# JSC DITTON PIEVADĶĒŽU RŪPNĪCA

**Reg. No. 40003030187**

**Višķu St.17, Daugavpils, LV-5410, Latvia**

**Annual Report for the Year 2017**

**(Translation from Latvian)**

**and**

**Corporate Governance Report**

PREPARED IN COMPLIANCE WITH THE

LAW ON ANNUAL ACCOUNTS AND CONSOLIDATED ANNUAL ACCOUNTS

and Independent Auditors` Report

**(01.01.2017 – 31.12.2017)**

**Daugavpils**

**2018**

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# INFORMATION ABOUT THE COMPANY

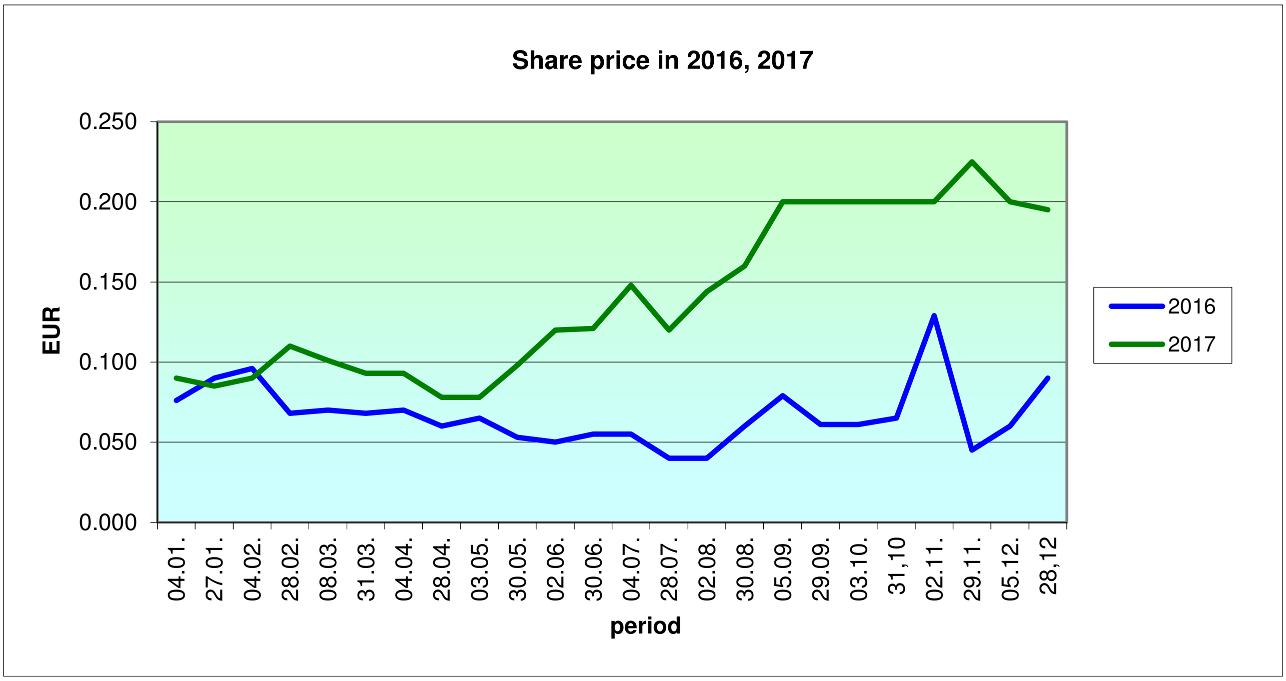
| | |
|---|---|
| Company name | Ditton pievadķēžu rūpnīca |
| Legal status | Joint Stock Company |
| Registration number | 40003030187 |
| Registration in Register of Enterprises | Rīga, 03.10.1991 |
| Registration in Commercial Register Office | Rīga, 29.08.2003. |
| NACE code | 28.15 Manufacture of bearings, gears, gearing and driving elements |
| Legal address | Višķu St. 17, Daugavpils, LV-5410, Latvia |
| Fixed capital | 10 360 000 EUR |
| Number of Public bearer shares | 7 400 000 |
| Nominal value of one share | 1.40 EUR |
| Chief Accountant | Jūlija Lavrecka, p.c.010891-10200 |
| Reporting year | 01.01.2017 – 31.12.2017 |
| Independent auditors and their address | Potapoviča and Andersone Ltd.<br>Reg. No. 40003612562<br>Ūdens St. 12-45, Rīga, LV-1007<br>License No.99<br><br>Sworn auditor of the Republic of Latvia<br>Kristīne Potapoviča |

Persons in charge for drawing up of the financial report:

Mr. Boriss Matvejevs, phone +371 65402333, e-mail dpr@dpr.lv
Ms. Nataļja Redzoba, phone +371 65402333, e-mail dpr@dpr.lv

# INFORMATION ON SHARES AND SHAREHOLDERS

## SHARE PRICE DEVELOPMENT




The paid in capital of the company amounts to EUR 10,360,000 split into 7 400 000 public bearer shares with nominal value of each share EUR 1.40. Each share is entitled to one vote, to one per share dividend and to one liquidation quota of the total number of dividends or liquidation quota, which is equal to the amount of shares of a given category. As Company`s shares are financial instruments (or transferable securities), their circulation and emissions is regulated by the Commercial Law, the Financial Instruments Market Law of the Republic of Latvia and by the provisions of the regulator of the financial instruments market.

## COMPANY SHAREHOLDERS (OVER 5%) *

| NAME | Ownership interest, % |
|---|---|
| Vladislavs Drīksne | 19,92 |
| MAX Invest Holding Ltd | 13,63 |
| Maleks S Ltd | 14,22 |
| DVINSK MNG Ltd | 9,46 |

** Note: 1) The Company does not keep any Share Register. Information presented is based on the lists of shareholders of the JSC Ditton pievadķēžu rūpnīca as at 07.11.2017 Nasdaq CSD has prepared this list for shareholders` meeting due to the Commercial Law of the Republic of Latvia and the Financial Instruments Market Law, taking into account the shareholders' notifications on acquisition and disposal significant holding in the Issuer's equity in accordance with the section 61 of the Financial Instruments Market Law.*

*2) As at 31 December 2017, the Company has no information at its disposal on distribution of stocks (20%) among heirs of E. Zavadskis and their records in financial instruments accounts pursuant to the section 125 of the Financial Instruments Market Law.*

Under the subsections $56^1$ (1) (2, 3, 4, 5, 6, 7, 8, 9, 10 and 11) of the Financial Instruments Market Law on Additional Information to be Included in the Annual Report, the Management Board has no additional information at its disposal on any additional information.

# COMPANY BACKGROUND

As a result of privatisation, the State Daugavpils Driving Chain Factory became the joint-stock company Daugavpils pievadķēžu rūpnīca due to the order of the Cabinet No.375-r dated 09 August 1994 and the resolution of the Board of the state joint-stock company Privatization agency dated 2 March 1995 (the report No.25), having transformed the state company into a joint-stock company.

The Company has received the status of a public joint-stock company after its registration on 30 August 1995 under the No. 000303018 in the Enterprise Register.

On 8 January 2002, the JSC Daugavpils pievadķēžu rūpnīca was renamed into JSC Ditton pievadķēžu rūpnīca receiving new registration No. 40003030187.

On 29 August 2003, the JSC Ditton pievadķēžu rūpnīca was included into the Commercial Register (under the unified registration No. 40003030187).

On 23 January 2015, there have been carried out denomination of the fixed capital of the Company pursuant to the Law on the Procedure for Introduction of Euro of the Republic of Latvia.

Being the successor of rights and obligations of the State Driving Chain Factory due to conditions of privatization, the Company acts according to the Articles of Association.

Some types of activities of the Company:

- manufacture of parts and accessories for motor vehicles;
- repair of fabricated metal products, machinery and equipment;
- installation of industrial machinery and equipment;
- sale of motor vehicle parts and accessories;
- sale, maintenance and repair of motorcycles, related parts and accessories;
- manufacture of structural metal products;
- manufacture of tanks, reservoirs and containers of metal;
- forging, pressing, stamping and roll-forming of metal; powder metallurgy;
- treatment and coating of metals; machining;
- manufacture of other fabricated metal products;
- warehousing and storage;
- buying and selling of own real estate;
- rental and operating of own or leased real estate;
- real estate activities on a fee or contract basis;
- combined facilities support activities;
- etc.

# INFORMATION ON THE MANAGEMENT BOARD AND COUNCIL MEMBERS

## THE MANAGEMENT BOARD

Chairman of the Management Board
Rolands Zarāns, elected 15.01.2014
Member of the Management Board
Nataļja Redzoba, elected 29.08.2003

**Information on shares owned by Members of the Management Board**

| Members of the Management Board | Share ownership * | |
|---|---|---|
| | Quantity | % |
| Rolands Zarāns, elected 15.01.2014 | no shares | - |
| Nataļja Redzoba, elected 29.08.2003 | no shares | - |

## THE COUNCIL

Chairman of the Council
Boriss Matvejevs, elected 05.05.2005
Deputy Chairman of the Council
Georgijs Sorokins, elected 06.11.2000
Members of the Council
Anželina Titkova, elected 14.08.2009
Genādijs Zavadskis, elected 15.02.2017
Vadims Kazačonoks, elected 15.02.2017

**Information on shares owned by Members of the Council**

| Members of the Council | Share ownership * | |
|---|---|---|
| | Quantity of shares | % |
| Boriss Matvejevs | no shares | - |
| Georgijs Sorokins | 5 678 | 0,08 |
| Anželina Titkova | no shares | - |
| Genādijs Zavadskis | no shares | - |
| Vadims Kazačonoks | no shares | - |

For more detailed information on professional background of members of the Management Board and of the Council please refer to our website: www.dpr.lv.

* as at 07.11.2017

# REPORT
# ON CORPORATE GOVERNANCE

§ 1

By arranging corporate governance of the Issuer, the Management Board and the Council follow Corporate Governance Principles, which have been approved by the JSC NASDAQ Rīga (formerly known as JSC NASDAQ OMX Rīga) and entered into force on 1 June 2010.

Information about application of the above-mentioned Principles regarding shareholders` responsibility is presented to shareholders on the annual general meeting, when the annual report is approved. The shareholders may familiarize themselves with information comprised by Corporate Governance Principles on the website of NASDAQ Rīga http://www.nasdaqbaltic.com/files/riga/corp_gov_May_2010_final_EN.pdf or by submitting an appropriate written request to the Issuer.

