



LATVENERGO AS

(incorporated in the Republic of Latvia as a public limited company with registration number 40003032949)

Third Programme for the Issuance of Notes in the Amount of EUR 200,000,000

Under this Third Programme for the Issuance of Notes in the Amount of EUR 200,000,000 (the “**Programme**”) described in this base prospectus (the “**Base Prospectus**”) Latvenergo AS, a public limited company (in Latvian – *akciju sabiedrība*) incorporated in and operating under the laws of the Republic of Latvia, registered with the Commercial Register of the Republic of Latvia under registration number: 40003032949 and having its legal address at Pulkveža Brieža iela 12, Riga, LV-1230 (the “**Issuer**” or the “**Company**”), may issue and offer from time to time in one or several series (the “**Series**”) non-convertible unsecured and unguaranteed notes denominated in EUR, having maturity up to 10 years and with fixed interest rate (the “**Notes**”). Each Series may comprise one or more tranches of Notes (the “**Tranches**”). The maximum aggregate nominal amount of all Notes from time to time outstanding will not at any time exceed EUR 200,000,000.

To the extent not set forth in this Base Prospectus, the specific terms of any Notes will be included in the relevant final terms (the “**Final Terms**”) (a form of which is contained herein). This Base Prospectus should be read and construed together with any supplement hereto and with any other documents incorporated by reference herein, and, in relation to any Tranche of Notes and with the Final Terms of the relevant Tranche of Notes.

This Base Prospectus has been prepared in connection with the offering and listing of the Notes pursuant to the requirements of the Regulation (EU) 2017/1129 (the “**Prospectus Regulation**”), the Financial Instruments Market Law (in Latvian - *Finanšu instrumentu tirgus likums*) and the Commission Delegated Regulation No 2019/980/EU (the “**Delegated Regulation**”), in particular the Annexes 6 and 14 thereof. The Financial and Capital Market Commission (in Latvian - *Finanšu un kapitāla tirgus komisija*), as competent authority under the Prospectus Regulation, has approved this Base Prospectus and has notified the approval of the Base Prospectus to the competent authority in Lithuania (the Bank of Lithuania (in Lithuanian - *Lietuvos Bankas*)). The Financial and Capital Market Commission only approves this Base Prospectus as meeting the standards of completeness, comprehensibility and consistency imposed by the Prospectus Regulation. Such approval should not be considered as an endorsement of the Issuer nor as an endorsement of the quality of any Notes that are the subject of this Base Prospectus. Investors should make their own assessment as to the suitability of investing in the Notes.

This Base Prospectus is valid for a period of twelve months from the date of approval. The obligation to supplement the Base Prospectus in the event of significant new factors, material mistakes or material inaccuracies does not apply when the Base Prospectus is no longer valid.

Application will be made to Akciju sabiedrība “Nasdaq Riga”, registration number: 40003167049, legal address: Valņu 1, Riga, LV- 1050, Latvia (“**Nasdaq Riga**”) for admitting each Tranche to listing and trading on the official bond list (the Baltic Bond List) of Nasdaq Riga according to the requirements of Nasdaq Riga not later than within 3 (three) months after the Issue Date of the respective Tranche. Nasdaq Riga is a regulated market for the purposes of the Markets in Financial Instruments Directive 2014/65/EU, as amended (“**MiFID II**”).

The Notes shall be issued in the bearer dematerialised form and registered with Nasdaq CSD SE, registration number: 40003242879, legal address: Valņu 1, Riga, LV-1050, Latvia (the “**Depository**”) in book-entry form. Investors may hold the Notes through participants of the Depository, including credit institutions and investment brokerage firms.

The Notes have not been, and will not be, registered under the U.S. Securities Act 1933 (as amended) (the “**Securities Act**”), or with any securities regulatory authority of any state of the United States. This Base Prospectus or the Final Terms are not to be distributed to the United States or in any other jurisdiction where it would be unlawful. The Notes may not be offered, sold, pledged or otherwise transferred, directly or indirectly, within the United States or to, for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act (the “**Regulation S**”)), except to a person who is not a U.S. Person (as defined in Regulation S) in an offshore transaction pursuant to Regulation S.

Investment in the Notes to be issued under the Programme involves certain risks. Prospective investors should carefully acquaint themselves with such risks before making a decision to invest in the Notes. The principal risk factors that may affect the Issuer’s ability to fulfil its obligations under the Notes are discussed in Section “*Risk Factors*” below.

Arrangers and Dealers

Luminor Bank AS

Swedbank AB (publ)

The date of this Base Prospectus is 14 April 2020

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RESPONSIBILITY STATEMENT

This Base Prospectus comprises a base prospectus for the purposes of Article 8 of the Prospectus Regulation and for the purpose of giving information with regard to the Issuer, the Issuer and its subsidiaries taken as a whole (the “**Group**”) and the Notes which, according to the particular nature of the Issuer and the Notes, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses and prospects of the Issuer.

The Issuer, represented by the members of its Management Board, accepts responsibility for the information contained in this Base Prospectus and in any Final Terms which complete this Base Prospectus for each Tranche of Notes issued hereunder and declares that, to the best of its knowledge, the information contained in this Base Prospectus is in accordance with the facts and that the Base Prospectus does not omit anything likely to affect the import of such information.

Management Board of Latvenergo AS:

Chairman of the Management Board
Āris Žīgurs

Member of the Management Board
Guntars Baļčūns

Member of the Management Board
Uldis Bariss

Member of the Management Board
Kaspars Cikmačs

IMPORTANT INFORMATION

To the fullest extent permitted by law, the Arrangers and Dealers accept no responsibility whatsoever for the contents of this Base Prospectus. Each Arranger and Dealer accordingly disclaims all and any liability which it might otherwise have in respect of this Base Prospectus.

Neither the Arrangers and Dealers nor any of their respective affiliates have authorised the whole or any part of this Base Prospectus and none of them make any representation or warranty or accepts any responsibility as to the accuracy or completeness of the information contained in this Base Prospectus or any responsibility for any acts or omissions of the Issuer or any other person in connection with issue and offering of the Notes.

No person is authorised to give any information or to make any representation not contained in this Base Prospectus and any information or representation not so contained must not be relied upon as having been authorised by or on behalf of the Issuer, the Arrangers or the Dealers. Neither the delivery of this Base Prospectus nor any sale made in connection herewith shall, under any circumstances, create any implication that there has been no change in the affairs of the Issuer since the date hereof or the date upon which this Base Prospectus has been most recently amended or supplemented or that there has been no adverse change in the financial position of the Issuer since the date hereof or the date upon which this Base Prospectus has been most recently amended or supplemented or that the information contained in it or any other information supplied in connection with the Notes is correct as of any time subsequent to the date on which it is supplied or, if different, the date indicated in the document containing the same.

Neither this Base Prospectus, any Final Terms nor any other information supplied in connection with the offering of the Notes (a) is intended to provide the basis of any credit or other evaluation or (b) should be considered as a recommendation by the Issuer or any of the Arrangers or Dealers that any recipient of this Base Prospectus, any Final Terms or any other information supplied in connection with the offering of the Notes should purchase any Notes. Each investor contemplating purchasing any Notes should make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of the Issuer. Neither this Base Prospectus nor any other information supplied in connection with the offering of the Notes constitutes an offer or invitation by or on behalf of the Issuer or any of the Arrangers or Dealers, to any person to subscribe for or to purchase any Notes.

Each potential investor in the Notes must make their own assessment as to the suitability of investing in the Notes. In particular, each potential investor should:

- (i) have sufficient knowledge and experience to make a meaningful evaluation of the Notes, the merits and risks of investing in the Notes and the information contained in this Base Prospectus;
- (ii) have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Notes and the impact the Notes will have on its overall investment portfolio;
- (iii) have sufficient financial resources and liquidity to bear all of the risks of an investment in the Notes, including where the currency for principal or interest payments is different from the potential investor's currency;
- (iv) understand thoroughly the terms of the Notes and be familiar with the behaviour of any relevant financial markets; and
- (v) be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (i) Notes are legal investments for it, (ii) Notes can be used as collateral for various types of borrowing and (iii) other restrictions apply to its purchase or pledge of any Notes. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of Notes under any applicable risk-based capital or similar rules.

The Notes are governed by Latvian law and any disputes arising in relation to the Notes shall be settled exclusively by the courts of the Republic of Latvia in accordance with Latvian law.

DISTRIBUTION OF THE BASE PROSPECTUS AND SELLING RESTRICTIONS

The distribution of this Base Prospectus and any Final Terms may in certain jurisdictions be restricted by law, and this Base Prospectus and any Final Terms may not be used for the purpose of, or in connection with, any offer or solicitation by anyone in any jurisdiction in which such offer or solicitation is not authorised or to any person to whom it is unlawful to make such offer or solicitation. No actions have been taken to register or qualify the Notes, or otherwise to permit a public offering of the Notes, in any jurisdiction other than the Republic of Latvia and the Republic of Lithuania. The Issuer, the Arrangers and the Dealers expect persons into whose possession this Base Prospectus or any Final Terms comes to inform themselves of and observe all such restrictions. Neither the Issuer nor the Arrangers or Dealers accept any legal responsibility for any violation by any person, whether or not a prospective purchaser of the Notes is aware of such restrictions. In particular, this Base Prospectus and any Final Terms may not be sent to any person in the United States, Australia, Canada, Japan, Hong Kong, Singapore or any other jurisdiction in which it would not be permissible to deliver the Notes and the Notes may not be offered, sold, resold, transferred or delivered, directly or indirectly, in or into any of these countries.

The Notes have not been, and will not be, registered under the U.S. Securities Act 1933 (as amended) (the “**Securities Act**”), or with any securities regulatory authority of any state of the United States. This Base Prospectus or the Final Terms are not to be distributed to the United States or in any other jurisdiction where it would be unlawful. The Notes may not be offered, sold, pledged or otherwise transferred, directly or indirectly, within the United States or to, for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act (the “**Regulation S**”)), except to a person who is not a U.S. Person (as defined in Regulation S) in an offshore transaction pursuant to Regulation S.

The Financial and Capital Market Commission (in Latvian - *Finanšu un kapitāla tirgus komisija*), as competent authority under the Prospectus Regulation, has approved this Base Prospectus and has notified the approval of the Base Prospectus to the competent authority in Lithuania (the Bank of Lithuania (in Lithuanian - *Lietuvos Bankas*)). However, in relation to each member state of the European Economic Area (the “**EEA**”) (except the Republic of Latvia and the Republic of Lithuania), the Dealers have represented and agreed that they have not made and will not make any public offer of Notes prior to that EEA member state’s authority receiving a certificate of approval of the Financial and Capital Market Commission attesting that the Base Prospectus has been drawn up in accordance with the Prospectus Regulation together with a copy of the Base Prospectus.

Accordingly, any person making or intending to make an offer within the EEA of Notes which are the subject of an offering contemplated by this Base Prospectus and the relevant Final Terms (other than the offer of Notes in the Republic of Latvia and in the Republic of Lithuania) may only do so in circumstances in which no obligation arises for the Issuer or the Dealers to publish a prospectus pursuant to Article 3 of the Prospectus Regulation or supplement a prospectus pursuant to Article 23 of the Prospectus Regulation, in each case, in relation to such offer.

MIFID II PRODUCT GOVERNANCE/TARGET MARKET: The Final Terms in respect of any Notes will include a legend entitled “MiFID II Product Governance” which will outline the target market assessment in respect of the Notes and which channels for distribution of the Notes are appropriate. Any person subsequently offering, selling or recommending the Notes (a “**distributor**”) should take into consideration the target market assessment; however, a distributor subject to MiFID II is responsible for undertaking its own target market assessment in respect of the Notes (by either adopting or refining the target market assessment) and determining appropriate distribution channels.

A determination will be made in relation to each issue about whether, for the purpose of the MiFID Product Governance rules under EU Delegated Directive 2017/593 (the “**MiFID Product Governance Rules**”), any Dealer subscribing for any Notes is a manufacturer in respect of such Notes, but otherwise neither the Arrangers nor the Dealers nor any of their respective affiliates will be a manufacturer for the purpose of the MiFID Product Governance Rules.

IMPORTANT – EEA RETAIL INVESTORS – If the Final Terms in respect of any Notes include a legend entitled “Prohibition of Sales to EEA Retail Investors”, the Notes are not intended to be offered, sold or otherwise made

available to, and should not be offered, sold or otherwise made available to, any retail investor in the EEA. For these purposes, a retail investor means a person who is one (or more) of: (i) a retail client as defined in point (11) of Article 4(1) of MiFID II, (ii) a customer within the meaning of Directive (EU) 2016/97 (as amended or superseded), where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II; or (iii) not a qualified investor as defined in Regulation (EU) 2017/1129 (as amended, the **"Prospectus Regulation"**).

The Notes will have a fixed rate of interest and the redemption amount will be fixed as described in the Base Prospectus. Accordingly, the Notes fall out of scope of Regulation (EU) No 1286/2014 (as amended, the **"PRIIPs Regulation"**) and consequently no key information document will be prepared by the Issuer.

PRESENTATION OF FINANCIAL AND OTHER INFORMATION

With the exception of certain alternative performance measures (“**APMs**”), the financial information as of and for the year ending 31 December 2019 and as of and for the year ending 31 December 2018, included in this Base Prospectus has been derived from the Group's consolidated and the Company's annual report, representing audited consolidated and standalone financial statements for the financial year ending 31 December 2019 prepared in accordance with the International Financial Reporting Standards as adopted by the E.U. (“**IFRS**”) (the “**2019 Financial Statements**”), and the Group's consolidated and the Company's annual report, representing audited consolidated and standalone financial statements for the financial year ending 31 December 2018 prepared in accordance with IFRS (the “**2018 Financial Statements**”, and together with the 2019 Financial Statements, the “**Audited Financial Statements**”).

PricewaterhouseCoopers SIA (“**PwC**”) audited the 2019 Financial Statements and issued an unqualified auditor's report on the aforementioned financial statements. In addition, PwC audited the 2018 Financial Statements and issued an unqualified auditors' report on the aforementioned financial statements.

Changes in accounting policies and presentation of financial information

Discontinued operations

In the 2019 Financial Statements the Company's subsidiary Latvijas elektriskie tīkli AS was classified as a discontinued operation in accordance with IFRS 5, "Non-current Assets Held for Sale and Discontinued Operations". In the Statement of Financial Position the Group presented assets, reserves and liabilities held for distribution and in the Statement of Profit or Loss – profit from discontinued operations for the year 2019. Comparative information for 2018 in the Statement of Profit or Loss was also restated to present profit for discontinued operations.

In the Group's operating segments, financial results of Latvijas elektriskie tīkli AS are disclosed in transmission system assets lease segment because the Management Board of the Company will continue to review financial results of this operating segment until the termination of its ownership.

IFRS 16 implementation

The Group and the Company have applied IFRS 16 Leases in 2019 Financial Statements with an initial application date as of 1 January 2019. As lessees, the Group and the Company adopted IFRS 16 by recognising in the 2019 Financial Statements the right-of-use assets and lease liabilities. Upon implementation of IFRS 16, the Group and the Company made an assessment of the identified right-of-use assets, non-cancellable lease terms and lease payments. The Group and the Company use a single accounting model for all lease contracts. 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.

For further information please see Note 2 in the 2019 Financial Statements. Due to change in presentation of comparative information for 2018, for purposes of this Base Prospectus financial data for 2019 and 2018 is disclosed in accordance with revised presentation, derived from the 2019 Financial Statements.

Alternative performance measures

This Base Prospectus includes certain references to APMs derived from the Group's Financial Statements such as EBITDA, net debt, return on equity (ROE), net debt to equity and net debt to EBITDA. The Group uses these APMs to evaluate its performance, and this additional financial information is presented in this Base Prospectus. This information should be viewed as supplemental to the Audited Financial Statements. Investors are cautioned not to place undue reliance on this information and should note that the APMs, as calculated by the Group, may differ materially from similarly titled measures reported by other companies, including the Group's competitors.

The APMs presented in this section are not defined in accordance with IFRS. An APM should not be considered in isolation from, or as substitute for any analysis of, financial measures defined according to IFRS. Investors

are advised to review these APMs in conjunction with the Audited Financial Statements contained in this Base Prospectus.

The following tables present the selected APMs of the Group for the indicated periods or as of the indicated dates:

| | | Year ended 31 December | | | | |
|---------------------------------|-----------|------------------------|------|------|------|------|
| | | 2015 | 2016 | 2017 | 2018 | 2019 |
| EBITDA * | € million | 263 | 347 | 498 | 282 | 244 |
| Net Debt (adjusted) * | € million | 605 | 529 | 497 | 505 | 564 |
| Return on equity (ROE) | per-cent | 4.1 | 5.8 | 12.2 | 2.9 | 4.1 |
| Net debt to equity (adjusted) * | per-cent | 29 | 22 | 17 | 22 | 25 |
| Net debt to EBITDA (adjusted) * | | 2.3 | 1.6 | 1.0 | 1.8 | 2.2 |

(*) Excluding discontinued operations (transmission system assets). On 8 October 2019, the Cabinet of Ministers of the Republic of Latvia decided to support full unbundling of ownership of the electricity transmission system operator until 1 July 2020.

EBITDA, net debt, return on equity (ROE), net debt to equity and net debt to EBITDA measures should not be used instead of, or considered as alternatives to, the Group's consolidated historical financial results based on IFRS. The non-IFRS measures relate to the reporting periods and are not meant to be predictive of future results. Management of the Group uses EBITDA, net debt, return on equity (ROE), net debt to equity and net debt to EBITDA measures because the Issuer believes that these measures are commonly used by lenders, investors and analysts.

These measures are presented for purposes of providing investors with a better understanding of the Issuer's financial performance, cash flows or financial position as they are used by the Issuer when managing its business.

EBITDA

EBITDA should not be considered as alternative to profit before tax as defined by IFRS or to cash flows from operating activities (or any other performance measure determined in accordance with IFRS) or as indicator of operating performance or as measure of the Group's liquidity. In particular, EBITDA should not be considered as measures of discretionary cash available to the Group to invest in the growth of the Group's businesses.

EBITDA has certain limitations as an analytical tool, and should not be considered in isolation, or as a substitute for financial information as reported under IFRS. Investors should not place undue reliance on this data. EBITDA in this Base Prospectus is presented, for each period, as: earnings before interest, corporate income tax, share of profit or loss of associates, depreciation and amortisation, and impairment of intangible and fixed assets, excluding discontinued operations (ownership unbundling of transmission system assets).

No statement in this Base Prospectus is intended as a profit/EBITDA forecast and no statement in this Base Prospectus should be interpreted to mean that the earnings of the Group for the current or future years would necessarily match or exceed the historical published earnings of the Group.

The table below presents reconciliation of EBITDA to the net profit:

| | | Year ended 31 December | | | | |
|-------------------------------------|-----------|------------------------|------|------|------|------|
| | | 2015 | 2016 | 2017 | 2018 | 2019 |
| Net profit | € million | 85 | 131 | 322 | 76 | 94 |
| Profit from discontinued operations | € million | 19 | 10 | 52 | 10 | 10 |
| Income tax* | € million | (6) | (18) | 65 | (9) | (8) |
| Finance costs, net* | € million | (16) | (12) | (10) | (7) | (8) |

| | | | | | | |
|---|------------------|------------|------------|------------|------------|------------|
| Depreciation, amortisation and impairment of intangible assets and property, plant and equipment* | € million | (175) | (196) | (283) | (200) | (143) |
| EBITDA* | € million | 263 | 347 | 498 | 282 | 244 |

(*) Excluding discontinued operations (transmission system assets). On 8 October 2019, the Cabinet of Ministers of the Republic of Latvia decided to support full unbundling of ownership of the electricity transmission system operator until 1 July 2020.

Net Debt (adjusted)

Net debt consists of borrowings at the end of the year, less the amount of Latvijas Elektriskie tīkli AS borrowings at the end of the year, less cash and cash equivalents, excluding Latvijas Elektriskie tīkli AS cash and cash equivalents at the end of the year. It is used for the purpose of calculating the debt ratio by which the Group monitors its capital.

The following table illustrates the methodology the Group uses to determine its net debt:

| | | Year ended 31 December | | | | |
|--|------------------|------------------------|--------------|--------------|--------------|--------------|
| | | 2015 | 2016 | 2017 | 2018 | 2019 |
| Borrowings | € million | 797.5 | 791.6 | 826.7 | 814.3 | 882.7 |
| Less Latvijas elektriskie tīkli AS borrowings from the Company | € million | 88.1 | 78.9 | 95.5 | 179.7 | 196.3 |
| Less Cash and cash equivalents* | € million | 104.6 | 184.0 | 236.0 | 129.5 | 122.7 |
| Plus Latvijas elektriskie tīkli AS Cash and cash equivalents | € million | 0.3 | 0.3 | 1.5 | 0.3 | 0.3 |
| Net Debt (adjusted)* | € million | 605.1 | 529.0 | 496.7 | 505.4 | 564.0 |

(*) Excluding discontinued operations (transmission system assets). On 8 October 2019, the Cabinet of Ministers of the Republic of Latvia decided to support full unbundling of ownership of the electricity transmission system operator until 1 July 2020.

Return on equity (ROE)

Return on equity (ROE) is the ratio of net profit at the end of the year to the average value of total equity at the beginning and the end of the year. Return on equity (ROE) is a measure of profitability of the equity. It is a measure of efficiency of equity usage in profit generation of the Group.

Net Debt to Equity (adjusted)

Net debt to equity is the ratio of net debt at the end of the year to equity at the end of the year and is used as a measure of both indebtedness and borrowing capacity.

Net Debt to EBITDA (adjusted)

Net debt to EBITDA is the ratio of the average value of net debt at the beginning and the end of the year divided by 12-months rolling EBITDA and is used as a measure of financial leverage and the Group's ability to pay off its debt. Essentially, the net debt to EBITDA ratio gives an indication as to how long the Group's would need to operate at its current level to pay off all its debt.

Rounding

Certain figures included in this Base Prospectus have been subject to rounding adjustments; accordingly, figures shown for the same category presented in different tables may vary slightly and figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

Currencies

In this Base Prospectus, financial information is presented in euro (EUR), the official currency of the European Union Member States in the Eurozone.

Date of information

This Base Prospectus is drawn up based on information which was valid as of the date of the Base Prospectus. Where not expressly indicated otherwise, all information presented in this Base Prospectus (including the consolidated financial information of the Group, the facts concerning its operations and any information on the markets in which it operates) must be understood to refer to the state of affairs as of the aforementioned date. Where information is presented as of a date other than the date of the Base Prospectus, this is identified by specifying the relevant date.

Certain publicly available information

Certain statistical data and other information appearing in this Base Prospectus have been extracted from public sources identified in this Base Prospectus. None of the Arrangers, the Dealers or the Issuer accepts responsibility for the factual correctness of any such statistics or information, but the Issuer accepts responsibility for accurately extracting and transcribing such statistics and information and believes, after due inquiry, that such statistics and information represent the most current publicly available statistics and information from such sources at the dates and for the periods with respect to which they have been presented. The Issuer confirms that all such third-party information has been accurately reproduced and, so far as the Issuer is aware and has been able to ascertain from that published information, no facts have been omitted which would render the reproduced information inaccurate or misleading.

Websites

Information contained in any website referred to herein does not form part of this Base Prospectus, other than the Issuer's Green Bond Framework, which is available for viewing on the following website: www.latvenergo.lv/lv/investoriem and is incorporated by reference to this Base Prospectus and forms a part of the Base Prospectus.

FORWARD-LOOKING STATEMENTS

This Base Prospectus includes statements that are, or may be deemed to be, “forward-looking statements”. These forward-looking statements may be identified by the use of forward-looking terminology, including the terms “believes”, “estimates”, “plans”, “projects”, “anticipates”, “expects”, “intends”, “may”, “will” or “should” or, in each case, their negative or other variations or comparable terminology, or by discussions of strategy, plans, objectives, goals, future events or intentions. These forward-looking statements include all matters that are not historical facts. They appear in a number of places throughout this Base Prospectus and include, but are not limited to, statements regarding the Group’s or the Issuer’s intentions, beliefs or current expectations concerning, among other things, the Group’s results of operations, financial condition, liquidity, prospects, growth, strategies and the industry in which the Group operates.

By their nature, forward-looking statements involve risk and uncertainty because they relate to future events and circumstances. Forward-looking statements are not guarantees of future performance and the financial position and results of operations of the Group, and the development of the markets and the industries in which members of the Group operate, may differ materially from those described in, or suggested by, the forward-looking statements contained in this Base Prospectus. In addition, even if the Group’s results of operations and financial position, and the development of the markets and the industries in which the Group operates, are consistent with the forward-looking statements contained in this Base Prospectus, those results or developments may not be indicative of results or developments in subsequent periods. A number of risks, uncertainties and other factors could cause results and developments to differ materially from those expressed or implied by the forward-looking statements. See Section “*Risk Factors*” below.

These forward-looking statements are made only as of the date of this Base Prospectus. Except to the extent required by law, the Issuer is not obliged to, and does not intend to, update or revise any forward-looking statements made in this Base Prospectus whether as a result of new information, future events or otherwise. All subsequent written or oral forward-looking statements attributable to the Issuer, or persons acting on the Issuer’s behalf, are expressly qualified in their entirety by the cautionary statements contained throughout this Base Prospectus. As a result of these risks, uncertainties and assumptions, a prospective purchaser of the Notes should not place undue reliance on these forward-looking statements.

OVERVIEW OF THE PROGRAMME

The following overview does not purport to be complete and is taken from, and is qualified in its entirety by, the remainder of this Base Prospectus and, in relation to the General Terms and Conditions of any particular Tranche of Notes, the applicable Final Terms. This overview must be read as an introduction in conjunction with the other parts of the Base Prospectus (including any documents incorporated therein). Any decision to invest in the Notes should be based on a consideration by the investor of the Base Prospectus as a whole.

Words and expressions defined in “General Terms and Conditions of the Notes” below or elsewhere in this Base Prospectus have the same meanings in this overview.

This overview constitutes a general description of the Programme for the purposes of Article 25(1) of the Delegated Regulation.

| | |
|---------------------------------------|---|
| Issuer: | Latvenergo AS |
| Legal Entity Identifier (LEI): | 213800DJRB539Q1EMW75 |
| Programme Limit: | Up to EUR 200,000,000 aggregate nominal amount of Notes outstanding at any one time. |
| Risk Factors: | Investing in Notes issued under the Programme involves certain risks. The principal risk factors that may affect the ability of the Issuer to fulfil its obligations under the Notes are discussed in Section “ <i>Risk Factors</i> ” below. |
| Arrangers or the Programme: | Luminor Bank AS Swedbank AB (publ) |
| Dealers: | Luminor Bank AS Swedbank AB (publ) |
| Method of Issue: | The Notes shall be issued in Series. Each Series may comprise one or more tranches of Notes. The Notes of each Tranche will all be subject to identical terms, except that the Issue Dates and the Issue Prices thereof may be different in respect of different Tranches. |
| Form of the Notes: | The Notes will be issued in dematerialized form and book-entered with Nasdaq CSD SE. |
| Status and Security: | The Notes constitute direct, unsecured and unguaranteed obligations of the Issuer ranking <i>pari passu</i> without any preference among each other and with all other unsecured, unguaranteed and unsubordinated indebtedness of the Issuer, save for such obligations as may be preferred by mandatory provisions of law. |
| Currency: | EUR |
| Denomination: | The nominal amount of each Note shall be specified in the Final Terms. |
| Issue Price: | The Notes may be issued at their nominal amount or at a discount or a premium to their nominal amount. |
| Minimum Investment Amount: | The Notes will be offered for subscription for a minimum investment amount EUR 100,000 (one hundred thousand euro). |
| Interest: | The Notes will bear interest at a fixed annual interest rate. |

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| Maturity: | The Notes shall be repaid in full at their nominal amount on the date which will be specified in the Final Terms. Each Series of Notes may have a maturity up to 10 (ten) years. |
| Early Redemption: | The Issuer is entitled to redeem each Series of Notes, in whole but not in part, at any time during the period of 3 (three) month prior to their maturity at a price equal to the nominal amount of the Notes together with the accrued interest, as more fully set out in Clauses 9.3 and 9.4 of the General Terms and Conditions of the Notes. |
| Redemption for tax reasons: | The Issuer is entitled to redeem the Notes, in whole but not in part, at a price equal to the nominal amount of the Notes together with the accrued interest for tax reasons as described in Clause 11. |
| Change of Control: | Following the occurrence of a Change of Control the Noteholders will be entitled to request the Issuer to redeem or, at the Issuer's option, procure the purchase of their Notes, as more fully set out in Clause 14 of the General Terms and Conditions of the Notes. |
| Negative Pledge: | The Notes will have the benefit of a negative pledge as described in Clause 15 of the General Terms and Conditions of the Notes. |
| Cross Default: | The Notes will have the benefit of a cross default provision as described in Clause 16 of the General Terms and Conditions of the Notes. |
| Listing: | Application will be made to Nasdaq Riga for admitting each Tranche to listing and trading on the official bond list (the Baltic Bond List) according to the requirements of Nasdaq Riga not later than within 3 (three) months after the Issue Date of the respective Tranche. |
| Taxation: | All payments in respect of the Notes by the Issuer shall be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature (" Taxes "), unless the withholding or deduction of the Taxes is required by the laws of the Republic of Latvia. In such case, the Issuer shall pay such additional amounts as will result in receipt by the Noteholders after such withholding or deduction of such amounts as would have been received by them had no such withholding or deduction been required, except that no such additional amounts shall be payable in respect of any Note held by or on behalf of a Noteholder which is liable to such Taxes in respect of such Note by reason of its having some connection with the Republic of Latvia other than the mere holding of the Note. |
| Rating: | <p>As of the date of this Base Prospectus, the Issuer has a credit rating Baa2 by Moody's. The outlook is stable. A Series of Notes to be issued under the Programme may be rated or unrated.</p> <p>A rating is not a recommendation to buy or sell or hold Notes and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency. Up-to-date information should always be sought by direct reference to the relevant rating agency.</p> |
| Governing Law: | Latvian law. |
| Dispute Resolution: | Any disputes relating to or arising in relation to the Notes shall be settled solely by the courts of the Republic of Latvia of competent jurisdiction. |
| Selling Restrictions: | For a description of certain restrictions on offers, sales and deliveries of Notes and on the distribution of the Base Prospectus in the United States of America, the EEA (with respect to retail investors), the Republic of Latvia, the Republic of Lithuania and other jurisdictions, see Section " <i>Distribution of the Base Prospectus and Selling Restrictions</i> ". |

RISK FACTORS

Prospective investors are advised to carefully consider the risk factors and other information provided in this Base Prospectus. Investing in the Notes involves certain risks including but not limited to the risks described herein.

The Issuer believes that if one or more of the risk factors described herein emerges, it could have a negative effect on the Issuer's business operations, financial position and/or business results and, thereby, the Issuer's ability to fulfil its obligations under the Notes as well as the market price and value of the Notes. If these risks were to lead to a decline in the market price of the Notes, prospective investors could lose all or part of their investment.

The risks and uncertainties described herein are the risks which the Issuer has deemed material; however, they are not the only factors affecting the Issuer's activities. Therefore, the Issuer does not claim that the statements below regarding the risks of acquiring and/or holding any Notes are exhaustive. Also, other factors and uncertainties than those mentioned herein, which are currently unknown or deemed immaterial, could negatively affect the Issuer's business operations, financial position and/or business results and, thereby, the Issuer's ability to fulfil its obligations under the Notes as well as the market price and value of the Notes.

Most of these risk factors are contingencies which may or may not occur and the Issuer is not in a position to assess or express a view on the likelihood of any such contingency occurring.

The most material risk factors have been presented at the beginning in each category. The order of presentation of the remaining risk factors in each category in this Base Prospectus is not intended as an indication of the probability of their occurrence or of their potential effect on the Issuer's ability to fulfil its obligations under the Notes.

All investors should make their own evaluations of the risks associated with an investment in the Notes and should consult with their own professional advisers if they consider it necessary.

Risks related to macroeconomic conditions

Exposure of business results to macroeconomic developments

The results of the Group's operations are dependent on Latvia's macroeconomic situation. In particular, the Group's operations are affected by such factors as the level of Latvia's GDP, the level of industrial production, the rate of inflation, fuel prices, the unemployment rate, changes in consumer affluence levels, and the fiscal policy of the Republic of Latvia. The Baltic region is a small open economy that is closely linked to the global economy and especially to the macroeconomic conditions in the Eurozone countries and global developments.

The Group's expansion into neighbouring energy markets creates growing exposure of its business and financial results to regional and international macroeconomic developments. The Group's business is influenced by electricity price trends in local and Nordic markets, commodities prices (including, but not limited to, natural gas and oil), consumer behaviour and electricity demand in the Baltic countries, and other indices that may reflect local and global macroeconomic trends and have a material adverse effect on the Group's business and financial position.

The Group has a strong balance sheet and operates in a relatively non-cyclical or late-cyclical industry. However, an unexpected downturn in the economy could have an impact on the Group's customers and negatively affect its growth and results of operations through reduced electricity consumption. Also, households' capability to fulfil their obligations towards the Group may deteriorate, which could lead to an increase in the Group's overdue portfolio, creating adverse effect on the Group's business and financial position.

In addition, the rapid spread of coronavirus Covid-19 poses major challenges to the global economy, including the economy of Latvia and the extent of the potential economic impact will largely depend on the scale and duration of the virus.

Covid-19 has affected investment sentiment on a global scale, causing a significant volatility in the global capital markets. In addition, the outbreak has resulted in restrictions on international travel and public transport, delays in transportation of goods, and prolonged closures of workplaces which may have a material adverse effect on the global economy and Latvia.

A state of emergency has been declared in Latvia until 12 May 2020 and Latvia has taken a number of temporary preventative measures to contain the outbreak and slow the spread of Covid-19, including implementing restrictions on international travel, restrictions on gatherings of groups of people and the closure of universities, schools and other public institutions. On 20 March 2020, a special fixed-term law on measures for preventing and overcoming the national threat and the consequences thereof related to the spread of Covid-19 stipulating a special support mechanisms and crisis expenditure directly related to financing the containment was approved by the Saeima. The law will take effect retrospectively as of 12 March 2020, when the state of emergency was declared in Latvia. However, the efficacy of any preventive measures may be insufficient to contain the spread of Covid-19 in Latvia and limit its impact on Latvia and its economy.

As of March 2020, certain sectors of the economy of Latvia are being significantly affected, including, but not limited to, tourism, and the accommodation and transport sector, especially, airport traffic.

While the final effects of Covid-19 pandemic are at this stage difficult to assess, it is possible that it will have substantial negative effect on the economies where the Group operates in and may also take place in future in case of any possible future outbreaks. Any negative effect on the economy may decrease incomes of the Group's customers and the demand for the Group's products. Such effects may also result in insolvency of the Group's business partners, which could affect the operations of the Group, as well as its financial standing. Lastly, in case of an economic downturn, the price of the Notes and the ability of the Group to acquire further financing may be adversely affected. The Group considers the outbreak of Covid-19 to be a non-adjusting post balance sheet event for 2019. As the situation is uncertain and rapidly evolving, the Company does not consider practicable to provide a quantitative estimate of the potential impact of this outbreak on the Group.

The Group's estimate for the exposure of business results to macroeconomic developments is medium.

Risks related to strategy

Capital investment projects risk

The Group has a capital investment programme, aimed at upgrading the Group's generating facilities, as well as its transmission and distribution system assets.

The Group has commenced an upgrading of the Daugava hydropower plants (the "HPPs"). The project includes reconstruction of 21 hydro units in 3 HPPs and is scheduled for completion in 2023.

The main areas of investment in the distribution segment are restoration of power lines, reconstruction of transformer substations, installation of remote-controlled circuit breakers and fault location detectors. The Group commenced the "*smart electricity meters*" project in 2014, which is scheduled for completion in 2022, and will improve customer awareness of electricity consumption and promote electricity consumption efficiency and cost reduction for the distribution system operator, customers and electricity traders.

The largest investment projects in the transmission system's development, until complete ownership unbundling of transmission system assets, are the third Latvia–Estonia transmission network interconnection project and the power transmission line Riga CHPP-2 – Riga HPP project, which are scheduled for completion by the end of 2020. Both projects are co-financed by the European Union, and there is a risk that failure to meet co-financing requirements could lead to a request for reimbursement of the co-financing.

There is a risk, that cost overruns and project delays or similar aspects related to the execution of current or future capital investment projects could have a material adverse effect on the Group's business and financial position.

Besides the above-mentioned projects, the Group may implement other capital-intensive investment and maintenance projects that could increase its exposure to operational and/or financial risk levels or negatively impact its value or reputation, thus creating an adverse effect on its business and financial position.

The Group's estimate for the capital investment project risk profile is medium.

Strategic decision risk

Strategic decisions risk is a possible source of loss that might arise from the pursuit of faulty strategic decisions when entering into the new markets or new businesses.

Simultaneously with the opening of the electricity markets in neighbouring countries Estonia and Lithuania, the Group commenced its operations in these markets. There are risks and opportunities inherent to the further developments of these markets, such as an expected increase in the number of clients switching between electricity suppliers and possible changes in the legal environment, which could influence the Group's operations. The market share in the Baltic countries indicates the Group's current standing, but there is a risk that the market share could decrease or that the Group could be unable to attain its anticipated market share growth, thus causing adverse effects on its business and financial position. Furthermore, there is also a risk of exiting any of the current markets subject to various reasons, including economic and strategic, as well as suffering losses upon entering new markets. This could affect the Group's operations and financial position.

With increased competition in energy trading, the Group is ready to invest in a new business and develop new products or services that complement traditional ones, promoting synergies with the existing businesses and customer base. After careful evaluation of the electricity market and entry barriers, the Group is ready to start electricity trading in its geographically closest markets – the Nordic countries, Poland and Lithuania, offering existing products. The Group may also face risks related to failure to introduce new technology and new products, given the rapid evolution of the energy sector.

The Group's strategic risk is mitigated through business plans and analyses, as well as engaging experienced professionals from the energy sector. Furthermore, entries into new markets and businesses are preceded by an analysis and engaging experts in the particular field. However, despite the measures taken by the Group, the materialisation of strategic decision risk could have a material adverse effect on the Group's operations, financial condition and results of operations.

The Group's estimate for the strategic decisions risk profile is medium.

Corporate governance risk

The sole shareholder of the Company is the Republic of Latvia and the rights and duties of the shareholder are awarded to the Ministry of Economics of the Republic of Latvia. Certain and substantial shareholder's decisions altering the Group's strategy or decisions in respect of dividend policy, capital structure and other relevant issues could have a material adverse effect on the Group.

The Law on the Management of Public Persons' Capital Shares and Capital Companies (in Latvian - *Publiskas personas kapitāla daļu un kapitālsabiedrību pārvaldības likums*), stipulates formation of the Supervisory Board as a supervisory body in large state-owned companies. The Company and the Company's subsidiaries Sadales tīkls AS and Latvijas elektriskie tīkli AS all qualify in this category. The Supervisory Board approves the Group's strategy, major investment decisions, development plans, and key policies and elects and recalls members of the Management Board. At the date of this Base Prospectus the Company has three Members of the Supervisory Board, however, in August 2019, the Ministry of Economics as the Shareholder of the Company announced a tender for five positions of Members of the Supervisory Board of the Company. Changes in the composition of the Supervisory Board may influence the Company's currently selected strategic direction, development plans, goals and policies, lower risk aversion, thus adversely affecting the Group.

The management of the Group is ensured by the Company's Management Board, whose main duties include defining the Group's strategic development plans, goals and policies. The term of office for three of the four

current members of the Company's Management Board expires on 3 November 2020. Replacement of some or all of the current members of the Company's Management Board could negatively influence the Company's strategic direction, development plans, goals and policies, thus adversely affecting the Group.

The Group's estimate for the corporate governance risk profile is low.

Operational Risks

Daugava hydropower plant geotechnical failure risk

Most of the electricity produced by the Company comes from the three largest HPPs in the country - Plavinas HPP, Riga HPP and Kegums HPP. Operating hydro facilities includes operational risks that can lead to physical damage, technical disruptions, third-party liabilities, environmental issues and other damage or loss events. To manage such risks, the Company continuously monitors the condition of the dams and performs regular inspections and measurements to ensure their safety. There is a systematic long-term investment programme ("*Safety improvement action plan*") to ensure that the dams are maintained in an appropriate condition and to transfer risks to the insurance market, where such insurance is commercially available. In certain circumstances adequate insurance coverage may not be available, as a result of either a lack of relevant insurance or excessive costs. In addition, insurance proceeds received may be inadequate to fully cover replacement costs for damaged assets, sequential financial losses due to business interruption, liabilities to third parties, and similar costs and expenses associated with such asset damages. Despite the measures taken, no assurance can be given that an HPP geotechnical failure will not occur in the future. Should such risk materialise, it could result in a compensation of damages and additional operating costs for the Group, thus adversely affecting the Group's financial position and the Issuer's ability to fulfil its obligations under the Notes.

The Group's estimate for the Daugava hydropower plant geotechnical failure risk profile is high.

Combined heat and power plant damage risk

Most of the Company's thermal energy generation volume is generated by two combined heat and power plants (the "**CHPPs**"). In the case of a fire or explosion in a CHPP, there is a risk of losing either the entire CHPP or a single power unit. To minimize such risks, the Company continuously monitors the condition of the CHPPs, performs regular inspections and measurements to ensure their safety and transfers risks to the insurance market, where such insurance is commercially available. In certain circumstances adequate insurance coverage may not be available, as a result of either a lack of relevant insurance or excessive costs. In addition, insurance proceeds received may be inadequate to fully cover replacement costs for damaged assets, sequential financial losses due to business interruption, liabilities to third parties, and similar costs and expenses associated with such asset damages. Should such risk materialise, it could result in a compensation of damages and additional operating costs for the Group, thus adversely affecting the Group's financial position and the Issuer's ability to fulfil its obligations under the Notes.

The Group's estimate for the CHPP damage risk profile is high.

Electricity distribution/transmission infrastructure damage risk

Major risks related to distribution / transmission (power lines and 330 kV and 110 kV substations, until complete ownership unbundling of transmission system assets) infrastructure failures include mass failures in the distribution / transmission infrastructure caused by atmospheric surges, branches or trees falling on power lines or power equipment, strong winds, ice, and rapid changes in air temperature. Based on the experience of the last 20 years, the largest mass failures in the distribution infrastructure occurred in 2005 and 2010/2011. To minimize the risk, there is a long-term investment programme for electricity distribution / transmission infrastructure renovation and reconstruction. In addition, the Group also transfers risks to the insurance market, where such insurance is commercially available. In certain circumstances, adequate insurance coverage may not be available, as a result of either a lack of relevant insurance or excessive costs. In addition, insurance proceeds received may be inadequate to fully cover replacement costs for damaged assets, sequential financial losses due to business interruption, liabilities to third parties, and similar costs and expenses

associated with such asset damages. Should such risk materialise, it could result in a compensation of damages and additional operating costs for the Group, thus adversely affecting the Group's financial position and the Issuer's ability to fulfil its obligations under the Notes.

The Group's estimate for the electricity distribution/transmission infrastructure damage risk profile is medium.

Energy market price fluctuation risk

The Company operates a vertically integrated power portfolio. At the first instance the generation assets are used to cover the open retail fixed price commitments. Where the market price risk is covered by the production of the CHPPs, the natural gas procurement costs and carbon emission costs are hedged forward. The Group's electricity generation portfolio does not fully cover the needs of the electricity supply portfolio, thus throughout the year approximately one third of the Group's annual electricity supply to the retail sector is subject to market price risk. The Group uses financial derivative contracts to mitigate electricity market price risk for the part of its supply portfolio without generation asset coverage and for fixing of natural gas procurement costs.

Hedging is an efficient way to protect the Group against unfavourable changes in energy market prices. However, currently the availability of hedging instruments in the Baltic markets is limited due to low liquidity in the electricity derivatives' market, and for that reason hedging costs might be high. Therefore, the Group implements a proxy hedging strategy where Nordic system futures contracts and Finnish area price contracts are used for hedging the market price risk. In recent years Nordic-Baltic market interconnectivity has increased with the opening and stabilisation of operations of new transmission capacities between Lithuania and Sweden. The Nordic and Baltic markets are demonstrating greater price convergence, thus a proxy hedge effectively closes the market price risk for the Group's retail portfolio. Since usually the pricing of natural gas physical deliveries are based on German (Gaspool) or Dutch (TTF) Month ahead indices, Gaspool and/or TTF swap contracts are used for fixing the price for major part of the planned natural gas procurement.

Usually the Group has hedged the market price risk for most of its electricity sales portfolio.

Notwithstanding this, there is a risk that hedging will not provide the required efficiency. This could have a material adverse effect on the Group's financial position.

The Group's estimate for the energy market price fluctuation risk profile is medium.

Seasonality and climate changes

The Group's core business operations, particularly electricity generation at the HPPs and the CHPPs, are influenced by weather conditions. The HPPs' ability to generate electricity is dependent on the water inflow in the Daugava River; thus, total electricity generation volumes fluctuate annually. Effective operation of the CHPPs is largely dependent on thermal energy consumption, which is affected by weather conditions, i.e. external air temperature and duration of the heating season.

Due to this, the Group's overall financial position may be influenced by seasonality, weather fluctuations, and long-term shifts in climate affecting electricity generated at the HPPs and/or the number of working hours of the CHPPs operating in an effective cogeneration mode. A decrease in the annual water inflow volume in the Daugava River below long-term average flow level and/or untypically mild weather conditions during autumn and winter months could result in a reduced volume of annual electricity generation at the Group's power plants, exposing the Group to electricity procurement price risk and lower profitability margins. Long-term shifts in climate conditions could result in more permanent changes to the generation patterns and thus create an adverse effect on the Group's business and financial position.

The Group's estimate for the seasonality and climate risk profile is medium.

Covid-19 pandemic and possible similar future outbreaks

Different regions in the world have from time to time experienced outbreaks of various viruses. At this time, a wide-spread global pandemic of coronavirus Covid-19 (COVID-19), is taking place. As the virus and the

diseases it causes are relatively new, effective cure and vaccines are yet to be developed. While COVID-19 is still spreading and the final implications of the pandemic are difficult to estimate at this stage, it is clear that it will affect the lives of a large portion of the global population and cause significant effects. At this time, the pandemic has caused state of emergencies being declared in various countries, travel restrictions being imposed, quarantines been established and various institutions and companies being closed.

The ongoing Covid-19 pandemic and any possible future outbreaks of viruses may have a significant adverse effect on the Group. Firstly, a spread of such virus amongst the employees of the Group and any quarantines affecting the employees of the Group or the Group's facilities, may reduce the ability of the Group's personnel to carry out their work and thereby affect the Group's operations. Secondly, any quarantines or spread of viruses may affect the ability of the customers of the Group to carry out their operations, which may adversely affect the volume of energy consumption and credit risk exposure, thus create adverse effect on the Group's business and financial position.

The Group's estimate for the Covid-19 pandemic and possible similar virus risk profile is medium.

Information systems, communication network infrastructure and cyber-attack risks

An important element of the Group's operations is *the Latvenargo Corporate Network* (data and voice transmission services) consisting of backbone cables, access cables, radio towers and radio masts, communication rooms, a data transmission channel, and other network related equipment. The main factors that could critically affect *the Latvenargo Corporate Network* are physical damage (optical fibre and copper cable damage), technological failures (network equipment damage, software errors), power failure (interruptions, overvoltage effects), fire, floods, human error, third party malicious actions, cyber-attacks and a distributed denial of service attack on the Company's Internet resources.

The Group has developed, procured and uses a variety of off-the-shelf and custom-made information systems (IS) and web-based solutions in carrying out its everyday business operations and providing services to its customers. The main factors that could lead to total or partial loss of IS data are physical infrastructure damage (server, backup, disk array), technological failures, software failures, power failure (power outages, power surges), fire, floods, natural disasters, human error, third party failures to perform their duties (supplying faulty software or hardware, failing to provide support or maintenance service), distributed denial of service attack, cyber attacks, viruses, ransomware, and other forms of malware.

The Group has made significant investments in developing well-functioning and secure IS and is constantly working on improving such systems and developing adequate contingency procedures:

- IS infrastructure is located in several data centres;
- various IS virtualization technologies are used;
- backup of IS according to data backup and a maintenance plan of every IS;
- regular continuity tests of IS.

The Group applies the contingency procedures mentioned above and this reduces the probability of the risk; however, the continuity tests are not able to assess all possible scenarios, and there is a possibility of system unavailability or breakdown. Breakdowns and interruptions in the IS could jeopardize the Group's operations, causing errors in the execution of transactions, loss of customers, production breakdowns and other business interruptions.

The organizational complexity of the Group exposes the Group's assets to the risk of cyber-attack or threats of intentional disruption. The Group manages cyber security activities, which provide for the involvement of the relevant business areas, compliance with legal requirements and recommendations and the use of the best available technologies, yet the Group could be subject to cyber-attack and other security threats to its IS. In such circumstances, the Group could be unable to continue conducting its business in an effective manner, or to prevent, respond promptly and adequately to or mitigate the adverse effects of breakdowns or interruptions

in its IS infrastructure, with possible adverse effects on its reputation, financial condition, assets, business, and results of operations.

The Group's estimate for the IS, communication network infrastructure and cyber-attack risk profile is medium.

Environmental, health and safety risks

The Group's core business activities, such as electricity generation, distribution and lease of transmission system assets include operations with certain assets, mixtures, substances and processes that inherently have increased levels of riskiness, thus exposing the Group's personnel, third parties and the environment to potential damages or harm due to operational accidents or other sudden and unforeseen occurrences. Certain technological processes, including, but not limited to, the operation of the CHPPs and the HPPs, the operation of electricity transmission and distribution system assets and other processes, involve materials, mixtures or substances that are potentially dangerous in uncontrolled chemical processes, such as fires, explosions, emissions, major accidents or failures of equipment or structures. The consequences of an uncontrolled release of dangerous substances or other environmental risks, such as subsequent loss mitigation activities and clean-up costs, fines, penalties and similar costs imposed in accordance with relevant legislation, third party claims and other legal actions could adversely affect the Group's business and financial position.

The Group has made substantial investments into technologies and processes and takes risk mitigation measures, aimed at minimising any negative impact on the environment. Furthermore, the introduction of new legislative initiatives aimed at minimising environmental impact could impose additional costs on the Group.

The Group's personnel, as well as the personnel of the Group's subcontractors are exposed to increased health and safety risks by operating certain assets of the Group. Notwithstanding that the Group has implemented a wide array of activities and procedures aimed at mitigation of occupational health and safety risks, third party claims or claims by the Group's personnel in relation to personal damage or harm caused at the workplace could incur substantial costs to the Group, as well as negative publicity, leading to a material adverse effect on the Group.

The Group's estimate for the environmental, health and safety risk profile is medium.

Counterparty risk

Counterparty risk is inherent to all business activities the Group is engaged in. A counterparty's financial distress or suspension of its operation by any governmental and/or other institutional body due to, among other things, enforced economic sanction laws, regulations or embargoes could have a material adverse effect on the Group's business and/or financial position. Counterparty risk could result in material financial losses to the Group, including, but not limited to, revenues not being received from customers, the Group's own funds not being accessible in its current accounts, committed funding not being available, committed capital expenditure projects being suspended or delayed, etc. Suspension of or material delay in any counterparty's committed capital expenditure project that is significant in nominal amount could harm not only the Group's financial position but also its business operations, thus further affecting the quality of services provided by the Group itself or harming the Group's reputation.

The Group assesses its counterparties to mitigate risk. There are internal procedures in place for identifying and assessing counterparties. As to financial counterparties, the Group's policy is, among other things, to evaluate and group financial counterparties by the credit rating assigned to them by an independent credit rating agency. There are limits set for each group of financial institutions with respect to the transaction amount and expected maturity to be undertaken by the Group.

Although the Group monitors and manages its counterparty risk, an occurrence of the risk could have an adverse impact on the Group's business and financial position.

The Group's estimate for the counterparty risk profile is medium.

Risk of resource supply disruption

The Group's operations depend on consistent and commercially adequate resource supplies of natural gas required for the operation of the CHPPs and supply of electricity. Risk factors associated with resource availability include non-availability of supplies due to technological and/or other errors and accidents (including, but not limited to, accidents in natural gas supply networks and storage as well as accidents in high voltage transmission system networks connecting Latvia with neighbouring countries) and limitations on resource availability due to commercial, technological, geopolitical or other reasons. The risk that required supplies might not be available, or might only be available on commercially unfavourable terms, would affect the Group's profitability, which could adversely affect the Group's business and financial position.

The Group's estimate for the resources supply risk profile is low.

Legal and Regulatory Risks

The cancellation of mandatory procurement and capacity payment support scheme

Legislative acts of the Republic of Latvia currently entitle the Company's subsidiary Enerģijas publiskais tirgotājs AS to act as an agent in the mandatory procurement administration process.

With the political objective of reducing the amount of the mandatory procurement component in customer bills in Latvia, there is a risk that the cost of mandatory procurement could be reduced at the expense of the Group by stopping the CHPPs capacity support, which has already been reduced by 75 per-cent. On 27 February 2020, the Saeima included in its agenda the draft law "On Amendments to the Energy Law". The draft law provides for the deletion of certain rules from the Energy Law (in Latvian – *Enerģētikas likums*), which defines payments of a guaranteed fee for electrical capacity installed at cogeneration power plants. Also, it provides for terminating the order providing that the electricity costs incurred by the public trader in carrying out the statutory functions are borne by the final consumers.

The draft law may have impacts on the Group's profits and asset value. The interruption of the payment of capacity support to the CHPPs and a stipulated obligation to repay the State compensation (for more details on the compensation, please see Note 14 part d (I) in the Group's Annual Report 2018) of 75 per-cent of the CHPP capacity support could potentially lead to a material adverse effect on the financial position of the Group and consequently reduce the dividend potential of the Group.

The amendments in the regulation of the mandatory procurement resulting in changes of the mandatory procurement administration process or in incurred mandatory procurement costs not being recoverable to their full amount could have a material adverse effect on the Group's financial position.

The Group's estimate for the mandatory procurement risk is high.

Regulated market risk

The Group's revenues from regulated market activities are highly dependent on tariffs approved by the Public Utilities Commission (the "PUC") and/or regulated by legislative acts of the Republic of Latvia. Electricity distribution system service and heat tariffs are reviewed or approved by the PUC based on their approved calculation methodology.

In 2019, approximately 60 per-cent revenues and EBITDA of the Group were generated from regulated activities (distribution, lease of transmission system assets, payment for the installed electrical capacity and generation of thermal energy at the Company's CHPPs, generation of electricity and thermal energy at the Liepāja generation facilities and Aiviekste HPP). There is a risk that not all costs will be covered by such regulated tariffs due to an unduly low regulatory asset base or because the rate of return on capital included in the calculation of the price of the electricity distribution system service tariffs will not correspond to the market rate. Also, there is a risk of material adverse effect on the Group due to delayed regulatory decisions by state authorities in the markets where the Group operates or due to changes in the local or EU legislative environment governing relevant regulatory matters.

The Group's estimate for the regulated market risk profile is medium.

