



## **SUSTAINABILITY AND ANNUAL REPORT**

2018

(this page is intentionally left blank)

# CONTENTS

## ABOUT LATVENERGO GROUP 1

Foreword	5
About the Report	7
About the Group	8
Group Strategy	11
Corporate Social Responsibility	13
Awards	16

## CORPORATE GOVERNANCE 2

Corporate Governance Model	18
Governance Bodies	19
Group Management	25
Internal Control System and Risk Management	26
Group Procurement	28
Stakeholder Engagement	30

## OPERATING SEGMENTS 3

Generation and Trade	36
Generation	37
Trade	42
Mandatory Procurement	44
Distribution	45
Lease of Transmission System Assets	47

## PERFORMANCE INDICATORS 4

Materiality Assessment	50
Economic Topics	52
Social Topics	57
Product Responsibility	57
Society	61
Employees and the Work Environment	62
Environmental Topics	66

## ANNEXES TO THE SUSTAINABILITY REPORT 5

Green Bond Report	72
GRI Index	74
Abbreviations	77
Independent Practitioner's Assurance Report	78

## LATVENERGO GROUP CONSOLIDATED AND LATVENERGO AS ANNUAL REPORT 6

Key Figures	81
Management Report	83
Financial Statements	89
Statement of Profit or Loss	89
Statement of Comprehensive Income	89
Statement of Financial Position	90
Statement of Changes in Equity	91
Statement of Cash Flows	92
Notes to Financial Statements	93
Independent Auditor's Report	147





## ABOUT LATVENERGO GROUP

## DEAR READERS,



**Andris Ozoliņš**  
Chairman of the Supervisory Board  
of Latvenergo AS



**Āris Žigurs**  
Chairman of the Management Board  
and Chief Executive Officer  
of Latvenergo AS

Important events took place in the energy industry in 2018 because of its continuous and rapid development, and while this process is creating new challenges, it is also providing solutions to them. The word “energy” now means involvement, knowledge, mastering new habits and use of new services by customers. It is only natural that digitalisation, robotization, e-mobility and artificial intelligence are playing an increasingly important role in the daily operations of Latvenergo.

At the same time, the industry as a whole and the operations of Latvenergo Group are affected by global environmental and climate factors. Long drought and dry weather conditions across Europe reduced power generation at hydro power plants considerably. However, Latvenergo generated power successfully in this situation using the mutually complementary possibilities of its plants. This was possible because professional energy experts and engineers had taken decisions on reconstruction and maintenance of Latvenergo power plants in due time based on a long-term vision.

At the beginning of the year there was a very high water inflow into the Daugava, and the Latvenergo hydro power plants (HPPs) were working at their full capacity. Latvia even became the biggest power exporter in the Baltics for a time. This was followed by a long period

of warm and dry weather, and throughout the year the water inflow into rivers in Scandinavia as well as our Daugava was among the lowest in the history of observations and the power generation at hydro power plants was very low. Global factors and the low water level contributed to an increase in electricity prices in Latvia of 44% compared to the previous year, reaching 50 EUR per megawatt hour.

Latvenergo Group generated more than 5 TWh of electricity in 2018. Of this amount, 2.6 TWh were generated by the combined heat and power plants (CHPPs), 2.4 TWh were generated by the HPPs, and 47% of the total electricity output was generated from renewable energy resources. Optimally combining generation by the CHPPs and HPPs with import possibilities from other trading areas of the Nord Pool exchange, the prices for consumers in the Baltics are approaching those of the electricity market in Nordic countries, which is historically the region with the lowest prices in Europe. In total, 7 TWh of electricity were sold to retail customers in the Baltics in 2018. This amount is about the same as in the previous year and around a third of it was sold outside Latvia.

In October 2017 Latvenergo AS applied for a one-off compensation from the state, forgoing the receipt of 75% of the annual electricity capacity payment to cogeneration plants CHPP-1 and CHPP-2. Thus, the share of the CHPPs in the payment of the mandatory procurement and capacity decreased from 37% to 15%, i.e. by EUR 74.2 million, in 2018.

The development of trade has continued successfully in accordance with the Group's strategy. At the end of 2018, trade of natural gas was started in Lithuania under the brand *Elektrum* and at present Latvenergo Group is active in all the energy trade segments in Latvia, Lithuania and Estonia. The volume of natural gas sold to corporate customers continued to grow in the reporting year, and the number of customers exceeded 400 at the end of 2018. In February 2019, sale of natural gas to households in Latvia was begun.

Latvenergo actively used the opportunities offered by the free natural gas market. Since liberalisation of the gas market, deliveries of natural gas in Latvia have been diversified; in particular, during the first year of the free market, gas was delivered not only by

pipelines from Russia, but also from Lithuania and its liquefied natural gas terminal in Klaipėda. The opening of the market allows for working with several gas suppliers to obtain a better price. We store purchased resources according to necessity in the Inčukalns underground gas storage facility, and we provide heat and electricity in full to our customers and also offer natural gas to customers in all three Baltic countries.

Latvenergo continues to develop new business directions and services. Smart services are an area with a high growth potential; therefore, *Elektrum* has diversified its range of services by offering customers solar panels through its *Elektrum Solar* service. The service *Smart Home* allows for remote control of electrical appliances both at home and at companies according to one's needs. This is an opportunity to improve the comfort level and to save money during the heating season. We are glad to see that the number of customers of the service *Elektrum Insured* has continued to grow, reaching more than 41 thousand at the end of 2018. In 2018 Latvenergo started a pilot project for analysing the future business opportunities of e-mobility.

To ensure the competitiveness of Latvenergo in accordance with the Group Strategy 2017–2022, a strategic development and efficiency programme providing for review of the Group's business processes, their centralisation and digitalisation, is being implemented. Along with these efficiency measures until 2022, the number of staff at Latvenergo Group will be gradually reduced by one quarter. The number of employees at Sadales tīkls AS will decrease by 800, and this is possible thanks to an intense review of processes and digitalisation. Within the programme, smart meter installation and changes in the customer relations management processes are continuing, and the number of vehicles and technical bases is being reduced. More than 540 thousand smart electricity meters, accounting for approximately one half of the total fleet of meters, were installed by 31 December 2018.

EUR 95.1 million were invested in the distribution segment in 2018. The investments are aimed at promoting quality and reliable energy supply, reducing the frequency and duration of scheduled and unscheduled power supply outages due to damage, and ensuring adequate voltage quality. Investments in distribution network

upgrades have improved the quality of the distribution service: compared to 2017, the System Average Interruption Frequency Index per customer and the System Average Interruption Duration Index per customer were reduced by 11% and 13% respectively.

During the reporting year, EUR 87.1 million were invested in transmission system assets, an increase of 38% compared to the preceding year. The largest amount, EUR 65.2 million, was invested in the energy infrastructure project *Kurzeme Ring*.

At the end of 2018 Latvenergo organised a stakeholders' workshop to secure involvement of various partners important for the national economy in the sustainable development of the Group. During this event we evaluated the topics important for the sustainability of the Group, discussed current cooperation and learned about the possibilities for further improvement of cooperation as identified by the partners.

The XXVI Latvian Song and XVI Dance Festival took place in 2018. For its contribution to creating this important event, the trademark *Elektrum* received the gratitude of the Latvian National Culture Centre. Another event worth mentioning is FIZMIX Experiment, the first festival devoted to physics in Latvia. This event organised by Latvenergo Group gathered more than two thousand visitors, and it is the only event of this type and scale in the Baltics encouraging learning of exact sciences in the schools and universities of Latvia.

The Group is also successfully continuing various environmental initiatives. Latvenergo employees and their families participated in cleaning tributaries of the Daugava for the second year, and this year a section of the Perse River was cleaned. In cooperation with the association *Mēs zivīm*, artificial spawning nests were created

and deposited in the Daugava in the spring. We also help the Latvian Ornithological Society with the monitoring of white storks. The Group's employees have surveyed more than 12% of the nests covered by the programme.

It is good to know that our achievements are also appreciated by experts on a broader scale. 2018 marked the 10th time in a row that Latvenergo received the title of the most valuable company in Latvia in the TOP 101 most valuable Latvian companies, organised jointly by Prudentia AS and Nasdaq Riga AS.

The international credit rating agency Moody's approved the credit rating of Latvenergo AS as Baa2 (stable). The rating has remained unchanged for several years, thus attesting the security of the company's operations and its financial stability.

For the sixth year in a row Latvenergo received the Platinum or highest category award in the Sustainability Index, which assesses company sustainability according to international requirements in all areas of corporate social responsibility. It should be emphasised that in 2018 Latvenergo's overall score was the highest in the history of our participation: 97.2%. Such an evaluation was achieved through well-considered investment in modernisation of generation plants; care for the environment, employees and customers; good governance; and sustainable solutions in energy production and trade.

Improvement of the Group's corporate governance was also continued in 2018. The Group's strategic development and efficiency programme was updated, best practice in corporate governance was evaluated, an updated corporate governance policy was approved, an action plan for corporate governance was developed,

and the Strategic Communication Committee of the Supervisory Board was established.

This was the year of the hundredth anniversary of Latvia, when many of us did something for the benefit of our families and our state. A great achievement of Latvenergo Group in this anniversary year was the historically highest electricity output at our CHPPs since 1980, when CHPP-2 was put in operation. The role of our CHPPs in meeting regional demand in 2018 confirms the importance of these plants for national energy independence along with commercial gains. Guaranteeing and being able to ensure the national energy supply at any moment are the largest contributions by our Group. This has been the mission of the Group since the beginnings of Kegums HPP in 1939.

At present the energy industry is on the verge of very important changes. Modern technologies and demand for clean and carbon-free energy will have a major impact on the industry in the coming years. Further development of technologies will be decisive: electromobility, energy accumulation technologies and the increasingly important role of artificial intelligence in daily life. Electricity generators and traders will have to adjust to the new conditions and prepare offers for new, atypical customer groups, giving priority to pre-emptive changes in technologies and the products offered to customers in order to ensure long-term viability of businesses and sustainability in an increasingly competitive environment. Peer-to-peer network solutions, blockchains, e-mobility and other innovations should become a part of daily life in Latvia as well.

It is important for us to understand future challenges today since these processes will have a huge impact on the business of energy as a whole.

# ABOUT THE REPORT

Reporting period	1 January 2018 – 31 December 2018
Publication date	17 April 2019
Reporting frequency	Annually, since 2009, in accordance with the Global Reporting Initiative (GRI) guidelines.
Publication date of the previous report	18 April 2018
Global Reporting Initiative	The Sustainability Report 2018 has been prepared in accordance with the GRI Standards Core level requirements and includes non-financial information as stated by Directive 2014/95/EU of the European Parliament and of the Council and the Law on the Financial Instruments Market.
Scope of the report	The report discloses information about Latvenergo Group (see the section About the Group).
Principles for defining report content	<p>The report discloses information about the topics and indicators that are important to the operations and sustainability of the Group. General Standard Disclosures are fully covered according to the GRI Standards Core level requirements. Based on the materiality assessment, 16 material topics relevant to the sustainability of the Group and 31 Specific Standard Disclosures are disclosed (see the GRI Index table).</p> <p>The report preparation process is described in the section Materiality Assessment. The methods for measuring data have not been altered significantly compared to the sustainability reports for previous years.</p>
Independent auditor's assurance report	The assurance report on the Sustainability Report 2018 has been prepared by PricewaterhouseCoopers SIA.
Report format	<p>The report is available electronically:</p> <ul style="list-style-type: none"> <li>■ on the Latvenergo website <a href="http://www.latvenergo.lv">www.latvenergo.lv</a> (in Latvian and English);</li> <li>■ in the GRI Sustainability Disclosure Database <a href="http://database.globalreporting.org/">http://database.globalreporting.org/</a> (in English).</li> </ul>
Contact information	Please send any questions or suggestions regarding the Sustainability Report to: <a href="mailto:sustainability@latvenergo.lv">sustainability@latvenergo.lv</a>

## GRI Standards Disclosure Requirements

	Core level	Comprehensive level
General Standard Disclosures (GRI 100)	At least 33 disclosures from GRI 102	All disclosures from GRI 102
Specific Standard Disclosures (GRI 200, 300, 400)	At least one topic-specific disclosure for each material topic	All topic-specific disclosures for each material topic



# ABOUT THE GROUP

Latvenergo Group is one of the largest power suppliers in the Baltics. It operates in electricity and thermal energy generation and trade, electricity distribution services and the lease of transmission system assets.

The Group comprises the parent company Latvenergo AS with decisive influence and six subsidiaries. All shares of Latvenergo AS are owned by the Republic of Latvia, and they are held by the Ministry of Economics of the Republic of Latvia. Information about the participating interests in the subsidiaries and their locations is disclosed in Notes 1 and 15 to the Consolidated Annual Report.

The Group divides its operations into three operating segments: generation and trade, distribution, and lease of transmission system assets. More information is disclosed in the section Operating Segments.

## MISSION

To ensure high-quality, safe and environmentally friendly energy generation and supply to customers sustainably, thus promoting an increase in the long-term value of the Group



## VISION

To be one of the leading and primary customer-chosen providers of sustainable and high-quality power supply services in the Baltic markets.

## VALUES

### RESPONSIBILITY

We are reliable

### EFFICIENCY

We strive for excellence

### OPENNESS

We are transparent and open to new ideas



● Lease of transmission system assets ● Distribution ● Electricity and natural gas trade



# FACTS 2018

## Financial figures

		2018	2017
Revenue	MEUR	878.0	925.6
Profit	MEUR	76.0	322.0
Assets	MEUR	3,798.8	4,415.7
Investments	MEUR	220.6	243.8
Moody's credit rating		Baa2	Baa2

## Generation and trade

Installed electrical capacity	MW	2,591	2,583
Installed thermal capacity	MW	1,838	1,842
Electricity output	GWh	5,076	5,734
Thermal energy output	GWh	2,274	2,612
Generation efficiency of the Daugava HPPs	m³/kWh	18.6	18.6
Generation efficiency of the Latvenergo AS CHPPs	%	77%	88%
Market share in the Baltics	%	25%	25%
Retail electricity supply	GWh	6,954	6,923
Retail natural gas supply	GWh	147	33
Retail customers	thsd.	789	834

## Distribution

SAIDI	min	228	261
SAIFI	number	2.5	2.8
Length of distribution lines	km	93,175	93,560
Transformer capacity	MVA	5,930	5,913

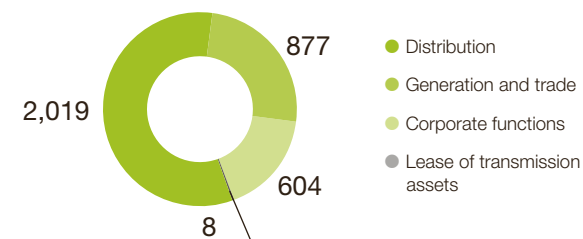
## Lease of transmission assets

Length of transmission lines	km	5,243	5,240
Transformer capacity	MVA	9,165	9,021

## Employees

2018

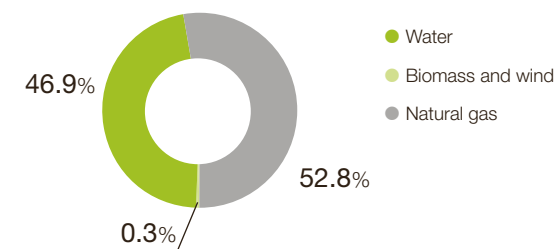
3 508



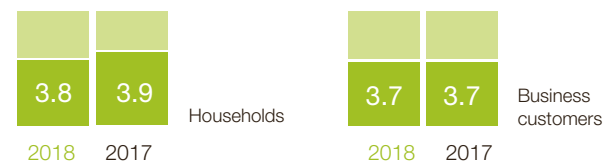
## Share of renewable energy generated

2018

47%



## Customer satisfaction (scale 1–6)



## HIGHLIGHTS 2018



### Latvenergo Group – the most valuable energy company in the Baltics

For the tenth time in a row, Latvenergo received the most valuable company award in the ranking TOP 101 Most Valuable Companies of Latvia. The Group was also among the top three most valuable enterprises in the Baltics.

### Continuing to improve distribution service quality

In 2018, the System Average Interruption Duration Index (SAIDI) was reduced by 13% and the System Average Interruption Frequency Index (SAIFI) was reduced by 11%. Over the last five years, we have reduced SAIDI by 51% and SAIFI by 34%.

### Historically highest electricity output at the CHPPs

As hot, dry weather conditions in Europe caused an unexpected rise in electricity prices, the Group used the advantages of its diversified facilities and generated the largest amount of electricity – 2.6 TWh – at the Latvenergo AS CHPPs.

### Developing trade in the Baltics

At the end of the year, the Group started trading natural gas in Lithuania, and as of February 2019 it also offers natural gas to Latvian households. *Elektrum Solar*, a service that offers the possibility to generate solar power independently, is now also available in Lithuania and Estonia. Latvenergo Group currently operates in all energy trade segments in Latvia, Lithuania and Estonia.

### Highest ever score in the Sustainability Index

In June, Latvenergo AS received the Platinum category from the Sustainability Index and the highest overall score in the history of its participation: 97.2%. Modernisation of generation facilities, good governance, and care for the environment, employees and customers were greatly appreciated. Sadales tīkls AS and Liepājas enerģija SIA, subsidiaries of the Group, were awarded the Gold category.

### Latvenergo organises the first ever physics festival in Latvia

In May, during the first FIZMIX Experiment festival in Riga, children, young people and parents could gain insight into the exact sciences in diverse and engaging workshops and activities. This is a unique event in the Baltics, and it brought together more than 2,000 visitors of different ages and organisations that promote young people's interest in the exact sciences.

### Latvenergo fosters reduction of the MPC

The decision of Latvenergo AS to apply for a reduction of the CHPP support payment made it possible to reduce the average MPC value by 15%, thus strengthening the competitiveness of Latvian companies. In 2018, the impact of the CHPPs on the mandatory procurement and capacity payment dropped from 37% to 15% or by EUR 74.2 million.



# GROUP STRATEGY

2018 brought both opportunities and challenges to the energy sector. Despite the fact that the weather conditions were not favourable for electricity generation at the Daugava HPPs, the year was nevertheless successful. Latvenergo Group strengthened its position in the Baltic natural gas markets, developed the range of the *Elektrum* services and products, continued the digitisation of internal processes and customer service, and implemented the efficiency programme of the Group as planned. The activities foreseen in the programme for 2018 were successfully fulfilled.

The Latvenergo Group's Strategy 2017–2022 defines the strategic operational and financial objectives and main development tasks of the Group. By implementing the strategy and at the same time adhering to the principles of sustainability, the Group contributes to satisfying the needs of society, fosters long-term energy supply security and increases the value of the Group.

## THE GROUP'S STRATEGIC OBJECTIVES

### 1. Strengthening a sustainable and economically sound market position in home markets (in the Baltics), while considering geographical and/or product/service expansion

This objective envisages excellence in the Group's trade operations and cost efficiency. It also includes development of new products and services to complement the traditional ones and promote synergy with the current business lines and customer base.

Latvenergo Group is one of the largest energy traders and the most valuable energy company in the Baltics. In 2018, the Group sold 7 TWh of electricity. Electricity sales outside Latvia amounted to 2.5 TWh and accounted for 1/3 of the total retail sales of electricity.

In the reporting year, the Group also started sales of natural gas in Lithuania. This means that Latvenergo currently operates in all energy trading segments in Latvia, Lithuania and Estonia. The Group has long been one of the largest consumers of natural gas in the Baltics, and this experience has made it possible to create a well-thought-out offer for customers. In the reporting year, 0.15 TWh of natural gas were sold to business customers in the Baltics.

## SUSTAINABILITY IN THE LATVENERGO GROUP

### RESPONSIBILITY FOR THE GROUP'S IMPACT ON THE ECONOMY, SOCIETY AND THE ENVIRONMENT

Economic development	Society	Environmental protection
Provision of energy to the national economy	Increasing the value of products and services	Environmentally friendly operations mitigating or preventing risks to the environment
Sustainable and well-considered investments in the energy generation and network infrastructure	Loyal and sustainable customer relations	Effective use of natural resources and promotion of energy efficiency
High efficiency standards	Reliable power supply	Fostering preservation of biodiversity
	Development of human resources and their competencies, and ensuring knowledge continuity	



In 2018, retail trade in other services in the Baltic states was expanded: *Elektrum Solar*, which gives customers an opportunity to consume independently generated solar energy, is now available in Lithuania and Estonia.

Keeping pace with development trends, the Group is actively working on e-mobility pilot projects as well.

### 2. Developing a generation portfolio adequate for synergy with trade and increasing the Group's value

This objective envisages reconstruction of the Daugava HPPs' hydropower units to ensure their sustainable and reliable operation. Furthermore, the aim is to move towards the development of generation capacities which meet the criteria for diversification of primary generation sources and low-emission projects.

In the reporting year, EUR 21.1 million were invested in the reconstruction of the Daugava HPPs' hydropower units, and three units were modernised ensuring their operation for the next 40 years. The performance indicators of the Latvenergo AS CHPPs in 2018 fully justified the investments made in their reconstruction in previous years. Both CHPPs played a very important role in providing generation capacities at a time when the water inflow in the Daugava River was low and capacity shortages were observed in regional interconnections.

In 2018, the Group was also exploring opportunities for a wind power plant pilot project. The know-how acquired in the project will be a prerequisite for the future expansion of the Group's generation portfolio.

### 3. Developing a functional, safe and efficient network corresponding to customer needs

This objective envisages increasing operational and cost efficiency of the distribution network, enhancing the quality and safety of distribution services and actively implementing the digitisation of the distribution network as well as the development of the transmission assets.

In 2018, the distribution network was further reconstructed and upgraded, which made it possible to reduce the System Average Interruption Duration Index (SAIDI) by 13% and the System Average Interruption Frequency Index (SAIFI) by 11%. The digitisation of the distribution network was also continuing rapidly and successfully. At the end of the reporting year, smart meters accounted for 49% of the total meter fleet and were metering 83% of the total amount of electricity distributed.

Reorganisation of the structure of Sadales tīkls AS, centralisation of processes and reduction of the number of vehicles, maintenance depots and employees were carried out as planned within the project for improvement of operational efficiency.

In line with the plan, the Group also continues to invest in the transmission asset development projects *Kurzeme Ring* and the third Latvia–Estonia transmission network interconnection.

## THE GROUP'S FINANCIAL OBJECTIVES

The 2017–2022 strategy also sets Latvenergo Group's objectives for profitability, capital structure and dividend policy.

Latvenergo Group's profit for 2018 amounted to EUR 76.0 million. The return on equity (ROE) was 2.9%. Both indicators were significantly influenced by lower electricity generation at the Daugava HPPs, which was considerably lower than the average multiannual outputs due to dry weather and almost twice as low as in 2017. The rapid rise in electricity prices, smaller intensity of support for Latvenergo AS CHPPs and changes in tax legislation also had a negative impact. In 2017, the Group's profit was comprised of its operating result: a profit in the amount of EUR 172.9 million and a deferred tax reversal in the amount of EUR 149.1 million as a result of the corporate income tax reform.

### The Group's financial objectives

Target group	Ratio	2016	2017	2018	2022	Industry average ratio*
<b>Profitability</b>						
<i>ambitious, yet achievable profitability, which is consistent with the average ratios of benchmark companies in the European energy sector and provides for an adequate return on the business risk</i>	Return on equity (ROE)	5.8%	12.2%	2.9%	> 6%	5 – 8%
<b>Capital structure</b>						
<i>an optimal and industry-relevant capital structure that limits potential financial risks</i>	Net debt to equity	25%	21%	30%	< 50%	30 – 50%
	Net debt to EBITDA	1.7	1.1	2.0	< 3	2.5 – 3
<b>Dividend policy</b>						
<i>a dividend policy that is consistent with the planned investment policy and capital structure targets</i>	Dividend payout ratio**	77.4 MEUR	90.1 MEUR	156.4 MEUR	> 80%	60 – 70%

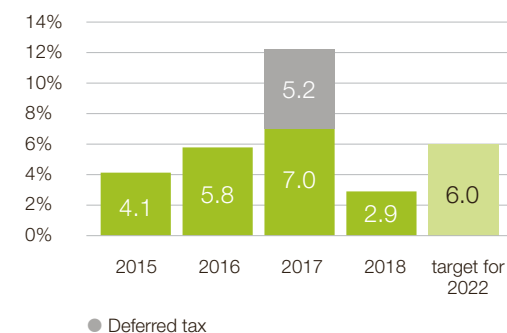
\* based on the data at the time of development of the strategy

\*\* dividends are paid in compliance with the legislation of the Republic of Latvia

The Strategic Development and Efficiency Programme launched by Latvenergo Group will contribute to reaching the financial objectives set for 2022. The estimated gain of the programme exceeds EUR 30 million.

The 2018 financial indicators of the capital structure met the set objectives and exceeded average industry indicators as well. The strong capital structure provides for dividend payments larger than the industry average. The dividend policy defined in the strategy sets the dividend payout ratio at more than 80% of the profit, while each year's dividend payout is set by the Shareholder Meeting upon evaluation of the actual results.

### Return on equity (ROE)





# CORPORATE SOCIAL RESPONSIBILITY

Latvenergo Group not only complies with statutory requirements, but also performs voluntary activities aimed at improving the public welfare and the environment. In its daily operations, the Group follows the principles of social responsibility in compliance with ISO 26000.

The Corporate Social Responsibility (CSR) Policy of the Group sets out the CSR forms, basic principles, directions and selection criteria for activities. The activities implemented raise public awareness of responsible business conduct and the energy industry, making a substantial long-term impact and ensuring the involvement of large groups of society. CSR activities are implemented by the Group in the following areas of its operations:

- science and education;
- raising public awareness of electrical safety;
- environmental protection;
- culture and energy industry heritage;
- social support and responsibility towards employees.

The corporate reputation study conducted by TNS Latvia SIA at the end of 2018 shows that the majority of industry experts and representatives of the general population, the business environment and the media believe that the companies of Latvenergo Group conduct business responsibly. The share of Latvian residents who express approval of the Group's CSR activities in the field of education and science has increased significantly.

One of the forms of social responsibility of Latvenergo AS comprises donations. Since 2018, the company has been donating funds for the cultural and social projects via tenders administered by partner organisations, thus expanding stakeholder engagement and involving experts from relevant areas in the decision-making process. The foundation *Ziedot.lv* administers the support for raising the quality of life of society and for people with special needs, while the State Culture Capital Foundation (SCCF) administers such support for national cultural events.

In June 2018, a survey of Latvian residents about Latvenergo AS donation activities was conducted. Most respondents consider the donation projects implemented to be appropriate for Latvenergo AS involvement. The linkage of the partners with the Latvenergo brand received a high assessment in the survey.

## Science and education

Latvenergo Group implements science and education CSR projects with a view to:

- promoting young people's interest in exact science-related subjects and engineering professions;
- supporting young people's excellence in the exact sciences;
- supplementing teaching materials for schoolteachers;

- supporting researchers' and teachers' scientific work in the field of energy that promotes the education of youth;
- raising public awareness of energy efficiency.

In cooperation with the Latvian Academy of Sciences, for 20 years Latvenergo Group has been awarding its Annual Award for outstanding and significant contributions to the energy industry and achievements of young researchers in the field. Each year, the Group runs competitions for students of higher educational institutions, awarding the best graduation papers on topical issues in the energy sector, and organises a scholarship competition for students. Employees of the Group participate in the bachelor's and master's thesis defence committees of Riga Technical University (RTU) and Latvia University of Agriculture (LUA).



In May 2018, the Group organised the first ever festival dedicated to physics in Latvia, bringing together a number of organisations that are keen to educate young people and promote interest in the exact sciences. In the course of the day, more than two thousand visitors participated in unusual experiments involving gravity, sound, light and electricity; learnt about the structure of a hydraulic robot, rockets, boats and solar cars; and tested their knowledge of physics and electrical safety.

Latvenergo Group organises the knowledge contest Fizmix Experiment for 8<sup>th</sup> and 9<sup>th</sup>-graders. In order to teach physics to young people in an interesting and comprehensive way, provide teachers with an idea base and auxiliary materials and raise the prestige of mastering physics, Latvenergo AS has developed the FIZMIX physics portal. The FIZMIX team also presents physics experiments at offsite workshops at schools in Latvia, at other events and in the knowledge game show *Smart, Even Smarter*. In 2018,

the Group created the *skolotajiem.fizmix.lv* portal, where teachers can share creative teaching methods. Since 2017, the Group has been supporting the participation of Latvian teams in the International Physics Olympics, and in 2019 it will also support the 3<sup>rd</sup> European Physics Olympiad in Riga.

The Energy Efficiency Centre in Jurmala provides everyone with the opportunity to take part in tours, workshops and events free of charge, while *esmuefektivs.lv* offers valuable and practical tips for the household on how to better care for nature and economise. The website also offers an interactive e-learning course for training employees on energy efficiency.

### Raising public awareness of electrical safety

Raising public awareness of electrical safety is one of the CSR priorities of Sadales tīkls AS. To reduce the number of electrical injuries due to insufficient knowledge, a number of projects aimed at electrical safety among children and young people are implemented in cooperation with educational institutions and experts. Particular attention is paid to ensuring that the information complies with the content and type of activities appropriate for each age group.

Since 2013, classes on electrical safety have been held at almost 700 educational institutions all over Latvia, educating more than 110 thousand children and young people. The main activities of 2018:

- continuing the electrical safety campaign *Don't Take Risks with Electricity! Survive!* and enhancing the website *www.arelektibuneriske.lv*;
- taking part in the education and safety projects *One Day for Safety and Be Safe, not Overconfident*, and participating in summer camps for children as well as various events dedicated to safety.

Sadales tīkls AS also educates people engaged in business operations, logging and agricultural work and urges them to take care of their own safety and the safety of those around them and to follow electrical safety rules near electricity lines.

### Culture and energy industry heritage

By supporting nationwide cultural events, the Group promotes the development of Latvia's cultural traditions and the strengthening of Latvian national identity.

In 2018, Latvenergo AS supported the XXVI Song and XVI Dance Celebration, which is among the central events of the celebration of the 100<sup>th</sup> Anniversary of the Latvian state. In cooperation with the SCCF, support was provided to the Latvian National Theatre Centenary project *I Want Latvia*, the festival *Rīgas ritmi 2018*, the international youth music festival *AVANTI!*, the 23<sup>rd</sup> International Baltic Ballet Festival, the XV Kremerata Baltica Festival *Amber Music* and the documentary film cycle *To Be a Latvian*.

The Museum of Energy of Latvenergo Group researches the history of energy in Latvia and the Group ensures collection, preservation and promotion of energy industry heritage and its availability. The museum offers exploratory tours and activities where everyone can gain insight into the history of energy in Latvia and Latvenergo Group and watch the film *How Kegums Power Plant Was Built. Memoirs of Kārlis Dumbrājs*. In 2018, the Museum of Energy published the photobook *Pride of Latvia's Energy Industry: Kegums Hydropower Plant in the Photographs by Eduards Kraucs*. For the first time in the cultural history of Latvia, the book presents 284 outstanding photographs depicting the construction of Kegums Power Plant taken by the prominent photographer and documentary filmmaker.

For an in-depth exploration of the exhibition, the museum in Kegums offers its visitors a mobile guide, which was recognised as one of the most innovative projects of Latvian museums by the Latvian Museums Association in 2018.

### Social support and responsibility towards employees

In cooperation with *Ziedot.lv*, Latvenergo AS supported 10 social projects in 2018, providing assistance to several thousand people throughout Latvia. Every year, the Group's employees donate a variety of useful everyday items to those in need.

On its own initiative, the Group provides additional social protection to its employees, which is not stipulated by legislation. More information is available in the section Employees and the Work Environment.

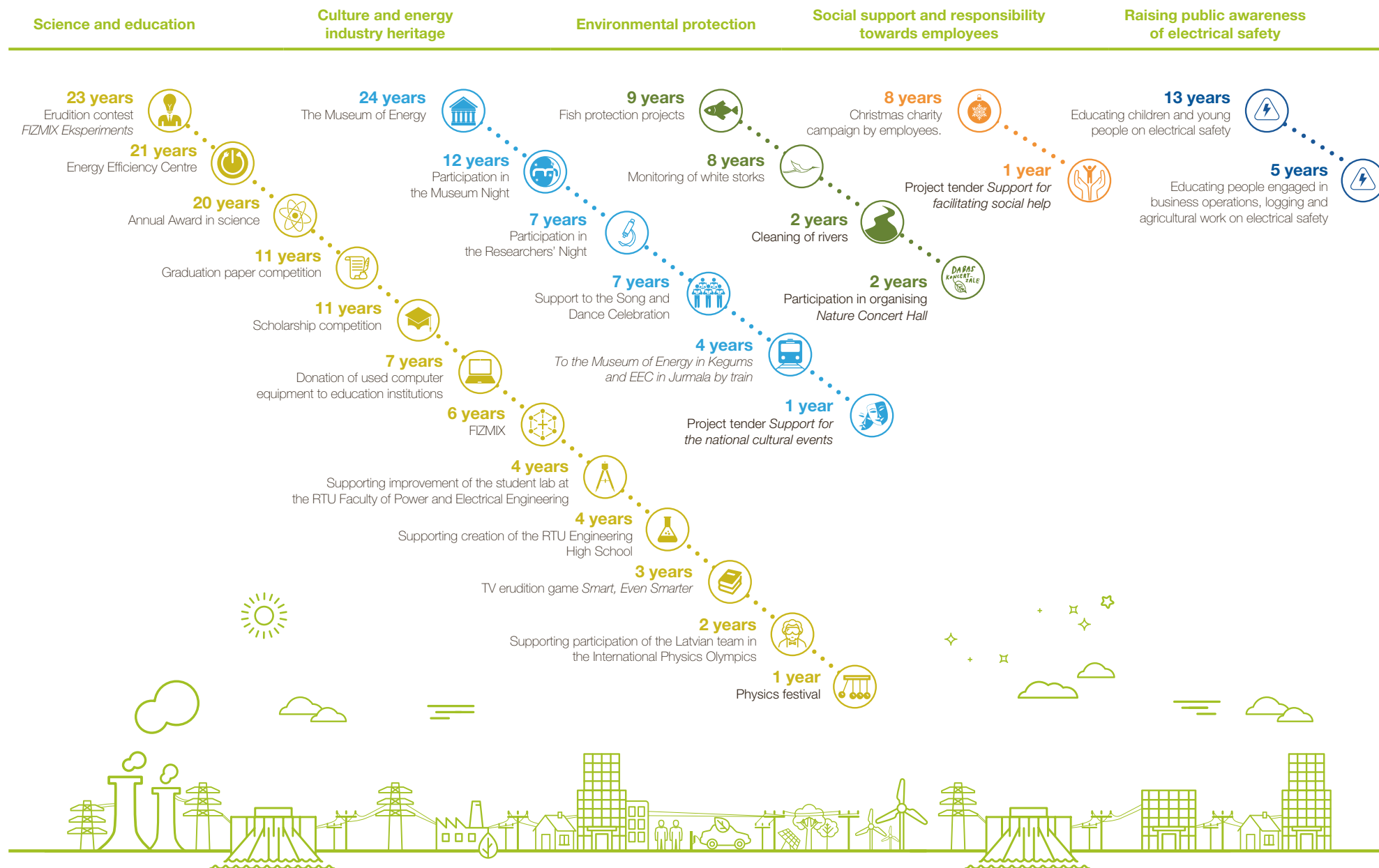
### Environmental protection

Preserving biodiversity and minimising the environmental impact of the Group's operations is among the core principles of the Group's Environmental Policy. Protection of birds and replenishment of fish stock are important areas of action in this regard. The Group cooperates with the Latvian Ornithological Society in matters related to the protection and study of birds and with *Mēs zivīm*, a fish conservation society, to promote the replenishment of stock of fish breeds characteristic of the Daugava River basin.

In 2017, a new environmental initiative was launched: cleaning up the tributaries of the Daugava River basin. In many places, they are blocked by fallen trees, beaver dams, debris and aquatic plant shoals, and the aim of the initiative is to help the streams regenerate naturally and to assess the impact of cleaning on biodiversity.



## CSR activities of Latvenergo Group





# AWARDS

2018



## The most valuable company in Latvia for 11 years

For the eleventh time in total and for the tenth time in a row, Latvenergo AS received the award for the most valuable company in the TOP 101 Most Valuable Companies of Latvia.



## Seven awards in the TOP 500 Companies of Latvia

Latvenergo AS received awards for the most valuable company, the largest state-owned company, the largest EBITDA maker, the most profitable company, the largest company in the energy sector, the company with the largest long-term investments and the largest corporate income tax payer.



## The highest ranking in the Sustainability Index: 97.2%

For the sixth year in a row, Latvenergo AS received the Platinum category from the Sustainability Index along with the highest overall assessment in the history of its participation. A Family-Friendly Company Certificate was received for the seventh year in a row. The Group subsidiaries Sadales tīkls AS and Liepājas enerģija SIA were awarded the Gold category.



## The Most Attractive Employer

For the sixth time, Latvenergo AS was ranked as the TOP employer in the production sector and as the fifth most popular employer in Latvia in a survey by CV-Online Latvia. In a study by Fontes, Latvenergo AS was also recognised as one of the fairest remuneration payers.



## The Safest Company Car Fleet

The Latvenergo Group light-duty vehicle fleet was awarded the Gold category and the Sadales tīkls AS special vehicle fleet received the Silver category in the competition The Safest Company Car Fleet.



## The first physics festival in Latvia organised by Latvenergo receives recognition

At the Annual Event Award ceremony, the festival received the gold prize as the best children's event in Latvia in 2018 and the silver prize as the best event idea. Second place in the category Event PR was awarded in the competition Mi&links: Baltic Communication Awards 2019.





## **CORPORATE GOVERNANCE**

# CORPORATE GOVERNANCE MODEL

The corporate governance model of Latvenergo Group has been developed in compliance with governance best practice on the basis of the regulatory framework and corporate governance guidelines. The elements included in the model are a prerequisite for achieving the Group's goals and increasing its value.

Every year since 2012, Latvenergo AS has prepared a corporate governance report according to the requirements of the Financial Instrument Market Law and the Principles of Corporate Governance and Recommendations on Their Implementation issued by Nasdaq Riga AS. In 2018, the company complied fully with 77 out of these 83 principles; the other six are not applicable to the company's operations. The full text of the report is available on the Latvenergo website and on the Nasdaq Baltic website.

## Ethics and Compliance

Latvenergo Group follows high standards of professional ethics and ensures the compliance of its operation with legislative requirements, thus creating an ethical business environment. In order to prevent corrupt or fraudulent activities, employees are regularly informed about ethics and compliance standards and the internal regulations of the Group are continuously improved. The Group also urges its partners to comply with the same ethical principles and, when entering into contracts, it asks for confirmation that mutual cooperation will be based on the principles of fair business cooperation. The Latvenergo Group Code of Ethics and fundamental ethical principles are published on the Latvenergo website.

## Roles, Responsibilities and Accountability

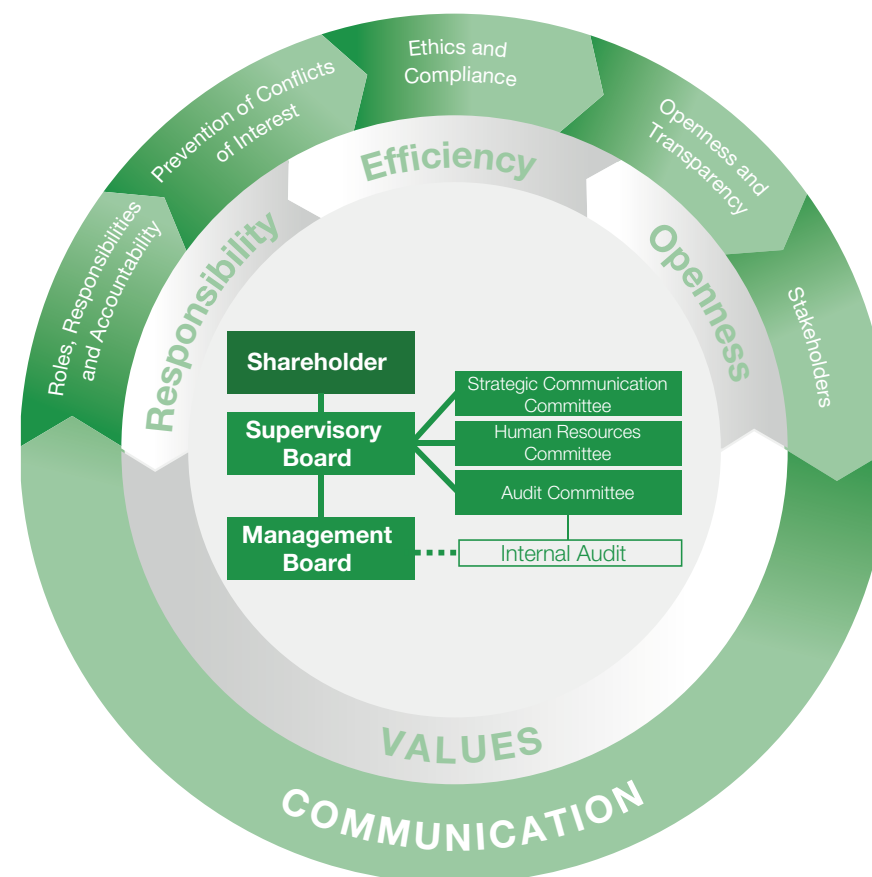
The roles, responsibilities and accountability of the governance bodies are clearly defined by laws and regulations and by the Group's internal documents. The most important of these are the companies' Articles of Association and regulations of the governance bodies, which are published on the Group's website.

## Openness and Transparency

Operational transparency is ensured through the publication of financial and non-financial information on the Latvenergo website and the Nasdaq Baltic website. The Sustainability and Annual Report and the Corporate Governance Report are published by the Group on a yearly basis. The Interim Financial Reports of the Group, Latvenergo AS and its subsidiaries are published on a quarterly basis. Virtual conferences on the Group's financial results and business developments are held every six months.

## Prevention of Conflicts of Interest

Members of supervisory boards and management boards of state capital companies have the status of public officials, which restricts their activities that fall outside the framework of their official powers in order to prevent personal or property interests in their activities. Members of supervisory boards and management boards are obliged to submit annual declarations of public officials.



The Group's Code of Ethics defines the types of conflict of interest and the measures to prevent such situations. Upon entering employment, new employees must confirm their commitment to prevent conflicts of interest within their activities. The Group organises trainings and informative events and has introduced conflict of interest declarations, which are submitted annually by employees who, as a part of their official duties, participate in decision-making.

## Stakeholders

Latvenergo Group is aware of its impact on stakeholders and vice versa and handles issues of material importance to its stakeholders with a sense of responsibility. More information on the Group's cooperation with stakeholders is provided in the section Stakeholder Engagement.

# GOVERNANCE BODIES

## SHAREHOLDER

100% of the shares of Latvenergo AS are owned by the state and held by the Ministry of Economics of the Republic of Latvia. The interests of the shareholder are represented at the Shareholder Meeting by the State Secretary of the Ministry of Economics or his/her authorised delegate. Shareholder Meetings are convened in accordance with the requirements and timelines stipulated by the Law on Governance of Capital Shares of a Public Person and Capital Companies.

The principal duties of the Latvenergo AS Shareholder Meeting include:

- approval of the Annual Report and decision-making on distribution of the company's profit from the preceding year;
- electing and dismissing members of the Supervisory Board and the Audit Committee; approval of their remuneration;
- appointment of the auditor, determining his/her remuneration.

Four Shareholder Meetings took place in 2018. The most important decisions passed in 2018 were the approval of the Annual Report 2017, distribution of dividends in the amount of EUR 156.4 million and appointment of the external auditor.

## SUPERVISORY BOARD

The Supervisory Board of Latvenergo AS Board is composed of five members and its term of office is five years. All members of the Supervisory Board are independent experts who are not engaged in the operational activities of the Group. The principal duties of the Supervisory Board include:

- approval of the medium-term operational strategy;
- continuous supervision of the Management Board's activities;
- election and dismissal of the Management Board members; approval of their remuneration;
- monitoring the compliance of the company's operations with legislation, its Articles of Association and the decisions of the Shareholder Meeting.

Ten meetings of the Supervisory Board took place in 2018. In addition to the principal duties, the following matters were reviewed:

- updating and monitoring of the Group's Strategic Development and Efficiency Programme;
- assessment of best practice in corporate governance, development of the action plan and approval of the updated Corporate Governance Policy;
- selection of the Management Board members;
- improvement of the internal control environment;
- establishment of the Strategic Communication Committee.

The Regulations of the Supervisory Board are available on the Group's website.

## Committees of the Supervisory Board

In compliance with the Regulations, the Supervisory Board of Latvenergo AS may form committees consisting of the members of the Supervisory Board for reviewing particular matters.

- *The Human Resources Committee* was established in 2017. Its tasks include ensuring the selection of the Management Board, the Audit Committee and the Internal Audit Director and evaluation of the remuneration, performance and combining of positions of the Management Board and the Internal Audit Director. Nine meetings of the Human Resources Committee were held in 2018. The Regulations of the Committee are available on the Latvenergo website.
- *The Strategic Communication Committee* was established at the end of 2018. Its tasks are to evaluate Latvenergo Group's strategic communication goals, components, costs and returns as well as the Group's stakeholder management. One meeting of the Strategic Communication Committee was held in 2018. The Regulations of the Committee are available on the Latvenergo website.

## MANAGEMENT BOARD

The Management Board of Latvenergo AS consists of five members elected by the Supervisory Board for a term of office of five years after evaluating their suitability with regard to necessary competences, experience and the intended responsibilities. The Management Board operates in compliance with the Articles of Association and the Regulations of the Management Board and reports to the Supervisory Board. All Management Board members are independent in their operation and hold no interest in the capital of cooperation partners or related companies.

The principal duties of the Management Board include:

- management and representation of the company;
- responsibility for the commercial activities of the capital company and for compliance with accounting legislation;
- management of the company's property;
- implementing the strategic direction of the Group, its development plans, goals and policies.

The Management Board members are jointly liable for compliance with all binding laws and regulations, execution of the decisions of the Shareholder Meeting and the Supervisory Board, and the financial performance of the Group.

In 2018, 68 meetings of the Management Board were held. Number of meetings attended: Ā. Žigurs (Chairman of the Management Board) – 66; G. Baļčūns – 66; U. Bariss – 65; G. Stafeckis (office held until 1 March 2018) – 10; M. Kuņickis (office held until 5 October 2018) – 46; K. Cikmačs (office held since 25 September 2018) – 20. The overall attendance rate was 97%.

As of this report's publication, the Management Board consists of four board members. The Regulations of the Management Board are available on the Latvenergo website.



## AUDIT COMMITTEE

An independent Audit Committee operates at Latvenergo AS, which reports on its operations and performance to the Supervisory Board. The Committee is composed of five members, of whom three are independent experts who are not engaged in the operational activities of the Group and two are simultaneously members of the Supervisory Board. The principal duties of the Audit Committee are to supervise:

- the financial reporting process;
- efficiency of the internal control and risk management systems;
- the work of the Internal Audit and the external auditor;
- implementation of the Fraud Risk Management Plan.

Six meetings of the Audit Committee were held in 2018. The Regulations of the Audit Committee are available on the Latvenergo website.

### Audit Committee Report

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

No restrictions have been imposed on the Committee's actions, and representatives of Latvenergo AS have ensured the availability of all necessary information. The Audit Committee has informed the members of the Management Board of its conclusions and recommendations based on the work of the Audit Committee. In 2018, the activities of the Audit Committee focused on reviewing the following issues, which are significant for the Group's operations:

- revision of the Group's risk management processes, including integration of the Group's risk assessments into the planning and execution of internal audits;
- supervision of the Fraud Risk Management Plan's implementation;
- monitoring of the operations of the Internal Audit and the external auditor, including the assessment of requests for engaging the external auditor in the provision of services that are not related to the audit.

The Audit Committee also assessed and commented on the external evaluation of corporate governance best practices and selected the Internal Audit Director.

Having assessed the information and processes reviewed during the financial year 2018, nothing has come to the Audit Committee's attention that would lead us to believe that the internal controls of Latvenergo AS do not provide a reliable basis for the preparation of the Annual Report 2018. The Committee submits the assessment summary to the Supervisory Board of Latvenergo AS in April 2019.

**Torben Pedersen**, Chairman of the Audit Committee  
**Marita Salgrāve**, Member of the Audit Committee  
**Svens Dinsdorfs**, Member of the Audit Committee  
**Andris Ozoliņš**, Member of the Audit Committee  
**Andris Liepiņš**, Member of the Audit Committee

## REMUNERATION POLICY FOR THE SUPERVISORY BOARD, THE AUDIT COMMITTEE AND THE MANAGEMENT BOARD

Remuneration of the Supervisory Board and the Management Board is regulated by the legislation of the Republic of Latvia: the Law on Governance of Capital Shares of a Public Person and Capital Companies as well as the Cabinet Regulations based on that law. The legislation provides for uniform regulation regarding remuneration of members of supervisory and management boards of the companies of a public person.

The monthly salary of the Chairman of the Supervisory Board and the Chairman of the Management Board is linked to the average monthly salary of employees in Latvia during the preceding year, as published by the Central Statistical Bureau, multiplied by a ratio specified according to the capital company's reference criteria (turnover, assets and number of employees). The maximum ratio applicable to the monthly salary of the chairman of a supervisory board is 3, and in 2018 this was applied to the monthly salary of the Chairman of the Supervisory Board of Latvenergo AS. The ratio applied to the monthly salary of the Chairman of the Management Board in 2018 was 10 based on the capital company's reference criteria.

The remuneration of supervisory board and management board members may not exceed 90% of the monthly salary of the chairman of a supervisory or management board respectively. Management board members are entitled to compensation for the performance of additional duties at the company. 20% of the uniform monthly salary of the Chairman and members of the Management Board comprises remuneration for performing the duties of Chief Executive Officer and Chief Officers.

Once a year, following the approval of the Annual Report and the performance evaluation, the Shareholder Meeting may decide on payment of bonuses to the Supervisory Board members. The amount of the bonus may not exceed the amount of their monthly salary. The Supervisory Board, in turn, may decide on payment of bonuses to the Management Board members once a year following the approval of the Annual Report. The bonuses are based on the company performance, the execution of the strategy and the achievement of the set targets. For Management Board members, bonuses may not exceed double their monthly salary. The authorisation agreements signed with the members of the Management Board provide for the possibility to receive a severance payment in the amount of three months' salary if they are recalled from their duties before the expiration of their term of office, including in the event of reorganisation or liquidation of the company. The remuneration policy does not provide for an option to pay remuneration in the form of shares or share options.

The remuneration of the Audit Committee is stipulated by the Regulations of the Audit Committee. The remuneration of the Audit Committee members is determined by the Shareholder Meeting, and its amount corresponds to the average monthly salary of employees in Latvia during the preceding year, as published by the Central Statistical Bureau of the Republic of Latvia. The monthly salaries of the Audit Committee members are determined for the entire term of their office, with the right to revise them once per year. Members of the Audit Committee who are simultaneously members of the Supervisory Board of Latvenergo AS are not compensated for duties performed in the Audit Committee.

Authorisation agreements are signed with the members of the Management Board, the Supervisory Board and the Audit Committee, and the provisions of the Collective Bargaining Agreement do not apply to them. The remuneration paid for 2018 to A. Ozoliņš, Chairman of the Supervisory Board, was EUR 33,807; for



A. Liepiņš, Deputy Chairman of the Supervisory Board, it was EUR 30,427; for M. Bičevskis, Member of the Supervisory Board, it was EUR 30,264; and for M. Sedlackis and B. A. Rubesa, Members of the Supervisory Board, it was EUR 29,754 each. The remuneration paid to each member of the Audit Committee of Latvenergo AS for the year 2018 was EUR 10,308, except for the members who are simultaneously members of the Supervisory Board. Members of the Supervisory Board committees do not receive remuneration for their work in these committees.

The aggregate remuneration for 2018 for Ā. Žigurs, Chairman of the Management Board and Chief Executive Officer, was EUR 163,794; for G. Baļčūns, Member of the Management Board and Chief Financial Officer, it was EUR 148,282; for U. Bariss, Member of the Management Board and Chief Commercial Officer, it was EUR 147,294; for M. Kuņickis, Member of the Management Board and Chief Operating Officer (office held until 5 October 2018), it was EUR 136,686; for G. Staļeckis, Member of the Management Board and Chief Technology and Support Officer (office held until 1 March 2018), it was EUR 43,129; and for K. Cikmačs, Member of the Management Board and Chief Technology and Support Officer (office held since 25 September 2018), it was EUR 31,816.

## INTERNAL AUDIT

The Internal Audit is an independent unit of Latvenergo AS and its objective is to evaluate and improve the effectiveness of internal control, risk management and corporate governance processes. Internal audits are performed in compliance with the International Standards for the Professional Practice of Internal Auditing.

The activities of the Internal Audit are supervised by the Audit Committee which also approves the annual internal audit plan. The internal audit reports on Latvenergo AS are submitted to the Audit Committee while internal audit reports on the Group's subsidiaries are submitted to the Supervisory Board of the relevant company or the Shareholder Meeting. Once a year, based on the audit results, a comprehensive opinion on the effectiveness of the Group's internal control system and recommendations for its improvement is submitted to the Management Board and the Audit Committee of Latvenergo AS.

Every year, the Internal Audit submits its activity report to the Supervisory Board, the Management Board and the Audit Committee. It comprises information on the audits carried out, assessments of the areas checked and recommendations made as well as quality assurance of the internal audit and compliance with international standards.

## DIVIDEND POLICY

The distribution of Latvenergo AS dividends is regulated by the Republic of Latvia Law on the Medium-Term Budgetary Framework for 2018, 2019 and 2020. In compliance with the regulations, the anticipated amount payable by Latvenergo AS in dividends is:

- EUR 132.9 million (including corporate income tax) in 2019;
- EUR 127.1 million (including corporate income tax) in 2020.

Latvenergo Group's capital structure ratios are sufficient to proceed with the dividend payout. The actual amount payable by Latvenergo AS in dividends is determined by the Shareholder Meeting after the approval of the Annual Report, upon evaluation of the results for the previous year.

## GOVERNANCE OF SUBSIDIARIES

Latvenergo Group subsidiaries are governed through key governance instruments such as strategy, organisational structure organised around functional units, and policies.

The activities of the Management Boards of Latvenergo AS subsidiaries Sadales tīkls AS, Latvijas elektriskie tīkli AS and Enerģijas publiskais tirgotājs AS are supervised by the Shareholder Meeting, where the interests of Latvenergo AS are represented by its Management Board. The supervisory body of the subsidiaries Elektrum Eesti OÜ and Elektrum Lietuva UAB, which operate outside the territory of Latvia, is their Supervisory Board. Latvenergo AS Management Board representatives as well as employees who are responsible for the relevant areas of operation at Latvenergo AS are appointed to the Supervisory Boards of the abovementioned subsidiaries. Supervisory functions at Liepājas enerģija SIA, where the equity share of Latvenergo AS is 51%, are carried out by a Supervisory Board of six individuals, half of whom are representatives of Latvenergo AS.

In March 2018, Sandis Jansons and Jānis Kirkovalds took office in the Management Boards of Sadales tīkls AS. During the reporting year, changes were also made in the composition of the Supervisory Board of Elektrum Lietuva UAB. In December, Arnis Kurgs left office in the Supervisory Board and Anita Kalniņa took office.



## LATVENERGO AS SUPERVISORY BOARD



**Andris Ozoliņš**

Chairman of the Supervisory Board



**Andris Liepiņš**

Deputy Chairman of the Supervisory Board



**Baiba Anda Rubesa**

Member of the Supervisory Board



**Mārtiņš Bičevskis**

Member of the Supervisory Board



**Martin Sedlacký**

Member of the Supervisory Board

<b>Term of office</b>	16.12.2016–15.12.2021	16.12.2016–15.12.2021	16.12.2016–15.12.2021	16.12.2016–15.12.2021
<b>Committee membership</b>				
Audit Committee	Audit Committee Human Resources Committee	Human Resources Committee Strategic Communication Committee (Chairman)	Human Resources Committee (Chairman) Strategic Communication Committee	
<b>Experience</b>				
2016–2018: Baltic International Bank AS, Member of the Supervisory Board 2013–2014: Reverta AS, Member of the Supervisory Board 2013–2014: Kredītinformācijas birojs AS, Member of the Supervisory Board 2010–2011: DNB Bank ASA, Member of the Management Board 1999–2012: DNB banka AS (NORD/LB Latvija AS), President and Chairman of the Management Board, Member of the Management Board 1997–1999: Irvin & Co Baltics SIA, Chief Executive Officer, Senior Consultant	2014–2016: Riga International Airport SJSC, Chairman of the Management Board 2011–2014: Air Baltic Corporation AS, Chairman of the Supervisory Board 2001–2014: Ministry of Economics, Deputy State Secretary 2002–2006: Latvenergo AS, Member of the Supervisory Board 1995–2001: Development Agency of Latvia, Member of the Management Board, Director of the Investment Department 1994–1995: Saeima, Member of Parliament, Ministry of Economics, Parliamentary Secretary 1994: Development Agency of Latvia, Member of the Management Board, Director of the Investment Department 1991–1994: Ministry of Economics, Department of External Economic Relations, Senior Specialist	2015–2018: RB Rail AS, Chairperson of the Management Board, Chief Executive Officer 2014–present: RFactor SIA, Owner and Chairperson of the Management Board 2012–2015: Citadele Banka AS, Member of the Supervisory Board 2010–2013: Statoil ASA, Vice President, Corporate Social Responsibility 2008–2010: Statoil Azerbaijan, Director, Government & Public Affairs 2002–2009: DnB NORD Banka AS, Member of the Supervisory Board 2001–2008: Latvija Statoil SIA, Managing Director 1996–2000: Statoil Baltic States, Director, Marketing & Public Affairs 1994–1996: Es un partneri SIA, Owner 1993–1993: Bell Sygma Inc., Assistant Vice President 1985–1992: Volkswagen Group, Manager of Corporate Image and Coordinator of International Public Relations	2016–present: State Real Estate SJSC, Chairman of the Supervisory Board 2012–2017: Employers' Confederation of Latvia, Vice President, Member of the Supervisory Council 2011–2016: Association of Latvian Commercial Banks, President, Member of the Board 2008–2011: Ministry of Finance, State Secretary 2004–2008: Ministry of Justice, State Secretary 2003–2004: Ministry of the Interior, Deputy State Secretary 2000–2003: Office of Citizenship and Migration Affairs, Head 1999–2000: Ministry of the Interior, Parliamentary Secretary 1999: Saeima, Member of Parliament 1999: Privatisation Agency, Member of the Supervisory Board	2012–present: Air Baltic Corporation AS, Member of the Management Board, Chief Operating Officer 2006–2012: The Boston Consulting Group (Prague and Kuala Lumpur offices), Project Manager
<b>Education</b>				
RTU Riga Business School, Master of Business Administration (2002) University of Latvia, Diploma in Philosophy (1991)	RTU Riga Business School, Master of Business Administration (2010) Columbia University in the City of New York, Master of International Relations (1997) University of Latvia, Master of Public Administration (1996) University of Latvia, Diploma in Economics (1993)	Shaw College, Degree in Business Administration (1975) York University, Bachelor of Arts (1974)	University of Latvia, Faculty of Law, Lawyer (1998)	University of Economics in Prague and Helsinki School of Economics, CEMS Master in International Management (2006) University of Economics in Prague, Engineer Degree in Economics (2006)

## LATVENERGO AS MANAGEMENT BOARD



**Āris Žigurs**

Chairman of the Management Board  
and Chief Executive Officer



**Guntars Baļčūns**

Member of the Management Board  
and Chief Financial Officer



**Uldis Bariss**

Member of the Management Board  
and Chief Commercial Officer



**Kaspars Cikmačs**

Member of the Management Board  
(since 25.09.2018)  
and Chief Technology and Support Officer

Term of office	16.11.2015–15.11.2020	16.11.2015–15.11.2020	16.11.2015–15.11.2020	25.09.2018–24.09.2023
<b>Experience</b>				
2016–present: Member of the Council of Higher Education	2016–present: Elektrum Eesti OÜ, Member of the Supervisory Board	2013–present: Latvenergo AS, Chief Commercial Officer	2018–present: Latvenergo AS, Chief Technology and Support Officer	
2015–present: Employers' Confederation of Latvia, Member of the Board	2016–present: Elektrum Lietuva UAB, Member of the Supervisory Board	2010–present: Elektrum Lietuva UAB, Chairman of the Supervisory Board	2018–present: Latvenergo AS, Member of the Management Board	
2013–present: Latvenergo AS, Chief Executive Officer	2016–present: Baltic Institute of Corporate Governance, Member of the Supervisory Board	2010–present: Elektrum Eesti OÜ, Chairman of the Supervisory Board	2010–2018: Citadeles banka AS, Member of the Management Board, Chief Operating Officer	
2011–present: RTU, Chairman of the Counsellor Convent	2015–present: Latvenergo AS, Chief Financial Officer	2005–present: Latvenergo AS, Member of the Management Board	2009–2010: Parex Banka AS, Head of Information Technologies	
2011–present: LUA, Member of the Counsellor Convent	2015–present: Latvenergo AS, Member of the Management Board	2005: Latvenergo AS, Project Director of Distribution Network Restructuring	2005–2009: Swedbank Baltic Banking, Head of IT Operations in the Baltics	
2011–present: Latvian National Committee of the World Energy Council, Vice President	2014–2015: Enerģijas publiskais tirgotājs AS, Member of the Management Board	2002–2004: Latvenergo AS, Economics Department Director	1996–2005: Hansabanka, Head of IT Monitoring in the Baltics, Head of Service Support and Monitoring, IT System Administrator	
2010–present: Latvenergo AS, Chairman of the Management Board	2005–2015: Latvenergo AS, Business Planning and Control Director, Corporate Strategy Project Manager	1996–2002: Lattelekom SIA, Head of the Financial Planning and Control Division, Head of the Management Accounting Sector		
2010–present: Eurelectric, Member of the Board of Directors				
1996–2010: Rīgas Siltums AS, President and Chairman of the Management Board				
<b>Education</b>				
RTU, Doctor of Sciences in Engineering, energy sector (2009)	RTU Riga Business School, Master of Business Administration (2016)	RTU, Doctor of Science in Engineering, Environmental Science (2017)	SSE Riga, Master of Business Administration (2012)	
RTU Riga Business School, Master of Business Administration (2004)	University of Latvia, Master of Economics (2005)	SSE Riga, Executive Master of Business Administration (2008)	INSEAD (France) Business Management (2006)	
LUA, Faculty of Engineering, engineer-mechanic (1988)	SSE Riga, Bachelor of Economics and Business Administration (2003)	University of Latvia, Master of Economics (2004)	University of Latvia, Bachelor of Computer Sciences (1999)	

### Members of the Management Board who left office in 2018



**Māris Kuņickis**

Member of the Management Board  
and Chief Operating Officer  
(until 05.10.2018)



**Guntis Stafeckis**

Member of the Management Board  
and Chief Technology and Support Officer  
(until 01.03.2018)



## LATVENERGO AS AUDIT COMMITTEE



**Torben Pedersen**  
Chairman of the Audit Committee



**Marita Salgrāve**  
Member of the Audit Committee



**Svens Dinsdorfs**  
Member of the Audit Committee

**Andris Ozoliņš**  
Member of the Audit Committee

**Andris Liepiņš**  
Member of the Audit Committee

Term of office				
03.03.2017–02.03.2020	03.03.2017–02.03.2020	03.03.2017–02.03.2020	03.03.2017–02.03.2020	03.03.2017–02.03.2020
Experience				
2015–present: Electronic House UAB, Member of the Supervisory Board	2017–present: International Organization of Supreme Audit Institutions, FIIP member	2017–present: INDEXO IPAS, Member of the Supervisory Board	Information about experience and education is available in the subsection Latvenergo AS Supervisory Board.	Information about experience and education is available in the subsection Latvenergo AS Supervisory Board.
2013–present: Vilnius International School, Shareholder Representative	2015–present: Latvenergo AS, Member of the Audit Committee	2015–present: Elko Grupa AS, Director, Member of the Management Board		
2012–present: Latvenergo AS, Chairman of the Audit Committee	2015–present: State Audit Office of the Republic of Latvia, Advisor to the Auditor General in strategic matters	2012–present: Latvenergo AS, Member of the Audit Committee		
2013–2014: Rus-Agro Team AS, Member of the Management Board	2007–2015: State Audit Office of the Republic of Latvia, Member of the Council, Director of the Fourth Audit Department	2006–2014: Elko Grupa AS, Finance Director, Member of the Management Board		
2012–present: Baltic Engineers UAB, Chairman of the Management Board	1998–2007: Central Finance and Contracting Agency, Deputy Director, Director of the Programme Management Department, Senior Procurement Specialist	2004–2006: Sirowa Riga AS, Finance Director		
2011–2016: Danish Chamber of Commerce in Lithuania, Member of the Supervisory Board	1993–1998: Ramboll AS, Project Manager	1998–2004: Air Baltic Corporation AS, Vice President of Strategic Development, Business Control Director		
2001–2010: Deloitte, Partner				
1994–2001: Arthur Andersen, Partner				
Education				
Aarhus School of Business, Master of Economics and Auditing (1974)	Sint-Aloysius School of Economics (EHSAL) (Belgium), Master of Business Administration (1998)	SSE Riga, Master of Finance and Economics (2003)		
Chartered Accountant qualification (Denmark)	University of Latvia, Faculty of Economics and Management, postgraduate qualification of an economist (accountant) (1997)	SSE Riga, Bachelor of Economics and Business Administration (1998)		
	Oxford College of Petroleum and Energy Studies, postgraduate qualification in energy and the environment (1995)			
	University of Latvia, Faculty of Chemistry, Master of Analytical Chemistry (1988)			



# GROUP MANAGEMENT

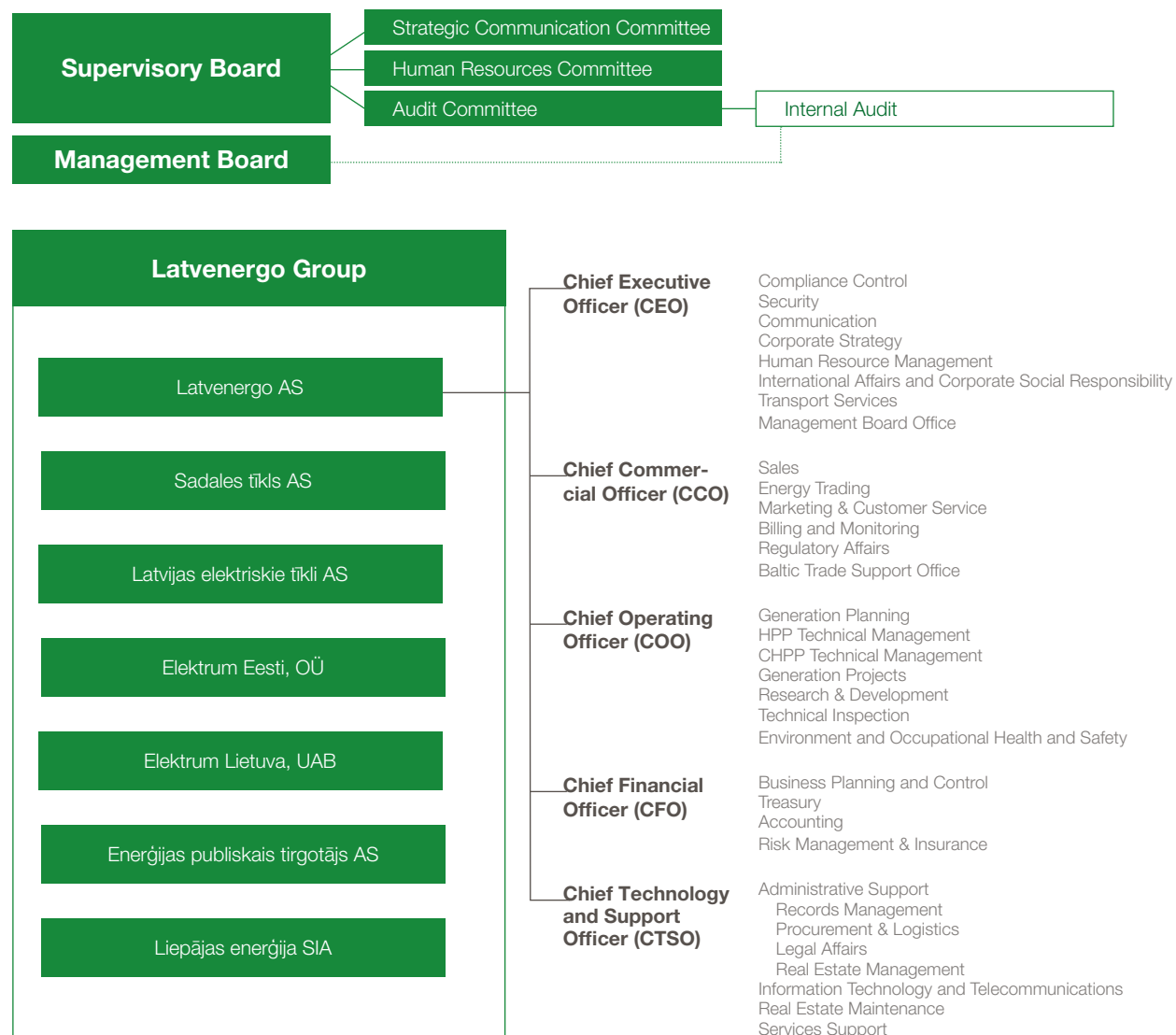
Latvenergo Group's management model is based on corporate governance best practice. In order to ensure effective Group governance, decision-making and achievement of goals, strategic and operational management are separate.