Information about the order, procedures, restrictions, exceptions and practice of application of Corporate Governance Principles in 2017 has been reflected in the annex to this report "Statement on corporate governance principles". Shareholders may review the information included into this annex in the appropriate section of the Issuer on the website of NASDAQ Rīga, in The Central Storage of Regulated Information system or on Issuer`s website in the internet.

§ 2

System of internal control is implemented in compliance with Corporate Governance Principles, including the internal audit carried out based on the Financial Instruments Market Law and Articles of Association of the Issuer. The Council's report on the internal revision regarding procedures on control and management of risks while compiling of the annual report for 2017 is presented to the annual general meeting of shareholders and enclosed in its materials.

In fact, the Issuer has developed a multistage system of compiling of the annual report, control and risk management.

- 1st stage: compiling of the annual report and internal control in subdivisions of the Issuer;
- 2nd stage: examining and approval of the annual report by the Management Board of the Issuer;
- 3rd stage: auditing of the annual report by an independent sworn auditor according to the Law On the Annual Financial Statements and Consolidated Financial Statements, Law on Accounting, Commercial Law and Financial Instrument Market Law;
- 4th stage: review of the annual report by the Issuer`s Council and reporting on activities of the Management Board and the Issuer in general, what is reflected in this report.
- 5th stage: review of the annual report, the effectiveness of internal monitoring and risk management, as well as of the independence of the sworn auditors and rectification of deficiencies what is implemented by the Audit Committee of the Company according to Financial Instruments Market Law, Regulation (EU) No. 537/2014 of the European Parliament and of the Council and Audit Committee Regulation of the Company, by reporting to shareholders' meeting;
- 6th stage: approving of the annual report in general shareholders` meeting of the Issuer.

It is obvious that activities of the institutions mentioned in stages 3, 4, 5 and 6 are independent from the Management Board of the Issuer and ensure accuracy of the annual report and independency.

§ 3

Under provisions of sections 56.[1] and 56.[2] of the Financial Instruments Market Law the Issuer provides additional information on following:

The following shareholders have a significant holding:
- Vladislavs Drīksne – 19,92%
- MAX Invest Holding Ltd. – 13,63%
- Maleks S Ltd. – 14,22%
- DVINSK MNG Ltd.– 9,46%

*Note:* *1) The Company does not keep any Share Register. Information presented is based on the lists of shareholders of the JSC Ditton pievadķēžu rūpnīca as at 07.11.2017 Nasdaq CSD has prepared this list for shareholders` meeting due to the Commercial Law of the Republic of Latvia and the Financial Instruments Market Law, taking into account the shareholders' notifications on acquisition and disposal significant holding in the Issuer's equity in accordance with the section 61 of the Financial Instruments Market Law.*
***2)*** *As at 31 December 2017, the Company has no information at its disposal on distribution of stocks (20%) among heirs of E. Zavadskis and their records in financial instruments accounts pursuant to the section 125 of the Financial Instruments Market Law.*

The Issuer has no shareholders with specific control rights, neither restrictions to the shareholders' voting rights arising from their shares.

Issuer`s order and procedures for amendments to founding documents (the Articles of Association), change of the composition of the Management Board and of the Council, such as rotation and/or recall, are determined by and applied pursuant to the Commercial Law, Civil Law, Labour Law, Law on the Enterprise Register of the Republic of Latvia, Law on Legal Force of Documents, Declaration on objectives and mission of the activity and development of JSC Ditton pievadķēžu rūpnīca and evaluation of these processes, Regulations on the convening and course of shareholders' meetings and other legal acts related to these procedures, as well as due to resolutions of shareholders` meetings.

The Commercial Law, the Articles of Association of the Issuer and Regulations of the Management Board stipulate rights of members of the Management Board. However, Management Board members have not been granted any additional powers, such as to issue or redeem shares.

§ 4

Governing bodies of the Issuer are:
- shareholders` meeting;
- Council of the Issuer;
- Management Board of the Issuer.

Each institution has its own competence (powers), rights and obligations, which are determined by laws of the Republic of Latvia, Corporate Governance Principles, the Articles of Association and internal documents of the Issuer, including Regulations of the Management Board and of the Council and resolutions of shareholder`s meetings. Institutions are independent.

Independence of shareholders' resolution is ensured pursuant to provisions of the Commercial Law (sections 268, 273-286), Financial Instrument Market Law (sections 54, 54.[1] - 54.[5]), Corporate Governance Principles, Articles of Association of the Issuer, Declaration on objectives and mission of the activity and development of the JSC Ditton pievadķēžu rūpnīca and evaluation of these processes, Regulations on the convening and course of shareholders' meetings and other legal acts and internal documents of the Issuer.

Under Commercial Law, Financial Instruments Market Law, Articles of Association, Declaration on objectives and mission of the activity and development of the JSC Ditton pievadķēžu rūpnīca and evaluation of these processes, Regulations of the Council and of the Management Board and other statutory acts and Issuer's internal documents, Council and Management Board members are independent in exercising their duties and report to shareholders due to provisions of legal acts.

Procedures of nominating and registration of the Council and Management Board members candidates, voting for the Council and Management Board members candidates, as well as election of Council and Board members and their registration in the Enterprise Register of the Republic of Latvia the Issuer organizes and puts into effect pursuant to the provisions of the Commercial Law (sections 268, 284, 292, 296, 305), Financial Instruments Market Law (sections 54, $54.^2$, $54.^6$), as well as provisions of the Issuer's Regulations on the convening and course of shareholders' meetings and Regulations of the Council and of the Management Board. The internal documents of the Issuer are available on the Issuer's website www.dpr.lv.

In January 2017, by the resolution of Council the mandate of the Board member which was expired according to Commercial Law (sections 292 and 305) and Articles of the Association of the Company (sections 6.3.9. and 6.4.2. )was extended. In February 2017, in view of expiry of the mandates and leaving the positon new members of the Council of the Company were elected by the resolution of the extraordinary shareholder`s meeting based on Commercial Law (sections 268 and 296) and Articles of the Association of the Company (sections 6.2.11., 6.3.2. and 6.3.5.).

Members of the Council and of the Management Board are specified on page 6 of the current annual report and on the Issuer's website www.dpr.lv.

Chairman of the Management Board
of the JSC Ditton pievadķēžu rūpnīca
24 April 2018

Rolands Zarāns

# COUNCIL REPORT
## to the annual report for the year 2017

Issued in conformity with the Commercial Law and the Articles of Association of the Company
Approved by Council resolution of the JSC Ditton pievadķēžu rūpnīca
dated 24.04.2018, Protocol No.211

The Council of the JSC Ditton pievadķēžu rūpnīca declares that the report of the Management Board of the Company to the regular shareholders' meeting and annual report for year 2017 truly reflects the commercial activity results and the financial position of the Company.

During the reporting period the Management Board was in charge of the production and operation management of the Company and represented the Company based on the Law of the Republic of Latvia, Articles of Association of the Company, Declaration on objectives and mission of the activity and development of the JSC Ditton pievadķēžu rūpnīca and evaluation of these processes, resolutions of shareholders` meeting and Council recommendations.

The shareholders as well as the Council members have not expressed or submitted any claims against the Management Board and its individual members. The Company has no information at its disposal about any violation of the principle of independence of the Management Board members.

On 7 July 2017, the ordinary meeting of shareholders of the Company, when approving the Annual report for the 2016, assessed operations of the Management Board in the previous period as positive and corresponding to aims and mission of the Company, and current market situation.

The indices of the closed year 2017 reveal the actual position of the Company and global economic circumstances. Causes, circumstances and obstacles that influenced these results are disclosed in the report of the Management Board.

As representative of shareholders, the Council of the Company expresses its solidarity with conclusions of the Management Report and shareholders, as well as with their assessment of the global market and situation on its sectors. The Council considers that comprehensive and objective assessment of the Company and market situation will boost the business plan of the Company and increase economic and production indices.

Under the Articles of Association of the Company and Law of the Republic of Latvia, the Council of the Company was representing interests of shareholders in between shareholders` meetings and supervising operations of the Management Board according to global economic conditions in the reporting period.

Altogether, there have been held twelve meetings of the Council during the reporting period. In four of the joint meetings of the Council and the Management Board financial statements of the Company for 12 months of 2016 and interim financial reports for 3, 6, and 9 months of the year 2017 have been reviewed and approved.

In addition, the following issues have been dealt with and resolved at Council meetings:
- reviewing of the Annual report for the year 2016 and approval of the Council report;
- reviewing of draft resolutions on the issues of the agenda of the ordinary shareholders` meeting convened (on 7 July 2017);
- extension of the mandates of the Council member N. Redzoba, which were to expire;
- reviewing of draft resolutions on the issues of the agendas of the extraordinary shareholders` meetings convened (on 15 February 2017 and on 10 November 2017);

- election of the Chairman and the Deputy Chairman of the Council due to re-election of Company`s Council;
- approval of Company`s investments for the purchase of industrial machinery;
- some other issues related to the activity of the Company and stipulated by the Articles of Association of the Company and the Law of the Republic of Latvia.

Apart from matters mentioned above, there have been six Council meetings as the Audit Committee of the Company within the limits of competences and powers of the Audit Committee. The report on these activities of the Council shall be included into Audit Committee report to the ordinary shareholder`s meeting, were the Annual report for the year 2017 shall be approved.

On 07.07.2017, the ordinary shareholders' meeting assessed operations of the Council as positive and corresponding to aims and mission of the Company.

Herewith the Council of the Company draws shareholders attention to the significant events presented below.

In the reports of previous years 2012 - 2016 the Council, based on expert opinion, informed the shareholders about objectivity of the annual report and their compliance with the actual Company`s position, as well as about market situation and Company`s prospects, as the Company is not isolated, but is a part of the global commercial system. That is why it depends on the indices of those states where the Company is represented on the market due to its geographical location, logistics and actual presence.

Therewith the actual market sales figures of the Company in 2017 rather correspond to predictions of the Council announced before in respect of sales volumes of production and services of the Company. Moreover, the Company retained its position in the global market, as well as partners, contracts and prospects of increasing production volumes.

