code and Law on Audit Services.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### ***Emphasis of Matter***

We draw attention to the Note 12 to the financial statements. At the end of 2016 the carrying value of tangible assets is EUR 12,8m, including carrying value of real estate of EUR 6,8m and production equipment of EUR 6m. The management has performed the impairment test by value in use method estimating the present value of future cash flows and has satisfied itself that no impairment of assets incurred. In the Note 31 to the financial statements, the Group discloses information on sharp decrease of customers' orders and revenues at the end of 2015 and in 2016 mostly caused by the economic sanctions towards Russia and its response by the way of trade restrictions. We pay attention to these negative external factors, and therefore, significant level of uncertainty related to the future cash flows that could have a material impact on the calculation of recoverable value of assets. Our opinion is not modified in respect of this matter.



## Key Audit Matters

Key Audit Matters are those matters that, in our professional judgement, were of most significance in our audit of the 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.

In addition to the matters described in the Emphasis of Matter section, we have determined the matters described below to be the key audit matters to be communicated in our report.

Key audit matters	How our audit addressed the key audit matters
<p><i>Recognition of the Joint arrangement's operations in General partnership DMU vilcieni</i></p> <p>As disclosed in the Notes 13 un 29 to the financial statements the Group, as a member of Partnership DMU vilcieni ("the Partnership), has performed the part of EUR 22m contract for modernization of diesel trains ("the Contract"). The Group has assessed its joint arrangement in Partnership as joint operation and recognizes the joint operation's assets, liabilities, income and expense in its consolidated financial statements.</p> <p>Our audit report on the Group's financial statements for the year ended 31 December 2015 was modified in respect of audit scope limitation for the measurement of Partnership's provisions, financial results and its impact to the Group financial statements.</p> <p>Partnership has incurred significant losses and as at 31 December 2016 the Contract's 2-year warranty period is in force.</p> <p>Taking into account the matters described above, the measurement of Partnership's financial results and position at the year and its recognition in the Group financial statements was determined as a key audit matter.</p>	<p>We assessed whether the Group's accounting policies in relation to Joint arrangement in Partnership are in compliance with IFRS.</p> <p>We assessed and discussed with the Group's management the outcome of the Contract, warranty obligations and other significant terms of the Contract as well as terms of agreement between the members of the Partnership for the split of work, obligations, liabilities and financial results. We have obtained the opinion of the Partnership's legal adviser on these issues.</p> <p>Based on unaudited Partnership's financial statements, future cash flow estimates and split of financial results between the members, the management prepared the financial results and position of joint operations to be included in the consolidated financial statements of the Group. We performed procedures to obtain the sufficient evidence on the Partnership's financial results and position as at 31 December 2016. We reviewed the principles and methods used by the management on the split of financial results between the members. We assessed management's estimates of the warranty liabilities of the remained warranty period, acquiring and analyzing information on the actual warranty costs and discussing the reasonableness of assumptions used. We examined whether the disclosures made in the financial statements met the requirements set out in IFRS.</p>
<p><i>Impairment assessment of inventories' balances</i></p> <p>As at 31 December 2016 the Group's inventories' balances, less impairment losses, are EUR 3,6m. As disclosed in the Note 14 to the financial statements the inventories comprises mostly materials and finished goods. Part of the inventories' items have slow moving ratios.</p> <p>Management's assessment of the impairment of the aforementioned assets involves judgmental estimates. Inventories are grouped by the types (models) of serviced or sold rolling stocks and future volume of its use in the course of production or its potential selling value is estimated. These</p>	<p>We assessed the assumptions and methods used by the management in their impairment test, in particular assumptions related to the forecasted sales orders and potential selling value.</p> <p>We reviewed whether the management impairment calculations prepared based on financial accounting data. We discussed with the management the assumptions for the volume of forecasted sales orders and its correlation with historical data. For individually significant items the management estimated the potential selling value. With professional criticism, we have assessed the management estimates and built our own estimates of significant</p>



