elering

GENERATING OPPORTUNITIES

Annual Report **2013**

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Management Report of Elering's Annual Report

Statement by the Chairman of the Management Board

TAAVI VESKIMÄGI

The Chairman of the Management Board

A year of achieving targets

In four years of independent operations, Elering has grown from the unit of Eesti Energia to one of the best state enterprises in the Baltic counties. Elering has become the cornerstone of security of supply of the Baltic electricity with a sufficient number of connections. The borders of EU member states are no longer important as the electricity supply of consumers in Tallinn would be secured equally by the power station in Olkiluoto in Finland and by the power station in Narva. This is the direct benefit of connections for consumers. European Union's vision with regard to the energy sector – common network, single market – is in the interest of Estonia.

Independent system operator

In 2013, the Estonian Competition Authority, in cooperation with the European Commission, confirmed that Elering complies with the requirements resulting from EU regulations and gave the company the right to operate in Estonia as the transmission system operator for electricity. In the opinion of the European Commission, the Ministry of Economic Affairs and Communications as the holder of sole shareholder rights of Elering and the Ministry of Finance as the holder of shareholder rights of Eesti Energia, are separate enough to ensure that Elering is sufficiently independent in exercising state rights.

Elering also fulfils the requirements that oblige the transmission system operator to ensure equal treatment of market participants, to have sufficient means to operate and develop the electricity system, to give sufficient information to other network operators, and to cooperate with transmission system operators of other countries.

The independence of the system operator is a key precondition in creating a competitive electricity market. Only the equal treatment of all market participants, based on the common electricity market of Nordic and Baltic countries, ensures greater public benefit in the long run. The most recent important steps in achieving this objective were the acquisition of the EstLink 1 interconnection and the implementation of the transmission capacity distribution mechanism on the Estonian-Latvian border that maximises the public benefit.

In addition to the Estonian Competition Authority and the European Commission, in 2013 the activities of Elering were directly or indirectly assessed also by others. For instance, the State Audit Office said in its report on the governance of commercial enterprises that out of nine audited commercial enterprises, the Supervisory Board of only one, i.e. Elering, comprehensively assesses the fulfilment of the strategy with its resolution once a year. In a pan-European comparison of efficiency of main network operators, Elering achieved the maximum possible result in efficiency,

i.e. 100%. Whereas due to network fees the public is under a misconception that network operation is becoming more expensive, the study confirms that Elering has clearly decreased unit costs of operating the electricity network in recent years. Among others, the study showed that, considering the actual size of the network, Elering has very few employees as a transmission system operator. On the basis of average indicators of transmission networks covered in the study and considering the size of the network, Elering could have a third more staff than at present.

The best financial result of all times

For Elering, the concluded financial year was the most succesful of all times. We earned 49 million euros in profit for the owner. At the same time we invested the profit that we earned and much more, totalling 203 million euros, back to the development of the Estonian electricity system.

In addition to normal revenue, Elering earned 14.2 million euros from the auction of transmission capacities. The auction revenue was aimed mainly at increasing the cross-border transmission capacity, but since the construction of the third interconnection between Estonia and Latvia is at present being prepared, we will re-distribute the revenue back to consumers through lower network fees so that the third Estonian-Latvian line can be developed at the end of the decade and financed by network fees. Elering's obligation is to eliminate physical restrictions on electricity trade between Estonia and Latvia. At the same time congestion income is not something that can be taken for granted in the future. It is not clear what will be the auction revenue in 2014 and therefore we cannot assume that the transmission service would become cheaper on the basis of this revenue source in the coming years.

Major projects nearing completion

Since December 2013, EstLink 2 has been at the market's disposal. EstLink 2 has a significant impact on the transmission capacity between Estonia and Finland, improving the functioning of the electricity market and also increasing the security of supply. After the takeover of EstLink 2, it is possible to transmit 1,000 MW of electricity between the two countries instead of the earlier 350 MW. In the direction from Finland to Estonia, the transmission capacity is limited to 860 MW until the second stage of the Kiisa reserve power station is completed in 2014. The total cost of the EstLink 2 project is approximately 320 million euros that is shared between Fingrid and Elering. The European Union supports the project with an investment subsidy of 100 million euros.

In the autumn 2013, Elering, Fingrid and Nordic Energy Link completed negotiations over the ownership of the

first Estonian-Finnish electricity interconnection EstLink 1. According to the signed contract, the ownership of EstLink 1 was transferred to system operators on 30 December. The total amount of the transaction was 77.6 million euros.

At the end of the year, Wärtsilä delivered to Elering the first stage of the Kiisa emergency reserve power plant with the capacity of 110 MW. Now Elering has the necessary emergency capacity at the best price in Estonia.

Development of a regional electricity market

2013 was the first year of open electricity market in Estonia. By the end of the year, almost 80% of consumption points had an electricity consumption contract. Only low-consumption customers (rural homes, summer cottages, etc.) are yet without a contract. In terms of the volume of consumed electricity, contractual customers accounted for more than 90% of the total consumption volume. During the year, approximately 6% of consumption points changed the supplier. This is definitely not a bad indicator, considering that the market opened only recently and the choice of the electricity supplier occurred for the first time. In the second half of the year, the activity in changing the supplier increased.

It is clear that the Estonian market has plenty of room for new participants and needs more electricity sellers. For a competitive market with several market participants, the market share of Eesti Energia among end-consumers is still too high. Starting from 2014, the commissioning of EstLink 2 brought about a principle change, creating the Estonian-Finnish electricity market with unified market regulation and prices. Already at the end of 2013 and at the beginning of 2014, during trial commissioning of the new connection, it was evident that power flows from Nordic countries through Estonia into other Baltic states are increasing. The new connection will also create better preconditions for attracting more Scandinavian electricity sellers into Estonia.

On 3 June 2013, Latvia joined the day-ahead power exchange of Nord Pool Spot. This means that all Baltic countries are now integrated into a common trading system. Earlier, on 15 March, Baltic transmission system operators (TSOs) signed an agreement on the operation of the Baltic electricity market after Latvia joins Nord Pool Spot (NPS) in order to make maximum commercial use of interconnections between EU member states and to develop a regional electricity market that is transparent and operates on the basis of common rules. The agreement covers the calculation and distribution of cross-border transmission capacities on the borders between the Baltic countries and on the border with Russia and Belarus.

For Estonia, the key was to reach an agreement to provide maximum transmission capacities between Estonia and Latvia as the capacity shortfall is restricting trade, especially in the summer. In accordance with the methods agreed between Baltic transmission operators, NPS directs all electricity imported from third countries to the NPS price area on the Lithuanian-Belarusian border. No commercial capacity will be allocated to the Estonian and Latvian border with Russia.

Reducing the impact of the integrated Russian electricity system

In accordance with the joint communiqué of the three Baltic Prime Ministers dated summer 2007 in which the three parties confirmed the strategic objective of connecting their networks to the electricity network of Continental Europe, the TSOs of the three Baltic countries carried out a feasibility study on the possible cost and timeframe of desynchronisation. The most important finding of the study was that synchronisation to the electricity system of Continental Europe is technically possible. The list of necessary investments included various expenses that must be made also for other purposes than the specific objective of desynchronisation. Moreover, the study confirmed the earlier assessment that the possible construction of a nuclear power plant with high unit capacity in Lithuania or Kaliningrad and connection to the synchronous grid of Continental Europe, are essentially mutually exclusive.

The preparation process for changing the synchronisation area is long and requires a step-by-step approach. Regardless of which specific technical solution will be chosen for connecting to the frequency area of Continental Europe, no desynchronisation will take place before 2025.

In summary

Elering has identified itself as an enterprise with a low risk profile that operates in 100% regulated business of providing consumers with a sense of security about the energy supply at all times. The economic activities in 2013 and the achievement of all objectives set for the year provide a strong foundation for launching new development directions that will increase the company value, taking into consideration the company's mission, values and risk profile.

Most importantly – the main asset of Elering is the unique know-how, skills and experience of its staff. This means that a significant share of the company's fixed assets leaves the company in evenings to go home. The task of the Management Board is to attract these people back to the job the next morning. Setting new objectives is possible only if there is a spark in the eyes of our employees!

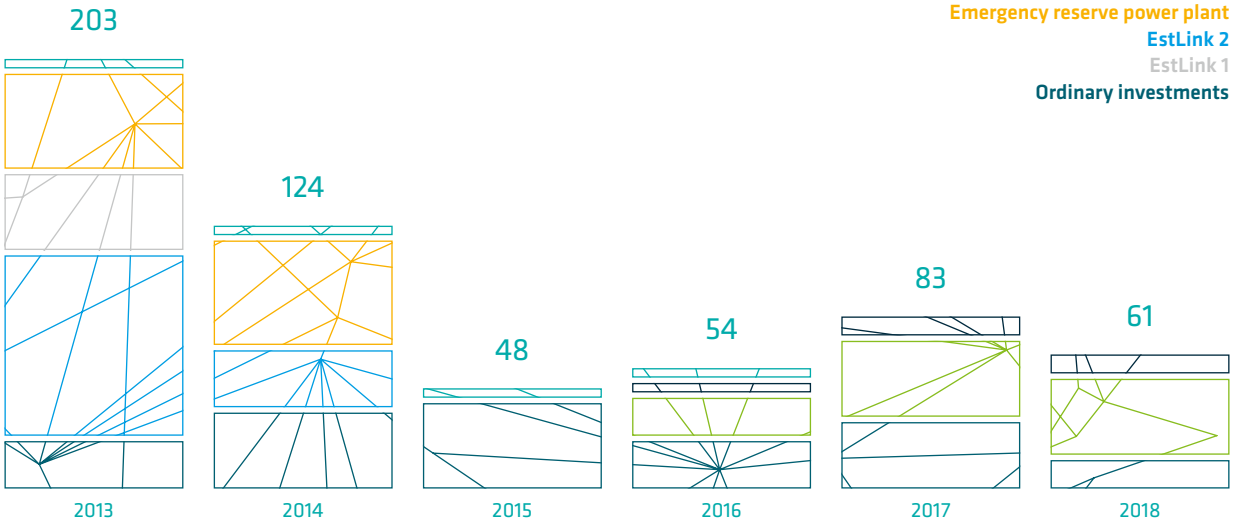
Brief overview of Elering

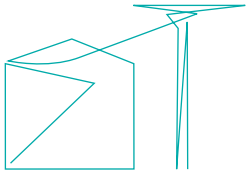
Elering is a transmission system operator that manages Estonia's electricity system in real time and is responsible for its functioning. Our goal is to ensure that our customers can enjoy a consistent, high-quality electricity supply at all times. To ensure security of supply, we create conditions for the functioning of the electricity market and develop cross-border interconnections.

370

MEUR, the investment program of Elering in the next five years

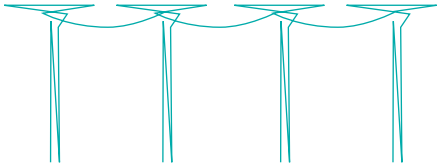
Distribution of Elering's investments in fixed assets in 2013-2018 (MEUR)



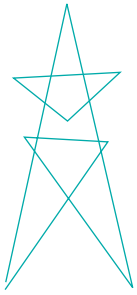


145

substations

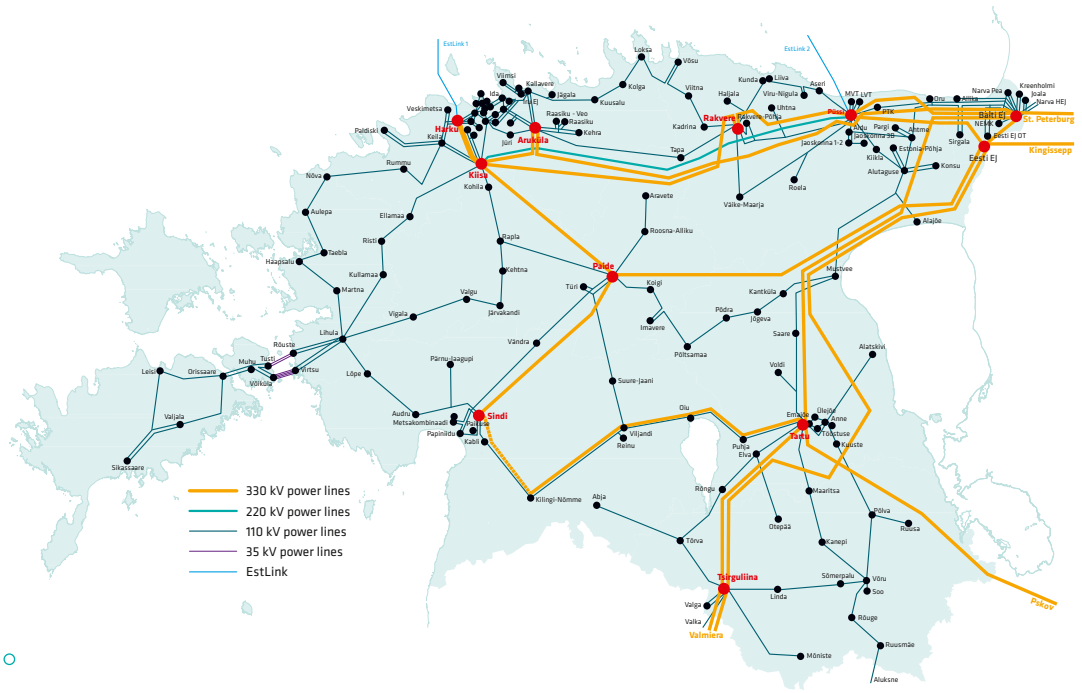


Cross-border connections with Finland, Latvia and Russia



5223

kilometres of high-voltage overhead and cable lines



1000

MW EstLink 2 transmission capacity with Finland

average age 42

average length of employment 15

147

employees, the share of women is 26%

Financial figures (MEUR)

	2010	*2011*	*2012*	***2013***
Revenue	89	94	109	**134**
Operating profit	21	29	41	**53**
Net profit	14	21	35	**49**
Borrowings	186	222	227	**312**
Equity	160	190	225	**274**
Assets	419	486	516	**671**
EBITDA	44	50	64	**77**
Investments in fixed assets	27	78	74	**203**
Dividends	0	0	0	**0**

Financial Ratios

ROE	9,0%	11,7%	16,8%	**19,6%**
Equity/Assets	38%	39%	44%	**41%**
Net Borrowings/EBITDA	3,3	4,0	3,3	**4,0**

$$ROE = \frac{\textit{Net profit}}{\textit{Average equity}}$$

Net Borrowings = interest-bearing liabilities – cash and cash equivalents
EBITDA = Operating profit + depreciation and amortization

Key indicators of the Estonian electricity system

Electricity balance

In 2013, Estonia's electricity consumption, including network losses, amounted to 8.06 TWh, i.e. 1% less than in 2012. The main reason for the decrease in electricity consumption was the unusually warm winter period.

In 2013, the Estonian electricity production totalled 11.66 TWh, which is 11% more than in 2012. Electricity generated in Estonia exceeded domestic consumption by 45%, making up the annual system balance surplus as much as 3.6 TWh.

Electricity balance (GWh)

	2013	*2012*	*Change*
Electricity production in Estonia	**11,655**	**10,459**	**11%**
Electricity given to Elering's network	11,410	9,200	24%
Production of renewable energy in Estonia	1,151	1,367	-16%
Electricity import from cross-border power lines	**2,416**	**2,585**	**-7%**
· incl. physical transmission from Finland	1,513	1,458	4%
· incl. physical transmission from Latvia and Russia	903	1,127	-20%
Total electricity given to the network	**14,071**	**13,044**	**8%**
Electricity consumption in Estonia	**8,060**	**8,139**	**-1%**
Elering's domestic transmission service for consumption	7,466	7,545	-1%
Elering's network losses	349	352	-1%
Electricity export through cross-border power lines	**6,011**	**4,905**	**23%**
· incl. physical transmission to Finland	506	393	29%
· Incl. physical transmission to Latvia and Russia	5,505	4,512	22%
Total electricity taken from the network	**14,071**	**13,044**	**8%**
Balance	**3,595**	**2,320**	**55%**

Electricity balances in Nordic and Baltic countries

In 2013, electricity production in the Nordic countries decreased by 6% to 380 TWh. Production in Norway and Sweden fell by 9%, while Finland's production remained on a par with the previous year. As the only exception, electricity production in Denmark increased 13% year on

year due to favourable wind conditions. The fall in the overall Nordic production was mainly caused by decreased consumption, as well as low fill rates of hydro reservoirs. The combined balance for Nordic countries had a deficit of 0.9 TWh in 2013. A year earlier, the Nordic countries exported 15.8 TWh of electricity.

In 2013, electricity generation in the Baltic countries totalled 21.2 TWh, which is 8% more than in 2012. Electricity production decreased only in Lithuania, while increasing in both Estonia and Latvia.

The combined electricity deficit of the three Baltic countries totalled 4.7 TWh, a decrease of 22% year on year. The biggest shortage was in Lithuania which imported approximately 67% of electricity necessary to cover its consumption.

Electricity trade balance

As in the previous year, the balance of cross-border electricity trade was marked by exports to Latvia and Lithuania and imports from Finland. Estonia's net exports increased 64% year on year, totalling 3,598 GWh.

Cross-border net eletricity trade (GWh)

	2013	*2012*	*Change*
· incl. exports on the Estonian-Latvian border	4650	3371	38%
· incl. exports from Estonia to Finland	-1052	-1183	-11%
Net balance	**3 598**	**2 189**	**64%**

In 2013, the shares of Estonian export were similar to 2012 – exports on the Estonian-Latvian border accounted for 91% and exports to Finland made up 9% of Estonia's total exports. Imports on the Estonian-Latvian border made up 38% of total imports, while imports from Finland accounted for 62% of total imports.

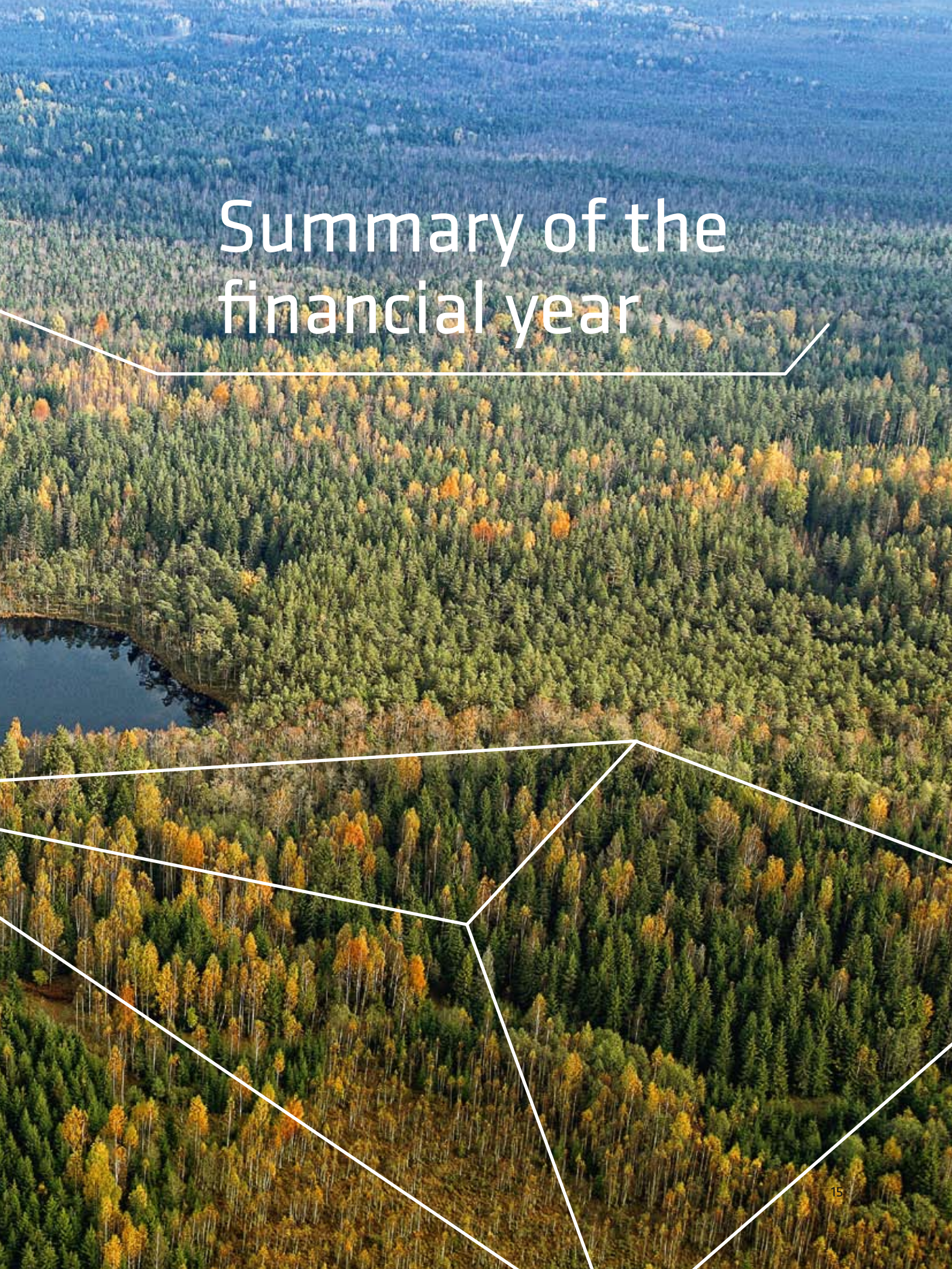
Cross-border electricity trade (GWh)

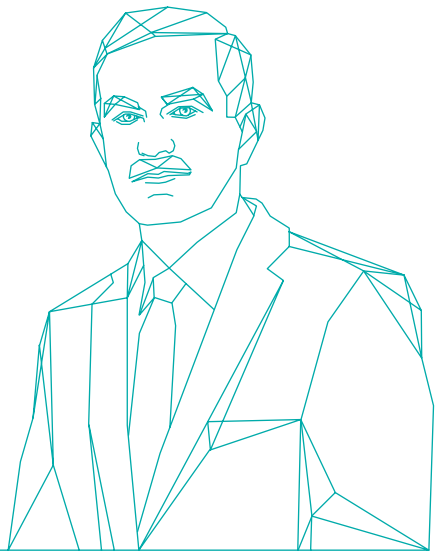
	2013	*2012*	*Muutus*
Total exports	**6,207**	**4,841**	**28%**
Exports on the Estonian-Latvian border	5,639	4,413	28%
Exports to Finland	568	428	33%
· incl. exports through the power exchange	5,288	3,547	49%
· incl. exports under bilateral contracts	919	1,294	-29%
Total imports	**2,609**	**2,652**	**-2%**
Imports on the Estonian-Latvian border	989	1,041	-5%
Imports from Finland	1,620	1,611	1%
· incl. imports through the power exchange	2,008	2,392	-16%
· incl. imports under bilateral contracts	601	261	130%
Balance	**3,598**	**2,189**	**64%**

** Cross-border electricity trade balance comprises of balance providers' deliveries and deliveries stated by the power exchange operator. Cross-border electricity trade balance does not include system imbalance deliveries and cross-border regulating deliveries.*

*** In June 2013, Nord Pool Spot opened the Latvian price area, replacing the NPS ELE price area that had been operating as a temporary solution. Therefore, electricity trade with Lithuania is included in the summarized trade volume on the Estonian-Latvian border.*

Summary of the financial year





PEEP SOONE

Member of the Management Board

The company ended the financial year with the total revenue of 134.4 million euros, as compared to 109.5 million euros in 2012.