The Council of the Company assesses its forecasts in view of global market outlooks and demand for Company's goods within the range from "slightly negative" to "moderately positive" by some geographical markets and categories of goods. Realization of projections depends not only upon the Company, but also on the future dynamics of the world economy development, as well as on the dynamics of development or termination of the crisis phenomena in relations with CIS countries. Consequently, it cannot be ruled out that due to negative development of these factors the Company's production volumes may decrease or remain at the current level.

Previously the Council has drawn the attention of the shareholders to the program of the Management Board, which is targeting the improvement of economic and financial indicators by optimizing costs and incomes of the Company, and by focusing on provision of high quality and high added value products and services. Moreover, the Council is highlighting the positive development of the Industrial and Technology Park of the Company on its premises.

The Council believes that this focus area is attractive and promising. The Company`s indicators, as well as the profit, achieved certify the prospects of this program.

Taking into account the performance indices of the Company in 2016 and especially in 2017, the Council agrees with the Management on usefulness of the partly implemented programs on improvement of operating activities, including optimization of costs, manufacturing and technology-related processes, equipment modernisation and introduction of energy- and resource-saving technologies by its updating and extension till the year 2021.

In view of the information mentioned above and the situation in the Company, the Council considers it appropriate to recommend to cover the loss of previous periods against the profit of 2017, as well as to invite the shareholders` support for this proposal. Taking into account the economic indicators, the Council deems it appropriate to advise the Management Board to respond more quickly to market changes (especially pricing), to update the Company`s plans and program without hesitation, as well as to optimize operational costs.

Chairman of the Council
24 April 2018

Boriss Matvejevs

## Information on the results of Company`s activities in 2017

The net-turnover in 12 months of 2017 reached € 5,637 thousand, being by € 1 361 thousand lower than the index in 12 months of 2016.

The export of the core products and services to Eastern and Western markets amounted to 73 per cent (45% eastwards and 28% westwards), 27% of products and services were sold on Latvian market.

The Company closed the year of 2017 with a pre-tax profit of € 945 thousand.

The average number of employees of JSC DITTON pievadķēžu rūpnīca in 2017 was 165 employees.

In 2017 the average salary of The Company`s employees amounted to € 550, that corresponds to the average salary in 2016 (€ 553)

The results of Company's activities and Annual report including financial statements (with appendixes), this Management Report and Report on corporate governance (with appendixes) were approved by the Company's Management Board (Management Board meeting Protocol No. 01/2018 dated 24 April 2018).

## Significant events. Market tendencies and development of the company. Risks.

Overall market tendencies.
After having analysed the Company's operating conditions and performance indices, as well as market situation in 2017, the Company's management considers the information given in the management report to the annual statements for the year 2015 and 2016 is fully up to date and relevant for the reporting period. It states that there were not observed any necessary growth tendencies in manufacturing industry, and namely in the field of metalworking and mechanical engineering, where the Company operates. This is reflected by performance indices of Company for the reporting period.

The analysis of the previous periods for the year 2015 and 2016 enclosed the following thesis, which are topical at present too. According to indices of the commodity output under the trade mark of JSC Ditton pievadķēžu rūpnīca, the sales market of the final consumers can be structurally split into two main shares as follows:

- Western market, i. e. mainly European country market, and
- Eastern market, i. e. market of the Russian Federation, Customs Union, CIS, Ukraine, as well as of the Asian countries.

The Company is integrated into production and economic systems of those countries, which belong to sales market shares of the Company mentioned above, regardless of procedures and systems applied for product promotion on these markets. Thus, all the trends, factors, risks, crises and other circumstances on these markets have direct influence on the Company, its operations, as well as the income gained from its activities.

The necessity to ensure Company's operation obliges the Company's management to undertake all of the measures in order to retain both market shares, such action as:

- operating due to conditions and factors of specific market shares,
- reaching compromises with partners, also unfavourable ones,
- retaining all the market shares, even those with temporary adverse factors or crisis phenomena.

Whereas the waiver for partnership with someone is possible only under condition, when production volumes are replaced by ones of the same level on another market share or by collaboration with other partners (more detailed analysis thereof is given in the management report to the annual statements for 2016 as well).

Western market share

After having analysed the Company's operating conditions and performance indices, as well as market situation in 2017, the Company's management considers the information given in the management report to the annual statements for the year 2015 and 2016 is fully up to date and relevant for the reporting period. There are no necessary growth tendencies in manufacturing industry, and namely in the field of metalworking and mechanical engineering, where the Company is operating, what is reflected by performance indices of Company for the reporting period.

The sales results of the Company`s goods show that there are no growth trends in the areas, where the Company's goods are utilised. The Management Board already drew attention to these circumstances in previous Management reports by giving relatively positive forecast regarding its operation indices. These forecasts, assessments of the market shares, as well as information on adverse factors, which had an impact on Company's activity, retain relevance even today.

According to these statistics, there is no reason to expect that sales volumes will significantly increase in this market share. Such increase is possible only in the result of joint projects with companies from countries in areas and technologies where the Company is not represented yet.

Eastern market share

The Management gave a detailed analysis of the situation in this market share in the annual report of the Company for 2015 and 2016, including the examination of stages and processes arisen there.

The Management Board pointed out that one of the disadvantages was instability of the exchange rate of the rouble being as a value in trading operations in the Customs Union. It was caused by transnational prohibition process, instability in oil values and crisis phenomena caused by these adverse factors in economies of the Customs Union and the CIS.

Therewith the Management marked out its hopes for improvements regarding this challenge in 2016 such as stabilisation of the rouble exchange rate against the euro within predictable and comprehensive "gap", what is already proven by the outcomes of 2016 and 2017 resulting improvement of Company's indices. Therefore, the positive forecast of the Management regarding this market share came true.

Other adverse factors stressed by the Management Board in the Company's Annual reports for 2015 and 2016, such as mutual sanctions policy are still ongoing and clearly expressed attraction of Chinese manufacturers, possible risks of loss, first of all, of customers and decreased demand for Company's goods, retain relevant and significant as well. Therefore, the Management Board finds it of utmost importance to focus shareholders` attention on these obstacles.

Besides, the state policy, such as Russian Federation, due to sanctions on this market share, is stipulating the internal enterprises to launch manufacturing of substitute goods for products of JSC Ditton pievadķēžu rūpnīca. Under such circumstances, sales of counterfeit products under Company's trademark are increasing. It shows the high quality of Company's goods and constant demand for these products, as well as Company's loss because of fake promotion by fictitious suppliers on this market share. Unfortunately, the Management forecast regarding this part came true and stays up to date.

Another result of the economic political relations between EU and Russian Federation mentioned above, are additional import duties for the metal produced in the Russian Federation (18 -30 per cent), which the Management Board noted in its reports previously. Unfortunately, these duties on certain types of metal products originated in the Russian Federation remain in force in the common backdrop of rising prices. Taking into account that the Company has used customary for the production metal goods from Russian because of their cost-efficiency, flexible delivery and payment conditions, this factor caused price increase of products in all market shares and reduction in sales. Similar European metal products are more expensive. Therefore, the substitution of Russian metal products with European is not cost effective but causes additional price growth. It is expected that the effect of this factor will slow down against the forthcoming backdrop of rising prices of European and Asian driving chain manufacturers.

Consequently, the risks and loss on this market share depend mainly not on the Company, but rather on circumstances, which the Company cannot influence and eliminate by reasonable and available means.

Along with this, the Company considers it necessary to continue operating in these market shares due to investments done into this market, gained contacts, visibility level of the trademark and image of a high-quality manufacturer. In addition, certain optimism arises by increasing customers' requirements for the price-quality ratio, ensuring the Company an obvious competitive advantage.

<u>Optimisation of Company`s manufacturing processes and costs management</u>
During the years 2015-2017 the Company was implementing a loss minimization program due to the optimization of the internal structure and due to use of infrastructural, intellectual and human resources. The Company sees its growth potential in generation of technology-intensive variety of high added value products, as well as in promotion of services and works in addition to the main production process.

Development plan for 2015-2017, endorsed by the shareholders' meeting in July 2015 and given to public, is in progress as the core stone for actions of Company's Management. By following the plan, the Management Board operates in the sequential way much more structurally and smart, as well as optimizes division of involved resources for improving financial standing of the Company. Thus way, dynamic of the Company's incomes towards expenses is significantly improving. The above-mentioned allowed reaching positive indices. In general, indices of 2017 are significantly better compared to the indices of 2016 and 2015. The year 2017 was closed with a profit, due to this the Company's development forecast is merely positive by now. The Company foresees to develop and specify the development forecast of the Company for the time spread 2019-2020 with regard to program development and performance results of the Company.

<u>Development of the Industrial and Technology Park.</u>
The Company is promoting the program on development of the Industrial and Technology Park on its premises as its commercial services. Within this program, the Company carried out modernisation of its production premises by using the aid of the European Union Funds (the project "Construction of industry premises in the free industrial area of JSC DITTON Driving Chain Factory"). Thereof effective saving of resources related to maintenance of production facilities was achieved. For example, according to calculations done the natural gas consumption for heat supply decreased by 35% in result of the stage I of modernisation (till the year 2011) and by next 30% in result of the stage II of modernisation (till the year 2015). Furthermore, production space was created with appropriate infrastructure for production needs for commercial rental offer. Moreover, in 2017, the territory of the Company together with the Industrial and Technology Park was included into Latgale special economic zone that shall boost the program implementation.

According to analysis of Company`s operations based on results in 2016 and in 2017, the Company`s profit from the running the Industrial and Technology Park takes the significant place in market shares of Company`s goods and services.

Risks of the Company
The Company's activity is subject to a variety of financial risks: foreign currency risk, interest rate risk, credit risk and liquidity risk.

**Foreign currency risk**
Foreign currency risk is the risk that the Company might have financial loss due to unfavorable fluctuations in exchange rates. This risk arises when financial assets in foreign currency do not match with financial liabilities in the same currency; herewith the Company has open currency positions.

**Interest rate risk**
Interest rate risk is the risk that the Company might have financial loss due to unfavorable fluctuations in interest rates. The Company experiences such interest rate risk of long- and short-term loans from credit institutions due to variable fixed rates, or when fixed interest period is less than the planned time of the loan repayment, or when credit interest is based on variables, or due to terms of the Loan agreement (refer to Appendix 17). The Company does not have any other choice and does not use any tools to mitigate the interest rate risk other than to fulfil loan-borrowing conditions in full and to cooperate with credit institutions.

**Credit risk**
Credit risk is the risk that the Company might have financial loss due to business partner who failed to comply with his obligations towards the Company. Cash, trade receivables and advance payments are the main cause of credit risk.