Disposal of Latvijas elektriskie tīkli AS assets

The government of the Republic of Latvia has supported the full transfer of the transmission system assets - 330kV and 110kV transmission lines, substations, and distribution points – to transmission system operator Augstsprieguma tīkls AS. The complete ownership unbundling model is expected to be completed by July 2020. The change of ownership of the assets entails reducing the share capital of the Company, excluding the share capital of Latvijas elektriskie tīkli AS and transferring the shares of Latvijas elektriskie tīkli AS to the balance sheet of the Ministry of Finance. After the change of ownership of Latvijas elektriskie tīkli AS shares, the shares will be invested as a tangible investment in Augstsprieguma tīkls AS share capital and Latvijas elektriskie tīkli AS will be added to Augstsprieguma tīkls AS. In 2019, the revenue of Latvijas elektriskie tīkli AS was EUR 41 million, and its profit was EUR 9.5 million. The asset value of the transmission system asset lease segment at the end of 2019 was EUR 642 million, while the value of Latvijas elektriskie tīkli AS share capital was EUR 234 million and the borrowings that all are loans granted by the Company constituted EUR 196 million. There is a risk that Latvijas elektriskie tīkli AS shares could be undervalued or that Augstsprieguma tīkls AS might not repay the loans granted by the Company within the due term, and this could potentially lead to a material adverse effect on the financial position of the Group.

The Group's estimate for risk involved in the disposal of Latvijas elektriskie tīkli AS assets risk is medium.

Regulatory actions and investigations risk

Several authorities (such as the PUC, the State Audit Office, the Competition Council, and the State Revenue Service) regularly perform investigations, examinations, inspections or audits of the Group's business, including, but not limited to, anti-money laundering (AML), payments, reporting, corporate governance, etc. Any determination by the authorities that the Company or any Group entities have not acted in compliance with all the applicable laws and regulations could have serious legal, reputational and financial consequences for the Group, including exposure to fines, criminal and civil penalties and other damages, increased prudential requirements or even business disruption in the respective fields.

Money laundering and terrorist financing risk

The Group is exposed to money laundering and terrorist financing risk. The Group's AML policy and procedures are clearly specified in writing, and communicated to all personnel. The procedures contain a clear description for employees of their obligations and instructions as well as guidance on how to keep the activity of the Group in compliance with regulations. There are internal procedures for detecting and reporting suspicious transactions. Failure in providing accounting and legal services, granting loans, or opening an account for the Group's companies as a result of non-compliance with AML requirements would most likely lead to serious financial, legal and reputational consequences for the Group, including exposure to fines, as well as criminal and civil penalties.

General Data Protection Regulation (GDPR) risk

The Group's data protection policy and regulations were revised in 2018 to align with the requirements of the General Data Protection Regulation (EU) 2016/679 (GDPR). The Group has created data protection specialist positions, the objective of which is to monitor GDPR compliance and carry out reviews and controls of GDPR fulfilment. The Group regularly monitors GDPR compliance. Failure in establishing and implementing appropriate technical and organizational measures to meet the data protection requirements of the GDPR could have serious financial, legal and reputational consequences for the Group, including exposure to fines and penalties.

International and national sanctions risk

Failure to comply with Latvian national sanctions or sanctions of international organizations (UN, EU, US) could have serious legal and reputational consequences for the Group, including exposure to fines as well as criminal and civil penalties. The Company has entered into two agreements with PJSC Power Machines. Since

26 January 2018, PJSC Power Machines in connection with its business in Crimea is included in the Specially Designated Nationals And Blocked Persons List by the U.S. Department of Treasury Office of Foreign Assets Control (OFAC), therefore further fulfilment of the agreements was stopped by the Company. After intense consultations with respective institutions in Latvia and the USA, an agreement was reached to terminate both agreements with PJSC Power Machines. Termination provides certain actions from both parties, including final payments to be made by the Company.

Fraud risk

Notwithstanding all the detection and prevention activities implemented within the Group with the aim to prevent any corruptive, fraudulent, coercive or collusive practices on the part of the Group's employees, directors and representatives, and with respect to any transaction the Group is involved in, there is a risk of such prohibited practices being performed. This could adversely affect the Group's reputation, business and financial position, as well as involve the Group in legal proceedings and disputes, including claims in relation to actions by regulatory and supervisory institutions.

Competition risk

According to the Competition Law (in Latvian – *Konkurences likums*), the Group is the dominant player in the heat and electricity market. In addition, a new provision of the Competition Law prohibits companies from violating the principles of equal competition and unjustifiably restricting the ability for private entrepreneurs to operate in the market. If the Competition Council found violations of the Competition Law, this could have serious legal, financial and reputational consequences for the Group.

REMIT regulation risk

As the Company operates in the wholesale energy market, there is a potential breach of the European Parliament and Council Regulation No 1227/2011 on Wholesale Energy Market Integrity and Transparency (REMIT), including a prohibition on insider dealing, a prohibition on market manipulation and a duty to provide information to the regulator and the Agency for the Cooperation of Energy Regulators. This could have serious legal, financial and reputational consequences for the Group.

Information disclosure risk

The Company's debt securities are listed on the Nasdaq Riga AS Bond List. There are information disclosure requirements that the Company must follow on an ongoing basis. These requirements stipulate when and how the information should be disclosed to the market. In circumstances where the Company fails to comply with information disclosure requirements, the Financial and Capital Market Commission and/or Nasdaq Riga AS may impose a fine for violation of these requirements, in the worst case scenario ending with delisting of securities. This exposes the Group to reputation risk, and the costs incurred due to such failure might negatively impact the Group's financial situation.

To mitigate this risk the Group has developed the Inside Information Disclosure Rules, which, among other things, contain a list of potential events that would require disclosure to investors.

The Group's estimate for the regulatory actions and investigations risk profile is medium.

Changes in legislation

The Group is dependent on the legislative environment in the markets where it operates, and on political and social decisions in these markets, as well as in the European Union (EU). One of such initiatives is the European Green Deal, aimed at transforming the EU into a fair and prosperous society, with a modern, resource-efficient and competitive economy where there are no net emissions of greenhouse gases in 2050 and where economic growth is decoupled from resource use. This exposes the Group to additional costs and commitments that might negatively impact the Group's financial situation.

The Group's estimate for pertaining to changes in legislation risk is low.

Failure to comply with the EU State aid rules or the capacity payment support criteria

The Treaty on the Functioning of the EU provides that Member States are obliged to notify the European Commission (EC) regarding any State aid scheme. There are certain criteria under which the State aid can be considered lawful and compatible with EU competition law. The State aid scheme implemented by Latvia has been harmonized with the EC, which means that the principle of support in the form of capacity payments to the CHPPs of the Company has also been harmonized. However, it is important that EU regulation emphasizes that power plants with an electrical capacity above 200 MW should be accepted for legitimacy separately from the general aid scheme. The operating aid for Riga CHPP-1 was approved under the State aid scheme SA.43140 "Support to renewable energy and CHP in Latvia" by the EC. The individual notification procedure for the operating aid to Riga CHPP-2 has been completed and awaiting approval from the EC. In case the EC decides that State support to Riga CHPP-2 is unlawful and interruptible, the State would be enforced to recover all operational aid that the Company received for Riga CHPP-2, which could potentially lead to a material adverse effect on the financial position of the Group.

The CHPPs receive State support for their installed capacity. To be eligible for the State support, the following criteria must be met:

- the primary energy savings of each CHPP should be at least 10% per annum;
- the installed electrical capacity of the CHPPs must be used at least 1200 hours per calendar year;
- each CHPP should be operational for at least 4,500 hours per year.

There is a risk of failure to comply with the State support criteria due to incorrect forecasts, a fire or explosion in the CHPPs, loss of the heat market share for other heat producers using biomass as fuel in the production process and other reasons. To manage such risk, the Group coordinates generation plans and continuously monitors actual developments at annual, monthly, next and current day levels. Should such risk materialise, it could adversely affect the Group's financial position.

The Group's estimate for the failure to comply with the EU State aid rules or the capacity payment support criteria risk profile is low.

Financial Risks

Mandatory prepayment of the Group's loan portfolio

The Group's existing long-term loan agreements and bond documentation include certain financial covenant clauses and other obligations and representations, the violation of which could lead to an event of default and acceleration of repayment of the loans and bonds issued. While the Group has not breached such provisions in the past, its ability to comply with covenants and restrictions contained in the loan agreements and bond documentation may be affected by events beyond its control, including prevailing economic, financial, legal, and industry conditions. If these obligations were to be breached, the creditors involved would be able to declare an event of default pursuant to the relevant loan agreements and bond documentation and require prepayment of the entire outstanding loan amounts and redemption of the outstanding bonds. Due to the cross-default clauses in the loan agreements and bond documentation, the Group might need to refinance a substantial part of its outstanding debt. The ability to raise funding for the refinancing of bank and market debt or negotiate other terms with existing lenders might be limited, thus causing significant going concern risk for the Group.

The Group has a policy for raising and managing borrowed funds to address the risk of mandatory prepayment of the Group's loan portfolio. The Group's policy is, among other things, to maintain a common list of covenants included in the loan agreements and bond documentation. Furthermore, financial covenants are considered in the business planning process.

The Group's estimate for the mandatory prepayment of the Group's loan portfolio risk profile is high.

Downgrade of the Company's credit rating

A downgrade of the Company's credit rating could increase the Group's costs of funding and/or reduce its access to funding and could require the Group to provide additional security for contracts, which could increase the costs of the transactions. In addition to a deterioration in the Company's own credit quality, the Company's credit rating might be downgraded if the credit rating of the Republic of Latvia is downgraded due to weak macroeconomic conditions or a change of the support assumptions provided by the Republic of Latvia.

The Group's estimate for downgrade of the Company's credit rating risk profile is low.

Financing and refinancing risk

The Group will need to raise further debt from time to time in order, among other things:

- to finance or refinance capital expenditure;
- to refinance any debt.

Therefore, the Group is exposed to financial and capital market risk resulting from mismatches between the Group's capital requirements and its access to capital. The Group's ability to raise funding may be influenced by, among other things, its own operating performance and general economic, financial, legal and industry conditions. If these conditions deteriorate, there could be an adverse effect on the Group's ability to finance or refinance capital expenditure and/or to refinance its existing debt as and when they are due.

The Group has a policy for raising and managing borrowed funds to address the financing and refinancing risk. The Group's policy is, among other things, to maintain centralized fundraising, to maintain financial planning, to ensure the necessary funding at least 1 year ahead and to diversify funding sources.

The Group's estimate for the financing and refinancing risk profile is low.

Liquidity risk

The Group is exposed to liquidity risk resulting from mismatches between the revenue generated by its business and the Group's capital requirements to meet its payment obligations as they fall due or to fund its capital investments. The Group's future capital requirements and level of costs will depend on numerous factors, including, weather conditions, the amount of cash generated from its operations and general industry and economic conditions. An inability to cover funding costs through revenue streams could have a material adverse effect on the Group's business, financial condition, and results of operations or prospects, which could impact the ability of the Company to meet its payment obligations under the Notes.

The Group has a Financial Risk Management Policy in place to address the liquidity risk. The Group's policy is, among other things, to maintain sufficient reserves of cash and cash equivalents and the availability of long and short term funding through an adequate amount of committed credit facilities to meet its payment commitments according to its strategic plans and to balance fluctuations in the cash flows.

The Group's estimate for the liquidity risk profile is low.

Interest rate risk

The Group's interest rate risk mainly arises from long-term borrowings at variable rates. This exposes the Group to the risk that borrowing costs might increase significantly in the event that the relevant benchmark market interest rates rise.

The Group has a Financial Risk Management Policy in place to address interest rate risk. The Group's policy is, among other things, to maintain a certain average duration and portion of fixed interest rate borrowings in its loan portfolio. Adverse interest rate fluctuations, if not hedged, might negatively impact the Group's operations, prospects and financial results. The Group could also find itself over-hedged which could lead to

loss of financial resources. Early termination of hedging agreements could also negatively impact the Group's financial results.

The Group's estimate for the interest rate risk profile is low.

Risks related to the Notes

Possibility to forfeit interest and principle amount invested

Should the Issuer become insolvent, legal protection proceedings or out-of-court legal protection proceedings of the Issuer are initiated during the term of the Notes, an investor may forfeit interest payable on, and the principle amount of, the Notes in whole or in part. An investor is always solely responsible for the economic consequences of its investment decisions.

No guarantee or security

The Notes will not constitute an obligation of anyone other than the Issuer and they will not be guaranteed. No one other than the Issuer will accept any liability whatsoever in respect of any failure by the Issuer to pay any amount due under the Notes.

The Notes are unsecured debt instruments and the Noteholders would be unsecured creditors in the event of the Issuer's insolvency.

Claims cannot be enforced against the Issuer's key assets

The Issuer holds a number of assets which under applicable laws of the Republic of Latvia can be owned only by the Issuer, the Issuer's wholly-owned subsidiaries or the companies that are wholly-owned by the state. As a consequence, such assets are not transferable to any other party except for the Issuer, its subsidiaries or the companies that are wholly-owned by the state. Section 20.¹ (2) of the Energy Law (in Latvian - *Enerģētikas likums*) lists the following non-transferable assets: (i) Plavinas, Kegums and Riga HPPs on the River Daugava; (ii) Riga CHPP-1 and Riga CHPP-2; and (iii) electricity transmission grid and distribution grid, telecommunication grid and equipment owned by the Issuer. Because of their non-transferable nature, no claims, either on the ground of the Notes or otherwise, can be enforced against these assets. Furthermore, in case of the Issuer's insolvency these assets will not be used for settling the creditors' claims.

The Notes do not contain covenants governing the Issuer's operations and do not limit its ability to merge or otherwise affect significant transactions that may have a material adverse effect on the Notes and the Noteholders

The Notes do not contain provisions designed to protect the Noteholders from a reduction in the creditworthiness of the Issuer. In particular, the General Terms and Conditions of the Notes do not, except for the Change of Control (see Clause 14 the General Terms and Conditions of the Notes), restrict the Issuer's ability to increase or decrease its share capital, to enter into a merger or other significant transaction that could materially alter its existence, jurisdiction of organization or regulatory regime and/or its composition and business. In the event that the Issuer enters into such a transaction, Noteholders could be materially adversely affected. Furthermore, the Change of Control condition does not restrict the current shareholder of the Issuer, namely, the Republic of Latvia, from disposing any or all of its shareholdings, in case the law, which at the date of this Base Prospectus restricts privatisation or alienation of the shares of the Issuer, is changed.

No limitation on issuing additional debt

The issuer is not prohibited from issuing further debt. If the Issuer incurs significant additional debt of an equivalent seniority with the Notes, it will increase the number of claims that would be equally entitled to receive the proceeds, including those related to the Issuer's possible insolvency. Further, any provision which confers, purports to confer, or waives a right to create security interest in favour of third parties, such as a negative pledge, is ineffective against third parties since: (i) it is an issue of a contractual arrangement only being binding upon the parties to such contractual arrangement; (ii) there is no specific legislation in Latvia providing

beneficiaries of negative pledge undertakings or covenants with a preferred position vis-a-vis the claims of third parties; and (iii) no registry or public record exists in Latvia through which negative pledge undertakings or covenants could be filed to obtain a preferred position. Should the Issuer breach its obligations under such undertakings and covenants and create a security interest in favour of a third party, such third party would obtain a valid and enforceable security interest over the pledged asset.

In respect of any Notes issued as Green Bonds, there can be no assurance that such use of proceeds will be suitable for the investment criteria of an investor. Any failure to use the net proceeds of any Tranche of Notes issued as Green Bonds in connection with green projects, and/or any failure to meet, or to continue to meet, the investment requirements of certain environmentally focused investors with respect to such Green Bonds may affect the value and/or trading price of the Green Bonds, and/or may have consequences for certain investors with portfolio mandates to invest in green assets.

The Issuer may issue Notes under the Base Prospectus where the use of proceeds is specified in the applicable Final Terms to be for the financing and/or refinancing of projects and activities that promote climate and other environmental purposes, in accordance with certain prescribed eligibility criteria set out in the Issuer's Green Bond Framework (as defined below) (any Notes which have such a specified use of proceeds are referred to as "**Green Bonds**").

In respect of any Notes issued as Green Bonds, there can be no assurance that such use of proceeds will be suitable for the investment criteria of an investor. The Final Terms relating to any specific Tranche of Notes may provide that it will be the Issuer's intention to apply the proceeds from an offer of those Notes specifically for one or more Eligible Projects (as defined under the Issuer's Green Bond Framework available on its website from time to time (the "**Green Bond Framework**"). Prospective investors should have regard to the information set out on the Issuer's website and must determine for themselves the relevance of such information for the purpose of any investment in the Notes together with any other investigation such investor deems necessary.

In particular no assurance is given by the Issuer that the use of such proceeds for any Eligible Projects will satisfy, whether in whole or in part, any present or future investor expectations or requirements as regards any investment criteria or guidelines with which such investor or its investments are required to comply, whether by any present or future applicable law or regulations or by its own by-laws or other governing rules or investment portfolio mandates, in particular with regard to any direct or indirect environmental, sustainability or social impact of any projects or uses, the subject of or related to, any Eligible Projects.

Furthermore, it should be noted that there is currently no clearly defined definition (legal, regulatory or otherwise) of, nor market consensus as to what constitutes, a "green" or "sustainable" or an equivalently-labelled project or as to what precise attributes are required for a particular project to be defined as "green" or "sustainable" or such other equivalent label nor can any assurance be given that such a clear definition or consensus will develop over time. Accordingly, no assurance is or can be given to investors that any projects or uses the subject of, or related to, any Eligible Projects will meet any or all investor expectations regarding such "green", "sustainable" or other equivalently-labelled performance objectives or that any adverse environmental, social and/or other impacts will not occur during the implementation of any projects or uses the subject of, or related to, any Eligible Projects.

No assurance or representation is given as to the suitability or reliability for any purpose whatsoever of any opinion or certification of any third party (whether or not solicited by the Issuer) which may be made available in connection with the issue of any Notes and in particular with any Eligible Projects to fulfil any environmental, sustainability, social and/or other criteria. For the avoidance of doubt, any such opinion or certification is not, nor shall be deemed to be, incorporated in and/or form part of this Base Prospectus. Any such opinion or certification is not, nor should be deemed to be, a recommendation by the Issuer or any other person to buy, sell or hold any such Notes. Any such opinion or certification is only current as of the date that opinion was initially issued. Prospective investors must determine for themselves the relevance of any such opinion or certification and/or the information contained therein and/or the provider of such opinion or certification for the purpose of any investment in such Notes. Currently, the providers of such opinions and certifications are not subject to any specific regulatory or other regime or oversight.

While it is the intention of the Issuer to apply the proceeds of any Notes so specified for Eligible Projects in, or substantially in, the manner described in this Base Prospectus, there can be no assurance that the relevant project(s) or use(s) the subject of, or related to, any Eligible Projects will be capable of being implemented in or substantially in such manner and/or accordance with any timing schedule and that accordingly such proceeds will be totally or partially disbursed for such Eligible Projects. None of the Arrangers or the Dealers will verify or monitor the proposed use of proceeds of the Notes issued under the Base Prospectus. Nor can there be any assurance that such Eligible Projects will be completed within any specified period or at all or with the results or outcome (whether or not related to the environment) as originally expected or anticipated by the Issuer. Any such event or failure by the Issuer will not constitute an Event of Default under the Notes.

Any such event or failure to apply the proceeds of any issue of Notes for any Eligible Projects as aforesaid and/or withdrawal of any such opinion or certification or any such opinion or certification attesting that the Issuer is not complying in whole or in part with any matters for which such opinion or certification is opining or certifying on may have a material adverse effect on the value of such Notes and also potentially the value of any other Notes which are intended to finance Eligible Projects and/or result in adverse consequences for certain investors with portfolio mandates to invest in securities to be used for a particular purpose.

Refinancing risk

The Issuer may be required to refinance certain or all of its outstanding debt, including the Notes. The Issuer's ability to successfully refinance its debt depends on the conditions of debt capital markets and its own financial condition. The Issuer's inability to refinance its debt obligations on favourable terms, or at all, could have a negative impact on the Group's operations, financial condition, earnings and on the Noteholders' recovery under the Notes.

Since the Notes bear interest at a fixed interest rate, movements in market interest rates can adversely affect the value of the Notes

The Notes bear interest on their outstanding principal amount at a fixed interest rate. A holder of a security with a fixed interest rate is exposed to the risk that the value of such security could fall as a result of changes in the market interest rate. While the nominal compensation rate of the Notes is fixed during the life of the Notes, the current interest rate on the capital market (market interest rate) typically changes on a daily basis. If the market interest rate increases, the value of a security such as the Notes typically falls, until the yield of such security is approximately equal to the market interest rate. If the market interest rate falls, the value of a security such as the Notes typically increases, until the yield of such a security is approximately equal to the market interest rate. Consequently, Noteholders should be aware that movements of the market interest rate can adversely affect the value of the Notes and can lead to losses for the Noteholders if they sell their Notes.

The market price of the Notes may be volatile

The market price of the Notes could be subject to significant fluctuations in response to actual or anticipated variations in the Group's operating results and those of its competitors, adverse business developments, changes to the regulatory environment in which the Group operates, changes in financial estimates by securities analysts and the actual or expected sale of a large number of the Notes, as well as other factors. In addition, in recent years the global financial markets have experienced significant price and volume fluctuations, which, if repeated in the future, could adversely affect the market price of the Notes without regard to the Group's results of operations, prospects or financial condition. Factors including increased competition or the Group's operating results, the regulatory environment, general market conditions, natural disasters, pandemics, terrorist attacks and war may have an adverse effect on the market price of the Notes.

An active market for the Notes may not develop

Although application(s) will be made for the Notes to be admitted to trading on Nasdaq Riga stock exchange, there is no assurance that such application(s) will be accepted and the Notes will be admitted to trading. In addition, admission of the Notes on a regulated market will not guarantee that a liquid public market for the Notes will develop or, if such market develops, that it will be maintained, and neither the Issuer, nor the

Arrangers or Dealers are under any obligation to maintain such market. Therefore, investors may not be able to sell their Notes easily or at prices that will provide them with a yield comparable to similar investments that have a developed secondary market. A lack of liquidity may have a material adverse effect on the market value of the Notes.

Exchange rate risk

The Issuer will pay principal and interest on the Notes in EUR. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the “**Investor's Currency**”) other than EUR. These include the risk that exchange rates may significantly change (including changes due to devaluation of EUR or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify currency exchange controls. An appreciation in the value of the Investor's Currency relative to EUR would decrease the Investor's Currency-equivalent: (i) yield on the Notes; (ii) value of the principal payable on the Notes; and (iii) market value of the Notes.

Credit ratings

The Issuer's credit ratings are an assessment by the relevant rating agency of its ability to pay its debts when due. Consequently, real or anticipated changes in its credit ratings will generally affect the market value of the Notes. One or more independent credit rating agencies may assign credit ratings to the Notes. In case the Notes are rated by credit rating agencies, such ratings may not reflect the potential impact of all risks related to the structure, market, additional factors discussed above, or other factors that may affect the value of the Notes. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time. Any adverse change in an applicable credit rating of the Issuer could adversely affect the trading price of the Notes.

No assurance on change of laws or practices

The Notes are governed by the laws of the Republic of Latvia. Latvian laws (including but not limited to tax laws) and regulations governing the Notes may change during the life of the Notes, and new judicial decisions can be issued and/or new administrative practices may be adopted. No assurance can be given as to the impact of any of such possible changes of laws or regulations, or new judicial decision or administrative practice taking place after the date of this Base Prospectus. Hence, such change may have a material adverse effect on the Issuer's business, financial condition, results of operations and/or future prospects and, thereby, the Issuer's ability to fulfil its obligations under the Notes, as well as taxation of the Notes, and the market price of the Notes. Such events may also result in material financial losses or damage to the Noteholders.

Redemption prior to maturity

The Notes are redeemable at the Issuer's option at a price equal to the nominal amount of the Notes together with the accrued interest (as more fully set out in Clauses 9.3 and 9.4 of the General Terms and Conditions of the Notes). The Notes are also redeemable due to tax reasons at a price equal to the nominal amount of the Notes together with the accrued interest (as more fully set out in Clause 11 of the General Terms and Conditions of the Notes). In addition, the Notes are redeemable on the occurrence of a Change of Control at a price equal to the nominal amount of the Notes together with the accrued interest (as more fully set out in Clause 14 of the General Terms and Conditions of the Notes). Furthermore, if 75 (seventy-five) per-cent or more in principal amount of the Notes then outstanding have been redeemed based on a Change of Control, the Issuer is entitled to redeem the remaining Notes at a price equal to the nominal amount of the Notes together with the accrued interest.

It is possible that the Notes are redeemed at a time when the prevailing interest rates may be relatively low. In such circumstances an investor may not be able to reinvest the redemption proceeds in a comparable security at an effective interest rate as high as that of the Notes. It is further possible that the Issuer will not have sufficient funds at the time of the occurrence of a Change of Control to make the required redemption of Notes.

No voting rights

Only the shareholder of the Issuer has voting rights in the shareholders' meetings of the Issuer. The Notes carry no such voting rights. Consequently, the Noteholders cannot influence any decisions by the Issuer's shareholder concerning, for instance, the capital structure of the Issuer.

Amendments to the Notes bind all Noteholders

The General Terms and Conditions of the Notes contain provisions for Noteholders to consider matters affecting their interests generally. The decisions of Noteholders (including amendments to the General Terms and Conditions of the Notes), subject to defined majorities requirements, will be binding to all Noteholders, including Noteholders who did not vote and Noteholders who voted in a manner contrary to the majority. This may cause financial losses, among other things, to all Noteholders, including the Noteholders who did not vote and Noteholders who voted in a manner contrary to the majority.

Certain material interests

The Arrangers and Dealers have engaged in, and may in the future engage in, investment banking and/or commercial banking or other services provided to the Group in the ordinary course of business. Therefore, conflicts of interest may exist or may arise as a result of an Arranger's or a Dealer's current or future engagement in transactions with other parties, having multiple roles or carrying out other transactions for third parties with conflicting interests.

Risks relating to the clearing and settlement in the Depository's book-entry system

The Notes will be affiliated to the account-based system of the Depository, and no physical notes will be issued. Clearing and settlement relating to the Notes will be carried out within the Depository's book-entry system as well as payment of interest and repayment of the principal. Investors are therefore dependent on the functionality of the Depository's account-based system.

GENERAL TERMS AND CONDITIONS OF THE NOTES

1. Principal amount and issuance of the Notes

- 1.1. Under this third programme for the issuance of notes (the “**Programme**”) the Issuer may issue notes up to an aggregate principal amount of EUR 200,000,000 (two hundred million euro) (the “**Notes**”).
- 1.2. The Notes shall be issued in series (the “**Series**”).
- 1.3. Each Series may comprise one or more tranches of Notes (the “**Tranches**”). The Notes of each Tranche will all be subject to identical terms, except that the Issue Dates (as defined below) and the Issue Prices (as defined below) thereof may be different in respect of different Tranches.
- 1.4. In order to identify each Series and Tranches, the Final Terms (as defined below) shall stipulate a serial number of the respective Series and a serial number of the respective Tranche.
- 1.5. The terms and conditions of each Tranche shall consist of these general terms and conditions of the Notes (the “**General Terms and Conditions**”) and the final terms (the “**Final Terms**”). The General Terms and Conditions shall apply to each Tranche.
- 1.6. Each Final Terms will be approved by the management board of the Issuer, published on the Issuer’s website www.latvenergo.lv/lv/investoriem and submitted to the Financial and Capital Market Commission, which will forward them to the Bank of Lithuania (in Lithuanian - *Lietuvos Bankas*).
- 1.7. The aggregate principal amount of a Tranche shall be specified in the Final Terms. The Issuer may increase or decrease the aggregate principal amount of a Tranche as set out in the Final Terms during the Placement Period (as defined below) of that Tranche.
- 1.8. The nominal amount of each Note shall be specified in the Final Terms.
- 1.9. The Notes will be offered for subscription for a minimum investment amount EUR 100,000 (one hundred thousand euro) (the “**Minimum Investment Amount**”).

2. Form of the Notes and ISIN

- 2.1. The Notes are freely transferable non-convertible debt securities, which contain payment obligations of the Issuer towards the holders of the Notes (the “**Noteholders**”).
- 2.2. The Notes are dematerialized debt securities in bearer form which are disposable without any restrictions and can be pledged. However, the Notes cannot be offered, sold, resold, transferred or delivered in such countries or jurisdictions or otherwise in such circumstances in which it would be unlawful or require measures other than those required under Latvian laws, including the United States, Australia, Japan, Canada, Hong Kong, South Africa, Singapore and certain other jurisdictions. In addition, the Noteholders are prohibited to resell, transfer or deliver the Notes to any person in a manner that would constitute a public offer of securities.
- 2.3. The Notes shall be book-entered with Nasdaq CSD SE (registration number: 40003242879, legal address: Valņu 1, Rīga, LV-1050, Latvia) (the “**Depository**”).
- 2.4. A separate ISIN will be assigned to each Series, which will be different from ISIN of other Series.
- 2.5. Before commencement of the offering of the Notes of the first Tranche of each Series, the Depository upon request of the Issuer will assign ISIN to the respective Series. Where a further Tranche is issued, which is intended to form a single Series with an existing Tranche at any point after the Issue Date of the existing Tranche, a temporary ISIN may be assigned to the Notes of such further Tranche, which is different from ISIN assigned to the relevant Series, until such time as the Tranches are consolidated and form a single Series.

- 2.6. ISIN of the respective Series and a temporary ISIN of the respective Tranche, if applicable, will be specified in the Final Terms.

3. Status and security

- 3.1. The Notes constitute direct, unsecured and unguaranteed obligations of the Issuer ranking *pari passu* without any preference among each other and with all other unsecured, unguaranteed and unsubordinated indebtedness of the Issuer, save for such obligations as may be preferred by mandatory provisions of law.
- 3.2. The Noteholders hereby waive their right to apply for any security (including security stipulated in the Commercial Law (in Latvian – *Komerclikums*)) in case of a decrease of the share capital of the Issuer as a result of disposal of the Issuer's shares in Latvijas elektriskie tīkli AS, registration number: 40103379313. No such security shall be granted to the Noteholders.

4. Currency of the Notes

The Notes will be issued in EUR.

5. Issue price and yield

- 5.1. The Notes may be issued at their nominal amount or at a discount or a premium to their nominal amount (the “**Issue Price**”). The Issue Price shall be determined by the Issuer and specified in the Final Terms.
- 5.2. The yield of each Tranche set out in the applicable Final Terms will be calculated as of the relevant Issue Date on an annual basis using the relevant Issue Price. It is not an indication of future yield.

6. Underwriting

None of the Tranches will be underwritten.

7. Issue date

The issue date of each Tranche (the “**Issue Date**”) shall be specified in the Final Terms.

8. Interest

- 8.1. The Notes shall bear interest at a fixed annual interest rate (the “**Interest Rate**”) which shall be determined by the Issuer and specified in the Final Terms.
- 8.2. The interest on the Notes will be paid annually on the dates specified in the Final Terms (“**Interest Payment Date**”) until the Maturity Date (as defined below) and will be calculated on the aggregate outstanding principal amount of the Notes of the respective Series.
- 8.3. Interest shall accrue for each interest period from and including the first day of the interest period to (but excluding) the last day of the interest period on the principal amount of the Notes of the respective Series outstanding from time to time. The first interest period commences on the Issue Date and ends on a day preceding the first Interest Payment Date (the “**First Interest Period**”). Each consecutive interest period begins on the previous Interest Payment Date and ends on a day preceding the following Interest Payment Date. The last interest period ends on the Maturity Date (as defined below).
- 8.4. Interest in respect of the Notes will be calculated on the basis of the actual number of days elapsed in the relevant interest period divided by 365 (or, in the case of a leap year, 366), i.e. a day count convention Act/Act (ICMA) will be used.
- 8.5. When interest is required to be calculated in respect of a period of less than a full year (other than in respect of the First Interest Period) it shall be calculated on the basis of (i) the actual number of days in the period from and including the date from which interest begins to accrue (the “**Accrual Date**”) to but

excluding the date on which it falls due, divided by (ii) the actual number of days from and including the Accrual Date to, but excluding the next following Interest Payment Date.

- 8.6. Interest on the Notes shall be paid through the Depository in accordance with the applicable rules of the Depository to the persons who were registered as the Noteholders by the end of the 8th (eighth) Business Day immediately preceding the Interest Payment Date.
- 8.7. Should any Interest Payment Date fall on a date which is not a Business Day, the payment of the interest due will be postponed to the next Business Day. The postponement of the payment date shall not have an impact on the amount payable.

"Business Day" means a day on which the Depository system is open and operational.

9. Redemption

- 9.1. The Notes shall be repaid in full at their nominal amount on the date which will be specified in the Final Terms (the **"Maturity Date"**), unless the Issuer has prepaid the Notes in accordance with Clauses 9.3 and 9.4, Clause 14 (*Change of control*) or Clause 16 (*Events of Default*) below or in case the Noteholders, upon proposal of the Issuer, pursuant to Clause 23 (*Decisions of the Noteholders*) have decided that the Notes shall be redeemed prior to the Maturity Date.
- 9.2. Each Series of Notes may have a maturity up to 10 (ten) years.
- 9.3. The Issuer may redeem each Series of Notes, in whole but not in part, at any time during the period commencing on the first Business Day falling 3 (three) months prior to the Maturity Date (such Business Day included) and ending on the Maturity Date (the Maturity Date excluded) (the **"Voluntary Redemption Period"**), at an amount equal to 100 (one hundred) per-cent of their nominal amount together with any accrued but unpaid interest to, but excluding, the date of voluntary redemption (the **"Voluntary Redemption Date"**).
- 9.4. Redemption in accordance with Clause 9.3 shall be made by the Issuer giving not less than 30 (thirty) but no more than 60 (sixty) calendar days' irrevocable notice specifying the Voluntary Redemption Date, which shall be a Business Day within the Voluntary Redemption Period, to the Noteholders in accordance with Clause 21 (*Notices*).
- 9.5. The principal of the Notes shall be paid through the Depository in accordance with the applicable rules of the Depository to the persons who were registered as the Noteholders by the end of the Business Day immediately preceding the payment.
- 9.6. Should the payment date fall on a date which is not a Business Day, the payment of the amount due will be postponed to the next Business Day. The postponement of the payment date shall not have an impact on the amount payable.

10. Taxation

All payments in respect of the Notes by the Issuer shall be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature (**"Taxes"**), unless the withholding or deduction of the Taxes is required by the laws of the Republic of Latvia. In such case, the Issuer shall pay such additional amounts as will result in receipt by the Noteholders after such withholding or deduction of such amounts as would have been received by them had no such withholding or deduction been required, except that no such additional amounts shall be payable in respect of any Note held by or on behalf of a Noteholder which is liable to such Taxes in respect of such Note by reason of its having some connection with the Republic of Latvia other than the mere holding of the Note.

11. Redemption for tax reasons

- 11.1. The Notes may be redeemed at the option of the Issuer in whole, but not in part, at any time on giving 30 (thirty) but no more than 60 (sixty) calendar days' irrevocable notice to the Noteholders at an amount equal to 100 (one hundred) per-cent of their nominal amount together with any accrued but unpaid interest to, but excluding, the date of redemption, if:
- (i) the Issuer has or will become obliged to pay additional amounts as provided or referred to in Clause 10 (*Taxation*) as a result of any change in, or amendment to, the laws or regulations of the Republic of Lithuania or any political subdivision or any authority thereof or therein having power to tax, or any change in the application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after the date of issue of the first Tranche of the Notes; and
 - (ii) such obligation cannot be avoided by the Issuer taking reasonable measures available to it,
- provided, however, that** no such notice of redemption shall be given earlier than 90 (ninety) days prior to the earliest date on which the Issuer would be obliged to pay such additional amounts if a payment in respect of the Notes were then due
- 11.2. Prior to the publication of any notice of redemption pursuant to this paragraph, the Issuer shall obtain an opinion of independent legal advisers of recognised standing to the effect that the Issuer has or will become obliged to pay such additional amounts as a result of such change or amendment.
- 11.3. Upon the expiry of any such notice as is referred to in this Clause 11, the Issuer shall be bound to redeem the Notes in accordance with this Clause 11.

12. Placement of the Notes

- 12.1. Initially the Notes of the respective Tranche will be book-entered in the distribution account of a Dealer specified in the Final Terms (the "**Settlement Agent**") with the Depository.
- 12.2. The placement period for each Tranche (the "**Placement Period**") will be specified in the Final Terms. The Issuer may decide on shortening or lengthening the Placement Period.
- 12.3. The investors wishing to purchase the Notes shall submit their orders to the Dealers to purchase the Notes (the "**Purchase Orders**") at any time during the Placement Period.
- 12.4. Total amount of the Notes to be purchased and provided in each Purchase Order shall be no less than the Minimum Investment Amount.
- 12.5. Purchase Orders by the same legal entity or person will be aggregated into one if all order parameters (except the purchase amount) are the same.
- 12.6. All Purchase Orders are binding and irrevocable commitment to acquire the allotted Notes.
- 12.7. On the same Business Day following the Placement Period the Issuer will decide whether to proceed with the issuance of the Notes of a respective Tranche or cancel the issuance. In case the issuance of the Notes of a respective Tranche is cancelled, the Issuer will publish an announcement on the Issuer's website www.latvenergo.lv.
- 12.8. The Issuer in consultation with the Dealers will decide on allotment of the Notes to the Investors. The Issuer reserves a right to reject any Purchase Order, in whole or in part, at its sole discretion.
- 12.9. The Dealers shall send to each investor by way of e-mail or through Bloomberg system a confirmation which will contain information on the extent of satisfaction or rejection of the Purchase Order submitted by the investor, the number of Notes allotted to the investor and the amount (price) payable for the Notes.

- 12.10. The settlement for the Notes will take place on the Issue Date and will be carried out by the Settlement Agent in accordance with the DVP (*Delivery vs Payment*) principle pursuant to the applicable rules of the Depository.
- 12.11. All paid up Notes shall be treated as issued. The Notes which are not paid up shall be cancelled.
- 12.12. Information about the placement results of the Notes will be published on the Issuer's website www.latvenergo.lv within 1(one) Business Day following the Issue Date.

13. Admission to trading

- 13.1. The Issuer shall submit an application regarding inclusion of each Tranche in the official list of Akciju sabiedrība "Nasdaq Riga", registration number: 40003167049, legal address: Valņu 1, Riga, LV-1050, Latvia ("**Nasdaq Riga**"). An application shall be prepared according to the requirements of Nasdaq Riga and shall be submitted to Nasdaq Riga within 3 (three) months after the Issue Date of the respective Tranche.
- 13.2. The Issuer shall use its best efforts to ensure that the Notes remain listed in the official list of Nasdaq Riga or, if such listing is not possible, to obtain or maintain, listed or traded on another regulated market. The Issuer shall, following a listing or admission to trading, take all reasonable actions on its part required as a result of such listing or trading of the Notes.
- 13.3. The Issuer will cover all costs which are related to the admission of the Notes to the relevant regulated market.

14. Change of control

- 14.1. If at any time while any Note remains outstanding: (i) there occurs a Change of Control (as defined below), and (ii) within the Change of Control Period (as defined below), a Rating Event (as defined below) in respect of that Change of Control occurs (such Change of Control and Rating Event not having been cured prior to the expiry of the Change of Control Period, together, a "**Change of Control Put Event**"), each Noteholder will have the option (the "**Change of Control Put Option**") (unless, prior to the giving of the Change of Control Put Event Notice (as defined below), the Issuer gives notice to redeem the Notes according to Clauses 9.3 and 9.4) to require the Issuer to redeem or, at the Issuer's option, to procure the purchase of, all or part of its Notes, on the Optional Redemption Date (as defined below) at an amount equal to 100 (one hundred) per-cent of their nominal amount together with any accrued but unpaid interest to, but excluding, the Optional Redemption Date.

A "**Change of Control**" shall be deemed to have occurred if at any time following the Issue Date of the first Tranche of the Notes, the Republic of Latvia ceases to own, directly or indirectly, at least 51 (fifty one) per-cent of the issued share capital of the Issuer or ceases to have the power, directly or indirectly, to cast, or control the casting of, at least 51 (fifty one) per-cent of the maximum number of votes that might be casted at a Shareholders' Meeting of the Issuer.

"**Change of Control Period**" means the period beginning on the date of the first public announcement by or on behalf of the Issuer by any bidder or any designated advisor, of the relevant Change of Control and ending 90 days after completion of the relevant Change of Control.

A "**Rating Event**" shall be deemed to have occurred in respect of a Change of Control if (within the Change of Control Period) either:

- (i) (A) the rating previously assigned to the Issuer by any Rating Agency solicited by the Issuer is (x) withdrawn or (y) changed from an investment grade rating (Baa3/BBB- or its equivalent for the time being, or better) to a non-investment grade rating (Ba1/BB+ or its equivalent for the time being, or worse) or (z) (if the rating previously assigned to the Issuer by any Rating Agency solicited by the Issuer was below an investment grade rating (as described above)), lowered by at least one full rating notch (for example, from Ba1 to Ba2, or their respective equivalents) and (B)

such rating is not subsequently upgraded (in the case of a downgrade) or reinstated (in the case of a withdrawal) within the Change of Control Period either to an investment grade credit rating (in the case of (x) and (y)) or to its earlier credit rating or better (in the case of (z)) by such Rating Agency; or

- (ii) the Issuer has not been previously assigned a credit rating solicited by the Issuer, and no Rating Agency assigns the Issuer an investment grade rating solicited by the Issuer within the Change of Control Period;

provided that the Rating Agency making the reduction in rating or deciding not to assign an investment grade rating announces or publicly confirms or, having been so requested by the Issuer, informs the Issuer in writing that the lowering or failure to assign an investment grade rating was the result, in whole or in part, of any event or circumstance comprised in or arising as a result of, or in respect of, the applicable Change of Control (whether or not the applicable Change of Control shall have occurred at the time of the Rating Event).

“Rating Agency” means Moody’s Investors Service Ltd., Standard & Poor’s Credit Market Services Europe Limited or Fitch Ratings Ltd.

- 14.2. Promptly upon the Issuer becoming aware that a Change of Control Put Event has occurred, the Issuer shall give notice (a **“Change of Control Put Event Notice”**) to the Noteholders in accordance with Clause 21 (*Notices*) specifying the nature of the Change of Control Put Event and the circumstances giving rise to it, and the procedure for exercising the Change of Control Put Option.
- 14.3. To exercise the Change of Control Put Option, a Noteholder within the period (the **“Change of Control Put Period”**) of 45 (forty-five) days after a Change of Control Put Event Notice is given must provide to the Issuer in writing a notice on exercise of the Change of Control Put Option (a **“Change of Control Put Option Notice”**).
- 14.4. A Change of Control Put Option Notice once given shall be irrevocable. The Issuer shall redeem or, at the option of the Issuer procure the purchase of, the Notes in respect of which the Change of Control Put Option has been validly exercised as provided above by the date which is the 5th (fifth) Business Day following the end of the Change of Control Put Period (the **“Optional Redemption Date”**).
- 14.5. For the avoidance of doubt, the Issuer shall have no responsibility for any cost or loss of whatever kind (including breakage costs) which the Noteholder may incur as a result of or in connection with such Noteholder’s exercise or purported exercise of, or otherwise in connection with, any Change of Control Put Option (whether as a result of any purchase or redemption arising therefrom or otherwise).
- 14.6. If 75 (seventy-five) per-cent or more in principal amount of the Notes then outstanding have been redeemed pursuant to this Clause 14, the Issuer may, on not less than 30 (thirty) nor more than 60 (sixty) days’ irrevocable notice to the Noteholders in accordance with Clause 21 (*Notices*) given within 30 (thirty) days after the Optional Redemption Date, redeem on a date to be specified in such notice at its option, all (but not some only) of the remaining Notes at 100 (one hundred) per-cent of their nominal amount, together with interest accrued to, but excluding, the date of redemption.

15. Negative pledge

So long as any Note remains outstanding, the Issuer shall not, and shall procure that none of its Material Subsidiaries create or permit to subsist mortgage, pledge or any other security interest (each a **“Security Interest”**), other than a Permitted Security Interest, upon the whole or any part of its present or future business, undertaking, assets or revenues to secure any Relevant Indebtedness or Guarantee of Relevant Indebtedness without (a) at the same time or prior thereto securing the Notes equally and rateably therewith, or (b) providing such other security for the Notes or other arrangement (whether or not it includes the granting of a security) as may be approved by the Noteholders pursuant to Clause 23 (*Decisions of the Noteholders*).

“Subsidiary” means a company:

- (i) whose affairs and policies the Issuer controls or has the power to control, whether by ownership of share capital, contract, the power to appoint or remove members of the governing body or otherwise; or
- (ii) whose financial statements are, in accordance with applicable law and generally accepted accounting principles, consolidated with those of the Issuer.

“Material Subsidiary” means at any time any Subsidiary:

- (i) whose total consolidated (or, if applicable, unconsolidated) assets (excluding intercompany loans, intercompany payables, intercompany receivables and intercompany unrealised gains and losses in inventories) represent not less than 10 (ten) per-cent of the total consolidated assets of the Issuer, or whose gross consolidated EBITDA (or, if applicable, unconsolidated) represents not less than 10 (ten) per-cent of the gross consolidated EBITDA of the Issuer, in each case as determined by reference to the most recent publicly available annual or interim financial statements of the Issuer prepared in accordance with IFRS and the latest financial statements of the Subsidiary determined in accordance with IFRS; or
- (ii) to which is transferred the whole or substantially all of the assets and undertakings of a Subsidiary which, immediately prior to such transfer, is a Material Subsidiary.

“EBITDA” means (i) the consolidated operating profit of the Group or (ii) in the case of a Material Subsidiary, the consolidated or unconsolidated operating profit of such Material Subsidiary, in the case of both (i) and (ii) before taking into account:

- (a) depreciation and amortisation;
- (b) finance income and finance costs;
- (c) revaluation of property, plant and equipment, and investment property;
- (d) impairment of property, plant and equipment;
- (e) current year income tax expense and deferred income tax (expense)/benefit;
- (f) any revaluation of non-current assets; and
- (g) exceptional items, as defined by IFRS or separately identified as such within the most recent publicly available annual or interim financial statements of the Issuer or the relevant Material Subsidiary (as the case may be), prepared in accordance with IFRS;

“Group” means the Issuer and its Subsidiaries from time to time.

“IFRS” means the International Financial Reporting Standards as adopted by the European Union.

“Permitted Security Interest” means any Security Interest created over any asset of any company which becomes a Subsidiary after the Issue Date of the first Tranche of the Notes, where such Security Interest is created prior to the date on which the company becomes a Subsidiary, provided that:

- (i) such Security Interest was not created in contemplation of the acquisition of such company; and
- (ii) the principal amount secured was not increased in contemplation of or since the acquisition (or proposed acquisition) of that company.

“Indebtedness” means any indebtedness (whether principal, premium, interest or other amounts) in respect of any bonds, notes or other debt securities or borrowed money by the Issuer or any of its

Subsidiaries (other than from the Issuer to any of its wholly-owned Subsidiaries and from any of the Issuer's wholly-owned Subsidiaries to the Issuer or to another wholly-owned Subsidiary).

"Relevant Indebtedness" means any Indebtedness which is in the form of, or represented by any bond, note or other debt security which is, or is capable of being, quoted, listed or traded on any stock exchange or in any securities market (including, without limitation, any over-the-counter market).

"Guarantee" means, in relation to any Indebtedness, any obligation to pay such Indebtedness including (without limitation):

- (i) any obligation to purchase such Indebtedness;
- (ii) any obligation to lend money, to purchase or subscribe shares or other securities or to purchase assets or services in order to provide funds for the payment of such Indebtedness;
- (iii) any indemnity against the consequences of a default in the payment of such Indebtedness; and
- (iv) any other agreement to be responsible for such Indebtedness.

16. Events of Default

16.1. If an Event of Default (as defined below) occurs, any Noteholder may by written notice to the Issuer declare the outstanding principal amount of the Notes and the interest accrued on the Notes to be prematurely due and payable at the earliest on the 10th (tenth) Business Day from the date such notice was received by the Issuer, provided that an Event of Default is continuing on the date of receipt of the notice by the Issuer and on the specified early repayment date (the **"Early Repayment Date"**). Interest on such Notes accrues until the Early Prepayment Date (excluding the Early Prepayment Date).

16.2. The Issuer shall notify the Noteholders about the occurrence of an Event of Default (and the steps, if any, taken to remedy it) in accordance with Clause 21 (*Notices*) promptly upon becoming aware of its occurrence.

16.3. Each of the following events shall constitute an event of default (an **"Event of Default"**):

- (i) **Non-payment:** the Issuer fails to pay any amount of principal in respect of the Notes on the due date for payment thereof or fails to pay any amount of interest in respect of the Notes on the due date for payment thereof and the default continues for a period of 5 (five) days in the case of principal and for a period of 14 (fourteen) days in the case of interest, unless the failure to pay is caused by a reason referred to in Clause 17 (*Force Majeure*);
- (ii) **Breach of other obligations:** the Issuer defaults in the performance or observance of any of its other obligations in respect of the Notes, and such default is not capable of remedy or remains unremedied for at least 30 (thirty) days after written notice thereof, addressed to the Issuer by any Noteholder, has been received by the Issuer;
- (iii) **Cross-default:**
 - (a) any Indebtedness of the Issuer or any of its Material Subsidiaries is not paid when due or (as the case may be) within any originally applicable grace period;
 - (b) any such Indebtedness becomes due and payable prior to its stated maturity otherwise than at the option of the Issuer or (as the case may be) the relevant Material Subsidiary or (**provided that** no event of default, howsoever described, has occurred) any person entitled to such Indebtedness;
 - (c) the Issuer or any of its Material Subsidiaries fails to pay when due any amount payable by it under any Guarantee of any Indebtedness;

provided that the amount of Indebtedness referred to in sub-paragraph (a) and/or sub-paragraph (b) above and/or the amount payable under any Guarantee referred to in sub-paragraph (c) above individually or in the aggregate exceeds EUR 25,000,000 (twenty-five million euro) (or its equivalent in any other currency or currencies);

- (iv) **Security enforced:** a secured party enforces a security over the whole or any substantial part of the undertaking, assets and revenues of the Issuer or any of its Material Subsidiaries;
- (v) **Cessation of business:** the Issuer or any of its Material Subsidiaries cease to carry on its current business in its entirety or a substantial part thereof, other than:
 - (a) pursuant to any sale, disposal, demerger, amalgamation, reorganization or restructuring or any cessation of business in each case on a solvent basis and within the Group;
 - (b) pursuant to disposal of the Issuer's shares in Latvijas elektriskie tīkli AS, registration number: 40103379313;
 - (c) in relation to a Material Subsidiary, if the cessation of the respective business (or substantial part thereof) of the Material Subsidiary is required by any specific EU regulations or laws of the Republic of Latvia or decisions of any regulatory authority in relation to the operation of the electricity markets, and it does not materially affect the Issuer's ability to fulfil its obligations with regard to the Notes; or
 - (d) for the purposes of, or pursuant to any terms approved by the Noteholders in accordance with Clause 23 (*Decisions of the Noteholders*);
- (vi) **Liquidation:** an effective resolution is passed for the liquidation of the Issuer or any of its Material Subsidiaries other than, in case of a Material Subsidiary:
 - (a) pursuant to an amalgamation, reorganization or restructuring in each case within the Group; or
 - (b) as a result of the cessation of the respective business required by any specific EU regulations or laws of the Republic of Latvia or decisions of any regulatory authority in relation to the operation of the electricity markets, and it does not materially affect the Issuer's ability to fulfil its obligations with regard to the Notes; or
 - (c) for the purposes of, or pursuant to any terms approved by the Noteholders in accordance with Clause 23 (*Decisions of the Noteholders*);
- (vii) **Insolvency:**
 - (a) the Issuer or any of its Material Subsidiaries is declared insolvent or bankrupt by a court of competent jurisdictions or admits inability to pay its debts; or
 - (b) the Issuer or any of its Material Subsidiaries enters into any arrangement with majority of its creditors by value in relation to restructuring of its debts or any meeting is convened to consider a proposal for such arrangement; or
 - (c) an application to initiate insolvency, restructuring (including proceedings such as legal protection proceedings and out-of-court legal protection proceedings) or administration of the Issuer or any of its Material Subsidiaries or any other proceedings for the settlement of the debt of the Issuer or of any of its Material Subsidiaries is submitted to the court by the Issuer or any of its Material Subsidiaries.

16.4. In case of the Issuer's liquidation or insolvency the Noteholders shall have a right to receive payment of the outstanding principal amount of the Notes and the interest accrued on the Notes according to the relevant laws governing liquidation or insolvency of the Issuer.

17. Force Majeure

17.1. The Issuer, the Arrangers and the Dealers shall be entitled to postpone the fulfilment of their obligations hereunder, in case the performance is not possible due to continuous existence of any of the following circumstances:

- (i) action of any authorities, war or threat of war, rebellion or civil unrest;
- (ii) disturbances in postal, telephone or electronic communications which are due to circumstances beyond the reasonable control of the Issuer, the Arrangers or the Dealers and that materially affect operations of any of them;
- (iii) any interruption of or delay in any functions or measures of the Issuer, the Arrangers or the Dealers as a result of fire or other similar disaster;
- (iv) any industrial action, such as strike, lockout, boycott or blockade affecting materially the activities of the Issuer, the Arrangers or the Dealers even if it only affects part of the employees of any of them and whether any of them is involved therein or not;
- (v) any epidemics, pandemics or quarantines that materially affect operations of the Issuer, the Arrangers or the Dealers; or
- (vi) any other similar force majeure or hindrance which makes it unreasonably difficult to carry on the activities of the Issuer, the Arrangers or the Dealers.

17.2. In such case the fulfilment of the obligations may be postponed for the period of the existence of the respective circumstances and shall be resumed immediately after such circumstances cease to exist, provided that the Issuer, the Arrangers and the Dealers shall put all best efforts to limit the effect of the above referred circumstances and to resume the fulfilment of their obligations as soon as possible.

18. Further Issues

The Issuer may from time to time, without the consent of and notice to the Noteholders, create and issue further Notes whether such further Notes form a single Series with already issued Notes or not. For the avoidance of doubt, this Clause 18 shall not limit the Issuer's right to issue any other notes.

19. Purchases

The Issuer or any of its Subsidiaries may at any time purchase the Notes in any manner and at any price in the secondary market. Such Notes may be held, resold or surrendered by the purchaser through the Issuer for cancellation. Notes held by or for the account of the Issuer or any of its Subsidiaries for their own account will not carry the right to vote at the Noteholders' Meetings or within Written Procedures and will not be taken into account in determining how many Notes are outstanding for the purposes of these General Terms and Conditions.

20. Time bar

In case any payment under the Notes has not been claimed by the respective Noteholder entitled to this payment within 10 (ten) years from the original due date thereof, the right to such payment shall be forfeited by the Noteholder and the Issuer shall be permanently released from such payment.

21. Notices

Noteholders shall be advised of matters relating to the Notes by a notice published in English and Latvian in the Central Storage of Regulated Information, on the website of Nasdaq Riga and on the Issuer's website www.latvenergo.lv. Any such notice shall be deemed to have been received by the Noteholders when published in the manner specified in this Clause 21.

22. Representation of the Noteholders

The rights of the Noteholders to establish and/or authorize an organization/person to represent interests of all or a part of the Noteholders are not contemplated, however, such rights are not restricted. The Noteholders should cover all costs/fees of such representative(s) by themselves.