The Group's strategic management is implemented by the Management Board, whose accountability is joint according to the Commercial Law, and operational management is ensured by Chief Officers, whose accountability is individual. The main duty of the Management Board is to lead the Group in order to reach the objectives set in the strategy. At minimum, the Management Board reports to the Supervisory Board on a quarterly basis and to the Shareholder on an annual basis. Chief Officers ensure the operational management of Latvenergo AS, including goal achievement and policy implementation; they also ensure their division's cooperation with the functions of other divisions and adoption of decisions in compliance with the Group's strategy and delegation. The divisions have been established in accordance with the strategic goals of the Group.

Considering their previous experience and knowledge of the Group's operations, the duties of Chief Officers are performed by the Members of the Management Board of Latvenergo AS. The division of duties in 2018 was as follows:

- Āris Žigurs – Chief Executive Officer;
- Guntars Baļčūns – Chief Financial Officer;
- Uldis Bariss – Chief Commercial Officer;
- Kaspars Cikmačs – Chief Technology and Support Officer (from 1 October 2018; Guntis Stafeckis – until 1 March 2018);
- Māris Kuņickis – Chief Operating Officer (until 5 October 2018).

Until the new member of the Management Board and Chief Operating Officer takes office, the duties have been temporarily reorganized and Aivars Kvesko is acting as Chief Operating Officer.



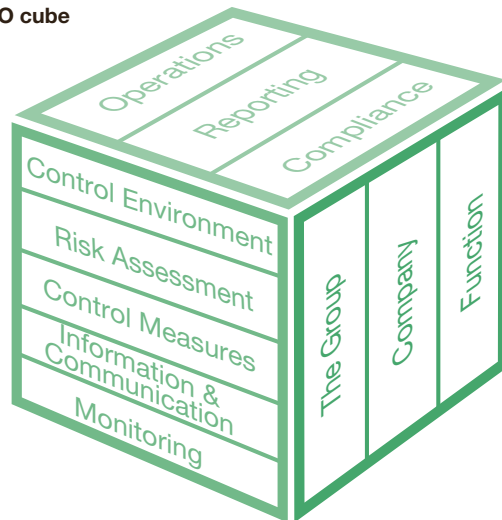
# INTERNAL CONTROL SYSTEM AND RISK MANAGEMENT

## INTERNAL CONTROL SYSTEM

To ensure the achievement of Latvenergo Group's strategic goals, successful supervision and operational efficiency, an internal control system has been introduced and is continuously improved. It has been developed taking into account the COSO (Committee of Sponsoring Organizations of the Treadway Commission) framework, which is among the internationally recognised internal control approach frameworks. Three key objectives of the internal control system are:

- efficiency of the Group's operations;
- credibility of the disclosed information;
- compliance of operations with laws and regulations.

**COSO cube**



### Efficiency of the work processes

To continue improving the competitiveness of the Group and to strengthen its position in the dynamically changing regional market, during the strategy period until 2022 an efficiency programme is being implemented, which provides for revision, centralisation and digitisation of the Group's processes.

### Reporting

Reporting includes both internal and external reports on financial and non-financial operations. Internal reports provide accurate and complete information to the Group's management for decision-making and supervision of company operations. External reports ensure that investors and other stakeholders are kept informed of the financial position of the Group and its performance.

### Compliance

The Group operates in compliance with laws and regulations. To ensure this compliance, internal regulatory documents and their compliance with external regulation are reviewed on a regular basis, potential risks are identified and evaluated, and additional controls are developed.

To achieve the above goals on the level of the Group, its subsidiaries and its divisions, the following internal control system elements are continuously improved:

- control environment;
- risk assessment;
- control measures;
- information and communication;
- monitoring.

### Control environment

The Group's management promotes business activities that are in line with the principles of good faith and comply with ethical standards; it also implements actions to prevent the risk of fraudulent conduct and corruption and to improve the control environment. Responsible persons for establishment and performance of controls are appointed on all organisational levels. To develop employee understanding of the internal control environment and processes, the Group holds regular employee trainings. The Internal Audit provides annually a comprehensive opinion on the effectiveness of the internal control and risk management system as well as recommendations for its improvement.

### Risk assessment

The Group continuously improves its risk management process to adapt to the changing business environment and market developments. The risk assessment process is increasingly integrated into all the company's governance processes. For more information on the Group's risk management process and major risks, see the section Risk Management.

### Control measures

The Group has introduced and continuously improves integrated control measures, such as the Group's governance policies, the regulations of structural units, the division of employee duties and responsibilities, etc. These are aimed at promoting strategy implementation and goal achievement by ensuring economical, productive and efficient operations compliant with ethical standards.

### Information and communication

The Group's internal information flow and control systems ensure verified, accurate and reliable information for communicating both internally and to external stakeholders. The Group's management provides regular information to employees on both long-term and short-term plans and results. The key information channels are the Intranet, the employee newsletter *Latvenergo Vēstis*, internal record-keeping systems and databases, and employee workshops. Internal opinion surveys, employee development interviews and competence assessments are carried out to ensure relevant feedback. Working groups include representatives with various skills and competencies to exchange opinions and knowledge and facilitate employee engagement in decision-making.

### Monitoring

The Group's management is responsible for regular assessment and improvement of controls. The management's performance is monitored by the Supervisory Board and the Audit Committee and checked by the Internal Audit. The external auditor issues an opinion on fairness and compliance of the audited annual financial statements with the IFRS. All the aforementioned institutions are independent in their operations.

## Supervisory institutions

Institution	Objective	Monitoring scope and tasks	Reporting
Auditor	To provide an opinion on compliance of the Group's financial statements with the IFRS	<ul style="list-style-type: none"> <li>Auditing financial statements and checking the sustainability report;</li> <li>Evaluation of accounting principles and justification of major management accounting estimates (as part of auditing financial statements).</li> </ul>	Once a year, after finalising the consolidated financial statements, the auditor reports to the Shareholder.
Supervisory Board	To represent the interests of the Shareholder in between the Shareholder Meetings and supervise the operation of the Management Board	<ul style="list-style-type: none"> <li>Supervision of the Management Board operations;</li> <li>Approval of the medium-term operational strategy of the Company;</li> <li>Evaluation of the Audit Committee work;</li> <li>Supervision of the Company's compliance with legislation, the Articles of Association and the decisions adopted by the Shareholder Meeting.</li> </ul>	At least once a year, the Supervisory Board reports to the Shareholder.
Audit Committee	To supervise the preparation of the Group's financial statements and the operation of internal control systems, thus stimulating transparency of company operations	<ul style="list-style-type: none"> <li>Supervising the preparation of financial statements;</li> <li>Supervising the effectiveness of the internal control system and risk management;</li> <li>Supervising the activities of the Internal Audit and the auditor as well as of the implementation of the Fraud Risk Management Plan;</li> <li>Ensuring the selection process of the sworn auditor.</li> </ul>	At least once a year, the Audit Committee reports on its activities and performance to the Supervisory Board.
Human Resources Committee	To ensure the supervisory functions of the Supervisory Board in the area of human resource management	<ul style="list-style-type: none"> <li>Ensuring the selection of the Management Board, the Audit Committee and the Internal Audit Director;</li> <li>Evaluation of the remuneration, performance and combining of positions of the Management Board and the Internal Audit Director.</li> </ul>	The Human Resources Committee reports on its activities and performance to the Supervisory Board.
Strategic Communication Committee	To ensure the supervisory functions of the Supervisory Board in communication with third parties	<ul style="list-style-type: none"> <li>Evaluation of the Group's strategic communication goals, costs and returns;</li> <li>Evaluation of the stakeholder management and provision of recommendations to the Supervisory Board.</li> </ul>	The Strategic Communication Committee reports on its activities and performance to the Supervisory Board.
Internal Audit	To evaluate and assist in improving the effectiveness of internal control, risk management and governance processes	<ul style="list-style-type: none"> <li>Evaluation of the effectiveness of internal control, risk management and governance processes, providing recommendations and supervising their implementation.</li> </ul>	Every quarter, the Internal Audit reports to the Audit Committee on the audits performed and the implementation of audit recommendations.

## RISK MANAGEMENT

The objective of Group's risk management is to identify significant risks in a timely manner and manage them to ensure achievement of the Group's strategic goals and minimise potential losses or harm to its reputation. Risk management is integrated in strategy development and implementation and in operational activities. In 2018, an improvement of the Risk Management Policy was initiated to determine the risk appetite or the acceptable level of risk in each area of activity and risk category.

Significant risks for the Group are divided into four categories:

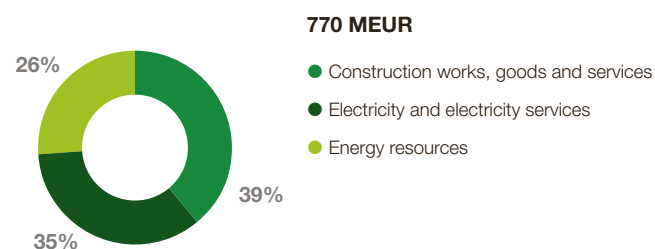
- *Strategic risks* are risks related to the implementation of strategically important capital expenditure projects, introduction of new, innovative technologies and expanding into new market and business areas. The main risk management instruments for this category are monitoring change and development trends in the energy sector and the political environment, participating in developments that affect the Group's operational aspects, and evaluating and implementing necessary changes in the Group;
- *Operational risks* are risks related to energy generation and ensuring the functionality of power plants and energy distribution. Operational risks are also associated with loss of assets, human health and safety, information technologies, environmental impact and other issues. These risks arise from imperfect or insufficiently effective processes and systems, employee errors or insufficient competence, damage to equipment or external events. The main risk management instruments for this category are maintenance of the internal control system and its continuous improvement as well as the use of insurance services;
- *Financial risks* include market risk, credit risk, liquidity and cash flow risk as well as tax and financial reporting risks. In its financial risk management, the Group uses fixed price supply contracts with customers, electricity derivatives, natural gas supplies at fixed prices, balanced placement of financial assets and instruments, and other risk management measures. Cash flow risk is restricted by obtaining funding in a timely manner and using the credit facilities granted by banks.
- *Legal and compliance risks* are risks arising from laws and regulations of the EU and the Republic of Latvia. The main risk management instruments for this risk category are monitoring changes and development trends in the legal environment that apply to the Group's operations, participation in the development process of new regulatory documents and implementation of necessary changes in the Group;
- *Fraud and corruption risks* involve the likelihood that an employee or a group of employees act intentionally to serve their own interests or interests of another person, gaining undue benefits and causing financial or reputational damage to the Group. To minimise the likelihood of such actions, the Group has a ban on accepting and offering gifts (except for things of insignificant material value) and a ban on combining of positions (except in cases where the employer's written consent has been received). An important instrument for managing this risk is the regular training of employees on issues of ethics, prevention of conflicts of interest, and prohibiting fraud and corruption.

Significant risks identified by the Group are analysed in internal working groups and in the Risk Management Committee, which is a specially established institution on the level of the Management Board of Latvenergo AS. Within the analysis, the probability and impact of a risk is evaluated, critical controls are identified, risk mitigation measures are developed, and the implementation of critical controls and risk mitigation measures is supervised. Any risks identified are conveyed to the internal audit system, thus allowing the risk assessment to be used for planning the activities of the Internal Audit.

# GROUP PROCUREMENT

For its operations, Latvenergo Group procures electricity, energy resources and various types of construction work, goods and services. Most of the Group's procurement comes from suppliers and service providers in the Baltics and the Nordic countries. The total number of suppliers exceeds 3.5 thousand.

## Types of procurement in 2018



The Group's procurement process complies with the legislation of the EU and the Republic of Latvia and the regulations of the countries in whose territory the Group carries out its commercial activity. The key principles of the Group's procurement are based on the requirements of Directives 2014/24/EU and 2014/25/EU of the European Parliament and the Council and those of the Law on Procurement of Public Service Providers of the Republic of Latvia. The Group is committed to ensuring the most efficient use of funds and, in selecting suppliers, ensures competition and fair and equal treatment and follows the principle of transparency of procurement. To ensure procurement efficiency, the Group has established a qualification system for suppliers of construction work and services, aimed at selecting and maintaining a list of qualified suppliers. The introduction of digital technologies also contributes to the openness and efficiency of the Group's procurement.

Latvenergo Group encourages its contractual partners to comply with comparable principles of ethics and, upon signing agreements, asks its partners to provide declarations of adherence to good faith principles of cooperation. The ethical principles for cooperation with contractual partners are published on the Group's website.

The Group regularly informs its business partners about planned investment projects and surveys its current and potential business partners to identify areas of cooperation where improvement is needed.

In procurement procedures, the Group follows the principles of green procurement where possible and economically feasible.

## Procurement of construction work, goods and services

In 2018, Latvenergo Group's costs for construction work, goods and services amounted to approximately EUR 300 million. Investment in both reconstruction of existing assets and construction of new ones accounts for the largest share of these costs. In 2018, the Group made investments amounting to EUR 220.6 million. To ensure high-quality power network service, technical indices and security of operations, a considerable amount of investment was made in network modernisation, accounting for 80% of the total investment. The Group is also continuing reconstruction of the hydropower units of the Daugava HPPs, where EUR 21.1 million was invested in the reporting year.

The other costs related to the procurement of construction work, goods and services consist of procuring materials, repair work and various services. The expenses of Latvenergo AS and Sadales tīkls AS account for more than 90% thereof.

## Procurement of electricity

The total costs of electricity procurement amounted to approximately EUR 270 million, including the costs of ancillary electricity services and electricity future transactions performed to reduce price risks. The Group sells all the electricity it generates and at the same time procures electricity for its customers on the Nord Pool power exchange, thus ensuring full transparency of procurement.

### Purchased electricity

	Units	2014	2015	2016	2017	2018
Purchased electricity	GWh	5,590	4,701	4,081	3,544	4,020

The electricity procurement process is targeted at cost optimisation and provides economic benefits to both Latvenergo Group and its customers. Generation volumes of the Latvenergo AS CHPPs and Daugava HPPs are linked to economically equivalent volumes of customer portfolios, thus achieving cost-effectiveness while excluding internal price risks between sale and purchase transactions. The Group's customer portfolio can be made larger than its generation volumes by including additional electricity financial instruments in the price risk management and making use of the flexibility of the Group's generation assets, switching strategically between electricity supply sources: the power exchange and the Group's own power plants. This way, Latvenergo Group is able to fulfil the profit potential of sales of the electricity generated, utilise possibilities to reduce the cost of procuring electricity necessary for customers and reduce its exposure to market price fluctuation risks.



## Procurement of energy resources

The energy resource procurement of the Group comprises natural gas, woodchips and diesel fuel. In 2018, its costs amounted to approximately EUR 200 million. The Latvenergo AS CHPPs accounted for more than 95% of fuel costs. Natural gas makes up the largest share of these expenses. It is used as the primary fuel by the CHPPs and as one of the fuel sources by the Liepāja plants. Since 2017, the Group has organised natural gas supplies to the CHPPs independently through wholesale purchases of natural gas. Liepājas enerģija SIA buys natural gas from Latvijas Gāze AS.

### Fuel consumption

	Units	2014	2015	2016	2017	2018
Natural gas*	thsd. nm <sup>3</sup>	517,119	569,004	598,425	465,947	667,256
Wood chips	loose m <sup>3</sup>	233,786	216,645	232,792	255,352	252,534
Diesel fuel	m <sup>3</sup>	111	120	18	12	10

\* as of 2017, also includes the volume of natural gas sold

In 2018, Latvenergo Group consumed 43% more natural gas than in the previous year. Consumption of natural gas depends on the demand for thermal energy and the electricity market conditions. Due to dry weather, power generation at hydropower plants both in Latvia and throughout the Nord Pool region was significantly lower, and this lack of capacity was offset by an increase in electricity generation at the CHPPs.

To ensure the reliability of thermal energy supply in situations where the supply of natural gas is interrupted, the CHPPs store backup fuel reserves of diesel. The boiler house of Liepājas enerģija SIA also uses diesel. Procurement of diesel fuel accounts for an insubstantial share of the overall costs of energy resources.

The Liepāja plants mainly use a renewable energy source, woodchips, which accounted for approximately 2% of the total energy resource costs in 2018.

Like all other goods and services, woodchips and diesel fuel are procured under the conditions of free competition.



# STAKEHOLDER ENGAGEMENT

The operation of Latvenergo Group affects a broad range of stakeholders which are identified, evaluated and grouped taking into account the GRI guidelines and the AA1000 Stakeholder Engagement Standard. The Group recognises and assesses the social, environmental and economic impact of its activities and engages stakeholders in addressing issues of mutual interest. Cooperation with stakeholders takes place at different levels:

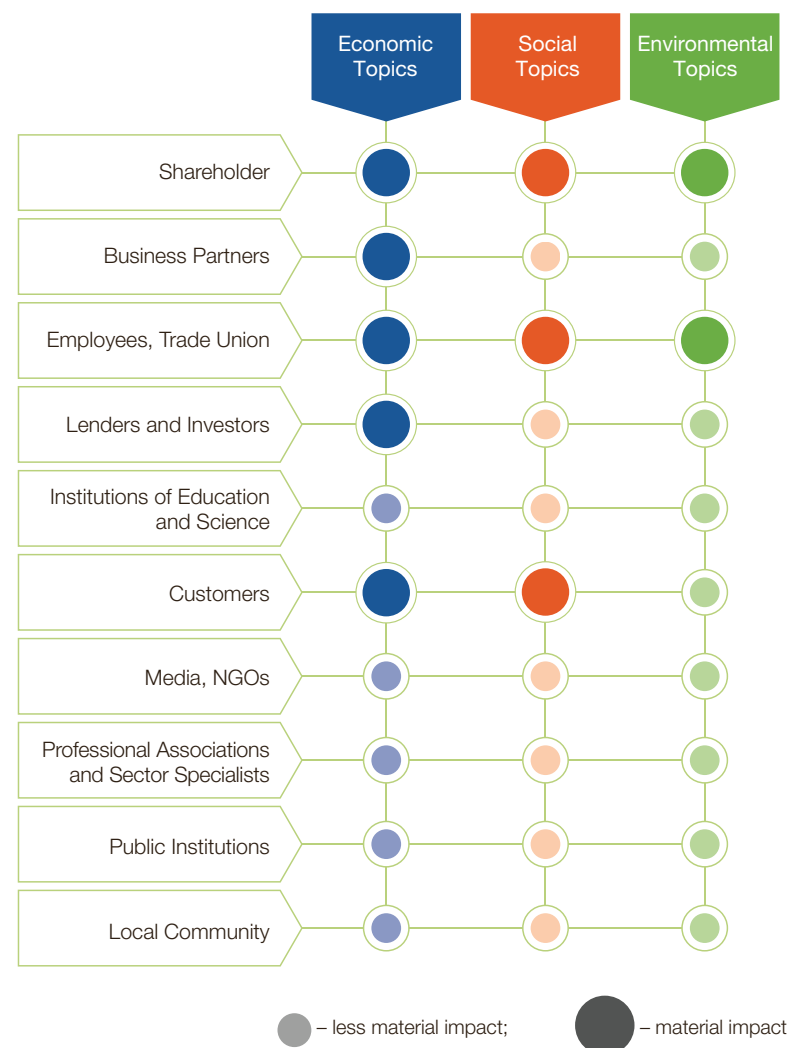
- consultation – identification of current issues;
- negotiation – participatory discussions;
- involvement – exchange of opinion without joint decision-making and cooperation;
- collaboration – joint decision-making and cooperation.

Continuing the practice started in 2015, the Group organised the second seminar for stakeholders in 2018 to find out their views on the cooperation so far and on aspects relevant to the sustainability of the Group. 60 recommendations for improvement were received at the seminar. Many of the recommendations are already being implemented by the Group, while those that are in line with the Group's objectives, but are not yet being implemented, are expected to be put into practice in the future. Some examples are creating a section dedicated to the media on the Latvenergo website, developing methods that allow for working in the medium-voltage network without voltage disconnection for the customer, and creating a digital map with up-to-date information about clearance work on electricity line routes and investment projects.

For more information on the sustainability aspects jointly defined by stakeholders and the Group, see the section Materiality Assessment.



**Mutual impact between Latvenergo Group and its stakeholders**



## List of stakeholders

Stakeholder	Representatives	Material issues / sustainability aspects	Engagement description	Level of engagement
Shareholder	Ministry of Economics of the Republic of Latvia	<ul style="list-style-type: none"> <li>• The Group's contribution to the national economy;</li> <li>• The Group's strategy, governance, investments and performance;</li> <li>• Compliance with the requirements of laws and regulations and fair competition.</li> </ul>	See the section Governance Bodies.	Collaboration
Business Partners	Construction companies, suppliers and service providers, energy generators and traders, transmission system operators	<ul style="list-style-type: none"> <li>• Clear and transparent procurement tenders; compliance with laws and regulations and fair competition;</li> <li>• Investments planned by the Group;</li> <li>• Efficiency, availability and security of distribution services.</li> </ul>	See the section Group Procurement.	Involvement
Employees, Trade Union	Existing and potential employees, trade union <i>Enerģija</i>	<ul style="list-style-type: none"> <li>• Occupational health and safety;</li> <li>• Collective Bargaining Agreement;</li> <li>• Involvement, development, productivity and motivation of employees.</li> </ul>	See information on employees and the working environment in the section Social Aspects.	Negotiation and involvement
Funders and Investors	Banks, European Commission (EC), bondholders	<ul style="list-style-type: none"> <li>• The Group's financial results, significant events, compliance with laws and regulations and agreements;</li> <li>• Fair competition; transparent and ethical marketing and communication practice.</li> </ul>	See information on openness and transparency in the section Corporate Governance Model.	Consultation and collaboration
Institutions of Education and Science	Academic institutions, institutions of higher, secondary and vocational education	<ul style="list-style-type: none"> <li>• Involvement of the Group in the development of educational programmes meeting the requirements of the labour market and involvement of the Group's experts in educational programmes;</li> <li>• Science and education projects; educational materials for children and youth.</li> </ul>	See information on science and education projects in the section Corporate Social Responsibility.	Collaboration
Customers	Current and potential customers (households and legal entities)	<ul style="list-style-type: none"> <li>• Products, services, their quality and price;</li> <li>• Reducing the frequency and duration of unscheduled power outages;</li> <li>• Availability of information.</li> </ul>	See the section Trade and Product Responsibility.	Involvement
Media, Non-Governmental Organisations (NGOs)	Journalists, NGOs	<ul style="list-style-type: none"> <li>• Availability of information on the Group's core operations and governance;</li> <li>• Current issues in energy sector policy;</li> <li>• Compliance with laws and regulations and fair competition.</li> </ul>	Cooperation with national and regional media includes press releases, media events and press conferences. The main topics are the Group's financial and operating results, current developments in the electricity market, cooperation with responsible authorities during the spring floods and development of smart technologies. The Group regularly provides information on its activities and answers questions from journalists on its website and social media. The Group also provides NGOs with information related to its core operations.	Consultation and involvement

Stakeholder	Representatives	Material issues / sustainability aspects	Engagement description	Level of engagement
Professional Associations and Sector Specialists	See the section Representation at Associations, Organisations and Unions	<ul style="list-style-type: none"> <li>• Efficiency of generation facilities and involvement in shaping the energy sector policy;</li> <li>• Compliance with laws and regulations and fair competition;</li> <li>• Community contribution;</li> <li>• Availability of information.</li> </ul>	Representatives of the Group regularly discuss the issues of energy and development of related sectors at various forums, conferences, seminars and working groups with sector experts. The most significant events in which the Group's representatives participated in 2018 include the forum Energy Sector on the Threshold of Change and Challenge, the conferences Energy Efficiency 2018 and Energy 2018, and the European Conference on Power Electronics of the European Power Electronics and Drives Association in Riga. During the reporting year, the Group also organised a discussion forum with local and international industry experts to promote the development of innovative areas of activity within the Group.	Consultation and involvement
Public Institutions	Ministry of Economics of the Republic of Latvia, Public Utilities Commission (PUC), Competition Council, Ministry of Environmental Protection and Regional Development, Procurement Monitoring Bureau, etc.	<ul style="list-style-type: none"> <li>• Development of Latvian and EU energy policies;</li> <li>• Efficiency of energy generation facilities and contingency management plans</li> <li>• Compliance with laws and regulations and fair competition;</li> <li>• Data security.</li> </ul>	In compliance with the procedure provided for by laws and regulations, the Group cooperates with the Competition Council and provides regular information on its operations, financial results and calculation of the MP components to the PUC. In 2018, the Group organised a seminar to discuss current procurement issues with the management of the Procurement Monitoring Bureau. Information on the Group's involvement in shaping the energy sector policy is available in the section Society.	Consultation and involvement
Local Community	Residents of Latvia, local governments, residents in the vicinity of the Group's facilities	<ul style="list-style-type: none"> <li>• Modernisation of generation facilities and network development projects; efficiency and availability of distribution services;</li> <li>• Compliance with environmental protection requirements;</li> <li>• The Group's CSR activities.</li> </ul>	<p>The Group cooperates with local governments on environmental impact assessment of the modernisation projects of the Group's facilities, while Sadales tīkls AS regularly informs local governments about the improvements in electricity supply and the planned electricity network renovation projects. Every spring, regular interinstitutional meetings are held to secure the preparedness of responsible services, institutions and local governments and their action during the spring flood period in the Daugava River basin.</p> <p>The Group engages the local community in discussing the modernisation projects of the Group's facilities, regularly surveys the opinion of Latvian residents through various opinion polls and implements a wide range of social responsibility activities. Their description is available in the section Corporate Social Responsibility.</p>	Consultation, involvement and negotiation

GRI 102-12

## OTHER INITIATIVES

The environment, energy efficiency and social responsibility are important topics for the sustainability of Latvenergo Group. Therefore, in addition to the provisions of laws and regulations, the Group complies with the requirements of international standards in its operations, which demonstrate to customers and other stakeholders that the Group follows a systematic approach in maintaining and improving its performance.

In order to promote the efficient use of energy sources and to ensure compliance with the requirements of Latvian and EU legislation related to energy efficiency, Latvenergo AS and Liepājas enerģija SIA have implemented and certified an energy management system in compliance with the international standard ISO 50001. The energy management principles of Sadales tīkls AS are integrated into its certified environmental management system.

Integrated management systems have been introduced and certified in the Latvenergo AS generation segment and at Sadales tīkls AS. These systems cover environmental management, quality management and labour protection and comply with the requirements of ISO 14001, ISO 9001, and OHSAS 18001 respectively. In the generation segment, project management has also been certified within the quality management system. An environmental management system has been implemented in all operating areas of Latvenergo AS and Liepājas enerģija SIA. In 2018, the occupational health and safety management system was expanded and implemented in all operating areas of Latvenergo AS. The subsidiaries Latvijas elektriskie tīkli AS and Liepājas enerģija SIA have certified and maintain quality management systems compliant with ISO 9001.

In cooperation with stakeholders, Latvenergo Group voluntarily integrates activities into its operations to improve public welfare and the environmental situation, following the principles of the ISO 26000 Social Responsibility Standard and the AA1000 Stakeholder Engagement Standard.



## REPRESENTATION AT ASSOCIATIONS, ORGANISATIONS AND UNIONS

Participation in national associations and professional organisations as well as international organisations and unions ensures representation of the interests of Latvenergo Group at the national and international level, including provision of information on current developments in the energy sector and related sectors and the possibility to participate in the development of policy documents, legislation and standards.

### International Organisations and Unions



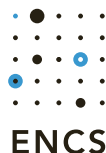
Baltic Institute of Corporate Governance



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



Union of the Electricity Industry – Eurelectric



European Network for Cyber Security



European Distribution System Operators' Association for Smart Grids



Organization for Economic Cooperation and Development, Business and Industry Advisory Committee

### National Associations and Professional Organisations



Latvian Association of Power Engineers and Energy Constructors



Latvian Association of Large Dams



Institute for Corporate Sustainability and Responsibility



World Energy Council, Latvian National Committee



Latvian Employers' Confederation



Latvian Chamber of Commerce and Industry



Latvian Association of Heat Supply Companies



**OPERATING  
SEGMENTS**

## Operating segments of Latvenergo Group



### Generation and Trade

Generation of electricity and thermal energy, electricity and natural gas trade in the Baltic states, and administration of the mandatory electricity procurement process in Latvia.



### Distribution

The distribution service ensures the flow of electricity from the transmission network to consumers. Sadales tīkls AS is the country's largest distribution system operator and covers approximately 99% of the territory of Latvia.

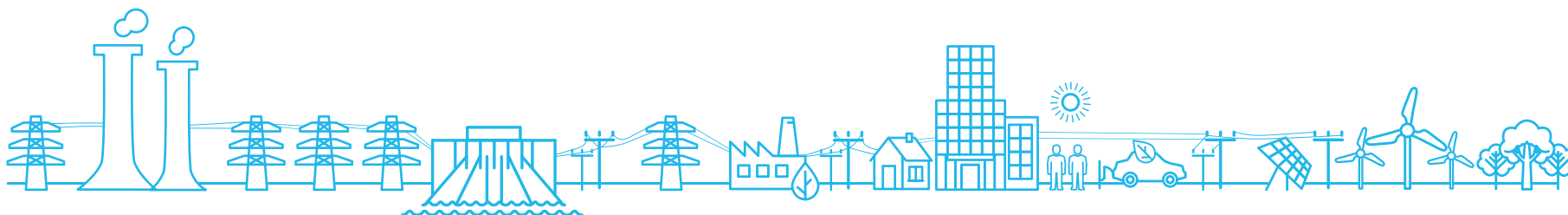
Distribution system service tariffs are approved by the Public Utilities Commission (PUC).



### Transmission

Leasing transmission system assets (330 kV and 110 kV electricity transmission lines, substations and distribution points) to the transmission system operator.

The lease payment for the transmission assets is calculated in compliance with the methodology approved by the PUC.



# GENERATION AND TRADE

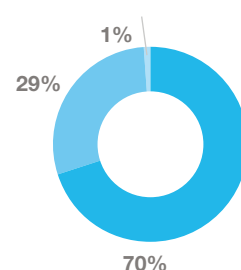
Generation and trade is the largest operating segment of Latvenergo Group in terms of both revenue and EBITDA value. In 2018, the majority or 85% of the segment's revenue was comprised of electricity and natural gas trade revenue, while thermal energy revenue accounted for 15%. The majority of generation and trade segment revenue is unregulated, while tariff-regulated operational revenue comprises revenue from:

- payment for the installed electrical capacity and generation of thermal energy at the Latvenergo AS CHPPs;
- generation of electricity and thermal energy at the Liepaja generation facilities and Aiviekste HPP.

In 2018, the Group generated more than 5 TWh or 51% of the total amount of electricity sold. 47% of the amount generated comes from renewable energy sources. Due to smaller output by the Daugava HPPs, the amount of electricity produced in 2018 decreased by 11%. The Latvenergo AS CHPPs, whose output increased by 87%, played a particularly important role in meeting electricity demand. For more information, see the section Generation.

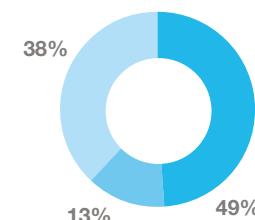
With a 25% market share, Latvenergo Group is one of the largest electricity traders in the Baltics. In the reporting year, the total amount of electricity sold, including auxiliary consumption, was more than 10 TWh, while the amount of natural gas consumed by the Group and sold to customers was around 7 TWh. 54% of the electricity sold in the retail trade was generated from renewable energy sources. For more information, see the section Trade.

**Latvenergo Group electricity balance sheet in 2018\***



**10,435 GWh**

- Retail electricity supply and operating consumption
- Wholesale electricity supply
- Technological electricity consumption



**10,435 GWh**

- Gross electricity generation
- Electricity procured within the MP scheme\*\*
- Purchased electricity

**Latvenergo Group electricity balance sheet\***

	Units	2014	2015	2016	2017	2018
Retail electricity supply and operating consumption	GWh	8,800	7,961	7,666	7,259	7,281
<i>incl. retail electricity supply</i>	GWh	8,800	7,961	7,666	6,923	6,954
Wholesale electricity supply	GWh	1,562	1,907	2,474	3,448	3,030
Technological electricity consumption	GWh	89	95	105	91	124
<b>TOTAL</b>	<b>GWh</b>	<b>10,451</b>	<b>9,963</b>	<b>10,245</b>	<b>10,798</b>	<b>10,435</b>
Gross electricity generation	GWh	3,625	3,882	4,707	5,734	5,076
Electricity procured within the MP scheme**	GWh	1,235	1,380	1,457	1,520	1,339
Purchased electricity	GWh	5,590	4,701	4,081	3,544	4,020
<b>TOTAL</b>	<b>GWh</b>	<b>10,451</b>	<b>9,963</b>	<b>10,245</b>	<b>10,798</b>	<b>10,435</b>

\* the amount of electricity generated at the Group's facilities, which has been traded and procured on the electricity exchange for auxiliary consumption purposes, is not included in the Group's electricity balance sheet

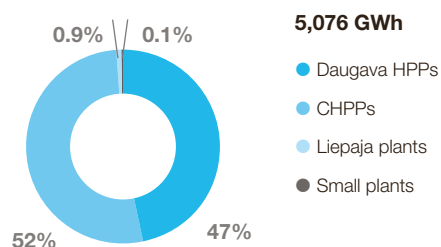
\*\* excluding electricity generated by the Group



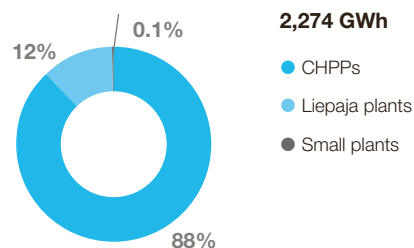
## GENERATION

Latvenergo Group has a balanced and environmentally friendly energy generation portfolio, consisting mostly of hydropower plants and highly efficient combined heat and power plants. Most of the electricity and thermal energy is generated by the three Daugava hydropower plants (HPPs) and two combined heat and power plants (CHPPs) of Latvenergo AS. Energy is also generated by Liepājas enerģija SIA, Aiviekste HPP and Ainazi Wind Power Plant (WPP). The total installed electrical capacity at the Group's generation facilities is 2,591 MW and the thermal capacity is 1,838 MW. In 2018, approximately 5 GWh of electricity and 2.3 GWh of thermal energy were generated.

### Electricity output in 2018



### Thermal energy output in 2018



### Installed electrical capacity of generation facilities

	Units	2014	2015	2016	2017	2018
Daugava HPPs	MW	1,536	1,536	1,536	1,550	1,558
CHPPs*	MW	1,025	1,025	1,025	1,025	1,025
Liepaja plants	MW	6	6	6	6	6
Small plants	MW	2	2	2	2	2
<b>TOTAL</b>	<b>MW</b>	<b>2,569</b>	<b>2,569</b>	<b>2,569</b>	<b>2,583</b>	<b>2,591</b>

\* installed capacity when CHPP-2 is in condensation mode

### Installed thermal energy capacity of generation facilities

	Units	2014	2015	2016	2017	2018
CHPPs	MW	1,617	1,617	1,617	1,617	1,617
Liepaja plants	MW	223	223	221	221	221
Small plants	MW	4	4	4	4	0
<b>TOTAL</b>	<b>MW</b>	<b>1,844</b>	<b>1,844</b>	<b>1,842</b>	<b>1,842</b>	<b>1,838</b>

### Electricity output

	Units	2014	2015	2016	2017	2018
Daugava HPPs	GWh	1,925	1,805	2,449	4,270	2,380
CHPPs	GWh	1,648	2,025	2,206	1,411	2,644
Liepaja plants	GWh	48	48	47	48	48
Small plants	GWh	4	3	5	5	4
<b>TOTAL</b>	<b>GWh</b>	<b>3,625</b>	<b>3,882</b>	<b>4,707</b>	<b>5,734</b>	<b>5,076</b>

### Thermal energy output

	Units	2014	2015	2016	2017	2018
CHPPs	GWh	2,308	2,175	2,417	2,349	2,004
Liepaja plants	GWh	248	229	253	258	267
Small plants	GWh	5	4	5	5	3
<b>TOTAL</b>	<b>GWh</b>	<b>2,560</b>	<b>2,408</b>	<b>2,675</b>	<b>2,612</b>	<b>2,274</b>

## Daugava HPPs

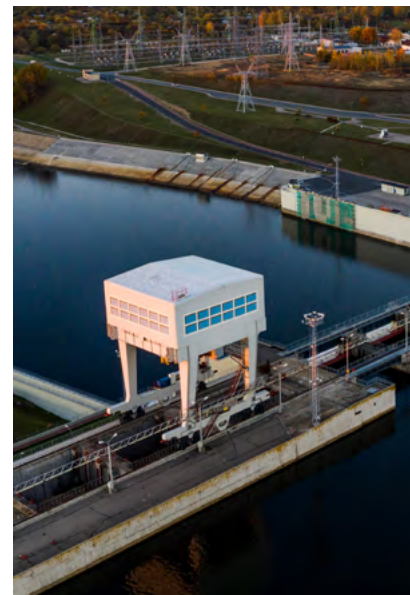
The Daugava HPPs are the biggest hydropower plants in the country, providing a large share of renewable energy not only in the Group, but also in Latvia as a whole.

The ability of the Daugava HPPs to generate electricity depends on the water inflow in the Daugava River. In years with normal inflow levels, the HPPs can operate at full capacity during the spring flooding season, which lasts for about one to two months annually. During this period, the water volume may exceed water inflow during low water periods (mainly during the summer months) more than ten times. During the spring flooding, it is possible to cover the demand for electricity of all Latvenergo Group's customers and trade the excess on the Nord Pool exchange. Outside the flooding season, the Daugava HPPs provide for the possibility to accumulate water and generate electricity when the demand and prices on the exchange are higher.

In 2018, the Daugava HPPs generated nearly 2.4 TWh of electricity, which constituted 47% of the Group's total electricity output. The electricity generation in 2018 was 44% lower than in the previous year due to significantly lower water inflow in the Daugava River.

In the reporting year, investments in the Daugava HPPs' assets amounted to EUR 24.4 million, including EUR 21.1 million invested in the programme for the reconstruction of hydropower units, which will ensure their operation at least for the next 40 years. The programme provides for the reconstruction of 11 hydropower units, of which four have already been modernised. The reconstruction process is scheduled for completion in 2022, and the total cost of the programme is expected to exceed EUR 200 million.

Replacement of outdated hydro turbines contributes to an increase in their capacity, efficiency rate and electricity output. This promotes reliable, efficient and competitive operations of the Daugava HPPs within the overall energy system and in the electricity market. More efficient use of water resources mitigates the negative impact of the Group on climate change. Each megawatt hour of electricity generated by the Daugava HPPs reduces CO<sub>2</sub> emissions by 0.345 t/MWh, assuming that this energy would otherwise be generated in condensation mode at combined heat and power plants by using natural gas as fuel.



### Kegums HPP

Start of operations: 1939  
Capacity: 248 MW  
Hydropower units: 7  
Energy source: water

Kegums HPP is the oldest Daugava hydropower plant. It consists of two separate power plants built at different times on the right and left banks of the Daugava River.

### Plavinas HPP

Start of operations: 1968  
Capacity: 908 MW  
Hydropower units: 10  
Energy source: water

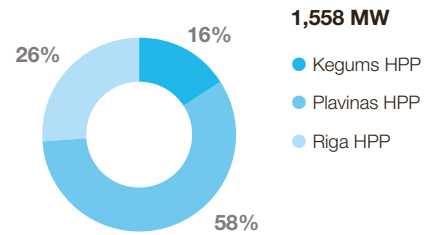
Plavinas HPP is the largest hydropower plant by installed capacity in the Baltic states and one of the largest in the European Union. It plays an important role in ensuring the stability of the Baltic power system in the event of unplanned outages or accidents at base plants. Plavinas HPP also serves as a synchronous compensator for voltage regulation in high voltage electricity networks.

### Riga HPP

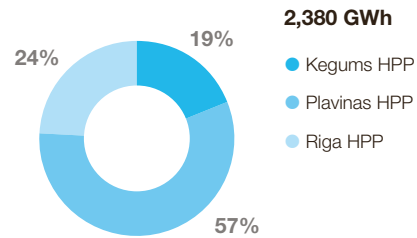
Start of operations: 1974  
Capacity: 402 MW  
Hydropower units: 6  
Energy source: water

Riga HPP is the newest of the Daugava hydropower plants. It also serves as a synchronous compensator for voltage regulation in high voltage electricity networks.

#### Installed electrical capacity at Daugava HPPs in 2018



#### Electricity output at Daugava HPPs in 2018

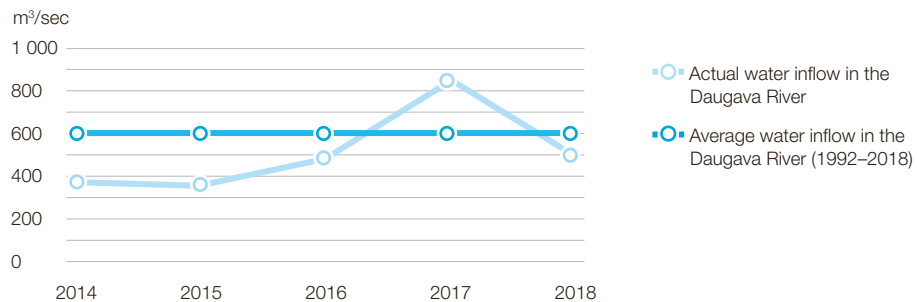


#### Electricity output at Daugava HPPs

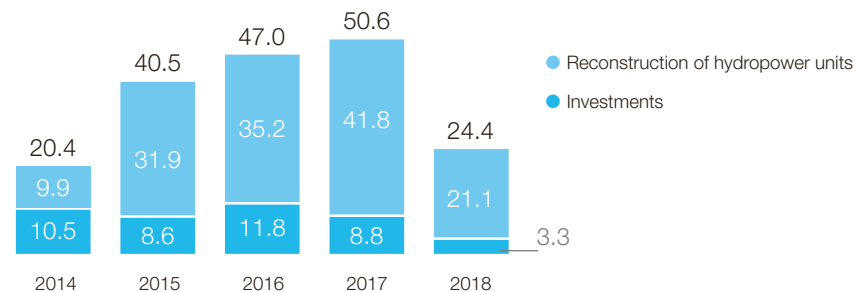
	Units	2014	2015	2016	2017	2018
Kegums HPP	GWh	376	350	475	825	457
Plavinas HPP	GWh	1,089	1,022	1,386	2,429	1,359
Riga HPP	GWh	460	433	588	1,016	564
<b>TOTAL</b>	<b>GWh</b>	<b>1,925</b>	<b>1,805</b>	<b>2,449</b>	<b>4,270</b>	<b>2,380</b>

#### Water inflow in the Daugava River

Source: Latvian Environment, Geology and Meteorology Centre



#### Investments in Daugava HPPs



## Latvenergo AS CHPPs

The upgraded CHPPs of Latvenergo AS are mostly operated in the highly efficient cogeneration mode in accordance with the thermal energy demand which in turn depends on weather conditions and the duration of the heating season. Electricity generation at the CHPPs is also influenced by market conditions like the electricity demand and the price for natural gas and CO<sub>2</sub> allowances.

The operation of Latvenergo AS CHPPs can be flexibly adjusted to the electricity market conditions and guarantees a significant baseload electricity capacity for Latvia. Both CHPPs can cover Latvian electricity consumption almost completely in circumstances where, due to certain factors, electricity imports from foreign countries are limited. In 2018, both plants played a very important role in meeting the demand for electricity, as dry weather conditions significantly reduced the water energy output both in Latvia and throughout the Nord Pool region, and capacity shortages were observed in regional interconnections. In the reporting year, the CHPPs generated about 2.6 TWh of electricity. This is 87% more than in the previous year and accounts for 52% of the Group's total electricity output.

The amount of thermal energy generated by CHPP-1 and CHPP-2 in 2018 was 2 TWh, a 15% decrease compared to the previous year. The drop was due to the increase in competition in the thermal energy market: four new heat producers started operating in the thermal energy zones of Latvenergo AS at the end of 2017 and at the beginning of 2018. The thermal energy generated is sold to Rīgas siltums AS at regulated tariffs.



### CHPP-1

Start of operations: 1958  
Electrical capacity: 144 MW

Thermal capacity: 493 MW  
Energy source: natural gas

CHPP-1 was completely reconstructed in 2005. Two gas turbines, one steam turbine and three water boilers are operated at the plant.



### CHPP-2

Start of operations: 1973  
Electrical capacity:  
832 MW (in cogeneration mode);  
881 MW (in condensation mode)  
Thermal capacity: 1124 MW  
Energy source: natural gas

Reconstruction of two power units was carried out from 2006 to 2013. Currently, Riga CHPP-2 is the most efficient and advanced combined-cycle power plant in the Baltics. Two combined-cycle gas turbine units and five water boilers are operated at the plant.

### Electricity output at CHPPs

	Units	2014	2015	2016	2017	2018
CHPP-1	GWh	487	464	613	595	643
CHPP-2	GWh	1,161	1,561	1,593	816	2,001
<b>TOTAL</b>	<b>GWh</b>	<b>1,648</b>	<b>2,025</b>	<b>2,206</b>	<b>1,411</b>	<b>2,644</b>

### Thermal energy output at CHPPs

	Units	2014	2015	2016	2017	2018
CHPP-1	GWh	966	978	1,110	1,195	1,105
CHPP-2	GWh	1,342	1,197	1,307	1,154	899
<b>TOTAL</b>	<b>GWh</b>	<b>2,308</b>	<b>2,175</b>	<b>2,417</b>	<b>2,349</b>	<b>2,004</b>

### Investments in CHPPs of Latvenergo AS

	Units	2014	2015	2016	2017	2018
Investments	MEUR	11.0	15.0	11.3	22.5	2.5



## “Liepājas enerģija” and Small Plants



### Liepāja plants

Liepājas enerģija SIA was founded in 2005  
Electrical capacity: 6 MW  
Thermal capacity: 221 MW  
Energy source: natural gas, woodchips

Latvenergo AS holds a 51% share in Liepājas enerģija SIA. The company ensures generation, transmission, distribution and supply of thermal energy in the city of Liepāja as well as generation of electricity in cogeneration mode. In 2018, the Liepāja plants generated 267 GWh of thermal energy and 48 GWh of electricity. Four heat pipeline sections with a total length of 1.5 km have been reconstructed in Liepāja with co-financing from the EU Cohesion Fund.



### Ainazi WPP

Start of operations: 1995  
Electrical capacity: 1 MW  
Energy source: wind

In 2013, full renovation of both generators was completed. In 2018, 1.3 GWh of electricity were generated at Ainazi WPP.



### Aiviekste HPP

Renovated: 1994  
Electrical capacity: 0.8 MW  
Energy source: water

Aiviekste HPP was the first hydropower plant in Latvia; it started generating electricity back in 1925. In 2018, 2.5 GWh of electricity were generated at Aiviekste HPP.

## TRADE

Latvenergo Group trades electricity and natural gas in the Baltic states under the *Elektrum* brand. The products and services are designed for different consumption and usage patterns so that each customer can choose the most suitable offer.

The Group is one of the leading energy traders in the Baltic states. Its market share accounts for about 25% of the Baltic electricity market, where the total consumption is around 28 TWh. In 2018, 7 TWh of electricity were sold to retail customers in the Baltics. More than 1/3 of this amount constitutes electricity sold outside Latvia, which has increased by 11% compared to the previous year and exceeds 2.5 TWh.

In the reporting year, Latvenergo Group was the second largest natural gas consumer in the Baltic states. The amount of natural gas consumed by the Group for its own use and sold to customers amounted to 6.9 TWh. Of this volume, 0.15 TWh were sold to retail customers. At the end of the year, Latvenergo had more than 400 retail natural gas customers in the Baltic states.

The Group continues to develop the trade of supplementary services in the Baltic states. The service *Elektrum Solar*, which provides for the possibility to use independently generated electricity from solar light, is now also available in Lithuania and Estonia. Approximately 100 customers have signed a contract for the installation of solar panels in the Baltics. In 2018, 370 *Elektrum Smart House* devices, which provide remote control of home heating and electrical appliances, were installed for customers. In the reporting year, the Group also started trading natural gas in Lithuania.

The Group has about 800 thousand customers across the Baltics. Of these, 96% are households and 4% are business customers. In 2018, the number of business customers increased by 1%, while the number of household customers fell by 6%. The main reason for the decrease is the growth of competition in the household segment, especially in Latvia.

### Trade in the Baltic states

#### Estonia 11% market share



Business customers  
~ **2.5 thousand**



Households  
~ **26 thousand**

#### Latvia 60% market share



Business customers  
~ **25 thousand**



Households  
~ **730 thousand**

#### Lithuania 13% market share



Business customers  
~ **7 thousand**

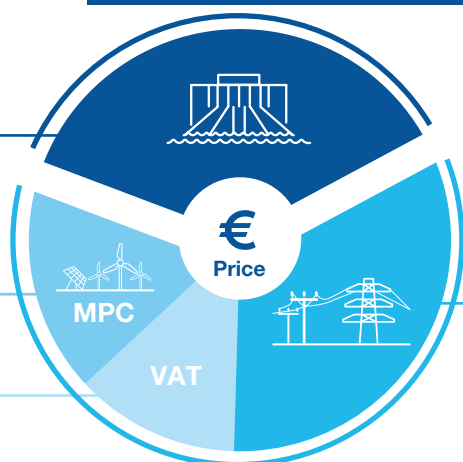


## Breakdown of an electricity bill in Latvia\*

### Price for electricity

includes costs of generation and trade

Price set by the market  
and competition



Regulated tariffs set by the state  
and value added tax  
are the same for all suppliers

### Mandatory procurement components

are set by the state to support generation  
of environmentally friendly energy

### Transmission and distribution services

are provided by Augstsprieguma tīkls AS  
and Sadales tīkls AS

### Value added tax

\* An estimate for a household customer who has 1-phase connection, consumes 100 kWh and uses the product *Elektrum Ekonomiskais* as of 01.01.2019.

## Energy Efficiency

Energy efficiency is gaining the attention of both energy consumers and legislators. The Energy Efficiency Directive 2012/27/EU sets out a series of measures aimed at promoting the energy efficiency of both generators and consumers and achieving total energy savings of 20% by 2020 at the EU level. According to the Directive, each EU Member State must establish an Energy Efficiency Obligation Scheme (EEOS), within which energy retailers must achieve cumulative savings of energy consumed by their customers.

Such a scheme was established in Latvia in 2017 and its first period runs from 2018 to 2020. EEOS-obligated parties comprise electricity traders whose annual electricity sales exceed 10 GWh. These traders must achieve a certain amount of annual savings of the energy consumed by their customers or make contributions to a dedicated energy efficiency national fund. The funding will be used to implement energy efficiency measures to an appropriate extent.

### Savings targets set for Latvenergo AS

2018	1.5 % of the amount of electricity sold in 2018**
2019	1.5 % of the amount of electricity sold in 2018 and 2019**
2020	1.5 % of the amount of electricity sold in 2018, 2019 and 2020**

\*\* Excluding the amount of electricity sold to large electricity consumers and large enterprises. Separate energy efficiency measures outside the EEOS have been established for these groups.

In 2018, Latvenergo AS has sold 4 345 GWh of electricity to consumers in Latvia, and 2 086 GWh of this amount were sold to large electricity consumers and large enterprises. Thus, the amount of savings to be achieved by Latvenergo AS amounts to 34 GWh in 2018.

Latvenergo AS started to take measures aimed at promoting energy efficiency in 2014, and by 2018 energy savings in customer consumption are estimated at 363.8 GWh. The key measures implemented by Latvenergo AS are:

- seminars at the Energy Efficiency Centre;
- provision of information to the public at various events and in the media;
- production of informational handouts;
- individual consultations;
- the improved customer portal *elektrum.lv*, where Latvenergo AS customers can receive information on hourly energy consumption and learn about the possibilities of reducing energy consumption;
- provision of information on the possibilities of improving energy efficiency to any interested person at Latvenergo AS customer service centres;
- an *Elektrum* mobile app that provides information on energy efficiency.

The progress made so far shows that by the end of the first period of the EEOS, Latvenergo AS will exceed its savings target significantly and ensure a substantial increase in energy efficiency.

## MANDATORY PROCUREMENT

Electricity mandatory procurement (MP) is a state-regulated support mechanism for electricity generators in Latvia. It is implemented as electricity procurement or guaranteed payments for the capacity installed at power plants.

The right to sell electricity generated within the MP or receive guaranteed payments for the installed capacity at power plants is granted to generators who generate electricity in efficient cogeneration or from renewable energy sources. The support in the form of a payment for the guaranteed capacity is received by cogeneration plants with installed capacity above 4 MW. The right to receive support in the form of the MP is granted by the Ministry of Economics; however, the issuance of new permits has been suspended since 2012. The provisions for electricity generation, the MP pricing and the amount of guaranteed capacity payments are governed by regulations of the Cabinet of Ministers. The amount of the MP support depends on the type of energy source used (wind, water, biomass, biogas or natural gas), the installed capacity, and, for natural gas cogeneration plants, the cost of natural gas.

Since 2017, support for the reduced mandatory procurement component (MPC) for energy-intensive processing industry companies has also been provided. The Ministry of Economics decides on the reduction of the MPC payments for energy-intensive companies.

In compliance with the Electricity Market Law, the functions of the public trader in Latvia are performed by Enerģijas publiskais tirgotājs AS. Expenditures associated with the MPC and the support for energy-intensive processing industry companies are compensated to the public trader from the MPC payments by electricity end-users and state budget grants.

### Mandatory procurement key indicators

	Units	2014	2015	2016	2017	2018
Power plants	number	386	400	402	408	374
Installed capacity	MW	1,354	1,364	1,379	1,394	1,360
Electricity purchased within the MP	GWh	1,284	1,427	1,503	1,567	1,385
MP costs above the market price (after SET)	MEUR	215.3	224.3	207.9	235.3	162.2
MPC reduction: state aid to energy-intensive processing industry companies	MEUR	0	0	0	3.0	4.8

As of 1 January 2018, the MPC comprises a variable part and a fixed part. The variable part is calculated in proportion to the electricity consumption and the fixed part (the capacity component) depends on the type of system service used. The amount of the MPC is set on the basis of the MP costs of the preceding year and is approved by the PUC.

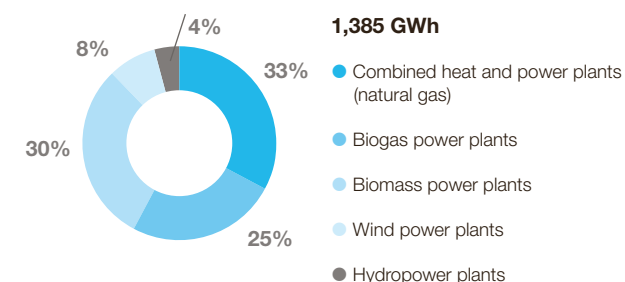
Enerģijas publiskais tirgotājs AS also receives a state budget grant every year. In previous years, the grant allowed the MPC value to remain unchanged, but in 2018 it also made it possible to reduce the said value regardless of the increase in the MP costs. The grant is financed mainly from the dividends of Latvenergo AS for the use of state capital.

### Mandatory Procurement: Key Indicators

In 2018, 12% less electricity was procured within the MP process compared to the previous year. The decrease was mainly due to the fact that the support period ended for 27 cogeneration plants in the second half of 2017 and in 2018, and the weather conditions were less favourable for the operation of wind and hydropower plants.

The support for generators, i.e. the costs above the market price, decreased by EUR 73.1 million in 2018, which was mainly due to a 75% decrease in the payment for the capacity of the Latvenergo AS CHPPs as of 1 January 2018. In 2018, the biggest support per generated kWh within the MP was received by biogas plants (12.5 cents/kWh) and small-scale hydropower plants (10.4 cents/kWh). Following the reduction of the intensity of support payments in 2018, the support payment to the Latvenergo AS CHPPs decreased to 0.9 cents/kWh (5.9 cents/kWh in 2017).

### Electricity purchased within the mandatory procurement

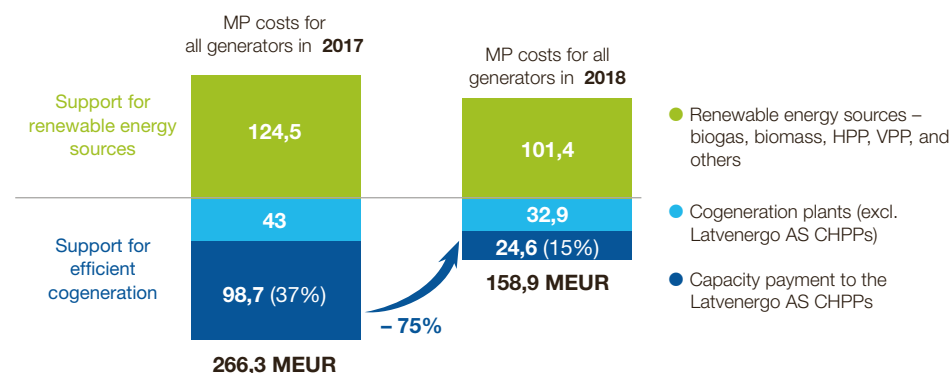


Taking into account both the reduction of the payment for the capacity of the Latvenergo AS CHPPs and the state grant received in 2018, the total MPC value was reduced to 2.268 cents/kWh on average as of 1 January 2018 and was 15% lower than at the end of 2017 (2.679 cents/kWh). In 2018, Enerģijas publiskais tirgotājs AS received a state grant of EUR 92.7 million, which compensates the public trader for the actual MP cost overrun over the MPC revenues from electricity end-users.

In 2018, the actual MP costs exceeded the revenues from end-user payments by EUR 2.8 million.

More information about the MP can be found on the website of Enerģijas publiskais tirgotājs AS.

### MP costs





## DISTRIBUTION

Among the operational segments of Latvenergo Group, the electricity distribution segment is the biggest in terms of assets and second biggest in terms of turnover. It ensures the flow of electricity from the electricity transmission network and electricity generators connected to the distribution networks to electricity consumers.

Sadales tīkls AS, a subsidiary of the Group, is the biggest distribution system operator in Latvia, providing electricity distribution service to approximately 811 thousand customers. The distribution system operator ensures equal access to electricity networks, which is one of the prerequisites for ensuring competition in the Latvian electricity market.

The length of low-voltage power lines has been decreasing every year, thus ensuring a more efficient structure for the electricity network and improving the quality and reliability of power supply. The share of cable lines increases year by year: it has grown from 30% to 36% of the overall line length of power lines over the last

five years. These measures have allowed for reducing the negative impact of weather conditions on electricity networks and the number of failures on lines. The volume of electricity not supplied to customers as a result of failures has decreased by 29% during the last five years, from 1,509 MWh in 2014 to 1,077 MWh in 2018.

Although the share of distributed electricity increased by 2% in 2018, electricity losses in the distribution system were reduced by 3%. The share of losses was only 4.4%, which is historically the lowest figure. Over the last five years, distribution losses have been reduced by 19 GWh or 5%.

Distribution system service tariffs are approved by the PUC. Balanced tariffs introduced in 2016 allow customers to evaluate the existing connection capacities and promote efficient use of the electricity network. Since the introduction of balanced tariffs, the capacity requested by users has decreased by 11%.

### Electricity received in distribution network

	Units	2014	2015	2016	2017	2018
From transmission network	GWh	5,470	5,236	5,304	5,225	5,520
From small generators	GWh	1,297	1,448	1,495	1 575	1,407
<b>TOTAL</b>	<b>GWh</b>	<b>6,767</b>	<b>6,684</b>	<b>6,799</b>	<b>6 800</b>	<b>6,927</b>

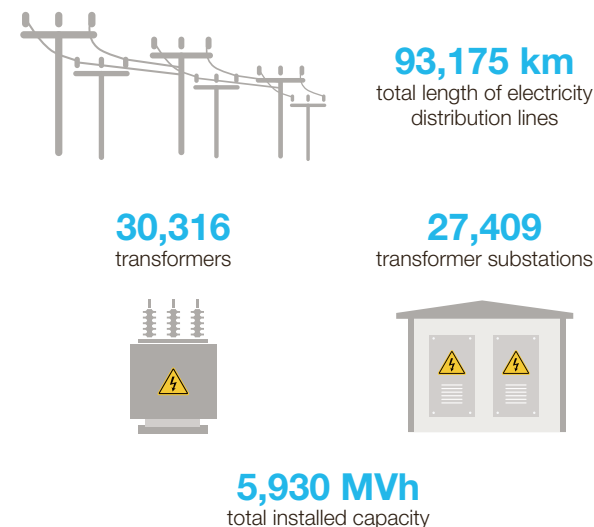
### Distributed electricity and losses

	Units	2014	2015	2016	2017	2018
Distributed electricity	GWh	6,421	6,263*	6,465	6,463	6,600
Electricity distribution losses, technological and operating consumption	GWh	346	328**	334	337	327
<b>TOTAL</b>	<b>GWh</b>	<b>6,767</b>	<b>6,591</b>	<b>6,799</b>	<b>6 800</b>	<b>6,927</b>
Electricity losses	%	4.8%	4.6%	4.6%	4.6%	4.4%

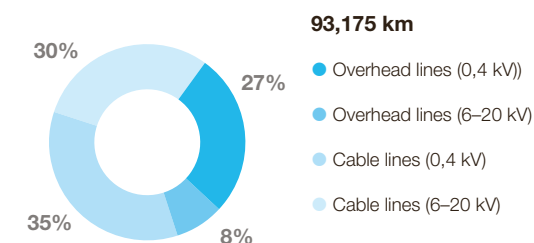
\* excluding 123 GWh which correspond to the regulated electricity tariff revenues received at the beginning of 2015 and recognized in 2014

\*\* 30 GWh added to the amount of losses due to recalculation of actual customer consumption and payments

### Distribution network



### Length of electricity distribution lines in 2018



## Investment and Maintenance

According to the development plan of Sadales tīkls AS, large investments are made in the maintenance and development of distribution networks every year. Their aim is to promote high-quality and reliable electricity supply, to reduce the frequency and duration of interruptions in electricity supply and to ensure efficient management of electricity networks. Renovation projects are assessed according to uniform criteria for the selection of facilities and planning guidelines.

The main areas of investment in the distribution segment are as follows:

- *Cable programme* – replacing overhead power lines with cable lines (mostly in forested areas), which helps to reduce the number of disruptions in the electricity supply system due to unfavourable weather conditions;
- *Restoration of lines and reconstruction of transformer substations*;
- *Automation programme* – installation of remote-controlled circuit breakers and fault location detectors and gradual connection of the 20 kV network to the automatic fault location system, which contributes to faster and more efficient elimination of faults.
- *Introduction of smart electricity meters*, which improves customer awareness of electricity consumption and promotes the efficiency of electricity consumption and cost reduction for the distribution system operator, customers and electricity traders. More than 544 thousand remotely read smart meters were installed by the end of 2018, accounting for 49% of the total fleet of meters and metering 83% of the total volume of electricity consumed by customers.