*Cash*
Credit risk related to cash at banks is managed by balancing the financial asset allocation in order to maintain the possibility of choosing the best offers and minimizing the loss of financial resources at the same time.

The Company oversees, assesses and mitigates this risk by appropriate work with Company's partners, for example, limiting or suspending the ongoing and future transactions with unfavorable partners, when the Company receives information about partners` possible problems with meeting their obligations.

**Liquidity risk**
Liquidity risk is the risk that the Company may be unable to meet its obligations timely and in full. Liquidity risk appears, when repayment terms of financial assets and liabilities do not match. The aim of the Company's liquidity risk management is to maintain an adequate amount of cash and cash equivalents, and ensure appropriate sufficient funding through credit lines issued by the banks (refer to the Appendix 17) so that the Company fulfils its obligations within the set time limits. The Company regularly monitors financial assets and liabilities mismatches, as well as stability of funding sources for long-term investments. See also chapter Going concern disclosure in appendix Accounting principles and valuation methods.

In the opinion of the Company's management, the Company will have sufficient cash resources to secure its liquidity.

# STATEMENT ABOUT MANAGEMENT LIABILITY

According to the information at our disposal, these financial statements for 12 months of the year 2017 have been prepared in compliance with the existing legislative requirements, gives a true and fair view of the assets, liabilities, financial standing and profits of the Company. The Management report contains truthful information.

Chairman of the Management Board
of JSC DITTON pievadķēžu rūpnīca
24 April 2018

Rolands Zarāns

# INCOME STATEMENT
# FOR THE YEAR 2017

| | Appendix | 2017 EUR | 2016 EUR |
|---|---|---|---|
| Net turnover | 1 | 5 636 931 | 6 998 006 |
| Production costs of goods sold, purchase costs of goods sold or services rendered | 2 | (4 222 104) | (6 910 193) |
| **Gross profit** | | **1 414 827** | **87 813** |
| Sales costs | 3 | (13 329) | (25 766) |
| Administrative expenses | 4 | (654 207) | (625 387) |
| Other income from operating activities | 5 | 690 084 | 916 391 |
| Other costs of operating activities | 6 | (376 064) | (211 948) |
| Interest payment and similar expenses | 7 | (116 184) | (123 182) |
| • *from other persons* | | *(116 184)* | *(123 182)* |
| **Profit before corporate income tax** | | **945 127** | **17 921** |
| Corporate income tax for the reporting year | 8 | - | - |
| **Profit for the reporting year** | | **945 127** | **17 921** |
| **Profit/diluted profit per share** | | **0,128** | **0,002** |

Appendixes from page 23 till 40 are integral parts of these financial statements.

According to the Management Board meeting Protocol the financial statements has been signed on behalf of the Company on 24 April 2018 by

Rolands Zarāns
Chairman of the Management Board

(signature)

Jūlija Lavrecka
Chief Accountant

(signature)

# BALANCE SHEET AS AT 31.12.2017

| ASSETS | Appendix | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|---|
| **Long-term investments** | | | |
| **Intangible investments** | | | |
| Concessions, patents, licenses, trademarks and similar rights | 9 | 16 110 | 21 185 |
| **Total intangible investments** | | **16 110** | **21 185** |
| **Fixed assets** | | | |
| Immovable property: | | | |
| Land | | 1 853 982 | 1 853 982 |
| Buildings and structures and permanent crop | | 1 403 347 | 1 487 884 |
| Investment properties – land | | 88 628 | 88 628 |
| Investment properties - buildings | | 994 011 | 1 051 915 |
| Technological equipment and devices | | 3 075 042 | 738 622 |
| Other fixed assets and inventory | | 17 240 | 24 935 |
| Costs of the establishment of fixed assets and unfinished building objects | | 12 649 | 12 649 |
| **Total fixed assets** | 10 | **7 444 899** | **5 258 615** |
| **Long-term financial investments** | | | |
| Other securities and investments | 11 | 67 160 | 67 160 |
| **Total long-term financial investments** | | **67 160** | **67 160** |
| **TOTAL LONG-TERM INVESTMENTS** | | **7 528 169** | **5 346 960** |
| **Current assets** | | | |
| **Inventories** | | | |
| Raw materials, consumables and supplies | | 526 011 | 560 183 |
| Work in progress | | 164 201 | 204 631 |
| Finished products and goods for sale | 12 | 213 112 | 228 977 |
| Goods en route | | 56 981 | - |
| Advance payments for inventories | 13 | 19 811 | 1 252 637 |
| **Total inventories** | | **980 116** | **2 246 428** |
| **Debtors** | | | |
| Trade receivables | 14 | 791 325 | 1 349 896 |
| Other debtors | 15 | 281 035 | 8 126 |
| Next period costs | | - | - |
| **Total debtors** | | **1 072 360** | **1 358 022** |
| **Cash** | | **1 378** | **6 987** |
| **TOTAL CURRENT ASSETS** | | **2 053 854** | **3 611 437** |
| **TOTAL ASSETS** | | **9 582 023** | **8 958 397** |

Appendixes from page 23 till 40 are integral parts of these financial statements.
According to the Management Board meeting Protocol the financial statements has been signed on behalf of the Company on 24 April 2018 by

Rolands Zarāns
Chairman of the Management Board ____________ (signature)

Jūlija Lavrecka
Chief Accountant ____________ (signature)

# BALANCE SHEET AS AT 31.12.2017

| LIABILITIES | Appendix | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|---|
| **Equity** | | | |
| Stock capital | 16 | 10 360 000 | 10 360 000 |
| Reserves: | | | |
| Other reserves | | 169 251 | 169 251 |
| Uncovered losses brought forward from the previous years | | (9 889 370) | (9 907 291) |
| Profit of the reporting year | | 945 127 | 17 921 |
| **Total equity** | | **1 585 008** | **639 881** |
| **Creditors** | | | |
| **Long-term creditors:** | | | |
| Loans from credit institutions | 17 | 4 533 505 | 1 858 390 |
| Next period income | 21 | 978 274 | 1 038 793 |
| **Total long-term creditors** | | **5 511 779** | **2 897 183** |
| **Short-terms creditors:** | | | |
| Loans from credit institutions | 17 | 883 198 | 162 134 |
| Other loans | 18 | 255 328 | 273 912 |
| Prepayments received from purchasers | | 20 720 | 63 387 |
| Accounts payable to suppliers and contractors | | 529 780 | 4 226 159 |
| Taxes and State mandatory social insurance payments | 19 | 463 598 | 384 158 |
| Other creditors | 20 | 138 540 | 132 567 |
| Deferred income | 21 | 60 520 | 60 520 |
| Accrued liabilites | 22 | 133 552 | 118 496 |
| **Total short-term creditors** | | **2 485 240** | **5 421 333** |
| **Total creditors** | | **7 997 015** | **8 318 516** |
| **TOTAL LIABILITIES** | | **9 582 023** | **8 958 397** |

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(signature)

Jūlija Lavrecka
Chief Accountant
(signature)

# CASH FLOW STATEMENT FOR THE YEAR 2017

| | Appendix | 2017 EUR | 2016 EUR |
|---|---|---|---|
| **I. Cash flows from operating activities** | | | |
| 1. Profit or loss before enterprise income tax | | 945 127 | 17 921 |
| *Adjustments to:* | | | |
| Depreciation of fixed assets | 10 | 255 404 | 231 223 |
| Depreciation of intangible assets | 9 | 5 075 | 3 609 |
| Other income (Investment and Development Agency of Latvia) | 5 | (60 520) | (62 628) |
| Interest payments and similar expenses | 7 | 116 184 | 123 182 |
| Income from sales of fixed assets | 10 | (300) | - |
| 2. Profit or loss before adjustments to fixed assets and short-term creditors | | 1 260 970 | 313 307 |
| *Adjustments to:* | | | |
| Increase or decrease in accounts receivables | | 285 662 | (604 004) |
| Increase or decrease in inventories | | 1 266 312 | 88 592 |
| Increase or decrease in accounts payable to suppliers, contractors and other creditors | | (3 638 573) | 1 255 389 |
| 3. Gross cash flows from operating activities | | (825 629) | 1 053 284 |
| **Net cash flows used in operating activities** | | (825 629) | 1 053 284 |
| **II. Cash flows from investing activities** | | | |
| Purchases of fixed assets and intangible investments | | (2 441 691) | (836 749) |
| Proceeds from sale of fixed assets and intangible investments | | 300 | 37 019 |
| Interest received | | - | 2 568 |
| **Net cash flows used in investing activities** | | (2 441 391) | (797 162) |
| **III. Cash flows from financing activities** | | | |
| Net change in borrowings | | 3 377 595 | (328 394) |
| Interest payments and similar expenses | | (116 184) | - |
| **Net cash flows used in financing activities** | | 3 261 411 | (328 394) |
| **Exchange differences** | | | |
| **Net decrease/increase in cash and cash equivalents** | | **(5 609)** | **(72 272)** |
| **Cash and cash equivalents at the beginning of the reporting year** | | **6 987** | **79 259** |
| **Cash and cash equivalents at the end of fiscal period** | | **1 378** | **6 987** |

Appendixes from page 23 till 40 are integral parts of these financial statements.

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Rolands Zarāns
Chairman of the Management Board ____________
(signature)

Jūlija Lavrecka
Chief Accountant ____________
(signature)

# STATEMENT OF CHANGES IN EQUITY FOR THE YEAR 2017

| | Equity capital | Reserves | Uncovered losses | Profit or loss of the reporting year | TOTAL |
|---|---|---|---|---|---|
| | EUR | EUR | EUR | EUR | EUR |
| **At 31 December 2015** | **10 360 000** | **169 251** | **(5 637 327)** | **(4 269 964)** | **621 960** |
| Loss of 2015 including into uncovered losses | - | - | (4 269 964) | 4 269 964 | - |
| Loss of the reporting year | - | - | - | 17 921 | 17 921 |
| **At 31 December 2016** | **10 360 000** | **169 251** | **(9 907 291)** | **17 921** | **639 881** |
| Profit of 2016 allotment | - | - | 17 921 | (17 921) | - |
| Profit of the reporting year | - | - | - | 945 127 | 945 127 |
| **At 31 December 2017** | **10 360 000** | **169 251** | **(9 889 370)** | **945 127** | **1 585 008** |

Appendixes from page 23 till 40 are integral parts of these financial statements.