The majority of the revenue (82%) came from the network service which is regulated by law. Elering has 29 network service customers in Estonia, of which five are distribution network operators, eight are large consumers and 16 are electricity producers. In addition, a significant part of network service revenue was also received from the cross-border transmission capacity auctions. Auction revenue occurs in the situation where cross-border electricity transmission requests between the EU member states exceed the technical possibilities. In this situation, transmission capacities are sold to market participants through different auction mechanisms. Such revenue is deducted when calculating the tariffs for the next period.

The most successful financial year in the history of Elering

In revenues, network service was followed by the balancing service, which accounted for 15% of the total revenue. In order to maintain stable frequency in the electricity system, the system must be balanced, i.e. generation must equal consumption at all times. For that aim, all market participants must be balanced and most of them purchase the balancing service from the balance providers. Elering in turn provides to the balance providers the service of reaching their energy balance. The balancing service has virtually no effect on the company's profit since the price of the balancing service is calculated so that the earned revenue covers the expenses necessary for providing the service.

The increase in revenues by 24.9 million euros mainly came from:

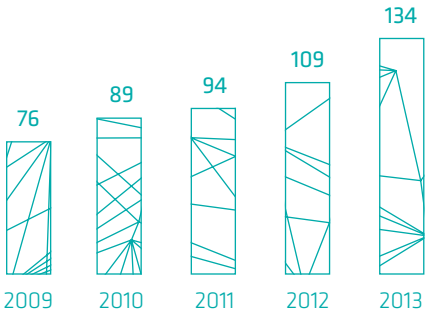
- cross-border transmission capacity auctions (10.2 million euros);
- revenue from domestic network service (9.0 million euros);
- balancing service (6.8 million euros).

Operating expenses totalled 81.1 million euros, having increased by 12.9 million euros. Main reasons for growth in expenses were:

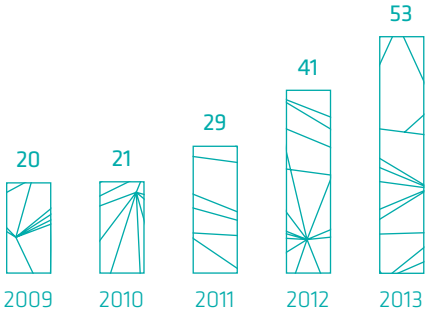
- increase in the volume of purchased balancing energy (6.1 million euros);
- growth in expenses for the purchase of energy losses (5.2 million euros) as a result of the abolishment of the regulated electricity tariffs starting from 2013.

Operating profit totalled 53.3 million euros, as compared to 41.3 million euros a year earlier.

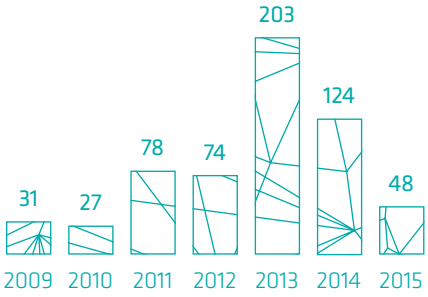
Revenues (MEUR)



Operating profit (MEUR)

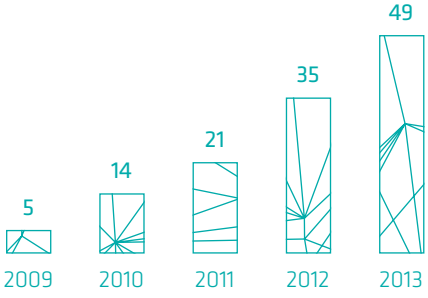


Investments in fixed assets* (MEUR)



* *Recognised in acquisition value*

Net profit (MEUR)



Net financing expenses decreased from 6.4 million euros in 2012 to 4.4 million euros in 2013. The decrease was mainly attributable to the growth in capitalised interest in the amount of 2.6 million euros. In accordance with the International Financial Reporting Standards, the interest expense of loan capital necessary for the acquisition of certain investments must be added to the acquisition cost of the investment and is not recognised in the income statement as interest expense.

Net profit was 49 million euros, as compared to 34.9 million euros a year earlier.

Financing

Cash flow from operating activities amounted to 80.5 million euros, an increase of 80% from a year earlier. Acquisition of assets totalled 188.3 million euros, as compared to 77.7 million euros in 2012. The difference between cash flows from operating activities and investments was covered by reducing the volume of deposits and cash (22.8 million euros) as well as by drawing loans from the European Investment Bank (75 million euros) and Nordic Investment Bank (10 million euros).

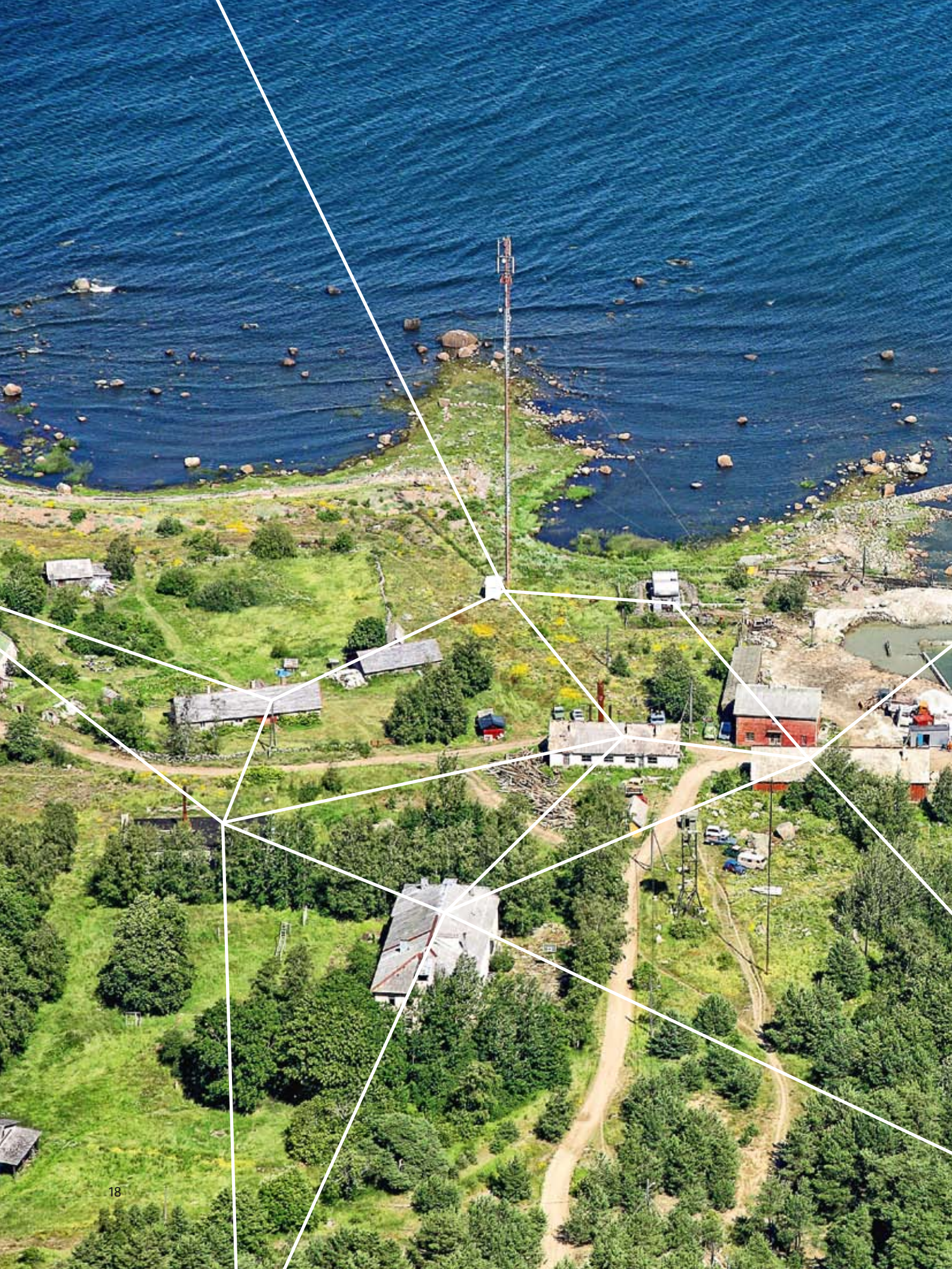
A year of record amount of investments

In terms of investment volume, 2013 was a record year, exceeding comparable levels in both the past and in the foreseeable future.

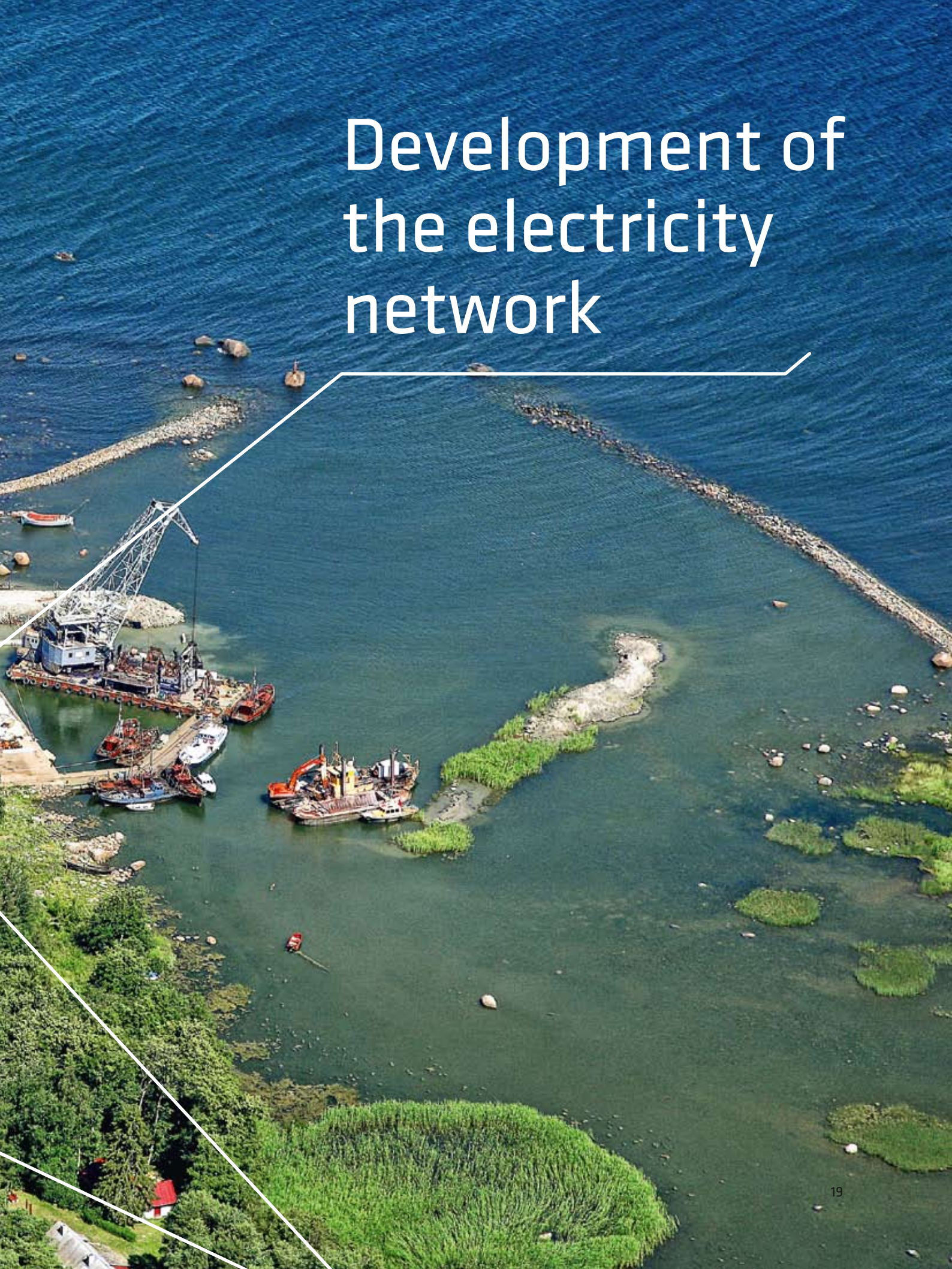
Elering has undrawn loans from the Nordic Investment Bank (35 million euros) and EU aid (35 million euros) for financing the interconnector EstLink 2 between Estonia and Finland.

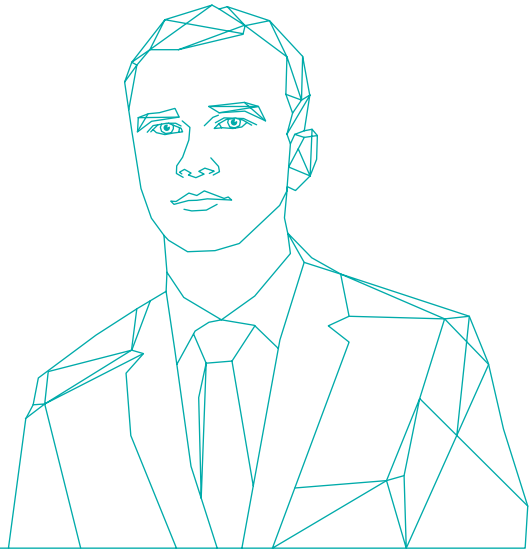
Rating agency Moody's confirmed the credit rating of Elering's long-term borrowings at a high level of A3 with a stable outlook that enables the company to borrow from the capital markets, if necessary. In the Moody's benchmark group (regulated electricity and gas infrastructure enterprises), Elering has very strong rating: 15% of enterprises had higher rating, 17% had the same rating and 68% of electricity and gas infrastructure enterprises had lower rating. Our objective is to preserve the single A credit rating also in the future.

Elering retained a high credit rating



Development of the electricity network





KALLE KILK

Member of the Management Board

The Nordic peoples have for centuries organised their life so that they spend spring, summer and autumn preparing to survive the harsh winter. In terms of developing the electricity network, for Elering the year 2013 was like the autumn season for farmers who harvest the fruits of earlier work. Several major investments that were extremely important for the security of supply and had been ongoing for several years were completed.

Without doubt, the biggest impact on the Estonian electricity system came from EstLink 2, the second high voltage direct current interconnection between Estonia and Finland that was given to the market's disposal at the start of December 2013. Already from the first days of commissioning the cable, it was clear that there was significant need for additional capacity – the load factor of EstLink 2 has been significant, on the basis of the demand and supply of the power exchange in different market areas. In addition to the fact that EstLink 2 triples the transmission capacity of the electricity market between Estonia and Finland in normal conditions, the availability of two connections, instead of one, means notably higher security of supply of the electricity system in emergency situations. In the final days of 2013, Elering also became the owner of the EstLink 1 interconnection after Elering and the Finnish transmission operator Fingrid acquired it from its previous owner, Nordic Energy Link. Therefore, the whole electricity network between Estonia and Finland is now operated by transmission system operators that serve public interests.

EstLink 2 triples the transmission capacity between Estonia and Finland

The first 110 MW stage of the emergency reserve power plant that is being built in Kiisa was commissioned in 2013. As a result, Elering no longer has to buy reserves from the Latvian electricity producer Latvenergo and the reserve power station near Tallinn increases the reliability against possible failures in the domestic electricity network, in addition to the economic effect. In preparing for the completion of the second stage of the emergency reserve power plant in 2014, most of the

Kiisa reserve power plant's second stage to be completed in autumn

equipment was manufactured and installed in 2013. The remaining activities include connecting, tuning and testing. The commissioning of the second stage with the capacity of 140 MW will also constitute the completion of the EstLink 2 project because this part of the emergency reserve power plant covers the need for additional reserve arising from the cable's high unit capacity. Since the second stage of the reserve power plant is not yet available, the capacity of interconnections from Finland to Estonia is limited to 860 MW. After the completion of the power plant, this restriction will be removed and the whole 1,000 MW capacity will be available in normal conditions for trade in both directions.

By the end of 2013, the construction of the 330/110 kV Tartu-Viljandi-Sindi line almost reached the town of Sindi. The completion of the final section between Kabli and Sindi in 2014 will significantly improve the security of supply in Western Estonia. In the course of the preparation of the construction of the Harku-Lihula-Sindi line, planning is well underway in cooperation with county governments. The completion of this line by 2020 is important both for securing domestic energy supply and for strengthening international electricity connections. Creating a strong connection between Harku and Sindi is part of building the third electricity line between Estonia and Latvia which is a key precondition not only for improving the possibilities of electricity trade, but also for connecting Baltic electricity systems to the synchronous grid of Continental Europe in the more distant future.

In addition to major investments mentioned above, renovation of existing substations and electric lines continued – the financial volume of so-called regular investments totalled 22 million euros in 2013. This amount covered smaller renovation works in substations, replacement of old power transformers by new ones and replacement of out-of-date power lines by new ones. While in terms of renovation of key substations, 2013 was an interim year, with various sites being prepared for investments, the installation of cables in the central Tallinn area was in full swing. In addition to replacing out-of-date and environmentally hazardous oil-containing cables with safer plastic-insulated cables, the replacement of out-of-date power lines with cables has also started.

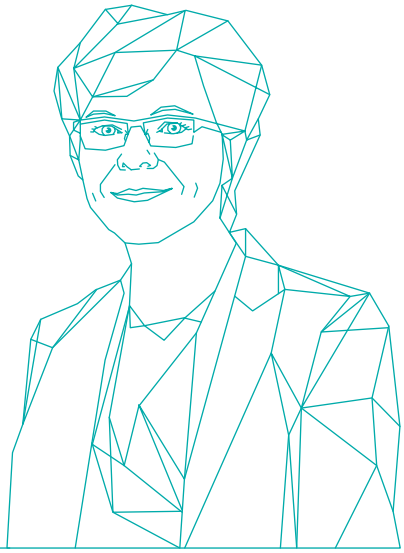
In addition to investments financed by network service consumer tariffs, networks were developed also on the initiative of customers connecting to the grid. On the basis of connection contracts, development of new connection capacities amounted to about four million euros.

Climatic conditions in 2013 offered plenty of challenges to electricity networks. There were a number of strong storms, and the number of registered cloud-to-ground lightning strikes was also notably higher than average. Although the indicators measuring the reliability of the Elering network show that the year was restless (there were more shutdowns of electrical equipment in the network than expected), it should be said that the natural forces and technical problems interrupted the energy supply to consumers less and that the undelivered volume of energy was notably below average. Both undelivered energy and equipment shutdown have an improving trend and, as a result of dedicated work, the trend is likely to continue also in the future. In the framework of the line reliability plan developed for this purpose, during 2013, line routes were expanded by about 250 hectares, corridors of one of the most important southward 330 kV lines from the Baltic substation to Tartu were expanded and individual gear was replaced in several substations.

In summary, for Elering 2013 was an exciting and successful year in terms of the development of the electricity network. Taking into account that the company's volume of assets has approximately doubled in only a few years, this will present significant challenges for Elering as a responsible owner also for the future.

In Tallinn old overhead lines are substituted by land cables

Developments of the electricity market



INGRID ARUS

Head of the Electricity Markets Department

At the beginning of 2013, Elering mainly focused on the full opening of the Estonian electricity market. During 2012, we had completed the necessary preparations, but the main challenge became the implementation of theory into practice.