<p>assumptions are driven by the general economic environment and conditions in the key markets the Group is operating.</p> <p>The abovementioned balances are material to the financial statements and therefore our audit procedures on the impairment tests are one of key audit matters.</p>	<p>assumptions and its impact to the total value of impairment.</p> <p>We examined whether the adequate disclosures made in the financial statements, including the impairment methods used, met the requirements set out in IFRS.</p>
<p><i>Use of going concern assumption</i></p> <p>As disclosed in the Note 32 the Group has finished the year ended 31 December 2016 with losses of EUR 2,3m. At this date the Company's current liabilities exceeded current assets by EUR 7.7m.</p> <p>As of 31 December 2016 the Group's major creditors are the largest shareholder's AS Skinest Rail group companies (8.2 mil. EUR) and AS Swedbank with loans outstanding (2.6 mil. EUR). The Group does not comply with financial covenants in AS Swedbank loan agreements. The Group received a comfort letter from its shareholder AS Skinest Rail that it will support the Group to continue as a going concern in 2017.</p> <p>As the result of audit we concluded that no material uncertainty exists that may cast significant doubt on the Group's ability to continue as a going concern at least in 2017. Nevertheless, the audit procedures on identified risk events and conditions, its mitigating factors and conclusions reached has been determined as one of the audit key matters.</p>	<p>We have concluded that estimates of future cash flows, the extension of repayment terms of bank's loan and the support from shareholders are the main aspects to consider for going concern issue.</p> <p>We have discussed with the management material assumptions and risks related to these uncertainties and management plans to mitigate them. We have obtained and assessed the budget for 2017 prepared by the management, and also reviewed contracts, historical information and ratios that supports management assumptions of projected level of revenues and expenses.</p> <p>We have assessed the terms of AS Swedbank loan agreements and discussed with the Group's and AS Skinest Rail management the actions taken to restructure bank loans. In respect of support letter from AS Skinest Rail we have assessed historical relationship between the Group and AS Skinest Rail and financial resources provided. We have obtained the interim and audited financial statements and analyzed, whether the AS Skinest Rail has sufficient resources to provide such support.</p> <p>We examined the disclosure of information in financial statements on the management's conclusion of the use of going concern assumption.</p>

### **Reporting on Other Information**

Management is responsible for the other information. The other information comprises:

- the Management Report, as set out on pages 4 to 5 of the accompanying Consolidated Annual Report,
- the Statement on Management Responsibility, as set out on page 6 of the accompanying Consolidated Annual Report,
- the Statement of Corporate Governance, as published on the Company's homepage [www.dlrr.lv](http://www.dlrr.lv).

Our opinion on the consolidated financial statements does not cover the other information included in the Annual Report, and we do not express any form of assurance conclusion thereon, except as described in the *Other reporting responsibilities in accordance with the legislation of the Republic of Latvia* section of our report.

In connection with our audit of the 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 financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed and in light of the knowledge and understanding of the Group and its environment obtained in the course of our audit, 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.



### ***Other reporting responsibilities in accordance with the legislation of the Republic of Latvia***

In addition, in accordance with the Law on Audit Services with respect to the Management Report, our responsibility is to consider whether the Management Report is prepared in accordance with the requirements of the Law On the Annual Reports and Consolidated Annual Reports.

Based solely on the work required to be undertaken in the course of our audit, in our opinion:

- the information given in the Management Report for the financial year for which the consolidated financial statements are prepared is consistent with the consolidated financial statements; and
- the Management Report has been prepared in accordance with the requirements of the Law On the Annual Reports and Consolidated Annual Reports.

In accordance with the Law on Audit Services with respect to the Statement of Corporate Governance, our responsibility is to consider whether the Statement of Corporate Governance includes the information required in section 56.1, first paragraph, clause 3, 4, 6,, 8 and 9, as well as section 56.2, second paragraph, clause 5, and third paragraph of the Financial Instruments Market Law and if it includes the information stipulated in section 56.2 second paragraph, clause 1, 2, 3, 4, 7 and 8 of the Financial Instruments Market Law.

In our opinion, the Statement of Corporate Governance includes the information required in section 56.1, first paragraph, clause 3, 4, 6, 8 and 9, as well as section 56.2, second paragraph, clause 5, and third paragraph of the Financial Instruments Market Law and it includes the information stipulated in section 56.2 second paragraph, clause 1, 2, 3, 4, 7 and 8 of the Financial Instruments Market Law.

### ***Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements***

Management is responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with IFRS as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the 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 Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

### ***Auditor's Responsibilities for the Audit of the Consolidated Financial Statements***

Our objectives are to obtain reasonable assurance about whether the 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 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 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.



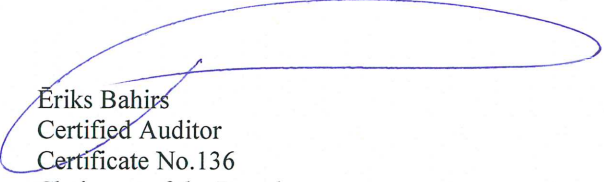
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the 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 to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves a fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the 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.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' 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 responsible certified auditor on the audit resulting in this independent auditors' report is Ēriks Bahirs.

Baker Tilly Baltics SIA  
Licence No. 80



Ēriks Bahirs  
Certified Auditor  
Certificate No.136  
Chairman of the Board

Riga, 2 May 2017