According to the Management Board meeting Protocol the financial statements has been signed on behalf of the Company on 24 April 2018 by

Rolands Zarāns
Chairman of the Management Board

(signature)

Jūlija Lavrecka
Chief Accountant

(signature)

# APPENDICES TO THE ANNUAL REPORT

## Accounting principles and valuation methods

### *Fundamental principles of the preparation of the financial statements*

The Annual report has been drawn in compliance with the Law on Accounting, Law on the Annual Financial Statements and Consolidated Financial Statements and Regulation No.775 on rules of application of the Law on the Annual Accounts and Consolidated Annual Accounts of the Cabinet of Ministers. Income statement is prepared in accordance with drawing set in the Appendix 3 of the Law on the Annual Financial Statements and Consolidated Financial Statements, e.g. expenses are classified by their function. Under the Section 5 of Law on the Annual Financial Statements and Consolidated Financial Statements, the Company is considered as a medium-sized enterprise. Financial statements of the Company are compiled pursuant to provisions of the Section 9 of the Law on the Annual Financial Statements and Consolidated Financial Statements. When comparing the principles of bookkeeping and methods of evaluation with the annual statements of the previous year they have not changed. In case of benchmark reclassification, which does not affect the results of previous periods and the amount of own assets, the explanations are provided either in the section on the accounting policies of the relevant item or in the relevant appendix of the financial statements. Key information on the Company is presented on page 3 of this annual report.

Items of the annual report are evaluated accordingly to the following accounting concepts:

a) The accounting policies used by the Company are consistent with those used in the previous accounting period
b) Measuring of the items has been carried out with due care, i.e.:
   - Only the profit accruing up to the balance sheet date has been included in the report;
   - All foreseeable risk amounts and losses incurred during the reporting year or in previous years have been taken into account, even though awareness thereof arose in the period between the balance sheet date and the date of signing of the annual report;
   - • All impairment, depreciation and amortisation amounts have been calculated and taken into account, regardless of whether the Company's performance for the reporting year is a profit or loss
c) The revenue and costs relating to the reporting year have been taken into account regardless of payment dates or invoice receipt or issue dates. Expenses have been matched with the revenue in the reporting year
d) The elements of asset and liability items have been measured separately;
e) Operating activities are identified according to their economic content and nature instead of their legal from.

In 2017, the bookkeeping was kept on united bookkeeping accounts, which have been approved on 13 May 1993, detailing the plan of accounts based on key aspect of the Company`s operational activities.

The bookkeeping register based on synthetic accounting is the General ledger, which contains records on transactions from all the accounts. There are various kinds of analytical accounting registers, such as books, cards, lists etc.

The financial statements cover the period 1 January 2017 through 31 December 2017.

### *Going concern disclosure*

These financial statements have been prepared under the going concern assumption. At 31 December 2017, the current liabilities of the Company exceeded its current assets by EUR 431,382. The current liabilities of the reporting period are lower than in the year 2016.

The Company has managed to come to an agreement with some of the creditors .on a deferred payment schedule. The Management of the Company has also submitted a deferred payment schedule offer to it`s other major creditors and is in negotiation with these creditors on the implementation of such options. The Company has a significant amount of overdue debts, which are only paid back within the terms of the oral agreement.

The Managament considers that it will be able to provide adequate funding to liquidity issues:

- by constantly adjusting debt repayment conditions (dates, amounts and write-off options) based on an agreement with the creditors in order to avoid the request to open insolvency proceedings. It is expected that the Company will be able to pay all the past due payables in full within one or two years;
- by reviewing contract terms with the current clients in order to raise sales prices and terminate burdensome contracts;
- by launching new projects in order to tap into new markets, and, thus,to ensure positive cash flow from operating activities;
- by making timely payments to credit institutions in order to avoid a situation in which the credit institution would require immediate and full repayment of the loan.

The Company's Management believes that the current situation is temporary and is taking steps to improve the Company's liquidity. The Management predicts that positive cash flow from operating activities will increase significantly within the next 12 months.

In 2017, the Company and DITTON Chain Ltd. assigned mutual securities for each other: the Company gave guarantee of EUR 4,4 million, DITTON Chain Ltd – EUR 2,3 million in turn. As at 1 January 2018, these guarantees lost their relevance as DITTON Chain Ltd. has met its credit obligations and its guarantee was complete therewith (refer to Appendix 26).

### *Foreign currency revaluation*

Data reflected in this financial report is in the European Monetary Unit - euro (EUR). All the monetary assets and liabilities are converted to euro applying the exchange rate of the European Central Bank on the balance sheet date.

| **31.12.2017** | **31.12.2016** |
|---|---|
| 1 USD = 1,1993 EUR | 1 USD = 1,0541 EUR |
| 1 RUB = 69,392 EUR | 1 RUB = 64,300 EUR |

The income and loss resulted from fluctuation of foreign currency exchange rate was included in the income statement of the appropriate period.

### *Long- and short-term items*

The amounts received, paid or written off which are due later than a year after the reporting period, are included in long-term items. The amounts received, paid or written off during the year are displayed as short-term items.

### *Intangible assets*

Intangible assets are listed at their cost of acquisition, which are depreciated in a straight-line basis. The depreciation period is 5 years. When events or changes in circumstances indicate that the carrying value of intangible assets may not be recoverable, the intangible assets are reviewed for impairment.

Loss from impairment is recognized when the carrying value of intangible assets exceeds its recoverable amount.

### *Fixed assets*

In accordance with the Company's accounting policies the bookkeeping practice of fixed assets comprises accounting of investment assets as well (refer to section "Investment assets").

Fixed assets are carried at their historical cost less accumulated depreciation and impairments. The initial value of fixed assets includes their acquisition cost, including import duties and as well as any other eligible costs regarding the preparation of the assets for their proper operation according to their intended purpose. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

| | **% a year** |
|---|---|
| Land | Depreciation is not to be calculated |
| Buildings and engineering structures | 5 - 10 |
| Technological equipment and devices | 6 - 33 |
| Other fixed assets and inventory | 20 - 70 |

Depreciation is calculated starting with the following month after the asset is put into operation or engaged in commercial activity.

When events or changes in circumstances indicate that the carrying value of tangible assets may not be recoverable, the fixed assets are reviewed for impairment. If there are signs, that the value is not recoverable, and if the carrying values exceeds the estimated recoverable amount, the asset or cash-generating unit are written down to its recoverable value. The recoverable amount is higher than asset`s net selling price 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 an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. The loss from impairment is recorded in profit and loss account.

An asset is de-recognized upon its disposal, or when no future economic benefits can be expected from its use. The gain or loss on de-recognition calculated as the net disposal proceeds, minus the asset's carrying value is recorded in the income statement in the year when the asset is de-recognized.

Tenant improvement allowance is recorded as a fixed asset and depreciated using the straight-line method over the shortest time spread of the useful life of the capital improvements and lease.

### *Investment properties*

Investment properties are recognised and presented based on International Financial Reporting Standards. Investment properties include land, buildings, engineering structures or their parts, which Company holds as an owner in order to gain rent or in anticipation of a future increase in price (value) and not for product manufacturing or provision of services, for administrative purposes or resell in the ordinary course of business. The Company books the investment properties at acquisition cost.
The value of the investment properties embodies the prime value of the constructions in progress, as well as borrowing costs and other directly attributable to funding of the appropriate object during the period of its preparation as a new object for its intended use.

Capitalisation of borrowing costs for investment properties measured at fair value is suspended during periods in which active development of the unfinished constructions is interrupted. The current repair and maintenance costs of the investment property are included into income statement for the period in which they incurred. Land is not subject to depreciation. Buildings recognised as investment properties are depreciated by the straight-line method over their useful life, in order to write off the acquisition value of the building to its estimated residual value at the end of the useful life period by using the following rates set by the Management:

| | **% a year** |
|---|---|
| Buildings and engineering structures | 5 - 10 |

### *Trade and other receivables*

Trade receivables are accounted and reflected in the balance according to original invoiced amount less provisions for doubtful debs. The company creates provisions for unsecured accounts receivable, on the basis of an individual assessment of the accounts receivable. Debts are written off when the retrieval is considered as impossible.

### *Inventories*

Raw materials, consumables and supplies are valued at acquisition cost, plus incidental costs of acquisition, on a strict lower-of-cost-or-market basis. Adequate write-downs have been applied at net selling price due impairment, full or partial outdating of inventories or when production or selling costs of inventories jumped up significantly. Inventories are valued using the FIFO method.

Work in progress is valued at the direct cost of materials used. The cost of finished goods are carried at the cost of manufacture, which includes adequate material and labor costs in addition to direct material and production overheads, e.g., energy, ancillary materials, equipment and maintenance costs, depreciation and general manufacturing costs – service costs related to production.

### *Cash*

Cash and cash equivalents comprise cash at bank. The cash flow statement has been compiled based on indirect method.

### *Accounts payable to suppliers and contractors*

Accounts payable to suppliers are recorder at their nominal value.

### *Loans and borrowings*

Loans and borrowings are initially recognized at cost, being the fair value of the proceeds received plus/net of issue costs associated with the borrowing. After initial recognition, borrowings are subsequently measured at amortized cost. Any difference between proceeds (less issue costs associated with the borrowing) and the redemption value is recognized in the income statement over the period of borrowings.

### *Borrowing costs*

Borrowing costs are expensed in the period they occur and disclosed in the income statement as interest or similar expense.

### *Contingencies*

Contingent liabilities are not recognised in these financial statements, as these liabilities are accepted only when as assumption of an outflow of resources has been confirmed. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognised in this financial report but disclosed until an inflow of economic benefits is probable. Contingent liabilities and assets are revealed when they are of essential matter.

### *Investments in capital of other parties*

Investments in capital of other parties are recorded on the base of the costs method. The cost method is investment accounting method when investments are accounted at its purchase costs. Investor recognizes income only when investor receives from investee distribution of accrued profit resulting after the date of acquisition. In cases when the value of the investment has significantly decreased as a result of conditions which cannot be considered temporary, the accounting value of the investment is decreased to the recoverable value.

### *Revenue*

Revenue is recognised under the assumption of economic benefits, which might flow to the Company, and to the extent, that the revenue can be reliably measured less value added tax and sales-related discounts. Revenue is recognized on an accrual basis. Revenue is recognized at the moment of acquisition when the ownership is transferred to the buyer. Income from interests is accounted on a time spread based on the accrual basis.