Data Warehouse

We successfully completed our task to develop and implement a platform for supporting data exchange, i.e. the Data Warehouse. The objective of creating the Data Warehouse was and is to support the processes taking place in the open electricity market, mainly supplier change, forwarding of measurement data from the network operator to the electricity seller, and management of customer contracts.

52% of consumption points with electricity contracts as the market opened – the best result in Europe!

The data provided by the Data Warehouse shows that by the beginning of 2013, approximately 52% of consumption points had a valid electricity contract which is probably the best result in transition to a free market in all of Europe. This was made possible by the arrival of new electricity sellers and clearly increased competition on the electricity market.

According to the Data Warehouse statistics, approximately 90,000 additional consumption points signed electricity contracts in 2013.

In 2013, the share of consumers of electricity as a general service decreased to 7% of total consumption. As a rule, these are small household consumers.

Average market shares of balance providers in 2013 that include both the network losses of network operators and the amounts of electricity consumed as a general service are provided in the table below.

Market share by consumption of electricity	*2013 average*
Eesti Energia AS balance portfolio	**71.9%**
Elektrum Eesti OÜ balance portfolio	**10.7%**
Baltic Energy Services OÜ balance portfolio	**9.1%**
· incl. VKG Energia	1.9%
· incl. 220 Energia OÜ	1.7%
· incl. VKG Elektrivõrgud OÜ	1.2%
· incl. TS Energia OÜ	1.1%
· incl. Sillamäe SEJ AS	0.8%
· incl. AS Loo Elekter	0.2%
Nordic Power Management OÜ balance portfolio	**2.4%**
· incl. Imatra Elekter AS	1.4%
· incl. Eesti Gaas AS	0.1%
Elektrimüügi AS balance portfolio	**1.4%**
Inter Rao Eesti OÜ balance portfolio	**0.2%**
Balance porftolio of Elering's grid losses	**4.3%**

Regional development

On the regional level, Elering is focusing mainly on the distribution and calculation of cross-border transmission capacities both on the borders within the Baltic States and on the borders with third countries.

The trilateral agreement between transmission system operators was signed on 15 March 2013. According to the agreement, the total cross-border transmission capacity is distributed between the Baltic countries by

implicit auction on the Nord Pool Spot (NPS) platform. The transmission capacity allocated for trading on the border with third countries is also distributed by NPS in the area set up on the Lithuanian-Belarusian border. No transmission capacity is allocated for the Estonian-Russian and Latvian-Russian border for trading.

The principles included in the trilateral agreement were approved before they were implemented by Baltic regulators. At the same time it was emphasised that transmission system operators were obliged to monitor congestion on borders and, if it occurs, to take additional measures for hedging risks of market participants. In accordance with the agreement, Elering developed in cooperation with the market participants and the Latvian transmission system operator Augstprieguma tīkls (AST) a product that is called limited PTR (Physical Transmission Right).

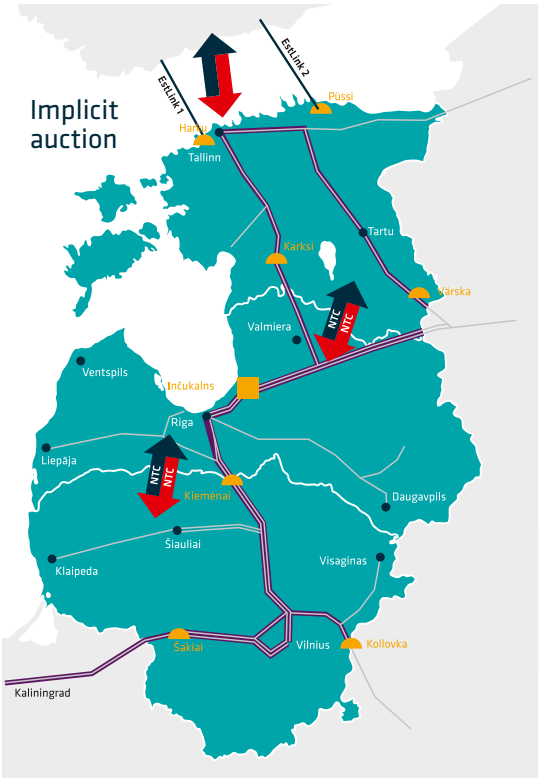
Limited auction of PTRs on the Estonian-Latvian border

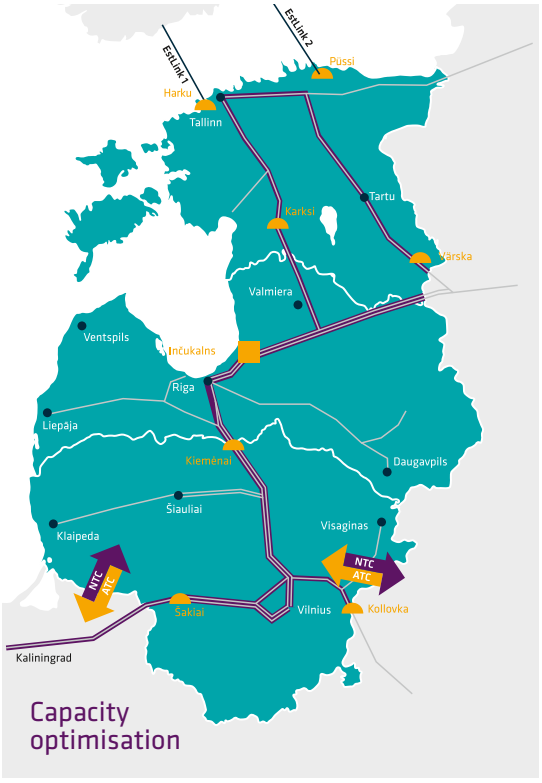
In accordance with the agreement between Estonian and Latvian transmission system operators Elering and AST, a direct limited distribution system of capacities is partially implemented on the Estonian and Latvian border starting from 2014 that enables market participants to additionally hedge regional price risks and/or to prevent price volatility. The first auction was held on 13 December and was attended by seven market participants, four of which made successful bids.

The sale of PTRs takes place at the terms of mandatory re-sale of capacity. Transmission system operators pay market participants a fee for re-purchased transmission capacity, the level of which is equal to the difference in the price of electricity on the power exchange in the corresponding period between the Estonian and Latvian price areas of NPS. Transmission system operators give the transmission capacity they

PTRs on the Estonian-Latvian border allow market participants to further hedge price risks

Cross-border transmission capacities´ allocation on the borders between the Baltic States





have repurchased from market particants to NPS for distribution on the day-ahead market. Therefore, the distribution mechanism that has been introduced does not reduce the total volume of transmission capacities distributed by NPS.

Summary of 2013 in the NPS Estonia price area

- Average price in NPS Estonia price area was 43.14 EUR/MWh;
- Average NPS system price was 38.10 EUR/MWh;
- Estonian market participants purchased from the day-ahead and intraday market electricity for internal consumption a total of 91.3% of consumption, i.e. 7.3 TWh;
- On 3 June, the price area of NPS ELE was closed and the NPS Latvian price area was opened for day-ahead trading;
- In connection with the opening of the NPS Latvia price area, the weekly explicit auctions on the Estonian-Latvian border were ended in June 2013 and the total capacity is provided by Elering and AST to NPS for allocation by implicit auctions;
- Prices of NPS Estonia and NPS ELE/ Latvia price area converged in the day-ahead market for 67% of hours;
- NPS Estonian and NPS Finnish prices converged in the day-ahead market for 69% of hours;
- On 6 December, in the framework of a trial operation period, the EstLink 2 interconnection that connects the Estonian and Finnish system areas was commissioned, ensuring maximum transmission capacity of 850 MW from Finland to Estonia and 1,000 MW from Estonia to Finland.

In 2013, the highest prices on the NPS power exchange were in the Baltic price areas (NPS Estonia, ELE/Latvia and Lithuania). From January until May, NPS system prices and Estonian prices were similar. Larger gaps between the NPS Estonian price and the NPS system price occurred after the opening of the NPS Latvian price area which also overlapped with the start of the summer period. The main factor influencing NPS Estonian, Latvian and Lithuanian prices is high demand by market participants from Latvia and Lithuania which do not have sufficient production capacities at competitive prices, especially in the summer (there is lack of hydropower and co-generation plants operate on low loads in the summer period).

Unlike in earlier years, there was a significant price difference between the NPS Estonian and NPS Latvian/ ELE price areas also in September and October. The cause for price differences was partly the reduction in the transmission capacity between Estonia and Latvia because of the shift of line maintenance works from summer to autumn, but the main cause was the lack of sale offers made to the Latvian and Lithuanian market.

NPS Estonia

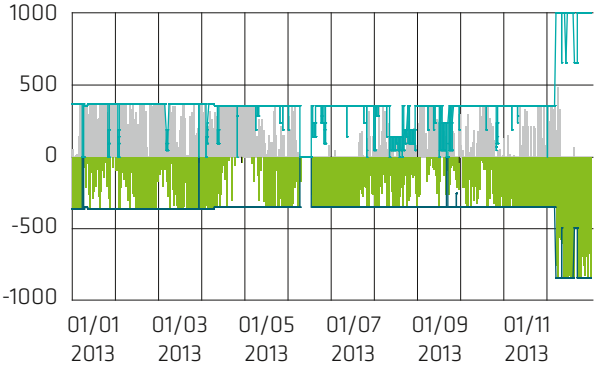
	2013	*2012*	*2011*
Openness of the electricity market (%)	100 %	37,6 %	33,2 %
Eligible consumers	all	213	201
Volumes of electricity bought in NPS EE price area (TWh)	7,3	6,0	4,6
Volumes of electricity sold in NPS EE price area (TWh)	10,7	4,9	5,8
Congestion income from implicit auction between Estonia and Finland (MEUR)	7,40	12,94	19,58
Congestion income from implicit auction between Estonia and Latvia (MEUR)*	28,24	6,52	-
Congestion income from explicit auction between Estonia and Latvia (MEUR)**	0,17	1,54	0,40

** Since the NPS ELE price area was created on June 18, 2012*
*** Since June 3, 2013, the total capacity is allocated through an implicit auction*

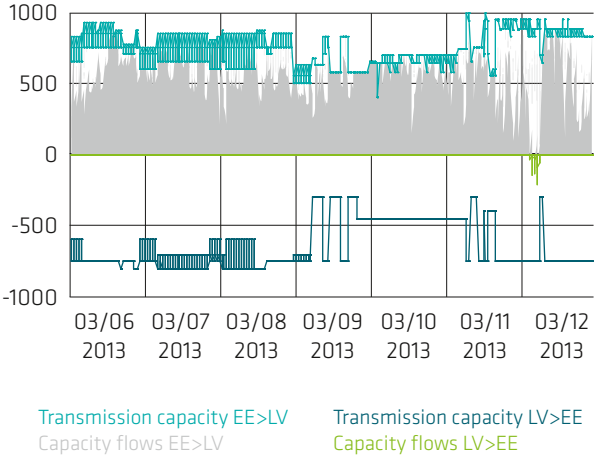
2013 (EUR/MWh)	*Average price*	*Max price*	*Min price*	*Average price in 2012*
NPS System	38.10	109.55	1.38	31.20
NPS Finland	41.16	210.01	1.38	36.64
NPS Estonia	43.14	210.01	5.08	39.20
NPS Latvia*	52.40	210.01	5.08	-
NPS ELE*	42.84	109.55	8.75	42.63**
NPS Lithuania	48.93	210.01	3.09	45.50**

** NPS Latvia price area was opened on 3 June 2013 and at the same time the NPS ELE price area was closed*
*** NPS ELE and Lithuania price areas were opened on 18 June 2012*

Power flows on the Estonian-Finnish border in 2013 (MW)



Power flows on the Estonian-Latvian border in 2013 (MW)



In 2013, the NPS Estonian and ELE/Latvian region prices were equal for 67% of the hours and NPS Estonian and Finnish prices were equal for 69% of the time (2012: 63%). In 2013, Estonia's average price was 1.98 EUR/MWh higher than the Finnish average price. Between 3 June and 31 December it was 9.26 EUR/MWh lower than the average NPS Latvian price.

In 2013 the power flows from Estonia to Finland and from Finland to Estonia varied considerably since NPS Estonian and Finnish prices were equal for 69% of the time or 6,060 hours. From June 10-19, the EstLink 1 interconnection was in planned maintenance and no trading took place between Estonia and Finland.

In 2013, power flows between Estonia and Latvia were mainly directed from Estonia to Latvia, the only exception being during the high water levels in Latvia. Until 3 June 2013, 20% of the Estonian-Latvian transmission capacity was allocated by Estonian and Latvian transmission system operators - Elering and AST – on weekly explicit auctions, and 80% was allocated by implicit auction in the day-ahead market managed by NPS. Starting from 3 June, the whole power has been allocated by NPS by implicit auction.

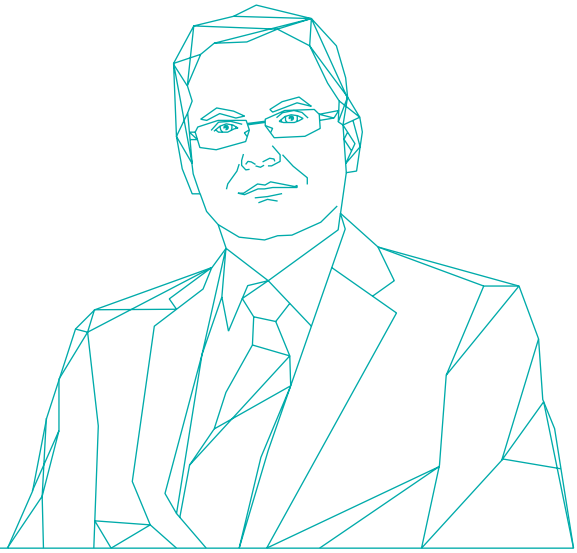
On the basis of day-ahead trading results in 2013, the NPS Estonia and NPS Latvia connections were allocated as the maximum during 33% of hours. After intraday trading, actual shortage of transmission capacities occurred in 10% of hours.

Elbas – intraday trading

On 10 December 2013, NPS together with the Latvian and Lithuanian TSOs opened the Elbas platform in their areas. The transmission capacity between Estonia and Latvia was given to the Elbas platform at the start of 2014.

In 2013, volumes purchased from the Elbas market totalled 109 GWh which is 1.5% of the total volume purchased in the Estonian price area. Sold volumes amounted to 57.5 GWh which is 0.5% of the all volumes sold in the Estonian price area of Elspot and Elbas.

Operation of the Estonian electricity system



MÄRT ALLIKA

Head of Power System Control Centre

As an electricity transmission system operator, Elering is responsible for planning the reliable operation of the entire Estonian electricity system and managing it in real time in order to ensure the operation of the transmission network, maximum cross-border transmission capacities and balance between output and consumption. The control centre of the electricity system meets these objectives on a daily basis. The reliability of the electricity system is constantly being analysed. The assessment covers the impact of the tripping of an electricity transmission line, a direct current interconnection or a generator on the functioning of an electricity system or, for instance, changes in consumption as compared to the planned levels. It is important to be ready to address all these possible events. In certain cases it is necessary to deploy preventive measures, while there must be contingency plans for events that have already taken place. All these activities ensure that Estonian consumers do not have to worry about the electricity supply.

Operation of the electricity system in 2013

The management of the operation of the Estonian electricity system in 2013 was quite similar to that in the earlier years. Renovation of transmission lines and main substations that are important for the operation of the Estonian electrical system continued. This meant solving two opposing tasks simultaneously – to enable outages of electrical equipment for safe renovation works and to ensure reliable operation of the electricity system. Such tasks included plenty of challenges in planning the operation of the electricity system and for people involved in renovation works. As shown by the results of 2013, these two tasks were completed successfully owing to good cooperation of all parties.

For Elering, 2013 was the first year when all network losses were purchased from the power exchange. The bigger part of losses were purchased from the day-ahead power exchange and within the day the losses were adjusted – either by purchasing more electricity to cover the deficit or selling back the surplus to the power exchange. In addition to carrying out acquisition and sale transactions of network losses, it was necessary to notably improve the process of forecasting losses. An application was implemented that in addition to forecasting day-ahead network losses also specifies the forecast during the day, on the basis of the latest available data about the expected operational state of the electricity system.

In 2013 all network losses were purchased from the power exchange

Cross-border power flows

The Estonian electricity system belongs to the same synchronous area together with the electricity systems of Latvia, Lithuania, Russia and Belarus. In addition, Estonia has direct current connections with the Finnish electrical system. The existence of these cross-border connections means that the Estonian electricity system is strongly integrated into the electricity systems of its neighbouring countries. This also means that we are influenced by what is happening at our neighbours', and vice versa. Accurate planning of physical cross-border flows and keeping them within the necessary limits for ensuring the reliable functioning of the electricity system can be successful only in close cooperation with the transmission system operators of neighbouring countries.

In terms of cross-border capacity flows, 2013 followed a similar trend that developed after the closure of the Ignalina nuclear power plant in Lithuania where physical power flows move through Baltic countries from north to south. This was particularly visible in December 2013 when the transmission capacity of EstLink 2, the second DC interconnection between Estonia and Finland, was given to the market's disposal, creating a possibility for large-scale transit of Nordic electricity through Estonia into Latvia and Lithuania.

In terms of real-time management of the operation of the electricity system, the biggest problems are cross-border lines between Estonia and Latvia. In 2013, to avoid congestion and ensure reliable operation of the electricity network, the Estonian and Latvian transmission system operators had to use countertrade, i.e. to jointly activate reserve capacities in order to return the power flows of those electricity transmission lines within the allowed limits. In 2013, countertrade totalled 329 hours. Overloads were mainly caused by a big deficit of the Latvian and Lithuanian electricity systems and the impact of the Russian electricity system on the operation of the electricity networks of Baltic countries.

The deficit of the electricity systems of Latvia and Lithuania also influenced commercial electricity flows between the countries. Commercial electricity flows between Estonia and Finland accounted for 67% of the hours from Finland into Estonia. 30% of the hours were from Estonia to Finland and 3% of the hours no transmission took place. At the same time, the direction of commercial power flows between Estonia and Finland could change several times within a day. Commercial electricity flows between Estonia and Latvia were from Estonia to Latvia 94% of the hours, and from Latvia to Estonia 6% of hours.

Maximum and minimum consumption and output in the Estonian electricity system in 2013

	Value	*Period*
Maximum net consumption in Estonia	1433 MW	18.01.2013 at 17.45-17.50
Minimum net consumption in Estonia	481 MW	07.07.2013 at 04.40-04.45
Average net consumption in Estonia	906 MW	
Maximum net output in Estonia	2052 MW	30.01.2013 at 16.10-16.15
Minimum net output in Estonia	497 MW	14.07.2013 at 23.15-23.20
Average net output in Estonia	1317 MW	
Maximum output of wind parks	230 MW	23.10.2013 at 16.10-16.15

Outlook into 2014

In 2014, one of the largest changes to impact the management of the electricity system operation is the notably increased transmission capacity between Estonia and Finland. After the official commissioning of EstLink 2, the second DC interconnection between Estonia and Finland in February 2014 the technical transmission capacity between Estonia and Finland increased to 1,000 MW in both directions. This means higher cross-border and domestic power flows and higher changes in power flows in transition from one hour to another.

With the activation of EstLink 2 the transmission capacity between Estonia and Finland has increased considerably

Starting from the beginning of 2014, Elering is operating the first of the two Kiisa emergency reserve

power plants. In autumn, the second plant with a capacity of 140 MW will be added. Real time management of reserve emergency power plants from the control centre is a new task for Elering.

Taking into consideration the increase in the transmission capacity between Estonia and Finland, and the deficit of the electricity systems of Latvia and Lithuania, it can be safely assumed that the management of Estonian-Latvian cross-border power flows will remain in the focus also in 2014.

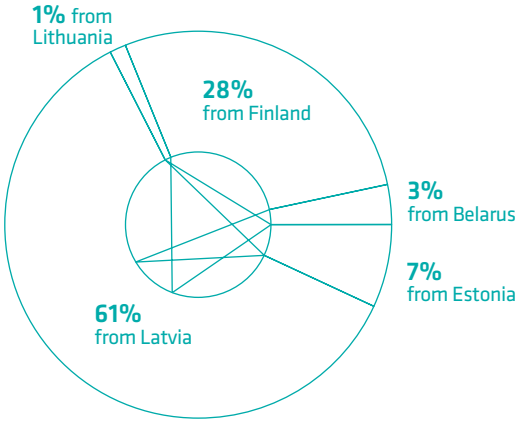
In addition, it is planned to launch in 2014 a procurement process for a new control system (SCADA) for the needs of real time control of the Estonian electricity system, and to create possibilities for training control centre operators in an environment as similar as possible to that of real-time daily operation of the electricity system.

Balancing deliveries

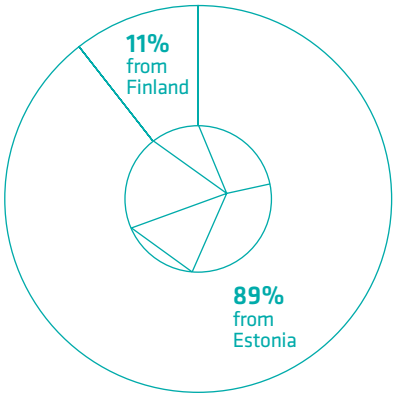
The fact that in 2013 the Estonian electricity market was opened also to household consumers meant significant changes in the portfolios of balance providers. In annual terms, the volume of total domestic imbalance energy increased 28% as compared to 2012. Annually, the system operator sold a total of 288 GWh of domestic imbalance energy and purchased 286 GWh of excess domestic imbalance energy.