## Efficiency Programme

Improvement of the operational efficiency of the distribution segment of Latvenergo Group is an important precondition for its balanced development and reduction of operational costs. In 2018, the implementation of the following efficiency projects continued:

- improvement of network management, customer service, dispatch control and support processes;
- revision of management and support processes and optimisation of resources required for operations;
- smart electricity meters are planned for all Sadales tīkls AS customers until 2020, thus reducing the costs of meter servicing and maintenance.

## Investments

	Units	2014	2015	2016	2017	2018
Investments	MEUR	103.2	102.0	106,4	107.7	114.3

## Reconstruction and construction

	Units	2014	2015	2016	2017	2018
Overhead lines constructed (0,4 kV)	km	19	37	22	18	39
Cable lines constructed (0,4 kV)	km	1,089	934	651	781	858
<b>TOTAL low-voltage power lines</b>	<b>km</b>	<b>1,107</b>	<b>972</b>	<b>673</b>	<b>799</b>	<b>897</b>
Overhead lines constructed (6–20 kV)	km	300	556	628	522	692
Cable lines constructed (6–20 kV)	km	104	189	140	115	108
Cable lines constructed (6–20 kV) (Cable programme)	km	207	210	208	211	187
<b>TOTAL medium-voltage power lines</b>	<b>km</b>	<b>611</b>	<b>955</b>	<b>976</b>	<b>848</b>	<b>987</b>
Transformer substations reconstructed	number	649	877	773	726	816
Connections constructed	number	8,510	7,588	9,353	8,907	9,445

From the launch of the efficiency programme in 2017 to the end of the reporting year, the number of jobs was reduced by about 19% or 480 jobs and the number of vehicles was curtailed by 17% or 157 units. 29 of the 70 maintenance depots were closed. Within the efficiency programme, a reduction in the number of Sadales tīkls AS employees of about 800 is planned.

On 20 August, the State Audit Office of the Republic of Latvia approved the audit report *The Efficiency of Costs Included in the Distribution System Services Tariffs of Sadales tīkls Public Limited Company*. The report included nine recommendations for improvement of the performance of Sadales tīkls AS. At the moment, all recommendations have been fulfilled and improvements have been implemented.

## LEASE OF TRANSMISSION SYSTEM ASSETS

The operation of the segment is ensured by Latvijas elektriskie tīkli AS, which is the holder of the distribution system assets (330 kV and 110 kV power transmission lines, substations and distribution points) and leases the assets to Augstsprieguma tīkls AS, the transmission system operator. The asset value exceeded EUR 550 million at the end of 2018. Lease of transmission system assets is a regulated segment, and the revenues are calculated according to the methodology approved by the PUC.

In 2018, EUR 87.1 million was invested in the transmission system development. The most important investment projects are the *Kurzeme Ring* project and the third Latvia–Estonia transmission network interconnection. Investments in transmission system assets are made in accordance with the development plan of Augstsprieguma tīkls AS approved by the PUC. Capital

investment projects in transmission system assets are organised by Augstsprieguma tīkls AS.

### The Kurzeme Ring project

The project, which was started in 2009, substantially improves the reliability of power supply in Kurzeme and Latvia as a whole. It allows for more efficient use of the Lithuania–Sweden sea cable *NordBalt* through even greater integration of the Baltic countries in the Nordic electricity market.

The project is being implemented in three stages, and the total planned length of the 330 kV transmission ring is approximately 330 km. The first stage of the project, the Riga Ring, was completed in 2012, and the second stage, *Grobiņa–Ventspils*, was commissioned

in 2014. For the final part, *Ventspils–Tume–Rīga*, 330 kV lines were built and 110 kV were renovated in a number of stages in the reporting year. A total of 550 poles (77% of the planned amount) were erected as part of the third stage, 155 km of cables were pulled (62% of the planned amount) and the 110 kV substations *Priedaine*, *Valdemārpils*, *Kandava* and *Dundaga* were renovated. Construction of the substations Imanta and Tume continues.

*Kurzeme Ring* is scheduled for completion in 2019. The total estimated construction costs amount to approximately EUR 230 million. The costs of the first and second stages of the project were EUR 95 million, and EUR 104.4 million was invested in the third stage by the end of 2018. An agreement was concluded with the EC Innovation and Networks Executive Agency for co-financing of the concluding stage in the amount of 45%. In addition, Augstsprieguma tīkls AS,

### Length of power transmission lines

	Units	2014	2015	2016	2017	2018
330 kV	km	1,381	1,360	1,346	1,346	1,346
110 kV	km	3,891	3,891	3,891	3,894	3,897
<b>TOTAL</b>	<b>km</b>	<b>5,273</b>	<b>5,251</b>	<b>5,237</b>	<b>5,240</b>	<b>5,243</b>

### Substations and transformers and their installed capacities

	Units	2014	2015	2016	2017	2018
Substations (330 kV)	number	16	16	16	16	16
Autotransformers (330 kV)	number	25	25	25	25	26
Installed capacity of autotransformers (330 kV)	MVA	3,825	3,825	3,825	3,825	3,950
Transformer substations (110 kV)	number	121	121	121	123	123
Transformers (110 kV)	number	246	246	245	248	248
Installed capacity of transformers (110 kV and 10 kV booster transformers)	MVA	5,075	5,102	5,125	5,196	5,215

### Investments in transmission system assets

	Units	2014	2015	2016	2017	2018
<i>Kurzeme Ring</i>	MEUR	11	0	4.5	34.7	65.2
Other	MEUR	20	17	21.0	28.4	21.9
<b>TOTAL</b>	<b>MEUR</b>	<b>31.8</b>	<b>17.5</b>	<b>25.5</b>	<b>63.1</b>	<b>87.1</b>

### Transmission network



**5,243 km**  
total length of electricity  
transmission lines

**16** 330 kV  
substations with a total  
autotransformer capacity of  
**3,950 MVA**



**123** 110 kV  
substations with a total  
transformer capacity of  
**5,215 MVA**



the transmission system operator, intends to earmark congestion charge revenues in the amount of EUR 11.5 million for financing the project.

### The third Estonia–Latvia power transmission network interconnection

The project is important for the entire Baltic region. It will increase the available throughput between the Latvian and Estonian energy systems and reduce the price differences between the Latvian/Lithuanian and Estonian bidding areas.

The length of the interconnection line in Latvia is about 190 km. It is scheduled for completion by the end of 2020. The overall construction costs of the project in Latvia are estimated to be up to EUR 100 million. An agreement was concluded with the EC Innovation and Networks Executive Agency that provides 65% co-financing. In addition, Augstsprieguma tīkls AS intends to earmark congestion charge revenues in the amount of EUR 31 million for financing the project. In 2018, the development of the construction design started and expert evaluation of the construction design was carried out for individual sections of the line. The new 330 kV power line route is being monitored and deforestation operations are underway. EUR 5.3 million was invested in the project in 2018.

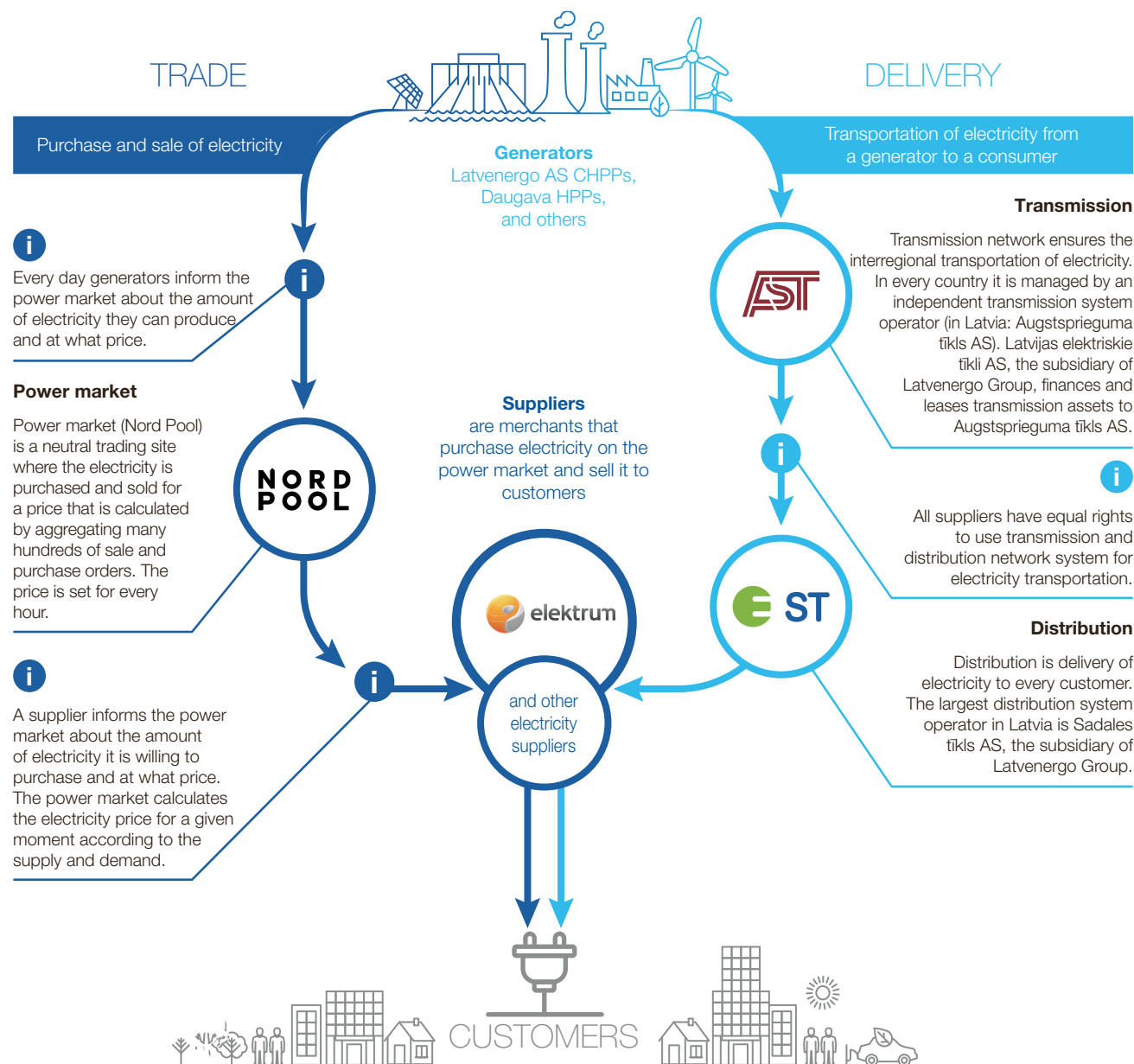
#### The power transmission line CHPP-2–Rīga HPP

The project was launched in 2017 to strengthen Latvia's internal network and ensure full functionality of the third Estonia–Latvia interconnection not only in normal modes but also in emergency and repair modes. In 2018, the development of the construction designs was started.

The estimated costs of the project are around EUR 20 million and an agreement was concluded with the EC Innovation and Networks Executive Agency that provides 50% co-financing. In addition, Augstsprieguma tīkls AS intends to earmark congestion charge revenues in the amount of EUR 9.9 million for financing the project. The reconstruction of the transmission line is scheduled for completion by the end of 2020. EUR 0.2 million was invested in the project by the end of 2018.

#### Other projects

To increase the stability of electricity supply and meet the capacity demand, switchgear at a number of substations was reconstructed in 2018. The 110 kV substation Stīpnieki was built and the construction work at the substation Skrunda continues. Renovation of individual 330 kV and 110 kV power transmission lines is underway as well.







## **PERFORMANCE INDICATORS**

# MATERIALITY ASSESSMENT

The content of the Latvenergo Group Sustainability Report is based on economic, social and environmental topics important to the Group and its stakeholders. These material topics have been defined in compliance with the GRI Guidelines and the materiality assessment methodology developed by Latvenergo Group. The process of defining the material topics and the relevant disclosures can be divided into four steps.

## Step 1

Identifying relevant sustainability topics.  
Identifying priority stakeholders.

## Step 2

Determining the most material sustainability topics.

## Step 3

Incorporating the most material topics into a matrix and verifying it. Selecting disclosures.

## Step 4

Reassessing sustainability topics and disclosures.

## Step 1

The list of potentially relevant topics initially comprised topics attributable to the operation of the Group that are potentially relevant to both the Group and its stakeholders. The list was based on the following sources of information:

- GRI Guidelines and GRI Electric Utilities Sector Disclosures;
- information disclosed by similar companies in the energy sector;
- Latvenergo Group strategy and policies;
- stakeholder opinion;
- a study of the Group's communications;
- information disclosed in previous sustainability reports, etc.

During this step in 2018, a total of 23 topics were identified as relevant to Latvenergo Group operations. The priority stakeholders of the Group were determined through a management survey and assessed by the responsible managers of the respective areas.

## Step 2

In 2018, the Group organised a stakeholder workshop to identify the key aspects of sustainability. It was attended by the management of the Group and about 50 participants, representing all of the priority stakeholders. During the workshop, both stakeholders and the management of the Group assessed the materiality of the aspects identified on a scale of 1 to 7 (from *no material impact on the sustainability of the Group* to a *highly material impact on the sustainability of the Group*). In addition, the participants split into working groups and discussed ideas and suggestions on how the Group could ensure sustainability for the topics which are most relevant to the particular working group. The results of the groups' discussions were presented in a panel discussion.

The previous stakeholder workshop was organised in 2015.

## Step 3

Within this step, the results of the stakeholder vote and the Latvenergo Group management vote were compiled and a materiality matrix of sustainability topics was drawn up. The matrix was assessed and approved by the top management of the Group.

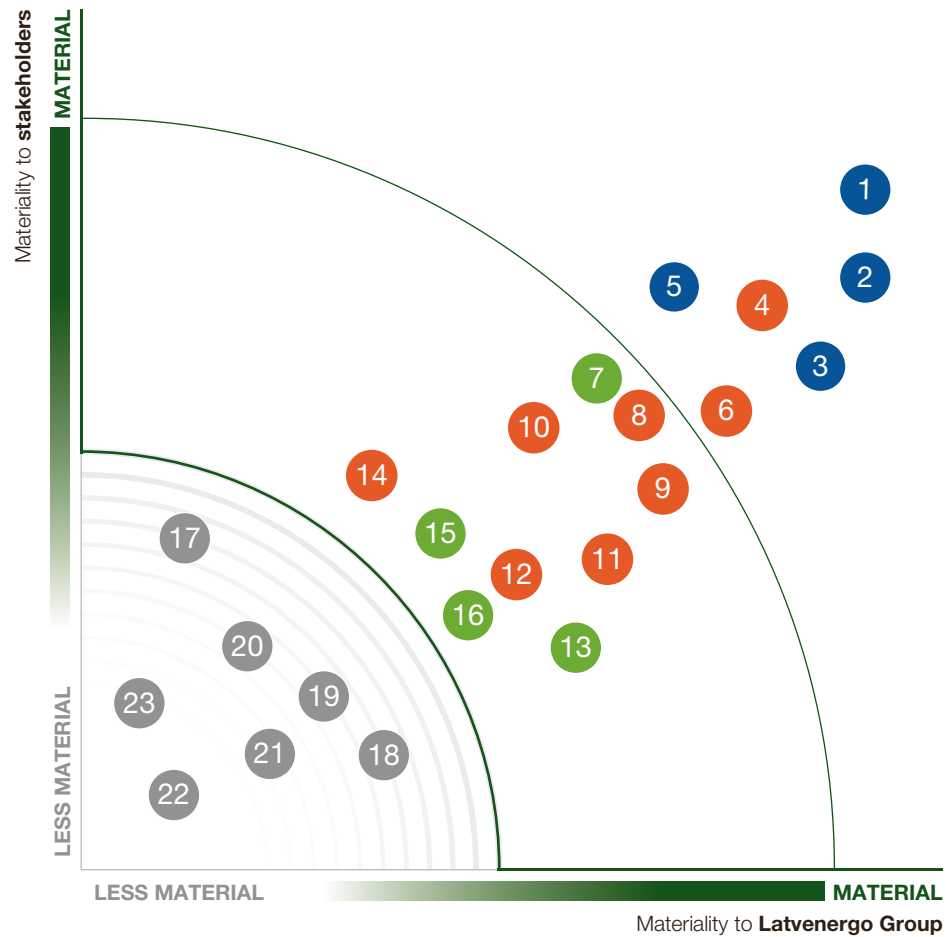
The materiality matrix comprises 23 sustainability topics identified as relevant to Latvenergo Group. The vertical axis of the matrix reflects the importance of the sustainability topics to the Group's stakeholders, and the horizontal axis reflects the importance of these topics from the Group's point of view. The matrix is divided into three parts: most material, moderately material and less material topics. Six topics were evaluated as being the most material, ten topics were recognised as being of moderate materiality and seven as being the less material. In the view of both the Group and stakeholders, economic topics remain the most material. In the social topics group, customer satisfaction was recognised as the most material, while environmental compliance was seen to have the highest materiality in this group.

The Sustainability Report covers the most material and moderately material topics. According to the GRI Guidelines, disclosures corresponding to these topics were identified. Overall, the report discloses information on 16 material sustainability topics for the Group and 31 specific standard disclosures (see the GRI Index).

## Step 4

The preparation of the report includes the annual re-evaluation of stakeholders' opinions, the topics identified and the relevant disclosures. This is done by the persons responsible for the relevant areas, considering changes in the operational environment and the Group's operations and the feedback received from stakeholders.

## Materiality matrix



## Economic topics

- 1 Efficiency of generation plants
- 2 Contribution to the economy
- 3 Efficiency and availability of distribution system
- 5 General compliance and fair business

## Social topics

- 4 Customer satisfaction
- 6 Emergency planning
- 8 Occupational health and safety
- 9 Safety of distribution services
- 10 Public policy engagement
- 11 Employee involvement and development
- 12 Security of personal data
- 14 Information availability
- 17 Work-life balance
- 18 Community contribution
- 19 Impact on local communities
- 21 Human rights and diversity in the workplace
- 23 Freedom of association

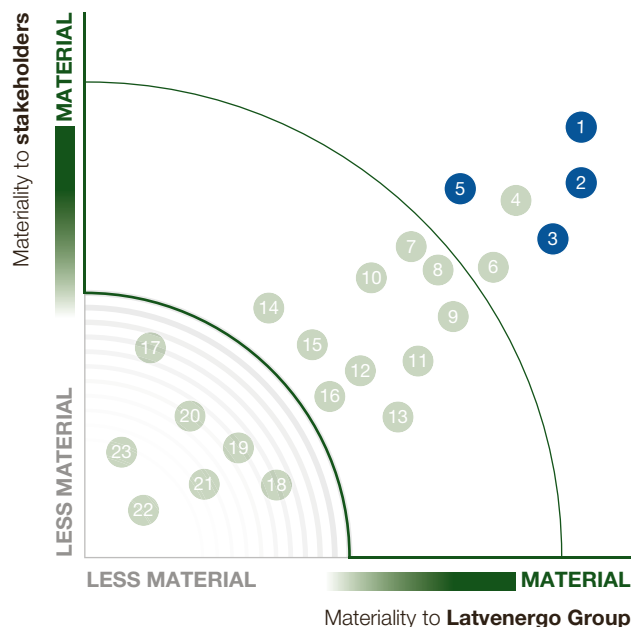
## Environmental topics

- 7 Environmental compliance
- 13 Air pollution
- 15 Resource and energy consumption
- 16 Renewable energy
- 20 Waste and wastewater
- 22 Biodiversity



# ECONOMIC TOPICS

## Economic performance



- 1 Efficiency of generation plants
- 2 Contribution to the economy
- 3 Efficiency and availability of distribution system
- 5 General compliance and fair business

## MANAGEMENT APPROACH

Latvenergo Group's provision of energy, the taxes and dividends it pays, and its procurements and investments are an invaluable contribution to the national economy. The operations of the Group focus on the efficient use of resources and well-considered investments in the energy generation and network infrastructure, thus improving the efficiency of the generation facilities and the quality of the distribution service. In its activities, the Group ensures compliance with laws and regulations, adheres to high ethical standards and encourages its partners to comply with equivalent ethical principles.

### EFFICIENCY OF GENERATION PLANTS

The Daugava HPPs and Latvenergo AS CHPPs, the Group's largest energy generation facilities, operate in conditions of free competition and trade all the electricity they generate on the Nord Pool power exchange. The efficiency of the energy generation facilities is very important for maintaining the competitiveness of the power plants in a changing market situation.

In 2018, the reconstruction of hydropower units continued at the Daugava HPPs. This allows for improving the hydropower turbine efficiency ratios and, consequently, increasing the annual electricity output. By 2022, the Group plans to gradually renovate the hydropower units that have not yet been reconstructed.

The Latvenergo AS CHPPs flexibly adjust their operating modes to the changing electricity market situation and are operated mostly in the highly efficient cogeneration mode. In 2018, work began on the development of a heat storage system at CHPP-2. The heat storage unit will make it possible to accumulate the thermal energy generated in cogeneration mode and thus further enhance the flexibility of the CHPP operating modes.

In unfavourable market conditions, generation at the Latvenergo AS CHPPs is reduced, utilising the opportunity to purchase cheaper electricity from the Nordic countries. The output of the Daugava

HPPs is planned considering the water inflow in the Daugava River and the possibility to accumulate water and generate electricity during periods when the demand and the exchange price is higher. Due to the optimal combination of the generation at the CHPPs and Daugava HPPs and the import opportunities from other Nord Pool bidding areas, consumers in the Baltics benefit from both price convergence to the Nordic price level and price stability in the long term.

A certified integrated management system in compliance with the requirements of ISO 9001, ISO 14001 and OHSAS 18001 and an energy management system in compliance with the requirements of ISO 50001 for electricity and thermal energy generation have been implemented and are maintained, thus confirming operational efficiency.

### CONTRIBUTION TO THE ECONOMY

Energy is one of the most important elements in the development of society, and the energy sector contributes directly to global economic growth. Latvenergo Group enhances the general public well-being both directly and indirectly: it provides sustainable and economically viable services in the energy sector and strengthens the economy in the form of taxes and dividends paid to the state budget, jobs creation, and substantial investment and procurement.

Latvenergo operates in all energy trade segments in Latvia, Lithuania and Estonia, thus having a major impact on economic growth throughout the Baltic region. In 2018, the Group made investments in the amount of EUR 220.6 million, with total investments over the past five years exceeding EUR 1 billion. Taking into account the global development trends of the energy sector, significant amounts have been invested in environmentally friendly energy generation and power network development projects. During the last five years, the biggest investment projects have been the Daugava HPP hydropower unit reconstruction programme and the energy infrastructure project *Kurzeme Ring* (see the annex Green Bond Report).

Latvenergo Group is among the biggest taxpayers in Latvia. In 2018, the Group paid EUR 331.1 million to the state budget of Latvia, including EUR 156.4 million as dividends for the use of state capital.



The amount of taxes paid in Lithuania and Estonia was EUR 13.8 and 6.6 million respectively. Latvenergo Group is also one of the biggest employers in Latvia, with a total of 3,508 employees as of the end of 2018. The Group provides its employees with competitive wages, contributions to their pension fund and training for improvement of professional skills.

At the end of the reporting year, the value of the Group's assets was almost EUR 3.8 billion and equity amounted to EUR 2.3 billion. Detailed information on the performance of the Group is available in the Latvenergo Consolidated Annual Report.

## EFFICIENCY AND AVAILABILITY OF DISTRIBUTION SYSTEM

Sadales tīkls AS is building a sustainable power grid, paying attention to the safety of the grid at each site individually and in the grid as a whole as well as to the quality of the equipment and materials supplied and the work performed. The power grid is being rebuilt using efficient technical solutions that are economically feasible in the long term.

The key performance indicators for quality of electricity supply are the System Average Interruption Duration Index (SAIDI) and the System Average Interruption Frequency Index (SAIFI). Both indicators are calculated as an average indicator on a per-customer-per-year basis. Compared to 2017, SAIFI was reduced by 11% and SAIDI was reduced by 13%. Sadales tīkls AS conducts regular detailed analysis of these indicators and takes measures to improve them. Major actions implemented during the reporting year:

- nearly 1,900 km of power lines were reconstructed, including the replacement of 190 km of overhead lines with cable lines and construction or reconstruction of over 800 transformer substations;
- clearance work on power line routes totalling approximately 4,600 km;
- 142 remote-controlled circuit breakers were built, separating power lines in densely populated places and forested areas;
- duration of scheduled interruptions was limited to 5 hours during winter and 6 hours during the rest of the year;
- an automatic fault localisation system is in the process of implementation and a grid repair and construction work method without voltage disconnection for the customer is being developed.

To reduce electricity losses in the distribution network, older transformers are replaced with more energy efficient equipment, monitoring of electricity consumption is continuously improved and the technical capabilities of smart meters are used.

Seeking to ensure high-quality services, Sadales tīkls AS continuously improves its customer service-related processes. If provision of electricity supply services is found to be inconsistent with quality requirements, customers are compensated for the losses incurred.

More information is available in the section Distribution.

## GENERAL COMPLIANCE AND FAIR COMPETITION

One of the cornerstones of Latvenergo Group corporate governance is ethics and compliance. The Code of Ethics of the Group defines the corporate values and professional conduct principles for ensuring that employees perform their responsibilities with the utmost integrity, are unbiased, and prevent fraud,

corruption and illegitimate or dishonest conduct in their activities. The Group also urges its contractual partners to adhere to equivalent ethical principles.

The Group has also introduced the Fraud and Corruption Risk Management Policy. It defines the basic principles for the management of this risk and the main tasks and responsibilities of the managers and employees of all levels. Along with the policy, the Group implements a range of measures to mitigate the likelihood of the fraud and corruption risk:

- annual fraud and compliance risk assessment and corrective action planning, quarterly monitoring of the implementation of risk mitigation measures;
- employees who take part in the decision-making process in the performance of their duties submit a conflict of interest declaration on an annual basis. Upon entering employment relations, new employees must confirm in writing their understanding of conflict of interest situations and commitment to prevent their occurrence;
- regular training on best control practices for the prevention and mitigation of fraud and corruption risks.

Financial and human resources are allocated to ensure the legal compliance of the Group's operations and mitigate the occurrence of compliance risks. The Group regularly keeps track of changes to laws and regulations, participates in public consultations and cooperates with the responsible institutions. The Group also develops and maintains internal procedures to ensure the compliance of its operations.

Considering that Latvenergo Group is one of the major players in the Latvian electricity market, increased attention is being paid to the principles of equal market competition. To reduce the probability of occurrence of competition risks, the Group has developed the Competition Law Manual and organises regular educational workshops for employees whose activities may impact the occurrence of risks.

## PERFORMANCE INDICATORS

GRI 201-1

### DIRECT ECONOMIC VALUE GENERATED AND DISTRIBUTED

In 2018, the economic value generated by Latvenergo Group dropped by 10% and corresponded to 3% of Latvia's GDP. The decrease was mainly due to the 75% smaller electrical capacity revenue at the Latvenergo AS CHPPs. In 2017, Latvenergo AS made a decision to opt out of 75% of further capacity payments for the CHPPs against a one-off compensation. This decision contributed to the reduction of the MPC, and in 2018 the impact of the CHPPs on the mandatory procurement and capacity payment dropped by EUR 74.2 million (from 37% to 15%).

The distributed economic value in 2018 amounted to 84% of the economic value generated. Two thirds of the distributed value were comprised of operating costs, including electricity procurement, electricity services, energy sources and other operational costs. The 19% increase in the distributed economic value was influenced by higher electricity, natural gas and CO<sub>2</sub> emissions allowance prices.

The added value generated by the Group in 2018 was distributed among the following stakeholders:

- business partners – remuneration for resources and services delivered to ensure the Group's operations;

- employees – direct and indirect remuneration for work;
- state authorities – taxes and duties paid, remuneration for the use of state capital (dividends);
- providers of debt capital and investors – remuneration for the use of borrowed capital;
- the local community – donations and aid.

Latvenergo Group is a significant payer of dividends for the use of state capital in Latvia. In 2018, dividends paid for 2017 comprised EUR 156.4 million, and retained earnings brought forward from previous years were also used for the distribution of dividends. Over the last five years, nearly EUR 400 million was paid as dividends into the state budget. Latvenergo AS dividends are also used as a source of funding for the state budget programme Electricity User Support, ensuring the reduction of the MPC.

In 2018, the undistributed economic value of the Group represented 16% of the economic value generated, and it was 60% lower than the previous year. This reduction was influenced by the distribution of dividends for 2017. In 2018, EUR 220.6 million was earmarked for investment.

#### Economic value generated and distributed

	Units	2017	2018
<b>Economic value generated</b>	<b>MEUR</b>	<b>1,076.8</b>	<b>972.4</b>
Revenue and other income	MEUR	1,075.6	971.3
Income from financial activities	MEUR	1.2	1.2
<b>Economic value distributed</b>	<b>MEUR</b>	<b>686.4</b>	<b>814.8</b>
Resources, materials, operational and other costs	MEUR	390.9	534.0
Employee remuneration	MEUR	113.3	103.8
Payments for the use of state capital	MEUR	90.1	156.4
Payments to providers of debt capital	MEUR	11.2	8.4
State imposed payments	MEUR	80.3	11.2
Charity and sponsorships	MEUR	0.7	1.0
<b>Retained economic value</b>	<b>MEUR</b>	<b>390.4</b>	<b>157.7</b>
Depreciation and amortisation	MEUR	189.1	192.4
Savings and reserves	MEUR	201.3	(34.7)

GRI 201-3

#### DEFINED BENEFIT PLAN OBLIGATIONS AND OTHER RETIREMENT PLANS

Latvenergo Group makes contributions to a pension fund and pays termination benefits to employees upon their retirement. These benefits apply to 97% of the Group's employees. For more information on the Collective Bargaining Agreement, see the section Employees and the Work Environment.

In compliance with the Collective Bargaining Agreement, the Group makes monthly contributions to the current account of Pirmais Slēgtais Pensiju fonds AS on behalf of employees until they reach the pensionable age for statutory pensions. The contributions amount to 5% of each pension fund member's

monthly remuneration (since 2015, employees can redirect part of this 5% towards endowment insurance). The accumulated private pensions become available to employees still employed at the Group after they reach the age of 60, to employees no longer employed at the Group after they reach the age of 55 or in case of Group 1 disability. If the employee draws on the accumulated pension after reaching the age of 60, the employer suspends contributions. The operations of Pirmais Slēgtais Pensiju fonds AS are supervised by the Financial and Capital Market Commission.

#### Contributions to the pension fund

	Units	2014	2015	2016	2017	2018
Contributions	MEUR	3.2	2.6	2.3	2.2	2.2

Termination benefits upon retirement apply to employees who terminate employment and are eligible for a state old-age pension or disability pension. The amount of the benefits depends on the duration of service at Latvenergo Group. The Group grants a benefit in the amount of an average weekly earnings for each year of employment. The amount of Latvenergo Group's obligation for the benefit plan is disclosed in Note 26 of the Annual Report.

GRI 201-4

#### FUNDING RECEIVED FROM THE STATE

Latvenergo Group did not receive foreign financial assistance in 2018. During the preceding years, co-financing from the EU was attracted for the implementation of major transmission network investment projects: the construction of *Kurzeme Ring* and the third Latvia–Estonia transmission network interconnection. As of 1 January 2015, transmission projects are implemented by Augstsprieguma tīkls AS (for more information, see the section Lease of Transmission System Assets).

In compliance with the Electricity Market Law, the functions of the public trader in Latvia are performed by Enerģijas publiskais tirgotājs AS, a subsidiary of the Group. Within the state budget programme Electricity User Support, Enerģijas publiskais tirgotājs AS receives a targeted grant from the state budget that has allowed for maintaining an unchanged MPC value since 2014 and allows for reducing it as of 2018. The revenue from Latvenergo AS dividends is used as the main source of funding for this state budget programme. In 2018, Enerģijas publiskais tirgotājs AS received a EUR 92.7 million targeted grant from the state budget.

#### Funding received from the state and the EU

	Cofunding source	Units	2014	2015	2016	2017	2018
<i>Kurzeme Ring</i>	EU	MEUR	0	18.0	0.2	0	0
Liepāja plants	EU	MEUR	2.2	0	0	0	0
Grant for limiting MPC*	state	MEUR	29.3	20.3	59.2	69.9	92.7
<b>TOTAL</b>		<b>MEUR</b>	<b>31.4</b>	<b>38.3</b>	<b>59.4</b>	<b>69.9</b>	<b>92.7</b>

\* as of 2017, includes payments to energy-intensive processing industry companies

**GRI 205-2****COMMUNICATION AND TRAINING ON ANTI-CORRUPTION POLICIES AND PROCEDURES**

In the reporting period, e-learning on the requirements of the Code of Ethics, prevention of conflicts of interest, and prevention of fraud and corruption was organised for all employees of Latvenergo Group. By 31 December 2018, 99% or 3,299 employees of the Group completed this programme (except for employees on long-term leave and employees whose employment was terminated in the reporting year).

During the reporting period, managers of Latvenergo AS, Sadales tīkls AS, Latvijas elektriskie tīkli AS and Enerģijas publiskais tirgotājs AS also participated in onsite training on work organisation, ethics, the internal control system and risk management.

**GRI 205-3****CONFIRMED INCIDENTS OF CORRUPTION AND ACTIONS TAKEN**

No cases of corruption were identified within Latvenergo Group in the reporting period. According to the risk assessment results, the risk of fraud and corruption at the Group is properly managed.

**GRI 206-1****LEGAL ACTIONS FOR ANTI-COMPETITIVE BEHAVIOUR AND MONOPOLY PRACTICES**

In 2018, no cases of anti-competitive behaviour or misuse of the dominant position by Latvenergo Group were identified, and no court proceedings against Latvenergo Group were initiated or are ongoing.

**GRI 419-1****NON-COMPLIANCE WITH LAWS AND REGULATIONS IN THE SOCIAL AND ECONOMIC AREA**

No significant fines or non-monetary sanctions were applied in 2018 for any failure by the Group to comply with laws and regulations in the social and economic area.

**GRI EU11****AVERAGE GENERATION EFFICIENCY OF THERMAL PLANTS**

Generation efficiency indicators are calculated as the ratio of electricity and thermal energy generated and the energy necessary for their generation. These indicators are affected by the operation modes chosen at the generation facility, which are adjustable according to electricity market conditions.

In 2018, the generation efficiency indicator of the Daugava HPPs did not change, whereas at the Latvenergo AS CHPPs this indicator decreased by 11 percentage points. In 2018, dry weather conditions

in Europe caused a rapid rise in electricity prices, so the Group used the advantages of its diversified generation facilities and generated the amount of electricity to meet the market demand at the CHPPs. Approximately 40% of the CHPPs' electricity output was generated in condensation mode when the CHPPs were only operated for electricity generation; therefore, the average efficiency indicators decreased.

Compared to other Baltic energy companies, the efficiency indicators of Latvenergo Group generation facilities are considered to be high.

**Generation facility efficiency indicators**

	Units	2014	2015	2016	2017	2018
Daugava HPPs	m <sup>3</sup> /kWh	18.7	18.8	18.9	18.6	18.6
CHPPs	%	80%	79%	83%	88%	77%
Liepāja plants	%	91%	90%	90%	91%	90%

**GRI EU12****DISTRIBUTION LOSSES AS A PERCENTAGE OF TOTAL ENERGY**

One of the most important indicators describing the efficiency of the distribution segment is distribution losses as a percentage of total electricity received in the grid. In 2018, Latvenergo Group reached the historically lowest electricity loss rate of 4.4%.

**Distribution losses**

	Units	2014	2015	2016	2017	2018
Distribution losses	%	4.8%	4.6%	4.6%	4.6%	4.4%

**GRI EU30****AVERAGE PLANT AVAILABILITY FACTOR**

The power plant availability factor for the generation facilities is calculated as the time period during which a plant provides its rated capacity. The remaining time is intended for scheduled and unscheduled repair work.

In 2018, the plant availability factor for the Daugava HPPs remained unchanged. It was still impacted by the Daugava HPP hydropower unit reconstruction programme, within which reconstruction of three hydropower units took place in the reporting year. The availability factors for the CHPPs were higher compared to the previous year, as the amount of repairs was smaller.

In 2018, the Daugava HPPs were operational for an average of 1,818 hours and on back-up for an average of 4,224 hours. The average annual duration of scheduled repair work per hydropower unit was 1,560 hours. Unscheduled repairs amounted to 13,308 hours in total.

The CHPPs were operational for an average of 2,402 hours and on back-up for an average of 5,791 hours. The average annual duration of scheduled repair work per unit was 529 hours. Unscheduled repairs amounted to 424 hours in total.

#### Average plant availability

	Units	2014	2015	2016	2017	2018
Daugava HPPs	%	93%	87%	81%	76%	76%
CHPPs	%	86%	82%	82%	80%	88%

GRI EU26

#### PERCENTAGE OF THE POPULATION UNSERVED IN LICENSED DISTRIBUTION OR SERVICE AREAS

The service area specified in the electricity distribution licence covers 99% of the territory of the Republic of Latvia. Electricity distribution services are ensured to over 811 thousand customers. Electricity distribution services are provided to all households that have concluded agreements on electricity supply within the service area specified in the licence.

GRI EU27

#### NUMBER OF RESIDENTIAL DISCONNECTIONS FOR NON-PAYMENT

In 2018, electricity supply was disconnected for 8,138 households due to failure to pay in a timely manner. 51% of disconnections lasted up to 48 hours. Cases where disconnections were longer than 1 month (21%) were due to changes of household users.

In accordance with laws and regulations, the distribution system operator is obliged to restore electricity supply within five days after it has received a full payment for the system services or upon receipt of a relevant notification from the trader. 89% of households had their electricity connection restored within 24 hours after the payment.

##### Number of residential disconnections for non-payment

	Units	2017	2018
Up to 48 hours	number	3,164	4,123
From 48 hours to 1 week	number	1,219	971
From 1 week to 1 month	number	1,460	1,297
From 1 month to 1 year	number	2,415	1,747
More than 1 year	number	3	0
<b>TOTAL</b>	<b>number</b>	<b>8,261</b>	<b>8,138</b>

##### Length of time between arrangement of payment and reconnection

	Units	2017	2018
Up to 24 hours	number	8,069	7,217
From 24 hours to 1 week	number	192	921
More than 1 week	number	0	0
<b>TOTAL</b>	<b>number</b>	<b>8,261</b>	<b>8,138</b>

GRI EU28; EU29

#### POWER OUTAGE FREQUENCY (SAIFI) AND AVERAGE POWER OUTAGE DURATION (SAIDI)

Well-targeted investment in the reconstruction of distribution networks and intensive clearance work on power line routes has contributed to substantially reduced SAIFI and SAIDI over the last five years. Part of the power line maintenance and repair work was carried out without cutting voltage for consumers.

##### System Average Interruption Frequency Index (SAIFI)

	Units	2014	2015	2016	2017	2018
Unscheduled: weather conditions (massive damage)	number	0.4	0.2	0.2	0.2	0.0
Unscheduled: damage (incl. by third parties)	number	2.4	2.1	2.2	2.0	1.9
Scheduled: network maintenance and overhaul	number	1.0	0.8	0.7	0.6	0.6
<b>TOTAL</b>	<b>number</b>	<b>3.8</b>	<b>3.2</b>	<b>3.1</b>	<b>2.8</b>	<b>2.5</b>

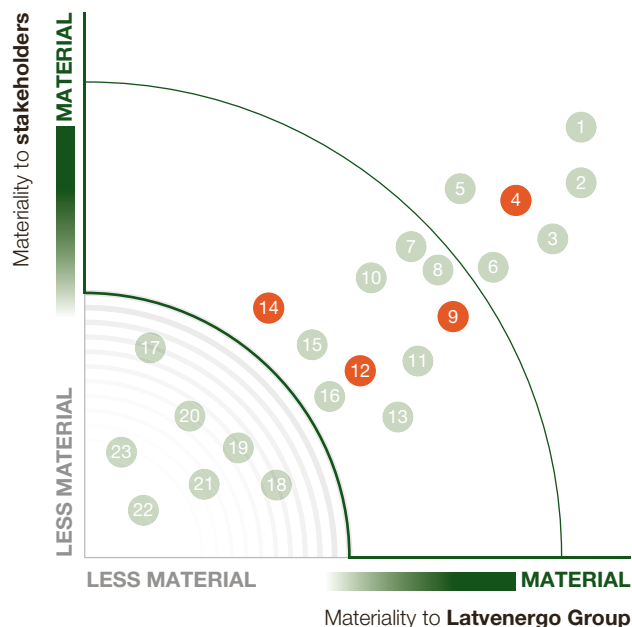
##### System Average Interruption Duration Index (SAIDI)

	Units	2014	2015	2016	2017	2018
Unscheduled: weather conditions (massive damage)	min	57	18	26	18	3
Unscheduled: damage (incl. by third parties)	min	153	126	104	100	102
Scheduled: network maintenance and overhaul	min	256	206	156	143	123
<b>TOTAL</b>	<b>min</b>	<b>466</b>	<b>350</b>	<b>286</b>	<b>261</b>	<b>228</b>



# SOCIAL ASPECTS

## Product responsibility



- 4 Customer satisfaction
- 9 Safety of distribution services
- 12 Security of personal data
- 14 Information availability

## MANAGEMENT APPROACH

Latvenergo Group's operations are targeted at developing and offering competitive services that meet customers' needs as well as at building long-term, mutually beneficial and loyal relationships with customers. Distribution services are based on the provision of high-quality and secure electricity supply in Latvia. To achieve these goals, the Group follows the principles of cost-effectiveness and operational excellence.

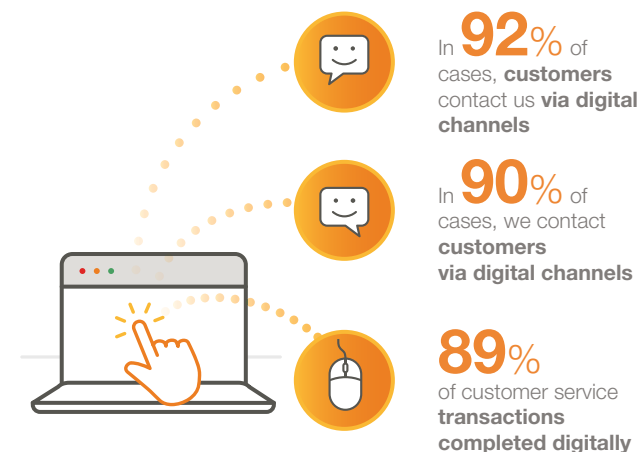
## CUSTOMER SATISFACTION

### Trade

In 2018, Latvenergo AS launched the Digital Transformation Programme. Its goal is to develop digital and automated solutions that provide customers with convenient, accessible and modern service as well as promote effective communication with the company. 100% of customer accessibility to self-service options on the *elektrum.lv* customer portal and mobile application has been achieved within the Digital Transformation Programme. In addition to the previously available self-service options, household customers can now prepare applications, terminate contracts and create payment plans and invoice analytics reports on the portal, and business customers can view and approve sales offers. Automated reminders for reporting meter readings and automatic recording of readings during calls have been introduced as part of communication with customers. Considering the rapid digitalisation, the number of onsite customer service centres was reduced in 2018.

### Customer service key performance indicators in Latvia

	Units	2014	2015	2016	2017	2018
Calls answered	%	90	90	87	89	83
Calls answered within 30 seconds	%	78	78	73	76	64
E-mails answered within 24 hours	%	n/a	n/a	54	90	58
The average waiting time at the customer service centres	min	n/a	n/a	10	7	11
Claims answered within 3 days	%	n/a	n/a	n/a	n/a	80
First call resolution for the household segment	%	n/a	n/a	91	90	91



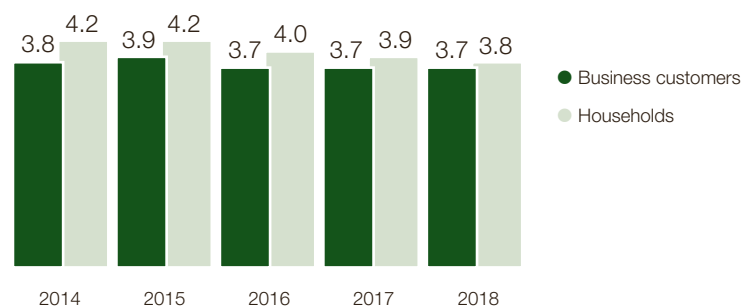
Customer satisfaction is substantially impacted by service quality, accessibility and convenience. To assess the quality of customer service and identify the opportunities for its improvement in a timely manner, a number of customer service key performance indicators have been defined at the Group (see table).

Compared to previous years, several indicators show a drop in performance as a result of the increase in customer contact time. It was in turn influenced by a number of factors: restructuring of customer service resources; a broader range of customer questions due to intensification of competition and changes in the MPC; and the General Data Protection Regulation introduced in 2018, which imposes changes to customer service processes.

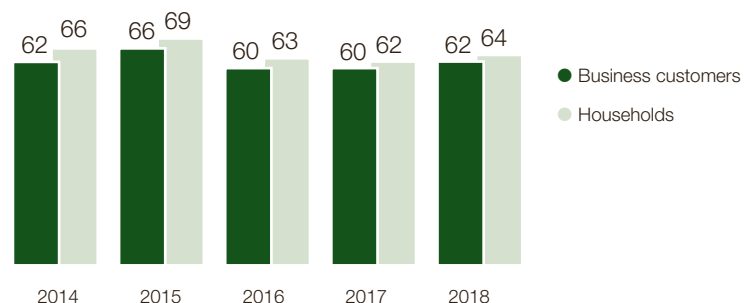
In cooperation with sociological research agencies, the Group conducts regular customer satisfaction and loyalty surveys in the household and business customer segments in Latvia. These surveys measure overall satisfaction with the Group, its services, customer service, payment options and the availability and content of information. Customer satisfaction is measured by an index on a 6-point scale, and customer loyalty is measured by an index on a 100-point scale. In 2018, there was no significant change in the customer satisfaction index, while customer loyalty increased in both the household and business customer segments.

During the year, *Elektrum* received 249 customer complaints, representing less than 1% of the Group's overall customer contacts. 19% of complaints regarding electricity trade were substantiated. Responses were given as promptly as possible: 80% of the complaints regarding electricity trade were handled within 3 working days.

#### Latvenergo customer satisfaction index in Latvia



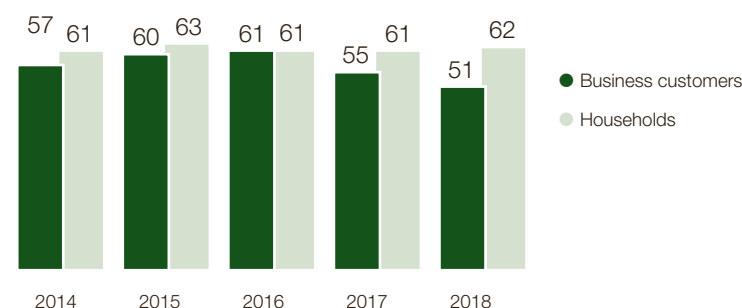
#### Latvenergo customer loyalty index in Latvia



## Distribution

In 2018, the total Sadales tīkls AS customer satisfaction index did not change significantly. Compared to the previous year, the index decreased in the segment of business customers, mainly in the group of small enterprises. In the group of large enterprises and in the household segment, customer satisfaction increased, while in the group of medium-sized enterprises, the assessment was equivalent to the previous year's result. In general, customers appreciate the performance of employees and the provision of prompt information; business customers are also satisfied with corporate customer service. The continuity of power supply is increasingly important for all customer groups and it was recognised as an area that should be improved.

#### Sadales tīkls AS customer satisfaction index



Continuing the digitisation of services and customer experiences begun in previous years, significant investment was made to improve solutions in 2018. This will facilitate the speed and convenience of service availability and reduce manual operations in customer service processes.

To assess the quality of customer service, Sadales tīkls AS carried out customer experience monitoring. The results are analysed and used by the company to improve customer service quality, informative materials and availability of information. In 2018, the overall rating of all services remained unchanged at 3.8 on a 5-point scale.

## SAFETY OF DISTRIBUTION SERVICES

Safe electricity supply is a priority for Sadales tīkls AS. Accidents at the company's electrical installations are most frequently associated with negligence in the vicinity of the electrical infrastructure when third parties have disregarded the requirements of the Protection Zone Law in business operations and touched 20 kV electricity line wires with machinery. Sadales tīkls AS educates people engaged in business operations, logging and agricultural work on a regular basis and urges them to observe electrical safety rules while working near electricity lines.

Sadales tīkls AS carries out a variety of preventive and educational activities aimed at adults, children and youth to reduce the number of electrical injuries and accidents. During these activities, the employees of the company, taking into consideration the level of knowledge of each age group, explain the nature of electrical hazards and what to do in the event of an accident, teaching them to recognise warning

signs at electrical installations and to pay attention to dangerous situations in daily life in order to protect themselves and others. Since 2013, electrical safety classes have been held at almost 700 educational institutions throughout Latvia, with more than 110,000 children and young people participating in them. In cooperation with other companies and organisations, Sadales tīkls AS also takes part in the implementation of the children's education and safety project *One Day for Safety* and the contest *Be Safe, not Overconfident*.

Information on electrical safety can also be found on the website of Sadales tīkls AS and on the electrical safety page (Elektrodrošība) on the *draugiem.lv* portal. On *arelektribuneriske.lv*, children and young people can find out about the dangers of electricity in an interactive and attractive way.

## SECURITY OF PERSONAL DATA

As of May 2018, the General Data Protection Regulation (EU) 2016/679 has been directly applicable throughout the European Union. In order to ensure the fulfilment of data subjects' rights set out in the Regulation, the employee data handling processes, customer service and sales processes, database management and other Group processes have been adjusted. The Group employs personal data protection specialists and has approved the Personal Data Processing Policy, the principles of processing personal data of customers and employees, and other documents. Regular workshops, forums and e-learning are organised for employees whose duties involve working with personal data.

The processing and maintenance of personal data stored in the databases held by Latvenergo Group is carried out in accordance with the requirements of the laws and regulations for the security of personal data and the respect of confidentiality. Data handling processes are adjusted so as to ensure the confidentiality of personal data, including on the *Elektrum* and *e-st.lv* customer portals and in direct communication activities. In the reporting year, a number of solutions were introduced to ensure the security of customers' personal data:

- a customer password and customer identification process was introduced in indirect contact;
- a campaign was implemented that allows customers to choose whether to receive information from the service provider and, if so, what kind;
- e-mail addresses for communication on personal data processing issues were created (*fpda@latvenergo.lv* for *Elektrum* customers; *personasdati@sadalestikls.lv* for Sadales tīkls AS customers);
- a system for recording and monitoring customers' personal data processing incidents was set up.

## INFORMATION AVAILABILITY

In communication with customers as well as in marketing and advertising activities, Latvenergo Group ensures compliance of the information with the law, fair competition standards, the Group's Code of Ethics and internal policies.

## Trade

A number of customer service channels are offered to maintain a high level of customer satisfaction and service quality and availability. The following service channels are available for customers in Latvia:

- the *elektrum.lv* customer portal, incl. online customer service;
- the *Elektrum* mobile application;
- customer service by phone;
- customer service onsite at the customer service centres in Riga and Daugavpils;
- an option to submit questions via e-mail;
- social networks.

In Lithuania and Estonia, customer service is ensured via the *elektrum.lt* and *elektrum.ee* customer service portals as well as by phone. Household customers in Estonia can also use a mobile application and ask questions on social networks.

The most popular customer service channel is the *elektrum.lv* portal, where the number of visits accounts for 83% of all customer contacts. Customers make active use of the portal to submit electricity meter readings and make payments. The popularity of the *Elektrum* mobile application continues to grow: it is used by more than 85 thousand customers, which is 11% of the total number of customers. The use of other service channels has been decreasing every year.

To facilitate access to information, customer service is also provided in Russian and English, while informational materials at customer service centres are also available in Russian. Customer service centres ensure access for customers with reduced mobility. To reduce the waiting time for customers with children and pregnant women, separate queues are arranged for them.

Based on customer interests and needs, the Group continues to raise the awareness of energy efficiency and electrical safety issues among customers and society in general. Advice on these issues is regularly published in the customer newsletter *Elektrum tavām mājām* (*Elektrum for Your Home*) and on the *Elektrum* social network accounts. The *Elektrum* Energy Efficiency Centre holds informative activities and campaigns focusing on energy efficiency issues.

## Distribution

In 2018, self-service options on the *e-st.lv* customer portal of Sadales tīkls AS were also expanded. 81% of applications for new connections and increasing the load and 67% applications for other services were submitted electronically via the portal.

A map of outages with up-to-date information on scheduled and emergency outages in the power network can be found on the website of Sadales tīkls AS and on the *e-st.lv* customer portal. Power network faults may be reported free of charge 24/7 by calling 8404.

For information on educating the public in electrical safety, see the section Corporate Social Responsibility.

## PERFORMANCE INDICATORS

GRI 417-3

### INCIDENTS OF NON-COMPLIANCE CONCERNING MARKETING COMMUNICATIONS

No cases of non-compliance of Latvenergo Group's marketing activities with legal or voluntary provisions were identified in 2018.

GRI 418-1

### COMPLAINTS REGARDING BREACHES OF CUSTOMER PRIVACY AND LOSSES OF CUSTOMER DATA

In 2018, three substantiated, one partially substantiated and eleven unsubstantiated complaints were registered concerning possible customer data privacy violations. The errors in customer data processing were eliminated immediately upon receipt of the complaints.

Complaints regarding breaches of customer privacy and losses of customer data						
	Units	2014	2015	2016	2017	2018
Substantiated complaints	number	1	5	2	2	3
Partially substantiated complaints	number	0	0	0	1	1
Unsubstantiated complaints	number	1	6	2	6	11

GRI EU25

### NUMBER OF INJURIES AND FATALITIES TO THE PUBLIC INVOLVING COMPANY ASSETS

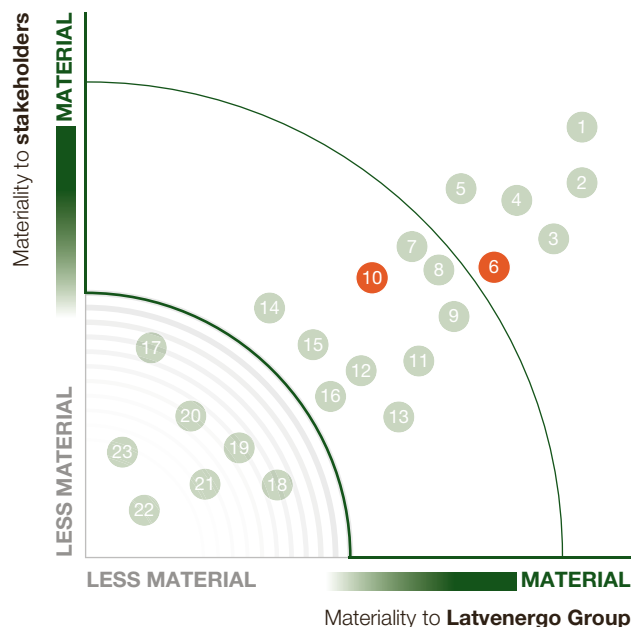
Three accidents involving third parties occurred at Sadales tīkls AS electrical installations. The accidents were due to touching electricity lines with machinery or a fishing rod; in one case, the electric shock was caused by damaging the cable insulation during excavation work.

#### Number of accidents to third parties

	Units	2014	2015	2016	2017	2018
Fatal	number	0	2	0	1	0
Serious	number	1	0	1	0	0
Not serious	number	2	5	2	5	3
<b>TOTAL</b>	<b>number</b>	<b>3</b>	<b>7</b>	<b>3</b>	<b>6</b>	<b>3</b>
Legal cases	number	0	0	0	0	0



## Society



## MANAGEMENT APPROACH

Latvenergo Group evaluates energy development trends, informs stakeholders about its activities and states its position on policy documents relevant to the Group and its stakeholders and legislation in the energy sector and related sectors. Emergency and crisis management and prevention plans have been developed for the Group's critical infrastructure. The Group carries out corporate social responsibility activities for the development of different groups of society.

### EMERGENCY PLANNING

Latvenergo Group has created an emergency and crisis management system. The purpose of the system is a common approach for resolving issues that arise during emergency or crisis situations in order to ensure continuous and reliable operations of the Group or their prompt and efficient recovery.

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

In cooperation with Augstsprieguma tīkls AS, annual emergency and crisis management training is carried out where possible emergency scenarios are simulated. These activities involve employees of Latvenergo Group and specialists from the Department of Management and Operations of the SFRS and from the National Armed Forces. To improve recovery response and reduce material losses, the training process is subsequently analysed and preventive measures to be taken are defined.

### PUBLIC POLICY ENGAGEMENT

Latvenergo Group engages in shaping energy sector policy to promote sustainable development of the Group, the sector and the economy. The Group's representatives participate in various energy policy forums and, in line with the Group's strategy, engage in drafting statements and opinions on Latvian and EU-level studies, guidelines, standards, policy documents and legislation pertaining to the energy sector and related sectors.

The Group's experts make recommendations for the development and improvement of various Latvian regulatory documents of the energy sector on a regular basis. In 2018, the most important activities in this regard included involvement in elaborating policy for further development of the electricity MP system as well as recommendations for improving regulation of the use of natural gas infrastructure and for upgrading state energy efficiency policy and regulation of its implementation.

The Group's involvement in shaping EU energy sector policy is ensured through its participation in the European electricity sector professional association Eurelectric and the Technical Association for Power and Heat Generation VGB PowerTech e.V. In 2018, the Group's experts contributed to the development of Eurelectric position papers on the legislative package Clean Energy for all Europeans as well as on the EC Action Plan for Financing Sustainable Growth and the EC Strategy for Long-Term EU Greenhouse Gas Emissions Reduction by 2050. Latvenergo Group also participates in the Eurelectric study on EU decarbonisation and electrification scenarios. In cooperation with the VGB Association, EU institutions have been presented with proposals for the further development of the EU Emissions Trading Scheme and the draft network codes developed by the European Network of Transmission System Operators for Electricity (ENTSO-E). The Group's experts also participated in the VGB's European Pollutant Release and Transfer Register emission reporting audit and the preparation of statistical guidelines for assessing emissions compliance.

Latvenergo Group regularly participates in energy and energy efficiency forums and conferences and thus contributes to the exchange of opinions on the future of energy. The key issues discussed in 2018 include zero-emissions generation, energy efficiency as an obligation for public service providers and moving towards European decarbonisation. The impact of improving the efficiency of Sadales tīkls AS performance on its customers was also relevant at the Latvian level.

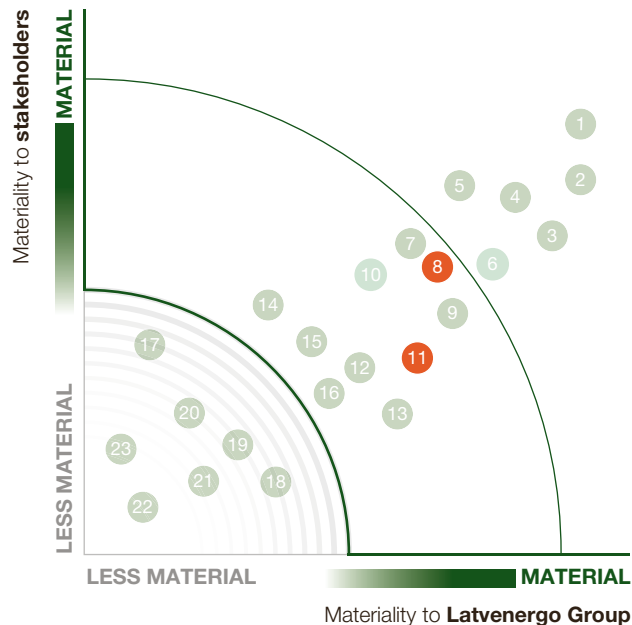
## PERFORMANCE INDICATORS

GRI 415-1

### POLITICAL CONTRIBUTIONS

In compliance with the requirements of the laws and regulations of the Republic of Latvia, the Latvenergo AS Donation Strategy and the Group Corporate Social Responsibility Policy, Latvenergo Group does not make any monetary and/or non-monetary contributions to political organisations.

## Employees and the work environment



- 8 Occupational health and safety
- 11 Employee involvement and development

## MANAGEMENT APPROACH

Latvenergo Group's management acknowledges that employees are the core value of the company. Diversity of employees and their different and complementary competencies are essential for achieving the Group's goals and growth. In 2018, the Excellence Programme was launched to promote employee engagement and willingness to implement innovative ideas.

### PERSONNEL MANAGEMENT POLICY AND BASIC PRINCIPLES

The main tasks of Latvenergo Group's human resource management are aimed at ensuring that the conduct of each and every employee is in line with the Group's values: responsibility, efficiency and openness. The Personnel Management Policy of the Group is subject to its strategy and supports the areas of personnel management outlined in it:

- employee engagement in order to promote growth, productivity and innovation;
- management of excellence-oriented skills and competences and leadership development;
- comprehensive diversity management, achieving full engagement of all employees and their ability to fulfil their potential, regardless of any constraints;
- a balanced motivation system that supports excellence and leadership.

The key principles characterising the Group's personnel management philosophy and attitude towards employees:

- social responsibility: a safe working environment, equal employment conditions and equal treatment of all employees are implemented and maintained;
- social dialogue with employees and their representatives;
- competence development, knowledge sharing and knowledge transfer;
- engagement and responsibility for the performance of work to ensure achievement of goals;
- support for diversity, new knowledge and innovation;
- honesty and mutual respect in the relationship between the employer and employees: the employer and employees are equal partners who build their relationship adhering to general ethical principles and taking care to avoid conflict of interest situations.

In all areas of its operation, the Group respects fundamental human

rights, which are enshrined in the Constitution, in applicable laws and in international treaties binding on Latvia. The work environment and processes are created so as to prevent the possibility that the human rights of the employees of the Group and its subcontractors are infringed or violated, insofar as the Group is able to influence this. Respect for human rights of the Group's employees and its cooperation partners is stipulated in the Code of Ethics.

### OCCUPATIONAL HEALTH AND SAFETY

Latvenergo Group pays special attention to occupational health and safety. To persistently minimise occupational health and safety risks, the Group has established and certified a management system in this area that meets OHSAS 18001 requirements. In accordance with the requirements of Latvian legislation, the Group develops an annual occupational health and safety action plan and carries out internal supervision of the work environment. Employees are provided with workspace personal protective equipment and technical resources that are appropriate for their job as well as training on occupational safety issues and safe working methods. In 2018, a new e-learning programme on first aid was prepared and a training video on employees' action in case of fire was created. In the future, the Group plans to develop new e-learning programmes and use them in training its employees and contractors.

The Group also provides briefing and training on safe work performance to all contractors' employees and monitors their activities at the Group's facilities.

### EMPLOYEE INVOLVEMENT

Employee engagement has a significant impact on the growth of the Group and achievement of its goals as well as on individual performance and productivity. The Group conducts an anonymous survey every year to find out employees' engagement level and their views on various factors of the work environment.

In order to promote employee awareness and understanding of the processes taking place in the company, in 2018, Latvenergo AS held 24 face-to-face meetings with managers and 49 meetings with employees. The Management Board of Sadales tīkls AS organises a meeting with all employees of the company and representatives of the trade union every year to inform them about accomplishments and the goals of the company in the coming years.

Considering the changes and challenges in the labour market, the Group plans to develop an integrated employee attraction programme. At the end of 2018, work began on creating an

employer image strategy. Its aim is to find ways to improve the motivation of current employees and to attract new employees. The project involves the Management Board and managers of the company as well as current and potential employees and the trade union.

The website [www.iesledzkarjeru.lv](http://www.iesledzkarjeru.lv) was launched in 2018 to attract new employees. It contains information on job and internship offers at Latvenergo AS and lists the benefits of being employed at the company. A chatbot, Tomass, was created on Facebook to provide online answers to questions about career opportunities at Latvenergo AS. In the future, the Group plans to expand the range of questions that Tomass can answer.

## EMPLOYEE DEVELOPMENT

Latvenergo Group's employees can improve their skills and knowledge both on the recommendation of managers and on their own initiative. This can be done through internal and external face-to-face training and the Group's e-learning platform. Educating managers and developing leadership skills play an important role in employee development. In order to ensure the uniform development of managers at all levels, in 2018, development of the Managers' Knowledge Standard was started, and the first e-learning section, Corporate Governance, was created, which was mastered by 77% of managers by the end of 2018. The Managers' Knowledge Standard will provide extensive information on Latvenergo Group and its operational processes, determining the amount of knowledge required for each management level.

Since 2017, March has become a non-traditional education month at Sadales tīkls AS. This is a good service month internally at the company, when employees improve internal collaboration skills in unconventional ways while also developing external customer service skills. During the campaign *A Strong Team Starts with You* in March 2018, employees shared their experience of dealing with non-standard situations in customer service, voted for the best team and the most helpful colleague, learned some tips and guidelines on the way to excellent communication and participated in a photo contest for the friendliest team. Sadales tīkls AS plans to run similar campaigns in the future too.

### Excellence Programme

In 2017, Latvenergo AS developed guidelines for working with high-potential employees and in 2018 launched the related Excellence Programme with the following main objectives:

- developing and using the potential of employees to address matters important to the company;
- involving and motivating excellent employees;
- promoting cross-department collaboration and a culture of excellence at the company.

Employees who are willing to share knowledge and implement innovative ideas are encouraged to join the programme. Over two years, participants will be implementing their individual development plans and contributing to the implementation of projects important to the Group. Twenty participants are expected to join the programme every year within a period of five years.

In 2018, 21 employees were admitted to the programme. The participants have made suggestions for improving the working environment and internal communication, developing e-learning materials, digitising processes, optimising production equipment performance and improving environmental protection measures. A pilot project on the use of the 60 GHz frequency band for wireless data transmission has been launched.

## Knowledge continuity

Ensuring knowledge continuity is essential for the sustainability of Latvenergo Group's operations. The Group encourages employees to accumulate knowledge and transfer it to colleagues and facilitates timely preparation of successors at workplaces that require specific technical knowledge. One of the priorities in terms of knowledge transfer is provision of quality practical training to students of higher and secondary vocational educational institutions. Every year, the Group offers paid internships. This opportunity was used by 78 students in 2018. The Group cooperates with educational institutions in Latvia, encouraging studies in the field of engineering sciences and the development of the future workforce in Latvia in general.

The quality of practical training is also improved through mentor programmes. In 2018, 61 mentors were trained under such programmes. The five best mentors also gained experience at the Italian energy company Enel Italia, Enel Distribuzione. Latvenergo's membership in the European Alliance for Apprenticeships demonstrates its ability to ensure the quality of practical training.