23. Decisions of the Noteholders

23.1. General provisions

- (i) The decisions of the Noteholders (including decisions on amendments to these General Terms and Conditions or the Final Terms of the Tranches of the relevant Series or granting of consent or waiver) shall be passed at a meeting of the Noteholders (the “**Noteholders’ Meeting**”) or in writing without convening the Noteholders’ Meeting (the “**Written Procedure**”) at the choice of the Issuer. However, the Issuer shall have a right to amend the technical procedures relating to the Notes in respect of payments or other similar matters without the consent of the Noteholders, if such amendments are not prejudicial to the interests of the Noteholders.
- (ii) The Issuer shall have a right to convene the Noteholders’ Meeting or instigate the Written Procedure at any time and shall do so following a written request from the Noteholders who, on the day of the request, represent not less than one-tenth of the principal amount of the Notes outstanding or the principal amount of the Notes of the relevant Series outstanding (as applicable) (excluding the Issuer and its Subsidiaries).
- (iii) In case convening of the Noteholders’ Meeting or instigation of the Written Procedure is requested by the Noteholders, the Issuer shall be obliged to convene the Noteholders’ Meeting or instigate the Written Procedure within 1 (one) month after receipt of the respective Noteholders’ written request.
- (iv) Only those who were registered as the Noteholders by the end of the 6th (sixth) Business Day prior to convening the Noteholders’ Meeting or instigation of the Written Procedure or proxies authorised by such Noteholders, may exercise their voting rights at the Noteholders’ Meeting or in the Written Procedure.
- (v) Quorum at the Noteholders’ Meeting or in respect of the Written Procedure only exists if one or more Noteholders holding 50 (fifty) per-cent in aggregate or more of the principal amount of the Notes outstanding or the principal amount of the Notes of relevant Series outstanding (as applicable):
 - (a) if at the Noteholders’ Meeting, attend the meeting; or
 - (b) if in respect of the Written Procedure, reply to the request.
- (vi) If the Issuer and/or its Subsidiaries are the Noteholders, their principal amount of the Notes will be excluded when a quorum is calculated.
- (vii) If quorum does not exist at the Noteholders’ Meeting or in respect of the Written Procedure, the Issuer shall convene a second Noteholders’ Meeting (in accordance with Clause 23.2 (a)) or instigate a second Written Procedure (in accordance with Clause 23.3 (a)), as the case may be. The quorum requirement in paragraph (iv) above shall not apply to such second Noteholders’ Meeting or Written Procedure, except for exclusion of Issuer and its Subsidiaries from calculation of a quorum.
- (viii) Consent of the Noteholders holding at least 75 (seventy-five) per-cent of the aggregate principal amount of the outstanding Notes attending the Noteholders’ Meeting or participating in the Written Procedure is required for agreement with the Issuer to amend Clause 3 (*Status and security*),

Clause 14 (*Change of control*), Clause 15 (*Negative pledge*), Clause 16 (*Events of Default*), Clause 23 (*Decisions of the Noteholders*) or Clause 24 (*Governing law and dispute resolution*).

- (ix) Consent of at least 75 (seventy-five) per-cent of the aggregate principal amount of the outstanding Notes of the respective Series attending the Noteholders' Meeting or participating in the Written Procedure is required for the following decisions:
 - (a) agreement with the Issuer to change the date, or the method of determining the date, for the payment of principal, interest or any other amount in respect of the relevant Series, to reduce or cancel the amount of principal, interest or any other amount payable on any date in respect of the relevant Series or to change the method of calculating the amount of interest or any other amount payable on any date in respect of the relevant Series;
 - (b) agreement with the Issuer to change the currency of the relevant Series;
 - (c) agreement with the Issuer on any exchange or substitution of the Notes of relevant Series for, or the conversion of the Notes of relevant Series into, any other obligations or securities of the Issuer or any other person;
 - (d) in connection with any exchange, substitution or conversion of the type referred to in paragraph (c) agreement with the Issuer to amend any of the provisions of the relevant Series describing circumstances in which the relevant Series may be redeemed or declared due and payable prior to their scheduled maturity.
- (x) Consent of simple majority of all Noteholders or the Noteholders of the respective Series (as applicable) attending the Noteholders' Meeting or participating in the Written Procedure is required to the decisions not covered in paragraph (viii) or (ix) above (as applicable).
- (xi) The Issuer shall have a right to increase the aggregate principal amount of the Notes to be issued under the Programme without the consent of the Noteholders.
- (xii) Information about decisions taken at the Noteholders' Meeting or by way of the Written Procedure shall promptly be provided to the Noteholders in accordance with Clause 21 (*Notices*), provided that a failure to do so shall not invalidate any decision made or voting result achieved.
- (xiii) Decisions passed at the Noteholders' Meeting or in the Written Procedure shall be binding on all Noteholders irrespective of whether they participated at the Noteholders' Meeting or in the Written Procedure.
- (xiv) All expenses in relation to the convening and holding the Noteholders' Meeting or a Written Procedure shall be covered by the Issuer.

23.2. Noteholders' Meetings

- (i) If a decision of the Noteholders is intended to be passed at the Noteholders' Meeting, then a respective notice of the Noteholders' Meeting shall be provided to the Noteholders in accordance with Clause 21 (*Notices*) no later than 10 (ten) Business Days prior to the meeting. Furthermore, the notice shall specify the time, place and agenda of the meeting, as well as any action required on the part of the Noteholders that will attend the meeting. No matters other than those referred to in the notice may be resolved at the Noteholders' Meeting.
- (ii) The Noteholders' Meeting shall be held in Riga, Latvia, and its chairman shall be the Issuer's representative appointed by the Issuer.
- (iii) The Noteholders' Meeting shall be organised by the chairman of the Noteholders' Meeting.

- (iv) The Noteholders' Meeting shall be held in English with translation into Latvian, unless the Noteholders present in the respective Noteholders' Meeting unanimously decide that the respective Noteholders' Meeting shall be held only in Latvian or English.
- (v) Representatives of the Issuer and persons authorised to act for the Issuer may attend and speak at the Noteholders' Meeting.
- (vi) Minutes of the Noteholders' Meeting shall be kept, recording the day and time of the meeting, attendees, their votes represented, matters discussed, results of voting, and resolutions which were adopted. The minutes shall be signed by the keeper of the minutes, which shall be appointed by the Noteholders' Meeting. The minutes shall be attested by the chairman of the Noteholders' Meeting, if the chairman is not the keeper of the minutes, as well as by one of the persons appointed by the Noteholders' Meeting to attest the minutes. The minutes from the relevant Noteholders' Meeting shall at the request of a Noteholder be sent to it by the Issuer.

23.3. Written Procedure

- (i) If a decision of the Noteholders is intended to be passed by the Written Procedure then a respective communication of the Written Procedure shall be provided to the Noteholders in accordance with Clause 21 (*Notices*).
- (ii) Communication in paragraph (i) above shall include:
 - (a) each request for a decision by the Noteholders;
 - (b) a description of the reasons for each request;
 - (c) a specification of the Business Day on which a person must be registered as a Noteholder in order to be entitled to exercise voting rights;
 - (d) instructions and directions on where to receive a form for replying to the request (such form to include an option to vote "yes" or "no" for each request), as well as a form of a power of attorney;
 - (e) the stipulated time period within which the Noteholder must reply to the request (such time period to last at least 10 (ten) Business Days from the communication pursuant to paragraph (i) above) and a manner of a reply; and
 - (f) a statement that if the Noteholder does not reply to the request in the stipulated time period, then it shall be deemed that the Noteholder has voted against each request.
- (iii) When the requisite majority consents pursuant to paragraphs (vii), (ix) or (x) (as applicable) of Clause 23.1 have been received in a Written Procedure, the relevant decision shall be deemed to be adopted pursuant paragraphs (vii), (ix) or (x) (as applicable) of Clause 23.1 even if the time period for replies in the Written Procedure has not yet expired.

24. Governing law and dispute resolution

24.1. The Notes are governed by the laws of the Republic of Latvia.

24.2. Any disputes relating to or arising in relation to the Notes shall be settled solely by the courts of the Republic of Latvia of competent jurisdiction.

FORM OF FINAL TERMS

Set out below is the form of Final Terms which will be completed for each Tranche of Notes issued under the Base Prospectus.

[PROHIBITION OF SALES TO RETAIL INVESTORS IN THE EUROPEAN ECONOMIC AREA]

The Notes are not intended to be offered, sold or otherwise made available to and should not be offered, sold or otherwise made available to any retail investor in the European Economic Area ("EEA"). For these purposes, a retail investor means a person who is one (or more) of: (i) a retail client as defined in point (11) of Article 4(1) of Directive 2014/65/EU (as amended) ("**MiFID II**"); (ii) a customer within the meaning of Directive (EU) 2016/97 (as amended or superseded), where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II; or (iii) not a qualified investor as defined in Regulation (EU) 2017/1129 (as amended, the "**Prospectus Regulation**").]

[MiFID II Product Governance / Eligible Counterparties and Professional Clients Only Target Market]

Solely for the purposes of [the] [each] manufacturer['s']['s'] product approval process, the target market assessment in respect of the Notes has led to the conclusion that (i) the target market for the Notes is eligible counterparties and professional clients only, each as defined in [Directive 2014/65/EU (as amended, "**MiFID II**")] [MiFID II]; and (ii) all channels for distribution of the Notes to eligible counterparties and professional clients are appropriate. **[specify further target market criteria] [specify negative target market, if applicable]**. Any person subsequently offering, selling or recommending the Notes (a "**Distributor**") should take into consideration the manufacturer['s']['s'] target market assessment; however, a Distributor subject to MiFID II is responsible for undertaking its own target market assessment in respect of the Notes (by either adopting or refining the manufacturer['s']['s'] target market assessment) and determining appropriate distribution channels.]

[MiFID II Product Governance / Eligible Counterparties, Professional Clients and Retail Clients Target Market]

Solely for the purposes of [the] [each] manufacturer['s'] ['s'] product approval process, the target market assessment in respect of the Notes has led to the conclusion that (i) the target market for the Notes is eligible counterparties, professional clients and retail clients, each as defined in [Directive 2014/65/EU (as amended, "**MiFID II**")] [MiFID II], and [(ii) all channels for distribution of the Notes are appropriate[, including investment advice, portfolio management, non-advised services and execution-only]] [(ii) the following channels for distribution of the Notes are appropriate: investment advice [,] [and] portfolio management [,] [and] [non-advised services] [and execution-only]] [(ii) all channels for distribution to eligible counterparties and professional clients are appropriate; and (iii) the following channels for distribution of the Notes to retail clients are appropriate: investment advice [,] [and] portfolio management [,] [and] [non-advised services] [and execution-only] [, subject to the distributor's suitability and appropriateness obligations under MiFID II, as applicable]. **[specify further target market criteria] [specify negative target market, if applicable]** Any person subsequently offering, selling or recommending the Notes (a "**Distributor**") should take into consideration the manufacturer['s']['s'] target market assessment; however, a Distributor subject to MiFID II is responsible for undertaking its own target market assessment in respect of the Notes (by either adopting or refining the manufacturer['s']['s'] target market assessment) and determining appropriate distribution channels.]

Final Terms dated [●]

Latvenergo AS

Legal entity identifier (LEI): 213800DJRB539Q1EMW75

Issue of [Aggregate Nominal Amount of Tranche] Notes due [●]

under the Third programme for the issuance of Notes in the amount of EUR 200,000,000

[to be consolidated and form a single series with [●]]

Terms used herein shall be deemed to be defined as such for the purposes of the General Terms and Conditions set forth in the Base Prospectus dated 14 April 2020 [and the supplement(s) to it dated [●] which [together] constitute[s] a base prospectus for the purposes of the Prospectus Regulation] (the “**Base Prospectus**”) for the purposes of Regulation (EU) 2017/1129 (the “**Prospectus Regulation**”).

This document constitutes the Final Terms of the Notes described herein for the purposes of the Prospectus Regulation and must be read in conjunction with the Base Prospectus. Full information on the Issuer and the offer of the Notes is only available on the basis of the combination of these Final Terms and the Base Prospectus.

The Base Prospectus has been published on the Issuer’s website www.latvenergo.lv/lv/investoriem.

A summary of the individual issue is annexed to these Final Terms.

1. Issuer: Latvenergo AS
2. Series Number: [●]
3. Tranche Number: [●]
4. ISIN: [[●]]/[Temporary ISIN: [●]. Upon admission of the Notes to the regulated market the Notes will be consolidated and form a single series with [●] and will have a common ISIN [●]]
5. Aggregate principal amount: [EUR [●] [in addition to [●]]]
6. Nominal amount of the Note: EUR [●]
7. Issue Date: [●]
8. Annual Interest Rate: [●]
9. Interest Payment Date: [●] each year
10. Maturity Date: [●]
11. Minimum Investment Amount: [●]
12. Issue Price: [●]
13. Yield: [●]

The yield is calculated at the Issue Date on the basis of the Issue Price. It is not an indication of future yield
14. Placement Period: [●]
15. Name of the Settlement Agent: [●]
16. Rating: the Notes to be issued [are not/have been/are expected to be] rated [by:[●]]
17. Use of Proceeds: [General Corporate Purposes]/[Green Bonds].
18. Information about the securities of the Issuer that [●]

are already admitted to
trading:

These Final Terms have been approved by the Management Board of the Issuer at its meeting on [*date*]
[*month*] [*year*].

Riga, [*date*] [*month*] [*year*]

[•]

USE OF PROCEEDS

The net proceeds from the issue of each Series of Notes will, unless otherwise specified in the applicable Final Terms, be used by the Issuer as follows:

- (i) where “General Corporate Purposes” is specified in the applicable Final Terms, for its general corporate purposes; or
- (ii) where “Green Bonds” is specified in the applicable Final Terms, the Issuer will apply an amount equivalent to the net proceeds from such issue of Notes specifically to finance or refinance, in part or in full, projects in renewable energy and related infrastructure, energy efficiency and environmentally sustainable management of living natural resources and land use, as set out in the Green Bond Framework (the “**Eligible Green Projects**”) available on the Issuer’s website www.latvenergo.lv.

INFORMATION ABOUT THE GROUP

General information

The legal and commercial name of the Company is Latvenergo AS. The Company is a public limited company (*akciju sabiedrība*) incorporated pursuant to the laws of the Republic of Latvia on 8 October 1991. The Company is registered with the Commercial Register of the Republic of Latvia and operates according to the legislation of the Republic of Latvia. All the shares of the Company are owned by the Republic of Latvia and held by the Ministry of Economics of the Republic of Latvia.

Basic information

Registration number: 40003032949
Legal Entity Identifier (LEI): 213800DJRB539Q1EMW75
Registered address: Pulkveža Brieža 12, Riga, LV-1230, Latvia
Website: www.latvenergo.lv
Telephone number: +371 67 728 222

The information on the Company's website www.latvenergo.lv does not form part of the Base Prospectus, other than the Issuer's Green Bond Framework, which is available in the Company's website: www.latvenergo.lv/lv/investoriem and is incorporated by reference to this Base Prospectus and forms a part of the Base Prospectus.

History and development of the Group

In October 1939, the first hydroelectric unit of Kegums hydropower plant - the first hydropower plant on the Daugava River – was launched.

On 22 December 1939, the National Electricity Company Kegums was founded, which is the historical starting point of the Group.

In the second half of the 20th century, a power system in the territory of Latvia was developed and the electrification of Latvia was launched. The main power plants were constructed and gradually put into operation, including Plavinas HPP (1965) and Riga HPP (1974) on the Daugava River, Riga CHPP-1 (1955) and Riga CHPP-2 (1975). The transmission and distribution systems were established during the respective time period.

From 1990-2014, reconstruction and renovation work was carried out on the power stations and transmission and distributions systems in order to improve capacity, efficiency and safety.

In 2001, the electric power transmission segment was separated from the operations of the Company and the wholly owned subsidiary Augstsprieguma tīkls AS was established. In 2005, Augstsprieguma tīkls AS started to function as a legally independent transmission system operator.

In 2005, a 51 percent controlling share in Liepājas Enerģija SIA was acquired. The Company's subsidiary deals with electricity and thermal energy generation, transmission and sales in the Liepaja district (Latvia).

In 2006, the electric power distribution segment was separated from the operations of the Company and the wholly owned subsidiary Sadales tīkls AS was established. In 2007, Sadales tīkls AS started to function as a legally independent distribution system operator.

In 2007-2008, the Group expanded its business abroad. The Company's wholly owned subsidiaries Latvenergo Kaubandus OÜ (in Estonia) and Latvenergo Prekyba UAB (in Lithuania) were established within the main business area – electricity trade – in each country. In 2012, the Estonian and Lithuanian subsidiaries were rebranded as Elektrum and registered as Elektrum Eesti OÜ (in Estonia) and Elektrum Lietuva UAB (in Lithuania).

In 2011-2012, for the purpose of fulfilling the requirements of legal and functional unbundling of transmission system ownership from generation, distribution and supply activities, the Company's wholly-owned subsidiary Latvijas elektriskie tīkli AS was established as the owner of the electricity transmission system assets, and the transmission system operator Augstsprieguma tīkls AS was sold to the Republic of Latvia, represented by the Ministry of Finance.

In 2014, a new wholly-owned subsidiary of the Company – Energijas publiskais tirgotājs AS – was established. In compliance with the Energy Law (in Latvian – *Enerģētikas likums*), the subsidiary performs the functions of public trader in Latvia.

On the date of publication of this Base Prospectus, the Company is the parent company of the Group. The Group includes seven subsidiaries, six of which are wholly-owned by the Company.

Key consolidated financial figures

The following table summarizes key consolidated financial data and operating figures as of and for each of the years ended 31 December 2015, 2016, 2017, 2018 and 2019. The information set out in the table below has been extracted (without any material adjustment) from, and is qualified by reference to and should be read in conjunction with the audited Group's consolidated and the Company's annual reports for the years ending 31 December 2018 and 31 December 2019.

| | | Year ended 31 December | | | | |
|---------------------------------------|-----------|------------------------|--------|--------|-------|-------|
| | | 2015 | 2016 | 2017 | 2018 | 2019 |
| Key Financial data (the Group) | | | | | | |
| Revenue * | € million | 885 | 886 | 881 | 839 | 842 |
| EBITDA * | € million | 263 | 347 | 498 | 282 | 244 |
| Operating profit * | € million | 89 | 151 | 214 | 82 | 100 |
| Profit | € million | 85 | 131 | 322 | 76 | 94 |
| Total assets | € million | 3,517 | 3,901 | 4,416 | 3,799 | 3,865 |
| Total equity | € million | 2,097 | 2,419 | 2,847 | 2,320 | 2,265 |
| Net Debt (adjusted) * | € million | 605 | 529 | 497 | 505 | 564 |
| Investments | € million | 190 | 201 | 244 | 221 | 229 |
| Return on equity (ROE) | per-cent | 4.1 | 5.8 | 12.2 | 2.9 | 4.1 |
| Net debt to equity (adjusted) * | per-cent | 29 | 22 | 17 | 22 | 25 |
| Net debt to EBITDA (adjusted) * | times | 2.3 | 1.6 | 1.0 | 1.8 | 2.2 |
| Net Cash-flow (the Group) | | | | | | |
| - from operating activities | € million | 246 | 341 | 338 | 303 | 315 |
| - from financing activities | € million | (63) | (84) | (56) | (171) | (67) |
| - from investing activities | € million | (171) | (178) | (230) | (238) | (255) |
| Operating Figures (the Group) | | | | | | |
| Total electricity supply, incl.: | GWh | 9,868 | 10,140 | 10,371 | 9,984 | 9,259 |
| Retail ¹⁾ | GWh | 7,961 | 7,665 | 6,923 | 6,954 | 6,505 |
| Wholesale ²⁾ | GWh | 1,907 | 2,474 | 3,448 | 3,030 | 2,754 |
| Retail natural gas | GWh | | | 33 | 147 | 303 |
| Electricity generation | GWh | 3,882 | 4,707 | 5,734 | 5,076 | 4,880 |
| Thermal energy generation | GWh | 2,408 | 2,675 | 2,612 | 2,274 | 1,842 |

(*) Excluding discontinued operations (transmission system assets). On 8 October 2019, the Cabinet of Ministers of the Republic of Latvia decided to support full unbundling of ownership of the electricity transmission system operator until 1 July 2020.

1) Including operating consumption

2) Including sale of energy purchased within mandatory procurement on the Nord Pool

There have not been any recent material events that would be relevant for assessing solvency of the Company and the Group.

The Group's strategy

The Group's Strategy 2017-2022 defines the strategic operational and financial goals 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.

After evaluating challenges in the external environment and the strong position of the Group, three strategic goals were identified:

1. strengthening a sustainable and economically sound market position in home markets (in the Baltics), while considering geographical and/or product/service expansion;
2. developing a generation portfolio adequate for synergy with trade and increasing the Group's value;
3. developing a functional, safe and efficient network corresponding to customer needs.

Strengthening the market position

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

The Group is one of the largest energy service providers in the Baltics and currently operates in all energy trading segments in Latvia, Lithuania and Estonia.

In 2019, the Group sold 6.5 TWh of electricity. Electricity sales outside Latvia amounted to 2.3 TWh and accounted for one third of the total retail sales of electricity.

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 well-considered gas offers for customers. During the strategy period, the Group sells natural gas to business customers in all three Baltic countries and since 2019, to Latvian households. In 2019, natural gas retail sales of the Group amounted to 303 GWh, which is two times more than in 2018. The amount of natural gas consumed by the Group for its own use and sold to customers amounted to 7.1 TWh in 2019.

During the strategy period, the Group has started to offer its customers in the Baltics a range of new products and services, such as solar panels, energy-risk insurance, *Smart House* technologies, and different electrical devices in the Elektrum online store. *Elektrum Solar* has become the most popular new service among customers, placing the Company among the leaders in the retail of solar panels in the Baltic region. The Group also sees the potential for development in the field of electromobility and took a significant step in 2019 by opening its first publicly available high and medium-speed charging stations in Riga and Jurmala.

Generation portfolio adequate for synergy with trade

The Group has a balanced portfolio of efficient, environmentally friendly electricity generation capacities – 1 025 MW at the CHPPs, 1 558 MW at the HPPs and 8 MW at other small plants – allowing the Group to operate successfully in both base and peak regimes and providing flexibility in adjusting operations to electricity market processes. In addition, the Group has also heat generation capacities – 1 617 MW at the CHPPs and 221 MW at other plants.

The renewal of the Daugava HPPs' hydropower units has continued successfully. Five of twenty-three hydropower units have been modernized over a three-year period and the reconstruction project is scheduled for completion in 2023 by reconstructing the remaining 6 units, while 12 units have been modernised in previous strategy periods. The programme increases the installed capacity, efficiency and amount of power

generated in hydropower units. More efficient use of renewable energy – namely, water, also reduces the Group's impact on climate change.

As the HPPs and the CHPPs are complementary sources of electricity production, both CHPPs play a very important role in providing generation capacities during periods when the water inflow in the Daugava River was low. In order to increase the efficiency of production in cogeneration mode, in 2019 the construction of the largest heat storage tank in the Baltic States was started at Riga CHPP-2. The construction is expected to be completed in 2020, and the increase in Riga CHPP-2's operational flexibility and efficiency will facilitate the operation of the power plant in adapting to changing market requirements while further reducing greenhouse gas emissions.

Along with the above-mentioned projects, research is being conducted regarding projects for new power generation facilities compliant with the criteria of diversification of primary resources and low emissions, for example wind power.

Functional, safe and efficient network

This goal 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.

Significant improvements in the continuity of supply have been achieved during the strategy period so far. Reconstruction and upgrading of the distribution network, as well as improvements in work process planning and management have been carried out. All these actions, since 2016, has reduced the System Average Interruption Duration Index (SAIDI) by 14 per-cent and the System Average Interruption Frequency Index (SAIFI) by 15 per-cent. The digitisation of the distribution network is also continuing rapidly and successfully – at the end of 2019, smart meters accounted for 63 per-cent of the total meter fleet and 86 per-cent of the total amount of electricity distributed.

In 2017, the Group launched the Efficiency Programme, the largest optimization plan in the last decade, which will allow the Group to maintain and enhance its long-term value and competitiveness. Within the framework of the programme the structure of the Company's subsidiary Sadales tīkls AS was reorganized, processes were centralized and the number of transport units, distribution bases and employees was significantly reduced. The cost reduction has made it possible to reduce the variable part of the distribution service tariff by an average of 5.5 per-cent from 1 January 2020.

INFORMATION ABOUT THE GROUP'S BUSINESS OPERATIONS

The operations of the Group are organised along three operating segments:

- (i) generation and trade;
- (ii) distribution; and
- (iii) lease of transmission system assets.

The generation and trade segment includes generation of electricity and thermal energy, conducted by the Company and Liepājas enerģija SIA, as well as electricity and natural gas trade in the Baltics carried out by the Company and its subsidiaries Elektrum Eesti OÜ and Elektrum Lietuva UAB and administration of the mandatory electricity procurement process in Latvia handled by the Company's subsidiary Enerģijas publiskais tirgotājs AS.

The distribution segment provides electricity distribution services in Latvia. The services are provided by the Company's subsidiary Sadales tīkls AS – the largest distribution system operator in Latvia.

The operations of lease of transmission system assets segment are managed by the Company's subsidiary Latvijas elektriskie tīkli AS – the owner of transmission system assets. The Republic of Latvia has applied the second unbundling model under EU Directive 2009/72/EC, which stipulates that the electricity transmission system assets shall remain with a vertically integrated utility, while the activities of the transmission system operator are independently managed. The assets are leased out to the Latvian transmission system operator Augstsprieguma tīkls AS. However, given that the second unbundling model is one of the rarest in Europe, and based on an assessment by the Ministry of Economics, on 8 October 2019 the Cabinet of Ministers of the Republic of Latvia decided to support full unbundling of ownership of the electricity transmission system operator until 1 July 2020, stipulating that transmission assets will be taken over from the Company by Augstsprieguma tīkls AS. Since the Company and Augstsprieguma tīkls AS are both state-owned companies, the change of ownership of assets will occur through the reduction of the share capital of the Company by withdrawing the capital shares of Latvijas elektriskie tīkli AS from the base of assets of the Company. After the capital shares of Latvijas elektriskie tīkli AS become the property of the State, it is intended to invest them in the share capital of Augstsprieguma tīkls AS.

The information set out in the table below has been extracted (without any material adjustment) from, and is qualified by reference to and should be read in conjunction with the audited Group's consolidated and the Company's annual reports for the years ending 31 December 2018 and 31 December 2019.

| | Year ended 31 December | | | | |
|---|------------------------|--------------|--------------|--------------|--------------|
| | 2015 | 2016 | 2017 | 2018 | 2019 |
| Key financial data divided in the operating segments: | | | | | |
| | (€ million) | | | | |
| Revenue | 929 | 932 | 926 | 878 | 878 |
| Generation and trade | 610 | 584 | 556 | 512 | 518 |
| Distribution | 284 | 308 | 321 | 323 | 320 |
| Lease of transmission system assets (discontinued operations) | 47 | 48 | 47 | 42 | 40 |
| Other* | -12 | -9 | 2 | 1 | 0 |
| EBITDA | 307 | 393 | 542 | 322 | 281 |
| Generation and trade | 164 | 224 | 373 | 147 | 103 |
| Distribution | 82 | 105 | 112 | 120 | 125 |
| Lease of transmission system assets (discontinued operations) | 45 | 47 | 45 | 41 | 40 |
| Other* | 16 | 16 | 12 | 14 | 13 |
| Assets | 3,517 | 3,901 | 4,416 | 3,799 | 3,865 |
| Generation and trade | 1,555 | 1,557 | 1,957 | 1,329 | 1,347 |
| Distribution | 1,337 | 1,629 | 1,641 | 1,670 | 1,681 |

| | | | | | |
|--|-----|-----|-----|-----|-----|
| Lease of transmission system assets (discontinued operations) | 432 | 449 | 501 | 579 | 642 |
| Other* | 193 | 266 | 317 | 221 | 195 |

* Including corporate functions, adjustments and eliminations

The Group reports financial results in respect of each operating segment since 2011.

Generation and trade

Generation and trade is the largest business segment of the Group by revenue.

Activities within this segment include electricity and thermal energy generation operations, electricity and natural gas trade in the Baltics and administration of mandatory procurement in Latvia.

The majority of generation and trade segment revenues are unregulated, while the tariff-regulated operational revenues comprise revenues from:

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

In 2019, the majority or 87 per-cent of the revenue of the segment was comprised of electricity and natural gas trade revenue, while thermal energy revenue accounted for 13 per-cent.

The generation business is subdivided according to generation types – the HPPs, the CHPPs and other generation units. The total installed electrical capacity of the Group's plants is 2,591 MW, of which 40 per-cent is installed at the CHPPs and 60 per-cent at the HPPs. The total installed thermal energy capacity of the Group is 1,838 MW.

Trade

The Group trades electricity and natural gas in the Baltic States under the *Elektrum* brand. The Group is one of the leading energy traders in the Baltic States. In 2019, its market share accounted for about 23 per-cent of the Baltic electricity market.

The size of the Baltic electricity market was approximately 28 TWh in 2019. The largest market is Lithuania, with 12 TWh, followed by the Estonian market with 9 TWh and the Latvian market with 7 TWh. The Lithuanian market is also the largest Baltic market in terms of number of customers. The Estonian electricity market is the largest among the three Baltic countries measured by per capita electricity consumption. The relatively higher electricity consumption level in Estonia is explained by the country's substantial level of industrialization and a relatively higher number of homes heated with electricity.

The Group is the electricity market leader in Latvia, holding 58 per-cent market share in 2019. The Group's market share in both Lithuania and Estonia was 11 per-cent in 2019. The Group's main competitor in the Baltic market is Eesti Energia AS, the market leader in Estonia. The market is more fragmented in Lithuania, where the Group is among the largest market players.

The amount of electricity supplied by the Group in the Baltics was 6,505 GWh in 2019. The amount of electricity supplied outside Latvia represents more than one third of the total retail electricity trade, reaching 2,293 GWh in 2019.

With the liberalization of the natural gas market, in 2017, the Group commenced natural gas sales to customers in the Baltics. In 2019, natural gas retail sales of the Group amounted to 303 GWh, which is 2 times more than in 2018. The Group is the second largest natural gas consumer in the Baltics. The amount of natural gas consumed by the Group for its own use and sold to customers amounted to 7.1 TWh in 2019.

The Group's strategic goals envisage development of new products and services to complement the traditional ones and promote synergy with the current business lines and customer base. The products and services are

designed for different consumption and usage patterns, so that each customer can choose the most suitable offer. Since 2017, the Group has provided *Elektrum Smart House* service, which allows for remote control of electricity and heating devices, and *Elektrum Solar* service, which allows for electricity generation using solar panels. In 2019, Elektrum e-shop, which offers electric appliances, including smart home appliances and solar panels, and the first Elektrum electrical vehicle fast charging stations were launched.

In 2019, the Group had 757,000 customers across the Baltics, including 35,000 outside of Latvia. Of these, 95 per-cent were households and 5 per-cent were business customers.

Mandatory procurement

The electricity public supplier licence includes an obligation for the Group to purchase electricity from supported generation types under the feed-in tariff scheme and to provide guaranteed payments for the capacity installed at power plants (cogeneration plants with installed capacity above 4 MW). In accordance with the Energy Law (in Latvian – *Enerģētikas likums*), as of 1 April 2014, the functions of public trader are performed by the Company's subsidiary Enerģijas publiskais tirgotājs AS.

The public trader is compensated for mandatory procurement net expenditures¹ through the mandatory procurement public service obligation fee (the “**PSO Fee**”) paid by the end-users in Latvia and a state budget grant. The amount of the PSO Fee is determined based on actual expenditures in the preceding year as approved by the PUC. As of 1 July 2018, the PSO Fee is EUR 2.268 cents per kWh on average.

Since 2017, support through the reduced PSO Fee for energy-intensive processing industry companies has also been provided. The Ministry of Economics decides on the reduction of the PSO Fee payments for energy-intensive companies

Wholesale

Since 2014, the Group has traded all its electricity on the Nord Pool Spot exchange and at the same time procured electricity to supply customer consumption, increasing electricity supply and turnover in the Latvian bidding area. The generation capacity of the Group also ensures the electricity supply support services, such as provision of emergency back-up capacity and supply of regulating electricity to transmission system operators as well as supply of balancing electricity.

The electricity wholesale process is targeted at cost optimisation and provides economic benefits to both the Group and its customers. Generation volumes of the CHPPs and the 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 between electricity supply sources: the power exchange and the Group's own power plants. This way, the Group can 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.

Generation

The Group has a balanced and environmentally friendly energy generation portfolio, consisting mostly of the HPPs and highly efficient CHPPs. Most of the electricity and thermal energy is generated by the three Daugava HPPs and two CHPPs. Energy is also generated by Liepājas enerģija SIA, Aiviekste HPP and Ainazi Wind Power Plant (WPP).

¹ Mandatory procurement net expenditures – costs of electricity procured within the mandatory procurement process and guaranteed payments for installed capacity at power plants minus revenues from trade of procured electricity on the Nord Pool Spot exchange

The total electrical capacity of generators installed at the Group's production facilities as of 31 December 2019 was 2,591 MW_{el}, whereas the total heat generation capacity of installed thermal generation facilities was 1,838 MW_{th}.

The Group's installed electrical capacity as of 31 December 2019:

| | 31 December 2019 |
|----------------|---------------------|
| | (MW _{el}) |
| Daugava HPPs | 1,558 |
| Riga CHPPs* | 1,025 |
| Liepaja plants | 6 |
| Small plants | 2 |
| Total | 2,591 |

*installed capacity in condensation mode

The Group's thermal energy capacity of installed generation facilities as per 31 December 2019:

| | 31 December 2019 |
|----------------|---------------------|
| | (MW _{th}) |
| CHPPs | 1,617 |
| Liepaja plants | 221 |
| Total | 1,838 |

Generation at the HPPs

The Group's three largest HPPs – the *Plavinas*, *Kegums* and *Riga* plants - are located on the Daugava River. These are the biggest HPPs in the country, providing a large share of renewable energy not only in the Group, but also in Latvia.

In 2019, the HPPs on the Daugava River generated more than 2 TWh of electricity, which constituted 42 per-cent of the Group's total electricity output. The output of the HPPs was 27 per-cent lower than the long-term average value for the period 1981-2018 (2.8 TWh). Although, the HPPs have a large installed capacity, their ability to generate electricity is dependent on the water inflow. The average water inflow in the Daugava River in 2019 was 401 m³/s, while in 2018 it was 485 m³/s. In 2019, it was 33 per-cent lower than the long-term average value. According to the Latvian Environment, Geology and Meteorology Centre, the average water inflow in the Daugava River was close to 600 m³/s for the period 1992–2019. In years with normal inflow levels, the HPPs usually operate at full capacity only during spring flooding, which typically lasts for about 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 flood, it is possible to cover the demand for electricity of all the Group's customers and trade the excess on the Nord Pool exchange. Outside the flooding season, the HPPs on the Daugava River provide for the possibility to accumulate water and generate electricity when the demand and prices on the exchange are higher.

The Plavinas HPP is the largest HPP in the Baltics in terms of installed capacity. 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. It started operations in 1968 with ten hydropower units with a total capacity of 825 MW_{el} at that time. Following a reconstruction of the hydropower units, the plant's installed capacity was increased, resulting in a total capacity of 908 MW_{el} as of 31 December 2019. The reconstruction of the hydropower units has resulted not only in increased capacities and efficiency ratios, but also in an increased share of energy produced from renewable sources.

The Kegums HPP is the oldest HPP on the Daugava River, built from 1936-1939 and restored from 1945-1947. The installed capacity of the plant reaches 248 MW_{el}. Currently, reconstruction of the plant's hydropower units is in progress.

The *Riga HPP* entered into service in 1974 and has six hydropower units with a total capacity of 402 MW_{el}. Currently, reconstruction of hydropower units of the plant is in progress.

Generation at the CHPPs

The CHPPs are mostly operated in a highly efficient cogeneration mode in accordance with the thermal energy demand. The CHPPs operate efficiently and flexibly, and the operating modes of the CHPPs are adjusted to the electricity market conditions. In 2018 and 2019, the Group's CHPPs 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 2019, for the second year in a row, the CHPPs generated historically the largest amount of electricity – 2.8 TWh, which is 5 per-cent more than in 2018.

The CHPPs receive electricity capacity payments. The support period ends in 2028. In 2017, the Company received a one-off compensation from the state in the amount of EUR 454.4 million, at the same time opting out of the receipt of 75 per-cent of the annual electrical capacity payments for the CHPPs. In 2019, the Company received EUR 24 million as the annual electrical capacity payments for the CHPPs. After 2020, this payment will decrease to about EUR 20 million as Riga CHPP-1 support period ends in late 2020. The compensation was financed by the capital release of the Company and was divided into two parts: EUR 140 million were recognized as other income in the profit and loss statement of the Company in 2017, while EUR 314 million were recognized as income spread evenly over the following reporting periods until fulfilment of liabilities at the end of the support period. In 2018, the Cabinet of Ministers decided to extend additional compensation in the amount of EUR 51.7 million by reducing the remaining part of the compensation proportionally to this amount until the end of the support period.

The thermal energy generated at the CHPPs is sold to Rīgas siltums AS at regulated tariffs. The Group competes with other thermal energy generators in the thermal energy market of Riga.

Riga CHPP-1 was built from 1954 -1958 and fully reconstructed in 2005. The installed electrical capacity and thermal capacity at Riga CHPP-1 is 144 MW_{el} and 493 MW_{th} respectively.

Riga CHPP-2 is the most efficient and advanced combined-cycle power plant in the Baltics, which was launched in 1973. The reconstruction of Riga CHPP-2 was commenced in 2006. The construction of the first power unit was completed in 2008, and the second unit was commissioned at the end of 2013. With the commissioning of the second power unit, the electrical capacity of Riga CHPP-2 in cogeneration mode reached 832 MW_{el}, and the total thermal energy capacity of the two power units is 544 MW_{th}. The total thermal energy capacity of Riga CHPP-2, including water boilers, is 1,124 MW_{th}.

The CHPPs comprise a guarantee of electricity base-load capacity and can cover almost all of Latvian electricity consumption in circumstances where due to certain factors electricity import from foreign countries is limited.

Other generation units

The Company holds 51 per-cent of the equity in Liepājas enerģija SIA. This company primary ensures generation and supply of thermal energy to Liepaja, a city in Latvia. The total installed thermal energy capacity of the Liepaja plants as of 31 December 2019 was 221 MW_{th}, including 40 MW_{th} from a renewable resource (wood chips). Installed electrical capacity totalled 6 MW_{el}.

Generation facilities within the energy system of the Group also include two small power plants: the Ainazi wind power plant (WPP) with a capacity of 1.0 MW_{el}, and the Aiviekste HPP with a capacity of 0.8 MW_{el}.

Distribution

Distribution is the largest operating segment within the Group in terms of asset value and the second largest in the terms of revenue. Its operations involve provision of distribution services to approximately 800,000 customers in Latvia at regulated tariffs.

The distribution system service is provided by the Company's subsidiary Sadales tīkls AS, the largest distribution system operator in Latvia. The distribution system operator ensures equal access to electricity distribution networks, which is one of the prerequisites for facilitating competition on the electricity market in Latvia. The electricity distribution network ensures the flow of electricity from the electricity transmission network and electricity generators to electricity consumers. The total length of low and medium-voltage cable and overhead lines at the end of 2019 was 92,958 km, with 30,437 transformers and 27,845 transformer substations with a total installed capacity of 6,110 MVA. The total volume of distributed electricity in 2019 was 6,532 GWh, and electricity losses were 3.7 per-cent, which is historically the lowest level.

The PUC develops the methodology and approves tariffs for distribution system operators. On 30 September 2019, the PUC announced amendments to the existing tariff methodology. Elements of a revenue cap approach with efficiency factors, a regulatory account and a five-year regulatory period were introduced. The new tariff regulation methodology provides incentives to reduce service costs and guarantees their recovery.

Considering the changes in the methodology of calculation of distribution tariffs set by the PUC, in October 2019, Sadales tīkls AS submitted and the PUC approved a draft of the electricity distribution service tariff for a period of 5 years as of 1 January 2020. The draft provides for a reduction of the tariff of 5.5 per-cent on average. The lower distribution tariff is possible due to the ambitious operational efficiency improvement programme of Sadales tīkls AS, which includes process improvement, as well as the reduction of personnel and the number of vehicles and real estate bases.

The electricity distribution service tariff takes into account recent changes in the weighted average cost of capital (WACC) calculation approved by the PUC in August 2019. The pre-tax real WACC rate was set at 3.31 per-cent. Since allowed revenue is calculated in real terms, an adjustment of the regulated asset base (RAB) is based on revaluation.

Lease of transmission system assets

The operation of the segment is ensured by the Company's subsidiary Latvijas elektriskie tīkli AS, which is the owner of the transmission 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.

At the end of 2019, the total length of electricity transmission lines was 5,424 km. Seventeen 330 kV substations with a total automatic transformer capacity of 4,075 MVA and one hundred twenty-three 110 kV substations with a total installed transformer capacity of 5,264 MVA are maintained in order to ensure the operation of the transmission network.

In order to comply with the EU requirements, in 2011 Latvia introduced an independent system operator model. However, such a transmission asset unbundling model is one of the rarest in Europe. Therefore, based on an assessment made by the Ministry of Economics, the Cabinet of Ministers of the Republic of Latvia decided to support the introduction of a full electricity transmission ownership unbundling model in Latvia by 1 July 2020. Since the Company and Augstsprieguma tīkls AS are both state-owned companies, the change of ownership of assets will occur through the reduction of the share capital of the Company by withdrawing the capital shares of Latvijas elektriskie tīkli AS from the base of assets of the Company. After the capital shares of Latvijas elektriskie tīkli AS become the property of the State, they will be invested in the share capital of Augstsprieguma tīkls AS.

Investments

The Group's operations are capital intensive and require significant investments. The following table summarises the total investments of the Group for the period 2015 -2019. The information set out in the table below has been extracted (without any material adjustment) from, and is qualified by reference to and should be read in conjunction with the audited Group's consolidated and the Company's annual reports for the years ending 31 December 2018 and 31 December 2019.

| | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|-------------|------|------|------|------|
| | (€ million) | | | | |
| Investments | 190 | 201 | 244 | 221 | 229 |
| incl. transmission system assets (discontinued operations) | 17 | 26 | 63 | 87 | 87 |

Along with the unbundling of transmission assets (see information before), the scope of investments in the coming years will decrease significantly.

On-going investments (committed capital expenditures) as of 31 December 2019

The table below provides information as of 31 December 2019 on contractually committed capital investments of the Group.

| | 2020 | 2021 | 2022 | Later |
|------------------------------------|-------------|-------------|------------|------------|
| | (€ million) | | | |
| Generation | 30.4 | 11.6 | 1.4 | 1.7 |
| <i>Daugava HPPs reconstruction</i> | 15.6 | 11.6 | 1.4 | 0.2 |
| Distribution | 32.9 | | | |
| Other | 6.7 | 0.4 | 0.2 | 0 |
| Total committed | 70.1 | 11.9 | 1.6 | 1.7 |

According to the development plan of Sadales tīkls AS, large investments are made in the maintenance and development of distribution networks each year. In 2019, investments in the distribution segment remained at the same level as in 2018 and comprised EUR 95.1 million or approximately 40 per-cent of the total amount of the Group's investment. Investments in the distribution segment are focused on modernisation of lines and reconstruction of transformer substations (65 per-cent of distribution investments in 2019). Other major areas of investment include connections of new customers (19 per-cent) and introduction of smart electricity meters (5 per-cent). Distribution investments exceeded the segment's depreciation in 2019 (EUR 75.3 million).

Currently, according to the Energy Law (in Latvian – *Enerģētikas likums*), the Company's subsidiary Latvijas elektriskie tīkli AS is obliged to finance investments in transmission system assets. The transmission system operator Augstsprieguma tīkls AS sets and the PUC approves the amount of investments for the next 10 years. Latvijas elektriskie tīkli AS assesses financing options and finances the investments implemented by Augstsprieguma tīkls AS. Latvijas elektriskie tīkli AS has the right to refuse the provision of financing, which means that Augstsprieguma tīkls AS may decide upon other financing options. The ten-year investment plan is annually revised by Augstsprieguma tīkls AS. According to the transmission system development plan, the contingent liabilities of the Group are EUR 62.9 million, EUR 25.0 million and EUR 45.0 million for 2020, 2021 and 2022 respectively. Total financing needs for transmission system assets amount to EUR 413 million according to the latest 10-year investment plan approved by the PUC. After the capital shares of Latvijas elektriskie tīkli AS become the property of Augstsprieguma tīkls AS, the obligation to finance investments in transmission assets will be transferred to Augstsprieguma tīkls AS.

The Group has one major on-going committed investment project - the reconstruction project of the Daugava HPPs – and, until the introduction of a full electricity transmission ownership unbundling model in Latvia by 1 July 2020, one ongoing contingent investment project: *Estonia–Latvia third interconnection*. Other commitments comprise regular maintenance and replacements.

Daugava HPPs hydropower unit reconstruction programme

The Group is pursuing gradual reconstruction of 11 Daugava HPPs hydropower units. The programme is scheduled for completion in 2023, with estimated total reconstruction costs exceeding EUR 200 million.

As of 31 December 2019, five reconstructed hydropower units have been put into operation within the programme and work completed within the scope of the contract reached EUR 166.1 million. The Group is

proceeding with a gradual overhaul of 6 Daugava HPPs' hydropower units. The rest of the HPPs' hydropower units were reconstructed fairly recently.

Estonia-Latvia third interconnection

Implementation of this project is part of the 10-year electricity transmission network development plan devised by Augstsprieguma tīkls AS. The new 330 kV interconnection will increase the available throughput between the Latvian and Estonian energy systems, decreasing the price difference between the Estonian and Latvian/Lithuanian bidding areas. Three parties are involved in the implementation of the project: the Estonian transmission system operator Elering OÜ, the Latvian transmission system operator Augstsprieguma tīkls AS and the Company's subsidiary Latvijas elektriskie tīkli AS as the owner of transmission system assets in Latvia. The planned length of the new 330 kV interconnection line is about 190 km in Latvia, and it is scheduled for completion by late 2020. The construction costs of the project on the Latvian side are expected to total about EUR 100 million. EU co-funding in the amount of 65 per-cent of all eligible costs of the project has been attracted.

Financing

In order to finance committed capital investments, the Group uses cash flow from operating activities and borrowed funds. External funding consists of bilateral bank loans and issued bonds. The Group has established long-standing funding cooperation with international investment banks and commercial banks. The Group has diversified borrowing sources by issuing bonds during preceding years. The outstanding principal amount of bonds issued is EUR 135 million (of which EUR 100 million are green bonds), representing 15 per-cent of the total debt as of 31 December 2019.

The Group's gross debt as of 31 December 2019 was EUR 882.7 million with the following debt maturity schedule:

| | 2020 | 2021 | 2022 | 2023 | 2024 | 2025-2034 | Total |
|-----------------------|--------------|--------------|--------------|--------------|-------------|--------------|--------------|
| | (€ million) | | | | | | |
| Debt repayment | 180.7 | 107.1 | 147.7 | 112.6 | 96.3 | 238.3 | 882.7 |

The table below provides information about the Group's borrowings by lender category as of 31 December 2019.

| | 31 December 2019 |
|--------------------------------|------------------|
| | (€ million) |
| International investment banks | 351.5 |
| Commercial banks | 394.3 |
| Issued bonds | 136.9 |
| Total | 882.7 |

Borrowings outstanding were used to fund the Group's investment programme including the modernisation of power generation, transmission and distribution assets.

In late 2019, the Company attracted a loan from the Nordic Investment Bank in the amount of EUR 100 million, and a loan agreement with a maturity of up to 2 years was concluded with OP Corporate Bank plc Latvian branch in the amount of EUR 15 million. As of 31 December 2019, the total amount of committed credit lines available to the Group was EUR 85 million. In January 2020, a loan agreement with a maturity of up to 2 years in the amount of EUR 60 million was signed with SEB banka AS, thereby increasing the amount of available committed credit lines.

All borrowings are denominated in euros. As of 31 December 2019, the weighted average repayment period was 4.2 years. With interest rate swaps, 45 per-cent of the borrowings had a fixed interest rate with a weighted

average interest fixing period of 1.8 years. The effective weighted average interest rate (with interest rate swaps) of the Group's outstanding borrowings was 1.5 per-cent.

ORGANISATIONAL STRUCTURE

As of the publication date of this Base Prospectus, the Group comprises the parent company Latvenergo AS and its seven subsidiaries:

| Company Name | Country of incorporation | Business activity | Proportion of ownership |
|--|--------------------------|--|-------------------------|
| Subsidiaries: | | | |
| Sadales tīkls AS | Latvia | Electricity distribution | 100 per-cent |
| Latvijas elektriskie tīkli AS | Latvia | Lease of transmission system assets | 100 per-cent |
| Enerģijas publiskais tirgotājs AS | Latvia | Administration of electricity mandatory procurement process | 100 per-cent |
| Elektrum Eesti OÜ | Estonia | Electricity and natural gas trade | 100 per-cent |
| Elektrum Latvija SIA (subsidiary of Elektrum Eesti OÜ) | Latvia | Electricity and natural gas trade | 100 per-cent |
| Elektrum Lietuva UAB | Lithuania | Electricity and natural gas trade | 100 per-cent |
| Liepājas Enerģija SIA | Latvia | Electricity and thermal energy generation and supply (in Liepāja city) | 51 per-cent |

The Company is a shareholder in an associated company, Pirmais Slēgtais Pensiju Fonds AS (Latvia), engaged in the management of retirement contributions on behalf of the Group's employees (the Company's and the Group's shareholding is 46.3 per-cent and 48.15 per-cent respectively). In addition, the Group has a financial investment in Rīgas siltums AS (0.005 per-cent), which is engaged in supply of thermal energy in Riga.

On 8 October 2019, the Cabinet of Ministers of the Republic of Latvia decided to support full unbundling of ownership of the electricity transmission system operator until 1 July 2020, stipulating that transmission assets will be transferred from the Company to Augstsprieguma tīkls AS. Since the Company and Augstsprieguma tīkls AS are both state-owned companies, the change of ownership of assets will occur through the reduction of the share capital of the Company by withdrawing the capital shares of Latvijas elektriskie tīkli AS from the base of assets of the Company. After the capital shares of Latvijas elektriskie tīkli AS become the property of the State, they will be invested in the share capital of Augstsprieguma tīkls AS.

ADMINISTRATIVE, MANAGEMENT AND SUPERVISORY BODIES

In accordance with the Commercial Law (in Latvian – *Komerclikums*), the Law on the Management of Public Persons' Capital Shares and Capital Companies (in Latvian - *Publiskas personas kapitāla daļu un kapitālsabiedrību pārvaldības likums*) and the Financial Instruments Market Law (in Latvian – *Finanšu instrumentu tirgus likums*), the Company has the following corporate governance structure:

- Shareholder;
- Supervisory Board;
- Audit Committee; and
- Management Board.

Shareholder

100% of the shares of the Company 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 the Management of Public Persons' Capital Shares and Capital Companies (in Latvian - *Publiskas personas kapitāla daļu un kapitālsabiedrību pārvaldības likums*).

The Shareholders' Meeting represents the shareholder interests, rights and obligations. The State Secretary of the Ministry of Economics of the Republic of Latvia or his authorised representative is the sole shareholder representative in the Shareholders' Meetings.

Supervisory Board

The principal duties of the Supervisory Board of the Company include:

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

The Supervisory Board of the Company is elected by the Shareholders Meeting of the Company. The most recent Supervisory Board of the Company was elected at the Shareholders Meeting of the Company on 9 October 2019. The current Supervisory Board is composed of three members, and they represent the Ministry of Economics.

On the date of publication of this Base Prospectus the members of the Supervisory Board of the Company are:

- Mr. Edmunds Valantis - Chairman of the Supervisory Board
- Mr. Edijs Šaicāns - Deputy of the Supervisory Board
- Ms. Irēna Bērziņa - Member of the Supervisory Board

In August 2019, the Ministry of Economics as the shareholder of the Company announced a tender for 5 positions as Members of the Supervisory Board of the Company. When the procedure stated is completed as stipulated, new members will be elected.

The activities of the Management Boards of the Company's subsidiaries Sadales tīkls AS, Latvijas elektriskie tīkli AS and Enerģijas publiskais tirgotājs AS are supervised by the Shareholder Meetings of those subsidiaries, where the interests of the Company are represented by the Company's 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. The representatives of the Company's Management Board, as well as employees, who are responsible for the relevant areas of operation at the Company, are appointed to the Supervisory Boards of the abovementioned subsidiaries. The supervisory functions at Liepājas enerģija SIA, where the equity share of the Company is 51 per-cent, are carried out by a Supervisory Board of six members, half of whom are representatives of the Company. The supervisory functions at Elektrum Eesti OÜ and Elektrum Lietuva UAB are ensured by two Management Board members of the Company.

The business address of each member of the Company's Supervisory Board is Pulkveža Brieža 12, Riga, LV-1230, Latvia.

Audit Committee

The Audit Committee operates under the Commercial Law (in Latvian – *Komerclikums*), the Financial Instruments Market Law (in Latvian – *Finanšu instrumentu tirgus likums*) and the Regulations of the Audit Committee approved by the Shareholder.

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 of the Group;
- implementation of the Group's Fraud Risk Management Plan.

The Audit Committee shall consist of five members elected by the Shareholder Meeting, of whom at least one shall be a member of the Supervisory Board of the Company. The Audit Committee is chaired by its chairperson, elected by the members of the Audit Committee from amongst themselves.

The Audit Committee reports its assessments and findings to the Shareholder Meeting at least once a year. In addition, the Audit Committee regularly informs the members of the Supervisory Board of its conclusions and recommendations based on its work.

No restrictions have been imposed on the Audit Committee's actions, and the representatives of the Company ensure the availability of all necessary information to the Audit Committee.

On the date of publication of this Base Prospectus the members of the Audit Committee are:

- Mr. Torben Pedersen - Chairman of the Audit Committee
- Mrs. Marita Salgrāve - Member of the Audit Committee
- Mr. Svens Dinsdorfs - Member of the Audit Committee
- Ms. Irēna Bērziņa - Member of the Audit Committee

The business address of each member of the Company's Audit Committee is Pulkveža Brieža 12, Riga, LV-1230, Latvia.

Management Board

All Management Board members are executive directors of the Company, and are involved in the daily operations of the Company. Their principal duties include:

- management and representation of the Company;
- responsibility for the commercial activities of the 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 and the Supervisory Board 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.

As per the Articles of Association of the Company, the Company's Management Board shall consist of five members, who should be elected by the Supervisory Board for a term of five years based on an evaluation of necessary competences, experience and expected sphere of responsibility. The Supervisory Board of the Company also appoints one of the members of the Management Board as a Chairman of the Management Board.