Due to the increase in the domestic imbalance, the volumes of balancing deliveries made by the transmission system operator for ensuring the capacity balance also increased, whereas the volumes of upward regulation deliveries increased approximately by half and the volumes of downward regulation deliveries more than doubled. In annual terms, upward regulation deliveries and activation of emergency reserves were purchased for balancing the system in the total volume of 48 GWh and downward regulation deliveries were sold in the total volume of 45 GWh.

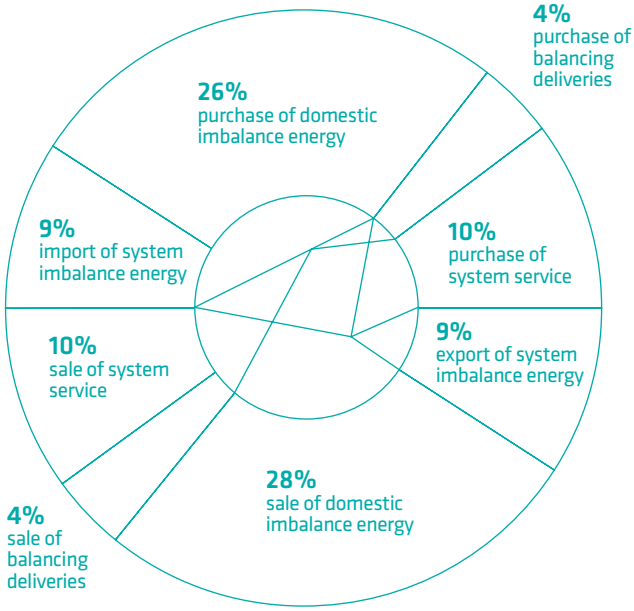
Upward regulation deliveries purchased in 2013



Sale of downward regulation deliveries in 2013



Balancing deliveries in 2013



In comparison with 2012 when the cross-border system imbalance was mainly on the export side, the import and export volumes of system imbalance energy in 2013 remained on the same level, at 98 and 100 GWh, respectively.

Mediation of regulating service to neighbouring transmission system operators amounted to 56 GWh, which is 9% less than in 2012. Mediation of regulation services included, as earlier, offering the regulating service through the EstLink 1 cable to the Finnish transmission system operator and the mediation of regulating service to the Lithuanian transmission system operator.

Prices of imbalance energy

In 2013, the highest price of imbalance energy was 279.39 EUR/MWh, caused by a high price of upward regulating delivery on 9 September at 08.00-09.00.

The lowest price of imbalance energy was 3.90 EUR/MWh that was recorded on 26 May at 08.00-09.00 as the downward regulation price for balancing Estonia.

Prices of imbalance energy (€/MWh)

	Average price	*MAX price*	*MIN price*
Prices of imbalance energy in 2013			
Sales price of imbalance energy	51.11	279.39	10.10
Purchase price of imbalance energy	46.93	121.90	3.90
Prices of imbalance energy in 2012			
Sales price of imbalance energy	41.75	168.82	9.50
Purchase price of imbalance energy	39.26	95.80	1.90

Elering and the environment

Elering is an infrastructure enterprise with strategic importance and our core business – to ensure the security of supply of Estonian electrical energy - is directly related to the environment and has a significant impact on it. Environmental protection is part of our relationship with the society and is linked to the wider responsibility in the principles and values of Elering's activities. Therefore, constant assessment of environmental impact, both in the specific legal sense and in the wider comprehensive sense is the natural part of our daily operations.

Environmental protection is linked to the wider responsibility in the principles and values of Elering's activities

For limiting the environmental footprint, it is important to further develop current measures and to find new measures. An assessment of environmental risks is an important part of the company's annual risk analysis.

Elering is guided in its activities by the following principles of environmental responsibility:

- We inform our staff and suppliers of legal and other environmental requirements and ensure that we comply with them;
- We avoid environmental pollution and reduce waste by using the best available technology;
- We consume resources in a sustainable manner;
- In tender documents we insist that suppliers act in an environmentally responsible manner and use environmentally sound technologies;
- Overview of the environmental impact related to the activities of Elering is published on the company's website

Environmental impact of construction of lines

Understandably, the construction and maintenance of high-voltage power lines has a significant environmental impact. Elering owns in Estonia more than 5,000 km of overhead power lines. They are divided into three voltage classes: 110 kV, 220 kV and 330 kV. The surface area of the company's line corridors is 26,600 hectares. Every power line has a protection zone which includes land, air or water body around various electrical installations, the use of which is restricted for safety purposes. The extent of the protection zone depends on the voltage of the specific electrical installation – in case of 110 kV voltage lines it is 25 metres to both sides from the line axle and 40 metres for 220 kV and 330 kV voltage lines.

The objective of developing and maintaining line corridors is, in addition to ensuring quality electricity supply, to reduce the danger of power lines to the surrounding environment and people. Trees falling on the power lines can cause extensive damage – it can start forest fires, and trees that remain under live voltage are dangerous to people and animals in the area. To partially offset the impact of felling trees in line corridors, Elering's staff has participated in tree planting campaigns and helped to restore semi-natural habitation.

To increase the reliability of power lines, Elering is installing bird barrier systems that also protect birds from getting into contact with high-voltage lines. In 2013, bird barriers were installed on 828 masts of nine Elering lines in the total length of 198 kilometres.

On new power lines such as Tartu–Viljandi–Sindi, the overhead power lines that are located in bird migration paths are equipped with so-called marker balls that enable birds to notice obstacles early and to prevent collision with overhead power lines.

Elering continues to collect and dispose materials that have been left in nature in the course of rebuilding of power lines in earlier decades including used insulators or parts of line masts. Last year almost 50,000 euros were spent on these activities.

Electromagnetic fields

The transmission of electricity in overhead power lines creates electric and magnetic fields the strength of which depends on the voltage and on how much current is passing through the line at a given time. The field is stronger in the immediate vicinity of the line, and further away the field strength decreases significantly. Values of electromagnetic fields in the protection zone and in the near vicinity of Elering's existing overhead power cables are significantly below the established limits.

New overhead lines

New overhead lines that are being developed will be fitting the surrounding environment better by being less visible. All masts are galvanized, i.e. grey-white or silver in colour and the upper layers of cables are made of aluminum wire which is also grey-white or silver in colour.

Underground cable lines

For increasing safety and reducing visual pollution, Elering has launched the project „Overhead power lines to underground cable" in Tallinn in which the company will in the next few years replace several tens of kilometres of almost obsolete out-of-date power lines with new cables. There is another significant project containing an environmental aspect underway in Tallinn – in the next few years we will replace obsolete and environmentally hazardous cables in Volta-Ranna and Ranna-Ida sections with new and oil-free cables.

Environmental impact related to substations

Elering owns 145 substations, in which the biggest environmental hazard is oil that is used in transformers and other gear, and sulfur hexafluoride (SF6) that is used as an electrical insulator. As at the end of 2013, Elering had 5,986 tons of oil and 10,845 kilograms of SF6 in its gear. To detect possible leaks of SF6, Elering acquired a measurement camera in 2013 that cost approximately 100,000 euros.

Investments into oil separation equipment of substations

2013 marked the completion of a project that took almost 10 years to complete concentrating on installing oil separation systems for collecting oil that can leak out of transformers. The last systems to be replaced were oil separation systems in Audru, Mõniste and Risti substations that cost approximately 90,000 euros last year. In addition, tens of thousands of euros are spent annually for the disposal of oil and other environmentally hazardous substances and for maintenance of oil separators.

In addition, Elering will replace for safety reasons the oil-filled power switches used in substations with environmentally friendlier ones. Persons in control of substations are constantly monitoring environmental risks of substations.

Noise

Noise can be a significant source of pollution and Elering is aware of it. All new transformers will be built according to strict regulations, preferring suppliers of transformers with lower noise levels. Permitted noise levels are especially strict on nature protection areas. For reducing the distribution of noise, Elering has in critical locations equipped transformers with noise barriers. In a year, Elering conducts 3-4 noise measurements and these prove that the noise level is in the permitted range.

Environmental activities in developing the electricity system

Environmental impact assessment of projects and notification of interested persons is an inseparable and significant part of all developments of new electrical systems of Elering. Assessment of environmental impact is a process in which the expected environmental impact of the planned activity is explained, assessed and described, the possibilities for preventing or alleviating the impact are analysed and the most suitable solution is determined. Including the public through public debates is the best way for interested persons to participate in the assessment of environmental impact and enables to find a common part at an early stage of a project.

Tartu–Viljandi-Sindi overhead power line

In addition to the environmental impact assessment for building the Tartu–Viljandi-Sindi overhead power line, an environmental report is prepared twice a year. The report analyses and provides an overview of environmental protection activities and results during the reporting period and lays down the priorities for the next period. In 2013, the priority was on the third stage of construction works, as well as marking of lines for birds, and maintenance of ground under masts. Since the next, fourth stage from Kilingi-Nõmme to Kabli includes land in protected nature areas, the next report will focus on construction works in areas that are inhabited by species that fall under the second protection category and Natura areas. In addition, construction works are being monitored for crossing rivers, building temporary roads, maintaining the surroundings of masts and for liquidating the traces of construction activities in areas of natural heritage and valuable habitats.

Strategic assessment of environmental impact is being carried out also in preparing the construction of the new Harku–Lihula–Sindi 330/110 kV high-voltage line.

Emergency reserve power plant

The Kiisa emergency reserve power plant belonging to Elering is included in the category B of enterprises liable to be affected by major accidents. Elering as the operator of the Kiisa power plant has developed a set of measures that must ensure operative response in case of accident. The emergency reserve power plant that will be completed in 2014 operates on natural gas and diesel fuel. For operating the plant, Elering must purchase carbon dioxide quota from the local market. The total volume of these quotas depends on the frequency and length of operation of the plant. All motors of the plant must be switched on for testing at least once a month. To operate every motor of the plant for one hour, the company must buy 5.1 tons of carbon dioxide quotas.

For operating the plant, Elering must purchase carbon dioxide quota from the local market

Research and Development

Starting from 2012, Elering has prepared an annual research and development (R&D) plan. The European Association of Transmission System Operators for Electricity (ENTSO-E) has been focusing increasingly on R&D since 2010. The European Union set requirements for R&D with the Third Energy Package, setting forward tasks for Member States, regulators and network operators.

Pursuant to the European Parliament and Council Regulation EC/714/2009, ENTSO-E has been made responsible for preparing research plans and provide R&D activities in its workplan. In accordance with this obligation, ENTSO-E prepared its first R&D plan targeted at European electricity transmission system operators in 2010 and updated it at the end of 2011. The current R&D plan 2013-2022 was published at the end of 2012: https://www.entsoe.eu/fileadmin/user_upload/_library/news/R_D_release/121217_ENTSO-E_R_D_Roadmap_2013_2022.pdf

A more detailed R&D implementation plan 2014-2016 was prepared as a separate document to the R&D plan: https://www.entsoe.eu/fileadmin/user_upload/_library/news/R_D_release/121220_ENTSO-E_Implementation_Plan_2014-2016.pdf

Also the European Commission has considered it necessary to finance R&D through its R&D framework programmes and other financing measures. Since framework programmes concern financing of cross-border projects, means for own financial contributions and financing of projects of domestic importance must be allocated from the transmission tariff.

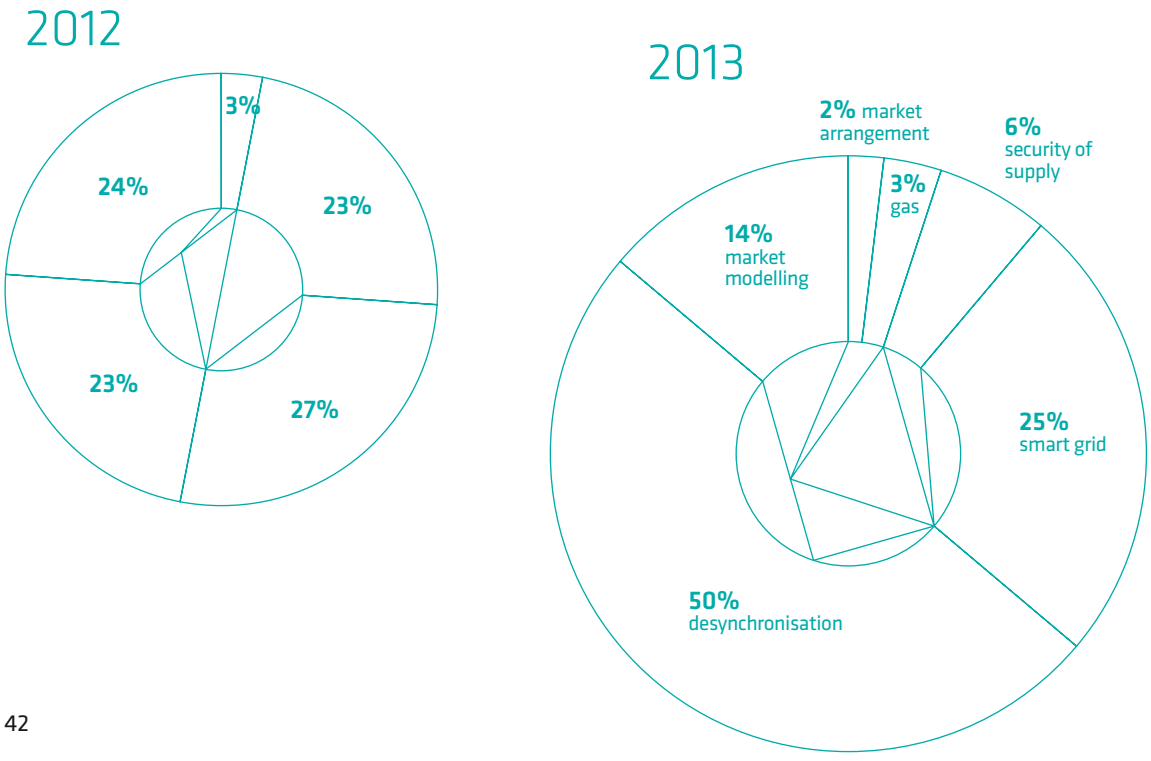
Directive 2009/72/EC lays down that the tariff for grid companies established by the regulator (Estonian Competition Authority) must be a sufficient incentive for contributing to R&D.

Costs of R&D and other technical studies 2012-2013

in thousands of euros	*2012*	*2013*
Development activities	7	11
Basic and applied research	176	284
Total R&D	**182**	**296**
Technical and commercial studies	202	405
TOTAL	**384**	**701**

The table above provides a summary of expenses related to R&D and other studies from 2012 and 2013 according to the functionality of expenses. Figure 1 shows the share of spending on R&D and other studies by research topics. Smart grid projects include consumption control, development of the WAMS system and projects dealing with electrical transport.

Share of R&D and expenses of other studies by sectors, 2012-2013



The table below provides the most significant research projects of Elering (research and development and other technical and commercial studies) that were carried out or initiated in 2012 and 2013, including project costs. Future expenses include only expenses approved by the research plan of Elering. The table below provides an overview of expenses to outsourced studies. The figures do not include labour costs, IT development costs, travel expenses, office expenses, etc.

Actual expenses related to R&D and other studies in 2012-2013 and forecast expenses from 2014

Cost, in thousands of euros

Project name	***2012***	***2013***	***2014 and later***
Quantitative study on energy market scenarios	82.5	82.5	0.0
Analysis of consumption patterns and possibilities to manage consumption	47.0	43.6	42.6
Analysis and development of the WAMS system	0.0	87.5	250.0
Impact of electric transport on the electricity system	14.1	48.4	50.0
Feasibility study on integration to the synchronous grid of Central Europe	103.2	363.0	0.0
Study of short-circuit currents caused by trees	0.0	10.5	0.0
Studies on market functioning and developments	0.0	12.0	150.0
Energy Data Feed Platform	0.0	8.5	27.5
Power to gas	0.0	0.0	50.0
Synchronisation with Continental Europe and reduction of technical dependence from third countries	0.0	0.0	50.0
Network planning model depending on the optimal level of total public expenses	0.0	0.0	40.0

Below are short descriptions of the projects that have been launched and carried out in 2013 (research and development projects and technical and commercial studies).

Quantitative study on energy market scenarios
The study was conducted as part of the process of updating the development plan of the Estonian energy sector. In 2012, Elering, the Ministry of Economic Affairs and Communications, Estonian Development Fund and Enterprise Estonia signed a cooperation agreement for updating the energy sector development plan. It was agreed that significant input in updating the development plan will be the modelling and analysis of possible long-term development scenarios. In the course of the project, several possible energy market development scenarios for Estonia and the whole Baltic Sea region until 2050 were modelled.

Analysis of consumption habits of large consumers and possibilities of managing consumption
Elering is analysing consumption schedules to get an overview about consumer behaviour and to offer more cost-effective solutions that benefit both customers and Elering. In the course of mapping consumption it is determined whether Elering's customers and large electricity consumers would be capable of offering system services to the network operator.

WAMPAC – analysis and development of the WAMS system
The objective of the project is to study the application of the WAMS system and its possible future development as well as to develop the electricity network operated by Elering in the most optimal manner. The goal is to study the possibilities of the wide measurement system in the wide control system of the electricity network that could improve the quality of operational planning, control and protection. The project gives an overview of the new concept of the control system and analyses its parametres if it is implemented in Elering's control system. One part of the study is dedicated to the applications of emergency-related automated systems on the basis of WAMS/WAMPAC system.

Electricity transport and its impact on the functioning of the electricity system
The objective of the project is to study the impact of large-scale electricity transport on the Estonian electricity system and on the energy sector as a whole. More specifically, the focus will be on the two main electricity transport systems that are being developed, i.e. electrical vehicles and the planned interstate high-speed railway project Rail Baltic.

Feasibility study on joining the synchronous grid of Continental Europe
In cooperation with Baltic transmission system operators, a technical and socio-economic feasibility study was conducted on the possibility to connect Baltic countries to the EU common market on electricity.

Study on short-circuit currents caused by trees
The objective of the project was to identify the safety of Elering's 110 kV lines in case of trees falling on them and to study measures for improving safety.

Studies on market arrangement and development

- In 2013, a feasibility analysis on the use of financial instruments on the Baltic electricity market was conducted.
- In 2014 it is planned to carry out a study on long-term market development with a focus on the impact on Elering and Estonian market participants of possible long-term developments on the European electricity market including the capacity market, subsidies, carbon dioxide price, etc.
- In 2014, it is planned to analyse the functioning of the Baltic electricity market with the view of studying the current situation and to make recommendations on how to improve it in order to ensure efficient functioning of the Nordic-Baltic electricity market and to achieve what has been agreed in the Baltic Electricity Market Interconnection Plan (BEMIP).

The Energy Data Feed Platform allows to monitor energy consumption and exchange information between electricity producers and consumers

Energy Data Feed Platform

The project is an initiative to shape, implement and test an open software platform that can be used for monitoring and managing consumption. The objective is to enable two-way communication with electricity networks, make data flows available in order to analyse energy consumption and to have more optimal investments into the electricity production and networks. The project aims to build a software platform for integrat-ing various data sources and to offer suitable services in order to change data into valuable information in managing, auditing and comparing energy flexibility.

Power to gas

The project studies solutions for recycling carbon dioxide created when burning fossil fuels and the possibilities of storing renewable electricity. By synthesising carbon dioxide and the surplus renewable energy in water vapour, it is possible to produce methane and methanol.