## PERFORMANCE INDICATORS

**GRI** 102-8, 102-41

### NUMBER OF EMPLOYEES AND THE COLLECTIVE BARGAINING AGREEMENT

The strategy of Latvenergo Group focuses on strengthening competitiveness and maximising efficiency. The efficiency programme launched in 2017 comprises a revision and centralisation of processes, with plans to downsize the number of employees by about a quarter until 2022. Since the start of the programme, the number of employees in the Group has been reduced by about 15%.

A large number of technical positions are characteristic of the energy industry; therefore, the workforce structure of the group has a relatively high proportion of male individuals: 71% of all employees in 2018 were male and 29% were female. This figure has not changed significantly in recent years.

#### Number of employees by operating segments

	Units	2014	2015	2016	2017	2018
Generation and trade	number	989	992	987	949	877
Distribution	number	2,545	2,568	2,521	2,344	2,019
Lease of transmission system assets*	number	443	11	10	9	8
Corporate functions	number	586	606	613	606	604
<b>TOTAL</b>	<b>number</b>	<b>4,563</b>	<b>4,177</b>	<b>4,131</b>	<b>3,908</b>	<b>3,508</b>

\* On 1 January 2015, 430 Latvenergo Group employees were transferred to Augstsprieguma tīkls AS along with the functions of transmission system asset construction and maintenance.

Most employment contracts are concluded as full-time open-ended contracts. In 2018, 12 employees or 0.3% of the total number of employees (0.2% of male and 0.8% of female employees) were employed on a part-time basis, and 1.8% of the employment contracts were concluded for a fixed term (0.8% of male and 4.3% of female employees). These figures have not changed significantly compared to previous years.

The Group's companies Latvenergo AS, Sadales tikls AS, Latvijas elektriskie tikli AS and Enerģijas publiskais tirgotājs AS have signed a Collective Bargaining Agreement with the trade union *Enerģija*. In addition to meeting the requirements of laws and regulations, the Collective Bargaining Agreement provides protection for the employees' economic and social interests. In 2018, the representatives of the Group met with the trade union at 23 meetings.

In 2018, the Collective Bargaining Agreement was applicable to 97% of the Group's employees, and in recent years this percentage has remained constant. The Collective Bargaining Agreement concluded applies not only to trade union members, who currently constitute approximately 60% of the Group's total number of employees, but also to all employees of those companies. Thus, equal treatment of social guarantees is ensured for all employees and the likelihood of conflict between employees and the employer is reduced.

**GRI** 402-1

## MINIMUM NOTICE PERIOD REGARDING OPERATIONAL CHANGES

The Group regularly notifies employees and the trade union about current business activities, development and planned structural changes. The Collective Bargaining Agreement provides that the employer must give no less than one month's notice to the trade union before a request for consent to terminate an employment contract. If collective redundancies are planned, consultations with the trade union must be started no later than one month before notifying the State Employment Agency. Employees must be informed about organisational changes leading to redundancies no later than five days following the decision.

**GRI** 403-2

## RATES OF INJURY, OCCUPATIONAL DISEASES, LOST DAYS AND ABSENTEEISM

Accidents at the Group are registered and investigated in compliance with the laws and regulations of the Republic of Latvia. Appropriate additional training for employees is also conducted.

One accident among contractors' employees was registered in 2018 (six in 2017).

### Rates of injury and absenteeism\*

	Units	2014	2015	2016	2017	2018
Injury rate (IR)	index	0.23	0.23	0.23	0.23	0.33
Occupational diseases rate (ODR)	index	0.10	0.03	0.20	0.15	0.10
Lost day rate (LDR)	index	8	15	8	22	17
Accidents (not serious)	number	8	5	7	6	7
Accidents (serious)	number	1	2	1	2	3
Accidents (fatal)	number	0	1	0	0	0
Occupational diseases	number	4	1	7	5	3
Absentee rate (AR) **	%	3.5%	4.5%	4.7%	5.1%	5.1%

### Rates of injury and absenteeism by gender\*

		2015		2016		2017		2018	
	Units	women	men	women	men	women	men	women	men
Injury rate (IR)	index	0	0.23	0.03	0.20	0.03	0.20	0	0.33
Occupational diseases rate (ODR)	index	0.03	0	0.11	0.09	0.09	0.06	0	0.10
Lost day rate (LDR)	index	0	14.6	0.3	7.4	0.2	21.8	0	16.5
Accidents (not serious)	number	0	5	1	6	0	6	0	7
Accidents (serious)	number	0	2	0	1	1	1	0	3
Accidents (fatal)	number	0	1	0	0	0	0	0	0
Occupational diseases	number	1	0	4	3	3	2	0	3
Absentee rate (AR) **	%	6.5%	3.7%	6.3%	4.1%	6.6%	4.4%	6.6%	4.4%

$$* \quad IR = \frac{\text{number of accidents}}{\text{total hours worked}} * 200\,000$$

$$LDR = \frac{\text{lost days due to accidents}}{\text{total hours worked}} * 200\,000$$

$$ODR = \frac{\text{number of occupational diseases}}{\text{total hours worked}} * 200\,000$$

$$AR = \frac{\text{number of missed (absentee) days}}{\text{planned number of working days}} * 100$$

\*\* including maternity leave and incapacity to work not related to occupational accidents and diseases (the numbers for 2014 do not include data on Elektrum Eesti OÜ and Elektrum Lietuva UAB)



**GRI 403-4**

## HEALTH AND SAFETY TOPICS COVERED IN FORMAL AGREEMENTS WITH TRADE UNIONS

The Latvenergo Collective Bargaining Agreement comprises labour protection issues and cooperation in their resolution. This includes the following:

- the employer, the trade union and the employees have confirmed their responsibility regarding the improvement of the occupational safety system, including the evaluation of working environment risks and minimisation of their impact;
- agreement on the term of office of trustees, which is five years, and their engagement in the improvement of occupational safety;
- the employer's obligations, including in a situation where an accident at work has occurred.

**GRI 404-1**

## AVERAGE HOURS OF TRAINING PER YEAR

In 2018, nearly 100,000 hours were dedicated to face-to-face training, which was attended by 2,250 employees of the Group. An average of 28 hours per employee was devoted to training. Male employees spent an average of 34 hours in training, while female employees spent an average of 14 hours in training. The number of training hours vary considerably by gender because a significant share of the total hours is mandatory training for technical professions where predominantly men are employed.

### Average hours of training per employee in 2018

Profession group	Average number of training hours	Percentage of employees who have undertaken training
Managers	32	78%
Specialists	23	58%
Craft and related trades workers	56	97%
Other professions	6	42%
<b>TOTAL average</b>	<b>28</b>	<b>66%</b>

To facilitate the acquisition of the latest technologies, the Group provides both internal courses and training by equipment suppliers for technical personnel. In 2018, 67 technical specialists were trained for a total of 1,500 hours. A total of 47 employees obtained professional qualifications through training financed by the employer, devoting about 30,000 hours to training. Internal courses and exchange of experience or discussions involving all employees of the Group are organised at least once a year.

**GRI EU15**

## PERCENTAGE OF EMPLOYEES ELIGIBLE TO RETIRE IN THE NEXT 5 AND 10 YEARS

The Group maintains a balanced succession and generational replacement according to the specifics of its working environment. Accordingly, no significant changes compared to 2017 have occurred in the share of employees who might retire within the next 5 and 10 years.

### Percentage of employees eligible to retire in the next 5 and 10 years

Profession group	5 years		10 years	
	Units	women	men	women
Managers	%	0.2	0.9	0.6
Specialists	%	2.7	5.7	4.9
Craft and related trades workers	%	0.1	2.8	0.1
Other professions	%	0.8	1.0	1.6
<b>TOTAL</b>	<b>%</b>	<b>3.8</b>	<b>10.4</b>	<b>7.2</b>

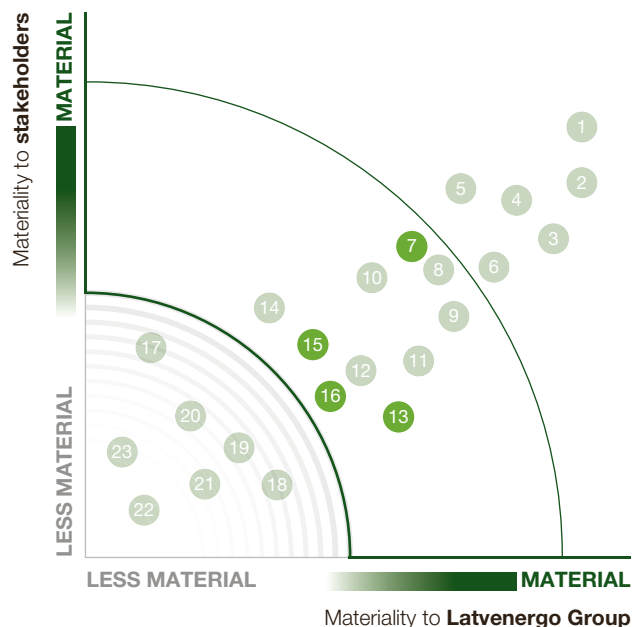
**GRI EU18**

## PERCENTAGE OF CONTRACTOR AND SUBCONTRACTOR EMPLOYEES THAT HAVE UNDERGONE RELEVANT HEALTH AND SAFETY TRAINING

The Group's labour safety specialists provide all (i.e. 100%) contractors' employees with occupational safety briefings as required by Latvian laws and regulations, energy standards and agreements signed with contractors. The instructions and applicable documents on safe performance of work with which contractors' employees must familiarise themselves are also available in electronic form.

# ENVIRONMENTAL ASPECTS

## Environmental protection



- 7 Environmental compliance
- 13 Air pollution
- 15 Resource and energy consumption
- 16 Renewable energy

## MANAGEMENT APPROACH

Latvenergo Group is aware of the importance of environmental protection to the sustainable development of the Group and implements the basic principles of environmental protection in all operational areas and processes of the Group. As regards environmental protection, the Group plans its activities and development in accordance with the basic principles of sustainable development, environmental legislation and the ISO 14001 standard. One of the operational priorities is to ensure environmentally friendly energy generation and supply processes.

## ENVIRONMENTAL POLICY AND MANAGEMENT

The Group's environmental philosophy, attitude towards the environment and the principles of environmental management are defined in the Group's Environmental Policy. The key principles of this policy are:

- ensuring effective management of environmental risks and industrial accident risks;
- promoting continuous improvement of environmental performance and efficient use of natural resources;
- reducing emissions of pollutants into the environment, the Group's impact on climate change and the amount of waste it generates;
- promoting the implementation of balanced and economically sound technologies and measures that reduce or prevent climate change impacts or ensure adaptation to them;
- assessing the impact of investment projects on the environment and society and ensuring maximum reduction of potential damage;
- fostering preservation of biodiversity;
- developing employees' environmental competence and their understanding of the environmental aspects relevant to the Group's operations;

- integrating the key principles of green procurement into procurement procedures;
- providing regular and open information to stakeholders about environmental activities of the Group.

The ability of Latvenergo Group to develop and enhance its environmental performance is evidenced by its Environmental Management System, certified in compliance with the ISO 14001 standard. An energy management system that meets the requirements of ISO 50001 also contributes to the sustainability of the Group. Its aim is to promote the efficient use of energy sources, thereby reducing both the costs of the Group and the environmental impact of its operations.

## ENVIRONMENTAL COMPLIANCE

Latvenergo Group complies with the environmental requirements set out in EU and Latvian legislation and in equipment operation permits. Compliance of the Group's operations is ensured by modernisation of equipment and introduction of the best available technologies as well as professional activities of employees. The Group actively cooperates with state environmental institutions, providing information related to environmental protection, fulfilling the conditions of permits for polluting activities and consulting on the application of environmental requirements. The Group complies with all legal requirements for environmental protection. In 2018, no warnings from environmental protection authorities or substantiated complaints from the public were received.

In compliance with applicable law, the Group makes annual contributions to replenish fish stocks in the Daugava River basin to minimise the impact of the Group's activities on biodiversity. In the reporting year, 1.5 million salmon, sea trout, pike perch, whitefish, vimba and pike fry and 6.9 million lamprey larvae were released into the Daugava River basin.

## Involvement of the Group in climate change mitigation

Climate change caused by greenhouse gases is one of the most pressing global environmental issues affecting the legislation

applicable to the Group's operations. Climate policy objectives and action after 2020 are set out in the Paris Agreement, which was also signed by the EU and Latvia. In order to participate in the achievement of common EU goals and fulfilment of international commitments on climate, work on development of a number of policy planning documents aimed at limiting and adapting to climate change continued in 2018. Documents that will affect the Group's future operations:

- National Energy and Climate Plan 2021–2030;
- Low Carbon Development Strategy of Latvia 2050;
- Climate Change Adaptation Strategy of Latvia 2030.

Attaining climate targets will be an important challenge in the coming years for Latvenergo Group as a major energy producer. That is why the Group is already planning targeted investments to develop and build a generation portfolio with low GHG emissions and contribute to climate change mitigation. The main areas of investment are:

- increasing the efficiency of energy generation and maximising the use of renewable energy sources in energy generation (including reconstruction of the Daugava HPPs);
- reducing losses in the electricity distribution system;
- developing products and services aimed at energy efficiency and low emission or zero emission generation.

The Group also engages in the exchange of knowledge and views on global environmental issues and solutions. In 2018, the Group participated in the preparation of the Hague initiative report on the business contribution of Poland and the Baltic States to climate action. The report was presented at the UN Climate Conference in Poland.

## AIR POLLUTION

In addition to CO<sub>2</sub> emissions, the natural gas and biomass combustion process also produces NO<sub>x</sub>, CO and particulate matter emissions into the air. In order to ensure compliance of the emissions levels with the levels established in legislation and permits, the Group carries out monitoring and recording of these emissions.

In 2017, the European Commission imposed stricter requirements on large combustion plants in regard to the concentration of harmful substances in flue gases. These requirements are also binding on CHPPs and must be implemented within four years. As both CHPPs have been reconstructed, the requirements have already been met. In 2018, the first information was submitted to the State Environmental Service on the compliance of both plants with these requirements.

## RESOURCE AND ENERGY CONSUMPTION

Efficient use of resources has become increasingly important at the Latvian, European and global level. In order to minimise wasteful consumption of energy, Latvenergo AS and Liepājas enerģija SIA have implemented an energy management system, while the principles of energy management of Sadales tīkls AS have been integrated into the environmental management system. This has contributed

to employees' awareness of energy efficiency and given additional motivation to implementing energy saving measures. The most important measures taken in 2018 include the renovation of heat pipelines and roofing, replacement of lighting, and improvement of energy and water consumption metering.

The Group has a balanced and environmentally friendly generation portfolio, consisting mostly of hydropower plants and highly efficient combined heat and power plants. Efficiency of the use of energy sources at the CHPPs is significantly affected by the selected operating mode:

- cogeneration, when both thermal energy and electricity are generated simultaneously;
- condensation, when only electricity is generated.

Operating a CHPP in cogeneration mode allows for the most efficient use of fuel and significantly reduces emissions per unit of energy generated. In 2018, the fuel utilisation factor in the CHPP cogeneration mode ranged from 81% to 90%, while in condensation mode it averaged 52%. Using the cogeneration potential, CHPP-1 saved 27.2% of primary energy sources and CHPP-2 saved 14.7%.

In order to ensure efficient use of energy sources and reduce the impact of the Group on the environment, maintenance and renovation of existing facilities as well as targeted investments in technological improvements are important. In 2017, CHPP-1 was equipped with a flue-gas condensing economiser, which allowed for saving 7.7 thousand tonnes of CO<sub>2</sub> by the end of the reporting year. In 2018, establishment of a heat storage system was begun at CHPP-2. The heat storage unit will make it possible to accumulate the thermal energy generated in cogeneration mode and thus optimise the adjustment of the CHPP operating modes to the changing market conditions and cover peak loads. The use of power units in the highly efficient cogeneration mode also means more efficient use of energy sources, including lower emissions per unit of energy generated. CO<sub>2</sub> savings from heat storage could reach about 4.5 thousand tonnes per year.

## RENEWABLE ENERGY

The group generates a substantial proportion of electricity and thermal energy using three types of renewable energy sources: water, wood and wind. The high share of renewable sources is characteristic of both total consumption of primary energy sources and total energy generation. In 2018:

- renewable energy sources accounted for 30% of the consumption of primary energy sources amounting to 31,867 TJ (for more information see GRI indicators 301-1 and 302-1);
- of 7.4 TWh of energy generated, 35% was produced from renewable sources (for more information see the section Generation).

Maintenance and renovation of the Daugava HPPs' capacities plays a vital role in maintaining a high proportion of renewable energy. The Group's strategy also provides for moving towards the development of generation capacities that meet the criteria for diversification of primary generation sources and low emission projects. In 2018, the Group worked on a pilot project for a wind power plant. The know-how acquired in the project will be a prerequisite for the future expansion of the Group's generation portfolio.

The Group also promotes the use of renewable energy by offering products to customers. The service *Elektrum Solar*, which provides for the possibility to use independently generated electricity from solar light, is available to customers in all three Baltic states.

## PERFORMANCE INDICATORS

GRI 301-1, 302-1

### MATERIAL AND ENERGY CONSUMPTION

In 2018, renewable energy sources accounted for 30% of the total consumption of primary energy sources, while fossil fuel accounted for 70%. The proportion of renewables and fossil fuels is different for electricity generation and thermal energy generation. By consumption of primary sources, the share of renewables in electricity generation was 38% and the share of such sources in thermal energy generation was 9%. The share of renewables in overall energy source consumption largely depends on the amount of energy generated, which is mainly determined by hydrological conditions and market factors (see the section Generation and Trade).

In 2018, energy consumption for the Group's own use to ensure generation processes was 167 GWh or 2.3% of the energy generated.

In 2018, the fuel used for vehicles comprised 862 thousand litres of petrol and 2,306 thousand litres of diesel fuel. Compared to the previous year, petrol consumption decreased by 19%, while diesel consumption increased by 25%.

Accounting and calculation of energy sources is carried out based on measurement or according to fuel suppliers' documentation and internal records and in compliance with the requirements of the greenhouse gas emissions permits and the legislation of the Republic of Latvia and the EU.

#### Consumption of primary energy resources

	Units	2014	2015	2016	2017	2018
Water, wind*	TJ	6,946	6,511	8,834	15,391	8,584
Wood	TJ	718	693	759	767	842
<i>Renewable energy resources</i>	<i>TJ</i>	<i>7,664</i>	<i>7,204</i>	<i>9,593</i>	<i>16,158</i>	<i>9,426</i>
Natural gas	TJ	17,459	19,194	20,185	15,607	22,440
Diesel fuel	TJ	6	2	1	1	1
<i>Fossil energy resources</i>	<i>TJ</i>	<i>17,465</i>	<i>19,196</i>	<i>20,186</i>	<i>15,608</i>	<i>22,441</i>
<b>TOTAL</b>	<b>TJ</b>	<b>25,129</b>	<b>26,400</b>	<b>29,779</b>	<b>31,766</b>	<b>31,867</b>

\* the amount of resources evaluated as the amount of energy generated using these resources (3.6 GJ=1 MWh)

#### Consumption of primary energy resources for electricity generation

	Units	2014	2015	2016	2017	2018
Water, wind*	TJ	6,946	6,511	8,834	15,391	8,584
Wood	TJ	173	181	193	189	61
<i>Renewable energy resources</i>	<i>TJ</i>	<i>7,119</i>	<i>6,692</i>	<i>9,027</i>	<i>15,580</i>	<i>8,645</i>
Natural gas	TJ	8,391	10,910	10,583	6,477	14,300
<i>Fossil energy resources</i>	<i>TJ</i>	<i>8,391</i>	<i>10,910</i>	<i>10,583</i>	<i>6,477</i>	<i>14,300</i>
<b>TOTAL</b>	<b>TJ</b>	<b>15,510</b>	<b>17,602</b>	<b>19,610</b>	<b>22,057</b>	<b>22,945</b>

\* the amount of resources evaluated as the amount of energy generated using these resources (3.6 GJ=1 MWh)

#### Consumption by primary energy resources for thermal energy generation

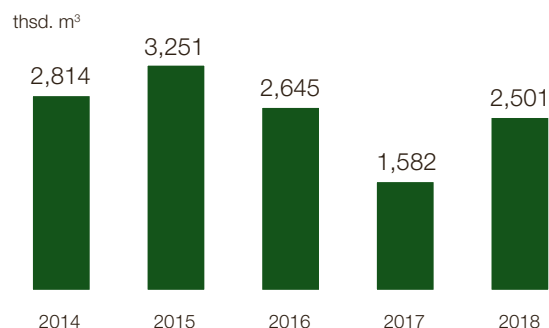
	Units	2014	2015	2016	2017	2018
Wood	TJ	545	512	566	578	781
<i>Renewable energy resources</i>	<i>TJ</i>	<i>545</i>	<i>512</i>	<i>566</i>	<i>578</i>	<i>781</i>
Natural gas	TJ	9,068	8,284	9,602	9,130	8,141
Diesel fuel	TJ	6	2	1	1	1
<i>Fossil energy resources</i>	<i>TJ</i>	<i>9,074</i>	<i>8,286</i>	<i>9,603</i>	<i>9,131</i>	<i>8,142</i>
<b>TOTAL</b>	<b>TJ</b>	<b>9,619</b>	<b>8,798</b>	<b>10,169</b>	<b>9,709</b>	<b>8,923</b>

GRI 303-1

### WATER CONSUMPTION

The Group uses water resources mainly for the support of generation processes. A small amount of water is used for other business needs and also for water supply to external users.

#### Water withdrawal





The Group's water consumption includes surface, underground and supply system water. Of the water used for operational needs in 2018, 93% was surface water, 4% was underground water and 3% was supply system water. The largest consumer of surface water is CHPP-2, which consumed 2,321 thousand m<sup>3</sup> of water in the reporting year. 81% of this amount was cooling water. The consumption of water resources at CHPP-2 is mainly affected by the operating modes of the generation facilities and the amount of energy generated. The largest consumer of underground water is CHPP-1, which consumed 37 thousand m<sup>3</sup> of underground water to feed the heating networks.

The data on water consumption are based on meter readings.

**GRI** 305-1, 305-4

## DIRECT GREENHOUSE GAS (GHG) EMISSIONS AND EMISSION INTENSITY

The amount of direct greenhouse gas emitted by Latvenergo Group is determined by fuel consumption, the amount of energy generated and the operating modes of the generation plants. CO<sub>2</sub> emissions intensity is measured per unit of electricity generated at the Group and is influenced by the share of renewable energy sources in the consumption of primary energy sources as well as the CHPP generation modes. The lower the specific emissions of CO<sub>2</sub>, the higher the share of electricity generated from renewable energy sources and the more efficient the CHPP equipment.

In 2018, the Group's CO<sub>2</sub> emissions increased by 41% compared to the previous year. Due to dry weather and the low water inflow in the Daugava River, much more electricity was generated by the combined heat and power plants, which use natural gas for energy generation. In addition, more than 20% of the electricity generated in the reporting year was produced in condensation mode, which entails higher emission levels than cogeneration mode.

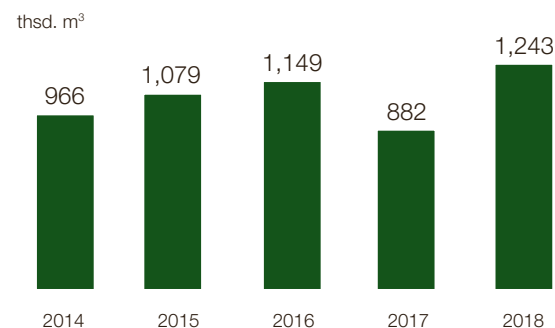
CO<sub>2</sub> emissions are calculated in compliance with the requirements of the emissions permits and legislation of the Republic of Latvia and the EU. The total amount of the Group's emissions is composed of:

- emissions from facilities that participate in the EU Emissions Trading Scheme (combustion plants with total rated thermal input exceeding 20 MW);
- emissions from non-participating facilities, which emitted about 10 thousand tonnes of CO<sub>2</sub> in the reporting year.

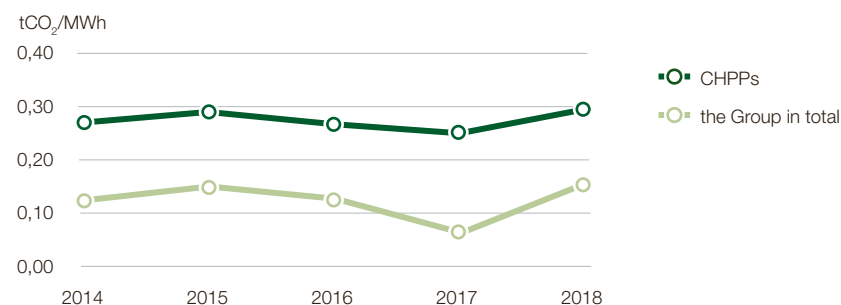
The total amount also includes emissions associated with supporting the energy generation process. In addition to the amount specified, CO<sub>2</sub> is emitted by transport fuel. CO<sub>2</sub> emissions from road vehicles amounted to 8.1 thousand tonnes in 2018.

The Group also operates plants that contain sulphur hexafluoride (SF<sub>6</sub>) gas and cooling installations that contain gases with an insignificant global warming potential. These are closed installations where no gas leakage has been detected; therefore, these gases are not included in the calculation.

### CO<sub>2</sub> emissions from combustion plants



### CO<sub>2</sub> emissions per unit of electricity generated



**GRI** 305-7

## NO<sub>x</sub>, SO<sub>2</sub> AND OTHER SIGNIFICANT AIR EMISSIONS

The emissions of harmful substances into the atmosphere depend directly on the amount of energy generated, the type of fuel used, the efficiency of its consumption and the technology.

- Natural gas is the most environmentally friendly type of fossil fuel, which is used by both Latvenergo AS CHPPs and some Liepaja plants. However, apart from carbon dioxide, combustion of natural gas emits nitrogen oxides (NO<sub>x</sub>) and carbon monoxide (CO) into the atmosphere.
- Latvenergo AS uses diesel as the back-up fuel at the CHPPs. When burning diesel fuel, insignificant amounts of sulphur dioxide (SO<sub>2</sub>) and particulate matter emissions are produced. Diesel fuel emits hydrocarbons during storage.
- Use of wood at the Liepaja plants produces NO<sub>x</sub>, CO and particulate matter emissions.

Emissions amounts from combustion plants that comply with the provisions of the Industrial Emissions Directive are determined on the basis of emissions measurement results. Emissions from small and medium-sized combustion plants (up to 50 MW installed capacity) are calculated using the emissions factors specified by laws and regulations.

#### NO<sub>x</sub>, CO, SO<sub>2</sub> and other emissions

	Units	2014	2015	2016	2017	2018
NO <sub>x</sub>	t	623	737	803	613	904
NO <sub>x</sub> from combustion plants	kg/MWh	0.16	0.17	0.16	0.15	0.18
NO <sub>x</sub> for the Group combined	kg/MWh	0.11	0.12	0.11	0.07	0.12
CO	t	415	319	361	318	426
CO from combustion plants	kg/MWh	0.10	0.08	0.07	0.08	0.09
CO for the Group combined	kg/MWh	0.07	0.05	0.05	0.04	0.06
SO <sub>2</sub>	t	1	4	4	5	5
Other*	t	17	4	17	19	15

\* incl. emissions of solid particles and hydrocarbons

GRI 307-1

#### NON-COMPLIANCE WITH ENVIRONMENTAL LAWS AND REGULATIONS

In 2018, seven scheduled thematic inspections were performed by the State Environmental Service and one scheduled control was carried out by the Health Inspectorate. No significant warnings or sanctions were issued by the regulatory bodies

GRI EU5

#### ALLOCATION OF CO<sub>2</sub> EMISSIONS ALLOWANCES BY CARBON TRADING FRAMEWORK

The EU Emissions Trading Scheme sets forth that free emissions allowances are granted only for thermal energy generation, and the number of allowance units granted will be gradually reduced to 30% of the necessary amount by 2020. One allowance unit is equivalent to one tonne of CO<sub>2</sub> emitted. See Note 13b to the Annual Report for the allowance units purchased, used and sold.

#### CO<sub>2</sub> emission allowances granted

	Units	2014	2015	2016	2017	2018
Riga CHPPs	number	442,778	392,255	343,330	295,942	250,091
Liepaja plants	number	29,025	29,855	21,158	18,218	15,374



## **ANNEXES TO THE SUSTAINABILITY REPORT**

# GREEN BOND REPORT

The green bond programme was launched in June 2015, with the first tranche of EUR 75 million. Thus, Latvenergo AS became the first state-owned company in Eastern Europe to issue green bonds. In April 2016, Latvenergo AS issued additional green bonds in the amount of EUR 25 million, completing the bond programme of EUR 100 million.

The green bonds issued by Latvenergo AS are listed on the Nasdaq Riga AS Baltic Bond List. The ISIN code of the bonds is LV0000801777. The bond issuance was organised by SEB banka AS. The maturity date of the bonds is 10 June 2022, with a fixed annual interest rate (coupon) of 1.9%.

The green bond programme was implemented as a continuation of the Latvenergo AS bond issue launched in 2012 and of the diversification of financing sources. Currently, the total amount of bonds outstanding is EUR 135 million, constituting 17% of the Group's total borrowings.

The main requirement for green bonds is that the funds raised are used exclusively for specified environmental projects, promoting the use of renewable energy sources, energy efficiency, environmental protection and a sustainable environment. The selection criteria

for eligible projects, the selection procedure, creation of a special account and regular reporting are set out in the Latvenergo Green Bond Framework available on the Latvenergo website.





The Green Bond Framework was awarded the highest possible rating – Dark Green – by CICERO, an independent environmental expert. This indicated the compliance of the planned eligible projects with long-term environmental protection and climate change reduction targets as well as good corporate governance and transparency.

On 7 June 2018, Moody's reaffirmed the highest grade – GB1 (excellent) – rating for the green bonds. The bonds have also been assigned the Baa2 rating with a stable outlook, which corresponds to Latvenergo's credit rating. Latvenergo was commended for its transparent and well-considered decision-making process, transparent and comprehensible management of proceeds from the bond issue, and effective reporting and disclosure practices.

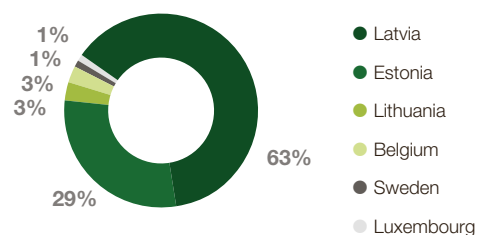
The funds raised within the green bond programme were invested in generation, transmission and distribution projects. The largest eligible projects are the Daugava HPP hydropower unit reconstruction programme and the energy infrastructure project *Kurzeme Ring*.

In 2017, an internal audit was conducted on the management of proceeds from the bond issue and the compliance of the selection of eligible projects with the Green Bond Framework. The audit concluded that the processes had been implemented appropriately.

## The eligible projects of the green bond programme are divided into four groups:

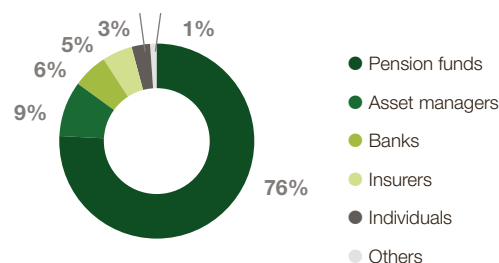
-  *renewable energy* – building of new renewable energy capacities and reconstruction of existing ones – hydropower, bioenergy (non-food), wind energy and related infrastructure;
-  *energy efficiency* – building and reconstruction of transmission and distribution networks to reduce network losses and ensure possibilities for the connection of renewable energy capacities; smart grid projects;
-  *environmental protection* – flood protection, waste management and water resource management;;
-  *sustainable environment* – environmental research and development, and programmes in the areas of environmental protection and biodiversity.

## Investors by region\*



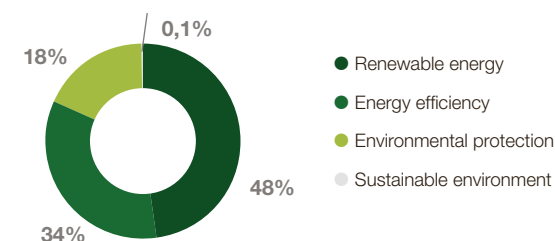
\* according to the coupon payment of June 2018

## Investors by type\*



\*according to the coupon payment of June 2018

## Investment by project group





## Eligible projects of the green bond programme

Group operating segment (share of total eligible costs)	Eligible projects	Eligible costs, EUR million	Project objectives and benefits	
<b>GENERATION</b> 	Reconstruction of hydropower units and technological equipment at Daugava HPPs	47.9	<p>Extending the service life of the hydropower units and increasing their capacity and efficiency ratios. Maintaining a high share of renewables in energy generation. Increasing the safety of operation of the Daugava HPPs. Reducing the oil leakage risk.</p> <p>Implementation of the programme allows for a reduction of CO<sub>2</sub> emissions of up to 16,300 tons per year. In 2018, the share of renewable energy generated by the Group was 47%.</p>	<b>Share of renewable energy generated</b>
	Renovation of hydroengineering structures at the Daugava HPPs and Aiviekste HPP	18.1	Improving the resilience and safety of hydroengineering structures and dams and extending their service life. Reducing accident risk probability at dams and managing flood risk more efficiently, thus diminishing the potential impact on the public, property and the environment.	
	Study of migratory fish replenishment in the Daugava River	0.07	<p>Reducing the impact on biodiversity.</p> <p>Potential measures to offset the impact of the Daugava HPPs on fish stocks more efficiently and to reduce the impact on biodiversity will be identified and explored.</p>	Reconstruction of hydropower units at Daugava HPPs <b>16,300 t/year</b> Reduction in distribution losses since 2014 <b>6,100 tons</b>
<b>DISTRIBUTION</b> 	Building and reconstruction of electricity lines and transformer points	7.2	<p>Reducing the duration of power interruptions and electricity losses. Extending the service life of the distribution grid.</p> <p>Since 2014, interruption duration and interruption frequency indexes have been reduced substantially (SAIFI by 34% and SAIDI by 51%). The reduction of CO<sub>2</sub> emissions a result of the decrease in distribution losses in this period is 6,100 tons.</p>	<b>Reduction of CO<sub>2</sub> emissions*</b>  <b>Reduction in SAIDI since 2014</b>
	Smart electricity meters	1.9	<p>Reducing the duration of power interruptions and electricity losses. Opportunities for more efficient electricity consumption and use of smart energy efficiency products and services.</p> <p>Since 2014, more than 544,000 smart meters have been installed; these account for 49% of the total fleet of electricity meters and measure 83% of the total amount of electricity consumed by customers.</p>	
	Annual monitoring of white storks	0.004	<p>Reducing the impact on biodiversity.</p> <p>Data on the stork population and the proportion of their nests located on electricity line poles have been obtained.</p>	
<b>LEASE OF TRANSMISSION SYSTEM ASSETS</b> 	Second stage of <i>Kurzeme Ring: Grobiņa-Ventspils</i>	24.9	<p>Expanding interconnection capacity (in accordance with the EU climate and energy targets for 2030), which in turn facilitates the integration of renewable energy sources into the transmission grid, increases the security of the electricity supply and promotes competition in the electricity market.</p> <p>The total length of the new 330 kV electricity lines of <i>Kurzeme Ring</i> is set to be around 330 km and the planned capacity is 800 MW. The length of the electricity lines built within the second phase <i>Grobiņa-Ventspils</i> is 117 km.</p>	
<b>TOTAL</b>		<b>100.0</b>		

\* Estimated reduction of CO<sub>2</sub> emissions as a result of reconstruction of the Daugava HPPs' hydropower units – up till 16,300 tons per year (at a CO<sub>2</sub> emissions intensity of 0.383 t CO<sub>2</sub>/MWh when operating Riga CHPP-2 in condensation mode); estimated reduction of CO<sub>2</sub> emissions as a result of reduction of distribution losses since 2014 – 6,100 tons.

# GRI INDEX

## General Disclosures

		Page	External assurance
<b>Organisation profile</b>			
102-1	Name of the organization	8	✓
102-2	Activities, brands, products, and services	8	✓
102-3	Location of headquarters	8	✓
102-4	Location of operations	8	✓
102-5	Ownership and legal form	8	✓
102-6	Markets served	8	✓
102-7	Scale of the organization	8	✓
102-8	Information on employees and other workers	63	✓
102-9	Supply chain	28–29	✓
102-10	Significant changes to the organization and its supply chain	8, 28–29, 35	✓
102-11	Precautionary principle or approach	26–27	✓
102-12	External initiatives	32	✓
102-13	Membership of associations	33	✓
EU1	Installed capacity, broken down by primary energy source and by regulatory regime	37–41	✓
EU2	Net energy output broken down by primary energy source and by regulatory regime	37–42	✓
EU3	Number of residential, industrial, institutional and commercial customer accounts	42, 45	✓
EU4	Length of above and underground transmission and distribution lines by regulatory regime	45–47	✓
EU5	Allocation of CO <sub>2</sub> emissions allowances or equivalent, broken down by carbon trading framework	70	✓
<b>Strategy</b>			
102-14	Statement from senior decision-maker	5–6	✓

		Page	External assurance
<b>Ethics and integrity</b>			
102-16	Values, principles, standards, and norms of behavior	8, 18, 26–27	✓
<b>Governance</b>			
102-18	Governance structure	18–21, 25	✓
<b>Stakeholder engagement</b>			
102-40	List of stakeholder groups	30–32	✓
102-41	Collective bargaining agreements	63	✓
102-42	Identifying and selecting stakeholders	30	✓
102-43	Approach to stakeholder engagement	30	✓
102-44	Key topics and concerns raised	30–32	✓
<b>Reporting practice</b>			
102-45	Entities included in the consolidated financial statements	8	✓
102-46	Defining report content and topic boundaries	50	✓
102-47	List of material topics	51	✓
102-48	Restatements of information	7	✓
102-49	Changes in reporting	7, 50	✓
102-50	Reporting period	7	✓
102-51	Date of most recent report	7	✓
102-52	Reporting cycle	7	✓
102-53	Contact point for questions regarding the report	7	✓
102-54	Claims of reporting in accordance with the GRI Standards	7	✓
102-55	GRI content index	74–76	✓
102-56	External assurance	26–27, 78–79	✓

## Specific standard disclosures

Sustainability topic	Materiality in the Group			GRI Standard	GRI disclosure	Page	External assurance	
	Generation and Trade	Distribution	Lease of Transmission Assets					
ECONOMIC TOPICS								
Efficiency of generation plants	✓			103 Management Approach 2016		52	✓	
				Electric Utilities Sector Disclosures (G4)	EU11	Average generation efficiency of thermal plants	55	✓
					EU30	Average plant availability factor	55-56	✓
Contribution to the economy	✓	✓	✓	103 Management Approach 2016		52–53	✓	
				201 Economic Performance 2016	201-1	Direct economic value generated and distributed	53–54	✓
					201-3	Defined benefit plan obligations and other retirement plans	54	✓
					201-4	Financial assistance received from government	54	✓
Efficiency and availability of distribution system		✓		103 Management Approach 2016		53	✓	
				Electric Utilities Sector Disclosures (G4)	EU12	Distribution losses as a percentage of total energy	55	✓
					EU26	Percentage of population unserved in licensed distribution or service areas	56	✓
					EU27	Number of residential disconnections for non-payment	56	✓
					EU28	Power outage frequency (SAIFI)	56	✓
					EU29	Average power outage duration (SAIDI)	56	✓
Compliance and fair business	✓	✓	✓	103 Management Approach 2016		53	✓	
				205 Anti-corruption 2016	205-2	Communication and training about anti-corruption policies and procedures	55	✓
					205-3	Confirmed incidents of corruption and actions taken	55	✓
				206 Anti-competitive Behavior 2016	206-1	Legal actions for anti-competitive behavior, anti-trust, and monopoly practices	55	✓
				419 Socioeconomic Compliance 2016	419-1	Non-compliance with laws and regulations in the social and economic area	55	✓
SOCIAL TOPICS								
Customer satisfaction	✓	✓		103 Management Approach 2016		57–58	✓	
Emergency planning	✓	✓		103 Management Approach 2016		61	✓	
Occupational health and safety	✓	✓	✓	103 Management Approach 2016		62	✓	
				403 Occupational Health and Safety 2016	403-2	Rates of injury, occupational diseases, lost days, and absenteeism	64	✓
					403-4	Health and safety topics covered in formal agreements with trade unions	65	✓
				Electric Utilities Sector Disclosures (G4)	EU18	Percentage of contractor and subcontractor employees that have undergone relevant health and safety training	65	✓

Sustainability topic	Materiality in the Group			GRI Standard	GRI disclosure	Page	External assurance
	Generation and Trade	Distribution	Lease of Transmission Assets				
Safety of distribution services		✓		103 Management Approach 2016		58–59	✓
				Electric Utilities Sector Disclosures (G4)	EU25 Number of injuries and fatalities to the public involving company assets	60	✓
Public policy engagement	✓	✓	✓	103 Management Approach 2016		61	✓
				415 Public Policy 2016	415-1 Political contributions	61	✓
Employee involvement and development	✓	✓	✓	103 Management Approach 2016		62–63	✓
				402 Labor-Management Relations 2016	402-1 Minimum notice periods regarding operational changes	64	✓
				404 Training and Education 2016	404-1 Average hours of training per year	65	✓
				Electric Utilities Sector Disclosures (G4)	EU15 Percentage of employees eligible to retire in the next 5 and 10 years broken down by job category	65	✓
Personal data security	✓	✓		103 Management Approach 2016		59	✓
				418 Customer Privacy 2016	418-1 Complaints concerning breaches of customer privacy and losses of customer data	60	✓
Information availability	✓	✓		103 Management Approach 2016		59	✓
				417 Marketing and Labeling	417-3 Incidents of non-compliance concerning marketing communications	60	✓
ENVIRONMENTAL TOPICS							
Environmental compliance	✓	✓		103 Management Approach 2016		66–67	✓
				307 Environmental Compliance 2016	307-1 Non-compliance with environmental laws and regulations	70	✓
Air pollution	✓			103 Management Approach 2016		67	✓
				305 Emissions 2016	305-1 Direct (Scope 1) GHG emissions	69	✓
					305-4 GHG emissions intensity	69	✓
					305-7 NO <sub>x</sub> , SO <sub>x</sub> , and other significant air emissions	69–70	✓
Resource and energy consumption	✓			103 Management Approach 2016		67	✓
				301 Materials 2016	301-1 Materials used by weight or volume	68	✓
				302 Energy 2016	302-1 Energy consumption within the organization	68	✓
				303 Water 2016	303-1 Water withdrawal	68–69	✓
Renewable energy	✓			103 Management Approach 2016		67	✓



# ABBREVIATIONS

AS	akciju sabiedrība (Eng. joint-stock company)	SET	subsidised electricity tax
CCO	Chief Commercial Officer	SFRS	State Fire and Rescue Service
CDO	Chief Development Officer	SIA	sabiedrība ar ierobežotu atbildību (Eng. limited liability company)
CEO	Chief Executive Officer	SJSC	state joint-stock company
CFO	Chief Financial Officer	TSO	transmission system operator
CHPP	combined heat and power plant	UAB	uzdaroji akcinē bendrovē (Eng. private limited-liability company)
CICERO	Center for International Climate and Environmental Research – Oslo	WPP	wind power plant
COO	Chief Operating Officer		
COSO	Committee of Sponsoring Organizations of the Treadway Commission		
CTSO	Chief Technology and Support Officer		
CSR	corporate social responsibility		
EC	European Commission		
ECL	Employers' Confederation of Latvia		
EU	European Union		
EU ETS	European Union Emission Trading Scheme		
GHG	greenhouse gas		
GRI	Global Reporting Initiative		
HPP	hydropower plant		
IFRS	International Financial Reporting Standards		
ISIN	International Securities Identification Number		
ISO	International Organization for Standardization		
LGA	local government agency		
LUA	Latvian University of Agriculture		
MP	mandatory procurement		
MPC	mandatory procurement component		
OHSAS	Occupational Health and Safety Assessment Series of Standards		
OÜ	osaühing (Eng. private limited company)		
PUC	Public Utilities Commission		
RTU	Riga Technical University		
SAIDI	system average interruption duration index		
SAIFI	system average interruption frequency index		
SES	Stakeholder Engagement Standard		



# INDEPENDENT PRACTITIONER'S ASSURANCE REPORT ON THE SUSTAINABILITY REPORT

## **To the Management Board of Latvenergo AS**

We have undertaken a limited assurance engagement in respect of the Sustainability report of Latvenergo AS ('the Company') and its subsidiaries ('Latvenergo Group') for the year ended 31 December 2018 on pages 4 to 77 of the 2018 Sustainability and Annual report of Latvenergo AS ('the 2018 Sustainability report').

### *Management's Responsibility*

The Management of the Company is responsible for the preparation and presentation of the 2018 Sustainability report, in accordance with the requirements of the Core level application of Global Reporting Initiative Guidelines ("GRI Guidelines"), issued by Global Reporting Initiative, a network-based non-profit organization with secretariat based in Amsterdam, the Netherlands (the "reporting criteria"). This responsibility includes the design, implementation and maintenance of internal control relevant to the preparation of the 2018 Sustainability Report that is free from material misstatement, whether due to fraud or error.

### *Our Responsibility*

Our responsibility is to express a limited assurance conclusion, based on our limited assurance procedures, on whether anything has come to our attention to indicate that the 2018 Sustainability report is not prepared, in all material respects, in accordance with the reporting criteria.

We conducted our limited assurance engagement in accordance with the International Standard on Assurance Engagements (ISAE) 3000, 'Assurance engagements other than audits or reviews of historical financial information', issued by the International Auditing and Assurance Standards Board. This Standard requires that we comply with ethical requirements and plan and perform the assurance engagement to obtain limited assurance about whether the 2018 Sustainability report is free from material misstatement.

This report, including the conclusion, has been prepared solely for the Management of the Company, to assist the Management in reporting on the Company's and Latvenergo Group's sustainability performance and activities. We permit the disclosure of this report within the 2018 Sustainability and Annual report.

To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Management of the Company, and the Company for our work or this report.

### *Independence and Quality Control*

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

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

### *Summary of the Work Performed*

Our procedures included examination, on a test basis, of evidence relevant to the 2018 Sustainability report. It also included an assessment of the significant estimates and judgements made by the Management in the preparation of the 2018 Sustainability report in accordance with the GRI guidelines.

Our work consisted of:

- Interviewing the management and senior executives to evaluate the application of the GRI guidelines and to obtain an understanding of the control environment related to sustainability reporting;
- Obtaining an understanding of the relevant processes for collecting, processing and presenting data included in the 2018 Sustainability report;
- Verifying the information included in the 2018 Sustainability report through inquiries to the relevant management personnel of the Company and its subsidiaries;



- Testing data included in the 2018 Sustainability report on a selective basis;
- Inspecting documentation to corroborate statements of management and senior executives in our interviews.
- Comparing the financial data included in the 2018 Sustainability report to the 2018 financial statements of Latvenergo Group; and
- Evaluating the overall format and content of the 2018 Sustainability report, taking into account the compliance of the disclosed information with the applicable criteria.

A limited assurance engagement is substantially less in scope than a reasonable assurance engagement in relation to both the risk assessment procedures, including an understanding of internal control, and the procedures performed in response to the assessed risks.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our limited assurance conclusion.

#### *Inherent Limitations*

Non-financial data is subject to more inherent limitations than financial data, given both the nature and the methods used for determining, calculating, sampling or estimating such data.

Qualitative interpretations of relevance, materiality and the accuracy of data are subject to individual assumptions and judgments.

We have not carried out any work on data reported for prior reporting periods nor in respect of future projections and targets included in the 2018 Sustainability report.

#### *Limited Assurance Conclusion*

Based on our work performed, nothing has come to our attention that causes us to believe that the 2018 Sustainability report is not prepared, in all material respects, in accordance with the reporting criteria.

PricewaterhouseCoopers SIA  
Certified audit company  
Licence No. 5

Juris Lapshe  
Certified auditor in charge  
Certificate No.116  
Persona per Procura

Rīga, Latvija  
16 April 2018



# LATVENERGO GROUP KEY FIGURES

## Financial figures

EUR'000

	2018	2017	2016	2015	2014
Revenue	878,008	925,627	931,619	929,128	1,010,757
EBITDA <sup>1)</sup>	321,582	541,696	393,399	307,015	236,838
Operating profit <sup>2)</sup>	95,762	234,082	160,773	108,188	49,243
Profit before tax <sup>3)</sup>	88,513	224,114	148,945	92,535	31,510
Profit	75,955	322,021	130,593	85,039	29,790
Dividends <sup>4)</sup>	156,418	90,142	77,413	31,479	23,605
Total assets	3,798,819	4,415,725	3,901,231	3,517,372	3,486,576
Non-current assets	3,364,534	3,343,404	3,388,954	3,113,719	3,109,253
Total equity	2,320,065	2,846,891	2,418,713	2,096,702	2,020,801
Borrowings	814,343	826,757	791,566	797,483	827,222
Net debt <sup>5)</sup>	684,888	590,754	607,586	692,940	706,211
Net cash flows from operating activities	302,869	338,209	341,186	246,278	135,329
Investments	220,607	243,811	200,677	190,461	177,607

In order to ensure an objective and comparable presentation of the financial results, Latvenergo Group and Latvenergo AS uses various financial figures and ratios that are derived from the financial statements.

Based on the most commonly used financial figures and ratios in the industry, the Latvenergo Group Strategy for 2017-2022 (see also the Management Report – section Further development, and Sustainability Report), as well as the binding financial covenants set in the Group's loan agreements, Latvenergo Group has set and therefore uses the following financial figures and ratios:

- profitability measures – EBITDA<sup>1)</sup>; EBITDA margin<sup>6)</sup>; operating profit margin<sup>7)</sup>; profit before tax margin<sup>8)</sup>; profit margin<sup>9)</sup>; return on assets (ROA)<sup>14)</sup>; return on equity (ROE)<sup>15)</sup>; return on capital employed (ROCE)<sup>16)</sup>;
- capital structure measures – net debt<sup>5)</sup>; equity-to-asset ratio<sup>10)</sup>; net debt / EBITDA<sup>11)</sup>; net debt / equity<sup>12)</sup>; current ratio<sup>13)</sup>;
- a dividend policy measure – dividend pay-out ratio<sup>17)</sup>.

The definitions and components of the financial figures and ratios are described below. The reported financial figures and ratios have not changed over previous period.

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

<sup>2)</sup> Operating profit – earnings before income tax, finance income and costs

<sup>3)</sup> Profit before tax – earnings before income tax

<sup>4)</sup> Dividends paid to the equity holder of the Parent Company.  
(see Note 20 b)

<sup>5)</sup> Net debt = borrowings at the end of the year minus cash and cash equivalents at the end of the year

## Financial ratios

	2018	2017	2016	2015	2014
EBITDA margin <sup>6)</sup>	36.6%	58.5%	42.2%	33.0%	23.4%
Operating profit margin <sup>7)</sup>	10.9%	25.3%	17.3%	11.6%	4.9%
Profit before tax margin <sup>8)</sup>	10.1%	24.2%	16.0%	10.0%	3.1%
Profit margin <sup>9)</sup>	8.7%	34.8%	14.0%	9.2%	2.9%
Equity-to-asset ratio <sup>10)</sup>	61%	64%	62%	60%	58%
Net debt / EBITDA <sup>11)</sup>	2.0	1.1	1.7	2.3	2.9
Net debt / equity <sup>12)</sup>	0.30	0.21	0.25	0.33	0.35
Current ratio <sup>13)</sup>	1.5	3.2	1.7	1.9	1.3
Return on assets (ROA) <sup>14)</sup>	1.8%	7.7%	3.5%	2.4%	0.8%
Return on equity (ROE) <sup>15)</sup>	2.9%	12.2%	5.8%	4.1%	1.5%
Return on capital employed (ROCE) <sup>16)</sup>	2.8%	6.8%	5.3%	3.8%	1.7%
Dividend pay-out ratio <sup>17)</sup>	104%	66%	82%	90%	92%

## Operational figures

	2018	2017	2016	2015	2014
Total electricity supply, incl.:					
Retail*	GWh 6,954	6,923	7,665	7,961	8,800
Wholesale**	GWh 3,030	3,448	2,474	1,907	627
Electricity generated	GWh 5,076	5,734	4,707	3,882	3,625
Thermal energy generated	GWh 2,274	2,612	2,675	2,408	2,560
Number of employees	3,508	3,908	4,131	4,177	4,563
Moody's credit rating	Baa2 (stable)	Baa2 (stable)	Baa2 (stable)	Baa2 (stable)	Baa3 (stable)

\* Including operating consumption

\*\* Including sale of energy purchased within the mandatory procurement on the Nord Pool

<sup>6)</sup> EBITDA margin = EBITDA / revenue

<sup>7)</sup> Operating profit margin = operating profit / revenue

<sup>8)</sup> Profit before tax margin = profit before tax / revenue

<sup>9)</sup> Profit margin = profit / revenue

<sup>10)</sup> Equity-to-asset ratio = total equity at the end of the year / total assets at the end of the year

<sup>11)</sup> Net debt / EBITDA = (net debt at the beginning of the year + net debt at the end of the year) \* 0.5 / EBITDA (12-months rolling)

<sup>12)</sup> Net debt / equity = net debt at the end of the year / equity at the end of the year

<sup>13)</sup> Current ratio = current assets at the end of the year / current liabilities at the end of the year

<sup>14)</sup> Return on assets (ROA) = profit / average value of assets ((assets at the beginning of the year + assets at the end of the year) / 2)

<sup>15)</sup> Return on equity (ROE) = profit / average value of equity ((equity at the beginning of the year + equity at the end of the year) / 2)

<sup>16)</sup> Return on capital employed (ROCE) = operating profit / (average value of equity ((equity at the beginning of the year + equity at the end of the year) / 2) + average value of borrowings ((borrowings at the beginning of the year + borrowings at the end of the year) / 2))

<sup>17)</sup> Dividend pay-out ratio = dividends / profit of the Parent Company



# LATVENERGO AS KEY FIGURES

## Financial figures

EUR'000

	2018	2017	2016	2015	2014*
Revenue	435,199	498,580	513,563	521,146	564,550
EBITDA <sup>1)</sup>	160,927	387,100	241,606	180,982	105,052
Operating profit <sup>2)</sup>	33,803	177,416	141,071	90,475	18,158
Profit before tax <sup>3)</sup>	212,760	185,906	156,290	103,212	35,045
Profit	212,733	150,891	137,441	94,750	34,800
Dividends <sup>4)</sup>	156,418	90,142	77,413	31,479	23,605
Total assets	3,141,109	3,649,200	3,204,394	3,124,054	3,104,592
Non-current assets	2,661,307	2,546,014	2,626,560	2,638,048	2,634,150
Total equity	1,993,823	2,382,638	2,177,069	2,114,900	2,047,666
Borrowings	802,268	814,772	778,323	782,965	810,681
Net debt <sup>5)</sup>	674,714	581,917	597,126	681,146	721,715
Net cash flows from operating activities	394,395	449,352	201,427	174,797	94,604
Investments	41,350	89,278	79,913	78,694	52,465

\* All financial figures for 2014 re-measured according to IFRS principles

## Financial ratios

	2018	2017	2016	2015	2014
EBITDA margin <sup>6)</sup>	37.0%	77.6%	47.0%	34.7%	18.6%
Operating profit margin <sup>7)</sup>	7.8%	35.6%	27.5%	17.4%	3.2%
Profit before tax margin <sup>8)</sup>	48.9%	37.3%	30.4%	19.8%	6.2%
Profit margin <sup>9)</sup>	48.9%	30.3%	26.8%	18.2%	6.2%
Equity-to-asset ratio <sup>10)</sup>	63%	65%	68%	68%	66%
Net debt / equity <sup>11)</sup>	0.34	0.24	0.27	0.32	0.35
Current ratio <sup>12)</sup>	2.0	4.3	2.3	3.0	1.9
Return on assets (ROA) <sup>13)</sup>	6.3%	4.4%	4.3%	3.0%	1.1%
Return on equity (ROE) <sup>14)</sup>	9.7%	6.6%	6.4%	4.6%	1.7%
Return on capital employed (ROCE) <sup>15)</sup>	1.1%	5.8%	4.8%	3.1%	0.6%
Dividend pay-out ratio <sup>16)</sup>	104%	66%	82%	90%	92%

## Operational figures

		2018	2017	2016	2015	2014
Retail electricity supply	GWh	4,406	4,619	5,290	5,422	5,748
Electricity generated	GWh	5,028	5,687	4,660	3,833	3,577
Thermal energy generation	GWh	2,007	2,354	2,422	2,179	2,312
Number of employees		1,355	1,431	1,472	1,464	1,439
Moody's credit rating		Baa2 (stable)	Baa2 (stable)	Baa2 (stable)	Baa2 (stable)	Baa3 (stable)

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

<sup>2)</sup> Operating profit – earnings before income tax, finance income and costs

<sup>3)</sup> Profit before tax – earnings before income tax

<sup>4)</sup> Dividends paid to the equity holder of the Parent Company.

(see Note 20 b)

<sup>5)</sup> Net debt = borrowings at the end of the year minus cash and cash equivalents at the end of the year

<sup>6)</sup> EBITDA margin = EBITDA / revenue

<sup>7)</sup> Operating profit margin = operating profit / revenue

<sup>8)</sup> Profit before tax margin = profit before tax / revenue

<sup>9)</sup> Profit margin = profit / revenue

<sup>10)</sup> Equity-to-asset ratio = total equity at the end of the year / total assets at the end of the year

<sup>11)</sup> Net debt / equity = net debt at the end of the year / equity at the end of the year

<sup>12)</sup> Current ratio = current assets at the end of the year / current liabilities at the end of the year

<sup>13)</sup> Return on assets (ROA) = profit / average value of assets ((assets at the beginning of the year + assets at the end of the year) / 2)

<sup>14)</sup> Return on equity (ROE) = profit / average value of equity ((equity at the beginning of the year + equity at the end of the year) / 2)

<sup>15)</sup> Return on capital employed (ROCE) = operating profit / (average value of equity ((equity at the beginning of the year + equity at the end of the year) / 2) + average value of borrowings ((borrowings at the beginning of the year + borrowings at the end of the year) / 2))

<sup>16)</sup> Dividend pay-out ratio = dividends / profit of the Parent Company

# MANAGEMENT REPORT

Latvenergo Group (the Group) is one of the largest power supply providers in the Baltics operating in electricity and thermal energy generation and trade, natural gas trade, electricity distribution services and lease of transmission system assets.

## *Latvenergo Group – one of the largest power suppliers in the Baltics*

The parent company of Latvenergo Group is Latvenergo AS which is a power supply utility operating in electricity and thermal energy generation and trade, as well as natural gas trade in Latvia.

## OPERATING ENVIRONMENT

In 2018, electricity prices increased significantly in the Nordics and the Baltics compared to the previous year. The increase in electricity prices was affected by the warm, dry weather in Europe, which resulted in lower water levels at the Scandinavian hydropower reservoirs and lower output of hydroelectricity. The insufficient electricity output at hydropower plants (HPPs) and wind farms fostered the increase in electricity generation at fossil fuel power stations. The cost of electricity generated at fossil fuel power stations was affected negatively by higher raw material prices and CO<sub>2</sub> emission allowance prices. The electricity spot price in Latvia was 44% higher than year ago reaching almost 50 EUR/MWh.

## *Electricity prices increased by more than 40% in the Baltics*

Due to the increase in oil, coal and CO<sub>2</sub> emission prices, there was an increase in the price of natural gas. In 2018, the average price of natural gas at the GASPOOL and TTF trading platforms was 30% higher than a year earlier.

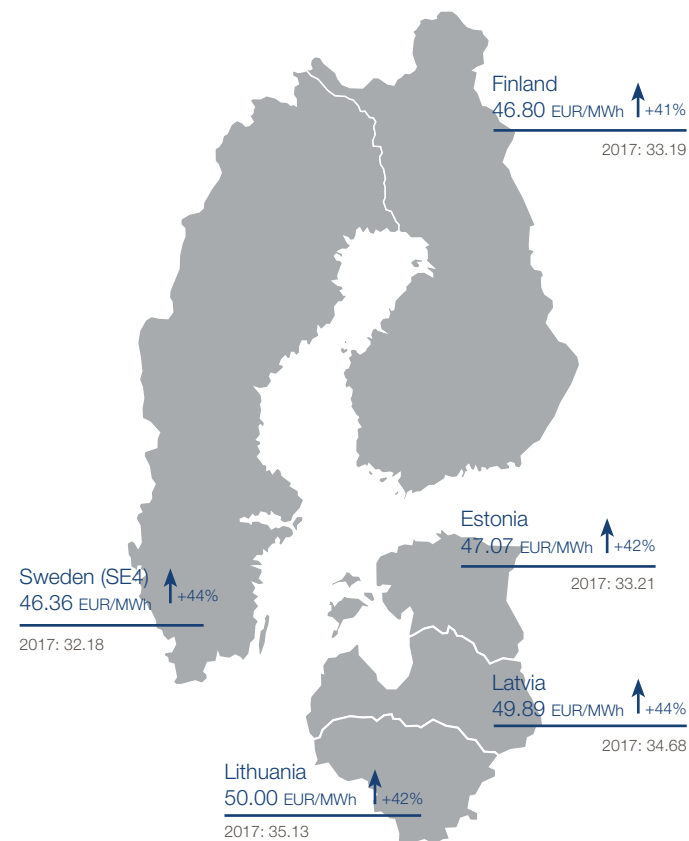
## SIGNIFICANT EVENTS

### CHANGES IN THE CAPACITY SUPPORT PAYMENT FOR LATVENERGO AS CHPPS

In October 2017, Latvenergo AS applied for a one-off compensation from the state, at the same time opting out of the receipt of 75% of the annual electrical capacity payments for cogeneration power plants CHPP-1 and CHPP-2. On 21 November 2017, the Cabinet of Ministers of the Republic of Latvia accepted an order which supports the reduction of the guaranteed support payments during the remaining support period for the installed capacity of Latvenergo AS CHPPs by paying out a one-off compensation in the amount of EUR 454.4 million, financed by the capital release of Latvenergo AS. The compensation was divided into two parts: EUR 140 million were to be recognised as other income in the profit or loss statement of Latvenergo AS in 2017, while EUR 314.4 million were to be recognised as income spread evenly over the following reporting periods until fulfilment of liabilities at the end of the support period on 23 September 2028.

On 26 September 2018, the Cabinet of Ministers decided to change conditions for a part of the grant in the amount of EUR 51.7 million stipulating it as unconditional, by reducing the remaining part of the compensation proportionally to this amount until the end of the support period. In 2018, EUR 81.0 million were recognised as other income of Latvenergo AS (in 2017: EUR 140 million).

### Electricity wholesale price on Nord Pool power exchange



### CHANGES IN CIT APPLICATION PROCEDURE

As of 1 January 2018 the application procedure for corporate income tax (CIT) in Latvia has changed. New CIT regulation eliminated all temporary differences between the financial accounting basis and tax basis of assets and liabilities as of 1 January 2018. As of 1 January 2018 distributed profits and conditionally distributed profits are taxed at a rate of 20% of the gross amount or 20/80 of the net amount. The Group recognises deferred tax liabilities in the balance sheet for the expected dividend payments of subsidiaries.

## OPERATING RESULTS

### GENERATION

In 2018, the total amount generated by Latvenergo Group's power plants comprised 5,076 GWh of electricity and 2,274 GWh of thermal energy (Latvenergo AS – 5,028 GWh and 2,007 GWh respectively).

Latvenergo AS CHPPs played a significant role in ensuring electricity demand this year. Dry weather significantly decreased output of hydroelectricity in Latvia and entire *Nord Pool* region and this led to a rapid rise in electricity prices throughout region.

*Electricity output at the Latvenergo AS CHPPs increased by 87%*

In 2018, the amount of power generated at the Daugava HPPs decreased by 44% compared to a year earlier and reached 2,380 GWh. The amount of power generated at the Daugava HPPs was impacted by almost twice lower water inflow in the river Daugava compared to the previous year. According to data from the Latvian Environment, Geology and Meteorology Centre, the average water inflow in the Daugava River in 2018 was 485 m<sup>3</sup>/s, which is 81% of the average long-term inflow. In 2018, the share of electricity generated from renewable energy sources at Latvenergo Group was 47% (in 2017 it was 75%).

The Latvenergo AS CHPPs operated in a market conjuncture by effectively planning operating modes and fuel consumption. The dry weather and higher electricity prices throughout the *Nord Pool* region contributed to an increase in electricity generation at Latvenergo AS CHPPs. In 2018, the amount increased by 87% compared to a year earlier, reaching 2,644 GWh. If the Latvenergo AS CHPPs were not available for generation in Latvia, we would have to use more expensive energy resources, for example a natural gas station in Lithuania or coal stations in Poland, to satisfy demand.

In 2018, the total amount of thermal energy generated by Latvenergo Group decreased by 13% compared to the previous year. The decrease was impacted by increasing competition in the thermal energy market. At the end of 2017 and at the beginning of 2018 four new competitors entered the territory of the Latvenergo AS CHPPs.

### TRADE

Latvenergo Group is one of the largest energy trading companies in the Baltics. With the launch of natural gas trade to business customers in Lithuania in October 2018, the Group now operates in all segments of the market in Latvia, Lithuania and Estonia.

*Latvenergo group operates in all energy trade segments in Latvia, Lithuania and Estonia*

In the reporting year, the Group supplied 7.0 TWh of electricity to retail customers, which is approximately the same as the previous year. The overall amount of retail electricity trade outside Latvia accounted for 1/3 of the total, reaching 2.5 TWh. The electricity trade volume in Latvia was 4.4 TWh, while in Lithuania it was 1.6 TWh and in Estonia it was 0.9 TWh. The total number of electricity customers comprises approximately 800 thousand, including more than 35 thousand foreign customers.

The amount of natural gas supplied to business customers continued to increase in the reporting year. As of 31 December 2018, the total amount of customers exceeds 400, and natural gas sales to these

customers amounted to 0.15 TWh. In the reporting year, the amount of natural gas used for both operating consumption and trade reached 6.9 TWh. Currently, Latvenergo Group is the second largest natural gas consumer in the Baltics. After the reporting year, in February 2019, Latvenergo expanded the range of services it provides to customers, thus implementing the goal set in the Latvenergo AS strategy, which is to develop new business directions. Under the Elektrum brand, it launched natural gas trade to households in Latvia.