On the date of publication of this Base Prospectus the Management Board of the Company consists of four Members of the Management Board:

- **Mr. Āris Žīgurs** - Chief Executive Officer and Chairman of the Management Board, responsible for corporate strategy, international affairs and corporate social responsibility, communication, human resource management, security and transport services. Mr. Žīgurs is a member of the Board of Directors at the Union of the Electricity Industry of Europe ("EURELECTRIC"), the vice-president of the Latvian National Committee of the World Energy Council, a member of the Board at the Employers' Confederation of Latvia and a member of the Council of Higher Education.
- **Mr. Guntars Baļčūns** - Chief Financial Officer, responsible for business planning and controlling, the treasury, accounting, risk management and insurance. Mr. Baļčūns is a member of the supervisory boards of the Company's subsidiaries Elektrum Eesti OÜ and Elektrum Lietuva UAB, as well as a member of the supervisory board of the Baltic Institute of Corporate Governance.
- **Mr. Uldis Bariss** - Chief Commercial Officer, responsible for sales, energy trading, marketing, customer service, customer settlements, and regulatory affairs. Mr. Bariss is the chairman of the supervisory boards of the Company's subsidiaries Elektrum Eesti OÜ and Elektrum Lietuva UAB.
- **Mr. Kaspars Cikmačs** - Chief Technology and Support Officer, responsible for managing IT&T, real estate, legal affairs, record management, procurement and logistics, and services support.

All members of the Management Board of the Company, except Mr. Cikmačs, were elected on 16 November 2015. Mr. Cikmačs was elected on 25 September 2018. The selection process of the fifth member of the Management Board is in progress.

The business address of each member of the Company's Management Board is Pulkveža Brieža 12, Riga, LV-1230, Latvia.

The Management Board and the Supervisory Board 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.

Conflict of interest

In accordance with the Law on Prevention of Conflict of Interest in the Activities of Public Officials (in Latvian – *Likums "Par interešu konflikta novēršanu valsts amatpersonu darbībā"*), all members of the management boards, the supervisory boards and the audit committees of state-owned companies have the status of state officials. As such, all Management Board, Supervisory Board and Audit Committee members of the Company and its fully owned subsidiaries in Latvia are state officials and subject to detailed requirements of this law. The law permits them to combine their office of public official only with activities which are indicated by the law as compatible (e.g., offices in a trade union, association or similar organisation, teaching, scientific and creative work) in order to prevent personal or material interest in their activity as a state official. In accordance with the law, all state officials are obliged to submit an annual declaration of interest.

The Company is not aware of any conflicts of interest or potential conflicts of interest between the Company duties of the members of the Management Board, Supervisory Board and Audit Committee and their private interests and/or their other duties.

Employees

As of 31 December 2019, the Group had 3,423 employees of whom 71 per-cent were men and 29 per-cent women. The average age of the employees was 44 years. In 2019, the Group's employee turnover was 5.1 per-cent.

The strategy of the 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 25 per-cent until 2022.

The opinions of all the Group's employees on issues pertaining to the Collective Bargaining Agreement are represented by "Enerģija" Trade Union in Latvia. About 60 per-cent of the Group's employees are members of this union. The Group notifies "Enerģija" Trade Union of, among other things, planned changes in the organisation of the Group and its subsidiaries or in remuneration. It also reports on the execution of the Collective Bargaining Agreement and on the fulfilment of occupational health and safety requirements. Furthermore, it agrees on terminations of employment of members of "Enerģija" Trade Union, if any.

SHAREHOLDERS

All shares of the Company are owned by the Republic of Latvia. The holder of the Company's shares is the Ministry of Economics of the Republic of Latvia, whose representative - the State Secretary of the Ministry of Economics or another authorised person appointed by the State Secretary of the Ministry of Economics, represents the Shareholder interests at Shareholder Meetings.

The Law on the Management of Public Persons' Capital Shares and Capital Companies (in Latvian - *Publiskas personas kapitāla daļu un kapitālsabiedrību pārvaldības likums*) provides that the Cabinet of Ministers has the right to appoint a specially established institution as the holder of the shares in state owned entities.

Pursuant to the current Energy Law (in Latvian - *Enerģētikas likums*), the Company's business is deemed to be of national importance and therefore, the Company's shares are not subject to privatisation or alienation.

SELECTED CONSOLIDATED FINANCIAL INFORMATION

The following table is a summary of the Group's consolidated financial performance and key performance indicators for the two financial years ending 31 December 2018 and 2019. The information set out in the table below has been extracted (without any material adjustment) from, and is qualified by reference to and should be read in conjunction with the audited Group's consolidated and the Company's annual reports for the years ending 31 December 2018 and 31 December 2019 each of which is attached to this Base Prospectus and forms an integral part of this Base Prospectus. The Group's consolidated and the Company's annual reports are prepared according to International Financial Reporting Standards (IFRS).

| | | Year ended 31 December | |
|---------------------------------------|-----------|------------------------|-------|
| | | 2018 | 2019 |
| Key Financial data (the Group) | | | |
| Revenue * | € million | 839 | 842 |
| EBITDA * | € million | 282 | 244 |
| Operating profit * | € million | 82 | 100 |
| Profit | € million | 76 | 94 |
| Total assets | € million | 3,799 | 3,865 |
| Total equity | € million | 2,320 | 2,265 |
| Net Debt (adjusted) * | € million | 505 | 564 |
| Investments | € million | 221 | 229 |
| Return on equity (ROE) | per-cent | 2.9 | 4.1 |
| Net debt to equity (adjusted) * | per-cent | 22 | 25 |
| Net debt to EBITDA (adjusted) * | times | 1.8 | 2.2 |
| Net Cash-flow (the Group) | | | |
| - from operating activities | € million | 303 | 315 |
| - from financing activities | € million | (171) | (67) |
| - from investing activities | € million | (238) | (255) |
| Operating Figures (the Group) | | | |
| Total electricity supply, incl.: | GWh | 9,984 | 9,259 |
| Retail ¹⁾ | GWh | 6,954 | 6,505 |
| Wholesale ²⁾ | GWh | 3,030 | 2,754 |
| Retail natural gas | GWh | 147 | 303 |
| Electricity generation | GWh | 5,076 | 4,880 |
| Thermal energy generation | GWh | 2,274 | 1,842 |

(*) Excluding discontinued operations (transmission system assets). On 8 October 2019, the Cabinet of Ministers of the Republic of Latvia decided to support full unbundling of ownership of the electricity transmission system operator until 1 July 2020.

1) Including operating consumption

2) Including sale of energy purchased within mandatory procurement on the Nord Pool

FINANCIAL AND TREND INFORMATION

Historical Financial Information

The Group's consolidated and the Company's annual reports as of and for the financial years ending 31 December 2018 and 31 December 2019 prepared according to IFRS are appended to this Base Prospectus and forms an integral part of it.

Legal and arbitration proceedings

Except as described below, the Group is not engaged in any governmental, legal or arbitration proceedings, nor is it aware of any such proceedings pending or threatened against it during the 12 month-period prior to the date of this Base Prospectus that may have, or have had in the recent past, a significant effect on the Company and/or the Group's financial position or profitability.

Incident of corruption

In June 2010, criminal proceedings were initiated against a number of executives of the Group suspected in corruption and money laundering. No charges have been brought against the Company or the subsidiaries of the Company. The Company has the status of a victim in the proceedings and has submitted an application for compensation in the total amount of EUR 25,249,048.80. As of January 2018, the case is being heard by the court of first instance.

The Group has reviewed internal processes for the purpose of bringing its internal control procedures in line with best practice, thus further reducing the risks of corruption, illegal activity or fraud within the Group.

Pricing commitment with the Competition Council of Latvia

On 20 November 2009, the Competition Council of the Republic of Latvia passed a decision closing the investigation against the Company regarding alleged exclusionary pricing practices in the thermal energy market in Riga City and accepting a written commitment (pricing commitment) from the Company. In 2019, the Company and the Competition Council started discussions aimed at updating the written commitment to reflect the current situation in the thermal energy market in Riga City. Discussions are still in progress.

Significant Changes in Financial Position

There has been no material adverse change in the Company's or the Group's financial or trading position since 31 December 2019.

Trend Information

On 27 February 2020, the Parliament of the Republic of Latvia (Saeima) included in the agenda the draft law "On Amendments to the Energy Law". The draft law provides for the deletion of some rules of the Energy Law, which defines payments of guaranteed fee for electrical capacity installed at cogeneration power plants. Also, it provides for terminating the order that states that the electricity costs incurred by the public trader in carrying out the statutory functions are borne by the final consumers. The draft law may cause impacts on the Group's profits and asset value.

There has been no other material adverse change in the prospects of the Company or the Group since the date of the audited consolidated annual financial statements of the Group for 2019.

There has been no significant change in in the financial performance of the Company or the Group since the date of the audited consolidated annual financial statements of the Group for 2019.

On the date of publication of this Base Prospectus there is no information on any known trends, uncertainties, demands, commitments or events that are reasonably likely to have a material effect on the Company's or the Group's prospects or the industries in which the Company or the Group operates.

Future Outlook

The Issuer has not made any profit forecast or profit estimate in this Base Prospectus.

ADDITIONAL INFORMATION

Share Capital

The amount of the share capital of the Company is EUR 834,883,449, and it is composed of 834,883,449 shares. All shares are paid up. All shares are registered shares and they are dematerialised. The nominal value of a share is EUR 1.

In accordance with the Energy Law (in Latvian - *Enerģētikas likums*), all shares of the Company are the property of the Republic of Latvia and they are not a subject to privatisation or alienation.

Articles of Association

The Company is registered with the Commercial Register of the Republic of Latvia under registration number 40003032949.

The objects and purposes of the Company are stated in Clause 2 of the Articles of Association of the Company; the main objects are to generate electricity and thermal energy, to trade electricity and natural gas.

Material Contracts

None of the Company nor any of its subsidiaries has entered into any contracts outside the ordinary course of its business, which could result in any of the Company or its subsidiaries being under an obligation or entitlement that is material to the ability of the Company, respectively to meet obligations in respect of the Notes being issued.

THE ECONOMY OF THE REPUBLIC OF LATVIA

General overview

After two years of impressive GDP growth, in 2019 the growth rate rather surprisingly slowed down to 2.2 per-cent. The deceleration of growth rate was underpinned by both internal factors (investments from EU funds had reached their pinnacle, developments in the financial sector, etc.) and external factors (global trade tensions, unfavourable developments in transit sector, slower demand growth in the EU). Domestic consumption still was the key driver of growth, although at a more moderate pace. Construction growth, which contributed significantly to GDP in 2017 and 2018, slowed down in 2019 to 2.9 per-cent and is expected to decline further in 2020. Manufacturing displayed a lacklustre performance growing only 2.1 per-cent where its main contributor - forestry industry experienced a reduction in output mainly due to lower product prices and weaker external demand. On the positive side, 2019 was a record year for grain harvest, with 3.2 million tonnes harvested, up by 1.1 million tonnes compared to the previous year. A lot of uncertainty still surrounds the overall prospects for the economy in 2020. The global consequences of Covid-19 outbreak will depend on the duration and the extent of the crisis, as well as the measures taken to contain it. At the time of publishing this Prospectus, it is clear that the crisis will hit most sectors of the economy and lead to a recession both in Europe and Latvia as factories and businesses suspend their activity, and workers stay at home to try to contain the virus.

| Real GDP growth, per-cent | 2015 | 2016 | 2017 | 2018 | 2019 |
|---------------------------|------|------|------|------|------|
| Latvia | 3.3 | 1.8 | 3.8 | 4.3 | 2.2 |
| EU (28) average | 2.3 | 2.0 | 2.6 | 2.0 | 1.5 |

Source: Eurostat

Inflation

Consumer price growth in Latvia continued at a steady rate of close but below 3 per-cent in 2019, and remained higher than the EU average, mainly fuelled by price pressures in the services industry. Average gross salaries in Latvia have been rising at more than 5 per-cent annual growth rate for the last six years, inevitably putting pressure on the prices. The trend will be reversed in 2020 as companies struggle to survive in an environment of low demand. Also, the price increases for goods will be subdued by developments in the global commodities markets, where prices have declined significantly. Weaker demand, due to global trade tensions and coronavirus outbreak spreading around the world, will likely lead to a very subdued price growth for 2020.

| Inflation, HICP, average, per-cent | 2015 | 2016 | 2017 | 2018 | 2019 |
|------------------------------------|------|------|------|------|------|
| Latvia | 0.2 | 0.1 | 2.9 | 2.6 | 2.7 |
| EU (28) average | 0.1 | 0.2 | 1.7 | 1.9 | 1.5 |

Source: Eurostat

Unemployment

Unemployment rate has been falling every year since the financial crisis, dropping to 6.3 per-cent in 2019. At the same time, the employment rate and the economic activity rate both have surpassed the pre-crisis levels. The number of vacancies has continued to grow and the labour market has been very favourable for job seekers. Shrinking working age population - the number of young adults added to the work force each year currently is lower than the number of people becoming eligible for pension, thus pressures in the job market will remain in the longer term. However, in the short to medium term the coronavirus crisis will bring a spike in the unemployment rate as some companies are laying-off non-essential workers and some are ceasing their business altogether. Once the crisis is over, the labour market will experience a sharp rebound as companies will resume hiring. It is, however, still very unclear whether the rebound could come already in 2020.

| Unemployment, per-cent | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------------|-------------|-------------|-------------|-------------|-------------|
| Latvia | 9.9 | 9.6 | 8.7 | 7.4 | 6.3 |
| EU (28) average | 9.4 | 8.6 | 7.6 | 6.8 | 6.3 |

Source: Eurostat

Public Finance

The central government budget for 2020 provides for 9.9 billion EUR in revenue and 10.0 billion EUR in expenditure, without major reforms in the tax regime. Although the government planned a 0.3 per-cent general budget deficit for 2020, it was based on an unrealistic GDP growth forecast of 2.8 per-cent and did not take into consideration the effects of the pandemic. Considering that the GDP growth will be negative in 2020 and that extra resources will be necessary to deal with the effects of Covid-19, it is expected that at least temporarily the deficit will increase considerably.

| General government balance, per-cent of GDP | 2015 | 2016 | 2017 | 2018 | 2019 |
|--|-------------|-------------|-------------|-------------|-------------|
| Latvia | -1.4 | 0.1 | -0.5 | -0.7 | N/A |
| EU (28) average | -2.4 | -1.7 | -1.0 | -0.7 | N/A |

Source: Eurostat; official data not available for 2019

On 21 February 2020, the international credit rating agency S&P Global Ratings upgraded Latvia's credit rating from "A" to "A+" while maintaining a stable outlook. The credit rating is at the highest level since 1997, when Latvia was first assigned a sovereign rating. Low public debt should provide Latvia's small and open economy with room for fiscal policy manoeuvres in case of external shocks. The ability to raise funding will be particularly important for combating the adverse effects that the coronavirus outbreak will have on the economy of Latvia. It is expected that public debt will increase considerably in 2020 as additional funds will be allocated to various parts of the economy.

| General government gross debt, per-cent of GDP | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|-------------|-------------|-------------|-------------|-------------|
| Latvia | 36.7 | 40.2 | 38.6 | 36.4 | N/A |
| EU (28) average | 84.9 | 83.8 | 82.1 | 80.4 | N/A |

Source: Eurostat; official data not available for 2019

Foreign Trade

In 2019, the foreign trade turnover of Latvia at current prices reached EUR 28.54 billion – 0.1 per-cent less than in 2018. The exports value constituted EUR 12.8 billion (an increase of 0.4 per-cent), whereas the imports value – EUR 15.75 billion (a drop of 0.3 per-cent). Wood and its products continue to be the dominant constituent of overall goods exports, while the exports of machinery, mechanical appliances and electrical equipment, from which more than half of the value is re-export, are close behind. The latter category also is by far the major part of country's imports. The other Baltic States, Russia, Germany and Poland continue to be the main trading partners for Latvia both in export and import. Foreign trade will also be negatively impacted by coronavirus crisis, as demand plummets all over the world.

| Current account balance, per-cent of GDP | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|-------------|-------------|-------------|-------------|-------------|
| Latvia | -0.9 | 1.4 | 1.0 | -0.7 | -0.5 |
| EU (28) average | 0.9 | 1.3 | 1.3 | 1.4 | 1.4 |

Source: Eurostat, Bank of Latvia

TAXATION

Tax legislation of the investor's member state and of the Issuer's country of incorporation may have an impact on the income received from the Notes.

The following is a general summary of certain tax consideration in the Republic of Latvia in relation to the Notes. It is not exhaustive and does not purport to be a complete analysis of all tax consequences relating to the Notes, as well as does not take into account or discuss the tax implications of any country other than the Republic of Latvia. The information provided in this section shall not be treated as legal or tax advice; and prospective investors are advised to consult their own tax advisors as to the tax consequences of the subscription, ownership and disposal of the Notes applicable to their particular circumstances.

This summary is based on the laws of Latvia as in force on the date of this Base Prospectus and is subject to any change in law that may take effect after such date, provided that such changes could apply also retroactively.

Latvia has entered into a number of tax conventions on elimination of the double taxation, which may provide more favourable taxation regime. Therefore, if there is a valid tax convention with the country of a non-resident prospective investor, it should be also examined. The procedures for application of tax conventions are provided in the Republic of Latvia Cabinet of Ministers' Regulations No. 178 "Procedures for Application of Tax Relief Determined in International Agreements for Prevention of Double Taxation and Tax Evasion" of 30 April 2001.

Taxation of the Noteholders individuals

Resident Individuals

An individual will be considered as a resident of Latvia for taxation purposes:

- if the individual's declared place of residence is in the Republic of Latvia; or
- if the individual stays in the Republic of Latvia 183 days or more within any 12-month period, starting or ending in the taxation year; or
- if the individual is a citizen of the Republic of Latvia employed abroad by the government of the Republic of Latvia.

In accordance with the Law on Personal Income Tax (in Latvian – *Likums "Par iedzīvotāju ienākuma nodokli"*) the interest income from the Notes for resident individuals will be subject to 20 per-cent withholding tax, deductible by the Issuer before the payment. The income from the alienation of the Notes will be subject to 20 per-cent tax, but the tax would be payable by the individual him/herself.

Non-resident individuals

In accordance with the Law on Personal Income Tax (in Latvian – *Likums "Par iedzīvotāju ienākuma nodokli"*) the interest income from the Notes being circulated publicly as well as income from the alienation of the publicly circulated Notes will not be subject to tax in Latvia.

Taxation of the Noteholders entities

Resident entities

An entity will be considered as a resident of Latvia for tax purposes if it is or should have been established and registered in the Republic of Latvia in accordance with the legislative acts of the Republic of Latvia. This also include permanent establishments of foreign entities in Latvia.

Interest payments on the Notes and proceeds from the disposal of the Notes received by Latvian resident companies will not be subject to withholding tax in Latvia. Under the Corporate Income Tax Law (in Latvian – *Uzņēmumu ienākuma nodokļa likums*) retained earnings are exempt from corporate income tax and only distributions are taxed. Corporate income tax rate on gross profit distribution is 20 per-cent. Corporate income tax on net amount of profit distribution is determined by dividing net amount with a coefficient of 0.8 (i.e., effective tax rate on net distributed profit is 25 per-cent).

Non-resident entities

In accordance with the Corporate Income Tax Law (in Latvian – *Uzņēmumu ienākuma nodokļa likums*) the interest income and income from the alienation of the Notes for non-resident entities will not be taxable in Latvia.

Taxation of low-tax non-residents

In general, payments (including interest payments) to non-residents located, registered or incorporated in a no-tax or low-tax country or territory as defined in the Regulations of the Cabinet of Ministers No.655 “Regulations on No-Tax or Low-Tax Countries and Territories”, adopted on 7 November 2017; effective as of 1 January 2018 (“**Low-Tax Non-Latvian Residents**”) are subject to withholding tax of 20 per-cent if the payer is a Latvian legal entity or 23 per-cent if the payer is a Latvian individual resident having obligation to withhold tax. However, pursuant to Article 5(6) of the Corporate Income Tax Law (in Latvian – *Uzņēmumu ienākuma nodokļa likums*) payments by Latvian legal entities to Low-Tax Non-Latvian Residents for securities publicly circulated in the EU or EEA are exempt from withholding tax if made at the market price. The State Revenue Service of the Republic of Latvia in a legally non-binding explanation to the Issuer has confirmed that pursuant to Article 5(6) of the of the Corporate Income Tax Law (in Latvian – *Uzņēmumu ienākuma nodokļa likums*) there is no withholding tax also on the interest payments made by the Issuer to the holders of the notes publicly circulated in the EU or EEA who are Low-Tax Non-Latvian Residents, provided that the payments are made at the market price.

GLOSSARY

| | |
|--------------------------------------|---|
| Aiviekste HPP | The Company's hydro power plant located at "Aiviekste 66", Aiviekste, Kalsnava county, Madona district, Latvia. |
| Ainazi Wind Power Plant (WPP) | The Company's wind power plant located at "Pūķi", Ainazi county, Salacgriva district, Latvia. |
| CHPPs | The Company's combined heat and power plants. |
| GW | Gigawatts, a unit for measuring the capacity to produce electricity. One gigawatt equals 1,000,000,000 watts. |
| GWh | Gigawatt hours, a unit for measuring the generation and consumption of electricity. |
| HPPs | The Company's hydro power plants. |
| Kegums HPP | The Company's hydro power plant located at Keguma prospekts 7/9, Kegums, Kegums district, Latvia. |
| kV | Kilovolts, a unit for measuring voltage or electrical tension. One kilovolt equals 1,000 volts. |
| MW | Megawatts, a unit for measuring the capacity to produce electricity. One megawatt equals 1,000,000 watts. |
| MWel | The capacity to produce electrical energy. |
| MWth | The capacity to produce thermal energy. |
| PUC | Public Utilities Commission. |
| Plavinas HPP | The Company's hydro power plant located at Energetiku street 2, Aizkraukle, Aizkraukle district, Latvia. |
| Riga CHPP-1 | The Company's combined heat and power plant located at Viskalu street 16, Riga, Latvia, LV-1026. |
| Riga CHPP-2 | The Company's combined heat and power plant located at Granīta street 31, Acone, Salaspils county, Salaspils district, Latvia. |
| Riga HPP | The Company's hydro power plant located at "Rīgas HES", Salaspils county, Salaspils district, Latvia. |
| TW | Terawatts. A unit for measuring the capacity to produce electricity. One terawatt equals 1,000,000,000,000 watts. |
| TWh | Terawatt hours, a unit for measuring the generation and consumption of electricity. One terawatt hour is equal to sustained electricity consumption of approximately 114 MW for a period of one year. |

GENERAL INFORMATION

Authorisation

The shareholder of the Issuer has at the Shareholders' Meeting held on 9 October 2019 authorised the issue of the Notes and authorised the Management Board of the Issuer to approve the characteristics of the Notes, the Base Prospectus and any of the documents thereto, as well as any amendments and supplements thereof.

Management Board of the Issuer has at its meeting held on 14 April 2020 approved the Base Prospectus and the General Terms and Conditions of the Notes.

Each Final Terms issued in respect of each issue of Notes shall be approved by a separate resolution of the Management Board of the Issuer.

Auditors

PricewaterhouseCoopers SIA, registration number: 40003142793, legal address: Kr.Valdemāra street 21-21, Riga, LV – 1010, Latvia, has audited the 2019 Financial Statements and the 2018 Financial Statements included in this Base Prospectus and issued an unqualified auditors' reports on the aforementioned financial statements.

PricewaterhouseCoopers SIA is included in the register of audit firms maintained by the Latvian Association of Certified Auditors and holds audit company license No.5. On behalf of PricewaterhouseCoopers SIA, the auditors' report on the 2019 Financial Statements was signed by Ilandra Lejiņa, holding auditor's certificate No. 168. The auditors' report on the 2018 Financial Statements was signed by Juris Lapše, holding auditor's certificate No.116.

Listing

Application will be made to Nasdaq Riga for admitting each Tranche to listing and trading on the official bond list (the Baltic Bond List) of Nasdaq Riga according to the requirements of Nasdaq Riga not later than within 3 (three) months after the Issue Date of the respective Tranche. Nasdaq Riga is a regulated market for the purposes of MiFID II.

Clearing of the Notes

The Notes shall be issued in the bearer dematerialised form and registered with Nasdaq CSD SE, registration number: 40003242879. The International Securities Identification Number (ISIN) in relation to the Notes of each Tranche will be specified in the relevant Final Terms.

The address of Nasdaq CSD SE is Valņu iela 1, Riga, LV-1050, Latvia.

Legal Entity Identifier

The Issuer's legal entity identifier is 213800DJRB539Q1EMW75.

Documents available

For as long as the Notes are listed on the official bond list (the Baltic Bond List) of Nasdaq Riga, the copies of the following documents will be available on the Issuer's website www.latvenergo.lv:

- (i) the Articles of Association of the Issuer;
- (ii) the Audited Financial Statements;
- (iii) the Green Bond Framework;

- (iv) each Final Terms; and
- (v) this Base Prospectus together with any supplement.

Arrangers and Dealers transacting with the Issuer

The Arrangers and Dealers have engaged in, and may in the future engage in, investment banking and/or commercial banking or other services provided to the Group in the ordinary course of business (see Section *Risk Factors – Risk related to the Notes - Certain material interests*).

Interests of natural and legal persons involved in the issue/offer of the Notes

Save for commissions to be paid to the Arrangers and the Dealers, so far as the Issuer is aware, no person involved in the issue/offer of the Notes has an interest material to the issue/offer.

Expenses Charged to the Investors

No expenses or taxes will be charged to the investors by the Issuer in respect to the issue of the Notes. However, the investors may be obliged to cover expenses which are related to the opening of securities accounts with the credit institutions or investment brokerage firms, as well as commissions which are charged by the credit institutions or investment brokerage firms in relation to the execution of the investor's purchase or selling orders of the Notes, the holding of the Notes or any other operations in relation to the Notes. Neither the Issuer, nor the Arrangers or the Dealers shall compensate the Noteholders for any such expenses.

Credit Ratings

As of the date of this Base Prospectus, the Issuer has a long-term credit rating Baa2 by Moody's. The outlook is stable.

Moody's Investors Service Ltd. is established in the EEA and is registered under Regulation (EU) No 1060/2009, as amended (the "**CRA Regulation**"), and is, as of the date of this Base Prospectus, included in the list of credit rating agencies published by the European Securities and Markets Authority ("**ESMA**").

Notes to be issued under the Programme may be rated or unrated. Where an issue of Notes is rated, the applicable rating will be specified in the relevant Final Terms. Such rating will not necessarily be the same as the rating(s) assigned to the Issuer or to Notes already issued (if applicable). Whether or not a credit rating applied for in relation to a relevant Series of Notes will be issued by a credit rating agency established in the EEA and registered under the CRA Regulation will be disclosed in the Final Terms.

A rating is not a recommendation to buy or sell or hold Notes and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency. Up-to-date information should always be sought by direct reference to the relevant rating agency.

INFORMATION INCORPORATED BY REFERENCE

The following documents have been incorporated by reference to this Base Prospectus and form a part of the Base Prospectus:

- the Issuer's Green Bond Framework, which is available for viewing on the following website:
www.latvenergo.lv/lv/investoriem

ANNEX I – FINANCIAL STATEMENTS

The Latvenergo Group Consolidated and Latvenergo AS Annual Report 2018, prepared in accordance with IFRS, together with the audit report in connection therewith.

The Latvenergo Group Consolidated and Latvenergo AS Annual Report 2019, prepared in accordance with IFRS, together with the audit report in connection therewith.



2018

**LATVENERGO GROUP CONSOLIDATED
AND LATVENERGO AS
ANNUAL REPORT**

Financial statements are prepared in accordance with international financial reporting standards as adopted by the EU

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FINANCIAL CALENDAR

Interim Condensed Financial Statements:

For the 3 months of 2019 (unaudited) – 31.05.2019

For the 6 months of 2019 (unaudited) – 30.08.2019

For the 9 months of 2019 (unaudited) – 29.11.2019

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 ¹⁾ | 321,582 | 541,696 | 393,399 | 307,015 | 236,838 |
| Operating profit ²⁾ | 95,762 | 234,082 | 160,773 | 108,188 | 49,243 |
| Profit before tax ³⁾ | 88,513 | 224,114 | 148,945 | 92,535 | 31,510 |
| Profit | 75,955 | 322,021 | 130,593 | 85,039 | 29,790 |
| Dividends ⁴⁾ | 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 ⁵⁾ | 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 – EBITDA¹⁾; EBITDA margin⁶⁾; operating profit margin⁷⁾; profit before tax margin⁸⁾; profit margin⁹⁾; return on assets (ROA)¹⁴⁾; return on equity (ROE)¹⁵⁾; return on capital employed (ROCE)¹⁶⁾;
- capital structure measures – net debt⁵⁾; equity-to-asset ratio¹⁰⁾; net debt / EBITDA¹¹⁾; net debt / equity¹²⁾; current ratio¹³⁾;
- a dividend policy measure – dividend pay-out ratio¹⁷⁾.

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.

¹⁾ EBITDA – earnings before interest, income tax, share of result of associates, depreciation and amortisation, and impairment of intangible assets and property, plant and equipment
²⁾ Operating profit – earnings before income tax, finance income and costs
³⁾ Profit before tax – earnings before income tax
⁴⁾ Dividends paid to the equity holder of the Parent Company.
(see Note 20 b)
⁵⁾ 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 ⁶⁾ | 36.6% | 58.5% | 42.2% | 33.0% | 23.4% |
| Operating profit margin ⁷⁾ | 10.9% | 25.3% | 17.3% | 11.6% | 4.9% |
| Profit before tax margin ⁸⁾ | 10.1% | 24.2% | 16.0% | 10.0% | 3.1% |
| Profit margin ⁹⁾ | 8.7% | 34.8% | 14.0% | 9.2% | 2.9% |
| Equity-to-asset ratio ¹⁰⁾ | 61% | 64% | 62% | 60% | 58% |
| Net debt / EBITDA ¹¹⁾ | 2.0 | 1.1 | 1.7 | 2.3 | 2.9 |
| Net debt / equity ¹²⁾ | 0.30 | 0.21 | 0.25 | 0.33 | 0.35 |
| Current ratio ¹³⁾ | 1.5 | 3.2 | 1.7 | 1.9 | 1.3 |
| Return on assets (ROA) ¹⁴⁾ | 1.8% | 7.7% | 3.5% | 2.4% | 0.8% |
| Return on equity (ROE) ¹⁵⁾ | 2.9% | 12.2% | 5.8% | 4.1% | 1.5% |
| Return on capital employed (ROCE) ¹⁶⁾ | 2.8% | 6.8% | 5.3% | 3.8% | 1.7% |
| Dividend pay-out ratio ¹⁷⁾ | 104% | 66% | 82% | 90% | 92% |

Operational figures

| | 2018 | 2017 | 2016 | 2015 | 2014 |
|----------------------------------|---------------|---------------|---------------|---------------|---------------|
| Total electricity supply, incl.: | | | | | |
| Retail* | GWh 9,984 | 10,371 | 10,140 | 9,868 | 9,427 |
| Wholesale** | GWh 6,954 | 6,923 | 7,665 | 7,961 | 8,800 |
| Electricity generated | GWh 3,030 | 3,448 | 2,474 | 1,907 | 627 |
| Thermal energy generated | GWh 5,076 | 5,734 | 4,707 | 3,882 | 3,625 |
| Number of employees | 2,274 | 2,612 | 2,675 | 2,408 | 2,560 |
| Moody's credit rating | 3,508 | 3,908 | 4,131 | 4,177 | 4,563 |
| | 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

⁶⁾ EBITDA margin = EBITDA / revenue

⁷⁾ Operating profit margin = operating profit / revenue

⁸⁾ Profit before tax margin = profit before tax / revenue

⁹⁾ Profit margin = profit / revenue

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

¹¹⁾ 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)

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

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

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

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

¹⁶⁾ 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))

¹⁷⁾ 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 ¹⁾ | 160,927 | 387,100 | 241,606 | 180,982 | 105,052 |
| Operating profit ²⁾ | 33,803 | 177,416 | 141,071 | 90,475 | 18,158 |
| Profit before tax ³⁾ | 212,760 | 185,906 | 156,290 | 103,212 | 35,045 |
| Profit | 212,733 | 150,891 | 137,441 | 94,750 | 34,800 |
| Dividends ⁴⁾ | 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 ⁵⁾ | 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 ⁶⁾ | 37.0% | 77.6% | 47.0% | 34.7% | 18.6% |
| Operating profit margin ⁷⁾ | 7.8% | 35.6% | 27.5% | 17.4% | 3.2% |
| Profit before tax margin ⁸⁾ | 48.9% | 37.3% | 30.4% | 19.8% | 6.2% |
| Profit margin ⁹⁾ | 48.9% | 30.3% | 26.8% | 18.2% | 6.2% |
| Equity-to-asset ratio ¹⁰⁾ | 63% | 65% | 68% | 68% | 66% |
| Net debt / equity ¹¹⁾ | 0.34 | 0.24 | 0.27 | 0.32 | 0.35 |
| Current ratio ¹²⁾ | 2.0 | 4.3 | 2.3 | 3.0 | 1.9 |
| Return on assets (ROA) ¹³⁾ | 6.3% | 4.4% | 4.3% | 3.0% | 1.1% |
| Return on equity (ROE) ¹⁴⁾ | 9.7% | 6.6% | 6.4% | 4.6% | 1.7% |
| Return on capital employed (ROCE) ¹⁵⁾ | 1.1% | 5.8% | 4.8% | 3.1% | 0.6% |
| Dividend pay-out ratio ¹⁶⁾ | 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) |

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

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

³⁾ Profit before tax – earnings before income tax

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

⁵⁾ Net debt = borrowings at the end of the year minus cash and cash equivalents at the end of the year

⁶⁾ EBITDA margin = EBITDA / revenue

⁷⁾ Operating profit margin = operating profit / revenue

⁸⁾ Profit before tax margin = profit before tax / revenue

⁹⁾ Profit margin = profit / revenue

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

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

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

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

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

¹⁵⁾ 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))

¹⁶⁾ 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 CO₂ 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 CO₂ 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.

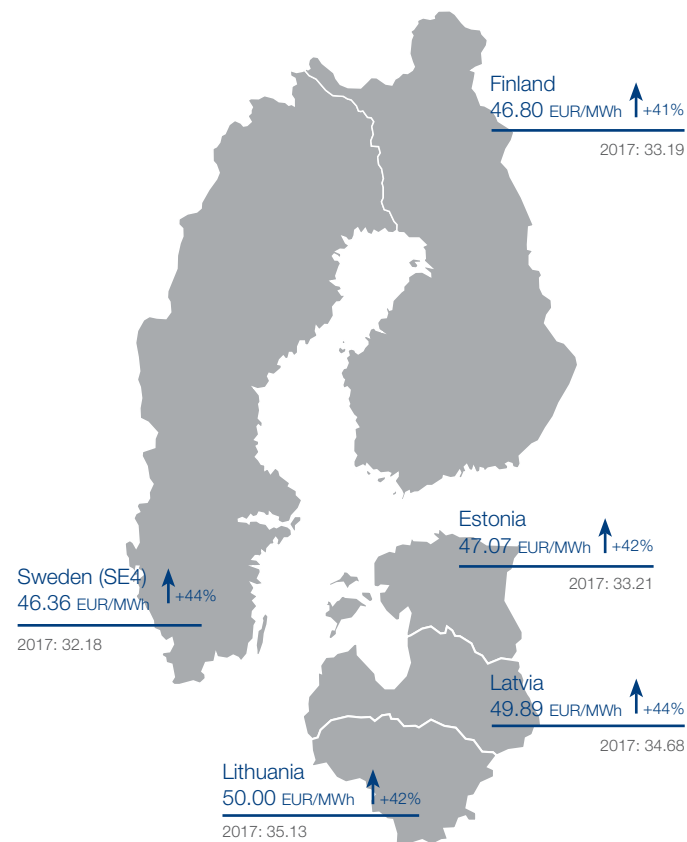
SIGNIFICANT EVENTS

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 m³/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.

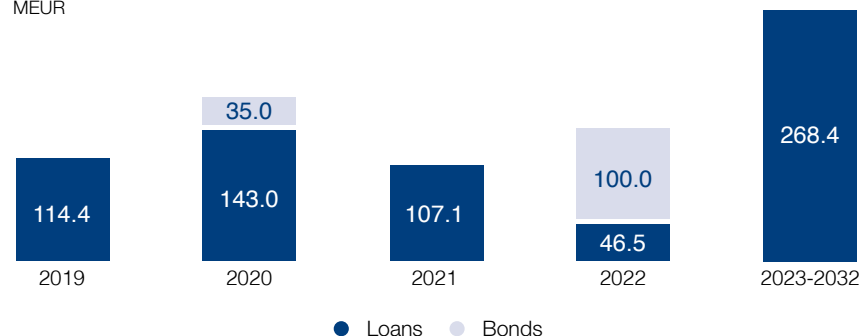
At the end of 2018, Latvenergo AS has committed loans from several banks for implementation of investment projects and in order to ensure loan refinancing risk management for a total amount of EUR 240 million with a repayment term of 7 and 10 years.

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 56⁴).

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 Cīkmačs

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) |
| Operating profit | | 95,762 | 234,082 | 33,803 | 177,416 |
| 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 |
| Profit before tax | | 88,513 | 224,114 | 212,760 | 185,906 |
| Current income tax | 12 | (261) | (51,199) | (27) | (45,097) |
| Deferred tax changes | 12 | (12,297) | 149,106* | – | 10,082* |
| Profit for the year | | 75,955 | 322,021 | 212,733 | 150,891 |
| Profit attributable to: | | | | | |
| – 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 15 to 68 are an integral part of these Financial Statements

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 COMPREHENSIVE INCOME

EUR'000

| | Notes | Group | | Parent Company | |
|---|------------|---------------|----------------|----------------|----------------|
| | | 2018 | 2017 | 2018 | 2017 |
| Profit for the year | | 75,955 | 322,021 | 212,733 | 150,891 |
| <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 |
| Net comprehensive income to be reclassified to profit or loss in subsequent periods | | 9,531 | 5,422 | 9,531 | 5,422 |
| <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 |
| Net comprehensive income / (loss) not to be reclassified to profit or loss in subsequent periods | | 436 | 192,280 | (108) | 139,398 |
| Comprehensive income for the year, net of tax | | 9,967 | 197,702 | 9,423 | 144,820 |
| TOTAL comprehensive income for the year | | 85,922 | 519,723 | 222,156 | 295,711 |
| Attributable to: | | | | | |
| – 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 15 to 68 are an integral part of these Financial Statements

Uldis Bariss

Member of the Management Board

Kaspars Cikmačs

Member of the Management Board

STATEMENT OF FINANCIAL POSITION

EUR'000

| | Notes | Group | | Parent Company | |
|--|---------|------------------|------------------|------------------|------------------|
| | | 31/12/2018 | 31/12/2017 | 31/12/2018 | 31/12/2017 |
| ASSETS | | | | | |
| Non-current assets | | | | | |
| 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 |
| TOTAL non-current assets | | 3,364,534 | 3,343,404 | 2,661,307 | 2,546,014 |
| Current assets | | | | | |
| 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 |
| TOTAL current assets | | 434,285 | 1,072,321 | 479,802 | 1,103,186 |
| TOTAL ASSETS | | 3,798,819 | 4,415,725 | 3,141,109 | 3,649,200 |

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 |
| EQUITY AND LIABILITIES | | | | | |
| EQUITY | | | | | |
| 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 |
| Equity attributable to equity holder of the Parent Company | | 2,311,607 | 2,838,849 | 1,993,823 | 2,382,638 |
| Non-controlling interests | | 8,458 | 8,042 | – | – |
| TOTAL equity | | 2,320,065 | 2,846,891 | 1,993,823 | 2,382,638 |
| LIABILITIES | | | | | |
| Non-current liabilities | | | | | |
| 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 |
| TOTAL non-current liabilities | | 1,183,439 | 1,238,556 | 913,221 | 1,009,959 |
| Current liabilities | | | | | |
| 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 |
| TOTAL current liabilities | | 295,315 | 330,278 | 234,065 | 256,603 |
| TOTAL EQUITY AND LIABILITIES | | 3,798,819 | 4,415,725 | 3,141,109 | 3,649,200 |

The notes on pages 15 to 68 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

| | Notes | Group | | | | | Parent Company | | | |
|---|----------|---|------------------|-------------------|------------------|-----------------------|---|----------------|-------------------|------------------|
| | | Attributable to equity holder of the Parent Company | | | | | Attributable to equity holder of the Parent Company | | | |
| | | Share capital | Reserves | Retained earnings | TOTAL | Non-control-interests | Share capital | Reserves | Retained earnings | TOTAL |
| As of 31 December 2016 | | 1,288,715 | 933,459 | 189,455 | 2,411,629 | 7,084 | 1,288,715 | 648,934 | 239,420 | 2,177,069 |
| Implementation effect of IFRS 15 'Revenue from Contracts with Customers' | | – | – | (10) | (10) | – | – | – | – | – |
| As of 1 January 2017 | | 1,288,715 | 933,459 | 185,845 | 2,411,619 | 7,084 | 1,288,715 | 648,934 | 238,334 | 2,177,069 |
| Dividends for 2016 | 20 b | – | – | (90,142) | (90,142) | (1,393) | – | – | (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 | – |
| TOTAL contributions and profit distributions recognised directly in equity | | – | (4,377) | (85,765) | (90,142) | (1,393) | – | (1,762) | (88,380) | (90,142) |
| Profit for the year | | – | – | 319,670 | 319,670 | 2,351 | – | – | 150,891 | 150,891 |
| Other comprehensive income | 12, 20 a | – | 196,646 | 1,056 | 197,702 | – | – | 144,509 | 311 | 144,820 |
| TOTAL comprehensive income for the year | | – | 196,646 | 320,726 | 517,372 | 2,351 | – | 144,509 | 151,202 | 295,711 |
| As of 31 December 2017 | | 1,288,715 | 1,125,728 | 424,406 | 2,838,849 | 8,042 | 1,288,715 | 791,681 | 302,242 | 2,382,638 |
| Implementation effect of IFRS 9 'Financial instruments' | 2.28 | – | – | (290) | (290) | – | – | – | (629) | (629) |
| As of 1 January 2018 | | 1,288,715 | 1,125,728 | 424,116 | 2,838,559 | 8,042 | 1,288,715 | 791,681 | 301,613 | 2,382,009 |
| Decrease in share capital | 19 | (454,413) | – | – | (454,413) | – | (454,413) | – | – | (454,413) |
| Increase in share capital | 14 a, 19 | 489 | – | – | 489 | – | 489 | – | – | 489 |
| Dividends for 2017 | 20 b | – | – | (156,418) | (156,418) | (2,116) | – | – | (156,418) | (156,418) |
| Disposal of non-current assets revaluation reserve | 20 a | – | (10,229) | 10,229 | – | – | – | (6,549) | 6,549 | – |
| TOTAL contributions and profit distributions recognised directly in equity | | (453,924) | (10,229) | (146,189) | (610,342) | (2,116) | (453,924) | (6,549) | (149,869) | (610,342) |
| Profit for the year | | – | – | 73,423 | 73,423 | 2,532 | – | – | 212,733 | 212,733 |
| Other comprehensive income | 12, 20 a | – | 9,967 | – | 9,967 | – | – | 9,423 | – | 9,423 |
| TOTAL comprehensive income for the year | | – | 9,967 | 73,423 | 83,390 | 2,532 | – | 9,423 | 212,733 | 222,156 |
| As of 31 December 2018 | | 834,791 | 1,125,466 | 351,350 | 2,311,607 | 8,458 | 834,791 | 794,555 | 364,477 | 1,993,823 |

The notes on pages 15 to 68 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 Keldere
Accounting director of Latvenergo AS

16 April 2019

STATEMENT OF CASH FLOWS

EUR'000

| Notes | Group | | Parent Company | |
|--|------------|----------------|----------------|----------------|
| | 2018 | 2017 | 2018 | 2017* |
| Cash flows from operating activities | | | | |
| Profit before tax | 88,513 | 224,114 | 212,760 | 185,906 |
| Adjustments: | | | | |
| – 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) |
| Operating profit before working capital adjustments | | 338,248 | 555,947 | 173,276 |
| 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 |
| Cash generated from operating activities | | 350,382 | 389,524 | 438,981 |
| 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) |
| Net cash flows from operating activities | | 302,869 | 338,209 | 394,395 |
| | | | | 449,352 |

Āris Žigurs
Chairman of the Management Board

Guntars Balčūns
Member of the Management Board

Liāna Keldere
Accounting director of Latvenergo AS

16 April 2019

Statement of Cash Flows (continued)

EUR'000

| Notes | Group | | Parent Company | |
|--|-------|------------------|------------------|------------------|
| | 2018 | 2017 | 2018 | 2017* |
| Cash flows from investing activities | | | | |
| 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 |
| Net cash flows used in investing activities | | (238,452) | (230,175) | (330,756) |
| Cash flows from financing activities | | | | |
| 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) |
| Net cash flows used in financing activities | | (170,965) | (56,011) | (168,940) |
| Net (decrease)/ increase in cash and cash equivalents | | (106,548) | 52,023 | (105,301) |
| Cash and cash equivalents at the beginning of the year | 18 | 236,003 | 183,980 | 232,855 |
| | | | | 181,197 |
| Cash and cash equivalents at the end of the year | 18 | 129,455 | 236,003 | 127,554 |
| | | | | 232,855 |

* See note 2.1.

The notes on pages 15 to 68 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 |
| Equity and liabilities | | | | | | |
| 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 |
| TOTAL equity | 2,846,891 | - | 2,846,891 | 2,382,638 | - | 2,382,638 |

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 |
|---|---------------------------------|------------------|--------------------------------|
| Operating profit before working capital adjustments | 392,716 | - | 392,716 |
| (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 |
| Cash generated from operating activities | 240,398 | 256,755 | 497,153 |
| Interest paid | (12,324) | 41 | (12,283) |
| Interest received | 11,632 | (10,242) | 1,390 |
| Net cash flows from operating activities | 202,798 | 246,554 | 449,352 |
| Cash flows from investing activities | | | |
| Loans issued to subsidiaries | (81,889) | (186,329) | (268,218) |
| Repayment of loans issued to subsidiaries | 60,225 | (60,225) | - |
| Net cash flows used in investing activities | (97,777) | (246,554) | (344,331) |
| Cash and cash equivalents at the end of the year | 232,855 | - | 232,855 |

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 |
|---|------------------------------|
| Buildings and facilities | |
| Assets of Hydropower plants: | 15 – 100 |
| ▪ hydropower plants' buildings and facilities, | 25 – 100 |
| ▪ hydropower plants' technology equipment and machinery | 10 – 40 |
| Transmission system electrical lines and electrical equipment: | |
| ▪ electricity transmission lines | 20 – 50 |
| ▪ electrical equipment of transformer substations | 12 – 40 |
| Distribution system electrical lines and electrical equipment: | |
| ▪ electricity distribution lines | 30 – 50 |
| ▪ electrical equipment of transformer substations | 30 – 35 |
| Technology equipment and machinery | 3 – 40 |
| Other property, plant and equipment | 2 – 25 |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (see 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 derivatives at FVOCI | Derivatives at FVPL | Financial assets at amortised cost | Hedging derivatives at FVOCI | Derivatives at FVPL |
| Financial assets as of 31 December 2018 | | | | | | | |
| 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 | – | – |
| | | 379,878 | 15,748 | 105 | 1,005,893 | 15,748 | 105 |
| Financial assets as of 31 December 2017 | | | | | | | |
| 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 | – | – |
| | | 1,003,417 | 4,074 | 545 | 1,449,641 | 4,074 | 545 |
| Financial liabilities as of 31 December 2018 | | | | | | | |
| 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 | – | – |
| | | 918,050 | 10,204 | – | 880,994 | 10,204 | – |
| Financial liabilities as of 31 December 2017 | | | | | | | |
| 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 | – | – |
| | | 942,499 | 8,061 | 23 | 894,113 | 8,061 | 23 |

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 |
| | | 395,731 | 1,008,036 | 1,021,746 | 1,454,260 |

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 |
| | 129,455 | 236,003 | 127,554 | 232,855 |

* 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 |
| As of 31 December 2018 | | | | | | | | | | |
| Borrowings from banks | 116,989 | 159,053 | 250,342 | 214,090 | 740,474 | 114,241 | 154,751 | 246,134 | 212,846 | 727,972 |
| Issued debt securities (bonds) | 2,880 | 37,769 | 104,228 | – | 144,877 | 2,880 | 37,769 | 104,228 | – | 144,877 |
| Derivative financial instruments | 14,362 | 2,864 | 2,708 | (1,145) | 18,789 | 14,362 | 2,864 | 2,708 | (1,145) | 18,789 |
| Trade and other current financial payables (Note 25) * | 103,707 | – | – | – | 103,707 | 78,726 | – | – | – | 78,726 |
| | 237,938 | 199,686 | 357,278 | 212,945 | 1,007,847 | 210,209 | 195,384 | 353,070 | 211,701 | 970,364 |
| As of 31 December 2017 | | | | | | | | | | |
| Borrowings from banks | 113,285 | 119,074 | 313,149 | 191,748 | 737,256 | 109,727 | 117,985 | 310,411 | 194,733 | 732,856 |
| Issued debt securities (bonds) | 2,880 | 2,880 | 142,041 | – | 147,801 | 2,880 | 2,880 | 142,041 | – | 147,801 |
| Derivative financial instruments | 5,304 | 5,077 | 3,273 | 318 | 13,972 | 5,304 | 5,077 | 3,273 | 318 | 13,972 |
| Trade and other current financial payables (Note 25) * | 115,742 | – | – | – | 115,742 | 79,341 | – | – | – | 79,341 |
| | 237,211 | 127,031 | 458,463 | 192,066 | 1,014,771 | 197,252 | 125,942 | 455,725 | 195,051 | 973,970 |

* 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 |
| Capital Ratio | 61% | 64% | 63% | 65% |

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 Kēguma 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 Energijas 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 |
| 2018 | | | | | | | | | | | | |
| Revenue | | | | | | | | | | | | |
| External customers | 510,434 | 321,232 | 39,203 | 7,139 | 878,008 | – | 878,008 | 386,510 | 48,689 | 435,199 | – | 435,199 |
| Inter-segment | 1,390 | 1,730 | 2,991 | 45,451 | 51,562 | (51,562) | – | 459 | 22,366 | 22,825 | (22,825) | – |
| TOTAL revenue | 511,824 | 322,962 | 42,194 | 52,590 | 929,570 | (51,562) | 878,008 | 386,969 | 71,055 | 458,024 | (22,825) | 435,199 |
| Results | | | | | | | | | | | | |
| EBITDA | 146,552 | 119,791 | 41,456 | 13,783 | 321,582 | – | 321,582 | 134,040 | 26,887 | 160,927 | – | 160,927 |
| Amortisation, depreciation and intangible assets and PPE impairment loss | (110,490) | (77,432) | (25,856) | (12,042) | (225,820) | – | (225,820) | (107,397) | (19,727) | (127,124) | – | (127,124) |
| Profit before tax | 36,062 | 42,359 | 15,600 | 1,741 | 95,762 | (7,249) | 88,513 | 26,643 | 7,160 | 33,803 | 178,957 | 212,760 |
| Assets at the end of the year | 1,329,274 | 1,669,710 | 579,327 | 86,350 | 3,664,661 | 134,158 | 3,798,819 | 1,212,681 | 161,577 | 1,374,258 | 1,766,851 | 3,141,109 |
| Liabilities at the end of the year | 295,168 | 192,016 | 95,123 | 6,535 | 588,842 | 889,912 | 1,478,754 | 298,328 | 7,882 | 306,210 | 841,076 | 1,147,286 |
| Capital expenditure | 28,909 | 95,117 | 87,136 | 12,411 | 223,573 | (2,966) | 220,607 | 26,921 | 14,429 | 41,350 | – | 41,350 |
| 2017 | | | | | | | | | | | | |
| Revenue | | | | | | | | | | | | |
| External customers | 554,489 | 318,851 | 44,415 | 7,872 | 925,627 | – | 925,627 | 448,660 | 49,920 | 498,580 | – | 498,580 |
| Inter-segment | 1,605 | 1,851 | 2,541 | 52,739 | 58,736 | (58,736) | – | 346 | 29,089 | 29,435 | (29,435) | – |
| TOTAL revenue | 556,094 | 320,702 | 46,956 | 60,611 | 984,363 | (58,736) | 925,627 | 449,006 | 79,009 | 528,015 | (29,435) | 498,580 |
| Results | | | | | | | | | | | | |
| EBITDA | 372,829 | 111,599 | 45,305 | 11,963 | 541,696 | – | 541,696 | 362,534 | 24,566 | 387,100 | – | 387,100 |
| Amortisation, depreciation and intangible assets and PPE impairment loss | (194,376) | (76,630) | (24,345) | (12,263) | (307,614) | – | (307,614) | (191,228) | (18,456) | (209,684) | – | (209,684) |
| Profit / (loss) before tax | 178,453 | 34,969 | 20,960 | (300) | 234,082 | (9,968) | 224,114 | 171,306 | 6,110 | 177,416 | 8,490 | 185,906 |
| Assets at the end of the year | 1,956,888 | 1,641,318 | 500,863 | 85,584 | 4,184,653 | 231,072 | 4,415,725 | 1,286,478 | 192,435 | 1,478,913 | 2,170,287 | 3,649,200 |
| Liabilities at the end of the year | 393,759 | 188,025 | 67,502 | 6,551 | 655,837 | 912,997 | 1,568,834 | 383,708 | 8,695 | 392,403 | 874,159 | 1,266,562 |
| Capital expenditure | 74,021 | 107,683 | 63,085 | 10,815 | 255,604 | (11,793) | 243,811 | 73,150 | 16,128 | 89,278 | – | 89,278 |

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 |
| Year ended 31 December 2018 | | | | | | | | | | |
| Revenue from contracts with customers recognised over time: | | | | | | | | | | |
| 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 |
| TOTAL revenue from contracts with customers | 510,434 | 321,117 | – | 5,686 | 837,237 | 837,237 | 386,510 | 32,702 | 419,212 | 419,212 |
| Other revenue: | | | | | | | | | | |
| 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 | – | – | – | – |
| TOTAL other revenue | – | 115 | 39,203 | 1,453 | 40 771 | 40 771 | – | 15,987 | 15,987 | 15,987 |
| TOTAL revenue, including: | 510,434 | 321,232 | 39,203 | 7,139 | 878,008 | 878,008 | 386,510 | 48,689 | 435,199 | 435,199 |
| 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 |
| Year ended 31 December 2017 | | | | | | | | | | |
| Revenue from contracts with customers recognised over time: | | | | | | | | | | |
| 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 |
| TOTAL revenue from contracts with customers | 554,487 | 318,725 | – | 6,132 | 879,344 | 879,344 | 448,659 | 33,999 | 482,658 | 482,658 |
| Other revenue: | | | | | | | | | | |
| 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 | – | – | – | – |
| TOTAL other revenue | 2 | 126 | 44,415 | 1,740 | 46,283 | 46,283 | 1 | 15,921 | 15,922 | 15,922 |
| TOTAL revenue, including: | 554,489 | 318,851 | 44,415 | 7,872 | 925,627 | 925,627 | 448,660 | 49,920 | 498,580 | 498,580 |
| 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) |
| Segment profit before tax | | 95,762 | 234,082 | 33,803 | 177,416 |
| 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 |
| Profit before tax | | 88,513 | 224,114 | 212,760 | 185,906 |

Reconciliation of assets

EUR'000

| | Notes | Group | | Parent Company | |
|---------------------------------------|-------|------------------|------------------|------------------|------------------|
| | | 31/12/2018 | 31/12/2017 | 31/12/2018 | 31/12/2017 |
| Segment operating assets | | 3,664,661 | 4,184,653 | 1,374,258 | 1,478,913 |
| 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 |
| TOTAL assets | | 3,798,819 | 4,415,725 | 3,141,109 | 3,649,200 |