Synchronisation into the grid of Continental Europe and reducing technical dependency on third countries

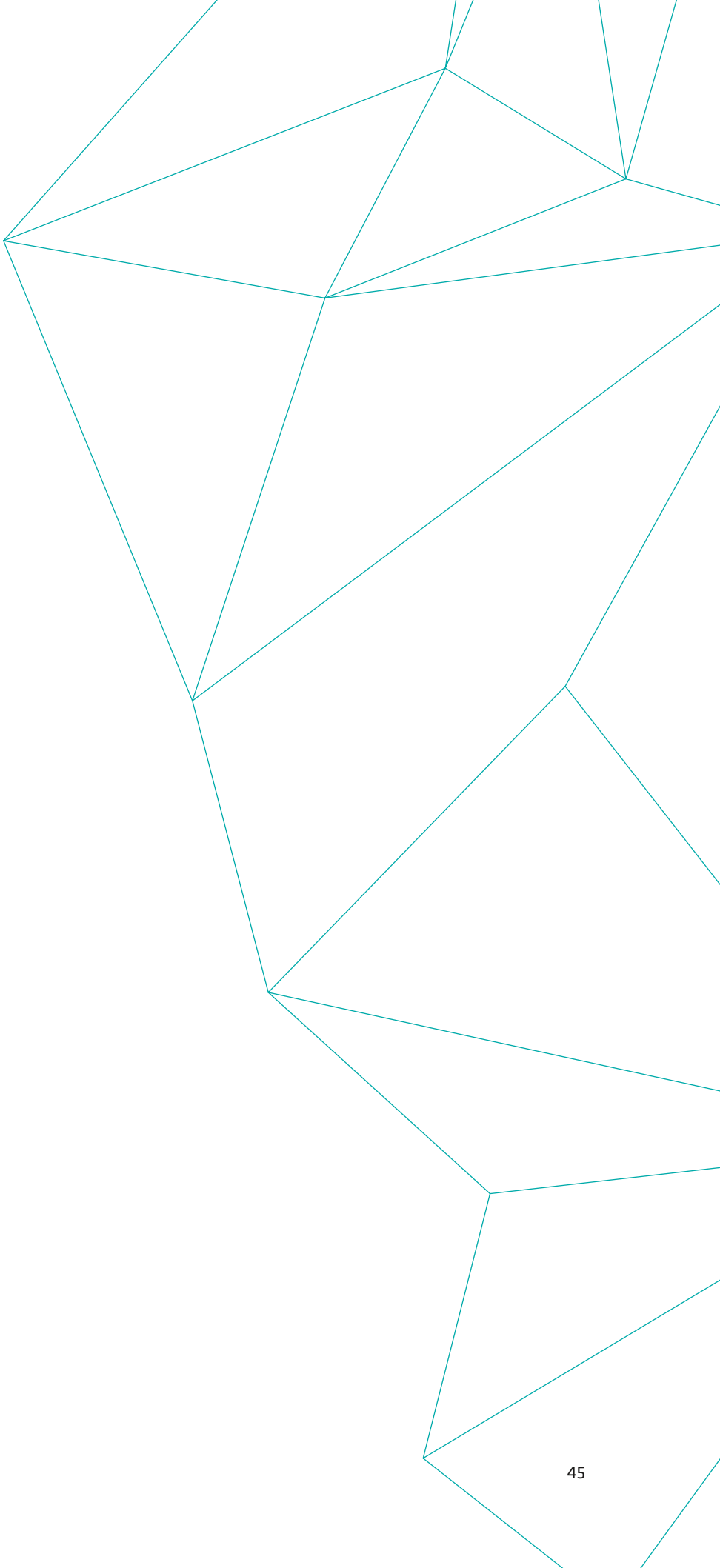
The study looks at both the period when Estonia is synchronised to the Russian system and the period when Estonia will be synchronised to the grids of Continental Europe or Scandinavia. In the course of the study, various options are considered with regard to domestic technical solutions and the needs for retuning/rebuilding power plants in different time horizons and synchronising options.

Methods and model development for network planning and preservation depending on the optimal level of total public costs in supplying electricity

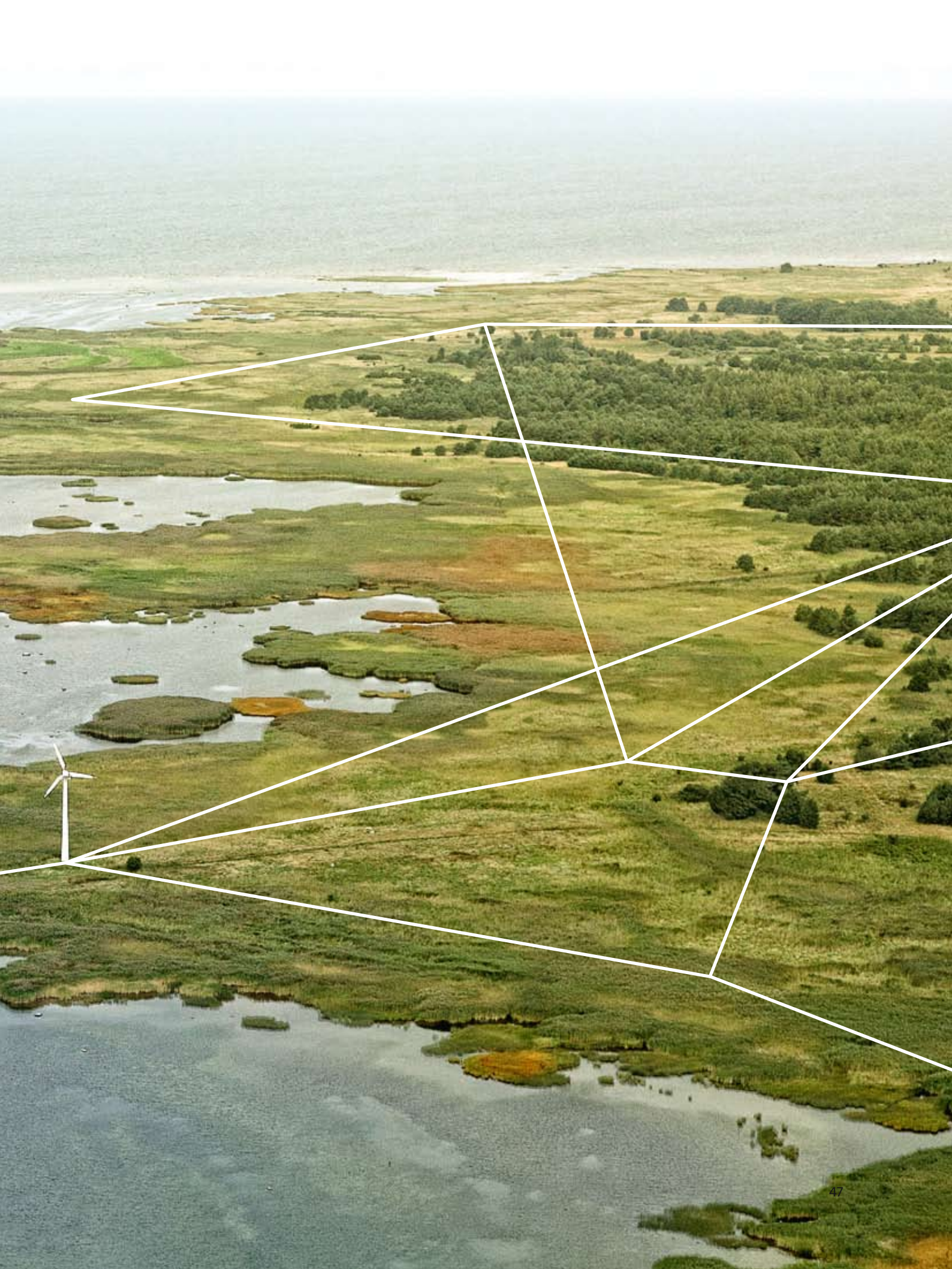
The objective of the study is to look at the security of supply criteria, considering the direct costs related to planning investments and network operation and the likelihood and impact of positive and negative external influences. A model for assessing the fulfilment of security of supply criteria is being developed. The model will be tested by connecting Hiiumaa to the „main grid".

On the basis of a government resolution, Elering spent 35,000 euros last year on carrying out studies and analyses for developing gas-related competence.

More information about studies carried out by Elering is available on the website at: http://elering.ee/research-and-development



Elering and social responsibility



As a guarantor of the security of supply of Estonia's electricity, Elering must be open to the whole public. At the same time our main day-to-day cooperation partners and customers are a relatively small number of distribution network enterprises, electricity producers and large electricity consumers. Our success depends on the competence of people, both the staff of Elering and employees of our partners and customers. We cooperate with universities to promote the development of energy-related thinking in Estonia as well as the studies, research work and self-development of outstanding students.

Elering as a competence centre

It is important for a competence centre in energy issues to distribute the know-how about the energy sectorand to introduce the key challenges and essential problems it is facing. This includes raising awareness through both mass media and specific publications and workshops. In its security of supply and production sufficiency reports, Elering provides an annual estimate of on the most important indicators of the Estonian electricity system.

In line with the vision of Elering, we look for and develop new business lines for making the Estonian energy sector more innovative and competitive. The competence centre encompasses active participation in research and development projects, promotion of energy education and raising the general awareness on key energy-related issues.

We see Elering as part of a network encompassing universities, state agencies, system operators of other countries and other partners. The main cooperation forms in research and development activities were determined by our framework contracts with Tallinn University of Technology in 2011 and with the University of Tartu in 2012. Elering also commenced the updating of the national energy strategy with the other parties in 2012.

Participation in the work of the Research and Development Committee gives a possibility to have an active say in prioritising the development directions of the European energy sector, which are set out in the research and development roadmap and implementation plan both regularly prepared by ENTSO-E.

Grants awarded in 2013

Elering awards grants and makes donations in accordance with the State Property Act and the company's internal rules. The grants must contribute to the achievement of Elering's operational and financial targets the security of energy supply in order to guarantee to Estonian consumers at all times. As a socially responsible company, Elering awards grants to guarantee security of energy supply, promote energy related education and raise general awareness of energy through:

- paying scholarships to students related to the energy sector;
- promoting educational, research and development activities in the area of energy;
- supporting the organisation of energy related events and distributing information on energy.

Elering may award grants also for improving the living envrionment of communities influenced by the company's investments.

Grants awarded in 2013

- Supporting the publication of the textbook „Energy Technology and the World" of the Tallinn University of Technology. The objective of the grant was to develop energy education and to promote acquisition of professional education.
- Supporting the organisation of the summer seminar of energy and chemistry students of the Tallinn University of Technology. The objective of the grant was to expand the knowledge of TUT students, increase interest towards the subject and to increase study motivation through the seminar held on 30.08.-1.09.2013.
- Supporting the Lennart Meri Conference organised by the International Centre of Defence Studies. The conferece focused on the traditional subjects of international relations and security issues, with a focus on energy topics.

Elering's energy scholarship programme

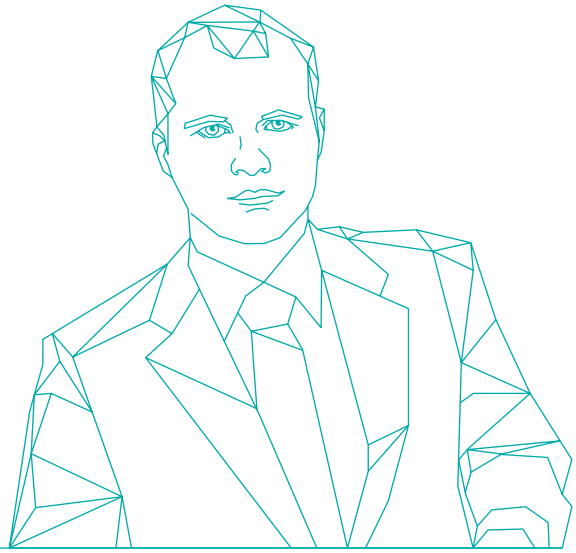
Elering's energy scholarship is a 10-month scholarship granted by the company to two students in the field of energy. Under Elering's scholarship programme, the master's students and doctoral students of the Tallinn University of Technology (TUT) are supported for studying the topical issues of energy. The scholarship programme is being implemented on the basis of a cooperation agreement signed between Elering and TUT for promoting the energy competence centre of Elering.

Elering continues granting scholarships to TUT students in the field of energy

In 2013, the study themes of grant holders were financial transactions and hedging risks on the electricity market and technical requirements for transmission lines of the main grid network.

An overview of the grants awarded by Elering is available on its website at http://elering.ee/principles-for-awarding-grants

Good corporate governance



KALLE KUKK

Strategy Manager

Elering is dedicated to complying with good corporate governance practices and to continuous improvement in that area. We consider this to be a prerequisite for achieving our strategic objectives and designing our organisational culture.

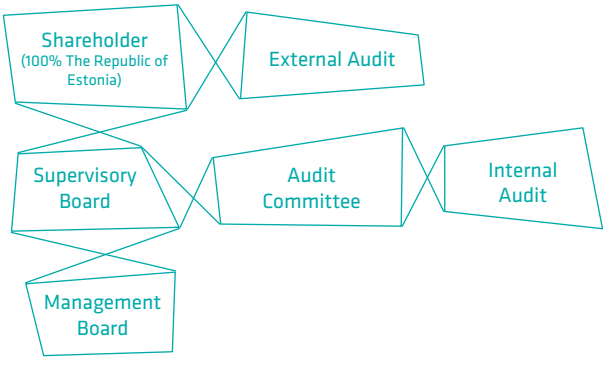
We confirm that:

- the company's risk management and control system are functioning and efficient;
- the company's financial reporting and annual report are based on a functioning system of risk management and internal control.

Elering publishes its good corporate governance report on its website www.elering.ee

Management

Organogram:



Elering is a fully state owned company represented at the general meeting by the Minister of Economic Affairs and Communications. Competences of the company's owner include: to amend the articles of association; to increase and decrease share capital; to elect and remove members of the Supervisory Board; to elect auditors; to designate a special audit; to approve the annual report and allocate profit; to decide on the merger, division, transformation and/or dissolution of the company.

Supervisory Board

In the company, the owner's interests are guaranteed by members of the Supervisory Board (representatives of the Ministry of Finance and the Ministry of Economic Affairs and Communications). The Supervisory Board gives the Management Board instructions for organising the management of the company and exercises supervision over the activities of the company's Management Board. The Supervisory Board regularly reviews and assesses the company's strategy, main actions, principles of risk management, annual report for the financial year and budget.

The Supervisory Board comprises of three to five members. The number of the members of the Supervisory Board is determined and the members are elected and removed by the representative of the owner, i.e. the Minister of Economic Affairs and Communications. Currently the Supervisory Board of Elering has five members. The articles of association set out restrictions on the selection of the members of the Supervisory Board. Fees of the members of the Supervisory Board are determined by a directive of the Minister of Economic Affairs and Communications.

Members of the Supervisory Board

- **Timo Tatar**, Chairman of the Supervisory Board, Head of the Energy Department, Ministry of Economic Affairs and Communications;
- **Heiki Tammoja**, Director of Electrical Power Engineering Institute, Tallinn University of Technology
- **Thomas Auväärt**, Head of the Financial Markets Department, Ministry of Finance
- **Jüri Raatma**, Adviser to the Ministry of Economic Affairs and Communications
- **Aivar Sõerd**, Member of the Parliament (until 18.02.2013)
- **Tarmo Mänd**, Member of the Parliament (from 18.02.2013)

The Audit Committee, established by a resolution of the Supervisory Board, is responsible for exercising supervision over risk management, internal control and financial reporting. The Audit Committee is an advisory body of the Supervisory Board in the area of accounting, audit, risk management, internal control and audit, exercise of supervision and preparation of the budget, and legality of activities.

The Audit Committee comprises five members who are elected and removed by a decision of the Supervisory Board. Members of the Audit Committee are elected for a term of three years and they elect from among themselves the chairman to organise the activities of the Audit Committee. The Chairman of the Supervisory Board shall not hold a position of the Chairman of the Audit Committee. The members of the Supervisory Board are paid an additional fee for participation in the Audit Committee.

The Chairman of the Audit Committee is Thomas Auväärt and the members are Timo Tatar, Heiki Tammoja, Jüri Raatma and Tarmo Mänd (Aivar Sõerd).

Management Board

The Management Board of Elering has complete freedom of decision and its everyday management decisions are made independently, without interference by the owner and the Supervisory Board. The Management Board needs the consent of the Supervisory Board for transactions and operations that are beyond the everyday economic activities of the company. The Management Board ensures that the members of the Supervisory Board have sufficient information on the company's economic condition as well as the most important matters related to its economic activities, and informs the Supervisory Board of the most important matters of the economic activities as necessary.

The Management Board comprises three members. Members of the Management Board are elected by the Supervisory Board for a term of five years. The Chairman of the Management Board organises the work of the Management Board as well as the everyday management and economic activities of the company. The person authorised by the Supervisory Board concludes contracts with the members of the Management Board which set out the rights and obligations of the Management Board with regard to the company in a greater detail.

A member of the Management Board may be paid a fee only on the basis of a contract of the management board member concluded with him or her. A member of the Management Board may be also paid an additional fee based on his or her performance in the amount of up to four months' fee. Bonuses may be paid on the basis of the annual results or any other grounds based on a resolution of the Supervisory Board. Fees of the members of the Supervisory Board are fixed and provided in a management board member contract. Elering has not established any long-term bonus systems. A member of the Management Board may be paid severance compensation only upon removal at the initiative of the Supervisory Board before expiry of the term of his or her authorities in the amount of up to three months' fees.

Members of the Management Board

- **Taavi Veskimägi**, Chairman of the Management Board
- **Peep Soone**, Member of the Management Board
- **Kalle Kilk**, Member of the Management Board

In order to ensure independence, a declaration of interests of members of the Management Board is submitted to the Ministry of Economic Affairs and Communications. Transactions concluded with related parties are also declared upon approval and audit of the annual report.

Employees

In the financial year 2013, the average number of employees in Elering was 147, of whom 74% were men and 26% women. Elering as an employer is characterised by a low employee turnover (2013: 7%) and the above-average length of employment (15 years as at 31.12.2013). Such stability of employees is based not only on the employees' dedication to their specialty, but also on the employer's support to professional development, the promotion of organisational culture favourable to dedication and performance, and the provision of recreational possibilities. The spirit of solidarity is also created by joint events, ranging from forest work to annual anniversary ceremonies of the company. At the latter event, we recognise our best staff with the "Best Colleague of the Year" title.

Succession planning and development of employees are of critical importance for ensuring continuous success of the company. We collaborate with several higher education institutions and offer selected students a thorough summer internship programme. Majority of our employees (84%) have a degree, approximately two-thirds of our staff have a Master's degree and 5% a PhD. Many employees combine work with studies - as of the end of 2013, 21% of Elering's staff members simultaneously studied for a degree in higher education institutions. In collaboration with Tallinn University of Technology, we organise energy-related in-service training courses for our engineering and technical staff.

As of the end of the year, the average age of employees was 41.5. One of the company's strengths lies in having representatives of different age groups in the staff mix. Nearly a third of our employees are over 50 and another third are 30 to 39 years old.

Risk management and internal control system

The Management Board is responsible for the functioning of the internal control system of the company. To ensure the functioning of the internal control system, the position of an internal auditor will be created on the basis of the articles of association or the internal auditor service will be outsourced to an audit company. Until the end of year 2013 the internal auditor service was outsourced from AS PricewaterhouseCoopers Advisors. At the end of the year a tender for a new internal audit service contract was executed as a result of which the internal audit services in 2014-2016 will be provided by KPMG Baltics OÜ. The risk management function of Elering is in compliance with the principles of Enterprise Risk Management (ERM) Model.

Risk management objectives in Elering are:

- to manage and describe the risk management processes in the company;
- to define the roles and responsibilities of the parties to the risk management process;
- to ensure that all risks are identifiable, assessable and they can be responded to;
- to help the managers better understand and manage risks.

The principles of risk management policy in Elering must ensure that:

- the culture, processes and structure of the company encourage the fulfilment of the company's strategic objectives and at the same also the identification, management, monitoring and, if possible, the hedging of risks;
- the monitoring and management of the company's risks and the internal control system are based on the internationally recognised "Enterprise Risk Management (ERM) Model" developed by the Committee of Sponsoring Organisations of the Treadway Commission (COSO), a voluntary organisation that promotes good corporate governance;
- all relevant legislation, standards, regulations and contractual obligations as well as requirements and expectations arising from society have been taken into account upon management of the company's risks;
- we are continuously improving the risk management activities in the company.

Equal treatment

Elering as a transmission system operator bears system responsibility in accordance with the Electricity Market Act. System responsibility is the obligation to ensure, at all times, the security of supply and the balance of the system. The transmission system operator exercises the rights and performs the obligations in compliance with the principles of equal treatment.

A transmission system operator may not produce nor sell electricity, except for performing the obligation of system responsibility. Electricity may be generated in the emergency reserve power plant in the event of an unexpected shutdown of the generation capacity or transmission capacity of the system or of an electricity system of another country electrically connected to the system or in the event of danger to the security of supply or when it is required for the purpose of periodical testing of the emergency reserve power plant.

A transmission system operator may not at the same time be a distribution network operator, or belong to the same group with any undertaking which engages in activities related to generating or selling electricity. Elering is not a part of any group of electricity companies. Neither does Elering have any dominant influence over another electricity undertaking nor has any other electricity enterprise dominant influence over Elering.

All Elering's back-office functions (information technology, accounting, personnel, law, public relations, administration) are separated from the market participants. The company outsources the legal, audit and communications services and, as necessary, also consultations.

For efficient performance of its duties, Elering has established internal procedures and, based on legislation, has specified the conditions for connection to the transmission network, the standard terms and conditions for the provision of network services, the standard terms and conditions for balance agreements, the terms and conditions for issuance of guarantees of origin. The standard terms and conditions are public and approved by the Estonian Competition Authority.

Management Operation of the power system is conducted pursuant to the procedure for operation of the Estonian power system and in conformity with the action plan for ensuring the continuous provision of services of vital importance.

Balance responsibility is exercised pursuant to the procedure of balance management and the standard terms and conditions for balance agreements. Confidentiality of information to be submitted to Elering as the system administrator is set out in the standard terms and conditions for balance agreements

The balancing electricity price is calculated on the basis of the common methodology for calculating balancing electricity, approved by the Estonian Competition Authority.

Regulating capacity is purchased on the basis of bilateral contracts in accordance with the conditions established in the Electricity Market Act: when purchasing the electricity and regulating capacity necessary to perform its obligations and when using other relevant services, the system administrator shall observe free market principles, act with regard to all market participants in accordance with the principles of equal treatment and transparency, and avoid establishing unreasonable restrictions.