### *Expenses*

Expenses are recognised in the period they are associated with irrespective of the date of payment.

### *Accruals for unused vacations*

The amount of accrued liabilities is calculated by multiplying employee's average salary (including social tax) of the reporting year and the number of accrued unused vacation days as at the balance sheet day.

***Provisions***

The provisions are present (legal or constructive) obligations of the Company arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits and amount of which can be reliably estimated.

***State aid***

State aid is not recognized until the Company has obtained a reasonable assurance on meting eligibility rules and receiving of the aid. State aid is noted in a systematic manner in the income statement for the period when Company included costs compensated by the state support into expenses. Therefore, state aid aimed as a long-term investment in the acquisition or establishment is recorded on the balance as deferred income and included in the income statement in a systematic and rational manner in accordance with the useful life of the fixed assets.

***Corporates income tax***

Corporate income tax is corporate income tax calculated for the reporting year. Corporate income tax for the reporting year is calculated by applying the tax rate of 15% to the taxable income of the relevant tax year.

As at 2017, deferred tax assets and liabilities are not assessed due to changes in Law that has changed the deferred tax base.

***Application of estimates and key assumptions***

The Law of the Republic of Latvia requires that when preparing the financial statements, the management of the Company is expected to share estimates and assumptions that affect the reported and off-balance sheet assets and liabilities on the day of preparation, as well as presented income and expenses of the reporting period. Actual results may differ from these estimates.

Critical judgments and key assumptions concerning the future as well as other uncertainties on the balance sheet date in view of the fact that there exists a substantial risk of the material adjustments to assets and liabilities in next financial years are listed as following.

- When assessing accounts receivable and loans, the Company evaluates their retrieval and creates provisions for doubtful accounts receivable and loans, if necessary. After the management of the Company has assessed accounts receivable and loans, it has taken a decision to create additional provisions as of 31 December 2017 (refer to Appendix 14).

- At the end of each reporting year, the Company reviews the useful lives of fixed assets. This assessment and the calculated depreciation may vary.

- The Company evaluates advance payments to assess their recoverability and, if necessary, makes provisions for irrecoverable advances. The management of the Company has reviewed the advances paid and believes that there is no necessity for additional provisions as at 31 December 2017.

### (1) Net turnover

Net turnover is income gained during the year from sale of produced and purchased products of the Company, as well as income from services net of VAT and less discounts.

Breakdown of net turnover by geographical markets:

| | 2017 EUR | 2016 EUR |
|---|---|---|
| **Market** | | |
| Eastern countries | 2 572 149 | 2 665 664 |
| Western countries | 1 558 576 | 1 464 522 |
| Latvia | 1 506 206 | 2 867 820 |
| **TOTAL:** | **5 636 931** | **6 998 006** |

### (2) Production costs of goods sold, purchase costs of goods sold or services rendered

| | 2017 EUR | 2016 EUR |
|---|---|---|
| Material costs | 1 979 519 | 4 518 455 |
| Salary costs for production staff | 673 997 | 724 452 |
| Electricity costs | 498 590 | 616 359 |
| Depreciation of fixed assets* | 181 518 | 155 540 |
| Depreciation of investment property* | 57 904 | 57 904 |
| Current repair expenses | 308 552 | 322 388 |
| State mandatory social insurance payments | 157 969 | 169 604 |
| Material delivery costs | 182 785 | 188 310 |
| Other production costs | 181 2709 | 157 181 |
| **TOTAL:** | **4 222 104** | **6 910 193** |

* Refer to Appendix 10.

### (3) Sales costs

| | 2017 EUR | 2016 EUR |
|---|---|---|
| Advertisement costs | 6 859 | 13 488 |
| Other sales costs | 6 470 | 12 278 |
| **TOTAL:** | **13 329** | **25 766** |

## (4) Administrative expenses

| | 2017 EUR | 2016 EUR |
|---|---|---|
| Administrative staff salaries | 415 546 | 388 200 |
| State mandatory social insurance payments | 96 887 | 90 078 |
| Security expenses | 43 987 | 43 160 |
| Business travel expenses | 23 485 | 25 175 |
| Depreciation and amortisation | 21 057 | 21 388 |
| Profesional fees | 12 925 | 16 546 |
| Other administration costs | 40 320 | 40 840 |
| **TOTAL:** | **654 207** | **625 387** |

## (5) Other income from operating activities

| | 2017 EUR | 2016 EUR |
|---|---|---|
| Decrease in provisions* | 600 636 | 316 630 |
| Assignment of Structural Funds to income | 60 520 | 62 628 |
| Income from growth of exchange rate | 22 889 | 54 650 |
| Net income from sale of fixed assets | 300 | 1 853 |
| Income for expenses of previous periods** | - | 459 275 |
| Other income | 5 739 | 21 355 |
| **TOTAL:** | **690 084** | **916 391** |

** Of which EUR 594 422 (2016: EUR 158 117) are received income from decrease of prior year provisions for doubtful receivables made and EUR 6 214 (2016: EUR 158 513) is decrease in provisions for inventories with low turnover rate due to stock sale.

* In relation to the contract No. L-IZI-14-0003 on implementation of the project "Construction of industry premises in the free industrial area of JSC Ditton pievadķēžu rūpnīca" signed with the Investment and Development Agency of Latvia in 2014 after assessment of the project cost estimate the sum of project costs accepted was lower than planned. This difference for nun-reimbursable expenses was claimed towards the contractor of the project construction works as refund of unreceived funding.

## (6) Other costs of operating activities

| | 2017 EUR | 2016 EUR |
|---|---|---|
| Penalties | 64 348 | 81 744 |
| Property tax | 61 127 | 61 037 |
| Increase in provisions for slow-moving inventories (Appendix 13) | 30 409 | 21 031 |
| Other costs of operating activities | 65 996 | 19 353 |
| Net loss from exchange rate differences | 14 016 | 13 592 |
| Net loss from decrease of exchange rate | 44 176 | - |
| Increase in provisions for vacations | 31 007 | 11 362 |
| Increase in provisions for doubtful accounts receivable (Appendix 14) | 64 985 | 3 829 |
| **TOTAL:** | **376 064** | **211 948** |

## (7) Interest payment and similar expenses

| | 2017 EUR | 2016 EUR |
|---|---|---|
| Interest payment for loans | 116 184 | 123 182 |
| **TOTAL:** | **116 184** | **123 182** |

## (8) Corporate income tax

| | 2017 EUR | 2016 EUR |
|---|---|---|
| Corporate income tax for the reporting year (Appendix 9) | - | - |
| **TOTAL:** | **-** | **-** |

On 31 December 2017, accumulated losses for provisions of enterprise income tax were EUR 6,123,081 (in 2016 EUR 5,353,689). The usage time limit as at 31 December 2017 extends to 5 years.

## (9) Intangible investments

| | Concessions, patents, licenses, trademarks and similar rights EUR |
|---|---|
| **At 31 December 2015** | |
| Initial value | 34 711 |
| Accumulated amortisation and deprecation | (34 081) |
| **Book value at 31 December** | **630** |
| **The year of 2016** | |
| Book value at 1 January | 630 |
| Purchase | 24 164 |
| Amortisation | (3 609) |
| Book value at 31 December | **21 185** |
| **At 31 December 2016** | |
| Initial value | 58 875 |
| Accumulated amortisation and deprecation | (37 690) |
| **Book value at 31 December** | **21 185** |
| **The year of 2017** | |
| Book value at 1 January | 21 185 |
| Purchase | - |
| Amortisation | (5 075) |
| **Book value at 31 December** | **16 110** |
| **At 31 December 2017** | |
| Initial value | 58 875 |
| Accumulated amortisation and deprecation | (42 765) |
| **Book value at 31 December** | **16 110** |

All fixed assets of the Company are pledged in favour of JSC Citadele Banka, refer to Appendix 19.

**(10) Fixed assets**

| | Land plots, buildings and engineering structures EUR | Investment properties (land and buildings) EUR | Technological equipment and machinery EUR | Other fixed assets EUR | Formation of fixed assets* EUR | TOTAL EUR |
|---|---|---|---|---|---|---|
| **At 31 December 2015** | | | | | | |
| Initial value | 14 749 647 | 1 246 700 | 5 290 097 | 476 841 | 12 649 | 21 775 934 |
| Accumulated amortisation and deprecation | (11 320 754) | (48 253) | (5 263 776) | (465 898) | - | (17 098 681) |
| Book value at 31 December | 3 428 893 | 1 198 447 | 26 321 | 10 943 | 12 649 | 4 677 253 |
| **The year of 2016** | | | | | | |
| Book value at 1 January | 3 428 893 | 1 198 447 | 26 321 | 10 943 | 12 649 | 4 677 253 |
| Purchased | - | | 779 898 | 32 687 | - | 812 585 |
| Initial value of disposed fixed assets | - | - | (3 675) | (31 491) | - | (35 166) |
| Accumulated depreciation of disclosed fixed assets | - | - | 3 675 | 31 491 | - | 35 166 |
| Accumulated depreciation of disclosed fixed assets | - | - | 3 675 | 31 491 | - | 35 166 |
| Disposal | (87 027) | (57 904) | (67 597) | (18 695) | - | (231 223) |
| Book value at 31 December | 3 341 866 | 1 140 543 | 738 622 | 24 935 | 12 649 | 5 258 615 |
| **At 31 December 2016** | | | | | | |
| Initial value | 14 749 647 | 1 246 700 | 6 066 320 | 478 037 | 12 649 | 22 553 353 |
| Accumulated amortisation and deprecation | (11 407 781) | (106 157) | (5 327 698) | (453 102) | - | (17 294 738) |
| **Book value at 31 December** | **3 341 866** | **1 140 543** | **738 622** | **24 935** | **12 649** | **5 258 615** |
| **The year of 2017** | | | | | | |
| Book value at 1 January | 3 341 866 | 1 140 543 | 738 622 | 24 935 | 12 649 | 5 258 615 |
| Purchased | - | | 2 437 549 | 4 142 | - | 2 441 691 |
| Initial value of disposed fixed assets | - | - | (16 401) | (1 181) | - | (17 582) |
| Accumulated depreciation of disclosed fixed assets | - | - | 16 401 | 1 181 | - | 17 582 |
| Disposal | (84 537) | (57 904) | (101 129) | (11 837) | - | (255 407) |
| Book value at 31 December | 3 257 329 | 1 082 639 | 3 075 042 | 17 240 | 12 649 | 7 444 899 |
| **At 31 December 2017** | | | | | | |
| Initial value | 14 749 648 | 1 246 700 | 8 487 468 | 480 994 | 12 649 | 24 977 458 |
| Accumulated amortisation and deprecation | (11 492 319) | (164 061) | (5 412 426) | (463 754) | - | (17 532 560) |
| **Book value at 31 December** | **3 257 329** | **1 082 639** | **3 075 042** | **17 240** | **12 649** | **7 444 899** |

On 31 December 2017, the fixed assets of the Company with the cost of EUR 16,964,366 (EUR 16,978,090 as at 31.12.2016) have been fully depreciated, but are still in operation.