Reconciliation of liabilities

EUR'000

| | Notes | Group | | Parent Company | |
|--|-------|------------------|------------------|------------------|------------------|
| | | 2018 | 2017 | 2018 | 2017 |
| Segment operating liabilities | | 588,842 | 655,837 | 306,210 | 392,403 |
| 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 |
| TOTAL liabilities | | 1,478,754 | 1,568,834 | 1,147,286 | 1,266,562 |

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 |
| TOTAL revenue from contracts with customers | 837,237 | 879,344 | 419,212 | 482,658 |

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 |
| TOTAL revenue recognised applying agent accounting principle | 110,597 | 126,141 | 311,769 | 339,344 |

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 |
| TOTAL liabilities | 156,765 | 154,632 |

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 |
|---|----------------|----------------|
| At the beginning of the year | 154,632 | 153,432 |
| Received fees (Note 27) | 14,726 | 12,848 |
| Credited to the Statement of Profit or Loss | (12,593) | (11,648) |
| At the end of the year | 156,765 | 154,632 |

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 |
| TOTAL other income | 93,260 | 149,950 | 91,181 | 147,502 |

* Information about compensation is disclosed in Note 4 i)

8. RAW MATERIALS AND CONSUMABLES USED

EUR'000

| | Group | | Parent Company | |
|--|----------------|----------------|----------------|----------------|
| | 2018 | 2017 | 2018 | 2017 |
| Electricity: | | | | |
| 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 |
| TOTAL electricity costs | 268,445 | 199,116 | 80,179 | 31,467 |
| 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 |
| TOTAL raw materials and consumables used | 497,293 | 349,690 | 284,592 | 156,103 |

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) | – |
| TOTAL personnel expenses, including remuneration to the management | 103,762 | 113,289 | 42,396 | 44,892 |
| Including remuneration to the management*: | | | | |
| 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 |
| TOTAL remuneration to the management* | 2,621 | 2,593 | 1,041 | 1,078 |

* 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 |
| TOTAL other operating expenses | 49,109 | 70,902 | 38,701 | 57,987 |

* 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 | – |
| TOTAL finance income | 1,157 | 1,243 | 11,446 | 11,433 |

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 |
| TOTAL finance costs | 8,406 | 11,211 | 10,135 | 12,054 |

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 |
| TOTAL income tax | 12,558 | (97,907) | 27 | 35,015 |

The movement on the deferred income tax balances:

EUR'000

| | Group | | Parent Company | |
|--|---------------|----------------|----------------|----------------|
| | 2018 | 2017 | 2018 | 2017 |
| Deferred tax liabilities at the beginning of the year | – | 315,759 | – | 126,260 |
| 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) |
| Deferred tax liabilities at the end of the year before reversal | 12,297 | 299,001 | – | 109,398 |
| Reversed to the Statement of comprehensive income | – | (169,978) | – | (119,503) |
| Reversed in the Statement of Profit or Loss | – | (129,023) | – | 10,105 |
| Deferred tax liabilities at the end of the year | 12,297 | – | – | – |

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 |
| Profit before tax | 224,114 | 185,906 |
| Tax at the applicable tax rate of 15% | 33,617 | 27,886 |
| Permanent differences: | | |
| 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) |
| Actual corporate income tax for the reporting year | 31,116 | 24,910 |
| Reversal of deferred tax | (129,023) | 10,105 |
| TOTAL income tax | (97,907) | 35,015 |
| Effective income tax rate | 13.9% | 13.4% |

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 |
| As of 31 December 2016 | | | | | | | | | | |
| Cost | 2,507 | – | 45,631 | 1,512 | 49,650 | 10,796 | – | 43,912 | 567 | 55,275 |
| Accumulated amortisation | (2,070) | – | (33,046) | – | (35,116) | (3,835) | – | (32,671) | – | (36,506) |
| Net book amount | 437 | – | 12,585 | 1,512 | 14,534 | 6,961 | – | 11,241 | 567 | 18,769 |
| Year ended 31 December 2017 | | | | | | | | | | |
| Additions | – | – | 468 | 2,120 | 2,588 | – | – | 468 | 2,063 | 2,531 |
| Transfers | – | – | 3,536 | (3,536) | – | – | – | 2,589 | (2,589) | – |
| Disposals | (212) | – | – | – | (212) | (656) | – | – | – | (656) |
| Amortisation charge | – | – | (3,497) | – | (3,497) | – | – | (3,183) | – | (3,183) |
| Closing net book amount | 225 | – | 13,092 | 96 | 13,413 | 6,305 | – | 11,115 | 41 | 17,461 |
| As of 31 December 2017 | | | | | | | | | | |
| Cost | 225 | – | 49,635 | 96 | 49,956 | 6,305 | – | 46,969 | 41 | 53,315 |
| Accumulated amortisation | – | – | (36,543) | – | (36,543) | – | – | (35,854) | – | (35,854) |
| Net book amount | 225 | – | 13,092 | 96 | 13,413 | 6,305 | – | 11,115 | 41 | 17,461 |
| Year ended 31 December 2018 | | | | | | | | | | |
| Additions | – | 17,789 | 2,641 | 88 | 20,518 | – | 17,789 | 2,439 | 124 | 20,352 |
| Transfers | (80) | – | – | – | (80) | (525) | – | (26) | – | (551) |
| Disposals | – | (11,066) | – | – | (11,066) | – | (11,066) | – | – | (11,066) |
| Amortisation charge | – | – | (3,706) | – | (3,706) | – | – | (3,383) | – | (3,383) |
| Closing net book amount | 145 | 6,723 | 12,027 | 184 | 19,079 | 5,780 | 6,723 | 10,145 | 165 | 22,813 |
| As of 31 December 2018 | | | | | | | | | | |
| Cost | 145 | 6,723 | 48,135 | 184 | 55,187 | 5,780 | 6,723 | 45,242 | 165 | 57,910 |
| Accumulated amortisation | – | – | (36,108) | – | (36,108) | – | – | (35,097) | – | (35,097) |
| Net book amount | 145 | 6,723 | 12,027 | 184 | 19,079 | 5,780 | 6,723 | 10,145 | 165 | 22,813 |

b) Greenhouse gas emission allowances:

| | Group | | Parent Company | |
|-------------------------------------|------------------------------|------------------------------|------------------------------|------------------------------|
| | 2018 Number of allowances | 2017 Number of allowances | 2018 Number of allowances | 2017 Number of allowances |
| At the beginning of the year | 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) |
| At the end of the year | 1,022,810 | 206,631 | 878,567 | (13,778) |

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 |
| As of 31 December 2016 | | | | | | | | | | | | | | |
| Cost or valuation | 464,503 | 1,855,929 | 2,826,157 | 932,444 | 625,712 | 156,039 | 153,890 | 7,014,674 | 318,262 | 1,855,929 | 600,721 | 135,062 | 119,350 | 3,029,324 |
| Accumulated depreciation and impairment | (137,778) | (1,146,091) | (1,357,781) | (534,495) | (370,284) | (106,458) | (5,990) | (3,658,877) | (91,253) | (1,146,091) | (362,168) | (101,436) | (5,858) | (1,706,806) |
| Net book amount | 326,725 | 709,838 | 1,468,376 | 397,949 | 255,428 | 49,581 | 147,900 | 3,355,797 | 227,009 | 709,838 | 238,553 | 33,626 | 113,492 | 1,322,518 |
| Year ended 31 December 2017 | | | | | | | | | | | | | | |
| Increase due PPE revaluation recognised in OCI (Note 20 a) | – | 22,167 | – | – | – | – | – | 22,167 | – | 22,167 | – | – | – | 22,167 |
| Decrease due PPE revaluation recognised in profit or loss | – | (2,260) | – | – | – | – | – | (2,260) | – | (2,260) | – | – | – | (2,260) |
| Additions | – | – | – | – | – | – | 241,220 | 241,220 | – | – | – | – | 84,373 | 84,373 |
| 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) | – | – | – | – | – | – | (1,182) | (1,059) | – | – | – | – | (1,059) |
| Reclassified from investment property | – | – | – | – | – | – | – | – | 8,335 | – | – | – | – | 8,335 |
| Disposals | (82) | – | (4,000) | (355) | (108) | (21) | (334) | (4,900) | (45) | – | (73) | (33) | (334) | (485) |
| Impairment charge | (261) | – | – | – | (116,799) | – | 814 | (116,246) | (261) | – | (116,799) | – | 803 | (116,257) |
| Depreciation | (13,807) | (25,991) | (66,979) | (23,055) | (40,471) | (15,308) | – | (185,611) | (9,653) | (25,991) | (38,971) | (11,263) | – | (85,878) |
| Closing net book amount as of 31 December 2017 | 330,190 | 722,609 | 1,478,510 | 385,939 | 118,767 | 49,399 | 223,571 | 3,308,985 | 239,839 | 722,609 | 103,389 | 31,954 | 133,663 | 1,231,454 |
| As of 31 December 2017 | | | | | | | | | | | | | | |
| Cost or valuation | 479,605 | 2,014,626 | 2,857,242 | 926,403 | 640,568 | 161,992 | 228,748 | 7,309,184 | 345,246 | 2,014,626 | 615,648 | 135,708 | 138,718 | 3,249,946 |
| Accumulated depreciation and impairment | (149,415) | (1,292,017) | (1,378,732) | (540,464) | (521,801) | (112,593) | (5,177) | (4,000,199) | (105,407) | (1,292,017) | (512,259) | (103,754) | (5,055) | (2,018,492) |
| Net book amount | 330,190 | 722,609 | 1,478,510 | 385,939 | 118,767 | 49,399 | 223,571 | 3,308,985 | 239,839 | 722,609 | 103,389 | 31,954 | 133,663 | 1,231,454 |
| Year ended 31 December 2018 | | | | | | | | | | | | | | |
| Additions | – | – | – | – | – | – | 217,389 | 217,389 | – | – | – | – | 38,300 | 38,300 |
| Invested in share capital (Note 19)* | 469 | – | 20 | – | – | – | – | 489 | 469 | – | 20 | – | – | 489 |
| 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) | – | – | – | – | – | – | (44) | (2,374) | – | – | – | – | (2,374) |
| Disposals | (931) | (36) | (4,904) | (841) | (709) | (90) | (101) | (7,612) | (2,158) | (36) | (1,279) | (10,442) | (95) | (14,010) |
| Impairment charge | 146 | – | – | – | (33,400) | – | (187) | (33,441) | 146 | – | (33,400) | – | – | (33,254) |
| Depreciation | (15,959) | (24,859) | (65,638) | (24,615) | (42,807) | (14,795) | – | (188,673) | (10,231) | (24,859) | (41,336) | (10,293) | – | (86,719) |
| Closing net book amount as of 31 December 2018 | 322,486 | 788,510 | 1,497,669 | 394,170 | 42,994 | 48,882 | 202,382 | 3,297,093 | 233,766 | 788,510 | 28,527 | 17,789 | 65,294 | 1,133,886 |
| As of 31 December 2018 | | | | | | | | | | | | | | |
| Cost or valuation | 485,098 | 2,055,572 | 2,889,265 | 933,079 | 637,706 | 147,744 | 207,746 | 7,356,210 | 349,581 | 2,055,572 | 612,253 | 103,877 | 70,349 | 3,191,632 |
| Accumulated depreciation and impairment | (162,612) | (1,267,062) | (1,391,596) | (538,909) | (594,712) | (98,862) | (5,364) | (4,059,117) | (115,815) | (1,267,062) | (583,726) | (86,088) | (5,055) | (2,057,746) |
| Net book amount | 322,486 | 788,510 | 1,497,669 | 394,170 | 42,994 | 48,882 | 202,382 | 3,297,093 | 233,766 | 788,510 | 28,527 | 17,789 | 65,294 | 1,133,886 |

* 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) |
| Net book amount at the beginning of the year | 753 | 563 | 64,107 | 72,335 | 700 | 498 | 64,807 | 72,833 |
| 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) |
| Net book amount at the end of the year | 467 | 753 | 61,363 | 64,107 | 433 | 700 | 61,796 | 64,807 |

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 | | |
| At revalued amounts | | | | |
| As of 31 December 2018 | | | | |
| 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) |
| Revalued net book amount | 788,510 | 1,497,669 | 394,170 | 2,680,349 |
| As of 31 December 2017 | | | | |
| 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) |
| Revalued net book amount | 722,609 | 1,478,510 | 385,939 | 2,587,058 |
| At amounts stated on historical cost basis | | | | |
| As of 31 December 2018 | | | | |
| Cost | 396,519 | 1,377,374 | 446,760 | 2,220,653 |
| Accumulated depreciation | (171,043) | (458,211) | (168,374) | (797,628) |
| Net book amount | 225,476 | 919,163 | 278,386 | 1,423,025 |
| As of 31 December 2017 | | | | |
| Cost | 311,854 | 1,289,349 | 418,917 | 2,020,120 |
| Accumulated depreciation | (170,115) | (371,348) | (161,275) | (702,738) |
| Net book amount | 141,739 | 918,001 | 257,642 | 1,317,382 |

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 |
| Rental income (the Group or the Parent Company is the lessor) (Note 6) | 40,267 | 45,779 | 15,987 | 15,922 |
| of which, Transmission system assets lease | 38,699 | 43,911 | – | – |
| Rental expense (the Group or the Parent Company is the lessee) | 1,248 | 1,577 | 1,149 | 1,267 |

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 |
| TOTAL rental income | 238,554 | 236,776 | 58,890 | 58,742 |

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 |
| TOTAL rental expense | 9,531 | 11,766 | 21,738 | 18,117 |

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 |
| At the beginning of the year | 40 | 40 | 817,048 | 817,048 |
| Invested in share capital* | – | – | 13,494 | – |
| At the end of the year | 40 | 40 | 830,542 | 817,048 |

* 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 |
| | 1,174,329 | 1,281,346 | 53,102 | 180,243 | 177,646 | 9,111 | 830,503 | 817,009 |

* 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) |
| TOTAL inventories | 71,975 | 76,328 | 58,410 | 61,824 |

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 |
| At the beginning of the year | 1,494 | 1,659 | 992 | 1,060 |
| Inventories written off | (287) | (62) | (260) | – |
| Charged to the Statement of Profit or Loss | (70) | (103) | 4 | (68) |
| At the end of the year | 1,137 | 1,494 | 736 | 992 |

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 |
| TOTAL receivables from contracts with customers | 117,955 | 105,247 | 105,369 | 81,025 | 82,684 | 82,799 |

* 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* |
| Receivables from contracts with customers: | | | | | | |
| – 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 |
| | 165,758 | 154,231 | 154,231 | 125,362 | 127,667 | 127,667 |
| Provisions for impaired receivables from contracts with customers: | | | | | | |
| – 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) | – |
| | (47,803) | (48,984) | (48,862) | (44,337) | (44,983) | (44,868) |
| Receivables from contracts with customers, net: | | | | | | |
| – 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 |
| | 117,955 | 105,247 | 105,369 | 81,025 | 82,684 | 82,799 |

* 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) | 105,964 | 91,644 | (183) | 91,461 | 69,557 | (160) | 69,397 | 65,637 | (156) | 65,481 |
| Less 30 days | 3% | 2,953 | (88) | 2,865 | 6,552 | (197) | 6,355 | 1,947 | (59) | 1,888 | 2,175 | (68) | 2,107 |
| Past due 30 - 59 days | 20% | 1,334 | (265) | 1,069 | 1,768 | (353) | 1,415 | 1,213 | (241) | 972 | 1,573 | (315) | 1,258 |
| Past due 60 - 89 days | 50% | 535 | (267) | 268 | 879 | (440) | 439 | 503 | (251) | 252 | 757 | (380) | 377 |
| Past due 90 - 179 days | 60% | 812 | (486) | 326 | 1,506 | (904) | 602 | 697 | (417) | 280 | 1,236 | (742) | 494 |
| Past due 180 - 359 days | 75% | 1,638 | (1,226) | 412 | 2,361 | (1,769) | 592 | 1,283 | (962) | 321 | 1,896 | (1,422) | 474 |
| Past due more than 360 days | 100% | 17,890 | (17,890) | - | 18,261 | (18,261) | - | 15,123 | (15,123) | - | 15,279 | (15,279) | - |
| Insolvent debtors* | 100% | 27,342 | (27,342) | - | 26,871 | (26,871) | - | 27,117 | (27,117) | - | 26,617 | (26,617) | - |
| | | 158,698 | (47,794) | 110,904 | 149,842 | (48,978) | 100,864 | 117,440 | (44,330) | 73,110 | 115,170 | (44,979) | 70,191 |

* 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 |
| Electricity, natural gas trade and related services receivables: | | | | | | | |
| Fully performing receivables | 0% | 70,290 | – | 70,290 | 46,956 | – | 46,956 |
| Past due 1 - 45 days | 0% | 7,183 | – | 7,183 | 3,134 | – | 3,134 |
| Past due 46 - 90 days | 50% | 743 | (371) | 372 | 657 | (329) | 328 |
| Past due 91 - 180 days | 75% | 1,173 | (880) | 293 | 1,110 | (833) | 277 |
| Past due more than 181 days | 100% | 17,623 | (17,623) | – | 16,780 | (16,780) | – |
| Individually impaired receivables with scheduled payments* | | 37,687 | (26,687) | 11,000 | 36,620 | (26,530) | 10,090 |
| TOTAL | | 134,699 | (45,561) | 89,138 | 105,257 | (44,472) | 60,785 |
| Heating and other receivables from contracts with customers: | | | | | | | |
| Fully performing receivables | 0% | 16,029 | – | 16,029 | 12,549 | – | 12,549 |
| Past due 1 - 30 days | 0% | 143 | – | 143 | 55 | – | 55 |
| Past due 31 - 90 days | 50% | 118 | (59) | 59 | 12 | (6) | 6 |
| Past due more than 91 days | 100% | 3,160 | (3,160) | – | 390 | (390) | – |
| Individually impaired receivables with scheduled payments* | | 82 | (82) | – | – | – | – |
| TOTAL | | 19,532 | (3,301) | 16,231 | 13,006 | (396) | 12,610 |
| Receivables from subsidiaries: | | | | | | | |
| Fully performing receivables | 0% | – | – | – | 9,404 | – | 9,404 |
| TOTAL | | – | – | – | 9,404 | – | 9,404 |
| TOTAL receivables from contracts with customers | | 154,231 | (48,862) | 105,369 | 127,667 | (44,868) | 82,799 |

* 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) | – |
| | 7,051 | 4,383 | 4,389 | 7,915 | 12,486 | 12,497 |

* 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) | – | – | – | – |
| TOTAL non-current receivables | 30,920 | 3,225 | 3,229 | 331 | 284 | 284 |
| Current financial receivables: | | | | | | |
| 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) |
| TOTAL current financial receivables | 84,613 | 641,668 | 641,832 | 14,233 | 17,939 | 17,938 |
| TOTAL other financial receivables | 115,533 | 644,893 | 645,061 | 14,564 | 18,223 | 18,222 |

* 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 |
| At the beginning of the year | 48,862 | 48,100 | 44,868 | 44,177 |
| 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 |
| At the end of the year | 47,803 | 48,862 | 44,337 | 44,868 |

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) | – | – | – | – |
| TOTAL non-current receivables | 30,920 | 3,225 | 3,229 | 331 | 284 | 284 |
| Current financial receivables: | | | | | | |
| 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) |
| TOTAL current financial receivables | 84,613 | 641,668 | 641,832 | 14,233 | 17,939 | 17,938 |
| TOTAL other financial receivables | 115,533 | 644,893 | 645,061 | 14,564 | 18,223 | 18,222 |

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 |
| Current non-financial receivables: | | | | |
| Pre-tax and overpaid taxes | 108 | 3,703 | 105 | 22 |
| Other current receivables | 109 | 1,226 | 107 | 119 |
| TOTAL current non-financial receivables | 217 | 4,929 | 212 | 141 |

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 |
| TOTAL cash and cash equivalents | 129,455 | 236,003 | 127,554 | 232,855 |

* 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 |
| As of 31 December 2016 | | 946,373 | (9,409) | (3,615) | 110 | 933,459 | 659,429 | (9,409) | (1,086) | 648,934 |
| Increase of non-current assets revaluation reserve as a result of revaluation | 14 a | 22,167 | – | – | – | 22,167 | 22,167 | – | – | 22,167 |
| Disposal of non-current assets revaluation reserve net of deferred tax | | (4,377) | – | – | – | (4,377) | (1,762) | – | – | (1,762) |
| Deferred tax related to non-current assets revaluation reserve | 12 | (3,325) | – | – | – | (3,325) | (3,325) | – | – | (3,325) |
| Reversed deferred corporate income tax | 12 | 169,560 | – | (638) | – | 168,922 | 119,384 | – | (192) | 119,192 |
| Gains on re-measurement on defined post-employment benefit plan | 26 a | – | – | 3,460 | – | 3,460 | – | – | 1,053 | 1,053 |
| Gains from fair value changes in derivative financial instruments | 23 | – | 5,422 | – | – | 5,422 | – | 5,422 | – | 5,422 |
| As of 31 December 2017 | | 1,130,398 | (3,987) | (793) | 110 | 1,125,728 | 795,893 | (3,987) | (225) | 791,681 |
| Disposal of non-current assets revaluation reserve | | (10,229) | – | – | – | (10,229) | (6,549) | – | – | (6,549) |
| Gains / (losses) on re-measurement on defined post-employment benefit plan | 26 a | – | – | 436 | – | 436 | – | – | (108) | (108) |
| Gains from fair value changes in derivative financial instruments | 23 | – | 9,531 | – | – | 9,531 | – | 9,531 | – | 9,531 |
| As of 31 December 2018 | | 1,120,169 | 5,544 | (357) | 110 | 1,125,466 | 789,344 | 5,544 | (333) | 794,555 |

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 |
| TOTAL other financial investments | 16,935 | 16,984 | 16,935 | 16,984 |

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 |
| TOTAL non-current borrowings | 700,028 | 718,674 | 690,568 | 710,125 |
| 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 |
| TOTAL current borrowings | 114,315 | 108,083 | 111,700 | 104,647 |
| TOTAL borrowings | 814,343 | 826,757 | 802,268 | 814,772 |

Movement in borrowings:

EUR'000

| | Group | | Parent Company | |
|--|----------------|----------------|----------------|----------------|
| | 2018 | 2017 | 2018 | 2017 |
| At the beginning of the year | 826,757 | 791,566 | 814,772 | 778,323 |
| 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) |
| At the end of the year | 814,343 | 826,757 | 802,268 | 814,772 |

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 |
| TOTAL borrowings | 814,343 | 826,757 | 802,268 | 814,772 |

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 |
| Fixed rate non-current and current borrowings: | | | | |
| – < 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 | – | – | – | – |
| TOTAL fixed rate borrowings | 205,227 | 255,276 | 205,227 | 255,276 |
| Floating rate non-current and current borrowings: | | | | |
| – < 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 |
| TOTAL floating rate borrowings | 609,116 | 571,481 | 597,041 | 559,496 |
| TOTAL borrowings | 814,343 | 826,757 | 802,268 | 814,772 |

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 |
| TOTAL borrowings | 814,343 | 826,757 | 802,268 | 814,772 |

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) | – | – |
| TOTAL outstanding fair values of derivatives | | 15,853 | (10,204) | 4,619 | (8,084) | 15,853 | (10,204) | 4,619 | (8,084) |

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) |
| TOTAL fair values of derivative financial instruments | | 15,853 | (10,204) | 4,619 | (8,084) | 15,853 | (10,204) | 4,619 | (8,084) |

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 |
| Outstanding fair value at the beginning of the year | 31 | (8,061) | – | (11,563) | 31 | (8,061) | – | (11,563) |
| Included in Statement of Comprehensive Income (Note 20 a) | (31) | 686 | 31 | 3,502 | (31) | 686 | 31 | 3,502 |
| Outstanding fair value at the end of the year | – | (7,375) | 31 | (8,061) | – | (7,375) | 31 | (8,061) |

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: 1,829,972 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 MWh) 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 |
| Outstanding fair value at the beginning of the year | 4,588 | (23) | 6,134 | (23) | 4,588 | (23) | 6,134 | (23) |
| 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 | – |
| Outstanding fair value at the end of the year | 15,853 | – | 4,588 | (23) | 15,853 | – | 4,588 | (23) |

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 |
| Outstanding fair value at the beginning of the year | – | – | – | – | – | – | – | – |
| Included in Statement of Comprehensive Income (Note 20 a) | – | (2,829) | – | – | – | (2,829) | – | – |
| Outstanding fair value at the end of the year | – | (2,829) | – | – | – | (2,829) | – | – |

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 | | | | Fair value measurement using | | | |
| | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) | TOTAL | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) | TOTAL |
| 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 |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| 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 |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| 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) | |
| As of 31 December 2018 | | | | | | | | |
| Liabilities measured at fair value | | | | | | | | |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| Interest rate swaps (Note 23) | – | 7,375 | – | 7,375 | – | 7,375 | – | 7,375 |
| Electricity and natural gas forwards and futures (Note 23) | | 2,829 | | 2,829 | | 2,829 | | 2,829 |
| Liabilities for which fair values are disclosed | | | | | | | | |
| Issued debt securities (bonds) (Note 22) | – | 137,001 | – | 137,001 | – | 137,001 | – | 137,001 |
| Floating rate borrowings (Note 22) | – | 677,342 | – | 677,342 | – | 665,267 | – | 665,267 |
| Trade and other financial current payables (Note 25) | – | – | 103,707 | 103,707 | – | – | 78,726 | 78,726 |
| As of 31 December 2017 | | | | | | | | |
| Liabilities measured at fair value | | | | | | | | |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| Interest rate swaps (Note 23, II) | – | 8,061 | – | 8,061 | – | 8,061 | – | 8,061 |
| Electricity and natural gas forwards and futures (Note 23) | – | 23 | – | 23 | – | 23 | – | 23 |
| Liabilities for which fair values are disclosed 7 | | | | | | | | |
| Issued debt securities (bonds) (Note 22) | – | 137,045 | – | 137,045 | – | 137,045 | – | 137,045 |
| Floating rate borrowings (Note 22) | – | 689,712 | – | 689,712 | – | 677,727 | – | 677,727 |
| Trade and other financial current payables (Note 25) | – | – | 115,742 | 115,742 | – | – | 79,341 | 79,341 |

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 |
| Financial assets | | | | | | | | |
| 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 |
| Financial liabilities | | | | | | | | |
| <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 |
| Financial liabilities: | | | | |
| 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 |
| TOTAL financial liabilities | 103,707 | 115,742 | 78,726 | 79,341 |
| Non-financial liabilities: | | | | |
| 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 |
| TOTAL non-financial liabilities | 31,301 | 31,330 | 13,336 | 15,348 |
| TOTAL trade and other current payables | 135,008 | 147,072 | 92,062 | 94,689 |

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 |
| Non-current: | | | | |
| – 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 |
| | 20,178 | 21,910 | 8,625 | 8,835 |
| Current: | | | | |
| – termination benefits | 779 | 3,390 | 342 | 903 |

a) Provisions for post-employment benefits

EUR'000

| | Group | | Parent Company | |
|--|---------------|---------------|----------------|--------------|
| | 2018 | 2017 | 2018 | 2017 |
| At the beginning of the year | 13,721 | 16,428 | 5,911 | 6,733 |
| 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) |
| At the end of the year | 12,767 | 13,721 | 5,868 | 5,911 |

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 |
| At the beginning of the year | 13,721 | 16,428 | 5,911 | 6,733 |
| (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 |
| At the end of the year | 12,767 | 13,721 | 5,868 | 5,911 |

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 EUROSAP 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 EUROSAP 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 |
| At the beginning of the year | 2,264 | 2,215 | 1,220 | 1,191 |
| Charged to the Statement of Profit or Loss | (1,044) | 49 | – | 29 |
| At the end of the year | 1,220 | 2,264 | 1,220 | 1,220 |

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 |
| I) Non-current deferred income | | | | |
| a) from contracts with customers | | | | |
| Deferred income from connection fees | 143,494 | 142,132 | – | – |
| | 143,494 | 142,132 | – | – |
| b) from lease | | | | |
| 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 |
| | 5,239 | 5,737 | 403 | 423 |
| c) other | | | | |
| 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 |
| | 298,280 | 345,189 | 209,702 | 285,662 |
| TOTAL non-current deferred income | 447,013 | 493,058 | 210,105 | 286,085 |

| EUR'000 | | | | |
|--|----------------|----------------|----------------|----------------|
| | Group | | Parent Company | |
| | 31/12/2018 | 31/12/2017 | 31/12/2018 | 31/12/2017 |
| II) Current deferred income | | | | |
| a) from contracts with customers | | | | |
| Deferred income from connection fees | 12,984 | 12,247 | – | – |
| Deferred income from use of allowed effective electrical load (distribution system services) | 287 | 253 | – | – |
| | 13,271 | 12,500 | – | – |
| b) from lease | | | | |
| Deferred income from connection fees | 449 | 449 | – | – |
| | 449 | 449 | – | – |
| c) other | | | | |
| 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 |
| | 25,989 | 31,279 | 24,022 | 29,358 |
| TOTAL current deferred income | 39,709 | 44,228 | 24,022 | 29,358 |
| TOTAL deferred income | 486,722 | 537,286 | 234,127 | 315,443 |

* 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 | | | | |
|--|----------------|----------------|----------------|----------------|
| | Group | | Parent Company | |
| | 2018 | 2017 | 2018 | 2017 |
| At the beginning of the year | 537,286 | 209,429 | 315,443 | 1,114 |
| 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) |
| At the end of the year | 486,722 | 537,286 | 234,127 | 315,443 |

* 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* |
| Income: | | | | | | |
| – 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 | – | – |
| TOTAL income from transactions with related parties | 54,006 | 50,681 | 78,698 | 14,248 | 155,338 | 6,298 |
| Expenses: | | | | | | |
| – 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 |
| TOTAL expenses from transactions with related parties | 76,363 | 76,090 | 346,641 | 5,422 | 344,054 | 5,367 |
| <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 | – |
| | – | – | 305,719 | – | 332,692 | – |

* 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 |
| Receivables from related parties: | | | | | | |
| – 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) | – |
| | 42,218 | 19,988 | 20,014 | 15,556 | 18,631 | 18,645 |
| Payables to related parties: | | | | | | |
| – 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 |
| | 12,262 | 17,293 | 17,293 | 31,909 | 32,013 | 32,013 |

* 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 |
| | – | – | 4,679 | 5,077 |

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 |
| | – | – | 5,657 | 1,176 |

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 |
| Non-current loans to subsidiaries | | | |
| 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) | – |
| TOTAL non-current loans | 595,004 | 397,705 | 397,976 |
| Current portion of non-current loans | | | |
| 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) | – |
| Current loans to subsidiaries | | | |
| 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) | – |
| TOTAL current loans | 170,811 | 700,561 | 700,805 |
| TOTAL loans to subsidiaries | 765,815 | 1,098,266 | 1,098,781 |

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 and impairment for expected credit loss is recognised 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 |
| At the beginning of the year | 1,098,781 | 622,704 |
| 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) | – |
| At the end of the year | 765,815 | 1,098,781 |

Interest received from related parties:

EUR'000

| | Parent Company | |
|-------------------|----------------|--------------|
| | 2018 | 2017 |
| Interest received | 2,103 | 1,682 |
| | 2,103 | 1,682 |

l) 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 |
| TOTAL | 298,076 | 160,856 | 93,883 | | |

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 |
| Non-current loan: | | |
| – < 1 year (current portion) | 8,176 | 8,490 |
| – 1 – 5 years | 109,724 | 64,790 |
| – > 5 years | 42,957 | 20,603 |
| | 160,856 | 93,883 |

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 |
| TOTAL | 951,643 | 492,582 | 363,497 | | |

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 |
| Non-current loan: | | |
| – < 1 year (current portion) | 49,853 | 50,915 |
| – 1 – 5 years | 322,786 | 238,425 |
| – > 5 years | 119,943 | 74,157 |
| | 492,582 | 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).

EUR'000

| | Parent Company | |
|---------------|----------------|-----------|
| | 2018 | 2017 |
| Interest paid | 37 | 41 |
| | 37 | 41 |

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 11 to 68 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

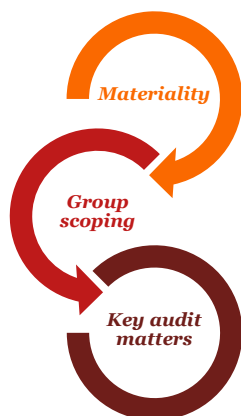
We are independent of the Company and the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) and the ethical requirements of the Law on Audit Services that are relevant to our audit of the financial statements 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.

| | |
|--|---|
| Overall Company and Group materiality | Overall materiality applied to the Company and the Group was EUR 7,600 thousand. |
| How we determined it | 5% of average profit before tax for the recent three years. |
| Rationale for the materiality benchmark applied | 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 35.

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 35 and 41, 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 3 to 10 of the accompanying Annual Report,
- Non-financial Report included in the Management Report as set out on page 8 of the accompanying 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), 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 56.² 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 56.² 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

Ģeogrāfiskās cenas



Latvenergo

Galvenie fakti

- Elektroenerģijas cenu pieaugumu ietekmēja:
 - sausie laika apstākļi
 - zemāks ūdens rezervāru aizpildījums Skandināvijā
 - mazāka HES izstrāde
 - augstākas CO₂ emisijas kvotu cenas
- Dabāgāzes vidējā cena par 19% pieauga, sasniegta 16,0 EUR/MWh (GASPOOL) un 15,7 EUR/MWh (TTF)
- CO₂ emisijas kvotu cena – 24,3 EUR/t, kas ir gandrīz 2x vairāk nekā pērn

Daugavas HES izstrāde



Latvenergo Group Consolidated and Latvenergo AS 2019 Annual Report



Latvenergo Group Consolidated and Latvenergo AS Annual Report

Financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS)

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| | | |
|-----------|--------|---|
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Financial calendar

Interim Condensed Financial Statements:

For the 3 months of 2020 (unaudited) – 29.05.2020

For the 6 months of 2020 (unaudited) – 28.08.2020

For the 9 months of 2020 (unaudited) – 27.11.2020



Latvenergo Group Key Figures

Financial Figures

EUR'000

| | 2019 | 2018 | 2017 | 2016 | 2015 |
|--|-----------|-----------|-----------|-----------|-----------|
| Revenue | 841,636 | 838,805 | 881,212 | 885,740 | 884,977 |
| EBITDA ¹⁾ | 243,526 | 281,947 | 497,731 | 347,312 | 263,293 |
| Operating profit ²⁾ | 100,365 | 81,983 | 214,462 | 151,101 | 88,694 |
| Profit before tax ³⁾ | 92,072 | 74,734 | 224,114 | 148,945 | 92,535 |
| Profit | 94,359 | 75,955 | 322,021 | 130,593 | 85,039 |
| Dividends ⁴⁾ | 132,936 | 156,418 | 90,142 | 77,413 | 31,479 |
| Total assets | 3,864,941 | 3,798,819 | 4,415,725 | 3,901,231 | 3,517,372 |
| Non-current assets | 2,798,712 | 3,364,534 | 3,343,404 | 3,388,954 | 3,113,719 |
| Total equity | 2,265,487 | 2,320,065 | 2,846,891 | 2,418,713 | 2,096,702 |
| Borrowings | 882,671 | 814,343 | 826,757 | 791,566 | 797,483 |
| Net debt (adjusted) ⁵⁾ | 563 959 | 505 419 | 496 730 | 528 980 | 605,112 |
| Net cash flows from operating activities | 315,433 | 302,869 | 338,209 | 341,186 | 246,278 |
| Investments | 229,427 | 220,607 | 243,811 | 200,677 | 190,461 |

Financial figures and ratios are presented by excluding discontinuing operations (unbundling transmission system asset ownership) – see Note 30 to the Financial Statements.

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

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

³⁾ Profit before tax – earnings before income tax

⁴⁾ Dividends paid to the equity holder of the Parent Company. (see Note 21 b)

⁵⁾ Net debt = (borrowings at the end of the year minus Latvijas elektriskie tīkli AS borrowings) minus (cash and cash equivalents at the end of the year minus Latvijas elektriskie tīkli AS cash and cash equivalents at the end of the year)

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 here and therefore uses the following financial figures and ratios:

- profitability measures – EBITDA¹⁾; EBITDA margin⁶⁾; operating profit margin⁷⁾; profit before tax margin⁸⁾; profit margin⁹⁾; return on assets (ROA)¹⁴⁾; return on equity (ROE)¹⁵⁾; return on capital employed (ROCE)¹⁶⁾;
- capital structure measures – net debt⁵⁾; equity-to-asset ratio¹⁰⁾; net debt / EBITDA¹¹⁾; net debt / equity¹²⁾; current ratio¹³⁾;
- a dividend policy measure – dividend pay-out ratio¹⁷⁾.

The definitions and components of the financial figures and ratios are described on the right side. Except excluding discontinued operations, the reported financial figures and ratios have not changed over previous period.

Financial ratios

| | 2019 | 2018 | 2017 | 2016 | 2015 |
|---|-------|------|-------|-------|-------|
| EBITDA margin ⁶⁾ | 29% | 34% | 56% | 39% | 30% |
| Operating profit margin ⁷⁾ | 11.9% | 9.8% | 24.3% | 17.1% | 10.0% |
| Profit before tax margin ⁸⁾ | 10.9% | 8.9% | 25.4% | 16.8% | 10.5% |
| Profit margin ⁹⁾ | 11.2% | 9.1% | 36.5% | 14.7% | 9.6% |
| Equity-to-asset ratio ¹⁰⁾ | 59% | 61% | 64% | 62% | 60% |
| Net debt / EBITDA (adjusted) ¹¹⁾ | 2.2 | 1.8 | 1.0 | 1.6 | 2.3 |
| Net debt / equity (adjusted) ¹²⁾ | 0.25 | 0.22 | 0.17 | 0.22 | 0.29 |
| Current ratio ¹³⁾ | 1.2 | 1.5 | 3.2 | 1.7 | 1.9 |
| Return on assets (ROA) ¹⁴⁾ | 2.5% | 1.8% | 7.7% | 3.5% | 2.4% |
| Return on equity (ROE) ¹⁵⁾ | 4.1% | 2.9% | 12.2% | 5.8% | 4.1% |
| Return on capital employed (ROCE) (adjusted) ¹⁶⁾ | 3.4% | 2.5% | 6.4% | 5.1% | 3.2% |
| Dividend pay-out ratio ¹⁷⁾ | 62% | 104% | 66% | 82% | 90% |

Operational figures

| | | 2019 | 2018 | 2017 | 2016 | 2015 |
|----------------------------------|-----|---------------|---------------|---------------|---------------|---------------|
| Total electricity supply, incl.: | GWh | 9,259 | 9,984 | 10,371 | 10,140 | 9,868 |
| Retail* | GWh | 6,505 | 6,954 | 6,923 | 7,665 | 7,961 |
| Wholesale** | GWh | 2,754 | 3,030 | 3,448 | 2,474 | 1,907 |
| Retail natural gas | GWh | 303 | 147 | 33 | – | – |
| Electricity generated | GWh | 4,880 | 5,076 | 5,734 | 4,707 | 3,882 |
| Thermal energy generated | GWh | 1,842 | 2,274 | 2,612 | 2,675 | 2,408 |
| Number of employees | | 3,423 | 3,508 | 3,908 | 4,131 | 4,177 |
| Moody's credit rating | | Baa2 (stable) | Baa2 (stable) | Baa2 (stable) | Baa2 (stable) | Baa2 (stable) |

⁶⁾ EBITDA margin = EBITDA / revenue

⁷⁾ Operating profit margin = operating profit / revenue

⁸⁾ Profit before tax margin = profit before tax / revenue

⁹⁾ Profit margin = profit / revenue

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

¹¹⁾ 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)

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

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

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

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

¹⁶⁾ 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 without Latvijas elektriskie tīkli AS + borrowings at the end of the year without Latvijas elektriskie tīkli AS) / 2))

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

* Including operating consumption

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

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Financial figures

| | 2019 | 2018 | 2017 | 2016 | 2015 |
|--|-----------|-----------|-----------|-----------|-----------|
| Revenue | 437,529 | 435,199 | 498,580 | 513,563 | 521,146 |
| EBITDA ¹⁾ | 112,651 | 160,927 | 387,100 | 241,606 | 180,982 |
| Operating profit ²⁾ | 45,108 | 33,803 | 177,416 | 141,071 | 90,475 |
| Profit before tax ³⁾ | 101,227 | 212,760 | 185,906 | 156,290 | 103,212 |
| Profit | 101,227 | 212,733 | 150,891 | 137,441 | 94,750 |
| Dividends ⁴⁾ | 132,936 | 156,418 | 90,142 | 77,413 | 31,479 |
| Total assets | 3,136,958 | 3,141,109 | 3,649,200 | 3,204,394 | 3,124,054 |
| Non-current assets | 2,615,113 | 2,661,307 | 2,546,014 | 2,626,560 | 2,638,048 |
| Total equity | 1,949,287 | 1,993,823 | 2,382,638 | 2,177,069 | 2,114,900 |
| Borrowings | 872,899 | 802,268 | 814,772 | 778,323 | 782,965 |
| Net debt ⁵⁾ | 751,638 | 674,714 | 581,917 | 597,126 | 681,146 |
| Net cash flows from operating activities | 378,142 | 394,395 | 449,352 | 201,427 | 174,797 |
| Investments | 48,269 | 41,350 | 89,278 | 79,913 | 78,694 |

EUR'000

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

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

³⁾ Profit before tax – earnings before income tax

⁴⁾ Dividends paid to the equity holder of the Parent Company. (see Note 21 b)

⁵⁾ Net debt = borrowings at the end of the year minus cash and cash equivalents at the end of the year

Financial ratios

| | 2019 | 2018 | 2017 | 2016 | 2015 |
|--|-------|-------|-------|-------|-------|
| EBITDA margin ⁶⁾ | 25.7% | 37.0% | 77.6% | 47.0% | 34.7% |
| Operating profit margin ⁷⁾ | 10.3% | 7.8% | 35.6% | 27.5% | 17.4% |
| Profit before tax margin ⁸⁾ | 23.1% | 48.9% | 37.3% | 30.4% | 19.8% |
| Profit margin ⁹⁾ | 23.1% | 48.9% | 30.3% | 26.8% | 18.2% |
| Equity-to-asset ratio ¹⁰⁾ | 62 % | 63% | 65% | 68% | 68% |
| Net debt / equity ¹¹⁾ | 0.39 | 0.34 | 0.24 | 0.27 | 0.32 |
| Current ratio ¹²⁾ | 1.8 | 2.0 | 4.3 | 2.3 | 3.0 |
| Return on assets (ROA) ¹³⁾ | 3.2% | 6.3% | 4.4% | 4.3% | 3.0% |
| Return on equity (ROE) ¹⁴⁾ | 5.1% | 9.7% | 6.6% | 6.4% | 4.6% |
| Return on capital employed (ROCE) ¹⁵⁾ | 1.6% | 1.1% | 5.8% | 4.8% | 3.1% |
| Dividend pay-out ratio ¹⁶⁾ | 62% | 104% | 66% | 82% | 90% |

Operational figures

| | | 2019 | 2018 | 2017 | 2016 | 2015 |
|----------------------------------|-----|---------------|---------------|---------------|---------------|---------------|
| Total electricity supply, incl.: | GWh | 5,502 | 5,826 | 6,265 | 6,039 | 5,693 |
| Retail* | GWh | 4 211 | 4,406 | 4,619 | 5,290 | 5,422 |
| Wholesale** | GWh | 1,290 | 1,419 | 1,645 | 749 | 272 |
| Retail natural gas | GWh | 294 | 145 | 33 | – | – |
| Electricity generated | GWh | 4,832 | 5,028 | 5,687 | 4,660 | 3,833 |
| Thermal energy generated | GWh | 1,603 | 2,007 | 2,354 | 2,422 | 2,179 |
| Number of employees | | 1,328 | 1,355 | 1,431 | 1,472 | 1,464 |
| Moody's credit rating | | Baa2 (stable) | Baa2 (stable) | Baa2 (stable) | Baa2 (stable) | Baa2 (stable) |

⁶⁾ EBITDA margin = EBITDA / revenue

⁷⁾ Operating profit margin = operating profit / revenue

⁸⁾ Profit before tax margin = profit before tax / revenue

⁹⁾ Profit margin = profit / revenue

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

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

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

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

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

¹⁵⁾ 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))

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

* Including operating consumption

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



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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.

Operating environment

In 2019, electricity prices in the Nordics and the Baltics were lower compared to the previous year due to the improvement of the Nordic hydrobalance and lower prices of other energy resources. In addition to the factors mentioned above, the price of electricity in the Baltics was affected by lower electricity generation in the Baltics, especially in Estonia, which resulted in higher electricity imports compared to the year 2018. The electricity spot price in Latvia was 7% lower than in 2018.

Electricity prices declined

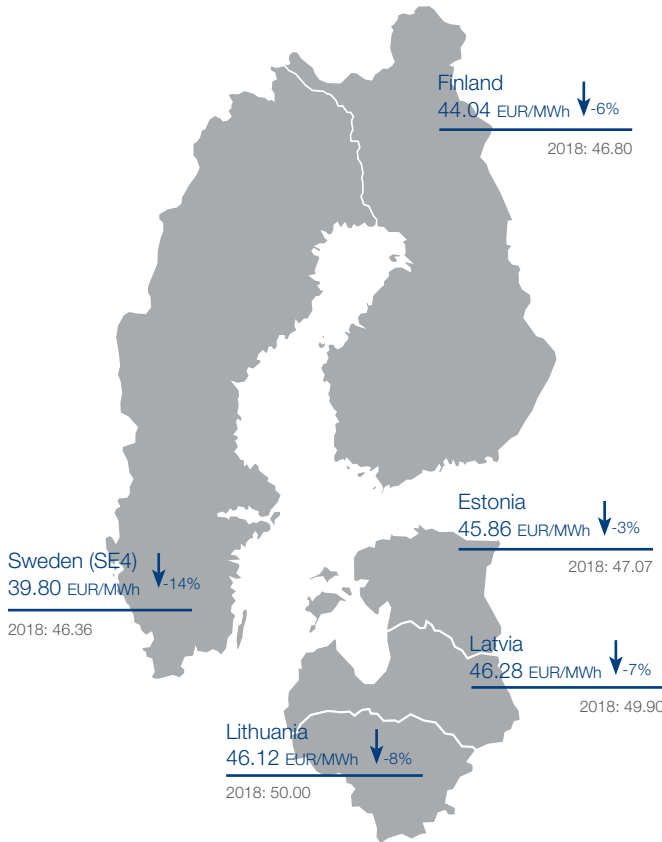
Due to the decrease in oil and coal prices, there was a decline in the price of natural gas. In 2019, the average price of natural gas at the GASPOOL and TTF trading platforms was 34% lower than a year earlier. The average price of CO₂ emission allowances in 2019 reached 25.2 EUR/t, which was almost twice as high as in 2018. CO₂ emission allowance prices increased due to the reform of the EU emissions trading system (ETS), reducing the permits available on the market.

Significant Events

Lower revenue from the installed electrical capacity at the Latvenergo AS CHPPs

In 2017, Latvenergo AS received a one-off compensation from the state in the amount of EUR 454.4 million, at the same time opting out of the receipt of 75% of the annual electrical capacity payments for Latvenergo AS cogeneration power plants CHPP-1 and CHPP-2. The compensation was financed by the capital release of Latvenergo AS. It was divided into two parts: EUR 140 million were to be recognized as other income in the profit and loss statement of Latvenergo AS in 2017, while EUR 314.4 million were to be recognized as income spread evenly over the following reporting periods until fulfilment of liabilities at the end of the support period in 2028. On 26 September 2018, the Cabinet of Ministers of Latvia decided to extend additional compensation in 2018 in the amount of EUR 51.7 million by reducing the remaining part of the compensation proportionally to this amount until the end of the support period. In 2019, EUR 24.0 million of the compensation were recognized as other income of Latvenergo AS (in 2018, the amount was EUR 81.0 million).

Electricity wholesale price on Nord Pool power exchange



As of 1 January 2020, the average distribution service tariff is reduced by 5.5%

Considering the changes in the methodology of calculation of distribution tariffs set by the Public Utilities Commission of Latvia (PUC), on 27 November 2019, the PUC approved a project on the electricity distribution service tariff for a period of 5 years until 2024 which was submitted by Sadales tīkls AS. The project provides for a reduction of the tariff of 5.5% on average.

Lower distribution tariffs are possible due to the ambitious operational efficiency improvement programme of Sadales tīkls AS, which includes process improvement and reduction of personnel and the number of vehicles and real estate bases.



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Unbundling transmission system asset ownership

An independent system operator model was introduced in Latvia and it was certified by the PUC. The transmission system assets were invested in Latvijas elektriskie tīkli AS (LET), while LET leases the assets to the transmission system operator (Augstsprieguma tīkls AS). The lease payment is calculated according to the methodology set by the PUC. LET is a subsidiary of Latvenergo AS, which provides management of Latvian power transmission network assets as well as fundraising for the maintenance of existing transmission networks and the construction of new ones. In 2019, the revenue of LET was EUR 41.1 million, and its profit was EUR 9.5 million. The asset value of the transmission system asset leasing segment at the end of 2019 was EUR 663 million.

Given that this model is one of the rarest in Europe, and based on an assessment by the Ministry of Economics of the Republic of Latvia, on 8 October 2019 the Cabinet of Ministers of the Republic of Latvia (CM) decided to support full unbundling of ownership of the electricity transmission system operator (TSO) until 1 July 2020, providing that transmission assets will be taken over from Latvenergo AS by Augstsprieguma tīkls AS. Since Latvenergo AS and Augstsprieguma tīkls AS are both state-owned companies, the change of ownership of assets will occur through the reduction of the share capital of Latvenergo AS by withdrawing the capital shares of LET from the base of assets of Latvenergo AS. After the capital shares of LET become property of the state, they will be invested in the share capital of Augstsprieguma tīkls AS. After the disposal of LET shares, the share capital of Latvenergo AS will be increased by investing retained earnings from previous years, but not in excess of the market value of LET shares determined by independent assessors. The market value of 100% LET shares is determined by KPMG Baltics AS.

In accordance with the CM informative report of 8 October 2019 “On the Directive 2009/72/EK requirements specified for the electricity transmission system operator in revaluating implementation of unbundling”, in December 2019 Latvenergo AS carried out a capital increase of LET by investing all real estate assets in amount of EUR 35 million and liabilities in amount of EUR 26 million belonging to the transmission system in LET. The value of LET equity as of December 31 is EUR 234 million.

On 15 October, 2019, the international credit rating agency *Moody's* affirmed the credit rating of Latvenergo AS at investment grade Baa2 with a stable outlook, also taking into account the planned unbundling of transmission system asset ownership.

Operating Results

Generation

In 2019, the total amount generated by Latvenergo Group's power plants comprised 4,880 GWh of electricity and 1,842 GWh of thermal energy (Latvenergo AS – 4,832 GWh and 1,603 GWh respectively).

The amount of power generated at the Daugava HPPs decreased by 14% compared to the previous year, reaching 2,047 GWh. The amount of power generated at the Daugava HPPs was impacted by lower water inflow in the Daugava river. The average water inflow in the Daugava River in 2019 was 401 m³/s, while a year earlier it was 485 m³/s. The share of electricity generated from renewable energy sources at Latvenergo Group was 42% (in 2018 it was 47%).

For the second year in a row, Latvenergo CHPPs had record-high electricity generation

In 2019, the amount generated at the CHPPs reached 2,780 GWh, which was 5% more than in the previous year and which is the most electricity produced historically. Such high generation was influenced by higher electricity demand in the region due to the fact that in 2019 electricity output at oil shale plants in Estonia fell significantly on account of high emission allowance prices. However, after reconstruction the Latvenergo AS CHPPs have minimized their CO₂ emissions and use energy resources to produce electricity in the most efficient way.

In 2019, the total amount of thermal energy generated by Latvenergo Group decreased by 19% compared to the previous year. The decrease was impacted by warmer weather conditions during the heating season and by competition. Data from the Central Statistical Bureau show that the average air temperature in Riga in the reporting year during the heating season was +4.1 C°, whereas in 2018 it was +2.1 C°.

Trade

In 2019, Latvenergo Group was one of the largest energy trading companies in the Baltics, while continuing to actively expand the range of products offered to customers.

Latvenergo – an energy company that operates in all segments of the market in Latvia, Lithuania and Estonia

In 2019, the Group supplied 6,505 GWh of electricity in the Baltics. The overall amount of retail electricity trade outside Latvia accounted for 1/3 of the total. The electricity trade volume in Latvia was 4.2 TWh, while in Lithuania it was 1.3 TWh and in Estonia it was 1.0 TWh. The total number of electricity customers comprised approximately 757 thousand, including more than 35 thousand foreign customers.

The natural gas retail sales volume doubled compared to the previous year and amounted to 303 GWh. In 2019, Latvenergo Group's natural gas consumption in the Baltics was 7.1 TWh, which was 3% more than in 2018. Currently, Latvenergo Group is the second largest natural gas consumer in the Baltics. At the end of 2019, the natural gas portfolio consisted of 770 business customers; meanwhile, the launch of gas trading to households in Latvia in February 2019 increased the natural gas portfolio by more than 5.4 thousand households.

In the reporting year, the retail activities of other services in the Baltic states continued. The number of solar panel contracts reached 320 with substantial growth in sales in Lithuania. In 2019, Latvenergo Group's market share in the Baltic solar panel market was approximately 9%. The number of Elektrum Insured customers continued to increase, reaching 65.9 thousand. Since launching in May 2019, the total turnover of the e-shop has continued to grow, providing more than 2,200 units sold. In August, the first Elektrum fast electric vehicle charging stations were launched and by the end of the reporting year approximately 1,450 charges had been made.



Financial Results

In 2019, Latvenergo Group's revenue reached EUR 841.6 million, which was EUR 2.8 million more than in the previous year. Meanwhile, the Groups profit increased by EUR 18.4 million or 24% compared to the previous year. Latvenergo Group's EBITDA decreased by 14% compared to the previous year, reaching EUR 243.5 million. EBITDA was impacted mainly by EUR 57.0 million lower compensation for the Latvenergo AS CHPPs' capacity payments recognised in the profit and loss statement of Latvenergo AS. In 2019, EUR 24.0 million of the compensation were recognized as other income of Latvenergo AS (in 2018, the amount was EUR 81.0 million).

Stable financial results

In 2019, the Latvenergo Group's results were negatively impacted by 14% or 333 GWh lower electricity output at the Daugava HPPs. Meanwhile, the higher sales price of electricity and the decrease in costs as a result of the approved efficiency programme, which was launched in 2017, had a positive impact on the results in 2019. The Group's ROE in 2019 reaches 4.1% which is 1.2 percentage points more than in 2018. The 2019 financial indicators of the capital structure ensured achievement of the goals set, exceeding the average industry indicators as well. For information on achievement of the financial goals, see the Sustainability Report section "Group Strategy".

Investments

In 2019, the total amount of investment comprised EUR 229.4 million, which was EUR 8.8 million more than in the previous year.

Latvenergo AS investment amounted EUR 48.3 million in 2019 (2018: EUR 41.4 million).

To ensure high-quality power network service, technical parameters and operational safety, a significant amount is invested in the modernization of the power network. In 2019, the amount invested in power network assets represented 79% of total investment.