In 2018 the retail activities of other products and services in the Baltic states continued. In the reporting year, we launched trade of *Elektrum Solārais* in Estonia. In 2018 we installed solar panels for about 70 customers in the Baltics. Also, the number of *Elektrum Insured* customers continued to increase, reaching more than 41,000 at the end of 2018.

## FINANCIAL RESULTS

In 2018, Latvenergo Group's revenue decreased by 5% and comprised EUR 878.0 million. Meanwhile, EBITDA decreased by 41% and reached EUR 321.6 million. In 2018 Group's profit amounted to EUR 76.0 million.

The Group's results in the reporting year were mainly negatively impacted by:

- 44% lower electricity output at the Daugava HPPs;
- 75% lower revenue from the installed electrical capacity at the Latvenergo AS CHPPs;
- Changes in the application procedure for corporate income tax. In 2017 the Group's profit consisted of the annual operating result in the amount of EUR EUR 172.9 million and a deferred tax reversal in the amount of EUR 149.1 million as a result of the corporate income tax reform.

The Group's ROE in 2018 reaches 2.9%. The 2018 financial indicators of the capital structure ensured achievement of the set goals, exceeding average industry indicators as well. For information on achievement of the financial goals, see the Sustainability Report section "Group Strategy".

## INVESTMENTS

In 2018, the total amount of investment decreased by 10% compared to the previous year; it comprised EUR 220.6 million.

Latvenergo AS investment amounted EUR 41.4 million in 2018 (2017: EUR 89.3 million).

To ensure high quality power network service, technical parameters and operational safety, a significant amount is invested in the modernisation of the power network. In the reporting year, the amount invested in power network assets represented 82% of total investment.

### *Investment in power network assets – 82% of the total amount*

Investments in distribution assets during the reporting year reached EUR 95.1 million. The purpose of investments in the distribution segment is to promote the quality and security of the energy supply, reduce the frequency and duration of power supply disruptions caused by planned and unplanned maintenance, and ensure the appropriate voltage quality. Investments in modernisation of distribution assets have increased the quality of distribution services by lowering SAIFI and SAIDI indicators. In 2018, SAIDI has decreased by 13% and SAIFI has decreased by 11%.

During the reporting year, investment in transmission system assets was in the amount of EUR 87.1 million. The amount of investments increased by 38% compared to the previous year. The largest investment was made in the energy infrastructure project *Kurzeme Ring*. In 2018, EUR 65.2 million was invested in this project. The Kurzeme Ring project will increase the safety level of power supply in the Kurzeme region and Latvia as a whole, providing an opportunity for more efficient use of the Lithuania-Sweden marine cable NordBalt and allowing further integration of the Baltics into the Nordic electricity market.

Contributing to environmentally friendly projects, in 2018, EUR 21.1 million was invested in the Daugava HPPs' hydropower unit reconstruction. Gradual overhaul of eleven Daugava HPPs hydropower units is planned for completion until 2022. It will provide for further 40-year operation of the units. As of 31 December 2018, four reconstructed hydropower units have been put into operation within the programme. The estimated total reconstruction costs will exceed EUR 200 million. At the end of the reporting year, work completed within the scope of the contract reached EUR 149.5 million.

## FUNDING

### *Diversified sources of funding*

Latvenergo Group finances its investments from its own resources and external long-term borrowings, which are regularly sourced in financial and capital markets in a timely manner.

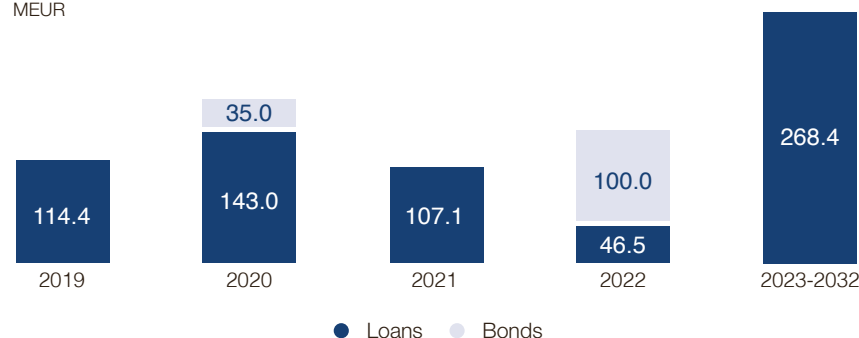
At the end of 2018, Latvenergo AS has committed loans from several banks for implementation of investment projects and in order to ensure loan refinancing risk management for a total amount of EUR 240 million with a repayment term of 7 and 10 years.

As of 31 December 2018, the Group's borrowings amount to EUR 814.3 million (31 December 2017: EUR 826.8 million), comprising loans from commercial banks, international investment banks, and bonds amounting to EUR 135 million, of which EUR 100 million are *green* bonds.

### **Latvenergo Group's debt repayment schedule**

Total borrowings as of 31 December 2018 – 814.3 MEUR

MEUR



As of 31 December 2018, the net borrowings of Latvenergo Group are EUR 684.9 million (31 December 2017: EUR 590.8 million), while the net debt / EBITDA ratio is 2.0 (31 December 2017: 1.1).

Moody's credit rating for Latvenergo AS has been stable for several years and is at the Baa2 level with a stable future outlook. The last credit rating affirmation was on 19 March 2019.

## CORPORATE GOVERNANCE

In the reporting year, we successfully continued to improve our corporate governance. In 2018, the Corporate Governance Policy was updated and corporate governance principles were published on the Latvenergo website.

In 2018, the Supervisory Board of Latvenergo AS established the Strategic Communication Committee with the aim of ensuring the supervisory functions of the Supervisory Board within the scope of the strategic communication of Latvenergo AS. The Committee consists of the Members of the Supervisory Board.

Along with the financial results of Latvenergo Group, also the Corporate Governance Report of Latvenergo AS for 2018 is published. The company has complied with all applicable principles of corporate governance in all key material aspects.

## NON-FINANCIAL REPORT

Latvenergo Group has prepared a non-financial report in accordance with the Law on the Financial Instruments Market (Article 56<sup>4</sup>).

*Non-financial report is in accordance with the GRI Standards*

For detailed information on Corporate Social Responsibility (hereinafter – CSR) activities, description of the policies and procedures in relation to those matters, the outcome of the policies, risks and risk management, and non-financial key performance indicators, please see the Sustainability Report 2018 which is available on the Latvenergo website: <http://www.latvenergo.lv>. The report is prepared in accordance with the GRI Standards – Core option requirements.

The sustainability report addresses such topics as corporate social responsibility, economic performance, society, product responsibility, environmental protection, employees and the work environment etc.

### CORPORATE SOCIAL RESPONSIBILITY

Latvenergo Group not only complies with statutory requirements, but also performs voluntary activities aimed at improving the public welfare and the environment and follows the principles of social responsibility in compliance with ISO 26000 in its daily operations.

Latvenergo CSR Policy specifies the basic CSR forms, principles, directions and selection criteria for activities. The Group supports CSR activities in line with its operations and strategic goals, contributing to raising public awareness of responsible business conduct and the energy industry, making a substantial long-term impact and ensuring the involvement of large groups of society.

### ECONOMIC PERFORMANCE

Latvenergo Group is one of the largest provider of power supply services and the most valuable power utility in the Baltic countries. The economic performance of the Group includes the commitment to encourage sustainable use of resources and long-term economic growth. The Group implements this commitment by offering modern and competitive products and services and by investing wisely in energy

production and power network development. Efficiency plays an important role across the whole energy production and supply process, thus improving the competitiveness and quality of services.

### SOCIETY

Responsibility is one of Latvenergo Group's values and a fundamental principle of corporate governance. The Group's management and employees undertake responsibility for tasks performed in compliance with the requirements of applicable laws and regulations and with best practice. Latvenergo Group conducts business in a transparent, ethical, safe, reliable and fair manner, ensuring provision of information to stakeholders and engaging them in its activities.

### PRODUCT RESPONSIBILITY

Latvenergo Group's operations are targeted at developing and offering competitive electricity services that meet customers' needs as well as building long-term, mutually beneficial and loyal relationships with customers. In turn, distribution services are based on the provision of high quality and secure electricity supply in Latvia. To achieve these goals, the Group follows the principles of cost effectiveness and operational excellence.

### ENVIRONMENTAL PROTECTION

Latvenergo Group is aware of the role of environmental protection in sustainable development and implements its key principles in all its operations. The Latvenergo Group Strategy has set environmental protection as one of its priorities in energy generation and supply processes.

### EMPLOYEES AND THE WORK ENVIRONMENT

Latvenergo Group's management acknowledges that its employees, with their diversity and variety of competences, provide a valuable opportunity to view operational aspects from different perspectives and thus achieve better results. The Group attracts and develops employees capable of driving its advancement. The Group ensures that its employees' competences contribute to the achievement of goals and future needs. Employee engagement and desire to implement innovative ideas in both improving the work environment and enhancing the Group's competitiveness is an important resource.

## FURTHER DEVELOPMENT

Latvenergo Group's strategy for 2017–2022 foresees:

- strengthening of a sustainable and economically sound market position in core markets (in the Baltics) while considering geographic and / or product / service expansion;
- development of a generation portfolio that fosters synergy with trade and that promotes an increase in value for the Group;
- development of a customer-driven, functional, safe and efficient power network.

### *Comprehensive Efficiency Programme*

Programme in 2017. While the strategic development section includes major strategic projects, the efficiency section provides for the revision, centralisation and digitalisation of the Group's processes in order to maintain the Group's profitability in the long term considering the increase in costs due to inflation.

Taking into consideration the defined development directions of the Group, Latvenergo AS approved the Strategic Development and Efficiency



The estimated efficiency potential for the Group's EBITDA is up to EUR 30 million. This is the Group's largest optimisation plan in the last decade, and it will allow the Group to increase its value in the long run and to remain competitive in an open market and a changing energy industry.

The activities planned in the strategy have been successfully implemented in 2018. For more information, please see the Sustainability Report section "Group Strategy".

Along with the strategy approval, Latvenergo Group's financial targets have been set. The targets are divided into three groups – profitability, capital structure and dividend policy.

The financial targets are set to ensure:

- ambitious, yet achievable profitability, which is consistent with the average ratios of benchmark companies in the European energy sector and provides for an adequate return on the business risk;
- an optimal and industry-relevant capital structure that limits potential financial risks;
- an adequate dividend policy that is consistent with the planned investment policy and capital structure targets.

Target group	Ratio	Year 2022
Profitability	Return on equity	> 6%
	Net debt to equity	< 50%
Capital structure	Net debt to EBITDA	< 3 times
	Dividend pay-out ratio	> 80%

## FINANCIAL RISK MANAGEMENT

The activities of Latvenergo Group and Latvenergo AS are exposed to a variety of financial risks: market risks, credit risk, and liquidity and cash flow risk. Latvenergo Group's Financial Risk Management Policy focuses on eliminating the potential adverse effects from such risks on financial performance. In the framework of financial risk management, Latvenergo Group and Latvenergo AS use various financial risk controls and hedging to reduce certain risk exposures.

### a) Market risks

#### i) Price risk

Price risk might negatively affect the financial results of the Group and the Parent Company due to falling revenue from generation and a mismatch between floating market prices and fixed retail prices.

The main sources of Latvenergo Group's and Latvenergo AS exposure to price risk are the floating market prices of electricity on the *Nord Pool* power exchange in Baltic bidding areas and the fuel price for CHPPs. The financial results of the Group and the Parent Company may be negatively affected by the volatility of the electricity market price, which depends on the weather conditions in the Nordic countries, global prices of resources, and the influence of local factors (water availability and ambient air temperature) on electricity generation opportunities. Due to supply-demand factors and seasonal fluctuations, natural gas price volatility may have a negative effect on the difference between fixed retail electricity prices in contracts with customers and variable generation costs at CHPPs.

In order to hedge the price risk, the Group and the Parent Company enter into long-term fixed price customer contracts, use electricity financial derivatives and enter into fixed price contracts for natural gas supply. The impact of price risk on generation is hedged gradually – 80%–90% of projected electricity output is sold prior to the upcoming year. Further hedging of risk is limited by the seasonal generation pattern of the Daugava HPPs.

### ii) Interest rate risk

Latvenergo Group's and Latvenergo AS interest rate risk mainly arises from non-current borrowings at variable interest rates. They expose the Group and the Parent Company to the risk that finance costs might increase significantly when the reference rate surges. Most of the borrowings from financial institutions have a variable interest rate, comprising 6 or 12-month EURIBOR and a margin. The Group's Financial Risk Management Policy stipulates maintaining at least 35% of its borrowings as fixed interest rate borrowings (taking into account the effect of interest rate swaps and issued bonds) with a duration of 2–4 years. Taking into account the effect of interest rate swaps and bonds with a fixed interest rate, 53% of the Group's and 54% of the Parent Company's borrowings had a fixed interest rate with an average period of 2.1 years both for the Group and the parent Company as of 31 December 2018.

### iii) Currency risk

Foreign currency exchange risk arises when future transactions or recognised assets or liabilities are denominated in a currency other than the functional currency which is euro.

As of 31 December 2018, all borrowings of Latvenergo Group and Latvenergo AS are denominated in euros, and during the reporting year, there was no substantial exposure to foreign currency risk in relation to the Group's investments. All revenues of Latvenergo Group and Latvenergo AS are generated in euros.

To manage the Group's and the Parent Company's foreign currency exchange risk arising from future transactions and recognised assets and liabilities, the Financial Risk Management Policy envisages use of forward contracts.

#### b) Credit risk

Credit risk is managed at the Latvenergo Group level. Credit risk arises from cash and cash equivalents, derivative financial instruments and deposits with banks, and receivables. Credit risk exposure of receivables is limited due to the large number of Group customers as there is no significant concentration of credit risk with any single counterparty or group of counterparties with similar characteristics.

Credit risk related to cash and short-term deposits with banks is managed by balancing the placement of financial assets in order to simultaneously choose the best offers and reduce the probability of incurrence of loss. No credit limits were exceeded during the reporting year, and the management does not expect any losses due to the occurrence of credit risk.

#### c) Liquidity risk and cash flow risk

Latvenergo Group's liquidity and cash flow risk management policy is to maintain a sufficient amount of cash and cash equivalents and the availability of long and short-term funding through an adequate amount of committed credit facilities in order to meet existing and expected commitments and compensate for fluctuations in cash flows due to the occurrence of a variety of financial risks. On 31 December 2018, Latvenergo Group's liquid assets (cash and short-term deposits up to 3 months) reached EUR 129.5 million (31/12/2017: EUR 236.0 million), while the Latvenergo AS liquid assets reached EUR 127.6 million (31/12/2017: EUR 232.9 million).

The Group and the Parent Company continuously monitor cash flow and liquidity forecasts, which comprise the undrawn borrowing facilities and cash and cash equivalents.

## EVENTS AFTER THE REPORTING PERIOD

All significant events that would materially affect the financial position of the Latvenergo Group and Latvenergo AS after the reporting period are disclosed in Note 30 of the Group's and the Parent Company's Financial Statements.

## STATEMENT OF MANAGEMENT RESPONSIBILITY

Based on the information available to the Management Board of Latvenergo AS, the Latvenergo Group Consolidated and Latvenergo AS Annual Report 2018, including the Management Report, have been prepared in accordance with the International Financial Reporting Standards as adopted by the EU and in all material aspects present a true and fair view of the assets, liabilities, financial position, profit and loss and its cash flows of Latvenergo Group and Latvenergo AS. Information provided in the Management Report is accurate.

### The Management Board of Latvenergo AS:

---

**Āris Žigurs**

Chairman of the Management Board

16 April 2019

---

**Guntars Baļčūns**

Member of the Management Board

## PROFIT DISTRIBUTION

Fulfilling the requirements of the Article No. 45 of the law "On the State budget 2019" that determines the amount of dividends payable in the year 2019, the Management Board of Latvenergo AS proposes to pay out in dividends EUR 132.9 million. The distribution of net profit and amount of dividends payable is subject to a resolution of the Latvenergo AS Shareholders Meeting. Net profit of the year 2018 is EUR 212.7 million.

---

**Uldis Bariss**

Member of the Management Board

---

**Kaspars Cikmačs**

Member of the Management Board

# FINANCIAL STATEMENTS

## STATEMENT OF PROFIT OR LOSS

EUR'000

	Notes	Group		Parent Company	
		2018	2017	2018	2017
Revenue	6	878,008	925,627	435,199	498,580
Other income	7	93,260	149,950	91,181	147,502
Raw materials and consumables used	8	(497,293)	(349,690)	(284,592)	(156,103)
Personnel expenses	9	(103,762)	(113,289)	(42,396)	(44,892)
Depreciation, amortisation and impairment of intangible assets and property, plant and equipment	13 a, 14 a	(225,820)	(307,614)	(127,124)	(209,684)
Impairment losses on financial assets, net		478	–	236	–
Other operating expenses	10	(49,109)	(70,902)	(38,701)	(57,987)
<b>Operating profit</b>		<b>95,762</b>	<b>234,082</b>	<b>33,803</b>	<b>177,416</b>
Finance income	11 a	1,157	1,243	11,446	11,433
Finance costs	11 b	(8,406)	(11,211)	(10,135)	(12,054)
Dividends from subsidiaries	15	–	–	177,646	9,111
<b>Profit before tax</b>		<b>88,513</b>	<b>224,114</b>	<b>212,760</b>	<b>185,906</b>
Current income tax	12	(261)	(51,199)	(27)	(45,097)
Deferred tax changes	12	(12,297)	149,106*	–	10,082*
<b>Profit for the year</b>		<b>75,955</b>	<b>322,021</b>	<b>212,733</b>	<b>150,891</b>
<b>Profit attributable to:</b>					
– Equity holder of the Parent Company		73,423	319,670	212,733	150,891
– Non-controlling interests		2,532	2,351	–	–
Basic earnings per share (in euros)	20 c	0.081	0.250	0.234	0.117
Diluted earnings per share (in euros)	20 c	0.081	0.250	0.234	0.117

\* In 2017 deferred tax liabilities reversed in the Statement of Profit or Loss in accordance with the changes of tax regulations and laws of the Republic of Latvia starting from 1 January 2018

The notes on pages 93 to 146 are an integral part of these Financial Statements

**Āris Žīgurs**

Chairman of the Management Board

**Guntars Baļčūns**

Member of the Management Board

**Uldis Bariss**

Member of the Management Board

**Kaspars Cikmačs**

Member of the Management Board

**Liāna Ķeldere**

Accounting director of Latvenergo AS

16 April 2019

## STATEMENT OF COMPREHENSIVE INCOME

EUR'000

	Notes	Group		Parent Company	
		2018	2017	2018	2017
<b>Profit for the year</b>		<b>75,955</b>	<b>322,021</b>	<b>212,733</b>	<b>150,891</b>
<i>Comprehensive income to be reclassified to profit or loss in subsequent periods (net of tax):</i>					
Gains from change in hedge reserve	20 a, 23	9,531	5,422	9,531	5,422
<b>Net comprehensive income to be reclassified to profit or loss in subsequent periods</b>		<b>9,531</b>	<b>5,422</b>	<b>9,531</b>	<b>5,422</b>
<i>Comprehensive income / (loss) not to be reclassified to profit or loss in subsequent periods (net of tax):</i>					
Gains on revaluation of property, plant and equipment	20 a	–	18,842	–	18,842
Gains / (losses) as a result of re-measurement on defined post-employment benefit plan	20 a, 26 a	436	3,460	(108)	1,053
Reversal of deferred income tax	12	–	169,978	–	119,503
<b>Net comprehensive income / (loss) not to be reclassified to profit or loss in subsequent periods</b>	<b>reclas-</b>	<b>436</b>	<b>192,280</b>	<b>(108)</b>	<b>139,398</b>
<b>Comprehensive income for the year, net of tax</b>		<b>9,967</b>	<b>197,702</b>	<b>9,423</b>	<b>144,820</b>
<b>TOTAL comprehensive income for the year</b>		<b>85,922</b>	<b>519,723</b>	<b>222,156</b>	<b>295,711</b>
<b>Attributable to:</b>					
– Equity holder of the Parent Company		83,390	517,372	222,156	295,711
– Non-controlling interests		2,532	2,351	–	–

The notes on pages 93 to 146 are an integral part of these Financial Statements

# STATEMENT OF FINANCIAL POSITION

EUR'000

	Notes	Group		Parent Company	
		31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>ASSETS</b>					
<b>Non-current assets</b>					
Intangible assets	13 a	19,079	13,413	22,813	17,461
Property, plant and equipment	14 a	3,297,093	3,308,985	1,133,886	1,231,454
Investment property	14 b	467	753	61,796	64,807
Non-current financial investments	15	40	40	830,542	817,048
Non-current loans to subsidiaries	28 e	–	–	595,004	397,976
Other non-current receivables	17 b	30,920	3,229	331	284
Investments in other financial assets	21	16,935	–	16,935	–
Investments in held-to-maturity financial assets	21	–	16,984	–	16,984
<b>TOTAL non-current assets</b>		<b>3,364,534</b>	<b>3,343,404</b>	<b>2,661,307</b>	<b>2,546,014</b>
<b>Current assets</b>					
Inventories	16	71,975	76,328	58,410	61,824
Receivables from contracts with customers	17 a	117,955	105,369	81,025	82,799
Other current receivables	17 b, c	84,830	646,761	14,445	18,079
Deferred expenses		2,598	3,241	1,552	2,205
Current loans to subsidiaries	28 e	–	–	170,811	700,805
Prepayment for income tax		11,619	–	10,152	–
Derivative financial instruments	23	15,853	4,619	15,853	4,619
Cash and cash equivalents	18	129,455	236,003	127,554	232,855
<b>TOTAL current assets</b>		<b>434,285</b>	<b>1,072,321</b>	<b>479,802</b>	<b>1,103,186</b>
<b>TOTAL ASSETS</b>		<b>3,798,819</b>	<b>4,415,725</b>	<b>3,141,109</b>	<b>3,649,200</b>

**Āris Žīgurs**

Chairman of the Management Board

**Guntars Baļčūns**

Member of the Management Board

**Liāna Ķeldere**

Accounting director of Latvenergo AS

16 April 2019

Statement of Financial Position (continued)

EUR'000

	Notes	Group		Parent Company	
		31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>EQUITY AND LIABILITIES</b>					
<b>EQUITY</b>					
Share capital	19	834,791	1,288,715	834,791	1,288,715
Reserves	20 a	1,125,466	1,125,728	794,555	791,681
Retained earnings		351,350	424,406	364,477	302,242
<b>Equity attributable to equity holder of the Parent Company</b>		<b>2,311,607</b>	<b>2,838,849</b>	<b>1,993,823</b>	<b>2,382,638</b>
Non-controlling interests		8,458	8,042	–	–
<b>TOTAL equity</b>		<b>2,320,065</b>	<b>2,846,891</b>	<b>1,993,823</b>	<b>2,382,638</b>
<b>LIABILITIES</b>					
<b>Non-current liabilities</b>					
Borrowings	22	700,028	718,674	690,568	710,125
Deferred income tax liabilities	12	12,297	–	–	–
Provisions	26	20,178	21,910	8,625	8,835
Derivative financial instruments	23	3,923	4,914	3,923	4,914
Deferred income from contracts with customers	27 I a	143,494	142,132	–	–
Other deferred income	27 I b, c	303,519	350,926	210,105	286,085
<b>TOTAL non-current liabilities</b>		<b>1,183,439</b>	<b>1,238,556</b>	<b>913,221</b>	<b>1,009,959</b>
<b>Current liabilities</b>					
Trade and other payables	25	135,008	147,072	92,062	94,689
Deferred income from contracts with customers	27 II a	13,271	12,500	–	–
Other deferred income	27 II b, c	26,438	31,728	24,022	29,358
Income tax payable		2	27,725	–	24,739
Borrowings	22	114,315	108,083	111,700	104,647
Derivative financial instruments	23	6,281	3,170	6,281	3,170
<b>TOTAL current liabilities</b>		<b>295,315</b>	<b>330,278</b>	<b>234,065</b>	<b>256,603</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>3,798,819</b>	<b>4,415,725</b>	<b>3,141,109</b>	<b>3,649,200</b>

The notes on pages 93 to 146 are an integral part of these Financial Statements

**Uldis Bariss**

Member of the Management Board

**Kaspars Cikmačs**

Member of the Management Board

# STATEMENT OF CHANGES IN EQUITY

EUR'000

		Group					Parent Company				
		Attributable to equity holder of the Parent Company					Attributable to equity holder of the Parent Company				
Notes		Share capital	Reserves	Retained earnings	TOTAL	Non-control-ling interests	TOTAL	Share capital	Reserves	Retained earnings	TOTAL
<b>As of 31 December 2016</b>		<b>1,288,715</b>	<b>933,459</b>	<b>189,455</b>	<b>2,411,629</b>	<b>7,084</b>	<b>2,418,713</b>	<b>1,288,715</b>	<b>648,934</b>	<b>239,420</b>	<b>2,177,069</b>
Implementation effect of IFRS 15 'Revenue from Contracts with Customers'		–	–	(10)	(10)	–	(10)	–	–	–	–
<b>As of 1 January 2017</b>		<b>1,288,715</b>	<b>933,459</b>	<b>185,845</b>	<b>2,411,619</b>	<b>7,084</b>	<b>2,418,703</b>	<b>1,288,715</b>	<b>648,934</b>	<b>238,334</b>	<b>2,177,069</b>
Dividends for 2016	20 b	–	–	(90,142)	(90,142)	(1,393)	(91,535)	–	–	(90,142)	(90,142)
Disposal of non-current assets revaluation reserve net of deferred income tax	20 a	–	(4,377)	4,377	–	–	–	–	(1,762)	1,762	–
<b>TOTAL contributions and profit distributions recognised directly in equity</b>		<b>–</b>	<b>(4,377)</b>	<b>(85,765)</b>	<b>(90,142)</b>	<b>(1,393)</b>	<b>(91,535)</b>	<b>–</b>	<b>(1,762)</b>	<b>(88,380)</b>	<b>(90,142)</b>
Profit for the year		–	–	319,670	319,670	2,351	322,021	–	–	150,891	150,891
Other comprehensive income	12, 20 a	–	196,646	1,056	197,702	–	197,702	–	144,509	311	144,820
<b>TOTAL comprehensive income for the year</b>		<b>–</b>	<b>196,646</b>	<b>320,726</b>	<b>517,372</b>	<b>2,351</b>	<b>519,723</b>	<b>–</b>	<b>144,509</b>	<b>151,202</b>	<b>295,711</b>
<b>As of 31 December 2017</b>		<b>1,288,715</b>	<b>1,125,728</b>	<b>424,406</b>	<b>2,838,849</b>	<b>8,042</b>	<b>2,846,891</b>	<b>1,288,715</b>	<b>791,681</b>	<b>302,242</b>	<b>2,382,638</b>
Implementation effect of IFRS 9 'Financial instruments'		–	–	(290)	(290)	–	(290)	–	–	(629)	(629)
<b>As of 1 January 2018</b>		<b>1,288,715</b>	<b>1,125,728</b>	<b>424,116</b>	<b>2,838,559</b>	<b>8,042</b>	<b>2,846,601</b>	<b>1,288,715</b>	<b>791,681</b>	<b>301,613</b>	<b>2,382,009</b>
Decrease in share capital	19	(454,413)	–	–	(454,413)	–	(454,413)	(454,413)	–	–	(454,413)
Increase in share capital	14 a, 19	489	–	–	489	–	489	489	–	–	489
Dividends for 2017	20 b	–	–	(156,418)	(156,418)	(2,116)	(158,534)	–	–	(156,418)	(156,418)
Disposal of non-current assets revaluation reserve	20 a	–	(10,229)	10,229	–	–	–	–	(6,549)	6,549	–
<b>TOTAL contributions and profit distributions recognised directly in equity</b>		<b>(453,924)</b>	<b>(10,229)</b>	<b>(146,189)</b>	<b>(610,342)</b>	<b>(2,116)</b>	<b>(612,458)</b>	<b>(453,924)</b>	<b>(6,549)</b>	<b>(149,869)</b>	<b>(610,342)</b>
Profit for the year		–	–	73,423	73,423	2,532	75,955	–	–	212,733	212,733
Other comprehensive income	12, 20 a	–	9,967	–	9,967	–	9,967	–	9,423	–	9,423
<b>TOTAL comprehensive income for the year</b>		<b>–</b>	<b>9,967</b>	<b>73,423</b>	<b>83,390</b>	<b>2,532</b>	<b>85,922</b>	<b>–</b>	<b>9,423</b>	<b>212,733</b>	<b>222,156</b>
<b>As of 31 December 2018</b>		<b>834,791</b>	<b>1,125,466</b>	<b>351,350</b>	<b>2,311,607</b>	<b>8,458</b>	<b>2,320,065</b>	<b>834,791</b>	<b>794,555</b>	<b>364,477</b>	<b>1,993,823</b>

The notes on pages 93 to 146 are an integral part of these Financial Statements

**Āris Žīgurs**  
Chairman of the Management Board

**Guntars Baļčūns**  
Member of the Management Board

**Uldis Bariss**  
Member of the Management Board

**Kaspars Cikmačs**  
Member of the Management Board

**Liāna Ķeldere**  
Accounting director of Latvenergo AS

16 April 2019



# STATEMENT OF CASH FLOWS

EUR'000

Notes	Group		Parent Company	
	2018	2017	2018	2017*
<b>Cash flows from operating activities</b>				
Profit before tax	88,513	224,114	212,760	185,906
<b>Adjustments:</b>				
– Amortisation, depreciation and impairment of intangible assets and property, plant and equipment	13 a, 14 a	225,820	307,614	209,684
– Loss from disposal of non-current assets		17,638	5,476	12,320
– Interest costs	11 b	8,267	9,825	10,020
– Interest income	11 a	(1,114)	(1,221)	(11,403)
– Fair value loss on derivative financial instruments	8, 11	417	3,435	417
– Dividends from subsidiaries	15	–	–	(177,646)
– (Decrease) / increase in provisions	26	(1,295)	6,726	(318)
– Unrealised income on currency translation differences	11 b	2	(22)	2
				(22)
<b>Operating profit before working capital adjustments</b>		<b>338,248</b>	<b>555,947</b>	<b>173,276</b>
Decrease / (increase) in inventories		4,353	(34,870)	3,414
Decrease / (increase) in receivables from contracts with customers and other receivables		98,125	(7,770)	140,461
(Decrease) / increase in trade and other liabilities		(90,344)	(123,783)	(79,741)
Impact of non-cash offsetting of operating receivables and liabilities from subsidiaries, net		–	–	201,571
				246,554
<b>Cash generated from operating activities</b>		<b>350,382</b>	<b>389,524</b>	<b>438,981</b>
Interest paid		(9,066)	(11,484)	(10,781)
Interest received		1,113	1,390	1,113
Paid corporate income tax		(39,560)	(41,221)	(34,918)
				(36,908)
<b>Net cash flows from operating activities</b>		<b>302,869</b>	<b>338,209</b>	<b>394,395</b>
				<b>449,352</b>

**Āris Žigurs**  
Chairman of the Management Board

**Guntars Balčūns**  
Member of the Management Board

**Liāna Ķeldere**  
Accounting director of Latvenergo AS  
16 April 2019

## Statement of Cash Flows (continued)

EUR'000

Notes	Group		Parent Company	
	2018	2017	2018	2017*
<b>Cash flows from investing activities</b>				
Loans issued to subsidiaries, net	28 e	–	–	(323,539)
Purchase of intangible assets and PPE		(238,501)	(233,744)	(60,644)
Proceeds from investments in subsidiaries	15	–	–	53,378
Proceeds from redemption of other financial investments		49	3,569	49
				3,569
<b>Net cash flows used in investing activities</b>		<b>(238,452)</b>	<b>(230,175)</b>	<b>(330,756)</b>
<b>Cash flows from financing activities</b>				
Repayment of issued debt securities (bonds)	22	–	(70,000)	–
Proceeds on borrowings from financial institutions	22	93,500	186,500	90,000
Repayment of borrowings	22	(105,931)	(80,976)	(102,522)
Dividends paid to non-controlling interests	20 b	(2,116)	(1,393)	–
Dividends paid to equity holder of the Parent Company	20 b	(156,418)	(90,142)	(156,418)
				(90,142)
<b>Net cash flows used in financing activities</b>		<b>(170,965)</b>	<b>(56,011)</b>	<b>(168,940)</b>
<b>Net (decrease)/ increase in cash and cash equivalents</b>		<b>(106,548)</b>	<b>52,023</b>	<b>(105,301)</b>
Cash and cash equivalents at the beginning of the year	18	236,003	183,980	232,855
				181,197
<b>Cash and cash equivalents at the end of the year</b>	18	<b>129,455</b>	<b>236,003</b>	<b>127,554</b>
				<b>232,855</b>

\* See note 2.1.

The notes on pages 93 to 146 are an integral part of these Financial Statements

**Uldis Bariss**  
Member of the Management Board

**Kaspars Cikmačs**  
Member of the Management Board

# NOTES TO THE FINANCIAL STATEMENTS

## 1. CORPORATE INFORMATION

All shares of public limited company Latvenergo, parent company of Latvenergo Group (hereinafter – Latvenergo AS or the Parent Company) are owned by the Republic of Latvia and are held by the Ministry of Economics of the Republic of Latvia. The registered address of the Parent Company is 12 Pulkveža Brieža Street, Riga, Latvia, LV-1230. According to the Energy Law of the Republic of Latvia, Latvenergo AS is designated as a national economy object of State importance and, therefore, is not subject to privatisation.

Latvenergo AS is power supply utility engaged in electricity and thermal energy generation, as well as sales of electricity and natural gas. Latvenergo AS is one of the largest corporate entities in the Baltics.

Latvenergo AS heads the Latvenergo Group (hereinafter – the Group) that includes the following subsidiaries:

- Sadales tīkls AS (since 18 September 2006) with 100% interest held;
- Elektrum Eesti OÜ (since 27 June 2007) and its subsidiary Elektrum Latvija SIA (since 18 September 2012) with 100% interest held;
- Elektrum Lietuva UAB (since 7 January 2008) with 100% interest held;
- Latvijas elektriskie tīkli AS (since 10 February 2011) with 100% interest held;
- Liepājas enerģija SIA (since 6 July 2005) with 51% interest held;
- Enerģijas publiskais tirgotājs AS (since 25 February 2014) with 100% interest held.

Latvenergo AS and its subsidiaries Sadales tīkls AS, Latvijas elektriskie tīkli AS and Enerģijas publiskais tirgotājs AS are also shareholders with 48.15% interest held in company Pirmais Slēgtais Pensiju Fonds AS that manages a defined-contribution corporate pension plan in Latvia.

Latvenergo AS shareholding in subsidiaries, associates and other non-current financial investments is disclosed in Note 15.

The Management Board of Latvenergo AS since 16 November 2015 until 1 March 2018 was comprised of the following members: Āris Žīgurs (Chairman of the Board), Uldis Bariss, Māris Kuņickis, Guntars Baļčūns and Guntis Stafeckis. From 1 March 2018 Guntis Stafeckis and from 5 October 2018 Māris Kuņickis does not continue work on the Management Board. Since 25 September 2018 Kaspars Cikmačs has been acting as a member of the Management Board of Latvenergo AS and until the end of the reporting period the Management Board of Latvenergo AS was comprised of the following members: Āris Žīgurs (Chairman of the Board), Uldis Bariss, Guntars Baļčūns and Kaspars Cikmačs.

On 16 December 2016 the Supervisory Board of Latvenergo AS was established and it was comprised of the following members: Andris Ozoliņš (Chairman), Andris Liepiņš (Deputy Chairman), Baiba Anda Rubesa, Mārtiņš Bičevskis and Martin Sedlacký.

The Supervisory body – Audit Committee since 3 March 2017 was comprised of the following members: Torben Pedersen (Chairman of the Committee), Svens Dinsdorfs, Andris Ozoliņš, Andris Liepiņš and Marita Salgrāve.

The Financial Statements for year 2018 include the financial information in respect of the Latvenergo Group and Latvenergo AS for the year ending 31 December 2018 and comparative information for year 2017. Where it has been necessary, comparatives for year 2017 are reclassified using the same principles applied for preparation of the Financial Statements for 2018 (Note 2.1.).

The Management Board of Latvenergo AS has approved the Latvenergo Group and Latvenergo AS Financial statements 2018 on 16 April 2019. The Financial Statements are subject to Shareholder's approval on the Shareholder's Meeting.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these Financial Statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

### 2.1. BASIS OF PREPARATION

The Financial Statements of the Latvenergo Group and Latvenergo AS are prepared in accordance with the International Financial Reporting Standards as adopted for use in the European Union (IFRS). Due to the European Union's endorsement procedure, the standards and interpretations not approved for use in the European Union are also presented in this note as they may have impact on the Financial Statements in the following periods if endorsed.

The Financial Statements are prepared under the historical cost convention, except for some financial assets and liabilities (including derivative financial instruments and non-current financial investments) measured at fair value and certain property, plant and equipment carried at revalued amounts as disclosed in the accounting policies presented below.

As of 31 December 2017 the Group and the Parent Company has reclassified individual positions in the Statement of Financial Position for post-employment benefit plan revaluation reserve and retained earnings. The Parent Company also has reclassified individual positions in the statement of cash flows for the year 2017 for the mutual offsetting with related parties.

**Reclassification of individual positions in the Group's and the Parent Company's Statement of Financial Position as of 31 December 2017:**

EUR'000

	Group			Parent Company		
	31/12/2017 before reclassifi- cation	Reclassifi- cation	31/12/2017 after reclassifi- cation	31/12/2017 before reclassifi- cation	Reclassifi- cation	31/12/2017 after reclassifi- cation
<b>Equity and liabilities</b>						
Equity						
Reserves	1,126,521	(793)	1,125,728	791,906	(225)	791,681
Retained earnings	423,613	793	424,406	302,017	225	302,242
<b>TOTAL equity</b>	<b>2,846,891</b>	<b>-</b>	<b>2,846,891</b>	<b>2,382,638</b>	<b>-</b>	<b>2,382,638</b>

**Reclassification of individual positions in the Parent Company's Statement of Cash Flows for the year ended 31 December 2017:**

EUR'000

	2017 before reclassification	Reclassification	2017 after reclassification
<b>Operating profit before working capital adjustments</b>	<b>392,716</b>	<b>-</b>	<b>392,716</b>
(Increase) / decrease in receivables from contracts with customers and other receivables	(123,095)	10,242	(112,853)
Increase / (decrease) in trade and other liabilities	6,790	(41)	6,749
Impact of non-cash offsetting of operating receivables and liabilities from subsidiaries, net	-	246,554	246,554
<b>Cash generated from operating activities</b>	<b>240,398</b>	<b>256,755</b>	<b>497,153</b>
Interest paid	(12,324)	41	(12,283)
Interest received	11,632	(10,242)	1,390
<b>Net cash flows from operating activities</b>	<b>202,798</b>	<b>246,554</b>	<b>449,352</b>
<b>Cash flows from investing activities</b>			
Loans issued to subsidiaries	(81,889)	(186,329)	(268,218)
Repayment of loans issued to subsidiaries	60,225	(60,225)	-
<b>Net cash flows used in investing activities</b>	<b>(97,777)</b>	<b>(246,554)</b>	<b>(344,331)</b>
<b>Cash and cash equivalents at the end of the year</b>	<b>232,855</b>	<b>-</b>	<b>232,855</b>

All amounts shown in these Financial Statements are presented in thousands of euros (EUR'000 or EUR thousand).

The preparation of the Financial Statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on the Management's best knowledge of current events and actions, actual results ultimately may differ from those. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the Financial Statements are disclosed in Note 2.2 and Note 4.

**ADOPTION OF NEW AND/OR REVISED IFRS AND INTERNATIONAL FINANCIAL REPORTING INTERPRETATIONS COMMITTEE (IFRIC) INTERPRETATIONS**

The following new and/or revised International Financial Reporting Standards or interpretations published or revised during the reporting year, which became effective for the reporting period started from 1 January 2018, have been adopted by the Group and the Parent Company:

**IFRS 9: Financial Instruments:**

The standard is effective for annual periods beginning on or after 1 January 2018.

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments that replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018. Except for hedge accounting, retrospective application is required but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

**a) Classification and measurement**

From a classification and measurement perspective, the new standard requires all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories have been replaced by fair value through profit or loss (FVPL), fair value through other comprehensive income (FVOCI) and amortised cost. IFRS 9 also allow entities to continue to irrevocably designate instruments that qualify for amortised cost or fair value through OCI instruments as FVPL, if doing so eliminates or significantly reduces a measurement or recognition inconsistency. Equity instruments that are not held for trading may be irrevocably designated as FVOCI, with no subsequent reclassification of gains or losses to the income statement. The accounting for financial liabilities is largely the same as the requirements of IAS 39.

**b) Impairment**

IFRS 9 also fundamentally change the credit loss recognition methodology. The standard replaces IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. IFRS 9 requires the Group and the Parent Company to record expected credit losses on all of its debt securities, loans, receivables from contracts with customers and cash and its equivalents, either on a 12-month or lifetime basis. The Group and the Parent Company have applied two expected credit loss models: counterparty model and portfolio model. Counterparty model is used on individual contract basis for deposits, investments in State Treasury bonds, loans, unsettled revenue on mandatory procurement PSO fee, cash and cash equivalents and trade receivables with large customers. The expected credit losses according to this model are based on

assessment of the individual counterparty's risk of default based on *Moody's* annual corporate default and recovery rates for the relevant industry of business partner. Portfolio model is used for trade receivables with consumers and small business customers and defined for basic business activities. For trade receivables grouped by portfolio model the Group and the Parent Company apply the simplified approach and record lifetime expected losses on receivables based on historical analysis of credit losses taking into account also expected future development. The Group and the Parent Company use provision matrix based on historical observed default rates, adjusted for forward-looking estimates. IFRS 9 impairment requirements are applied retrospectively, with transition impact recognised in retained earnings (see Note 4 b).

### c) Hedge accounting

Hedge accounting requirements were amended to align accounting more closely with risk management. The standard provides entities with an accounting policy choice between applying the hedge accounting requirements of IFRS 9 and continuing to apply IAS 39 to all hedges because the standard currently does not address accounting for macro hedging.

The Group and the Parent Company have applied IFRS 9 Financial Instruments, except for hedge accounting, for the first time in the 2018 financial statements with initial application date as of 1 January 2018 and have chosen a modified retrospective application of IFRS 9. The Group and the Parent Company have decided to continue to apply hedge accounting requirements of IAS 39.

Adoption of new standard is disclosed in Note 2.28.

The Group and the Parent Company has applied IFRS 15 Revenue from contracts with customers with initial application date as of 1 January 2017 and has chosen a modified retrospective application with cumulative effect.

Other new or revised standards or interpretations that have become effective in current accounting period do not have significant effect on the Group and the Parent Company.

## STANDARDS ISSUED AND NOT YET EFFECTIVE, BUT ARE RELEVANT FOR THE GROUP'S AND THE PARENT COMPANY'S OPERATIONS AND NOT EARLY ADOPTED BY THE GROUP AND THE PARENT COMPANY

### IFRS 16: Leases

The standard is effective for annual periods beginning on or after 1 January 2019. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). The new standard requires lessees to recognise most leases on their financial statements. Lessees will have a single accounting model for all leases, with certain exemptions. Lessor accounting is substantially unchanged. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Group and the Parent Company will adopt IFRS 16 for the financial year beginning as of 1 January 2019. The Group and the Parent Company have assessed that the impact of adoption of this Standard will be material on the Group's and the Parent Company's financial statements, and consider that as the lessee the Group and the Parent Company will have to recognise right-of-use assets in their financial statements. Upon implementation of IFRS 16, among other considerations, the Group and the Parent Company will make an assessment on the identified right-of-use assets, non-cancellable lease terms (including the extension and termination options) and lease payments (including fixed and variable payments, termination option penalties etc.).

The statement of profit or loss will also be affected because the total expense is typically higher in the earlier years of a lease and lower in later years. Additionally, operating expense will be replaced with interest expenses and depreciation, so key metrics like EBITDA (earnings before interest, income tax, depreciation and amortisation,

and impairment of intangible assets and property, plant and equipment) will change. Operating cash flows will be higher as cash payments for the principal portion of the lease liability are classified within financing activities. Only the part of the payments that reflects interest can continue to be presented as operating cash flows.

The Group and the Parent Company will apply simplified approach and will not restate any comparative information and cumulative effect of applying the standard will be recognised as an adjustment to the opening balance of retained earnings at the date of initial application. Right-of-use assets will be measured at the amount of the lease liability on adoption. The Group and the Parent Company will use an optional exemption for short-term and low-value leases.

Based on assessment for the remaining lease commitments, the Group expects to recognise right-of-use assets and lease liabilities of approximately EUR 9,392 thousand on 1 January 2019 (Parent Company: approximately EUR 4,978 thousand of right-of-use assets and lease liabilities).

The Group expects other operating expenses will decrease by EUR 1,440 thousand, depreciation will increase by EUR 1,364 thousand and interest expense for 2019 will increase by EUR 124 thousand. The Parent Company expects other operating expenses will decrease by EUR 513 thousand, depreciation will increase by EUR 473 thousand and interest expense for 2019 will increase by EUR 67 thousand.

The Group and the Parent Company as lessor do not expect any significant effect on the financial statements, however, some additional disclosures will be required from 2019.

Other new or revised standards or interpretations that will become effective in next accounting period (s) do not have significant effect on the Group and the Parent Company.

## 2.2. CONSOLIDATION (GROUP)

### a) Subsidiaries

Subsidiaries', which are those entities where the Group has control over the financial and operating policies of the entity, financial reports are consolidated. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee).

Subsidiaries' financial reports are consolidated from the date on which control is transferred to the Parent Company and are no longer consolidated from the date when control ceases. General information about entities included in consolidation and its primary business activities are disclosed in Note 15.

The acquisition method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured, as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Costs directly attributable to the acquisition are expensed to the Statement of Profit or Loss as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in business combination are measured initially at their fair values at the acquisition date.

Intercompany transactions, balances and unrealised gains on transactions between the Group's entities are eliminated. Unrealised losses are also eliminated but considered an impairment indicator of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

### b) Transactions with non-controlling interests and owners

The Group treats transactions with non-controlling interests as transactions with equity owners of the Group's Parent Company. Changes in a Parent's ownership interest in a subsidiary that do not result in the Parent losing control of the subsidiary are equity transactions (i.e. transactions with owners in their capacity as owners). For purchases from non-controlling interests, the difference between any

consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in the Group's equity.

#### c) Associates

Associates are all entities over which the Parent Company has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Currently the Group has no investments in associates (Note 15).

### 2.3. DISCLOSURES OF REPORTABLE SEGMENTS

For segment reporting purposes the division into operating segments is based on the Latvenergo Group's and the Parent Company's internal management structure, which is the basis for the reporting system, performance assessment and the allocation of resources by the operating segment decision maker.

The Group divides its operations into three main operating segments – generation and trade, distribution and lease of transmission system assets. The Parent Company divides its operations into one main operating segment – generation and trade.

In addition, corporate functions, that cover administration and other support services, are presented in the Group and the Parent Company as separate segment (Note 5).

### 2.4. FOREIGN CURRENCY TRANSLATION

#### a) Functional and presentation currency

Items included in the Financial Statements are measured using the currency of the primary economic environment in which the Group's entity operates ("the functional currency"). The Financial Statements have been prepared in euros (EUR), which is the Parent Company's functional currency, and presented in thousands of EUR. All figures, unless stated otherwise are rounded to the nearest thousand.

#### b) Transactions and balances

All transactions denominated in foreign currencies are translated into functional currency at the exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into functional currency using the exchange rate at the last day of the reporting year. The resulting gain or loss is charged to the Statement of Profit or Loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions.

### NON-FINANCIAL ASSETS AND LIABILITIES

#### 2.5. INTANGIBLE ASSETS

Intangible assets are measured on initial recognition at historical cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses.

Assets under development are recognised in Statement of Financial Position within intangible assets and measured at cost until the intangible assets are completed and received.

#### a) Usage rights, licenses and software

Usage rights, licenses and software are shown at historical cost less accumulated amortisation and accumulated impairment losses. Amortisation is calculated using the straight-line method to allocate the cost of usage rights, licenses and software over their estimated useful lives. Computer software development costs recognised as assets are amortised over their estimated useful lives, not exceeding a period of use defined in agreement or five years.

Connection usage rights are the payments for the rights to use the transmission or distribution system's power grid. Connection usage rights are recognised in the basis of upfront payments to transmission or distribution system operator for connection installation services. Connection usage rights are measured at cost net of amortisation and accumulated impairment that is calculated on straight-line basis to allocate the cost of connection usage rights to the residual value over the estimated period of relationship with a supplier (connection installer).

#### b) Greenhouse gas emission allowances

Emission rights for greenhouse gases (or allowances) are recognised at purchase cost when the Group or the Parent Company is able to exercise the control. Allowances received from the Government free of charge are recognised at zero cost. In those cases, when the quantity of emitted greenhouse gases exceeds the quantity of allowances allocated by the state free of charge, the Group and the Parent Company purchases additional allowances. Allowances are accounted for within 'Intangible assets' (see Note 13 b).

### 2.6. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment (PPE) are measured on initial recognition at cost. Following initial recognition PPE are stated at historical cost or revalued amount (see 2.8) less accumulated depreciation and accumulated impairment loss, if any.

The acquisition cost comprises the purchase price, transportation costs, installation, and other direct expenses related to the acquisition or implementation. The cost of the self-constructed item of PPE includes the cost of materials, services and workforce. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group or the Parent Company and the cost of an item can be measured reliably. All other repair and maintenance expenses are charged directly to the Statement of Profit or Loss when the expenditure is incurred. Borrowing costs are capitalised to fixed assets proportionally to the part of the cost of fixed assets under construction over the period of construction.

If an item of PPE consists of components with different useful lives and acquisition costs of such components are significant concerning the PPE value, these components are accounted as separate items.

Land is not depreciated. Depreciation on the other assets is calculated using the straight-line method to allocate their cost over their estimated useful lives, as follows:

Type of property, plant and equipment (PPE)	Estimated useful life, years
<b>Buildings and facilities</b>	
<b>Assets of Hydropower plants:</b>	<b>15 – 100</b>
▪ hydropower plants' buildings and facilities,	25 – 100
▪ hydropower plants' technology equipment and machinery	10 – 40
<b>Transmission system electrical lines and electrical equipment:</b>	
▪ electricity transmission lines	20 – 50
▪ electrical equipment of transformer substations	12 – 40
<b>Distribution system electrical lines and electrical equipment:</b>	
▪ electricity distribution lines	30 – 50
▪ electrical equipment of transformer substations	30 – 35
<b>Technology equipment and machinery</b>	<b>3 – 40</b>
<b>Other property, plant and equipment</b>	<b>2 – 25</b>



The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (see 2.9).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. Those are included in the Statement of Profit or Loss. If revalued property, plant and equipment have been sold, appropriate amounts are reclassified from revaluation reserve to retained earnings.

All fixed assets under construction are stated at historical cost and comprise of costs of construction of assets. The initial cost includes construction and installation costs and other direct costs related to construction of fixed assets. General and specific borrowing costs directly attributable to the acquisition or construction of qualifying assets are added to the cost of those assets, until such time as the assets are substantially ready for their intended use. Borrowing costs consist of interest and other costs that the Group or the Parent Company incur in connection with the borrowing of funds. Assets under construction are not depreciated as long as the relevant assets are completed and ready for intended use, impairment test is performed when there is indication for impairment, either individually or at the cash-generating unit level. The amount of any impairment loss identified is measured as the difference between the asset's carrying amount and the recoverable amount that is higher of the asset's the fair value less costs to sell and value in use.

## 2.7. INVESTMENT PROPERTY

Investment properties are land or a building or part of a building held by the Group or the Parent Company as the owner to earn rentals or for capital appreciation, rather than for use in the production of goods or supply of services or for administrative purposes, or sale in the ordinary course of business. Investment property generates cash flows independently of the other assets held. The investment properties are initially recognised at cost and subsequently measured at acquisition cost net of accumulated depreciation and impairment losses. The applied depreciation rates are based on estimated useful life set for respective fixed asset categories – from 15 to 80 years.

## 2.8. REVALUATION OF PROPERTY, PLANT AND EQUIPMENT

Revaluations have been made with sufficient regularity to ensure that the carrying amount of property, plant and equipment items subject to valuation does not differ materially from that which would be determined using fair value at the end of reporting period.

The following hydropower plants, transmission system and distribution system assets (property, plant and equipment) are revalued regularly but not less frequently than every five years:

- a) Assets of Hydropower plants:
  - hydropower plants' buildings and facilities,
  - hydropower plants' technology equipment and machinery;
- b) Transmission system electrical lines and electrical equipment:
  - electricity transmission lines,
  - electrical equipment of transformer substations;
- c) Distribution system electrical lines and electrical equipment:
  - electricity distribution lines,
  - electrical equipment of transformer substations.

Increase in the carrying amount arising on revaluation is recognised to the Statement of Comprehensive income as "Non-current assets revaluation reserve" in shareholders' equity. Decrease in the carrying amount arising on revaluation primarily offset previous increases recognised in 'Comprehensive income'

and if decrease exceeds revaluation reserve, it is recognised in the Statement of Profit or Loss.

At the date of revaluation, initial carrying amounts and accumulated depreciation are increased or decreased proportionately with the change in the carrying amount of the asset so that the carrying amount of the asset after the revaluation equals its revalued amount.

Non-current assets revaluation reserve is decreased and transferred to retained earnings at the moment, when revalued asset has been written off or disposed.

Revaluation reserve cannot be distributed in dividends, invested in share capital, used for indemnity, reinvested in other reserves, or used for other purposes.

## 2.9. IMPAIRMENT OF NON-FINANCIAL ASSETS

Assets that are subject to depreciation or amortisation, land and investments in subsidiaries are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. In assessing the value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market expectations regarding the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognised in the Comprehensive Income within PPE revaluation reserve for the assets accounted at revalued amount and in the Statement of Profit or Loss within amortisation, depreciation and impairment charge expenses for the assets that are accounted at cost, less depreciation and impairment, and for the assets accounted at revalued amount in case if impairment charge exceeds revaluation surplus previously recognised on individual asset.

The key assumptions used in determining recoverable amount of the asset are based on the Group entities' or the Parent Company's management best estimation of the range of economic conditions that will exist over the remaining useful life of the asset, on the basis of the most recent financial budgets and forecasts approved by the management for a maximum period of 10 years. Assets are reviewed for possible reversal of the impairment whenever events or changes in circumstances indicate that impairment must be reviewed. The reversal of impairment for the assets that are accounted at cost, less depreciation and impairment, is recognised in the Statement of Profit or Loss. Reversal of impairment loss for revalued assets is recognised in the Statement of Profit or Loss to the extent that an impairment loss on the same revalued asset was previously recognised in the Statement of Profit or Loss; the remaining reversals of impairment losses of revalued assets are recognised in Comprehensive Income.

## 2.10. LEASES

### a) The Group or the Parent Company is the lessee

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the Statement of Profit or Loss on a straight-line basis over the period of the lease (Note 14 e).

### b) The Group or the Parent Company is the lessor

Properties leased out under operating leases are recorded within investment property at historic cost or revalued amounts less depreciation and accumulated impairment loss. Rental income from operating lease less any incentives given to lessee are recognised in the Statement of Profit or Loss on a straight-line basis over the period of the lease (Note 14 e).

## 2.11. NON-CURRENT ASSETS HELD FOR SALE

The Group and the Parent Company classifies non-current assets as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use, and sale is considered highly probable. Non-current assets held for sale are measured at the lower of their carrying amount and fair value less costs to sell.

## 2.12. INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses. Cost is determined using the weighted average method, except of natural gas inventory where cost is determined using FIFO method.

Purchase cost of inventories consists of the purchase price, import charges and other fees and charges, freight-in and related costs as well as other costs directly incurred in bringing the materials and goods to their present location and condition. The value of inventories is assigned by charging trade discounts, reductions and similar allowances.

Existence of inventories as of the end of reporting period is verified during stock-taking.

At the end of each reporting year the inventories are reviewed for any indications of obsolescence. When obsolete or damaged inventories are identified allowances are recognised to their recoverable amount. Additionally, during the reporting year at least each month inspection of idle inventories is performed with the purpose to identify obsolete and damaged inventories. Allowances for an impairment loss are recognised for those inventories.

The following basic principles are used in determining impairment losses for idle inventories:

- Maintenance inventories for machinery and equipment of hydropower plants and thermal power plants that haven't turned over during last 12 months are impaired in amount of 90%, while inventories haven't turned over during last 6 months are impaired in amount of 45%
- All other inventories that haven't turned over during last 12 months are fully impaired, while inventories that haven't turned over during last 6 months are impaired in amount of 50%,
- Allowances are not calculated for the fuel necessary to ensure uninterrupted operations of hydropower and combined heat and power plants, for natural gas and scraps.

## 2.13. PENSIONS, POST-EMPLOYMENT AND EMPLOYEE TERMINATION BENEFITS

### a) Pension obligations

The Group and the Parent Company make monthly contributions to a closed defined contribution pension plan on behalf of their employees. The plan is managed by the non-profit public limited company *Pirmais Slēgtais Pensiju Fonds*, with the participation of the Group companies amounting for 48.15% (Parent Company – 46.30%) of its share capital. A defined contribution plan is a pension plan under which the Group and the Parent Company pay contributions into the plan. The Group and the Parent Company have no legal or constructive obligations to pay further contributions if the plan does not hold sufficient assets to pay all employees benefits relating to employee service in the current and prior periods. The contributions amount to 5% of each pension plan member's salary. The Group and the Parent Company recognise the contributions to the defined contribution plan as an expense when an employee has rendered services in exchange for those contributions.

### b) Provisions for post-employment obligations arising from collective agreement

In addition to the aforementioned plan, the Group and the Parent Company provide certain post-employment benefits to employees whose employment conditions meet certain criteria. Obligations for

benefits are calculated taking into account the current level of salary and number of employees eligible to receive the payment, historical termination rates as well as number of actuarial assumptions.

The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method.

The liability recognised in the Statement of Financial Position in respect of post-employment benefit plan is the present value of the defined benefit obligation at the end of the reporting period. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using weighted average discount rate of ELOPA risk-free interest rate, interest rates of Latvian government bonds (maturity of 3 and 5 years) and EURBMK BBB electricity industry rate. The discount rate used is determined by reference to market yields on government bonds due to lack of deep market on high quality corporate bonds. The Group and the Parent Company use projected unit credit method to establish the present value of fixed benefit obligation and related present and previous employment expenses. According to this method it has been stated that each period of service gives rise to an additional unit of benefit entitlement and the sum of those units comprises total Group's and the Parent Company's obligations of post-employment benefits. The Group and the Parent Company use objective and mutually compatible actuarial assumptions on variable demographic factors and financial factors (including expected remuneration increase and determined changes in benefit amounts).

Actuarial gains or losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to the Statement of Comprehensive Income in the period in which they arise. Past service costs are recognised immediately in the Statement of Profit or Loss.

### c) Provisions for termination benefits

Termination benefits are measured in accordance with IAS 19 and are payable when employment is terminated by the Group Companies before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Group and the Parent Company recognise termination benefits at the earlier of the following dates: (a) when the Group entity can no longer withdraw the offer of those benefits; and (b) when the Group entity recognises costs for a restructuring that is within the scope of IAS 37 and involves the payment of terminations benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to present value. Management judgements related to the measurement of provisions for termination benefits is disclosed in Note 4.

## 2.14. PROVISIONS

Provisions are recognised when the Group or the Parent Company has a present obligation as a result of past event; it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and when a reliable estimate can be made of the amount of the obligation. Provisions are not recognised for future operating losses.

Provisions are presented in the Statement of Financial Position at the best estimate of the expenditure required to settle the present obligation at the end of reporting period. Provisions are used only for expenditures for which the provisions were originally recognised and are reversed if an outflow of resources is no longer probable.

Provisions are measured at the present value of the expenditures expected to be required for settling the obligation by using pre-tax rate that reflects current market assessments of the time value of the money and the risks specific to the obligation as a discount rate. The increase in provisions due to passage of time is recognised as interest expense.

Environmental protection provisions are recognised to cover environmental damages that have occurred before the end of the reporting period when this is required by law or when the Group's or the Parent Company's past environmental policies have demonstrated that the Group or the Parent Company has a constructive present obligation to liquidate this environmental damage. Experts' opinions and prior experience in performing environmental work are used to set up the provisions (see Note 26 c).

## 2.15. GRANTS

### a) Government grants

Government grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. Government grants are recognised as income over the period necessary to match them with the related costs, for which they are intended to compensate, on a systematic basis.

For grants received as part of a package of financial or fiscal aid to which a number of conditions are attached, those elements which have different costs and conditions are identified. Treatment of the different elements determine the periods over which the grant will be earned.

#### I) Grants related to expense items

A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to a company with no future related costs are recognised in profit or loss of the period in which it becomes receivable. Related income is recognised in the Statement of Profit or Loss as 'Other income' (Note 7).

When a grant relates to an expense item, and it has a number of conditions attached, it is initially recognised at fair value as deferred income. Grants are credited to income on a systematic basis over the periods that the related costs, for which it is intended to compensate, are expensed (Note 27). Management judgements related to the measurement of government grants is disclosed in Note 4.

#### II) Grants related to assets

Property, plant and equipment received at nil consideration are accounted for as grants. Those grants are recognised at fair value as deferred income and are credited to the Statement of Profit or Loss on a straight-line basis over the expected lives of the related assets.

## FINANCIAL ASSETS AND LIABILITIES

### 2.16. CLASSIFICATION, INITIAL RECOGNITION, SUBSEQUENT MEASUREMENT AND DE-RECOGNITION

#### a) Accounting policies applied from 1 January 2018

##### I) Classification

From 1 January 2018, the Group and the Parent Company classify its financial assets and liabilities under IFRS 9 in the following measurement categories:

- those to be measured subsequently at fair value (either through other comprehensive income or through profit or loss), and
- those to be measured at amortised cost.

The classification depends on the entity's business model for managing the financial assets and liabilities and the contractual terms of the cash flows.

For assets and liabilities measured at fair value, gains and losses is either recorded in profit or loss or in other comprehensive income. For investments in equity instruments that are not held for trading, this depends on whether the Group and the Parent Company have made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

The Group and the Parent Company reclassify debt investments when and only when its business model for managing those assets changes.

##### II) Initial recognition and measurement

All financial instruments are initially measured at fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs. Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognised on the trade date, i.e., the date when the Group and the Parent Company commits to purchase or sell the asset.

##### III) Subsequent measurement

###### Debt instruments

Subsequent measurement of debt instruments depends on the Group's and the Parent Company's business model for managing the asset and the cash flow characteristics of the asset. The Group and the Parent Company classify all of their debt instruments:

- in Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost. Any gain or loss arising on de-recognition is recognised directly in profit or loss. Impairment losses are presented as separate line item in the statement of profit or loss.

###### Equity instruments

The Group and the Parent Company subsequently measure all equity investments at fair value. Where the Group's or the Parent Company's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the de-recognition of the investment. Dividends from such investments continue to be recognised in profit or loss when the Group's and the Parent Company's right to receive payments is established.

Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI or FVPL are not reported separately from other changes in fair value.

#### Financial Liabilities

Financial liabilities are classified as measured at amortised cost or FVPL. A financial liability is classified as at FVPL if it is classified as held-for-trading, it is a derivative or it is designated as such on initial recognition. Financial liabilities at FVPL are measured at fair value and net gains or losses, including any interest expense, are recognised in profit or loss. Other financial liabilities are subsequently measured at amortised cost using the effective interest method. Interest expense and foreign exchange gains and losses are recognised in profit or loss.

#### IV) De-recognition

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired,
- the Group and the Parent Company have transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Group and the Parent Company have transferred substantially all the risks and rewards of the asset, or (b) the Group and the Parent Company have neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

The Group and the Parent Company derecognise a financial liability when its contractual obligations are discharged or cancelled, or expire. The Group and the Parent Company also derecognise a financial liability when its terms are modified and the cash flows of the modified liability are substantially different, in which case a new financial liability based on the modified terms is recognised at fair value. On de-recognition of a financial liability, the difference between the carrying amount extinguished and the consideration paid (including any non-cash assets transferred or liabilities assumed) is recognised in profit or loss.

#### V) Impairment

From 1 January 2018, the Group and the Parent Company assess on a forward-looking basis the expected credit losses associated with their debt instruments carried at amortised cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

The Group and the Parent Company have applied two expected credit loss models: counterparty model and portfolio model.

Counterparty model is used on individual contract basis for deposits, investments in State Treasury bonds, loans to subsidiaries and cash and cash equivalents. The expected credit losses according to this model for those are based on assessment of the individual counterparty's risk of default based on *Moody's* 12 months corporate default and recovery rates if no significant increase in credit risk is identified. The circumstances indicating a significant increase in credit risk is significant increase in *Moody's* default and recovery rates (by 1 percentage point) and counterpart's inability to meet payment terms (overdue 30 days or more, insolvency or bankruptcy, or initiated similar legal proceedings and other indications on inability to pay). If significant increase in credit risk identified, calculated lifetime expected credit loss.

For estimation of expected credit loss for unsettled revenue on mandatory procurement PSO fee, individually significant other receivables and other receivables of energy industry companies and related parties the Group and the Parent Company apply the simplified approach and record lifetime expected losses based on corporate default and recovery rates.

Portfolio model is used for trade receivables by grouping together receivables with similar risk characteristics and the days past due and defined for basic business activities. For trade receivables grouped by portfolio model the Group and the Parent Company apply the simplified approach and record lifetime expected losses on receivables based on historical observed default rates, adjusted for forward-looking estimates.

#### Derivative financial instruments

Derivative financial instruments are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative. The Group and the Parent Company have decided to continue to apply hedge accounting requirements of IAS 39. Accounting principles for derivative financial instruments are disclosed in Note 2.19.

#### b) Accounting policies applied until 31 December 2017

##### I) Classification

The Group and the Parent Company classified financial assets within the scope of IAS 39 as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale financial assets or as derivatives designated as hedging instruments in an effective hedge, as appropriate. Meanwhile financial liabilities were classified as trade and other payables, loans and borrowings, financial liabilities at fair value through profit or loss or derivatives designated as hedging instruments in an effective hedge, as appropriate (see 2.19.). The classification of financial assets and liabilities was determined at initial recognition.