All fixed assets of the Company are pledged in favour of JSC Citadele Banka, refer to Appendix 17.

### (10) Fixed assets (cont.)

* On 14 March 2014, the Company signed with the Investment and Development Agency of Latvia an Agreement No.L-IZI-14-0003 on implementation of the project "Construction of industry premises in the free industrial area of JSC DITTON Driving Chain Factory". The project was launched on 14 March 2014 and completed on 7 July 2015. The total costs of the project amounted to EUR 3,376,313, including eligible costs EUR 2,796,430. Ditton Būve Ltd. has performed construction works within the project due to the Construction works contract No. DPR/2014/01 dated 25 July 2014. In accordance with the statement of completion and final acceptance of work dated 25 February 2015, construction works costed EUR 2,750,704. On 29 December 2015, the Company received the aid EUR 1,159,833 EUR from the Investment and Development Agency of Latvia (LIAA).

** The significant part of production premises of the Company are held for rent. Before 2017 property for rent was recorded as fixed assets. Starting from 2017, the value of Company`s property for rent (land and buildings) is recognized as investment property. Retrospective reclassification of cost, accumulated depreciation and depreciation expense of the relevant assets has been performed (refer to Appendix 2).

Fixed assets include the land on which the infrastructure facilities of the Company are located and which has been historically purchased on installment from a commercial company registered in Latvia and pledged in a commercial bank registered in Latvia as collateral security for the seller's loan. The title to the mentioned plot shall be completely transferred to the Company upon the payment of the purchase amount in full and registration in the Land Registry is practically impossible while the collateral exists. At the time of drawing up the Annual report, the biggest part of the loan and purchase amount have been paid and the remaining loan amount does not exceed EUR 150 thousand. Under the terms of the purchase agreement, the seller is not entitled to request the cancellation of the land purchase agreement.

The Company's management has assessed the value in use of its fixed assets and investment assets in the balance sheet and considers that their recoverable value is not lower than their carrying value.

### (11) Participation in the capital of related companies

| | 31.12.2017<br>EUR | 31.12.2016<br>EUR |
|---|---|---|
| Participation in the capital of the Ditton Chain Ltd. 15% from the fixed capital* | 67 160 | 67 160 |
| **TOTAL:** | **67 160** | **67 160** |

Ditton Chain Ltd., registration number 41503030309, legal address Vishku Street 17, Daugavpils, LV-5410, Latvia, was founded on 17 July 2002 and is administrated by two members. JSC Ditton pievadķēžu rūpnīca owns 53,358 (fifty three thousand three hundred fifty eight) or 15% of 355,717 (three hundred fifty five thousand seven hundred seventeen) shares in this Company.

Although the equity is negative according to the latest annual report of Ditton Chain Ltd. approved, the Company's management believes it will operate ness with good financial results and the investment made in its shares is recoverable.

## (12) Finished products and goods for sale

| | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|
| Finished products for sale | 282 763 | 274 432 |
| Provisions for slow-moving inventory | (69 651) | (45 455) |
| **TOTAL:** | **213 112** | **228 977** |

| | | |
|---|---|---|
| Provisions for inventory with low turnover rate: | | |
| As at the beginning of the year | (45 455) | (182 937) |
| Decrease/increase (appendices 5 and 6)* | (24 196) | 137 482 |
| As at the end of the year | **(69 951)** | **(45 455)** |

* The inventory for which provisions were made was sold.

## (13) Advance payments for inventories

In 2017, the economic activities of the Company were restructured. The balance of the advance payments for inventories reflected in the balance sheet of the Company as at 31 December 2016 was repaid on the course of this restructuring.

## (14) Trade receivables

| | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|
| Book value of trade receivables | 1 431 121 | 2 519 130 |
| Provisions for doubtful accounts receivable | (639 796) | (1 169 234) |
| **TOTAL:** | **791 325** | **1 349 896** |

| | | |
|---|---|---|
| Provisions for doubtful accounts receivable: | | |
| At the beginning of the year | 1 169 234 | 1 324 888 |
| Write-off | - | (1 366) |
| Recovered provisions (Appendix 5) | (594 422) | (158 117) |
| Increase in provisions (Appendix 6) | 64 985 | 3 829 |
| At the end of the year | **639 797** | **1 169 234** |

## (15) Other debtors

| | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|
| Input value added tax receivable (VAT) | 281 035 | 8 126 |
| **TOTAL:** | **281 035** | **8 126** |

### (16) Equity capital

The share capital of the Company is EUR 10,360,000 with nominal value of EUR 1,40 per share and a total paid shares of 7,400,000.

The shareholders owning over 5 per cent of the shares of the whole capital of the Company as at 31.12.2017 and as at 31.12.2017:

| NAME | Shares owned, % 31.12.2017 | Shares owned, % 31.12.2016 |
|---|---|---|
| Eduards Zavadskis* | 20,00 | 20,00 |
| Vladislavs Drīksne | 19,92 | 19,92 |
| MAX Invest Holding Ltd. | 13,63 | 13,63 |
| Maleks S Ltd. | 14,22 | 12,31 |
| DVINSK MNG Ltd. | 9,46 | 9,46 |

** Note: As at 31 December 2017, the Company has no information at its disposal on distribution of stocks (20%) among heirs of E. Zavadskis and their records in financial instruments accounts pursuant to the section 125 of the Financial Instruments Market Law.*

### (17) Loans from credit institutions

| **Long-term:** | | Repayment term | 31.12.2017 | 31.12.2016 |
|---|---|---|---|---|
| Credit line from JSC Citadele Banka | EUR | 09.09.2018 | - | 554 842 |
| Loan from JSC Citadele Banka | EUR | 15.11.2020 | 4 533 505 | 1 303 548 |
| **TOTAL long-term loans from credit institutions:** | | | **4 533 505** | **1 858 390** |

| **Short-term:** | | Repayment term | 31.12.2016 | 31.12.2015 |
|---|---|---|---|---|
| Loan from JSC Citadele Banka | EUR | 09.09.2019 | 388 049 | 116 976 |
| Credit line from JSC Citadele Banka | EUR | 09.09.2018 | 495 149 | 45 158 |
| **TOTAL short-term loans from credit institutions:** | | | **883 198** | **162 134** |
| **TOTAL loans from credit institutions:** | | | **5 416 703** | **2 020 524** |

| | 31.12.2017 | 31.12.2016 |
|---|---|---|
| Liabilities due within one year | 883 198 | 162 134 |
| Liabilities due after one year but not more than five years | 4 533 505 | 1 858 390 |
| **TOTAL:** | **5 416 703** | **2 020 524** |

Information on loans received by the JSC Citadele banka as at 31.12.2017 is as follows:

| **Number and date of the contract** | **Currency** | **Interest rate** | **Limit** | **Repayment term** |
|---|---|---|---|---|
| Long-term loan No.CI2010-2.3/1 dated 10.09.2010 | EUR | 4%+6M EURIBOR | 4 533 505 EUR | 15.11.2020 |
| Credit line No.CI2011-2.3/218 dated 25.11.2011 | EUR | 4%+6M EURIBOR 1% for reservation | 600 000 EUR | 09.09.2018 |

The loan is secured by the commercial pledge on all of the Company's assets, including intangible assets, fixed assets, investment assets, inventories, claim rights and Company`s financial instruments on bank accounts in JSC Citadele banka, as a pool of things at the moment of exercising the pledge right.

The guarantees of individual shareholders of the Company and commercial pledges, as well as guarantees of several cooperation partners and real estate pledge serve as an additional collateral security for loan repayment.

The Loan agreements contain covenants upon breach of which the JSC Citadele bank may request the pre-schedule loan repayment or increase the interest rate by 1%. The information available as at 31 December 2017, when the financial report has been drawn up is not sufficient to determine the fulfilment of all these covenants. The Management Board has submitted to the bank the available information needed for assessment of the covenants at its disposal. Negotiations with the bank on the possible change of term have been initiated. The Management Board is not aware of the bank's intentions to use the rights of JSC Citadele banka mentioned above to request pre-scheduled repayment.

### (18) Other borrowings

| **Short-term:** | | Repayment term | 31.12.2017. | 31.12.2016. |
|---|---|---|---|---|
| Borrowing from the owner of the Company* | EUR | 31.12.2018. | 249 528 | 167 912 |
| Other Borrowings** | EUR | 31.01.2018. | 5 800 | 106 000 |
| **TOTAL short-term borrowings from other persons:** | | | **255 328** | **273 912** |

* Borrowing currency - EUR. Fixed annual percentage rate - 4.75%.
** Borrowing currency - EUR. Fixed annual percentage rate - 3%.

Other borrowings are not secured.

### (19) Taxes and State mandatory social insurance payments

| | **31.12.2017 EUR** | **31.12.2016 EUR** |
|---|---|---|
| Property tax | 247 682 | 248 718 |
| Personal income tax | 70 548 | 78 441 |
| State mandatory social insurance payments | 56 448 | 56 659 |
| Nature resources tax | 192 | 281 |
| Penalties | 88 609 | - |
| Risk duty | 119 | 59 |
| **TOTAL:** | **463 598** | **384 158** |

**(20) Other creditors**

| | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|
| Salaries | 66 003 | 60 196 |
| Trade union membership fee | 51 525 | 52 398 |
| Debts for purchased shares | 19 636 | 19 636 |
| Other creditors | 812 | - |
| Receivables arising in favor of the personnel | 564 | 337 |
| **TOTAL:** | **138 540** | **132 567** |

**(21) Next period income**

| | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|
| Aid of the Investment and Development Agency of Latvia (LIAA) No. L-IZI-14-0003 (long-term) | 978 274 | 1 038 793 |
| Aid of the Investment and Development Agency of Latvia (LIAA) No. L-IZI-14-0003 (short-term) | 60 520 | 60 520 |
| **TOTAL:** | **1 038 794** | **1 099 313** |

On 14 March 2014, the Company signed an agreement with the Investment and Development Agency of Latvia No.L-IZI-14-0003 on implementation of the project "Construction of industry premises in the free industrial area of JSC DITTON Driving Chain Factory". The project was launched on 14 March 2014 and completed on 7 July 2015. The total cost of the project amounted to EUR 3,376,313, including eligible costs EUR 2,796,430. Under the Construction works contract No. DPR/2014/01 dated 25 July 2014 the Ditton Būve Ltd. has performed construction works within the project. In accordance with the statement of completion and final acceptance of work dated 25 February 2015, the construction cost amounted to EUR 2,750,704.