Investments in distribution remained at the same level as in 2018 and comprised 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 modernization of distribution assets have increased the quality of distribution services by lowering SAIFI and SAIDI indicators. Since 2016, both the SAIFI and SAIDI decreased by 14%.

Investment in power network assets – approximately 80% of the total

In 2019, investments in transmission system assets remained at the same level as a year earlier and comprised EUR 87.4 million. The largest investment project in the transmission system asset leasing

segment was *Kurzeme Ring*. In 2019, EUR 26.1 million was invested in this energy infrastructure project (in 2018: EUR 65.2 million). 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 2019, EUR 16.6 million was invested in the Daugava HPPs' hydropower unit reconstruction. Gradual overhaul of eleven Daugava HPPs hydropower units is planned for completion until 2023. It will provide for further 40-year operation of the units. As of 31 December 2019, five 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 166.1 million.

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.

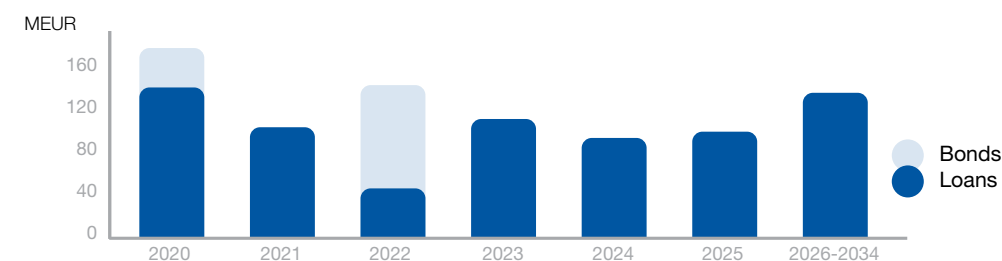
Diversified sources of funding

As of 31 December 2019, the Group's borrowings amounted to EUR 882.7 million (31 December 2018: EUR 814.3 million), comprising loans from commercial banks, international investment banks, and bonds amounting to EUR 135 million, of which EUR 100 million are green bonds.

At the end of 2019, Latvenergo AS attracted a loan of EUR 100 million from a foreign investment bank to finance investment projects.

Latvenergo Group's debt repayment schedule

Total borrowings as of 31 December 2019 – 882.7 MEUR



On 10 March 2020, the international credit rating agency *Moody's* repeatedly affirmed the credit rating of Latvenergo AS at investment grade Baa2 with a stable outlook. *Moody's* credit rating for Latvenergo AS has been stable for five years in a row, confirming the consistency of operations and financial soundness of Latvenergo Group.



Corporate Governance

Along with the financial results of Latvenergo Group, also the Corporate Governance Report of Latvenergo AS for 2019 is published. For detailed information see the Sustainability Report 2019.

Non-financial Report

Latvenergo Group has prepared a non-financial report in accordance with the Law on the Financial Instruments Market (Article 56⁴).

Non-financial report is in accordance with the GRI Standards

For detailed information on corporate social responsibility (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 2019 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, product responsibility, society, employees and the work environment, environmental protection and others.

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.

Taking into consideration the defined development directions of the Group, Latvenergo AS approved the Strategic Development and Efficiency Programme in 2017. While the strategic development section includes major strategic projects, the efficiency section provides for the revision, centralization and digitalization 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. The estimated efficiency potential for the Group’s EBITDA is up to EUR 30 million. This is the Group’s largest optimization 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 2019. 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% |
| Capital structure | Net debt to equity | < 50% |
| | Net debt to EBITDA | < 3 times |
| Dividend policy | Dividend payout 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 Latvenergo Group and Latvenergo AS due to falling revenue from generation and a mismatch between electricity purchases at floating market prices and retail sales at fixed 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 natural gas price volatility demand-supply factors and seasonal fluctuations, 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 Latvenergo Group and Latvenergo AS enter into long-term fixed price customer contracts, uses electricity and natural gas financial derivatives and enter into fixed price contracts for natural gas supply. The impact of price risk on generation is hedged gradually – price has been fixed for 80%–90% of projected electricity output 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 3, 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, 45% of

the Group's and of the Parent Company's borrowings had a fixed interest rate with an average period of 1.8 years both for the Group and the parent Company as of 31 December 2019. All necessary actions will be taken during the year 2020 to ensure the average fixed interest rate period within the limits stipulated by the Group's Financial Risk Management Policy.

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.

As of 31 December 2019, 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 as regards the Group's and the Parent Company's investments.

To manage the foreign currency exchange risk, the Financial Risk Management Policy envisages use of foreign exchange 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 2019, Latvenergo Group's liquid assets (cash and short-term deposits up to 3 months) reached EUR 122.7 million (31 December 2018: EUR 129.5 million), while the Latvenergo AS liquid assets reached EUR 121.3 million (31/12/2018: EUR 127.6 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.



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Events after the reporting period

At the beginning of 2020, the existence of the new coronavirus (Covid-19) was approved and it has currently spread all over the world, also in Latvia, disturbing business and affecting economic development. Latvenergo Group is constantly evaluating the impact of spreading of Covid-19 and implements measures for safety of customers and employees, as well ensures appropriate working regime in strategically important facilities – Daugava hydropower plants, combined heat and power plants in Riga and facilities of Sadales tīkls AS. Latvenergo Group continues to provide all services to its customers and any customer service issues are resolved using remote means of communication.

Spreading of the virus does not have a significant effect on the provision of services by Latvenergo Group. The Group continues to ensure continuity and availability to all customers of electricity generation, electricity and natural gas trading and distribution services. Management of Latvenergo Group considers that the spread of the virus is a non-adjusting event after the reporting period. Since the situation is unclear and is developing rapidly, it is currently not possible to provide a statistical estimate of the potential effect of spreading of the virus on Latvenergo Group, however COVID-19 influence could lead to economic downturn, with the most significant impact on electricity consumption and receivables.

All other significant events that would materially affect the financial position of the Latvenergo Group and Latvenergo AS after the reporting period are disclosed in Note 32 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 2019, 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.

Profit distribution

According to the state regulations, the expected amount of dividends to be paid by Latvenergo AS for the use of state capital in 2020 (for the reporting year 2019) amounted to EUR 127.1 million (incl. income tax). The distribution of net profit and amount of dividends payable is subject to a resolution of the Latvenergo AS Shareholders Meeting.

The Management Board of Latvenergo AS:

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Āris Žigurs

Chairman of the Management Board

7 April 2020

Guntars Balčūns

Member of the Management Board

Uldis Bariss

Member of the Management Board

Kaspars Cīkmačs

Member of the Management Board

Financial Statements

Statement of Profit or Loss

EUR'000

| | Notes | Group | | Parent Company | |
|---|----------------|----------------|----------------|----------------|----------------|
| | | 2019 | 2018 | 2019 | 2018 |
| Revenue | 6 | 841,636 | 838,805 | 437,529 | 435,199 |
| Other income | 7 | 25,863 | 91,098 | 23,558 | 91,181 |
| Raw materials and consumables used | 8 | (477,660) | (497,148) | (271,069) | (284,592) |
| Personnel expenses | 9 | (101,349) | (103,359) | (45,039) | (42,396) |
| Other operating expenses | 10 | (44,964) | (47,449) | (32,328) | (38,465) |
| EBITDA | | 243,526 | 281,947 | 112,651 | 160,927 |
| Depreciation, amortisation and impairment of intangible assets, property, plant and equipment and right-of-use assets | 13 a, 14 a, 15 | (143,161) | (199,964) | (67,543) | (127,124) |
| Operating profit | | 100,365 | 81,983 | 45,108 | 33,803 |
| Finance income | 11 | 1,187 | 1,157 | 12,995 | 11,446 |
| Finance costs | 11 | (9,480) | (8,406) | (11,734) | (10,135) |
| Dividends from subsidiaries | 16 | – | – | 54,858 | 177,646 |
| Profit before tax | | 92,072 | 74,734 | 101,227 | 212,760 |
| Current income tax | 12 | (8,565) | (261) | – | (27) |
| Deferred income tax | 12 | 620 | (8,948) | – | – |
| Profit for the year from continuing operations | | 84,127 | 65,525 | 101,227 | 212,733 |
| Profit for the year from discontinued operation | 30 | 10,232 | 10,430 | – | – |
| Profit for the year | | 94,359 | 75,955 | 101,227 | 212,733 |
| Profit attributable to: | | | | | |
| – Equity holder of the Parent Company | | 92,660 | 73,423 | 101,227 | 212,733 |
| – Non-controlling interests | | 1,699 | 2,532 | – | – |
| Basic earnings per share (in euros) | 21 c | 0.111 | 0.080 | 0.121 | 0.234 |
| Diluted earnings per share (in euros) | 21 c | 0.111 | 0.080 | 0.121 | 0.234 |

The notes on pages 15 to 62 are an integral part of these Financial Statements

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Āris Žigurs
Chairman of the Management Board

Guntars Balčūns
Member of the Management Board

Statement of Comprehensive Income

EUR'000

| | Notes | Group | | Parent Company | |
|---|----------|-----------------|---------------|-----------------|----------------|
| | | 2019 | 2018 | 2019 | 2018 |
| Profit for the year | | 94,359 | 75,955 | 101,227 | 212,733 |
| <i>Other comprehensive (loss) / income to be reclassified to profit or loss in subsequent periods:</i> | | | | | |
| – (losses) / gains from change in hedge reserve | 21 a, 24 | (11,771) | 9,531 | (11,771) | 9,531 |
| Net comprehensive (loss) / income to be reclassified to profit or loss in subsequent periods | | (11,771) | 9,531 | (11,771) | 9,531 |
| <i>Other comprehensive (loss) / income not to be reclassified to profit or loss in subsequent periods:</i> | | | | | |
| – (losses) / gains as a result of re-measurement on defined post-employment benefit plan | 21 a, 24 | (2,043) | 436 | (1,148) | (108) |
| Net other comprehensive (loss) / income not to be reclassified to profit or loss in subsequent periods | | (2,043) | 436 | (1,148) | (108) |
| Other comprehensive (loss) / income for the year | | (13,814) | 9,967 | (12,919) | 9,423 |
| TOTAL comprehensive income for the year | | 80,545 | 85,922 | 88,308 | 222,156 |
| Attributable to: | | | | | |
| – Equity holder of the Parent Company | | 78,846 | 83,390 | 88,308 | 222,156 |
| – Non-controlling interests | | 1,699 | 2,532 | – | – |

The notes on pages 15 to 62 are an integral part of these Financial Statements

Uldis Bariss
Member of the Management Board

Kaspars Cikmačs
Member of the Management Board

Liāna Keldere
Accounting director of Latvenergo AS

7 April 2020



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Statement of Financial Position

EUR'000

| | | Group | | Parent Company | |
|--|---------|------------------|------------------|------------------|------------------|
| | Notes | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| ASSETS | | | | | |
| Non-current assets | | | | | |
| Intangible assets | 13 a | 22,587 | 19,079 | 26,111 | 22,813 |
| Property, plant and equipment | 14 a | 2,752,945 | 3,297,093 | 1,109,001 | 1,133,886 |
| Right-of-use assets | 15 | 5,522 | – | 3,476 | – |
| Investment property | 14 b | 301 | 467 | 39,435 | 61,796 |
| Non-current financial investments | 16 | 39 | 40 | 831,350 | 830,542 |
| Non-current loans to related parties | 29 e | – | – | 588,434 | 595,004 |
| Other non-current receivables | 18 b | 433 | 30,920 | 421 | 331 |
| Other financial investments | 22 | 16,885 | 16,935 | 16,885 | 16,935 |
| Total non-current assets | | 2,798,712 | 3,364,534 | 2,615,113 | 2,661,307 |
| Current assets | | | | | |
| Inventories | 17 | 104,927 | 71,975 | 89,522 | 58,410 |
| Receivables from contracts with customers | 18 a | 111,530 | 117,955 | 82,973 | 81,025 |
| Other current receivables | 18 b, c | 77,085 | 84,830 | 13,328 | 14,445 |
| Deferred expenses | | 3,015 | 2,598 | 2,082 | 1,552 |
| Current loans to related parties | 29 e | – | – | 205,822 | 170,811 |
| Prepayment for income tax | | 140 | 11,619 | 140 | 10,152 |
| Derivative financial instruments | 24 | 6,717 | 15,853 | 6,717 | 15,853 |
| Cash and cash equivalents | 19 | 122,422 | 129,455 | 121,261 | 127,554 |
| Current assets excluding assets held for distribution | | 425,836 | 434,285 | 521,845 | 479,802 |
| Assets held for distribution | 30 | 640,393 | – | – | – |
| Total current assets | | 1,066,229 | 434,285 | 521,845 | 479,802 |
| TOTAL ASSETS | | 3,864,941 | 3,798,819 | 3,136,958 | 3,141,109 |

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Āris Žigurs
Chairman of the Management Board

Guntars Balčūns
Member of the Management Board

Statement of Financial Position (continued)

EUR'000

| | | Group | | Parent Company | |
|--|------------|------------------|------------------|------------------|------------------|
| | Notes | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| EQUITY AND LIABILITIES | | | | | |
| EQUITY | | | | | |
| Share capital | 20 | 834,883 | 834,791 | 834,883 | 834,791 |
| Reserves | 21 a | 1,075,235 | 1,125,466 | 778,162 | 794,555 |
| Retained earnings | | 318,555 | 351,350 | 336,242 | 364,477 |
| Reserves of disposal group classified as held for distribution | 30 | 28,936 | – | – | – |
| Equity attributable to equity holder of the Parent Company | | 2,257,609 | 2,311,607 | 1,949,287 | 1,993,823 |
| Non-controlling interests | | 7,878 | 8,458 | – | – |
| Total equity | | 2,265,487 | 2,320,065 | 1,949,287 | 1,993,823 |
| LIABILITIES | | | | | |
| Non-current liabilities | | | | | |
| Borrowings | 23 | 702,129 | 700,028 | 696,863 | 690,568 |
| Lease liabilities | 15 | 4,349 | – | 3,126 | – |
| Deferred income tax liabilities | 12 | 8,327 | 12,297 | – | – |
| Provisions | 27 | 18,491 | 20,178 | 8,489 | 8,625 |
| Derivative financial instruments | 24 | 6,149 | 3,923 | 6,149 | 3,923 |
| Deferred income from contracts with customers | 28 I a | 143,330 | 143,494 | 877 | – |
| Other deferred income | 28 I b, c | 194,033 | 303,519 | 186,297 | 210,105 |
| Total non-current liabilities | | 1,076,808 | 1,183,439 | 901,801 | 913,221 |
| Current liabilities | | | | | |
| Borrowings | 23 | 180,542 | 114,315 | 176,036 | 111,700 |
| Lease liabilities | 15 | 1,216 | – | 376 | – |
| Trade and other payables | 26 | 115,708 | 135,010 | 78,381 | 92,062 |
| Deferred income from contracts with customers | 28 II a | 13,764 | 13,271 | 63 | – |
| Other deferred income | 28 II b, c | 24,857 | 26,438 | 24,031 | 24,022 |
| Derivative financial instruments | 24 | 6,983 | 6,281 | 6,983 | 6,281 |
| Current liabilities excluding liabilities held for distribution | | 343,070 | 295,315 | 285,870 | 234,065 |
| Liabilities directly associated with the assets held for distribution | 30 | 179,576 | – | – | – |
| Total current liabilities | | 522,646 | 295,315 | 285,870 | 234,065 |
| Total liabilities | | 1,599,454 | 1,478,754 | 1,187,671 | 1 147,286 |
| TOTAL EQUITY AND LIABILITIES | | 3,864,941 | 3,798,819 | 3,136,958 | 3 141,109 |

The notes on pages 15 to 62 are an integral part of these Financial Statements

Uldis Bariss
Member of the Management Board

Kaspars Cikmačs
Member of the Management Board

Liāna Keldere
Accounting director of Latvenergo AS

7 April 2020

Statement of Changes in Equity

EUR'000

| | | Group | | | | | | | Parent Company | | | |
|--|----------|---|-----------|-------------------|--|-----------|---------------------------|-----------|----------------|----------|-------------------|-----------|
| | | Attributable to equity holder of the Parent Company | | | | | | | | | | |
| | Note | Share capital | Reserves | Retained earnings | Reserves classified as held for distribution | TOTAL | Non-controlling interests | TOTAL | Share capital | Reserves | Retained earnings | TOTAL |
| As of 1 January 2018 | | 1,288,715 | 1,125,728 | 424,116 | – | 2,838,559 | 8,042 | 2,846,601 | 1,288,715 | 791,681 | 301,613 | 2,382,009 |
| Decrease of share capital | 20 | (454,413) | – | – | – | (454,413) | – | (454,413) | (454,413) | – | – | (454,413) |
| Increase of share capital | 14 a, 20 | 489 | – | – | – | 489 | – | 489 | 489 | – | – | 489 |
| Dividends for 2017 | 21 b | – | – | (156,418) | – | (156,418) | (2,116) | (158,534) | – | – | (156,418) | (156,418) |
| Disposal of non-current assets revaluation reserve | 21 a | – | (10,229) | 10,229 | – | – | – | – | – | (6,549) | 6,549 | – |
| Total transactions with owners and other changes in equity | | (453,924) | (10,229) | (146,189) | – | (610,342) | (2,116) | (612,458) | (453,924) | (6,549) | (149,869) | (610,342) |
| Profit for the year | | – | – | 73,423 | – | 73,423 | 2,532 | 75,955 | – | – | 212,733 | 212,733 |
| Other comprehensive income for the year | 21 a | – | 9,967 | – | – | 9,967 | – | 9,967 | – | 9,423 | – | 9,423 |
| Total comprehensive income for the year | | – | 9,967 | 73,423 | – | 83,390 | 2,532 | 85,922 | – | 9,423 | 212,733 | 222,156 |
| As of 31 December 2018 | | 834,791 | 1,125,466 | 351,350 | – | 2,311,607 | 8,458 | 2,320,065 | 834,791 | 794,555 | 364,477 | 1,993,823 |
| Increase of share capital | 14 a, 20 | 92 | – | – | – | 92 | – | 92 | 92 | – | – | 92 |
| Dividends for 2018 | 21 b | – | – | (132,936) | – | (132,936) | (2,279) | (135,215) | – | – | (132,936) | (132,936) |
| Disposal of non-current assets revaluation reserve | 21 a | – | (7,481) | 7,481 | – | – | – | – | – | (3,474) | 3,474 | – |
| Discontinued operation | 30 | – | (28,936) | – | 28,936 | – | – | – | – | – | – | – |
| Total transactions with owners and other changes in equity | | 92 | (36,417) | (125,455) | 28,936 | (132,844) | (2,279) | (135,123) | 92 | (3,474) | (129,462) | (132,844) |
| Profit for the year | | – | – | 92,660 | – | 92,660 | 1,699 | 94,359 | – | – | 101,227 | 101,227 |
| Other comprehensive loss for the year | 21 a | – | (13,814) | – | – | (13,814) | – | (13,814) | – | (12,919) | – | (12,919) |
| Total comprehensive (loss) / income for the year | | – | (13,814) | 92,660 | – | 28,936 | 1,699 | 80,545 | – | (12,919) | 101,227 | 88,308 |
| As of 31 December 2019 | | 834,883 | 1,075,235 | 318,555 | 28,936 | 2,257,609 | 7,878 | 2,265,487 | 834,883 | 778,162 | 336,242 | 1,949,287 |

The notes on pages 15 to 62 are an integral part of these Financial Statements

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Āris Žigurs
Chairman of the Management Board

Guntars Balčūns
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

7 April 2020



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Statement of Cash Flows

EUR'000

| | Notes | Group | | Parent Company | |
|---|----------------|----------------|----------------|----------------|----------------|
| | | 2019 | 2018 | 2019 | 2018 |
| Cash flows from operating activities | | | | | |
| Profit before tax | | 92,072 | 74,734 | 101,227 | 212,760 |
| Profit before tax from discontinued operation | 30 | 12,667 | 13,779 | – | – |
| Profit before tax, total | | 104,739 | 88,513 | 101,227 | 212,760 |
| Adjustments: | | | | | |
| – Amortisation, depreciation and impairment of intangible assets, property, plant and equipment (PPE) and right-of-use assets | 13 a, 14 a, 15 | 167,918 | 225,820 | 67,543 | 127,124 |
| – Loss from disposal of non-current assets | | 26,980 | 17,638 | 21,965 | 12,320 |
| – Interest costs | 11 | 9,346 | 8,267 | 11,590 | 10,020 |
| – Interest income | 11 | (1,034) | (1,114) | (12,842) | (11,403) |
| – Fair value loss on derivative financial instruments | 8 | 293 | 417 | 293 | 417 |
| – Dividends from subsidiaries | 16 | – | – | (54,858) | (177,646) |
| – Decrease in provisions | 27 | (3,691) | (1,295) | (1,283) | (318) |
| – Unrealised (income) / loss on currency translation differences | 11 | (54) | 2 | (54) | 2 |
| Operating profit before working capital adjustments | | 304,497 | 338,248 | 133,581 | 173,276 |
| (Increase)/ decrease in inventories | | (32,990) | 4,353 | (31,112) | 3,414 |
| Decrease in receivables from contracts with customers and other receivables | | 41,083 | 98,125 | 45,110 | 140,461 |
| Increase / (decrease) in trade and other liabilities | | 11,757 | (90,344) | (38,789) | (79,741) |
| Impact of non-cash offsetting of operating receivables and liabilities from subsidiaries, net | | – | – | 270,009 | 201,571 |
| Cash generated from operating activities | | 324,347 | 350,382 | 378,799 | 438,981 |
| Interest paid | | (9,483) | (9,066) | (11,741) | (10,781) |
| Interest paid on leases | 15 | (54) | – | – | – |
| Interest received | | 1,084 | 1,113 | 1,084 | 1,113 |
| Paid corporate income tax | | (461) | (39,560) | 10,000 | (34,918) |
| Net cash flows from operating activities | | 315,433 | 302,869 | 378,142 | 394,395 |

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Āris Žigurs

Chairman of the Management Board

Guntars Balčūns

Member of the Management Board

Statement of Financial Position (continued)

EUR'000

| | Notes | Group | | Parent Company | |
|---|-------|------------------|------------------|------------------|------------------|
| | | 2019 | 2018 | 2019 | 2018 |
| Cash flows from investing activities | | | | | |
| Loans issued to subsidiaries, net | 29 e | – | – | (272,401) | (323,539) |
| Purchase of intangible assets and PPE | | (254,947) | (238,501) | (70,981) | (60,644) |
| Dividends received from subsidiaries | 16 | – | – | 21,115 | 53,378 |
| Proceeds from redemption of other financial investments | | 49 | 49 | 49 | 49 |
| Net cash flows used in investing activities | | (254,898) | (238,452) | (322,218) | (330,756) |
| Cash flows from financing activities | | | | | |
| Proceeds on borrowings from financial institutions | 23 | 180,291 | 93,500 | 180,000 | 90,000 |
| Repayment of borrowings | 23 | (112,102) | (105,931) | (109,513) | (102,522) |
| Received financing from European Union | | 579 | – | 250 | – |
| Lease payments | 15 | (821) | – | (18) | – |
| Dividends paid to non-controlling interests | 21 b | (2,279) | (2,116) | – | – |
| Dividends paid to equity holder of the Parent Company | 21 b | (132,936) | (156,418) | (132,936) | (156,418) |
| Net cash flows used in financing activities | | (67,268) | (170,965) | (62,217) | (168,940) |
| Net decrease in cash and cash equivalents | | (6,733) | (106,548) | (6,293) | (105,301) |
| Cash and cash equivalents at the beginning of the year | 19 | 129,455 | 236,003 | 127,554 | 232,855 |
| Cash and cash equivalents at the end of the year | 19 | 122,722 | 129,455 | 121,261 | 127,554 |

The notes on pages 15 to 62 are an integral part of these Financial Statements

Uldis Bariss

Member of the Management Board

Kaspars Cikmačs

Member of the Management Board

Liāna Keldere

Accounting director of Latvenergo AS

7 April 2020



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 16.

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 year 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.

The Supervisory Board of Latvenergo AS since 16 December 2016 until 19 June 2019 was comprised of the following members: Andris Ozoliņš (Chairman of the Board), Andris Liepiņš (Deputy Chairman), Baiba Anda Rubesa, Mārtiņš Bičevskis and Martin Sedlacky. Since 19 June 2019 until 1 July 2019 the Supervisory Board of Latvenergo AS was comprised of the following members: Pāvels Rebenoks (Chairman of the Board), Renārs Degro (Deputy Chairman), Inese Kubicka, Kristaps Stepanovs and Artūrs Šnoriņš. Since 8 October 2019 until the election of new members of the Supervisory Board of Latvenergo AS in accordance with the candidate selection procedure started in August 2019, the Supervisory Board of Latvenergo AS is comprised of the following members: Edmunds Valantis (Chairman), Edijs Šaicāns (Deputy Chairman) and Irēna Bērziņa.

The Supervisory body – Audit Committee since 3 March 2017 until 19 June 2019 was comprised of the following members: Torben Pedersen (Chairman of the Committee), Svens Dinsdorfs, Andris Ozoliņš, Andris Liepiņš and Marita Salgrāve. Since 19 June 2019 until 1 July 2019 Audit Committee was comprised of the following members: Torben Pedersen, Svens Dinsdorfs, Marita Salgrāve, Renārs Degro and Kristaps Stepanovs. Since 8 October 2019 Audit Committee was comprised of the following members: Torben Pedersen, Svens Dinsdorfs, Marita Salgrāve and Irēna Bērziņa.

The Management Board of Latvenergo AS has approved the Latvenergo Group and Latvenergo AS Financial statements 2019 on 7 April 2020. 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 as a whole are set out below, while remaining accounting policies are described in the notes to which they relate. These policies have been consistently applied to all the years presented, unless otherwise stated.

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.

The Financial Statements for year 2019 include the financial information in respect of the Latvenergo Group and Latvenergo AS for the year ended 31 December 2019 and comparative information for year 2018. Where it has been necessary, comparatives for year 2018 are reclassified using the same principles applied for preparation of the Financial Statements for 2019 for discontinued operation according to IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations' (Note 30), except for the adoption of IFRS 16 'Leases' (see section 'Changes in accounting policies' of Note 2 and Note 15).

The Latvenergo Group's and Latvenergo AS Financial Statements had been prepared in euros (EUR) currency and all amounts shown in these Financial Statements except non-monetary items are presented in thousands of EUR (EUR'000).

All figures, unless stated otherwise are rounded to the nearest thousand. Certain monetary amounts, percentages and other figures included in this report are subject to rounding adjustments. On occasion, therefore, amounts shown in tables may not be the arithmetic accumulation of the figures that precede them, and figures expressed as percentages in the text and in tables may not total 100 percent.

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 4.

Adoption of new and/or changed IFRS and International Financial Reporting Interpretations Committee (IFRIC) interpretations

a) Standards issued and which became effective, and are relevant for the Group's and the Parent Company's operations

• IFRS 16: Leases

From 1 January 2019 The Group and the Parent Company applies IFRS 16. In accordance with the transitional provisions of IFRS 16, the standard is applied retrospectively with evaluation of its cumulative effect as of 1 January 2019. The Group as the lessee recognised right-of-use assets and lease liabilities in amount of EUR 8,075 thousand (the Parent Company: EUR 3,870 thousand) in financial statements. The Parent Company applied simplified approach and did not restate comparative information. Right-of-use assets were measured equal to the lease liabilities at the date of initial application. At the date of initial application, no cumulative effect of initial application was recognised as an adjustment to the opening balance of retained earnings.

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.

Upon adopting IFRS 16, the Group and the Parent Company used a single recognition and measurement approach for all leases, with certain exemptions and made 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 etc.). The Parent Company used practical expedient for short-term leases.

The Group's and the Parent Company's as lessor accounting is substantially unchanged and do not have significant impact on financial statements.

New standard accounting and measurement principles are disclosed in Note 15, but the initial adoption is disclosed in the section Change in accounting policy of this Annex.

b) Standards and its amendments issued and not yet effective, but are relevant for the Group's and the Parent Company's operations

• Amendments to the Conceptual Framework for Financial Reporting

Amendments are effective for the periods beginning on or after 1 January 2020, not yet adopted by the EU. The revised Conceptual Framework includes a new chapter on measurement; guidance on reporting financial performance; improved definitions and guidance - in particular the definition of a liability; and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting. The Group and the Parent Company makes assessment on the impact of these amendments on its financial statements and disclosures, but does not consider them to have a significant impact on its financial results.

• Amendments to IFRS 3 - Definition of a business

Effective from 1 January 2020, not yet adopted by the EU. The amendments revise definition of a business. A business must have inputs and a substantive process that together significantly contribute to the ability to create outputs. The new guidance provides a framework to evaluate when an input and a substantive process are present, including for early stage companies that have not generated outputs. An organised workforce should be present as a condition for classification as a business if are no outputs. The definition of the term 'outputs' is narrowed to focus on goods and services provided to customers, generating investment income and other income, and it excludes returns in the form of lower costs and other economic benefits. It is also no longer necessary to assess whether market participants are capable of replacing missing elements or integrating the acquired activities and assets. An entity can apply a 'concentration test'. The assets acquired would not represent a business if substantially all of the fair value of gross assets acquired were concentrated in a single asset (or a group of similar assets). The Group and the Parent Company makes further assessment on the impact of these amendments. The amendments may result in changes in accounting policies but will not have a material effect on the Group's and the Parent Company's financial statements.

• Amendments to IAS 1 and IAS 8 - Definition of materiality

Effective from 1 January 2020, not yet adopted by the EU. The amendments clarify the definition of material and how it should be applied by including in the definition guidance that until now has featured elsewhere in IFRS. In addition, the explanations accompanying the definition have been improved. Finally, the amendments ensure that the definition of material is consistent across all IFRS Standards. Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general-purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity. The Group and the Parent Company makes assessment on the impact of these amendments on its financial statements but does not expect them to have a material impact on the Group's and the Parent Company's financial position and estimates and judgements used in preparation of financial statements.

Consolidation

a) Subsidiaries

Subsidiaries are all entities over which the Group has control. The Group controls an entity where the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity.

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 16.

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 a business combination are measured initially at their fair values at the acquisition date.

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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 economic entity. Changes in a Parent's ownership interest in a subsidiary that do not result in the Parent losing control over 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.

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.

Financial assets and liabilities

The Group and the Parent Company classify its financial assets 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 the contractual terms of the cash flows. 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.

For assets 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.

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.

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:

- at 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 item in the statement of profit or loss position 'Other operating expenses'.

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.

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.



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Impairment

The Group and the Parent Company assess on a forward-looking basis the expected credit loss 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. Rules for estimating and recognising impairment losses are described per Note 4 b.

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 public service obligation (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, if any significant exists.

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 24.

Changes in accounting policies

Adoption of IFRS 16 in the reporting year

From 1 January 2019 the Group and the Parent Company applied IFRS 16 for the first time. In accordance with the transitional provisions of IFRS 16, the standard is applied retrospectively with evaluation of its cumulative effect as of 1 January 2019. The Group as the lessee recognised in financial statements right-of-use assets and lease liabilities in the amount of EUR 8,075 thousand (the Parent Company: EUR 3,870 thousand), which had been previously classified as 'operating leases' under the principles of IAS 17.

In accordance with IFRS 16, lease liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019 – 1.549 %.

The Group and the Parent Company applied simplified approach and did not restate comparative information. Right-of-use assets measured equal to the lease liability at the date of initial application. At the date of initial application, no cumulative effect of initial application recognised as an adjustment to the opening balance of retained earnings.

The Group and the Parent Company has concluded several agreements for lease of land and real estate, as well has concluded an agreement until 2028 on a lease of the fiber of the combined optical cable (OPGW - optical ground wire with dual function).

Accounting policy related to lease transactions disclosed in Note 15. The Group and the Parent Company did not have finance leases before adoption of the new standard as of 1 January 2019.

In applying IFRS 16 for the first time, the Group and the Parent Company has used the following permitted practical expedients:

- single discount rate to a portfolio of leases with reasonably similar characteristics;
- accounting for operating leases with a remaining lease term of less than 12 months as of 1 January 2019 as short-term leases;
- excluding initial direct costs for the measurement of the right-of-use asset at the date of initial application;
- using hindsight in determining the lease term where the contract contains options to extend or terminate the lease.



The following individual line items were affected in the Group's and the Parent Company's Statement of Financial Position as of 1 January 2019 upon adoption of IFRS 16 (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):

EUR'000

| | Group | | | Parent Company | | |
|--------------------------------------|---|----------------------------|-----------------------------------|---|----------------------------|-----------------------------------|
| | Balance as of 31/12/2018 before adjustments | Effect of IFRS 16 adoption | Adjusted balance as of 01/01/2019 | Balance as of 31/12/2018 before adjustments | Effect of IFRS 16 adoption | Adjusted balance as of 01/01/2019 |
| ASSETS | | | | | | |
| Non-current assets | | | | | | |
| Right-of-use assets | – | 8,075 | 8,075 | – | 3,870 | 3,870 |
| Total non-current assets | 3,364,534 | 8,075 | 3,372,609 | 2,661,307 | 3,870 | 2,665,177 |
| TOTAL ASSETS | 3,798,819 | 8,075 | 3,806,894 | 3,141,109 | 3,870 | 3,144,979 |
| EQUITY AND LIABILITIES | | | | | | |
| LIABILITIES | | | | | | |
| Non-current liabilities | | | | | | |
| Lease liabilities | – | 6,839 | 6,839 | – | 3,500 | 3,500 |
| Total non-current liabilities | 1,183,439 | 6,839 | 1,190,278 | 913,221 | 3,500 | 916,721 |
| Current liabilities | | | | | | |
| Lease liabilities | – | 1,236 | 1,236 | – | 370 | 370 |
| Total current liabilities | 295,315 | 1,236 | 296,551 | 234,065 | 370 | 234,435 |
| TOTAL EQUITY AND LIABILITIES | 3,798,819 | 8,075 | 3,806,894 | 3,141,109 | 3,870 | 3,144,979 |

The initial application of standard has the following impact: increase of total assets impacted by the capitalisation of the right-of-use assets and increase of total liabilities induced by recognition of relevant lease liabilities.

If the lease contract includes an extension options and if management has reasonable confidence to exercise this option, The Group's and the Parent Company's has used actual historical experience to determine lease terms. Lease contracts are usually concluded for a fixed period with different maturities, as agreed with counterparties, and may include options to extend lease terms. Management applies judgement to determine the lease term evaluating facts and circumstances that may affect the lease term. Management's estimates are reviewed for any material events or significant changes in circumstances, that are under the lessee's control.

Preliminary measurement of lease liabilities by the adoption of IFRS 16:

EUR'000

| | Group 01/01/2019 | Parent Company 01/01/2019 |
|--|---------------------|------------------------------|
| Operating lease commitments disclosed as of 31 December 2018 as per IAS17 | 9,531 | 21,738 |
| Adjustments for lease evaluation for compliance with IFRS 16 requirements | (1,388) | (17,413) |
| Adjustments as a result of the assessment of the possibility of renewal and termination of contracts | 986 | – |
| Adjustments for variable lease payments | (93) | – |
| Excluded short-term leases | (149) | (149) |
| Discounted value using the incremental borrowing rate of at the date of initial application | (812) | (306) |
| Lease liabilities recognised as of 1 January 2019 | 8,075 | 3,870 |
| Of which are: | | |
| – current | 6,839 | 3,500 |
| – non-current | 1,236 | 370 |

The adoption of IFRS 16 did not require for the Group and the Parent Company, as lessor, to make adjustments to the accounting for assets held as for lessor.



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, interest rate risk and price risk), credit 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

| | | Group | | | Parent Company | | |
|---|-------|---------------------------------------|---------------------------------|--|---------------------------------------|---------------------------------|--|
| | Notes | Financial assets at amortised cost | Derivatives used for hedging | Financial instruments at fair value through the profit or loss | Financial assets at amortised cost | Derivatives used for hedging | Financial instruments at fair value through the profit or loss |
| Financial assets as of 31 December 2019 | | | | | | | |
| Receivables from contracts with customers | 18 a | 111,530 | – | – | 82,973 | – | – |
| Other current financial receivables | 18 b | 76,891 | – | – | 13,221 | – | – |
| Loans to related parties | 29 e | – | – | – | 794,256 | – | – |
| Other non-current financial receivables | 18 b | 433 | – | – | 421 | – | – |
| Derivative financial instruments | 24 l | – | 4,684 | 2,033 | – | 4,684 | 2,033 |
| Other financial investments | 22 | 16,885 | – | – | 16,885 | – | – |
| Cash and cash equivalents | 19 | 122,422 | – | – | 121,261 | – | – |
| | | 328,161 | 4,684 | 2,033 | 1,029,017 | 4,684 | 2,033 |
| Financial assets as of 31 December 2018 | | | | | | | |
| Receivables from contracts with customers | 18 a | 117,955 | – | – | 81,025 | – | – |
| Other current financial receivables | 18 b | 84,613 | – | – | 14,233 | – | – |
| Loans to related parties | 29 e | – | – | – | 765,815 | – | – |
| Other non-current financial receivables | 18 b | 30,920 | – | – | 331 | – | – |
| Derivative financial instruments | 24 l | – | 15,748 | 105 | – | 15,748 | 105 |
| Other financial investments | 22 | 16,935 | – | – | 16,935 | – | – |
| Cash and cash equivalents | 19 | 129,455 | – | – | 127,554 | – | – |
| | | 379,878 | 15,748 | 105 | 1,005,893 | 15,748 | 105 |
| Financial liabilities as of 31 December 2019 | | | | | | | |
| Borrowings | 23 | 882,671 | – | – | 872,899 | – | – |
| Derivative financial instruments | 24 l | – | 10,204 | 2,220 | – | 10,912 | 2,220 |
| Lease liabilities | 15 | 5,565 | – | – | 3,502 | – | – |
| Trade and other financial current payables | 26 | 91,410 | – | – | 68,249 | – | – |
| | | 979,646 | 10,912 | 2,220 | 944,650 | 10,912 | 2,220 |
| Financial liabilities as of 31 December 2018 | | | | | | | |
| Borrowings | 23 | 814,343 | – | – | 802,268 | – | – |
| Derivative financial instruments | 24 l | – | 10,204 | – | – | 10,204 | – |
| Trade and other financial current payables | 26 | 103,707 | – | – | 78,726 | – | – |
| | | 918,050 | 10,204 | – | 880,994 | 10,204 | – |



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a) Market risk

I) Foreign currencies exchange risk

As of 31 December 2019, and 31 December 2018 the Group and the Parent Company had borrowings denominated only in euros (Note 23). Their revenues and most of the financial assets and liabilities were denominated in euros. Accordingly, neither the Group nor 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 2019 and 2018 the Group and the Parent Company had no capital expenditure project which expected transactions would create significant currency risk.

II) 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 2019, 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 633 thousand higher (2018: EUR 875 thousand) and the Parent Company's income from the cash reserves held at bank for the year would have been EUR 621 thousand higher (2018: EUR 860 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 229.4 million (2018: EUR 225.1million) (Note 24 II). 45% of the total Group's and 45% the Parent Company's borrowings as of 31 December 2019 (31/12/2018: 53% and 54% respectively) had fixed interest rate (taking into account the effect of the

interest rate swaps) and average fixed rate duration was 1.8 years for the Group and the Parent Company (2018: 2.1 years for the Group and the Parent Company respectively). All necessary actions will be taken during the year 2020 to ensure the average fixed interest rate period within the limits stipulated by the Group's Financial Risk Management Policy.

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 2,297 thousand lower (over the next 12 months period after 31/12/2018: EUR 1,999 thousand), the Parent Company's profit for the year would have been EUR 255 thousand lower (over the next 12 months period after 31/12/2018: EUR 1,946 thousand).

As of 31 December 2019, 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 4,634 thousand higher (31/12/2018: EUR 4,649 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 4,815 thousand lower (31/12/2018: EUR 4,834 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 2019 and 2018 has purchased electricity forward and future contracts and natural gas forward contracts (Note 24 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 concentration 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 Latvenergo 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 19), receivables from contracts with customers and other receivables (Note 18), derivative financial instruments (Note 24) and other financial investments (Note 22).



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Assessment of maximum possible exposure to credit risk:

EUR'000

| | Notes | Group | | Parent Company | |
|---|-------|----------------|----------------|------------------|------------------|
| | | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Receivables from contracts with customers | 18 a | 111,530 | 117,955 | 82,973 | 81,025 |
| Other non-current financial receivables | 18 b | 433 | 30,920 | 421 | 331 |
| Other current financial receivables | 18 b | 76,891 | 84,613 | 13,221 | 14,233 |
| Loans to subsidiaries | 29 e | – | – | 794,256 | 765,815 |
| Cash and cash equivalents | 19 | 122,422 | 129,455 | 121,261 | 127,554 |
| Derivative financial instruments | 24 | 6,717 | 15,853 | 6,717 | 15,853 |
| Other financial investments | 22 | 16,885 | 16,935 | 16,885 | 16,935 |
| | | 334,878 | 395,731 | 1,035,734 | 1,021,746 |

Under IFRS 9 the Group and the Parent 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 and 18)

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. Depending on set credit limits, the cash held in one bank or financial institution can not exceed fifty percent of total balance of cash. 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. Credit risk assessment related to receivables from contracts with customers and other financial receivables described per Notes 4 b and 18.

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 | |
|--|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Investment level credit rating* | 117,347 | 126,483 | 116,186 | 124,582 |
| No or non-investment level credit rating | 5,075 | 2,972 | 5,075 | 2,972 |
| | 122,422 | 129,455 | 121,261 | 127,554 |

* Investment level credit rating assigned for the parent companies of banks.

The table represents exposure to banks and financial counterparties broken down per rating class according to Moodys rating scale. The expected credit losses are not significant (below 1%) as the majority of cash and cash equivalents are held at banks and financial institutions with investment level credit rating and financial assets are considered to have good credit worthiness.

EUR'000

| | Group | | Parent Company | |
|------------------------------------|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Aa2 | 70,621 | 51,376 | 69,468 | 49,556 |
| Aa3 | 1,926 | 22,248 | 1,926 | 22,247 |
| Baa1 | 40,466 | 48,201 | 40,458 | 48,121 |
| Baa2 | 4,334 | 4,658 | 4,334 | 4,658 |
| Non-investment level credit rating | 5,075 | 2,972 | 5,075 | 2,972 |
| | 122,422 | 129,455 | 121,261 | 127,554 |

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 Level 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 19) 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.



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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 |
| As of 31 December 2019 | | | | | | | | | | |
| Borrowings from banks | 148,892 | 112,531 | 267,429 | 243,819 | 772,671 | 144,303 | 110,795 | 264,260 | 243,315 | 762,673 |
| Issued debt securities (bonds) | 37,849 | 1,900 | 102,203 | – | 141,952 | 37,849 | 1,900 | 102,203 | – | 141,952 |
| Derivative financial instruments | 8,740 | 3,959 | 3,003 | 1,154 | 16,856 | 8,740 | 3,959 | 3,003 | 1,154 | 16,856 |
| Lease liabilities * | 1,261 | 1,062 | 1,670 | 2,399 | 6,392 | 428 | 428 | 1,284 | 1,612 | 3,752 |
| Trade and other current financial payables (Note 26) ** | 91,410 | – | – | – | 91,410 | 68,249 | – | – | – | 68,249 |
| | 288,152 | 119,452 | 374,305 | 247,372 | 1,029,281 | 259,569 | 117,082 | 370,750 | 246,081 | 993,482 |
| As of 31 December 2018 | | | | | | | | | | |
| Borrowings from banks | 116,989 | 159,053 | 250,342 | 214,090 | 740,474 | 114,241 | 154,751 | 246,134 | 212,846 | 727,972 |
| Issued debt securities (bonds) | 2,880 | 37,769 | 104,228 | – | 144,877 | 2,880 | 37,769 | 104,228 | – | 144,877 |
| Derivative financial instruments | 6,673 | 3,000 | 4,239 | 1,755 | 15,667 | 6,673 | 3,000 | 4,239 | 1,755 | 15,667 |
| Trade and other current financial payables (Note 26) ** | 103,707 | – | – | – | 103,707 | 78,726 | – | – | – | 78,726 |
| | 230,249 | 199,822 | 358,809 | 215,845 | 1,004,725 | 202,520 | 195,520 | 354,601 | 214,601 | 967,242 |

* The carrying amount of the lease (discounted) the Group's is EUR 5,565 thousand (the Parent Company's: EUR 3,502 thousand)
** Excluding advances received, deferred income, tax related liabilities and other non-current or current non-financial payables

3.2. Capital 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 2019 nor 2018), 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. 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 | |
|---------------|------------|------------|----------------|------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Total equity | 2,265,487 | 2,320,065 | 1,949,287 | 1,993,823 |
| Total assets | 3,864,941 | 3,798,819 | 3,136,958 | 3,141,109 |
| Capital Ratio | 59 % | 61 % | 62 % | 63 % |



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 are defined separate cash-generating units. 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 are 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 the 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

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 Parent Company uses judgement in making these assumptions and selecting the inputs to the impairment calculation, based on the Group’s and the Parent 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 and 18).

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 3 years 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 other non-current and current financial 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 Level 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) (Level 1).

c) Estimates concerning revenue recognition from contracts with customers

I) 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 6).

Management has considered the 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 6).

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 and accounted as deferred income (contract liabilities) from contracts with customers under IFRS 15 (see Note 6 and 28). 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 6).

d) Recognition and reassessment of provisions

As of 31 December 2019, the Group had set up provisions for environmental protection, post-employment benefits and termination benefits totalling EUR 20.1 million (31/12/2018: EUR 21.0 million) and the Parent Company in amount of EUR 9.0 million (31/12/2019: EUR 9.0 million) (Note 27). 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, 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 27.

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 25).

f) Lease term and classification

In determining the lease term, management considers all facts and circumstances that create an economic incentive to exercise an extension option, or not exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended (or not terminated). The assessment is reviewed if a significant event or a significant change in circumstances occurs which affects this assessment and is within the control of the lessee.

The Group has entered into the lease agreement as a lessor with licenced transmission system operator



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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. By the end of 2019 no amendments to the lease agreement had been received and under the terms of the contract - 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 till the adoption of IFRS 16. In making the judgement on lease classification management assessed the criteria included in IAS 17 'Leases' / IFRS 16 '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, periods after 2025 need not to be taken into account when assessing the substance of the current lease agreement. Carrying amount of leased assets (property, plant and equipment) as of 31 December 2019 is disclosed in Note 30.

g) Recognition of connection service fees to transmission system (IFRS 16 / 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) 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 28:

- an unconditional grant in amount of EUR 140,000 thousand recognised as 'Other income' 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 Enerģijas 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. For Enerģijas publiskais tirgotājs AS to ensure financing of compensation, the Parent Company concluded agreement on loan issue in amount equal to the grant receivable.

On 20 March 2018 decreased share capital of the Parent Company in amount of EUR 454,413 thousand (Note 20).

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 23,990 thousand were recognised as 'Other income' in the Group's and Parent Company's statement of profit or loss in 2019 (2018: EUR 81,004 thousand) (Note 7). Consequently, EUR 209,419 thousand remained recognised as deferred income as of 31 December 2019 (31 December 2018: EUR 233,409 thousand) and to be allocated to income on a straight-line basis until fulfilling obligation till the end of the support period – 23 September 2028.

i) Deferred tax recognition

The untaxed 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 (Note 12). Management of the Parent Company has made judgement on the expected timing and extent of the distribution profits of subsidiaries and recognised in the Group's Consolidated Financial Statements deferred tax liability related to profit of its subsidiaries to be distributed.



5. Operating segment information

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 trade | 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 |
| 2019 | | | | | | | | | | | | |
| Revenue | | | | | | | | | | | | |
| External customers | 516,626 | 318,105 | 36,643 | 6,905 | 878,279 | – | 878,279 | 395,727 | 41,802 | 437,529 | – | 437,529 |
| Inter-segment | 1,315 | 1,611 | 3,387 | 45,739 | 52,052 | (52,052) | – | 767 | 22,520 | 23,287 | (23,287) | – |
| TOTAL revenue | 517,941 | 319,716 | 40,030 | 52,644 | 930,331 | (52,052) | 878,279 | 396,494 | 64,322 | 460,816 | (23,287) | 437,529 |
| Results | | | | | | | | | | | | |
| EBITDA | 103,347 | 125,093 | 39,798 | 12,729 | 280,967 | – | 280,967 | 92,550 | 20,101 | 112,651 | – | 112,651 |
| Depreciation, amortisation and impairment of intangible assets, PPE and right-of-use assets | (56,485) | (75,276) | (24,756) | (11,400) | (167,917) | – | (167,917) | (53,196) | (14,347) | (67,543) | – | (67,543) |
| Segment profit before tax | 46,862 | 49,817 | 15,042 | 1,329 | 113,050 | (8,293) | 104,757 | 39,354 | 5,754 | 45,108 | 56,119 | 101,227 |
| Segment assets at the end of the year | 1,346,937 | 1,681,422 | 642,151 | 87,966 | 3,758,476 | 106,465 | 3,864,941 | 1,197,434 | 168,915 | 1,366,349 | 1,770,609 | 3,136,958 |
| Segment liabilities at the end of the year | 275,638 | 189,399 | 179,576 | 12,018 | 656,631 | 942,824 | 1,599,455 | 273,037 | 12,936 | 285,973 | 901,698 | 1,187,671 |
| Capital expenditure | 32,823 | 95,139 | 87,406 | 14,763 | 230,131 | (704) | 229,427 | 31,484 | 16,785 | 48,269 | – | 48,269 |
| 2018 | | | | | | | | | | | | |
| Revenue | | | | | | | | | | | | |
| External customers | 510,434 | 321,232 | 39,203 | 7,139 | 878,008 | – | 878,008 | 386,510 | 48,689 | 435,199 | – | 435,199 |
| Inter-segment | 1,390 | 1,730 | 2,991 | 45,451 | 51,562 | (51,562) | – | 459 | 22,366 | 22,825 | (22,825) | – |
| TOTAL revenue | 511,824 | 322,962 | 42,194 | 52,590 | 929,570 | (51,562) | 878,008 | 386,969 | 71,055 | 458,024 | (22,825) | 435,199 |
| Results | | | | | | | | | | | | |
| EBITDA | 146,552 | 119,791 | 41,456 | 13,783 | 321,582 | – | 321,582 | 134,040 | 26,887 | 160,927 | – | 160,927 |
| Depreciation, amortisation and impairment of intangible assets, PPE and right-of-use assets | (110,490) | (77,432) | (25,856) | (12,042) | (225,820) | – | (225,820) | (107,397) | (19,727) | (127,124) | – | (127,124) |
| Segment profit before tax | 36,062 | 42,359 | 15,600 | 1,741 | 95,762 | (7,249) | 88,513 | 26,643 | 7,160 | 33,803 | 178,957 | 212,760 |
| Segment assets at the end of the year | 1,329,274 | 1,669,710 | 579,327 | 86,350 | 3,664,661 | 134,158 | 3,798,819 | 1,212,681 | 161,577 | 1,374,258 | 1,766,851 | 3,141,109 |
| Segment liabilities at the end of the year | 295,168 | 192,016 | 95,123 | 6,535 | 588,842 | 889,912 | 1,478,754 | 298,328 | 7,882 | 306,210 | 841,076 | 1,147,286 |
| Capital expenditure | 28,909 | 95,117 | 87,136 | 12,411 | 223,573 | (2,966) | 220,607 | 26,921 | 14,429 | 41,350 | – | 41,350 |

* In the financial statements operating segment of lease of transmission system assets is classified as discontinued operation (Note 30)



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 |
| 2019 | | | | | | | | | | |
| Revenue from contracts with customers recognised over time: | | | | | | | | | | |
| Trade of energy and related supply services | 440,435 | 3,063 | – | – | 443,498 | 443,498 | 332,486 | – | 332,486 | 332,486 |
| Distribution system services | 1 | 299,332 | – | – | 299,333 | 299,333 | – | – | – | – |
| Heat sales | 68,148 | 75 | – | 12 | 68,235 | 68,235 | 56,842 | 12 | 56,854 | 56,854 |
| Other revenue | 8,042 | 15,532 | – | 5,731 | 29,305 | 29,305 | 6,399 | 31,826 | 38,225 | 38,225 |
| TOTAL revenue from contracts with customers | 516,626 | 318,002 | – | 5,743 | 840,371 | 840,371 | 395,727 | 31,838 | 427,565 | 427,565 |
| Other revenue: | | | | | | | | | | |
| Lease of transmission system assets | – | – | 36,116 | – | 36,116 | 36,116 | – | – | – | – |
| Lease of other assets | – | 103 | – | 1,162 | 1,265 | 1,265 | – | 9,964 | 9,964 | 9,964 |
| Other revenue | – | – | 527 | – | 527 | 527 | – | – | – | – |
| TOTAL other revenue | – | 103 | 36,643 | 1,162 | 37,908 | 37,908 | – | 9,964 | 9,964 | 9,964 |
| TOTAL revenue, including | 516,626 | 318,105 | 36,643 | 6,905 | 878,279 | 878,279 | 395,727 | 41,802 | 437,529 | 437,529 |
| – Latvia | 339,153 | 318,091 | 36,643 | 6,565 | 700,452 | 700,452 | 322,141 | 40,509 | 362,650 | 362,650 |
| – Outside Latvia | 177,473 | 14 | – | 340 | 177,827 | 177,827 | 73,586 | 1,293 | 74,879 | 74,879 |
| 2018 | | | | | | | | | | |
| Revenue from contracts with customers recognised over time: | | | | | | | | | | |
| 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 |
| TOTAL revenue from contracts with customers | 510 434 | 321 117 | – | 5 686 | 837 237 | 837 237 | 386 510 | 32 702 | 419 212 | 419 212 |
| Other revenue: | | | | | | | | | | |
| Lease of transmission system assets | – | – | 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 | – | – | – | – |
| TOTAL other revenue | – | 115 | 39 203 | 1 453 | 40,771 | 40,771 | – | 15 987 | 15 987 | 15 987 |
| TOTAL revenue | 510 434 | 321 232 | 39 203 | 7 139 | 878 008 | 878 008 | 386 510 | 48 689 | 435 199 | 435 199 |
| – 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 |

* In the financial statements operating segment of lease of transmission system assets is classified as discontinued operation (Note 30)



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.