##### II) Initial recognition and measurement

All financial assets were recognised initially at fair value plus transaction costs, except in the case of financial assets recorded at fair value through profit or loss. The Group and the Parent Company classified it financial assets as loans and receivables, held-to-maturity investments, available-for-sale financial assets and as derivatives financial instruments (see 2.19.).

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) were recognised on the trade date, i.e., the date that the Group and the Parent Company committed to purchase or sell the asset.

All financial liabilities were recognised initially at fair value and, in the case of trade and other payables and loans and borrowings, net of directly attributable transaction costs.

##### III) Subsequent measurement

#### Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss. Financial assets were classified as held for trading if they were acquired for the purpose of selling or repurchasing in the near term. Derivatives were also categorised as held for trading unless they were designated as hedges. Assets in this category were classified as current assets if expected to be settled within 12 months; otherwise, they were classified as non-current. Financial assets at fair value through profit or loss were carried in the statement of financial position at fair value with net changes in fair value presented as expense (negative net changes in fair value) or income (positive net changes in fair value) in the Statement of Profit or Loss. Financial assets designated upon initial recognition at fair value through profit or loss were designated at their initial recognition date and only if the criteria under IAS 39 were satisfied. The Group and the Parent Company has not designated any financial assets at fair value through profit or loss.



Derivatives embedded in host contracts were accounted for as separate derivatives and recorded at fair value if their economic characteristics and risks were not closely related to those of the host contracts and the host contracts were not held for trading or designated at fair value through profit or loss. These embedded derivatives were measured at fair value with changes in fair value recognised in profit or loss.

#### **Loans and receivables**

Loans and receivables were non-derivative financial assets with fixed or determinable payments that were not quoted in an active market. After initial measurement, such financial assets were subsequently measured at amortised cost using the effective interest rate (hereinafter – EIR) method, less impairment. The losses arising from impairment were recognised in the Statement of Profit or Loss in other operating expenses for receivables.

#### **Held-to-maturity investments**

Listed, non-derivative financial assets with fixed or determinable payments and fixed maturities were classified as held to maturity when exists positive intention and ability to hold them to maturity. After initial measurement, held to maturity investments were measured at amortised cost using the EIR, less impairment. If the Group and the Parent Company were to sell other than an insignificant amount of held-to-maturity financial assets, the whole category would be tainted and reclassified as available for sale. Held-to-maturity financial assets with maturities more than 12 months from the end of the reporting period were included in non-current assets, however those with maturities less than 12 months from the end of the reporting period were classified as current assets.

The Group and the Parent Company followed the IAS 39 guidance on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification required significant judgement. In making this judgement, the Group and the Parent Company evaluated its intention and ability to hold such investments to maturity.

#### **Available-for-sale financial assets**

Available-for-sale financial assets include equity instruments and debt securities. After initial measurement available-for-sale financial assets were subsequently measured at fair value with gains or losses recognised in other comprehensive income and credited in the available-for-sale financial assets reserve until the investment is derecognised. The Group and the Parent Company does not have such assets.

#### **Financial liabilities at fair value through profit or loss**

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss. This category includes derivative financial instruments entered into by the Group and the Parent Company that were not designated as hedging instruments in hedge relationships as defined by IAS 39. Separated embedded derivatives were also classified as held for trading unless they were designated as effective hedging instruments. Gains or losses on liabilities held for trading were recognised in the Statement of Profit or Loss.

#### **Loans and borrowings**

Loans and borrowings were recognised initially at fair value. After initial recognition, interest bearing loans and borrowings were subsequently measured at amortised cost using the EIR method. Gains and losses were recognised in profit or loss when the liabilities were derecognised as well as through the EIR amortisation process. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that were an integral part of the EIR. The EIR amortisation is included as finance costs in the Statement of Profit or Loss, except for the capitalised part. Borrowings were classified as current liabilities unless the Group and the Parent Company has an unconditional right to

defer settlement of the liability at least for 12 months after the end of reporting period.

#### **Trade and other payables**

The Group's and the Parent Company's trade payables were recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

#### **IV) De-recognition**

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired,
- the Group and the Parent Company has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Group and the Parent Company has transferred substantially all the risks and rewards of the asset, or (b) the Group and the Parent Company has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled, or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability were substantially modified, such an exchange or modification is treated as the de-recognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the Statement of Profit or Loss.

### **2.17. RECEIVABLES FROM CONTRACTS WITH CUSTOMERS AND OTHER RECEIVABLES**

Receivables from contracts with customers and other receivables are classified in groups:

- Energy and related services sales, including distribution system services,
- Heating sales,
- Other sales (IT & telecommunication services, connection service fees and other services),
- Receivables from subsidiaries,
- Other financial receivables.

Receivables from contracts with customers are recognised initially when they originated. Receivables without a significant financing component are initially measured at the transaction price.

After initial recognition receivables from contracts with customers are measured at amortised cost if they meet both of the following conditions:

- they are held within a business model whose objective is to hold assets to collect contractual cash flows;
- and their contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

The Group and the Company consider the evidence of impairment for the receivables from contracts with customers and other receivables at both an individual and a collective level. All individually significant receivables and receivables of energy industry companies and related parties are individually assessed for impairment. Those found not to be impaired are then collectively assessed for any impairment that has been incurred but not yet individually identified. Receivables that are not individually significant are collectively assessed for impairment using the portfolio model. Collective assessment is carried out by grouping together receivables with similar risk characteristics and the days past due. The Group and the Company have applied two expected credit loss models: portfolio model and counterparty model.



Under the portfolio model receivables from contracts with customers and other receivables are grouped as disclosed in Note 17 a).

The expected loss rates are based on the payment profiles of sales over a period of 2 years before 1 January 2018 and the corresponding historical credit losses experienced within this period. The Group and the Parent Company apply the IFRS 9 simplified approach to measuring expected credit losses of these receivables which uses a lifetime expected loss allowance (see Note 4 b).

For individually significant other receivables and other receivables of energy industry companies and related parties' receivables the counterparty model is used based on individual contract basis. The expected credit losses according to this model are based on assessment of the individual counterparty's risk of default based on *Moody's* corporate default and recovery rates for the relevant industry's entity.

## 2.18. CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash balances on bank accounts, demand deposits at bank and other short-term deposits with original maturities of three months or less. Cash and cash equivalents also are consisting of restricted cash, if it is readily convertible to cash.

## 2.19. DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

The Group and the Parent Company use derivatives such as interest rate swaps, electricity forward and future contracts and natural gas swap contracts to hedge risks associated with the interest rate and purchase price fluctuations, respectively. The Group and the Parent Company have decided to continue to apply hedge accounting requirements of IAS 39 for derivatives.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. Fair values are obtained from quoted market prices and discounted cash flow models as appropriate (see 2.20.).

The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, on the nature / content of the item being hedged. Other derivatives are accounted for at fair value through profit or loss.

The Group and the Parent Company designate certain derivatives as hedges of a particular risk associated with highly probable forecasted transactions or variable rate borrowings (cash flow hedge). The Group and the Parent Company document at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Group and the Parent Company also document their assessment, both at hedge inception and on an on-going basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

The fair value of the derivative instruments is presented as current or non-current based on settlement date. Derivative instruments that have maturity of more than twelve months and have been expected to be held for more than twelve months after the end of the reporting year are classified as non-current assets or liabilities. Derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

### a) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and accumulated in equity within 'Hedging reserve'. The gain or loss relating to the ineffective portion, if such arise, would be recognised immediately in the Statement of Profit or Loss.

Amounts accumulated in equity are recognised in the Statement of Profit or Loss in the periods when the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the Statement of Profit or Loss.

## 2.20. FAIR VALUE MEASUREMENT

The Group and the Parent Company measure financial instruments, such as, derivatives, at fair value at each balance sheet date. Non-financial assets such as investment properties are measured at amortised cost, but some items of property, plant and equipment at revalued amounts. Also, fair values of financial instruments measured at amortised cost are disclosed in Note 24.

The fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair values are estimated based on market prices and discounted cash flow models as appropriate.

The fair value of financial instruments traded in active markets is based on quoted market prices at the end of reporting period. The quoted market prices used for financial assets held by the Group and the Parent Company are the actual closing prices.

The fair value of financial instruments that are not traded in active market is determined by using valuation techniques. The Group and the Parent Company use a variety of methods and make assumptions that are based on market conditions existing at each end of reporting period. Estimated discounted cash flows are used to determine fair value for the remaining financial instruments.

The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows, by discounting their future contractual cash flows using euro annual bond 6 month Euribor forward starting interest rate swap curve.

The fair value of electricity forward and future contracts and natural gas swap contracts is calculated as discounted difference between actual market and settlement prices multiplied by the volume of the agreement.

If counterparty is a bank, then fair values of financial instruments are obtained from corresponding bank's revaluation reports and in financial statements fair values of financial instruments as specified by banks are disclosed. In case of electricity forward and future contracts and natural gas swap contracts are concluded with counterparties others than a bank; fair values as calculated by the Group and the Parent Company are disclosed in Financial Statements.

## 2.21. REVENUE RECOGNITION

### REVENUE FROM CONTRACTS WITH CUSTOMERS (IFRS 15)

Revenue from contracts with customers in scope for IFRS 15 encompasses sold goods or services provided as output of the entity's ordinary activities. The Group and Parent Company use the following criteria to identify contracts with customers:

- the parties to the contract have approved the contract (in writing, orally or in accordance with other customary business practices) and are committed to perform their respective obligations;
- each party's rights regarding the goods or services to be transferred can be identified;
- the payment terms for the goods or services to be transferred can be identified;
- the contract has commercial substance (i.e. the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract);

- it is probable that the company will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer.

In evaluating whether collectability of an amount of consideration is probable, the Group and the Parent Company use portfolio approach practical expedient for all energy and related supply services, distribution system services and heat sales customers. Group and the Parent Company reasonably expects that the effects on the financial statements from applying these requirements to the portfolio would not differ materially from applying the requirements to the individual contracts within the portfolio. Collectability is assessed individually for other customers.

The Group and the Parent Company consider only the customer's ability and intention to pay that amount of consideration when it is due.

Performance obligations are promises in the contracts (either explicitly stated or implied) with Group's and the Parent Company's customers to transfer to the customers either distinct goods or services, or series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

Promised goods or services represent separate performance obligations if the goods or services are distinct. A promised good or service is considered distinct if the customer can benefit from the good or service on its own or with other readily available resources (i.e. distinct individually) and the good or service is separately identifiable from other promises in the contract (distinct within the context of the contract). Both of these criteria must be met to conclude that the good or service is distinct.

Major distinct performance obligations identified in the contracts with customers by the Group and the Parent Company include sale of energy and related supply services, provision of distribution system services and sale of heat. Group has assessed that connecting a customer to the distribution grid as a separate performance obligation is not distinct as connection fees to distribution system are not distinct within the context of the contract due to being highly interrelated to sales of distribution services (Note 4 c III).

The Group and the Parent Company have further assessed that in providing Mandatory procurement PSO fees it is acting as an agent due to lack of control over PSO fee (Note 4 c I). The Parent Company has also concluded that it is acting as an agent in the provision of distribution system services and transmission system services because the Parent Company has no control over these services (Note 4 c II).

Where contracts with customers include variable consideration, the Group and the Parent Company estimate at contract inception the variable consideration expected over the life of the respective contracts and updates that estimate each reporting period. A constrained variable consideration is identified in relation to sales of distribution system services.

The Group and the Parent Company recognise revenue when (or as) it satisfies a performance obligation to transfer a promised good or service to a customer. Revenue is recognized when customer obtains control of the respective good or service.

The Group and the Parent Company use output method to measure progress towards complete satisfaction of a performance obligations. Revenue from sale of energy and related supply services, provision of distribution system services and sale of heat are recognised over time as a continuous delivery of these goods and services is made over the term of the respective contracts.

Revenue from satisfied performance obligations under such contracts is recognised over time, if one of the following criteria is met:

- customer simultaneously receives and consumes the benefits;
- customer controls the asset as it is created or enhanced;
- the Group's and Parent Company's performance does not create an asset with an alternative use and has a right to payment for performance completed.

Revenue from satisfaction of performance obligations is recognised based on identified transaction price. Transaction price reflects the amount to which the Group and the Parent Company have rights under the present contract. It is allocated to the distinct performance obligations based on standalone selling prices of the goods or services promised in the contract. The Group and the Parent Company allocate transaction price to the distinct performance obligations in proportion to their observable stand-alone selling prices and recognises revenue as those performance obligations are satisfied.

Payment terms for goods or services transferred to customers according to contract terms are within 20 to 45 days from the provision of services or sale of goods. Invoices are mostly issued monthly.

Revenue from contracts with customers is recognised as follows:

#### **I) Revenue recognised over time**

##### **Trade of energy and related supply services**

Revenue from electricity and natural gas sales are recognised on the basis of issued invoices to customers for supplied electricity on the basis of reported meter readings. Revenue from other energy and related supply services are recognised on the basis of goods delivered or provided services and prices included in contracts with customers. Revenues from trade of electricity in *Nord Pool* power exchange are based on the calculated market prices in accordance with contract terms, therefore 'right to invoice' practical expedient is used to recognise revenue from such contracts as the amount corresponds directly with the value of the performance completed to date.

##### **Sales of distribution system services (the Group)**

Revenues from electricity distribution services are based on regulated tariffs that are subject to approval by the Public Utilities Commission and regulations by Cabinet of Ministers of the Republic of Latvia 'Regulations on electricity trade and usage'. The Group recognises revenue from sales of distribution system services at the end of each month on the basis of the automatically made meter readings or customers' reported meter readings, on the period in which the services are rendered. Revenue is recognised in the amount for which the Group has right to invoice.

##### **Heat sales**

Revenue from sales of thermal energy is recognised at the end of each month on the basis of the meter readings and corresponds to the invoiced amount.

##### **Connection fees to distribution system (the Group)**

Connection fees to distribution system are non-refundable upfront fees paid by customers to secure connection to the distribution network, such fees are not distinct performance obligations as are highly interrelated with distribution system services. Connection fees partly reimburses for the cost of infrastructure to be built needed to connect the respective customer to the network. Connection fees to distribution system fee is calculated in accordance with Latvian regulatory authority (Public Utilities Commission) stated methodology.

Revenue from connection fees to distribution system are initially recognised as contract liabilities and recognised over the estimated customer relationship period of 20 years (Note 4 c III).

## Sales of IT & telecommunication services

Other revenue (Note 6), mainly includes revenues derived from information technology services (internet connection services, data communication services), open electronic communication network and telecommunication services to customers. Revenues are recognised on the basis of invoices which are prepared for clients upon usage of services listed in telecommunications billing system. Revenue is recognised in the amount for which the Group and the Parent Company have right to invoice.

### II) Revenue recognised applying agent accounting principle

#### Mandatory procurement PSO fees

Mandatory procurement PSO fees

Revenue from mandatory procurement public service obligation (PSO) fees in the Group is recognised on net (agent) basis. PSO fee is managed within the context of mandatory procurement process by subsidiary Enerģijas publiskais tirgotājs AS (hereinafter – EPT) and is the difference (residual) between the revenue from the sale of electricity in *Nord Pool* power exchange by market price, received mandatory procurement PSO fee, received government grant for compensating the increase of mandatory procurement costs and the related costs – costs of purchased electricity under the mandatory procurement from electricity producers, as well as guaranteed fees for installed electrical capacity in cogeneration plants. EPT is acting as agent in administration of the mandatory procurement process and receives revenue from mandatory procurement administration services (agent fee), which is recognised over time in the Group's Statement of Profit or Loss as "Other revenue" (Notes 6 and 4 c, I).

PSO fees are included in invoices issued by trader (Parent Company – Latvenergo AS) and by distribution system operator (Sadales tīkls AS) and are paid by customers together with unite invoice for electricity and distribution or transmission system services. System operators have the obligation to collect revenues of PSO fees from customers or traders and further to transfer these revenues to EPT. PSO fees are based on regulated tariffs that are subject to approval by the Public Utilities Commission. Due to lack of influence and control over PSO fees, the Group and the Parent Company consider themselves an agent in these transactions. Therefore, PSO fees obtained from electricity end-users and transferred to EPT are recognised in the Statement of Profit or Loss in net amount by applying the agent accounting principles (Note 6, Note 4 c, I).

#### Distribution system and transmission system services (Parent Company)

The Parent Company on behalf of distribution system operator (DSO) and transmission system operator (TSO) issues unite invoice including the fees for the distribution system or transmission system services, and transfers these fees to DSO or TSO accordingly.

Distribution system services and transmission system services are based on regulated tariffs that are subject to approval by the Public Utilities Commission. The Parent Company considers itself an agent in these transactions, therefore, the fees for distribution system and transmission system services obtained from customers and transferred to DSO and TSO are recognised in the Statement of Profit or Loss in net amount by applying the agent accounting principles (Note 4 c, II).

## REVENUE FROM OTHER SOURCES

### Lease of transmission system assets (IAS 17) (Group)

Revenues from lease of transmission system assets are recognised on the basis of lease payment amount which are calculated for transmission system operator accordingly to determined fee per lease agreement and recognised on a straight-line basis over term of the lease. Concluded agreements on the lease of transmission system assets meet IAS 17 'Leases' criteria that is used for revenue recognition from lease. Revenue is disclosed per Note 6 and 14 e.

### Connection fees to transmission system (IAS 17) (Group)

Revenue from connection fees to transmission system are within the scope of IAS 17. Connection fees to transmission system are received as upfront payments from lessee under operating lease agreement. Upfront payments are recognised as deferred income (Note 27).

Connection fees to transmission system are carried in the Statement of Financial Position as deferred income and amortised to Statement of Profit or Loss on a straight-line over basis estimated lease period (see Note 4 f).

Electricity connection fees to transmission system are recognised by the Group based on the necessity for a connection to the transmission network based on the request of lessee, which acts on behalf of users. For each connection fee a separate arrangement within the base lease agreement is concluded. Connection fee to transmission system partly reimburses the cost of infrastructure to be built and is needed for connection of transmission system user to the network. Connection service fee to transmission system is calculated in accordance with Latvian regulatory authority (Public Utilities Commission) stated methodology.

## 2.22. DIVIDEND DISTRIBUTION

Dividend distribution to the Parent Company's shareholders is recognised as a liability in the Financial Statements in the period in which the dividends are approved by the Parent Company's shareholders.

## 2.23. INCOME TAX

Corporate income tax includes current and deferred taxes.

### a) Corporate income tax

#### Latvia

Legal entities are not required to pay income tax on earned profits starting from 1 January 2018 in accordance with amendments made to the Corporate Income Tax Law of the Republic of Latvia issued on 28 July 2017. Corporate income tax is paid on distributed profits and deemed profit distributions. Consequently, current and deferred tax assets and liabilities are measured at the tax rate applicable to undistributed profits. Both distributed profits and deemed profit distributions are subject to the tax rate of 20% of their gross amount, or 20/80 of net expense. Corporate income tax on dividends is recognised in the statement of profit or loss as expense in the reporting period when respective dividends are declared, while, as regards other deemed profit distribution items, at the time when expense is incurred in the reporting year.

#### Lithuania

Current corporate income tax is applied at the rate of 15% on taxable income generated by a company during the taxation period.

Income tax expense for the period comprises current income tax and deferred income tax. Current income tax charges are calculated on current profit before tax using the tax rate 15% in accordance with applicable tax regulations as adjusted for certain non-deductible expenses/non-taxable income and are based on the taxable income reported for the taxation period.

## Estonia

Under the Income Tax Act, the annual profit earned by entities is not taxed in Estonia. Corporate income tax is paid on dividends, fringe benefits, gifts, donations, costs of entertaining guests, non-business related disbursements and adjustments of the transfer price. The tax rate on the net dividends paid out of retained earnings is 20/80. In certain circumstances, it is possible to distribute dividends without any additional income tax expense. The corporate income tax arising from the payment of dividends is accounted for as a liability and expense in the period in which dividends are declared, regardless of the actual payment date or the period for which the dividends are paid.

### b) Deferred income tax

#### Latvia

Following the amendments to the tax legislation of the Republic of Latvia effective from 1 January 2018 deferred tax liability is recognised in the consolidated financial statements on undistributed profits of the subsidiaries which has been generated as of 1 January 2018 and which will be subject to taxation upon distribution in foreseeable future. No other deferred tax assets and liabilities are recognised. Accordingly, deferred tax liabilities which have been calculated and recognised before the year 2017, in 2017 were reversed through the current statement of profit or loss or other comprehensive income (depending on whether the original entry was recorded in the statement of profit or loss or other comprehensive income) in the financial statements for the year ended 31 December 2017, as it is laid down in the IAS 12, changes in the tax legislation must be presented in financial statements in the period when they are adopted (Note 12).

#### Lithuania

Deferred income tax is provided in full, using the liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted by the end of reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability settled. Deferred income tax assets are recognised to the extent that it is probable that future taxable profit of the respective Group entity will be available against which the temporary differences can be utilised.

## Estonia

Due to the nature of the taxation system, the entities registered in Estonia do not have any differences between the tax bases of assets and liabilities and their carrying amounts and hence, no deferred income tax assets and liabilities arise.

## 2.24. SUBSIDISED ENERGY TAX

In order to limit the increase of the mandatory procurement public service obligation (PSO) fee for electricity consumers in Latvia, a Subsidised Energy Tax (SET) had been introduced for a four-year period as of 1 January 2014, which was applied to state support for generators of subsidised electricity. The SET applied both to income from electricity supplied under the mandatory procurement process as well as to mandatory procurement capacity payments for installed capacity at cogeneration plants, achieved from 1 January 2014 till 31 December 2017. SET applied for the subsidised electricity produced was recognised in the Statement of Profit or Loss as 'Other operating expenses' (Note 10) at gross amount.

## 2.25. RELATED PARTIES

The parties are considered related when one party has a possibility to control the other one or has significant influence over the other party in making financial and operating decisions. Related parties of the Group and the Parent Company are Shareholder of the Company who controls the Company in accepting operating business decisions, members of Latvenergo Group entities' management boards, members of the Supervisory board of the Company, members of Supervisory body of the Company – the Audit Committee and close family members of any above-mentioned persons, as well as entities over which those persons have control or significant influence.

As the shares of Latvenergo AS belong 100% to the Republic of Latvia, the related parties also include entities under the control or significant influence of the state (Note 28).

## 2.26. SHARE CAPITAL

The Group's share capital consists of the Parent Company's ordinary shares. All shares have been fully paid.

## 2.27. EVENTS AFTER THE REPORTING PERIOD

Events after the reporting period that provide significant additional information about the Group's and the Parent Company's position at the balance sheet date (adjusting events) are reflected in the financial statements. Events after the reporting period that are not adjusting events are disclosed in the notes when material.

## 2.28. CHANGES IN ACCOUNTING POLICIES

The Group and the Parent Company have applied IFRS 9 *Financial instruments*, except for hedge accounting, for the first time in the 2018 financial statements with initial application date: 1 January 2018. IFRS 9 was adopted without restating comparative information, the reclassifications and the adjustments arising from new impairment rules are therefore recognised in the opening balance of statement of financial position on 1 January 2018 and the impact of the IFRS 9 adoption has been only recognised for the new impairment requirements based on the expected credit loss model. Reclassification of financial instruments into the IFRS 9 categories had no impact on their respective measurement basis and therefore no adjustment to retained earnings related to classification and measurement as of 1 January 2018 was recognised.

All relevant figures in the financial statements for the year ended 31 December 2018 have been presented in accordance with IFRS 9.

The following tables show the adjustments recognised for each individual line item. Line items that were not affected by the changes have not been included. As a result, the sub-totals and totals disclosed cannot be recalculated from the numbers provided.

**Impact on Statement of Financial Position upon adoption of IFRS 9:**

EUR'000

Statement of Financial Position (extract)			Measurement category		Group			Parent Company				
			Original (IAS 39)	New (IFRS 9)	31/12/2017	Effect on IFRS 9 adoption	Positions reclassified	01/01/2018	31/12/2017	Effect on IFRS 9 adoption	Positions reclassified	01/01/2018
ASSETS												
Non-current assets												
Non-current financial investments	Available for sale		FVOCI		40	–	–	40	39	–	–	39
Non-current loans to related parties	Loans and receivables		Amortised cost		–	–	–	–	397,976	(271)	–	397,705
Other non-current receivables	Loans and receivables		Amortised cost		3,229	(4)	–	3,225	284	–	–	284
Investments in held-to-maturity financial assets	Held-to-maturity		–		16,984	–	(16,984)	–	16,984	–	(16,984)	–
Investments in other financial assets	–		Amortised cost		–	–	16,984	16,984	–	–	16,984	16,984
TOTAL non-current assets					3,343,404	(4)	–	3,343,400	2,546,014	(271)	–	2,545,743
Current assets												
Receivables from contracts with customers	Loans and receivables		Amortised cost		105,369	(122)	–	105,247	82,799	(115)	–	82,684
Other current receivables	Loans and receivables		Amortised cost		646,761	(164)	–	646,597	18,079	1	–	18,080
Current loans to related parties	Loans and receivables		Amortised cost		–	–	–	–	700,805	(244)	–	700,561
Derivative financial instruments*	Hedging derivatives at FVOCI		Hedging derivatives at FVOCI		4,074	–	–	4,074	4,074	–	–	4,074
	Derivatives at FVPL		Derivatives at FVPL		545	–	–	545	545	–	–	545
Cash and cash equivalents	Loans and receivables		Amortised cost		236,003	–	–	236,003	232,855	–	–	232,855
TOTAL current assets					1,072,321	(286)	–	1,072,035	1,103,186	(358)	–	1,102,828
TOTAL ASSETS					4,415,725	(290)	–	4,415,435	3,649,200	(629)	–	3,648,571
EQUITY												
Retained earnings					423,613	(290)	–	423,323	302,017	(629)	–	301,388
TOTAL equity					2,846,891	(290)	–	2,846,601	2,382,638	(629)	–	2,382,009
LIABILITIES												
Non-current liabilities												
Borrowings	Amortised cost		Amortised cost		718,674	–	–	718,674	710,125	–	–	710,125
Derivative financial instruments*	Hedging derivatives at FVOCI		Hedging derivatives at FVOCI		4,914	–	–	4,914	4,914	–	–	4,914
TOTAL non-current liabilities					1,238,556	–	–	1,238,556	1,009,959	–	–	1,009,959
Current liabilities												
Borrowings	Amortised cost		Amortised cost		108,083	–	–	108,083	104,647	–	–	104,647
Trade and other payables	Amortised cost		Amortised cost		96,489	–	–	96,489	69,753	–	–	69,753
Derivative financial instruments*	Hedging derivatives at FVOCI		Hedging derivatives at FVOCI		3,147	–	–	3,147	3,147	–	–	3,147
	Derivatives at FVPL		Derivatives at FVPL		23	–	–	23	23	–	–	23
Other current liabilities	Amortised cost		Amortised cost		12,787	–	–	12,787	6,197	–	–	6,197
TOTAL current liabilities					330,278	–	–	330,278	256,603	–	–	256,603
TOTAL EQUITY AND LIABILITIES					4,415,725	(290)	–	4,415,435	3,649,200	(629)	–	3,648,571

\* The Group and the Parent Company have decided to continue to apply hedge accounting requirements of IAS 39

While other non-current financial debt investments in State Treasury bonds are also subject to the impairment requirements of IFRS 9, the identified impairment loss was immaterial as these debt investments are considered by the management to have low credit risk because the issuer has a strong capacity to meet its contractual cash flow obligations in the near term and an investment grade credit rating with at least one major rating agency.

While cash and cash equivalents are also subject to the impairment requirements of IFRS 9, the identified impairment loss was immaterial, considering also fact that almost all of cash and cash equivalents are held in financial institutions with the credit rating grade of the institution or its parent bank at investment grade credit rating (mostly 'A level' credit rating).



## 3. FINANCIAL RISK MANAGEMENT

### 3.1. FINANCIAL RISK FACTORS

The Group's and the Parent Company's activities expose them to a variety of financial risks: market risk (including currency risk, fair value and cash flow interest rate risk), credit risk, price risk and liquidity risk. The Group's and the Parent Company's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's and the Parent Company's financial performance. The Group and the Parent Company use derivative financial instruments to hedge certain risk exposures.

Risk management (except for price risk) is carried out by the Parent Company's Treasury department (the Group Treasury) according to the Financial Risk Management Policy approved by the Parent Company's

Management Board. The Group Treasury identifies, evaluates and hedges financial risks in close co-operation with the Group's operating units / subsidiaries. The Parent Company's Management Board by approving the Financial Risk Management Policy provides written principles for overall risk management, as well as written policies covering specific areas, such as interest rate risk, foreign exchange risk, liquidity risk, and credit risk, use of financial instruments and investment of excess liquidity. Price risk management is carried out by the Parent Company's Electricity Trading department according to Electricity Wholesale Regulation approved by the Parent Company's Management Board.

#### Financial assets and financial liabilities that are exposed to financial risks disclosed in the table below by measurement categories:

EUR'000

	Notes	Group			Parent Company		
		Financial assets at amortised cost	Hedging de- rivatives at FVOCI	Derivatives at FVPL	Financial assets at amortised cost	Hedging de- rivatives at FVOCI	Derivatives at FVPL
<b>Financial assets as of 31 December 2018</b>							
Receivables from contracts with customers	17 a	117,955	–	–	81,025	–	–
Other current receivables	17 b	84,613	–	–	14,233	–	–
Loans to related parties	28 e	–	–	–	765,815	–	–
Other non-current receivables	17 b	30,920	–	–	331	–	–
Derivative financial instruments	23 l	–	15,748	105	–	15,748	105
Other financial investments	21	16,935	–	–	16,935	–	–
Cash and cash equivalents	18	129,455	–	–	127,554	–	–
		<b>379,878</b>	<b>15,748</b>	<b>105</b>	<b>1,005,893</b>	<b>15,748</b>	<b>105</b>
<b>Financial assets as of 31 December 2017</b>							
Receivables from contracts with customers	17 a	105,369	–	–	82,799	–	–
Other current receivables	17 b	641,832	–	–	17,938	–	–
Loans to related parties	28 e	–	–	–	1,098,781	–	–
Other non-current receivables	17 b	3,229	–	–	284	–	–
Derivative financial instruments	23 l	–	4,074	545	–	4,074	545
Held-to-maturity financial assets	21	16,984	–	–	16,984	–	–
Cash and cash equivalents	18	236,003	–	–	232,855	–	–
		<b>1,003,417</b>	<b>4,074</b>	<b>545</b>	<b>1,449,641</b>	<b>4,074</b>	<b>545</b>
<b>Financial liabilities as of 31 December 2018</b>							
Borrowings	22	814,343	–	–	802,268	–	–
Derivative financial instruments	23 l	–	10,204	–	–	10,204	–
Trade and other financial current payables	25	103,707	–	–	78,726	–	–
		<b>918,050</b>	<b>10,204</b>	<b>–</b>	<b>880,994</b>	<b>10,204</b>	<b>–</b>
<b>Financial liabilities as of 31 December 2017</b>							
Borrowings	22	826,757	–	–	814,772	–	–
Derivative financial instruments	23 l	–	8,061	23	–	8,061	23
Trade and other financial current payables	25	115,742	–	–	79,341	–	–
		<b>942,499</b>	<b>8,061</b>	<b>23</b>	<b>894,113</b>	<b>8,061</b>	<b>23</b>

## **a) Market risk**

### **I) Foreign currencies exchange risk**

As of 31 December 2018 and 31 December 2017 the Group and the Parent Company had borrowings denominated only in euros (Note 22). Their revenues and most of the financial assets and liabilities were denominated in euros. Accordingly, neither the Group or the Parent Company were subject to a significant foreign currencies exchange risk.

Foreign currencies exchange risk arises when future transactions or recognised assets or liabilities are denominated in a currency that is not the Group's and the Parent Company's functional currency.

The Group Treasury's Financial Risk Management Policy is to hedge all anticipated cash flows (capital expenditure and purchase of inventory) in each major foreign currency that might create significant currency risk. During 2018 and 2017 the Group and the Parent Company had no capital expenditure project which expected transactions would create significant currency risk.

### **II) Cash flow and fair value interest rate risk**

As the Group and the Parent Company have significant floating interest-bearing assets and liabilities exposed to interest rate risk, the Group's and the Parent Company's financial income and operating cash flows are substantially dependent on changes in market interest rates.

During 2018, if euro interest rates had been 50 basis points higher with all other variables held constant, the Group's income from the cash reserves held at bank for the year would have been EUR 875 thousand higher (2017: EUR 994 thousand) and the Parent Company's income from the cash reserves held at bank for the year would have been EUR 860 thousand higher (2017: EUR 986 thousand).

The Group's and the Parent Company's cash flow interest rate risk mainly arises from long-term borrowings at variable rates. They expose the Group and the Parent Company to a risk that finance costs might increase significantly when interest rates rise up. The Group's policy is to maintain at least 35% of its borrowings as fixed interest rates borrowings (taking into account the effect of interest rate swaps) with duration between 2–4 years.

The Group and the Parent Company analyse their interest rate risk exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions and hedging. Based on these scenarios, the Group and the Parent Company calculate the impact on profit and loss as well as on cash flows of a defined interest rate shift.

Generally, the Group and the Parent Company raise long-term borrowings at floating rates and based on the various scenarios, the Group and the Parent Company manage their cash flow interest rate risk by using floating-to-fixed interest rate swaps. Such interest rate swaps have the economic effect of converting borrowings from floating rates to fixed rates. Thereby fixed rates are obtained that are lower than those available if the Group and the Parent Company borrowed at fixed rates directly. Under the interest rate swaps, the Group and the Parent Company agree with other parties to exchange, at specified intervals (primarily semi-annually), the difference between fixed contract rates and floating-rate interest amounts calculated by reference to the agreed notional amounts.

To hedge cash flow interest rate risk, the Group and the Parent Company have entered into interest rate swap agreements with total notional amount of EUR 225.1 million (2017: EUR 193.5 million) (Note 23 II). 53% of the total Group's and 54% the Parent Company's borrowings as of 31 December 2018 (31/12/2017: 54% and 55% respectively) had fixed interest rate (taking into account the effect of the interest rate swaps) and average fixed rate duration was 2.1 years for the Group and the Parent Company (2017: 2.0 years for the Group and the Parent Company respectively).

If interest rates on euro denominated borrowings at floating base interest rate (after considering hedging effect) had been 50 basis points higher with all other variables held constant over the period until the next annual report, the Group's profit for the year would have been EUR 1,999 thousand lower (over the next 12 months period after 31/12/2017: EUR 1,750 thousand), the Parent Company's profit for the year would have been EUR 1,946 thousand lower (over the next 12 months period after 31/12/2017: EUR 1,690 thousand).

The borrowings with floating rates do not impose fair value interest rate risk. Derivatives such as interest rate swaps are the source of fair value interest rate risk.

As of 31 December 2018, if short and long term euro interest rates had been 50 basis points higher with all other variables held constant fair value of interest rate swaps would have been EUR 4,649 thousand higher (31/12/2017: EUR 51 thousand higher), which would have been attributable to the Statement of Comprehensive Income as hedge accounting item. However, if short and long term euro interest rates had been 50 basis points lower with all other variables held constant fair value of interest rate swaps would have been EUR 4,834 thousand lower (31/12/2017: EUR 51 thousand lower), which would have been attributable to the Statement of Comprehensive Income as hedge accounting item.

### **III) Price risk**

Price risk is the risk that the fair value and cash flows of financial instruments will fluctuate in the future due to reasons other than changes in the market prices resulting from interest rate risk or foreign exchange risk. The purchase and sale of goods produced and the services provided by the Group and the Parent Company under the free market conditions, as well as the purchases of resources used in production is impacted by the price risk.

The most significant price risk is related to purchase of electricity and natural gas. To hedge the risk related to changes in the price of electricity and natural gas the Parent Company during 2018 and 2017 has purchased electricity forward and future contracts and during 2018 natural gas forward contracts (Note 23 III, IV).

## **b) Credit risk**

Credit risk is managed at the Group level. Credit risk arises from cash and cash equivalents, favourable derivative financial instruments and at fair value through profit or loss (FVPL), deposits with banks, financial assets carried at amortised cost, including outstanding receivables. Credit risk exposure in connection with receivables is limited due to broad range of the Group's and the Parent Company's customers. The Group and the Parent Company have no significant concentration of credit risk with any single counterparty or group of counterparties having similar characteristics, except receivables from state for unsettled revenue on mandatory procurement PSO fee, loans to and receivables from subsidiaries and receivables from transmission system operator (Augstsprieguma tīkls AS). When assessing the credit risk for the loans to subsidiaries for the Parent Company, it is taken into account that Latvenego AS has granted loans to subsidiaries in which it holds all the shares, and accordingly monitors the operations and financial situation of the subsidiaries (borrowers). Impairment loss has been deducted from gross amounts.

The maximum credit risk exposure related to financial assets (see table below) comprises of carrying amounts of cash and cash equivalents (Note 18), receivables from contracts with customers and other receivables (Note 17), derivative financial instruments (Note 23) and other financial investments previously classified as held-to-maturity financial assets (Note 21).

**Assessment of maximum possible exposure to credit risk:**

EUR'000

	Notes	Group		Parent Company	
		31/12/2018	31/12/2017	31/12/2018	31/12/2017
Receivables from contracts with customers	17 a	117,955	105,369	81,025	82,799
Other non-current financial receivables	17 b	30,920	3,229	331	284
Other current financial receivables	17 b	84,613	641,832	14,233	17,938
Loans to subsidiaries	28 e	–	–	765,815	1,098,781
Cash and cash equivalents	18	129,455	236,003	127,554	232,855
Derivative financial instruments	23	15,853	4,619	15,853	4,619
Other financial investments	21	16,935	–	16,935	–
Held-to-maturity financial assets	21	–	16,984	–	16,984
		<b>395,731</b>	<b>1,008,036</b>	<b>1,021,746</b>	<b>1,454,260</b>

In the prior year, the impairment of trade receivables was assessed based on the incurred loss model under IAS 39. Under IFRS 9 the Group and the Company measure the probability of default upon initial recognition of a receivable and at each balance sheet date consider whether there has been a significant increase of credit risk since the initial recognition (see Notes 2.16. and 2.17.)

For banks and financial institutions, independently rated parties with own or parent bank's minimum rating of investment grade are accepted. Otherwise, if there is no independent rating, management performs risk control to assess the credit quality of the financial counterparty, taking into account its financial position, past co-operation experience and other factors. After performed assessment individual credit limits are set based on internal ratings in accordance with principles set by the Financial Risk Management Policy. The basis for estimating the credit quality of individually significant financial assets not past due is credit ratings assigned by the rating agencies or, in their absence, the earlier credit behaviour of clients and other parties to the contract.

Credit risk related to cash and short-term deposits with banks is managed by balancing the placement of financial assets in order to maintain the possibility to choose the best offers and to reduce probability to incur losses.

**The table below shows the balance of cash and cash equivalents by financial counterparties at the end of the reporting period:**

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Investment level credit rating*	126,483	227,686	124,582	224,538
No or non-investment level credit rating	2,972	8,317	2,972	8,317
	<b>129,455</b>	<b>236,003</b>	<b>127,554</b>	<b>232,855</b>

\* Investment level credit rating assigned for the parent companies of banks

Set limits of credit exposure to the financial counterparties were not exceeded during the reporting period, and the Group and the Parent Company management does not expect any losses arising from a potential default of financial counterparty, financial counterparties are in Stage 1.

The Group and the Parent Company invest only in listed debt instruments with very low probability of default (State Treasury bonds).

**c) Liquidity risk**

Latvenergo Group's liquidity and cash flow risk management policy is to maintain a sufficient amount of cash and cash equivalents (Note 18) and the availability of long and short-term funding through an adequate amount of committed credit facilities in order to meet existing and expected commitments and compensate for fluctuations in cash flows due to the occurrence of a variety of financial risks.

The table below analyses the Group's and the Parent Company's financial liabilities into relevant maturity groupings based on the settlement terms. The amounts disclosed in the table are the contractual undiscounted cash flows. Contractual undiscounted cash flows originated by the borrowings are calculated taking into account the actual interest rates at the end of the reporting period.

**Liquidity analysis (contractual undiscounted gross cash flows)**

EUR'000

	Group					Parent Company				
	Less than 1 year	From 1 to 2 years	From 3 to 5 years	Over 5 years	TOTAL	Less than 1 year	From 1 to 2 years	From 3 to 5 years	Over 5 years	TOTAL
<b>As of 31 December 2018</b>										
Borrowings from banks	116,989	159,053	250,342	214,090	<b>740,474</b>	114,241	154,751	246,134	212,846	<b>727,972</b>
Issued debt securities (bonds)	2,880	37,769	104,228	–	<b>144,877</b>	2,880	37,769	104,228	–	<b>144,877</b>
Derivative financial instruments	14,362	2,864	2,708	(1,145)	<b>18,789</b>	14,362	2,864	2,708	(1,145)	<b>18,789</b>
Trade and other current financial payables (Note 25) *	103,707	–	–	–	<b>103,707</b>	78,726	–	–	–	<b>78,726</b>
	<b>237,938</b>	<b>199,686</b>	<b>357,278</b>	<b>212,945</b>	<b>1,007,847</b>	<b>210,209</b>	<b>195,384</b>	<b>353,070</b>	<b>211,701</b>	<b>970,364</b>
<b>As of 31 December 2017</b>										
Borrowings from banks	113,285	119,074	313,149	191,748	<b>737,256</b>	109,727	117,985	310,411	194,733	<b>732,856</b>
Issued debt securities (bonds)	2,880	2,880	142,041	–	<b>147,801</b>	2,880	2,880	142,041	–	<b>147,801</b>
Derivative financial instruments	5,304	5,077	3,273	318	<b>13,972</b>	5,304	5,077	3,273	318	<b>13,972</b>
Trade and other current financial payables (Note 25) *	115,742	–	–	–	<b>115,742</b>	79,341	–	–	–	<b>79,341</b>
	<b>237,211</b>	<b>127,031</b>	<b>458,463</b>	<b>192,066</b>	<b>1,014,771</b>	<b>197,252</b>	<b>125,942</b>	<b>455,725</b>	<b>195,051</b>	<b>973,970</b>

\* Excluding advances received, deferred income, tax related liabilities and other non-current or current non-financial payables

**3.2. CAPITAL RISK MANAGEMENT**

The Group's and the Parent Company's objectives when managing capital are to safeguard the Group's and Parent Company's ability to continue as a going concern as well as to ensure necessary financing for investment program and to avoid breaches of covenants (no breaches in 2018 nor 2017), which are linked to capital structure and are stipulated in the majority of loan agreements.

In order to maintain or adjust the capital structure, the Group and the Parent Company may evaluate the amount and timing of raising new debt due to investment programs or initiate new investments in the share capital by shareholder. Also asset revaluation directly influences the capital structure. To comply with loan covenants, the Group and the Parent Company monitor capital on the basis of the capital ratio.

This ratio is calculated by dividing the equity by the sum of total assets and nominal value of issued and outstanding financial guarantees. According to the Group's strategy and defined loan covenants as per loan agreements the capital ratio shall be maintained at least at 30% level.

**The capital ratio figures were as follows:**

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Total equity	2,320,065	2,846,891	1,993,823	2,382,638
Total assets	3,798,819	4,415,725	3,141,109	3,649,200
<b>Capital Ratio</b>	<b>61%</b>	<b>64%</b>	<b>63%</b>	<b>65%</b>

## 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgments are regularly evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group and the Parent Company make estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

### a) Estimates concerning property, plant and equipment

#### I) Useful lives of property, plant and equipment

The Group and the Parent Company make estimates concerning the expected useful lives and residual values of property, plant and equipment. These are reviewed at the end of each reporting period and are based on the past experience as well as industry practice. Previous experience has shown that the actual useful lives have sometimes been longer than the estimates. Values of fully depreciated property, plant and equipment are disclosed in Note 14 a. Quantifying an impact of potential changes in the useful lives is deemed impracticable therefore sensitivity analysis is not disclosed.

#### II) Recoverable amount of property, plant and equipment

The Group and the Parent Company perform impairment tests for items of property, plant and equipment when the events and circumstances indicate a potential impairment. For the items of PPE the following separate cash-generating units are defined – the distribution system assets, transmission system assets, assets of HPPs (Riga, Plavīnu, Keguma and Aiviekste HPPs) and assets of Latvenergo combined heat and power plants as disclosed in Note 14 d. According to these tests assets are written down to their recoverable amounts, if necessary. When carrying out impairment tests management uses various estimates for the cash flows arising from the use of the assets, sales, maintenance and repairs of the assets, as well as in respect of the inflation and discount rates. The estimates are based on the forecasts of the general economic environment, consumption and the estimated sales price of electricity. If the situation changes in the future, either additional impairment could be recognised, or the previously recognised impairment could be partially or fully reversed. Such factors as high maintenance and reconstruction costs, low load of several auxiliaries, comparatively substantial maintenance expense, limited facilities to sell property, plant and equipment in the market and other essential factors have an impact of decreasing of the recoverable amounts. Impairment charges recognised during the current reporting year are disclosed in Note 14 d.

#### III) Revaluation

Revaluation for part of the Group's and the Parent Company's property, plant and equipment is performed by independent, external and certified valuers by applying the depreciated replacement cost model or income method. Valuation has been performed according to international standards on property valuation, based on current use of property, plant and equipment that is estimated as the most effective and best use of these assets. As a result of valuation, depreciated replacement cost was determined for each asset. Depreciated replacement cost is difference between the cost of replacement or renewal of similar asset at the time of revaluation and the accumulated loss of an asset's value that encompasses physical deterioration, functional (technological) obsolescence and economic (external) obsolescence. Physical depreciation was determined proportionally to the age of the property, plant and equipment item. In assessment for property, plant and equipment items for which a reconstruction is planned in the near future additional functional depreciation was assessed. Remaining useful lives of property, plant and equipment items after revaluation were estimated according to estimated total depreciation. Income method is based on the identification and analysis of generation capacity, forecasting of electricity trade prices, analysis of historical generation and operating expenses and forecast of future costs, capital expenditure, net cash flows, as well calculation of discount and capitalisation rates, based on market data.

For detailed most recent revaluation results see Note 14 c.

### b) Impairment of financial assets

Until 31 December 2017 the estimated collectability of accounts receivable was assessed under IAS 39 on the basis of receivables from contracts with customers aging analysis according to estimates defined by the Group entities management and the Parent Company's management based on the incurred loss model. In case individual assessment was not possible due to the large number of individual balances, receivables were classified into three groups of similar credit risk characteristics (electricity, natural gas trade and related services receivables, heating and other receivables from contracts with customers and receivables from subsidiaries) and were collectively assessed for impairment, using historical loss experience. Historical loss experience was adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience was based and to remove the effects of conditions in the historical period that did not exist currently. The circumstances indicating an impairment loss may include initiated insolvency of the debtor and inability to meet payment terms.

Since 1 January 2018 the Group and the Parent Company have six types of financial assets that are subject to the expected credit loss model:

- non-current and current loans to related parties (the Parent Company)
- other non-current receivables
- other financial investments
- receivables from contracts with customers
- other current receivables
- cash and cash equivalents.

The loss allowances for financial assets are based on assumptions about risk of default and expected loss rates. The Group and the Company uses judgement in making these assumptions and selecting the inputs to the impairment calculation, based on the Group's and the Company's past history, existing market conditions as well as forward looking estimates at the end of each reporting period.

The Group and the Parent Company apply two expected credit loss models: portfolio model and counterparty model (Note 2.16.)

Using the portfolio model the Group and the Parent Company apply the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for trade receivables of basic business activities (electricity, natural gas and heat and supporting services sales, IT and telecommunication services sales). To measure expected credit losses these receivables have been grouped based on shared credit risk characteristics and the days past due. The Group and the Parent Company therefore have concluded that the expected loss rates for these receivables are a reasonable approximation of the credit risk exposure. The expected loss rates are based on the payment profiles of sales over a period of 2 years before 1 January 2018 and the corresponding historical credit losses experienced within this period. There are no adjustments made to the historical loss rates that would reflect current and forward-looking information on macroeconomic factors affecting the ability of the customers to settle the receivables as the Group and the Parent Company have assumed that macroeconomic factors, such as GDP or the unemployment rates in Latvia have insignificant impact on expected credit loss as macroeconomic projections foresee stable outlook of these indicators.

Counterparty model is used on individual contract basis for non-current and current loans to subsidiaries, other financial investments and cash and cash equivalents. If no significant increase in credit risk is identified, the expected credit losses according to this model are based on assessment of the individual counterparty's or counterparty's industry risk of default and recovery rate assigned by *Moody's* credit rating agency for 12 months expected losses rates. The circumstances indicating a significant increase in credit risk is significant increase in *Moody's* default and recovery rates (by 1 percentage point) and counterpart's inability to meet payment terms (overdue 30 days or more, insolvency or bankruptcy, or



initiated similar legal proceedings and other indications on inability to pay). If significant increase in credit risk identified, calculated lifetime expected credit loss.

Counterparty model also used for non-current receivables, individually significant receivables, receivables of energy industry companies and related parties by calculating lifetime expected losses based on corporate default and recovery rates.

All of the Group's and the Parent Company's other financial investments measured at amortised cost (investments in State Treasury bonds) do not have significant increase in credit risk and are considered to have low credit risk (*Moody's* credit rating – A3) and are in Stage 1, the loss allowance therefore was immaterial and wasn't recognised.

While cash and cash equivalents are also subject to the impairment requirements of IFRS 9, the identified impairment loss was immaterial, considering also fact that almost all of cash and cash equivalents are held in financial institutions with the credit rating grade of the institution or its parent bank at investment grade credit rating (mostly 'A level' credit rating) (Stage 1).

## **c) Estimates concerning revenue recognition from contracts with customers**

### **l) Recognition of mandatory procurement PSO fees**

The Group and the Parent Company have applied significant judgement for use of agent principle for recognition of mandatory procurement PSO fee (see also Note 2.21.).

Management has considered following indicators that the Group and the Parent Company are acting as agents because:

- do not have control over the mandatory procurement PSO fee before transferring to the customer;
- have duty for including the mandatory procurement PSO fee in invoices issued to the end customers, but are not entitled for revenues from mandatory procurement PSO fee. These fees are determined by state support mechanism and are covered by all electricity end-users in proportion to their electricity consumption;
- have no discretion in establishing mandatory procurement PSO fees price, either directly or indirectly;
- do not have exposure to rewards associated with mandatory procurement PSO fees.

### **II) Recognition of distribution system services and transmission system services (Parent Company)**

Management has evaluated that it does not have influence and control over distribution system services and transmission system services, therefore the Parent Company acts as an agent. In particular, Management has considered the following indicators that the Parent Company is acting as an agent because:

- does not control provision of distribution system and transmission system services;
- includes the distribution system and transmission system services in invoices issued to the customers on behalf of distribution system operator or transmission system operator and receives payment, but is not entitled to the respective revenues;
- has no discretion in distribution system or transmission system services price, either directly or indirectly (see also Note 2.21.).

### **III) Recognition of connection service fees to distribution system (Group)**

Connection fees to distribution system are not considered as separate (distinct) performance obligations, as are not distinct individually or within the context of the contract. Sales of distribution services are provided after customers have paid for the network connection, therefore network connection fees and sales of distribution services are highly interdependent and interrelated.

Income from connection and other income for reconstruction of distribution system assets on demand of clients are deferred as an ongoing service is identified as part of agreement to provide distribution system services with customers (Note 2.21) and accounted as deferred income from contracts with customers under IFRS 15 (see Note 27). Connection fees are recognised as income over the estimated customer

relationship period. Based on Management estimate, 20 years is the estimated customer relationship period, which is estimated as period after which requested power output for connection object could significantly change due to technological reasons.

Thus period over which revenue is recognised is based on Management estimate, as it is reasonably certain that assets, whose costs are partly reimbursed by connection service fees, will be used to provide distribution system services for a longer period than the term stated in agreement with the customer (Note 2.21).

## **d) Recognition and reassessment of provisions**

As of 31 December 2018, the Group had set up provisions for environmental protection, post-employment benefits and termination benefits totalling EUR 21.0 million (31/12/2017: EUR 25.3 million) and the Parent Company in amount of EUR 9.0 million (31/12/2017: EUR 9.7 million) (Note 26). The amount and timing of the settlement of these obligations is uncertain. A number of assumptions and estimates have been used to determine the present value of provisions, including the amount of future expenditure, inflation rates, and the timing of settlement of the expenditure. The actual expenditure may also differ from the provisions recognised as a result of possible changes in legislative norms, technology available in the future to restore environmental damages, and expenditure covered by third parties. For revaluation of provisions for post-employment obligations probabilities of retirement in different employees' aging groups as well as variable demographic factors and financial factors (including expected remuneration increase and determined changes in benefit amounts) have been estimated. The probabilities and other factors are determined on the basis of previous experience. According to defined development directions per Strategy of Latvenergo Group for the period 2017-2022, the management of the Parent Company approved the Strategic Development and Efficiency Programme. Provisions for employees' termination benefits are recognised on a basis of Strategic Development and Efficiency Programme of Latvenergo Group for the period in which it is planned to implement the efficiency program (including Latvenergo AS and Sadales tīkls AS efficiency activities), by which it is intended to reduce gradually the number of employees by the year 2022. The key assumptions made to determine the amount of provisions are provided in Note 26.

## **e) Evaluation of effectiveness of hedging instruments**

The Group and the Parent Company have concluded significant number of forward and future contracts and swap agreements to hedge the risk of the changes in prices of electricity and natural gas as well as interest rate fluctuations to which cash flow risk hedge accounting is applied and the gains and losses from changes in the fair value of the effective hedging instruments and items secured against risk are included in respective equity reserve. The evaluation of the effectiveness of the hedging is based on Management's estimates with regard to future purchase transactions of electricity and natural gas and signed variable interest loan agreements. When hedging instruments turn out to be ineffective, gains/losses from the changes in the fair value are recognised in the Statement of Profit or Loss (Note 24).

## **f) Lease classification**

The Group has entered into the lease agreement with licenced transmission system operator for the lease of transmission system network infrastructure and land, buildings and facilities related to this infrastructure till the end of 2019. At the end of lease agreement the parties may review terms of the agreement. If the parties do not agree on a new lease agreement, the existing agreement is prolonged for further 5 years subject to transmission system operator having a valid licence for electricity transmission. Based on an evaluation of the terms of the agreement, such as rights of the ownership is not transferred as determined by Energy Law of the Republic of Latvia, the lessor retains all the significant risks and rewards of ownership of these assets, the Group accounts this agreement as operating lease. In making the judgement on lease classification the management assessed the criteria included in IAS 17 'Leases' and considered the following circumstances:

- The lease does not transfer ownership of the assets at the end of the lease term,
- The lessee has no option to purchase the assets at a price sufficiently lower than the fair value,
- The Group is entitled to lease payments ensuring the rate of return on assets approved by Public Utilities Commission (PUC) and bears risks and rewards related to ownership and the changes in the fair value of the leased assets,

- The lease agreement could be prolonged up to 2025, until when transmission system operator has valid licence for electricity transmission. The lease term does not cover the major part of the economic life of leased assets,
- The lease payments are determined by methodology for transmission system services approved by PUC, considering the rate of return on assets approved by PUC and the lease payments during the predictable lease term do not amount to substantially all of the estimated fair value of the leased assets,
- The assets can only be operated by a lessee holding the licence for electricity transmission. In accordance with the effective legislation, the Group cannot obtain the licence itself. Thus, after 2025 when the current licence for electricity transmission issued to transmission system operator expires, the Group will have to lease the transmission system assets to a company having the licence for electricity transmission. Analysing the current valid lease agreement and considering that PUC determines the rate of return on assets used for the calculation of lease payments and it is reset on a regular basis, the lease payments beyond 2025 will be on market terms. Thus, these periods need not to be taken into account when assessing the substance of the current lease agreement.

#### **g) Recognition of connection service fees to transmission system (IAS 17)**

Connection fees to transmission system are recognised as income over the estimated lease period. The estimated lease period is based on the Management estimate.

Income from connection to transmission system and other service fees is deferred as an ongoing service is identified as part of the agreement with the lessee. Operating lease agreement term is 5 years, the period over which revenue from connection fees is recognised is longer, as it is reasonably certain that assets, whose costs are partly reimbursed by connection fees will be leased for a longer period than defined original lease term.

#### **h) Impact of sanctions applied to a supplier of hydroelectric units**

Latvenergo AS has concluded contracts with PJSC Power Machines for reconstruction of Pļavinas HPP's hydroelectric units HA1 and HA3 and reconstruction of Keguma HPP's hydroelectric units HA5, HA6 and HA7 until the year 2020 with the total amount of contracts EUR 78,045 thousand. Of the total contracted amount, the Parent Company has received assets and services in total amount of EUR 50,521 thousand as at 31 December 2018 (31/12/2017: 49,807 EUR thousand) including assets under construction (not installed) of EUR 16,562 thousand as of 31 December 2018 (31/12/2017: EUR 35,473 thousand).

On 26 January 2018 U.S. Department of Treasury Office of Foreign Assets Control (hereinafter – OFAC) published a statement on persons subjected to sanctions of USA, according to this statement PJSC Power Machines is under abovementioned sanctions. As a result, the realisation of the project has been suspended. On 10 December 2018 Latvenergo AS submitted repeated the application to OFAC with a request to wind down of contractual relationship with PJSC Power Machines. In negative scenario there is possibility of mutual future claims, but the outcome cannot be determined at the moment of approval of the Financial Statements.

The Management has made assessment that there is no basis for recognition of impairment for the assets under construction and no provision related to resolution to this matter needs to be recognised. In reaching the above conclusions, the management has also used external independent expert assessment, including the possibility to use supplied, but not yet installed items for the reconstruction of hydroelectric units.

#### **i) Recognition of one-off compensation in relation to cogeneration power plants**

In October 2017, the Parent Company applied for a one-off compensation from the state, at the same time opting out of the receipt of 75% of the guaranteed annual payments for installed electrical capacity in combined heat and power plant CHPP-1 and CHPP-2. The one-off compensation was calculated as 75% of the discounted future guaranteed payments for installed electrical capacity. On 21 November 2017, the Cabinet of Ministers of the Republic of Latvia accepted an order on one-off compensation to Latvenergo AS on guaranteed support for the installed capacity of cogeneration power plants, therefore the Parent

Company obtained a government grant in the amount of EUR 454,413 thousand.

The grant was divided into two parts and recognised in accordance with accounting policy stated in Note 2.15 a:

- an unconditional grant in amount of EUR 140,000 thousand recognised as 'Other income' (Note 7) in the Group's and the Parent Company's statement of profit or loss in 2017
- a conditional grant in amount of EUR 314,413 thousand recognised as deferred income in the Group's and the Parent Company's statement of financial position and to be allocated to income on a straight-line basis until fulfilling obligation till the end of the support period – 23 September 2028.

The decision on settlement of one-off compensation was made separately. Following the order No. 685 of the Cabinet of Ministers of the Republic of Latvia on 28 November 2017 a trilateral agreement was concluded between Republic of Latvia (represented by Ministry of Economics), the Parent Company and its subsidiary Energijas publiskais tirgotājs AS (public trader) on settlement of the one-off compensation. Accordingly, public trader recognised receivable from state for one-off compensation in the amount of EUR 454,413 thousand. This balance was recognised as government grant receivable in Group financial statements (Note 17 b). For Energijas publiskais tirgotājs AS to ensure financing of compensation, the Parent Company concluded agreement on loan issue in amount equal to the grant receivable (see Note 28 e).

On 20 March 2018 registered changes in share capital of the Parent Company by decreasing share capital in amount of EUR 454,413 thousand (Note 19).

On 26 March 2018, in accordance with the trilateral agreement, the Parent Company settled its liability towards Ministry of Economics for the capital release by netting off the balance with the respective grant receivable from the state and netted balances with public trader on the same date.

On 26 September 2018, the Cabinet of Ministers decided to change conditions for a part of the grant in the amount of EUR 51,700 thousand stipulating it as unconditional, by reducing the remaining part of the grant proportionally to this amount until the end of the support period. As a result, of this and the previous order, EUR 81 004 thousand were recognised as 'Other income' in the Group's and Parent Company's statement of profit or loss in 2018. Consequently, EUR 233,409 thousand remained recognised as deferred income as of 31 December 2018 and to be allocated to income on a straight-line basis until fulfilling obligation till the end of the support period – 23 September 2028.

#### **j) Deferred tax recognition**

The untaxed 2018 profits of the subsidiaries are subject to deferred tax charge in the Consolidated Financial Statements to the extent that the Parent Company as shareholder will decide in a foreseeable future on distribution of this profit through dividends which will be taxed on distribution with tax rate 20/80 (see Note 2.23.). The management of the Parent Company has made judgement on the expected timing and extent of the distribution of the 2018 profits of subsidiaries and as of 31 December 2018 recognised in the Group's Consolidated Financial Statements deferred tax liability in the amount of EUR 12,297 thousand related to year 2018 profit of its subsidiaries to be distributed.

## **5. OPERATING SEGMENT INFORMATION**

### **OPERATING SEGMENTS**

For segment reporting purposes, the division into operating segments is based on internal management structure, which is the basis for the reporting system, performance assessment and the allocation of resources by the operating segment decision maker – management of the Group's company operating in each of segments. The Management Board of the Parent Company reviews financial results of operating segments.

The profit measure monitored by the chief operating decision maker primarily is EBITDA, but it also monitors operating profit. In separate financial statements operating profit excludes the dividend income and interest income from subsidiaries. The subsidiaries operate independently from the Parent Company under

the requirements of EU and Latvian legislation and their businesses are different from that of the Parent Company. Therefore, the Parent Company's chief operating decision maker monitors the performance of the Parent Company and makes decisions regarding allocation of resources based on the operating results of the Parent Company.

The Group divides its operations into three main operating segments – generation and trade, distribution and lease of transmission system assets. The Parent Company divides its operations into one main operating segment – generation and trade.

In addition, corporate functions, that cover administration and other support services, are presented in the Group and the Parent Company as separate segment.

**Corporate functions** provide management services to subsidiaries as well as provides IT and telecommunication, rental services to external customers.

**Generation and trade** comprises the Group's electricity and thermal energy generation operations, which are organised into the legal entities: Latvenergo AS and Liepājas enerģija SIA; electricity and natural gas trade

(including electricity and natural gas wholesale) in the Baltics carried out by Latvenergo AS, Elektrum Eesti OÜ and Elektrum Lietuva UAB, as well as administration of the mandatory procurement process provided by Enerģijas publiskais tirgotājs AS.

**The operations of the distribution operating segment** relate to the provision of electricity distribution services in Latvia and is managed by the subsidiary Sadales tīkls AS (the largest distribution system operator in Latvia).

**The operations of the lease of transmission system assets operating segment** is managed by Latvijas elektriskie tīkli AS – the owner of transmission system assets (330 kV and 110 kV transmission lines, substations and distribution points), which provides financing of investments in these assets.

The following table presents revenue, financial results and profit information and segment assets and liabilities of the Group's and the Parent Company's operating segments. Inter-segment revenue is eliminated on consolidation and reflected in the 'adjustments and eliminations' column. All transactions between segments are made based on the regulated tariffs, where applicable, or on an arm's length principle.