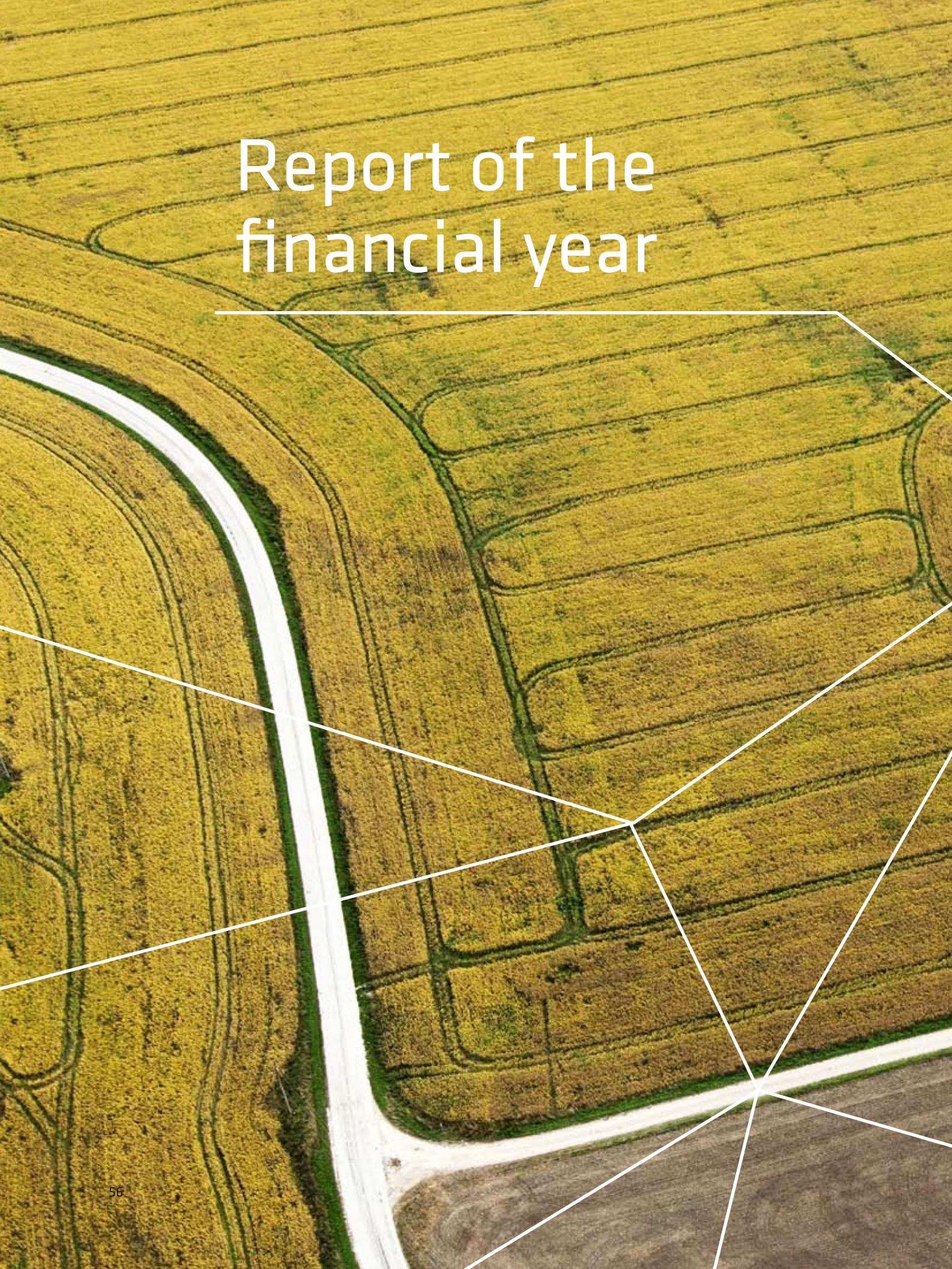
The setting of charges for connection to the transmission network, the preparation and conclusion of connection agreements, also the rights to refuse connection to the network are provided in the connection procedure and the terms and conditions for connection to the transmission network.

The setting of a charge for using a network connection and preparation of network contracts, also the principles for refusing to provide the network service and interrupting the provision of the network service are regulated by the procedure for provision of the network service and the standard terms and conditions for provision of the network services.

The services and works may be purchased, inter alia from market participants, pursuant to the Public Procurements Act and the procedure for carrying out procurements.

The company's website presents a separate list of data that is subject to disclosure by Elering on the basis of the legislature. The website presents annual reports, financial results, operating information, main activities, structure, strategy, news and notices as well as other information that is necessary for investors and the public at large. The website is also available in English. The information on website www.elering.ee is continuously updated (incl. news and announcements).

Report of the financial year



Statement of Financial Position

in thousands of euros	*Note*	*31.12.2013*	*31.12.2012*
ASSETS			
Current assets			
Cash and cash equivalents	6	1,145	12,957
Deposits at banks with maturities of over 3 months	7	0	11,000
Inventories	9	347	0
Trade and other receivables	8	22,858	24,700
Total current assets		**24,350**	**48,657**
Non-current assets			
Available-for-sale financial assets	2	1,946	1,946
Property, plant and equipment	10	640,925	461,003
Intangible assets	11	3,713	4,123
Total non-current assets		**646,584**	**467,072**
TOTAL ASSETS		**670,934**	**515,729**
LIABILITIES			
Current liabilities			
Trade and other payables	13	41,717	24,319
Total current liabilities		**41,717**	**24,319**
Non-current liabilities			
Borrowings	12	312,390	227,013
Deferred income	14	28,176	24,487
Government grants	14	14,564	14,774
Total non-current liabilities		**355,130**	**266,274**
TOTAL LIABILITIES		**396,847**	**290,593**
EQUITY			
Share capital	15	149,890	149,890
Statutory reserve capital	15	6,259	4,515
Retained earnings	15	117,939	70,731
TOTAL EQUITY		**274,087**	**225,136**
TOTAL LIABILITIES AND EQUITY		**670,934**	**515,729**

The notes on pages 62 to 93 are an integral part of these financial statements.

Statement of Comprehensive Income

in thousands of euros	*Note*	*2013*	*2012*
Revenue	16	133,836	108,932
Other income	17	595	551
Goods, raw materials and services	18	-48,885	-37,374
Other operating expenses	19	-3,776	-3,605
Staff costs	20	-4,670	-4,250
Depreciation and amortisation	10;11	-23,662	-22,845
Other expenses	21	-123	-118
Operating profit		**53,315**	**41,291**
Financial income	22	103	385
Financial costs	22	-4,467	-6,809
Profit before income tax		**48,951**	**34,867**
Profit for the year		**48,951**	**34,867**
Total comprehensive income for the year		**48,951**	**34,867**

The notes on pages 62 to 93 are an integral part of these financial statements.

Cash Flow Statement

in thousands of euros	*Note*	*1.01.2013-31.12.2013*	*1.01.2012-31.12.2012*
Cash flows from operating activities			
Profit before income tax		48,951	34,867
Adjustments for:			
▪ Gain on sale of property, plant and equipment	17	-5	-40
▪ Depreciation, amortisation and impairment	10,11	23,662	22,845
▪ Government grants expended and amortised	14	-327	-325
▪ Subsidies received	14	117	0
▪ Interest expenses	22	4,464	6,806
▪ Interest income	22	-71	-385
▪ Other financial income	22	-32	0
▪ Changes in inventories	9	-347	0
▪ Changes in receivables and prepayments related to operating activities	8	1,837	-6,138
▪ Changes in liabilities and prepayments related to operating activities	13	9,036	-3,129
Changes in deferred income from connection and other service fees	14	3,689	410
Cash generated from operations		**90,974**	**54,911**
Interest paid	22	-10,555	-10,487
Interest received	22	76	418
Net cash used in operating activities		**80,495**	**44,842**
Cash flows from investing activities			
Purchases of property, plant and equipment and intangible assets	10,11	-188,323	-77,708
Deposits with maturities of over 3 months	7	11,000	19,000
Foreign grants to acquire non-current assets	14	0	54
Proceeds from sale of property, plant and equipment		90	165
Paid on acquisition of available-for-sale financial assets	2	0	-1,946
Net cash used in investing activities		**-177,234**	**-60,435**
Cash flows from financing activities			
Long-term bank loans received	12	84,895	5,000
Other proceeds from financial activities	22	32	0
Net cash used in financing activities		**84,927**	**5,000**
Net increase/decrease in cash and cash equivalents		**-11,812**	**-10,593**
Cash and cash equivalents at the beginning of the year	**6**	**12,957**	**23,550**
Cash and cash equivalents at the end of the year	**6**	**1,145**	**12,957**

The notes on pages 62 to 93 are an integral part of these financial statements.

Statement of Changes in Equity

in thousands of euros	*Share capital*	*Statutory reserve capital*	*Retained earnings*	*Total*
Balance as of 01.01.2012	**149,890**	**3,490**	**36,889**	**190,269**
Comprehensive income for financial year	0	0	34,867	34,867
Transfers to statutory reserve capital	0	1,025	-1,025	0
Balance as of 31.12.2012	**149,890**	**4,515**	**70,731**	**225,136**
Comprehensive income for financial year	0	0	48,951	48,951
Transfers to statutory reserve capital	0	1,743	-1,743	0
Balance as of 31.12.2013	**149,890**	**6,259**	**117,939**	**274,087**

More detailed information on share capital and other equity items is set out in Note 15.

The notes on pages 62 to 93 are an integral part of these financial statements.

Notes to the Financial Statements

Note 1

ELERING AS AND ITS OPERATIONS

The financial statements of Elering AS (the "Company") for the year ended 31 December 2013 have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union.

The Company is domiciled in the Republic of Estonia. The Company's registered address is Kadaka tee 42, 12915 Tallinn, Estonia. The Company's principal business activity is electricity transmission within the Republic of Estonia. The economic activities of the Company are regulated by the Estonian and EU legislation. The Estonian Competition Board monitors the Company's network activities and provision of balancing service, and approves network tariffs and standard terms of respective contracts.

The sole shareholder of the Company is the Republic of Estonia.

The Management Board approved these financial statements on 17 March 2014. Pursuant to the Commercial Code of the Republic of Estonia, the annual report shall be presented for approval to the Company's Supervisory Board and the General Meeting of Shareholders.

Note 2

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Bases of preparation
These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union under the historical cost convention. 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 periods presented, unless otherwise stated.

Operating segments
The Management Board is responsible for allocating resources and assessing performance of the Company. The Management Board monitors activities of the Company as a single operating segment. The internal reporting provided to the Management Board has been prepared using the accounting policies and presentation consistent with those used in preparation of the financial statements.

Functional and presentation currency
The financial statements of the Company are presented in euros which is the Company´s functional and presentation currency. The financial statements of the Company are presented in thousands of euros.

Foreign currency translation
Foreign currency transactions are translated into the functional currency using the exchange rates of the European Central Bank prevailing on the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at year-end exchange rates are recognised in the income statement.

Financial assets
The purchases and sales of financial assets are recognised on the trade date – the date on which the Company commits to purchase or sell a certain financial asset. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Depending on the purpose for which financial assets were acquired as well as management's intentions, financial assets are classified into the following categories at initial recognition according to IAS 39:

- financial assets at fair value through profit or loss;
- loans and receivables;
- held-to-maturity investments;
- available-for-sale financial assets.

As at 31 December 2013, the Company had no other classes of financial assets than those classified under the category of 'loans and receivables' and 'available-for-sale financial assets' (as at 31 December 2012, 'loans and receivables' and 'available-for-sale financial assets'). As of balance sheet date the Company had no derivative instruments.

Loans and receivables
Loans and receivables are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Company intends to sell in the near term. Financial assets that are not recognised at fair value through profit or loss are initially recognised at fair value to which transaction costs are added. After initial recognition, loans and receivables are accounted for at amortised cost using the effective interest rate method unless the payment date falls within 30 days.

The Company assesses at the end of each reporting period whether there is objective evidence that a financial asset is impaired. A financial asset is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. The criteria that the Company uses to determine that there is objective evidence of an impairment loss include: significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and a breach of contract, such as a default or delinquency in payments for more than 90 days.

The amount of the loss is the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the impairment loss is recognised in the income statement.

Uncollectible loans and receivables are written off against the related allowance account.

The Company recognises the following financial assets in the category of 'loans and receivables': "Cash and cash equivalents", "Deposits at banks with maturities of over 3 months" and "Trade and other receivables".

Available-for-sale financial assets
Available-for-sale financial assets are non-derivative financial assets that the Company intends to sell immediately or in the short term or that are not classified in any of the others categories above. Available-for-sale financial assets are carried as non-current financial investments except when the financial asset expires or the Company intends to sell it during 12 months after the end of the reporting period. Available-for-sale financial assets are initially recognised at fair value, including transaction costs. Available-for-sale financial assets are subsequently carried at fair value; gains and losses arising from changes in fair value of available-for-sale financial assets are included in the statement of comprehensive income. Generally, the basis to determine the fair value is considered to be the market price in the active market or if that is not considered reliable, then the value established by using commonly accepted valuation techniques. If the fair value of a financial asset cannot be measured reliably, they are measured at cost less any impairment losses.

Available-for-sale financial assets include shares of Nord Pool Spot AS. The principal business activity of Nord Pool Spot AS Group, registered in Norway, is the organisation of electricity exchanges in the Nordic countries, Great Britain and the Baltic States. The investment was made with a long-term strategic goal of taking part in the decision-making process concerning the development of electricity market in the Nordic-Baltic region.

As at the balance sheet date, the Company does not have any current financial information on AS Nord Pool Spot; nor are its shares traded in the financial markets. It is also unlikely that those shares will be actively traded in the future or that the company will start publishing periodic information on future forecasts. Therefore, the fair value of those shares cannot be reliably measured and those shares are subsequently recognised at their cost.

Cash and cash equivalents
Cash and cash equivalents include cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at amortised cost using the effective interest method.

Prepayments
Prepayments are carried at cost less a provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which itself will be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Company has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Company. Other prepayments are written off to profit or loss when the goods or services relating to the prepayments are received. If there is an indication that the assets, goods or services relating

to a prepayment will not be received, the carrying amount of the prepayment is written down accordingly and a corresponding impairment loss is recognised in profit or loss.

Inventories
Inventories are initially recorded at cost, consisting of the purchase costs and other costs incurred in bringing the inventories to their present location and condition.

The purchase costs of inventories include the purchase price, customs duties and other non-refundable taxes and direct transportation costs related to the purchase, less discounts and subsidies. Inventories are expensed using the FIFO method.

Inventories are measured in the balance sheet at the lower of acquisition cost and net realisable value. Net realisable value is calculated by deducting estimated expenses that are necessary for preparing the product for sale and for completing the sale from the estimated sales price used in the ordinary course of business.

Property, plant and equipment
Property, plant and equipment are tangible assets that are used in business activities and the useful life of which is longer than one year. Property, plant and equipment are recognised in the statement of financial position at the carrying amount which constitutes historical cost less any accumulated depreciation and any impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Other than the purchase price, cost of the acquired property, plant and equipment includes transportation and installation expenses, as well as other expenses directly related to acquisition and putting such assets into operation. Cost includes borrowing costs incurred on specific or general funds borrowed to finance construction of qualifying assets.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only if they meet respective criteria for property, plant and equipment. The carrying amount of the replaced part is derecognised. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

If property, plant and equipment consist of components with significantly different useful lives, the components are recognised as separate items of property, plant and equipment.

Land is not depreciated. Depreciation of other items of property, plant and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives:

	Useful lives in years
Buildings	25-40
Facilities – electricity transmission lines	30-60
Other facilities	10-30
Machinery and equipment - electricity transmission equipment	7-25
Other property, plant and equipment	3-20

The residual value of an asset is the estimated amount that the Company would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, on each balance sheet date.

On each reporting date management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in the income statement. An impairment loss recognised for an asset in prior years is reversed where appropriate if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Gains and losses on disposals and write-offs determined by comparing proceeds with the carrying amount are recognised in profit or loss.

Intangible assets
An intangible asset is initially recognised at its cost, comprising its purchase price, any directly attributable expenditure on preparing the asset for its intended use and borrowing costs that relate to assets that take a substantial period of time to get ready for use. After initial recognition, an intangible asset is carried at its acquisition cost less any accumulated amortisation and impairment losses.

Acquired software licences are capitalised on the basis of the costs incurred to acquire and bring them to use.

Personal right of use
Payments made for rights of superficies and servitudes meeting the criteria for recognition as intangible assets are recognised as intangible assets. The costs related to rights of use of land are depreciated according to the contract period, not exceeding 100 years.

Intangible assets are amortised using the straight-line method over their useful lives:

	Useful lives in years
Software licences	3-5 years
Personal rights of use	50-100 years

If impaired, the carrying amount of intangible assets is written down to the higher of value in use and fair value less costs to sell.

Impairment of non-financial assets
Land and assets that are subject to depreciation/amortisation 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 an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets that suffered an impairment loss are reviewed for possible reversal of impairment on each reporting date.

Leases
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 or received under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

Financial liabilities
Financial liabilities have the following measurement categories: (a) held for trading which also includes financial derivatives and (b) other financial liabilities. The Company has financial liabilities only in the category of 'other financial liabilities'.

Other financial liabilities are initially recognised at fair value, net of transaction costs incurred and are subsequently carried at amortised cost. The amortised cost of current liabilities normally equals their nominal value; therefore current liabilities are stated in the statement of financial position in their redemption value. Non-current liabilities are subsequently carried at amortised cost. The difference between the amortised cost and the redemption value is recognised as an interest expense in the income statement over the period of the borrowings using the effective interest rate method. The borrowing costs associated with the assets meeting respective requirements are capitalised as cost of the assets.

Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred and treated as a transaction cost when the draw-down occurs.

A financial liability is classified as current when it is due within 12 months after the balance sheet date or the Company does not have an unconditional right to defer the payment for longer than 12 months after the balance sheet date. Borrowings with a due date of 12 months or less after the balance sheet date that are refinanced into non-current borrowings after the balance sheet date but before the approval of the annual report, are classified as current. Borrowings that the lender has the right to recall due to the violation of terms specified in the contract if such right is established by the balance sheet date are also classified as current liabilities.

Provisions and contingent liabilities
Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Company has a present legal or constructive obligation as a result of past events and, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Other possible or present obligations arising from past events but whose settlement is not probable or the amount of which cannot be measured with sufficient reliability are disclosed as contingent liabilities in the notes to the financial statements.

Development costs
Development costs are costs that are incurred in applying research findings for the development of specific new products or processes. Development costs are capitalised if all of the criteria for recognition specified in IAS 38 have been met. Capitalised development costs are amortised over the period during which the products are expected to be used. Expenses related to research carried out for collecting new scientific or technical information are not capitalised.

Share capital
The Company does not have any preference shares. Incremental costs directly attributable to the issue of new shares are recognised as a reduction of equity. Any excess of the fair value of consideration received over the par value of shares issued is recorded as share premium in equity.

Dividends
Dividends are recorded as a liability and deducted from equity in the period in which they are declared and approved. Any dividends declared after the balance sheet date and before the financial statements are authorised for issue are disclosed in the notes to the financial statements.

Statutory reserve capital
Statutory reserve capital is formed to comply with the requirements of the Commercial Code. Reserve capital is formed from annual net profit allocations. During each financial year, at least one-twentieth of the net profit shall be entered in reserve capital, until reserve capital reaches one-tenth of share capital. Reserve capital may be used to cover a loss, or to increase share capital. Payments shall not be made to shareholders from reserve capital.

Revenue recognition
Revenue is measured at the fair value of the consideration received or receivable, net of VAT and discounts.

Revenue from sales of goods is recognised at the point of transfer of risks and rewards of ownership of the goods, normally when the goods are shipped.

Sales of services are recognised in the accounting period in which the services are rendered.

Transmission service
The Company measures the quantity of electricity transmission by remotely read metres in customers' connection points. The transmission service fees are calculated on the basis of the volumes of electricity transmitted in these points and regulated transmission tariffs.

Balancing service
The Company prepares on an hourly basis the energy balance in kilowatt-hours of the Estonian electricity system that consists of the energy balances of the Company itself and balance providers that have entered into a balance agreement with the Company. Energy balances are prepared by comparing the measurement data of the Company and that received from distribution network operators with balancing plans of balance providers. In a trading period when the real consumption of electricity, based on the measurement data, is bigger than electricity volume presented in the energy balance, the Company sells the balance providers the shortage of energy. In a trading period when the situation is opposite, the Company buys from the balance providers the surplus of energy. The sale and purchase prices are calculated by the Company for each trading period on a cost basis.

Congestion income
In situations where market participants place more requests for cross-border transmission of electricity than is technically possible, transmission rights for cross-border electricity are sold in special auctions. Under the principle used in these auctions, 50% of auction income belongs to the transmission system operator of either country. In hourly auctions that are organized by Nord Pool Spot, the latter shall transfer 50% to the relevant transmission system operators. In auctions organized by the Company, the Company first received the whole auction income and then immediately transferred the 50% share to the transmission system operator in question. In this case the income was recognised by the net method, ie only for the 50% part that remained to the Company.

Recognition of connection fees

When connecting to the electricity network, the clients must pay a connection fee based on the actual costs of infrastructure to be built in order to connect to the network. The revenue from connection fees is deferred and recognised as income evenly over the estimated customer relationship period. The amortisation period of connection fees is 25 years. Deferred connection fees are carried in the statement of financial position as long-term deferred income.

Interest income

Interest income is recognised on a time-proportion basis using the effective interest method.

Government grants

Government grants are recognised at fair value when there is a reasonable assurance that the Company will comply with all the conditions attached to government grants and that the grant will be received. The government grants are recognised in profit or loss on a systematic basis over the periods in which the Company incurs the related costs which the grants are intended to compensate.