Reconciliation of profit before tax

EUR'000

| | Notes | Group | | Parent Company | |
|--|-------|----------------|----------------|----------------|----------------|
| | | 2019 | 2018 | 2019 | 2018 |
| EBITDA | | 280,967 | 321,582 | 112,651 | 160,927 |
| Amortisation, depreciation and intangible assets and PPE impairment loss | | (167,917) | (225,820) | (67,543) | (127,124) |
| Segment profit before tax | | 113,050 | 95,762 | 45,108 | 33,803 |
| Finance income | 11 | 1,187 | 1,157 | 12,995 | 11,446 |
| Finance costs | 11 | (9,480) | (8,406) | (11,734) | (10,135) |
| Dividends received from subsidiaries | 16 | – | – | 54,858 | 177,646 |
| Profit before tax | | 104,757 | 88,513 | 101,227 | 212,760 |

Reconciliation of assets

EUR'000

| | Notes | Group | | Parent Company | |
|---------------------------------------|-------|------------------|------------------|------------------|------------------|
| | | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Segment operating assets | | 3,758,476 | 3,664,661 | 1,366,349 | 1,374,258 |
| Connection usage rights | | (39,739) | (39,744) | – | – |
| Non-current financial investments | 16 | 39 | 40 | 831,350 | 830,542 |
| Loans to related parties | 29 e | – | – | 794,256 | 765,815 |
| Other financial investments | 22 | 16,885 | 16,935 | 16,885 | 16,935 |
| Derivative financial instruments | 24 | 6,717 | 15,853 | 6,717 | 15,853 |
| Prepayment for income and other taxes | | 141 | 11,619 | 140 | 10,152 |
| Cash and cash equivalents | 19 | 122,422 | 129,455 | 121,261 | 127,554 |
| TOTAL assets | | 3,864,941 | 3,798,819 | 3,136,958 | 3,141,109 |

Reconciliation of liabilities

EUR'000

| | Notes | Group | | Parent Company | |
|--|-------|------------------|------------------|------------------|------------------|
| | | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Segment operating liabilities | | 656,631 | 588,842 | 285,973 | 306,210 |
| Deferred income tax liabilities | 12 | 8,327 | 12,297 | – | – |
| Current corporate income tax liabilities | | 2 | 2 | – | – |
| Borrowings | 23 | 882,671 | 814,343 | 872,899 | 802,268 |
| Derivative financial instruments | 24 | 13,132 | 10,204 | 13,132 | 10,204 |
| Provisions and other payables | | 38,692 | 53,066 | 15,667 | 28,604 |
| TOTAL liabilities | | 1,599,455 | 1,478,754 | 1,187,671 | 1,147,286 |

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 2019 for the Group amounted to EUR 58,161 thousand and for the Parent Company EUR 58,161 thousand (2018: EUR 66,454 thousand and 66,454 thousand) arising from sales by the generation and trade segment.

6. Revenue

Accounting policy

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. The Group has assessed that connecting a customer to the distribution network as a separate performance obligation is not distinct within the context of the contract due to being highly interrelated to sales of distribution services (Note 4 c III).

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 recognised 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.

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 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 based on 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 based on the meter readings and corresponds to the invoiced amount.

Sales of IT & telecommunication services

Other revenue 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 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.

| EUR'000 | | | | | |
|--|---------------------------|----------------|----------------|----------------|----------------|
| | IFRS or IAS applied | Group | | Parent Company | |
| | | 2019 | 2018 | 2019 | 2018 |
| Revenue from contracts with customers recognised over time: | | | | | |
| Trade of energy and related supply services | 15. SFPS | 443,498 | 425,718 | 332,486 | 312,994 |
| Distribution system services | 15. SFPS | 299,333 | 303,439 | – | – |
| Heat sales | 15. SFPS | 68,235 | 78,580 | 56,854 | 66,263 |
| Other revenue | 15. SFPS | 29,305 | 29,500 | 38,225 | 39,955 |
| TOTAL revenue from contracts with customers | | 840,371 | 837,237 | 427,565 | 419,212 |
| Other revenue: | | | | | |
| | 16. SFPS / | | | | |
| Lease of other assets | 17. SGS | 1,265 | 1,568 | 9,964 | 15,987 |
| TOTAL other revenue | | 1,265 | 1,568 | 9,964 | 15,987 |
| TOTAL revenue | | 841,636 | 838,805 | 437,529 | 435,199 |

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 | |
| | | 2019 | 2018 | 2019 | 2018 |
| Latvia | | 662,544 | 658,071 | 352,686 | 343,329 |
| Outside Latvia | | 177,827 | 179,166 | 74,879 | 75,883 |
| TOTAL revenue from contracts with customers | | 840,371 | 837,237 | 427,565 | 419,212 |



Accounting policy

The Group and the Parent Company have 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).

Mandatory procurement PSO fees

Revenue from mandatory procurement public service obligation 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 an 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”.

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.

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.

Gross amounts invoiced to customers by applying agent accounting principle, recognised on net basis under trade of energy and related supply services:

| | Group | | Parent Company | |
|---|----------------|----------------|----------------|----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Mandatory procurement PSO fees | 88,082 | 98,459 | 90,605 | 101,852 |
| Distribution system services | 11,181 | 10,576 | 198,092 | 208,304 |
| Transmission system services | 1,557 | 1,562 | 1,596 | 1,613 |
| TOTAL revenue recognised applying agent accounting principle | 100,820 | 110,597 | 290,293 | 311,769 |

Net effect in revenue from applying agent accounting principle is 0.

Accounting policy

Revenue from contracts with customers

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 deferred income (contract liabilities) and recognised over the estimated customer relationship period of 20 years (Note 4 c III).

Revenue from other sources

Lease of transmission system assets (IFRS 16) (Group, discontinued operation (Note 30)). 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 IFRS 16 ‘Leases’ criteria that is used for revenue recognition from lease.

Connection fees to transmission system (IFRS 16) (Group, discontinued operation (Note 30)). Revenue from connection fees to transmission system are received as upfront payments from lessee under lease agreement and 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 (Note 4 g).

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.

Until 31 December 2018, the Group applied IAS 17 ‘Leases’ for the recognition of abovementioned revenues. Revenue recognition principles have not changed upon implementation of IFRS 16.

The Group has recognised the following deferred income from contracts with customers:

| | Koncerns | |
|---|----------------|----------------|
| | 31/12/2019 | 31/12/2018 |
| Non–current deferred income from connection fees (Note 28 I, a) | 142,453 | 143,494 |
| Current deferred income from connection fees (Note 28 II, a) | 13,629 | 12,984 |
| Non-current other deferred income (Note 28 I, a) | 877 | – |
| Current other deferred income (Note 28 II, a) | 135 | 287 |
| TOTAL liabilities | 157,094 | 156,765 |

Movement in deferred connection fees from contracts with customers for the Group (non-current and current part):

| | Koncerns | |
|--|----------------|----------------|
| | 2019 | 2018 |
| At the beginning of the year | 156,765 | 154,632 |
| Received connection fees for connection to distribution system (Note 28) | 12,902 | 14,725 |
| Received advance payments for contracts with customers (Note 28) | 940 | – |
| Credited to the Statement of Profit or Loss | (13,513) | (12 592) |
| At the end of the year | 157 094 | 156 765 |



7. Other income

EUR'000

| | Group | | Parent Company | |
|---|---------------|---------------|----------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| Compensation from the state on state support for the installed capacity of CHPPs (Note 4 h) | 23,990 | 81,004 | 23,990 | 81,004 |
| Fines and penalties | (175) | 7,357 | (1,135) | 5,812 |
| Net gain on disposal of assets held for sale and property, plant and equipment | 398 | – | 378 | – |
| Net gain from sale of assets held for sale and PPE | (20) | 1,051 | – | 3,763 |
| Net gain from sale of current assets | – | 12 | – | 2 |
| Compensations and insurance claims | 745 | 551 | 232 | 279 |
| Other operating income | 925 | 1,123 | 93 | 321 |
| TOTAL other income | 25,863 | 91,098 | 23,558 | 91,181 |

8. Raw materials and consumables used

EUR'000

| | Group | | Parent Company | |
|--|----------------|----------------|----------------|----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Electricity | | | | |
| Purchased electricity | 168,699 | 196,660 | 56,701 | 78,747 |
| Loss on fair value changes on electricity forwards and futures (Note 24 l) | 2,326 | 417 | 2,326 | 417 |
| Electricity transmission services costs (Note 29 a) | 71,552 | 71,368 | 1,015 | 1,015 |
| | 242,577 | 268,445 | 60,042 | 80,179 |
| Natural gas and other energy resources costs | 205,905 | 197,485 | 199,027 | 190,139 |
| Gains on fair value changes on natural gas forwards (Note 24 l) | (2,033) | – | (2,033) | – |
| Raw materials, spare parts and maintenance costs | 31,211 | 31,218 | 14,033 | 14,274 |
| TOTAL raw materials and consumables used | 477,660 | 497,148 | 271,069 | 284,592 |

9. Personnel expenses

EUR'000

| | Group | | Parent Company | |
|---|----------------|----------------|----------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| Wages and salaries | 77,075 | 73,220 | 34,081 | 31,164 |
| State social insurance contributions | 18,370 | 17,613 | 8,152 | 7,448 |
| Expenditure of employment termination | (265) | 6,070 | 162 | 1,199 |
| Pension costs – defined contribution plan | 2,066 | 2,249 | 919 | 893 |
| Other benefits defined in the Collective Agreement | 1,108 | 1,191 | 420 | 426 |
| Life insurance costs | 3,161 | 3,180 | 1,326 | 1,289 |
| Capitalised personnel expenses | (166) | (164) | (21) | (23) |
| TOTAL personnel expenses, including remuneration to the management | 101,349 | 103,359 | 45,039 | 42,396 |
| Including remuneration to the management: | | | | |
| Wages and salaries | 2,183 | 1,992 | 763 | 769 |
| State social insurance contributions | 513 | 499 | 183 | 186 |
| Expenditure of employment termination | – | 75 | – | 75 |
| Pension costs – defined contribution plan | 11 | 24 | 6 | 4 |
| Life insurance costs | 21 | 31 | 4 | 7 |
| TOTAL remuneration to the management* | 2,728 | 2,621 | 956 | 1,041 |

* 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).

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.

Number of employees

| | Group | | Parent Company | |
|---|-------|-------|----------------|-------|
| | 2019 | 2018 | 2019 | 2018 |
| Number of employees at the end of the year | 3,423 | 3,508 | 1,328 | 1,355 |
| Average number of employees during the year | 3,476 | 3,617 | 1,342 | 1,387 |

10. Other operating expenses

EUR'000

| | Group | | Parent Company | |
|---|---------------|---------------|----------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| Selling expenses and customer services | 5,360 | 6,154 | 3,937 | 4,788 |
| Information technology maintenance | 5,336 | 5,115 | 4,963 | 4,771 |
| Transportation expenses | 5,592 | 6,411 | 1,833 | 2,164 |
| Environment protection and work safety | 7,658 | 7,836 | 6,799 | 8,125 |
| Real estate maintenance and utilities expenses | 5,129 | 5,582 | 5,401 | 6,372 |
| Lease of real estate and fixed assets | 165 | 1,618 | 450 | 1,149 |
| Telecommunications services | 1,964 | 2,047 | 2,150 | 2,275 |
| Real estate tax | 961 | 1,095 | 1,061 | 1,083 |
| Public utilities regulation fee | 1,860 | 1,906 | 893 | 932 |
| Audit fee* | 93 | 93 | 45 | 45 |
| Changes in impairment losses on financial assets, net | (1,495) | (503) | (1,245) | (236) |
| Net losses from sale of assets held for sale and PPE | 4,515 | – | 319 | – |
| Other expenses | 7,826 | 10,105 | 5,722 | 6,997 |
| TOTAL other operating expenses | 44,964 | 47,449 | 32,328 | 38,465 |

* audit fee consists from audit of the Group's entities financial statements in the amount of EUR 93 thousand; Parent Company - EUR 41 thousand (2018: EUR 93 thousand; Parent Company - EUR 41 thousand)), audit of The Group's Sustainability report and financial covenants - EUR 4 thousand (2018: EUR 4 thousand), while Latvijas elektriskie tīkli AS audit fee in the amount of EUR 7 thousand (2018: EUR 7 thousand) included per expenses of discontinued operation (Note 30). In addition to audit services, in 2019 auditors also provided other services, the costs of which are included in the position 'Other expenses'; for the Group in the amount of EUR 8 thousand, Parent Company – EUR 7 thousand.



11. Finance income and costs

| EUR'000 | | | | |
|---|--------------|--------------|----------------|---------------|
| | Group | | Parent Company | |
| | 2019 | 2018 | 2019 | 2018 |
| Finance income: | | | | |
| Interest income | 1,088 | 1,113 | 1,086 | 1,113 |
| Interest income on loans to subsidiaries | – | – | 11,811 | 10,289 |
| Net gain on issued debt securities (bonds) | 44 | 44 | 44 | 44 |
| Net gain on currency exchange rate fluctuations | 55 | – | 54 | – |
| TOTAL finance income | 1,187 | 1,157 | 12,995 | 11,446 |
| Finance costs: | | | | |
| Interest expense on borrowings | 6,776 | 6,276 | 9,077 | 8,029 |
| Interest expense on issued debt securities (bonds) | 2,880 | 2,880 | 2,880 | 2,880 |
| Interest expense on assets lease | 96 | – | 57 | – |
| Capitalised borrowing costs | (423) | (889) | (423) | (889) |
| Net losses on redemption of other financial investments | 49 | 49 | 49 | 49 |
| Net losses on currency exchange rate fluctuations | – | 2 | – | 2 |
| Other finance costs | 102 | 88 | 94 | 64 |
| TOTAL finance costs | 9,480 | 8,406 | 11,734 | 10,135 |

12. Income tax

Accounting policy

Corporate income tax

Latvia

Corporate income tax is paid on distributed profits which has been generated as of 1 January 2018 and not previously taxed (less dividends received from subsidiaries), and deemed profit distributions. 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, representation costs, non-business related disbursements and transfer

pricing adjustments. The tax rate on the net dividends paid out of retained earnings is 20/80. Since 2019, it is possible to apply a tax rate of 14/86 to dividend payments. This more favorable tax rate can be used for dividend payments up to the average dividend payout of the previous three financial years, taxed 20/80 rate. In calculating the average dividend payment for the three preceding financial years, 2018 was the first year to be considered. 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.

Deferred income tax

Latvia and Estonia

Deferred tax liabilities are recognised in the consolidated financial statements on undistributed profits of the subsidiaries (in Latvia for the profits 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.

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.

| | Group | | Parent Company | |
|---------------------------------|--------------|--------------|----------------|-----------|
| | 2019 | 2018 | 2019 | 2018 |
| Current income tax for the year | 8,565 | 261 | – | 27 |
| Deferred income tax changes | (620) | 8,948 | – | – |
| TOTAL income tax | 7,945 | 9,209 | – | 27 |

13. Intangible assets

a) Intangible assets

Accounting policy

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.

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 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).



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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 |
| As of 31 December 2017 | | | | | | | | | | |
| Cost | 225 | – | 49,635 | 96 | 49,956 | 6,305 | – | 46,969 | 41 | 53,315 |
| Accumulated amortisation | – | – | (36,543) | – | (36,543) | – | – | (35,854) | – | (35,854) |
| Net book amount | 225 | – | 13,092 | 96 | 13,413 | 6,305 | – | 11,115 | 41 | 17,461 |
| 2018 | | | | | | | | | | |
| Additions | – | 17,789 | 2,641 | 88 | 20,518 | – | 17,789 | 2,439 | 124 | 20,352 |
| Transfers | (80) | – | – | – | (80) | (525) | – | (26) | – | (551) |
| Disposals | – | (11,066) | – | – | (11,066) | – | (11,066) | – | – | (11,066) |
| Amortisation charge | – | – | (3,706) | – | (3,706) | – | – | (3,383) | – | (3,383) |
| Closing net book amount | 145 | 6,723 | 12,027 | 184 | 19,079 | 5,780 | 6,723 | 10,145 | 165 | 22,813 |
| As of 31 December 2018 | | | | | | | | | | |
| Cost | 145 | 6,723 | 48,135 | 184 | 55,187 | 5,780 | 6,723 | 45,242 | 165 | 57,910 |
| Accumulated amortisation | – | – | (36,108) | – | (36,108) | – | – | (35,097) | – | (35,097) |
| Net book amount | 145 | 6,723 | 12,027 | 184 | 19,079 | 5,780 | 6,723 | 10,145 | 165 | 22,813 |
| 2019 | | | | | | | | | | |
| Additions | – | 25,607 | – | 2,348 | 27,955 | – | 25,607 | – | 2,233 | 27,840 |
| Transfers | – | – | 2,384 | (2,384) | – | 1 | – | 2,249 | (2,250) | – |
| Disposals | (13) | (21,306) | – | – | (21,316) | (458) | (21,306) | – | – | (21,764) |
| Amortisation charge | – | – | (3,128) | – | (3,128) | – | – | (2,778) | – | (2,778) |
| Closing net book amount | 132 | 11,024 | 11,283 | 148 | 22,587 | 5,323 | 11,024 | 9,616 | 148 | 26,111 |
| As of 31 December 2019 | | | | | | | | | | |
| Cost | 132 | 11,024 | 50,494 | 148 | 61,798 | 5,323 | 11,024 | 47,467 | 148 | 63,962 |
| Accumulated amortisation | – | – | (39,211) | – | (39,211) | – | – | (37,851) | – | (37,851) |
| Net book amount | 132 | 11,024 | 11,283 | 148 | 22,587 | 5,323 | 11,024 | 9,616 | 148 | 26,111 |

b) Greenhouse gas emission allowances:

Accounting policy

Emission rights for greenhouse gases (or allowances) are recognised and subsequently measured 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.

| | Group | | Parent Company | |
|--|----------------------|----------------------|----------------------|----------------------|
| | 2019 | 2018 | 2019 | 2018 |
| | Number of allowances | Number of allowances | Number of allowances | Number of allowances |
| At the beginning of the year | 1,805,556 | 1,062,060 | 1,661,313 | 841,651 |
| Allowances allocated free of charge* | 218,345 | 265,465 | 205,721 | 250,091 |
| Purchased allowances | 1,040,552 | 1,425,000 | 1,035,000 | 1,425,000 |
| Written off verified allowances | (1,229,089) | (874,969) | (1,213,122) | (855,429) |
| Sold allowances | (51,000) | (72,000) | – | – |
| At the end of the year | 1,784,364 | 1,805,556 | 1,688,912 | 1,661,313 |
| including estimated allowances used during the reporting year (unverified) | (1,219,149) | (1,213,122) | (1,219,149) | (1,213,122) |
| Allowances available at the end of the year | 565,215 | 592,434 | 469,763 | 448,191 |

* The number of allowances received by the Group and the Parent Company 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. Therefore, their carrying amount as of 31 December 2019 was nil (31/12/2018: nil). Received European Union Allowances (EUA) must be used until the end of 2020.



14. Property, plant and equipment

a) Property, plant and equipment

Accounting policy

Property, plant and equipment (PPE) are measured on initial recognition at cost. Following initial recognition PPE are stated at historical cost or revalued amount 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 |
|--|------------------------------|
| Buildings and facilities | 15 – 100 |
| Assets of Hydropower plants: | |
| • hydropower plants' buildings and facilities, | 25 – 100 |
| • hydropower plants' technology equipment and machinery | 10 – 40 |
| Transmission system electrical lines and electrical equipment: | |
| • electricity transmission lines | 20 – 50 |
| • electrical equipment of transformer substations | 12 – 40 |
| Distribution system electrical lines and electrical equipment: | |
| • electricity distribution lines | 30 – 50 |
| • electrical equipment of transformer substations | 30 – 35 |
| Technology equipment and machinery | 3 – 40 |
| Other property, plant and equipment | 2 – 25 |

he 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.

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.

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.



Net book amounts and movements of property, plant and equipment by groups, including groups of revalued categories 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 | Property, plant and equipment TOTAL | Land, buildings and facilities | Assets of Hydro Power Plant | Technology equipment and machinery | Other PPE | Assets under construction | Property, plant and equipment TOTAL |
| As of 31 December 2017 | | | | | | | | | | | | | | |
| Cost or valuation | 479,605 | 2,014,626 | 2,857,242 | 926,403 | 640,568 | 161,992 | 228,748 | 7,309,184 | 345,246 | 2,014,626 | 615,648 | 135,708 | 138,718 | 3,249,946 |
| Accumulated depreciation and impairment | (149,415) | (1,292,017) | (1,378,732) | (540,464) | (521,801) | (112,593) | (5,177) | (4,000,199) | (105,407) | (1,292,017) | (512,259) | (103,754) | (5,055) | (2,018,492) |
| Net book amount | 330,190 | 722,609 | 1,478,510 | 385,939 | 118,767 | 49,399 | 223,571 | 3,308,985 | 239,839 | 722,609 | 103,389 | 31,954 | 133,663 | 1,231,454 |
| Year ended 31 December 2018 | | | | | | | | | | | | | | |
| Additions | – | – | – | – | – | – | 217,389 | 217,389 | – | – | – | – | 38,300 | 38,300 |
| Invested in share capital (Note 20) | 469 | – | 20 | – | – | – | – | 489 | 469 | – | 20 | – | – | 489 |
| 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) | – | – | – | – | – | – | (44) | (2,374) | – | – | – | – | (2,374) |
| Disposals | (931) | (36) | (4,904) | (841) | (709) | (90) | (101) | (7,612) | (2,158) | (36) | (1,279) | (10,442) | (95) | (14,010) |
| Impairment charge | 146 | – | – | – | (33,400) | – | (187) | (33,441) | 146 | – | (33,400) | – | – | (33,254) |
| Depreciation | (15,959) | (24,859) | (65,638) | (24,615) | (42,807) | (14,795) | – | (188,673) | (10,231) | (24,859) | (41,336) | (10,293) | – | (86,719) |
| Closing net book amount as of 31 December 2018 | 322,486 | 788,510 | 1,497,669 | 394,170 | 42,994 | 48,882 | 202,382 | 3,297,093 | 233,766 | 788,510 | 28,527 | 17,789 | 65,294 | 1,133,886 |
| As of 31 December 2018 | | | | | | | | | | | | | | |
| Cost or valuation | 485,098 | 2,055,572 | 2,889,265 | 933,079 | 637,706 | 147,744 | 207,746 | 7,356,210 | 349,581 | 2,055,572 | 612,253 | 103,877 | 70,349 | 3,191,632 |
| Accumulated depreciation and impairment | (162,612) | (1,267,062) | (1,391,596) | (538,909) | (594,712) | (98,862) | (5,364) | (4,059,117) | (115,815) | (1,267,062) | (583,726) | (86,088) | (5,055) | (2,057,746) |
| Net book amount | 322,486 | 788,510 | 1,497,669 | 394,170 | 42,994 | 48,882 | 202,382 | 3,297,093 | 233,766 | 788,510 | 28,527 | 17,789 | 65,294 | 1,133,886 |
| 2019 | | | | | | | | | | | | | | |
| Additions | – | – | – | – | – | – | 226,986 | 226,986 | – | – | – | – | 45,941 | 45,941 |
| Invested in share capital (Note 20) | 87 | – | – | – | 5 | – | – | 92 | 87 | – | – | – | – | 92 |
| Transfers | 10,111 | 20,332 | 84,723 | 141,808 | 5,465 | 17,315 | (279,754) | – | 3,048 | 20,332 | 5,373 | 8,638 | (37,391) | – |
| Reclassified to investment property | (135) | – | – | – | – | – | – | (135) | 304 | – | – | – | (2,243) | (1,939) |
| Reclassified to non-current assets for sale | – | – | – | – | – | (146) | – | (146) | – | – | – | – | – | – |
| Disposals | (441) | (1) | (5,154) | (224) | (323) | (42) | (56) | (6,241) | (6,057) | (1) | (307) | (154) | (457) | (6,976) |
| Reversed impairment charge | 288 | – | – | – | 19,475 | – | 7 | 19,770 | 288 | – | 19,475 | – | – | 19,763 |
| Depreciation | (15,154) | (25,864) | (65,465) | (23,439) | (40,630) | (12,747) | – | (183,299) | (10,118) | (25,864) | (39,067) | (6,717) | – | (81,766) |
| Assets attributable to the discontinuing operation (Note 30) | (33,538) | – | – | (512,315) | – | (202) | (55,120) | (601,175) | – | – | – | – | – | – |
| Closing net book amount as of 31 December 2019 | 283,704 | 782,977 | 1,511,773 | – | 26,986 | 53,060 | 94,445 | 2,752,945 | 221,318 | 782,977 | 14,006 | 19,556 | 71,144 | 1,109,001 |
| As of 31 December 2019 | | | | | | | | | | | | | | |
| Cost or valuation | 456,257 | 2,050,409 | 2,921,846 | – | 637,869 | 157,052 | 99,802 | 6,323,235 | 341,761 | 2,050,409 | 612,341 | 105,335 | 76,199 | 3,186,045 |
| Accumulated depreciation and impairment | (172,553) | (1,267,432) | (1,410,073) | – | (610,883) | (103,992) | (5,357) | (3,570,290) | (120,443) | (1,267,432) | (598,335) | (85,779) | (5,055) | (2,077,044) |
| Net book amount | 283,704 | 782,977 | 1,511,773 | – | 26,986 | 53,060 | 94,445 | 2,752,945 | 221,318 | 782,977 | 14,006 | 19,556 | 71,144 | 1,109,001 |

Impairment charge or reversed 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 2019, cost of fully depreciated PPE which are still in use for the Group amounted to EUR 545,956 thousand (31/12/2018: EUR 312,028 thousand) and for the Parent Company amounted to EUR 313,243 thousand (31/12/2018: EUR 241,396 thousand).

In 2019 the Group and the Parent Company have capitalised borrowing costs in the amount of EUR 423 thousand (2018: EUR 889 thousand) (see Note 11). Rate of capitalised borrowing costs was of 1.03% (2018: 0.93%).

Information about the pledged property, plant and equipment is disclosed in Note 23 I.

b) Investment property

Accounting policy

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.

| | Group | | Parent Company | | | | EUR'000 | |
|--|---|---------|----------------------------------|----------|---|---------|---------------------------|----------|
| | Investment property held for capital appreciation | | Investment properties for lease* | | Investment property held for capital appreciation | | TOTAL Investment property | |
| | 2019 | 2018 | 2019 | 2018 | 2019 | 2018 | 2019 | 2018 |
| Cost at the beginning 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 beginning of the year | (1,171) | (1,544) | (33,263) | (32,067) | (1,171) | (1,544) | (34,434) | (33,611) |
| Net book amount at the beginning of the year | 467 | 753 | 61,363 | 64,107 | 433 | 700 | 61,796 | 64,807 |
| Reclassified to investment property held for capital appreciation | 135 | 44 | – | (13) | 135 | 44 | 135 | 31 |
| Reclassified from property, plant and equipment to investment property | – | – | 1,804 | 3,734 | – | – | 1,804 | 3,734 |
| Reclassified to property, plant and equipment | – | – | – | (1,360) | – | – | – | (1,360) |
| Disposal | – | – | (21,412) | (1,259) | – | – | (21,412) | (1,259) |
| Sold | (929) | (341) | (223) | (78) | (929) | (322) | (1,152) | (400) |
| Impairment charge | 636 | 17 | – | – | 636 | 17 | 636 | 17 |
| Depreciation | (8) | (6) | (2,364) | (3,768) | (8) | (6) | (2,372) | (3,774) |
| Cost at the end of the year | 910 | 1,638 | 64,377 | 94,626 | 876 | 1,604 | 65,253 | 96,230 |
| Accumulated depreciation and impairment at the end of the year | (609) | (1,171) | (25,209) | (33,263) | (609) | (1,171) | (25,818) | (34,434) |
| Net book amount at the end of the year | 301 | 467 | 39,168 | 61,363 | 267 | 433 | 39,435 | 61,796 |

* leased property, plant and equipment and real estate related to distribution and transmission system assets

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.

c) Property, plant and equipment revaluation

Accounting policy

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.



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The carrying amounts of revalued categories of property, plant and equipment groups at revalued amounts and their cost basis are as follows:

EUR'000

| | Group | | | |
|--|---|--|--|--------------------------|
| | Revalued property, plant and equipment groups | | | |
| | Assets of Hydropower plants (the Parent Company) | Distribution system electrical lines and electri- cal equipment | Transmission system electrical lines and electri- cal equipment | TOTAL revalued PPE |
| At revalued amounts | | | | |
| As of 31 December 2019 | | | | |
| Revalued | 2,050,409 | 2,921,846 | 1,059,864 | 6,032,119 |
| Accumulated depreciation | (1,267,432) | (1,410,073) | (547,549) | (3,225,054) |
| Revalued net book amount | 782,977 | 1,511,773 | 512,315 | 2,807,065 |
| As of 31 December 2018 | | | | |
| 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) |
| Revalued net book amount | 788,510 | 1,497,669 | 394,170 | 2,680,349 |
| At amounts stated on historical cost basis | | | | |
| As of 31 December 2019 | | | | |
| Cost | 413,734 | 1,377,374 | 586,842 | 2,377,950 |
| Accumulated depreciation | (176,619) | (458,211) | (180,153) | (814,983) |
| Net book amount | 237,115 | 919,163 | 406,689 | 1,562,967 |
| As of 31 December 2018 | | | | |
| Cost | 396,519 | 1,377,374 | 446,760 | 2,220,653 |
| Accumulated depreciation | (171,043) | (458,211) | (168,374) | (797,628) |
| Net book amount | 225,476 | 919,163 | 278,386 | 1,423,025 |

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.

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 50,270 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 53,241 thousand. If electricity price would increase by 1%, the value of assets would increase by EUR 26,840, if the prices would be by 1% less, the value of assets would decrease by EUR 26,840.

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 External valuer at the moment of the revaluation of electrical lines evaluated the replacement or renewing costs by 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. At the moment of the revaluation of electrical equipment, external valuer evaluated how have changed the components of the replacement or renewal costs of the same property, plant and equipment items since the previous revaluation, 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.

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. 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 the previous revaluation, 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.

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.

d) Impairment

Accounting policy

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.



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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 h). 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. Latvenergo AS obtained a government grant in the amount of EUR 454,413 thousand that was divided into two parts - an unconditional grant in amount of EUR 140,000 thousand was recognised in the Group's and Parent Company's statement of profit or loss in 2017, while a conditional grant in amount of EUR 314,413 thousand was 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. In 2019, EUR 23,990 thousand were recognised as 'Other income' in the Group's and Parent Company's statement of profit or loss. Consequently, EUR 209,419 thousand remained recognised as deferred income as of 31 December 2019.

As of 31 December 2019, the future discounted cash flows generated by the operation of Latvenergo AS CHPPs are evaluated in the amount of EUR 6,208 thousand (see below). Consequently, the value of Latvenergo CHPPs assets is estimated as the sum of to the deferred income and the future cash flows as of 31 December 2019 – EUR 215,628 thousand.

As a result of the above transactions, reversal of an impairment in the amount of EUR 19,475 thousand was recognised for Latvenergo AS CHPPs in 2019 (2018: additional impairment EUR 33,400 thousand). The recognised reversal of an impairment is included in the Statement of Profit or Loss position 'Depreciation, amortisation and impairment of intangible assets and property, plant and equipment'.

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 2020 – 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 2020, the service maintenance agreements and assumed inflation. Nominal pre-tax discount rate used to determine value in use of cash-generating

unit by discounting cash flows is 7.5% (2018: 7.5%). As a result of calculation, the future discounted cash flows generated by Latvenergo AS CHPPs are evaluated in the amount of EUR 6,208 thousand. A 1% rise in the discount rate would have an impact of EUR 1.4 million (2018: nil) on the recoverable amount of the assets. 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 revenue from electricity production.

The accumulated impairment as of 31 December 2019 amounted to EUR 234,634 thousand (31/12/2018: EUR 254,109 thousand).

15. Leases

a) Right-of-use assets and lease liabilities

Accounting policy applied from 1 January 2019

From 1 January 2019, the Group and the Parent Company applies IFRS 16 'Leases'. Comparative figures have not been changed. All related information disclosed in Note 2 (see 'Changes in accounting policies').



Accounting policy

At the time of conclusion of the contract, the Group and the Parent Company assesses whether the contract is a lease or contains a lease. A contract is a lease, or contains a lease, when the contract gives the right to control the use of an identified asset throughout the period of time in exchange for consideration.

Lessee

To assess whether the contract is a lease or contains a lease, the Group and the Parent Company assesses whether:

- the contract provides for the use of an identified asset: the asset may be designated, directly or indirectly, and must be physically separable or represent the total capacity of the asset from the physically separable asset. If the supplier has a significant right to replace the asset, the asset is not identifiable;
- the Group and the Parent Company has the right to obtain all economic benefits from the use of the identifiable asset over its useful life;
- the Group and the Parent Company has the right to determine the use of the identifiable asset. The Group and the Parent Company has the right to determine the manner in which the asset will be used, when it can decide how and for what purpose the asset will be used. Where the relevant decisions about how and for what purpose an asset is used are predetermined, the Group and the Parent Company should assess whether it has the right to dispose of the asset or designate the asset in a particular manner, or the Group and the Parent Company has developed an asset in a manner that predetermines how and for what purpose the asset will be used.

At initial measurement or in the case of reassessment of a lease that contains a lease component or several lease components, the Group and the Parent Company attributes each of the lease components to their relative individual price.



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Leases and right-of-use assets are recognised for all long-term leases that meet the criteria of IFRS 16 (the remaining lease term exceeds 12-months at the date of implementation of the standard).

Low value leases are fully accounted without additional exemption.

Leases are recognised as right-of-use assets and the corresponding lease liabilities at the date when leased assets are available for use of the Group and the Parent Company. The cost of the right-of-use an asset consists of:

- the amount of the initial measurement of the lease liability;
- any lease payments made at or before the commencement date less any lease incentives received;
- any initial direct costs.

The right-of-use the asset is recognised as a separate item in the composition of non-current assets and is classified according to groups of property, plant and equipment.

The Group and the Parent Company accounts right-of-use assets of land, buildings and facilities.

The right-of-use asset is amortised on a straight-line basis from the commencement date to the end of the useful life of the underlying asset. Depreciation is calculated on a straight-line basis from the commencement date of the lease to the end of the lease term, unless an asset is scheduled to be redeemed. The right-of-use asset is periodically reduced for impairment losses, if any, and adjusted for any revaluation of the lease liabilities.

Assets and liabilities arising from leases at commencement date are measured at the amount equal to the present value of the remaining lease payments, discounted by the interest rate implicit in the lease, if that rate can be readily determined. If that rate cannot be readily determined, the lessee shall use the incremental interest rate.

Lease liabilities include the present value of the following lease payments:

- fixed lease payments (including in-substance fixed lease payments), less any lease incentives receivable;
- variable leases payments that are based on an index or a rate;
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option;
- payments of penalties for terminating the lease, if the lease term reflects lessee exercising that option.

Lease liabilities are subsequently measured when there is a change in future lease payments due to changes of an index or a rate used to determine these payments, when the Group's and the Parent Company's estimate of expected payments changes, or when the Group and the Parent Company changes its estimate of the purchase option, lease term modification due to extension or termination. When a lease liability is subsequently remeasured, the corresponding adjustment is made to the carrying amount of the right-of-use asset or recognised in the statement of profit or loss if the carrying amount of the right-of-use asset decreases to zero.

Each lease payment is divided between the lease liability and the interest expense on the lease. Interest expense on lease is recognised in the statement of profit or loss over the lease term to form a constant periodic interest rate for the remaining lease liability for each period.

Lease payments related to short-term leases are recognised as an expense in the statement of profit or loss on a straight-line basis. Short-term leases are leases with a lease term of 12 months or less at the commencement date.

Accounting policy applied until 31 December 2018

The Group and the Parent Company has applied IFRS 16 retrospectively but has chosen not to restate comparative positions. As a result, comparative positions are accounted in accordance with the Group's and the Parent Company's previous accounting policy. All related information disclosed in Note 2.



Accounting policy

Operating lease

The Group and 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. Operating lease agreement can't be classified as finance lease as it does not provide that lessee overtakes all risks and benefits associated with the overtaking of lease object in its possession. 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.

The Group and the Parent Company is the lessor

Assets leased out under operating leases are recorded within property, plant and equipment at historic cost or revaluated amounts less depreciation and accumulated impairment loss, if any. 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.

The Group and the Parent Company has concluded several agreements for lease of land and real estate, as well has concluded an agreement until 2028 on a lease of the fiber of the combined optical cable (OPGW - optical ground wire with dual function) (Note 2).

The Group and the Parent Company has recognised right-of-use assets for land, buildings and facilities.

Right-of-use assets

| | EUR'000 | |
|--|---------|----------------|
| | Group | Parent Company |
| Net book amount | | |
| As of 31 December 2018 | – | – |
| Initial recognition value | 8,075 | 3,870 |
| As of 1 January, 2019 | 8,075 | 3,870 |
| Recognised changes in lease agreements | (230) | 3 |
| Excluded right-of-use assets of discontinued operation (Note 30) | (1,099) | – |
| Amortisation | (1,224) | (397) |
| As of 31 December 2019 | 5,522 | 3,476 |

Lease liabilities

| | EUR'000 | |
|--|---------|----------------|
| | Group | Parent Company |
| As of 31 December 2018 | – | – |
| Initial recognition value | 8,075 | 3,870 |
| As of 1 January 2019 | 8,075 | 3,870 |
| Of which are: | | |
| Non-current | 6,839 | 3,500 |
| Current | 1,236 | 370 |
| Recognised changes in lease agreements | (222) | 3 |
| Excluded lease liabilities of discontinued operation (Note 30) | (1,107) | – |
| Decrease of lease liabilities | (1,277) | (428) |
| Recognised interest liabilities | 96 | 57 |
| As of 31 December 2019 | 5,565 | 3,502 |
| Of which are | | |
| Non-current | 4,349 | 3,126 |
| Current | 1,216 | 376 |



Lease payments are allocated between principal and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

b) Expenses from leases

The following amounts are recognised in profit or loss:

| | Group | | Parent Company | |
|--|--------------|--------------|----------------|--------------|
| | 2019 | 2018 | 2019 | 2018 |
| | (IFRS 16) | (IAS 17) | (IFRS 16) | (IAS 17) |
| Depreciation for the right-of-use assets (land buildings and facilities) | 1,224 | – | 397 | – |
| Interest expense on lease liabilities (included in financial costs) | 96 | – | 57 | – |
| Short-term lease expenses | 165 | – | 450 | – |
| Operating lease expense (IAS 17) | – | 1,618 | – | 1,149 |
| TOTAL expenses from leases | 1,485 | 1,618 | 904 | 1,149 |

In the Statement of Cash Flows of the Group and the Parent Company for the year 2019, lease payments in amount of EUR 400 thousand have been made by non-cash offsetting and included in cash flows from operating activities in working capital adjustments. Other lease payments of the Group in amount of EUR 875 thousand (the Parent Company: EUR 18 thousand) are included in the cash flows from financing activities (payments of principal on leases) and in cash flows from operating activities (payments of interest on leases).

c) Income from leases

| | Group | | Parent Company | |
|---|--------------|--------------|----------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| | | | | |
| Income from leases (the Group and the Parent Company is the lessor) (Note 6) | 1,265 | 1,568 | 9,964 | 15,987 |

Future minimum lease payments receivable under operating lease contracts by due dates (the Group and the Parent Company are the lessor):

| | Group | | Parent Company | |
|----------------------------|--------------|--------------|----------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| | | | | |
| – < 1 year | 1,251 | 997 | 9,964 | 7,673 |
| – 1–5 years | 3,693 | 3,718 | 15,110 | 48,424 |
| – > 5 years | 2,002 | 2,691 | 2,002 | 2,793 |
| TOTAL rental income | 6,946 | 7,406 | 27,076 | 58,890 |

16. Non-current financial investments

The Parent Company’s participating interest in subsidiaries and other non-current financial investments:

| Name of the company | Country of incorporation | Business activity held | 31/12/2019 | | 31/12/2018 | |
|--|--------------------------|---|------------------|---------|------------------|---------|
| | | | Interest held, % | EUR'000 | Interest held, % | EUR'000 |
| Investments in subsidiaries: | | | | | | |
| Latvijas elektriskie tīkli AS | Latvia | Lease of transmission system assets | 100 % | 186,432 | 100 % | 185,624 |
| Sadales tīkls AS | Latvia | Electricity distribution | 100 % | 641,150 | 100 % | 641,150 |
| 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, electricity generation | 51 % | 3,556 | 51 % | 3,556 |
| TOTAL | | | | 831,311 | | 830,542 |
| 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, electricity generation | 0.0051 % | 3 | 0.0051 % | 3 |
| TOTAL | | | | 39 | | 39 |

The Group’s non-current financial investments:

| Name of the company | Country of incorporation | Business activity held | 31/12/2019 | | 31/12/2018 | |
|--|--------------------------|---|------------------|---------|------------------|---------|
| | | | 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 % | 36 | 48.15 % | 37 |
| Rīgas siltums AS | Latvia | Thermal energy generation and trade, electricity generation | 0.0051 % | 3 | 0.0051 % | 3 |
| TOTAL | | | | 39 | | 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.

Accounting policy on investments in subsidiaries and non-current investments disclosed per Note 2.

Movement in non-current investments:

| | Group | | Parent Company | |
|------------------------------|-------|------|----------------|---------|
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 40 | 40 | 830,542 | 817,048 |
| Invested in share capital | – | – | 808 | 13,494 |
| Discontinued operation | (1) | – | – | – |
| At the end of the year | 39 | 40 | 831,350 | 83,542 |

In 2019, the Parent Company invested in the share capital of Latvijas elektriskie tīkli AS, by investing the Parent Company's real estate related to transmission system, its lease, supervisory and governance activities and its related liabilities (borrowings):

| | Parent Company | Latvijas elektriskie tīkli AS |
|--|----------------|-------------------------------|
| Invested assets at cost | 26,846 | – |
| Invested assets at valuated (fair) value | – | 35,493 |
| Related liabilities (borrowings) | (26,038) | (26,038) |
| Investment in subsidiary | 808 | – |
| Invested in share capital | – | 9,455 |

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:

| Subsidiaries | Equity | | Net profit for the year | | Dividends from subsidiaries* | | Carrying amount of interest from investment | |
|-----------------------------------|------------|------------|-------------------------|--------|------------------------------|---------|---|------------|
| | 31/12/2019 | 31/12/2018 | 2019 | 2018 | 2019 | 2018 | 31/12/2019 | 31/12/2018 |
| Latvijas elektriskie tīkli AS | 233,757 | 232,759 | 9,486 | 13,394 | 17,945 | 50,463 | 186,432 | 185,624 |
| Sadales tīkls AS | 917,097 | 922,421 | 29,317 | 33,743 | 33,743 | 124,268 | 641,150 | 641,150 |
| Enerģijas publiskais tirgotājs AS | 40 | 40 | – | – | – | – | 40 | 40 |
| Elektrum Eesti OÜ | 960 | 922 | 288 | 250 | 250 | 232 | 35 | 35 |
| Elektrum Lietuva, UAB | 881 | 925 | 504 | 548 | 548 | 481 | 98 | 98 |
| Liepājas enerģija SIA | 17,075 | 17,262 | 4,464 | 5,167 | 2,372 | 2,202 | 3,556 | 3,556 |
| | 1,169,810 | 1,174,329 | 44,059 | 53,102 | 54,858 | 177,646 | 831,311 | 830,503 |

* in 2019 dividends from subsidiaries received in cash in the amount of EUR 21,115 thousand and with non-cash offset in the amount of EUR 33,743 thousand (2018: EUR 53,378 thousand received in cash and with non-cash offset in the amount of EUR 124,268 thousand)

Summarised financial information for non-controlling interests:

| Non-controlling interest of subsidiaries | Non-current assets | | Current assets | | Non-current liabilities | | Current liabilities | |
|--|--------------------|------------|----------------|------------|-------------------------|------------|---------------------|------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Liepājas enerģija SIA (49 %) | 16,706 | 17,645 | 1,302 | 2,027 | 6,320 | 8,602 | 3,320 | 2,611 |

17. Inventories

Accounting policy

Accounting policy

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 held per Inčukalns underground gas storage 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.

| | Group | | Parent Company | |
|---|------------|------------|----------------|------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2019 |
| Raw materials and materials | 15,114 | 13,257 | 762 | 873 |
| Natural gas | 80,907 | 49,757 | 80,907 | 49,757 |
| Goods for sale | 1,874 | 1,608 | 421 | 413 |
| Other inventories | 8,156 | 8,292 | 8,065 | 8,070 |
| Prepayments for inventories | 163 | 198 | 41 | 33 |
| Allowance for raw materials and other inventories | (1,287) | (1,137) | (674) | (736) |
| TOTAL inventories | 104,927 | 71,975 | 89,522 | 58,410 |

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 | |
|--|--------------|--------------|----------------|------------|
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 1,137 | 1,494 | 736 | 992 |
| Inventories written off | – | (287) | – | (260) |
| Charged to the Statement of Profit or Loss | 150 | (70) | (62) | 4 |
| At the end of the year | 1,287 | 1,137 | 674 | 736 |

18. Receivables from contracts with customers and other receivables

Accounting policy

Receivables from contracts with customers and other receivables are classified in groups:

- a) Energy and related services sales, including distribution system services,
- b) Heating sales,
- c) Other sales (IT & telecommunication services, connection service fees and other services),
- d) Receivables from subsidiaries,
- e) 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 and subsequently are measured at amortised cost.

The Group and the Parent 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 Parent Company have applied two expected credit loss models: portfolio model and counterparty model.

The expected loss rates used for portfolio model are based on the payment profiles of sales over a period of 3 years and the corresponding historical credit losses experienced within this period and are adjusted to reflect current and forward-looking information. The Group and the Parent Company apply the IFRS 9 simplified approach to measuring expected credit losses of the collectively assessed receivables (portfolio model) using lifetime expected loss allowance.

For individually significant other receivables and other receivables of energy industry companies and related parties' receivables the Group and the Parent Company apply the IFRS 9 general approach to measuring expected credit losses (counterparty model) using expected credit loss allowance on assessment of significant increase of credit risk. 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 Latvenergo group's and the relevant industry's entities (Note 4 b).

Receivables from contracts with customers grouped by the expected credit loss (ECL) assessment model, net:

EUR'000

| | Group | | Parent Company | |
|---|----------------|----------------|----------------|---------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Individually assessed receivables with lifetime ECL assessment (counterparty model) | 5,105 | 7,051 | 9,068 | 7,915 |
| Receivables with lifetime ECL assessment by simplified approach (portfolio model) | 106,425 | 110,904 | 73,905 | 73,110 |
| TOTAL receivables from contracts with customers | 111,530 | 117,955 | 82,973 | 81,025 |

a) Receivables from contracts with customers, net

EUR'000

| | Group | | Parent Company | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Receivables from contracts with customers: | | | | |
| – Electricity, natural gas trade and related services customers (portfolio model) | 138,926 | 138,308 | 107,721 | 102,154 |
| – Heating customers (portfolio model) | 9,210 | 14,715 | 7,127 | 11,955 |
| – Other receivables from contracts with customers (portfolio model) | 5,019 | 5,675 | 2,571 | 3,331 |
| – Other receivables from contracts with customers (counterparty model) | 5,112 | 7,060 | 2,452 | 3,203 |
| – Subsidiaries (counterparty model) | – | – | 6,623 | 4,719 |
| | 158,267 | 165,758 | 126,494 | 125,362 |
| Provisions for impaired receivables from contracts with customers: | | | | |
| – Electricity, natural gas trade and related services customers (portfolio model) | (44,108) | (44,953) | (43,187) | (43,968) |
| – Heating customers (portfolio model) | (325) | (342) | (315) | (334) |
| – Other receivables from contracts with customers (portfolio model) | (2,297) | (2,499) | (12) | (28) |
| – Other receivables from contracts with customers (counterparty model) | (7) | (9) | (3) | (4) |
| – Subsidiaries (counterparty model) | – | – | (4) | (3) |
| | (46,737) | (47,803) | (43,521) | (44,337) |
| Receivables from contracts with customers, net: | | | | |
| – Electricity, natural gas trade and related services customers (portfolio model) | 94,818 | 93,355 | 64,534 | 58,186 |
| – Heating customers (portfolio model) | 8,885 | 14,373 | 6,812 | 11,621 |
| – Other receivables from contracts with customers (portfolio model) | 2,722 | 3,176 | 2,559 | 3,303 |
| – Other receivables from contracts with customers (counterparty model) | 5,105 | 7,051 | 2,449 | 3,199 |
| – Subsidiaries (counterparty model) | – | – | 6,619 | 4,716 |
| | 111,530 | 117,955 | 82,973 | 81,025 |

**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 | | | | | |
|--------------------------------------|----------|----------------|-----------------|----------------|----------------|-----------------|----------------|----------------|-----------------|---------------|----------------|-----------------|---------------|
| | | 31/12/2019 | | | 31/12/2018 | | | 31/12/2019 | | | 31/12/2018 | | |
| | | Receivables | Impairment loss | Net | Receivables | Impairment loss | TOTAL | Receivables | Impairment loss | Net | Receivables | Impairment loss | TOTAL |
| On time | 0.20 % | 100,773 | (221) | 100,552 | 106,194 | (230) | 105,964 | 69,391 | (154) | 69,237 | 69,557 | (160) | 69,397 |
| Less 30 days | 3 % | 4,139 | (124) | 4,015 | 2,953 | (88) | 2,865 | 3,193 | (96) | 3,097 | 1,947 | (59) | 1,888 |
| Past due 30 - 59 days | 20 % | 1,194 | (239) | 955 | 1,334 | (265) | 1,069 | 1,083 | (217) | 866 | 1,213 | (241) | 972 |
| Past due 60 - 89 days | 50 % | 470 | (235) | 235 | 535 | (267) | 268 | 432 | (216) | 216 | 503 | (251) | 252 |
| Past due 90 - 179 days | 60 % | 785 | (471) | 314 | 812 | (486) | 326 | 562 | (337) | 225 | 697 | (417) | 280 |
| Past due 180 - 359 days | 75 % | 1,414 | (1,060) | 354 | 1,638 | (1,226) | 412 | 1,055 | (791) | 264 | 1,283 | (962) | 321 |
| Past due more than 360 days | 100 % | 17,971 | (17,971) | – | 17,890 | (17,890) | – | 15,405 | (15,405) | – | 15,123 | (15,123) | – |
| Insolvent debtors* | 100 % | 26,409 | (26,409) | – | 27,342 | (27,342) | – | 26,298 | (26,298) | – | 27,117 | (27,117) | – |
| TOTAL | | 153,155 | (46,730) | 106,425 | 158,698 | (47,794) | 110,904 | 117,419 | (43,514) | 73,905 | 117,440 | (44,330) | 73,110 |

* receivables under insolvency process and with an established payment schedule

The expected loss rates used for portfolio model are based on the payment profiles of sales over a period of 3 years and the corresponding historical credit losses experienced within this period. Adjusting by forward-looking information disclosed in Note 4 b.

Receivables from contracts with customers with lifetime expected credit losses (ECL) assessed on the counterparty model basis:

EUR'000

| | Group | | Parent Company | |
|--|--------------|--------------|----------------|--------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Other receivables from contracts with customers | 5,112 | 7,060 | 2,452 | 3,203 |
| Impairment loss on other receivables from contracts with customers | (7) | (9) | (3) | (4) |
| Receivables from subsidiaries (Note 29 b) | – | – | 5,022 | 4,398 |
| Accrued income from subsidiaries (Note 29 c) | – | – | 1,601 | 321 |
| Impairment loss on subsidiaries receivables (Note 29 b) | – | – | (4) | (3) |
| TOTAL | 5,105 | 7,051 | 9,068 | 7,915 |

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.

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 2019 amounted to EUR 6,818 thousand (31/12/2018: EUR 11,626 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.

Movements in loss allowances for impaired receivables from contracts with customers:

EUR'000

| | Group | | Parent Company | |
|--|---------------|---------------|----------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 47,803 | 48,862 | 44,337 | 44,868 |
| Effect of IFRS 9 'Financial instruments' adoption | – | 122 | – | 115 |
| Receivables written off during the year as uncollectible | (1,935) | (2,549) | (1,422) | (2,074) |
| Allowance for impaired receivables | 869 | 1,368 | 606 | 1,428 |
| At the end of the year | 46,737 | 47,803 | 43,521 | 44,337 |



b) Other financial receivables (assessed on the counterparty model basis)

EUR'000

| | Level of SICR | Group | | Parent Company | |
|--|---------------|---------------|----------------|----------------|---------------|
| | | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Non-current financial receivables | Stage 1 | – | 30,617 | – | – |
| Loss allowances for expected credit loss | Stage 1 | – | (40) | – | – |
| TOTAL non-current financial receivables | | – | 30,577 | – | – |
| Current financial receivables: | | | | | |
| Unsettled revenue on mandatory procurement PSO fee recognised as assets* | Stage 1 | 74,938 | 74,497 | – | – |
| Receivables for lease | Stage 1 | 76 | 7,646 | 71 | 49 |
| Receivables for lease from subsidiaries (Note 29 b) | Stage 1 | – | – | 615 | 1,061 |
| Other financial receivables from subsidiaries (Note 29 b) | Stage 1 | – | – | 9,640 | 6,745 |
| Other accrued income from subsidiaries (Note 29 c) | Stage 1 | – | – | 1,864 | 4 358 |
| Other accrued income | Stage 1 | 872 | 872 | 872 | 883 |
| Other current financial receivables | Stage 1 | 1,236 | 1,782 | 300 | 1,279 |
| | Stage 3 | 1,877 | 2,364 | 1,234 | 1,651 |
| Loss allowances for expected credit loss on subsidiaries receivables (Note 29 b) | Stage 1 | – | – | (7) | (6) |
| Loss allowances for expected credit loss | Stage 1 | (231) | (184) | (134) | (136) |
| | Stage 3 | (1,877) | (2,364) | (1,234) | (1,651) |
| TOTAL current financial receivables | | 76,891 | 84,613 | 13,221 | 14,233 |
| TOTAL other financial receivables | | 76,891 | 115,190 | 13,221 | 14,233 |

* by applying agent principle unsettled revenue on mandatory procurement PSO fee is recognised as assets in net amount, as difference between revenue and costs recognised under the mandatory procurement

The Group and the Parent Company have 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 2019 including receivables from contracts with customer amounted to 39,870 thousand EUR (31/12/2018: 42,218 thousand EUR) (see Note 29 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 other financial receivables assessed individually and based on counterparty's model (Note 4).

c) Other non-financial receivables

EUR'000

| | Group | | Parent Company | |
|--|------------|------------|----------------|------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Non-current non-financial receivables | 433 | 343 | 421 | 331 |
| Total non-current non-financial receivables | 433 | 343 | 421 | 331 |
| Current non-financial receivables: | | | | |
| Pre-tax and overpaid taxes | 69 | 108 | 58 | 105 |
| Other current receivables | 125 | 109 | 49 | 107 |
| Total current non-financial receivables | 194 | 217 | 107 | 212 |
| TOTAL non-financial receivables | 627 | 560 | 528 | 543 |

None of the receivables are secured with pledges or otherwise. The carrying amounts of other receivables are assumed to approximate their fair values.

19. Cash and cash equivalents

Accounting policy

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.

EUR'000

| | Group | | Parent Company | |
|--|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Cash at bank | 85,664 | 95,094 | 84,504 | 93,193 |
| Short-term bank deposits | 30,000 | 30,000 | 30,000 | 30,000 |
| Restricted cash and cash equivalents* | 6,758 | 4,361 | 6,757 | 4,361 |
| Cash and cash equivalents | 122,422 | 129,455 | 121,261 | 127,554 |
| Cash attributable to discontinued operation (Note 30) | 300 | – | – | – |
| TOTAL cash and cash equivalents with discontinued operation | 122,722 | 129,455 | 121,261 | 127,554 |

* Restricted cash and cash equivalents as of 31 December 2019 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 2019 the average annual effective interest rate earned on short-term cash deposits was 0.15% (2018: 0.102%).

The carrying amounts of cash and cash equivalents are assumed to be approximate to their fair values.

20. Share capital

As of 31 December 2019, the registered share capital of the Latvenergo AS is EUR 834,883 thousand (31/12/2018: EUR 834,791 thousand) and consists of 834,883 thousand ordinary shares (31/12/2018: 834,791 thousand) with the nominal value of EUR 1 per share (31/12/2018: EUR 1 per share). All shares have been fully paid. In June 2019, in accordance with the Directive No. 177 of the Cabinet of Ministers of the Republic of Latvia, dated 16 April 2019 – “On the Investment of the State's property units in the Share Capital of Latvenergo AS”, real estate in the amount of EUR 92 thousand was invested in the share capital of Latvenergo AS (Note 14 a).