On 29 December 2015, the Company received aid in the amount of EUR 1,159,833 EUR from the Investment and Development Agency of Latvia (LIAA) under a 5-year period ban on alienation.

**(22) Accumulated liabilities**

| | 31.12.2017 EUR | 31.12.2016 EUR |
|---|---|---|
| Accrued liabilities for goods and services | 50 243 | 66 194 |
| Unused employees holidays | 83 309 | 52 302 |
| **TOTAL:** | **133 552** | **118 496** |

**(23) Number of employees in the Company**

| | 2017 | 2016 |
|---|---|---|
| Average number of employees of the Company during the year: | **165** | **165** |
| - Council members | 5 | 3 |
| - Management Board members | 2 | 2 |
| - Other employees | 158 | 160 |

## (24) Report on remuneration of Council and Management Board members

| | Council | Management Board | TOTAL |
|---|---|---|---|
| | **EUR** | **EUR** | **EUR** |
| Salaries and remuneration | 19 929 | 33 334 | 53 263 |
| State mandatory social insurance payments | 4 701 | 7 863 | 12 564 |
| **TOTAL:** | **24 630** | **41 197** | **65 827** |

## (25) Financial risk management

The Company’s activity is subject to a variety of financial risks: foreign currency risk, interest rate risk, credit risk and liquidity risk.

**Foreign currency risk**
Foreign currency risk is the risk that the Company might have financial loss due to unfavourable fluctuations in exchange rates. This risk arises when financial assets in foreign currency do not match with financial liabilities in the same currency; herewith the Company has open currency positions.

**Interest rate risk**
Interest rate risk is the risk that the Company might have financial loss due to unfavourable fluctuations in interest rates. The Company experiences such interest rate risk of long- and short-term loans from credit institutions due to variable fixed rates, or when fixed interest period is less than the planned time of the loan repayment, or when credit interest is based on variables, or due to terms of the Loan agreement (refer to Appendix 17). The Company does not have any other choice and does not use any tools to mitigate the interest rate risk other than to fulfil loan-borrowing conditions in full and to cooperate with credit institutions.

**Credit risk**
Credit risk is the risk that the Company might have financial loss due to business partner who failed to comply with his obligations towards the Company. Cash, trade receivables and advance payments mainly cause the credit risk.

**Cash**
Credit risk related to cash at banks is managed by balancing the financial asset allocation in order to maintain the possibility of choosing the best offers and minimizing the loss of financial resources at the same time.

The Company oversees, assesses and mitigates this risk by appropriate work with Company's partners, for example, limiting or suspending the ongoing and future transactions with unfavourable partners, when the Company receives information about partners` possible problems with meeting their obligations.

**Liquidity risk**
Liquidity risk is the risk that the Company may be unable to meet its obligations timely and in full. Liquidity risk appears, when repayment terms of financial assets and liabilities do not match. The aim of the Company’s liquidity risk management is to maintain an adequate amount of cash and cash equivalents, and ensure appropriate sufficient funding through credit lines issued by the banks (refer to the Appendix 17) so that the Company fulfils its obligations within the set time limits. The Company regularly monitors financial assets and liabilities mismatches, as well as stability of funding sources for long-term investments.

In the opinion of the Company's management, the Company will have sufficient cash resources to secure its liquidity.

## (26) Eventual liabilities, pledges and guarantees

In order to provide collateral securities to commitments of the cooperation partner Ditton Chain Ltd., under registration number 41503030309, within the Loan agreement No. CI2010-2.3/2 dated 10 September 2010 with JSC Citadele Banka the Company did as follows:

- signed Pledge Agreement on Company's immovable property
- signed Commercial Pledge Agreement over Company's movable property
- signed Financial Collateral Agreement secured by Company`s cash in bank accounts
- provided Guarantee.

As at 31 December 2017, the Ditton Chain Ltd. fulfilled all its loan obligations mentioned above against the JSC Citadele Banka, therefore the collateral securities of the Company described above are released by the 1 January 2018. The de-registration process regarding securities mentioned above in all the Latvian public registries shall be done within time periods agreed with JSC Citadele Banka. (Please refer to Appendix 16).

## (27) Related Person Transactions

The Company has no significant transactions with related persons to report on.

## (28) Distribution of profit proposed by the Board

The board of the Company proposes to retain the profit for the year 2017 in order to cover loss of previous years.

## (29) Subsequent events

There are no subsequent events since the last date of the reporting year, which would have a significant effect on the financial position of the Company as at 31 December 2017.

According to the Minutes of the Management Board meeting the financial statements have been signed on behalf of the Company on 24 April 2018 by

Rolands Zarāns
Chairman of the Management Board
(signature)

Jūlija Lavrecka
Chief Accountant
(signature)

POTAPOVIČA
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**Independent Auditor's Report**

**To the shareholder of JSC Ditton pievadķēžu rūpnīca**

*Our Qualified Opinion on the Financial Statements*

We have audited the accompanying financial statements of JSC Ditton pievadķēžu rūpnīca ("the Company") set out on pages 18 to 40 of the accompanying annual report, which comprise:

- the balance sheet as at 31 December 2017,
- the profit and loss statement for the year then ended,
- the statement of changes in equity for the year then ended,
- the statement of cash flows for the year then ended, and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory notes.

In our opinion, except for the effects of the matters presented in the paragraph *Basis for Qualified Opinion* below, the accompanying financial statements give a true and fair view of the financial position of JSC Ditton pievadķēžu rūpnīca as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with the 'Law On the Annual Reports and Consolidated Annual Reports' of the Republic of Latvia.

*Basis for Qualified Opinion*

Comparative information for 2016 in the profit or loss statement of the Company comprises income at amount of 459 thousand euros which is presented in Other operating income and relates to settlements for reconstruction of a building owned by the Company. In our opinion, based on the economic substance it would have been appropriate to recognise this amount as income over the useful life of the respective building, as a result of which profit for 2017 would be by 23 thousand euros higher (profit for the previous year –by 436 thousand lower respectively), but deferred income as at 31 December 2017 would increase by 417 thousand euro (as at 31 December 2016 – by 440 thousand euros respectively).

In accordance with the Law on Audit Services of the Republic of Latvia 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 Financial Statements* section of our report. We are independent of the Company 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 of the Republic of Latvia that are relevant to our audit of the 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 of the Republic of Latvia.

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

*Key Audit Matters*

Key audit matters are those matters that, in our professional judgment, 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. We have determined the matters described below to be the key audit matters to be communicated in our report:

| *Audit matter* | *Response* |
|---|---|
| *Recoverable amount of real estate* | |
| The Company's balance sheet includes land, where infrastructure which is important for the Company's operations is situated. However property rights for this land have not been fully transferred to the Company. Information on these matters is presented in appendix 10 "Fixed assets" in the financial statements.<br><br>Auditors of the Company's financial statements for 2016 have qualified their opinion in this respect. | On the course of the audit, among other procedures:<br>• we obtained information on the legal status of the land plot under consideration, the terms of acquisition, encumbrances and the expected future scenario;<br>• we assessed the actual and potential use of the property by substance and evaluated the Company's chances to release the encumbrances;<br>• In the context of the results of operations for 2017 and the future projections we assessed the recoverable value of the asset, including it's value in use as part of the relevant cash generating unit; |

| *Audit matter* | *Response* |
|---|---|
| We consider this as important matter due to the fact that this asset is crucial for the Company' operations and it's value is material in the context of the Company's balance sheet. | • We corroborated all the evidence available to us we came to a conclusion that the land plot under consideration is presented according to it's actual use and allocation of risks and rewards. |
| <u>*Restructuring of operations*</u> | |
| The Company's results and financial position in 2017 significantly differs from prior years which is caused by substantial changes in the Company's co-operation model with partners, pricing policies, financing arrangements, as well as overall cost optimisation.<br><br>Changes in the Company's operations and their results are very extensive therefore we considered t proper accounting and presentation of these changes to be an important audit matter. | During the audit, apart from other procedures:<br>• We performed detailed tests of transactions and accounts with partners with whom the co-operation model has been changed;<br>• We obtained understanding of the factors giving rise to the changes and events and performed corresponding analytical and detailed procedures;<br>• We performed direct written account reconciliation with the Company's partners;<br>• We evaluated contracts with partners and their effects on and presentation in accounts. |

*Reporting on Other Information*

The Company management is responsible for the other information. The other information comprises:

- the Management Report, as set out on pages 13 to 16 of the accompanying Annual Report,
- the Statement on Management Responsibility, as set out on page 17 of the accompanying Annual Report,
- the Statement of Corporate Governance, as set out on pages 10 to 12 of the accompanying Annual Report.

Our opinion on the 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 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 entity 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 of the Republic of Latvia 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' of the Republic of Latvia.
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 financial statements are prepared is consistent with the 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' of the Republic of Latvia.

In accordance with the Law on Audit Services of the Republic of Latvia 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 Financial Statements*

Management is responsible for the preparation of the financial statements that give a true and fair view in accordance with the 'Law On the Annual Reports and Consolidated Annual Reports' of the Republic of Latvia and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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

*Auditor's Responsibility for the Audit of the Financial Statements*

Our objectives are to obtain reasonable assurance about whether the 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 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 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 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 financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves a fair presentation.

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 objectivity, 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 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 Kristīne Potapoviča.

On behalf of
SIA Potapoviča un Andersone,
Ūdens street 12-45, Riga, LV-1007
Certified Auditors Company licence No. 99

Kristīne Potapoviča
Responsible Certified Auditor
Certificate No. 99
Chairman of the Board

24 April 2018