Government grants are presented using the gross method, according to which the government grant is recognised in the statement of financial position under liabilities as deferred income from government grants. The acquired asset is depreciated and the grant is credited to income over the estimated useful life of the asset.

Inter-transmission system operator compensation mechanism (ITC)

ITC is a mechanism for the compensation of cross-border energy flows, as designated by the EU regulation No 838/2010, in which transmission system operators of over 30 countries participate. The mechanism works under the principle that a transmission system operator of a country compensates, through the ITC fund, the other transmission network operators for additional expenses caused by cross-border energy flows in case if that country has exported or imported electricity during the reporting period, and it receives compensation from the fund if a transit flow caused by market participants of other countries has crossed the country. Such accounting is kept by specifically authorised administrators in Switzerland, who submit to the members of the mechanism the data in the form of net amounts to be paid each month. The Company recognises the net amounts in the statement of comprehensive income depending whether it is net income or net expense under "Revenue" or under "Goods, raw materials and services" respectively.

Subsidies to electricity producers

The law obliges the Company to participate in supporting mechanism for eligible electricity producers (first and foremost power plants using renewable sources of energy). The Company collects subsidies from consumers and distribution network operators and pays it out to those electricity producers who meet the criteria.

In accordance with current principles, the Company prepares an estimate of the amount of subsidies for the following calendar year, based on estimates on the amount of electricity produced by these producers, and the amount of network services to be provided to the end users in Estonia. The Company uses these estimates to determine the charge of subsidy for the following calendar year per kWh (kilowatt-hour) of network services, taking into account any difference between estimated and actual amounts of subsidies paid during the previous period (from November to October), interest earned on over collected amounts or

interest paid on under collected amounts and justified expenses incurred for management of subsidies.

For different reasons the actual amounts paid out and received as subsidies always differ from the estimated amounts. Over or under collected subsidies are shown in the statement of financial position as either Trade and other payables (in case of surplus) or Trade and other receivables (in case of deficit). These balances are taken into account when determining the charge for the next period as described above. Collecting and paying of subsidies has no impact on the comprehensive income of the Company. See also Note 13.

Employee benefits
Employee short-term benefits include wages, salaries and social taxes, benefits related to temporary suspension of employment contracts (holiday or other similar pay). These benefits are recognised in the income statement in the year in which the associated services are rendered by the employees of the Company. Any amounts unpaid by the balance sheet date are recognised as a liability.

If during the reporting period, an employee has provided services for which payment of compensation is to be expected, the Company will recognise a liability (accrued expense) in the amount of forecasted compensation, from which all amounts already paid, will be deducted.

Taxation
According to 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 21/79. The corporate income tax arising from the payment of dividends is recognised as a liability and an income tax expense in the period in which dividends are declared, regardless of the period for which the dividends are paid or the actual payment date. An income tax liability is due on the 10th day of the month following the payment of dividends.

Due to the nature of the taxation system, the companies registered in Estonia do not have any differences between the tax bases of assets and their carrying amounts and hence, no deferred income tax assets and liabilities arise. A contingent income tax liability which would arise upon the payment of dividends is not recognised in the statement of financial position. The maximum income tax liability which would accompany the distribution of Company's retained earnings is disclosed in the notes to the financial statements.

Tax rates

The following tax rates were applicable in 2013:

Tax	*Tax rate*
Social security tax	33% of the paid payroll to employees and fringe benefits
Unemployment insurance tax	1.0% of the payroll paid to employees
Fringe benefit income tax	21/79 of fringe benefits paid to employees
Land tax	1%-2.5% on taxable value of land per annum
Excise tax on electricity	4.47 euros per MWh of electricity
Corporate income tax on non-business related expenses	21/79 on non-business related expenses

Note 3

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Company makes estimates and assumptions that affect the amounts recognised in the financial statements and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Useful lives of property, plant and equipment
The estimated useful lives of items of property, plant and equipment (Note 10) are based on management's estimates regarding the period during which the asset will be used. The estimation of economic lives is based on historical experience and takes into consideration production capacity and physical condition of the assets. Previous experience has shown that the actual useful lives have sometimes been longer than the estimates. In the reporting period, depreciation amounted to EUR 22,107 thousand (2012: EUR 21,547 thousand). If depreciation rates were increased/decreased by 20%, the depreciation charge for the year would increase/decrease by EUR 4,421 thousand (2012: EUR 4,309 thousand).

Note 4

NEW ACCOUNTING PRONOUNCEMENTS

Adoption of new or revised standards and interpretations
The new standards, amendments to published standards and interpretations that became effective for the Company from 1 January 2013 had no effect on the financial statements and have no importance with respect to the Company's business activity.

New or revised standards and interpretations
New or revised standards or interpretations that have not yet become effective are not expected to have significant effect on the Company.

Note 5

FINANCIAL RISK MANAGEMENT

The risk management function is performed at the Company in accordance with internationally approved Enterprise Risk Management Mode methodology, which has been developed by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's risks are assessed in four categories: strategic, operational, financial and external risks. Financial risk comprises market risk (including electricity price risk, currency risk, interest rate risk), credit risk and liquidity risk. The primary objectives of the financial risk management function are to establish risk limits, and then to ensure that exposure to risks stays within these limits. Risk management is monitored at the Management Board level and the results are reported to the Audit Committee. The Company's liquidity, interest rate and currency risks are managed at the Company's Finance Department.

The following table provides reconciliation of classes of financial assets and financial liabilities of the Company in accordance with the measurement categories of IAS 39:

Financial assets

in thousands of euros	*31.12.2013*	*31.12.2012*
Loans and receivables		
Cash and cash equivalents (Note 6)	1,145	12,957
Deposits at banks with maturities of over 3 months (Note 7)	0	11,000
Trade and other receivables (Note 8)	22,698	24,574
Total loans and receivables	**23,843**	**48,531**
Available-for-sale financial assets	1,946	0
Total financial assets	**25,789**	**50,477**

Financial liabilities

in thousands of euros	*31.12.2013*	*31.12.2012*
Other financial liabilities		
Trade and other payables (Note 13)	40,592	21,329
Borrowings (Note 12)	312,390	227,013
Total financial liabilities	**352,982**	**248,342**

Credit risk

The Company takes on exposure to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Exposure to credit risk arises as a result of the Company's sales on credit terms and other transactions with counterparties giving rise to financial assets. In accordance with the Company's risk management principles, the Company's short-term available cash resources can be deposited in the following domestic financial instruments: overnight deposits or term deposits at acceptable credit institutions. The following principles are followed when depositing short-term available cash resources: ensuring of liquidity, capital preservation, revenue generation.

The Company's assets exposed to credit risk as of balance sheet days were as follows:

in thousands of euros	*31.12.2013*	*31.12.2012*
Cash and cash equivalents (Note 6)	1,145	12,957
Deposits at banks with maturities of over 3 months (Note 7)	0	11,000
Trade and other receivables (Note 8)	22,698	24,574
Total exposure of assets to credit risk in the statement of financial position	**23,843**	**48,531**

The Company structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to counterparties or groups of counterparties or by applying additional instruments for credit risk management. The Company established criteria for holding financial assets at credit institutions. According to the given criteria maximum permitted limits depend on the credit rating and equity of the credit institution. Limits on the level of credit risk are approved regularly by management. Such risks are monitored on an ongoing basis and they are subject to a biannual review.

The Company's Accounting Department reviews ageing analysis of outstanding trade receivables and follows up on past due balances each week. The results are reported to the CFO of the Company. The Company has identified circumstances under which the collection of debt is passed over to a collection agency. Information about credit risk is disclosed in Note 8.

Credit risk concentration

The Company is exposed to concentrations of credit risk. Management monitors and discloses concentrations of credit risk by reports, which list exposures to counterparty with aggregated balances in excess of 5% of the Company's equity. On 31.12.2013, the Company had one counterparty (31.12.2012: one counterparty) with an aggregated receivables balance of EUR 17,473 thousand (31.12.2012: EUR 19,404 thousand) or 77% of the gross amount of trade and other receivables (31.12.2012: 79%). In 2013 as well as in 2012 the major part of receivables was to the wholly state owned company. The company acts as a natural monopolist in distribution network field. Therefore Management believes that the credit risk arising from the concentration of receivables is not significant.

Market risk

The Company is exposed to market risk. Market risk arises mainly from changes in the electricity price, as well as from open positions in foreign currencies and interest bearing assets and liabilities. Management sets limits on the value of exposed positions that may be accepted, which is monitored on a daily basis. However, the use of this approach does not completely prevent losses outside of these limits, but limits their maximum amounts.

Sensitivities to market risks shown below are based on a change in one factor while holding all other factors constant. In practice, this is unlikely to occur and changes in some of the factors may be correlated – for example, changes in the interest rate and changes in foreign currency rates.

Electricity price risk

For offsetting network losses, the Company primarily buys electricity in the electricity exchange. The average electricity exchange price of the last period is used for calculation of network charges. In a situation where the stock price is different from the prices used to calculate tariffs no compensation is paid in the next tariff period. As a result the company may earn profit or loss from buying electricity in a short perspective. The company believes the risk of creating big losses is not significant and therefore there are no financial instruments in place to reduce the risk.

Currency risk

Currency risk is the risk that in the future fair value of financial instruments of cash flow will fluctuate due to changes in currency rates. As most of the Company's transactions and balances are denominated in euros, the Company is not exposed to significant currency risk. The Company established separate limits for open currency positions depending on the currency and duration. Transactions in other currencies are insignificant; there were no financial instruments denominated in other currencies as of 31.12.2013 and 31.12.2012.

Interest rate risk

The financial instruments with floating interest rate expose the Company to cash flow interest rate risk, i.e. the risk that an increase in market interest rates will cause an increase in the Company's interest expense. At the same time, in case of short-term deposits, a change in market interest rates has effect on the Company's interest income arising from investment of available resources into new deposits. The Company established the minimum limit for fixed interest-bearing liabilities at 60% of all liabilities. The Company is somewhat protected against the changes in interest rates due to the fact that in accordance with the regulation, tariffs are calculated on the basis of the average market price over the last five years. Fixed interest financial instruments create fair value interest rate risk. Since the Company does not recognise interest-bearing financial instruments at fair value, change in market interest rates does not have effect on balance value of available assets or liabilities, nor interest income or expense arising from them.

As of 31.12.2013 long-term bonds with fixed interest rate constituted 71% (as of 31.12.2012 98%) of long-term borrowings carried at amortised cost; the remaining 29% (as of 31.12.2012 2%) of the abovementioned liabilities were long-term bank loans with a floating interest rate carried at amortised cost. Long-term bonds were issued on 12.07.2011 with the maturity of seven years and the nominal value of EUR 225 million. The bonds' coupon is fixed at 4.625% p.a. and interest payments are made once a year. The floating interest rate of bank loans is based on the 6-month Euribor and it is fixed twice a year.

The Company's interest-bearing financial assets are overnight deposits and term deposits. The rate for overnight deposits is being fixed once a day and term deposits have a fixed interest rate for the whole term of the deposit.

The table below summarises the Company's exposure to interest rate risks in 2013 and 2012. The table presents the aggregated amounts of the Company's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual interest repricing and maturity dates.

in thousands of euros	*On demand and less than 1 month*	*From 1 to 12 months*	*From 12 months to 5 years*	*Total*
31.12.2013				
Cash and cash equivalents (Note 6)	1,145	0	0	1,145
Long-term bonds (Note 12)	0	-89,832	-222,558	-312,390
Net interest sensitivity gap on 31.12.2013	**1,145**	**-89,832**	**-222,558**	**-311,245**

in thousands of euros	*On demand and less than 1 month*	*From 1 to 12 months*	*Over 5 years*	*Total*
31.12.2012				
Cash and cash equivalents (Note 6)	12,957	0	0	12,957
Deposits at banks with maturities of over 3 months (Note 7)	0	11,000	0	11,000
Long-term bonds (Note 12)	0	-4,925	-222,088	-227,013
Net interest sensitivity gap at 31.12.2012	**12,957**	**6,075**	**-222,088**	**-203,056**

The Company did not have other financial instruments exposed to risk of change in interest rate.

Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. The Company is exposed to daily calls on its available cash resources. The Company's objective is to obtain a stable funding base primarily consisting of amounts due to banks and bonds. The liquidity position is monitored and regular liquidity stress testing under a variety of scenarios covering both normal and more severe market conditions is performed by the Finance Department.

As at 31.12.2013, the Company had negative working capital, but the liquidity risk is fully covered by available overdraft facility and undrawn loans (Note 12).

The table below shows liabilities on 31.12.2013 and 31.12.2012 by their remaining contractual maturity. The amounts disclosed in the maturity table are contractual undiscounted cash flows. When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing on the reporting date. Foreign currency payments are translated using exchange rate at the balance sheet date. The cash flows of subsequent periods are calculated on the basis of loan interest rates effective at balance sheet date.

The maturity analysis of financial liabilities on 31.12.2013 is as follows:

in thousands of euros	*On demand and less than 1 month*	*From 1 to 12 months*	*From 12 months to 5 years*	*Over 5 years*	*Total*
Liabilities*					
Trade and other payables (Note 13)	23,868	11,607	0	0	35,475
Borrowings (Note 12)	0	11,278	284,791	91,419	387,488
Total future payments	**23,868**	**22,885**	**284,791**	**91,419**	**422,963**

* *including interest expenses*

The maturity analysis of financial liabilities on 31.12.2012 is as follows:

in thousands of euros	*On demand and less than 1 month*	*From 1 to 12 months*	*From 12 months to 5 years*	*Over 5 years*	*Total*
Liabilities*					
Trade and other payables (Note 13)	11,966	4,429	0	0	16,395
Borrowings (Note 12)	0	10,475	37,018	245,386	292,879
Total future payments	**11,966**	**14,904**	**37,018**	**245,386**	**309,274**

* *including interest expenses*

For ensuring liquidity and better management of cash flows, the Company has concluded an overdraft contract amounting to EUR 20,000 thousand and holds its money in liquid bank deposits. As of 31.12.2013, the Company's total available cash resources (cash and cash equivalents) amounted to EUR 1,145 thousand (as of 31.12.2012: EUR 23,957 thousand). See further information in Notes 6 and 7.

In addition, as of 31.12.2013 the Company had undrawn borrowing facilities amounting to EUR 35,000 thousand (31.12.2012: EUR 110,000 thousand). The Company was granted irrecoverable financial help amounting to EUR 50,000 thousand from the European Union for building of Estlink 2 electricity interconnector between Estonia and Finland, of which EUR 15,000 thousand was transferred in 2010. The Company is eligible to receive the remaining part over 2014-2015 in accordance with completion of the project stages.

Capital Management

The Company's main goal in capital risk management is to ensure the Company's sustainability of operations in order to generate return for its shareholder and provide a sense of security to creditors and thereby, preserve an optimal capital structure and lower the cost of capital. In order to preserve or improve the capital structure, the Company can regulate the dividends payable to the shareholders, buy back shares from shareholders, issue new shares or bonds and take new loans.

According to the widespread industry practice, the Company uses the equity to asset ratio for monitoring the Company's capital structure, arrived at by dividing total equity by total assets as of the balance sheet date. The Company's target has been to preserve the ratio of equity to assets at 35% - 45%. The equity to asset ratio is presented in the table below:

in thousands of euros	*31.12.2013*	*31.12.2012*
Equity	274,087	225,136
Total assets	670,934	515,729
Equity to asset ratio	**41%**	**44%**

Fair Value of Financial Instruments

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best expressed by an active quoted market price.

The tables below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

Level 1
quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2
inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly;

Level 3
inputs for the asset or liability that are not based on observable market data.

Estimated fair values of financial instruments have been determined by the Company using available market information, where it exists, and appropriate valuation methodologies. The additional estimations are used for interpreting market data to determine the fair value.

Financial assets carried at amortised cost
Carrying amounts of trade and other financial receivables approximate their fair values.

Liabilities carried at amortised cost
Carrying amounts of trade and other payables approximate their fair values.

The estimated fair value of non-current borrowings with a fixed interest rate is determined using their quoted price (Level 1). The estimated fair value of non-current borrowings with a floating interest rate (Level 3) is determined using valuation techniques, based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity.

The Company had the following borrowings as of 31.12.2013: bonds, the market value of which without accrued interest was EUR 255,415 thousand (nominal value EUR 225,000 thousand) and bank loans, the market value of which without accrued interest was EUR 79,121 thousand (nominal value EUR 90,000 thousand). The liabilities as of 31.12.2012 consisted of bonds the market value of which without accrued interest was EUR 251,739 thousand (nominal value EUR 225,000 thousand) and a bank loan, the market value of which without accrued interest was EUR 4,578 thousand (nominal value EUR 5,000 thousand).

Note 6

CASH AND CASH EQUIVALENTS

in thousands of euros	*31.12.2013*	*31.12.2012*
Bank accounts	298	861
Short-term deposits	847	12,096
Total cash and cash equivalents	**1,145**	**12,957**

Bank accounts and deposits with maturities of up to 3 months

in thousands of euros	*31.12.2013*	*31.12.2012*
Bank accounts and short-term deposits at banks:		
with Moody's credit rating of Aa3	6	38
with Moody's credit rating of A2	793	10,821
with no Moody's credit rating*	346	2,098
Total bank accounts and short-term deposits at banks	**1,145**	**12,957**

* *Two banks without credit rating at which the Company holds its money are Estonia-based subsidiaries of international banks with Moody's credit ratings of A1.*

Note 7

DEPOSITS AT BANKS WITH MATURITIES OF OVER 3 MONTHS

in thousands of euros	*31.12.2013*	*31.12.2012*
Deposits at banks with maturities of over 3 months	0	11,000
Total deposits at banks with maturities of over 3 months	**0**	**11,000**

Deposits at banks with maturities of over 3 months

in thousands of euros	*31.12.2013*	*31.12.2012*
with Moody's credit rating of Aa3	0	6,000
with Moody's credit rating of A2	0	5,000
Total deposits at banks with maturities of over 3 months	**0**	**11,000**

During the financial year, effective interest rates of deposits with maturities of over 3 months were 0.14%-0.62% (2012: 0.37%-1.88%).

Note 8

TRADE AND OTHER RECEIVABLES

in thousands of euros	*31.12.2013*	*31.12.2012*
Trade receivables		
Accounts receivable	22,653	24,524
▪ incl. allowance for doubtful receivables	-12	-7
Other receivables	45	50
▪ incl. other receivables	45	45
▪ incl. interest receivables	0	5
Total financial assets within trade and other receivables in the statement of financial position	**22,698**	**24,574**
Tax receivables	5	3
Prepayments	154	123
Total trade and other receivables	**22,858**	**24,700**

Analysis by credit quality of trade receivables is as follows:

in thousands of euros	*31.12.2013*	*31.12.2012*
Accounts receivable not yet due		
▪ Distribution networks operators	18,987	21,053
▪ Other clients	3,345	3,417
Total accounts receivable not yet due	**22,332**	**24,470**
Accounts receivable past due but not classified as doubtful (IAS 39)		
▪ 1 to 90 days overdue	321	54
Total accounts receivable past due but not classified as doubtful	**321**	**54**
Accounts receivable classified as doubtful		
▪ over 90 days overdue	12	7
Total accounts receivable classified as doubtful	**12**	**7**
Total accounts receivable past due	**333**	**61**
Total trade receivables	**22,653**	**24,524**

In the financial year, the Company wrote off uncollectible receivables in amount of EUR 3 thousand, which were not settled as at 31.12.2013 and the due date of which was 31.12.2012 and earlier (in 2012 the respective amount was EUR 7 thousand).

Further information on receivables from related parties is disclosed in Note 24.

Note 9

INVENTORIES

in thousands of euros	*31.12.2013*	*31.12.2012*
Raw material and materials at warehouses	347	0
Total inventories	**347**	**0**

The Company keeps inventories of reserve fuel for emergency reserve power plants.