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 h. 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).

21. Reserves, dividends and earnings per share

a) Reserves

EUR'000

| | | Group | | | | | | | Parent Company | | | |
|--|-------|--|---------------|--|----------------|--|------------------------------------|-----------|--|---------------|--|----------|
| | Notes | Non-current assets revaluation reserve | Hedge reserve | Post-employment benefit plan revaluation reserve | Other reserves | Reserves classified as held for distribution | Reserves of discontinued operation | TOTAL | Non-current assets revaluation reserve | Hedge reserve | Post-employment benefit plan revaluation reserve | TOTAL |
| As of 31 December 2017 | | 1,130,398 | (3,987) | (793) | 110 | 1,125,728 | – | 1,125,728 | 795,893 | (3,987) | (225) | 791,681 |
| Disposal of non-current assets revaluation reserve | | 14 a | (10,229) | – | – | (10,229) | – | (10,229) | (6,549) | – | – | (6,549) |
| Gains / (losses) on re-measurement of defined post-employment benefit plan | | 27 a | – | – | 436 | – | 436 | 436 | – | – | (108) | (108) |
| Gains from fair value changes of derivative financial instruments | | 24 | – | 9,531 | – | – | 9,531 | 9,531 | – | 9,531 | – | 9,531 |
| As of 31 December 2018 | | 1,120,169 | 5,544 | (357) | 110 | 1,125,466 | – | 1,125,466 | 789,344 | 5,544 | (333) | 794,555 |
| Non-current assets revaluation reserve related to discontinued operation | | 30 | (29,171) | – | – | (29,171) | 29,171 | – | – | – | – | – |
| Post-employment benefit plan revaluation reserve related to discontinued operation | | 30 | – | – | (18) | – | (18) | 18 | – | – | – | – |
| Disposal of non-current assets revaluation reserve | | 30 | (7,226) | – | – | (7,226) | (255) | (7,481) | (3,474) | – | – | (3,474) |
| (Losses) / gains on re-measurement of defined post-employment benefit plan | | 27 a, 30 | – | – | (2,045) | – | (2,045) | (2,043) | – | – | (1,148) | (1,148) |
| Losses from fair value changes of derivative financial instruments | | 24 | – | (11,771) | – | (11,771) | – | (11,771) | – | (11,771) | – | (11,771) |
| As of 31 December 2019 | | 1,083,772 | (6,227) | (2,420) | 110 | 1,075,235 | 28,936 | 1,104,171 | 785,870 | (6,227) | (1,481) | 778,162 |

Non-current assets revaluation reserve, 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

Accounting policy

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.

The dividends declared to equity holders of the Parent Company for 2018 were EUR 132,936 thousand or EUR 0.15923 per share (2017: EUR 156,418 thousand or EUR 0.17183 per share).

According to the state regulations, the expected amount of dividends to be paid by Latvenergo AS for the use of state capital in 2020 (for the reporting year 2019) amounted to EUR 127,1 million (incl. income tax). The distribution of net profit and amount of dividends payable is subject to a resolution of the Latvenergo AS Shareholders Meeting.

c) Earnings per share

Accounting policy

The Group's share capital consists of the Parent Company's ordinary shares. All shares have been fully paid.

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 20). As there are no potential ordinary shares, diluted earnings per share are equal to basic earnings per share in all comparable periods.

EUR'000

| | Group | | Parent Company | |
|--|---------|---------|----------------|---------|
| | 2019 | 2018 | 2019 | 2018 |
| Profit attributable to the equity holder of the Parent Company (in thousand EUR) | 92,660 | 73,423 | 101,227 | 212,733 |
| Weighted average number of shares (thousand) | 834,845 | 910,323 | 834,845 | 910,323 |
| Basic earnings per share (in euros) | 0.111 | 0.081 | 0.121 | 0.234 |
| Diluted earnings per share (in euros) | 0.111 | 0.081 | 0.121 | 0.234 |



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22. Other financial investments

Carrying (amortised cost) amount of other financial investments:

EUR'000

| | Group | | Parent Company | |
|--|---------------|---------------|----------------|---------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Financial investments in Latvian State Treasury bonds: | | | | |
| – non-current | 16,885 | 16,935 | 16,885 | 16,935 |
| TOTAL other financial investments | 16,885 | 16,935 | 16,885 | 16,935 |

As of 31 December 2019 the entire Group's and the Parent Company's other financial investments 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. In 2019 in connection with the amortisation of other financial investments net losses in the amount of EUR 49 thousand (2018: EUR 49 thousand) (Note 11) are recognised from changes in the value of the purchased bonds. All 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 2019 the fair value of other financial investments is higher than the carrying amount by EUR 2,031 thousand (2018: EUR 3,132 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).

23. Borrowings

EUR'000

| | Group | | Parent Company | |
|---|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Non-current borrowings from financial institutions | 601,826 | 564,711 | 596,560 | 555,251 |
| Issued debt securities (bonds) | 100,303 | 135,317 | 100,303 | 135,317 |
| TOTAL non-current borrowings | 702,129 | 700,028 | 696,863 | 690,568 |
| Current portion of non-current borrowings from financial institutions | 142,885 | 112,102 | 138,691 | 109,512 |
| Issued debt securities (bonds) | 34,969 | – | 34,969 | – |
| Current borrowings | 291 | – | – | – |
| Accrued interest on non-current borrowings | 713 | 529 | 692 | 504 |
| Accrued coupon interest on issued debt securities (bonds) | 1,684 | 1,684 | 1,684 | 1,684 |
| TOTAL current borrowings | 180,542 | 114,315 | 176,036 | 111,700 |
| TOTAL borrowings | 882,671 | 814,343 | 872,899 | 802,268 |

Movement in borrowings:

EUR'000

| | Group | | Parent Company | |
|--|----------------|----------------|----------------|----------------|
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 814,343 | 826,757 | 802,268 | 814,772 |
| Borrowings received | 180,291 | 93,500 | 180,000 | 90,000 |
| Borrowing repaid | (112,102) | (105,931) | (109,513) | (102,522) |
| Change in accrued interest on borrowings | 183 | 61 | 188 | 62 |
| Changes in outstanding value of issued debt securities (bonds) | (44) | (44) | (44) | (44) |
| At the end of the year | 882,671 | 814,343 | 872,899 | 802,268 |

Borrowings by categories of lenders:

EUR'000

| | Group | | Parent Company | |
|--------------------------------|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Foreign investment banks | 351,458 | 374,864 | 351,458 | 374,864 |
| Commercial banks | 394,257 | 302,478 | 384,485 | 290,403 |
| Issued debt securities (bonds) | 136,956 | 137,001 | 136,956 | 137,001 |
| TOTAL borrowings | 882,671 | 814,343 | 872,899 | 802,268 |

Borrowings by contractual maturity, excluding the impact of derivative instruments to the interest rate:

EUR'000

| | Group | | Parent Company | |
|--|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Fixed rate non-current and current borrowings: | | | | |
| – < 1 year (current portion of non-current borrowings) | 86,700 | 19,910 | 86,700 | 19,910 |
| – 1–5 years | 100,303 | 185,317 | 100,303 | 185,317 |
| TOTAL fixed rate borrowings | 187,003 | 205,227 | 187,003 | 205,227 |
| Floating rate non-current and current borrowings: | | | | |
| – < 1 year (current borrowings) | 292 | – | 1 | – |
| – < 1 year (current portion of non-current borrowings) | 93,675 | 94,405 | 89,459 | 91,790 |
| – 1–5 years | 363,360 | 313,404 | 358,595 | 305,158 |
| – > 5 years | 238,341 | 201,307 | 237,841 | 200,093 |
| TOTAL floating rate borrowings | 695,668 | 609,116 | 685,896 | 597,041 |
| TOTAL borrowings | 882,671 | 814,343 | 872,899 | 802,268 |

Borrowings by repricing of interest, including the impact of derivative instruments:

EUR'000

| | Group | | Parent Company | |
|-------------------------|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| – < 1 year | 522,950 | 385,765 | 513,178 | 373,690 |
| – 1–5 years | 259,721 | 353,578 | 259,721 | 353,578 |
| – > 5 years | 100,000 | 75,000 | 100,000 | 75,000 |
| TOTAL borrowings | 882,671 | 814,343 | 872,899 | 802,268 |

As of 31 December 2019 and as of 31 December 2018 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.

Lease liabilities of the Group and the Parent Company disclosed in Note 15.



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I) Pledges

As of 31 December 2019 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 25 million (31/12/2018: EUR 28 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 23 million and the claims on the receivables accounts in the amount of EUR 2 million (31/12/2018: EUR 25 million and EUR 3 million, respectively).

II) Un-drawn borrowing facilities

As of 31 December 2019, the un-drawn committed non-current credit facilities amount to EUR 85 million (31/12/2018: EUR 130 million). After the end of the reporting period, in January 2020, another contract with a maturity of up to two years was signed for EUR 60 million.

As of 31 December 2019, the Group had entered into two overdraft agreements with total notional amount of EUR 19 million (31/12/2018: four overdraft agreements of EUR 38.2 million) of which one overdraft agreements were entered by the Parent Company with total notional amount of EUR 15 million (31/12/2018: three overdraft agreements of EUR 34 million). In respect of all the overdraft agreements all conditions precedent have been met. At the end of the reporting year, EUR 291 thousand of credit lines were 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 1.48% (2018: 1.37%), weighted average effective interest rate for current borrowings was 0.87% (2018: 0.87%). At 31 December 2019 interest rates for non-current borrowings in euros were 6 and 12 month EURIBOR+ 0.99% (31/12/2018: +0.99%) for the Group and 6 and 12 month EURIBOR+ 0.98% (31/12/2018: +0.98%) for Latvenergo AS. As of 31 December 2019, the total notional amount of interest rate swap agreements concluded by the Group amounts to EUR 229.4 million (31/12/2018: EUR 225.1 million) and the interest rate was fixed for the initial periods from 7 to 10 years.

IV) Issued and outstanding debt securities (bonds)

In 2013 the Parent Company (Latvenergo AS) 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 December 2019 and 31 December 2018 were 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 2019, the fair value of issued debt securities (bonds) exceeds their carrying amount by EUR 3,515 thousand (31/12/2018: EUR 4,532 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).

24. Derivative financial instruments

Accounting policy

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.

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. 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.

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.

I) Outstanding fair values of derivatives and their classification

In the table below outstanding fair values of derivatives are disclosed as follows:

| | Notes | Group | | | | Parent Company | | | |
|---|--------|--------------|-----------------|---------------|-----------------|----------------|-----------------|---------------|-----------------|
| | | 31/12/2019 | | 31/12/2018 | | 31/12/2019 | | 31/12/2018 | |
| | | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities |
| Interest rate swaps | 24 II | – | (9,216) | – | (7,375) | – | (9,216) | – | (7,375) |
| Electricity forwards and futures | 24 III | – | (3,916) | 15,853 | – | – | (3,916) | 15,853 | – |
| Natural gas forwards | 24 IV | 6,717 | – | – | (2,829) | 6,717 | – | – | (2,829) |
| TOTAL outstanding fair values of derivatives | | 6,717 | (13,132) | 15,853 | (10,204) | 6,717 | (13,132) | 15,853 | (10,204) |

EUR'000

| | | Group | | | | Parent Company | | | |
|--|--|--------------|-----------------|---------------|-----------------|----------------|-----------------|---------------|-----------------|
| | | 31/12/2019 | | 31/12/2018 | | 31/12/2019 | | 31/12/2018 | |
| | | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities |
| Non-current | | – | (6,149) | – | (3,923) | – | (6,149) | – | (3,923) |
| Current | | 6,717 | (6,983) | 15,853 | (6,281) | 6,717 | (6,983) | 15,853 | (6,281) |
| TOTAL fair values of derivative financial instruments | | 6,717 | (13,132) | 15,853 | (10,204) | 6,717 | (13,132) | 15,853 | (10,204) |

EUR'000

Gains / (losses) on fair value changes as a result of realised hedge agreements:

EUR'000

| | | Group | | Parent Company | |
|--|--------|-----------------|--------------|-----------------|--------------|
| | Notes | 2019 | 2018 | 2019 | 2018 |
| Included in the Statement of Profit or Loss | | | | | |
| Electricity forwards and futures | 8 | (2,326) | (417) | (2,326) | (417) |
| Natural gas forwards | | 2,033 | – | 2,033 | – |
| | | (293) | (417) | (293) | (417) |
| Included in the Statement of Comprehensive Income (Note 21 a) | | | | | |
| Interest rate swaps | 24 II | (1,841) | 655 | (1,841) | 655 |
| Electricity forwards and futures | 24 III | (17,443) | 11,705 | (17,443) | 11,705 |
| Natural gas forwards | 24 IV | 7,513 | (2,829) | 7,513 | (2,829) |
| TOTAL (loss) / gains on fair value changes | | (11,771) | 9,531 | (11,771) | 9,531 |

II) Interest rate swaps

As of 31 December 2019, the Group and the Parent Company had interest rate swap agreements with total notional amount of EUR 229.4 million (31/12/2018: EUR 225.1 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 2019, fixed interest rates vary from 0.087% to 2.5775% (31/12/2018: from 0.315% to 2.5775%).

As at the end of the year all the outstanding interest rate swap agreements with total notional amount of EUR 229.4 million were eligible for 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 | | | |
|--|--------|----------------|-----------|----------------|----------------|----------------|-----------|----------------|
| | 2019 | | 2018 | | 2019 | | 2018 | |
| | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities |
| Outstanding fair value at the beginning of the year | – | (7,375) | 31 | (8,061) | – | (7,375) | 31 | (8,061) |
| Included in Statement of Comprehensive Income (Note 21 a) | – | (1,841) | (31) | 686 | – | (1,841) | (31) | 686 |
| Outstanding fair value at the end of the year | – | (9,216) | – | (7,375) | – | (9,216) | – | (7,375) |

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 2019 45% (31/12/2018: 53%) of the Group's and 45% (2018: 54%) 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 1.8 years (2018: 2.1 years) for the Group and 1.8 years (2018: 2.1 years) for the Parent Company. All necessary actions will be taken during the year 2020 to ensure the average fixed interest rate period within the limits stipulated by the Group's Financial Risk Management Policy.

III) Electricity forwards and futures

As of 31 December 2019, the Group and the Parent Company have entered into electricity forward and future contracts with total outstanding electricity purchase volume of 1,676,105 MWh (31/12/2018: 1,689,784 MWh) and notional value of EUR 41 million (31/12/2018: EUR 40 million). Electricity forward and future contracts are concluded for the maturities from one quarter to one year during the period from 1 January 2020 to 31 December 2022.

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 1,247,040 MWh as of 31 December 2019 are designated to comply with hedge accounting treatment (31/12/2018: 1,689,784) 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 21 a).

Fair value changes of electricity forward and future contracts

EUR'000

| | Group | | | | Parent Company | | | |
|--|---------------|----------------|---------------|-------------|----------------|----------------|---------------|-------------|
| | 2019 | | 2018 | | 2019 | | 2018 | |
| | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities |
| Outstanding fair value at the beginning of the year | 15,853 | – | 4,588 | (23) | 15,853 | – | 4,588 | (23) |
| Included in the Statement of Profit or Loss (Note 8) | (105) | (2,221) | (440) | 23 | (105) | (2,221) | (440) | 23 |
| Included in Statement of Comprehensive Income (Note 21 a) | (15,748) | (1,695) | 11,705 | – | (15,748) | (1,695) | 11,705 | – |
| Outstanding fair value at the end of the year | – | (3,916) | 15,853 | – | – | (3,916) | 15,853 | – |

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 3,690,000 MWh (31/12/2018: 990,000 MWh) and notional value of EUR 71 million (31/12/2018: EUR 23 million). Natural gas swap contracts are concluded for the maturities from one month to one quarter during the period of July 1, 2020 to March 31, 2021. 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 1,650,000 MWh as of 31 December 2019 are designated to comply with hedge accounting treatment (31/12/2018: of 990,000 MWh) 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 | | | |
|--|--------------|----------------|----------|----------------|----------------|----------------|----------|----------------|
| | 2019 | | 2018 | | 2019 | | 2018 | |
| | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities | Assets | Liabilities |
| Outstanding fair value at the beginning of the year | – | (2,829) | – | – | – | (2,829) | – | – |
| Included in the Statement of Profit or Loss (Note 8) | 2,033 | – | – | – | 2,033 | – | – | – |
| Included in Statement of Comprehensive Income (Note 21 a) | 4,684 | 2,829 | – | (2,829) | 4,684 | 2,829 | – | (2,829) |
| Outstanding fair value at the end of the year | 6,717 | – | – | (2,829) | 6,717 | – | – | (2,829) |

25. Fair values and fair value measurement

Accounting policy

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.

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 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 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 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; In case of electricity forward and future contracts and natural gas swap contracts are concluded with counterparties, fair values as calculated by the Group and the Parent Company are disclosed in Financial Statements;



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 2019, the nominal pre-tax discount rate used to determine the fair value of investments is 4.61% (2018: 4.2%) as included in the electricity distribution and transmission system service tariff calculation methodology.

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 assets | Group | | | | Parent Company | | | |
|---|--|---|---|------------------|--|---|---|----------------|
| | Fair value measurement using | | | | Fair value measurement using | | | |
| | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) | TOTAL | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) | TOTAL |
| As of 31 December 2019 | | | | | | | | |
| Assets measured at fair value | | | | | | | | |
| Revalued property, plant and equipment (Note 14 c) | – | – | 2,807,065 | 2,807,065 | – | – | 782,977 | 782,977 |
| Non-current financial investments (Note 16) | – | – | 39 | 39 | – | – | 39 | 39 |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| – Natural gas forwards and futures (Note 24) | – | 6,717 | – | 6,717 | – | 6,717 | – | 6,717 |
| Assets for which fair values are disclosed | | | | | | | | |
| Investment properties (Note 14 b) | – | – | 301 | 301 | – | – | 39,435 | 39,435 |
| Other financial investments (Note 22) | – | 16,885 | – | 16,885 | – | 16,885 | – | 16,885 |
| Floating rate loans to subsidiaries (Note 29 e) | – | – | – | – | – | 151,289 | – | 151,289 |
| Fixed rate loans to subsidiaries (Note 29 e) | – | – | – | – | – | 642,967 | – | 642,967 |
| Non-current financial receivables (Note 18 b) | – | – | 433 | 433 | – | – | 421 | 421 |
| Current financial receivables (Note 18 a, b) | – | – | 188,421 | 188,421 | – | – | 96,194 | 96,194 |
| Cash and cash equivalents (Note 19) | – | 122,422 | – | 122,422 | – | 121,261 | – | 121,261 |
| As of 31 December 2018 | | | | | | | | |
| Assets measured at fair value | | | | | | | | |
| Revalued property, plant and equipment (Note 14 c) | – | – | 2,680,349 | 2,680,349 | – | – | 788,510 | 788,510 |
| Non-current financial investments (Note 16) | – | – | 40 | 40 | – | – | 39 | 39 |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| – Electricity forwards and futures (Note 24) | – | 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 22) | – | 16,935 | – | 16,935 | – | 16,935 | – | 16,935 |
| Floating rate loans to subsidiaries (Note 29 e) | – | – | – | – | – | 171,858 | – | 171,858 |
| Fixed rate loans to subsidiaries (Note 29 e) | – | – | – | – | – | 592,647 | – | 592,647 |
| Non-current financial receivables (Note 18 b) | – | – | 30,920 | 30,920 | – | – | 331 | 331 |
| Current financial receivables (Note 18 a, b) | – | – | 202,568 | 202,568 | – | – | 95,258 | 95,258 |
| Cash and cash equivalents (Note 19) | – | 129,455 | – | 129,455 | – | 127,554 | – | 127,554 |

There have been no transfers for assets between Level 1, Level 2 and Level 3 during the reporting period.

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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) | |
| As of 31 December 2019 | | | | | | | | |
| Liabilities measured at fair value | | | | | | | | |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| – Interest rate swaps (Note 24) | – | 9,216 | – | 9,216 | – | 9,216 | – | 9,216 |
| – Electricity and natural gas forwards and futures (Note 24) | – | 3,916 | – | 3,916 | – | 3,916 | – | 3,916 |
| Liabilities for which fair values are disclosed | | | | | | | | |
| Issued debt securities (bonds) (Note 23) | – | 136,956 | – | 136,956 | – | 136,956 | – | 136,956 |
| Borrowings (Note 23) | – | 745,668 | – | 745,668 | – | 745,668 | – | 745,668 |
| Trade and other financial current payables (Note 26) | – | – | 91,410 | 91,410 | – | – | 68,249 | 68,249 |
| As of 31 December 2018 | | | | | | | | |
| Liabilities measured at fair value | | | | | | | | |
| <i>Derivative financial instruments, including:</i> | | | | | | | | |
| – Interest rate swaps (Note 24) | – | 7,375 | – | 7,375 | – | 7,375 | – | 7,375 |
| – Natural gas forwards and futures (Note 24) | – | 2,829 | – | 2,829 | – | 2,829 | – | 2,829 |
| Liabilities for which fair values are disclosed | | | | | | | | |
| Issued debt securities (bonds) (Note 23) | – | 137,000 | – | 137,000 | – | 137,000 | – | 137,000 |
| Borrowings (Note 23) | – | 677,342 | – | 677,342 | – | 665,267 | – | 665,267 |
| Trade and other financial current payables (Note 26) | – | – | 103,707 | 103,707 | – | – | 78,726 | 78,726 |

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:

| | Group | | | | Parent Company | | | |
|---|-----------------|------------|------------|------------|-----------------|------------|------------|------------|
| | Carrying amount | | Fair value | | Carrying amount | | Fair value | |
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Financial assets | | | | | | | | |
| Fixed rate loans to subsidiaries | – | – | – | – | 642,967 | 592,647 | 673,987 | 616,332 |
| Other financial investments | 16,885 | 16,935 | 19,016 | 20,067 | 16,885 | 16,935 | 18,916 | 20,067 |
| Financial liabilities | | | | | | | | |
| <i>Interest-bearing liabilities, including:</i> | | | | | | | | |
| – issued debt securities (bonds) | 136,956 | 137,000 | 140,471 | 141,532 | 136,956 | 137,000 | 140,471 | 141,532 |

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.

26. Trade and other payables

| | Group | | Parent Company | |
|---|----------------|----------------|----------------|---------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Financial liabilities: | | | | |
| Payables for materials and services | 55,900 | 63,198 | 55,971 | 63,009 |
| Payables for electricity and natural gas | 24,803 | 30,627 | 6,193 | 9,954 |
| Accrued expenses | 9,106 | 7,817 | 4,702 | 4,142 |
| Other financial current payables | 1,601 | 2,065 | 1,383 | 1,621 |
| TOTAL financial liabilities | 91,410 | 103,707 | 68,249 | 78,726 |
| Non-financial liabilities: | | | | |
| State social security contributions and other taxes | 12,031 | 15,624 | 4,776 | 7,353 |
| Advances received | 8,403 | 12,024 | 3,641 | 4,399 |
| Other current payables | 3,864 | 3,655 | 1,715 | 1,584 |
| TOTAL non-financial liabilities | 24,298 | 31,303 | 10,132 | 13,336 |
| TOTAL trade and other current payables | 115,708 | 135,010 | 78,381 | 92,062 |

The carrying amounts of trade and other payables are assumed to approximate their fair values.

27. Provisions

Accounting policy

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.



| EUR'000 | | | | |
|---|---------------|---------------|----------------|--------------|
| | Group | | Parent Company | |
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Non-current: | | | | |
| – post-employment benefits (recognised in profit or loss) | 12,666 | 12,411 | 5,608 | 5,536 |
| – post-employment benefits (recognised in equity) | 2,420 | 356 | 1,480 | 332 |
| – termination benefits | 2,744 | 6,191 | 740 | 1,537 |
| – environmental provisions | 661 | 1,220 | 661 | 1,220 |
| | 18,491 | 20,178 | 8,489 | 8,625 |
| Current: | | | | |
| – termination benefits | 1,631 | 779 | 517 | 342 |

a) Provisions for post-employment benefits

Accounting policy

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 EIOPA risk-free interest rate, interest rates of Latvian government bonds (maturity of 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.

| EUR'000 | | | | |
|--|---------------|---------------|----------------|--------------|
| | Group | | Parent Company | |
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 12,767 | 13,721 | 5,868 | 5,911 |
| Current service cost | 1,170 | 1,238 | 522 | 523 |
| Interest cost | 134 | 261 | 62 | 112 |
| Post-employment benefits paid | (989) | (2,017) | (512) | (786) |
| Losses / (gains) as a result of changes in actuarial assumptions (Note 21 a) | 2,043 | (436) | 1,148 | 108 |
| Discontinued operation (Note 30) | (39) | – | – | – |
| At the end of the year | 15,086 | 12,767 | 7,088 | 5,868 |

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):

| EUR'000 | | | | |
|--|---------------|---------------|----------------|--------------|
| | Group | | Parent Company | |
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 12,767 | 13,721 | 5,868 | 5,911 |
| Credited/ (charged) to the Statement of Comprehensive Income (Note 21 a) | 2,043 | (436) | 1,148 | 108 |
| Credited/ (charged) to the Statement of Profit or Loss | 315 | (518) | 72 | (151) |
| Discontinued operation (Note 30) | (39) | – | – | – |
| At the end of the year | 15,086 | 12,767 | 7,088 | 5,868 |

Weighted average discount rate used for discounting benefit obligations was 1.05% (2018: 1.90%), considering EIOPA risk-free interest rate, interest rates of Latvian government bonds and EURBMK BBB electricity industry rate 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% (2018: 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.



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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 | 31/12/2019 | 1,948 | (1,596) | 1,880 | (1,577) | 2,084 | (1,722) | 827 | (675) | 798 | (667) | 885 | (728) |
| | 31/12/2018 | 1,519 | (1,252) | 1,479 | (1,247) | 1,646 | (1,366) | 610 | (501) | 593 | (499) | 661 | (547) |

The sensitivity analysis above has been determined based on a method that extrapolates the impact on post-employment benefits 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 2020.

Expected contributions to post-employment benefit plan for the year ending 31 December 2020 are EUR 1,942 thousand.

The weighted average duration of the defined benefit obligation is 19.51 years (2018 – 20.47 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 | 31/12/2019 | 2,397 | 2,143 | 10,546 | 15,086 | 1,734 | 1,082 | 4,272 | 7,088 |
| | 31/12/2018 | 2,481 | 1,745 | 8,541 | 12,767 | 1,676 | 955 | 3,237 | 5,868 |

b) Termination benefits

Accounting policy

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 d.

Termination benefits paid out 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 2019 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 | |
|------------------------------|---------|---------|----------------|---------|
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 6,970 | 9,315 | 1,878 | 2,607 |
| Termination benefits paid | (939) | (8,136) | (158) | (1,478) |
| Changes in provisions | (1,656) | 5,795 | (463) | 749 |
| At the end of the year | 4,375 | 6,974 | 1,257 | 1,878 |

According to defined development directions per Strategy of Latvenergo Group for the period 2017–2022, 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 2020 by 3.5% (2018: 9.6%) and in the following years by 3.0% for Latvenergo AS and in the year 2020 by 2.3% (2019: 2.6%) and in the following years by 2.5% for Sadales tīkls AS, average employee length of service at the time of termination, the State Social Insurance Contributions rate is 24.09% in 2020 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 2019, using the fixed discount rate of 0.651% as adopted by the Latvenergo Group (31/12/2018: 0.855%). The discount rate is comprised of a 3-year EUROSAP rate of -0.243% and a corporate risk premium of 0.894% (determined on the basis of interest rate on Latvenergo AS issued bonds yield spreads above the market rate) (31/12/2018: 4-year EUROSAP rate – 0.040%, corporate risk premium – 0.815%).



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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 | 31/12/2019 | (89) | 92 | 68 | (67) | 7 | (102) | (24) | 25 | 37 | (36) | 7 | (7) |
| | 31/12/2018 | (192) | 201 | 147 | (145) | 39 | 39 | (47) | 49 | 47 | (46) | 11 | (11) |

c) Environmental provisions



Accounting policy

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.

EUR'000

| | Group | | Parent Company | |
|--|-------|---------|----------------|-------|
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 1,220 | 2,264 | 1,220 | 1,220 |
| Charged to the Statement of Profit or Loss | (559) | (1,044) | (559) | – |
| At the end of the year | 661 | 1,220 | 661 | 1,220 |

The environmental provision for the Group represents the estimated cost for Latvenergo AS of cleaning up CHPP–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.

28. Deferred income



Accounting policy

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.

Grants related to expense items

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. Management judgements related to the measurement of government grants is disclosed in Note 4.

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).

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.

Accounting policy on recognition of deferred income from connection fees to distribution and transmission system disclosed per Note 6.

EUR'000

| | Group | | Parent Company | |
|---|----------------|----------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| I) Non–current deferred income | | | | |
| a) contracts with customers | | | | |
| From connection fees | 142,453 | 143,494 | – | – |
| Other deferred income | 877 | | 877 | |
| | 143,330 | 143,494 | 877 | – |
| b) operating lease | | | | |
| From connection fees | – | 3,852 | – | – |
| On transmission system assets reconstruction | – | 984 | – | – |
| Other deferred income | 383 | 403 | 383 | 403 |
| | 383 | 5,239 | 383 | 403 |
| c) other | | | | |
| On grant for the installed electrical capacity of CHPPs | 185,429 | 209,419 | 185,429 | 209,419 |
| On financing from European Union funds | 7,889 | 57,851 | 256 | 18 |
| On financing receivable from European Union funds | – | 30,617 | – | – |
| Other deferred income | 332 | 393 | 229 | 265 |
| | 193,650 | 298,280 | 185,914 | 209,702 |
| TOTAL non–current deferred income | 337,363 | 447,013 | 187,174 | 210,105 |



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| EUR'000 | | | | |
|--|----------------|----------------|----------------|----------------|
| | Group | | Parent Company | |
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| II) Current deferred income | | | | |
| a) contracts with customers | | | | |
| From connection fees | 13,629 | 12,984 | – | – |
| Other deferred income | 135 | 287 | 63 | – |
| | 13,764 | 13,271 | 63 | – |
| b) operating lease | | | | |
| From connection fees | – | 449 | – | – |
| Other deferred income | 20 | 20 | 20 | 20 |
| | 20 | 469 | 20 | 20 |
| c) other | | | | |
| On grant for the installed electrical capacity of CHPPs* | 23,990 | 23,990 | 23,990 | 23,990 |
| On financing from European Union funds | 787 | 1,941 | 12 | 12 |
| Other deferred income | 60 | 38 | 9 | – |
| | 24,837 | 25,969 | 24,011 | 24,002 |
| TOTAL current deferred income | 38,621 | 39,709 | 24,094 | 24,022 |
| TOTAL deferred income | 375,984 | 486,722 | 211,268 | 234,127 |

* see Note 4 h

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.

Movement in deferred income (non-current and current part):

| EUR'000 | | | | |
|---|----------------|----------------|----------------|----------------|
| | Group | | Parent Company | |
| | 2019 | 2018 | 2019 | 2018 |
| At the beginning of the year | 486,722 | 537,286 | 234,127 | 315,443 |
| Received deferred non-current income (financing) | 46,337 | 31,537 | 259 | – |
| Received advance payments for contracts with customers (Note 6) | 940 | – | 940 | – |
| Received connection fees for connection to distribution system (Note 6) | 12,902 | 14,725 | – | – |
| Received connection fees for connection to transmission system | 1,795 | – | – | – |
| Compensation for the installed electrical capacity of CHPPs credited to the Statement of Profit or Loss | (23,990) | (81,004) | (23,990) | (81,004) |
| Transferred to deferred income of discontinued operation (Note 30) | (132,507) | – | – | – |
| Credited to the Statement of Profit or Loss | (16,215) | (15,822) | (68) | (312) |
| At the end of the year | 375,984 | 486,722 | 211,268 | 234,127 |

29. Related party transactions

Accounting policy

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.

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 quantitative 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.



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a) Income and expenses from transactions with related parties:

EUR'000

| | Group | | Parent Company | | | |
|--|------------------------------|---------------|----------------|------------------------------|----------------|------------------------------|
| | 2019 | 2018 | 2019 | | 2018 | |
| | Government related entities* | | Subsidiaries | Government related entities* | Subsidiaries | Government related entities* |
| Income: | | | | | | |
| – Trade of energy and related services | 7,540 | 10,724 | 24,754 | 7,483 | 25,370 | 10,656 |
| – Lease of transmission system assets | 36,116 | 38,699 | – | – | – | – |
| – Other revenue from corporate services | – | – | 27,475 | – | 28,505 | – |
| – Other revenue | 3,197 | 3,175 | – | 3,077 | – | 3,024 |
| – Lease of assets | 223 | 372 | 8,802 | 223 | 14,534 | 372 |
| – Interest income | – | – | 11,810 | – | 10,289 | – |
| – Other income | 735 | 1,036 | 7 | – | – | 196 |
| TOTAL income from transactions with related parties | 47,811 | 54,006 | 72,848 | 10,783 | 78,698 | 14,248 |
| Expenses: | | | | | | |
| – Distributions system services | – | – | 195,652 | – | 207,096 | – |
| – Public service obligation fees | – | – | 87,379 | – | 98,623 | – |
| – Purchased electricity and heat | 5,175 | 4,131 | 19,856 | 4,959 | 37,461 | 4,131 |
| – Electricity transmission services costs (Note 8) | 71,552 | 71,368 | – | 1,015 | – | 1,015 |
| – Construction services for leased assets | – | – | 2,272 | – | 1,867 | – |
| – Other expenses | 739 | 864 | 1,494 | 267 | 1,594 | 276 |
| TOTAL expenses from transactions with related parties | 77,466 | 76,363 | 306,653 | 6,241 | 346,641 | 5,422 |
| <i>including gross expenses from transactions with subsidiaries recognised in net amount through profit or loss:</i> | | | | | | |
| – Sadales tīkls AS | – | – | 283,032 | – | 305,719 | – |
| – Enerģijas publiskais tirgotājs AS | – | – | – | – | – | – |
| | – | – | 283,032 | – | 305,719 | – |

* Transmission system operator – Augstsprieguma tīkls AS

b) Balances at the end of the year arising from sales / purchases of goods and services:

EUR'000

| | Group | | Parent Company | |
|--|---------------|---------------|----------------|---------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| Receivables from related parties: | | | | |
| – subsidiaries (Note 18 a, b) | – | – | 15,277 | 12,204 |
| – government related and other related parties* | 39,924 | 42,273 | 1,213 | 3,365 |
| – loss allowances for expected credit loss from receivables of subsidiaries (Note 18 a, b) | – | – | (11) | (9) |
| – loss allowances for expected credit loss from receivables of government related and other related parties* | (54) | (55) | (2) | (4) |
| | 39,870 | 42,218 | 16,477 | 15,556 |
| Payables to related parties: | | | | |
| – subsidiaries | – | – | 26,182 | 30,865 |
| – government related and other related parties* | 10,753 | 12,262 | 722 | 1,044 |
| | 10,753 | 12,262 | 26,904 | 31,909 |

c) Accrued income raised from transactions with related parties:

EUR'000

| | Group | | Parent Company | |
|---|------------|------------|----------------|--------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| – for goods sold/services provided for subsidiaries (Note 18 a, b) | – | – | 1,842 | 2,859 |
| – for interest received from subsidiaries (Note 18 a, b) | – | – | 1,622 | 1,820 |
| – for goods sold/services provided for government related entities* | – | 474 | – | – |
| | – | 474 | 3,464 | 4,679 |

d) Accrued expenses raised from transactions with related parties:

EUR'000

| | Group | | Parent Company | |
|--|--------------|------------|----------------|--------------|
| | 31/12/2019 | 31/12/2018 | 31/12/2019 | 31/12/2018 |
| – for purchased goods/received services from subsidiaries | – | – | 1,335 | 5,657 |
| – or purchased goods/received services from government related entities* | 1,460 | – | – | – |
| | 1,460 | – | 1,335 | 5,657 |

*Related parties included transmission system operator – Augstsprieguma tīkls AS and Pirmais Slēgtais Pensiju Fonds AS

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 and Note 21 b, respectively.

Dividends received from subsidiaries are disclosed in Note 16.



e) Loans to related parties (Parent Company)

Non-current and current loans to related parties:

| | EUR'000 | |
|---|----------------|----------------|
| | Parent Company | |
| | 31/12/2019 | 31/12/2018 |
| Non-current loans to subsidiaries | | |
| Sadales tīkls AS | 427,351 | 442,728 |
| Latvijas elektriskie tīkli AS | 161,460 | 152,681 |
| Impairment for expected credit loss | (377) | (405) |
| TOTAL non-current loans | 588,434 | 595,004 |
| Current portion of non-current loans | | |
| Sadales tīkls AS | 75,377 | 49,854 |
| Latvijas elektriskie tīkli AS | 27,259 | 8,175 |
| Impairment for expected credit loss | (66) | (39) |
| Current loans to subsidiaries | | |
| Latvijas elektriskie tīkli AS | 7,228 | 18,541 |
| Sadales tīkls AS | 15,182 | 6,502 |
| Elektrum Eesti OÜ | 7,052 | 7,882 |
| Elektrum Lietuva, UAB | 3,967 | 11,740 |
| Enerģijas publiskais tirgotājs AS | 69,889 | 68,233 |
| Impairment for expected credit loss | (66) | (77) |
| TOTAL current loans | 205,822 | 170,811 |
| TOTAL loans to subsidiaries | 794,256 | 765,815 |

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 and impairment for expected credit loss is recognised 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 – 'Baa2 level' creditrating. Since the initial recognition of loans, credit risk has not increased significantly that matches stage 1.

All current loans to related parties as of 31 December 2019 will be settled in 2020.

Movement in loans

| | EUR'000 | |
|---|----------------|------------------|
| | Parent Company | |
| | 2019 | 2018 |
| At the beginning of the year | 765,815 | 1,098,781 |
| Change in current loans in cash (net) | 272,103 | 323,539 |
| Change in current loans by non-cash offsetting of operating receivables and payables (net) | (219,388) | (720,848) |
| Issued non-current loans by non-cash offset for dividends | 33,743 | 124,268 |
| Reduction of non-current loans by non-cash offsetting of operating receivables and payables | (58,029) | (59,404) |
| Effect of IFRS 9 'Financial instruments' adoption | – | (515) |
| Impairment for expected credit loss | 12 | (6) |
| At the end of the year | 794,256 | 765,815 |

Interest received from related parties:

| | EUR'000 | |
|-------------------|----------------|--------------|
| | Parent Company | |
| | 2019 | 2018 |
| Interest received | 948 | 2,103 |
| | 948 | 2,103 |

l) Non-current loans, including current portion

Concluded non-current loan agreements with Latvijas elektriskie tīkli AS:

| Agreement conclusion date | Principal amount of the loan | EUR'000 | | Interest rate | Maturity date |
|---------------------------|------------------------------|----------------|----------------|------------------|-------------------|
| | | 31/12/2019 | 31/12/2018 | | |
| | | | | 6 months EURIBOR | |
| 1 April 2011 | 97,467 | 97,467 | 12,826 | + fixed rate | 1 April 2025 |
| 3 September 2013 | 44,109 | 44,109 | 27,568 | fixed rate | 10 September 2023 |
| 10 June 2016 | 156,500 | 156,500 | 120,462 | fixed rate | 10 June 2028 |
| TOTAL | 298,076 | 298,076 | 160,856 | | |

As of 31 December 2019, total outstanding amount of non-current loans to Latvijas elektriskie tīkli AS amounted to EUR 188,718 thousand (31/12/2018: EUR 160,856 thousand), including current portion of the loan repayable in 2019 – EUR 27,259 thousand (31/12/2018: EUR 8,176 thousand). As of 31 December 2019, for 5% (31/12/201: 8%) 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 2019 the effective average interest rate of non-current loans was 1.72% (2018: 1.81%). As of 31 December 2019, is recognised impairment for expected credit loss of non-current loans to Latvijas elektriskie tīkli AS in the amount of 121 thousand EUR (31/12/2018: EUR 109 thousand). 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 | |
| | 31/12/2019 | 31/12/2018 |
| Non-current loan: | | |
| – < 1 year (current portion) | 27,259 | 8,176 |
| – 1 – 5 years | 101,039 | 109,724 |
| – > 5 years | 60,420 | 42,957 |
| | 188,718 | 160,856 |



Concluded non-current loan agreements with Sadales tīkls AS:

EUR'000

| Agreement conclusion date | Principal amount of the loan | Outstanding loan amount | | Interest rate | Maturity date |
|---------------------------|------------------------------|-------------------------|----------------|-------------------------------|-------------------|
| | | 31/12/2019 | 31/12/2018 | | |
| 29 September 2011 | 316,271 | 38,316 | 47,966 | 6 months EURIBOR + fixed rate | 1 September 2025 |
| 6 February 2013 | 42,686 | 10,672 | 14,940 | fixed rate | 10 September 2022 |
| 18 September 2013 | 42,686 | 17,074 | 21,343 | fixed rate | 10 August 2023 |
| 29 October 2014 | 90,000 | 50,000 | 60,000 | fixed rate | 10 September 2024 |
| 20 October 2015 | 90,000 | 60,000 | 70,000 | fixed rate | 21 October 2025 |
| 22 August 2016 | 60,000 | 46,667 | 53,333 | fixed rate | 22 August 2026 |
| 22 August 2016 | 50,000 | 40,000 | 45,000 | fixed rate | 14 June 2027 |
| 14 December 2018 | 260,000 | 240,000 | 180,000 | fixed rate | 14 December 2028 |
| TOTAL | 951,643 | 502,729 | 492,582 | | |

As of 31 December 2019, total outstanding amount of non-current loans with Sadales tīkls AS amounted to EUR 502,729 thousand (31/12/2018: EUR 492,582 thousand), including current portion of the loan repayable in 2019 – EUR 75,377 thousand (31/12/2018: EUR 49,853 thousand). As of 31 December 2019, for 8% of the loans issued to Sadales tīkls AS (31/12/2018: 10%) was set floating interest rate, which was influenced by 6 months EURIBOR interbank rate fluctuations. During 2019 the effective average interest rate of non-current loans was 1.65% (2018: 1.65%). As of 31 December 2019, is recognised impairment for expected credit loss of non-current loans to Sadales tīkls AS in the amount of EUR 322 thousand EUR (31/12/2018: EUR 335 thousand). Non-current loans are not secured with a pledge or otherwise.

Non-current loans to Sadales tīkls AS by maturity:

EUR'000

| | Parent Company | |
|------------------------------|----------------|----------------|
| | 31/12/2019 | 31/12/2018 |
| Non-current loan: | | |
| – < 1 year (current portion) | 75,377 | 49,853 |
| – 1 – 5 years | 278,198 | 322,786 |
| – > 5 years | 149,154 | 119,943 |
| | 502,729 | 492,582 |

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, current loans 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 2019 the effective average interest rate was 0.48% (2018: 0.51%).

On 31 March 2019 an agreement was concluded between Latvenergo AS and Enerģijas publiskais tirgotājs AS for issue of the current loan in amount of EUR 110,000 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 2020 or 31 March 2020 upon a condition neither of parties propose a termination of the agreement one month before the expiry of the agreement. An agreement concluded on 29 March 2018 with amount of EUR 150,000 thousand and maturity date - 31 March 2019 is repaid. Loan annual interest rate is fixed at 1.115% (2018: 0.730%). As of 31 December 2019, net outstanding amount of current loan is EUR 67,971 thousand (31/12/2018: EUR 68,233 thousand).

As of 31 December 2019 impairment for expected credit loss of current loans to related parties is recognised in the amount of 66 thousand EUR (31/12/2018: 77 thousand EUR).

f) Interest paid to related parties (Parent Company)

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 2019 the effective average interest rate was 0.48% (2018: 0.51%). At the end of the reporting year Latvenergo AS has no borrowings from related parties (31/12/2018: nil).

EUR'000

| | Parent Company | |
|---------------|----------------|-----------|
| | 2019 | 2018 |
| Interest paid | 38 | 37 |
| | 38 | 37 |

30. Discontinued operations



Accounting policy

A discontinued operation is a component of the entity that has been disposed of or is classified as held for sale or distribution and that represents a separate major line of business or geographical area of operations, is part of a single co-ordinated plan to dispose of such a line of business or area of operations, or is a subsidiary acquired exclusively with a view to resale.

The Group classify assets and liabilities held for distribution if the discontinued operation is available for immediate distribution in its present condition and distribution is highly probable, as well is measured at the lower of their carrying amount and fair value less costs to distribute.

Assets and liabilities classified as held for distribution are presented separately from the other assets and other liabilities in the Statement of Financial Position.

Discontinued operations are excluded from the results of continuing operations and are presented as a single amount as profit for the year from discontinued operation in the Statement of Profit or Loss. as profit for the year from discontinued operation in the Statement of Profit or Loss.



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On 8 October 2019, the Cabinet of Ministers of the Republic of Latvia supported the implementation of the “full ownership unbundling” model for the electricity transmission system operator by its Protocol Decision No. 46 §38. It is expected that the ownership of Latvijas elektriskie tīkli AS by Latvenergo AS to be terminated and the ownership of Latvijas elektriskie tīkli AS by Augstsprieguma tīkls AS to be commenced by 1 July 2020. Since Latvenergo AS and Augstsprieguma tīkls AS are both state-owned companies, the change of ownership of assets will occur through the reduction of the share capital of Latvenergo AS by withdrawing the capital shares of Latvijas elektriskie tīkli AS from the base of assets of Latvenergo AS. After the capital shares of Latvijas elektriskie tīkli AS become property of the state, they will be invested in the share capital of Augstsprieguma tīkls AS.

In Latvenergo Group’s financial statements as of 31 December 2019 subsidiary Latvijas elektriskie tīkli AS was classified as a discontinued operation in accordance with IFRS 5, “Non-current Assets Held for Sale and Discontinued Operations”. In the Statement of Financial Position are disclosed assets, reserves and liabilities held for distribution and in the Statement of Profit or Loss – profit for the year 2019 and comparatives for discontinued operations. In the Group’s operating segments results financial results of Latvijas elektriskie tīkli AS are disclosed in transmission system assets lease segment because the Management Board of the Parent Company will continue review financial results of this operating segment until the termination of its ownership.

Financial information of discontinued operation disclosed in tables below includes financial results of transmission system assets lease business, amounts of net assets, reserves in equity, liabilities and cash flows results.

Statement of Profit or Loss

| | Group | | EUR'000 |
|--|---------------|---------------|---------|
| | 2019 | 2018 | |
| Revenue | 36,643 | 39,203 | |
| Other income | 1,664 | 2,162 | |
| Raw materials and consumables used | (21) | (144) | |
| Personnel expenses | (450) | (403) | |
| Other operating expenses | (395) | (1,184) | |
| EBITDA | 37,441 | 39,634 | |
| Depreciation, amortisation and impairment of intangible assets and property, plant and equipment | (24,756) | (25,856) | |
| Operating profit | 12,685 | 13,778 | |
| Finance costs | (17) | – | |
| Profit before tax | 12,668 | 13,778 | |
| Income tax | (2,436) | (3,348) | |
| Profit for the year from discontinued operation | 10,232 | 10,430 | |

The major classes of assets, reserves and liabilities classified as held for distribution:

| | Group | | EUR'000 |
|--|------------------|------------|---------|
| | 31/12/2019 | 31/12/2018 | |
| Assets | | | |
| Property, plant and equipment (Note 14 a) | 601,175 | – | |
| Right-of-use assets (Note 15) | 1,099 | – | |
| Inventories | 184 | – | |
| Receivables | 37,635 | – | |
| Cash and cash equivalents (Note 19) | 300 | – | |
| Assets held for distribution | 640,393 | – | |
| Liabilities | | | |
| Provisions (Note 27) | (39) | – | |
| Lease liabilities (Note 15) | (1,107) | – | |
| Deferred tax liability | (2,435) | – | |
| Deferred income (Note 28) | (132,507) | – | |
| Trade and other payables | (43,488) | – | |
| Liabilities directly associated with assets held for distribution | (179,576) | – | |
| Net assets directly associated with disposal group | 460,817 | – | |
| Amounts included in accumulated other comprehensive income: | | | |
| Non-current assets revaluation reserve (Note 21) | 28,916 | – | |
| Post-employment benefit plan revaluation reserve (Note 21) | 20 | – | |
| Reserves of disposal group classified as held for distribution | 28,936 | – | |

Net cash flows from discontinued operations

| | Group | | EUR'000 |
|---|----------|----------------|---------|
| | 2019 | 2018 | |
| Net cash flows from operating activities | 85,853 | 85,583 | |
| Net cash flows used in investing activities | (85,825) | (86,783) | |
| Net cash flows used in financing activities | (28) | – | |
| Net changes in cash and cash equivalents | – | (1,200) | |



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31. Commitments and contingent liabilities

As of 31 December 2019, the Group had commitments amounting to EUR 156.3 million (31/12/2018: EUR 189.8 million) and the Parent Company had commitments amounting to EUR 52.3 million (31/12/2018: EUR 58.5 million) for capital expenditure contracted but not delivered at the end of the reporting period.

Latvenergo AS has issued support letters to its subsidiaries – on 19 February 2020 to Latvijas elektriskie tīkli AS, on 20 February 2020 to Enerģijas publiskais tirgotājs AS and on 3 March 2020 to Sadales tīkls 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.

32. Events after the reporting year

Accounting policy

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.

On 14 January 2020, Latvenergo AS signed a loan agreement with SEB banka AS for EUR 60 million and with a repayment term up to 2 years.

On 27 February 2020, the Saeima included in the agenda the draft law “On Amendments to the Electricity Market Law”, but on 5 March 2020 it was submitted for review to Economic, Agricultural, Environmental and Regional Policy Committee. The draft law provides for the deletion of some rules of the Electricity

Market Law, which defines payments of guaranteed fee for electrical capacity installed at cogeneration power plants. Also, it provides for terminating the order that states that the electricity costs incurred by the public trader in carrying out the statutory functions are borne by the final consumers. The draft law may cause impacts on the Latvenergo Group's profits and asset value.

At the beginning of 2020, the existence of the new coronavirus (Covid-19) was approved and it has currently spread all over the world, also in Latvia, disturbing business and affecting economic development. Latvenergo Group is constantly evaluating the impact of spreading of Covid-19 and implements measures for safety of customers and employees, as well ensures appropriate working regime in strategically important facilities – Daugava hydropower plants, combined heat and power plants in Riga and facilities of Sadales tīkls AS. Latvenergo Group continues to provide all services to its customers and any customer service issues are resolved using remote means of communication.

Spreading of the virus does not have a significant effect on the provision of services by Latvenergo Group. The Group continues to ensure continuity and availability to all customers of electricity generation, electricity and natural gas trading and distribution services. Management of Latvenergo Group considers that the spread of the virus is a non-adjusting event after the reporting period. Since the situation is unclear and is developing rapidly, it is currently not possible to provide a statistical estimate of the potential effect of spreading of the virus on Latvenergo Group, however Covid-19 influence could lead to economic downturn, with the most significant impact on electricity consumption and receivables.

There have been no other significant events subsequent to the end of the reporting year that might have a material effect on the Latvenergo Consolidated and Latvenergo AS Financial Statements for the year ending 31 December 2019.

This document is signed with a secure digital signature and contains a time stamp

Āris Žigurs
Chairman of the Management Board

Guntars Balčūns
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

7 April 2020



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 (together the Group) as at 31 December 2019, and of their separate and consolidated financial performance and their 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 27 March 2020.

What we have audited

The financial statements presented on pages 11 to 62 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 profit or loss for the year ended 31 December 2019;
- the separate and consolidated statement of comprehensive income for the year ended 31 December 2019;
- the separate and consolidated statement of financial position as at 31 December 2019;
- 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

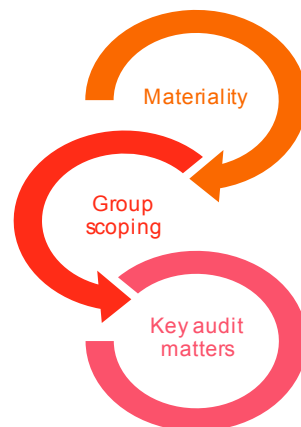
We are independent of the Company and the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Law on Audit Services that are relevant to our audit of the financial statements in 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 2019 to 31 December 2019, are disclosed in Note 10 to the financial statements.

Our audit approach

Overview



Materiality

- Overall Company and Group materiality: EUR 6,800 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

- Discontinued operations

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.

Overall Company and Group materiality

Overall materiality applied to the Company and the Group was EUR 6,800 thousand.

How we determined it

5% of average profit before tax from continuing and discontinued operations for the recent three years.

Rationale for the materiality benchmark applied

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 (2017-2019) 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 680 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.



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Key audit matters

How our audit addressed the key audit matter

Discontinued operations

Refer to Note 30 to the financial statements on pages from 60 to 61.

In 2019 the Cabinet of Ministers of the Republic of Latvia decided to support the scenario presented by the Ministry of Economics and the Ministry of Finance on the implementation of electricity transmission system operator ownership model “Complete separation of ownership”, which foresees transfer of “Latvijas elektriskie tīkli” (LET) shares from Latvenergo group to “Augstsprieguma tīkli” (AST) by 1 July 2020.

Management had to apply judgement in evaluating if the planned transfer of LET shares meets the criteria of a disposal group under IFRS 5 “Non-current assets held for distribution and discontinued operations” as at 31 December 2019. According to IFRS 5 classification of a disposal group as assets held for distribution is only achieved if the asset is available for immediate distribution in its present condition and the distribution is highly probable (including management’s commitment to the plan, unlikely significant changes to the plan, the probability of shareholder’s approval). Management also had to make judgement on classification of transactions between continuing and discontinued operations.

We focused on this area because classification, measurement and presentation of discontinued operations and assets held for distribution and the related liabilities have material impact on the Group’s financial statements as at 31 December 2019 and for the year then ended.

We examined the Cabinet of Ministers decision on “Complete separation of ownership” in relation to electricity transmission system operator ownership model and evaluated the Group’s management assessment of the probability of the transaction, the Group’s management commitment to the plan to distribute the assets, actions taken to initiate the distribution, timing of the planned distribution, likelihood of the significant changes to the plan and the probability of the shareholder’s approval.

We evaluated the Group’s management judgement on classification of transactions between continuing and discontinued operations.

We performed detailed audit procedures on the classification of the discontinued operations revenue and expenses and the assets held for distribution and the related liabilities in the Group’s financial statements as at 31 December 2019 and for the year then ended and in the comparative statement of profit or loss for the year ended 31 December 2018.

We assessed whether the information disclosed in the financial statements in relation to discontinued operations meets the requirements of IFRS 5.

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.

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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 3 to 10 of the accompanying Annual Report,
- Non-financial Report included in the Management Report as set out on page 8 of the accompanying 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.

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 56.² 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 56.2 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.



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- 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 2019 by resolution of general meeting of shareholders dated 8 May 2019. This is our second year of the appointment.

PricewaterhouseCoopers SIA
Certified audit company
License No. 5

Ilandra Lejiņa
Certified auditor in charge
Certificate No.168
Member of the Board

Riga, Latvia
7 April 2020

Independent Auditor's Report is signed electronically with a secure electronic signature and contains a time stamp.

ISSUER

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