EUR'000												
	Group							Parent Company				
	Generation and trad	Distribution	Lease of transmission system assets	Corporate functions	TOTAL segments	Adjustments and eliminations	TOTAL Group	Generation and trade	Corporate functions	TOTAL segments	Adjustments and eliminations	TOTAL Parent Company
<b>2018</b>												
<b>Revenue</b>												
External customers	510,434	321,232	39,203	7,139	<b>878,008</b>	–	<b>878,008</b>	386,510	48,689	<b>435,199</b>	–	<b>435,199</b>
Inter-segment	1,390	1,730	2,991	45,451	<b>51,562</b>	(51,562)	<b>–</b>	459	22,366	<b>22,825</b>	(22,825)	<b>–</b>
<b>TOTAL revenue</b>	<b>511,824</b>	<b>322,962</b>	<b>42,194</b>	<b>52,590</b>	<b>929,570</b>	<b>(51,562)</b>	<b>878,008</b>	<b>386,969</b>	<b>71,055</b>	<b>458,024</b>	<b>(22,825)</b>	<b>435,199</b>
<b>Results</b>												
EBITDA	146,552	119,791	41,456	13,783	<b>321,582</b>	–	<b>321,582</b>	134,040	26,887	<b>160,927</b>	–	<b>160,927</b>
Amortisation, depreciation and intangible assets and PPE impairment loss	(110,490)	(77,432)	(25,856)	(12,042)	<b>(225,820)</b>	–	<b>(225,820)</b>	(107,397)	(19,727)	<b>(127,124)</b>	–	<b>(127,124)</b>
Profit before tax	36,062	42,359	15,600	1,741	<b>95,762</b>	(7,249)	<b>88,513</b>	26,643	7,160	<b>33,803</b>	178,957	<b>212,760</b>
Assets at the end of the year	1,329,274	1,669,710	579,327	86,350	<b>3,664,661</b>	134,158	<b>3,798,819</b>	1,212,681	161,577	<b>1,374,258</b>	1,766,851	<b>3,141,109</b>
Liabilities at the end of the year	295,168	192,016	95,123	6,535	<b>588,842</b>	889,912	<b>1,478,754</b>	298,328	7,882	<b>306,210</b>	841,076	<b>1,147,286</b>
Capital expenditure	28,909	95,117	87,136	12,411	<b>223,573</b>	(2,966)	<b>220,607</b>	26,921	14,429	<b>41,350</b>	–	<b>41,350</b>
<b>2017</b>												
<b>Revenue</b>												
External customers	554,489	318,851	44,415	7,872	<b>925,627</b>	–	<b>925,627</b>	448,660	49,920	<b>498,580</b>	–	<b>498,580</b>
Inter-segment	1,605	1,851	2,541	52,739	<b>58,736</b>	(58,736)	<b>–</b>	346	29,089	<b>29,435</b>	(29,435)	<b>–</b>
<b>TOTAL revenue</b>	<b>556,094</b>	<b>320,702</b>	<b>46,956</b>	<b>60,611</b>	<b>984,363</b>	<b>(58,736)</b>	<b>925,627</b>	<b>449,006</b>	<b>79,009</b>	<b>528,015</b>	<b>(29,435)</b>	<b>498,580</b>
<b>Results</b>												
EBITDA	372,829	111,599	45,305	11,963	<b>541,696</b>	–	<b>541,696</b>	362,534	24,566	<b>387,100</b>	–	<b>387,100</b>
Amortisation, depreciation and intangible assets and PPE impairment loss	(194,376)	(76,630)	(24,345)	(12,263)	<b>(307,614)</b>	–	<b>(307,614)</b>	(191,228)	(18,456)	<b>(209,684)</b>	–	<b>(209,684)</b>
Profit / (loss) before tax	178,453	34,969	20,960	(300)	<b>234,082</b>	(9,968)	<b>224,114</b>	171,306	6,110	<b>177,416</b>	8,490	<b>185,906</b>
Assets at the end of the year	1,956,888	1,641,318	500,863	85,584	<b>4,184,653</b>	231,072	<b>4,415,725</b>	1,286,478	192,435	<b>1,478,913</b>	2,170,287	<b>3,649,200</b>
Liabilities at the end of the year	393,759	188,025	67,502	6,551	<b>655,837</b>	912,997	<b>1,568,834</b>	383,708	8,695	<b>392,403</b>	874,159	<b>1,266,562</b>
Capital expenditure	74,021	107,683	63,085	10,815	<b>255,604</b>	(11,793)	<b>243,811</b>	73,150	16,128	<b>89,278</b>	–	<b>89,278</b>

## The Group's and the Parent Company's revenue from external customers (Note 6):

EUR'000

	Group						Parent Company			
	Generation and trade	Distribution	Lease of transmission system assets	Corporate Functions	TOTAL segments	TOTAL Group	Generation and trade	Corporate Functions	TOTAL segments	TOTAL Parent Company
<b>Year ended 31 December 2018</b>										
<b>Revenue from contracts with customers recognised over time:</b>										
Trade of energy and related supply services	422,673	3,045	–	–	425,718	425,718	312,994	–	312,994	312,994
Distribution system services	1	303,438	–	–	303,439	303,439	–	–	–	–
Heat sales	78,489	86	–	5	78,580	78,580	66,258	5	66,263	66,263
Other revenue	9,271	14,548	–	5,681	29,500	29,500	7,258	32,697	39,955	39,955
<b>TOTAL revenue from contracts with customers</b>	<b>510,434</b>	<b>321,117</b>	<b>–</b>	<b>5,686</b>	<b>837,237</b>	<b>837,237</b>	<b>386,510</b>	<b>32,702</b>	<b>419,212</b>	<b>419,212</b>
<b>Other revenue:</b>										
Lease of transmission system assets (Note 14 e)	–	–	38,699	–	38,699	38,699	–	–	–	–
Lease of other assets	–	115	–	1,453	1,568	1,568	–	15,987	15,987	15,987
Other revenue	–	–	504	–	504	504	–	–	–	–
<b>TOTAL other revenue</b>	<b>–</b>	<b>115</b>	<b>39,203</b>	<b>1,453</b>	<b>40 771</b>	<b>40 771</b>	<b>–</b>	<b>15,987</b>	<b>15,987</b>	<b>15,987</b>
<b>TOTAL revenue, including:</b>	<b>510,434</b>	<b>321,232</b>	<b>39,203</b>	<b>7,139</b>	<b>878,008</b>	<b>878,008</b>	<b>386,510</b>	<b>48,689</b>	<b>435,199</b>	<b>435,199</b>
Latvia	331,617	321,232	39,203	6,790	698,842	698,842	311,921	47,395	359,316	359,316
Outside Latvia	178,817	–	–	349	179,166	179,166	74,589	1,294	75,883	75,883
<b>Year ended 31 December 2017</b>										
<b>Revenue from contracts with customers recognised over time:</b>										
Trade of energy and related supply services	464,030	3,096	–	–	467,126	467,126	370,626	–	370,626	370,626
Distribution system services	1	301,873	–	–	301,874	301,874	–	–	–	–
Heat sales	83,156	75	–	8	83,239	83,239	71,413	9	71,422	71,422
Other revenue	7,300	13,681	–	6,124	27,105	27,105	6,620	33,990	40,610	40,610
<b>TOTAL revenue from contracts with customers</b>	<b>554,487</b>	<b>318,725</b>	<b>–</b>	<b>6,132</b>	<b>879,344</b>	<b>879,344</b>	<b>448,659</b>	<b>33,999</b>	<b>482,658</b>	<b>482,658</b>
<b>Other revenue:</b>										
Lease of transmission system assets (Note 14 e)	–	–	43,911	–	43,911	43,911	–	–	–	–
Lease of other assets	2	126	–	1,740	1,868	1,868	1	15,921	15,922	15,922
Other revenue	–	–	504	–	504	504	–	–	–	–
<b>TOTAL other revenue</b>	<b>2</b>	<b>126</b>	<b>44,415</b>	<b>1,740</b>	<b>46,283</b>	<b>46,283</b>	<b>1</b>	<b>15,921</b>	<b>15,922</b>	<b>15,922</b>
<b>TOTAL revenue, including:</b>	<b>554,489</b>	<b>318,851</b>	<b>44,415</b>	<b>7,872</b>	<b>925,627</b>	<b>925,627</b>	<b>448,660</b>	<b>49,920</b>	<b>498,580</b>	<b>498,580</b>
Latvia	404,136	318,851	44,415	7,272	774,674	774,674	386,513	48,407	434,920	434,920
Outside Latvia	150,353	–	–	600	150,953	150,953	62,147	1,513	63,660	63,660

## ADJUSTMENTS AND ELIMINATIONS

Finance income and expenses, fair value gains and losses on financial assets, financial instruments and deferred taxes are not allocated to individual segments as the underlying instruments are managed on a group basis. Taxes and certain financial assets and liabilities, including loans and borrowings are not allocated to those segments as they are also managed on a group basis.

Capital expenditure consists of additions of property, plant and equipment, intangible assets and investment properties including assets from the acquisition of subsidiaries.

Segment EBITDA is equal to total EBITDA, therefore reconciliation is not made.

### Reconciliation of profit before tax

EUR'000

	Notes	Group		Parent Company	
		31/12/2018	31/12/2017	31/12/2018	31/12/2017
EBITDA		321,582	541,696	160,927	387,100
Amortisation, depreciation and intangible assets and PPE impairment loss		(225,820)	(307,614)	(127,124)	(209,684)
<b>Segment profit before tax</b>		<b>95,762</b>	<b>234,082</b>	<b>33,803</b>	<b>177,416</b>
Finance income	11 a	1,157	1,243	11,446	11,433
Finance costs	11 b	(8,406)	(11,211)	(10,135)	(12,054)
Dividends received from subsidiaries	15 a	–	–	177,646	9,111
<b>Profit before tax</b>		<b>88,513</b>	<b>224,114</b>	<b>212,760</b>	<b>185,906</b>

### Reconciliation of assets

EUR'000

	Notes	Group		Parent Company	
		31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>Segment operating assets</b>		<b>3,664,661</b>	<b>4,184,653</b>	<b>1,374,258</b>	<b>1,478,913</b>
Connection usage rights		(39,744)	(26,652)	–	–
Non-current financial investments	15	40	40	830,542	817,048
Loans to subsidiaries	28 f	–	–	765,815	1,098,781
Held-to-maturity financial assets	21	–	16,984	–	16,984
Other financial investments	21	16,935	–	16,935	–
Derivative financial instruments	23	15,853	4,619	15,853	4,619
Prepayment for income and other taxes		11,619	78	10,152	–
Cash and cash equivalents	18	129,455	236,003	127,554	232,855
<b>TOTAL assets</b>		<b>3,798,819</b>	<b>4,415,725</b>	<b>3,141,109</b>	<b>3,649,200</b>

## Reconciliation of liabilities

EUR'000

	Notes	Group		Parent Company	
		2018	2017	2018	2017
<b>Segment operating liabilities</b>		<b>588,842</b>	<b>655,837</b>	<b>306,210</b>	<b>392,403</b>
Deferred income tax liabilities	12	12,297	–	–	–
Current corporate income tax liabilities		2	27,725	–	24,739
Borrowings	22	814,343	826,757	802,268	814,772
Derivative financial instruments	23	10,204	8,084	10,204	8,084
Provisions and other payables		53,066	50,431	28,604	26,564
<b>TOTAL liabilities</b>		<b>1,478,754</b>	<b>1,568,834</b>	<b>1,147,286</b>	<b>1,266,562</b>

Non-current assets that consist of intangible assets, property, plant and equipment and investment properties are located in the Group's country of domicile – Latvia.

Revenue from major customer in 2018 for the Group amounted to EUR 66,454 thousand and for the Parent Company EUR 66,454 thousand (2017: EUR 72,788 thousand and 72,785 thousand) arising from sales by the generation and trade segment.

## 6. REVENUE

EUR'000

	IFRS or IAS applied	Group		Parent Company	
		2018	2017	2018	2017
Revenue from contracts with customers recognised over time:					
Trade of energy and related supply services	IFRS 15	425,718	467,126	312,994	370,626
Distribution system services	IFRS 15	303,439	301,874	–	–
Heat sales	IFRS 15	78,580	83,239	66,263	71,422
Other revenue	IFRS 15	29,500	27,105	39,955	40,610
TOTAL revenue from contracts with customers		837,237	879,344	419,212	482,658
Other revenue:					
Lease of transmission system assets (Note 14 e)	IAS 17	38,699	43,911	–	–
Lease of other assets (Note 14 e)	IAS 17	1,568	1,868	15,987	15,922
Other revenue	IAS 17	504	504	–	–
TOTAL other revenue		40,771	46,283	15,987	15,922
TOTAL revenue		878,008	925,627	435,199	498,580



The Group and the Parent Company derive revenue from contracts with customers from Latvia and outside Latvia – Estonia, Lithuania, Nordic countries.

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
Latvia	658,071	728,391	343,329	418,998
Outside Latvia	179,166	150,953	75,883	63,660
<b>TOTAL revenue from contracts with customers</b>	<b>837,237</b>	<b>879,344</b>	<b>419,212</b>	<b>482,658</b>

**Gross amounts invoiced to customers by applying agent accounting principle (see Note 4 c), recognised on net basis under trade of energy and related supply services:**

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
Mandatory procurement PSO fees	98,459	114,266	101,852	119,562
Distribution system services	10,576	10,125	208,304	217,999
Transmission system services	1,562	1,750	1,613	1,783
<b>TOTAL revenue recognised applying agent accounting principle</b>	<b>110,597</b>	<b>126,141</b>	<b>311,769</b>	<b>339,344</b>

Net effect in revenue from applying agent accounting principle is 0.

**The Group has recognised the following liabilities from contracts with customers:**

EUR'000

	31/12/2018	31/12/2017
Non-current contract liabilities on deferred income from connection fees (Note 27 I, a)	143,494	142,132
Current contract liabilities on deferred income from connection fees (Note 27 II, a)	12,984	12,247
Contract liabilities – deferred income from use of allowed effective electrical load (distribution system services) (Note 27 II, a)	287	253
<b>TOTAL liabilities</b>	<b>156,765</b>	<b>154,632</b>

**Movement in deferred connection fees – contract liability from contracts with customers for the Group (non-current and current part):**

EUR'000

	31/12/2018	31/12/2017
<b>At the beginning of the year</b>	<b>154,632</b>	<b>153,432</b>
Received fees (Note 27)	14,726	12,848
Credited to the Statement of Profit or Loss	(12,593)	(11,648)
<b>At the end of the year</b>	<b>156,765</b>	<b>154,632</b>

## 7. OTHER INCOME

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
One-off compensation from the state on state support for the installed capacity of CHPPs*	81,004	140,000	81,004	140,000
Fines and penalties	7,359	6,900	5,812	5,907
Net gain from sale of assets held for sale and PPE	1,254	254	3,763	929
Net gain from sale of current assets	91	–	2	–
Compensations and insurance claims	618	803	279	579
Other operating income	2,934	1,993	321	87
<b>TOTAL other income</b>	<b>93,260</b>	<b>149,950</b>	<b>91,181</b>	<b>147,502</b>

\* Information about compensation is disclosed in Note 4 i)

## 8. RAW MATERIALS AND CONSUMABLES USED

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>Electricity:</b>				
Purchased electricity	196,660	124,637	78,747	27,187
Fair value loss on electricity forwards and futures (Note 23, I)	417	3,435	417	3,435
Electricity transmission services costs (Note 28 a)	71,368	71,044	1,015	845
<b>TOTAL electricity costs</b>	<b>268,445</b>	<b>199,116</b>	<b>80,179</b>	<b>31,467</b>
Energy resources costs	197,485	118,185	190,139	112,248
Raw materials, spare parts and maintenance costs	31,363	32,389	14,274	12,388
<b>TOTAL raw materials and consumables used</b>	<b>497,293</b>	<b>349,690</b>	<b>284,592</b>	<b>156,103</b>

## 9. PERSONNEL EXPENSES

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
Wages and salaries	73,523	74,453	31,164	31,233
State social insurance contributions	17,685	17,526	7,448	7,307
Expenditure of employment termination	6,078	15,086	1,199	3,845
Pension costs – defined contribution plan	2,256	2,225	893	901
Other benefits defined in the Collective Agreement	1,200	1,048	426	378
Life insurance costs	3,192	3,131	1,289	1,228
Capitalised personnel expenses	(172)	(180)	(23)	–
<b>TOTAL personnel expenses, including remuneration to the management</b>	<b>103,762</b>	<b>113,289</b>	<b>42,396</b>	<b>44,892</b>
<b>Including remuneration to the management*:</b>				
Wages and salaries	1,992	1,880	769	865
State social insurance contributions	499	451	186	206
Expenditure of employment termination	75	206	75	–
Pension costs – defined contribution plan	24	30	4	–
Life insurance costs	31	26	7	7
<b>TOTAL remuneration to the management*</b>	<b>2,621</b>	<b>2,593</b>	<b>1,041</b>	<b>1,078</b>

\* Remuneration to the Group's management includes remuneration to the members of the Management Boards of the Group entities, the Supervisory Board and the Supervisory body (Audit Committee) of the Parent Company. Remuneration to the Parent Company's management includes remuneration to the members of the Parent Company's Management Board, the Supervisory Board and the Supervisory body (Audit Committee).

	Group		Parent Company	
	2018	2017	2018	2017
Number of employees at the end of the year	3,508	3,908	1,355	1,431
Average number of employees during the year	3,617	4,075	1,387	1,467

## 10. OTHER OPERATING EXPENSES

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
Selling expenses and customer services	6,154	6,093	4,788	4,723
Information technology maintenance	5,115	5,143	4,771	4,931
Transportation expenses	6,411	6,204	2,164	2,185
Environment protection and work safety	7,858	11,900	8,125	11,205
Real estate maintenance and utilities expenses	7,448	8,261	6,992	7,825
Telecommunications services	2,049	2,224	2,275	2,552
Real estate tax	1,095	1,086	1,083	1,074
Public utilities regulation fee	1,993	1,996	932	932
Subsidised energy tax (SET)	–	15,087	–	14,859
Audit fee*	100	93	45	38
Other expenses	10,886	12,815	7,526	7,663
<b>TOTAL other operating expenses</b>	<b>49,109</b>	<b>70,902</b>	<b>38,701</b>	<b>57,987</b>

\* Audit fee consists from audit of the Group's entities financial statements in the amount of EUR 96 thousand; Parent Company - EUR 41 thousand (2017: EUR 85 thousand; Parent Company - EUR 30 thousand) and audit of The Group's Sustainability report and financial covenants - EUR 4 thousand (2017: EUR 8 thousand)

## 11. FINANCE INCOME AND COSTS

### a) Finance income

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
Interest income on bank accounts and deposits	36	16	36	16
Interest income on loans to related parties	–	–	10,289	10,189
Interest income from held-to-maturity financial assets	–	1,085	–	1,085
Interest income from other financial investments	1,076	–	1,076	–
Net gain on issued debt securities (bonds)	44	120	44	120
Net gain from currency exchange rate fluctuations	–	22	–	23
Income on financing component	1	–	1	–
<b>TOTAL finance income</b>	<b>1,157</b>	<b>1,243</b>	<b>11,446</b>	<b>11,433</b>

**b) Finance costs**

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
Interest expense on borrowings	6,276	7,643	8,029	8,505
Interest expense on issued debt securities (bonds)	2,880	4,753	2,880	4,753
Net losses on redemption of held-to-maturity financial assets	–	50	–	50
Net losses on redemption other financial investments	49	–	49	–
Capitalised borrowing costs (Note 14 a)	(889)	(1,359)	(889)	(1,359)
Net losses on currency exchange rate fluctuations	2	–	2	–
Other finance costs	88	124	64	105
<b>TOTAL finance costs</b>	<b>8,406</b>	<b>11,211</b>	<b>10,135</b>	<b>12,054</b>

## 12. INCOME TAX

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
Current income tax for the year	261	51,199	27	45,097
Deferred income tax changes	12,297	(20,083)	–	(20,187)
Reversal of deferred tax	–	(129,023)	–	10,105
<b>TOTAL income tax</b>	<b>12,558</b>	<b>(97,907)</b>	<b>27</b>	<b>35,015</b>

**The movement on the deferred income tax balances:**

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>Deferred tax liabilities at the beginning of the year</b>	<b>–</b>	<b>315,759</b>	<b>–</b>	<b>126,260</b>
Attributable to non-current assets revaluation reserve in equity (Note 20 a)	–	3,325	–	3,325
Changes recognised in the Statement of Profit or Loss	12,297	(20,083)	–	(20,187)
<b>Deferred tax liabilities at the end of the year before reversal</b>	<b>12,297</b>	<b>299,001</b>	<b>–</b>	<b>109,398</b>
Reversed to the Statement of comprehensive income	–	(169,978)	–	(119,503)
Reversed in the Statement of Profit or Loss	–	(129,023)	–	10,105
<b>Deferred tax liabilities at the end of the year</b>	<b>12,297</b>	<b>–</b>	<b>–</b>	<b>–</b>

The Group has recognised deferred tax liability for the year 2018 profit of its subsidiaries as in a foreseeable future will be decided on distribution of this profit through dividends which will be taxed on distribution.

**Actual corporate income tax charge for the reporting year, if compared with theoretical calculations:**

EUR'000

	Group	Parent Company
	2017	2017
<b>Profit before tax</b>	<b>224,114</b>	<b>185,906</b>
Tax at the applicable tax rate of 15%	33,617	27,886
<b>Permanent differences:</b>		
Received dividends from subsidiaries	–	(1,367)
Non-operating expenses	272	120
Other expenses	17,310	18,458
Deferred income tax changes	(20,083)	(20,187)
<b>Actual corporate income tax for the reporting year</b>	<b>31,116</b>	<b>24,910</b>
Reversal of deferred tax	(129,023)	10,105
<b>TOTAL income tax</b>	<b>(97,907)</b>	<b>35,015</b>
<b>Effective income tax rate</b>	<b>13.9%</b>	<b>13.4%</b>

## 13. INTANGIBLE ASSETS

### a) Intangible assets

EUR'000

	Group					Parent Company				
	Usage rights and licences	Greenhouse gas emission allowances	Software	Assets under development	TOTAL	Usage rights and licences	Greenhouse gas emission allowances	Software	Assets under development	TOTAL
<b>As of 31 December 2016</b>										
Cost	2,507	–	45,631	1,512	<b>49,650</b>	10,796	–	43,912	567	<b>55,275</b>
Accumulated amortisation	(2,070)	–	(33,046)	–	<b>(35,116)</b>	(3,835)	–	(32,671)	–	<b>(36,506)</b>
<b>Net book amount</b>	<b>437</b>	<b>–</b>	<b>12,585</b>	<b>1,512</b>	<b>14,534</b>	<b>6,961</b>	<b>–</b>	<b>11,241</b>	<b>567</b>	<b>18,769</b>
<b>Year ended 31 December 2017</b>										
Additions	–	–	468	2,120	<b>2,588</b>	–	–	468	2,063	<b>2,531</b>
Transfers	–	–	3,536	(3,536)	<b>–</b>	–	–	2,589	(2,589)	<b>–</b>
Disposals	(212)	–	–	–	<b>(212)</b>	(656)	–	–	–	<b>(656)</b>
Amortisation charge	–	–	(3,497)	–	<b>(3,497)</b>	–	–	(3,183)	–	<b>(3,183)</b>
<b>Closing net book amount</b>	<b>225</b>	<b>–</b>	<b>13,092</b>	<b>96</b>	<b>13,413</b>	<b>6,305</b>	<b>–</b>	<b>11,115</b>	<b>41</b>	<b>17,461</b>
<b>As of 31 December 2017</b>										
Cost	225	–	49,635	96	<b>49,956</b>	6,305	–	46,969	41	<b>53,315</b>
Accumulated amortisation	–	–	(36,543)	–	<b>(36,543)</b>	–	–	(35,854)	–	<b>(35,854)</b>
<b>Net book amount</b>	<b>225</b>	<b>–</b>	<b>13,092</b>	<b>96</b>	<b>13,413</b>	<b>6,305</b>	<b>–</b>	<b>11,115</b>	<b>41</b>	<b>17,461</b>
<b>Year ended 31 December 2018</b>										
Additions	–	17,789	2,641	88	<b>20,518</b>	–	17,789	2,439	124	<b>20,352</b>
Transfers	(80)	–	–	–	<b>(80)</b>	(525)	–	(26)	–	<b>(551)</b>
Disposals	–	(11,066)	–	–	<b>(11,066)</b>	–	(11,066)	–	–	<b>(11,066)</b>
Amortisation charge	–	–	(3,706)	–	<b>(3,706)</b>	–	–	(3,383)	–	<b>(3,383)</b>
<b>Closing net book amount</b>	<b>145</b>	<b>6,723</b>	<b>12,027</b>	<b>184</b>	<b>19,079</b>	<b>5,780</b>	<b>6,723</b>	<b>10,145</b>	<b>165</b>	<b>22,813</b>
<b>As of 31 December 2018</b>										
Cost	145	6,723	48,135	184	<b>55,187</b>	5,780	6,723	45,242	165	<b>57,910</b>
Accumulated amortisation	–	–	(36,108)	–	<b>(36,108)</b>	–	–	(35,097)	–	<b>(35,097)</b>
<b>Net book amount</b>	<b>145</b>	<b>6,723</b>	<b>12,027</b>	<b>184</b>	<b>19,079</b>	<b>5,780</b>	<b>6,723</b>	<b>10,145</b>	<b>165</b>	<b>22,813</b>

### b) Greenhouse gas emission allowances:

	Group		Parent Company	
	2018	2017	2018	2017
	Number of allowances	Number of allowances	Number of allowances	Number of allowances
<b>At the beginning of the year</b>	206,631	795,153	(13,778)	546,409
Allowances allocated free of charge	265,465	314,160	250,091	295,942
Purchased allowances	1,425,000	–	1,425,000	–
Used allowances	(802,286)	(871,982)	(782,746)	(855,429)
Sold allowances	(72,000)	(30,700)	–	(700)
<b>At the end of the year</b>	<b>1,022,810</b>	<b>206,631</b>	<b>878,567</b>	<b>(13,778)</b>

The number of allowances in the Group received in 2018 from the Government free of charge, in accordance with the law "On Pollution" and Directives of the Ministry of Environmental Protection and Regional Development of the Republic of Latvia, was 265,465 (2017: 314,160), the number of allowances Latvenergo AS received in 2018 from the Government free of charge was 250,091 (2017: 295,942). Therefore, their carrying amount as of 31 December 2018 was nil (31/12/2017: nil). Received European Union Allowances (EUA) must be used until the end of 2020.

## 14. PROPERTY, PLANT AND EQUIPMENT

### a) Property, plant and equipment

Net book amounts and movements of property, plant and equipment by groups, including groups of revalued categories (see Note 2.8.) are as follows:

EUR'000

	Group								Parent Company					
	Land, buildings and facilities	Assets of Hydro Power Plant	Distribution system electrical lines and electrical equipment	Transmission system electrical lines and electrical equipment	Technology equipment and machinery	Other PPE	Assets under construction and advance payments	Property, plant and equipment TOTAL	Land, buildings and facilities	Assets of Hydro Power Plant	Technology equipment and machinery	Other PPE	Assets under construction and advance payments	Property, plant and equipment TOTAL
<b>As of 31 December 2016</b>														
Cost or valuation	464,503	1,855,929	2,826,157	932,444	625,712	156,039	153,890	<b>7,014,674</b>	318,262	1,855,929	600,721	135,062	119,350	<b>3,029,324</b>
Accumulated depreciation and impairment	(137,778)	(1,146,091)	(1,357,781)	(534,495)	(370,284)	(106,458)	(5,990)	<b>(3,658,877)</b>	(91,253)	(1,146,091)	(362,168)	(101,436)	(5,858)	<b>(1,706,806)</b>
<b>Net book amount</b>	<b>326,725</b>	<b>709,838</b>	<b>1,468,376</b>	<b>397,949</b>	<b>255,428</b>	<b>49,581</b>	<b>147,900</b>	<b>3,355,797</b>	<b>227,009</b>	<b>709,838</b>	<b>238,553</b>	<b>33,626</b>	<b>113,492</b>	<b>1,322,518</b>
<b>Year ended 31 December 2017</b>														
Increase due PPE revaluation recognised in OCI (Note 20 a)	–	22,167	–	–	–	–	–	<b>22,167</b>	–	22,167	–	–	–	<b>22,167</b>
Decrease due PPE revaluation recognised in profit or loss	–	(2,260)	–	–	–	–	–	<b>(2,260)</b>	–	(2,260)	–	–	–	<b>(2,260)</b>
Additions	–	–	–	–	–	–	241,220	<b>241,220</b>	–	–	–	–	84,373	<b>84,373</b>
Transfers	18,797	18,855	81,113	11,400	20,717	15,147	(166,029)	–	15,513	18,855	20,679	9,624	(64,671)	–
Reclassified to investment property	(1,182)	–	–	–	–	–	–	<b>(1,182)</b>	(1,059)	–	–	–	–	<b>(1,059)</b>
Reclassified from investment property	–	–	–	–	–	–	–	–	8,335	–	–	–	–	<b>8,335</b>
Disposals	(82)	–	(4,000)	(355)	(108)	(21)	(334)	<b>(4,900)</b>	(45)	–	(73)	(33)	(334)	<b>(485)</b>
Impairment charge	(261)	–	–	–	(116,799)	–	814	<b>(116,246)</b>	(261)	–	(116,799)	–	803	<b>(116,257)</b>
Depreciation	(13,807)	(25,991)	(66,979)	(23,055)	(40,471)	(15,308)	–	<b>(185,611)</b>	(9,653)	(25,991)	(38,971)	(11,263)	–	<b>(85,878)</b>
<b>Closing net book amount as of 31 December 2017</b>	<b>330,190</b>	<b>722,609</b>	<b>1,478,510</b>	<b>385,939</b>	<b>118,767</b>	<b>49,399</b>	<b>223,571</b>	<b>3,308,985</b>	<b>239,839</b>	<b>722,609</b>	<b>103,389</b>	<b>31,954</b>	<b>133,663</b>	<b>1,231,454</b>
<b>As of 31 December 2017</b>														
Cost or valuation	479,605	2,014,626	2,857,242	926,403	640,568	161,992	228,748	<b>7,309,184</b>	345,246	2,014,626	615,648	135,708	138,718	<b>3,249,946</b>
Accumulated depreciation and impairment	(149,415)	(1,292,017)	(1,378,732)	(540,464)	(521,801)	(112,593)	(5,177)	<b>(4,000,199)</b>	(105,407)	(1,292,017)	(512,259)	(103,754)	(5,055)	<b>(2,018,492)</b>
<b>Net book amount</b>	<b>330,190</b>	<b>722,609</b>	<b>1,478,510</b>	<b>385,939</b>	<b>118,767</b>	<b>49,399</b>	<b>223,571</b>	<b>3,308,985</b>	<b>239,839</b>	<b>722,609</b>	<b>103,389</b>	<b>31,954</b>	<b>133,663</b>	<b>1,231,454</b>
<b>Year ended 31 December 2018</b>														
Additions	–	–	–	–	–	–	217,389	<b>217,389</b>	–	–	–	–	38,300	<b>38,300</b>
Invested in share capital (Note 19)*	469	–	20	–	–	–	–	<b>489</b>	469	–	20	–	–	<b>489</b>
Transfers	8,615	90,796	89,681	33,687	1,143	14,368	(238,290)	–	8,075	90,796	1,133	6,570	(106,574)	–
Reclassified to investment property	(44)	–	–	–	–	–	–	<b>(44)</b>	(2,374)	–	–	–	–	<b>(2,374)</b>
Disposals	(931)	(36)	(4,904)	(841)	(709)	(90)	(101)	<b>(7,612)</b>	(2,158)	(36)	(1,279)	(10,442)	(95)	<b>(14,010)</b>
Impairment charge	146	–	–	–	(33,400)	–	(187)	<b>(33,441)</b>	146	–	(33,400)	–	–	<b>(33,254)</b>
Depreciation	(15,959)	(24,859)	(65,638)	(24,615)	(42,807)	(14,795)	–	<b>(188,673)</b>	(10,231)	(24,859)	(41,336)	(10,293)	–	<b>(86,719)</b>
<b>Closing net book amount as of 31 December 2018</b>	<b>322,486</b>	<b>788,510</b>	<b>1,497,669</b>	<b>394,170</b>	<b>42,994</b>	<b>48,882</b>	<b>202,382</b>	<b>3,297,093</b>	<b>233,766</b>	<b>788,510</b>	<b>28,527</b>	<b>17,789</b>	<b>65,294</b>	<b>1,133,886</b>
<b>As of 31 December 2018</b>														
Cost or valuation	485,098	2,055,572	2,889,265	933,079	637,706	147,744	207,746	<b>7,356,210</b>	349,581	2,055,572	612,253	103,877	70,349	<b>3,191,632</b>
Accumulated depreciation and impairment	(162,612)	(1,267,062)	(1,391,596)	(538,909)	(594,712)	(98,862)	(5,364)	<b>(4,059,117)</b>	(115,815)	(1,267,062)	(583,726)	(86,088)	(5,055)	<b>(2,057,746)</b>
<b>Net book amount</b>	<b>322,486</b>	<b>788,510</b>	<b>1,497,669</b>	<b>394,170</b>	<b>42,994</b>	<b>48,882</b>	<b>202,382</b>	<b>3,297,093</b>	<b>233,766</b>	<b>788,510</b>	<b>28,527</b>	<b>17,789</b>	<b>65,294</b>	<b>1,133,886</b>

\* In June 2018, in accordance with the Directive No. 765 of the Cabinet of Ministers of the Republic of Latvia, dated 19 December 2017 – “On the Investment of the State's property units in the Share Capital of Latvenergo AS”, real estate in the amount of EUR 489 thousand was invested in the share capital of Latvenergo AS



Impairment charge is included in the Statement of Profit or Loss under 'Depreciation, amortisation and impairment of intangible assets and property, plant and equipment'.

As of 31 December 2018 cost of fully depreciated PPE which are still in use for the Group amounted to EUR 312,028 thousand (31/12/2017: EUR 237,692 thousand) and for the Parent Company amounted to EUR 241,396 thousand (31/12/2017: EUR 194,531 thousand).

In 2018 the Group and the Parent Company have capitalised borrowing costs in the amount of EUR 889 thousand (2017: EUR 1,359 thousand) (see Note 11 b). Rate of capitalised borrowing costs was of 0.93% (2017: 1.23%).

Information about the pledged property, plant and equipment is disclosed in Note 22 I.

## b) Investment property

The Group and the Parent Company apply the cost model in valuation of investment properties. Land or a building or part of a building held by the Group or the Parent Company as the owner to earn rentals or for capital appreciation, rather than for use in the production of goods or supply of services or for administrative purposes, or sale in the ordinary course of business, after decision of the Group's or the Parent Company's management are initially recognised as investment properties at cost and subsequently measured at acquisition cost net of accumulated depreciation and impairment losses (Note 2.7.).

EUR'000

	Group		Parent Company				TOTAL Investment property	
	Investment property held for capital appreciation		Investment properties for lease	Investment property held for capital appreciation				
	2018	2017	2018	2017	2018	2017	2018	2017
Cost at the beginning of the year	2,297	855	96,174	104,272	2,244	782	98,418	105,054
Accumulated depreciation and impairment at the beginning of the year	(1,544)	(292)	(32,067)	(31,937)	(1,544)	(284)	(33,611)	(32,221)
<b>Net book amount at the beginning of the year</b>	<b>753</b>	<b>563</b>	<b>64,107</b>	<b>72,335</b>	<b>700</b>	<b>498</b>	<b>64,807</b>	<b>72,833</b>
Reclassified to investment property held for capital appreciation	44	–	(13)	(125)	44	125	31	–
Reclassified from property, plant and equipment to investment property	–	1,183	3,734	2,373	–	1,060	3,734	3,433
Reclassified to property, plant and equipment	–	–	(1,360)	(8,334)	–	–	(1,360)	(8,334)
Disposal	–	(2)	(1,259)	(34)	–	(2)	(1,259)	(36)
Sold	(341)	(284)	(78)	–	(322)	(275)	(400)	(275)
Impairment charge	17	(685)	–	–	17	(685)	17	(685)
Depreciation	(6)	(22)	(3,768)	(2,108)	(6)	(21)	(3,774)	(2,129)
Cost at the end of the year	1,638	2,297	94,626	96,174	1,604	2,244	96,230	98,418
Accumulated depreciation and impairment at the end of the year	(1,171)	(1,544)	(33,263)	(32,067)	(1,171)	(1,544)	(34,434)	(33,611)
<b>Net book amount at the end of the year</b>	<b>467</b>	<b>753</b>	<b>61,363</b>	<b>64,107</b>	<b>433</b>	<b>700</b>	<b>61,796</b>	<b>64,807</b>

### c) Property, plant and equipment revaluation

Assets of Hydropower plants were revalued in 2017. The revaluation was performed by an independent, external and certified valuer by applying the income method or the replacement cost model. Income method is based on average perennial water inflow in each HPP, power exchange (Nordpool spot) forecasts of electricity prices, analysis of historical generation and operating expenses, forecast of expenses based on public available state statistics, forecast of capital expenditure, forecast of net cash flows, as well as discount and capitalisation rate calculation using the weighted average cost of capital (WACC) formula based on market data.

Considering that the estimated replacement cost of the assets exceeded the value determined by using income method, the value of each of the hydropower plant assets item was reduced to recognise the economic depreciation. The replacement cost was determined according to technical characteristics of property, plant and equipment, current technical requirements and the cost of replacement of functional analogue less physical, functional and economic depreciation.

As a result of revaluation in 2017 the carrying amounts of property, plant and equipment of hydropower plants increased by EUR 19,907 thousand. Increase of property, plant and equipment in the amount of EUR 22,167 thousand, less deferred income tax, is included in the equity as non-current assets revaluation reserve (see Note 20 a), while impairment charge due to property, plant and equipment revaluation in the amount of EUR 2,260 thousand – in the Statement of Profit or Loss position 'Depreciation, amortisation and impairment of intangible assets and property, plant and equipment'.

The nominal pre-tax discount rate used in valuation is 7.5%. If the pre-tax rate would be increased by 0.1% then the value of the revalued assets of hydropower plants would decrease by EUR 17 283 thousand. If the pre-tax rate would be decreased by 0.1%, the value of the revalued assets of hydropower plants would increase by EUR 17,945 thousand. If electricity price would increase by 1%, the value of assets would increase by EUR 18,467, if the prices would be by 1% less, the value of assets would decrease by EUR 18,462.

Distribution system electrical lines and electrical equipment was revalued in 2016. The revaluation was performed by an external valuer valuating the replacement or renewing costs for each item of property, plant and equipment considering actual costs of construction or purchase of analogue or similar property, plant and equipment shortly before the revaluation as based on the Sadales tīkls AS accounting. Estimated replacement or renewal value for each item of property, plant and equipment was reduced by its functional and physical depreciation as assessed by external valuer.

Transmission system electrical lines and electrical equipment was revalued in 2016. The revaluation was performed by an external valuer valuating the replacement or renewing costs for each item of property, plant and equipment considering actual costs of construction or purchase of analogue or similar property, plant and equipment shortly before the revaluation as based on Latvijas elektriskie tīkli AS accounting. For property, plant and equipment invested as a property investment in Latvijas elektriskie tīkli AS share capital in 2011 external valuer at the moment of the revaluation evaluated how have changed the components of the replacement or renewal costs of the same property, plant and equipment items since they were invested in the Latvijas elektriskie tīkli AS share capital, adjusting the values of individual sub-categories of property, plant and equipment with changes of material costs and indexing the wage component on the basis of publicly available national statistics on wage increases over the relevant period. Estimated replacement or renewal value for each item of property, plant and equipment was reduced by its functional and physical depreciation as assessed by external valuer.

The management has evaluated changes in the input data used in valuation since revaluation and has estimated that their changes do not have a significant impact on the value of revalued property, plant and equipment groups.

The carrying amounts of revalued categories of property, plant and equipment groups (see Note 2.8.) at revalued amounts and their cost basis are as follows: EUR'000

	Group		Parent Company	
	Revalued property, plant and equipment groups		Transmission system electrical lines and electrical equipment	TOTAL revalued PPE
	Assets of Hydropower plants (the Parent Company)	Distribution system electrical lines and electrical equipment		
<b>At revalued amounts</b>				
<b>As of 31 December 2018</b>				
Revalued	2,055,572	2,889,265	933,079	5,877,916
Accumulated depreciation	(1,267,062)	(1,391,596)	(538,909)	(3,197,567)
<b>Revalued net book amount</b>	<b>788,510</b>	<b>1,497,669</b>	<b>394,170</b>	<b>2,680,349</b>
<b>As of 31 December 2017</b>				
Revalued	2,014,626	2,857,242	926,403	5,798,271
Accumulated depreciation	(1,292,017)	(1,378,732)	(540,464)	(3,211,213)
<b>Revalued net book amount</b>	<b>722,609</b>	<b>1,478,510</b>	<b>385,939</b>	<b>2,587,058</b>
<b>At amounts stated on historical cost basis</b>				
<b>As of 31 December 2018</b>				
Cost	396,519	1,377,374	446,760	2,220,653
Accumulated depreciation	(171,043)	(458,211)	(168,374)	(797,628)
<b>Net book amount</b>	<b>225,476</b>	<b>919,163</b>	<b>278,386</b>	<b>1,423,025</b>
<b>As of 31 December 2017</b>				
Cost	311,854	1,289,349	418,917	2,020,120
Accumulated depreciation	(170,115)	(371,348)	(161,275)	(702,738)
<b>Net book amount</b>	<b>141,739</b>	<b>918,001</b>	<b>257,642</b>	<b>1,317,382</b>

#### **d) Impairment**

##### **I) Latvenergo AS combined heat and power plants (Latvenergo AS CHPPs)**

Impairment review performed for Latvenergo AS CHPPs is based on value in use calculations. The cash-generating unit is defined as the assets of Latvenergo AS CHPPs.

In October 2017, Latvenergo AS applied for a one-off compensation from the state, at the same time opting out of the receipt of 75% of the annual electrical capacity payments for cogeneration power plants CHPP-1 and CHPP-2 (Note 4 i). On 21 November 2017, the Cabinet of Ministers of the Republic of Latvia accepted an order which supports the reduction of the guaranteed support payments during the remaining support period for the installed capacity of Latvenergo CHPPs. According to the order, Latvenergo AS obtained a government grant in the amount of EUR 454,413 thousand that was divided into two parts, with the stipulation that EUR 140,000 thousand should be recognised in the Group's and Parent Company's statement of profit or loss in 2017, while EUR 314,413 thousand should be recognised as deferred income in even distribution over the coming reporting periods and fulfilling obligations until the end of the support period.

On 26 September 2018, the Cabinet of Ministers decided to change conditions for a part of the grant in the amount of EUR 51,700 thousand stipulating it as unconditional, by reducing the remaining part of the grant proportionally to this amount until the end of the support period. As a result of this and the previous order, EUR 81 004 thousand were recognised as 'Other income' in the Group's and Parent Company's statement of profit or loss in 2018. Consequently, EUR 233,409 thousand remained recognised as deferred income as of 31 December 2018.

Taking into account the assessment that the future cash flows generated by the operation of Latvenergo AS CHPPs are approximately equal to nil (see below), the value of Latvenergo CHPPs assets is estimated equal to the deferred income as of 31 December 2018 – EUR 233,409 thousand.

As a result of the above transactions, additional impairment in the amount of EUR 33,400 thousand was recognised for Latvenergo AS CHPPs in 2018 (2017: EUR 116,799 thousand). The recognised impairment charge is included in the Statement of Profit or Loss position 'Depreciation, amortisation and impairment of intangible assets and property, plant and equipment'.

In addition to the above, to ensure the carrying value is in line with recognised impairment, the future cash flows expected to be derived from the operation of Latvenergo AS CHPPs were evaluated. Forecasted period is 2019 – 2028 and the terminal value appraisal, evaluated as a fraction of the balance sheet's assets value, is included. Revenue stream forecast mainly corresponds to the remaining intensity of electrical capacity payments and the support period till September 23, 2028, as it is set out in regulations by Cabinet of Ministers of the Republic of Latvia No. 221, dated 10 March 2009. The forecast of expenses is based on historical data, the budget approved by the management for 2019, the service maintenance agreements and assumed inflation. As a result of calculation, the future revenue stream is close to the amount of expenses – the future cash flows generated by Latvenergo AS CHPPs are approximately equal to nil. Nominal pre-tax discount rate used to determine value in use of cash-generating unit by discounting cash flows is 7.5% (2017: 7.5%). The calculation is not discount rate sensitive. If the annual electrical capacity payments for cogeneration power plants CHPP-1 and CHPP-2 would be discontinued, then impairment of approximately EUR 80 million would be recognised. Impairment is estimated by assuming that capacity payment revenue decrease would be partly offset by a higher revenues from electricity production.

The accumulated impairment as of 31 December 2018 amounted to EUR 254,109 thousand (31/12/2017: EUR 220,709 thousand).

##### **II) Distribution system assets (Group)**

Impairment review based on value in use calculations is performed for electricity distribution system assets and is performed to ensure that no additional economic depreciation has to be recognised. As a result of impairment test there is no impairment loss to be recognised (2017: nil). The cash-generating unit is defined as all distribution system assets. In 2018 nominal pre-tax discount rate used to determine value in use of cash-generating units by discounting cash flows is 4.2% (2017: 5.3%) as included in the electricity distribution system service tariff calculation methodology. Revenue stream forecasts are based on the tariff calculation methodology and assumptions related investment plans. The forecast of expenses and investments is based on historical data, the budgets approved by the management and assumed inflation. The growth rate used for the terminal value appraisal is in line with the assumed distributed electricity growth.

##### **III) Transmission system assets (Group)**

Impairment review based on value in use calculations is performed for electricity transmission system assets and is performed to ensure that no additional economic depreciation has to be recognised. As a result of impairment test there is no impairment loss to be recognised (2017: nil). The cash-generating unit is defined as all transmission system assets. In 2018 nominal pre-tax discount rate used to determine value in use of cash-generating units by discounting cash flows is 4.2% (2017: 5.3%) as included in electricity transmission system service tariff calculation methodology. Revenue stream forecasts are based on the tariff calculation methodology and assumptions related investment plans. The forecast of expenses and investments is based on historical data, the budgets approved by the management and assumed inflation. The growth rate used for the terminal value appraisal is in line with the assumed transmitted electricity growth.

##### **IV) Daugava hydropower plants (HPPs)**

Impairment review based on value in use calculations is performed for Daugava HPPs at the end of reporting period assets and is performed to ensure that no additional economic depreciation has to be recognised. No impairment loss has to be recognised in addition to impairment already recognised as part of HPPs revaluation (Note 14 c). The cash-generating unit is defined as Daugava HPPs assets. In 2018 nominal pre-tax discount rate used to determine value in use of cash-generating units by discounting cash flows is 7.5% (2017: 9.0%). Revenue stream forecasts are based on the most recent long-term forecasts of electricity prices and long-term output of electricity. The forecast of expenses and investments is based on historical data, the budget approved by the management for 2019 and assumed inflation. The growth rate used for the terminal value appraisal is in line with the assumed inflation.

## e) Leases

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>Rental income (the Group or the Parent Company is the lessor) (Note 6)</b>	<b>40,267</b>	<b>45,779</b>	<b>15,987</b>	<b>15,922</b>
of which, Transmission system assets lease	38,699	43,911	–	–
<b>Rental expense (the Group or the Parent Company is the lessee)</b>	<b>1,248</b>	<b>1,577</b>	<b>1,149</b>	<b>1,267</b>

### Future minimum lease payments receivable under operating lease contracts by due dates (the Group and the Parent Company are the lessor):

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
– < 1 year	38,579	39,781	7,673	15,355
– 1–5 years	158,650	193,775	48,424	40,167
– > 5 years	41,325	3,220	2,793	3,220
<b>TOTAL rental income</b>	<b>238,554</b>	<b>236,776</b>	<b>58,890</b>	<b>58,742</b>

Transmission system assets had been leased out by the Group to Augstsprieguma tīkls AS under non-cancellable operating lease agreement.

### Future minimum lease payments under operating lease contracts by due dates (the Group and the Parent Company are the lessee):

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
– < 1 year	1,447	1,350	1,509	1,566
– 1–5 years	3,804	3,919	5,909	6,252
– > 5 years	4,280	6,497	14,320	10,299
<b>TOTAL rental expense</b>	<b>9,531</b>	<b>11,766</b>	<b>21,738</b>	<b>18,117</b>

## 15. NON-CURRENT FINANCIAL INVESTMENTS

### The Parent Company's participating interest in subsidiaries and other non-current financial investments:

Name	Country of incorporation	Business activity held	31/12/2018		31/12/2017	
			Interest held, %	EUR'000	Interest held, %	EUR'000
Subsidiaries:						
Latvijas elektriskie tīkli AS	Latvia	Lease of transmission system assets	100%	185,624	100%	185,624
Sadales tīkls AS	Latvia	Electricity distribution	100%	641,150	100%	627,656
Enerģijas publiskais tirgotājs AS*	Latvia	Administration of mandatory electricity procurement process	100%	40	100%	40
Elektrum Eesti OÜ	Estonia	Electricity and natural gas trade	100%	35	100%	35
Elektrum Lietuva, UAB	Lithuania	Electricity and natural gas trade	100%	98	100%	98
Liepājas enerģija SIA	Latvia	Thermal energy generation and trade in Liepāja, electricity generation	51%	3,556	51%	3,556
Other non-current financial investments:						
Pirmais Slēgtais Pensiju Fonds AS	Latvia	Management of pension plans	46.30%	36	46.30%	36
Rīgas siltums AS	Latvia	Thermal energy generation and trade in Rīga, electricity generation	0.0051%	3	0.0051%	3
TOTAL financial investments of the Parent Company				830,542		817,048

### The Group's non-current financial investments:

Name	Country of incorporation	Business activity held	31/12/2018		31/12/2017	
			Interest held, %	EUR'000	Interest held, %	EUR'000
Other non-current financial investments (Group):						
Pirmais Slēgtais Pensiju Fonds AS	Latvia	Management of pension plans	48.15%	37	48.15%	37
Rīgas siltums AS	Latvia	Thermal energy generation and trade in Riga, electricity generation	0.0051%	3	0.0051%	3
TOTAL financial investments of the Group				40		40

The Group owns 48.15% of the shares of the closed pension fund Pirmais Slēgtais Pensiju Fonds AS (Latvenergo AS – 46.30%). However, the Group and the Parent Company are only a nominal shareholder as all risks and benefits arising from associate's activities will accrue to the employees who are members of the pension fund.

**Movement in non-current investments:**

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>40</b>	<b>40</b>	<b>817,048</b>	<b>817,048</b>
Invested in share capital*	–	–	13,494	–
<b>At the end of the year</b>	<b>40</b>	<b>40</b>	<b>830,542</b>	<b>817,048</b>

\* In 2018, the Parent Company invested property, plant and equipment in the share capital of Sadales tīkls AS. In the Statement of Financial Position of the Parent Company investment is recognised at cost of disposed PPE in the amount of EUR 13,494 thousand, while share capital of Sadales tīkls AS increased by fair value of invested property, plant and equipment in the amount of EUR 19,143 thousand

**Summarised financial information for subsidiaries:**

EUR'000

Subsidiaries	Equity		Net profit for the year		Dividends from subsidiaries*		Carrying amount of interest from investment	
	31/12/2018	31/12/2017	2018	2017	2018	2017	31/12/2018	31/12/2017
Latvijas elektriskie tīkli AS	232,759	269,801	13,394	50,463	50,463	6,852	185,624	185,624
Sadales tīkls AS	922,421	993,329	33,743	124,268	124,268	3	641,150	627,656
Enerģijas publiskais tirgotājs AS	40	40	–	–	–	–	40	40
Elektrum Eesti OÜ	922	904	250	232	232	264	35	35
Elektrum Lietuva, UAB	925	859	548	481	481	542	98	98
Liepājas enerģija SIA	17,262	16,413	5,167	4,799	2,202	1,450	3,556	3,556
	<b>1,174,329</b>	<b>1,281,346</b>	<b>53,102</b>	<b>180,243</b>	<b>177,646</b>	<b>9,111</b>	<b>830,503</b>	<b>817,009</b>

\* In 2018 dividends from subsidiaries received in cash in the amount of EUR 53,378 thousand and with non-cash offset in the amount of EUR 124,268 thousand (2017: EUR 9,111 thousand received in cash)

## 16. INVENTORIES

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Raw materials and materials	14,865	16,547	1,286	1,583
Natural gas	49,757	53,079	49,757	53,078
Other inventories	8,292	8,115	8,070	8,075
Prepayments for inventories	198	81	33	80
Allowance for raw materials and other inventories	(1,137)	(1,494)	(736)	(992)
<b>TOTAL inventories</b>	<b>71,975</b>	<b>76,328</b>	<b>58,410</b>	<b>61,824</b>

Changes in the allowance for raw materials and materials at warehouses are included in the Statement of Profit or Loss position 'Raw materials and consumables used'.

**Movement on the allowance for inventories:**

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>1,494</b>	<b>1,659</b>	<b>992</b>	<b>1,060</b>
Inventories written off	(287)	(62)	(260)	–
Charged to the Statement of Profit or Loss	(70)	(103)	4	(68)
<b>At the end of the year</b>	<b>1,137</b>	<b>1,494</b>	<b>736</b>	<b>992</b>



## 17. RECEIVABLES FROM CONTRACTS WITH CUSTOMERS AND OTHER RECEIVABLES

Receivables from contracts with customers grouped by the expected credit loss (ECL) assessment model, net:

EUR'000

	Group			Parent Company		
	31/12/2018	01/01/2018	31/12/2017*	31/12/2018	01/01/2018	31/12/2017*
Individually assessed significant receivables (counterparty model)	7,051	4,383	4,389	7,915	12,486	12,497
Receivables with lifetime ECL assessment by simplified approach (portfolio model)	110,904	100,864	100,980	73,110	70,198	70,302
<b>TOTAL receivables from contracts with customers</b>	<b>117,955</b>	<b>105,247</b>	<b>105,369</b>	<b>81,025</b>	<b>82,684</b>	<b>82,799</b>

\* By IAS 39

a) Receivables from contracts with customers, net

EUR'000

	Group			Parent Company		
	31/12/2018	01/01/2018	31/12/2017*	31/12/2018	01/01/2018	31/12/2017*
<b>Receivables from contracts with customers:</b>						
– Electricity, natural gas trade and related services customers	138,308	134,699	134,699	102,154	105,257	105,257
– Heating customers	14,715	10,922	10,922	11,955	8,851	8,851
– Other receivables from contracts with customers (portfolio model)	5,675	4,221	4,221	3,331	1,062	1,062
– Other receivables from contracts with customers (counterparty model)	7,060	4,389	4,389	3,203	3,093	3,093
– Subsidiaries	–	–	–	4,719	9,404	9,404
	<b>165,758</b>	<b>154,231</b>	<b>154,231</b>	<b>125,362</b>	<b>127,667</b>	<b>127,667</b>
<b>Provisions for impaired receivables from contracts with customers:</b>						
– Electricity, natural gas trade and related services customers	(44,953)	(45,785)	(45,561)	(43,968)	(44,559)	(44,472)
– Heating customers	(342)	(351)	(329)	(334)	(331)	(310)
– Other receivables from contracts with customers (portfolio model)	(2,499)	(2,842)	(2,972)	(28)	(82)	(86)
– Other receivables from contracts with customers (counterparty model)	(9)	(6)	–	(4)	(4)	–
– Subsidiaries	–	–	–	(3)	(7)	–
	<b>(47,803)</b>	<b>(48,984)</b>	<b>(48,862)</b>	<b>(44,337)</b>	<b>(44,983)</b>	<b>(44,868)</b>
<b>Receivables from contracts with customers, net:</b>						
– Electricity, natural gas trade and related services customers	93,355	88,914	89,138	58,186	60,698	60,785
– Heating customers	14,373	10,571	10,593	11,621	8,520	8,541
– Other receivables from contracts with customers (portfolio model)	3,176	1,379	1,249	3,303	980	976
– Other receivables from contracts with customers (counterparty model)	7,051	4,383	4,389	3,199	3,089	3,093
– Subsidiaries	–	–	–	4,716	9,397	9,404
	<b>117,955</b>	<b>105,247</b>	<b>105,369</b>	<b>81,025</b>	<b>82,684</b>	<b>82,799</b>

\* By IAS 39

**Receivables from contracts with customers with lifetime expected credit losses (ECL) assessed on the portfolio model basis and grouped by past due days:**

EUR'000

Late payment delay in days by IFRS 9	ECL rate	Group						Parent Company					
		31/12/2018			01/01/2018			31/12/2018			01/01/2018		
		Receivables	Impairment loss	TOTAL	Receivables	Impairment loss	TOTAL	Receivables	Impairment loss	TOTAL	Receivables	Impairment loss	TOTAL
On time	0.20%	106,194	(230)	<b>105,964</b>	91,644	(183)	<b>91,461</b>	69,557	(160)	<b>69,397</b>	65,637	(156)	<b>65,481</b>
Less 30 days	3%	2,953	(88)	<b>2,865</b>	6,552	(197)	<b>6,355</b>	1,947	(59)	<b>1,888</b>	2,175	(68)	<b>2,107</b>
Past due 30 - 59 days	20%	1,334	(265)	<b>1,069</b>	1,768	(353)	<b>1,415</b>	1,213	(241)	<b>972</b>	1,573	(315)	<b>1,258</b>
Past due 60 - 89 days	50%	535	(267)	<b>268</b>	879	(440)	<b>439</b>	503	(251)	<b>252</b>	757	(380)	<b>377</b>
Past due 90 - 179 days	60%	812	(486)	<b>326</b>	1,506	(904)	<b>602</b>	697	(417)	<b>280</b>	1,236	(742)	<b>494</b>
Past due 180 - 359 days	75%	1,638	(1,226)	<b>412</b>	2,361	(1,769)	<b>592</b>	1,283	(962)	<b>321</b>	1,896	(1,422)	<b>474</b>
Past due more than 360 days	100%	17,890	(17,890)	<b>-</b>	18,261	(18,261)	<b>-</b>	15,123	(15,123)	<b>-</b>	15,279	(15,279)	<b>-</b>
Insolvent debtors*	100%	27,342	(27,342)	<b>-</b>	26,871	(26,871)	<b>-</b>	27,117	(27,117)	<b>-</b>	26,617	(26,617)	<b>-</b>
		<b>158,698</b>	<b>(47,794)</b>	<b>110,904</b>	<b>149,842</b>	<b>(48,978)</b>	<b>100,864</b>	<b>117,440</b>	<b>(44,330)</b>	<b>73,110</b>	<b>115,170</b>	<b>(44,979)</b>	<b>70,191</b>

\* Receivables under insolvency process and with an established payment schedule

The expected loss rates are based on the payment profiles of sales over a period of 2 years before 1 January 2018 and the corresponding historical credit losses experienced within this period. As of 31 December 2018 assessment of expected credit losses is based on the same ECL rates.

**Receivables from contracts with customers by IAS 39 grouped by past due days:**

EUR'000

Late payment delay in days by IAS 39:	ECL rate	Group			Parent Company		
		31/12/2017			31/12/2017		
		Receivables	Impairment loss	TOTAL	Receivables	Impairment loss	TOTAL
<b>Electricity, natural gas trade and related services receivables:</b>							
Fully performing receivables	0%	70,290	–	<b>70,290</b>	46,956	–	<b>46,956</b>
Past due 1 - 45 days	0%	7,183	–	<b>7,183</b>	3,134	–	<b>3,134</b>
Past due 46 - 90 days	50%	743	(371)	<b>372</b>	657	(329)	<b>328</b>
Past due 91 - 180 days	75%	1,173	(880)	<b>293</b>	1,110	(833)	<b>277</b>
Past due more than 181 days	100%	17,623	(17,623)	<b>–</b>	16,780	(16,780)	<b>–</b>
Individually impaired receivables with scheduled payments*		37,687	(26,687)	<b>11,000</b>	36,620	(26,530)	<b>10,090</b>
<b>TOTAL</b>		<b>134,699</b>	<b>(45,561)</b>	<b>89,138</b>	<b>105,257</b>	<b>(44,472)</b>	<b>60,785</b>
<b>Heating and other receivables from contracts with customers:</b>							
Fully performing receivables	0%	16,029	–	<b>16,029</b>	12,549	–	<b>12,549</b>
Past due 1 - 30 days	0%	143	–	<b>143</b>	55	–	<b>55</b>
Past due 31 - 90 days	50%	118	(59)	<b>59</b>	12	(6)	<b>6</b>
Past due more than 91 days	100%	3,160	(3,160)	<b>–</b>	390	(390)	<b>–</b>
Individually impaired receivables with scheduled payments*		82	(82)	<b>–</b>	–	–	<b>–</b>
<b>TOTAL</b>		<b>19,532</b>	<b>(3,301)</b>	<b>16,231</b>	<b>13,006</b>	<b>(396)</b>	<b>12,610</b>
<b>Receivables from subsidiaries:</b>							
Fully performing receivables	0%	–	–	<b>–</b>	9,404	–	<b>9,404</b>
<b>TOTAL</b>		<b>–</b>	<b>–</b>	<b>–</b>	<b>9,404</b>	<b>–</b>	<b>9,404</b>
<b>TOTAL receivables from contracts with customers</b>		<b>154,231</b>	<b>(48,862)</b>	<b>105,369</b>	<b>127,667</b>	<b>(44,868)</b>	<b>82,799</b>

\* Receivables under insolvency process and other individually impaired receivables

**Receivables from contracts with customers with lifetime expected credit losses (ECL) assessed on the counterparty model basis:** EUR'000

	Group			Parent Company		
	31/12/2018	01/01/2018	31/12/2017*	31/12/2018	01/01/2018	31/12/2017*
Other receivables from contracts with customers	7,060	4,389	4,389	3,203	3,093	3,093
Impairment loss on other receivables from contracts with customers	(9)	(6)	–	(4)	(4)	–
Receivables from subsidiaries (Note 28 b)	–	–	–	4,398	9,390	9,390
Accrued income from subsidiaries (Note 28 c)	–	–	–	321	14	14
Impairment loss on subsidiaries receivables (Note 28 b)	–	–	–	(3)	(7)	–
	<b>7,051</b>	<b>4,383</b>	<b>4,389</b>	<b>7,915</b>	<b>12,486</b>	<b>12,497</b>

\* By IAS 39

Allowances for impairment loss are calculated based on Moody's credit rating agency corporate default and debt recovery rate assigned for credit rating level - Baa2 (stable) (for receivables from related parties) and corporate default and debt recovery rate assigned for energy utilities industry.

**b) Other financial receivables**

	Group			Parent Company		
	31/12/2018	01/01/2017	31/12/2017	31/12/2018	01/01/2017	31/12/2017
Other non-current receivables*	30,960	3,229	3,229	331	284	284
Loss allowances for expected credit loss	(40)	(4)	–	–	–	–
<b>TOTAL non-current receivables</b>	<b>30,920</b>	<b>3,225</b>	<b>3,229</b>	<b>331</b>	<b>284</b>	<b>284</b>
<b>Current financial receivables:</b>						
Receivable of guaranteed fee for the installed electrical capacity of cogeneration power plants CHPP-1 and CHPP-2**	–	454,413	454,413	–	–	–
Unsettled revenue on mandatory procurement PSO fee recognised as assets***	74,497	164,365	164,365	–	–	–
Receivables for lease	7,646	3,535	3,535	49	–	–
Receivables for lease from subsidiaries (Note 28 b)	–	–	–	1,061	1,727	1,727
Other financial receivables from subsidiaries (Note 28 b)	–	–	–	6,745	6,317	6,317
Other accrued income from subsidiaries (Note 28 c)	–	–	–	4,358	5,063	5,063
Other accrued income	872	3,572	3,572	883	872	872
Other current financial receivables	4,146	17,529	17,529	2,930	5,214	5,214
Loss allowances for expected credit loss on subsidiaries receivables (Note 28 b)	–	–	–	(6)	(6)	–
Loss allowances for expected credit loss	(2,548)	(1,746)	(1,582)	(1,787)	(1,248)	(1,255)
<b>TOTAL current financial receivables</b>	<b>84,613</b>	<b>641,668</b>	<b>641,832</b>	<b>14,233</b>	<b>17,939</b>	<b>17,938</b>
<b>TOTAL other financial receivables</b>	<b>115,533</b>	<b>644,893</b>	<b>645,061</b>	<b>14,564</b>	<b>18,223</b>	<b>18,222</b>

\* Other non-current receivables of the Group as of 31 December 2018 include financing for capital expenditure project "Construction of the 330 kV Kurzemes loks" in the amount of EUR 30,617 thousand (31/12/2017: EUR 2,941 thousand)

\*\* On 21 November 2017, the Cabinet of Ministers of the Republic of Latvia accepted an order on one-off compensation to Latvenergo AS on guaranteed support for the installed capacity of cogeneration power plants in the amount of EUR 454,413 thousand (see Note 4 i)

\*\*\* By applying agent principle unsettled revenue on mandatory procurement PSO fee is recognised as assets in net amount as difference between revenue from sale of electricity in Nord Pool power exchange by market price, received mandatory procurement PSO fees, received government grant for compensating the increase of mandatory procurement costs and costs of purchased electricity under the mandatory procurement from electricity generators who generate electricity in efficient cogeneration process or using renewable energy sources, as well as guaranteed fees for installed electrical capacity in cogeneration plants (over 4 MW)

There is no significant concentration of credit risk with respect to receivables from contracts with customers as the Group and the Parent Company have a large number of customers except major heating customer the net debt of which as of 31 December 2018 amounted to EUR 11,626 thousand (31/12/2017: EUR 8,627 thousand).

The Management assumptions and methodology for estimation of impairment for receivables from contracts with customers and evaluation of impairment risk are described in Note 4 b.

**Movements in loss allowances for impaired receivables from contracts with customers:** EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>48,862</b>	<b>48,100</b>	<b>44,868</b>	<b>44,177</b>
Receivables written off during the year as uncollectible	(2,549)	(1,710)	(2,074)	(1,343)
Effect of IFRS 9 'Financial instruments' adoption	122	–	115	–
Allowance for impaired receivables	1,368	2,472	1,428	2,034
<b>At the end of the year</b>	<b>47,803</b>	<b>48,862</b>	<b>44,337</b>	<b>44,868</b>

**Other financial receivables** EUR'000

	Group			Parent Company		
	31/12/2018	01/01/2017	31/12/2017	31/12/2018	01/01/2017	31/12/2017
Other non-current receivables*	30,960	3,229	3,229	331	284	284
Loss allowances for expected credit loss	(40)	(4)	–	–	–	–
<b>TOTAL non-current receivables</b>	<b>30,920</b>	<b>3,225</b>	<b>3,229</b>	<b>331</b>	<b>284</b>	<b>284</b>
<b>Current financial receivables:</b>						
Receivable of guaranteed fee for the installed electrical capacity of cogeneration power plants CHPP-1 and CHPP-2**	–	454,413	454,413	–	–	–
Unsettled revenue on mandatory procurement PSO fee recognised as assets***	74,497	164,365	164,365	–	–	–
Receivables for lease	7,646	3,535	3,535	49	–	–
Receivables for lease from subsidiaries (Note 28 b)	–	–	–	1,061	1,727	1,727
Other financial receivables from subsidiaries (Note 28 b)	–	–	–	6,745	6,317	6,317
Other accrued income from subsidiaries (Note 28 c)	–	–	–	4,358	5,063	5,063
Other accrued income	872	3,572	3,572	883	872	872
Other current financial receivables	4,146	17,529	17,529	2,930	5,214	5,214
Loss allowances for expected credit loss on subsidiaries receivables (Note 28 b)	–	–	–	(6)	(6)	–
Loss allowances for expected credit loss	(2,548)	(1,746)	(1,582)	(1,787)	(1,248)	(1,255)
<b>TOTAL current financial receivables</b>	<b>84,613</b>	<b>641,668</b>	<b>641,832</b>	<b>14,233</b>	<b>17,939</b>	<b>17,938</b>
<b>TOTAL other financial receivables</b>	<b>115,533</b>	<b>644,893</b>	<b>645,061</b>	<b>14,564</b>	<b>18,223</b>	<b>18,222</b>

There is no significant concentration of credit risk with respect to other financial receivables except the transmission system operator – Augstsprieguma tīkls AS the net debt of which to the Group as of 31 December 2018 including receivables from contracts with customer amounted to 42,218 thousand EUR (31/12/2017: 20,014 thousand EUR) (see Note 28 b) and receivable from State of guaranteed fee for the installed electrical capacity of cogeneration power plants and unsettled revenue on mandatory procurement PSO fee recognised as assets. Loss allowance for these financial receivables assessed individually and based on counterparty's model (see Note 4 b).

### c) Other non-financial receivables

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>Current non-financial receivables:</b>				
Pre-tax and overpaid taxes	108	3,703	105	22
Other current receivables	109	1,226	107	119
<b>TOTAL current non-financial receivables</b>	<b>217</b>	<b>4,929</b>	<b>212</b>	<b>141</b>

None of the receivables are secured with pledges or otherwise. The carrying amounts of other receivables are assumed to approximate their fair values.