Note 10

PROPERTY, PLANT AND EQUIPMENT

in thousands of euros	*Land*	*Buildings*	*Facilities*	*Machinery and equipment*	*Other*	*Construction in progress*	*Total*
Property, plant and equipment on 01.01.2012							
Cost at 01.01.2012	4,839	17,326	236,957	216,322	54	0	475,498
Accumulated depreciation	0	-3,317	-75,737	-62,093	-33		-141,180
Carrying amount on 01.01.2012	**4,839**	**14,009**	**161,220**	**154,229**	**21**	**0**	**334,318**
Construction in progress	0	0	0	0	0	76,116	76,116
Total property, plant and equipment on 01.01.2012	**4,839**	**14,009**	**161,220**	**154,229**	**21**	**76,116**	**410,434**
Movements 01.01.2012-31.12.2012							
Additions	387	0	0	0	0	68 162	68 549
Reclassified from construction in progress	0	784	5 795	23 256	0	-29 835	0
Capitalised borrowing costs (Note 22)	0	0	0	0	0	4,140	4,140
Disposals and write-offs at carrying amount	-2	0	0	-123	0	0	-125
Depreciation charge	0	-515	-10,049	-10,970	-13	0	-21,547
Impairment	0	0	-274	-175	0	0	-449
Total movements 01.01.2012-31.12.2012	**385**	**269**	**-4,528**	**11,988**	**-13**	**42,467**	**50,568**
Cost at 31.12.2012	5,224	18,064	240,959	237,383	54	0	501,684
Accumulated depreciation	0	-3,786	-84,266	-71,166	-46	0	-159,264
Carrying amount on 31.12.2012	**5,224**	**14,278**	**156,693**	**166,217**	**8**	**0**	**342,420**
Construction in progress	0	0	0	0	0	118,583	118,583
Total property, plant and equipment on 31.12.2012	**5,224**	**14,278**	**156,693**	**166,217**	**8**	**118,583**	**461,003**

in thousands of euros	*Land*	*Buildings*	*Facilities*	*Machinery and equipment*	*Other*	*Construction in progress*	*Total*
Movements 01.01.2013-31.12.2013							
Additions	0	1 665	13 651	23 056	0	157 262	195 634
Reclassified from construction in progress	0	10 958	100 393	101 185	0	-212 536	0
Capitalised borrowing costs (Note 22)	0	0	0	0	0	6,755	6,755
Disposals and write-offs at carrying amount	-6	0	0	-78	0	0	-84
Depreciation charge	0	-559	-9,590	-11,952	-6	0	-22,107
Impairment	-3	0	-4	-268	0	0	-275
Total movements 01.01.2013-31.12.2013	**-9**	**12,064**	**104,450**	**111,943**	**-6**	**-48,519**	**179,923**
Property, plant and equipment on 31.12.2013							
Cost on 31.12.2013	5,215	30,687	354,542	361,072	54	0	751,570
Accumulated depreciation	0	-4,345	-93,399	-82,912	-52	0	-180,708
Carrying amount on 31.12.2013	5,215	26,342	261,143	278,160	2	0	570,862
Construction in progress	0	0	0	0	0	70,063	70,063
Total property, plant and equipment on 31.12.2013	**5,215**	**26,342**	**261,143**	**278,160**	**2**	**70,063**	**640,925**

In the financial year, the facilities and equipment of the electricity connection between Estonia and Finland, EstLink 1 and Estlink 2 with the cost of EUR 38,289 thousand and EUR 135,968 thousand respectively and the first emergency reserve electricity plant with the cost of EUR 56,739 thousand have been put into operation.

Construction in progress mainly consists of the second emergency reserve electricity plant, substations and electricity transmission lines. Upon completion, cost of these assets is recognised as cost of buildings, machinery and equipment and facilities.

Additions to construction in progress during the financial year include capitalised borrowing costs of EUR 6,755 thousand (2012: EUR 4,140 thousand). The capitalisation rate was 4.5% (2012: 4.9%).

Further information on operating lease of property, plant and equipment is disclosed in Note 23.

Submerged cables of EstLink 1 and EstLink 2, electrical connections between Estonia and Finland, are used jointly with the Finnish transmission system operator Fingrid OYj. All expenses related to the above cables are divided equally between the partners, irrespective of in which part of the cable the expense was incurred.

Lisa 11

INTANGIBLE ASSETS

in thousands of euros	*Acquired software and licenses*	*Right of use of land*	*Total*
Intangible assets on 01.01.2012			
Cost at 01.01.2012	2,631	1,210	3,841
Accumulated amortisation	-289	-57	-346
Carrying amount on 01.01.2012	**2,342**	**1,153**	**3,495**
Intangible assets not yet available for use	228	0	228
Total intangible assets on 1.01.2012	**2,570**	**1,153**	**3,723**
Movements 01.01.2012-31.12.2012:			
Additions	1,196	34	1,230
Capitalised borrowing costs (Note 22)	20	0	20
Amortisation charge	-835	-14	-849
Total movements 1.01.2012-31.12.2012	**381**	**20**	**401**
Intangible assets on 31.12.2012			
Cost at 31.12.2012	4,074	1,244	5,318
Accumulated amortisation	-1,123	-72	-1,195
Carrying amount on 31.12.2012	**2,951**	**1,172**	**4,123**
Intangible assets not yet available for use	0	0	0
Total intangible assets on 31.12.2012	**2,951**	**1,172**	**4,123**
Movements 01.01.2013-31.12.2013			
Additions	525	344	869
Capitalised borrowing costs (Note 22)	1	0	1
Amortisation charge	-1,266	-14	-1,280
Total movements 01.01.2013-31.12.2013	**-740**	**330**	**-410**
Intangible assets on 31.12.2013			
Cost at 31.12.2013	3,265	1,587	4,852
Accumulated amortisation	-1,276	-85	-1,361
Carrying amount 31.12.2013	**1,989**	**1,502**	**3,491**
Intangible assets not yet available for use	222	0	222
Total intangible assets on 31.12.2013	**2,211**	**1,502**	**3,713**

Note 12

BORROWINGS

in thousands of euros	*31.12.2013*	*31.12.2012*
Long-term borrowings		
Long-term bank loan	89,832	4,925
Issued bonds	222,558	222,088
Total long-term borrowings	**312,390**	**227,013**

The Company's borrowings are denominated in the following currencies

in thousands of euros	*31.12.2013*	*31.12.2012*
Borrowings denominated in euros	312,390	227,013
Total borrowings	**312,390**	**227,013**

The average effective interest on borrowings was 4.6% in 2013 (2012: 4.8%).

The Company has used the following types of facilities for financing purposes:

Loan from the European Investment Bank
In August and November 2013, the Company collected the loan in the amount of EUR 75,000 thousand in two parts. The maturity date of the loan is 2033, the interest rate is floating which is the sum of 6-month Euribor and the margin and repayments of the loan will start in 2018.

Loans from the Nordic Investment Bank
In October 2013, the Company collected the first portion of the loan in the amount of EUR 10,000 thousand (the loan contract entered into 01.07.2013). The maturity date of the loan is 2033, the interest rate is floating which is the sum of 6-month Euribor and the margin and repayments of the loan will start in 2018.

In December 2012, the Company collected the first portion of the loan in the amount of EUR 5,000 (the loan contract entered into 20.10.2010). The maturity date of the loan is 2025, the interest rate is floating which is the sum of 6-month Euribor and the margin and repayments of the loan will start in 2015.

Eurobonds
In 2011, the Company issued Eurobonds with the maturity of seven years and the nominal value of EUR 225 million and listed them on London Stock Exchange. Bonds' coupon is fixed at 4.625% p.a. and interest payments are made once a year.

Overdraft
The Company has an overdraft contract in the amount of EUR 20,000 thousand. The contract is valid until 2016 and it can be terminated with a 6-month notice. The interest payable on the used portion is floating. As of 31.12.2013 and 31.12.2012, the Company did not use overdraft.

As of the balance sheet date, the undrawn loan limit of the Company's valid loan contracts totalled EUR 35,000 thousand (31.12.2012: EUR 110,000 thousand). All or some of these loans can be withdrawn until 31.12.2014. The interest on all undrawn loans is floating and it is determined immediately prior to the withdrawal of the loan.

Note 13

TRADE AND OTHER PAYABLES

in thousands of euros	*31.12.2013*	*31.12.2012*
Trade payables	14,314	10,496
Payables for purchased property, plant and equipment and intangible assets	9,554	1,374
Received prepayments due to electricity producers	11,326	4,397
Other payables	281	128
Total financial liabilities within trade and other payables without accrued interests	35,475	16,395
Accrued interests	5,117	4,934
Total financial liabilities within trade and other payables in the statement of financial position	**40,592**	**21,329**
Taxes payable		
VAT	147	2,152
Social security tax	229	172
Personal income tax	128	94
Unemployment insurance tax	18	16
Contributions to mandatory funded pension	11	8
Corporate income tax and income tax on fringe benefits	6	4
Excise tax	169	110
Total taxes payable	**708**	**2,556**
Accrued expenses - employee benefits		
Wages and salaries	208	198
Bonuses	75	85
Holiday pay	79	90
Social security and unemployment insurance tax	52	60
Total accrued expenses - employee benefits	**414**	**433**
Other payables	**3**	**1**
Total trade and other payables	**41,717**	**24,319**

Further information on payables to related parties is disclosed in Note 24.

Note 14

DEFERRED INCOME AND GOVERNMENT GRANTS

Connection and other service fees

in thousands of euros	*2013*	*2012*
Deferred income from connection and other service fees at the beginning of the period	**24,487**	**24,077**
Connection and other service fees received	4,753	1,690
Connection and other service fees recognised as revenue	-1,064	-1,280
Deferred income from connection and other service fees at the end of the period	**28,176**	**24,487**

Government grants

in thousands of euros	*2013*	*2012*
Deferred income from government grants at the beginning of the period	**14,774**	**15,045**
Subsidies received	117	54
Subsidies used to cover operating expenses (Note 17)	-152	0
Subsidies used for acquisition of property, plant and equipment (Note 17)	-175	-325
Deferred income from government grants at the end of the period	**14,564**	**14,774**

Note 15

EQUITY

The Company's share capital consists of 149,890 shares with the nominal value of EUR 1,000 (31.12.2012: 149,890 shares with the nominal value of EUR 1,000). The shares have been paid for in full.

No dividends were paid in the financial years 2013 and 2012.

As of 31.12.2013, the Company's statutory reserve capital totalled EUR 6,259 thousand (31.12.2012: EUR 4,515 thousand). As at 31.12.2013, the Company has the obligation to additionally transfer EUR 2,448 thousand (31.12.2012: EUR 1,743 thousand) to reserve capital.

The retained earnings of the Company as of 31.12.2013 amounted to EUR 117,939 thousand (31.12.2012: EUR 70,731 thousand). The income tax applicable to the net profit distributable as dividends is 21/79. As of 31.12.2013, it would be possible to distribute EUR 91,238 thousand as net dividends (31.12.2012: EUR 54,500 thousand) and the corresponding income tax would amount to EUR 24,253 thousand (31.12.2012: EUR 14,487 thousand).

Note 16

REVENUE

Analysis of revenue by activity

in thousands of euros	*2013*	*2012*
Sales of balancing and control electricity		
Balancing electricity	19,630	12,792
Control service	629	254
Total Sales of balancing and control electricity	**20,259**	**13,046**
Sales of network services		
Transmission services	93,716	84,727
Other network services	15,492	5,559
▪ incl. congestion income	14,208	4,031
Revenue from connection fees (Note 14)	1,064	1,280
Total sales of network services	**110,272**	**91,566**
Sales of other goods and services		
Lease of transmission equipment (Note 23)	848	840
Sales of scrap metal	333	181
Sales of other services	2,119	3,293
Other goods	5	6
Total sales of other goods and services	**3,305**	**4,320**
Total revenue	**133,836**	**108,932**

Analysis of revenue by geographical location of customers

in thousands of euros	*2013*	*2012*
Estonia	114,810	99,480
Norway	14,122	3,258
Latvia	2,094	2,111
Finland	579	2,032
Lithuania	972	580
Russia	383	428
Other	876	1,043
Total revenue	**133,836**	**108,932**

Note 17

OTHER INCOME

in thousands of euros	*2013*	*2012*
Fines, penalties and compensations received	262	186
Gain on disposal of property, plant and equipment	5	40
Foreign grants for operating expenses (Note 14)	153	0
Government grants related to acquisition of property, plant and equipment (Note 14)	175	325
Total other income	**595**	**551**

Note 18

GOODS, RAW MATERIALS AND SERVICES

in thousands of euros	*2013*	*2012*
Electricity purchased to provide the balancing service		
Purchase of balancing electricity	16,373	10,398
Purchase of power regulation service	3,316	2,226
Total electricity purchased to provide the balancing service	**19,688**	**12,624**
System services		
Purchased electricity reserves	4,323	4,225
Reactive energy	431	423
Countertrade	947	806
Operating expenses of emergency reserve power plant	3	0
Total system services expenses	**5,704**	**5,454**
Electricity to compensate for network losses		
Electricity from non-renewable sources	15,694	10,525
Total electricity to compensate for network losses	**15,694**	**10,525**
Maintenance and repair works		
On facilities and equipment related to core activities	4,420	4,093
On production buildings and sites	510	457
Disassembly works and waste processing	109	115
Other	184	277
Total maintenance and repair works	**5,223**	**4,942**

in thousands of euros	*2013*	*2012*
Other costs		
Operative switching and dispatching management expenses	669	665
Other	1,907	3,164
Total other costs	**2,576**	**3,829**
Total goods, raw materials and services	**48,885**	**37,374**

Note 19

OTHER OPERATING EXPENSES

in thousands of euros	*2013*	*2012*
Transportation and tools	131	122
Security, insurance and occupational safety	74	88
Office expenses	322	361
Research and development costs (R&D)	296	188
Research and consulting	717	450
Telecommunication	971	938
Information technology	466	439
Training and other miscellaneous operating expenses	799	1,019
Total other operating expenses	**3,776**	**3,605**

Note 20

STAFF COSTS

in thousands of euros	*2013*	*2012*
Base salaries, additional remuneration, bonuses, vacation pay	3 338	3 043
Termination benefits	10	4
Other remuneration	113	119
Total remuneration to employees	**3 461**	**3 166**
Social security tax	1 178	1 046
Unemployment insurance tax	31	38
Total staff costs	**4 670**	**4 250**

▪ inc. compensations to the members of the Management and Supervisory Board		
Salaries, additional remuneration bonuses, vacation pay	250	233
Fringe benefits	24	23
Social security tax	90	84
Total compensations to the members of the Management and Supervisory Boards	**364**	**340**

The average monthly pay was EUR 1,892 (2012: EUR 1,749).

The members of the Management Board receive compensation for premature termination of their employment contracts, such compensation amounts up to the three months' salary.

Note 21

OTHER EXPENSES

in thousands of euros	*2013*	*2012*
Non-business related expenses	75	62
Fines, penalties and compensations paid	7	34
Foreign exchange net losses	0	1
Income tax from expenses not related to business	18	13
Other	24	8
Total other expenses	**123**	**118**

Note 22

FINANCIAL INCOME AND COSTS

in thousands of euros	*2013*	*2012*
Financial income		
Other financial income	32	0
Interest income	71	385
Total financial income	**103**	**385**
Financial costs		
Interest expenses	-11,220	-10,966
Foreign exchange losses	-1	-1
Other financial costs	-2	-2
Total financial costs	**-11,223**	**-10,969**
Less: capitalised borrowings costs (Notes 10 and 11)	6,756	4,160
Total financial costs recognised in the statement of comprehensive income	**-4,467**	**-6,809**
Net financial income (costs)	**-4,364**	**-6,424**

Note 23

OPERATING LEASE

Company as a lessor

Operating lease revenue

in thousands of euros	*2013*	*2012*
Buildings	203	330
Facilities	848	840
Total operating lease revenue	**1,051**	**1,170**

Facilities

The Company has an operating lease contract under which the free fibres of the fibre-optic cable fixed to the line masts are leased out. This cable also acts as a lightning protection cord for the lines and the fibres are used by the Company for its technical communication. The free fibres have been leased out to Televõrgu AS. The lease contract contains a restriction under which the Company cannot give its transmission equipment out for use by other companies operating in the telecommunications field. The contract is effective until 31.03.2025. Annual lease payments vary depending on the length of fibres leased out during the year.

Information about assets (facilities) leased out under operating leases

in thousands of euros	*31.12.2013*	*31.12.2012*
Cost	5,707	5,805
Accumulated depreciation at the end of period	-3,326	-2,937
Carrying amount	**2,381**	**2,868**

Depreciation charge

in thousands of euros	*2 013*	*2 012*
Depreciation charge	399	349

Estimated future lease payments under operating leases

in thousands of euros	*31.12.2013*	*31.12.2012*
Not later than 1 year	855	848
Later than 1 year and not later than 5 years	3,420	3,392
Later than 5 years	5,344	6,148
Total future minimum lease payments	**9,619**	**10,388**

Company as a lessee

Operating lease expenses

in thousands of euros	*2013*	*2012*
Buildings	36	36
Transport equipment	86	82
Other machinery and equipment	21	19
Total operating lease expenses	**143**	**137**

All operating leases where the Company is a lessee can be terminated upon a short notice.

Note 24

BALANCES AND TRANSACTIONS WITH RELATED PARTIES

Parties are generally considered to be related if the parties are under common control or if one party has the ability to control the other party or can exercise significant influence or joint control over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

In preparing financial statements of the Company, the following parties have been considered as related parties:

(I) Republic of Estonia and the entities under its control or significant influence
(II) Management and Supervisory Boards
(III) Close relatives of the persons described above and the entities under their control or significant influence

The outstanding balances with related parties were as follows

in thousands of euros	*31.12.2013*	*31.12.2012*
Trade receivables		
Companies controlled or significantly influenced by the State	19,162	20,889
Total trade receivables	**19,162**	**20,889**
▪ incl. from network operators	17,661	19,640
Trade payables and other liabilities		
Companies controlled or significantly influenced by the State	3,524	2,981
Total trade payables and other liabilities	**3,524**	**2,981**

Income and expense items with related parties were as follows

in thousands of euros	*Related party*	*2013*	*2012*
Revenue from sale of goods	Companies controlled or significantly influenced by the State	14,120	7,096
Revenue from sales of services	Companies controlled or significantly influenced by the State	85,255	79,070
Total revenue from sale of goods and services		**99,375**	**86,166**
Purchase of goods	Companies controlled or significantly influenced by the State	3,132	14,706
Purchase of services	Companies controlled or significantly influenced by the State	6,407	10,065
Total purchase of goods and services		**9,539**	**24,771**
Expenditures on non-current assets	Companies controlled or significantly influenced by the State	**39,299**	**1,932**
▪ incl. purchase of electricity interconnector Estlink 1 between Estonia and Finland		38,499	0

- Revenue from sales of goods is incurred by the sale of balancing electricity and reactive energy
- Revenue from sales of services is incurred mainly from sale of network services and lease of fibre-optic cable.
- The purchase of goods results from the purchase of balancing electricity and reactive energy and purchase of electricity to compensate losses.

- Purchase of services mainly includes power regulation service, lease of capacity of the Estonian-Finnish undersea cable, operative switching and dispatching management services and maintenance and repair services.

Transactions with companies under the significant influence of the members of the Supervisory and Management Boards or their close relatives

in thousands of euros	*2013*	*2012*
Sales of services	**51**	**0**

Key management personnel compensations are disclosed in Note 20.

Receivables and payables to related parties are disclosed in Notes 8 and 13. The receivables from related parties were written off neither in 2013 nor 2012.

Note 25

CONTINGENT LIABILITIES AND BINDING COMMITMENTS

Network development obligations
Under the Electricity Market Act, the network operator must develop the network within its service area in a way that ensures the continued provision of network services in accordance with the set requirements.

Capital expenditure commitments
On 31.12.2013, the Company has contractual capital expenditure commitments in respect of property, plant and equipment totalling EUR 100,999 thousand (31.12.2012: EUR 232,678 thousand). The largest of them are the contracts for the construction of the second undersea electricity cable Estlink 2 between Estonia and Finland (EUR 24,759 thousand) and expenditure on the emergency reserve power plant (EUR 52,613 thousand).

Tax liabilities
The tax authorities have the right to verify the Company's tax records up to 5 years from the time of submitting the tax declaration and upon finding errors, impose additional taxes, interest and fines. The Company's management estimates that there are not any circumstances which may lead the tax authorities to impose additional significant taxes on the Company.

Other disputes
A claim in the amount of EUR 9,170 thousand has been filed against the Company. According to the claim, transmission system operators of Baltic countries caused one market participant damages by failing, when distributing cross-border transmission capacities, to implement mechanisms provided by the law and therefore, all three transmission system operators are equally liable for such damages. In the Company's opinion, the claim is groundless and the likelihood of its realisation is low.

INDEPENDENT AUDITOR'S REPORT

(Translation of the Estonian original)*

To the Shareholder of Elering AS

Report on the Financial Statements

We have audited the accompanying financial statements of Elering AS (the Company), which comprise the statement of financial position as of 31 December 2013 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

Management Board's Responsibility for the Financial Statements

Management Board is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the European Union, and for such internal control as the Management Board determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control[1]. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of 31 December 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Report on Other Legal and Regulatory Requirements

During the audit we have not noted any material inconsistencies between the accompanying financial statements and the regulatory requirements as set out in Electricity Market Act and legislation established on the basis thereof.

AS PricewaterhouseCoopers

Stan Nahkor
Auditor's Certificate No. 508

17 March 2014

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[*] *This version of our report is a translation from the original, which was prepared in Estonian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.*

PROFIT ALLOCATION PROPOSAL

The retained earnings of Elering AS as of 31.12.2013 were EUR 117,939 thousand.

The Management Board of Elering AS proposes to the sole shareholder to allocate the retained earnings as follows:

Statutory legal reserve	EUR 2,448 thousand
Retained earnings	EUR 115,491 thousand

SIGNATURES OF THE MANAGEMENT TO THE 2013 ANNUAL REPORT

The signing of Elering AS 2013 Annual Report on 17 March 2014.

Taavi Veskimägi
Chairman of the Management Board

Kalle Kilk
Member of the Management Board

Peep Soone
Member of the Management Board

THE REVENUE OF ELERING AS ACCORDING TO EMTAK 2008

The revenue of Elering AS is divided by the main areas of activities as follows:

EMTAK area of activity*	*1.01.2013 - 31.12.2013*	*1.01.2012 - 31.12.2012*
35121 Transmission of electricity – transmission through the transmission network	112,188	94,529
35141 Trade of electricity (balancing electricity)	20,259	13,046
77399 Renting and leasing of other machinery, equipment and tangible goods n.e.c.	848	840
47770 Retail sale of other second-hand goods	338	187
68201 Renting and operating of own or leased real estate	203	330

* *EMTAK – classification of Estonian economic activities*

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Estonia was captured by sky photographer Andres Tarto