## 18. CASH AND CASH EQUIVALENTS

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Cash at bank	95,094	233,624	93,193	230,476
Short-term bank deposits	30,000	–	30,000	–
Restricted cash and cash equivalents*	4,361	2,379	4,361	2,379
<b>TOTAL cash and cash equivalents</b>	<b>129,455</b>	<b>236,003</b>	<b>127,554</b>	<b>232,855</b>

\* Restricted cash and cash equivalents as of 31 December 2018 consist of the financial security for participating in NASDAQ OMX Commodities Exchange. Financial security is fully recoverable after termination of participation without any penalties, therefore restricted cash is considered as cash equivalent

In existing rate environment, cash at bank balances practically don't earn any interests. Short-term deposits are placed for different periods between several days and three months depending on the immediate cash needs of the Group and the Parent Company and cash flow forecasts. During 2018 the average annual effective interest rate earned on short-term cash deposits was 0.102% (2017: 0.175%). See also Note 3.1.b.

The carrying amounts of cash and cash equivalents are assumed to be approximate to their fair values.

## 19. SHARE CAPITAL

As of 31 December 2018, the registered share capital of the Latvenergo AS is EUR 834,791 thousand (31/12/2017: EUR 1,288,715 thousand) and consists of 834,791 thousand ordinary shares (31/12/2017: 1,288,715 thousand) with the nominal value of EUR 1 per share (31/12/2017: EUR 1 per share). All shares have been fully paid.

In March 2018 a decrease of share capital in the amount of EUR 454,413 thousand was registered, related to the trilateral agreement between Republic of Latvia, Latvenergo AS and Enerģijas publiskais tirgotājs AS (EPT) on mutual settlement of the receivable of the grant from the Republic of Latvia by EPT as disclosed in Note 4 i).

In June 2018, in accordance with the Directive No. 765 of the Cabinet of Ministers of the Republic of Latvia, dated 19 December 2017 – “On the Investment of the State's property units in the Share Capital of Latvenergo AS”, real estate in the amount of EUR 489 thousand was invested in the share capital of Latvenergo AS. (Note 14 a).

## 20. RESERVES, DIVIDENDS AND EARNINGS PER SHARE

### a) Reserves

EUR'000

	Notes	Group				TOTAL	Parent Company			
		Non-current assets revaluation reserve	Hedge reserve	Post-employment benefit plan revaluation reserve	Other reserves		Non-current assets revaluation reserve	Hedge reserve	Post-employment benefit plan revaluation reserve	TOTAL
<b>As of 31 December 2016</b>		<b>946,373</b>	<b>(9,409)</b>	<b>(3,615)</b>	<b>110</b>	<b>933,459</b>	<b>659,429</b>	<b>(9,409)</b>	<b>(1,086)</b>	<b>648,934</b>
Increase of non-current assets revaluation reserve as a result of revaluation	14 a	22,167	–	–	–	<b>22,167</b>	22,167	–	–	<b>22,167</b>
Disposal of non-current assets revaluation reserve net of deferred tax		(4,377)	–	–	–	<b>(4,377)</b>	(1,762)	–	–	<b>(1,762)</b>
Deferred tax related to non-current assets revaluation reserve	12	(3,325)	–	–	–	<b>(3,325)</b>	(3,325)	–	–	<b>(3,325)</b>
Reversed deferred corporate income tax	12	169,560	–	(638)	–	<b>168,922</b>	119,384	–	(192)	<b>119,192</b>
Gains on re-measurement on defined post-employment benefit plan	26 a	–	–	3,460	–	<b>3,460</b>	–	–	1,053	<b>1,053</b>
Gains from fair value changes in derivative financial instruments	23	–	5,422	–	–	<b>5,422</b>	–	5,422	–	<b>5,422</b>
<b>As of 31 December 2017</b>		<b>1,130,398</b>	<b>(3,987)</b>	<b>(793)</b>	<b>110</b>	<b>1,125,728</b>	<b>795,893</b>	<b>(3,987)</b>	<b>(225)</b>	<b>791,681</b>
Disposal of non-current assets revaluation reserve		(10,229)	–	–	–	<b>(10,229)</b>	(6,549)	–	–	<b>(6,549)</b>
Gains / (losses) on re-measurement on defined post-employment benefit plan	26 a	–	–	436	–	<b>436</b>	–	–	(108)	<b>(108)</b>
Gains from fair value changes in derivative financial instruments	23	–	9,531	–	–	<b>9,531</b>	–	9,531	–	<b>9,531</b>
<b>As of 31 December 2018</b>		<b>1,120,169</b>	<b>5,544</b>	<b>(357)</b>	<b>110</b>	<b>1,125,466</b>	<b>789,344</b>	<b>5,544</b>	<b>(333)</b>	<b>794,555</b>

Non-current assets revaluation reserve, currency translation, post-employment benefit plan revaluation and hedge reserves cannot be distributed as dividends. Other reserves are maintained with the aim to maintain stability in the operations of the Group entities.

### b) Dividends

The dividends declared to equity holders of the Parent Company for 2017 were EUR 156,418 thousand or EUR 0.17183 per share (2016: EUR 90,142 thousand or EUR 0.06995 per share) and to non-controlling interests – EUR 2,116 thousand or EUR 0.619 per share (2016: EUR 1,393 thousand or EUR 0.408 per share).

Fulfilling the requirements of the Article No. 45 of the law "On the State budget 2019" that determines the amount of dividends payable in the year 2019, the Management Board of Latvenergo AS proposes to pay out in dividends EUR 132.9 million. The distribution of net profit and amount of dividends payable is subject to a resolution of the Latvenergo AS Shareholders Meeting. Net profit of the year 2018 is EUR 212.7 million.

### c) Earnings per share

Basic earnings per share are calculated by dividing profit attributable to the equity holders of the Parent Company by the weighted average number of ordinary shares outstanding (Note 19). As there are no potential ordinary shares, diluted earnings per share are equal to basic earnings per share in all comparable periods.

	Group		Parent Company	
	2018	2017	2018	2017
Profit attributable to the equity holder of the Parent Company (in thousand EUR)	73,423	319,670	212,733	150,891
Weighted average number of shares (thousand)	910,323	1,288,715	910,323	1,288,715
Basic earnings per share (in euros)	0.081	0.250	0.234	0.117
Diluted earnings per share (in euros)	0.081	0.250	0.234	0.117



## 21. OTHER FINANCIAL INVESTMENTS

### OTHER FINANCIAL INVESTMENTS PREVIOUSLY CLASSIFIED AS HELD-TO-MATURITY FINANCIAL ASSETS (2017)

Carrying (amortised) amount of other financial investments: EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Financial investments in Latvian State Treasury bonds: – non-current	16,935	16,984	16,935	16,984
<b>TOTAL other financial investments</b>	<b>16,935</b>	<b>16,984</b>	<b>16,935</b>	<b>16,984</b>

As of 31 December 2018 the entire Group's and the Parent Company's other financial investments, till 31 December 2017 classified as held-to-maturity financial assets, were Latvian State Treasury bonds with 5-year and 10-year maturity, which were purchased with the purpose to invest liquidity reserve in the low risk financial instruments with higher yield. During 2018 in connection with the amortisation of other financial investments are recognised net losses from changes in the value of the purchased bonds in the amount of EUR 49 thousand (2017: EUR 50 thousand) (Note 11 b). All other financial investments are denominated in euros. The maximum exposure to credit risk at the reporting date is the carrying amount of other financial investments.

In 2018 the fair value of other financial investments is greater than the carrying amount by EUR 3,132 thousand (2017: EUR 4,108 thousand). Other financial investments in Latvian State Treasury bonds are listed. The fair value of other financial investments is calculated by discounting their future cash flows and using as discount factor the market quoted yield to maturity rates of the respective bonds as of the end of the reporting period (Level 2).

## 22. BORROWINGS

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Non-current borrowings from financial institutions	564,711	583,313	555,251	574,764
Issued debt securities (bonds)	135,317	135,361	135,317	135,361
<b>TOTAL non-current borrowings</b>	<b>700,028</b>	<b>718,674</b>	<b>690,568</b>	<b>710,125</b>
Current portion of non-current borrowings from financial institutions	112,102	105,931	109,512	102,522
Accrued interest on non-current borrowings	529	468	504	441
Accrued coupon interest on issued debt securities (bonds)	1,684	1,684	1,684	1,684
<b>TOTAL current borrowings</b>	<b>114,315</b>	<b>108,083</b>	<b>111,700</b>	<b>104,647</b>
<b>TOTAL borrowings</b>	<b>814,343</b>	<b>826,757</b>	<b>802,268</b>	<b>814,772</b>

### Movement in borrowings:

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>826,757</b>	<b>791,566</b>	<b>814,772</b>	<b>778,323</b>
Borrowings received	93,500	186,500	90,000	185,000
Borrowings repaid	(105,931)	(80,976)	(102,522)	(78,221)
Change in accrued interest on borrowings	61	(126)	62	(123)
Repaid issued debt securities (bonds)	–	(70,000)	–	(70,000)
Changes in outstanding value of issued debt securities (bonds)	(44)	(207)	(44)	(207)
<b>At the end of the year</b>	<b>814,343</b>	<b>826,757</b>	<b>802,268</b>	<b>814,772</b>

### Borrowings by categories of lenders:

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Foreign investment banks	374,864	426,102	374,864	426,102
Commercial banks	302,478	263,610	290,403	251,625
Issued debt securities (bonds)	137,001	137,045	137,001	137,045
<b>TOTAL borrowings</b>	<b>814,343</b>	<b>826,757</b>	<b>802,268</b>	<b>814,772</b>

### Borrowings by contractual maturity, excluding the impact of derivative instruments to the interest rate:

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>Fixed rate non-current and current borrowings:</b>				
– < 1 year (current portion of non-current borrowings)	19,910	51,733	19,910	51,733
– 1–5 years	185,317	203,543	185,317	203,543
– > 5 years	–	–	–	–
<b>TOTAL fixed rate borrowings</b>	<b>205,227</b>	<b>255,276</b>	<b>205,227</b>	<b>255,276</b>
<b>Floating rate non-current and current borrowings:</b>				
– < 1 year (current borrowings)	–	–	–	–
– < 1 year (current portion of non-current borrowings)	94,405	56,350	91,790	52,915
– 1–5 years	313,404	338,240	305,158	330,119
– > 5 years	201,307	176,891	200,093	176,462
<b>TOTAL floating rate borrowings</b>	<b>609,116</b>	<b>571,481</b>	<b>597,041</b>	<b>559,496</b>
<b>TOTAL borrowings</b>	<b>814,343</b>	<b>826,757</b>	<b>802,268</b>	<b>814,772</b>

### Borrowings by repricing of interest, including the impact of derivative instruments:

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
– < 1 year	385,765	379,854	373,690	367,869
– 1–5 years	353,578	396,903	353,578	396,903
– > 5 years	75,000	50,000	75,000	50,000
<b>TOTAL borrowings</b>	<b>814,343</b>	<b>826,757</b>	<b>802,268</b>	<b>814,772</b>

As of 31 December 2018 and as of 31 December 2017 all of the Group's and the Parent Company's borrowings were denominated in euros.

The fair value of current and non-current borrowings with floating interest rates and twelve-month-fixed interest rates approximate their carrying amount, as their actual floating interest rates approximate the market price of similar financial instruments available to the Group and the Parent Company, i.e., the floating part of the interest rate corresponds to the money market price while the added part of the interest rate corresponds to the risk premium the lenders in financial and capital markets require from companies of similar credit rating level; therefore, the effect of fair value revaluation is not significant.

#### **I) Pledges**

As of 31 December 2018 the Group's and the Parent Company's assets are not pledged to secure the borrowings, except the pledge on assets of Liepājas Enerģija SIA of maximum secured claims in the amount of EUR 28 million (31/12/2017: EUR 32.3 million) to secure its current and non-current borrowings. As of the end of the reporting year there has been pledged the property, plant and equipment in the net book amount of EUR 25 million and the claims on the receivables accounts in the amount of EUR 3 million (31/12/2017: EUR 27 million and EUR 5.3 million, respectively).

#### **II) Un-drawn borrowing facilities**

As of 31 December 2018 the un-drawn committed non-current credit facilities amount to EUR 130 million (31/12/2017: EUR nil).

As of 31 December 2018 the Group had entered into four overdraft agreements with total notional amount of EUR 38.2 million (31/12/2017: EUR 34 million) of which three overdraft agreements were entered by the Parent Company with total notional amount of EUR 34 million (31/12/2017: EUR 34 million). In respect of all the overdraft agreements all conditions precedent had been met. At the end of the reporting year overdrafts were not used.

#### **III) Weighted average effective interest rate**

During the reporting year the weighted average effective interest rate (including interest rate swaps) on non-current borrowings was 1.37% (2017: 1.73%), weighted average effective interest rate for current borrowings was 0.87% (2017: 0.87%). At 31 December 2018 interest rates for non-current borrowings in euros were 6 and 12 month EURIBOR+ 0.99% (31/12/2017: +0.96%) for the Group and 6 and 12 month EURIBOR+ 0.98% (31/12/2017: +0.95%) for Latvenergo AS. At 31 December 2018 the total notional amount of interest rate swap agreements concluded by the Group amounts to EUR 225.1 million (31/12/2017: EUR 193.4 million) and the interest rate was fixed for the initial periods from 7 to 10 years.

#### **IV) Bonds outstanding**

The Parent Company (Latvenergo AS) in 2013 issued bonds in the amount of EUR 35 million with maturity date – 22 May 2020 (ISIN code – LV0000801165) with the annual coupon rate of 2.8%. In 2015 and in 2016, Latvenergo AS issued green bonds in the total amount of EUR 100 million with the maturity date 10 June 2022 (ISIN code – LV0000801777) with the annual coupon rate of 1.9%. The total nominal amount of outstanding bonds as of 31.12.2018 and 31.12.2017 amount to EUR 135 million. All issued bonds are quoted in NASDAQ Baltic Stock Exchange. The issued debt securities (bonds) are measured at amortised cost at the end of reporting year.

As of 31 December 2018 the fair value of issued debt securities (bonds) exceeds their carrying amount by EUR 4,532 thousand (31/12/2017: EUR 5,546 thousand). The fair value of debt securities (bonds) issued is calculated by discounting their future cash flows and using the market quoted yield to maturity rates of the respective bonds as of the end of the reporting year as discount factor (Level 2).

## 23. DERIVATIVE FINANCIAL INSTRUMENTS

### I) Outstanding fair values of derivatives and their classification

In the table below outstanding fair values of derivatives are disclosed as follows:

EUR'000

	Notes	Group				Parent Company			
		31/12/2018		31/12/2017		31/12/2018		31/12/2017	
		Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
Interest rate swaps	23 II	–	(7,375)	31	(8,061)	–	(7,375)	31	(8,061)
Electricity forwards and futures	23 III	15,853	–	4,588	(23)	15,853	–	4,588	(23)
Natural gas forwards	23 IV	–	(2,829)	–	–	–	(2,829)	–	–
<b>TOTAL outstanding fair values of derivatives</b>		<b>15,853</b>	<b>(10,204)</b>	<b>4,619</b>	<b>(8,084)</b>	<b>15,853</b>	<b>(10,204)</b>	<b>4,619</b>	<b>(8,084)</b>

EUR'000

		Group				Parent Company			
		31/12/2018		31/12/2017		31/12/2018		31/12/2017	
		Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
Non-current		–	(3,923)	–	(4,914)	–	(3,923)	–	(4,914)
Current		15,853	(6,281)	4,619	(3,170)	15,853	(6,281)	4,619	(3,170)
<b>TOTAL fair values of derivative financial instruments</b>		<b>15,853</b>	<b>(10,204)</b>	<b>4,619</b>	<b>(8,084)</b>	<b>15,853</b>	<b>(10,204)</b>	<b>4,619</b>	<b>(8,084)</b>

### Gains / (losses) on fair value changes as a result of realised hedge agreements: EUR'000

		Group		Parent Company	
	Notes	2018	2017	2018	2017
Included in the Statement of Profit or Loss					
Electricity forwards and futures	8	(417)	(3,435)	(417)	(3,435)
		(417)	(3,435)	(417)	(3,435)
Included in the Statement of Comprehensive Income (Note 20 a)					
Interest rate swaps	23 II	655	3,533	655	3,533
Electricity forwards and futures	23 III	11,705	1,889	11,705	1,889
Natural gas forwards	23 IV	(2,829)	–	(2,829)	–
TOTAL gains on fair value changes		9,531	5,422	9,531	5,422

### II) Interest rate swaps

As of 31 December 2018 the Group and the Parent Company had interest rate swap agreements with total notional amount of EUR 225.1 million (31/12/2017: EUR 193.4 million). Interest rate swaps are concluded with 7 to 10 year initial maturities and hedged floating rates are 6 month EURIBOR. As of 31 December 2018 fixed interest rates vary from 0.315% to 2.5775% (31/12/2017: from 0.315% to 2.5775%).

At the end of the year all of outstanding interest rate swap agreements are designated to comply with hedge accounting and were assessed prospectively and retrospectively to test whether they are effective within the hedging period (31/12/2018: 100% with notional amount of EUR 225.1 million). All contracts are designed as cash flow hedges. It was established that they are fully effective and therefore there is no ineffective portion to be recognised within profit or loss in the Statement of Profit or Loss.

**Fair value changes of interest rate swaps:**

EUR'000

	Group				Parent Company			
	2018		2017		2018		2017	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
<b>Outstanding fair value at the beginning of the year</b>	<b>31</b>	<b>(8,061)</b>	<b>–</b>	<b>(11,563)</b>	<b>31</b>	<b>(8,061)</b>	<b>–</b>	<b>(11,563)</b>
Included in Statement of Comprehensive Income (Note 20 a)	(31)	686	31	3,502	(31)	686	31	3,502
<b>Outstanding fair value at the end of the year</b>	<b>–</b>	<b>(7,375)</b>	<b>31</b>	<b>(8,061)</b>	<b>–</b>	<b>(7,375)</b>	<b>31</b>	<b>(8,061)</b>

The main interest rate hedging criteria stated in the Financial Risk Management policy is to ensure average fixed rate duration from 2 to 4 years and fixed rate portion at more than 35% of borrowings. As of 31 December 2018 53% (31/12/2017: 54%) of the Group's and 54% (2017: 55%) of the Parent Company's borrowings had fixed interest rates (taking into account the effect from the interest rate swaps), and average remaining time to interest re-pricing was 2.1 years (2017: 2.0 years) for the Group and 2.1 years (2017: 2.0 years) for the Parent Company.

**III) Electricity forwards and futures**

As of 31 December 2018 the Group and the Parent Company have entered into electricity forward and future contracts with total outstanding electricity purchase volume of 1,689,784 MWh (31/12/2017: 1,838,732 MWh) and notional value of EUR 40 million (31/12/2017: EUR 29.0 million). Electricity forward

and future contracts are concluded for the maturities from one quarter to one year during the period from 1 January 2019 to 31 December 2020.

The Group and the Parent Company enters into electricity future contracts in the Nasdaq Commodities power exchange, as well as concludes electricity forward contracts with other counterparties. Electricity forward and future contracts are intended for hedging of the electricity price risk and are used for fixing the price of electricity purchased in the *Nord Pool* AS power exchange.

Electricity forward and future contracts with total outstanding volume of 1,689,784 MWh as of 31 December 2018 are designated to comply with hedge accounting treatment (31/12/2017: 1,829,972) and were reassessed prospectively and retrospectively to test whether they are effective within the hedging period. All contracts are designed as cash flow hedges. For the contracts which are fully effective contracts fair value gains are included in other comprehensive income (Note 20 a).

**Fair value changes of electricity forward and future contracts:**

EUR'000

	Group				Parent Company			
	2018		2017		2018		2017	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
<b>Outstanding fair value at the beginning of the year</b>	<b>4,588</b>	<b>(23)</b>	<b>6,134</b>	<b>(23)</b>	<b>4,588</b>	<b>(23)</b>	<b>6,134</b>	<b>(23)</b>
Included in the Statement of Profit or Loss (Note 8)	(440)	23	(3,435)	–	(440)	23	(3,435)	–
Included in Statement of Comprehensive Income (Note 20 a)	11,705	–	1,889	–	11,705	–	1,889	–
<b>Outstanding fair value at the end of the year</b>	<b>15,853</b>	<b>–</b>	<b>4,588</b>	<b>(23)</b>	<b>15,853</b>	<b>–</b>	<b>4,588</b>	<b>(23)</b>

**IV) Natural gas forwards**

The Group and the Parent Company have entered into natural gas price swap contracts with total outstanding natural gas purchase volume of 990,000 MWh (31/12/2017: 0 MWh) and notional value of EUR 23 million (31/12/2017: nil). Natural gas swap contracts are concluded for the maturities from one month to one quarter during the period of 1 July 2019 to 1 October 2019. The Group and the

Parent Company have concluded natural gas swap contracts with other counterparties. Natural gas swap contracts are intended for hedging of the natural gas price risk and are used for fixing the price of natural gas purchased in wholesale gas market. Natural gas swap contracts with total outstanding volume of 990,000 MWh as of 31 December 2018 are designated to comply with hedge accounting treatment (31/12/2017: nil) and were reassessed prospectively and retrospectively to test whether they are effective within the hedging period.

**Fair value changes of natural gas forward contracts:**

EUR'000

	Group				Parent Company			
	2018		2017		2018		2017	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
<b>Outstanding fair value at the beginning of the year</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
Included in Statement of Comprehensive Income (Note 20 a)	–	(2,829)	–	–	–	(2,829)	–	–
<b>Outstanding fair value at the end of the year</b>	<b>–</b>	<b>(2,829)</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>(2,829)</b>	<b>–</b>	<b>–</b>

## 24. FAIR VALUES AND FAIR VALUE MANAGEMENT

In this Note are disclosed the fair value measurement hierarchy for the Group's and the Parent Company's financial and non-financial assets and liabilities.

### Quantitative disclosures of fair value measurement hierarchy for assets at the end of the year:

EUR'000

Type of liability	Group				Parent Company			
	Fair value measurement using			TOTAL	Fair value measurement using			TOTAL
	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)		Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
As of 31 December 2018								
Revalued property, plant and equipment (Note 14 c)	–	–	2,680,349	2,680,349			788,510	788,510
Non-current financial investments (Note 15)	–	–	40	40	–	–	39	39
Derivative financial instruments, including:								
Electricity forwards and futures (Note 23)	–	15,853	–	15,853	–	15,853	–	15,853
Assets for which fair values are disclosed								
Investment properties (Note 14 b)	–	–	467	467	–	–	61,796	61,796
Other financial investments (Note 21)	–	16,935	–	16,935	–	16,935	–	16,935
Floating rate loans to subsidiaries (Note 28 e)	–	–	–	–	–	171,858	–	171,858
Fixed rate loans to subsidiaries (Note 28 e)	–	–	–	–	–	593,957	–	593,957
Non-current financial receivables (Note 17 b)	–	–	30,920	30,920	–	–	331	331
Current financial receivables (Note 17 a, b)	–	–	202,568	202,568	–	–	95,258	95,258
Cash and cash equivalents	–	129,455	–	129,455	–	127,554	–	127,554
As of 31 December 2017								
Assets measured at fair value								
Revalued property, plant and equipment (Note 14 c)	–	–	2,587,058	2,587,058	–	–	722,609	722,609
Non-current financial investments (Note 15)	–	–	40	40	–	–	39	39
Derivative financial instruments, including:								
Electricity forwards and futures (Note 23)	–	4,588	–	4,588	–	4,588	–	4,588
Interest rate swaps (Note 23)	–	31	–	31	–	31	–	31
Assets for which fair values are disclosed								
Investment properties (Note 14 b)	–	–	753	753	–	–	64,807	64,807
Other financial investments (Note 21)	–	16,984	–	16,984	–	16,984	–	16,984
Floating rate loans to subsidiaries (Note 28 e)	–	–	–	–	–	714,165	–	714,165
Fixed rate loans to subsidiaries (Note 28 e)	–	–	–	–	–	384,616	–	384,616
Non-current financial receivables (Note 17 b)	–	–	3,229	3,229	–	–	284	284
Current financial receivables (Note 17 a, b)	–	–	747,201	747,201	–	–	100,737	100,737
Cash and cash equivalents	–	236,003	–	236,003	–	232,855	–	232,855

There have been no transfers for assets between Level 1, Level 2 and Level 3 during the reporting period.



Quantitative disclosures of fair value measurement hierarchy for liabilities at the end of the year:

EUR'000

Type of liability	Group				Parent Company			
	Fair value measurement using			TOTAL	Fair value measurement using			TOTAL
	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)		Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
<b>As of 31 December 2018</b>								
<b>Liabilities measured at fair value</b>								
<i>Derivative financial instruments, including:</i>								
Interest rate swaps (Note 23)	–	7,375	–	<b>7,375</b>	–	7,375	–	<b>7,375</b>
Electricity and natural gas forwards and futures (Note 23)		2,829		<b>2,829</b>		2,829		<b>2,829</b>
<b>Liabilities for which fair values are disclosed</b>								
Issued debt securities (bonds) (Note 22)	–	137,001	–	<b>137,001</b>	–	137,001	–	<b>137,001</b>
Floating rate borrowings (Note 22)	–	677,342	–	<b>677,342</b>	–	665,267	–	<b>665,267</b>
Trade and other financial current payables (Note 25)	–	–	103,707	<b>103,707</b>	–	–	78,726	<b>78,726</b>
<b>As of 31 December 2017</b>								
<b>Liabilities measured at fair value</b>								
<i>Derivative financial instruments, including:</i>								
Interest rate swaps (Note 23, II)	–	8,061	–	<b>8,061</b>	–	8,061	–	<b>8,061</b>
Electricity and natural gas forwards and futures (Note 23)	–	23	–	<b>23</b>	–	23	–	<b>23</b>
<b>Liabilities for which fair values are disclosed 7</b>								
Issued debt securities (bonds) (Note 22)	–	137,045	–	<b>137,045</b>	–	137,045	–	<b>137,045</b>
Floating rate borrowings (Note 22)	–	689,712	–	<b>689,712</b>	–	677,727	–	<b>677,727</b>
Trade and other financial current payables (Note 25)	–	–	115,742	<b>115,742</b>	–	–	79,341	<b>79,341</b>

There have been no transfers for liabilities between Level 1, Level 2 and Level 3 during the reporting period.

The fair value hierarchy for the Group's and the Parent Company's financial instruments that are measured at fair value, by using specific valuation methods, is disclosed above.

Set out below, is a comparison by class of the carrying amounts and fair value of the Group's and the Parent Company's financial instruments, other than those with carrying amounts which approximates their fair values:

EUR'000

	Group				Parent Company			
	Carrying amount		Fair value		Carrying amount		Fair value	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017	31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>Financial assets</b>								
Fixed rate loans to subsidiaries	–	–	–	–	593,957	384,616	618,046	399,215
Other financial investments	16,935	16,984	20,067	21,092	16,935	16,984	20,067	21,092
<b>Financial liabilities</b>								
<i>Interest-bearing liabilities, including:</i>								
– issued debt securities (bonds)	137,001	137,045	141,532	142,591	137,001	137,045	141,532	142,591

The management assessed that cash and short-term deposits, receivables, trade payables, bank overdrafts and other current liabilities approximate their carrying amounts largely due to the short-term maturities of these instruments. The fair value of the financial assets and liabilities is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The following methods and assumptions were used to estimate the fair values:

a) The fair values of borrowings with floating interest rates approximate their carrying amount, as their actual floating interest rates approximate the market price of similar financial instruments available to the Group and the Parent Company, i.e., the floating part of the interest rate corresponds to the money market price while the added part of the interest rate corresponds to the risk premium the lenders in financial and capital markets require from companies of similar credit rating level (Level 2);

b) The fair value of loans to subsidiaries with fixed rates calculations are based on discounted cash flows using discount factor of respective maturity EUR swap rates increased by average market margin of short term financing;

c) The Group and the Parent Company enter into derivative financial instruments with various counterparties, principally financial institutions with investment grade credit ratings. The derivative financial instruments are determined by using various valuation methods and models with market observable inputs. The models incorporate the credit quality of counterparties, foreign exchange spot and forward rates. The fair values of interest rate swaps are obtained from corresponding bank's revaluation reports and in financial statements fair values of financial instruments as specified by banks are disclosed. To make sure the fair values of interest rate swaps are accurate in any material aspect, the Group and the Parent Company makes its own interest rate swaps fair value calculations by discounting financial instruments future contractual cash flows using euro annual bond 6 months Euribor forward starting interest rate swap curve. The fair value of electricity forward and future contracts is calculated as discounted difference between actual market and settlement prices for the volume set in the agreements. If counterparty is a bank, calculated fair values of financial instruments are compared to bank's revaluation reports and the bank's calculated fair values of the financial instruments are used in the financial reports;

d) The fair value of the bonds issued and financial investments in government bonds are calculated by discounting their future cash flows using the market quoted yield to maturity rates of the respective bonds as of the end of the reporting year as discount factor.

e) The fair value of investment properties is determined using the income method, by discounting expected future cash flows. In 2018, the nominal pre-tax discount rate used to determine the fair value of investments is 4.2% (2017: 5.3%) as included in the electricity distribution and transmission system service tariff calculation methodology.

## 25. TRADE AND OTHER PAYABLES

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>Financial liabilities:</b>				
Payables for materials and services	63,198	75,395	63,009	68,820
Payables for electricity and natural gas	22,869	21,094	2,197	933
Accrued expenses	7,817	10,093	4,142	4,722
Other financial current liabilities	9,823	9,160	9,378	4,866
<b>TOTAL financial liabilities</b>	<b>103,707</b>	<b>115,742</b>	<b>78,726</b>	<b>79,341</b>
<b>Non-financial liabilities:</b>				
State social security contributions and other taxes	15,624	15,919	7,353	9,025
Advances received	12,024	11,784	4,399	4,993
Other current payables	3,653	3,627	1,584	1,330
<b>TOTAL non-financial liabilities</b>	<b>31,301</b>	<b>31,330</b>	<b>13,336</b>	<b>15,348</b>
<b>TOTAL trade and other current payables</b>	<b>135,008</b>	<b>147,072</b>	<b>92,062</b>	<b>94,689</b>

The carrying amounts of trade and other payables are assumed to approximate their fair values.

## 26. PROVISIONS

EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>Non-current:</b>				
– post-employment benefits (recognised in profit or loss)	12,411	12,928	5,536	5,687
– post-employment benefits (recognised in equity)	356	793	332	224
– termination benefits	6,191	5,925	1,537	1,704
– environmental provisions	1,220	2,264	1,220	1,220
	<b>20,178</b>	<b>21,910</b>	<b>8,625</b>	<b>8,835</b>
<b>Current:</b>				
– termination benefits	779	3,390	342	903

### a) Provisions for post-employment benefits

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>13,721</b>	<b>16,428</b>	<b>5,911</b>	<b>6,733</b>
Current service cost	1,238	1,392	523	572
Interest cost	261	304	112	124
Post-employment benefits paid	(2,017)	(943)	(786)	(465)
(Gains) / losses as a result of changes in actuarial assumptions (Note 20 a)	(436)	(3,460)	108	(1,053)
<b>At the end of the year</b>	<b>12,767</b>	<b>13,721</b>	<b>5,868</b>	<b>5,911</b>

Total charged / (credited) provisions are included in the Statement of Profit or Loss position 'Personnel expenses' within state social insurance contributions and other benefits defined in the Collective agreement (Note 9), while gains / (losses) as a result on re-measurement on defined post-employment benefit plan is included in the Statement of Comprehensive Income, according to IAS 19 *Employee Benefits*:

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>13,721</b>	<b>16,428</b>	<b>5,911</b>	<b>6,733</b>
(Charged) / credited to the Statement of Comprehensive Income less of deferred income tax (Note 20 a)	(436)	(3,460)	108	(1,053)
(Charged) / credited to the Statement of Profit or Loss	(518)	753	(151)	231
<b>At the end of the year</b>	<b>12,767</b>	<b>13,721</b>	<b>5,868</b>	<b>5,911</b>

Weighted average discount rate used for discounting benefit obligations was 1.90% (2017: 1.85%), considering the market yields on government bonds at the end of the reporting year. The Group's Collective Agreement provides indexation of employees' wages at least at the level of inflation. Long-term inflation determined at the level of 3.0% (2017: 3.0%) when calculating long-term post-employment benefits. In calculation of these liabilities also the probability, determined on the basis of previous experience, of retirement in different employees' aging groups was also considered.

A quantitative sensitivity analysis for significant assumptions on provisions for post-employment benefits as of the end of the year is as shown below:

EUR'000

Assumptions	Date of valuation	Group						Parent Company					
		Discount rate		Future salary changes		Retirement probability changes		Discount rate		Future salary changes		Retirement probability changes	
		1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease
Impact on provisions for post-employment benefits	31/12/2018	1,519	(1,252)	1,479	(1,247)	1,646	(1,366)	610	(501)	593	(499)	661	(547)
	31/12/2017	1,508	(1,246)	1,468	(1,240)	1,634	(1,360)	594	(488)	578	(486)	644	(533)

The sensitivity analysis above has been determined based on a method that extrapolates the impact on defined benefit obligation as a result of reasonable changes in key assumptions occurring at the end of the reporting period.

Contributions are monitored on an annual basis and the current agreed contribution rate is 5%. The next valuation is due to be completed as at 31 December 2019. Expected contributions to post-employment benefit plan for the year ending 31 December 2019 are EUR 2,389 thousand.

The weighted average duration of the defined benefit obligation is 20.47 years (2017 – 19.32 years).

EUR'000

	Date of valuation	Group				Parent Company			
		Less than 1 year	From 1 to 5 years	Over 5 years	TOTAL	Less than 1 year	From 1 to 5 years	Over 5 years	TOTAL
Defined benefit obligation	31/12/2018	2,481	1,745	8,541	12,767	1,676	955	3,237	5,868
	31/12/2017	3,105	2,060	8,556	13,721	1,854	827	3,230	5,911

**b) Termination benefits**

Termination benefits paid out in 2017 are included in the Statement of Profit or Loss position 'Personnel expenses' within expenditure of employment termination (Note 9), while termination benefits and projected future liability values for years 2018 to 2022 is recognised as a liability in the Statement of Financial Position and as accrued costs within expenditure of employment termination (Note 9):

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
At the beginning of the year	9,315	–	2,607	–
Termination benefits paid	(8,136)	(3,974)	(1,478)	(407)
Changes in provisions	5,795	13,289	749	3,014
At the end of the year	6,974	9,315	1,878	2,607

According to defined development directions per Strategy of Latvenergo Group for the period 2017-2022, the management of the Parent Company approved the Strategic Development and Efficiency Programme. Provisions for employees' termination benefits are recognised on a basis of Strategic Development and Efficiency Programme of Latvenergo Group for the period in which it is planned to implement the efficiency program (including Latvenergo AS and Sadales tīkls AS efficiency activities), by which it is intended to reduce gradually the number of employees by the year 2022.

Assumptions used in calculation of termination benefits are as follows – average employee earnings at the time of termination - average earnings per year, with projected increase (salary indexation) in the in the year 2019 by 9.6% (2018: 3.0%) and in the following years by 3.0% for Latvenergo AS and in the year 2019

by 2.6% (2018: 2.5%) and in the following years by 3.0% for Sadales tīkls AS, average employee length of service at the time of termination, the State Social Insurance Contributions rate is 24.09% in 2019 and in subsequent years.

The amount of provisions at the end of reporting year is estimated in accordance with the estimated future liability value as of 31 December 2018, using the fixed discount rate of 0.855% as adopted by the Latvenergo Group (31/12/2017: 1.093%). The discount rate is comprised of a 4-year EUROWAP rate of 0.040% and a corporate risk premium of 0.815% (determined on the basis of interest rate on Latvenergo AS issued bonds yield spreads above the market rate) (31/12/2017: 5-year EUROWAP rate – 0.314%, corporate risk premium – 0.779%).

**A quantitative sensitivity analysis for significant assumptions used for calculation of termination benefits as of the end of the year is as shown below:**

EUR'000

Assumptions	Date of valuation	Group						Parent Company					
		Discount rate		Future salary changes		Average employee length of service		Discount rate		Future salary changes		Average employee length of service	
		1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease	1% increase	1% decrease
Impact on provisions for termination benefits	31/12/2018	(192)	201	147	(145)	39	39	(47)	49	47	(46)	11	(11)
	31/12/2017	(134)	138	261	(254)	53	(53)	(68)	71	69	(67)	15	(15)

**c) Environmental provisions**

EUR'000

	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>2,264</b>	<b>2,215</b>	<b>1,220</b>	<b>1,191</b>
Charged to the Statement of Profit or Loss	(1,044)	49	–	29
<b>At the end of the year</b>	<b>1,220</b>	<b>2,264</b>	<b>1,220</b>	<b>1,220</b>

The environmental provision in the amount of EUR 1,220 thousand (31/12/2017: EUR 2,264 thousand) for the Group represents the estimated cost for Latvenergo AS of cleaning up TEC–1 combined heat and power plant ash–fields in accordance with the requests made by the regional Environmental Authority of Riga and feasibility study on this project in the amount of EUR 1,220 thousand (31/12/2017: EUR 1,220 thousand and Liepājas Enerģija SIA provision for the environmental recovery measures in the amount of EUR 1,044 thousand). The amount of the provisions is calculated taking into account the construction cost index (data from the Central Statistical Bureau of the Republic of Latvia).



## 27. DEFERRED INCOME

EUR'000				
	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>I) Non-current deferred income</b>				
<b>a) from contracts with customers</b>				
Deferred income from connection fees	143,494	142,132	–	–
	<b>143,494</b>	<b>142,132</b>	<b>–</b>	<b>–</b>
<b>b) from lease</b>				
Deferred income from connection fees	3,852	4,319	–	–
Deferred income on transmission system assets reconstruction	984	995	–	–
Other deferred income	403	423	403	423
	<b>5,239</b>	<b>5,737</b>	<b>403</b>	<b>423</b>
<b>c) other</b>				
Deferred income on grant for the installed electrical capacity of CHPPs*	209,419	285,109	209,419	285,109
Deferred income on financing from European Union funds	57,851	45,090	18	270
Deferred income on financing receivable from European Union funds	30,617	14,707	–	–
Deferred income from plant and equipment received free of charge	393	283	265	283
	<b>298,280</b>	<b>345,189</b>	<b>209,702</b>	<b>285,662</b>
<b>TOTAL non-current deferred income</b>	<b>447,013</b>	<b>493,058</b>	<b>210,105</b>	<b>286,085</b>

EUR'000				
	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
<b>II) Current deferred income</b>				
<b>a) from contracts with customers</b>				
Deferred income from connection fees	12,984	12,247	–	–
Deferred income from use of allowed effective electrical load (distribution system services)	287	253	–	–
	<b>13,271</b>	<b>12,500</b>	<b>–</b>	<b>–</b>
<b>b) from lease</b>				
Deferred income from connection fees	449	449	–	–
	<b>449</b>	<b>449</b>	<b>–</b>	<b>–</b>
<b>c) other</b>				
Other deferred income	58	121	20	20
Deferred income on grant for the installed electrical capacity of CHPPs*	23,990	29,304	23,990	29,304
Deferred income on financing from European Union funds	1,941	1,854	12	34
	<b>25,989</b>	<b>31,279</b>	<b>24,022</b>	<b>29,358</b>
<b>TOTAL current deferred income</b>	<b>39,709</b>	<b>44,228</b>	<b>24,022</b>	<b>29,358</b>
<b>TOTAL deferred income</b>	<b>486,722</b>	<b>537,286</b>	<b>234,127</b>	<b>315,443</b>

\* See Note 4. i)

The Group and the Parent Company ensures the management, application of internal controls and accounting for the Group's and the Parent Company's projects financed by the European Union funds, according to the guidelines of the European Union and legislation of the Republic of Latvia.

Accounting of the transactions related to the projects financed by the European Union is ensured using separately identifiable accounts. The Group and the Parent Company ensure separate accounting of financed projects with detailed income and expense, non-current investments and value added tax in the relevant positions of the Statement of Profit or Loss and Statement of Financial Position.

EUR'000				
Movement in deferred income (non-current and current part):				
	Group		Parent Company	
	2018	2017	2018	2017
<b>At the beginning of the year</b>	<b>537,286</b>	<b>209,429</b>	<b>315,443</b>	<b>1,114</b>
Received deferred non-current income (financing)	31,537	14,707	–	–
Received connection fees	14,726	12,848	–	–
Received income from compensation for the installed electrical capacity of CHPPs*	–	314,413	–	314,413
Compensation for the installed electrical capacity of CHPPs credited to the Statement of Profit or Loss*	(81,004)	–	(81,004)	–
Credited to the Statement of Profit or Loss (in Note 6 as "Other revenue")	(15,823)	(14,111)	(312)	(84)
<b>At the end of the year</b>	<b>486,722</b>	<b>537,286</b>	<b>234,127</b>	<b>315,443</b>

\* See Note 4. i)

## 28. RELATED PARTY TRANSACTIONS

The Parent Company and, indirectly, its subsidiaries are controlled by the Latvian state. Related parties of the Latvenergo Group and the Parent Company are Shareholder of the Parent Company who controls over the Parent Company in accepting operating business decisions, members of Latvenergo Group entities' management boards, members of the Supervisory board of the Parent Company, members of Supervisory body of the Parent Company – the Audit Committee and close family members of any above-mentioned persons, as well as entities over which those persons have control or significant influence.

Trading transactions taking place under normal business activities with the Latvian government including its departments and agencies and transactions between state-controlled entities and providers of public utilities are excluded from the scope of related party disclosures. The Group and the Parent Company enters into transactions with many of these bodies on an arm's length basis. Transactions with government related entities include sales of energy and related services and does not contain individually significant transactions and quantitative disclosure of transactions with those related parties is impossible due to broad range of the Latvenergo Group's and the Parent Company's customers, except for transactions with transmission system operator – Augstsprieguma tīkls AS.

### a) Income and expenses from transactions with related parties: EUR'000

	Group		Parent Company			
	2018	2017	2018	2017		
	Government related entities*		Subsidiaries	Government related entities*	Subsidiaries	Government related entities*
<b>Income:</b>						
– Trade of energy and related services	10,724	2,605	25,370	10,656	101,227	2,535
– Lease of transmission system assets	38,699	43,911	–	–	–	–
– Other revenue from corporate services	–	–	28,505	–	29,741	–
– Other revenue	3,175	3,249	–	3,024	–	3,118
– Lease of assets	372	645	14,534	372	14,181	645
– Interest income	–	–	10,289	–	10,189	–
– Other income	1,036	271	–	196	–	–
<b>TOTAL income from transactions with related parties</b>	<b>54,006</b>	<b>50,681</b>	<b>78,698</b>	<b>14,248</b>	<b>155,338</b>	<b>6,298</b>
<b>Expenses:</b>						
– Distributions system services	–	–	207,096	–	217,735	–
– Public service obligation fees	–	–	98,623	–	114,957	–
– Purchased electricity and heat	4,131	4,253	37,461	4,131	4,198	4,253
– Electricity transmission services costs (Note 8)	71,368	71,044	–	1,015	–	845
– Construction services for leased assets	–	–	1,867	–	5,391	–
– Other expenses	864	793	1,594	276	1,773	269
<b>TOTAL expenses from transactions with related parties</b>	<b>76,363</b>	<b>76,090</b>	<b>346,641</b>	<b>5,422</b>	<b>344,054</b>	<b>5,367</b>
<i>including gross expenses from transactions with subsidiaries recognised in net amount through profit or loss:</i>						
– Sadales tīkls AS	–	–	305,719	–	332,172	–
– Enerģijas publiskais tirgotājs AS	–	–	–	–	520	–
	<b>–</b>	<b>–</b>	<b>305,719</b>	<b>–</b>	<b>332,692</b>	<b>–</b>

\* Transmission system operator – Augstsprieguma tīkls AS

### b) Balances at the end of the period arising from sales/purchases of goods and services: EUR'000

	Group			Parent Company		
	31/12/2018	01/01/2018	31/12/2017	31/12/2018	01/01/2018	31/12/2017
<b>Receivables from related parties:</b>						
– Subsidiaries (Note 17 a, b)	–	–	–	12,204	17,434	17,434
– Government related and other related parties*	42,273	20,014	20,014	3,365	1,211	1,211
– Loss allowances for expected credit loss from receivables of subsidiaries (Note 17 a, b)	–	–	–	(9)	(13)	–
– Loss allowances for expected credit loss	(55)	(26)	–	(4)	(1)	–
	<b>42,218</b>	<b>19,988</b>	<b>20,014</b>	<b>15,556</b>	<b>18,631</b>	<b>18,645</b>
<b>Payables to related parties:</b>						
– Subsidiaries	–	–	–	30,865	30,994	30,994
– Government related and other related parties*	12,262	17,293	17,293	1,044	1,019	1,019
	<b>12,262</b>	<b>17,293</b>	<b>17,293</b>	<b>31,909</b>	<b>32,013</b>	<b>32,013</b>

\* Transmission system operator – Augstsprieguma tīkls AS and Pirmais Slēgtais Pensiju Fonds AS

### c) Accrued income raised from transactions with related parties: EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
– For goods sold / services provided for subsidiaries (Note 17 a, b)	–	–	2,859	3,202
– For interest received from subsidiaries (Note 17 b)	–	–	1,820	1,875
	<b>–</b>	<b>–</b>	<b>4,679</b>	<b>5,077</b>

### d) Accrued expenses raised from transactions with related parties: EUR'000

	Group		Parent Company	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
– For purchased goods / received services from subsidiaries	–	–	5,657	1,176
	<b>–</b>	<b>–</b>	<b>5,657</b>	<b>1,176</b>

The Group and the Parent Company have not incurred write-offs of trade payables and receivables from transactions with related parties, as all debts are recoverable.

Receivables and payables with related parties are current balances for services and goods. None of the amounts at the end of the reporting year are secured.

Remuneration to the Latvenergo Group's management includes remuneration to the members of the Management Boards the Group entities, the Supervisory Board and the Supervisory body (Audit Committee) of the Parent Company. Remuneration to the Parent Company's management includes remuneration to the members of the Parent Company's Management Board, the Supervisory Board and the Supervisory body (Audit Committee). Information disclosed in Note 9.

Dividend payments to Shareholder of the Parent Company and share capital contributions are disclosed in Note 20 b and Note 19, respectively.

Dividends received from subsidiaries are disclosed in note 15.

## e) Loans to related parties (Parent Company)

### Non-current and current loans to related parties:

EUR'000

	Parent Company		
	31/12/2018	01/01/2018	31/12/2017
<b>Non-current loans to subsidiaries</b>			
Sadales tīkls AS	442,728	312,582	312,582
Latvijas elektriskie tīkli AS	152,681	85,394	85,394
Impairment for expected credit loss	(405)	(271)	–
<b>TOTAL non-current loans</b>	<b>595,004</b>	<b>397,705</b>	<b>397,976</b>
<b>Current portion of non-current loans</b>			
Sadales tīkls AS	49,854	50,914	50,914
Latvijas elektriskie tīkli AS	8,175	8,490	8,490
Impairment for expected credit loss	(39)	(40)	–
<b>Current loans to subsidiaries</b>			
Latvijas elektriskie tīkli AS	18,541	1,294	1,294
Sadales tīkls AS	6,502	28,157	28,157
Elektrum Eesti OÜ	7,882	5,134	5,134
Elektrum Lietuva, UAB	11,740	2,172	2,172
Enerģijas publiskais tirgotājs AS	68,233	604,644	604,644
Impairment for expected credit loss	(77)	(204)	–
<b>TOTAL current loans</b>	<b>170,811</b>	<b>700,561</b>	<b>700,805</b>
<b>TOTAL loans to subsidiaries</b>	<b>765,815</b>	<b>1,098,266</b>	<b>1,098,781</b>

Counterparty model is used on individual contract basis for assessment of expected credit risk for non-current and current loans to subsidiaries. The expected credit losses according to this model are based on assessment of the individual counterparty's risk of default and recovery rate assigned by *Moody's* credit rating agency for 12 months expected losses (Note 4 b). Credit risk of subsidiaries is assessed at the same level as Latvenergo AS credit risk considering that they are 100% controlled by Latvenergo AS. Since the initial recognition of loans, credit risk has not changed significantly.

All current loans to related parties as of 31 December 2018 will be settled in 2019.

### Movement in loans:

EUR'000

	Parent Company	
	2018	2017
<b>At the beginning of the year</b>	<b>1,098,781</b>	<b>622,704</b>
Change in current loans in cash (net)	323,539	268,218
Change in current loans by non-cash offsetting of operating receivables and payables (net)	(720,848)	268,084
Issued non-current loans by non-cash offset with dividends (Note 15)	124,268	–
Reduction of non-current loans by non-cash offsetting of operating receivables and payables	(59,404)	(60,225)
Effect of IFRS 9 'Financial Instruments' adoption (Note 2.28.)	(515)	–
Impairment for expected credit loss	(6)	–
<b>At the end of the year</b>	<b>765,815</b>	<b>1,098,781</b>

## Interest received from related parties:

EUR'000

	Parent Company	
	2018	2017
Interest received	2,103	1,682
	<b>2,103</b>	<b>1,682</b>

## I) Non-current loans, including current portion

### Concluded non-current loan agreements with Latvijas elektriskie tīkli AS:

EUR'000

Agreement conclusion date	Principal amount of the loan	Outstanding loan amount		Interest rate	Maturity date
		31/12/2018	31/12/2017		
1 April 2011	97,467	12,826	15,801	6 months EURIBOR + fixed rate	1 April 2025
3 September 2013	44,109	27,568	33,082	fixed rate	10 September 2023
10 June 2016	156,500	120,462	45,000	fixed rate	10 June 2028
<b>TOTAL</b>	<b>298,076</b>	<b>160,856</b>	<b>93,883</b>		

As of 31 December 2018 total outstanding amount of non-current loans to Latvijas elektriskie tīkli AS amounted to EUR 160,856 thousand (31/12/2017: EUR 93,883 thousand), including current portion of the loan repayable in 2019 – EUR 8,176 thousand (31/12/2017: EUR 8,490 thousand). As of 31 December 2018 for 8% (31/12/2017: 17%) of the loans issued to Latvijas elektriskie tīkli AS was set floating interest rate, which was influenced by 6 months EURIBOR interbank rate fluctuations. During 2018 the effective average interest rate of non-current loans was 1.81% (2017: 2.36%). As of 31 December 2018 is recognised impairment for expected credit loss of non-current loans to Latvijas elektriskie tīkli AS in the amount of 109 thousand EUR (31/12/2017: nil; 01/01/2018: 64 thousand EUR). Non-current loans are not secured with a pledge or otherwise.

### Non-current loans to Latvijas elektriskie tīkli AS by maturity:

EUR'000

	Parent Company	
	31/12/2018	31/12/2017
<b>Non-current loan:</b>		
– < 1 year (current portion)	8,176	8,490
– 1 – 5 years	109,724	64,790
– > 5 years	42,957	20,603
	<b>160,856</b>	<b>93,883</b>

### Concluded non-current borrowing agreements with Sadales tīkls AS:

EUR'000

Agreement conclusion date	Principal amount of the loan	Outstanding loan amount		Interest rate	Maturity date
		31/12/2018	31/12/2017		
29 September 2011	316,271	47,966	58,676	6 months EURIBOR + fixed rate	1 September 2025
6 February 2013	42,686	14,940	19,209	fixed rate	10 September 2022
18 September 2013	42,686	21,343	25,612	fixed rate	10 August 2023
29 October 2014	90,000	60,000	70,000	fixed rate	10 September 2024
20 October 2015	90,000	70,000	80,000	fixed rate	21 October 2025
22 August 2016	60,000	53,333	60,000	fixed rate	22 August 2026
22 August 2016	50,000	45,000	50,000	fixed rate	14 June 2027
14 December 2018	260,000	180,000	–	fixed rate	14 December 2028
<b>TOTAL</b>	<b>951,643</b>	<b>492,582</b>	<b>363,497</b>		

As of 31 December 2018 total outstanding amount of non-current loans with Sadales tīkls AS amounted to EUR 492,582 thousand (31/12/2017: EUR 363,497 thousand), including current portion of the loan repayable in 2019 – EUR 49,853 thousand (31/12/2017: EUR 50,915 thousand). As of 31 December 2018 for 10% of the loans issued to Sadales tīkls AS (31/12/2017: 16%) was set floating interest rate, which was influenced by 6 months EURIBOR interbank rate fluctuations. During 2018 the effective average interest rate of non-current loans was 1.65% (2017: 1.84%). As of 31 December 2018 is recognised impairment for expected credit loss of non-current loans to Sadales tīkls AS in the amount of 335 thousand EUR (31/12/2017: nil; 01/01/2018: 247 thousand EUR). Non-current loans are not secured with a pledge or otherwise.

**Non-current loans to Sadales tīkls AS by maturity:** EUR'000

	Parent Company	
	31/12/2018	31/12/2017
<b>Non-current loan:</b>		
– < 1 year (current portion)	49,853	50,915
– 1 – 5 years	322,786	238,425
– > 5 years	119,943	74,157
	<b>492,582</b>	363,497

## II) Current loans

To ensure efficiency and centralised management of Latvenergo Group companies' financial resources and using the functionality of Group accounts and possibility for non-cash offsetting of mutual invoices between the parties, short term credit funds are provided. In the reporting period Latvenergo AS issued loans to subsidiaries in accordance with mutually concluded agreement 'On provision of mutual financial resources', allowing the subsidiaries to borrow and to repay the loan accordingly to daily operating needs and including non-cash offsetting of operating receivables and payables. In 2018 the effective average interest rate was 0.51% (2017: 0.52%).

In the reporting period Enerģijas publiskais tirgotājs AS received current loan from Latvenergo AS in accordance with mutually concluded agreement 'On provision of mutual financial resources', using Group accounts.

On 29 March 2018 an agreement was concluded between Latvenergo AS and Enerģijas publiskais tirgotājs AS for issue of the current loan in amount of EUR 150,000 thousand to ensure Enerģijas publiskais tirgotājs AS financial resources for the fulfilment of public supplier duties and mandatory procurement process administration. Maturity date of the loan is 31 March 2019. An agreement concluded on 31 March 2017 with amount of EUR 200,000 thousand and maturity date - 31 March 2018 is repaid. Loan annual interest rate is fixed at 0.730% (2017: 1.000%). As of 31 December 2018, issued, but unpaid net amount of current loan is EUR 68,233 thousand (31/12/2017: EUR 150,231 thousand).

On 29 November 2017 an agreement was concluded between Latvenergo AS and Enerģijas publiskais tirgotājs AS for issue a short term loan in amount of EUR 454,413 thousand. Loan amount equalled to the government grant receivable and loan was intended to ensure Enerģijas publiskais tirgotājs AS financial resources for financing of one-off compensation. On 26 March 2018 the loan was settled with mutual non-monetary offset (see Note 4 i).

As of 31 December 2018 is recognised impairment for expected credit loss of current loans to related parties in the amount of 77 thousand EUR (31/12/2017: nil; 01/01/2018: 204 thousand EUR).

## f) Current borrowings from related parties

Financial transactions between related parties have been carried out by using current loans with a target to effectively and centrally manage Latvenergo Group companies' financial resources, using Group accounts. In the reporting period Latvenergo AS has received borrowings from subsidiaries in accordance with mutually concluded agreement 'On provision of mutual financial resources'. In 2018 the effective average interest rate was 0.51% (2017: 0.52%). At the end of the reporting year Latvenergo AS has no borrowings from related parties (31/12/2017: nil).

	Parent Company	
	2018	2017
Interest paid	37	41
	<b>37</b>	<b>41</b>

## 29. COMMITMENTS AND CONTINGENT LIABILITIES

As of 31 December 2018 the Group had commitments amounting to EUR 189.8 million (31/12/2017: EUR 225.6 million) and the Parent Company had commitments amounting to EUR 58.5 million (31/12/2017: EUR 105.2 million) for capital expenditure contracted but not delivered at the end of the reporting period.

On 5 March 2019 Latvenergo AS has issued support letters to its subsidiaries Enerģijas publiskais tirgotājs AS, Sadales tīkls AS and Latvijas elektriskie tīkli AS acknowledging that its position as the shareholder is to ensure that subsidiaries are managed so that they have sufficient financial resources and are able to carry their operations and settle their obligations.

## 30. EVENTS AFTER THE REPORTING YEAR

On 19 March 2019 *Moody's* credit rating for Latvenergo AS affirmed at the Baa2 level with a stable future outlook.

On 31 March 2019 a loan agreement was concluded between Latvenergo AS and Enerģijas publiskais tirgotājs AS in the amount till EUR 110 million with the maturity 31 March 2020.

There have been no other significant events subsequent to the end of the reporting year that might have a material effect on the Financial Statements for the year ended 31 December 2018.

---

**Āris Žīgurs**

Chairman of the Management Board

---

**Guntars Baļčūns**

Member of the Management Board

---

**Uldis Bariss**

Member of the Management Board

---

**Kaspars Cikmačs**

Member of the Management Board

---

**Liāna Keldere**

Accounting director of Latvenergo AS

16 April 2019





## **INDEPENDENT AUDITOR'S REPORT**

**To the shareholder of Latvenergo AS**

**Report on the audit of the separate and consolidated financial statements**

### **Our opinion**

In our opinion, the separate and consolidated financial statements give a true and fair view of the separate and consolidated financial position of Latvenergo AS (the Company) and its subsidiaries (the Group) as at 31 December 2018, and of its separate and consolidated financial performance and its separate and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Our opinion is consistent with our additional report to the Audit Committee dated 3 April 2019.

### ***What we have audited***

The financial statements presented on pages 89 to 146 which consist of the separate financial statements of the Company and the consolidated financial statements of the Group (together "the financial statements") comprise:

- the separate and consolidated statement of financial position as at 31 December 2018;
- the separate and consolidated statement of profit or loss for the year then ended;
- the separate and consolidated statement of comprehensive income for the year then ended;
- the separate and consolidated statement of changes in equity for the year then ended;
- the separate and consolidated statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

### **Basis for opinion**

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

## Independence

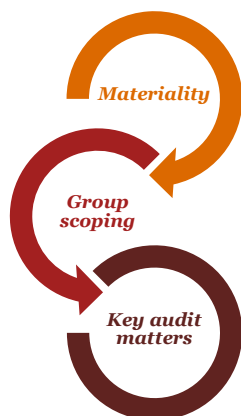
We are independent of the Company and the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) and the ethical requirements of the Law on Audit Services that are relevant to our audit of the financial statements in the Republic of Latvia. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code and the ethical requirements of the Law on Audit Services.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the Company and the Group are in accordance with the applicable law and regulations in Latvia and that we have not provided non-audit services that are prohibited under Article 37.6 of Law on Audit Services of the Republic of Latvia.

The non-audit services that we have provided to the Company and the Group, in the period from 1 January 2018 to 31 December 2018, are disclosed in Note 10 to the financial statements.

## Our audit approach

### Overview



#### Materiality

- Overall Company and Group materiality: EUR 7,600 thousand.

#### Audit scope

- Full scope audit was conducted for all seven Group entities, five of them are in Latvia (including the Company), one in Estonia and one in Lithuania.
- The Group audit team performed the work on all five Latvian entities.
- Estonian and Lithuanian subsidiaries were audited by component audit teams located in the respective countries.

#### Key audit matters

- Impact of USA sanctions applied to a supplier of hydroelectric units.
- Implications of changes in the tax law on deferred tax recognition.

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.



## **Materiality**

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Company and Group materiality separately for the separate and consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

<b>Overall Company and Group materiality</b>	Overall materiality applied to the Company and the Group was EUR 7,600 thousand.
<b>How we determined it</b>	5% of average profit before tax for the recent three years.
<b>Rationale for the materiality benchmark applied</b>	We chose profit before tax as the base benchmark because, in our view, it is the benchmark against which the performance of the Company and the Group is most commonly measured by users of the financial statements, and it is a generally accepted benchmark. We decided to use average profit for the recent three years (2016-2018) due to significant volatility in profit before tax during these years due to fluctuations in the market price of electricity, arising mainly from unstable weather conditions in Latvia and Nordic countries. We chose 5%, which is within the range of acceptable quantitative materiality thresholds.

We agreed with the Audit Committee that we would report to them the misstatements identified during our audit above EUR 760 thousand, both with respect to the Company and the Group, as well as the misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

## **Key audit matters**

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

## **Key audit matters**

### ***Impact of USA sanctions applied to a supplier of hydroelectric units***

*Refer to Note 4 to the financial statements on page 113.*

In January 2018 USA applied sanctions to a Russia based supplier who has been contracted by the Group to reconstruct five hydroelectric units of the Hydro Power plants of the Group for a total amount of EUR 78,045 thousand. By 31 December 2018 only a part of the contracted equipment and works have been completed and further supplies have been suspended due to the sanctions against the supplier.

The most significant judgements made by the management in respect of this matter relate to:

- assessment whether there is an impairment of the construction in progress within property, plant and equipment of EUR 16,562 thousand as at 31 December 2018, including the machinery supplied and not yet installed, related to the above contract;
- assessment whether there is a need to recognise a provision or disclose a contingent liability related to the resolution of the matter as at 31 December 2018.

The management has engaged external independent experts to advise in assessing the impact and determining the course of action. The management has concluded that no impairment of the construction in progress has incurred and no provision needs to be recognised as at 31 December 2018.

We focused on this area because the sanctions applied by USA to a supplier who is responsible for delivering and installing hydroelectric units may have a material impact on the financial statements and the assessment of the impact is subject to management's judgement.

## **How our audit addressed the key audit matter**

We discussed the matter with the management and the Company's internal lawyers. We examined the detailed written assessment made by the management in respect of the impact of the matter on the financial statements. We also obtained and read the contract with the supplier and other evidence serving as a basis for the management's judgement, including the reports prepared by the external independent experts and the Company's correspondence with the USA Department of Treasury Office of Foreign Assets Control which is an institution publishing the list of the companies subject to the USA sanctions.

We also performed detailed tests and examined the work papers of predecessor auditor to obtain evidence on the opening balances of the construction in progress within property, plant and equipment related to this matter.

Based on the audit evidence obtained we exercised our judgement in assessing the appropriateness of the management's assessment of the impact of the matter on the financial statements.

We also assessed whether the information disclosed in the financial statements adequately describes the circumstances and basis for the management's judgement.

---

### ***Implications of changes in the tax law on deferred tax recognition***

*Refer to Notes 4 and 12 to the financial statements on pages 113 and 119, respectively.*

Following the changes in Latvian tax legislation from 1 January 2018 corporate income tax is levied on profit generated after 2017 only if it is distributed to the shareholders. The tax becomes payable when the shareholders declare dividends. Accordingly, the profits of the Company and its subsidiaries (except Lithuanian subsidiary whose annual profit is subject to income tax in the same year) generated in 2018 will be subject to taxation when and to the extent distributed to the shareholders. The profits of the subsidiaries generated in 2018 are subject to recognition of deferred tax liability and expense in the consolidated financial statements unless it is probable that the profit will not be distributed in a foreseeable future. The management had to make judgement on the expected timing and extent of the distribution of the profits of the subsidiaries. The Group has recognised deferred tax liability of EUR 12,297 thousand related to the 2018 profit of its subsidiaries in the consolidated financial statements as at 31 December 2018.

We focused on this area because 2018 is the first year of application of the amended tax legislation and the management had to make the judgement as described above.

We examined the Group's accounting policy on deferred tax recognition applicable to the amended tax legislation.

We discussed with the management the basis for their judgement on the timing and extent of the distribution of profits of the Group's subsidiaries.

We performed detailed tests of the calculation of the deferred tax liability in the consolidated financial statements as at 31 December 2018 by applying statutory tax rate to the 2018 profit of subsidiaries expected by the Company's management to be distributed in a foreseeable future.

We also assessed whether the information disclosed in the financial statements adequately describes the circumstances and meets the requirements of the respective standard.

---

### ***How we tailored our Group audit scope***

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

Full scope statutory audit was performed for the Company and all its subsidiaries by us or by other PwC network firms. Where work was performed by component auditors, we determined the level of involvement we needed to have to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the consolidated financial statements as a whole. We also audited the consolidation process.





## **Reporting on other information including the Management Report**

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

- Latvenergo Group Key Figures, Latvenergo AS Key Figures and Management Report as set out on pages 81 to 88 of the accompanying Sustainability and Annual Report,
- Non-financial Report included in the Management Report as set out on page 86 of the accompanying Sustainability and Annual Report, and
- the Corporate Governance Report, set out in separate statement prepared by the Company's management and available on the Company's website <http://www.latvenergo.lv> section Investors as at the date of this audit report,

(but does not include the financial statements and our auditor's report thereon, and the Sustainability Report as set out on pages 4 to 77 of the accompanying Sustainability and Annual Report to which we have issued separately a limited assurance report on pages 78 to 79), which we obtained prior to the date of this auditor's report.

Our opinion on the financial statements does not cover the other information identified above.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above 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.

With respect to the Management Report, we also performed the procedures required by Law on Audit Services. Those procedures include considering whether the Management Report is prepared in accordance with the requirements of the applicable legislation.

In accordance with the Law on Audit Services of the Republic of Latvia with respect to the Corporate Governance Report, our responsibility is to consider whether the Corporate Governance Report includes the information required by section (3) of Article 56.<sup>2</sup> of the Financial Instruments Market Law.

Based on the work undertaken in the course of our audit, in our opinion, in all material respects:

- the information given in the other information identified above for the financial year for which the financial statements are prepared is consistent with the financial statements;
- the Management Report has been prepared in accordance with the requirements of the Law on Annual Reports and Consolidated Annual Reports; and
- the Statement of Corporate Governance, available on the Company's website <http://www.latvenergo.lv> as at the date of this audit report, includes the information required by section (3) of Article 56.<sup>2</sup> of the Financial Instruments Market Law.

In addition, in light of the knowledge and understanding of the Company and the Group and their environment obtained in the course of the audit, we are required to report if we have identified material misstatements in the Management Report and the other information listed above that we obtained prior to the date of this auditor's report. We have nothing to report in this respect.

Furthermore, in accordance with the Law on Audit Services with respect to the Non-financial Report, our responsibility is to report whether the Group has prepared Non-financial Report and whether the Non-financial Report is included in the Management Report or prepared as a separate element of the Annual Report.



We hereby report that the Group has prepared a Non-financial Report, and it is included in the Management Report.

### **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 International Financial Reporting Standards as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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

### **Auditor's responsibilities 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 judgement and maintain professional skepticism 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 and the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's and the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company or the Group to cease to continue as a going concern.



- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

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

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

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

## **Report on other legal and regulatory requirements**

### ***Appointment***

We were appointed as auditors of the Company and the Group for the year ended 31 December 2018 by resolution of general meeting of shareholders dated 9 May 2018. This is our first year of the appointment.

PricewaterhouseCoopers SIA  
Certified audit company  
License No. 5

Juris Lapše  
Certified auditor in charge  
Certificate No.116  
Persona per procura

Riga, Latvia  
16 April 2019